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- Are Proposals by States to Recast SALT Payments as Charitable Contributions a Valid End-Run Around the New $10,000 Limitation?
  Charitable Contributions

  Richard L. Fox of Buchanan Ingersoll & Rooney P.C. analyzes whether state and local taxes in high-taxed states really can be characterized as deductible charitable contributions under federal tax law. The author discusses federal court decisions and IRS guidance and rulings that indicate merely enacting state legislation that recasts SALT payments as charitable contributions may not result in an allowable deduction for federal tax purposes and explores legislative alternatives that may accomplish such result.

  By Richard L. Fox

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  Introduction

  The $10,000 annual limitation on the deductibility of state and local tax (SALT) payments brought about by the Tax Cuts and Job Act (Tax Act) has created a firestorm of controversy and prompted high-taxed states to consider legislative proposals that would allow their residents to avoid the new limitation. One such proposal being considered by at least three states, California, New York, and New Jersey, is recasting SALT payments as charitable contributions and providing state tax credits up to the full amount of the contributions, in effect providing an end-run around the $10,000 annual deduction limitation on SALT payments that does not apply to charitable contributions.

  States are still in the process of considering sustainable approaches in this context. Legislation has already been introduced in California, SB 227, the “Protect California Taxpayers Act,” that would allow taxpayers to receive a dollar-for-dollar state tax credit for amounts they contribute to the “California

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Excellence Fund," a fund created "to accept monetary contributions for exclusively public purposes as specified under Section 170 of the Internal Revenue Code, relating to charitable, etc., contributions and gifts" for which "[a]ll amounts in the fund shall be used for those public purposes upon appropriation by the Legislature." New York Gov. Andrew M. Cuomo (D) has called for the creation of two charitable funds through which New Yorkers could contribute for the state's education and health care needs, contributions to which would be eligible for a state tax credit.

The provision of state or local tax credits to encourage charitable giving is by no means a new concept. Many states and cities across the country already have existing programs in place aimed at encouraging charitable giving to advance specified purposes, such as education or economic development, by providing tax credits to encourage donors to make charitable contributions to certain qualified organizations.

The issue that arises in this context, of course, is whether a purported charitable contribution to a state is deductible under Section 170(a) in light of the donor receiving a "quid pro quo" benefit in the form of state tax credits in return for the contribution. Although Section 170(c) makes it clear that a state is qualified to receive tax deductible contributions (but only if the contribution "is made for exclusively public purposes"), it is black letter law that when a donor makes a purported charitable contribution and receives equal fair market value in return, the transfer will be considered to lack donative intent and will therefore not be deductible under Section 170(a).

It is interesting, however, that there is legal authority supporting the position that the receipt of a state tax credit as a result of a contribution to charity does not result in a "quid pro quo transaction" for purposes of Section 170(a) and therefore should not cause an otherwise allowable charitable deduction to be reduced and recharacterized as a state tax payment. The application of this authority to legislative proposals ultimately enacted under a state law provision seeking to recast SALT payments as charitable contributions may depend upon the specific nature of the legislation, as a purported charitable contribution made in lieu of a SALT payment that is considered to lack charitable intent and not to have been made voluntarily will be characterized as the equivalent of a state tax payment for purposes of Section 170(a) and, therefore, subject to the $10,000 SALT deduction cap.

Deductibility of Charitable Contributions Made to a State

Section 170(a) allows as a deduction any "charitable contribution" as defined in Section 170(c). Section 170(c), in turn, provides that the term "charitable contribution" means a contribution or gift to or for the use certain specified entities under Section 170(c)(1) through (5). The deduction available for a contribution to a state is derived from Section 170(c)(1), which permits a deduction for a contribution made to a "State, a possession of the United States, or any political subdivision of any of the foregoing, or the United States or the District of Columbia, but only if the contribution or gift is made for exclusively public purposes." (Emphasis added.)

The "exclusively public purposes" requirement under Section 170(c)(1) is intended to ensure that a deduction is not allowed where a contribution is made for a donor to achieve a private benefit, although it has long been the position of the Internal Revenue Service that some private benefit resulting from an otherwise qualified charitable contribution will not result in disallowance of a deduction under Section 170(a) provided, however, that the private benefit is incidental in comparison to the benefit inuring to the public at large. See, e.g., Revenue Ruling 67-446 (benefit resulting to local merchants on relocation of railroad facilities was found incidental to that inuring to general public by alleviation of congestion in central shopping area and, therefore, Section 170 deduction was allowed for contributions to a city to

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effect relocation); Rev. Rul. 69-90 (Section 170 deduction allowed for contributions to a city to construct unrestricted public parking facilities in a central shopping area; benefit to individual merchants was determined to be indirect and incidental compared to those inuring to the general public).

The term “exclusively public purposes” should also be contrasted from the purposes requirement of Section 170(c)(2), which permits a deduction under Section 170(a) for a contribution made to a domestic entity organized and operated “exclusively for religious, charitable, scientific, literary, or educational purposes,” which generally includes an organization described under Section 501(c)(3). Thus, a contribution to a state for exclusively public purposes will be deductible even if it is not used for one of the purposes enumerated under Section 170(c)(2). Indeed, the courts have determined that a contribution made for “public purposes” may be utilized for different and broader uses than a contribution that is made for religious, charitable, scientific, literary, or educational purposes. This concept was specifically recognized in Continental Illinois National Bank & Trust Co. of Chicago v. United States, where the court stated:

It seems to us that the word “public” embodies a broader concept, and envisions gifts to domestic governmental bodies for purposes other than the ordinary philanthropic purposes most people associate with “charity.” Consequently, it is our opinion that the use of the word “public” shows a congressional intention to bring within the statutory exemption gifts which could be used for such standard governmental functions as the payment of salaries to policemen and firemen. We think there is a clear indication that Congress considered that many contributions which would benefit domestic municipalities are not charitable, because the exemption permits different and broader uses of a bequest than those which are exclusively for charitable purposes.

The court further recognized that many activities of government are in no sense charitable, and in fact are generally available only to paying customers. That court stated that these are “proprietary activities and include the operation of golf courses, wharves, market places, transportation facilities, and such public utilities as gas, water, and electric systems. It is a meaningful distinction to say that while these activities are not ‘charitable,’ they nevertheless are for public purposes, as the local government conceives the needs of its public.”

Meaning of a Charitable Contribution Under Section 170

Not every payment to a qualified organization under Section 170(c), which includes a state or local government, constitutes a charitable contribution for income tax purposes. See, e.g., Murphy v. Commissioner; Estate of Wood v. Commissioner. In order to be considered a “charitable contribution,” a transfer of cash or property must constitute a “contribution or gift” within the meaning of Section 170(c). The requirement that a payment to charity be a “contribution or gift” is “intended to differentiate between unrequited payments to qualified recipients and payments made to such recipients in return for goods and services.” Hernandez v. Commissioner. See also United States v. American Bar Endowment.

Under the case law that has developed, a transfer of cash or property will be considered a “contribution or gift” under Section 170(c) where it is made (1) with a donative intent; (2) voluntarily; and (3) without the receipt of full and adequate consideration. See, e.g., American Bar Endowment. ([T]he “sine qua non of a charitable contribution is a transfer of money or property without adequate consideration. The taxpayer, therefore, must at a minimum demonstrate that he purposely contributed money or property in excess of the value of any benefit he received in return”); DeJong v. Commissioner (“A gift is generally defined as a voluntary transfer of property by the owner to another without consideration thereof”); Rev. Rul. 71-112 (“A gift is generally defined as a voluntary transfer of property by its owner to another with donative intent

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and without consideration"). Thus, where a taxpayer makes a transfer to a charitable organization in return for full and adequate consideration, or where the transfer is not voluntary or is motivated by reasons other than a donative intent, an income tax charitable contribution deduction will not be available.

Donative Intent Generally

A taxpayer must have a donative intent in order for a transfer to a qualified charity to constitute a contribution or gift for purposes of Section 170(c). Where the transfer to a charitable organization lacks donative intent, but is impelled primarily by some expected benefit to the donor beyond the mere satisfaction that flows from the performance of a generous act, it is not considered a contribution or gift. Commissioner v. Duberstein; DeJong; Singer Co. v. United States; Grinslade v. Commissioner. Therefore, no charitable deduction is allowable where the donor has an expectation of receiving some substantial benefit by virtue of making a transfer to charity, even though the expectation is not supported by an enforceable contractual claim or the benefit is not received directly from the charity. Singer Co.; Marquis v. Commissioner (there can be an expectation of a benefit even in the absence of an enforceable contractual quid pro quo).

The historical test for "donative intent" requires that the transfer be an expression of a "detached and disinterested generosity." This test was originally formulated by the U.S. Supreme Court in the Duberstein case, involving the issue of whether a purported gift of a Cadillac from one business associate to another was a nontaxable gift or taxable compensation. The taxpayer received the Cadillac from a business associate with whom he had occasional business dealings. After a number of dealings, the business associate insisted that the taxpayer accept the car as a gift. The donor treated the cost of the gift as a business expense, but the taxpayer did not report its value as income, viewing it as a nontaxable gift. The IRS asserted a tax deficiency based on the taxpayer's failure to report the value of the car as income. The Tax Court and later the Supreme Court, agreed with the position of the IRS that the value of the car was taxable compensation.

In reaching its conclusion, the Supreme Court placed great reliance on the Tax Court's factual finding that the gift was not motivated by "detached and disinterested generosity," stating that "it was at bottom a recompense for Duberstein's past services, or an inducement for him to be of further service in the future." The fact that there was no specific legal obligation to make the transfer of the car was irrelevant, as the test of whether a gift occurred was based upon the motivation of the taxpayer in making the transfer.

Although Duberstein was not a charitable deduction case, the principle of "detached and disinterested generosity" has been applied in determining whether a transfer to a qualified charitable organization constitutes a contribution or gift for income tax purposes. In DeJong, for example, the court stated that the "detached and disinterested generosity" test "is clearly applicable to a charitable deduction under §170." In that case, the taxpayer sought to deduct payments made to an educational organization where his children attended school. Although the payments were not legally required and could otherwise, therefore, be considered voluntary, the parents of students at the school were expected to contribute towards the costs of the schooling and, in return for such payments, anticipated that their children would receive an education. In such a case, the payments did not meet the detached and disinterested generosity test and a charitable contribution deduction was not allowable. See McLennan v. United States; Skripak v. Commissioner; Allen v. Commissioner. See also Chief Counsel Advice 200435001.

"Quid pro Quo" Test as Measure of Donative Intent

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Under the Duberstein "detached and disinterested generosity" test, the most critical consideration is the transferor's intention. In lieu of the Duberstein test, which focuses on motive alone, courts have more recently tended to focus on an objective standard by applying a "quid pro quo" test. See Neher v. Commissioner (quoting the court in Haak v. United States, where the court stated: "More recently … courts have tended to reject the 'pure' Duberstein test focusing on motive alone in favor of a 'fundamental objective' or 'quid pro quo' test"), although these tests are somewhat related.

Under the quid pro quo test, a transfer to a charitable organization will be considered to lack a donative intent and, therefore, not be considered a gift or contribution, where the transferor receives or expects to receive a financial return commensurate with the value transferred to the charity. Thus, "[w]hen a donation is made with an expectation of receiving something in return as a quid pro quo for the transfer, no charitable contribution is allowed," even where there is no legally enforceable right to receive any quid pro quo. Transamerica Corp. v. United States; Neher; Haak ("Thus, where a transfer is made to a charitable organization with the expectation of receiving a specific tangible benefit in return, there should be no deduction under section 170"); Rev. Rul. 86-63 ("A contribution for purposes of section 170 of the Code is a voluntary transfer of money or property that is made with no expectation of procuring financial benefit commensurate with the amount of the transfer. See section 1.170A-1(c)(5) of the Income Tax Regulations and H.R. Rep. No. 1337, 83d Con., 2d Sess. A44 (1954)").

In ascertaining whether a given payment is made with the expectation of a quid pro quo, the courts have examined the external features of the transaction in question, rather than examining the transferor's subjective intention. See, e.g., Singer Co.; American Bar Endowment; Hernandez. This practice has the advantage of obviating the need for the IRS to conduct imprecise inquiries into the motivations of individual taxpayers, given that the focus of the quid pro quo test is not on the taxpayer's motivation. Instead, the test is based upon an objective examination, on the basis of all of the surrounding facts and circumstances, as to whether the transfer to charity is being made by the donor in exchange for a commensurate benefit.

The quid pro quo approach was specifically approved by the Supreme Court in Hernandez ("In ascertaining whether a given payment was made 'with the expectation of any quid pro quo,'… the IRS has customarily examined the external features of the transaction in question. This practice has the advantage of obviating the need for the IRS to conduct imprecise inquiries into the motivations of the taxpayers. The lower courts have generally embraced this structural analysis").

The use of the "quid pro quo" test has been utilized in a variety of cases. In Ottawa Silica Co. v. United States, for example, Ottawa Silica had acquired a large parcel of rural land. It retained a consultant to draft a development plan. The consultant's plan called for long-range development with the eventual use of the land for residential housing. Shortly after the plan became final, but before any development had taken place, the company was approached by the local school board about donating a site for a new high school. After substantial negotiations, the company agreed, transferred the property, and claimed a charitable deduction for the value of the land. In reviewing the transaction, the court determined, based on the surrounding facts and circumstances, that the taxpayer anticipated receiving a substantial benefit in return for the transfer, namely, faster development of surrounding acreage and additional access roads, and was therefore not entitled to a charitable deduction.

Dual Character Payments: Transfer in Return for Less Than Full and Adequate Consideration

The courts, as well as the IRS, have recognized that a payment to a charity may have a "dual character" as part contribution and part payment for goods or services. See e.g., Rev. Rul. 68-432 (noting possibility

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that payment to charitable organization may have "dual character"); Rev. Rul. 67-246 (price of ticket to charity ball deductible to extent it exceeds market value of admission); see also HR Rep. No. 103-111, at 785 (1993) (a charitable deduction is limited to the amount exceeding the value of the consideration received). In Rev. Rul. 67-246, the IRS established a two-part test for determining when part of a "dual character payment" is deductible, which was subsequently approved by the Supreme Court in American Bar Endowment. First, the payment is deductible only if and to the extent it exceeds the fair market value of the benefit received. Second, the excess payment must be "made with the intention of making a gift." Treasury Regulations Section 1.170A-1(h)(1) adopts a consistent approach, whereby no part of a payment that a taxpayer makes to a charitable organization that is in consideration for goods or services is a contribution or gift within the meaning of Section 170 unless the taxpayer:

• Intends to make a payment in an amount that exceeds the fair market value of the goods or services, and

• Makes a payment in an amount that exceeds the fair market value of the goods or services.

In determining the portion of a contribution to a charitable organization that constitutes a charitable income tax deduction, the fair market value of all consideration received in return for the contribution from any source must be subtracted, whether that source is the donee charity or a third-party. Thus, deductibility in a quid pro quo situation is a function of the fair market value of the benefit received by the donor in return for the contribution, no matter what the source of the benefit. See Rev. Rul. 67-246 ("In determining the portion of the payment to a charitable organization which is deductible as a charitable contribution in these circumstances, the FMV of any consideration received for the payment from any source must be subtracted from the total payment").

Authority Involving Effect of State Tax Credits Provided in Return for Charitable Contributions

In CCA 201105010, pursuant to a state program awarding state tax credits in return for charitable contributions earmarked for economic development, the taxpayers submitted applications to the State Department of Economic Development for approval to make a certain amount of the charitable contributions under the program. The applications were accepted and the taxpayers were granted state income tax credits equal to a specified percentage of the approved contributions. Pursuant to the parameters of the program, the taxpayers used a certain amount of the state income tax credit to offset their year 1 state income tax liability; sold a certain amount of the state income tax credits to other individuals; and carried forward the remaining amount of the state income tax credits to future years. The IRS ruled that the state income tax credits were not treated as benefits received by the donor that would reduce the amount of the charitable contribution deduction, stating that "the payment is considered a charitable contribution under §170, not a payment of tax possibly deductible under §164."

In its analysis, the IRS specifically acknowledged the firmly established legal principle that serves to eliminate or reduce an otherwise available charitable income tax deduction where the contribution is made in return for specified monetary consideration:

Generally, to be deductible as a charitable contribution under §170, a transfer to a charitable organization or government unit must be a gift. A gift for this purpose is a transfer of money or property without receipt of adequate consideration, made with charitable intent. A transfer is not made with charitable intent if the transferor expects a direct or indirect return benefit commensurate with the amount of the transfer. If a taxpayer receives a benefit in return for a transfer to a charitable organization, the transfer may be deductible as a charitable contribution, but only to the extent the amount transferred exceeds the fair

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market value of the benefit received, and only if the excess amount was transferred with the intent of making a gift. See United States v. American Bar Endowment, 477 U.S. 105, 116-118 [58 AFTR 2d 86-5190] (1986); Hernandez v. Commissioner, 490 U.S. 680, 689-691 [63 AFTR 2d 89-1395] (1989); §1.170A-1(h)(1) and (2) of the Income Tax Regulations.

If the benefits expected to be received by a donor are substantial (that is, greater than those incidental benefits that inure to the general public from transfers for charitable purposes), then the transferor has received a quid pro quo sufficient to remove the transfer from the realm of deductibility under §170. Singer Co. v. United States, 449 F.2d 413, 422-423 [28 AFTR 2d 71-5822] (Ct. Cl. 1971).

In determining that the tax credits provided in return for the charitable contribution did not constitute a quid pro quo that would reduce or eliminate any part of the charitable income tax deduction, the IRS, citing federal case law, stated that the "tax benefit of a federal or state charitable contribution deduction is not regarded as a return benefit that negates charitable intent, reducing or eliminating the deduction itself." See McLennan ("a donation of property for the exclusive purpose of receiving a tax deduction does not vitiate the charitable nature of the contribution"); Skripak ("However, as stated above, the deduction for charitable contributions was intended to provide a tax incentive for taxpayers to support charities. A taxpayer's desire to avoid or eliminate taxes by contributing cash or property to charities cannot be used as a basis for disallowing the deduction for the charitable deduction"); Allen; see Browning v. Commissioner (value of state and federal tax benefits not part of the amount realized from a bargain sale of donated property). The IRS then ruled that the tax benefit in the form of a state tax credit was not distinguishable from the benefit of a state tax deduction for purposes of applying Section 170, stating:

Based on our analysis of existing authorities, we conclude that the position reflected in McLennan, Browning, and similar case law generally applies. There may be unusual circumstances in which it would be appropriate to recharacterize a payment of cash or property that was, in form, a charitable contribution as, in substance, a satisfaction of tax liability. Generally, however, a state or local tax benefit is treated for federal tax purposes as a reduction or potential reduction in tax liability. As such, it is reflected in a reduced deduction for the payment of state or local tax under §164, not as consideration that might constitute a quid pro quo, for purposes of §170 … In this respect, we see no reason under McLennan, Browning, and similar case law to distinguish between the value of a state tax deduction, and the value of a state tax credit, or to draw a bright-line distinction based on the amount of the tax benefit in question.

It is interesting that for purpose of applying the quid pro quo rules of Section 170 in CCA 201105010, the IRS equated the benefit of the income tax savings resulting from a federal income deduction to the benefit of a state income tax credit, so that in both cases the charitable deduction otherwise available Section 170(a) is not reduced by the resulting tax savings. This was the case notwithstanding that it would likely have been more favorable from the perspective of the IRS to treat the charitable deduction as the equivalent of a state income tax payment because unlike a charitable contribution deduction, a state income tax payment is subject to the alternative minimum tax, potentially exposing the taxpayer to greater federal taxes.

The approach taken in CCA 201105010 appears to have been adopted by the Tax Court in Tempel v. Commissioner . In that case, the taxpayers, Colorado residents, donated a qualified conservation easement. Colorado granted its eligible residents income tax credits for donating perpetual conservation easements, which the taxpayer were entitled as a result of their donation. The State granted a state income tax credit equal to 100 percent of the value of such a donation up to $100,000 and to the extent a donation's value exceeded $100,000, additional credit was limited to 40 percent of the value in excess of

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$100,000. Based on the value of their donation, the taxpayers were entitled to the maximum allowable tax state income credit of $260,000.

The court's discussion specifically noted that the IRS contended and the taxpayers did not contend otherwise that the “receipt of State tax credits as a result of their conservation easement contribution was [not] a quid pro quo transaction.” In footnote 17, the court, specifically referring to CCA 201105010, stated that “Some commentators have suggested a State's grant of State income tax credits to taxpayers who make charitable donations of qualified conservation easements should be treated as a transaction that is in part a sale and in part a gift. The Commissioner has eschewed this approach, and neither party has advocated it here. See Chief Counsel Advice 201105010 (Feb. 4, 2011); see also Browning v. Commissioner, 109 T.C. 303 (1997).” Note, of course, that CCA 201105010 may not be used or cited as precedent. And, it should be further noted that the approach applied in CCA 201105010 was not absolute, as the IRS specifically stated, as indicated above, that “[t]here may be unusual circumstances in which it would be appropriate to recharacterize a payment of cash or property that was, in form, a charitable contribution as, in substance, a satisfaction of tax liability.”

Issues to Consider Where a State Provides Tax Credits in Return for Charitable Contributions to the State Itself

The quid pro quo rules in the context of charitable contributions have historically been applied by the IRS and the courts quite broadly, such that any consideration (other than a mere incidental benefit) provided to a donor, flowing from the donee charity itself or from a third-party, has caused either the elimination or reduction of the charitable deduction otherwise available, potentially providing a powerful argument that a state tax benefit received in return for a charitable contribution should reduce the deduction otherwise available under Section 170(a).

Notwithstanding, the underlying rationale of CCA 201105010, and its apparent adoption in Tempel, offers support for the proposition that any tax benefit conferred upon a donor to encourage a contribution to charity should not be considered a quid pro quo for purposes of Section 170(a). Indeed, the U.S. tax regime has long been used as a mechanism to provide tax incentives to encourage donors to make contributions to qualified charitable organizations and such incentives have no effect on the amount allowable as a charitable income tax deduction. See Bliss v. Commissioner (addressing the charitable deduction introduced into the income tax law by Section 1201(2) of the War Revenue Act of 1917, the court stated that the “obvious purpose was to encourage gifts for charity, education, and science”). There would appear to be no reason why a state taxing regime cannot similarly provide tax incentives to encourage charitable giving without affecting the charitable income tax deduction otherwise allowable for federal income tax purposes.

While charitable contributions made to a state for exclusively public purposes are generally deductible for federal income tax purposes under Section 170(a), when state tax credits are provided by a state under a program to encourage a charitable contribution not to one or more specified third-party charities that a donor chooses to support, but to the very state providing the tax credits, greater scrutiny appears warranted in the context of Section 170(a). Even accepting the position that a state tax benefit provided to encourage charitable giving does not result in a quid pro quo transaction for Section 170(a) purposes, a charitable deduction is still premised upon the transfer being motivated by a charitable intent and made on a voluntary basis.

Contributions to one or more third-party charities chosen by a donor, even under a state program providing state tax benefits to encourage such contributions, presumably should be considered to be

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motivated by a charitable intent and made on a voluntary basis. In this situation, the donor has a choice that may be freely exercised: make a contribution to a charity the donor seeks to support or pay taxes to the state.

Where a donor makes a purported contribution to a qualified charity of an amount that he or she would otherwise be required or expected to pay to the very same organization, however, the actual substance of the payment will control the characterization of the payment for federal income tax purposes. In Rev. Rul. 83-104, for example, a private school described in Section 170(c) requested parents to contribute $400x to the school for each of their children enrolled in the school. Parents who did not make the $400x contribution were required to pay $400x tuition for each child enrolled in the school. Parents who neither made the contribution nor paid tuition could not enroll a child in the school. The IRS, citing federal case law and legislative history of Section 170, ruled that because a parent had to either make the contribution or pay the tuition charge, the “payment is not voluntary and no [charitable] deduction is allowed.” The IRS stated that “a plan allowing taxpayers either to pay tuition or to make ‘contributions' in exchange for schooling” creates a “presumption that the payment is not a charitable contribution.” In the same ruling, the IRS stated that “factors suggesting that a contribution policy has been created as a means of avoiding the characterization of payments as tuition” are indicative of the payments not being a charitable contribution.

Thus, if a purported charitable contribution made by a resident of a state is merely a substitute for a tax payment otherwise required to be made to the state if the contribution is not made, the characterization of such a payment as a charitable contribution for federal income tax purposes will be in jeopardy, particularly where it is made under a legislative plan adopted for the very purpose of avoiding the characterization of the payments as taxes. Indeed, this situation would seem to fall within the language of CCA 201105010 that there “may be unusual circumstances in which it would be appropriate to recharacterize a payment of cash or property that was, in form, a charitable contribution as, in substance, a satisfaction of tax liability.”

It would appear that a state seeking to adopt a legislative proposal to recast SALT payments as charitable contributions will be best situated if it actually gives its residents some discretion as to the public purposes to which their contributions will be used, so that the contributions are not essentially equivalent to a tax payment that would otherwise be required to be paid to the state but, instead, may be considered motivated by some form of charitable intent and made on a voluntary basis. This could include, for example, providing the donor with a choice of allocating a contribution among the wide array of activities, operations, programs and functions carried out by the state for exclusively public purposes that the donor seeks to support or by any other manner that clearly differentiates the contributions from otherwise mandated tax payments. Contributions could be made to separate and distinct funds administered by the state solely for those public purposes the donor desires to support. Presumably, the greater the choice a donor has with respect to the use of a purported charitable contribution to a state and the less the contribution will be used in the same manner as an ordinary tax payment, the better the position that the contribution is motivated by charitable intent and is voluntary, and is not merely a substituted tax payment to be used solely as determined by the state Of course, such a choice of funding provided to a potential donor has to be reconciled with the financial and budgetary needs of the state in order to provide necessary government services to its citizens.

Even where a state believes that its legislative proposal withstands scrutiny, a donor making a charitable contribution in lieu of a SALT payment can only deduct such contribution for federal income tax purposes under Section 170(a) if he or she receives a contemporaneous written acknowledgment pursuant to Section 170(f)(8) from the donee organization (assuming the amount of the contribution is $250 or more)

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that includes the amount of the contribution and indicates whether any consideration was received in return. In order for the donor to deduct the full amount of the contribution, the state receiving the charitable contribution for which it will issue a state tax credit in return would have to indicate on such acknowledgment that no consideration was provided in return for the contribution or otherwise note the tax benefit provided but indicate that it is a disregarded benefit for purposes of Section 170(f)(8). In this regard, there is no IRS penalty imposed on a donee organization for not issuing a contemporaneous written acknowledgment, although penalties may be applied for providing a false acknowledgment.

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