

170(f)(5) and this section shall, without regard to whether any reduction may be required by paragraph (b) of this section, also be reduced for interest which has been paid, or is to be paid, by the taxpayer on indebtedness incurred or continued to purchase or carry such bond, and which is attributable to any period before the making of the contribution. However, the reduction referred to in this paragraph shall be made only to the extent that such reduction does not exceed the interest (including bond discount and other interest equivalent) receivable on the bond, and attributable to any period before the making of the contribution which is not, by reason of the taxpayer's method of accounting, includible in the taxpayer's gross income for any taxable year. For purposes of section 170(f)(5) and this section the term *bond* means any bond, debenture, note, or certificate or other evidence of indebtedness.

(d) *Illustrations.* The application of this section may be illustrated by the following examples:

Example 1. On January 1, 1970, A, a cash basis taxpayer using the calendar year as the taxable year, contributed to a charitable organization real estate having a fair market value and adjusted basis of \$10,000. In connection with the contribution the charitable organization assumed an indebtedness of \$8,000 which A had incurred. On December 31, 1969, A prepaid one year's interest on that indebtedness for 1970, amounting to \$960, and took an interest deduction of \$960 for such amount. The amount of the gift, determined without regard to this section, is \$2,960 (\$10,000 less \$8,000, the outstanding indebtedness, plus \$960, the amount of prepaid interest). In determining the amount of the deduction for the charitable contribution, the value of the gift (\$2,960) must be reduced by \$960 to eliminate from the computation of such deduction that portion thereof for which A has been allowed an interest deduction.

Example 2. (a) On January 1, 1970, B, an individual using the cash receipts and disbursements method of accounting, purchased for \$9,950 a 5 1/2 percent \$10,000, 20-year M Corporation bond, the interest on which was payable semiannually on June 30 and December 31. The M Corporation had issued the bond on January 1, 1960, at a discount of \$720 from the principal amount. On December 1, 1970, B donated the bond to a charitable organization, and, in connection with the contribution, the charitable organization as-

sumed an indebtedness of \$7,000 which B had incurred to purchase and carry the bond.

(b) During the calendar year 1970 B paid accrued interest of \$330 on the indebtedness for the period from January 1, 1970, to December 1, 1970, and has taken an interest deduction of \$330 for such amount. No portion of the bond discount of \$36 a year (\$720 divided by 20 years) has been included in B's income, and of the \$550 of annual interest receivable on the bond, he included in income only the June 30, 1970, payment of \$275.

(c) The market value of the bond on December 1, 1970, was \$9,902. Such value includes \$229 of interest receivable which had accrued from July 1 to December 1, 1970.

(d) The amount of the charitable contribution determined without regard to this section is \$2,902 (\$9,902, the value of the property on the date of gift, less \$7,000, the amount of the liability assumed by the charitable organization). In determining the amount of the allowable deduction for charitable contributions, the value of the gift (\$2,902) must be reduced to eliminate from the deduction that portion thereof for which B has been allowed an interest deduction. Although the amount of such interest deduction was \$330, the reduction required by this section is limited to \$262, since the reduction is not in excess of the amount of interest income on the bond (\$229 of accrued interest plus \$33, the amount of bond discount attributable to the 11-month period B held the bond).

(e) *Effective date.* This section applies only to contributions paid in taxable years beginning after December 31, 1969.

[T.D. 7207, 37 FR 20775, Oct. 4, 1972]

§ 1.170A-4 Reduction in amount of charitable contributions of certain appreciated property.

(a) *Amount of reduction.* Section 170(e)(1) requires that the amount of the charitable contribution which would be taken into account under section 170(a) without regard to section 170(e) shall be reduced before applying the percentage limitations under section 170(b):

(1) In the case of a contribution by an individual or by a corporation of ordinary income property, as defined in paragraph (b)(1) of this section, by the amount of gain (hereinafter in this section referred to as ordinary income) which would have been recognized as gain which is not long-term capital gain if the property had been sold by the donor at its fair market value at

the time of its contribution to the charitable organization,

(2) In the case of a contribution by an individual of section 170(e) capital gain property, as defined in paragraph (b)(2) of this section, by 50 percent of the amount of gain (hereinafter in this section referred to as long-term capital gain) which would have been recognized as long-term capital gain if the property had been sold by the donor at its fair market value at the time of its contribution to the charitable organization, and

(3) In the case of a contribution by a corporation of section 170(e) capital gain property, as defined in paragraph (b)(2) of this section, by 62 1/2 percent of the amount of gain (hereinafter in this section referred to as long-term capital gain) which would have been recognized as long-term capital gain if the property had been sold by the donor at its fair market value at the time of its contribution to the charitable organization.

Section 170(e)(1) and this paragraph do not apply to reduce the amount of the charitable contribution where, by reason of the transfer of the contributed property, ordinary income or capital gain is recognized by the donor in the same taxable year in which the contribution is made. Thus, where income or gain is recognized under section 453(d) upon the transfer of an installment obligation to a charitable organization, or under section 454(b) upon the transfer of an obligation issued at a discount to such an organization, or upon the assignment of income to such an organization, section 170(e)(1) and this paragraph do not apply if recognition of the income or gain occurs in the same taxable year in which the contribution is made. Section 170(e)(1) and this paragraph apply to a charitable contribution of an interest in ordinary income property or section 170(e) capital gain property which is described in paragraph (b) of § 1.170A-6, or paragraph (b) of § 1.170A-7. For purposes of applying section 170(e)(1) and this paragraph it is immaterial whether the charitable contribution is made "to" the charitable organization or whether it is made "for the use of" the charitable organization. See § 1.170A-8(a)(2).

(b) *Definitions and other rules.* For purposes of this section:

(1) *Ordinary income property.* The term *ordinary income property* means property any portion of the gain on which would not have been long term capital gain if the property had been sold by the donor at its fair market value at the time of its contribution to the charitable organization. Such term includes, for example, property held by the donor primarily for sale to customers in the ordinary course of his trade or business, a work of art created by the donor, a manuscript prepared by the donor, letters and memorandums prepared by or for the donor, a capital asset held by the donor for not more than 1 year (6 months for taxable years beginning before 1977; 9 months for taxable years beginning in 1977), and stock described in section 306(a), 341(a), or 1248(a) to the extent that, after applying such section, gain on its disposition would not have been long-term capital gain. The term does not include an income interest in respect of which a deduction is allowed under section 170(f)(2)(B) and paragraph (c) of § 1.170A-6.

(2) *Section 170(e) capital gain property.* The term *section 170(e) capital gain property* means property any portion of the gain on which would have been treated as long-term capital gain if the property had been sold by the donor at its fair market value at the time of its contribution to the charitable organization and which:

(i) Is contributed to or for the use of a private foundation, as defined in section 509(a) and the regulations thereunder, other than a private foundation described in section 170(b)(1)(E),

(ii) Constitutes tangible personal property contributed to or for the use of a charitable organization, other than a private foundation to which subdivision (i) of this subparagraph applies, which is put to an unrelated use by the charitable organization within the meaning of subparagraph (3) of this paragraph, or

(iii) Constitutes property not described in subdivision (i) or (ii) of this subparagraph which is 30-percent capital gain property to which an election under paragraph (d)(2) of § 1.170A-8 applies.

For purposes of this subparagraph a fixture which is intended to be severed from real property shall be treated as tangible personal property.

(3) *Unrelated use*—(i) *In general.* The term *unrelated use* means a use which is unrelated to the purpose or function constituting the basis of the charitable organization's exemption under section 501 or, in the case of a contribution of property to a governmental unit, the use of such property by such unit for other than exclusively public purposes. For example, if a painting contributed to an educational institution is used by that organization for educational purposes by being placed in its library for display and study by art students, the use is not an unrelated use; but if the painting is sold and the proceeds used by the organization for educational purposes, the use of the property is an unrelated use. If furnishings contributed to a charitable organization are used by it in its offices and buildings in the course of carrying out its functions, the use of the property is not an unrelated use. If a set or collection of items of tangible personal property is contributed to a charitable organization or governmental unit, the use of the set or collection is not an unrelated use if the donee sells or otherwise disposes of only an insubstantial portion of the set or collection. The use by a trust of tangible personal property contributed to it for the benefit of a charitable organization is an unrelated use if the use by the trust is one which would have been unrelated if made by the charitable organization.

(ii) *Proof of use.* For purposes of applying subparagraph (2)(ii) of this paragraph, a taxpayer who makes a charitable contribution of tangible personal property to or for the use of a charitable organization or governmental unit may treat such property as not being put to an unrelated use by the donee if:

(a) He establishes that the property is not in fact put to an unrelated use by the donee, or

(b) At the time of the contribution or at the time the contribution is treated as made, it is reasonable to anticipate that the property will not be put to an unrelated use by the donee. In the case of a contribution of tangible personal

property to or for the use of a museum, if the object donated is of a general type normally retained by such museum or other museums for museum purposes, it will be reasonable for the donor to anticipate, unless he has actual knowledge to the contrary, that the object will not be put to an unrelated use by the donee, whether or not the object is later sold or exchanged by the donee.

(4) *Property used in trade or business.* For purposes of applying subparagraphs (1) and (2) of this paragraph, property which is used in the trade or business, as defined in section 1231(b), shall be treated as a capital asset, except that any gain in respect of such property which would have been recognized if the property had been sold by the donor at its fair market value at the time of its contribution to the charitable organization shall be treated as ordinary income to the extent that such gain would have constituted ordinary income by reason of the application of section 617 (d)(1), 1245(a), 1250(a), 1251(c), 1252(a), or 1254(a).

(5) *Nonresident alien individuals and foreign corporations.* The reduction in the case of a nonresident alien individual or a foreign corporation shall be determined by taking into account the gain which would have been recognized and subject to tax under chapter 1 of the Code if the property had been sold or disposed of within the United States by the donor at its fair market value at the time of its contribution to the charitable organization. However, the amount of such gain which would have been subject to tax under section 871(a) or 881 (relating to gain not effectively connected with the conduct of a trade or business within the United States) if there had been a sale or other disposition within the United States shall be treated as long-term capital gain. Thus, a charitable contribution by a nonresident alien individual or a foreign corporation of property the sale or other disposition of which within the United States would have resulted in gain subject to tax under section 871(a) or 881 will be reduced only as provided in section 170(e)(1)(B) and paragraph (a)(2) or (3) of this section, but only if the property contributed is described in

subdivision (i), (ii), or (iii) of subparagraph (2) of this paragraph. A charitable contribution by a nonresident alien individual or a foreign corporation of property the sale or other disposition of which within the United States would have resulted in gain subject to tax under section 871(a) or 881 will in no case be reduced under section 170(e)(1)(A) and paragraph (a)(1) of this section.

(c) *Allocation of basis and gain*—(1) *In general.* Except as provided in subparagraph (2) of this paragraph:

(i) If a taxpayer makes a charitable contribution of less than his entire interest in appreciated property, whether or not the transfer is made in trust, as, for example, in the case of a transfer of appreciated property to a pooled income fund described in section 642(c)(5) and § 1.642(c)-5, and is allowed a deduction under section 170 for a portion of the fair market value of such property, then for purposes of applying the reduction rules of section 170(e)(1) and this section to the contributed portion of the property the taxpayer's adjusted basis in such property at the time of the contribution shall be allocated under section 170(e)(2) between the contributed portion of the property and the noncontributed portion.

(ii) The adjusted basis of the contributed portion of the property shall be that portion of the adjusted basis of the entire property which bears the same ratio to the total adjusted basis as the fair market value of the contributed portion of the property bears to the fair market value of the entire property.

(iii) The ordinary income and the long-term capital gain which shall be taken into account in applying section 170(e)(1) and paragraph (a) of this section to the contributed portion of the property shall be the amount of gain which would have been recognized as ordinary income and long-term capital gain if such contributed portion had been sold by the donor at its fair market value at the time of its contribution to the charitable organization.

(2) *Bargain sale.* (i) Section 1011(b) and § 1.1011-2 apply to bargain sales of property to charitable organizations. For purposes of applying the reduction rules of section 170(e)(1) and this sec-

tion to the contributed portion of the property in the case of a bargain sale, there shall be allocated under section 1011(b) to the contributed portion of the property that portion of the adjusted basis of the entire property that bears the same ratio to the total adjusted basis as the fair market value of the contributed portion of the property bears to the fair market value of the entire property. For purposes of applying section 170(e)(1) and paragraph (a) of this section to the contributed portion of the property in such a case, there shall be allocated to the contributed portion the amount of gain that is not recognized on the bargain sale but that would have been recognized if such contributed portion had been sold by the donor at its fair market value at the time of its contribution to the charitable organization.

(ii) The term *bargain sale*, as used in this subparagraph, means a transfer of property which is in part a sale or exchange of the property and in part a charitable contribution, as defined in section 170(c), of the property.

(3) *Ratio of ordinary income and capital gain.* For purposes of applying subparagraphs (1)(iii) and (2)(i) of this paragraph, the amount of ordinary income (or long-term capital gain) which would have been recognized if the contributed portion of the property had been sold by the donor at its fair market value at the time of its contribution shall be that amount which bears the same ratio to the ordinary income (or long-term capital gain) which would have been recognized if the entire property had been sold by the donor at its fair market value at the time of its contribution as (i) the fair market value of the contributed portion at such time bears to (ii) the fair market value of the entire property at such time. In the case of a bargain sale, the fair market value of the contributed portion for purposes of subdivision (i) is the amount determined by subtracting from the fair market value of the entire property the amount realized on the sale.

(4) *Donee's basis of property acquired.* The adjusted basis of the contributed portion of the property, as determined under subparagraph (1) or (2) of this paragraph, shall be used by the donee

in applying to the contributed portion such provisions as section 514(a)(1), relating to adjusted basis of debt-financed property; section 1015(a), relating to basis of property acquired by gift; section 4940(c)(4), relating to capital gains and losses in determination of net investment income; and section 4942(f)(2)(B), relating to net short-term capital gain in determination of tax on failure to distribute income. The fair market value of the contributed portion of the property at the time of the contribution shall not be used by the donee as the basis of such contributed portion.

(d) *Illustrations.* The application of this section may be illustrated by the following examples:

Example 1. (a) On July 1, 1970, C, an individual, makes the following charitable contributions, all of which are made to a church except in the case of the stock (as indicated):

Property	Fair market value	Adjusted basis	Recognized gain sold
Ordinary income property	\$50,000	\$35,000	\$15,000
Property which, if sold, would produce long-term capital gain:			
(1) Stock held more than 6 months contributed to—			
(i) A church	25,000	21,000	4,000
(ii) A private foundation not described in section 170(b)(1)(E)	15,000	10,000	5,000
(2) Tangible personal property held more than 6 months (put to unrelated use by church)	12,000	6,000	6,000
Total	102,000	72,000	30,000

(b) After making the reductions required by paragraph (a) of this section, the amount of charitable contributions allowed (before application of section 170(b) limitations) is as follows:

Property	Fair market value	Reduction	Contribution allowed
Ordinary income property	\$50,000	\$15,000	\$35,000
Property which, if sold, would produce long-term capital gain:			
(1) Stock contributed to:			
(i) The church	25,000	25,000
(ii) The private foundation	15,000	2,500	12,500
(2) Tangible personal property	12,000	3,000	9,000
Total	102,000	20,500	81,500

(c) If C were a corporation, rather than an individual, the amount of charitable contributions allowed (before application of section 170(b) limitation) would be as follows:

Property	Fair market value	Reduction	Contribution allowed
Ordinary income property	\$50,000	\$15,000	\$35,000
Property which, if sold, would produce long-term capital gain:			
(1) Stock contributed to:			
(i) The church	25,000	25,000
(ii) The private foundation	15,000	3,125	11,875
(2) Tangible personal property	12,000	3,750	8,250
Total	102,000	21,875	80,125

Example 2. On March 1, 1970, D, an individual, contributes to a church intangible property to which section 1245 applies which has a fair market value of \$60,000 and an adjusted basis of \$10,000. At the time of the contribution D has used the property in his business for more than 6 months. If the property had been sold by D at its fair market value at the time of its contribution, it is assumed that under section 1245 \$20,000 of the gain of \$50,000 would have been treated as ordinary income and \$30,000 would have been long-term capital gain. Under paragraph (a)(1) of this section, D's contribution of \$60,000 is reduced by \$20,000.

Example 3. The facts are the same as in *Example 2* except that the property is contributed to a private foundation not described in section 170(b)(1)(E). Under paragraph (a) (1) and (2) of this section, D's contribution is reduced by \$35,000 (100 percent of the ordinary income of \$20,000 and 50 percent of the long-term capital gain of \$30,000).

Example 4. (a) In 1971, E, an individual calendar-year taxpayer, contributes to a church stock held for more than 6 months which has a fair market value of \$90,000 and an adjusted basis of \$10,000. In 1972, E also contributes to a church stock held for more than 6 months which has a fair market value of \$20,000 and an adjusted basis of \$10,000. E's contribution base for 1971 is \$200,000; and for 1972, is \$150,000. E makes no other charitable contributions for these 2 taxable years.

(b) For 1971 the amount of the contribution which may be taken into account under section 170(a) is limited by section 170(b)(1)(D)(i) to \$60,000 (\$200,000×30%), and A is allowed a deduction for \$60,000. Under section 170(b)(1)(D)(ii), E has a \$30,000 carryover to 1972 of 30-percent capital gain property, as defined in paragraph (d)(3) of §1.170A-8. For 1972 the amount of the charitable contributions deduction is \$45,000 (total contributions of \$50,000 [\$30,000+\$20,000] but not to exceed 30% of \$150,000).

(c) Assuming, however, that in 1972 E elects under section 170(b)(1)(D)(iii) and paragraph (d)(2) of § 1.170A-8 to have section 170(e)(1)(B) apply to his contributions and carryovers of 30-percent capital gain property, he must apply section 170(d)(1) as if section 170(e)(1)(B) had applied to the contribution for 1971. If section 170(e)(1)(B) had applied in 1971 to his contributions of 30-percent capital gain property, E's contribution would have been reduced from \$90,000 to \$50,000, the reduction of \$40,000 being 50 percent of the gain of \$80,000 (\$90,000 - \$10,000) which would have been recognized as long-term capital gain if the property had been sold by E at its fair market value at the time of its contribution to the church. Accordingly, by taking the election into account, E has no carryover of 30-percent capital gain property to 1972 since the charitable contributions deduction of \$60,000 allowed for 1971 in respect of that property exceeds the reduced contribution of \$50,000 for 1971 which may be taken into account by reason of the election. The charitable contributions deduction of \$60,000 allowed for 1971 is not reduced by reason of the election.

(d) Since by reason of the election E is allowed under paragraph (a)(2) of this section a charitable contributions deduction for 1972 of \$15,000 (\$20,000 - [(\$20,000 - \$10,000) × 50%]) and since the \$30,000 carryover from 1971 is eliminated, it would not be to E's advantage to make the election under section 170(b)(1)(D)(iii) in 1972.

Example 5. In 1970, F, an individual calendar-year taxpayer, sells to a church for \$4,000 ordinary income property with a fair market value of \$10,000 and an adjusted basis of \$4,000. F's contribution base for 1970 is \$20,000, and F makes no other charitable contributions in 1970. Thus, F makes a charitable contribution to the church of \$6,000 (\$10,000 - \$4,000 amount realized), which is 60% of the value of the property. The amount realized on the bargain sale is 40% (\$4,000/\$10,000) of the value of the property. In applying section 1011(b) to the bargain sale, adjusted basis in the amount of \$1,600 (\$4,000 adjusted basis × 40%) is allocated under § 1.1011-2(b) to the noncontributed portion of the property, and F recognizes \$2,400 (\$4,000 amount realized less \$1,600 adjusted basis) of ordinary income. Under paragraphs (a)(1) and (c)(2)(i) of this section, F's contribution of \$6,000 is reduced by \$3,600 (\$6,000 - [\$4,000 adjusted basis × 60%]) (i.e., the amount of ordinary income that would have been recognized on the contributed portion had the property been sold). The reduced contribution of \$2,400 consists of the portion (\$4,000 × 60%) of the adjusted basis not allocated to the noncontributed portion of the property. That is, the reduced contribution consists of the portion of the adjusted basis allocated to the contributed portion. Under sections 1012

and 1015(a) the basis of the property to the church is \$6,400 (\$4,000 + \$2,400).

Example 6. In 1970, G, an individual calendar-year taxpayer, sells to a church for \$6,000 ordinary income property with a fair market value of \$10,000 and an adjusted basis of \$4,000. G's contribution base for 1970 is \$20,000, and G makes no other charitable contributions in 1970. Thus, G makes a charitable contribution to the church of \$4,000 (\$10,000 - \$6,000 amount realized), which is 40% of the value of the property. The amount realized on the bargain sale is 60% (\$6,000/\$10,000) of the value of the property. In applying section 1011(b) to the bargain sale, adjusted basis in the amount of \$2,400 (\$4,000 adjusted basis × 60%) is allocated under § 1.1011-2(b) to the noncontributed portion of the property, and G recognizes \$3,600 (\$6,000 amount realized less \$2,400 adjusted basis) of ordinary income. Under paragraphs (a)(1) and (c)(2)(i) of this section, G's contribution of \$4,000 is reduced by \$2,400 (\$4,000 - [\$4,000 adjusted basis × 40%]) (i.e., the amount of ordinary income that would have been recognized on the contributed portion had the property been sold). The reduced contribution of \$1,600 consist of the portion (\$4,000 × 40%) of the adjusted basis not allocated to the noncontributed portion of the property. That is, the reduced contribution consists of the portion of the adjusted basis allocated to the contributed portion. Under sections 1012 and 1015(a) the basis of the property to the church is \$7,600 (\$6,000 + \$1,600).

Example 7. In 1970, H, an individual calendar-year taxpayer, sells to a church for \$2,000 stock held for not more than 6 months which has an adjusted basis of \$4,000 and a fair market value of \$10,000. H's contribution base for 1970 is \$20,000, and H makes no other charitable contributions in 1970. Thus, H makes a charitable contribution to the church of \$8,000 (\$10,000 - \$2,000 amount realized), which is 80% of the value of the property. The amount realized on the bargain sale is 20% (\$2,000/\$10,000) of the value of the property. In applying section 1011(b) to the bargain sale, adjusted basis in the amount of \$800 (\$4,000 adjusted basis × 20%) is allocated under § 1.1011-2(b) to the noncontributed portion of the property, and H recognizes \$1,200 (\$2,000 amount realized less \$800 adjusted basis) of ordinary income. Under paragraphs (a)(1) and (c)(2)(i) of this section, H's contribution of \$8,000 is reduced by \$4,800 (\$8,000 - [\$4,000 adjusted basis × 80%]) (i.e., the amount of ordinary income that would have been recognized on the contributed portion had the property been sold). The reduced contribution of \$3,200 consists of the portion (\$4,000 × 80%) of the adjusted basis not allocated to the noncontributed portion of the property. That is, the reduced contribution consists of the portion of the adjusted basis allocated to the contributed portion. Under

sections 1012 and 1015(a) the basis of the property to the church is \$5,200 (\$2,000+\$3,200).

Example 8. In 1970, F, an individual calendar-year taxpayer, sells for \$4,000 to a private foundation not described in section 170(b)(1)(E) property to which section 1245 applies which has a fair market value of \$10,000 and an adjusted basis of \$4,000. F's contribution base for 1970 is \$20,000, and F makes no other charitable contributions in 1970. At the time of the bargain sale, F has used the property in his business for more than 6 months. Thus F makes a charitable contribution of \$6,000 (\$10,000-\$4,000 amount realized), which is 60% of the value of the property. The amount realized on the bargain sale is 40% (\$4,000/\$10,000) of the value of the property. If the property had been sold by F at its fair market value at the time of its contribution, it is assumed that under section 1245 \$4,000 of the gain of \$6,000 (\$10,000-\$4,000 adjusted basis) would have been treated as ordinary income and \$2,000 would have been long-term capital gain. In applying section 1011(b) to the bargain sale, adjusted basis in the amount of \$1,600 (\$4,000 adjusted basis \times 40%) is allocated under § 1.1011-2(b) to the non-contributed portion of the property, and F's recognized gain of \$2,400 (\$4,000 amount realized less \$1,600 adjusted basis) consists of \$1,600 (\$4,000 \times 40%) of ordinary income and \$800 (\$2,000 \times 40%) of long-term capital gain. Under paragraphs (a) and (c)(2)(i) of this section, F's contribution of \$6,000 is reduced by \$3,000 (the sum of \$2,400 (\$4,000 \times 60%) of ordinary income and \$600 [(\$2,000 \times 60%) \times 50%] of long-term capital gain) (*i.e.*, the amount of gain that would have been recognized on the contributed portion had the property been sold). The reduced contribution of \$3,000 consists of \$2,400 (\$4,000 \times 60%) of adjusted basis and \$600 [(\$2,000 \times 60%) \times 50%] of long-term capital gain not used as a reduction under paragraph (a)(2) of this section. Under sections 1012 and 1015(a) the basis of the property to the private foundation is \$6,400 (\$4,000+\$2,400).

Example 9. On January 1, 1970, A, an individual, transfers to a charitable remainder annuity trust described in section 664 (d)(1) stock which he has held for more than 6 months and which has a fair market value of \$250,000 and an adjusted basis of \$50,000, an irrevocable remainder interest in the property being contributed to a private foundation not described in section 170(b)(1)(E). The trusts provides that an annuity of \$12,500 a year is payable to A at the end of each year for 20 years. By reference to § 20.2031-7A(c) of this chapter (Estate Tax Regulations) the figure in column (2) opposite 20 years is 11.4699. Therefore, under § 1.664-2 the fair market value of the gift of the remainder interest to charity is \$106,626.25 (\$250,000 - [\$12,500 \times 11.4699]). Under paragraph (c)(1)(ii) of this section, the adjusted basis allocated to

the contributed portion of the property is \$21,325.25 (\$50,000 \times \$106,626.25/\$250,000). Under paragraphs (a)(2) and (c)(1) of this section, A's contribution is reduced by \$42,650.50 (50 percent \times [\$106,626.25 - \$21,325.25]) to \$63,975.75 (\$106,626.25 - \$42,650.50). If, however, the irrevocable remainder interest in the property had been contributed to a section 170(b)(1)(A) organization, A's contribution of \$106,626.25 would not be reduced under paragraph (a) of this section.

Example 10. (a) On July 1, 1970, B, a calendar-year individual taxpayer, sells to a church for \$75,000 intangible property to which section 1245 applies which has a fair market value of \$250,000 and an adjusted basis of \$75,000. Thus, B makes a charitable contribution to the church of \$175,000 (\$250,000-\$75,000 amount realized), which is 70% (\$175,000/\$250,000) of the value of the property, the amount realized on the bargain sale is 30% (\$75,000/\$250,000) of the value of the property. At the time of the bargain sale, B has used the property in his business for more than 6 months. B's contribution base for 1970 is \$500,000, and B makes no other charitable contributions in 1970. If the property had been sold by B at its fair market value at the time of its contribution, it is assumed that under section 1245 \$105,000 of the gain of \$175,000 (\$250,000-\$75,000 adjusted basis) would have been treated as ordinary income and \$70,000 would have been long-term capital gain. In applying section 1011(b) to the bargain sale, adjusted basis in the amount of \$22,500 (\$75,000 adjusted basis \times 30%) is allocated under § 1.1011-2(b) to the noncontributed portion of the property and B's recognized gain of \$52,500 (\$75,000 amount realized less \$22,500 adjusted basis) consists of \$31,500 (\$105,000 \times 30%) of ordinary income and \$21,000 (\$70,000 \times 30%) of long term capital gain.

(b) Under paragraphs (a)(1) and (c)(2)(i) of this section B's contribution of \$175,000 is reduced by \$73,500 (\$105,000 \times 70%) (*i.e.*, the amount of ordinary income that would have been recognized on the contributed portion had the property been sold). The reduced contribution of \$101,500 consists of \$52,500 [\$75,000 \times 70%] of adjusted basis allocated to the contributed portion of the property and \$49,000 [\$70,000 \times 70%] of long-term capital gain allocated to the contributed portion. Under sections 1012 and 1015(a) the basis of the property to the church is \$127,500 (\$75,000+\$52,500).

(e) *Effective date.* This section applies only to contributions paid after December 31, 1969, except that, in the case of a charitable contribution of a letter, memorandum, or property similar to a

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letter or memorandum, it applies to contributions paid after July 25, 1969.

[T.D. 7207, 37 FR 20776, Oct. 4, 1972; 37 FR 22982, Oct. 27, 1972, as amended by T.D. 7728, 45 FR 72650, Nov. 3, 1980; T.D. 7807, 47 FR 4510, Feb. 1, 1982; T.D. 8176, 53 FR 5569, Feb. 25, 1988; T.D. 8540, 59 FR 30102, June 10, 1994]

§ 1.170A-4A Special rule for the deduction of certain charitable contributions of inventory and other property.

(a) *Introduction.* Section 170(e)(3) provides a special rule for the deduction of certain qualified contributions of inventory and certain other property. To be treated as a “qualified contribution”, a contribution must meet the restrictions and requirements of section 170(e)(3)(A) and paragraph (b) of this section. Paragraph (b)(1) of this section describes the corporations whose contributions may be subject to this section, the exempt organizations to which these contributions may be made, and the kinds of property which may be contributed. Under paragraph (b)(2) of this section, the use of the property must be related to the purpose or function constituting the ground for the exemption of the organization to which the contribution is made. Also, the property must be used for the care of the ill, needy, or infants. Under paragraph (b)(3) of this section, the recipient organization may not, except as there provided, require or receive in exchange money, property, or services for the transfer or use of property contributed under section 170(e)(3). Under paragraph (b)(4) of this section, the recipient organization must provide the contributing taxpayer with a written statement representing that the organization intends to comply with the restrictions set forth in paragraph (b) (2) and (3) of this section on the use and transfer of the property. Under paragraph (b)(5) of this section, the contributed property must conform to any applicable provisions of the Federal Food, Drug, and Cosmetic Act (as amended), and the regulations thereunder, at the date of contribution and for the immediately preceding 180 days. Paragraph (c) of this section provides the rules for determining the amount of reduction of the charitable contribution under section 170(e)(3). In

general, the amount of the reduction is equal to one-half of the amount of gain (other than gain described in paragraph (d) of this section) which would not have been long-term capital gain if the property had been sold by the donor-taxpayer at fair market value at the date of contribution. If, after this reduction, the amount of the deduction would be more than twice the basis of the contributed property, the amount of the deduction is accordingly further reduced under paragraph (c)(1) of this section. The basis of contributed property which is inventory is determined under paragraph (c)(2) of this section, and the donor’s cost of goods sold for the year of contribution must be adjusted under paragraph (c)(3) of this section. Under paragraph (d) of this section, a deduction is not allowed for any amount which, if the property had been sold by the donor-taxpayer, would have been gain to which the recapture provisions of section 617, 1245, 1250, 1251, or 1252 would have applied. For purposes of section 170(e)(3) the rules of § 1.170A-4 apply where not inconsistent with the rules of this section.

(b) *Qualified contributions—(1) In general.* A contribution of property qualifies under section 170(e)(3) of this section only if it is a charitable contribution:

(i) By a corporation, other than a corporation which is an electing small business corporation within the meaning of section 1371(b);

(ii) To an organization described in section 501(c)(3) and exempt under section 501(a), other than a private foundation, as defined in section 509(a), which is not an operating foundation, as defined in section 4942(j)(e);

(iii) Of property described in section 1221 (1) or (2);

(iv) Which contribution meets the restrictions and requirements of paragraph (b) (2) through (5) of this section.

(2) *Restrictions on use of contributed property.* In order for the contribution to qualify under this section, the contributed property is subject to the following restrictions in use. If the transferred property is used or transferred by the donee organization (or by any subsequent transferee that furnished to the donee organization the written statement described in paragraph