Philanthropic Giving Strategies for Your Clients

By Gary Garcia, Senior Director of Philanthropic Partnerships, The Dallas Foundation

While obtaining a tax benefit is never the real purpose of charitable giving for your clients, when possible it is still wise to give in a way that reduces their lifetime or estate taxes. Whether they personally benefit from the tax savings or choose to pass it on to their favorite charities through additional donations, these tax-planning techniques are worth consideration.

BUNCHING

Under The Tax Cut and Jobs Act (TCJA), the standard deduction is now nearly double –$12,000 for individuals and $24,000 for married couples– making it harder for people to itemize on their tax return and benefit from the charitable income tax deduction.

One common strategy is to "bunch" charitable donations by donating more in one tax year to receive a more significant deduction and then donating less in future years to compensate. For example, a donor could bunch two to three years of giving into one tax year, instead of spreading the donations over multiple tax years; the donor's total giving amount stays the same, but bunching multiple years of giving into one tax year achieves an itemized deduction greater than the standard deduction (thereby recovering the charitable tax deduction) and reduces taxable income.

QUALIFIED CHARITABLE DISTRIBUTIONS (QCDs)

If your clients are 70 1/2 years of age or older and in a position to take a Qualified Charitable Distribution (QCDs) from an IRA, remember that several programs and funds of The Dallas Foundation can be the recipient of such gifts.

While a QCD may not be made to a donor advised fund, your clients can still support their favorite charities or causes through a designated fund, the Community Impact Fund or the Mary M. Jalonick Women's Philanthropy Institute.

THE MANY USES OF DONOR ADVISED FUNDS

To Accelerate Donations or "Pre-fund" Charitable Giving into Desired Tax Year

A donor-advised fund allows for the decoupling of the timing of the charitable contribution that provides the deduction and when the actual donations (grants from the fund) are made to specific charities. A donor-advised fund could offer your clients the opportunity to lock in the deduction for charitable gifts and then grant out from the fund in future years. For clients with larger income tax events in one particular year, a donor-advised fund offers an income tax deduction in the year of the income event but allows for the smoothing out of charitable contributions consistent with the client's usual charitable giving.

To Accept Complicated or Unusual Assets

With the current top capital gains tax rate at 20% along with the 3.8% Medicare investment surcharge, both of which are still applicable post-TCJA, the incentive to donate appreciated property remains high. In most cases, the donor can get a charitable deduction for the current fair value of the gift and avoid paying capital gains tax on the unrealized gain. Charitable gifts of appreciated property are now more attractive than ever.

Although cash and publicly traded appreciated securities are the most common assets utilized to establish a donor-advised fund, donating more complicated assets, such as privately held business interests, might also make sense. This is especially true if the donation occurs in connection with the sale of the business and a substantial income (and consequent income tax) event to the donor.

To convert IRA Assets to a "Philanthropic Inheritance"

Retirement plan assets constitute the largest asset holding of many Americans. IRA beneficiary designations could potentially affect the transfer of several trillion dollars. Unfortunately, plan assets left to individuals are heavily taxed and consequently "expensive" to inherit. Donor-advised funds can be the beneficiary of an IRA or qualified pension plan. Depending on how the decedent sets up the fund, his or her adult children can receive a "philanthropic inheritance" consisting of an inherited fund from which to make charitable grants, saving their own income or assets for other purposes. An "inherited" donor-advised fund is a shift from the traditional "it's yours to spend freely" to "it's yours to support charity" for some share of the family wealth.

To Receive a Bequest

Donor-advised funds are most commonly thought of in connection with formalizing a donor's giving during their lifetime. However, many charitably inclined donors choose to create or add to donor-advised funds through their estate plan for a number of reasons. Perhaps they plan to donate a complicated asset that they need the use or enjoyment of during their lifetime. Perhaps they want to plan for a postmortem donor-advised fund to receive the assets of their private foundation in order to ensure their intent is carried forward or to ease the burden on future generations. With the support of The Dallas Foundation's philanthropic advising services, a donor may decide that a donor-advised fund would equip successor generations with the support needed to carry out effective charitable giving.

A bequest of artwork, collections, jewelry, coins or other tangible personal property could be a wonderful way to leave a charitable legacy while simultaneously relieving your clients' heirs of the worry about how to effectively and fairly dispose of such meaningful items. The "related use" requirement does not apply to charitable estate gifts, so the estate will be able to deduct the full fair market value of the bequest.

To transfer a Private Foundation

Many individuals, families and corporations head down the private foundation path without any awareness of simpler, less costly, turn-key alternatives available through The Dallas Foundation. Therefore, an increasing number of private foundations have been terminated in recent years. They can be time-consuming and expensive; filing requirements and tax rules are complicated; and family members may differ as to grantmaking priorities or management of the foundation. In volatile economic times, the amount of money available for grantmaking based on asset base and investment income can be reduced perhaps to the point where it does not make sense for the private foundation to continue as an independent entity. If the asset base has been reduced or was never sufficiently large to begin with, or if managing the private foundation becomes too burdensome, it may make sense to consider transferring the private foundation assets to a donor-advised fund.

The board of the private foundation can choose to continue in a very similar capacity as the advisory committee of the donor-advised fund to recommend charitable uses of the private foundation-turned donor-advised fund assets. The IRS permits the termination of a private foundation in either corporate or trust form and a distribution of its assets to a public charity, provided the charity has been in existence for five years preceding the distribution. The Dallas Foundation quite frequently accepts the transfer of private foundation assets into donor-advised funds. No advance IRS approval or notice is necessary and dissolution is straightforward and relatively simple.

To Use Alongside a Charitable Lead Trust (CLT)

Now that interest rates are declining again, a charitable lead trust can be a great tool in conjunction with a donor advised fund. The ideal candidate for a CLT includes: A donor who does not need current income from the trust; Has charitable intent; Is looking for a tax-efficient means to make a future transfer to heirs; And is concerned about income tax or estate tax exposure.

The donor can name the donor advised fund as the income beneficiary of the CLT. This provides the donor and their family the flexibility as to whom and how they direct their charitable giving and the donor's financial advisor can continue to oversee the investment management of the remainder assets.

In short, the DAF enhances the CLT and provides considerable flexibility to the donor to give during their lifetime as well as providing a nest egg for heirs when the term of the CLT concludes.

Conversely, a donor advised fund may also be designated to receive all or a portion of the remainder of a Charitable Remainder Trust, which first disperses income to beneficiaries for a specific period of time and then donates the remainder to a designated charity.

To make the 199A deduction work for owners of pass-through entities.

With the new tax law in effect, charitable contributions may provide additional benefits related to the Section 199A deduction. The phase-out for the Section 199A deduction is based on taxable income versus Adjusted Gross Income (AGI). As a result, charitable contributions can be utilized to decrease taxable income and potentially allow taxpayers to qualify for part, or potentially all, of the 20 percent deduction. In certain situations, the combined cash outlay for charitable contributions and calculated tax will be less than the tax due had there been no charitable contribution. In other words, clients can pay less (tax plus charitable contributions) when contributions pull them back into that phase-out range.

Since the Section 199A deduction is calculated at the individual level, an opportunity arises for certain individuals owning pass-through entities with Qualified Business Income (QBI) to qualify for the 20 percent deduction when individual taxable income would normally reduce or eliminate the deduction.

For 2019, the 20 percent deduction will be limited or phased out when taxable income falls between $315,000 and $415,000 for Married Filing Jointly taxpayers ($160,000 and $207,500 for Single taxpayers). If the taxpayer's taxable income falls between the ranges above, then a percentage of the total phase-out range will apply when calculating the components of the 20 percent deduction.

Make batch charitable contributions in a single year to a donor-advised fund to maximize itemized deductions. This can also be used to precisely target a $315,000 taxable income. Thereafter, the proceeds can continue to grow in the donor-advised fund to be given to charity in the timetable originally intended.

To help offset the tax cost of a ROTH IRA Conversion

Tax deductions can help offset the tax cost of a Roth IRA conversion and perhaps allow conversion of a larger amount at a lower tax cost. Among the more flexible of deductions, especially for high-income earners, are charitable contributions.

The tax deduction for a contribution to a public charity can be up to 60% of adjusted gross income (AGI) for cash donations and up to 30% for donations of securities (generally deductible at fair market value when long-term appreciated securities are gifted) each year. And if a contribution exceeds these limits, the excess can generally be carried forward for up to 5 years. (Note: These limits are generally applicable, but there are exceptions, and the rules are complex. Professional tax advice should be sought when considering a large charitable contribution.)

The amount of the charitable deduction available to claim can generally be estimated by adding the taxable portions of a conversion amount to AGI. For example, for those planning to convert $200,000 to a Roth IRA, with a $150,000 AGI before the conversion, the estimated AGI would be $350,000 after the conversion. Up to $210,000 (60% of $350,000) of a charitable cash contribution or $105,000 (30% of $350,000) of a charitable donation of securities with long-term appreciation, could potentially be deducted.

Charitable deductions may be worth more if taxes go up in the future, because they may be deducted against a higher tax rate.

A tax deduction taken in the year of the Roth conversion can help offset the conversion taxes. A large contribution into a donor advised fund can provide a "ready reserve" to support many charitable causes over time.

To Direct Closely Held Stock Toward Charitable Purposes

Gifts of closely held stock create the same tax advantages as gifts of other assets: Immediate charitable deduction, a reduction of estate taxes and avoidance of capital gains.

Making a gift of stock rather than of dividends avoids taxes at both the corporate and shareholder levels. That means more of the stock's value can be directed to your client's charitable goals.

Although there can be no prearranged agreement at the time of a stock gift, it is likely that The Dallas Foundation would be receptive to an offer from company owners should they wish to buy stock back in the future. This is advantageous because the company may be able to avoid penalties on excess profit by using that profit to buy back stock, or the stock can be retired in order to reduce the number of outstanding shares and therefore increase the stock value for other shareholders.

CONCLUSION

While obtaining a tax benefit is never the real purpose of charitable giving for your clients, when possible, it is still wise to give in a way that reduces their lifetime or estate taxes. Whether they personally benefit from the tax savings or choose to pass it on to their favorite charities through additional donations, these tax-planning techniques are worth consideration.

The Dallas Foundation provides a simple, powerful, and highly personal approach to giving and we offer a variety of giving tools to help people and organizations achieve their charitable goals. We welcome the opportunity to work with you and your clients to fulfill their unique charitable objectives.

If you need assistance with adding assets to your fund or establishing a new fund or bequest, or gifts of complex assets, please contact Julie Diaz, vice president of philanthropic partnerships (jdiaz@dallasfoundation.org) or Gary Garcia, senior director, philanthropic partnerships (gwgarcia@dallasfoundation.org).