Charitable gifts and bequests of works of art offer a means for art collectors to provide the public with the opportunity to view the art that they have collected while simultaneously generating a tax benefit for the collectors or their estates. This column examines the various income tax, gift tax, and estate tax aspects of charitable contributions of works of art.

**Income tax deductions**

A person who contributes a work of art to a charity, in addition to satisfying the donor’s goal of benefiting the donee organization, generally wants to receive an income tax charitable deduction for the contribution. The income tax rules regarding such contributions can be extremely complex and require careful attention to ensure that the donor receives the maximum deduction allowable for the contribution.

**Deductible amount.** A charitable contribution of a work of art, outright and free of trust, entitles the donor to an income tax charitable deduction equal to the fair market value of the work contributed, if the contribution satisfies all of the following requirements:

- The donee is a public charity, a private operating foundation or a private foundation that generally distributes all of its contributions each year.
- The work of art, if sold by the donor, would generate long-term capital gain for income tax purposes (commonly referred to as “long-term capital gain property”).
- The donee charity must use the work in a manner that is related to the charity’s tax-exempt purpose (commonly referred to as the “related-use requirement”).

If the contribution fails to satisfy any of these requirements, the donor’s income tax charitable deduction is generally the lesser of (1) the donor’s tax cost basis for the work contributed or (2) the work’s fair market value at the time of the contribution.

**Classification of charities.** Charities to which contributions are deductible for income tax purposes pursuant to Section 170(a) are generally classified under Section 509(a) as public charities (i.e., religious organizations, educational or medical institutions, and publicly supported charities), private operating foundations, or other private foundations. A charity’s classification can be determined by obtaining a copy of the communication that the charity received from the IRS setting forth that classification, or by reference to IRS
Publication 78, *Cumulative List of Exempt Organizations.*

**Long-term capital gain property.** In order to be long-term capital gain property, the work of art:

1. Must be a capital asset.
2. Must have appreciated in value.
3. Must have been held by the donor for more than one year.

Thus, “long-term capital gain property” would exclude the following assets:

- A work of art contributed by the person who created it, as a sale of such work by the artist would generate ordinary income.
- A work of art contributed by a person who received it as a gift from the individual who created the work, as the sale of such work by the owner would similarly generate ordinary income.
- A work of art contributed by a dealer who held it as inventory, as the sale of such work would also produce ordinary income.
- A work of art held by the donor for less than one year, as its sale at a gain would generate short-term capital gain.

**Related-use requirement.** A donor who contributes a work of art to a charity can treat the gift as being put to a related use if the donor establishes that the property is not in fact put to an unrelated use by the donee, or if at the time of the contribution it is reasonable to anticipate that the property will not be put to an unrelated use by the charity, unless the donor has actual knowledge to the contrary.  

In addition, even if the charity uses the contributed work of art in a manner that is related to its tax-exempt purpose, the donor’s income tax charitable deduction is generally limited to his or her tax cost basis for the work of art if the charity sells the property before the end of the year in which the donor made the contribution, unless the charity either:

1. Certifies that its use of the property was substantial and related to its tax-exempt purpose, and describes how it used that property and how such use furthered that purpose.
2. Describes its intended use of the property at the time of the contribution and certifies that such intended use became impossible or infeasible to implement.  

Furthermore, if the donee charity disposes of the work of art after the close of the tax year in which the donor made the contribution and before the end of the three-year period beginning on the date of the contribution, the donor must recapture the deduction for the contribution in excess of the donor's tax cost basis in the contributed property, unless the donee charity makes the certification described above.  

**Gifts of partial interests.** A person may prefer to contribute partial interests in a work of art to a charity over time, rather than contributing the entire work at one time. In general, an income tax charitable deduction for a contribution of a partial interest in property to a charity is prohibited. However, a charitable gift of a partial interest in property will qualify for an income tax charitable deduction if:

- The contribution is part of a series of contributions in which all of the interests of the taxpayer in the property are given to charitable organizations.  
- The contribution is the donor's entire interest in the property.  
- The contribution is an undivided portion of the donor's entire interest in the property.  

Additional rules, however, apply in connection with a charitable contribution of a partial interest in a work of art. A taxpayer cannot claim an income tax charitable deduction for a contribution of an undivided portion of the taxpayer's entire interest in a work of art, unless all of the interests in that property are held immediately before the contribution by the taxpayer, or by the taxpayer and the charitable donee. Thus, if a husband and wife together own a work of art and contribute a fractional interest in the work to a charity, the rule stated in the immediately preceding sentence might prevent them from claiming an income tax charitable deduction for the contribution.  

Section 170(o)(1)(B), however, authorizes the Service by regulation to provide exceptions to this rule where all the persons who hold
an interest in the property make proportional contributions to a charity of an undivided portion of the entire interest in the property that such persons hold. Although the Service has not yet issued regulations that cover this point, those regulations, when issued, may address the case of a husband and wife both contributing a fractional interest in a work of art to a charity.

In addition, when the donor makes a subsequent contribution of a fractional interest in the work of art, the subsequent contribution is the fractional interest contributed, multiplied by the lesser of the fair market value of the work of art at the time of the first fractional contribution, or the fair market value of the work of art at the time of the later contribution. Thus, if the value of the work of art has appreciated between the date of the first fractional contribution and the date of the subsequent fractional contribution, the donor's income tax charitable deduction for the subsequent contribution is determined by reference to the work's fair market value at the time of the first contribution. If the value of the work of art has decreased between the date of the first contribution and the date of the subsequent contribution, the income tax charitable deduction is determined by reference to the work's value on the date of the subsequent contribution.

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Onerous provisions regarding the recapture of the income tax benefit generated by a charitable contribution of a fractional interest in a work of art apply if the donor does not contribute the balance of his or her interest in that work to the charity within a specified period. These provisions stipulate that if a person contributes a fractional interest in a work of art to a charity, the income tax charitable deduction generated by that contribution (plus interest) will be recaptured, unless the donor contributes all of his or her remaining interests in that property to the charity within ten years after the date of the initial fractional contribution, or by the date of the donor's death, if earlier.

In addition, the recapture will also apply if the donee charity has not had substantial physical possession of the contributed property, or has not used the contributed property in a manner that is related to the charity's tax-exempt purpose during the period beginning on the date of the initial fractional contribution and ending on the earlier of the above-mentioned ten-year period or the date of the donor's death. Furthermore, in the case of such recapture, the donor's income tax for the tax year of the recapture is increased by 10% of the recaptured amount. Thus, in the case of a charitable contribution of a fractional interest of a work of art, it is imperative that the donor contribute his or her remaining interest in the work to the donee charity within the above-described time period in order to obtain the desired income tax charitable deduction and to avoid the 10% "penalty" imposed by that section in the event of such recapture.

Gifts in trust. Instead of contributing a work of art to a charity, outright and free of trust, a donor may consider the desirability of contributing the work to a trust in which the donor retains an interest for his or her life and that provides for the disposition of the trust's assets to a charity on the donor's death (commonly referred to as a charitable remainder trust). However, an income tax charitable deduction ordinarily will not be allowed for the remainder interest of a transfer of property in trust, unless the trust is a charitable remainder annuity trust (CRAT), a charitable remainder unitrust (CRUT), or a pooled income fund.

A CRAT requires the trust to pay an annuity annually to the trust's noncharitable beneficiary or beneficiaries, and a CRUT ordinarily requires the trust to pay a fixed percentage of the trust's annual fair market value to the trust's noncharitable beneficiary or beneficiaries each year. This type of contribution may appear especially desirable in the case of a work of art that has appreciated substantially in value, because a charitable remainder trust is exempt from income tax. The trustee therefore can sell the work of art without the grantor paying income tax on the sale, and the grantor of the trust would be entitled to an income tax charitable deduction based on the present value of the remainder interest in the trust holding the work.

A work of art, however, ordinarily is not an income-producing asset. As a result, a CRAT or a CRUT to which a work of art is contributed usually will not have any income from which to pay the amount required to be distributed annually by the trust to its noncharitable beneficiary or beneficiaries. In addition, if the trust does not require the trustee to sell the work of art promptly after acquiring it, the Service may determine that the trust does not qualify as a charitable remainder trust, because it cannot make the required periodic distributions to the noncharitable beneficiary or beneficiaries. In such event, the grantor would be denied an income tax charitable deduction for the contribution to the trust, and the trust would be required to pay income tax on any gain realized from its sale of the work. For these reasons, a contribution of a work of art to a trust is generally inadvisable.

Despite the foregoing, it may be possible to contribute a work of art to a CRUT and avoid these potential problems. In order to do so, the trust should direct that it will distribute to the noncharitable beneficiary or beneficiaries each year only its net income, if less than the stated pay-out percentage, and that it will "make up" such shortfall in subsequent years to the extent that the trust's net income in those years exceeds the stated pay-out percentage (commonly referred to as a net income make-up charitable remainder unitrust, or...
However, a taxpayer’s aggregate amount of charitable contributions to public charities and private operating foundations ("50% charities") in any year is limited to 50% of the taxpayer's adjusted gross income for that year. In addition, a taxpayer’s aggregate income tax charitable deductions for contributions to private foundations, other than private operating foundations ("30% charities"), is generally limited to 30% of the taxpayer’s adjusted gross income for that year. However, a taxpayer’s aggregate amount of charitable deductions for contributions of appreciated property, the sale of which would generate long-term capital gain, to "50% charities," or to "30% charities," is generally limited to 30%, or 20%, respectively, of the taxpayer’s adjusted gross income for that year. Moreover, further percentage limitations may apply to charitable contributions of works of art.

In general, a taxpayer’s aggregate charitable deductions for contributions to public charities and private operating foundations ("50% charities") in any year is limited to 50% of the taxpayer's adjusted gross income for that year. In addition, a taxpayer’s aggregate income tax charitable deductions for contributions to private foundations, other than private operating foundations ("30% charities"), is generally limited to 30% of the taxpayer’s adjusted gross income for that year. However, a taxpayer’s aggregate amount of charitable deductions for contributions of appreciated property, the sale of which would generate long-term capital gain, to "50% charities," or to "30% charities," is generally limited to 30%, or 20%, respectively, of the taxpayer’s adjusted gross income for that year. Moreover, further percentage limitations may apply to charitable contributions of works of art.

If a donor contributes a work of art that is long-term capital gain property to a public charity or a private operating foundation and is eligible for an income tax charitable deduction for the full fair market value of the work, then the maximum allowable deduction for the contribution is the lesser of 30% of the donor's adjusted gross income, or the donor's 50% limitation described above that remains after taking into account the donor's other contributions to public charities. The donor may elect, however, to deduct only his or her tax cost basis in the work of art contributed, rather than its full fair market value; if this election is made, the 50% limitation will apply—without regard to the 30% limitation.

If the donor contributes a work of art to a private foundation, the allowable income tax deduction for the contribution is limited to the lesser of 20% of the donor's adjusted gross income for the year in which the contribution is made, or the excess of 30% of the donor's adjusted gross income for that year that remains after taking into account his or her contributions of long-term capital gain property to charities that qualify for the 50% limitation. The election, described above, for the contribution of long-term capital gain property to public charities is not available for contributions to private foundations.

Generally, the donor can carry forward for five years the portion of the income tax charitable deduction that is not used by reason of these percentage limitations.

Substantiation requirements. In addition to the requirements and limitations described above, Section 170(a)(1) provides that an income tax charitable deduction for a charitable contribution will be allowable only if it is verified in accordance with regulations prescribed by the Service. Section 170(f)(11), in relevant part, provides that certain income tax charitable deductions are not allowed
unless the requirements of that subsection, described below, are satisfied. Thus, these requirements are a prerequisite to the allowance of an income tax charitable deduction, and the failure to satisfy them results in the disallowance of the claimed deduction.

In the case of a charitable contribution of tangible personal property for which an income tax deduction of more than $5,000 is claimed, the taxpayer must obtain a “qualified appraisal” of the property prepared by a “qualified appraiser.” In addition, the taxpayer must attach to his or her income tax return for the tax year in which the contribution is made the information regarding the contributed property and regarding the appraisal that the Service may require by regulation. These requirements include attaching IRS Form 8283 to the taxpayer’s income tax return. For a claimed deduction of more than $5,000, the form requires:

- A description of the donated property and its condition at the time of the gift.
- The property’s appraised fair market value.
- The date on which the donor acquired the property and how he or she acquired it.
- The donor’s tax cost basis for the property.

In addition, Form 8283 requires that the taxpayer must attach such appraisal to his or her income tax return.

Qualified appraisal. For this purpose, the term “qualified appraisal” means an appraisal that includes:

- A detailed description of the property.
- The property’s physical condition.
- The date or the expected date of the charitable contribution of the property.
- A detailed description of the appraiser’s background and qualifications.
- A statement that the appraisal was prepared for income tax purposes.
- The date on which the property was valued.
- The property’s appraised fair market value.
- The method of valuation used by the appraiser to determine the property’s fair market value (e.g., the income approach, market-data approach, or replacement-cost-less-depreciation approach).
- The specific basis used by the appraiser for determining the property’s fair market value (e.g., specific comparable sales transactions or statistical sampling).
- A description of the fee arrangement between the appraiser and the donor of the property. The appraiser’s fee for preparing the appraisal cannot be based on or related to the appraised value of the property. Furthermore, the appraisal must be made within 60 days preceding the date of the charitable contribution of the work of art that is being appraised.

Qualified appraiser. The term “qualified appraiser” means an individual who:

- Has earned an appraisal designation from a recognized professional appraiser organization or has otherwise satisfied certain minimum education and experience requirements.
- Regularly performs appraisals for compensation.
- Demonstrates verifiable education and experience in valuing the type of property subject to the appraisal.
- Successfully completed college- or professional-level course work that is relevant to the property being valued.
- Has at least two years of experience in the trade or business of buying, selling, or valuing the type of property being appraised.

In addition, the appraisal must contain a declaration by the appraiser that he or she understands that a substantial or gross valuation misstatement resulting from the appraisal of the value of the property that the appraiser knows, or reasonably should have known, will be used in connection with a tax return or a claim for a tax refund, may subject the appraiser to a civil penalty under Section 6695A.

Gift tax deductions

An outright contribution of a work of art to a charity entitles the donor to a gift tax charitable deduction for the contribution. The gift
tax charitable deduction is the fair market value of the work of art contributed, regardless of whether it is long-term capital gain property, and regardless of whether the donee charity is a public charity or a private foundation.

No gift tax charitable deduction is allowed for the contribution of a gift of a fractional interest in a work of art, unless all of the interests in the property are held immediately before the contribution by the taxpayer, or by the taxpayer and the donee charity. As in the case of an income tax charitable deduction for a contribution of a fractional interest in a work of art, Section 2522(e)(1)(B)—regarding the gift tax charitable deduction for such gifts—similarly authorizes the Service by regulation to provide exceptions to the rule stated in the immediately preceding sentence, where all of the persons holding an interest in the property contributed to charity make proportional contributions of a undivided portion of the entire interest in the property that such persons hold. Again, regulations, when issued, could address the question of a gift tax charitable deduction for a charitable contribution of a fractional interest in a work of art that is owned by a husband and wife.

In addition, gift tax charitable deduction recapture rules that are similar to the recapture rules, discussed above, with respect to the income tax charitable deduction (including the 10% penalty discussed above) apply if the donor does not contribute all the remaining interests in the property to the donee charity before the earlier of ten years after the date of the initial fractional contribution or the date of the donor's death, or if the donee charity has not had substantial physical possession of the property and used it for a purpose related to its charitable exemption during the period.

Estate tax deductions

A person may decide to bequeath a work of art to charity on his or her death, rather than donating the work to a charity during the donor’s life. In such event, the donor's estate will receive an estate tax charitable deduction for the fair market value of the work of art bequeathed to charity, regardless of whether the work would have been "long-term capital gain" property if the person had made a lifetime contribution of the work to charity, and regardless of whether the charitable beneficiary is a public charity or a private foundation.

In the case of a bequest of a work of art to a split-interest charitable trust, an estate tax charitable deduction is not allowable unless the bequest is made to a CRAT or a CRUT. For the same reasons discussed above with respect to a lifetime transfer of a work of art to a CRAT or CRUT, a testamentary transfer of a work of art to a CRAT or a CRUT is generally inadvisable.

In addition, as described above, a major benefit of a contribution during the donor’s life of a highly appreciated work of art to a CRAT or a CRUT is the ability of the trust to sell the work without paying income tax on the gain realized on the sale. Absent further legislation, that consideration is inapplicable in the case of a bequest of a work of art for the estate of a person who dies after 2010, because the testator's estate will receive a "stepped-up basis” in the work to its estate tax value at the testator's death. Thus, in such case, any unrealized appreciation prior to the testator's death will not be subject to income tax on the sale of the work.

Conclusion

As can be seen from the foregoing, the rules regarding the income tax, gift tax, and estate tax deductions for contributions of works of art to a charity can be extremely complex. A person considering any such charitable transfer must fully comply with these requirements to ensure that the desired tax result is achieved.

2. Section 170(e)(1)(B)(i)(II).
3. Section 170(e)(7).
4. Section 170(f)(3).
Reg. 1.170A-7(a)(2)(i).


Section 170(o).

Section 170(o)(2).

Section 170(o)(3)(A)(i).

Section 170(o)(3)(A)(ii).

Section 170(f)(2)(A).

Section 664.

Sections 170(b)(1)(A) and 170(b)(1)(B).

Section 170(b)(1)(C)(i).

Section 170(b)(1)(C)(iii).

Section 170(b)(1)(D).

Section 170(d).

Section 170(f)(11)(C).

Reg. 1.170A-13(c).


Reg. 1.170A-13(c)(b)(i).

Section 170(f)(11)(E); Notice 2006-96, supra note 21

Section 2522.

Section 2522(e).

Section 2522(e)(2).

Section 2055.

Section 2055(e).