Staying Charitable to Charities – Not the IRS

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When individuals are considering donating to charity, their sole focus is supporting a cause, aiding in a project, or helping those in need. Their personal benefit doesn't enter into the equation. That said, in the past, it was fairly straightforward – being charitable generally resulted in a lower tax bill. Since the introduction of the 2018 Tax Cuts and Jobs Act, however, that is no longer the case.

Several revisions were implemented under the new tax reform. With regard to deductions, the two critical changes were the $10k cap placed on SALT deductions (state, local, real estate taxes) and the substantial increase of the standard deduction (roughly 2x).

The combination of these tax code adjustments is leading many to claim the standard deduction for the first time in years. And because of that, charitable contributions are no longer reducing one's tax bill. Enter two strategies – the qualified charitable distribution and bunching contributions, also referred to as front-loading.

Qualified Charitable Distribution

A qualified charitable distribution or "QCD" is a powerful strategy for those who have reached age 70 ½. This age is also known as the Required Minimum Distribution age or "RMD" age. Upon reaching RMD age, individuals are required to start distributions from their IRAs, 401(k)s, and other retirement plans, whether they need the funds or not. These distributions are federally taxable.

The QCD strategy allows you to send funds directly from your IRA to the charitable organization. By doing so, you satisfy a portion of your RMD and avoid recognizing that amount as taxable income. Not only does this save the average taxpayer 15-20% in federal taxes, but it can also help lessen exposure to Social Security taxes, and Medicare Part B premium increases.

In short, this strategy is a no brainer if you're RMD age, charitably minded, and lukewarm towards higher taxes. So, what if you haven't reached age 70 ½?

Bunching Contributions

If you're unable to itemize deductions given the reasons outlined earlier, then you're not realizing any tax savings on your charitable contributions. Introducing a second strategy - bunching contributions or front-loading.

As an example, this approach would entail doubling or tripling your typical annual donation in a given year – then subsequently foregoing donations in the following two or three years. In the present year, you'd overcome the standard deduction, increasing tax savings. In the succeeding years, you'd take the standard deduction – no different than you would have otherwise.

This strategy obviously hinges on your after-tax portfolio and cash flow capacity. Assuming it's feasibility, front-loading can be further amplified by using a charitable gift trust and/or transferring appreciated securities.

Reach out to a CERTIFIED FINANCIAL PLANNER™ to learn more and determine whether these strategies make sense for you and your family. Have a happy and safe New Year!

Note: This article is for financial planning purposes. Please consult with a qualified tax professional for advice on your specific situation.

November 2019