SCHWAB CHARITABLE®

Contributing Privately Held Business Interests (C-Corps, S-Corps, LLCs, LPs) to Charity

by Barbara Benware, Vice President – Investment Oversight and Risk

For philanthropically minded business owners, assets that have appreciated most in value can be among the most tax-advantaged items to contribute to charity. They enable the donor to potentially eliminate capital gains tax liability on the sale of the asset, enjoy a current year tax deduction, if the donor itemizes, while allowing the charities they support to receive the most money possible.

Many executives and entrepreneurs find that their most appreciated assets come in the form of non-cash assets (privately held C- and S-Corp stock, limited partnerships or LLC interests), often with a low cost basis and significant current market value, resulting in large capital gains taxes when sold. By donating a portion of these highly appreciated privately held business interests to a public charity (including a donor-advised fund account), they can potentially eliminate capital gains tax liability on the sale and take a full, fair market value income tax deduction, if they itemize. Contributions of similar assets to a private foundation would generally be deductible, for those who itemize, at the lower of cost basis or market value. Such interests are generally appropriate to give to charity when a sale, exchange or buyback program will enable the charity to convert the illiquid interest into cash.

Considerations include:

- If a sale is expected, the terms of the sale should still be under negotiation. The documentation must not have proceeded to the point at which the IRS would consider it a prearranged sale. That could result in the donor bearing the tax liability for any gain on the sale.

- Contributions of privately held stock to a public charity or donor-advised fund account are generally deductible, for those who itemize, at fair market value on the date of contribution—as determined by a qualified appraisal—whereas such contributions to a private foundation are generally deductible at the lower of cost basis or market value.

- The company's shareholder agreements and other governing documents must be reviewed to understand transfer restrictions, timing and process to complete the charitable transfer.

- For gifts of privately held stock >$10,000 or LP/LLC interests >$5,000, donors must obtain a qualified appraisal of the shares to substantiate the charitable deduction claimed, for those who itemize. Appraisals must be obtained no earlier than 60 days before the date of donation and no later than the due date of the donor's tax return (including extensions) for the year of the gift. Appraisals depend on the facts and circumstances at the time of contribution and may be discounted for lack of marketability and/or lack of control.

- Gifts of indebted interests may trigger negative tax consequences for donors and recipients, including donor tax liability and a reduced charitable deduction, for those who itemize. In addition, the deduction for gifts of S-Corp, LP and LLC interests must be reduced by the amount of ordinary income that would have been realized if the donor had sold the interest at fair market value on the date contributed. Please consult with a tax advisor prior to donating interests in privately held businesses.

- For S-Corp shares: The charity or donor-advised fund account will generally be subject to unrelated business income tax (UBIT) on its gain from the sale of the shares and on its share of any income generated by the S-Corp during the charity's ownership of the shares. The charity or donor-advised fund provider may use the proceeds of the sale to pay these taxes, and may escrow a portion of the proceeds in a separate account for three years to match the IRS "look back" period, during which the IRS can challenge the cost basis of the shares and the taxes paid.

Case Study

An executive at a privately held company would like to convert some of her concentrated holding in long-held, highly appreciated shares of the company into cash to fund her philanthropic activities. Her company has a buyback program in place for shares donated to charity. She is a board member of several nonprofit organizations sponsoring programs for disadvantaged youth and these organizations are not able to accept non-cash contributions. She wishes to minimize taxes in order to maximize her gifts to charity.

	Tender stock to the company and donate proceeds to charity	Donate stock directly to charity
Asset Value	$1,000,000	$1,000,000
Capital Gains (100% Long-Term)	$950,000	$950,000
Taxes Paid*	$226,100	$ -
Gift to Charity	$773,900	$1,000,000
Charitable Deduction (for those who itemize)†	$773,900	$900,000
Donor Tax Savings	$286,343§	$333,000

The executive decides to establish a donor-advised fund account and to fund the account with shares of the company stock. The donor-advised fund takes ownership of the shares and tenders them back to the company as part of the charitable buyback program. The transaction closes within a week, and the executive begins to recommend investments and grants to charities of her choice. She itemizes and claims a fair market value deduction (as determined by a qualified appraisal).

Learn More

For more information about the advantages of contributing privately held business interests to charity and for a detailed consultation about your specific situation, please call us at 800-746-6216 or visit us at www.schwabcharitable.org.

Gifts of appreciated private equity can involve complicated tax analysis and advanced planning. The above article is meant only to be a general overview of some of the considerations and is not intended to provide tax or legal guidance. If you would like to consider a donation, please consult with your tax advisor.

* Hypothetical case study, for illustrative purposes only. Assumes cost basis of $50,000, that the investment has been held for more than a year and that all realized gains are subject to the 20% federal long-term capital gains tax rate plus the 3.8% Medicare net investment income surtax. Does not take into account any state or local taxes. Assumes no indebtedness associated with the gifted interest.

† Gifts to charity of private equity fund interests are typically deductible, for those who itemize, at fair market value, as determined by a qualified appraisal for donated interests with a value exceeding $5,000. Such valuations may be subject to discounts or premia depending on the current market for the interests and projected cash flow. Such discounts/premia vary widely. A 10% discount was assumed for this example. The example assumes there are no liabilities associated with the interests. The example assumes full deductibility, for those who itemize, (gifts to a public charity [including donor-advised funds] of property held for more than one year are generally limited to 30% of AGI with a 5-year carryover of unused amount).

§ Capital gains tax taken into account by using the after-tax value of the gift

Schwab Charitable is the name used for the combined programs and services of Schwab Charitable Fund™, an independent nonprofit organization. The Schwab Charitable Fund has entered into service agreements with certain affiliates of The Charles Schwab Corporation.

©2018 Schwab Charitable. All rights reserved. REF (0518-831J) MKT83112-03 (5/18) 00212114