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I was asked to analyze the Form 1040 for 1970 as it applies to charitable contributions and speak to you for several minutes on the subject.

After careful and minute study of the Schedule A in Form 1040 for 1970, especially as it is compared to the 1969 form, which you are all familiar with, I determined the major change in the form itself was the reduction in the number of lines on which to list in detail the recipients of contributions. They were reduced from seventeen (17) lines to eleven (11) to make room for a summary of itemized deductions on the bottom of Schedule A, which is a major step forward in the design of the form.

Even when turning to the instructions for contributions in the respective forms, they appear similar, except, that a limitation was raised from 30% to 50%. The 1970 instructions add a notation to see Publication 526 for special rules, definitions and limitations on charitable deductions and there is a run-on sentence that the deduction for contributions of long-term capital gain property generally may not exceed 30 percent of line 18 Form 1040.

Thus, we must go much further to see how the Tax Reform Act of 1969 has changed the substantive rules of reporting and deducting charitable donations.

One major liberalization was to raise the contribution limitation from 30% to 50%. At the same time, Congress is phasing out the unlimited deduction rule. None of my clients are included in the hundred or so U.S. taxpayers who took advantages of the unlimited deduction, however, for those of you who are fortunate to have a client like that, who I am sure reduced his taxable income by paying substantial fees for tax advice, note, that the decrease in unlimited contribution deduction is being accomplished by a transitional percentage phase out starting in 1970 and ending in 1974, when all men will be equal for contribution rules.

For those of you who have clients like mine, you must recognize the '69 Reform Act has limited the opportunities for combining tax saving with Philanthropy. Congress has attempted to plug some of the so-called loopholes in making a profit from charitable giving.

It is no longer possible to get a tax break by contributing property which would have resulted in some ordinary income or short-term capital gain had the donor sold the property at its fair market value instead of contributing it. This would affect contributions of:

a. inventory or stock in trade
b. capital assets held six (6) months or less
c. Section 306 "bail out" stock
d. art objects, literary or music works produced by the taxpayer, and letters, memoranda and similar property produced by or for the taxpayer, which, by another change of the Reform Act are now non-capital assets
e. Property subject to recapture of depreciation or the new recapture farm loss or farm development expenditure deductions to the extent of the recapturable part

All the donor can deduct in 1970, and thereafter, is the fair market value of the property, less the amount which would be ordinary income, if the property had been sold. In other words, the taxpayer generally can deduct only his basis for the property.

For example, a donor who contributes $2,000 worth of inventory which cost $1,200 would have the deduction limited to $1,200. This is the value of the inventory at $2,000 less the ordinary income appreciation $800. And if the taxpayer had a zero basis for the property, as is the case with a farmer using a cash basis for crops produced or a businessman who had expensed office supplies, no deduction is allowable.

While the potential ordinary income or short-term gain doesn't give the donor a tax saving contribution deduction, the profit isn't taxed to him either.

The deductible amount may differ from the basis, if the appreciation is partly ordinary income and partly long-term capital gain. Then the amount deemed contributed is the fair market value of the property, reduced by the part that would be treated as ordinary income on the sale.

For example, if the donor held depreciable property for more than six months, and contributed it when it was worth $10,000, had a cost basis of $8,000 on which $3,000 recapturable depreciation had been taken, the deduction would be $7,000. That is, the $10,000 fair market value minus the $3,000 ordinary income recapture element. If the recapturable depreciation had been $1,000 then the deduction would have been $9,000. That is, the $10,000 fair market value minus the $1,000 ordinary recapture element. Note that the acquisition basis of $8,000 doesn't enter into the computation.

Contributions of appreciated property, whose sale would not result in any ordinary income, continue to enjoy the same tax benefits as before the Tax Reform Act. There is a full deduction for the appreciation, with no tax on the increased value. However, two new exceptions were added to the Code.

1. Contributed tangible personal property which is unrelated to the charity's exempt function, such as art which the charity doesn't need and will sell.
2. Contributed capital assets of any kind, including stocks, property or art, given to certain types of private charitable foundations.

In these cases, an individual's deduction for the contribution, is the fair market value, less 50% of the long-term capital gain appreciation. For a corporate donor, the fair market value is reduced by 62½% of the appreciation to arrive at the deductible amount.

For tangible personal property which would give rise partially to ordinary income recapture and partially to long-term capital gain, the contribution deduction is the fair market value reduced by the full amount of the ordinary income recapture portion and reduced by 50% of the long-term capital gain portion. This same rule applies to all capital assets given to a private foundation, which is not a private operating foundation or community foundation and which does not, within 2½ months after the close of the year in which it receives the gift, make qualifying distributions equal to the amount of contribution.

Bargain sales have lost most of their appeal, since it is no longer possible, to avoid gain by selling appreciated property to a charity at cost. The sale is now treated as if part of the property was sold for the fair market value and the rest was given to charity with the donor's cost allocated between these two parts. The net effect is the same as if the donor had made a taxable sale of part of the property, and then contributed the proceeds from this sale, plus the rest of the property to the charity.

The seller's basis for measuring gain, is that portion of the actual basis, which the bargain selling price bears to the fair market value of the property.

For example, a taxpayer owning long-term capital stock worth $2,700 with a basis of $1,800 sells the stock to a charity for $1,800. The taxpayer would have a $900 charitable deduction and have to pick up $600 long-term capital gain.

The donor's basis for the part sold is $1,200 ($1,800 Selling Price/ $2,700 FMV x $1,800 Basis); the long-term capital gain is computed by deducting the $1,200 basis from the $1,800 selling price to arrive at the $600 profit.

Remember, if the stock had been held for six (6) months or less and sold for the donor's basis, no deduction is allowable and no tax is imposed on the appreciation.

You can see that greater care must now be exercised in selecting the property to be donated and in selecting the donee charity.

Where appreciated property is involved, long-term property should be selected. There is no longer any tax advantage in contributing crops or inventory instead of cash. The rules impose the same treatment had the inventory been sold and the proceeds donated.

It may be advisable to hold on to short-term property and donate it after the property has achieved long-term status.

In planning a gift of a capital asset, which is appreciated tangible personal property held more than six (6) months, the donor must select a "suitable" donee. For example, give a painting to a museum for display rather than to a church for resale.

The amount deductible for donating a painting to a hospital, may depend on whether they are going to add it to their art collection for display or resell it. Also, IRS's interpretation whether the display of art in a hospital is in accordance with their exempt function is a question still to be determined.

In my opening remarks, I alluded to the increase in charitable deduction ceiling for those few individuals who contribute more than 30% of their income to charity. For 1970, and thereafter, with certain exceptions, an individual may deduct up to 50% of his "contribution base." This is a new tax term added by the Reform Act for an old concept. "Contribution base" is the adjusted gross income computed without deduction for any net operating loss carryback.

The new 50% deduction limitation, applies to contributions which previously qualified for the former 30% limitation and is expanded to include so-called community foundations and certain private foundations.

The former 20% limitation continues for contributions to other organizations such as war veterans' groups and most private foundations.

An exception to the rule of raising the former 30% limitation to 50% arises when appreciated long-term capital gain property is donated. Here, the 30% ceiling continues, unless a special election is made.

If an individual's 50% charities exceed 50% of his contribution base, they may be carried over and deducted in the five (5) succeeding years. An excess contribution from 1969, or before which is carried over to 1970, or after, is deductible up to 50% of the contribution base in the year which it is carried. This is true even if the pre-1970 contribution was a gift of appreciated long-term capital gain property.

Property contributions in 1970, and after which are subject to the 30% ceiling, may be carried over and deducted in the five (5) succeeding years, but again subject to the 30% limitation.

When a taxpayer makes gifts qualifying for the 50% limitation and also gifts of appreciated property subject to the 30% limitation, gifts qualifying for the full 50% ceiling are counted first in determining whether contributions exceed 50% of contribution base. Donations of appreciated property subject to the 30% limitation are then counted only to the extent that they don't exceed 30% of contribution base and also when added to the 50% deduction, don't exceed 50% of contribution base. Gifts in excess of these ceilings are carried over. Contributions subject to the 20% limitation are counted only after the 50% and 30% gifts are accounted for. There is no carryover, however, for any unused portion of 20% charities.

For example, a taxpayer has a contribution base of $100,000. He contributes $15,000 in cash and $40,000 in appreciated long-term capital gain property to 50% charities and $10,000 to 20% charities. The maximum deduction is $50,000 (50% of his contribution base). The $15,000 cash to the 50% charity is deductible, only $30,000 of the $40,000 appreciated property is deductible with $10,000 carried over, and $5,000 of the $10,000 given to 20% charities is deductible with no carryover for the remaining $5,000.

Throughout the Internal Revenue Code we have exceptions to exceptions. The Reform Act added another one, in permitting a donor of capital gain property, otherwise subject to the 30% ceiling to elect the 50% ceiling, if he is willing to reduce the amount of his contribution by one-half of the appreciation.

It usually will not pay to make this election, unless the appreciation is nominal or a maximum immediate deduction is needed. The election, if made, applies to all contributions of capital gain property made during the taxable year.

Up to this point I have covered about one-half of the charitable contribution changes made by the Reform Act. Another afternoon seminar can be programmed for the second half.

Briefly, deductions have been narrowed and even eliminated for gifts of future interests and present income interest. The old two (2) year charitable trust has been repealed and is now part of history. Deductions for gifts with charitble remainders in trust have been narrowed and stricter valuation rules instituted. Deductions of less than the taxpayers' entire interest in property have been eliminated subject to important exceptions, such as the right to live in a residence that had been contributed to a charity. The deduction for the value of a charity's use of property is specifically denied.

There have been few areas that have been left unscathed by the scalpel of the Reform Act.

Deductions for contributions of property which have not appreciated in value and contributions of pure unadulterated cash are unchanged by the New Law except for new ceiling limitations.

The net revenue increase because of all these charitable deduction changes has been estimated as low as five million dollars. My sympathy goes out to you, the tax practitioner, who has to implement this law in the next few months.