BURNING DOWN THE HOUSE AND THE CHARITABLE DEDUCTION

*Rodney P. Mock**

ABSTRACT 354
I. INTRODUCTION 354
II. *SCHARF* POSTURED ALONE AMONG THE RUBBLE 355
III. THE QUID PRO QUO DEBACLE 367
IV. FROM ZERO TO FAIR MARKET VALUE 379
V. CONCLUSION 392

* Rodney P. Mock, J.D., LL.M, California Polytechnic State University, Associate Professor, Business Building (03), Office No. 03 - 424, Telephone No. (805) 756 - 2730, Email: rmock@calpoly.edu. This article was submitted for publication in March 2010.

ABSTRACT

This article reviews the legal issue of whether or not a charitable deduction should be allowed under section 170(a)(1) with respect to buildings donated to local fire departments to conduct controlled burns. The article questions whether the incidental benefit doctrine set forth in the U.S. Tax Court case of *Scharf* still stands under such circumstances in light of the two-part "gift" test adopted by Rev. Rul. 67-246, the Supreme Court case of *American Bar Endowment,* and as promulgated in Treas. Reg. § 1.170A-1(h)(1). The article also reviews the ancillary issues associated with the deduction under the substantiation rules of Treas. Reg. § 1.170A-13(c)(2)(i), the demolition expense disallowance of section 280B, and the Service's recent assertion of the partial interest rule under section 170(f)(3).

I. INTRODUCTION

The Internal Revenue Service (IRS) is heating up its audits of adventuresome taxpayers claiming a charitable deduction based on donations to fire departments for training personnel and testing equipment.[1] From the smoldering ashes of such questionable "charitable contributions" springs an arsenal of unsettled taxpayer issues. The first issue, arguably the most fundamental, involves whether the deduction should be allowed under § 170(a)(1).[2] In confronting the aforementioned, this article examines, among other things, the incidental benefit doctrine and the evolution of the charitable gift test as it relates to quid pro quo exchanges. This test is judicially and administratively evolving from a subjective test, focusing on taxpayer motivation, to a more objective structural analysis of the external features of the exchange transaction.[3] As such, this article questions whether the U.S. Tax Court case of *Scharf v. Commissioner*[4] continues to stand as substantial authority supporting the charitable deduction, particularly after a recent

---

1. Meghan Barr, *Deduction is a Burning Issue*, SFGate, October 4, 2009, http://articles.sfgate.com/2009-10-04/business/17184215_1_fire-department-fire-training-burns.

2. I.R.C. § 170(a)(1) (2006) ("There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary.").

3. Hernandez v. Comm'r, 490 U.S. 680, 690-91 (1989).

4. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247 (1973).

case denied the deduction to taxpayers in similar circumstances.[5] This article concludes by contending taxpayers must now comply with the substantiation rules of the regulations and be prepared for possible attack by the Service, possible demolition loss and expense disallowance under § 280B, and charitable deduction disallowance under the partial interest rule of § 170(f)(3). Moreover, recent cases highlight the possibility that future taxpayers will find it difficult to demonstrate that the value of the donated structure to the fire department has any significant value.

II. *SCHARF* POSTURED ALONE AMONG THE RUBBLE

Before embarking down the taxpayer-excursion-turned-cinder-hot as a result of a fire department burning down one's residence (or any other taxpayer building), prudent tax practitioners in the planning stage must wrestle with the general dearth of legal authority supporting such an exotic application of the charitable deduction. Section 170(a)(1) generally permits deductions for "charitable contributions" as defined in subsection (c).[6] Subsection (c) defines "charitable contributions" as a *contribution or gift* to or for the use of, "[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."[7]

---

5. *See* Rolfs v. Comm'r, 135 T.C. 271 (2010).

6. I.R.C. § 170(a)(1) ("There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary.").

7. *Id.* § 170(c) ("For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of - (1) 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. (2) A corporation, trust, or community chest, fund, or foundation – (A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State, the District of Columbia, or any possession of the United States; (B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals; (C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and (D) which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office. A contribution or gift by a corporation to a trust, chest, fund, or foundation shall be deductible by reason of this paragraph only if it is to be used within the United States or any of its possessions

In the past, taxpayers were particularly concerned about the issue of whether or not contributions to a "volunteer" fire department fell within the purview of § 170(c)(1).[8] Taxpayers successfully argued in the U.S. Tax Court (and before the IRS) that unincorporated volunteer fire departments relieved their associated "political subdivisions" of a function they normally would perform — namely fighting fires — and therefore, any contributions to such organizations should rightfully be construed as if directly contributed to the corresponding political subdivision.[9] Contributions to "incorporated" volunteer fire departments are now deductible under § 170(c)(2), so long as the statutory requirements are satisfied (i.e., organized exclusively for charitable purposes, no part of the net earnings inure to a private shareholder or individual, and the organization is not disqualified from section 501(c)(3) status by reason of attempting to influence legislation).[10] The donee charitable organization's

---

exclusively for purposes specified in subparagraph (B). Rules similar to the rules of section 501(j) shall apply for purposes of this paragraph.").

8. *See, e.g.*, *Scharf*, 32 T.C.M. at 1248 (taking up the issue).

9. *See* Sheldon v. Comm'r, 6 T.C. 510, 519 (1946) (holding that the taxpayers' "contribution [of cash] to the Jamestown Fire Department Association should be allowed as a charitable contribution under section 23(o)(2)" of the Internal Revenue Code of 1939); McKenna v. Comm'r, 5 T.C. 712, 713-14 (1945), *acq.*, 1974-2 C.B. 1 (holding that contributions to "unincorporated associations of individuals organized and operated for the prevention of fires and the protection of life and property from loss by fire and other disasters in the municipalities where they are located" are deductible under § 23(o)(1) of the Internal Revenue Code of 1939 as contributions for the use a political subdivision or exclusive public purposes); Smith v. Comm'r, 8 T.C.M. (CCH) 1086, 1088 (1949) (following *McKenna v. Comm'r* by permitting a deduction pertaining to the conveyance of a lot to an independent fire company); Rev. Rul. 80-77, 1980-1 C.B. 56 (permitting charitable deduction under section 170 for contribution of money to volunteer fire department's annual fund drive); Rev. Rul. 71-47, 1971-1 C.B. 92-93 ("In the cases of *McKenna v. Comm'r*, 5 T.C. 712 (1945), and *Sheldon v. Comm'r*, 6 T.C. 510 (1946), the court held that contributions to a volunteer fire department are deductible under section 23(o)(1) of the Internal Revenue Code of 1939 (now section 170(c)(1) of the 1954 Code) on the alternative ground that contributions to a volunteer fire department relieve a political subdivision of a State of the burden of a function normally performed by the political subdivision . . . . Accordingly, contributions or gifts to nonprofit organizations of volunteer firemen are deemed to be for the use of a political subdivision of a State for exclusively public purposes and, therefore, are deductible under section 170(c)(1) of the Code.").

10. Rev. Rul. 74-361, 1974-2 C.B. 160 ("The organization is operated exclusively for charitable purposes and, accordingly, it is exempt from Federal income tax under section 501(c)(3) of the Code. . . . Rev. Rul. 71-47, 1971-1 C.B. 92, which holds that contributions or gifts to nonprofit volunteer fire companies are deemed to be for the use of a political subdivision of a State for exclusively public purposes and are deductible under section 170(c)(1) of the Code, is clarified to remove any implication that contributions to a volunteer fire company organized in the United States and described in section 501(c)(3) would not be deductible under section 170(c)(2).").

volunteer status is thereby no longer an issue.[11] If allowed, a deduction may be claimed by the donor under § 170(c)(1) or (2), depending on the type of fire department involved.[12]

The more critical issue remaining is whether or not such contributions constitute a "contribution or gift" to the charitable organization to begin with. Section 170 and its extensive set of accompanying regulations make no mention of the proper tax treatment for a contribution of a building to a local fire department (volunteer or otherwise) for the purposes of conducting "live burns" to train fire personnel, test new equipment, etc. In other words, it is one thing to contribute cash or real or personal property outright to a charitable organization. However, a taxpayer contributing a building or land improvements, but not the underlying land itself, is another matter.[13]

Nevertheless, a number of taxpayers in several states over the years, including the well-known ESPN football analyst Kirk Herbstreit, have been doing just that in an elaborate effort to obtain the golden egg deduction.[14] From the landowner's perspective, allowing a fire department to burn down an existing structure saves substantial demolition costs, which are normally non-deductible under § 280B, and which would have to be added to the basis of the land.[15] Of course, "land apart from the improvements or physical development added to it" is non-depreciable.[16] Taxpayers also argue that such "generous" taxpayer contributions allow local fire departments to conduct live burn training scenarios they could not otherwise conduct,

---

11. *See id.* ("Thus, under the circumstances, this organization's provision of recreational facilities for members does not disclose an independent social purpose, but rather is in furtherance of its charitable purpose.").

12. I.R.C. § 170(c)(1)-(2); *see also* Rev. Rul. 74-361, 1974-2 C.B. 160.

13. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247 (1973).

14. Meghan Barr, *A Home Donation Flare-Up*, HOUSTON CHRONICLE, Sept. 26, 2009, *available at* http://www.chron.com/disp/story.mpl/ nation/6638041.html ("A home donated by ESPN college football commentator Kirk Herbstreit was intentionally burned during a training exercise by the Upper Arlington, Ohio, Fire Department. Herbstreit's claim of a $330,000 tax deduction was rejected a year later.").

15. I.R.C. § 280B ("In the case of the demolition of any structure - **(1)** no deduction otherwise allowable under this chapter shall be allowed to the owner or lessee of such structure for - (A) any amount expended for such demolition, or (B) any loss sustained on account of such demolition; and **(2)** amounts described in paragraph (1) shall be treated as properly chargeable to capital account with respect to the land on which the demolished structure was located.").

16. Treas. Reg. § 1.167(a)-2 (1960) ("The depreciation allowance in the case of tangible property applies only to that part of the property which is subject to wear and tear, to decay or decline from natural causes, to exhaustion, and to obsolescence.").

and if all works out, the donor receives a substantial tax benefit.[17]

To the dismay of taxpayers, there is not exactly a buffet of legal authorities squarely on point permitting such an extravagant use of the charitable deduction. The exclusive authority that stands alone in support of said proposition is *Scharf v. Commissioner*.[18] This case involved taxpayer deficiencies for joint income tax returns Morris and Francis Scharf filed for the tax years 1968 and 1969.[19] In 1949, the Scharfs purchased a parcel of land with a building situated thereon for $15,000.[20] Of that amount, $13,500 was allocated to the cost basis of the building, and the remaining $1,500 was allocated to the cost basis of the land.[21] Over a number of years, the Scharfs leased the property out to various tenants until a fire partially destroyed the building in 1967.[22] The Scharfs received insurance proceeds in 1968 totaling $5,914.05.[23] The building, however, was so damaged that it could not be leased without substantial improvements.[24] As a result, the city scheduled the building for condemnation.[25] With land values rising significantly in the area, the land itself had become far more profitable to simply rebuild on versus restoring the existing 40-year old structure to a suitable condition.[26]

Faced with such an economic conundrum, a neurological lever of pure taxpayer ingenuity must have been pulled: burn that baby, retain the land (which would have increased in market value), and take a charitable deduction under section 170(a)(1) of the Internal Revenue Code of 1954.[27] The opinion does not identify the exact moment when the intent to take the charitable tax deduction was formed. Instead, after "encouragement of municipal authorities," and the 1968 condemnation

---

17. *See Scharf*, 32 T.C.M. at 1251.
18. *See id.* at 1251-52.
19. *Scharf*, 32 T.C.M. at 1248.
20. *Id.*
21. *Id.*
22. *Id.* at 1248-49.
23. *Id.*
24. *Id.* at 1249.
25. *Id.*
26. *Id.* ("The Margolin building was so badly damaged by the fire in 1967 that it could not be rented without substantial renovation. By early 1968 the building was about to be condemned because of its unsafe condition. In addition, steadily rising land values in that area had made the land far more valuable than the damaged building, and the petitioner decided it would not be economically feasible to restore the existing building.").
27. Treas. Reg. § 1.170-1 (as amended in 1972) (before amendment by Tax Reform Act of 1969).

determination, the Scharfs arranged for a volunteer fire department to use the building to conduct drills, test new equipment, and ultimately burn the building completely to the ground.[28] Mr. Scharf testified that in the past he had donated similar old buildings to volunteer fire departments.[29] Furthermore, a taxpayer's motivation to receive the "tax benefit" of a charitable deduction (i.e., the tax savings) is not a fatal error in the charitable gift determination. Otherwise, all charitable contributions would fall victim to disallowance, except in the case of oblivious taxpayers.[30]

Shortly after the contribution, the fire department razed the building, and the Scharfs claimed on their 1968 joint return a charitable deduction equal to the value of the fire-damaged building donated.[31] It is also worth noting that the transfer of the building to the fire department was not represented by a deed or any other formal conveyance documents.[32] On three separate occasions, however, the fire department requested the Scharfs' advanced consent before a live burn.[33]

At trial, the Service's position was simple: the Scharfs were not entitled to a charitable deduction because, faced with impending condemnation, they had no motivation whatsoever to rebuild.[34] Therefore, they donated it to the fire department with

---

28. *Scharf*, 32 T.C.M. at 1249 ("With the encouragement of municipal authorities, the petitioner arranged for the Mahwah Volunteer Fire Department to use the building to conduct fire drills and test the use of its new fire equipment. During three ensuing fire drills conducted by the fire department with petitioner's consent, the Margolin building was completely burned down. After the fire there was debris around the building which petitioner covered and filled in. He also had the rest of the foundation and the chimney pushed over to avoid injury to persons nearby.").

29. *Id.* at 1251.

30. Sheppard v. United States, 361 F.2d 972, 981-82 (Ct. Cl. 1966) ("The court is not unmindful of the tax benefits which flow from affording full recognition to the plaintiff's admittedly tax-motivated transactions in this case. Such motivation demands special analysis and scrutiny, but its presence is essentially immaterial except as an eye-opening mechanism or interpreter of equivocal conduct. It will not negative the effect of transactions which have really occurred.").

31. *Scharf*, 32 T.C.M. at 1249 ("On their 1968 Federal income tax return the petitioners claimed a deduction for a charitable contribution of $13,131.65 for the value of the fire-damaged building donated to the volunteer fire department. Respondent disallowed the claimed charitable deduction in its entirety. By an amendment to their petition filed February 15, 1973, the petitioners alleged that the value of their charitable contribution is $28,500 rather than the $13,131.65 originally claimed on their Federal income tax return for 1968, and that they are entitled to an increased charitable contribution carryover to 1969 and subsequent years.").

32. *Id.* ("The Margolin building was given by the petitioner to the fire department partly for the purpose of having it burned down. The transfer was not evidenced by any deed or other formal conveyance.").

33. *See id.*

34. *See id.*

an "expectation" of free demolition which, coincidently, would increase the value of their land.[35] Stated more precisely, the Service unsuccessfully argued that there was not a "contribution or gift" to the charitable organization within the meaning of § 170(c) because the taxpayers expected an economic return benefit from the fire department — namely, a clearer track of land.[36] In its argument alleging a gift was not made, the Service used a trio of judicial precedent in an effort to define what constitutes a "gift" for charitable deduction purposes.[37] Lacking any specific judicial or statutory guidance, the Supreme Court, in 1960, took an initial stab at developing a judicial test to define the illusive term "gift."[38] Although not set in a charitable deduction context, *Duberstein* involved the income tax issue of whether a Cadillac received by a taxpayer, at no cost from a business associate, constituted a gift excluded from income under § 22(b)(3) of the Internal Revenue Code of 1939 or whether such was compensation includable in gross income.[39] In its holding, the court stated that a gift is made out of "detached and disinterested generosity . . . out of affection, respect, admiration, charity or like impulses," and that the transferor's intention or motivation behind the transfer is thereby controlling.[40] Hence, the Supreme Court's *Duberstein* gift test was born.

The U.S. Tax Court cited the *Duberstein* test numerous times in the context of charitable deduction cases and thus tied the knot with respect to its application to the charitable deduction.[41] On the other hand, there were also a series of other

---

35. *See id.* at 1251 ("Respondent contends that the arrangement whereby petitioner permitted the Mahwah Volunteer Fire Department to conduct fire drills on the Margolin building does not qualify as a charitable contribution within the intendment of section 170. He argues that when faced with the impending condemnation of the building, the petitioner had no desire to rebuild and therefore donated it with the expectation that its demolition would increase the value of the land and make the property easier to convert to a more productive use.").

36. *See* I.R.C. § 170(c) (2006). Not defined in § 170 (or its counterpart regulations), the terms "contribution" and "gift" have been used synonymously by the courts. *See, e.g.*, Channing v. United States, 4 F. Supp. 33, 34 (D. Mass. 1933), *aff'd*, 67 F.2d 986 (1st Cir. 1983); Sutton v. Comm'r, 57 T.C. 239, 242 (1971).

37. *See* Comm'r v. Duberstein, 363 U.S. 278, 285-86 (1960); *Sutton*, 57 T.C. at 242-43; Singer Co. v. United States, 449 F.2d 413, 414 (Ct. Cl. 1971).

38. *See Duberstein*, 363 U.S. at 285-86.

39. *See id.* at 280-81.

40. *Id.* at 285–86.

41. *See, e.g.*, Howard v. Comm'r, 39 T.C. 833, 838 (1963) ("There is considerably more evidence on the subject and the record as a whole clearly shows that the three payments in question were not charitable gifts, proceeding from a 'detached and disinterested generosity' or 'out of affection, respect, admiration, charity or like impulses' but instead proceeded from 'the incentive of anticipated benefit.'"); Dejong v. Comm'r, 36 T.C. 896, 899 (1961), *aff'd*, 309 F.2d 373 (9th Cir. 1962) ("A gift is generally defined as a

court cases which did not consistently follow the landmark "detached and disinterested generosity" standard.[42]

In 1971, the U.S. Tax Court settled the case of *Sutton v. Commissioner*.[43] *Sutton* involved husband and wife taxpayers who conveyed a strip of land to the City of Westminister, California, for use in widening the street adjoining their property.[44] Widening the street permitted the Suttons' retained land to be zoned for commercial, industrial and multiple-residential uses.[45] The Suttons claimed a charitable deduction

---

voluntary transfer of property by the owner to another without consideration therefor. If a payment proceeds primarily from the incentive of anticipated benefit to the payor beyond the satisfaction which flows from the performance of a generous act, it is not a gift."); Ruddel v. Comm'r, 71 T.C.M. (CCH) 2419, 2421 (1996) ("The term 'gift' does not include payments that proceed primarily from a legal duty or moral obligation imposed on the donor, or from the inducement of some anticipated benefit (beyond the incidental enjoyment which flows from performing a generous act)"); Williamson v. Comm'r, 62 T.C.M.(CCH) 610, 613 (1991) ("The Supreme Court has described the nature of a 'gift' as proceeding from 'detached and disinterested generosity'; something given 'out of affection, respect, admiration, charity, or like impulses'. . . . Therefore, petitioner must prove that he transferred the moneys to the Temple with 'detached and disinterested generosity' and not with 'the incentive of anticipated benefit.'").

42. *See, e.g.*, United States v. Transamerica Corp., 392 F.2d 522, 524 (9th Cir. 1968) ("This language was drawn from Commissioner of Internal Revenue v. Duberstein, 363 U.S. 278, 80 S. Ct. 1190, 4 L. Ed. 2d 1218 (1960), which dealt not with charitable contributions but with the exclusion of a gift from income of the recipient under section 102 of the Internal Revenue Code. In *DeJong* this court held that the *Duberstein* criteria are applicable to a charitable deduction under section 170. *DeJong* involved an individual taxpayer, as to whom the quoted language is a not inappropriate way of phrasing the converse of a purpose to gain a direct economic benefit. It does not seem appropriate, however, to demand of a corporate entity such impulses as affection, respect or admiration. Further, an absolute requirement of detached and disinterested generosity or lack of any business purpose would tend to render *ultra vires* substantially all charitable contributions and thus to frustrate the congressional intent that corporations should enjoy such deductions."); Crosby Valve & Gauge Co. v. Comm'r, 380 F.2d 146, 147 (1st Cir. 1967) ("While the law recognizes gifts to individuals and organizations other than charities, it does not so positively encourage them. And, particularly when the transfer of property without consideration is made beyond a family setting and in a business atmosphere, it is properly subjected to a searching inquiry as to the real motivation of the transferor. But in the case of a contribution to a charitable organization, the law's policy finds charity in the purposes and works of the qualifying organization, not in the subjective intent of the contributor.").

43. Sutton v. Comm'r, 57 T.C. 239, 239 (1971).

44. *Id.* at 240 ("In 1965, the City of Westminster had a master plan for the development of streets in the area of Sutton's property. This plan called for the eventual widening of Golden West Street to a width of 100 feet (50 feet each side of the center of the street). At that time Golden West Street was 60 feet in width (30 feet each side of center). In 1965 and 1966, Westminster did not have funds for the acquisition of land by condemnation along the streets to be widened. The City, however, had adopted an ordinance prescribing standards for the width of streets and for improvements. This ordinance provides that no building may be constructed on land in designated zones if the land is to be used for commercial, industrial, or multiple-residential purposes, unless the abutting street is a prescribed width or the owner dedicates or offers to dedicate a right-of-way sufficient for widening the street to the prescribed width.").

45. *Id.*

for the commercial value of the strip of land dedicated to the city on their tax return.[46]

After reviewing a litany of cases involving charitable transfers to political subdivisions, the *Sutton* court held that the charitable deduction should be denied when a taxpayer's "primary incentive, motive, or purpose which prompted the transfers of property was to obtain a direct or indirect benefit in the form of enhancement in the value or utility of the taxpayer's remaining land or otherwise to benefit the taxpayer."[47] Further, the court stated that "[o]nly where the anticipated or potential economic benefit, if any, to the taxpayer was not significant, or was only 'incidental' to an important public-spirited, altruistic, or charitable benevolence, has the court allowed the claimed charitable contribution."[48] Hence, the newly formed sprouts of the "incidental benefit doctrine" were born. However, unfortunately for the Suttons, having found that the benefit received was substantial (i.e., not incidental), the court disallowed the deduction.[49]

The U.S. Court of Claims case *Singer v. United States* involved the sewing machine manufacturer The Singer Company ("Singer").[50] Singer sold a number of sewing machines to local schools and various other charitable organizations in 1954.[51] Singer discounted the sewing machines 45% from the manufacturer's published list price, resulting in breakeven prices for the company with no resulting loss or profit.[52] As a response to a Service audit of the company's 1954 consolidated return, Singer filed a claim for a refund in that year, alleging that the

---

46. *See id.* at 242.

47. *Id.* at 244 ("We do not think the grant of the easement can be regarded as a 'charitable contribution.' Sutton has shown no public-spirited, altruistic, benevolent, or charitable purpose which he sought to serve through granting the easement . . . we think it clear that Sutton's transfer was made in the expectation of the receipt of specific direct economic benefits in the form of additional utility and value which may be realized through the commercial development of the remainder of the land . . . Sutton was fully aware that such development was not possible without complying with the city ordinance on street widening. Although he was not compelled to make the transfer, and he testified that he had no immediate plans for the commercial development of his land, the widening of the street had the effect of making his land usable for commercial purposes at any time in the future if he so desires . . . . In light of all this evidence, we are convinced the transfer proceeded from the 'incentive of anticipated benefit of an economic nature.'").

48. *Id.* at 243.

49. *Id.* at 244.

50. *See* Singer Co. v. United States, 449 F.2d 413, 415 (Ct. Cl. 1971).

51. *Id.*

52. *Id.* at 416 ("These sales were made at breakeven prices and resulted in no overall immediate net profit or loss to plaintiff. As can be seen from the chart, the discount for the school group was 45 percent.").

discounted sales to the charitable organizations permitted the company to claim a charitable deduction in an amount equal to the discount.[53] Neither the court nor the Service took any issue with whether or not the schools were charitable organizations under § 170(c).[54] The central issue before the court was whether the below market sales to the schools were in fact gifts within the framework of § 170(c) of the Internal Revenue Code of 1954.[55]

The government in *Singer* contended that even though *Duberstein* was an income tax case, the court should follow the "detached and disinterested generosity" test for the purposes of its gift determination under § 170(c).[56] On the other hand, Singer argued that *Duberstein's* subjective test should not be used in a charitable contribution case, but rather that the court's construction of a gift should be governed exclusively by § 170 – particularly when applied to corporate contributions, which by their very nature do not evidence a "subjective" motivation.[57]

The court, turning slightly away from what it called the "old saw" *Duberstein* test, held,

> "[I]f the benefits received, or expected to be received, are substantial, and meaning by that, benefits greater than those that inure to the general public from transfers for charitable purposes (which benefits are merely *incidental* to the transfer), then in such case we feel the transferor has received, or expects to receive, a quid pro quo sufficient to remove the transfer from the realm of deductibility under section 170."[58]

---

53. *Id.*

54. *See id.* at 418.

55. *See id.* ("[T]he resolution of said issue depends then on considerations which involve the definition of a gift.").

56. *See id.* ("Said formulation was '[a] gift in the statutory sense, on the other hand, proceeds from a *'detached and disinterested generosity'* . . . . It is this language that later cases have used, not to define 'gift' for purposes of section 102(a), but for purposes of defining 'gift' as used in section 170(c). . . . This is also the definition of 'gift' that the defendant would have us follow in this case even though here we are dealing with section 170.").

57. *See id.* at 419 ("As an alternative to the subjective approach described above plaintiff argues that (1) the definition of 'gift' as used in *Duberstein, supra,* does not apply to 'gift' in a charitable contribution case and (2) that voluntary contributions are governed solely by I.R.C. section 170; and therefore contributions to charities should not be considered as business expense deductions under I.R.C. sections 162(a) and 162(b) unless there is a specific and direct *quid pro quo* flowing from the transfer.").

58. *Id.* at 423.

The court, in essence, followed the objective quid pro quo analysis of *Sutton* rather than the more subjective *Duberstein* test.[59]

Further, the court stated the sewing company's predominate reason for below market sales of sewing machines to local schools was to encourage those institutions to train and interest young women in the art of sewing, thereby enlarging their future market of prospective purchasers.[60] Because the company expected a substantial quid pro quo beneficial return from its discount sales (i.e., increased market share), the court denied the company's § 170(c) deduction in full for the local school sales.[61] Singer's motivation for leading the court away from *Duberstein*, and towards the more objective quid pro quo test, was so it could make the argument that its benefit derived was merely "indirect" and not "direct" and thereby therefore qualified the discounted sales to the local schools for the charitable deduction.[62] In applying the quid pro quo test, however, the court was unwilling to interpret the test so narrowly and constrict itself to an abstract indirect/direct donor benefit distinction.[63] Further, in denying the charitable deduction, the court also determined that the company could have deducted the below market sale contributions under § 162(a) as a business expense - if only the company would have taken such a return position.[64]

---

59. *Id.* ("With this standard, we feel that the subjective approach of 'disinterested generosity' need not be wrestled with. . . ."); *see also* Comm'r v. Duberstein, 363 U.S. 278, 288 (1960).

60. *Singer Co.*, 449 F.2d at 423-24 ("It is from this finding, together with careful scrutiny of other relevant facts, that we hold these discounts not to be of a charitable nature . . . we are convinced, as was our commissioner, that the plaintiff's predominant reason for granting such discounts was other than charitable . . . although allowing the discounts even with a total monopoly, 'would still be interested in increasing the size of that market by supporting the schools' efforts in teaching young women to sew.' . . . This expectation, even though perhaps not fully realized, provided a *quid pro quo* for those discounts which was substantial. We, therefore, deny the deduction for discounts to the school group.").

61. *Id.* at 424.

62. *Id.* at 422-23 ("Plaintiff does not disagree that the above described alternative to the 'disinterested generosity' test is relevant. It does, however, reduce that alternative to the rather narrow interpretation advocated in reference to section 162(b), *supra*. That is, plaintiff would have us decide the case by distinguishing between a *direct* or *indirect* benefit derived. In other words, plaintiff would say that if the transferor received, or expected to receive, benefits from a transfer to a charitable transferee, which benefits were to be received only *indirectly*, then regardless of the magnitude of those benefits, the transfer would still qualify as a charitable contribution deduction under section 170. However, if those same benefits were received, or expected to be received, *directly* from the transferee, plaintiff would concede that, given a substantial *quid pro quo*, the transfer would not come within the definition of a 'gift' or 'contribution' for purposes of deductibility under section 170. Obviously, we cannot agree with plaintiff's distinction.").

63. *See id.*

64. *See id.* at 421 ("By concluding as we do with reference to section 162(b) we, in effect, reject plaintiff's first argument that section 170 has *exclusive* control over all

In reviewing the above trio of cases, the *Scharf* court agreed with the Service's recitation of the gift test as it stood at the time (i.e., the *Duberstein* test, fogged over with the more objective quid pro quo test for donor/donee exchanges).[65] The court acknowledged that "the ascertainment of a donor's subjective intent is frequently difficult to determine," as if backing away from the "old saw" *Duberstein*.[66] The court continued, citing a series of cases where courts denied the charitable deduction because the quid pro quo flowing back to the donor exceeded the satisfaction flowing from the performance of the generous act to the general public.[67]

Drilling down in its analysis of *Sutton* and *Singer*, the *Scharf* court noted that there are certain exchanges in which the incidental or small benefit inuring to the donor in comparison to the greater public benefit should be ignored, and thus, should not destroy the charitable deduction right of the donor.[68] In applying the incidental benefit doctrine to the Scharfs' situation, the court concluded that "the benefit flowing back to petitioner, consisting of clearer land, was far less than the greater benefit flowing to the fire department training and equipment testing operations."[69] In addition, after the fire training was over, the Scharfs still had to remove remaining debris, the foundation, and chimney before they could successfully market the land.[70]

---

voluntary and gratuitous transfers to charities. In other words, we are of the opinion that if the transfer to a charitable organization does not qualify as a section 170 type deduction because it is made with expectations of financial return commensurate with the gift, it might be deductible under section 162(a), if all other requirements are met. This is the case even if the benefits expected do not flow *directly* from the transferee and even though the transfer was made without compulsion.").

65. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247, 1251 (1973) ("Respondent correctly states the tests developed by the *Duberstein, Sutton* and *Singer* cases in determining whether a
claimed charitable deduction will be allowed.").

66. *Id.* at 1252.

67. *Id.*

68. *Id.* ("In each of these above-cited cases the quid pro quo which flowed back to the donor did not disqualify the claimed charitable contribution deduction. Thus, where the primary benefit inures to the general public with only lesser and incidental benefits flowing back to the donor, then a charitable deduction will be allowed.").

69. *Id.* at 1252-53 ("The Margolin building, even after razing, still was not completely cleared from the land. Petitioner needed to remove the debris, demolish the foundation and chimney and cover the land before he could market the property. We think the petitioner benefited only incidentally from the demolition of the building and that the community was primarily benefited in its fire control and prevention operations. Consequently, on balance, we hold that the petitioner is entitled to a charitable contribution deduction.").

70. *Id.*

In ascertaining the exact amount of the deduction, the Service argued the deduction amount should be limited to the fair market value of the "use of" the building, which the Scharfs coincidently failed to establish.[71] In its fact-finding, the court determined that the fair market value of the fire damaged building, when donated for the purposes of the deduction, was $12,835.95.[72] The court calculated this sum amount by subtracting the value of the building for insurance loss purposes from the insurance proceeds actually received by the donor after the fire.[73] In weighing the Service's "donated use" valuation position over the taxpayers' "building value" position, the court concluded that they were both identical under the circumstances.[74] Phrased another way, the court gracefully sidestepped a short distance from a determinative decision on the more pressing valuation issue that could have been used in future fire department contribution cases.

After the *Scharf* decision, Chief Counsel for the IRS issued an Action on Decision recommending Service acquiesce concerning the incidental benefit doctrine, as applied in *Scharf.*[75] He also noted the court's finding that the right to destroy the building was of the same value as the building itself under the unique fact set of *Scharf.*[76] Before *Rolfs,* discussed in greater

---

71. *Id.* at 1253. ("Respondent contends that the petitioner donated only the use of the building rather than the building itself; and that the petitioner has failed to establish a marketable value for the privilege of using the building for fire drills.").

72. *Id.* ("Petitioner contends that the fair market value of the Margolin building when donated was $22,585.95. His selected figure is closely related to testimony regarding the reproduction cost for the Margolin building. Respondent claims these costs bear little, if any, relation to the actual fair market value of the building, which was poorly maintained and badly fire-damaged, when donated. We agree . . . . Using our best judgment, based upon careful consideration of all the evidence herein, we conclude, as reflected in our findings of fact, that the fair market value of the Margolin building when donated was $12,835.95. This amount represents the value ($18,750) of the building for insurance loss purposes less the amount ($5,914.05) of insurance proceeds recovered.").

73. *Id.*

74. *Id.* ("We need not choose here between the value of the donated use of the building and its fair market value in its damaged condition because in these circumstances we find they are the same.").

75. Scharf v. Comm'r, 32 T.C.M. (CCH) 1247 (1973), *action on dec.*, 1973-265 (March 20, 1974) ("The Court found as a fact that the benefits flowing back to petitioners, consisting of clearer land, were far less than the greater benefit flowing to the fire department and that petitioners benefited only incidentally. There was evidence in the record to support this factual finding and such finding is not clearly erroneous. In view of the Court's finding that the benefits received by petitioners were incidental, the mere fact that petitioners were benefited is not sufficient to deny the deduction . . . .").

76. *Id.* ("Respondent also argued that petitioners donated only the use of the building and that petitioners established neither the fair market value of the building nor the fair market value of its use. In effect, the Court held that under the circumstances of this case, donation of the right to destroy a building is the same as donation of the building itself. Such finding is correct.").

detail infra, one could only speculate on how the facts of *Scharf* would reconcile under the more evolved quid pro quo test for charitable deductions as advanced by the Service and the U.S. Supreme Court.

III. THE QUID PRO QUO DEBACLE

A more sophisticated inquiry into the development of *Scharf* in the context of donations to fire departments thus travels a bit deeper, beyond the opinion, and into an analysis of the gift test as applied to return donor benefit transactions (i.e., exchanges). The gift test applied to such reciprocal transactions has evolved significantly since the Cadillac days foregone of *Duberstein, Sutton* and *Singer*.[77] In fact, *Scharf* was arguably a minor instrumentality in both the judicial and administrative shift from the purely subjective *Duberstein* test towards the more objective quid pro quo test in such exchange transactions.[78]

In *Scharf*, the court mentioned *Duberstein* as a part of the gift test, made a passing reference to its subjective nature, and then applied a quid pro quo analysis, which included an incidental benefit exception thereto.[79] The subsequent Action on Decision took notice of the court's infirm approval of *Duberstein* and judicial leaning towards a quid pro quo test, stating that "the Service will no longer make this argument" in future cases.[80] Because the quid pro quo test, also referred to as the "dual payment rule," has also evolved since *Scharf* into a much more mechanical test, the *Scharf* holding has significantly weakened for those would-be modern day home burners.[81] Under the current state of the law, the quid pro quo test is much more exacting than the previous version of the test applied in *Scharf*.[82] For example, the valuation component of the modern dual payment rule, described infra, most likely will eliminate the

---

77. *See* Rev. Rul 67-246, 1967-2 C.B. 104 (dictating a two part test for quid pro quo charitable contributions).

78. *See id.*; *see generally Scharf*, 32 T.C. at 1252 (noting that the subjective intent of the donor is often very difficult to determine and lays out a more objective test for charitable donations based on the benefit to the public).

79. *See Scharf*, 32 T.C.M. at 1251-52.

80. *See* Singer Co. v. United States, 449 F.2d 413, 422-23 (Ct. Cl. 1971) ("Respondent argued that, for a donation of property to qualify as a charitable contribution, it must stem from 'detached and disinterested generosity,' citing Commissioner *v. Duberstein*, 363 U.S. 278, 80 S. Ct. 1190, 4 L. Ed. 2d 1218 (1960). Notwithstanding that the Court in dicta appeared to approve this position, the Service will no longer make this argument.").

81. *See generally* Rev. Rul. 67-246, 1967-2 C.B. 104.

82. *See Rolfs v. Comm'r*, 135 T.C. 271 (2010).

donor's charitable deduction in all but a few remaining scenarios.[83]

The current version of the quid pro quo rule for charitable exchange transactions sets forth a mechanical two-part gift test for the contributions.[84] Although issued several years prior to *Scharf,* the court made no mention of its existence in its opinion. Instead, following the reasoning of *Sutton* and *Singer*, the *Scharf* court determined the incidental benefit flowing back to the donors did not disqualify the deduction (i.e., because such was not substantial), and thus allowed the charitable deduction in full without any corresponding reduction for the incidental benefit received by the donors.[85] There are a number of "dual payment" examples where various charities received payments from taxpayers as admission sales or pursuant to other fund raising activities (e.g., gift solicitations) in exchange for various taxpayer privileges or benefits connected to the events.[86]

Further, the two-prong test is utilized by taxpayers and the Service in such dual payment transactions.[87] The valuation prong requires the taxpayer prove:

> the portion of the payment claimed as a gift represents the excess of the total amount paid over the value of the consideration received therefor. This may be established by evidence that the payment exceeds the fair market value of the privileges or other benefits received by the amount claimed to have been paid as a gift.[88]

---

83. *Id.*

84. Rev. Rul. 67-246, 1967-2 C.B. 104.

85. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247, 1252-53 (1973).

86. *See* Rev. Rul. 67-246, 1967-2 C.B. 107-11.

87. *Id.* at 105 ("As a general rule, where a transaction involving a payment is in the form of a purchase of an item of value, the presumption arises that no gift has been made for charitable contribution purposes, the presumption being that the payment in such case is the purchase price. Thus, where consideration in the form of admissions or other privileges or benefits is received in connection with payments by patrons of fund-raising affairs of the type in question, the presumption is that the payments are not gifts. In such case, therefore, if a charitable contribution deduction is claimed with respect to the payment, the burden is on the taxpayer to establish that the amount paid is not the purchase price of the privileges or benefits and that part of the payment, in fact, does qualify as a gift.").

88. *Id.* ("In showing that a gift has been made, an essential element is proof that the portion of the payment claimed as a gift represents the excess of the total amount paid over the value of the consideration received therefor. This may be established by evidence that the payment exceeds the fair market value of the privileges or other benefits received by the amount claimed to have been paid as a gift.").

The intent prong requires the taxpayer prove "that the payment in excess of the value received was made with the intention of making a gift."[89] If a charitable deduction is claimed in any quid pro quo exchange, the taxpayer bears the burden to satisfy both prongs of the test.[90]

In one example, a taxpayer paid $60 for two orchestra tickets when similar tickets sold for $10 each.[91] If the taxpayer could demonstrate similar tickets sold for such, and that the taxpayer intended to make a contribution of the excess, then the taxpayer could deduct $40.[92] In another example, a charity agreed to award a free transistor radio valued at $15 to each taxpayer who contributed $50 or more.[93] A taxpayer contributed $100 and received a radio in exchange.[94] The taxpayer was therefore entitled to a charitable deduction of $85.[95]

In 1986, the Supreme Court in *United States v. American Bar Endowment* officially adopted the gift test for such "dual character" contributions (i.e., part payment for goods or services/part charitable contribution).[96] *American Bar Endowment* involved taxpayers who were members of a tax-exempt association that provided certain insurance benefits for its members.[97] When the insurance costs were lower than the premiums paid by the charitable organization to third-party insurers, the charity received excess payment refunds, curiously called "dividends," which were then used for the entity's charitable purpose.[98] In order to participate in the program,

---

89. *Id.* ("Another element which is important in establishing that a gift was made in such circumstances, is evidence that the payment in excess of the value received was made with the intention of making a gift. While proof of such intention may not be an essential requirement under all circumstances and may sometimes be inferred from surrounding circumstances, the intention to make a gift is, nevertheless, highly relevant in overcoming doubt in those cases in which there is a question whether an amount was in fact paid as a purchase price or as a gift.").

90. *See id.*

91. *Id.* at 107-08.

92. *See id.*

93. *Id.* at 111.

94. *Id.*

95. *Id.*

96. *See* United States v. Am. Bar Endowment, 477 U.S. 105, 117 (1986) ("A taxpayer may therefore claim a deduction for the difference between a payment to a charitable organization and the market value of the benefit received in return, on the theory that the payment has the 'dual character' of a purchase and a contribution . . . . In Rev. Rul. 67-246, *supra*, the IRS set up a two-part test for determining when part of a 'dual payment' is deductible. First, the payment is deductible only if and to the extent it exceeds the market value of the benefit received. Second, the excess payment must be 'made with the intention of making a gift.'").

97. *Id.* at 106.

98. *Id.* at 107-08.

members were required to allow the charity to keep the refunded payments; however, the members were informed by the organization that they could claim as a charitable deduction an amount equal to their respective excess premium refunds.[99]

In denying the taxpayers' charitable deductions, the Supreme Court expressly approved of and used the two-part gift test of Rev. Rul. 67-246.[100] In its analysis, the Court determined that certain taxpayers failed under the first prong to prove that the value of the insurance provided to them was less than the premiums paid.[101] The taxpayer who successfully established the valuation discrepancy, however, failed to prove that he had actual knowledge of the discrepancy, and therefore, "intentionally paid more than market value for ABE's insurance because he wished to make a gift."[102] In disallowing the charitable deduction, the Court summarized the rule's essence, stating that the "*sine qua non* of a charitable contribution is a transfer of money or property without adequate consideration."[103]

After *American Bar Endowment's* adoption of the two-part gift test, it was eventually incorporated into Treas. Reg. § 1.170A-1(h).[104] The treasury regulation provides that a taxpayer's payment to a charitable organization in consideration for goods or services is presumed not to be a gift within the meaning of § 170(c), unless the taxpayer can demonstrate with respect to all or part of the payment that: (1) the taxpayer "intend[ed] to make a payment in an amount that exceeds the fair market value of the goods or services;" and (2) a payment was actually made "in an amount that exceeded the fair market value of the goods or services" provided.[105] The deduction

---

99. *Id.* at 108.

100. *Id.* at 117-19.

101. *Id.* at 117-18.

102. *Id.* ("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 . . . . Had respondent Sherwood known that he could purchase comparable insurance for less money, ABE's insurance would necessarily have declined in value to him. Because Sherwood did not have that knowledge, however, we again must assume that he valued ABE's insurance equivalently to those competing policies of which he was aware. Because those policies cost as much as or more than ABE's, Sherwood has failed to demonstrate that he intentionally gave away more than he received.").

103. *Id.* at 118 ("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. The most logical test of the value of the insurance respondents received is the cost of similar policies.").

104. *Compare Am. Bar Endowment*, 477 U.S. at 117-18 (supporting the Claims Court's application of the two-part test), *with* Temp. Treas. Reg. § 1.170A-1(h) (2009) (stating the two-part test).

105. Temp. Treas. Reg. § 1.170A-1(h)(1).

amount is further limited in that it "may not exceed the excess of the amount of cash paid and fair market value of any property transferred by the taxpayer" to the tax-exempt organization "over the fair market value of the goods or services the organization provides in return."[106]

As with all charitable contributions, the amount of the property qualifying for the deduction may be further limited by the limitation rules for contributions of long-term capital gain property and ordinary income property under § 170(e).[107] Under the regulation, a taxpayer makes a payment "in consideration for" the goods or services of the charitable organization when the taxpayer "receives or expects to receive goods or services in exchange for the payment."[108] Notice how, unlike in *Singer*, which focused to a degree on a taxpayer's "expectation" of a return benefit, the regulation does not limit dual payment transactions to such, as simply "receiving" a return benefit will suffice.[109] In other words, one could argue under *Singer* that if he did not "expect" a return benefit, the entire contribution should be deductible with no offset.

Circling back to *Scharf*, the court merely determined that the benefit flowing back to the donor was incidental and permitted the entire deduction without any corresponding reduction in the charitable amount.[110] In other words, the *Scharf* quid pro quo analysis was an all or nothing proposition for the donor.[111] Where a donor's contribution was contingent upon an expectation that the remaining property would directly or indirectly increase in value, or that the donor would benefit in general for the contribution, the charitable deduction for that contribution would be denied.[112] If, however, the benefit received was incidental to the contribution, the deduction was allowed in

---

106. *Id.* § 1.170A-1 (h)(2).

107. *See* I.R.C. § 170(e)(i) (2006). Generally the amount of the deduction for long-term capital gain property is the property's fair market value, I.R.C. § 170(C)(iv) (2006), and the amount for ordinary income is the asset's adjusted basis, 26 C.F.R. § 1.755-1(b)(2)(i) (2010).

108. Temp. Treas. Reg. § 1.170A-13(f)(6) (2009) ("A donee organization provides goods or services in consideration for a taxpayer's payment if, at the time the taxpayer makes the payment to the donee organization, the taxpayer receives or expects to receive goods or services in exchange for that payment.").

109. *Compare* Singer Co. v. United States, 449 F.2d 413, 421 (1971) (stating that a charitable transfer does not constitute a "section 170 type deduction because it is made with expectations of financial return commensurate with gift," but "it might be deductible under section 162(a) if all other requirements are met"), *with* Temp. Treas. Reg. § 1.170A-13(f)(6).

110. Scharf v. Comm'r, 32 T.C.M. (CCH) 1247, 1252 (1973).

111. *See id.* at 1251-52.

112. *See id.* at 1251.

full.[113] In *American Bar Endowment*, the court reasoned that a total denial of charitable deduction "would not serve the purposes of § 170," since sometimes a taxpayer does not receive a significant benefit quid pro quo for his contribution.[114] In such situations, the Court stated that "a taxpayer could claim a deduction for the difference between the payment to the charitable organization and the market value of the benefit received in return, on the theory that the payment has the 'dual character' of a purchase and a contribution."[115]

What is clear from the various tax court memos and revenue rulings concerning the dual payment rule is that no charitable deduction is permitted if the benefit flowing back to the donor equals or exceeds the benefit inuring to the charitable organization.[116] What is not so clear is whether or not the regulatory test *only* applies to incidental donor benefits received, substantial donor benefits received, or both. Also, questions remain as to whether substantial donor benefits are always equal to or greater than the benefit flowing to the general public; whether incidental donor benefits are always less than the benefit passing to the charitable organization; and whether the regulatory test evaluates only substantial donor benefits, reducing incidental donor benefits to a mere de minimis or nominal exception that *never* offsets the charitable deduction. There are a number of cases and revenue rulings in which courts, similar to *Scharf,* completely excluded the return benefit from the charitable deduction equation once an incidental benefit was determined.[117] The problem with these cases and revenue

---

113. *Id.* at 1252.

114. United States v. Am. Bar Endowment, 477 U.S. 105, 116-17 (1986) ("Where the size of the payment is clearly out of proportion to the benefit received, it would not serve the purposes of § 170 to deny a deduction altogether.").

115. *Id.* at 117.

116. *See* Derby v. Comm'r, 95 T.C.M. (CCH) 1177, 1194 (2008) (denying petitioners' deductions because they "received a commensurate quid pro quo" on the sale of their medical practice); Ruddel v. Comm'r, 71 T.C.M. (CCH) 2419, 2422 (1996) (denying a deduction of the amount taxpayer paid to police department for the return of his own property); Werbianskyj v. Comm'r, 34 T.C.M. (CCH) 467, 468 (1975) (refusing deduction of taxpayer's purchase of products from youth groups); Rev. Rul. 72-506, 1972-2 C.B. 106 (ruling that taxpayer's gift to nursing home was not deductible because the value was equal to admission into the home).

117. *See, e.g.*, Citizens & S. Nat'l Bank v. United States, 243 F. Supp. 900, 906-07 (W.D.S.C. 1965) (allowing a full deduction of the fair market value of a bank's donation to the city of a right-of-way based upon the court's determination that the bank's return benefit of enhanced access to its office building was only incidental to the public purpose served in assisting the city with the completion of a new highway); McLennan v. United States, 24 Cl. Ct. 102, 107 (1991) (granting taxpayer a charitable deduction for his donation of a scenic easement to a conservatory based on its finding that "any benefit from the conveyance was merely incidental to an important, public spirited, charitable

rulings are that their facts do not involve live burns scenarios, and *American Bar Endowment*, Treas. Reg. § 1.170A-1(h)(1) and Rev. Rul. 67-246 do not express such a clear exception out of the quid pro quo test.[118] As stated previously, the current regulation also does not hinge allowance or disallowance of the deduction on a taxpayer's "expectation" of a return benefit.[119]

In *Transamerica Corporation,* the taxpayer argued, among other things, that a donor's receipt of an expected substantial benefit is not a fatal error as long as the benefit is less than the benefit to the charitable donee.[120] The taxpayer further contended that the court needed only to compare the dollar values of the respective benefits received by each party in its charitable deduction analysis.[121] The court disagreed, and instead stated that if a taxpayer receives a substantial return benefit in its transfer, a "rebuttable presumption" arises that a charitable contribution was not made, and the taxpayer must rebut the presumption under the *American Bar Endowment* test.[122] The court did not want to relegate the application of the quid pro quo test to a mere mathematical computation as suggested by the taxpayer.[123] Therefore, from the perspective of the U.S. Court of Appeals, the application of the test is arguably limited to exchanges in which the donor receives a substantial return benefit, and a deduction may or may not be allowed depending on whether the taxpayer successfully rebuts the presumption.[124] The Court made no mention of incidental benefit

---

purpose"); Rev. Rul. 81-307, 1981-2 C.B. 78 (holding that a taxpayer's monetary donation to a police department as reward money for finding his child's murderer was a charitable deduction, notwithstanding any incidental return benefit); Rev. Rul. 80-77, 1980-1 C.B. 56 (permitting a charitable deduction on a taxpayer's donation to daughter's Girl Scout unit); Rev. Rul. 67-446, 1967-2 C.B. 120 (holding that the return benefit to donors of the rejuvenation of the shopping district was incidental and therefore an allowable deductible for their gift of money to the city to encourage the railroad company's removal of its facilities outside the city).

118. *See Am. Bar Endowment,* 477 U.S. at 116-18 (stating the general rule that a payment is deductible when it "exceeds the market value of the benefit received" and is "made with the intention of making a gift"); 26 C.F.R. § 1.170A-1(h)(1) (2009) (stating the general rule that a contribution or gift is one in which the taxpayer intends to make a payment that exceeds the fair market value of goods and services and makes such a payment); Rev. Rul. 67-246, 1976-2 C.B. 104 (stating the general rule that a presumption arises against a gift bring made for charitable contribution purposes if the transaction payment is made in the form of a purchase of an item of value).

119. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247, 1251 (1973).

120. Transamerica Corp. v. United States, 902 F.2d 1540, 1544 (Fed. Cir. 1990).

121. *Id.*

122. *Id.* at 1545.

123. *Id.*

124. Paul M. Mahoney, Jr., Note, *Transfer of Antique Films to the Library of Congress: Outright Gift, Dual Transaction, or Quid Pro Quo Under Section 170? Transamerica Corp. v. United States,* 44 BULL. SEC. TAX'N 958, 965 (1991) ("By

exchanges in its opinion and was, therefore, unclear as to whether or not they are exempt entirely from the test and the court's rebuttable presumption.[125]

Contrary to *Transamerica Corporation*, however, a close reading of *American Bar Endowment* indicates that in the Court's adoption of the quid pro quo test, it did not restrict its application to substantial benefit transactions alone.[126] Also, *American Bar Endowment* does not discuss substantial benefit transactions as being the only donor benefit creating a rebuttable presumption of disallowance.[127] In fact, one could argue the two-part test set forth in *American Bar Endowment* only applies to incidental benefit transactions, and that there is no rebuttable presumption of disallowance for substantial benefit transactions because they are *never* charitable gifts.[128] Rev. Rul. 67-246 also makes no mention of a substantial benefit as being the exclusive benefit creating a rebuttable presumption of disallowance.[129] Nor does the test as promulgated in Treas. Reg. § 1.170A-1(h).[130] The treasury regulation only states that the presumption arises that no gift has been made when a transaction involves a payment in the form of a purchase of an item of value.[131] Presumably, this means that if the donor receives *any* return benefit, whether substantial or incidental, the presumption arises.[132]

In *Singer* on the other hand, once the U.S. Court of Claims court determined there was an expectation of a substantial donor benefit, the deduction was disallowed in its entirety with no discussion of a rebuttable presumption.[133] The court defined a substantial donor benefit as "benefits greater than those that

---

implementing a rebuttable presumption standard in connection with the dual character test, the Court of Appeals for the Federal Circuit made explicit the determination of the Claims Court: once a substantial benefit to the taxpayer has been established, the only way that a taxpayer can salvage a partial deduction is to demonstrate that the benefit to the recipient outweighs the benefit to the taxpayer, and that the taxpayer intended to provide such excess to the recipient.").

125. *See Transamerica Corp.*, 902 F.2d at 1540-46.

126. *See* United States v. Am. Bar Endowment, 477 U.S. 105, 117 (1986) (holding that a taxpayer may claim a deduction for "the difference between a payment to a charitable organization and the market value of the benefit received in return, on the theory that the payment has the "dual character" of a purchase and a contribution").

127. *See id.*

128. *See id.*

129. *See* Rev. Rul. 67-246, 1976-2 C.B. 104.

130. *See* Treas. Reg. § 1.170A-1(h)(1) (2009).

131. *See id.* (hinging the characterization of the donation as a contribution or gift on the intent of the taxpayer and the amount that the payment exceeds the fair market value of the goods or services).

132. *See id.*

133. *See* Singer Co. v. United States, 449 F.2d 413 (Ct. Cl. 1971).

inure to the general public from transfers for charitable purposes."[134] The court, however, recognized the incidental benefit exception stating, "we do not contend that absolutely no benefits can be derived from an otherwise charitable contribution or gift. It is only when the benefits derived are substantial enough to provide a quid pro quo for the transfer that the deduction is not allowed."[135] *Singer* was decided after the release of Revenue Ruling 67-246.[136] Notice the court defined substantial donor benefits as "greater than" those inuring to the general public.[137] A taxpayer in the U.S. Court of Claims can therefore assume its definition of "substantial" entails donor benefits received in excess of the donee benefit, in which case, the charitable deduction will always be disallowed when a substantial benefit is received.[138] The *Singer* court in essence defined a quid pro quo as an expectation of a substantial donor benefit, thus leaving no room for even a partial deduction under Rev. Rul. 67-246.[139]

In 1989, the U.S. Supreme Court again confronted the quid pro quo test in the case of *Hernandez v. Commissioner*.[140] In *Hernandez,* the dispute involved members of the Church of Scientology ("Church"), who attempted to deduct certain payments made to the Church for its "auditing" and "training" sessions on their federal income tax returns as charitable contributions. [141] The issue before the Supreme Court was whether such taxpayer payments were in fact gifts within the meaning of § 170 or disguised payments for the Church's auditing and training services.[142]

As a condition of membership in the Church of Scientology, the Church would frequently charge its members certain fixed

---

134. *Id.* at 423.

135. *Id.*

136. *See* Rev. Rul. 67-246, 1967-2 C.B. 104.

137. *Singer*, 449 F.2d at 423.

138. *Id.* at 422-23.

139. *Id.* at 414.

140. *See* Hernandez v. Comm'r, 490 U.S. 680 (1989).

141. *Id.* at 684-85 ("The Church charges a 'fixed donation,' also known as a 'price' or a 'fixed contribution,' for participants to gain access to auditing and training sessions. These charges are set forth in schedules, and prices vary with a session's length and level of sophistication. In 1972, for example, the general rates for auditing ranged from $625 for a 12½-hour auditing intensive, the shortest available, to $4,250 for a 100-hour intensive, the longest available. Specialized types of auditing required higher fixed donations: a 12½-hour 'Integrity Processing' auditing intensive cost $750; a 12½-hour 'Expanded Dianetics' auditing intensive cost $950. This system of mandatory fixed charges is based on a central tenet of Scientology known as the 'doctrine of exchange,' according to which any time a person receives something he must pay something back.").

142. *Id.* at 689.

donation fees for its auditing and training sessions.[143] The price, provided in a schedule, would "vary [depending on] a session's length and level of sophistication."[144] Further, proceeds from such sessions constituted the Church's primary source of income.[145] The Service, in a battle spanning back decades with the Church of Scientology over the legitimacy of its tax-exempt status, altered its litigation strategy by deciding to move its attack to the individual donors and disallowing in full their charitable deductions claimed.[146] The issue before the Court was whether the contributions were in fact gifts within the meaning of § 170 or mere payments for the Church's services.[147]

In answering this question, the Supreme Court reviewed the legislative history of the statute, stating, in relevant part: "Congress intended to differentiate between unrequited payments to qualified recipients and payments made to such recipients in return for goods or services. Only the former were deemed deductible."[148] The court then analyzed whether the donations were made with "the expectation of any quid pro quo."[149] Back-pedaling slightly from the *Duberstein's* "detached and disinterested generosity" standard, and propping up the more objective inquires conducted by *Singer* and *American Bar Endowment*, the court embraced a "structural analysis" of the "external features" of the transaction.[150] By adopting such a structural analysis, the court in essence eliminated the need to conduct an imprecise expedition into the subjective motivations

---

143. *Id.* at 685.

144. *Id.*

145. *Id.*

146. *Id.* at 686.

147. *Id.*

148. *Id.* at 690 ("The legislative history of the 'contribution or gift' limitation, though sparse, reveals that Congress intended to differentiate between unrequited payments to qualified recipients and payments made to such recipients in return for goods or services. Only the former were deemed deductible. The House and Senate Reports on the 1954 tax bill, for example, both define 'gifts' as payments 'made with no expectation of a financial return commensurate with the amount of the gift.'" (quoting S. REP. No. 1622 (1954); H.R. REP. No. 1337 (1954))).

149. *Id.*

150. *Id.* at 690-91 ("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 individual taxpayers. The lower courts have generally embraced this structural analysis. We likewise focused on external features in *United States* v. *American Bar Endowment* to resolve the taxpayers' claims that they were entitled to partial deductions for premiums paid to a charitable organization for insurance coverage . . . we stressed that '[t]he *sine qua non* of a charitable contribution is a transfer of money or property *without adequate consideration*.'") (internal citations omitted).

of the respective taxpayers.[151] The court held the taxpayer donations were part of a "quintessential quid pro quo exchange" for the church's auditing and training sessions.[152] The exchange was inherently reciprocal in nature, and thus, a quid pro quo exchange.[153] As a quid pro quo exchange, the court concluded the contributions were not gifts within the statutory expression of § 170, and thus, disallowed the taxpayers' charitable deductions in full.[154]

The *Hernandez* court made no mention of the substantial versus incidental issue.[155] Instead, it threw further darkness on the issue in a footnote, stating that the taxpayers never argued that their payments qualified as "dual payments," and that they are therefore entitled to a partial deduction.[156] As a result, the court "had no occasion to decide this issue."[157]

The problem with the court's remote footnote conversation on the dual payment rule is that such is by definition a quid pro quo transaction;[158] this means that a payment or transfer of property is made by the taxpayer with the expectation of a benefit in return – hence the quid pro quo exchange.[159] If the return benefit is merely incidental (i.e., less than the donee benefit), a charitable deduction exists, assuming the two-part regulatory test is satisfied.[160] If the benefit is substantial (i.e., equal to or greater than the donee benefit), the deduction is arguably disallowed entirely.[161] The mechanical nature of the two-part gift test mandates such, notwithstanding *Transamerica Corporation*.[162] This is also where the *Singer* court got it wrong,

---

151. *Id.*

152. *Id.* at 691 ("In light of this understanding of § 170, it is readily apparent that petitioners' payments to the Church do not qualify as 'contribution[s] or gift[s].' As the Tax Court found, these payments were part of a quintessential *quid pro quo* exchange: in return for their money, petitioners received an identifiable benefit, namely, auditing and training sessions.").

153. *See id.* at 691-92.

154. *See id.* at 692-94.

155. *See id.*

156. *Id.* at 694 n.10 ("Petitioners have not argued here that their payments qualify as 'dual payments' under IRS regulations and that they are therefore entitled to a partial deduction to the extent their payments exceeded the value of the benefit received.").

157. *Id.*

158. *See* Sklar v. Comm'r, 549 F.3d 1252, 1257 (9th Cir. 2008); *see also* United States v. Am. Bar Endowment, 490 U.S. 105, 117 (1986).

159. *See Hernandez,* 490 U.S. at 691.

160. *See Id.* at 710.

161. *See id.*

162. *Compare Sklar,* 549 F.3d at 1260, 1264 (allowing no deduction in whole or in part, even if some part of benefit received was religious in nature), *with Transamerica Corp.*, 902 F.2d at 1545 (stating that "[a] taxpayer may, in certain circumstances be able to rebut the above presumption at least in part, and thereby, obtain a partial deduction.").

as just as there are unacceptable quid pro quo transactions there are acceptable ones - namely, when the return benefit is merely incidental.[163]

Justice O'Connor and Justice Scalia, who dissented in the *Hernandez* opinion, contended that the court was incorrect in its majority opinion.[164] The dissent argued that the majority misapplied the longstanding practice of permitting charitable contributions to religious organizations, and that along the way the court violated the Establishment Clause.[165] The dissent, written by Justice O'Connor, stated that the "quid" flowing back to the taxpayers was merely spiritual or religious, just like it is with any other exchanges between worshipers and their tax-exempt churches (e.g., Christians, Mormons, Jews, etc.).[166] If the taxpayers had received benefits of "commercial value," and not "spiritual," then the allowable portion of the claim would be determined by subtracting the value of the physical benefit received from the total amount paid.[167] The aforementioned was an obvious recitation of the dual payment/quid pro quo rule.[168] With regard to spiritual or religious benefits, however, the dissent stated that there is no market against which one can price such intangibles.[169] It would therefore be both inconsistent

---

163. *See Hernandez*, 490 U.S. at 710.

164. *See id.* at 713 ("In my view, the IRS has misapplied its longstanding practice of allowing charitable contributions under § 170 in a way that violates the Establishment Clause. It has unconstitutionally refused to allow payments for the religious service of auditing to be deducted as charitable contributions in the same way it has allowed fixed payments to other religions to be deducted.") (O'Connor, J., dissenting).

165. *Id.*

166. *Id.* at 710-11 ("There is no discernible reason why there is a more rigid connection between payment and services in the religious practices of Scientology than in the religious practices of the faiths described above. Neither has respondent explained why the benefit received by a Christian who obtains the pew of his or her choice by paying a rental fee, a Jew who gains entrance to High Holy Day services by purchasing a ticket, a Mormon who makes the fixed payment necessary for a temple recommend, or a Catholic who pays a Mass stipend, is incidental to the real benefit conferred on the 'general public and members of the faith,' while the benefit received by a Scientologist from auditing is a personal accommodation.") (internal citation omitted) (O'Connor, J., dissenting).

167. *Id.* at 706 ("When a taxpayer claims as a charitable deduction part of a fixed amount given to a charitable organization in exchange for benefits that have a commercial value, the allowable portion of that claim is computed by subtracting from the total amount paid the value of the physical benefit received. If at a charity sale one purchases for $ 1,000 a painting whose market value is demonstrably no more than $ 50, there has been a contribution of $ 950.") (O'Connor, J., dissenting).

168. *See id.*

169. *Id.* at 707 ("Confronted with this difficulty, and with the constitutional necessity of not making irrational distinctions among taxpayers, and with the even higher standard of equality of treatment among *religions* that the First Amendment imposes, the Government has only two practicable options with regard to distinctively religious *quids pro quo:* to disregard them all, or to tax them all. Over the years it has chosen the former course.") (O'Connor, J., dissenting).

with prior judicial precedent and a violation of the Establishment Clause for the Service (and the court) to analyze all fixed religious contributions on a case-specific basis under an ad hoc quid pro quo standard.[170] In scolding the majority for singling out the Church of Scientology for selective quid pro quo scrutiny, the dissent illuminated the majority's improper quid pro quo versus dual payment distinction.[171]

Congress has since resolved the religious benefit issue in *Hernandez* by enacting § 6115(b), which states in pertinent part that "[a] quid pro quo contribution does not include any payment made to an organization, organized exclusively for religious purposes, in return for which the taxpayer receives solely an intangible religious benefit that generally is not sold in a commercial transaction outside the donative context."[172] The majority opinion's dicta distinguishing a dual payment as something other than a quid pro quo transaction, however, remains a mystery at sea.

IV. FROM ZERO TO FAIR MARKET VALUE

Post *Scharf,* in applying the two-part gift test to similar contributions, one must ask what exactly is the fair market value of the demolition services provided by the fire department. Is not the fire department providing a valuable service that is the functional equivalent of demolition services? Are such services received incidental or substantial donor benefits in relation to the donee benefits? If the donor benefits received are merely incidental to the donee benefits, the taxpayer may argue under *Scharf* the charitable deduction should be permitted in full with no corresponding return benefit offset.[173] As previously explained, however, the aforementioned argument is weak, and contrary to *American Bar Endowment*, Rev. Rul. 67-246, and the regulations - none of which exempt incidental donor benefits from the quid pro quo test.[174] This was also the argument made,

---

170. *See id.* at 712-13.

171. *See id.* at 704-13.

172. I.R.C. § 6115(b) (2006) ("For purposes of this section, the term 'quid pro quo contribution' means a payment made partly as a contribution and partly in consideration for goods or services provided to the payor by the donee organization. A quid pro quo contribution does not include any payment made to an organization, organized exclusively for religious purposes, in return for which the taxpayer receives solely an intangible religious benefit that generally is not sold in a commercial transaction outside the donative context.").

173. *See* Scharf v. Comm'r, 265 T.C.M. (CCH) 1247, 1252 (1973).

174. *See* United States v. Am. Bar Endowment, 477 U.S. 105, 117-18 (1986); Rev. Rul. 67-246, 1967-2 C.B. 105.

unsuccessfully, by the taxpayers in *Rolfs*.[175] The taxpayer's exact charitable deduction consequences, of course, are taxpayer specific and depend on the facts and circumstances of each case, not the taxpayer's characterization.[176]

Demolition services provided by a fire department presumably have value beyond incidental in most situations.[177] The mere fact that a donated structure will be used exclusively by the organization for charitable purposes has no bearing on the fair market value of the demolition services.[178]

The U.S. Tax Court case of *Rolfs* just might have been the final death knell for *Scharf,* as it substantially constricted, if not eliminated, any reliance on *Scharf* for future charitable deduction cases.[179] *Rolfs* involved husband and wife taxpayers who purchased a 3-acre lakefront property in the State of Wisconsin.[180] The house was originally built in the early 1900s, and had been renovated several times since.[181] Nevertheless, in the taxpayers' view, the residence needed more significant improvements.[182] The taxpayers were therefore initially undecided as to whether or not they should renovate the house or simply tear it down.[183]

The mother of one of the taxpayers suggested they demolish the house, build a new structure in its place to the mother's specifications, and then exchange it for her residence.[184] The taxpayers liked this proposal, and decided to proceed with it. The taxpayers determined it would cost approximately $10,000 to $15,000 to demolish the existing lake house.[185] Similar to *Scharf,* the taxpayers quickly learned they could donate the structure to the fire department for live burn practice and magically receive the tax benefit of a charitable deduction.[186]

---

175. Rolfs v. Comm'r, 135 T.C. 271, 278 (2010).

176. *See, e.g.*, De Jong v. Comm'r, 36 T.C. 896, 899-900 (1961) (determining that part of taxpayers' alleged charitable contribution to a religious school for the taxpayers' children was a non-deductible tuition payment, notwithstanding the label).

177. *See Scharf*, 265 T.C.M. at 1252-53.

178. *See id.* at 1253; Rev. Rul. 67-246, 1967-2 C.B. 106 ("The fact that the full amount or a portion of the payment made by the taxpayer is used by the organization exclusively for charitable purposes has no bearing upon the determination to be made as to the value of the admission or other privileges and the amount qualifying as a contribution.").

179. *Rolfs*, 135 T.C. at 271.

180. *Id.* at 273.

181. *Id.* at 274.

182. *Id.*

183. *Id.*

184. *Id.*

185. *Id.*

186. *Id.* at 274-75.

The taxpayers therefore made all the necessary arrangements with the fire department so that the fire department and the police could use the structure for the limited purpose of training exercises, and then ultimately burn it down when they were finished.[187] Again, similar to *Scharf,* the taxpayers transferred the residence without a deed or any formal conveyance document.[188] The fire department of course proceeded with its various training exercises, and then destroyed the structure in a practice fire drill, leaving nothing but the remnants of the burn and the concrete foundation of the lake house.[189]

The taxpayers claimed a charitable deduction equal to the fair market value of the lake front house in the amount of $76,000, along with other various charitable deductions on their return.[190] Unfortunately, the taxpayers were audited, and then naturally ensued the long anticipated post-*Scharf* showdown between the taxpayers and the Service, which lead the case to the U.S. Tax Court.[191] The Service's position for denying the charitable deduction was threefold: (1) the taxpayers received a substantial benefit in exchange for the contribution, namely demolition services, which had a value in excess of the contribution, (2) the taxpayers transferred less than their entire interest under the partial interest rule, and (3) the donated lake house was essentially worthless.[192] The taxpayers on the other hand contended: (1) under *Scharf* the quid pro quo return benefit was only "incidental" to the taxpayers, (2) they transferred the entire interest in the property as it was demolished, and (3) they should therefore receive a deduction equal to the property's replacement cost or its fair market value.[193]

---

187. *Id.*

188. *Id.*

189. *Id.* at 282.

190. *Id.* at 275.

191. *Id.*

192. *Id.* at 278 ("Respondent contends that petitioners are not entitled to a deduction for a charitable contribution in connection with their donation of the lake house to the VFD because they anticipated and received a substantial benefit in exchange for the contribution; namely, demolition services. Petitioners therefore did not make a charitable contribution within the meaning of section 170(c), as interpreted in United *States v. Am. Bar Endowment,* supra, because the fair market value of the lake house as donated did not exceed the fair market value of the demolition services petitioners received from the VFD in exchange for the donation (quid pro quo argument). Respondent argues in the alternative that (1) the charitable contribution deduction in dispute is disallowed under section 170(f)(3)(A) because petitioners transferred to the VFD less than their entire interest in the lake house; and (2) the lake house as donated to the VFD was worthless.").

193. *Id.* ("Petitioners first contend that the burden of proof on all issues is shifted to respondent pursuant to section 7491(a). Petitioners assert that the Court should not

In addressing *Scharf,* the court acknowledged it was "quintessentially a quid pro quo case" involving similar facts, which therefore warranted an analysis that was not a new matter, as the taxpayers argued, but rather was the basis for their charitable deduction position.[194] The court next recognized *American Bar Endowment* and the two-part dual payment test as appropriate for determining whether a charitable deduction exists.[195] First, the payment is deductible only if and to the extent it exceeds the market value of the benefit received.[196] Second, the excess payment must be made with the intention of making a gift.[197]

The court then stated the *Scharf* test lacks "vitality," as it differs from that announced in *American Bar Endowment.*[198] Whereas *Scharf* examined whether or not the "public benefit" of the donation exceeded the value of the benefit received by the donor, *American Bar Endowment* examined whether the "fair market value" of the contributed property exceeded the fair market value of the benefit received by the donor.[199] In other words, the test is still quintessentially a quid pro quo test, but just more mechanical and exacting in nature from that applied in *Scharf.*

In applying the first prong of the dual payment analysis, each side presented various experts to appropriately value the donated structure and provide input on the demolition costs.[200]

---

consider respondent's quid pro quo argument (to the effect that petitioners received a benefit in exchange for their donation) because this argument constitutes new matter that respondent raised for the first time in his opening brief. However, if respondent is allowed to raise the quid pro quo argument, petitioners contend that they donated property with a fair market value of $76,000 (according to a qualified appraisal) which they have shown should be valued at its reproduction cost of $235,350 and that they received only an 'incidental benefit' in return. Petitioners contend that section 170(f)(3)(A) is inapplicable because in transferring the lake house to the VFD with the right to demolish it, they transferred their entire interest in the property.").

194. *Id.* at 280.

195. *Id.* at 281.

196. *Id.*

197. *Id.*

198. *Id.*

199. *Id.* at 281-82 ("The test applied in *Scharf,* which examines whether the value of the public benefit of the donation exceeded the value of the benefit received by the donor, differs from the Supreme Court's test announced 13 years later in *United States v. Am. Bar Endowment,* 477 U.S. 105, 106 S. Ct. 2426, 91 L. Ed. 2d 89 (1986). The *Am. Bar Endowment* test examines whether the fair market value of the contributed property exceeded the fair market value of the benefit received by the donor. The test applied in *Scharf* has no vitality after Am. Bar Endowment. Instead, we must consider whether the value of the lake house as donated exceeded the value of the demolition services petitioners received.").

200. *Id.* at 276–78.

With regard to the value of the benefit received by the taxpayers, namely, the demolition costs, the court concluded the taxpayers saved approximately $10,000 by having the fire department burn the building versus hiring a company to demolish it.[201] As for the value of the property donated, the taxpayers' expert asserted in his appraisal based on a "before and after" approach that the structure had a value of approximately $76,000.[202] The court, however, rejected this before and after approach because the methodology failed to take into account that the structure was severed from the land and substantial restrictions were placed on its use.[203] In the alternative, the taxpayers asserted the value of the lake front house was equal to its "replacement cost" because it was "unique" and was "special use" property in the hands of the donee.[204] Again, the court disagreed.[205]

In the end, the court determined the value of the property was essentially zero.[206] The court arrived at this conclusion by considering the Service's moving experts, who suggested the value of the structure moved from its lake front lot was virtually worthless, as it would cost more to move the house than it was worth.[207] Certainly, nobody in the nearby exclusive neighborhood

---

201. *Id.* at 282.

202. *Id.* at 283 ("Petitioners offered the appraisal of their expert, Mr. Larkin, in support of their claim that the lake house had a fair market value of at least $76,000 when donated. In his appraisal Mr. Larkin opined that the lake house had a 'contributory value' of $76,000 on the basis of a 'before and after' approach to value, which treated the value of the donated lake house as equal to the difference between the fair market value of the lake property with the lake house and the fair market value of the lake property without the lake house.").

203. Id. at 284 ("Thus, the $76,000 'contributory value' of the lake house postulated by Mr. Larkin at best reflects the value of the lake house before taking into account its severance from the underlying land, the prohibition on residential use, and the condition that it be burned down promptly. Consequently, the property interest Mr. Larkin appraised is not comparable to the property interest that petitioners donated to the VFD.").

204. *Id.* ("Petitioners alternatively contend that the fair market value of the lake house as contributed to the VFD was $235,350, its reproduction cost as estimated by Mr. Larkin. Petitioners offer no expert testimony in support of this proposition.").

205. *Id.* at 284–85.

206. *Id.* at 285.

207. *Id.* ("We consider first the impact of the severance of the lake house structure from the underlying land. The price at which the lake house would change hands would undoubtedly be affected by the condition that the structure could not remain affixed to its underlying land indefinitely. Petitioners offered no evidence concerning the impact of this condition. Respondent offered the testimony of two experts in the field of house moving regarding the price at which the lake house would likely sell if required to be moved from its existing site. Both house moving experts concluded that the likelihood of a buyer's purchasing the lake house to move it from the site was virtually nil, because the characteristics of the lake house and its site rendered a relocation of the structure infeasible. We are persuaded that the expert testimony concerning the market for the lake house as a structure to be moved provides a reasonable basis for estimating the impact on

would want such an outdated house, and therefore, transporting it to a more distant area, coupled with the various costs of removing certain structural barriers, set the value of the severed residence at zero.[208]

In addition, the court stated even if the severed structure had value, it should nevertheless be discounted by the two restrictions placed on it: (1) the house was limited to police and fire training exercises for a limited period of time, and (2) there was a condition that the building be burned down shortly after its conveyance.[209] The court, however, did not need to address these valuation discounts issues any further, but rather left them dangling for future cases, as the structure was worthless without them.[210] Distinguishing itself, the court stated *Scharf* involved a building that was condemned and partially destroyed, whereas, in the present case, the residence was not condemned, and the decision to donate it to the fire department was entirely voluntary, therefore using the insurance loss value in *Scharf* was appropriate.[211] The taxpayers' charitable deduction was thus denied.[212]

If a taxpayer blazes ahead despite *Rolfs* and the array of other legal uncertainty discussed in this article, and relinquishes his or her residence to the flames of destruction, the allowed deduction should be limited to that amount which the fair market value of the transferred building exceeds the value of the demolition services.[213] And as stated in *Rolfs*, the value of the structure may be discounted significantly as a result of the various restrictions placed on its use by the taxpayer.[214] Of course, this is assuming the taxpayer is to use the fair market value of the structure itself versus the value of its "use," as argued for by the Service in *Scharf,* and *on* which the Service never acquiesced.[215] *Rolfs* on the other hand, made no mention of the use value of the structure.

---

fair market value of the severance of the lake house from its underlying land. We find that the severance rendered the lake house virtually worthless.").

208. *Id.*

209. *Id.* at 283.

210. *Id.* at 285.

211. *Id.* at 281–82 n.12.

212. *Id.* at 285.

213. *See* Scharf v. Comm'r, 265 T.C.M. (CCH) 1247, 1253 (1973) ("Where a charitable contribution is made in property other than money, the allowable deduction is measured by the fair market value of the property at the time of the contribution."); Rev. Rul. 67-246, 1967-2 C.B. 105.

214. *Rolfs*, 135 T.C. at 285.

215. *See Scharf*, 265 T.C.M. at 1253.

The taxpayer must also demonstrate under the second prong of the test that the excess was intended as a gift.[216] *Rolfs* never had to address this issue because the taxpayers could not overcome the first prong.[217] Such an exacting jump was not previously required of the taxpayers in *Scharf*.[218] In *Scharf,* when evaluating the taxpayers' charitable motivation, the court simply stated that there was "no doubt" the Scharfs were motivated to donate their building for a clearer, more valuable track of land.[219] This point notwithstanding, the court determined there was also "no doubt" Mr. Scharf was motivated by a desire to have a volunteer fire department burn the building to the ground.[220] Because the dual payment rule preserves a modified form of the subjective intent element of *Duberstein* in the second prong,[221] one must query whether such is a more difficult taxpayer hurdle in dual payment situations. Looking back at *American Bar Endowment*, the single taxpayer who successfully proceeded to the second prong failed to prove he had "actual knowledge" that he could have purchased comparable insurance for less money and intentionally gave away more than he received.[222]

Today, the Scharfs would not only have to demonstrate that the value of the structure, as discounted by any restrictions, exceeds the value of the demolition services provided[223] but also that they had actual knowledge of the valuation discrepancy and intentionally contributed the excess to the fire department.[224]

A taxpayer's intent may be inferred from the surrounding circumstances, which is highly relevant in overcoming doubt in dual payment situations.[225] Evidencing taxpayer intent to donate the "excess" in dual character exchanges is distinguishable from *Scharf*, as in this case it was an all or nothing proposition.[226] The transaction was not parsed down into

---

216. *See* Rev. Rul. 67-246, 1967-2 C.B. 105.

217. *Rolfs*, 135 T.C. at 285.

218. *See Scharf*, 265 T.C.M. at 1252 ("Thus, where the primary benefit inures to the general public with only lesser and incidental benefits flowing back to the donor, then a charitable deduction will be allowed.").

219. *Scharf*, 265 T.C.M. at 1251.

220. *Id.*

221. Comm'r v. Duberstein, 363 U.S. 278, 285-86 (1960).

222. United States v. Am. Bar Endowment, 477 U.S. 105, 118 (1986).

223. *See* Rev. Rul. 67-247, 1967-2 C.B. 105.

224. *See Am. Bar Endowment*, 477 U.S. at 118.

225. *See id.* at 117-18.

226. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247, 1251-53 (1973).

its respective component parts of deductible and non-deductible portions.[227]

In many situations, such as in *Scharf*, where a structure is so badly damaged that it must be razed, the fair market value of the asset is minimal.[228] Under the current charitable gift rules, the Scharfs would have been well advised to obtain an appraisal of the structure *before* its donation and an estimate of the fair market value of demolition services or comparable services.[229] Placing a value on the fire department's "use of" the structure would be exceedingly difficult, and the taxpayer ultimately has the burden of proof.[230] As discussed in greater detail below, this valuation issue is now statutorily resolved in that a donation of the mere "right to use" the donor's property is disallowed entirely under the partial interest rule.[231] Furthermore, *Rolfs* looked to the value of the severed structure itself.[232]

Another wrinkle with any remaining taxpayer reliance on *Scharf* is statutory § 280B, which came into effect for tax years beginning after 1983.[233] Section 280B(1) prohibits owner and lessee taxpayers from claiming a deduction for the costs and losses associated with the demolition of any structure, regardless of when the taxpayer's intent was formed to demolish the structure.[234] Any amounts expended (or losses sustained) as a result of a demolition are added to the basis of the underlying land and not to the basis of any replacement structure.[235] At the moment, there is no formal definition concerning what exactly constitutes a "demolition" in the Code, regulations, or pertinent

---

227. *See id.* at 1253.

228. *See, e.g., id.* at 1249 ("The fair market value of the Margolin building at the time it was given to the fire department was $12,835.95.").

229. *See* Treas. Reg. § 1.170-1(a),(c) (amended 1972).

230. *See* Rev. Rul. 67-246, 1967-2 C.B. 104, 105.

231. *See* I.R.C. § 170(f).

232. Rolfs v. Comm'r, 135 T.C. 271, 283 (2010).

233. *See* I.R.C. § 280B; *see generally* Karen S. Muraskin, *Charitable Contribution Deductions – An Alternative to Capitalization of Demolition Costs*, THE TAX ADVISER, July 1, 1994, *available at* http://www.thefreelibrary.com/Charitable+deductions+-+an+alternative+to+capitalization. . .-a015596108 ("Prior to 1984, the taxpayer's intent on acquisition of property generally governed the tax treatment of costs incurred to demolish an existing structure; that is, a current deduction was allowed if the intent to demolish the structure was formed subsequent to the time of acquisition, while capitalization was required if the intent to demolish existed at the time of purchase. For tax years beginning after 1983, Sec. 280B prohibits a current deduction for the cost of demolition, regardless of when the intent to demolish was formed. Instead, the cost of demolition and any loss incurred is added to the basis of the underlying land, and not to the basis of any replacement structure. The determination as to when the taxpayer actually made the decision to demolish a structure has effectively been eliminated by Sec. 280B.").

234. *See* I.R.C. § 280B.

235. *See id.*

case law.[236] Yet, a taxpayer requesting a fire department to raze its existing structure to the ground certainly falls within the statutory sense of a demolition in § 280B.[237] All that being said, if a structure simply burns in part, arguably such would constitute a partial demolition or no demolition at all if the infrastructure remains fully intact.[238] The Service did not assert any § 280B arguments in *Rolfs,* at least in the opinion.[239]

The term "structure" is defined in Treas. Reg. § 1.48-1(e) as a "building" and its "structural components."[240] Section 280B was enacted in response to taxpayers attempting to deduct uninsured losses sustained as a result of intentional demolitions under § 165(a) and Treas. Reg. § 1.165-3.[241] Applied in the context of live burn donations, a Service argument exists that taxpayers should not be permitted to navigate around the § 280B loss and deduction prohibition over to the more taxpayer-friendly § 170(c) by requesting a charitable organization provide the demolition services (cloaked of course, as fire personnel training and equipment testing).[242]

The Service may also assert again in future cases that a taxpayer is not entitled to a charitable deduction because only a "partial interest" of the property has been transferred, and

---

236. Tonawanda Coke Corp. v. Comm'r, 95 T.C. 124, 131 (1990) ("Neither the applicable regulations, nor the case law interpreting the regulations, define 'demolition'. However, we believe that the meaning of 'demolish' as commonly used is appropriate in this context (citation omitted). Black's Law Dictionary (5th ed. 1979) defines 'demolish' as 'To throw or pull down; to raze; to destroy the fabrication of; to pull to pieces; hence to ruin or destroy.' Funk & Wagnall's New Standard Dictionary (1959) defines 'demolish' as 'To destroy by tearing or throwing down, as a building, wall, or the like; separate the fabric or ruin the structure of; raze; dismantle.'").

237. *See id.*

238. *See id.* at 131-32 (finding that although a small area of the plant was destroyed by a fire, the infrastructure of the plant remained intact, and therefore no "demolition" had occurred, and expenses were thus properly capitalized and added to the plant's basis).

239. Rolfs v. Comm'r, 135 T.C. 271 (2010).

240. Treas. Reg. § 1.48-1(e)(1) (1964) ("The term 'building' generally means any structure or edifice enclosing a space within its walls, and usually covered by a roof, the purpose of which is, for example, to provide shelter or housing, or to provide working, office, parking, display, or sales space. The term includes, for example, structures such as apartment houses, factory and office buildings, warehouses, barns, garages, railway or bus stations, and stores.").

241. *See* I.R.C. § 165(a) (2006); Treas. Reg. § 1.165-3 (amended 1976).

242. *See* I.R.S. Notice 90-21, 1990-1 C.B. 332, 333 ("Section 280B of the Code does not disallow casualty losses allowable under section 165, but it does apply to amounts expended for the demolition of a structure damaged or destroyed by casualty, and to any loss sustained on account of such a demolition. If a casualty damages or destroys a structure, and the structure is then demolished, the basis of the structure must be reduced by the casualty loss allowable under section 165 before the 'loss sustained on account of' the demolition is determined.").

therefore, the deduction is not permitted under § 170(f)(3)(A).[243] The Service successfully argued this position against ESPN commentator Kirk Herbstreit.[244] The Service also alleged this in *Rolfs*, but the court determined, under Wisconsin law, that a "constructive severance" had occurred and thus the partial interest rule did not apply.[245] Section 170(f)(3) generally disallows a charitable deduction for a contribution of less than the donor's entire interest in the transferred property, unless one of the three exceptions provided in § 170(f)(3)(B) apply or if the interest contributed would have been allowable as a deduction under § 170 (if the interest had been transferred into a charitable trust arrangement).[246] The three exceptions to § 170(f)(3)(A) do not apply to garden variety live burn contributions as such is not: "(1) a contribution of a remainder interest in a personal residence or farm, (2) a contribution of an undivided portion of the taxpayer's entire interest in the property, [or] (3) a qualified conservation contribution."[247] With regard to the deduction being permitted for certain transfers that otherwise would have qualified for the charitable deduction, if the property would have been transferred directly into a permitted trust arrangement, this exception also does not apply to live burn contributions, as such has nothing to do with the charitable remainder trusts under § 664.[248]

The discussion supra is assuming the structure transferred is a split interest in the first place.[249] As provided in *Rolfs,* if the state where the real property is located has a constructive severance doctrine or a similar law, then the entire interest presumably will be regarded as transferred.[250] Nevertheless, the law is not entirely clear as to whether the taxpayer is contributing the entire structure to the fire department or merely

---

243. *See* I.R.C. § 170(f)(3)(A) ("In the case of a contribution (not made by a transfer in trust) of an interest in property which consists of less than the taxpayer's entire interest in such property, a deduction shall be allowed under this section only to the extent that the value of the interest contributed would be allowable as a deduction under this section if such interest had been transferred in trust. For purposes of this subparagraph, a contribution by a taxpayer of the right to use property shall be treated as a contribution of less than the taxpayer's entire interest in such property.").

244. *See* Barr, *supra* note 1 ("The IRS maintains in court papers in the Wisconsin case that the homeowners do not qualify for a deduction because they are donating only a 'partial interest' in their home, rather than the entire property. The agency also says homeowners are letting firefighters only use the property, not donating it in full.").

245. Rolfs v. Comm'r, 135 T.C. 271, 283 (2010).

246. I.R.C. § 170(f)(3)(B).

247. *Id.* § 170(f)(3)(B)(i)-(iii).

248. *See* I.R.C. § 664.

249. *See supra* note 216 and accompanying text.

250. *Rolfs,* 135 T.C. at 283.

the "right to use" the structure. In most situations, the fire department does not remove the structure, and oftentimes elements of the structure are left remaining on the lot for the taxpayer to clean up, as was the case in *Scharf* (e.g., the chimney, debris, etc.).[251] If an entire interest is being transferred by the taxpayer, does the fire department need to raze the building completely? Should the fire department be responsible for removing any remaining debris, the chimney, etc., given the fact it belongs to charitable organization once transferred? If an entire interest is transferred, should it be evidenced by a deed or without such, as in *Scharf*? In *Rolfs*, the court determined the taxpayers' letter to the fire department was sufficient to convey the property under the Wisconsin statue of frauds.[252] Section 170(f)(3)(A) makes it clear that "a contribution by a taxpayer of the right to use property shall be treated as a contribution of less than the taxpayer's entire interest in such property," and therefore, the deduction is disallowed.[253] Based on this statutory language, if the taxpayer is merely granting the fire department the right to use the property for a live burn, no deduction should be allowed under § 170(f)(3)(A), and the Service's use valuation argument contended in *Scharf* is now moot.[254] On the other hand, if the taxpayer is not donating a right of use, but rather the structure in its entirety, such is the transfer of the taxpayer's entire interest.[255]

In the U.S. Tax Court case *Zand v. Commissioner*, the taxpayer donated a single-family stucco house to the City of Columbus, Ohio, on the condition the city remove the structure to a nearby city park.[256] The taxpayer also provided the city with $13,000 to account for the removal costs of the structure.[257] The taxpayer claimed a charitable deduction for the money and property contributed to the city on his 1976 income tax return.[258]

---

251. *See* Scharf v. Comm'r, 32 T.C.M. (CCH) 1247, 1252-53 (1973).

252. *Rolfs*, 135 T.C. at 288 n.14.

253. *See* I.R.C. § 170 (f)(3)(A) (2006).

254. *See Scharf*, 32 T.C.M. at 1253.

255. *See id.* at 1253.

256. Zand v. Comm'r, Nos. 32434-88, 32435-88, 1996 WL 23266, at *55, 99 (U.S. T.C., Jan. 23, 1996), *aff'd*, 148 F.3d 1393 (11th Cir. 1998) ("On Schedule A of his 1976 income tax return, petitioner claimed a deduction for a charitable contribution of $51,662.62 to the City of Columbus for a house that had been situated on the lot he purchased in 1975 at 3404 Riverside Drive, Columbus, Ohio, adjacent to CTC's office building. The house had been rented, but petitioner decided to give it to the city by moving it across the road on the other side of the river where it would be used as a public place. He also gave the city $13,000 for the expense of moving the house to the park.").

257. *Id.*

258. *Id.*

The Service alleged (pre-§ 280B) that the house was acquired with the intention to remove or demolish it, and thus, the taxpayer's associated costs should be considered land acquisition costs under Treas. Reg. § 1.165-3(a)(1).[259] The court disagreed with the Service, holding that the taxpayer did not acquire the stucco house with the intent to demolish it, and that the structure was merely removed - not demolished.[260]

Along the path of *Zand* and *Rolfs,* if a taxpayer presently wanted to be incredibly clear in an effort to avoid any Service arguments under the split-interest rule, the taxpayer could request the structure be removed to another location to resolve all partial interest doubts.[261] Removal of the structure from the taxpayer's property would still, however, trigger quid pro quo issues with any removal costs inuring to the benefit of the donor if paid for by the fire department.[262] For most landowners, physically removing the structure from the lot would also be cost prohibitive, as was the case in *Rolfs.*[263] Finally, the *Zand* case sends a warning shot to taxpayers that the Service in similar circumstances (e.g., live burns scenarios) may find itself arguing the § 280B wrinkle.[264]

Taxpayers contributing structures to fire departments must also comply with the substantiation requirements under the regulations promulgated by the Secretary.[265] Treas. Reg. § 1.170A-13(c)(2)(i) requires charitable contributions in excess of $5,000 be evidenced by a "qualified appraisal," of which, a summary is attached to the tax return, and adequate records of

---

259. *See id.* ("The claimed charitable deduction was disallowed by respondent on the ground that the house was acquired with the intention to remove or demolish it when it was acquired . . . consequently, the cost should be considered land acquisition cost, with the house having no fair market value at the time of the transfer. Where property is purchased with the intent of demolishing an existing building, either immediately or subsequently, the entire basis of the property is allocated to the land, increased by the net cost of demolition, and no loss is allowed for the demolition of the building.").

260. *Id.* at *100 ("We reject respondent's contention that petitioner intended to demolish the house when he purchased it some 14 months before he gave it to the City of Columbus, Department of Recreation and parks.").

261. Zand v. Comm'r, 71 T.C.M. (CCH) 1829-30 (1996) ("The provisions of section 1.165-3, Income Tax Regs., are inapplicable in these circumstances for two reasons. . . . The second reason is that the house was not demolished, but was removed to a park and apparently is still being used.").

262. *See* Singer Co. v. United States, 449 F.2d 413, 423 (Ct. Cl. 1971).

263. For a discussion of the various costs relating to structure removal, see http://www.comeandtakeithousemovers.com/house_moving_faq.php.

264. *See* Muraskin, *supra* note 241.

265. I.R.C. § 170(a)(1) (2006) ("A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary.").

the structure's donation must be maintained.[266] An appraisal of the donated building is not "qualified" unless it is made no earlier than 60-days prior to the date of contribution to the fire department, nor later than the due date of the return on which the deduction was claimed.[267] The taxpayer must also complete and attach to the return a Form 8283 (Noncash Charitable Contributions).[268] If a taxpayer fails to obtain a timely written appraisal, as required by the regulations, the charitable deduction will be disallowed.[269]

Fire departments participating in quid pro quo exchanges with taxpayers also have certain disclosure requirements under§ 6115(a).[270] Under § 6115, a charitable organization involved in a quid pro quo exchange in excess of $75 is required to provide the donor with

> a written statement which – (1) informs the donor that the amount of the contribution that is deductible for Federal income tax purposes is limited to the excess of the amount of any money and the value of any property other than money contributed by the donor over the value of the goods or services provided by the organization, and (2) provides the donor with a good faith estimate of the value of such goods or services.[271]

A good faith estimate of the fair market value of the services provided by the fire department may be made by using any

---

266. Treas. Reg. § 1.170A-13(c)(2)(i) (1996) ("Except as provided in paragraph (c)(2)(ii) of this section, a donor who claims or reports a deduction with respect to a charitable contribution to which this paragraph (c) applies must comply with the following three requirements: (A) Obtain a qualified appraisal (as defined in paragraph (c)(3) of this section) for such property contributed. If the contributed property is a partial interest, the appraisal shall be of the partial interest. (B) Attach a fully completed appraisal summary (as defined in paragraph (c)(4) of this section) to the tax return (or, in the case of a donor that is a partnership or S corporation, the information return) on which the deduction for the contribution is first claimed (or reported) by the donor. (C) Maintain records containing the information required by paragraph (b)(2)(ii) of this section.").

267. *Id.* § 1.170A-13(c)(3)(i).

268. *See* Instructions for Form 8283, http://www.irs.gov/pub/irs-pdf/i8283.pdf (last visited Oct. 9, 2010).

269. Diess v. Dep't of Revenue, No. TC-MD 0700245D, 2008 WL 495480, at *4-5 (Or. T.C. 2008). In *Diess*, the Oregon tax court denied the taxpayers' charitable deduction because they failed to obtain a qualified appraisal within the specified time period in the regulations. *Id.*

270. *See* I.R.C. § 6115(a) (2006).

271. *Id.*

reasonable method in good faith.[272] If the services are not otherwise commercially available, such as is the case with fire personnel burns, the charitable organization may determine fair market value by making reference to the "value of similar or comparable goods or services."[273] The fair market value of demolition services provided by a third-party demolition company should suffice, as both services result in ultimate demolition.

V. CONCLUSION

Taxpayers wishing to claim a charitable deduction for a live burn contribution are thus faced with the assortment of thorny legal issues mentioned supra with varying degrees of legal uncertainty. The days of *Scharf* and its loose application of the quid pro quo doctrine and incidental benefit exception are history. Taxpayers now must arm themselves for a fiery battle with the Service when taking such an aggressive position. A blanket declaration that the quid flowing back to the donor is merely incidental and that the taxpayer is somehow relieved from the two-part gift test will not suffice, as such is a misinterpretation of the relevant case law, administrative rulings, and regulations. As discussed in this article, the judicial and administrative tidal drift away from *Duberstein,* and towards the more objective structural analysis of Revenue Ruling 67-246 and *American Bar Endowment*, mandate a much tighter application of the quid pro quo rule as provided for in *Rolfs*.

Prudent taxpayer preparation thereby entails at a minimum a qualified appraisal of the structure and valuation of the demolition services *before* the donation is made.[274] As demonstrated in *American Bar Endowment,* the taxpayer must prove actual knowledge of the excess value donated to the

---

272. Treas. Reg. § 1.6115-1(a)(1) (1996) ("A good faith estimate of the value of goods or services provided by an organization described in section 170(c) in consideration for a taxpayer's payment to that organization is an estimate of the fair market value, within the meaning of § 1.170A-1(c)(2), of the goods or services. The organization may use any reasonable methodology in making a good faith estimate, provided it applies the methodology in good faith. If the organization fails to apply the methodology in good faith, the organization will be treated as not having met the requirements of section 6115. See section 6714 for the penalties that apply for failure to meet the requirements of section 6115.").

273. *Id.* § 1.6115-1(a)(2) ("A good faith estimate of the value of goods or services that are not generally available in a commercial transaction may be determined by reference to the fair market value of similar or comparable goods or services. Goods or services may be similar or comparable even though they do not have the unique qualities of the goods or services that are being valued.").

274. Treas. Reg. § 1.170A-13(c)(2)(i) (1996).

charitable organization.[275] Without appraisals beforehand, how could one evidence such? Merely presuming that the donated structure's value is in excess of the demolition services will not suffice.[276] Remember, the *sine qua non* of such a charitable transfer should be the transfer of a structure to the fire department without adequate consideration.[277] Section 280B is also a formidable roadblock the Service may erect in its deduction disallowance argument, as well as the split-interest rule of § 170(f)(3).[278] *Rolfs* also has closed the door for taxpayers claiming the deduction, arguably completely, as it has significantly strangulated the fair market value of the donee benefit, while enhancing the value of the donor benefit.

When claiming the charitable deduction, one must also be aware of the tax preparer penalty and the substantial understatement accuracy related penalty under §§ 6694(a)(2) and 6662(d)(2)(B) respectively.[279] Both penalties require "substantial authority" for undisclosed tax return positions and a "reasonable basis" for disclosed positions.[280] Further, "[t]he substantial authority standard is less stringent than the more likely than not standard . . . but more stringent than the reasonable basis standard."[281] Substantial authority only exists if the weight of the authority supporting the desired tax treatment of an item is "substantial in relation to the weight of authorities supporting contrary treatment."[282] The exact weight of a particular authority depends on its "relevance [in light of subsequent developments], persuasiveness, and the type of document providing the authority."[283] *Scharf* postured alone is not substantial authority. Revenue Ruling 67-246, *American Bar Endowment*, Treasury Regulation § 1.170A-1(h)(1), and *Rolfs* arguably require contrary treatment.[284] A return position is adequately disclosed if the relevant facts affecting the item's tax treatment are adequately disclosed on the return or a statement attached to the return.[285] Therefore, a taxpayer or tax

---

275. *See* United States v. Am. Bar Endowment, 477 U.S. 105, 118 (1986).

276. *See id.*

277. *Id.*

278. I.R.C. §§ 170(f)(3), 280B (2006).

279. *Id.* §§ 6694(a), 6662(d)(2)(B).

280. *Id.*

281. Treas. Reg. § 1.6662-4(d)(2) (1996).

282. *Id.* § 1.6662-4(d)(3)(i).

283. *Id.* § 1.6662-4(d)(3)(ii).

284. *See* Rev. Rul. 67-246, 1967-2 C.B. 104; United States v. Am. Bar Endowment, 477 U.S. 105 (1986); Treas. Reg. § 1.170A-1(h)(1) (2008).

285. *See* I.R.C §6662(d)(2)(B)(ii)(I).

practitioner claiming a charitable deduction attributable to a live burn would be well advised to disclose such on the return or the appropriate form.[286]

286. Disclosure that is not evident on the return itself is made on Form 8275, unless the position is contrary to a treasury regulation in which case Form 8275-R is used. Instructions for form 8275 can be found at http://www.irs.gov/pub/irs-pdf/i8725.pdf.