Andrew 0:04
Hello, and welcome to JGUA Financial Commentary Podcast. I'm your host, Andrew Baron. And our topic today, in this month of December 2020, is charitable gifting. But first, a quick disclosure. The contents of this podcast are strictly for informational purposes only, and nothing said shall be taken as investment, tax, or legal advice. Any strategies discussed may not be suitable for the listener specifically, and JGUA encourages consulting with your advisor before implementing any strategies to ensure that they meet your individual objectives. I'd like to welcome Senior Advisor Amanda Herrick-Smith. Welcome, Amanda.

Amanda 0:47
Hi, Andrew, thank you so much for having me join today.

Andrew 0:51
Could you give us a little bit of background with yourself and the firm?

Amanda 0:54
I've been with the firm for 14 years; I am a senior advisor. I help our clients with education planning to do taxes and tax preparation, tax planning, estate planning, a lot of the different areas of financial planning. Since I am a Certified Financial Planner.

Andrew 1:13
I just want to give what I thought were interesting stats around charitable giving in 2019. This is just Americans, I didn't look at the worldwide stats—but Americans gave $449 billion. I thought the breakdown is actually the most interesting part of that. Although, that is a huge number, nearly half a trillion, which is nothing to sneeze at. But the breakdown of it I thought was more interesting. The breakdown goes: $21 billion from corporations, $75 billion from foundations, and the huge lion's share portion, $309 billion is just from individuals like you and me. Which is a little telling with especially the corporations being a small part. And then one of the largest is the famous Bill and Melinda Gates Foundation, which has over $50 billion. That's what? Nearly a ninth of the annual giving from last year? So with that, why don't we start with the most common: your regular cash donations. Why don't you talk a little about the process and maybe the tax benefits.

Amanda 2:16
So cash donations, as you mentioned Andrew, is the most common way that people give to a charity. So often we'll send a check to your favorite charity. Maybe we get a mailing or we see something we want to support and go online and make a donation with either a debit card or credit card. This is the most common way that people give to charities. And as far as the tax side of things, if people are able to itemize their deductions, they may be able to get an additional benefit for donating to a charity. Now there is some limitations, you can only donate up to 60% of your adjusted gross income in a typical year. Now, this is not a typical year for us. So we're actually able to donate up to 100% of your adjusted gross income due to the CARES Act. What that means if someone makes $50,000 for the year, they can actually donate up to 100% of what they make or 100% of the $50,000. Now there's another key if the donation is going to a private foundation, there is a limitation of 30% of one's adjusted gross income, is what they could donate and receive a tax benefit. Also new this year is the $300 above the line tax deduction. What that

means if someone is unable to itemize their deductions, maybe the standard deduction is higher since you get to take the higher of the two. So for just this year, they could donate up to $300 in the form of a cash donation and be able to offset $300 of their income.

Andrew 4:02
The reason that might be important, I feel like especially for this year, is a few years ago, you could write it off on your taxes. But since they raised the standard deduction, we're seeing less people qualified to actually see the tax benefit of making those charitable donations. So it is nice to see $300 top of line does add up to a little bit of benefit.

Amanda 4:19
Yeah, especially for the charities. Because with the pandemic, a lot of them are hurting so every little bit that can help them as well as help our own clients and be able to take that tax deduction. That's fantastic.

Andrew 4:34
And then I guess the one thing I did want to touch on, on the charities, is it's very important to check the status of the charity. Just because you give money to an organization does not mean it is a charitable gift. So always be sure it is a qualified charity.

Amanda 4:50
Yes, agreed.

Andrew 4:51
Another thing I think we see quite a bit of is if you happen to donate to a fundraiser or a dinner, you don't get the whole donation. And oftentimes, if they give you a receipt, you will see that there's the total cost, and then there's the charitable amount that you could actually use.

Amanda 5:09
Yes, and good point, Andrew. So you must have supporting documentation in order to be able to itemize your donation. If you make a charitable donation of more than $250, you will need to have a receipt for that donation made. So most often charities will actually send a letter in the mail or maybe send you an email in appreciation of your gift. And also for receipt for your income taxes.

Andrew 5:35
When they give you that little piece of paper, make sure you put it somewhere safe and don't just shove it under the seat.

Amanda 5:39
Exactly.

Andrew 5:40
I did want to touch on the next interesting strategy, which is gifting appreciate stock. It's important, as you know, as investment advisor that we touch on this subject, because we see quite a bit of it. Kind of walkthrough appreciate stock, meaning that you've held it for a long

time, this probably works strategy works best if you've had something for 10 years, when you've really seen a big rise in the bull market over the last decade. What are the advantages of using stock to gift versus just making a cash contribution after selling the stock?

Amanda 6:11
Yes. So appreciated stock can benefit a lot of different people, especially those that have purchased stock maybe a long time ago, maybe they were gifted stock from a family member. And it's grown and appreciated over time. How the strategy works and it would, it only works if the stock is in like a taxable account such as like an individual account or joint account, if it's in a retirement account, this strategy doesn't work in this case. So what someone would do is if they have stock, we'll call it XYZ stock, that's 100 shares of XYZ. And it's grown from $5,000, when it first started, let's say 20 years ago, and now it's worth $20,000. So there's that huge appreciation from 5000 to 20,000. That's, you know, $15,000 gain, and the individual wants to donate maybe some or all of the stock to a charity. So they would fill out what's called a letter of authorization to gift the stock to the charity submitted to their broker, and the broker would receive this request, and the broker would act on it and actually send the shares of stock directly to the charity. So why is this important? You know, why would we want to go this route? Well, it's because the charity can then take the stock and sell it, they pay practically zero income taxes, so they don't have to pay tax on that $15,000 gain. Now, let's say Andrew, if you and I had this stock, and we wanted to gift it ourselves to the charity, we would have to pay probably if it's long term stock around 15% federal tax. And if we're in New York, let's say maybe we're in that 5% tax bracket for New York. So you're looking at maybe 20 to 21% of just income taxes, we're paying on that $15,000 gain. And then if we turn around and then take the cash, into a cash donation, the charity is losing out on the opportunity of that tax that was paid to the Internal Revenue Service or the estate tax system. So it's a good win-win for both the individual and the charity. It's another win for the individual because not only do they not have to pay tax on the gain, if they are able to itemize their income tax deduction, they're able to take that market value and able to put that as an itemized deduction on their income tax return. So it could help to further reduce income tax and not have to pay as much tax.

Andrew 8:54
So that's substantial. I know we've gone back and forth between standard deduction and itemized taxes, which leads us to an optimal strategy for gifting. Sometimes you'll see it as bunching or lumpy or grouping, but some form of gathering a group in one year of charitable donations. I've actually seen people at the firm where because of the high standard deduction thresholds that we see today, you have to hit a big hurdle to actually see the benefit. So for some people, if you do three, four years, in one year, at least as currently written, you might see a bigger tax benefit than making level, similar amounts year over year. Anything to add to that?

Amanda 9:38
Yes, Andrew, that's a fantastic strategy. In fact, just a couple weeks ago, I was working with one of our clients and that specific strategy actually came up in our conversation. The reason why the lumping, that is what we call it, works so well and that's lumping sometimes it's real estate taxes, but most often it's charitable donations and how that would work is our client would make a charitable contribution, maybe in January. And then that same year, they make that charitable contribution in also December. And so it's taking pretty much two charitable contribution years

in pooling it all in one year. Because of the recent tax law changes in 2018, the standard deduction practically doubled. So for simplicity for a single person, you know, it went from $6,000 to $12,000. Because an individual gets to take the higher of the two, in order to get to that $12,000 for most people include real estate taxes, including state taxes paid, and that's subject to a cap of $10,000. And also any charitable donations and mortgage interest. Those are usually the three common ones we see. So this doubling of the charitable contributions every other year, helps to push that individual up and over the standard taking benefit anything in addition to that standard deduction. So for example, if someone had made charitable contributions so that their itemized deductions are $20,000, instead of the $12,000 standard deduction, they get that additional benefit. And the benefit in lies with it helps offset income, therefore paying less income tax. And so the following year, since they already pooled both of their contributions in one year, they would just take the standard deduction the following year. So every other year, they would be taking the itemized deduction and every other year, the standard deduction instead of just the standard deduction every year,

Andrew 11:46
I think that was a very comprehensive summary. Thank you. I did want to touch on something we are seeing more and more of which is Donor Advised Funds maybe talk us through that a little bit. And I know there are some technical parts, though.

Amanda 11:59
Yes, so our donor advised fund is a way that an individual can donate to their favorite cause, to their favorite charity, and be able to take the tax donation for the full amount that's donated into this fund. But the key is they don't necessarily have to take the entire fund and gift it out this year. Unlike a cash donation where in order to get a tax benefit, you have to actually donate the cash. For example, let's say someone has $50,000 that they'd like to donate, or put into this Donor Advised Fund, they can receive the $50,000 income tax deduction this year, however, they can pick and choose which charity to take the fund and donate it to over a period of time. Maybe they want to donate $10,000 over the next five years, or so forth. And the reason why this could be beneficial this year is since people are able to take 100% of their adjusted gross income as a limitation to their charitable donations. It's a higher threshold, other than instead of the 60% limitation this year of adjusted gross income, it's a 100% limitation for Adjusted Gross Income.

Andrew 13:17
There is a difference between the standard deduction and the and itemizing deductions, there was less benefit in the recent change. Another thing we are seeing is what we call on the firm, lumpy charitable gifting where you take a group and it could kind of combine the strategies we've talked about where you could take a large amount of highly appreciated stock and give that to a donor advised fund. And you could do that every three to five years versus every year. And you could see a substantial tax benefit to that.

Amanda 13:48
And the reason why that'd be such a great tax planning opportunity to either, you know, double up on the contributions two times a year, maybe a client donates in January. And they also donate in December of doing that Donor Advised Fund donation multiple throughout, you know, five year period or whatnot, is they get the benefit of itemizing in those years that that

contribution is made in the years that the contribution is not made to the charity, they would take the standard deduction. And the reason why people do that these days is because of the changes in 2018 to the standard deduction it practically doubled. So a lot less people are able to itemize their deductions. So by doing the lumpy strategy where you know, donate to your charity twice in one year or donate to a donor advised fund. It helps in being able to benefit every other year in itemizing your deductions and that example and then taking the standard deductions on those off years.

Andrew 14:55
The next strategy one touch on has some restrictions around it. It's kind of reserved only for our senior clients, qualified charitable distributions, kind of walk us through the restrictions and the benefits surrounding that.

Amanda 15:09
So a qualified charitable distribution is where the individual that is 70 and a half takes part of their IRA and donates it directly to their charity. The reason why they would want to do this is it's one opportunity where they can actually do a distribution from their IRA without having to pay income taxes. Because when someone takes a withdrawal from their IRA, it's subject to the marginal tax rates, which is the same as how wage income is taxed. So it's subject to those tax brackets that we hear often about. With those that are 72, because the law changed, they're required to take a minimum amount out of their IRA every year. And if they don't, then they're subject to a 50% penalty. So the reason why some of our clients are looking at doing qualified charitable distributions is it helps reduce their income. For example, if they decided they want to do a $5,000 qualified charitable distribution from their IRA, their income, their taxable income is then reduced by $5,000. So it's an automatic off the top reduction in their income, therefore, they're not paying tax on that income. They're in a situation where you're unable to itemize their deductions, they're taking the standard deduction, doing the QCDs could be very helpful. Another thing is there is an additional Medicare Part B, which is the hospital component of Medicare, and also Medicare Part D, which is the prescription component of Medicare, where a portion of its called an excess premium amount is subject to one's adjusted gross income. So maybe they're in that point where they're idling on falling into the tier of having to pay their access, because their income and over that level, or maybe they're pushed into multiple, you know, different tiers, where the premium amount is going to go up. By doing a qualified charitable distribution, they're able to reduce their income, and hopefully either reduce or eliminate the excess premium amount, which is also called IRMAA So almost often people hear the term IRMAA,

Andrew 17:34
That's double A. I-R-M-A-A, we see lots of acronyms.

Amanda 17:40
We certainly do in this financial field, don't we? We got RMDs, QCDs, IRAs, all sorts of them.

Andrew 17:49
And I think it's important for listeners to think about that even though RMDs were suspended for 2020 QCDs are still fully valid, up to the amount you could have taken. The only other thing is I

think it's important to mention is, while we were talking about acronyms, there's quite a few different retirement plans out there. And while some of them have IRA in the name, this strategy really only works for the traditional IRA. There are the SIMPLE and the SEP, it's important that those are excluded or inactive, at least.

Amanda 18:24
Correct

Andrew 18:25
Kind of surrounding an outline about IRAs would be naming a charity as the beneficiary. And I think this used to be less common, because I think people used to want to provide money to their children with IRAs. But with the change in how you have to spend IRAs down over a 10 year period, etc. I think that naming a charity can be a big and useful strategy.

Amanda 18:48
Andrew, I definitely could. Let's say someone has an individual account in also an IRA. And they're looking at options of you know, where they want to give to their favorite charity, do they want to use, you know, their individual account? Maybe it's a bequest and their will, you know, when they demise. Or do they want to list the beneficiary, you know, in their IRA, it's best for them to list the charity as a beneficiary of their IRA instead. Because it's one opportunity where the portion of the IRA could be sent directly to the charity and that charity would not have to pay income tax or very little income tax. Well, if that IRA was gifted to an individual, the individual would have to when they inherit that asset, if it's a non-spouse, beneficiary, they would have to withdraw from that account, right have at least that account would not be in existence within 10 years, they have to withdraw completely out of the account in a 10 year period, and all of that would be taxable to them.

Andrew 19:53
Thank you so much for joining us. Amanda. Could you give us a wrap or your closing thoughts on this?

Amanda 19:58
Well, I just want to give a little bit of a wrap up of everything we covered today. So we covered the cash donations, which is one of the most common ways for people to donate to their favorite cause. However, it's not always the best way from a tax standpoint. So maybe other opportunities could be donating a highly appreciated stock maybe directly to a Donor Advised Fund or setting up a Donor Advised Fund. Or if they're 70 and a half, we'd be looking at qualified charitable distributions, which go directly from an individual's IRA to a charity, reducing income taxes right off the top. And there's also so many other forms in different ways to be able to donate. It could be by adding the beneficiary on someone's IRA to a charity, maybe doing a charitable remainder trust. There's, you know, different forms of estate bequests that can be drawn up written in one’s will, private foundation or even a family foundation. I work with one of my clients that actually has a private family foundation. Community foundations are also other great ways, doing in-kind donations just like we talked about today with the stock in in-kind meaning if the item is donated as it is today. So if it's a stock in-kind donation, it'd be donated to the charity in the form of stock. For my own college people donate equipment to the college. So

that's another form of in kind donation, that's tax deductible. So there's so many different ways to be able to give to a charity and it's so important to work with professionals to be able to help identify the best ways to give and you know, if anyone ever has any questions, you know, feel free to reach out to myself, Amanda Herrick-Smith at John Ullman and Associates.

Andrew 21:56
Thank you so much for Amanda, and thank you to our listeners for joining as well. We know your time is valuable. If you do have any further questions, please send an email to info@jgua.com or check out our website and our social media for additional content. Until our next podcast everyone, stay smart.