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Strengthening Communities Through Legal Services

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Legal Alert: A Guide to Acknowledging Donations

Hopefully your nonprofit organization has been lucky enough to receive some charitable contributions during the end-of-the-year giving season, whether those contributions were in the form of cash, goods, or volunteer hours. If so, that is great! But it is also important that your organization follow the IRS guidelines for the proper acknowledgment and recording of those donations. This short guide will address the acknowledgment requirements for donated cash, goods, and services to your nonprofit organization.

When is Documentation of a Donation Required?

Usually, the donor bears the responsibility for acquiring the proper documentation to claim tax deductions. However, it is a good practice to always provide donors with acknowledgment documentation for two reasons. First, this covers the organization in the few situations where documentation from the organization is actually required by the IRS. Second, donors expect a "thank you" from the organization, so prompt follow up with donation documentation can help build better donor relationships.

Cash Donations

A donor must have a contemporaneous written acknowledgment from the organization in order to deduct any single contribution over $250. The organization can help the donor by providing a written statement acknowledging the donation. In order for the acknowledgement to be "contemporaneous," the donor must receive it by (i) the date the donor files his or tax return, or (ii) the due date of the donor's tax return, whichever is earlier. The organization should include the following information in the acknowledgement:

a. The name of the organization,

b. The date of the contribution, and

c. The amount of the cash contribution, or a description of the non-cash contribution.

When a donor contributes more than $75 and receives goods or services from the organization in return, it is considered a "quid pro quo contribution." These types of contributions *must* be acknowledged in writing by the organization. For example, if a donor contributes $100 and receives a charity dinner valued at $40, the organization is obligated to provide the donor with a written acknowledgment. The acknowledgement should be provided either at the time of the solicitation or when the contribution is received. These written acknowledgments should include (a) through (c) listed above, in addition to:

1. A statement informing the donor that the deductible amount is limited to the amount of the contribution *beyond* the value of the goods or services received, and

2. A good faith estimate of the fair market value of the goods or services received. (For more information on estimating the fair market value, see the following section)

Note, however, that there is an exception to the quid pro quo contribution acknowledgment requirement for token items provided by the organization. An example token item would be a mug or calendar given to a donor. In this scenario, the organization is not required to describe or value the token item in the acknowledgement. For more specifics on what qualifies at a token item, see IRS Publication 1771.

Valuing Non-Cash Donations

It is easy to know the value of a cash donation, but things can get more complicated when donors give other types of goods to a charitable organization, or when the organization needs to determine the value of goods or services provided to a donor. Generally, the donor is allowed to deduct the fair market value (FMV) of donated goods. The FMV is the value that the property would sell for on the open market. The IRS highlights three important factors that can be used to determine an item's FMV:

1. The Cost or Selling Price

The cost to the donor can be used to determine the FMV if the item was purchased near the time of the donation in an arms-length transaction. The further back in time the item was purchased, the less likely the purchase price will accurately reflect the item's current value. Also, if the organization sells the item soon after the donation was received, the sale price can be used to identify the FMV at the time of the donation.

2. Comparable Sales

The sale of a similar piece of property can help determine the value of the donated property. Factors in determining a comparable sale include the degree of similarly between the two pieces of property, the time of the sale, the market conditions, and the circumstances of the sale (e.g., whether it was an arm's length transaction). The FMV also must take into account any restrictions on the use of the property. For example, if donated land is restricted for residential use, the FMV must reflect its value as residential property, even if the land would have a higher value if converted to commercial use.

3. Replacement Cost

The cost to replace the donated item by either buying or building property similar to the donated item can be used to help value the property. However, there must be a reasonable relationship between the replacement cost and the FMV for this factor to be included. For example, if the supply of the donated property is more or less than the demand for the property, the replacement cost will likely be a poor reflection of the property's FMV.

Remember, even if the donor cannot deduct their non-cash donation, organizations should still record the value of the donations in their financial statements.

Donation of Services and Volunteer Time

A donor's services to a charitable organization are not deductible. For example, if an attorney volunteers to do legal work for a nonprofit organization, the attorney cannot take a deduction for the hourly value of her legal services. Therefore, the organization does not need to provide any formal written acknowledgement of donated services to the volunteer. However, volunteers can deduct out-of-pocket expenses that are directly related to serving as a volunteer, such as parking and gas expenses for transportation to the volunteer site. Additionally, even though the volunteer cannot deduct the value of their donated time, the organization still received the value of their services, and that should be reflected in the organization's own financial statements as a contribution to the organization.

Remember, the IRS does not always require documentation of a donor's gift, but it is a good idea to provide an acknowledgement for every donation that your organization receives. This ensures that your organization will be covered in the situations where there is an IRS documentation requirement, and it will help build relationships with donors and express your gratitude for their generosity. Best of luck with your fundraising in the New Year!

For more information on this topic, see the following IRS publications:

Publication 1771: Charitable Contributions, Substantiation and Disclosure Requirements: http://www.irs.gov/pub/irs-pdf/p1771.pdf

Publication 561: Determining the Value of Donated Property: http://www.irs.gov/pub/irs-pdf/p561.pdf

Publication 4302: A Charity's Guide to Vehicle Donations: http://www.irs.gov/pub/irs-pdf/p4302.pdf