ABC’S OF CHARITABLE GIVING

I.
WHY DO WE GIVE TO CHARITIES?

You can share your commitment in being a philanthropist; you can share your good fortune in being a philanthropist; you can have personal satisfaction in being a philanthropist and you can save income and/or gift and estate taxes when you give to a charity.

Having a lot of wealth does not make a philanthropist, but rather, philanthropy is an individuals desire to promote human welfare by an act of giving.

The main reasons often expressed by people of why they give to a charity include but are not limited to the following:

A. Personal satisfaction in sharing their good fortune with others.

B. Having a desire to transmit family values and social responsibility to successive generations.

C. Having a strong desire to see that the purpose of the Charity is sustained and ensuring that the Charity has the financial ability to accomplish it’s goals.

D. Utilizing the income tax laws to sell assets without capital gains to achieve greater diversification of investments in order to provide a larger amount of money for investment and resulting in a greater income stream during lifetime for him or her.

E. Utilizing the income tax laws to reduce current income taxes through the income tax charitable deduction.

F. Utilizing the gift and estate tax laws to reduce or eliminate federal estate taxes at the time of death.

II.

INCOME, GIFT AND ESTATE TAX CHARITABLE DEDUCTIONS

The Federal Government encourages charitable giving to qualified organizations by allowing income, gift and estate tax deductions to the individuals who make such gifts.

While some of the documents for accomplishing the objectives of the donor are fairly straight forward, the tax issues are quite complicated.

A. Income tax Charitable Deduction.

In general there are three factors that affect how much you can deduct as a charitable gift on your income tax return. The first factor is the individual's Adjusted Gross Income. The second factor relates to how much of the value of the asset qualifies for the deduction. In some situations the deduction can be less than fair market value of the gift.
The third factor is the type of organization to which the donation is made.

All three factors are dependant on the type of property donated and whether the gift is made to the organization or whether the gift is for the use of such organization.

1. When making a gift during your lifetime and you are going to take an income tax charitable deduction you need to take into consideration the following:

a. What type of Charity is it?

Public.

Lincoln Unitarian Foundation International is a Public Charity.

Semi Public.

Typical semipublic charities are private foundations.

b. What is the asset that is to be given to the Charity?

Cash.

Appreciated short term gain property.

Appreciated long term gain property.

c. What is the purpose of the gift to the Charity?

Outright.

For the use of the Charity.

d. The answers these questions determines:

How much of the value of the asset qualifies for the deduction, and

The amount of Adjusted Gross Income that can be offset with the deduction.

2. Adjusted Gross Income Limit for Cash Gifts.

For purposes of the limits based on Adjusted Gross Income we have to distinguish between Public Charities and All other Charities.

IT IS PRESUMED FOR PURPOSES OF THIS PRESENTATION THAT THE CHARITY TO WHOM YOU MIGHT WANT TO MAKE A GIFT IS EXEMPT FROM INCOME TAX, GIFT TAX AND FEDERAL ESTATE TAX.

a. The amount of the income tax deduction for gifts of cash made to public charities is limited to 50% of the taxpayer's Adjusted Gross Income.

b. The amount of the income tax deduction for gifts made to all other charities is limited to 30% of the taxpayer's Adjusted Gross Income.

3. Adjusted Gross Income Limit for Non Cash Gifts

a. If the gift to a public charity consists of appreciated long term capital gain property, then the amount of the tax deduction is limited to 30% of the taxpayer's Adjusted Gross Income rather than the 50% of the taxpayer's Adjusted Gross Income for gifts of cash.

b. If the gift to the semipublic charity consists of appreciated long term capital gain property, then the amount of the tax deduction is limited to 20% of the taxpayer's Adjusted Gross Income rather than the 30% of the taxpayer's Adjusted Gross Income for gifts of cash.

4. Less than Fair Market Value Limit.

Generally the amount available for the income tax deduction will be equal to the fair market value of the assets contributed.

a. If the gift to the public charity consists of appreciated property and the gain on a sale would have been deemed to be ordinary income (i.e. short term capital gain property) rather than long term capital gain income; the amount available for the deduction will be limited to the basis of the property. An example of this type of property the contribution of a life insurance policy.

b. If the gift to the semi public charity consists of appreciated property and the gain on a sale would have been deemed to be ordinary income (i.e. short term capital gain property) rather than long term capital gain income; the amount available for the deduction will be limited to 20% of the taxpayer's contribution base.

5. Any amounts over the 50%, 30% or 20% not used in the year of the gift can

be used on income tax returns in the following 5 years.

B. Gift and Estate Tax Charitable Deduction.

If a gift is made during an individuals lifetime, then the value of the gift also may be subject to the payment of gift tax. Likewise, gifts made to beneficiaries at the time of death may be subject to the payment of federal estate tax.

1. Transfers of property to qualified charities generally are fully exempt from gift and estate taxes. Thus the gift and estate tax charitable deduction potentially is unlimited. NO LIMITS LIKE THE INCOME TAX CHARITABLE DEDUCTIONS.

2. All non cash gifts such as real estate, stocks, bonds, mutual funds or securities whether the asset has been held short or long term allows you to receive a gift or estate tax deduction of the fair market value (no reduction of the value to a contribution base).

3. If a gift is being made to a public charity through the provisions of a will, often the best asset to use to satisfy the gift is property that is called IRD (Income in Respect of a Decedent). This is property that has accrued income on it that must be counted as income to the person who receives the proceeds. Such property would include retirement accounts, annuities, E or HH bonds, etc. This allows you to remove the amount representing deferred income from your income tax bracket. The qualified charity would pay no income tax on the deferred income.

III.

METHODS OF GIVING TO THE CHARITY

There are several methods of giving to charities.

A. The type of method used may depend on:

1. Whether you want to benefit the charity but not reduce the amounts given to your relatives;

2. Whether or not you want to give up income from the asset;

3. Whether you are looking for a current income tax deduction;

4. Whether or not you want to increase your current income while avoiding the realization of large capital gains; or

5. Whether you want to immediately benefit the charity but have the asset returned to you in the future.

While the following methods may look and sound intimidating, they are fairly straight forward in their structure, purpose and result. These methods are valuable estate and income tax planning tools that are not just for the extremely wealthy.

B. Outright Gifts.

The easiest form of gift is an outright transfer of money or other assets to the charity. By making an outright transfer you:

1. Give up ownership of the asset.

2. Give up future income from the asset.

3. Eliminate the value of the asset from your estate and reduce the amount of federal estate tax that might be paid at the time of death.

C. Life Insurance.

1. Name the Charity as the primary beneficiary, co-beneficiary, or successor beneficiary of an existing policy while retaining ownership. No current income tax deduction.

2. Buy a new policy or change a current policy with the Charity as owner and beneficiary. Nebraska allows charities to own or purchase life insurance on the lives of those who consent. The Charity would then make the premium payments.

3. Name the Charity as owner of a current policy or have the Charity purchase a new policy with the Charity paying one half of the premium and the donor paying one half of the premium. This enhances the endowment fund.

4. Where we have spouses, have the Charity purchase a second to die policy. The death benefit is usually higher than the single life policy for the same amount of premium dollar. This is because the policy is not paid until the second person dies.

5. Name the Charity as sole revocable Beneficiary of group term life insurance in excess of $50,000.00. The advantage of this is that it eliminates the need of the taxpayer from reporting the income tax cost of the term insurance coverage in excess of the $50,000.00 as income as long as the Charity remains the beneficiary. You do not get a charitable income tax deduction, but income tax is avoided on the value of "premiums" required to provide protection in excess of $50,000.00. The conservative approach is to name the Charity as sole Beneficiary of the entire amount of the group term life policy.

6. Give a paid up policy to the Charity. Remember that you are limited to your basis in the insurance policy for the income tax charitable deduction.

7. Assign your annual dividends on your policy to the Charity.

8. There are a number of reasons for using life insurance as the vehicle to make your charitable gift:

a. It provides a guaranteed death benefit.

b. It allows you to give a larger gift for the amount paid in premiums because a relatively small amount of premium can translate into a large meaningful gift.

c. It allows you to satisfy your desire to make a charitable contribution to a Charity at a low cost.

d. It allows you to satisfy your desire to make a charitable contribution to a Charity without taking from the assets you will be giving to your children or other beneficiaries.

e. It involves none of the cost, delay or uncertainty of probate.

f. In Nebraska it is not subject to the claims of creditors at the time of death.

g. You retain the right to use the policy cash values as collateral for loans.

C. Donor Assisted Funds.

Donor assisted funds is a charitable giving device established by an individual with a non profit organization. Any non profit organization can create a Donor Assisted Funds program and act as the “host” Charity. Usually these programs are run by Community Foundations, however, the Fidelity financial service company created the Fidelity Charitable Gift Fund which is recognized as a public charity.

The way they work is as follows:

1. The Donor Assisted Fund is owned and operated by the non profit organization.

2. The Donor enters into a fund agreement with the non profit organization. The Donor can retain the ability to give advice on distributions from the funds income and principal.

3. The fund agreement can allow the Donor or those designated by him or her to act in an advisory capacity with regard to investment strategy and grant making.

4. After considering the Donor’s recommendations, the Board of the non profit organization makes the grant to a qualified charity.

5. There are a number of reasons for utilizing the Donor Assisted Fund as the vehicle to make your charitable gift:

a. It has no start up costs.

b. The income tax deduction for cash gifts is 50% of Adjusted Gross Income.

c. The income tax deduction for publically traded securities is 30% of Adjusted Gross Income.

d. Allows family involvement through multiple successive generations.

e. There is no gift tax.

f. The estate is reduced by the value of the gift.

D. Remainders in Personal Residence or Farm.

An individual can get income and estate tax benefits by making a charitable gift of his or her personal residence or farm, even though the right to the life enjoyment is retained by him or her.

D. Charitable Remainder Unitrusts.

The Charitable Remainder Trust allows you to make a charitable contribution of property and still keep an income stream for yourself or for someone else. The income stream can be for life or for a fixed term. These trusts are the type of trust that is most attractive for the income tax benefits they give to individuals who own appreciated property that is non liquid and/or produces insufficient income.

Not only can you convert a non liquid asset to one that pays income, you also receive a charitable deduction when you transfer the property into trust. The Charity then benefits after you no longer need the income.

If you are attempting to get the charitable income tax deduction you create an irrevocable charitable remainder trust into which you place the appreciated property. The Trustee then sells the appreciated property and invests the proceeds. Since the charitable remainder trust is exempt from tax on the capital gain from the sale of the this appreciated property, the proceeds are fully available for investment and is not reduced by federal income taxes.

1. The three main reasons for having this trust are:

a. It allows the sale of an asset without paying capital gains tax leaving more to generate income.

b. It allows the conversion of a non liquid asset into a lifetime income stream.

c. It provides an income tax charitable deduction when the property is put into the trust or an estate tax charitable deduction at the time of death.

2. There are three types of charitable remainder unitrusts.

a. Charitable Remainder Annuity Trust

Provides a guaranteed fixed annuity each year. The annuity is a fixed percentage of assets valued when assets are first given to trust.

b. Charitable Remainder Unitrust

Provides income that varies each year. Annual income is a fixed percentage of value of assets as valued each year.

c. Pooled Income Fund

Assets added to other individuals and paid income based on pro-rata share of fund.

3. The following is an example of this arrangement using the charitable remainder annuity trust. In this example we assume the following:

a. Husband and wife have an unmortgaged piece of farm ground worth $250,000.00 that they will transfer to the charitable remainder annuity trust;

b. The basis in the farm ground is $50,000.00;

c. Their capital gain is $200,000.00.

d. Their effective tax rate is 33%.

e. They want to make a contribution to their favorite charity and provide themselves with added income for their retirement; and

f. They specify that they want an annuity that is 6% of the value of the land payable annually for the rest of their joint lives.

g. Husband and wife are both 65.

The trustee sells the land and reinvests the proceeds. If the sale would have occurred prior to transferring, then the couple would have paid around $66,000.00 in income taxes. This amount was saved and was available for investment to generate additional income. In addition to the capital gains tax savings, the couple gets an income stream of $15,000.00 per year; they get an immediate income tax charitable deduction; they have turned low income producing property into higher income producing property; and they have benefitted their favorite charity.

E. Charitable Lead Trusts

You would like to help a charity, but you would also like to help my kids.

With a Charitable Lead Trust you do not have to choose between the two goals.

Charitable Lead Trusts are a type of trust that is most attractive for the income tax benefits it gives to individuals who have substantial income. This trust is nearly identical to the Charitable Remainder Trust except that the charity receives the income for a specified term of years. At the end of the term the assets revert to you or to other beneficiaries designated by you.

1. The three main reasons for having this trust are:

a. It provides an income tax charitable deduction when the property is put into the trust or an estate tax charitable deduction at the time of death.

b. It allows the diversion of income away from a high income tax bracket to the Charity which pays no income tax because of it's exempt tax status.

c. It allows you to ultimately get back the property when you would normally be in a lower income tax bracket or to give the property to other relatives.

The Charitable Lead Trust allows you to make a charitable contribution of property and to divert income from yourself. You still maintain control over the ultimate transfer of the property. The Charity benefits immediately.

For any gift you make you should consult with your accountant and/or your attorney in addition to the charity. Be sure you know the benefits and utilize the method best suited for you.

YOU CAN AND WILL MAKE A DIFFERENCE WITH YOUR GIFT TO YOUR FAVORITE CHARITY.