



Philanthropic Estate Planning*

By Janet Nava Bandera

Vehicle Donation Programs Are on the Rise—Are They Legitimate?

Radio and television are full of advertisements soliciting charitable donations of automobiles. These donations create awareness of an organization and are an important source of revenue for a number of charities. But, many questions have arisen regarding whether the public is aware that the amount the charity actually receives may be far less than the value of the vehicle. There is also debate as to whether taxpayers are claiming appropriate tax deductions.

Background

The Tax Code allows individuals and businesses to make noncash contributions (e.g., vehicles, paintings, used clothing and household goods) to qualifying charities by allowing taxpayers to claim deductions for their donations on their tax returns. IRS guidance instructs donors to establish the value for their donation based on its “fair market value.” For donated vehicles, that is what the item would sell for on the market, taking into account its condition, including mileage. As is the case for all noncash contributions, the IRS does not require donors to obtain an independent appraisal for a vehicle’s value unless they claim over \$5,000 for the donated property. IRS guidance suggests that donors use used car guides, comparable sales and other sources to assist in establishing the fair market value for their donated vehicles.

Vehicle Donation Process

The vehicle donation process generally consists of four steps: (1) solicitation/donor contact, (2) vehicle pick-up, (3) vehicle sale, and (4) distribution of proceeds. Most charities use third-party agents for some or all of these steps rather than relying on in-house resources, and some have arrangements with more than one agent.

General Accounting Office (GAO) Investigation

The GAO investigated and reported on vehicle donations from October 2002 thru October 2003. The report

discussed (1) the number of charities with vehicle donation programs; (2) the number of taxpayers claiming deductions for vehicle donations; (3) the vehicle donation process; (4) proceeds received by charities from vehicle donations compared to what donors claim for vehicle donation deductions; (5) IRS and state compliance activities directed at vehicle donations and the results of these activities; and (6) guidance available to taxpayers and charities to help them make informed decisions regarding vehicle donations.

Participation by Charities

An estimated 4,300 U.S. charities with annual revenue of \$100,000 or more are operating vehicle donation programs. This is less than three percent of the 157,500 charities with income at or exceeding this level. Based on GAO estimates, tax deductions for donated vehicles were claimed on about 733,000 tax returns for tax year 2000, or an estimated 0.6 percent of the 129 million individual returns filed that year. These deductions lowered taxpayers’ income tax liability by an estimated \$654 million.

Charity Proceeds Much Less Than Values Claimed by Donors

The GAO study revealed that charities receive between zero and 54 percent of the value claimed by donors, with most receiving five percent or less of the amount the value donors claimed as a deduction on their tax returns. Two factors contribute to this difference: (1) vehicles are often sold at auto auc-

Janet Nava Bandera, J.D., is the Principal of The Bandera Law Firm, P.C. Ms. Bandera specializes in estate and charitable planning and serves on the Boards of two private foundations as well as The Heritage League of The American Cancer Society in St. Louis. She may be reached at The Bandera Law Firm, 700 Corporate Park Drive, Suite 340, Clayton, MO, 63105, (314) 691-4386.

tions for salvage or at wholesale prices, which are typically lower than prices that would be received if the donor sold the vehicle themselves, and (2) processing costs and fees (such as towing, advertising, program administration and third-party agent fees) are deducted from gross sales revenue, further reducing charity proceeds.

For some vehicle donation sales, charities receive no proceeds after the costs of vehicle donations are deducted. For six of the 54 donated vehicles the GAO tracked, the processing costs exceeded the sales price for the vehicle. For charities using third-

party agents, whether the loss is absorbed by the third-party agent or deducted from charity proceeds from another higher value donated vehicle depends on the agreement between the parties.

Example

In a case tracked by the GAO, a 1983 GMC Jimmy truck was donated in 2001 to a charity whose vehicle donation program is operated by a third-party agent. The gross sale price for the truck, which sold at an auction, was \$375. After deducting third-party and advertising expenses, net proceeds from the ve-

Appendix I: Vehicle Donation Guidance

Government and consumer organizations provide guidance to donors to assist them in making informed decisions about donating vehicles. Guidance is also available to charities to assist them in selecting, hiring and managing third-party agents. A partial list of resources is included below.

1. Internal Revenue Service—www.irs.gov. Lists tax-exempt organizations that may qualify donors for tax deductions (Pub. 78). The IRS also suggests Guidestar (see below) as a resource. Describes contributions that qualify for tax deductions and recordkeeping requirements (Pub. 526). Describes information necessary for donors to value and deduct noncash contributions (Pub. 561). Provides guidance for exempt organizations on documenting charitable contributions (Pub. 1771). Provides an annual brochure called *Exempt Organizations Implementing Guidelines: Vehicle Donations* that advises how exempt organizations can avoid problems with vehicle donation programs.

2. Federal Trade Commission—www.ftc.gov. Provides tips on how to recognize and avoid deceptive solicitations. In conjunction with state officials, the FTC launched Operation Phony Philanthropy to identify fraudulent fundraising activities; none of these cases to date have involved vehicle donations.

3. State Charity Regulators—The National Organization of State Charity Officials—www.nasconet.org. Lists contacts for state regulators overseeing charitable solicitations, including those with vehicle donation programs, and general information state regulators need to know.

4. Individual state Web sites. Provide information to donors on making contribution decisions, including financial information on charities or their fundraisers.

5. Guidestar—www.guidestar.org. Provides a national database of U.S. charitable organizations and general information relevant to IRS-recognized nonprofits.

6. Better Business Bureau's Wise Giving Alliance—www.give.org/tips/usedcar.asp. Provides a Vehicle Donations Checklist that, among its seven tips, advises the donor to take a photo of the car for tax records and to keep copies of current classified ads or guide value estimates for similar vehicles. Provides general standards charities should meet, including those with vehicle donation programs, enabling donors to evaluate (1) how charities are governed, (2) the ways they spend money, (3) the truthfulness of their representations, and (4) their willingness to disclose basic information to the public. Standards also help charities maintain overall good governance of their vehicle donation programs.

7. Charity Navigator—www.charitynavigator.org. Provides advice to donors of used vehicles, such as urging donors who have to use third-party agents to research the percentage the charity ultimately receives.

8. American Institute of Philanthropy—www.charitywatch.org. Provides search capability to locate tax-exempt organizations that may qualify vehicle donors for tax deductions. Provides tips to donors of used vehicles, such as encouraging them to get a receipt from the charity for their vehicle donation.

9. Chronicle of Philanthropy—<http://philanthropy.com>. Provides general information for subscribers on all matters involving philanthropic enterprises, including fundraisers who may process vehicle donations.

hicle sale totaled \$62. This amount was split 50/50 between the third-party agent and charity, leaving the charity with \$31 from the vehicle donation. The taxpayer claimed a \$2,400 tax deduction for the donated vehicle on his/her tax return, based on the fair market value of the vehicle listed in a used car guidebook.

California is the only state that collects data on the proceeds received by charities from vehicle donation programs. According to the California Attorney General's records, 145 charities using third-party agents who had filed the required financial reports received approximately \$16 million, or 35 percent of the \$45.8 million raised from reported donated vehicle sales, during 2001. The amount of proceeds these charities received in California ranged from two percent to 80 percent of proceeds after third-party costs were deducted.

Audit Risk

While more compliance resources are being devoted to higher priority audit issues such as abusive tax shelters and high-income nonfilers, the IRS's National Research Program is to provide data on compliance problems associated with noncash contributions, including deductions for donated vehicles. Under the program, the IRS randomly selected about 47,000 tax year 2001 returns to determine whether taxpayers complied with statutory income, expense and tax reporting requirements. Returns with noncash contributions, including donated vehicles, could be subject to audit to verify donation claims. Once this project is completed in December 2004, the IRS plans to assess individuals' compliance related to deductions for noncash contributions and determine what actions are needed to help ensure proper reporting in this area.

Identifying Legitimate Programs

The IRS, state officials and other organizations provide guidance to taxpayers and charities to help them donate or accept vehicles. Guidance to taxpayers includes such things as helping them identify legitimate, well-run charities; avoid personal liability for their donated vehicles; claim appropriate tax deductions; and protect themselves from fraudulent marketing solicitations. Guidance to charities helps charities select and manage professional fund-raisers and suggested documentation to maintain for donated vehicles.

In addition to oversight by the IRS and state agencies, some private sector organizations develop standards to promote ethical charitable practices and collect information on charitable organizations. Charity "watchdog" organizations, such as the Better Business Bureau's Wise Giving Alliance, Council of Better Business Bureaus, American Institute of Philanthropy, Association of Fund-Raising Professionals and the Independent Sector, provide insight to the public on various fund-raising activities. These organizations collect information on charitable organizations and develop standards to promote ethical practices. They disseminate these standards in an effort to "inspire public confidence." These standards include the voluntary disclosure of an organization's activities, finances, fundraising practices, and governance. Appendix I lists specific sources for donor guidance.

Conclusion

Automobile contributions can be a legitimate source of revenue for charities, but the donor must choose carefully among the programs and carefully determine and accurately report the value of the donation on their tax return.

ENDNOTES

* Author's Note: The source of the information contained in this column is US Government General Accounting Office Report "GAO 04-73."

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