

## TAX-SMART CHARITABLE GIVING, ESPECIALLY WITH RETIREMENT ASSETS

# The Greater Cincinnati Planned Giving Council

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CHRISTOPHER R. HOYT  
University of Missouri - Kansas City  
School of Law

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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?

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## 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 2022?

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## 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 1/2 should make *ALL* of their charitable gifts from their IRAs:  
*"Qualified Charitable Distributions" (QCDs)*

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## “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 \$25,000 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

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## 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 or investments**

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## 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 50% of grants made from private foundations

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## Who Offers Donor Advised Funds?

- Traditionally – Local Community Foundations
  - *The Greater Cincinnati 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*

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## Donor Advised Funds

### 2021 Donor-Advised Fund Report

*National Philanthropic Trust*

- 1,005,099 – Number of DAFs in 2020
- \$160 billion – assets held by DAFs
- \$ 48 billion – contributions to DAFs
- \$ 35 billion – grants paid by DAFs

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### Growth in Number of Donor Advised Funds

Year	Number of DAFs
2016	290,111
2017	469,749
2018	732,128
2019	864,197
2020	1,005,099

**Over 70% of the nation's DAFs  
are less than five years old**

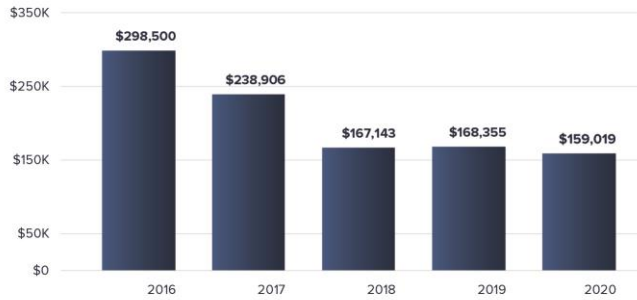
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# Average Dollars in Each DAF Continues to Decline

***New DAFs tend to be established  
with smaller dollar amounts***

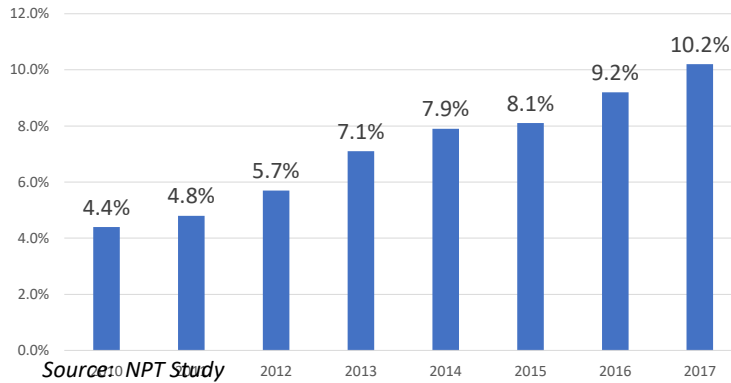
National Philanthropic Trust  
2021 DONOR-ADVISED FUND REPORT

**FIGURE 6:** Average Donor-Advised Fund Account Size



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



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# 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"

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The image shows a portion of the IRS Form 1041, 'Income Tax Return for Beneficiaries of IRAs, RR's, and Annuities'. The form is annotated with yellow arrows and text to illustrate a Qualified Charitable Distribution (QCD) scenario.

- Line 15a:** IRA distributions are reported as 10,000.
- Line 15b:** Taxable amount is 6,000. A yellow arrow points from this amount to line 14.
- Line 14:** Other gains or (losses). A yellow arrow points from line 15b to this line, and another yellow arrow points from this line to line 22.
- Line 22:** Total income. A yellow arrow points from line 14 to this line.
- Annotations:** A large yellow arrow labeled "QCD" points from line 15b to line 14. Another yellow arrow points from line 15b to line 16b.

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## Qualified Charitable Distribution -- Lifetime Gifts from IRAs --

- IRA owner must be over age 70 1/2
- Maximum: \$100,000 per year
- Yes! Charitable gift satisfies required minimum distribution requirement from IRA!

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## 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)

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## 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

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## LEGAL REQUIREMENTS

- Over age 70 ½
- IRA (only) – not 403(b), 401(k), etc.
- “Directly” from the IRA to charity
  - “IRA checkbooks” are OK

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## LEGAL REQUIREMENTS

- ELIGIBLE CHARITY – Public charity or private *operating* foundation
  - however, a PF, donor advised fund or supporting org is not eligible
- Must qualify for full charitable deduction – no dinners; no CGAs

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## 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

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## 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 who is over age 70 ½ can make charitable gifts of required distributions

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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.

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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 all 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 all taxable years preceding the current taxable year.***

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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

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**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

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**Only the \$7,000 IRA deduction is a problem for QCDs**

The screenshot shows the 'Adjustments to Income' section of a 2019 Schedule 1 Form 1040s1.pdf. Line 19, 'IRA deduction', is highlighted with a yellow box and an arrow pointing to it from the text: '\$7,000 IRA deduction is claimed on line 19'. Another yellow box with an arrow points to line 15, 'Self-employed SEP, SIMPLE, and qualified plans', with the text: 'SEP deduction is NOT IRA dedn'. A large yellow box spans lines 16 through 18a, containing the text: 'As long as there is never a deduction reported on line 19 after age 70 ½, then there will not be a problem excluding QCDs made from an IRA from taxable income. REASON: No deduction was claimed under Section 219.'

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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 \$144k (\$214k married))
- Self-employed? Contribute to an SEP-IRA  
 (but don’t make a QCD from the SEP that same year)

*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 2022 if AGI is over \$78,000 (\$129,000 on married joint returns). IRS Tax Tip 2021-170.

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## 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
- Inherited IRA distributions are taxable income
- *A \$1million IRA will shrink to \$700k in 10 years*  
 (oversimplified)

Outright charitable bequest?  
 Family & charity combined: philanthropy (PF or DAF)

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## 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?”*

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### 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

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## 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***

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## 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)

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## 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*

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### 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 !]*

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## 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

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## 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

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## 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	<b>\$50,000</b>		
Income tax	<u>-400,000</u>				
After-tax	<b>\$600,000</b>	<family gets	<b>\$30,000</b>		

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## 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		<b>\$50,000</b>	\$30,000	\$20,000
Income tax	<u>-400,000</u>		Income tax >>>		<u>-\$8,000</u>
			Net annual investment		<b>\$12,000</b>
After-tax	<b>\$600,000</b>	Purchase	\$600k	life insurance?	<b>&lt;50 years?</b>

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

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

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

5% CRUT -- Investments earn 5% -- Tax rate: 20%					
			5% Annual		
			<u>Income</u>	<u>Consume</u>	<u>Save</u>
CRT	\$1,000,000		<b>\$50,000</b>	\$40,000	\$10,000
Income tax	<u>-200,000</u>		<i>Income tax &gt;&gt;&gt;</i>		<u>-\$2,000</u>
			<i>Net annual investment</i>		<b>\$8,000</b>
After-tax	<b>\$800,000</b>				<b>&lt;50 years?</b>

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## 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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## CRUT Can Offer Other Benefits

- A steady income-stream to the child that will last for the child's entire lifetime
- Asset protection provisions can be included in the CRT in the event of a divorce or other financial challenge
- Professional asset management is possible with a corporate trustee, which could be particularly helpful for a child who would have likely mismanaged a large lump-sum inheritance

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