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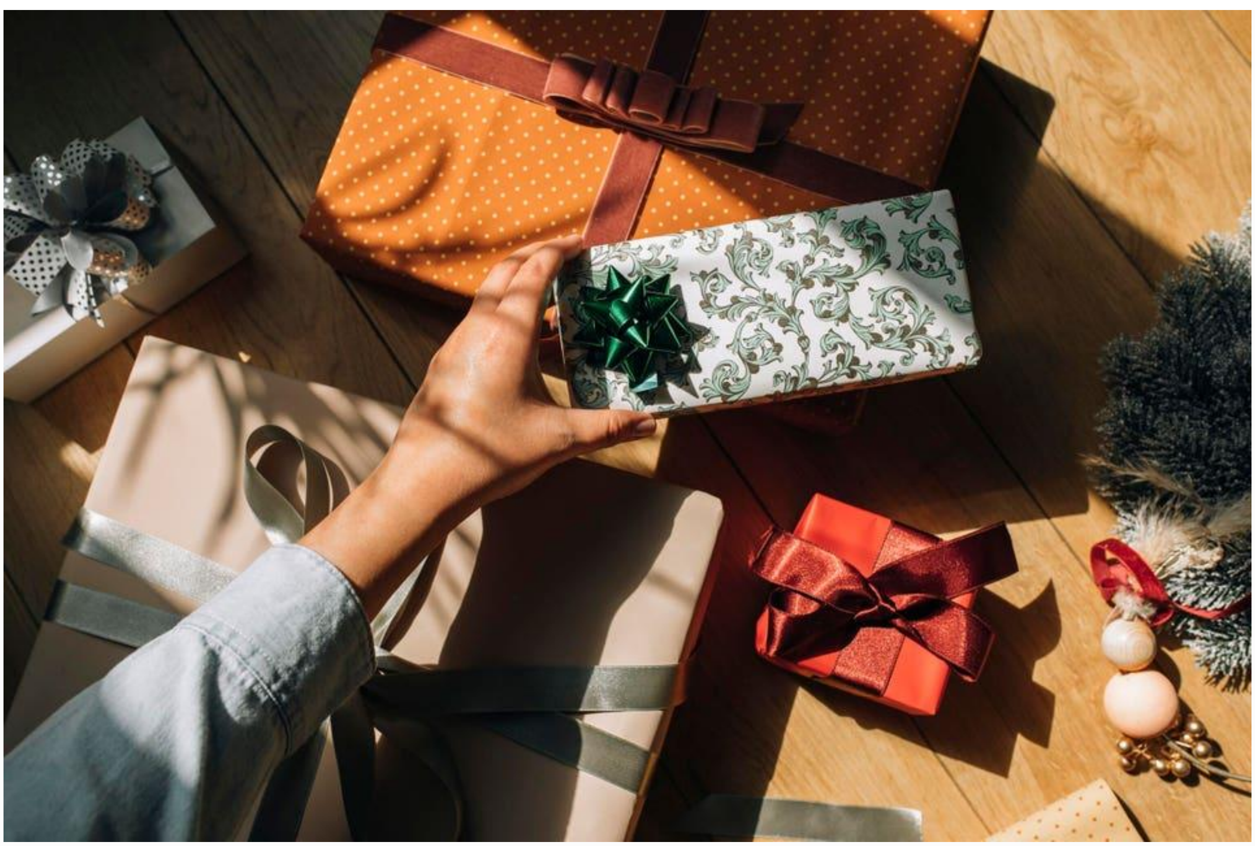
Navigating Tax Rules During The Season Of Giving



During the holidays, many people give gifts or donations, but distinguishing between the two can be important for tax purposes. The season begins with Thanksgiving. The classic [O. Henry story] "Two Thanksgiving Gentlemen" illustrates the spirit of giving. Each year, a homeless man receives a grand dinner hosted by a successful businessman. Ironically, the businessman is down on his luck and must pinch pennies to afford the meal, while the homeless man has already eaten other dinners that day and attends because he knows how important the tradition is to the businessman.

Charitable Contributions Are Different

Despite the generosity on both sides, the charity the two Thanksgiving gentlemen exchange isn't tax deductible. The IRS says business gifts made in the course of trade or business are deductible up to $25 per person. Is that amount reasonable today? Hardly. The limit hasn't kept pace and isn't tied to inflation.

Donations to recognized charities are different, but even if you give to a charity, you can't deduct the value of your time or services. That's true even if you usually bill by the hour and donate many hours of otherwise billable time. You also can't deduct gifts made directly to people in need, even if you're trying to make sure your money does some good. You can read the IRS' take on charitable contributions [here].

Even if you've checked an organization's credentials and [IRS tax-exempt status], how do you know how much goes to overhead and what your money really supports? Public charities and churches are supposed to benefit the general public, not private individuals. Some charities pay executive salaries and offer perks that can make you squirm. Many funnel money to full

501(c)(3) charities, making contributions to those organizations tax deductible for donors. The stakes are high, and nonprofits often face IRS scrutiny.

Lavish spending and private inurement are classic problems for some nonprofits. When the IRS finds this, penalties can be assessed, and in extreme cases, the government can threaten to revoke the charity's tax exemption. Large payments for goods or services don't necessarily violate the law, but the IRS reviews them to ensure there's no private inurement. The key to such arrangements is whether the terms and conditions are at arm's length — the kind of deal unrelated parties would strike.

If a tax-exempt church or charity pays a founder or someone else more than fair value for goods or services, it can jeopardize the organization's tax-exempt status. There's a particularly big risk if it looks like the charity is the founder's private fiefdom. How does the IRS find out? Although tax-exempt, these charities must file tax returns on IRS Form 990.

What About Gift Tax?

Gifts are not taxed as income to the recipient, so if any gift tax is due, the giver pays it. There is a $19,000 annual exclusion from gift tax for as many people as you want, regardless of whether they are family. That's the amount for 2025, and it will stay the same in 2026. If you go over $19,000 per person — including birthdays and Christmas — it counts against your lifetime gift and estate tax exclusion, which is about $15 million for 2026.

The moral? When it comes to giving, don't be guided solely by taxes, like the two Thanksgiving gentlemen. Better yet, get tax advice before you act. And make sure your donee can use what you give. In O. Henry's "The Gift of the Magi," a struggling young couple wants to exchange something special for

Christmas. Della cuts her flowing hair and sells it to a wig maker to buy a platinum chain for her husband Jim's heirloom pocket watch. Jim sells his prized watch to buy combs for Della's hair. It's a lovely story about the spirit of giving, but each ends up with something they can no longer use. Sometimes, tax deductions are like that too.