William Blair

Private Wealth Management
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Thinking Strategically About Charitable Giving

Using charitable giving strategies to enhance the tax-efficiency of your donations plays a vital role in maximizing the impact of your gifts.

Introduction

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Enhancing the impact that you and your family can have in supporting causes near to your hearts also requires more than just generosity and good intentions. It takes careful planning and an in-depth understanding of the various vehicles that can be used to facilitate your charitable gifts and the tax laws related to those gifts.

Just as no two families' philanthropic legacies are identical, the strategies used to achieve these legacies should be carefully crafted to each family's unique set of goals, resources, time frame, and tax considerations. These strategies must also be designed as an integrated piece of the family's comprehensive wealth-management plan.

Developing your philanthropic strategy requires answering four primary questions:

1. How much do you want to give?
2. Which assets should you contribute?
3. What causes do you care about?
4. Which charitable giving vehicle(s) will be the most effective and tax-efficient in achieving your goals?

Navigating an Evolving Tax Landscape

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Taxes in all their forms—ordinary income, capital gains, and wealth transfer—play a large role in determining the right charitable gifting strategy for many investors. Part of the challenge in developing a tax-efficient charitable gifting strategy is that tax laws change periodically and anticipating these changes can be extremely difficult.

Over the past several years, there have been a host of significant tax law changes that directly or indirectly influence charitable planning. These include:

- The 2017 Tax Cuts and Jobs Act (TCJA) doubled the size of the standard deduction and created limits on deductions for state and local taxes. These changes have made a "bunching" strategy for charitable gifts—in which donors bunch several years' worth of gifts into a single year and itemize their deductions, and then take the standard deduction in other years—more attractive for many people. The TCJA also increased the deductibility threshold for cash gifts to public charities; eliminated the Pease limitation, which limited the value of certain itemized deductions; and significantly increased the federal estate tax exemption amount. Many of these changes are scheduled to sunset after 2025.
- The SECURE Act raised the age at which you must start taking required minimum distribution (RMDs) from tax-deferred retirement accounts, but left the QCD age at 70 ½.

The fluidity and unpredictability of tax laws highlight the importance of maintaining an ongoing dialogue with your wealth advisor. In some situations, individuals may be well-served to implement strategies before proposed changes are enacted. In other situations, the unpredictability of what changes will come to fruition highlights the value of maintaining flexibility.

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CASE STUDY

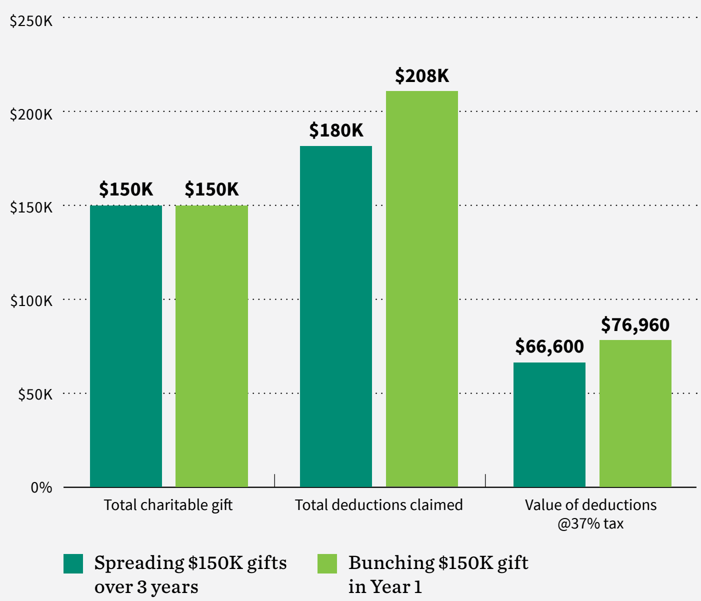
Bunching Charitable Gifts Can Maximize Tax Savings

For taxpayers who are looking to make large gifts, it may be beneficial to concentrate the donations in a single year, as opposed to spreading them over multiple years.

A family that is looking to contribute a total of $150,000 might typically spread those gifts evenly over three years, which would enable them to claim itemized deductions totaling $180,000 over that span. This total represents $50,000 of charitable deductions per year in addition to $10,000 in annual state and local tax (SALT) deductions.

Or, they could make the full $150,000 gift in year 1 plus claim the annual SALT deduction ($10,000 per year), and then take the standard deduction ($24,000 per year) in years 2 and 3. This approach would result in total deductions of $208,000 over those three years.

Spreading a Donation Across 3 Years vs. Bunching Into 1 Year



Deciding How Much to Give

Deciding How Much to Give

The first, and in many ways most important, decision in developing a philanthropic strategy is to determine how much you will contribute to charities. At William Blair, we help our clients answer this question by thinking about "core" vs. "surplus" assets. Core assets represent the amount needed to support your lifetime spending needs. The amount remaining beyond that, or surplus assets, becomes what is available to fund your wealth transfer or philanthropic goals.

Deciding how to prioritize between philanthropic and wealth-transfer goals is a deeply personal decision, and there is no one right way to make this decision. It is important to realize, however, that these decisions should not be made in a vacuum. In a carefully crafted wealth-management strategy, the lifestyle, philanthropic, and wealth-transfer goals are all working in concert and executed in a tax-efficient manner.

Deciding Which Assets to Contribute

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After quantifying how much you want to give, the next step is determining which assets to use in funding those gifts. This requires understanding the potential benefits tied to donating different types of assets.

Cash

Writing a check is the simplest way to make a charitable contribution. You do not have to transfer stock certificates, titles, or other ownership documents, or worry about your basis or valuations for tax purposes. Your deduction simply equals the amount you donate less the value of any goods and services you receive in return. But, in some cases, contributing cash may not maximize the potential tax benefits or efficacy of your gift.

Appreciated Assets

If you own assets that have appreciated significantly since you acquired them and you have owned them for more than one year, donating these assets, rather than cash, may help you maximize the tax benefits of your gift. When you donate long-term capital gain property, such as publicly traded stock, shares in a private company, and, in some situations, real estate, you can deduct the asset's full fair market value (FMV) at the time of the gift. In addition to enjoying the deduction, you will avoid having to pay capital gains tax on the appreciation. The charity can either hold the stock as an investment or, because of its tax-exempt status, sell the stock immediately without any tax impact. When contributing less marketable assets, such as shares of a privately owned company or real estate, you may need to obtain a qualified appraisal from a valuation professional.

"Loss" Assets

If you would like to dispose of assets that are worth less than your basis, it is not advisable to donate them to charity. Rather, sell the assets so that you can recognize the loss on your income tax return and then donate the sale proceeds to charity.

Complex Assets

Charitable giving encompasses more than just cash and stock donations. You may be able to attain a new level of giving you may not have considered possible through assets you already own. Some charities and donor-advised funds can accept complex assets, including gifts of real estate, closely held stock, partnership interests, artwork, royalties, copyrights, patents, valuable collectibles, IRAs, life insurance, and retirement plans. Given the nature of complex asset gifts, additional due diligence and expertise is required. However, such gifts can provide a rewarding and powerful tool to meet a donor's philanthropic vision.

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CASE STUDY

Quantifying the Benefits of Giving Appreciated Stock

Susan is planning to make a sizable donation to a charity that supports cancer research. To fund the donation, she plans to use stock that she purchased 10 years ago for $40,000 that today has a fair market value of $75,000. Rather than selling the stock and then writing a check to the charity, she instead chooses to gift the stock directly to the charity. This approach, which allows Susan to avoid paying the 23.8% capital gains and Medicare tax on the stock's $35,000 of appreciation, is a double-win because it allows her to donate $8,330 more to the charity and generates an additional $11,412 in net tax savings. These savings would be even greater when taking into account any applicable capital gains taxes at the state level, as well as the impact of state income taxes in high-tax states.

* Donor's tax savings = (Contribution amount x ordinary tax rate) - capital gains tax paid

Deciding Which Charitable Giving Vehicles to Use

There are five primary vehicles, or methods, for making charitable gifts. These methods vary considerably in terms of how simple or complex they are to execute and administer, how much control and flexibility the donor has, the timing of when the gifts are made, and the nature of the tax benefits. As a result, each vehicle has its own unique set of pros and cons. Determining which vehicle is best suited for your plans requires a careful assessment of your philanthropic goals, balance sheet, and tax exposure.

Direct Gifts

The most straightforward form of charitable giving is making gifts directly to a public charity during your lifetime. Whether the gift is of cash, stock, or another asset, the charity is able to benefit from the resources immediately and you, as the donor, are able to claim the full tax deduction, within adjusted gross income (AGI) deductibility limits (discussed in detail on the next page), in the year that the gift is made. Direct gifts often work well for individuals who are not focused on estate-planning concerns and who are looking to make an immediate impact for a specific charity. In addition to being the simplest and fastest way to make a charitable impact, direct gifts are also the least expensive, since they do not involve any administrative fees or excise taxes.

Donor-Advised Funds

For individuals or families who want to establish a sizable charitable giving vehicle now but want flexibility to determine when and to which charities those funds are distributed, donor-advised funds (DAFs) can be an attractive option. Establishing a DAF is one of the easiest and most tax-advantageous ways to give to charity. A DAF is a charitable investment account set up in the donor's name but held by an organization that manages the investments, administers the funds, and makes the qualifying grants at the donor's request. With a DAF, the donor gets to deduct the full value of the assets contributed to the DAF, within AGI contribution limits, in the year of the contribution, but the decisions about when and how to distribute the funds can be made in subsequent years. The donor also gets to decide how the funds are invested within the DAF, and those funds grow tax-free. In terms of AGI deductibility limits, gifts to DAFs are treated as gifts to a public charity.

Charitable Remainder Trusts

With a charitable remainder trust (CRT), the donor makes an irrevocable gift of assets—usually highly appreciated assets—to the trust and designates 1) beneficiaries to receive an income stream during the term of the trust and 2) one or more charities to receive the assets that remain in the trust after the trust term expires. The donor, who can also be one of the beneficiaries, receives an income tax deduction in the year of the contribution based on the expected value of the assets remaining in the trust at the end of the trust term. Because the trust does not have to pay capital gains tax on the contributed assets, CRTs can be especially appealing to business owners or others who have low-basis, highly appreciated assets. CRTs allow donors to diversify their assets in a tax-efficient manner and generate an income stream. Because the gift to the trust needs to be irrevocable, however, these vehicles require careful planning and involve set-up and administrative costs.

Charitable Lead Trusts

In many ways, charitable lead trusts (CLTs) are the inverse of CRTs. With a CLT, one or more charities receive an income stream during the life of the trust, and the value of the assets remaining at the end of the trust term pass to one or more named beneficiaries, often children or grandchildren. If structured properly, CLTs can be an effective tool for passing wealth to younger generations in a tax-efficient manner while supporting charities in the meantime. If the trust is structured as a grantor trust, meaning that the income earned by the assets in the trust is taxable to the donor, the donor receives an income tax deduction in the year of the contribution equal to the present value of the income stream to the charity. As with CRTs, CLTs involve set-up and administrative costs.

Private Foundations

For donors who are looking to foster continued family involvement in the management of the family's philanthropic legacy, establishing a private foundation can be an appealing option. Private foundations provide the highest levels of control over the administration, investment management, and distribution decisions. These vehicles can also provide opportunities for younger generations to be actively involved in carrying out their family's philanthropic mission. Private foundations require annual administration expenses, and the investment income may be subject to excise tax. Plus, the deductibility limitations for donations to private foundations are more restrictive than gifts to public charities.

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EXHIBIT 1

Comparison of Charitable Giving Methods

	Direct Gifts to Public Charities[1]	Charitable Remainder Trust	Charitable Lead Trust	Private Foundation	Donor-Advised Fund
Advantages	Simplicity and immediate benefit to charity.	Donor receives current cash flow and is able to diversify without incurring immediate recognition of capital gain.	Charity receives current cash flow. Donor or designated heirs receive assets at trust termination. Significant tax deduction can be enjoyed or wealth can be transferred in a tax-efficient manner.	Family-name legacy is created with continued family involvement and control over administration, investments, management, and distributions.	Easy to establish and maintain with nominal contributions allowed. Ability to participate in distribution decisions. Treated as a public charity for deductibility purposes.
Disadvantages	No involvement in grant-making decisions.	Annual administration required.	Annual administration required. Income tax deduction requires establishing CLT as a grantor trust.	Annual administration requirements. Excise tax on investment income depending on circumstances. Deductibility limitations are more restrictive than contributions to public charities.	Limited control over fund management and administration.
Suitability	Individuals who identify the charity they want to support and would like to create impact immediately.	Individuals who own low basis, highly appreciated securities and would like to increase cash flow and diversify assets in a tax-efficient manner.	Financially secure individuals who wish to transfer wealth to heirs in a tax-efficient manner and provide current cash flow to a designated charity.	Individuals who do not require income from donated assets and are interested in furthering charitable endeavors with greater control.	Individuals who do not require income from donated assets and would like to avoid cost and administration of a private foundation.

1 Individuals over 70-1/2 may contribute a qualified charitable distribution (QCD), an otherwise taxable distribution from their IRA (not SEP or SIMPLE IRA), directly to a qualified charity and exclude up to $108,000 from gross income for the year. The QCD may be used to satisfy all or part of the IRA required minimum distribution (RMD) for the year. Taxpayers must make their QCD during the calendar year.

Deciding Which Charitable Giving Vehicles to Use (continued)

EXHIBIT 2

Donor-Advised Funds vs. Private Foundations

Many high-net-worth individuals and families assume that a private foundation is the most appropriate tool for creating an enduring philanthropic legacy. While foundations certainly have features that help families achieve these goals in a tax-efficient manner, donor-advised funds (DAFs) can deliver many of these benefits, but with lower expenses and less administrative burden. In some cases, you may consider both a DAF and a trust or private foundation to accomplish your goals.

	Donor-Advised Fund	Private Foundation
Deductibility of Cash Gifts	60% of AGI	30% of AGI
Deductibility of Appreciated, Long-Term Stock or Real Estate	30% of AGI	20% of AGI
Excise Tax	None	1%–2% annually of net investment income
Valuation of Gifts	Fair market value	Fair market value for publicly traded stocks, cost basis for certain other gifts including closely held stock and real estate
Control	Donor may advise but organization makes final decision	Donor family has authority for distribution and makes final investment decisions, subject to IRS rules
Annual Payout Requirements	None	Must distribute 5% of net assets, valued annually, regardless of how much assets can earn
Privacy	Individual donors may be anonymous	Donors must file public tax returns
Perpetuity	Can exist in perpetuity	Can exist in perpetuity

Understanding Deductibility Limits

As you decide which assets to give and which types of giving vehicles to use, you will want to consider the annual deductibility limits. As shown in Exhibit 3, these limits are based on AGI, as well as the type of property donated and whether it is given directly or through a planned giving vehicle. Any amount beyond the limit can be carried forward for up to five years.

If your income fluctuates significantly from year to year, or if you anticipate having a one-time event, such as selling a business, that may cause your income to surge one year, concentrating charitable gifts in the year(s) of higher income can help maximize the tax benefits of those gifts and initiate meaningful philanthropic planning.

Deciding Which Charitable Giving Vehicles to Use (continued)

EXHIBIT 3

Maximum Percentage of AGI That Can be Deducted Annually

Contribution	Direct Gifts to Public Charities	Charitable Remainder Trust	Charitable Lead Trust	Private Foundation	Donor-Advised Fund
Cash	60%[1]	60%[1]	30%	30%	60%[1]
Ordinary-income property[2]	50%	50%	30%	30%	50%
Short-term capital-gain property[2]	50%	50%	30%	30%	50%
Long-term capital-gain property	30%	30%	30%	20%	30%
Tangible-personal property	50%	50%	30%	20%	50%

1 The Tax Cuts and Jobs Act of 2018 increased this limit from 50% to 60%. The 60% limit is slated to sunset after 12/31/2025 and revert to 50%
2 Deduction limited to cost basis

Qualified Charitable Donations for IRA Assets

If you are age 70 ½ or older, you can contribute up to $108,000 a year from your IRAs directly to a charity. This strategy, known as a qualified charitable distribution (QCD), has several potential benefits. Making the contribution directly from your IRA to the charity, as opposed to having the distribution go to you and then making a gift to a charity, means that the money won't be included in your taxable AGI. In addition, the QCD can count toward your required minimum distributions (RMDs), which start at age 73.

Furthermore, some investors may be considering converting a traditional IRA to a Roth IRA to take advantage of the potential benefits of a Roth IRA, including tax-free growth, no RMDs, and no tax liability for descendants who inherit the assets. A Roth conversion may be particularly appealing for investors who are concerned that tax rates will increase in the future. Making charitable donations in the year of a Roth conversion can help offset the increased tax bill that will be generated by the conversion.

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Deciding Which Charitable Giving Vehicles to Use (continued)

LLCs

EXHIBIT 4

Advantages, Disadvantages, Suitability

Advantages	An LLC can invest in for-profit companies and make political donations. Gifts of appreciated stock can be made directly to charities, with the LLC owners able to use the charitable deduction. LLCs also do not have disclosure requirements and do not have minimum distribution requirements.
Disadvantages	No tax minimization. No reduction in taxable estates, which could have been accomplished by donating stock to other charitable entities.
Suitability	Founders of companies who transfer stocks to an LLC who wish to retain voting rights. Philanthropists more interested in engaging in lobbying and a higher degree of control, flexibility, and privacy.

While philanthropy may initially appear uncomplicated, it is a complex process with multiple considerations. It is important to enlist the support of experienced philanthropy advisors, tax, and estate planning professionals who work through these issues with clients on a daily basis and can advise on the most effective plan.

William Blair's Approach to Philanthropic Planning

At William Blair, we believe that a family's true philanthropic legacy is measured not by the amount of money contributed, but by the impact that the family has on the lives of those around them. Strengthening this impact across multiple generations requires vision and careful planning that effectively uses the various charitable giving vehicles.

Many clients seek to create alignment with their values and purpose not just in how they give, but also in how they invest. For clients who prioritize environment, social, and governance (ESG) issues and/or impact investing, we work closely with them to build customized portfolios that reflect these values. This approach can be particularly powerful when applied to the portfolio funding a private foundation or DAF.

For 90 years, we have been committed to helping clients and their families navigate the many decisions that go into building philanthropic legacies. To learn more about how to get started in developing a tax-efficient and strategic plan for your charitable giving, please contact us.

For more information, please contact your William Blair wealth advisor or:

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