Quick Take- Charitable Deduction Abuses

Friday, October 20, 2023

Take-Away: The IRS and victimized investors are aggressively pursuing charitable income tax deduction promoters.

Background: It was a bad week for those who promote aggressive charitable donation schemes in order for their investors to claim excessive charitable income tax deductions.

Artwork: In IR-2023-1585 issued on October 5, 2023 the IRS warned taxpayers about promotions that involve exaggerated artwork deductions that target high-income individuals. While there is nothing inherently wrong with the donation of artwork, apparently some promoters in their solicitations are promising inflated art values, thus leading to even larger charitable deductions when the artwork is given to charity. Apparently the promoter encourages a wealthy individual to purchase the art, wait to donate the art, and then take a large tax deduction for the artwork that is donated to charity. The promoter encourages that high-income individual to purchase various types of artwork at a 'discounted price.' The price includes the 'additional services' of the promoter for storage, shipping, arranging appraisals, and the donation of the artwork to identified charities. The promoter tells the purchaser that the artwork is worth significantly more than its purchase price (which price reflects the promoter's additional services.) The scheme encourages the purchaser to donate the artwork after waiting at least one year and then claim an income tax charitable deduction for that inflated fair market value, which is significantly higher than what was initially paid for the artwork. The promoter's scheme encourages the individual purchaser to donate artwork annually and allows/facilitates the individual to purchase a quantity of artwork that guarantees a specific deductible dollar amount. The IRS now has multiple audits of the donation of artwork in progress searching for promotional abuses. In the release that accompanied IR-2023-1585 IRS Commissioner Werfel stated: *"Creativity in art is a beautiful thing, but aggressive creativity in art donation can paint a bad picture for people pulled into* *these schemes. This is another example where people should be careful when it comes to aggressive marketing and promotions."*

Syndicated Charitable Conservation Easements: In a federal District Court in Atlanta, the Department of Justice obtained jury trial verdicts against two promoters for conspiracy to defraud the United States, conspiracy to commit wire fraud, aiding and assisting the filing of false tax returns, and subscribing to false tax returns. One promoter was also convicted of money laundering. The promoters had marketed and sold to high-income individuals abusive syndicated conservation easement tax shelters based on fraudulently inflated charitable contribution tax deductions, promising the investors deductions 4.5 times the amount the individual's had paid for their interest in the conservation easement investment. Over $1.3 billion in income tax charitable deductions had been claimed by the investors in this fraudulent scheme. As for other 'players' in the syndication scheme, its appraiser had pled guilty, and its accountant pled guilty and testified for the government.

Real Estate Sales: In *American Properties, Co. G.P. v. The Welfont Group, LLC, et.al,* an investor, who is currently being audited by the IRS, filed the lawsuit against the promoters. The investor claims that it had been sold real property for below market value based on the promoters' false representation that the investor would receive a substantial income tax charitable deduction with its purchase. The investor's claim is that the grounds for the claimed charitable income tax deduction was to have been a purported *qualified appraisal* of $4,755,000 for the real estate that would be issued in connection with the investor's subsequent sale of that real property to a charity for $2,160,000. In its audit the IRS determined that a *qualified appraisal* was not used and that under any conditions it undermined the deduction because the charity was an *alter ego* of one of the promoters, i.e., the same promoter then immediately purchased the real property from the charity for $2,650,000. A default judgment was entered by the state trial court against the promoters who did not appear to defend the claims against them. The investors lawsuit against the promoters asserts that it was damaged to the tune of $1,321,013 with this audited scheme. However, that amount will be subject to further trial court proceedings. At the same time, the investor is appealing the IRS's adverse determination against it on audit regarding its claimed charitable income tax deduction from the sale of the real property to the charity.

Conclusion: If the promoter's promised charitable income tax deduction is too good to be true, it is too good to be true.