

AUGUST 9, 2012

IRS Issues Guidance on the Deductibility of Donations to LLC Subsidiaries of Section 501(c)(3) Organizations

The past week saw the publication of guidance from the IRS that the charitable sector has been awaiting for eleven years: under **Notice 2012-52**, *donors to a limited liability company (LLC) wholly owned by a Section 501(c)(3) organization can claim a charitable deduction under Section 170. The notice is effective for contributions made on or after July 31, 2012.*

*Notice 2012-52 comes thirteen years after the IRS first clarified, in 1999, that the activities of a single-member LLC owned by a Section 501(c)(3) organization would be attributed directly to the parent. Two years later, the IRS mentioned in its **2001 Exempt Organizations CPE Text** that it was considering whether donations to these LLCs were eligible for a charitable deduction. Until last week, however, there had been no further word on this item, even though two years ago the IRS **indicated** that a grant to one of these LLCs would be treated as having been made directly to the underlying charity itself, and the foundation would not be required to exercise expenditure responsibility. It was unclear whether the delay in concluding the Section 170 deduction issue was caused simply by bureaucratic machinery moving very slowly, or whether it reflected deeper, substantive concerns that needed to be resolved. In any event, the Tax Section of the New York State Bar Association sent a **letter** to the Treasury Department in January 2012 essentially arguing that there was no logical reason to disallow a Section 170 deduction for contributions to an LLC that was otherwise entirely disregarded for federal income tax purposes. This letter seems finally to have done the trick.*

This development should help to broaden the use of the LLC subsidiaries by charities and should also increase the attractiveness of Model L fiscal sponsorship, where a fiscal sponsor operates a charitable project with a high exposure to liability—for example, a public program that involves chaperoning children in outdoor activities—through an LLC. (See my **2011 article** introducing the Model L concept.) Until last week, the lack of clarity on whether contributions to the LLC qualified for a charitable deduction meant that project donors needed to write their checks to the fiscal sponsor, which sometimes causes confusion. Now, donors can contribute directly to the Model L project and claim a charitable deduction for it.

That said, there are still a couple of caveats for both charities and their donors. First (and more relevant to donors), Notice 2012-52 does not address the treatment of contributions for gift and estate tax purposes. Second, charities looking to set up an LLC subsidiary still need to consider whether state-level taxes and fees outweigh the benefits of using the LLC form. (For example, California charges an annual “fee”

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indexed to the LLC's income from all sources worldwide, which is not waived for LLCs wholly owned by charities.) Ultimately, though, Notice 2012-52 is likely to prove a big step forward.