



GIANT, IMPORTANT DISCLAIMER: WE AREN'T GIVING LEGAL, TAX OR FINANCIAL ADVICE. PLEASE SEEK YOUR OWN COUNSEL FOR ANY DONATIONS. MANY OF THESE QUESTIONS ARE OPEN TO SOME INTERPRETATION, ARE GENERAL IN NATURE OR ARE UNIQUE TO A PARTICULAR JURISDICTION. ASSUME ALL ANSWERS ARE WRONG UNTIL YOU/YOUR DONOR CONFIRMS WITH HER/HIS ADVISOR.

**Q & A from “DEBT: The Four Letter Word of Noncash Transactions”
<Mar, 2024>**

<p>Do you serve as Trustee for CRTs across the country?</p>	<p>Yes, we can cover every state. Dechomai Foundation is the trustee and then the remainder comes into a shell DAF and then 30 days later is granted out. Paul on our team leads this area with Gary Snerson. We tend to work best if the donor doesn't want to self-trustee (or shouldn't, or it was a good fit when the donor was 68 but not at 88), and/or for non-cash assets, or for charities who don't want to serve as trustee or when the minimum levels are too high with a financial institution (our minimum is \$500K).</p>
<p>We received business interests in an estate whereby the partner / owner did a ReFi for commercial property improvements, and while this generated additional income to us besides the actual value of the business interests received, our tax counsel advised us that we did benefit from the rule of not owing UBTI since the gift was received from an estate, and not intervivos ... first we learned of the provision and thankfully we were not exposed to UBTI although our internal counsel prepared a small holdback "just in case" of exposure. Thankfully, more gift went to the ministry's use so the ReFi of the LLC manager was a smart move we benefitted from "going along with" as his silent partner.</p>	<p>This is a great example, and a good way to show how the bequest path is one way to “solve” some of the issues associated with debt-financed property donations.</p>

<p>Do you use your cash to pay off debt at the closing of the donation deed transfer? Wouldn't that simplify the nonprofit's UBIT issues?</p>	<p>Generally, we don't pay off debt at closing of the gift. In some cases, we would consider doing so, but would treat it as a loan to the donor's DAF account (since we'd be fronting the cash). It would simplify the UBIT picture. And of course, the debt will be paid off at closing on the <u>sale</u> of the donated property in nearly every case.</p>
<p>Can you give an example of how debt held by an LLC would affect the charity and donor when LLC interest in donated?</p>	<p>Covered in the presentation (this question came in early) but generally the debt flows through on the K-1 so a similar bargain sale and acquisition indebtedness analysis occurs.</p>
<p>Please clarify what Ryan said - is the income that is 100% taxed, referring to the acquisition indebtedness that's counted as income? Or is the sample property an income-producing property, like a rental?</p>	<p>When average acquisition indebtedness exceeds basis, it "taints" 100% of the realized income from the donated property as taxable, whether that is rental income or capital gains from sale.</p>
<p>Average acquisition indebtedness is the amount of outstanding principal indebtedness during that portion of the year the property is held. It is computed by determining the principal indebtedness of the property for the first day in each calendar month it existed and averaging all the sums.</p>	<p>Note that this viewer comment clarifies exactly how average acquisition indebtedness is calculated.</p>
<p>Would we be able to turn to you on these two types of deal killers? :-)</p>	<p>No - and even though we primarily get referrals for 100 mph curveballs with grease and mustard on them... we are VERY open to referrals that are slow fastballs down the middle. :-) It is baseball season hence the incredibly timely metaphor!</p>
<p>Does Charitable Solutions ever use "spare cash" to eliminate debt on a property going into a CRT per your discussion just a moment ago?</p>	<p>Great question... and generally, yes. Through Dechomai, we can buy down the proportional debt in exchange for proportional ownership. We must pull those funds from our operating reserve/endowment, so we require a 1% per month return for the cash invested/fronted (minimum 6% or it just isn't worth the maneuver). We do this about once a year, not often but can work well if trying to fund a CRT.</p>



<p>We have asked donor to pay off or segregate the debt to a separate LLC from the transferring LLC of the gift. That works well when the donor truly cares to not have the charity encounter debt unnecessarily. A donor with clear charitable intent will mitigate or remove the debt.</p>	<p>This is a great solution. It is not always possible unfortunately, even when the donor is willing. Debt may not be easily movable. But it is almost always worth asking the donor if they can just do this to clear the debt from the donated asset.</p>
<p>What if the donor splits the property into 2 parcel and asks the lender to allocate the remaining debt to only one parcel? Donor keeps that parcel. The donor then gives the other parcel (without the debt) to the CRT.</p>	<p>This would work, but would create significantly more complexity during the gift planning phase, since the splitting of the property will take some work. And then when the charity goes to sell, title will need to see this split clearly.</p>
<p>Will the slides be shared to registrants after the presentation?</p>	<p>Sort of - we don't typically send out the slide deck (past attribution issues). BUT we will send a link to a recording of this webinar, which will have the slides. That will go out to all attendees probably next week.</p>
<p>If there is UBTI, all of the income (rental payments, sale proceeds) is subject to tax, not just a portion, yes? In other words, the taxable income is not prorated based on the ratio of debt to equity. Correct?</p>	<p>It depends on the ratio of average acquisition indebtedness to basis. If debt exceeds basis, then this is correct. Otherwise, it would be pro-rata.</p>
<p>So Ryan if a charity holds an asset for 1 month - the average acquist indebt calc needs to be figured for the entire year, yes</p>	<p>It should only need to be calculated for that 1-month holding period.</p>
<p>What about a gift and sale in which the donor's debt is paid off in escrow from the proceeds of the sale</p>	<p>That won't matter unfortunately - if the charity receives it with debt, all these issues are triggered. Paying it off through escrow won't absolve those issues.</p>
<p>So if the charity decides to accept it, then holding period is critical for the charity.</p>	<p>Yes - one of the most important factors when the charity is evaluating! A clear pathway to sale is vital.</p>

<p>What if the donor pays off the debt prior to donation - is there a look back or is this a good strategy?</p>	<p>If there is no debt on the property on the day of the gift, no problem, no lookback.</p>
<p>Thank you. The gift is limited to the equity in the property and basis prorated to the sale portion?</p>	<p>Yes - basis is allocated between the gift and sale portions, and the donor recognizes gain only to the extent the debt exceeds the pro-rata basis.</p>
<p>If a donor bequeaths an apartment building (with rental income) that is worth \$6M (0 cost basis) but has about \$3M in debt, how is the donor's charitable estate tax deduction determined?</p>	<p>The net value is three, but because this transaction is occurring at death, basis is the full six. Also, the charity will not have a UBTI problem for ten years. Not a bad result!</p>
<p>From the charity perspective - is it possible to be gifted a partnership with debt that isn't considered acquisition indebtedness - so no UBIT issue</p>	<p>None that I have ever seen unless there is some kind of C-corp blocker which creates other issues that Ryan mentioned.</p>
<p>What triggers a call to Charitable Gift Solutions? When we decline a gift?</p>	<p>Basically yes, if the charity is going to decline or you are holding your nose or biting your lip, you can call too. This is for any noncash, CGA, CRT or potentially estate gift situation. We basically function like a "floating" foundation behind your foundation where a charity can hub and spoke into us on a case-by-case basis.</p>
<p>And for UBIT, how many states!</p>	<p>Any state that has an income tax and in which UBTI is sourced, yes this is a problem.</p>
<p>If a charity converts private residence into rental, are they free of the UBTI issue for up to ten years, or did it have to be income producing at death?</p>	<p>Assuming this means a private residence with debt, received via bequest – it should be exempt for ten years. That is, unless the charity “pay[s] the indebtedness secured by the mortgage, or if the organization makes any payment for the equity in the property owned by the decedent or the donor.”</p>