

Charitable Giving Considerations in the Face of New Legislation

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The Consolidated Appropriations Act of 2021¹ was passed at the end of 2020 and created some very compelling opportunities for giving. However, for quite some time, we've heard rumblings about the possibility of higher taxes and less generous provisions regarding tax and estate planning for wealthy individuals in the not-so-distant future.

With President Biden's initial proposal now revealed², we believe the most important takeaway is that 2021 is the year to act as any changes would likely become effective as of January 1, 2022. Since tax incentives to give charitably are much stronger now, it's time to determine which assets may be candidates for giving and how to best accomplish donations in the current environment.

CONSIDERATIONS

1. Charitable giving deductions for itemizers and high earners may be reduced.

Currently, cash contributions made directly to public charities are deductible up to 100% of the donor's adjusted gross income (AGI) for itemizers. In other words, if someone makes \$600k/year and gives \$600k cash to charity, they pay no Federal tax because they would have no taxable income. Assuming the donor is in the top Federal tax bracket, this provision represents a 37% savings on the deduction. Under the current proposal, however, the deduction may be limited to just a 28% benefit and PEASE limitations (which restrict the benefit of itemized deductions and are a stealth tax on upper income earners) may impact those with incomes over \$400k.

Planning Opportunity: Front-loading charitable donations is beneficial from a tax perspective and can be a very powerful strategy. Consider bunching itemized deductions into 2021 when the deductions are more valuable. You may have other recurring itemized deductions too, such as mortgage interest and up to \$10k on property taxes, that together make this quite an interesting strategy. Then, perhaps in 2022 and 2023, take the standard deduction and back away from charitable giving for those years.

2. The Federal Estate Tax exemption amount may be significantly reduced.

The exemption is currently \$11.7 million per person at a 40% rate but may be limited to \$3.5 million per person with the rate increasing to 45%. This amount is above and beyond the \$15,000/year (2021 amount) that each person can gift to other individuals each calendar year.

Planning Opportunity: Front-load taxable gifts in the near-term to reduce large estates. I have seen a lot of action taken in this area ahead of the potential change in law. While this strategy does not pertain directly to charitable giving, gifting to heirs could be made more challenging in the future so accelerating gifts may make good sense, especially with regard to property that is expected to further appreciate in the future. This should be considered in the context of other assets that may be suitable for charitable giving.

3. The capital gains tax rate may be increasing for high earners.

The long-term capital gains tax rate is currently 20% for higher income taxpayers. Even after tacking on the 3.8% Medicare surtax, this is still a very attractive rate. Under the President's current proposal, capital gains and dividends could be taxed at 39.6% on income over \$1m. This is clearly a dramatic shift.

Planning Opportunity: Consider recognizing gains for stock held long-term at lower rates to either lock in gains at a lower tax rate or to subsequently buy stock back at a higher tax basis that is intended to be held long-term. If capital gains rates do increase, the value of a tax deduction for gifting low basis stock held long-term to charities directly or via a Donor Advised Fund or other vehicle may become more attractive.

4. The “step up” in tax basis may be reduced or eliminated.

During my last blog, I discussed the challenging predicament facing those of us in the sandwich generation. When it comes to helping elderly parents, a change in “step up” rules could complicate plans that are already in place for disposing of a family home once the matriarch or patriarch passes away.

It is currently a good strategy for low basis assets, such as stock or property, to remain owned by older individuals (as there would be a “step up” in basis of the asset upon the owner’s death). The property can then be sold by heirs to raise cash for liquidity needs without a significant tax consequence.

Planning Opportunity: If the “step up” in basis at death is either modified or repealed, property owners may want to consider making transfers during life instead of to heirs where the cost basis and holding period of the grantor shifts to the recipient.

NEXT STEPS

I recently had the pleasure of speaking on this topic for the Jewish Home Foundation. If you’d like to watch the full presentation to learn more, please click [here](#). If you have any questions or would like to talk further about how these proposed changes may affect you and your financial plan, please reach out to me anytime.

All the best to you and yours.

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Sources:

¹ <https://www.congress.gov/116/bills/hr133/BILLS-116hr133enr.pdf>

² <https://taxfoundation.org/joe-biden-tax-plan-2020/#Details>

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