Key Private Bank

2020 year-end charitable gift strategies

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As the holiday season approaches, those who are charitably inclined are exploring tax-efficient ways to help the causes they believe in during these challenging times. This article highlights the top six charitable planning strategies that can help you make the most of your giving this year, including some unique considerations created by the Coronavirus Aid, Relief and Economic Security (CARES) Act. These strategies should be evaluated in light of your personal goals and circumstances and in consultation with your Key Private Bank advisor and your tax advisor.

I. 2020 planning under the CARES Act

The CARES Act was signed into law on March 27, 2020, to lessen the financial impact of COVID-19 on individuals and businesses. To encourage charitable giving during this time, the legislation includes provisions that create some attractive opportunities for individuals making charitable contributions in 2020 only.

- **100% charitable deduction.** The CARES Act provides a one-time unlimited cap on certain cash donations for 2020. Individuals who itemize their deductions (total itemized deductions greater than $12,400 for individuals and $24,800 for married filing jointly) can deduct up to 100% (as compared with the previous limit of 60%) of their adjusted gross income for certain cash contributions made to a public charity or certain foundations. Donations to non-operating private foundations, supporting organizations, or donor-advised funds (DAFs) do not qualify for this increased deduction amount. Any charitable contributions made in excess of adjusted gross income (AGI) limitations in 2020 will be carried forward for five years, subject to the standard limitations.
- **Above-line deduction.** The CARES Act also allows individuals who do not itemize their deductions the ability to deduct up to $300 of cash contributions made to a public charity or certain foundations. This limit applies to the tax-filing unit, so married taxpayers filing jointly appear to be limited to a $300 deduction also. Donations to non-operating private foundations, supporting organizations, or donor-advised funds do not qualify for this increased deduction amount.

II. Gift of appreciated securities

Your gift can make a bigger impact by donating long-term appreciated securities directly to charity rather than just writing a check. Compared with donating cash or selling securities with a low cost basis and contributing the after-tax proceeds, making a gift of highly appreciated stock may enable you to automatically increase your gift and tax deduction and save on capital gains taxes. This is how it works: When you donate appreciated assets to charity, you generally take a tax deduction for the full fair market value of the asset rather than your basis. As a result, the value of your gift and the amount of your tax deduction increase and you eliminate your capital gains tax exposure. When the charity later sells the stock, it pays no tax on the gain. Even if you take the standard deduction this year and don't use your charitable deduction, you still benefit by eliminating the capital gains tax. This is a win for your favorite charity and a win for you.

III. Donor-advised fund

If you are charitably inclined, you might consider a contribution to a donor-advised fund to offset unexpectedly high earnings and year-end bonuses. A DAF is a contractual arrangement that you, as a donor, enter into with a sponsoring charity to establish an account that benefits your chosen charities. A DAF allows you to make a charitable contribution and qualify for an immediate tax deduction without needing to decide which public charities to support until you are ready to recommend grants. Private foundations also use DAFs to fulfill the 5% mandatory annual distribution requirement when the foundation is not ready to make a final decision about where to make their grants at the end of the year.

IV. Offsetting the tax costs of a Roth IRA conversion

If you are considering a Roth IRA conversion, a charitable gift could save you taxes. Roth IRAs offer two important tax advantages: (1) Unlike traditional IRA withdrawals, qualified Roth IRA withdrawals are free of federal income tax and usually are free of state income tax; and (2) withdrawals are exempt from required minimum distribution rules associated with traditional IRAs. A change in the tax law and political developments could result in higher future taxes. If you believe your current tax rate is lower than it will be in the years you will be making withdrawals from your IRA, a Roth conversion can be viewed as insurance against future tax rate increases that would otherwise apply to withdrawals from a traditional IRA. As a result, more retirement dollars will go to beneficiaries. However, the amount you convert from a traditional IRA to a Roth IRA is taxed as ordinary income in the year of conversion and may push you into a higher marginal federal income tax bracket. If you are charitably inclined and plan to do a Roth conversion before the end of the year, a large itemized charitable tax deduction can help offset the taxes due to the Roth conversion.

V. Charitable IRA rollover

A charitable rollover—also known as a qualified charitable distribution (QCD)—can be an effective vehicle for charitable giving. Even though the CARES Act temporarily waives required minimum distributions from retirement plans for the 2020 tax year, QCDs are still a viable tax strategy this year. QCDs enable an individual over 70½ to make tax-advantaged charitable donations of up to $100,000 per year from their IRAs during their lifetime if the distribution is made directly to a charity. QCDs are not included in adjusted gross income and would generally count toward your required minimum distribution. Any potential income taxes owed on these distributions are eliminated.

VI. Charitable trusts

For individuals with taxable estates (assets exceeding $11.58 million per individual, $23.16 million per married couple), historically low interest rates and lower asset values create a unique opportunity to plan with charitable lead annuity trusts (CLATs). A CLAT is an irrevocable trust that distributes a predetermined amount to a charitable beneficiary for a term of years; the amount remaining at the end of the term is distributed to non-charity beneficiaries, such as your children. You receive a current charitable deduction to offset the taxable transfer to your beneficiaries, which is sensitive to the IRS interest rate (Section 7520 rate). The lower the interest rate (0.4 percent in October 2020), the higher the deduction. The greater the difference between the projected average rate of return of CLAT assets over the trust term and the Section 7520 rate, the greater the potential tax-free wealth transfer to the younger generation.

Individuals with large retirement accounts should consider naming a Charitable Remainder Trust (CRT) as beneficiary, particularly in light of a recent law (SECURES Act) that requires that retirement account benefits must be distributed within 10 years after the year of the owner's death. In general, a CRT provides a current income tax charitable deduction and a stream of income to non-charitable beneficiaries, such as your children, for a term of no more than 20 years or the life of one or more of the non-charitable beneficiaries. By lengthening the payout term, a CRT can potentially avoid subjecting a beneficiary to a higher tax bracket and the 3.8% surtax on net investment income. When the trust term ends, the remainder passes to a charity or charities.

If you are considering making gifts to your favorite charities this year, consult your Key Private Bank advisor and your legal or tax advisor to determine which strategy could help maximize the benefit for you, your family, and your chosen charitable causes.

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