

NEW RULES FOR CHARITABLE GIVING: Highlights of the Pension Protection Act

ALTHOUGH THE PENSION PROTECTION ACT OF 2006 ("THE ACT") PRINCIPALLY ADDRESSED RETIREMENT SAVINGS (AS SUGGESTED BY THE ACT'S TITLE), IT ALSO CONTAINED SOME IMPORTANT CHARITABLE GIVING PROVISIONS. FIDELITY CHARITABLE SERVICES® WELCOMES THE ACT'S PROVISIONS THAT INCREASE CHARITABLE GIVING AND PREVENT ABUSES. IN THIS SUMMARY, FIDELITY CHARITABLE SERVICES HIGHLIGHTS SOME OF THE ACT'S CHARITABLE PROVISIONS THAT MAY AFFECT YOUR CLIENTS.

- **STATUTORY DEFINITION OF DONOR-ADVISED FUNDS.** For the first time, the Act creates a statutory definition of a donor-advised fund as part of the Internal Revenue Code. The statute provides that a donor-advised fund is a separate fund (or account) of a sponsoring charitable organization with respect to which a donor (or person named by the donor) can recommend grants to other charitable organizations, or may make investment recommendations.

Fidelity Charitable Services notes that this provision is an important development even though it only codifies a definition that many sponsoring organizations of donor-advised funds, including the *Fidelity Charitable Gift Fund*SM (the "Gift Fund"), have long employed. In short, the Act reflects the growth of donor-advised funds, and the important role that they play in the charitable sector.

- **CHARITABLE IRA ROLLOVER.** The new law permits people 70 1/2 and older to make direct transfers of IRA assets to qualified public charities without paying income tax on the withdrawals. (Donors are able to exclude the charitable IRA rollover from their taxable income, and are therefore not permitted also to take a deduction for a charitable contribution.) This provision expires at the end of 2007 and is relatively narrow in scope:
 - Donors must be already required to take annual IRA distributions (those over age 70 1/2).
 - Annual distributions eligible for charitable IRA rollover limited to \$100,000.
 - Eligible recipient charities generally include all public charities, but the statute expressly excludes donor-advised funds and supporting organizations from the group of qualified public charities eligible to receive charitable IRA rollovers.

- **DOCUMENTATION OF CASH CONTRIBUTIONS.** The Act tightens up the documentation requirements for charitable contribution deductions. Under the Act, a donor must have documentary evidence (a canceled check or a receipt from the charity) for any contribution in any amount (previously required only for contributions of \$250 or more).

Fidelity Charitable Services notes that this more onerous documentation requirement may cause an increasing number of donors to centralize and simplify their recordkeeping by utilizing donor-advised funds.

- **RULE AGAINST EXCESS BUSINESS HOLDINGS.** The Act extends the “excess business holdings” rules, which previously applied to private foundations, to donor-advised funds and Type III Supporting Organizations. Under this rule as applied to donor-advised funds, an individual donor-advised fund will be limited in the percentage (generally 20%) of an enterprise the donor-advised fund can hold, also taking into account the ownership interest of the donor and related persons. Under this rule, especially relevant to donors of closely held stock, the donor-advised fund must dispose of the shares within five years by redeeming them or finding a buyer.

Fidelity Charitable Services notes that this provision is unlikely to affect those donor-advised fund programs, including the Gift Fund, that have already established policies of selling contributed property as promptly as possible.

- **PENALTY PROVISIONS.** The Act included a number of provisions increasing penalties and applying new penalties to certain abusive transactions. Of particular interest to donor-advised funds and their donors:
 - A penalty on grant recommendations that result in “more than incidental benefit” to a donor, the donor’s family, or an entity in which they have at least 35% control (the penalty is 125% of benefit amount).
 - Automatic “excess benefit” penalties on grants, loans, compensation or similar payments by a donor-advised fund to a donor, advisor or relative. This provision would require that the offending party repay the entire amount, plus pay a 25% penalty to the government.
 - Application of the broader “excess benefit” penalty provisions to other transactions between (1) a transaction between a sponsoring organization and its investment advisors and related persons, and (2) a transaction (not covered by the “automatic excess benefit” rule described above) between a donor-advised fund and its donor or other related person.

Fidelity Charitable Services notes that many donor-advised fund programs, including the Gift Fund, have already established policies that prevent these types of impermissible payments.

- **INCREASED EXCISE TAXES FOR PRIVATE FOUNDATIONS.** The Act doubles many of the penalty excise taxes that are imposed on private foundations with respect to certain prohibited transactions.

- **PROVISIONS REGARDING SUPPORTING ORGANIZATIONS.** The Act also included a number of provisions clarifying the definition of “supporting organizations” under the Code. In addition, the Act imposes important new penalties and prohibitions regarding certain transactions between supporting organizations and substantial contributors or other “disqualified persons.”

- CONTRIBUTIONS OF PARTIAL INTERESTS OF TANGIBLE PERSONAL PROPERTY. The Act imposes new requirements on contributions of “partial interests” (less than complete ownership and possession) in property. (For example, it has become a common practice for donors to contribute partial interests in a work of art to a museum.) Under the new provision, donors must contribute the remaining interest in the property within 10 years (or upon their earlier death), or the donor will lose the initial deduction and also have to pay a 10% penalty. In addition, the donor’s charitable contribution deduction upon that later contribution is limited to the lesser of the fair market value of the contributed property at the time of the initial partial contribution or at the time of the later residual contribution. Moreover, the Act increases the requirements regarding the charity’s possession of the property, requiring that the charity have “significant possession” of the property.

- DEDUCTIONS FOR CLOTHING AND HOUSEHOLD ITEMS. The Act prohibits deductions for these items unless they are in “good used condition” or better, although it doesn’t define the term. The new rule doesn’t apply if the deduction for any single item is more than \$500, and the taxpayer files a qualified appraisal with their tax return.

If you have questions or would like to discuss any of these provisions further,
please contact a Fidelity Charitable Services representative at 800.280.6357

The *Fidelity* Charitable Gift Fund (“Gift Fund”) is an independent public charity with a donor-advised fund program. Various Fidelity companies provide non-discretionary investment management and administrative services to the Gift Fund.

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