

GIVING IT BACK: Returning Donations

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Once upon a time, churches thought that it owned the offerings it received. A church could spend the money because it became the church's money once it was placed in the offering plate. But now churches are being confronted with requests to turnover donations at a dizzying pace. This article will discuss the general rules governing such requests.

REAL LIFE EXAMPLES

No. 1. The Securities and Exchange Commission (SEC) recently contacted several churches. The SEC is investigating Mr. Q regarding securities fraud. Since Mr. Q donated \$100,000.00 to each church the SEC is requesting the churches to turnover donations received from Mr. Q.

No. 2. A church was contacted by the police about donations received from a certain Mr. R. The police claim that Mr. R embezzled \$70,000.00 from his employer and donated the money to the church's building program. Mr. R's employer demanded that it turnover the money received from Mr. R.

No. 3. Still another church was contacted by the spouse of a member. During a recent capital campaign at the church, the member donated \$400,000.00 to the campaign. The spouse is requesting that the church turnover the \$400,000.00 because the member did not own the \$400,000.00. It came from the spouse's separate property.

No. 4. Mr. A typically donated 10% of his adjusted gross income (AGI) to his church and also gave 10% of his AGI in the year before he filed a bankruptcy petition. Ms. B typically donated 5% of her AGI to the church. In the year before her bankruptcy filing, she donated 25% of her AGI to her church. In each instance, the Bankruptcy Trustee informed the churches that a member had filed bankruptcy and requested the churches to turnover donations received from the member who filed bankruptcy.

No. 5. During a recent stewardship campaign, a church member gave a donation under the condition that the money must be spent on the church organ within twelve months. The church accepted the donation, along with the conditions. The church did not spend the money on the organ as required by the donor. The donor requests the church to turnover the donation since the conditions were not met.

No. 6. Recently a long time, prominent member lost his executive position. His savings have run out and he will lose his house to foreclosure next month. Last year he gave a special offering of \$25,000.00 to help the church when the regular

offerings fell short of paying the church's bills. He now requests that the church return the \$25,000.00 to help him pay his bills.

These are just a few examples where churches have been requested to turnover a donation. What are the rules?

ESTABLISHING OWNERSHIP

Investment schemes are alive and well in the church. SEC regulates investment schemes. Christian investors will donate their gains to the church. Sometimes those gains have been derived from fraudulent or illegal investment schemes. The SEC reports that recent fraudulent investment schemes perpetrated through churches have resulted in investor losses exceeding \$1.5 billion. Due to the investors' donations, the church becomes a part of the SEC investigation and a recipient of fraudulently acquired moneys.

If an initial transfer is due to fraud, then the courts are mixed whether the transfer is effective to transfer ownership. The courts use a facts and circumstances to determine the ownership. Generally, the court will allow a government agency, such as the SEC, to recover property that was part of a fraudulent scheme.

Sometimes, a church member will receive stolen property or money (on purpose or by accident). The stolen property or money is donated to the church, sometimes to cover the theft.

When one steals property or money the ownership does not change. The thief cannot give away something he does not own. So, if the thief gives the church stolen property or money, then ownership remains with the original owner and the church is obligated to give it to the rightful owner.

When the church first becomes aware that it may have received stolen property, the church should attempt to determine the rightful owner's identity. When the property is titled (such as a car), it is usually easy to determine ownership. If the property is not titled (such as a bicycle), then it is more difficult to establish ownership. Cash is the most difficult to establish ownership. Generally, the church must allow the courts to determine ownership of nontitled assets and cash. Cash ownership is established by tracing the possession of the cash from the rightful owner to the thief and from the thief to the church. To avoid large legal fees, the church may turnover the assets to the registry of the court. The court then has the obligation to determine the rightful owner and turnover that property to that person or entity.

When an individual is married, different ownership classes are created for property: marital property and separate property. Every state has different rules to classify property ownership and authority to spend the property. Generally, one spouse has no rights to transfer the separate property of the other spouse. If a spouse acts without authority to transfer the other spouse's property, then it is treated the same as fraudulently conveyed property.

Applying these rules to the examples above, the church probably received stolen property or nonowned spousal property in Example Nos. 1, 2 and 3 above. Assuming the courts can trace the funds from the rightful owner to the church, then the church must turnover the donation.

BANKRUPTCY

Bankruptcy law in the United States goes back to the original constitution. One fundamental goal of bankruptcy law is treating all similarly situated creditors the same. To prevent the debtor from giving away his assets in the year before the bankruptcy filing, the Bankruptcy Code allows the Bankruptcy Trustee to recover such donations from the recipient. In 1998, Congress amended the Bankruptcy Code to exclude certain charitable and religious gifts from the general rule. The Bankruptcy Trustee may recover from the church the donations received from a debtor in the year before the bankruptcy petition filing to the extent the donations exceed the greater of (1) 15% of the debtors AGI or (2) the average percentage of AGI that the debtor typically donated to the charity or church.

In Example No. 4 above, since Mr. A's donation percentage was less than 15% of Mr. A's AGI, the church will not be required to pay any amount to the Bankruptcy Trustee. In Ms. B's case, the church will be required to turnover to the Bankruptcy Trustee 10% of Ms. B's AGI (25% less 15%) that it received as a donation.

CONDITIONAL GIFTS

Sometimes donors attach conditions to their donations. The donor may require that the funds be spent on a specific project. Other times, the donors require that the funds be spent by a certain date. Conditions are not the same as a designation. A donor may designate that a donation be placed in a certain fund, while a condition requires (without excuse) that the church meet certain specific conditions. In a conditional gift, the donor retains control over the gift until the condition is fulfilled, while a gift to a designated fund transfers control of the gift to the church. Generally, a condition is evidenced by a written agreement between the donor and the church. Sometimes the donor puts the conditions in a letter or the church and donor will reach an understanding about the conditions.

First, conditional gifts are not tax deductible until all the conditions are removed. Second, ownership does not transfer to the church until the conditions are met. Applying these principles to Example No. 5 above, the church must return the gift.

REQUESTS FOR RETURN OF DONATIONS

Churches are frequently requested to return donations for a variety of reasons. Sometimes the donor changes her mind. Other times, circumstances have changed, such as a pastoral change, and the donor no longer wants to support the church.

These circumstances are difficult at best. There is no pat answer. The church must act in its best interest under these circumstances. Sometimes, no legal obligation exists that requires the return of the donation. If the church sets a pattern of allowing returns of donations, then the IRS may claim that church is serving the private interest of the donors and not an exempt purpose. Sometimes, the church becomes an unknowing participant in a money-laundering scheme. In some cases, the church may feel a moral obligation to honor the request.

Every request of a return of a donation is serious. If the request is denied, the donor may sue the church. If the request is granted without a firm legal basis, the church may lose its tax-exempt status or become part of an illegal scheme. Due to the material risks involved, the church should engage competent legal counsel every time before considering the request.

In Example No. 6, the church should engage an attorney to advise them concerning this request. Under the circumstances, the church may consider the request not a return of a donation, but a request for benevolence. If the request meets the church's policy for benevolence, then it may pay the member his qualifying needs, without regard to his prior donations.

CONCLUSION

Churches should not consider turnover of material donations without competent legal advice. Very few lawyers have been involved in cases like these, so securing quality legal advice is difficult. The church should ask about the lawyer's experience representing churches under these circumstances before hiring them.

The church should also establish written policies governing large donations. The policy should include follow-up with donors to ascertain the risks, if any, associated with such a gift. The church may want to establish reserves to allow it to turnover gifts if it is served with notice of a potential turnover situation.