

Restricted Gifts to Churches ... it's all about honoring the restrictions

By Dan Busby

DONORS SOMETIMES RESTRICT THE CHARITABLE GIFTS they make to a church. Some of these restricted gifts are encouraged by churches when funds are raised for a capital campaign, missions or other projects.

Donor-imposed restrictions create specific responsibilities for the church—starting with the fundamental principle of honoring the donor's restrictions. It's essential for churches to:

1. Understand the difference between donor restrictions and donor preferences. Though seemingly subtle, the distinction between a donor's restriction and a donor's preference is very important. This distinction can make a difference between the donor's eligibility for a charitable tax deduction and no tax deduction.

A donor's *restriction* on a gift limits the church's use of the funds to the purposes specified by the donor, e.g., "This gift is made on the condition that . . ." or "This gift is restricted for XYZ project." Restricted gifts may be problematic for churches (and donors) if the restrictions accompanying a gift:

- prevent the church from using the donation in the furtherance of its charitable purposes. For example, if a donor restricts a gift for the benefit of a specific individual (such as a particular benevolent recipient, an employee of the church, etc.), the gift is generally not deductible as a charitable contribution.
- are incompatible with the mission of the church. Even though a restricted gift is exclusively charitable, it would be inappropriate for a church to accept a gift requiring the expenditure of funds outside its mission.
- are at odds with the best interests of the church. A restricted gift could be exclusively charitable and compatible with the mission of the church and still not be in the best interests of the church. A church might not have the capacity to comply with gift restrictions. Or, the administrative requirements of a restricted gift could consume an inordinate amount of the church's resources.

A donor's *preference* stops short of a restriction in that the donor is simply communicating a desire and not a restriction (e.g., when the donor expresses a wish, desire or preference that the gift be used for a certain project, but the church has full discretion to decide whether to use the gift for the certain project or use it for any other purpose).

The exact wording used by the donor (or wording of a

solicitation to which the donor responded) will often determine whether the donor restricts a gift, or simply indicates a preference. In the latter case, even when the preference is for the funds to go to a particular individual, the gift will often qualify for a charitable tax deduction, if the church exercises adequate due diligence with respect to the gift.

2. Understand the difference between church and donor control. A common misconception is that the control a church must exercise over any donor-restricted gift is in conflict with, or contradictory to, stipulations by donors. *This is not true.* Some believe that churches should not follow donor restrictions, from time to time, to demonstrate their control. *This is inappropriate.*

Church control and donor restrictions are really a "hand in glove" concept. It's not *either/or*, but *both/and!* Restricted gifts must be used for a specific exempt purpose, whereas unrestricted gifts may be used for any exempt purpose.

The church must control all contributions to ensure the funds are used exclusively for its exempt purposes. In addition, the church must provide reasonable measures to ensure that donor-restricted gifts are used for the intended exempt purpose(s).

Notifying the donor on the gift response vehicle that the church will exercise control and discretion over the gift does not remove the donor's restriction placed on a gift. Churches must exercise control and discretion over *all* charitable gifts, whether unrestricted (may be used for any exempt purpose) or restricted (may be used for a specific purpose) by the donor.

3. Understand that restrictions are only made by donors, not by a church's governing board. Only donors can restrict a gift—either temporarily or permanently.

Designations of unrestricted assets by a church do not result in restricted contributions or restricted net assets, since the designations may be reversed by the church and they do not alter the nature of the donor's contribution. For example, unrestricted assets or net assets do not become restricted merely because a church governing board designates a portion of them to fund future expenditures for a new building.

Churches can designate (and subsequently undesignate) unrestricted net assets, but churches cannot unrestrict otherwise donor-restricted gifts. However, donors do have the power to unrestrict gifts.

Summary. Donor-restricted gifts are often win-win situations for the church and the donor. To maintain integrity, churches must step up in their responsibility to properly administer these restricted gifts.

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