

Giving real estate to charity is rewarding, but beware of tax traps

Published on August 25, 2016

Did you know that the estate of director John Hughes donated the family's Illinois mansion to a nonprofit hospital? After allowing another charity to use the home for a fundraising event, the hospital sold the home and used the proceeds to expand its campus.

In this instance, two organizations were able to enjoy this gift. If you're considering donating real estate to charity, beware of these four potential tax traps:

1. When you donate real estate to a public charity, you generally can deduct the property's fair market value. But when you donate it to a private foundation, your deduction is limited to the lower of fair market value or your cost basis in the property.
2. If the property is subject to a mortgage, you may recognize taxable income for all or a portion of the loan's value. And charities might not accept mortgaged property because it may trigger unrelated business income tax. For these reasons, it's a good idea to pay off the mortgage before you donate the property or ask the lender to accept another property as collateral for the loan.
3. Failure to properly substantiate your donation can result in loss of the deduction and overvaluation penalties. Generally, real estate donations require a qualified appraisal. You'll also need to complete Form 8283, *Noncash Charitable Contributions*, have your appraiser sign it and file it with your federal tax return. If the property is valued at more than \$500,000, you'll generally need to include the appraisal report as well.
4. If the charity sells the property within three years, it must report the sale to the IRS. If the price is substantially less than the amount you claimed, the IRS may challenge your deduction. To avoid this result, be sure your initial appraisal is accurate and well documented.

Before taking action, please consult us to ensure that you avoid these traps.

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