

# Should Your Congregation Establish a Special Endowment Fund to Enable Donors to Reap Unprecedented Tax Benefits?

*by Craig M. Johnson, CPA, Fargo*

The 2007 and 2011 North Dakota Legislatures have passed legislation which allows a significant income tax credit for certain gifts to “permanent, irrevocable” endowment funds of qualified North Dakota charitable organizations (including religious organizations). This legislation pertains to certain “business” gifts made in a taxable year beginning after December 31, 2006 and also to certain gifts made by **individuals and “businesses”** made in taxable years beginning after 2010. **Qualified donors will likely find that well over 50% of their gifts will be “subsidized” through State and Federal tax incentives!**

The purpose of an endowment fund is to provide ongoing financial support in furtherance of the mission of your congregation. The operating policies of a **qualified** endowment fund allow for only very limited distributions from the donors’ gift contributions (principal). The income and net appreciation (and a portion of principal in certain situations) from the fund’s invested assets may be used to support the mission of the charitable organization. **Since many congregations have endowment funds which allow for major invasions of principal through a congregational vote, such existing funds would not be qualified for purposes of this tax credit. In such case, another special fund would have to be established to be in compliance with the legislation.**

## Eligible “Business” Donors

Gifts from the following entities may benefit from this tax legislation:

1. “C” corporations (pay tax at the corporate level)
2. “Pass-through” entities (tax credit usually claimed by owners)
  - a. Subchapter “S” corporations
  - b. Partnerships
  - c. Limited liability companies
3. Estates (if file income tax return)
4. Trusts

The tax credit for gifts from estates and trusts will be allocated between these entities and their beneficiaries based on the portion of income which is distributed to those beneficiaries.

## How the Tax Credit Works for “Business Gifts”

An income tax credit is far more valuable than a deduction since a credit offsets the computed income tax. This particular tax credit is claimed on the North Dakota income tax return. The amount of the credit is 40% of the value of a gift made to a qualified (permanent, irrevocable) endowment fund of a ND nonprofit organization, provided that the gift is deductible for Federal tax purposes. The tax credit allowed in any one year may not exceed the current year tax liability; unused credits may be carried forward for up to three additional tax years.

The annual limitation on this tax credit is \$10,000, determined at the entity level. Therefore, eligible gifts totaling up to \$25,000 per year will bring about the maximum annual credit.

## Big News - Tax Credit Now Applies to Individual Donors

The 2011 legislation allows a 40% tax credit for gifts by individuals to a qualified endowment fund held by a qualifying North Dakota non-profit organization (including religious organizations). If an individual makes a

gift(s) to such an endowment fund, **the aggregate of the year's gifts to a particular fund must be \$5,000 or more.** The maximum credits that may be claimed under this subsection are \$10,000 (\$25,000 in gifts) for an individual or \$20,000 (\$50,000 in gifts) for married individuals filing jointly.

### **Example of Tax Benefit to Individual Taxpayer**

*Mrs. Smith, a North Dakota resident, donates \$20,000 in cash to a qualified endowment fund. She receives an \$8,000 tax credit (40%) on her ND return. If she is in the 28% Federal tax bracket, her Federal tax savings are \$3,360 (28% of \$12,000; \$12,000 is the difference between the \$20,000 charitable deduction offset by an \$8,000 reduction in the state income tax deduction). **The "cost" of her \$20,000 gift is offset by \$11,360 in tax savings (56.8% of the gift amount).***

### **Call to Action for Eastern North Dakota Congregations, Donors and Advisors**

It is important to realize that the 40% tax credit is a direct reduction of the previously – computed tax. Therefore, the tax benefit in North Dakota is usually far in excess of the Federal tax savings! Because of this unprecedented tax “subsidy”, congregations should seriously consider establishing a qualified endowment fund(s). The Eastern ND Synod has established such a fund as we work to sustain rural ministries and quality pastoral leadership. Several congregations in our Synod have also established the above-described qualified endowment fund.

If there is a decision to move forward, I suggest that congregations work with professional counsel to prepare appropriate documents so that your fund's governing documents allow it to qualify as a **“permanent, irrevocable fund”** as required by this law. It is critical that your fund is operated as a “true endowment” rather than a “quasi endowment” fund in order that the favorable tax benefits can be achieved.

Once the fund has been properly established, donor benefits should be communicated through personal contacts, brochures, web sites, seminars and the like.

*The author of this article is a charitable giving consultant residing in Fargo. Craig is “of counsel” to our Synod. For questions regarding this article and the steps for moving forward, he can be reached at: 701-799-1108 or by e-mail at: [cmjohnson@hotmail.com](mailto:cmjohnson@hotmail.com)*

**Disclaimer:** *The above article is intended to provide information of a general nature only. It should not be construed as legal, tax and/ financial advice. Readers are urged to consult their own professional advisors for their specific situations.*