JOHN D. DOVICH & ASSOCIATES, LLC

Charitable Giving

- By Chris Brennan, CFP® and Nick Groman, CFP®

As the holiday season approaches, individuals and families often renew their focus on the idea of supporting the less fortunate. Sometimes, in the midst of the holiday madness, we lose sight of the tax implications and strategies that ought to be considered when making these gifts. While there are more complex tax strategies available for large gifts, such as Charitable Lead/Remainder Trusts, this article focuses on the less complex strategies that you may want to consider when contemplating how to gift to a charity.

In previous articles, we identified how the Tax Cut and Jobs Act (TCJA) that took effect on January 1, 2018 will impact taxpayers. One of the biggest changes is the standard deduction having doubled for everyone. For example, married couples filing jointly are now entitled to a standard deduction of $24,000 in 2018. Because of this higher standard deduction, the ability for many individuals and couples to itemize their deductions will be lost. Even though the tax deduction is not the primary motivation of giving, taxpayers will want to be conscientious of these changes as they contemplate charitable giving in the future. Therefore, we would like to remind you of a few strategies that individuals can employ to be effective with their charitable gifts.

Bunching of Charitable Gifts

As noted previously, the standard deduction doubled for most taxpayers on January 1, 2018. This increase, along with other changes, such as the $10,000 limit per year on state and local tax deductions, will result in a lot less individuals and couples itemizing their deductions. Due to these changes, the concept of "bunching" charitable contributions has been re-introduced. When bunching contributions, an individual who gives a certain amount of money each year elects to "lump" two or three (or more) years of charitable contributions into one. By doing so, an individual can itemize in one year (the giving year) while claiming the standard deduction in the other years (the non-giving years). As the illustration below shows, depending on the circumstances, some taxpayers can save additional money by bunching their charitable gifts.

Example of Non-Bunching vs. Bunching	**Non-Bunching Contributions**		**Bunching Contributions**	
Deduction	**Year 1**	**Year 2**	**Year 1**	**Year 2**
State & Local Taxes (Max Amount)	$ 10,000	$ 10,000	$ 10,000	$ 10,000
Mortgage Interest	$ 7,500	$ 7,000	$ 7,500	$ 7,000
Charitable Contributions	$ 10,000	$ 10,000	$ 20,000	$ 0
Total Itemized Deductions	$ 27,500	$ 27,000	$ 37,500	$ 17,000
Standard Deduction	$ 24,000	$ 24,000	$ 24,000	$ 24,000
Standard or Itemized Deduction Applied	Itemized	Itemized	Itemized	Standard
Tax Benefit @ 32%	$ 8,800	$ 8,640	$ 12,000	$ 7,680
Total Two Years Tax Savings	$ 17,440		$ 19,680	
Additional Savings			$ 2,240	

Information regarding changes from the TCJA can be found in IRS Publication 5307, at https://www.irs.gov/pub/irs-pdf/p5307.pdf

Donor Advised Funds

Individuals often find themselves wanting to give to multiple charities in different years. This can be a potential problem for individuals who elect to bunch contributions. However, this problem can be easily remedied by establishing a Donor Advised Fund. A Donor Advised Fund is a fund that allows individuals to contribute to an entity while receiving a corresponding tax deduction in the year in which they contribute. The contributions can be invested and become available for grants to charities along with their earnings. After the contributions have been made to the fund, individuals can then elect when to make grants to charities of their choice. Therefore, Donor Advised Funds allow for individuals to maximize the tax-effectiveness of their charitable giving while affording themselves the flexibility associated with the timing of their gifts.

Furthermore, when using a Donor Advised Fund, individuals will want to contribute to the fund using appreciated assets, such as individual stocks (long term capital gains only). This makes the tax deduction even more valuable because this will allow the individual to avoid paying taxes on the imbedded capital gains that haven't been recognized with the asset. Additionally, individuals that choose to use a Donor Advised Fund are not able use their grants to satisfying a pledge to a charitable organization.

Qualified Charitable Distributions

Now let's say that an individual's charitable giving, despite bunching, does not result in enough deductions to warrant itemizing. Qualified Charitable Distributions (QCDs) will allow this individual to be a little more strategic about how they gift to charities. QCDs are distributions made by individuals over the age of 70.5 directly from an IRA to a charitable institution. The amount that is distributed to the charity is not treated as taxable income for the individual because the individual does not receive any of the distribution – it goes straight to the charity. Additionally, a QCD can be used to satisfy required minimum distributions (RMDs). As a reminder, RMDs are the annual distribution amounts the IRS requires individuals to take from an IRA once the individual has reached age 70.5. Why is this important? When using a QCD to make a gift you would have otherwise made with after-tax dollars, you can avoid the income you would have recognized with the RMD. Below is an example of the QCDs impact:

- Scenario Not Using A QCD:
  Jane Doe has an RMD of $5,000 for the year of 2018 from her IRA and wants to provide a $5,000 gift to her church at the end of the year. Jane receives a check for her RMD and deposits it into her bank account. Jane then sends a check to the church for $5,000 for her gift. By providing a gift in this fashion, Jane took possession of the RMD first. Because of this, she will recognize the $5,000 as income. If Jane does not itemize her taxes this year, she won't benefit from the charitable gift on her tax return.

- Scenario Using A QCD:
  Jane Doe has an RMD of $5,000 for the year of 2018 from her IRA and wants to provide a $5,000 gift to her church at the end of the year. Jane initiates a QCD from her IRA, and requests the funds be sent directly to her church. By providing a gift in this fashion, Jane does not have to recognize the $5,000 as income, therefore avoiding $5,000 of income that otherwise would have been taxed.

As evident from the example, QCDs can be a very powerful strategy for individuals. There are a few notes that we would like to reference regarding some of the limitations for the QCD. QCDs are again, only available to IRA owners over the age of 70.5. QCD distributions can only be made to charitable organizations that are recognized as a 501(c)3 organizations. QCDs are also capped at $100,000 per person, per year ($200,000 for married individuals).

We recognize that these strategies do not apply to every person. Individuals that give to charities occasionally, and in relatively inconsequential amounts, may not see value in these strategies. However, we encourage you to reach out to us if you, or any family members, have any questions pertaining to these strategies, or are interested in becoming more charitably inclined.

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Disclosures:

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