



Guide to Smart Giving, Part 1

By Chad Davidson, Good Fellow CFO

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How Donations to a 501(c)(3) Work and Why They Matter

When you make a donation to charity, you might not think about all the details behind the scenes. However, knowing how donations to 501(c)(3) organizations work can help you understand the impact of your contribution—and might even save you some money on taxes! In this article, we'll explain the basics of 501(c)(3) donations in a simple way, so you can feel confident about how your generosity helps both the cause and your wallet.

What Is a 501(c)(3)?

A 501(c)(3) organization is a type of nonprofit group that has a special tax-exempt status under U.S. law. This means that these organizations don't have to pay federal income taxes like businesses or individuals do. But not all nonprofits are 501(c)(3)s—so what makes these groups different?

To qualify as a 501(c)(3), an organization must be set up for a purpose that benefits the public. These purposes usually fall into categories like:

- Charitable work: Helping people in need, such as through food banks or homeless shelters.
- Educational purposes: Teaching and providing resources, like schools or libraries.
- Religious groups: Churches, temples, and other faith-based organizations.
- Scientific research: Advancing knowledge for the benefit of everyone.

Organizations that meet these criteria can apply to the IRS (Internal Revenue Service) for 501(c)(3) status. If approved, they can accept donations that are tax-deductible for the donor.

How Your Donation Helps

When you give to a 501(c)(3), your donation is used to support the organization's mission. But where exactly does your money go? This depends on the charity. Some donations might be used to:

- Fund programs that directly help people or advance a cause, like feeding the hungry or protecting the environment.
- Pay staff and volunteers who run these programs.
- Cover operational costs such as rent, utilities, or the purchase of supplies.



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Reputable 501(c)(3) organizations will typically share how they use donations, either on their websites or in reports. This transparency helps donors like you understand how your money is being spent, so you can trust it's making a difference.

How You Can Get a Tax Deduction for Your Donation

One of the biggest benefits of donating to a 501(c)(3) is the potential tax deduction you can receive. A tax deduction reduces the amount of income you are taxed on, which can lower your overall tax bill. Here's how it works.

1. **Itemizing your deductions:** To claim a charitable donation as a deduction, you'll need to "itemize" your deductions on your tax return. This means listing all the deductions you're eligible for, instead of just taking the standard deduction (a set amount everyone gets by default). If your itemized deductions are higher than the standard deduction, it makes sense to itemize.
2. **Types of donations that qualify:** Not every donation is eligible for a tax deduction, but most contributions to 501(c)(3)s are. These include:
 - **Cash donations:** Money you give through check, credit card, or even apps like PayPal or Venmo.
 - **Property donations:** Things like clothing, furniture, or even cars can be donated, and you may be able to deduct their fair market value.
 - **Stocks or investments:** If you own stock that has gone up in value, you can donate it and avoid paying capital gains taxes.
3. **How much can you deduct?** In general, you can deduct up to 60% of your adjusted gross income (AGI) for cash donations. If you donate property or stocks, there are different rules, but the deduction is typically based on the value of the item at the time of the donation. Anything over these limits can usually be carried forward to future tax years.

What Records Do You Need?

To make sure you can take the deduction, the IRS requires that you keep certain records. These vary depending on the size and type of your donation:

- **For cash donations under \$250:** A receipt, bank statement, or other written confirmation from the charity will work.



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- For cash donations over \$250: You'll need a written acknowledgment from the organization that says how much you gave and whether you received any goods or services in return.
- For non-cash donations: If you're donating something other than money, like clothes or a car, you'll need to document what you gave and how much it's worth. For donations over \$500, you may need to fill out an extra IRS form (Form 8283).

If your donation is worth more than \$5,000 (like a valuable piece of art or a large stock gift), you'll also need a professional appraisal to back up its value.

Are There Limits on How Much You Can Deduct?

While the government wants to encourage charitable giving, there are limits on how much you can deduct. Generally, you can deduct up to 60% of your AGI in donations each year. However, for non-cash donations, the limit is often lower (typically around 30% of your AGI).

If your donations exceed the limit, don't worry—you can carry forward the excess deductions for up to five years, applying them to future tax returns.

Why Donating Matters

Donating to a 501(c)(3) organization doesn't just help you with your taxes—it helps make a real difference in the world. Your contributions support causes you care about, whether it's helping people, protecting animals, or fighting for the environment. And because these organizations are tax-exempt, they can use your donation more effectively to further their mission.

Plus, when you give to a charity, you're part of a larger movement. Even small donations add up, and together, we can create positive change in our communities and beyond.

Conclusion

Understanding how donations to a 501(c)(3) work can empower you to make informed decisions about your giving. Not only do these donations help important causes, but they also provide valuable tax benefits. By keeping good records and following the rules, you can make sure your generosity benefits both you and the organizations you care about.