# 2023 Charitable Giving Guide

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The Key Wealth Institute is a team of highly experienced professionals from across wealth management, dedicated to delivering commentary and financial advice. From strategies to manage your wealth to the latest political and industry news, the Key Wealth Institute provides proactive insights to help grow your wealth.

One of the most meaningful aspects of accumulating wealth is the ability to give back in significant, influential ways. Families and individuals donate for a whole host of reasons, and taking advantage of tax breaks is low on the list of motivations. Still, tax benefits are an important secondary consideration when giving, one that requires a closer look. Charitable giving strategies should be evaluated by taking into consideration your personal goals and circumstances and in consultation with your advisor and your tax advisor.

Since 1917, individual taxpayers who itemized have been able to receive a tax break on their charitable gifts. However, the enactment of the Tax Cuts and Jobs Act in 2017 has reduced the federal tax benefit for many households. Beginning in 2018, the standard deduction nearly doubled. As a result, far fewer taxpayers are itemizing and receiving an actual tax break for their charitable gifts.

### Understanding the factors impacting tax benefits

For itemizing taxpayers, the tax benefits of charitable giving will depend on factors that include:

- The type of asset contributed (e.g., cash, long-term capital gain property, short-term capital gain property, tangible personal property, self-created property).
- The basis and fair market value of the assets donated.
- The type of charity to which the gift is donated — a public charity or a private foundation.
- The income level and tax bracket of the taxpayer. As a rule, an individual cannot offset their entire income in a year with a sufficiently large charitable gift. The amount you can deduct for charitable contributions is generally limited to no more than 60% of your adjusted gross income (AGI). Your deduction may be further limited to 50%, 30%, or 20% of your AGI limit depending on the type of property you give and the type of organization you give it to. For large charitable gifts, amounts in excess of those limits can be carried forward for five more years.

Planned gifts can make it possible for you to give more than would otherwise be the case, while providing important tax advantages to you. There are a variety of planned giving options.

## Gift appreciated stock

Some of the most tax-efficient assets to give to charity are publicly traded stocks held 12 months or longer that have appreciated with unrealized capital gains. By donating these directly to the charity, you receive a deduction based on the fair market value of the security, and neither you nor the charity pays a tax on the capital gains if the security is subsequently sold by the charity.

Donating 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 cost basis or the amount you paid for the stock. 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.

To maximize your charitable giving strategy, you must have enough deductions to make itemizing worthwhile. You need to have at least $13,850 in deductions for single filers and $27,700 for married couples filing jointly to make it worth it. However, even if you take the standard deduction this year and do not itemize 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.

As an example, assume you are debating whether to donate $15,000 of cash, sell $15,000 in stock and donate the cash proceeds or donating $15,000 worth of stock outright to the charity. What are the net tax savings of the different strategies?

| $15,000 Fair Market Value of Stock, $5,000 Cost Basis, Bought 5 Years Ago | Donate $15,000 Stock Outright | Donate $15,000 Cash | Sell $15,000 Stock and Donate Cash Proceeds |
|---|---:|---:|---:|
| Charitable donation | $15,000 | $15,000 | $15,000 |
| Ordinary income tax savings (assume 37% rate) | $ 5,550 | $ 5,550 | $ 5,550 |
| Capital gains tax paid (assumes 20% tax on $10,000 gain) | $ 2,000 saved | NA | $ 2,000 paid |
| **Net tax savings** | **$ 7,550** | **$ 5,550** | **$ 3,550** |

**Note:** If your stock is worth less than you paid for it, it is better to sell the stock first, and then donate the cash so that you can take the capital tax loss against current or future capital gains.

### What is Fair Market Value?

For publicly trading stock, that is the average of the high and low market price on the transfer date. Private company stock requires an appraisal unless the estimated value is less than $10,000.

## Donor-advised fund (DAF)

You might consider a contribution to a DAF to satisfy your charitable giving wishes. DAFs are often used to offset unexpectedly high earnings, year-end bonuses, and Roth conversions.

The basic concept of a DAF is straightforward:

- You contribute to the fund and subsequently recommend specific grants to favorite charities when you are ready.
- Keep in mind that your recommendations are subject to final approval and release of the funds by the administrating organization.
- You can claim a tax deduction for the year in which you put assets into a DAF; the amount and timing of any actual grant has no bearing on the tax deduction.
- DAFs are typically invested and grow tax free.
- Donor-advised funds enhance giving flexibility. You do not have to identify nonprofit beneficiaries when you make tax-deductible contributions to your DAF, and you can distribute your contributions and investment gains to recipients over as long a period as you wish.
- Some DAFs can continue over successive generations and are an ideal way to involve heirs.

## Offsetting the tax costs of a Roth IRA conversion

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. Roth IRAs offer two important tax advantages: (1) Unlike traditional IRAs and employer-sponsored plans distributions, qualified Roth IRA distributions are tax free; and (2) Unlike traditional IRAs and employer-sponsored plans, Roth IRAs are not subject to required minimum distribution (RMD) rules that must begin at age 73. The bad news about a Roth conversion is 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. Keep in mind that not all states tax distributions from retirement accounts (check with your tax preparer to see if state income taxes will apply to your Roth conversion).

For reasons NOT to do a Roth conversion please see Wealth Institute article Defer No More Part II: The Year of the Roth (July 2023).

A Roth conversion may push your taxable income high enough to cause an income-related monthly adjustment amount (IRMAA) in Medicare premiums if you are over age 65.

## Featured case study

Jessica and Bruce Jones, both age 57, discuss with their advisor their concern over rising tax rates. They are well aware that their financial plan projects that they will be in a similar tax bracket in retirement as they are now and that their required minimum distributions (that must begin by age 73) will cause them to receive more income than they need or want in retirement. Their advisor recommends that they consider converting a portion of their traditional IRA balances to a Roth IRA over a period of time. She explains that there are many benefits to doing a Roth conversion, but it is a particularly advantageous way to reduce RMDs. For more advantages (and cons) of converting to a Roth IRA, please see the article Defer No More Part II: The Year of the Roth (July 2023).

There is no RMD requirement for Roth IRAs for the lives of both spouses, and as a result the couple will reduce their taxable income in retirement. The couple think it is a great idea but express concern over the tax liability produced by executing a Roth conversion. The conversion to a Roth IRA would be taxable at the ordinary income tax rate which currently is 24% for the couple. As Florida residents, they will pay no state income tax on the conversion. Knowing the couple currently donate significant amounts to charity each year, the advisor recommends establishing and contributing to a donor-advised fund. Their advisor then shared a charitable offset strategy that can be used with a Roth conversion.

After consulting with their tax advisor, they instruct their advisor to convert $100,000 from their traditional IRA to a Roth IRA and to establish a DAF with an initial contribution of appreciated stock (cost basis $50,000) with a fair market value of $100,000 (see table on page 4).

By funding their DAF with $100,000, they net an additional $24,000 in federal tax savings and offset the taxes owed due to the Roth conversion. They also avoid incurring long-term capital gain tax of $7,500 on their highly appreciated donated stock.

The couple can support the charities they care about by making grant recommendations from their DAF over a span of several years. To continue their charitable legacy after their passing, they can name their children as successor donor-advisors.

| | With $100,000 Roth Conversion | Without Roth Conversion |
|---|---|---|
| Current Year Adjusted Gross Income, Married Filing Jointly | $335,000 | $235,000 |
| Ordinary Income Tax Bracket | 24% | 24% |
| Itemized Deductions in 2023 (prior to DAF contribution) | -$35,000 | -$35,000 |
| Taxable Income | $300,000 | $200,000 |
| **Tax Amount Owed** | **$72,000** | **$48,000** |
| **$100,000 Stock Contributed to DAF (Subject to 30% Charitable Deduction Limit on AGI)** | **-$24,000** | |
| **Tax Amount Owed** | **$48,000** | |

## Utilize Split-Interest Charitable Trusts

Split-interest trusts are popular due to their dual beneficial interests: They can benefit a qualified charity and a noncharitable beneficiary.

A charitable remainder trust (CRT) provides noncharitable beneficiaries with exclusive rights to distributions until their interests terminate; at that time, charitable beneficiaries receive the assets left over in the trust. CRTs have been particularly useful for investors who want to diversify highly appreciated assets but have been concerned about incurring the capital gains tax. The deferral or avoidance of capital gains tax has been a popular feature for funding CRTs with appreciated assets.

Individuals with large retirement accounts should consider naming a CRT as beneficiary, particularly in light of a recent law (The SECURE Act, 2019) that requires retirement account benefits to be distributed within 10 years after the year of the retirement account owner's death. In general, a CRT provides a current income tax charitable deduction and a stream of income to noncharitable beneficiaries, such as your children, for a term of no more than 20 years or the life of one or more of the noncharitable beneficiaries. By using a longer 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.

## Make qualified charitable distribution

The new SECURE Act 2.0 modified and added some provisions related to qualified charitable distributions (QCDs). A QCD is an otherwise taxable distribution from an IRA (other than a SEP or SIMPLE IRA receiving contributions) owned by an individual who is age 70½ or older that is paid directly from the IRA to a qualified charity. Taxpayers can exclude up to $100,000 of QCDs from their gross income each year. Beginning in 2024, the $100,000 maximum will be indexed for inflation. The QCD will satisfy or help satisfy your required minimum distribution associated with IRAs that must begin at age 73 (age 75 for those born in 1960 or later). QCDs are not included in adjusted gross income, which makes QCDs beneficial for standard deduction filers. If you have IRAs with nondeductible contributions or multiple IRAs, there are special rules to determine what portion of deductible and nondeductible contributions has been distributed as a QCD and what portion of the remaining IRA is treated as including nondeductible contributions.

### New in 2023

Beginning in 2023, the SECURE Act expands the definition of QCDs to include one-time distributions to create life income plans, also called Legacy QCD.

Previously, QCDs could only be used to make an outright gift. The new life income plan or Legacy QCD, however, allows for a tax-free withdrawal from your IRA to establish a charitable gift annuity (CGA)[1]. Similar to the current QCD rules, the Legacy QCD will count toward the IRA owner's annual RMD if the gift comes directly from the IRA by the end of a calendar year. There are several considerations to keep in mind:

- It is a once-in-a-lifetime election.
- A donor may contribute up to $50,000 through one or more life-income gifts to multiple charities.
- The CGA can only benefit you and/or your spouse, and payments of at least 5% of the donated value must start within 1 year of the gift.
- The $50,000 counts toward the overall $100,000 QCD maximum annual limit.
- All payments by the CGA funded by the QCD must be fully taxable at the recipient's ordinary income tax rate.

[1] While not addressed in this article, the ability to complete a one-time distribution to create a life income plan includes the use of charitable remainder unitrusts or annuity trusts.

## Gift planning summary of outright charitable contributions – 2023

| Outright Contribution | Income Tax Deduction | Capital Gain Considerations | Method of Transfer | Special Considerations |
|---|---|---|---|---|
| **Cash** | Amount of cash, up to 60% of donors' AGI for gifts to public charities (50% charities); up to 30% of AGI for gifts to private foundations. Five-year carryover allowed for excess deductions. | None | Checks or other cash equivalents including credit card charges, electronic transfer, and physical delivery of cash. | Carried-over deductions from cash gifts are considered before carryovers of property gifts. |
| **Marketable Securities** | Current market value if long-term transferred to a 50% charity, up to 30% AGI or long-term transferred to a 30% charity, up to 20% of AGI. Limited to cost basis if short-term gain up to 60% of AGI (30% for private foundations). Five-year carryover for excess. | No gain reportable when donor gives appreciated securities. | Transfer can be made to charity's account or be delivered to charity's agent in negotiable form. | Donors or appreciated securities can qualify for the 50% AGI ceiling by electing to reduce their contribution deductions by 100% of the gain. Strategy could be effective where long-term capital gain is insubstantial. |

## Gift planning summary of outright charitable contributions – 2023 (continued)

| Outright Contribution | Income Tax Deduction | Capital Gain Considerations | Method of Transfer | Special Considerations |
|---|---|---|---|---|
| **Donor Advised Funds (DAF)** | Donor receives charitable deduction when contributions are made to a DAF. No additional deduction allowed when DAF makes transfer to a recipient charity. | No gain reportable if donor gives appreciated assets to a DAF. | Account owner can make recommendations of gifts to individual charities, but DAF retains ownership and control over distributions. | Good if donor does not have individual charities identified yet but still wants current year tax deduction. Currently no minimum annual distribution required by a DAF account. |
| **Real Property** | Current value of appreciated real estate held long-term, less any indebtedness transferred to a 50% charity, up to 30% of AGI with 5-year carryover for excess deduction. Transfer to 30% charity is deductible at cost basis only, up to 20% of AGI with five-year carryover. | No gain reportable by donor. | Transfer of title of contributed realty is generally made by quit-claim deed. | Verify charity's policy on accepting real estate gifts. |
| **Closely Held Securities** | Current value of appreciated closely held securities if long-term transferred to a 50% charity, up to 30% AGI with five-year carryover of excess deduction. Transfer to 30% charity deductible at cost basis only, up to 20% of AGI. | No gain reportable by donor. | Delivery of securities in negotiable form to charity or agent by transfer of certificate into charity's name. | Gifts of closely held securities are often negotiated with anticipation of corporate redemption of charity's stock. Gifts may also be attractive where sale of corporation is anticipated. Be aware of pre-arranged sales that could cause the gain to be recognized by donor. |
| **Life Insurance** | FMV of policy (interpolated terminal reserve value) or donor's costs basis, whichever is less, subject to 60% of AGI ceiling (30% for private foundations). Policy loans reduce deductions. No deduction for term policies. | Ordinary income property. Generally, no recognition of gain unless policy is subject to a loan. | Ownership of policy is transferred to charity by an endorsement by the donor on forms supplied by the insurance company and accompanied by delivery of the insurance policy. | If the donor continues to pay the policy premium, donor receives a charitable income tax deduction. |
| **Qualified Charitable Distributions from IRAs (QCDs)** | No deduction. But, qualified donors (IRA owners age 70½ and older) do not include the distribution (up to $100,000) in income. Also counts toward RMD requirement. | None | IRA owner can request trustee or custodian of account to make a QCD to a qualified charity (does not include a DAF, supporting organization, CRT or CGA). | Currently, employer-sponsored retirement plans are ineligible for QCDs. |

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.

For more information, please contact your advisor.

## About the Author

As a Relationship Manager for Key Private Bank, Gretchen focuses on ensuring her clients' wealth management plans are carried through to meet their unique financial objectives and grow and preserve wealth. Gretchen coordinates the implementation of wealth management strategies with the relationship team and ensures clients have the tools and information to keep track of their financial situation and make informed decisions. She also coordinates regular communications and updates with the team, and proactively delivers the latest insights and advice to benefit clients' particular situations.

Gretchen has more than 30 years of experience in financial services and is well qualified to help clients implement strategies to achieve their goals. Most recently, prior to joining Key, Gretchen served as Director of Advanced Planning for Prudential Financial, where she was a subject matter expert on financial and estate planning and on retirement topics such as Social Security, Medicare, and tax efficient distribution strategies. Gretchen earned a Bachelor of Science degree in Management from Springfield College and an MBA from the University of Phoenix. Gretchen obtained her certification as a Certified Financial Planner.™ Most recently she obtained her Certified Divorce Financial Analyst® certification in 2023. She is a member of the Financial Planning Association, the Investments & Wealth Institute, and the Institute for Divorce Financial Analysts.®





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