



The Educator

ISSUED BI-MONTHLY BY

FLORIDA INSTITUTE OF TECHNOLOGY

MELBOURNE, FLORIDA

May, 1976

"Pay to the order of . . ."

(Some Reasons for Giving Cash)

*Most Modest-sized Gifts
Are Made with Cash
Because of the Convenience
of Simply Writing a Check*

IN the early days of this nation, gifts to charitable organizations of tobacco, farm products, animals and rum were not unusual. Today, contributions range from cash and marketable securities to real estate, life insurance and a host of other kinds of property. While many of the larger gifts we receive are made with property other than cash, some large gifts and most of the modest-sized gifts are made in cash—usually in the form of a check.

A gift by check is often the most practical way to make a modest-sized contribution. Such gifts fit smoothly into the personal or household accounting system where they can be budgeted with other expenditures. Also, when a check is used, the cancelled check serves as convenient proof of the amount of the gift.

A check is sometimes the most advantageous way of making a larger gift. This issue of the bulletin discusses some of the reasons why sizable gifts are sometimes made with cash.

Convenience

A GIFT by check may be a most convenient way of making a sizable gift. For example, assume that some months after her husband's death Mrs. A decided to make a substantial gift to us as a memorial to Mr. A. She did not have any securities that had appreciated significantly in value, but she had just received a sizable distribution of cash from Mr. A's estate. At her attorney's suggestion, and as a matter of her own convenience, Mrs. A decided to write a check for the full amount of her gift.

The Maximum (50%) Charitable Deduction Limitation

IN addition to the convenience of giving cash, Mrs. A enjoyed an important income tax benefit from having made her gift in the form of

*A Gift by Check Is
Sometimes a Practical Way
to Make a Larger Gift*

*Gifts of Cash Qualify for
the Maximum (50%)
Limitation and Its Five-Year
Carryover Privilege*

cash.¹ For instance, assume that her gift amounted to \$100,000 and that her adjusted gross income in the year of the gift and in each of the five years thereafter will be \$36,000. Mrs. A's gift entitled her to an income tax deduction of \$100,000. In addition, since it was made with cash, it qualified for the maximum annual federal income tax limitation (i.e. 50% of adjusted gross income) and its five-year carryover privilege.

In the year of the gift, Mrs. A deducted \$18,000 (50% of \$36,000). In each of the next four years, she will also deduct \$18,000—making a total of \$90,000 ($5 \times \$18,000$). Finally, in the fifth year after the gift, the final carryover year, she will deduct the remaining \$10,000 of her \$100,000 deduction.

If instead of giving cash Mrs. A had given \$100,000 worth of appreciated securities or real estate which, if sold, would have produced long-term capital gain, she would have been entitled to the same \$100,000 deduction. However, her deduction would have been subject to the 30% of adjusted gross income limitation and the five-year carryover provision that applies to such gifts. In brief, in the year of the gift and in each of the carryover years, her deduction would have been limited to \$10,800 (30% of \$36,000). This would have meant that over the six year period she could have deducted only \$64,800 ($6 \times \$10,800$), leaving her with an unusable deduction of \$35,200.

Cash Is Not Always the Best Way to Make a Gift

WHILE a gift of cash is usually convenient and sometimes provides unique income tax advantages, cash is not the only way to make a gift, and it frequently is not the most advantageous way. Unfortunately, however, many people think that cash is the only way to make a charitable contribution. And, acting on this mistaken impression, some donors sell property and pay a long-term capital gain tax in order to raise cash to make their charitable gifts.

*Giving Cash Is Not the
Only Way to Make a
Gift to Us*

For example, assume that Mr. B wanted to make a \$25,000 gift to us and thought that he had to give us cash. Consequently, to raise cash to make the gift, he sold marketable securities worth \$25,000 that had cost him \$9,000 some years ago. In raising the cash, Mr. B generated a \$16,000 capital gain. Assuming the \$16,000 gain was taxed to him at a 25% capital gain tax rate, it cost him an extra \$4,000 to make the gift by using cash. Had he given the securities instead, he would have been entitled to a \$25,000 deduction, and he would have avoided the \$4,000 capital gain tax.

*A Gift of Cash Is Sometimes
a Costly Way to Give*

In brief, gifts of appreciated securities and real estate that qualify as *long-term* capital gain property entitle the donor to an income tax deduction for their full fair market value, and no capital gain tax is payable on the appreciation.² This "double-barrelled" tax benefit often makes such gifts particularly attractive.

However, as the example of Mrs. A indicates, if a person regularly

¹ This bulletin discusses only the *federal* income tax consequences of a gift. A deduction is also usually allowed in states which have income taxes.

² This bulletin does not discuss gifts of long-term capital gain *tangible personal* property. Such gifts are subject to a special *related in use* rule.

gives up to his or her maximum limitation, it should be borne in mind that the deduction for gifts of appreciated long-term capital gain property qualify for only a 30% (of adjusted gross income) limitation. Furthermore, gifts of long-term capital gain property are taken into account each year only *after* all gifts that qualify for the 50% limitation have been counted.³ In other words, long-term capital gain deductions are the first to be carried over each year. This increases the danger that some portion of the deduction will ultimately be lost if other substantial gifts are made and it is necessary to carry the gift of appreciated property over beyond the five year period.

Using Cash Instead of *Short-Term* Capital Gain and *Ordinary Income* Property

*Giving the Proceeds of Sale
Is More Advantageous
Than Giving Appreciated
Short-term Capital Gain
or Ordinary Income Property*

GENERALLY speaking, it is *disadvantageous* to make a charitable gift with appreciated *short-term* capital gain property or property which, if sold, would produce *ordinary income*. A charitable gift of such property entitles the donor to a deduction for only his or her cost or other income tax basis in the property. Consequently, rather than give such property, it is usually better to give cash—even if the donor has to sell the available property in order to raise the cash to make the gift.

In other words, if a person gives us securities, now worth \$10,000, that he purchased four months ago for \$5,000, he is entitled to a deduction not for \$10,000 but for only \$5,000. Obviously, this is an expensive way to make a gift. Therefore, in the case of appreciated short-term capital gain property or property which, if sold, would produce ordinary income, it is better to sell the property, pay the tax on the gain and give the remaining proceeds to us.

Using Cash Instead of Property That Has Depreciated in Value

*Giving the Proceeds of Sale
Provides More Advantages
Than Giving Property That
Has Depreciated in Value*

IT is also costly to give a capital asset that is worth *less* than it cost. This is true because a capital loss deduction is not available when such property is given, and the charitable deduction is limited to the fair market value of the property.

Consequently, instead of using property that has *depreciated* in value for a gift, it is better (1) to sell the property in order to establish the capital loss and (2) to give the proceeds of the sale. In such a case, two deductions are generated—one for the capital loss and the other for the charitable deduction.

A Reason for Using Cash to Fund a Charitable Remainder Trust

SOMETIMES, a person would like to make a sizable gift to us but feels that he or she cannot give up the income the gift property will

³ By a special provision in current law, when gifts to us of long-term capital gain property exceed the 30% limitation, the donor can elect to bypass the 30% limitation and bring the 50% limitation into play. This is accomplished by electing to have the charitable deduction reduced to the extent of half of the appreciation in all of the long-term gifts.

*Cash Is Usually Used to
Fund a Charitable Remainder
Trust Where the Trustee
Will Invest in
Tax-exempt Securities*

*We Will Be Happy to Talk
With You About How You
Might Make a Gift to Us*

produce. Fortunately, there are a number of ways in which gifts can be made with income reserved. For instance, a gift with income retained can be made through a charitable remainder annuity trust or unitrust. In fact, it is frequently possible through the use of such a trust to greatly increase the rate of return from the gift property without sacrificing any of the assets to capital gain taxes.⁴

Sometimes, a person who creates a charitable remainder trust wants the trustee to invest in tax-exempt securities. The Internal Revenue Service has ruled, however, that if the trustee is required, either expressly or by implication, to sell property that has appreciated in value and invest the proceeds in tax-exempt securities, the gain on any such sale will be taxed to the donor. This ruling is an important reason why some charitable remainder trusts are funded with cash.

Where a person creates a charitable remainder annuity trust or unitrust that is to invest in tax-exempt securities, cash is usually used to fund the trust. This avoids the danger that the capital gain would be taxed to the individual if appreciated property had been transferred to the trustee and then sold to invest the proceeds in tax-exempt securities.

Conclusion

WHEN making a gift to us, it is quite natural to think first of making the gift with cash. In a great many cases, a gift by check is the most convenient and advantageous way to make the gift. In a number of cases, however, gifts of appreciated long-term capital gain property offer multiple tax advantages of great value. We will be happy to talk with you about the various ways in which you can make a gift to us.

⁴ This increased rate of return is made possible by the fact that when appreciated long-term capital gain securities (and real estate) are used to fund such a trust, no capital gain tax is payable when the assets are transferred to the trust or when the assets are later sold by the trustee.

This bulletin has been compiled by qualified estate and tax specialists and presents, in simple and non-technical language, facts and practical illustrations on estate and tax problems. Necessarily, the information is general, and the legal principles involved should be applied by your attorney.

The Development Department of Florida Institute of Technology welcomes an opportunity to cooperate with you and your financial advisors in planning a current or deferred gift to the university. F.I.T. will also be happy to provide you with details of its Development plans and its many special programs in which you might have an interest.

Any inquiries will receive the personal and confidential attention of a member of F.I.T.'s experienced staff.

Vice President for Development Affairs
Florida Institute of Technology
Box 1150 • Melbourne, Florida 32901
(305) 723-3701

F.I.T. admits students of any race, color, and national or ethnic origin.