TAX-SMART CHARITABLE GIVING,
ESPECIALLY WITH RETIREMENT ASSETS

Hawaiʻi Community Foundation
Hawaiʻi Estate Planning Council
Hawaiʻi Gift Planning Council

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TAX-SMART CHARITABLE GIVING

- Fewer deduct charitable gifts after 2017 TCJA
- Donor advised funds
  - “bunching” tax deductions into tax years
- QCDs from IRAs
  - Advantages
  - Trap after the SECURE Act – how to avoid
- Stretch an Inherited IRA with a CRT?

CARES Act
Charitable Planning Implications

On Year 2020 federal income tax returns:

1. **For donors who don't itemize tax deductions,**
   - **a. Up to a $300 income tax deduction for charitable cash gifts.**
   - **b. In 2021 – same, and also up to $600 on married joint returns**

2. In 2020 and 2021, For donors who do itemize deductions, the maximum income tax deduction for cash charitable gifts can be increased to 100% of AGI, (from 60% of AGI).

$ to DAFs, SO & PFs not eligible; be careful not to waste other dedns

3. In 2020 and 2021, Corporations can deduct up to 25% of taxable income for charitable gifts, up from 10%.

Who Gets Tax Benefits from Charitable Gifts?

- Donors who itemize tax deductions
  (who don't take the "standard deduction")

Impact of 2017 tax changes

- Number of taxpayers who deducted charitable gifts fell from 33 million tax returns in 2017 to just 12 million tax returns in 2018.

* Will Congress eliminate $10,000 SALT in 2021?

WHAT TO DO ?
Tax Saving Strategies for Charitable Gifts

- Don't forget the 11% who itemize their tax deductions
- "Bunching" charitable gifts every few years
  -- donor advised funds have become more popular
- Most donors over age 70 ½ should make *ALL* of their charitable gifts from their IRAs:
  "Qualified Charitable Distributions" (QCDs)

"Bunching" Gifts

- Example: Married donors contribute $10,000 per year to charities.
  - But with $10,000 SALT limit, their itemized deductions are only $20,000.
  - So they take the $24,000 standard deduction instead
  - They get no tax benefit from their charitable gifts
- BUNCH gifts: Contribute $40,000 to a DAF.
  - They can itemize this year. Tax savings from gifts.
  - The DAF distributes $10,000 annually over the next four years to their favorite charities

PHILANTHROPIC CHOICE OF CHARITABLE ENTITY

- **DONOR ADVISED FUND**

  -- a fund or account owned by a sponsoring public charity where the donor (or person appointed by the donor) can recommend grants <u>or</u> investments

PHILANTHROPIC CHOICE OF CHARITABLE ENTITY

- **DONOR ADVISED FUND**

  -- lower administrative costs

  -- grants to any public charity

  -- very popular: grants from donor advised funds already exceed 40% of grants from private foundations

Who Offers Donor Advised Funds?

- Traditionally – Local Community Foundations
  - *The Greater Kansas City Community Foundation*
  - *Hawai'i Community Foundation*
- Since 1993, "National DAFs" Associated With Financial Establishments
  - *Fidelity, Schwab, Vanguard, Goldman Sachs, etc.*
- And, national charities, colleges and universities,
  - *The National Christian Foundation*
  - *Harvard University*
  - *University of Hawai'i*

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Donor Advised Funds

2019 Donor-Advised Fund Report
National Philanthropic Trust

- 729,000 – Number of DAFs in 2018
- $121 billion – assets held by DAFs
- $ 37 billion – contributions to DAFs
- $ 23 billion – grants paid by DAFs
- 2,500 – Organizations with DAFs

Growth in Number of Donor Advised Funds

Year	Number
2015	273,000
2016	290,000
2017	463,000
2018	729,000

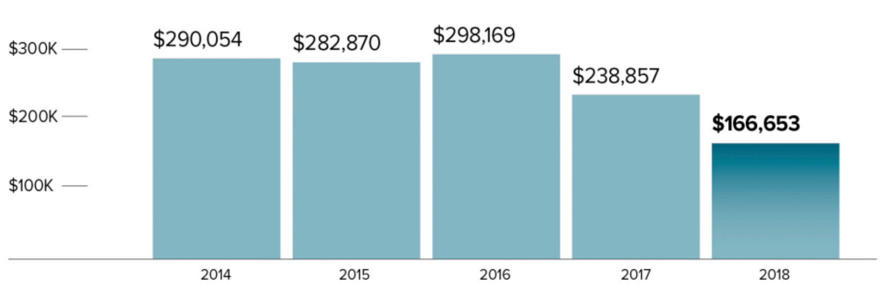
The vast majority of DAFs are less than five years old

Average Dollars in Each DAF Continues to Decline

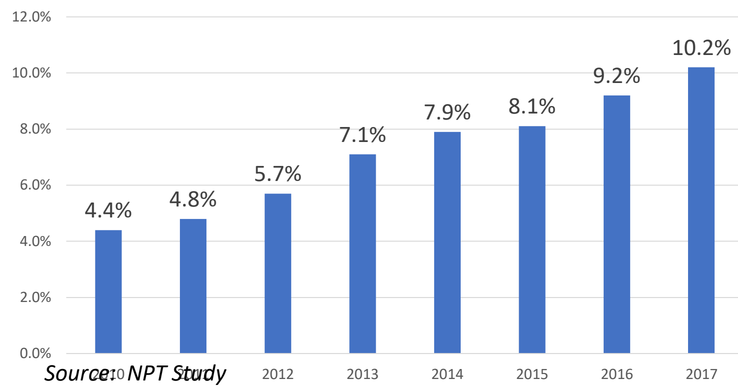
New DAFs tend to be established with smaller dollar amounts

2019 DONOR-ADVISED FUND REPORT

FIGURE 6: Average Donor-Advised Fund Size



2018: Gifts to DAFs Were 10% of All Individual Charitable Giving



Source: NPT Study

Qualified Charitable Distribution -- Lifetime Gifts from IRAs –

- Law Permanent! 2015 PATH Act Dec 20.2015
- Eligible Donors:

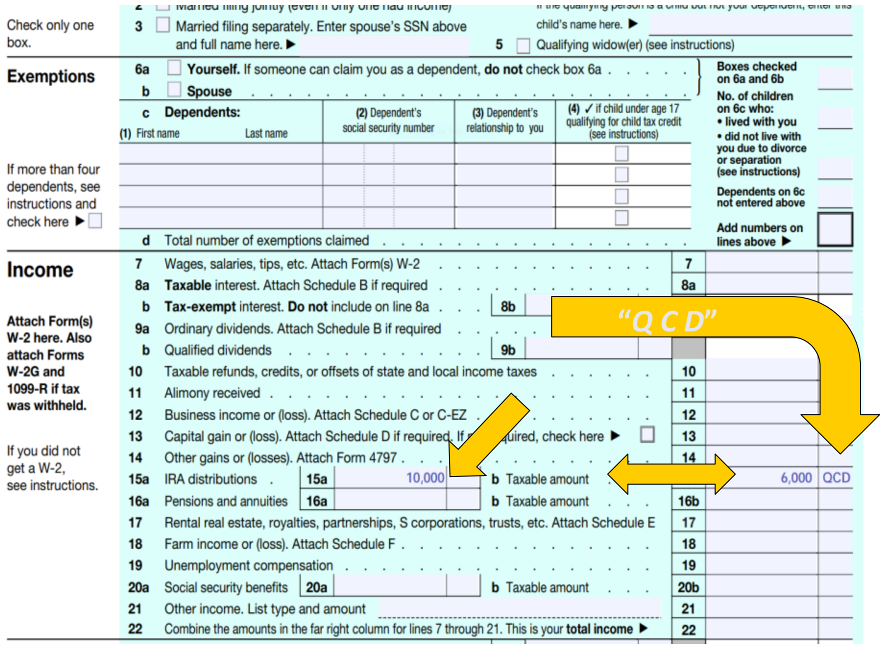
  -- Won't report charitable gifts from IRAs as taxable income

  -- Not entitled to charitable income tax deduction

❑ Example: Donor, age 75, who has a $10,000 RMD from IRA, says:

- ❑"Issue a check to a charity for $4,000
- ❑"Issue a check to me for $6,000"

s frc



Qualified Charitable Distribution -- Lifetime Gifts from IRAs --

- IRA owner must be over age 70 ½
- Maximum: $100,000 per year
- Yes! Charitable gift satisfies required minimum distribution requirement from IRA!

WHO WINS?

- Donors who do not itemize tax deductions ("standard deduction")
- Donors who live in states where the state income tax laws do not permit deductions for charitable contributions (Ohio, Indiana, etc)

WHO WINS ?

- Donors who incur taxes as their income increases

-- social security benefits taxable

-- Medicare "B" premiums

-- 3.8% health tax if AGI>$200,000

- The heirs

-- inherited stock gets step-up tax basis

-- inherited IRAs are taxable income

LEGAL REQUIREMENTS

- Over age 70 ½
- IRA (only) – <u>not</u> 403(b), 401(k), etc.
- "Directly" from the IRA to charity

  -- "IRA checkbooks" are OK

LEGAL REQUIREMENTS

- ELIGIBLE CHARITY – Public charity or private *operating* foundation

  -- however, a PF, donor advised fund

  or supporting org is <u>not</u> eligible
- Must qualify for full charitable deduction – no dinners; no CGAs

LEGAL REQUIREMENTS

- Taxable part of IRA distributions (only)
  -- tax-free distributions protected
- Donor must have letter from charity that donor received no goods or services in exchange for the gift

TECHNICAL ISSUES

- Yes! Charitable IRA gifts can satisfy legally binding pledges!
- Joint return? Up to $200,000
- No withholding taxes
- Beneficiary of an inherited IRA <u>who is over age 70 ½</u> can make charitable gifts of required distributions

Want to make charitable gifts from your IRA ("QCD")?
Then NEVER make a tax-deductible contribution to your IRA after attaining age 70 ½

SECURE Act: Beginning in the year 2020, employed taxpayers over age 70 ½ are permitted to make tax-deductible contributions to a traditional IRA (e.g, up to $7,000 per year)

HOWEVER: If a person ever makes a tax-deductible contribution to an IRA after age 70 ½, then the amount of the qualified charitable distribution from an IRA that can be excluded from taxable income is reduced by that amount.

Want to make charitable gifts from your IRA ("QCD")?
Then NEVER make a tax-deductible contribution to your IRA after attaining age 70 ½

New last sentence added to end of Sec 408(d)(8)(A):

The amount of distributions not includible in gross income by reason of the preceding sentence for a taxable year (determined without regard to this sentence) shall be reduced (but not below zero) by an amount equal to the excess of—

- ***(i) the aggregate amount of deductions allowed to the taxpayer under section 219 for <u>all</u> taxable years ending on or after the date the taxpayer attains age 70 ½, over***
- ***(ii) the aggregate amount of reductions under this sentence for <u>all</u> taxable years preceding the current taxable year.***

Want to make charitable gifts from your IRA ("QCD")? *Then NEVER make a tax-deductible contribution to your IRA after attaining age 70 ½*

LEGISLATIVE INTENT

- To get a tax benefit from a charitable gift, a taxpayer must generally itemize deductions (state taxes, mortgage interest, etc)
- Only 11% of tax returns itemized deductions in 2018
- A working senior could (a) contribute $7,000 to an IRA and then (b) distribute $7,000 that same year to charities, and indirectly deduct charitable gifts via IRA contributions

ADMINISTRATIVE and BOOKEEPING HEADACHES

- People in their 80s and 90s will need to keep all tax records after age 70 ½ and then make cumulative computations

Want to make charitable gifts from your IRA ("QCD")? *Then NEVER make a tax-deductible contribution to your IRA after attaining age 70 ½*

EXAMPLE

- I. Work's RMD both for this year and next year is $5,000
- She donates each year's RMD to charity; would be QCD
- She is employed. This year she deducts $7,000 for IRA.
  Next year she does not deduct any IRA contribution
- How much can she EXCLUDE from income for QCD?

Year	Donate	Exclude	Taxable
This year	$5,000	-0-	$5,000*
Next year	$5,000	$3,000	$2,000*

* Taxpayer can claim an *itemized* charitable deduction

Want to make charitable gifts from your IRA ("QCD")? *Then NEVER make a tax-deductible contribution to your IRA after attaining age 70 ½*

STRATEGIES

- If ever want to make a QCD, don't contribute after age 70 ½
- Working seniors can contribute to plan at work (401(k), etc.)
- Working seniors can contribute to a Roth IRA (if income under $139k ($206k married))
- Self-employed? Contribute to an SEP-IRA

  (but <u>don't</u> make a QCD from the SEP that <u>same year</u>)

Footnote: Employed upper-income taxpayers can't even make tax-deductible contributions to an IRA if there is a plan at work (e.g., 401(k)). No tax deduction is permitted in year 2020 if AGI is over $75,000 ($124,0000 on married joint returns). IRS Notice 2019-59.

Stretch IRA

- "Stretch IRA" means an inherited retirement account (e.g., IRA), where payments are gradually made over the beneficiary's life expectancy
- Until the enactment of the SECURE Act, it was fairly easy for any beneficiary who inherited a retirement account to receive distributions until the age of 83 (or older for beneficiaries who inherited at an older age)
- Beginning 2020: General rule is a ten year liquidation
- *"Would you like your descendants to be able to get an income stream from all of your retirement assets for the rest of their lives?"*

LIQUIDATE INHERITED IRAs IN TEN YEARS

IMPLICATIONS FOR CHARITIES

Donors more likely to consider

- Outright bequests
- Retirement assets to tax-exempt CRT
  - Child: income more than 10 years; then charity

CHARITABLE REMAINDER TRUST

- Payment to non-charitable beneficiary (ies) for *life* *or* for a *term of years*
  (maximum 20 years)
- Remainder interest distributed to charity
- *Exempt from income tax*

LIQUIDATE INHERITED IRAs IN TEN YEARS

IMPLICATIONS FOR CHARITIES

Donors more likely to consider

- Outright bequests
- Retirement assets to tax-exempt CRT
  - Child: income more than 10 years; then charity
  - Spouse & children (no estate tax marital deduction)

2-GENERATION CHARITABLE REMAINDER UNITRUST

- Typically pays 5% to elderly surviving spouse for life, then 5% to children for life, then liquidates to charity
- Like an IRA, a CRT is exempt from income tax
- Can be like ***a QTIP trust for IRD assets***

LIQUIDATE INHERITED IRAs IN TEN YEARS

STRATEGIES:

- **Lotsa beneficiaries! Share the love! Spread the wealth!**
  Example: Children and grandchildren, rather than just children
- **Lifetime Roth IRA conversions, if current income tax rate is likely to be less than future tax rates**
- **Are any beneficiaries "eligible designated beneficiaries"?** They can receive distributions over their remaining life expectancy. They are exceptions to the ten year rule.
- **Name a tax-exempt charitable remainder trust as the beneficiary.** Make distributions for entire life of the family member, with remainder interest paid to a charity

Theory: Tax advantage of income tax deferral !

Move IRD tax-free after death from one tax exempt trust (e.g., the IRA) to another tax-exempt trust (the CRT)

*[**compare:***

a charitable lead trust is NOT tax-exempt;

don't name a CLT as an IRA beneficiary !]

Theory: Tax advantage of income tax deferral !

Move IRD tax-free after death from one tax exempt trust (e.g., the IRA) to another tax-exempt trust (the CRT)

It can be done! PLR 199901023

- No taxable income to beneficiaries until they receive distributions from CRT

Can a CRT Produce More Family Wealth Than a Ten Year Liquidation?

Yes. It is possible. But usually not likely.

- It can happen with long-term CRUTS (e.g., 40 or 50 years) and beneficiaries who pay high income tax rates
- Outcomes vary with investment returns and tax rates

Can a CRT Produce More Family Wealth Than a Ten Year Liquidation?

5% CRUT -- Investments earn 5% -- Tax rate: 40%					
			5% Annual		
			<u>Income</u>		
CRT	$1,000,000	< charity	**$50,000**		
Income tax	<u>-400,000</u>				
After-tax	**$600,000**	<family gets	**$30,000**		

Can a CRT Produce More Family Wealth Than a Ten Year Liquidation?

5% CRUT -- Investments earn 5% -- Tax rate: 40%					
			5% Annual		
			<u>Income</u>	<u>*Consume*</u>	<u>*Save*</u>
CRT	$1,000,000		**$50,000**	*$30,000*	*$20,000*
Income tax	<u>-400,000</u>		*Income tax >>>*		<u>*-$8,000*</u>
			Net annual investment		***$12,000***
After-tax	**$600,000**	*Purchase*	*$600k*	*life insurance?*	**<50 years?**

Can a CRT Produce More Family Wealth Than a Ten Year Liquidation?

5% CRUT -- Investments earn 5% -- Tax rate: 20%					
			5% Annual		
			Income		
CRT	$1,000,000	< charity	**$50,000**		
Income tax	-200,000				
After-tax	**$800,000**	<family gets	**$40,000**		

Can a CRT Produce More Family Wealth Than a Ten Year Liquidation?

5% CRUT -- Investments earn 5% -- Tax rate: 20%					
			5% Annual		
			Income	*Consume*	*Save*
CRT	$1,000,000		**$50,000**	*$40,000*	*$10,000*
Income tax	-200,000		*Income tax >>>*		*-$2,000*
			Net annual investment		***$8,000***
After-tax	**$800,000**				**<50 years?**

Can a CRT Produce More Family Wealth Than a Ten Year Liquidation?

Yes. It is possible. But usually not likely.

- It can happen with long-term CRUTS (e.g., 40 or 50 years) and beneficiaries who pay high income tax rates
- Outcomes vary with investment returns and tax rates
- A CRT is best for someone with charitable intentions who also wants to benefit family. It should not be foisted on people who have no charitable intent.

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