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From: [redacted]
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To: [redacted]
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Subject: Charitable Donation of a large number of items

You have presented us with a scenario in which the taxpayer claims a charitable contribution deduction for a gift of large number of items.

Donor Treated as a Dealer

Under section 170(e)(1), the amount of any charitable contribution of property is reduced by the amount of gain that would not be long-term capital gain if the property were sold at its fair market value. In other words, if the contribution were a sale that would have resulted in ordinary income (such as the sale of property held by the donor primarily for sale to customers in the ordinary course of his trade or business), then the amount of the deductible charitable contribution would be generally limited to the LESSER of the donor's basis, or fair market value. See Treas. Reg. sec. 1.170A-4(a).

In Rev. Rul. 79-256, 1979-2 C.B. 105, Situation 2, the taxpayer, who was not an art dealer, purchased a substantial part of the total limited edition of a lithographic print for a total price of $25x. After holding the prints for more than one year, she donated the prints to art museums. The fair market value at the time of contribution was $100x. The Service concludes that the taxpayer's "bulk acquisition and subsequent disposal of the prints" are substantially equivalent to the activities of a commercial art dealer, and therefore the prints are treated as ordinary income property. Further, the contribution was not made after a period of accumulation and enjoyment by the donor. Thus, the Service concludes, the amount of the taxpayer's charitable contribution must be reduced by the hypothetical ordinary income gain, and the contribution is limited to the taxpayer's cost. See also G.C.M. 37611 (July 25, 1978).

In Rev. Rul. 79-419, 1979-2 C.B. 107, the taxpayer, who was not a dealer in books, purchased 100 books through a promoter at a volume discount, stored them for just over 12 months, and then donated them to various charities. The Service concludes that the taxpayer's activity in this case is "tantamount to the activity of a dealer selling books", and the books are treated as ordinary income property. Thus, if the fair market value is more than the taxpayer's basis in the books, the amount of the charitable contribution deduction must be reduced by the theoretical ordinary income gain on the property. Furthermore, if the fair market value is equal to or less than the taxpayer's basis, the amount of the charitable deduction is limited to that lesser amount.

In Pasqualini v. Commissioner, 103 T.C. 1 (1994), the Tax Court declined to apply these two revenue rulings, noting that application of the factors in determining whether the taxpayers' activities are substantially equivalent to the activities of a dealer are "inherently factual".

Fair Market Value - May Take into Account Bulk Sales

Generally, under section 1.170A-1(c)(1) of the regulations, the amount of a charitable contribution of property is the fair market value of the property at the time of the contribution, reduced as provided in section 170(e)(1) of the Code. Section 1.170A-1(c)(2) defines fair market value as the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.

In Skripak v. Commissioner, 84 T.C. 285 (1985), the taxpayers purchased approximately 150,000 books at a substantial discount, held them for the long-term capital gain holding period, then donated them to various libraries. The Court noted that the regulations under section 170 do not specify whether a wholesale or retail market is to be used, but found that the "sheer number of [donated] books . . . would require a substantial discount from the [list price]. The simultaneous marketing of all those books would substantially depress the market". Also, the Court found that a willing, knowledgeable buyer would demand and receive a substantial discount for the purchase of any of the excess inventory, particularly in the quantities donated to the various libraries. The Court concluded that the taxpayers' purchase of the books was an arm's-length transaction, and the fair market value of the books was no more than 20% of the catalog list price.

In Rimmer v. Commissioner, T.C. Memo. 1995-215, the taxpayer, who was not a dealer in sheet music, purchased approximately 85,000 pieces of Yiddish and Hebrew sheet music for $10,000 and subsequently contributed nearly all of the sheet music to a section 170(c) organization. The taxpayer obtained an appraisal for his donation, valuing it at $220,120. The Court found that the existing market for this sheet music was small, and concluded that "the addition of 85,000 pieces of sheet music on the public market either would depress the market for each title or, perhaps more likely, would result in many copies being unsalable for a considerable period of time." Thus, the Court concluded that a discount in the nature of a discount to reflect blockage was appropriate. Compare Rev. Rul. 80-69, 1980-1 C.B. 55, stating that the best evidence of fair market value depends on actual transactions, and the price at which a promoter sold gems to a taxpayer who subsequently donated the gems may be the best evidence of the maximum fair market value of the gems.

In Rev. Rul. 80-233, 1980-2 C.B. 69, the taxpayer purchased 500 copies of the Bible for $100x from a promoter who advised that $100x was a considerable discount from retail price. The promoter stored the Bibles for the taxpayer for 13 months, and at the taxpayer's direction, mailed the Bibles to a charity selected by the taxpayer. At the time the taxpayer contributed the Bibles to the charity, wholesale dealers were selling similar lots of Bibles to members of the general public at $100x. The Service holds that to determine fair market value, reference is made to the most active and comparable marketplace at the time of the donor's contribution. Thus, the fair market value of the Bibles is $100x, the price at which the Bibles were sold to the taxpayer and were still being sold to others.