

Tax Advantages of Rare Coins

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There is very little we do in the United States today that is not somehow affected by the tax laws. Buying and selling coins is no exception. But compared to other investment assets, rare coins have certain advantages. An understanding of these will not only assure compliance with the law, but may save you money as well. Of course, although I have tried to accurately present this complicated subject, be warned that tax laws change quite often and that differences in geography, income, and overall portfolio may change considerably the effect of taxes. You should always consult a competent attorney or tax advisor to update yourself and to tailor any tax strategies to your particular situation.

I – EXEMPTIONS FROM SALES AND USE TAX

State and local governments impose a sales tax on retailers for the privilege of retailing goods. Many tangible assets such as art and jewelry are exempt from sales tax if they are purchased from dealers located in a different state from the taxpayer. But rare coins, which are considered “monetized bullion”, are exempt from sales and use taxes in many states if they are purchased in amounts over \$1,000 or \$1,500 in a single invoice, even from dealers located in the taxpayer’s state. By avoiding sales tax, rare coin investors retain more of their investment while still having the option of doing business with local dealers.

II - INCOME TAX BENEFITS

Rare coins can be quite profitable investments. But unlike stocks, whose dividends are taxed annually even if they are in the form of new stock and not cash, income from the sale of coins is tax-deferred until the coins are sold. In other words, a coin investor can defer taxable gains until a time of his or her own choosing. However, rare coins remain capital assets for purposes of the reduced tax rate once the taxpayer has held them for 6 months. There are other potential benefits as well.

Treatment of Expenses and Capital Losses

Rare coin investors can deduct expenses relating to their coin portfolios such as grading fees, insurance, security, membership dues for collectors' clubs and subscriptions to relevant periodicals. The key to qualifying as an investor for tax purposes (rather than a collector) is whether the taxpayer is buying coins primarily for profit or for enjoyment. Of course, investors also enjoy their coins. But investors who show a profit from their coin purchases for three of the past five years, rely on the advice of experts when making their purchases, and who risk at least the possibility of losses in any particular year, will be classified as investors for tax purposes as well.

Serious coin enthusiasts might also consider taking the position that they buy and sell coins as part of a trade or business, i.e. as dealers. By doing so, they pay taxes on profits at ordinary income rates, but may deduct their expenses and net losses from coin sales against their other (non-capital gain) income. The IRS may resist, but over the years the regulations in this area have become much more taxpayer-friendly.

Deferring Taxes Through Like-Kind Exchanges

The "like-kind" exchange under Section 1031 of the Internal Revenue Code is another potential benefit of buying coins for investment. That Code provision allows investors to trade items which have appreciated in value for items of the same "nature or character" without recognizing income or capital gains on the transaction. The IRS has consistently held that coins qualify for Section 1031 treatment, such as in the following cases: Rev. Rul. 76-214 (Mexican 50-peso gold coins for Austrian 100-corona gold coins); Rev. Rul. 76-249 (pre-1964 U.S. silver coins for real estate); 79-143 (U.S. \$20 gold coins for Krugerrands – not like kind). For investors interested in shifting from one area to another, this can be a good tax-avoidance technique. However, it must be carefully done to conform to the Code, so I recommend doing this with a reputable dealer involved.

The initial requirement is that the items being traded and those received must be held purely for investment purposes, just as I described above for distinguishing investors from collectors. Then, the items must truly be of "like-kind", which trips up many investors in other types of assets but is not a difficult issue with rare coins. Basically, the taxpayer may not trade a pre-1933 \$20 gold piece for a "bullion" coin (such as a 2014 \$50 Buffalo gold piece) because the rare coin is seen as held for its collectible value while the modern coin is seen purely as a precious metal investment. However, for all intents and purposes any pre-1933 gold coin is considered "like" with any other such coin. Through like-kind exchanges, the taxpayer may defer income tax on any profit until final disposition, without limit. For example, an investor who purchases generic pre-1933 \$20 Saint Gaudens gold pieces and is in a substantial profit position may "trade up" to proof gold \$20s and not recognize any taxable gain, and later trade those coins for still other coins.

Holding Coins in IRAs

Until the Reagan 1981 tax law took effect on January 1, 1982, rare coins could be purchased for placement in an IRA or other retirement plan. Since that date, purchase of "collectibles" by a retirement plan has been deemed a distribution for tax purposes. However, in 1986 Congress began re-introducing coins into IRAs with the U.S. Mint American Eagle program. U.S. commemorative gold and silver coins dated 1986 and later may now be purchased for retirement accounts. IRA-eligible coins include American Buffalos, American Eagles and Proof American Eagles. When Congress designates such coins as IRA-eligible, it is indirectly encouraging Americans to invest in them. Every year, bills are introduced to expand the categories of coins eligible for inclusion in IRAs to all U.S. legal tender coins, which would encompass pre-1986 coins and return IRAs to their original intent.

Recently, taxpayers have begun asserting more control over their IRAs by holding assets in the name of a limited liability company (LLC) that they own, but which for legal purposes is sufficiently independent to act as an IRA trustee. The court cases decided so far (including one in 2014) are unanimous that this structure is legal in principle. Here's how it works. An IRA acquires an LLC and uses the LLC's bank account to buy coins. This conforms to all IRA requirements, provided no other "prohibited transactions" take place. For example, taxpayers should not pay themselves management fees or hire family members to manage the LLCs.

Avoiding 1099 Filing Requirements

IRS reporting requirements apply to dealers purchasing certain precious metal coins and bars from collectors and investors beyond established dollar thresholds, meaning that the dealer will issue a Form 1099 notifying the IRS of the date and gross amount of the purchase, as well as the taxpayer's name, address and Social Security number. Which coins and in what quantities is complicated, but suffice it to say that rare coins are not subject to any 1099 filing requirements whatsoever, a huge advantage for precious metal investors concerned with privacy.

For a short time after passage of the Affordable Care Act in 2010, much was written about a provision in that law that required businesses to file 1099s whenever they made purchases of any kind in excess of \$600. There was concern that coin investors' privacy would be invaded, with 1099s being filed every time an investor sold a coin. While most of the Obamacare law remains intact, this particular provision was repealed by a bi-partisan vote in Congress before it even took effect.

III – TAXES/DUTIES ON IMPORTING OR EXPORTING COINS

Simply put, there aren't any. Rare coins enter and leave the U.S. duty-free and tax-free. For pre-1933 U.S. coins in particular, there are no duties because the coins remain legal tender and were originally manufactured in the U.S. While large values of coins should be declared when imported into the U.S., there is no duty. The same is true for the exportation of coins.

Moreover, while the U.S. requires reporting of exportation or importation of more than \$10,000 in currency or currency-type instruments, pre-1933 U.S. coins are not considered currency beyond their stated face values. So for currency control purposes, a 1927 \$20 gold piece is valued at its legal tender value of \$20, even if its numismatic value is much higher

IV - ESTATE PLANNING AND CHARITABLE DONATIONS OF ART AND COLLECTIBLES

Estate Tax

Most taxpayers need not concern themselves with estate tax avoidance. Based on current (2014) estate tax thresholds, only those whose estates are likely to exceed \$5,340,000 have any estate tax liability. In addition, the unlimited marital deduction is still in effect, allowing a taxpayer to bequeath his or her entire estate to a spouse tax-free. Nevertheless, these tax thresholds change and taxpayers likely to leave substantial estates upon death should work with competent professionals to develop an appropriate estate plan. All taxpayers possessing substantial coin collections should be aware of the basic rules governing their part in an estate plan.

Under Section 1014(a) of the Internal Revenue Code, the decedent's basis in his or her coin portfolio will be "stepped-up" to the fair market value at time of death. This can be a huge benefit if proper planning is done. For example, by bequeathing coins to a spouse, the decedent allows the spouse to acquire the coins tax-free at their fair market value at the time of death, and not at what the decedent originally paid for the coins. The spouse can then sell the coins without recognizing any gain or income, years' worth of appreciation in value going untaxed. Most of these same benefits also accrue to taxpayers who make gifts of coins to their spouses during their lifetimes, although certain guidelines should be followed when doing this. The stepping-up is also beneficial to non-spouses who receive coins in the decedent's will.

Charitable Gifts of Art or Collectibles

Taxpayers often make lifetime or testamentary (by will) gifts of appreciated art and collectibles to charitable organizations. Indeed, many taxpayers create charities just to receive, manage, and distribute their collections. The intricacies of using tax-exempt organizations for philanthropic or tax-avoidance purposes is beyond this article, but here are a few basic questions to consider.

The first question is whether the coins being donated are long-term capital gain property. If so, the donor may deduct the full fair market value of the coins at the time of the gift, including market appreciation. If not, the donor can deduct only his or her actual basis in the coins, which is generally the amount the donor paid to purchase them. Generally speaking, coins held over one year will be considered long-term capital gain property.

The next question is the use to which the charity puts the donated coins. Charities sometimes accept gifts for their own use as part of their regular activities, and in other cases charities sell gift items as part of their fund-raising. According to the Internal Revenue Code, items of tangible personal property which the charity puts to a use "not unrelated" to the charity's tax exempt purpose may be deducted to their full fair market value, but items which the charity uses for "unrelated" purposes may not. Here is the example given by the IRS in Publication 526, entitled "Charitable Deductions":

"If a painting contributed to an educational institution is used by that organization for educational purposes by being placed in its library for display and study by art students, the use is not an unrelated use. But if the painting is sold and the proceeds are used by the organization for educational purposes, the use is an unrelated use."

The most common "unrelated use" in the art and collectibles field is the charity auction, where collectors donate items to be sold for the benefit of charitable organizations. The IRS's example demonstrates the peculiar nature of the "related-unrelated" distinction. A collector choosing between two organizations to which to donate a particular item might well find that one organization would put the item to a related use while the other would not. An example would be donating a coin collection to the American Numismatic Association rather than to the local ballet company. If the coins have appreciated greatly over time, donating to the ANA might result in a much higher tax deduction. Be sure to get expert advice here.

Valuations/Qualified Appraisals

Valuation of coin portfolios is very important to obtain maximum tax benefits. An executor of an estate will want to understate values in the taxable estate while at the same time hoping to get away with overstating the value of items bequeathed to a spouse. Taxpayers also want high valuations for coins they donate to charity (for their income tax deductions) and low valuations for gifts to non-spouses (to reduce or eliminate gift tax). The IRS, if it reviews the appraised values, will tend toward the opposite positions in each situation (low valuations for charitable gifts and high valuations in estate situations), and the IRS employs experts who often back up their positions. This is an inherent conflict that shows up quite often in evaluating estate tax returns and charitable deductions of art and collectibles.

We start with the purpose and use of an appraisal. Insurance appraisals have different requirements and can represent different values than estate tax or charitable donation appraisals. Appraisals that will be used for tax purposes require the use of “fair market value”. IRS regulations define fair market value as “the price that property would sell for on the open market. It is the price that would be agreed on between a willing buyer and a willing seller, with neither being required to act, and both having reasonable knowledge of the relevant facts.” Experts will disagree over what “market” to use in measuring fair market value, as between retail, wholesale, or auction. Substantial differences may exist between these different market levels, and taxpayers may expect the IRS to seek the prices most favorable to their positions.

The best way to minimize valuation problems is to employ a professional appraiser who follows guidelines set forth in IRS Publication 561, “Determining the Value of Donated Property.” These guidelines require appraisals to include references to sales of comparable items, such as other works by the same artist for works of art, as well as some statement regarding the present market in the type of item being appraised. They also limit who can act as an appraiser in this context. He or she must either be a certified appraiser or met certain minimum education and experience requirements, and have demonstrated verifiable education and experience in valuing specific type of property valued. For coins, look for an experienced national dealer rather than the local coin shop. The IRS imposes additional requirements for appraisals supporting charitable deductions.

Acknowledgment and Reporting Requirements

For any donation of over \$250 in value, the donor must receive an acknowledgment from the charity at the time of the donation in order to take a charitable deduction on the item(s). This acknowledgment must be in writing, must be signed by an appropriate person within the charity, and must describe in reasonable detail the item being donated. Note that the acknowledgment is not sent to the IRS by either the donor or the charity.

If the donation exceeds \$500 in value, the donor must file IRS Form 8283 with his or her tax return. That form requires information regarding the charity, the date of the gift, a description of the property and the donor’s original cost basis in the property.

For donations above \$5,000, the donor must get a written appraisal, must summarize the appraisal on Form 8283, and must have the charity sign the Form 8283. By signing the Form 8283 the charity does not agree that the donor’s valuation of the item is correct. The donor does not send the appraisal itself to the IRS, but only a summary.

Finally, when donating art valued at over \$20,000, the written appraisal itself must be attached to IRS Form 8283 and filed with the donor’s tax return. For items valued at \$50,000 or more, the IRS will (for a fee) provide a statement of value from its Art Advisory Panel, which statement can be used in connection with the taxpayer’s tax return.

CONCLUSION

Coins bring much enjoyment to their owners, but they can also provide substantial benefits to knowledgeable collectors and investors. These areas are complex, and there's no "one size fits all" strategy for maximizing these benefits. It's best to work with dealers, attorneys and financial advisors who understand coins' tax treatment and also know the taxpayer's particular situation.

About Rare Coin Wholesalers:

Rare Coin Wholesalers specializes in high-end, investment grade rare U.S. coins. The principals of RCW have performed over \$1 billion in rare coin transactions and owned or participated in the purchase or sale of over 70 of the "100 Greatest U.S. Coins". In addition to the inventory of fine rarities, Steve Contursi, President of Rare Coin Wholesalers, has been a proud custodian of some of our nation's greatest national treasures.

Major purchases to date include the 1794 Flowing Hair Silver Dollar, the "Unique" 1787 Brasher Doubloon, and the finest-graded specimen of America's "Most Beautiful Coin" the MCMVII 1907 Proof Ultra High Relief Double Eagle.



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