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Estate Planning Update July 2018 - The Increased Standard Deduction: Impact on Charitable Giving

The Tax Cuts and Jobs Act of 2017 (the Act) essentially doubled the size of the standard deduction available to single and joint filers while limiting the ability for individuals to take certain itemized deductions. Under the Act, the 2018 standard deduction is $24,000 for married couples filing a joint return and $12,000 for individuals. As a result, many individuals may be better off taking the increased standard deduction on future income tax returns rather than itemizing deductions. Some have expressed concern about the impact this will have on charities, as some individuals may be less likely to give to charity without the benefit of the charitable income tax deduction. There are, however, several strategies taxpayers can use to maximize available deductions while continuing to provide support to charitable causes.

One strategy an individual might use is to "bunch" or "stack" charitable donations. Consider, for example, a donor who provides annual support to a charity in the amount of $20,000. Rather than giving the charity $20,000 each year, the donor could consider giving the charity $40,000 every other year. Using this approach, the donor can exceed the applicable standard deduction threshold and maximize the amount of itemized deductions that can be claimed. This approach, however, can be difficult for charities whose budgets rely on a consistent annual flow of funds from a group of loyal supporters.

To address the effect on charities that rely on consistent annual support from donors, a donor might couple the "stacking" technique with a donor-advised fund. A donor who has a donor-advised fund would make the $40,000 charitable gift to that donor-advised fund every other year, with the income tax benefits noted above. However, the donor (as the donor-adviser of the donor-advised fund) could recommend grants from the donor-advised fund of $20,000 to the charity each year, thus providing the consistent annual support to the charity while maximizing the tax benefits to the donor. This technique could be similarly used by a donor who has a separate private foundation–the donor would make the $40,000 charitable gift to the private foundation every other year and the private foundation would make annual grants of $20,000 to the charity.

In addition to "stacking" and donor-advised funds or private foundations, there are other strategies donors can consider to maximize their charitable giving in a tax-efficient manner. In lieu of taking a fully taxable distribution from an IRA, donors over the age of 70½ may be able to make a qualified charitable distribution. Up to $100,000 can be directed to be distributed from an IRA to one or more "eligible charities" (this does not include private foundations or donor-advised funds). This distribution counts toward the donor's required minimum distribution from the IRA but is entirely excluded from the donor's taxable income. There are many reasons why excluding these amounts from income is better than realizing the income and then making a charitable gift. In addition to the federal limitations to itemized deductions discussed above, there is an added benefit to a donor who lives in a state without a state charitable income tax deduction. The IRA charitable distribution can also be used to satisfy a binding pledge of a donor. Donors can also consider certain trusts such as charitable remainder trusts and grantor trusts as well as charitable gift annuities to make contributions. While the complexity of these entities and giving methods can vary, they can be used to provide donors with substantial deductions.

It will likely take time before the effects of the Act on the nonprofit sector are fully understood. In the meantime, with some thoughtful planning, donors have options that allow them to maximize their charitable contributions while also taking advantage of related tax benefits.