THE SALVATION ARMY

Charitable Intent

DOING THE MOST GOOD

PLANNING NEWS AND IDEAS FOR THE PROFESSIONAL ADVISER

CHARITABLE GIVING AFTER THE TAX CUTS AND JOBS ACT OF 2017

Unlike some other itemized expenses, deductions for charitable gifts were made more generous under the Tax Cuts and Jobs Act signed at the end of 2017. Cash gifts are now deductible up to 60% of a donor's adjusted gross income, versus 50% previously. That increase is not likely to result in more donors itemizing, however, due to cutbacks in other deductions and an almost doubling of the standard deductions. It's estimated that the percentage of taxpayers itemizing will drop from about 30% to about 5%.

The estate tax charitable deduction will also be of use in far fewer estates with the credit sheltering estates up to $11.2 million in 2018. Clients with smaller estates might instead find it worthwhile to accelerate their charitable bequests into lifetime gifts, including life-income arrangements, that provide larger income tax deductions.

Lifetime gifts

There are several options for philanthropic clients whose only other itemized deduction might be the $10,000 allowed for state and local taxes.

■ ***Bunching*** – Donors might make two or three years' worth of charitable gifts in one year, allowing them to itemize every second or third year.

■ ***Qualified charitable distributions from IRAs*** – Although no income tax charitable deduction is allowed for QCDs, the distributions can take the place of required minimum distributions that would otherwise be subject to tax at rates up to 37%. Clients age 70½ and older may give up to $100,000 annually to public charities. QCDs cannot be used to arrange charitable remainder trusts or charitable gift annuities and cannot be given to private foundations or donor advised funds.

■ ***Capital gains*** – Clients with significant gains in the stock market can lock in some appreciation by using the shares to arrange life-income gifts such as charitable remainder trusts and charitable gift annuities. With either vehicle, the donor receives lifetime payments based on the full fair market value of the stock, with no loss to capital gains tax. The deductions allowed for the trusts and gift annuities might enable donors to exceed the standard deductions.

■ ***Remainder interests in homes and farms*** – A donor who planned to leave a home or farm to charity at death can transfer the real estate now, while retaining a life estate [Code §170(f)(3)(B)(i)]. The donor can continue using the home or farm, or even rent the property for income during their lifetime. An income tax deduction is available for charity's right to eventually receive the property.

Estate gifts

Charitable gifts will continue to play an important role for clients whose estates are subject to tax, but even those with estates far below the $11.2 million sheltered amount may find reasons to include charitable bequests.

■ ***Sheltering income in respect of a decedent*** – Income tax planning is important for estates of any size with retirement accounts, U.S. savings bonds and other items of IRD. Income tax is avoided entirely when these assets pass to charity. Clients can also have IRD assets pass at death to a charitable remainder trust that will make payments for life to family members. The immediate income tax is avoided [Letter Ruling 9237020]. The same is true where charity is named the beneficiary of IRD assets, contingent on the establishment of a testamentary charity gift annuity [Letter Ruling 200230018].

■ ***Non-qualified charitable remainder trusts*** – Clients not concerned with the estate tax charitable deduction have greater flexibility in establishing testamentary charitable remainder trusts. Trusts can provide for all income, and even corpus, to be distributed to loved ones before the remainder passes to charity and need not have a 10% charitable remainder. A non-qualified charitable remainder trust is not tax-exempt, but because estate assets receive a stepped-up basis at death, there will be little capital gains if assets are liquidated soon after death.

GUIDANCE ON DAFS FROM IRS

The IRS recently issued interim guidance on donor advised funds while it works on proposed regulations regarding incidental benefits to donors.

Event sponsorship

The IRS gave an example of a charity event for which the tickets were $1,000, of which $900 represents the charitable portion and $100 is the fair market value of what the donor receives. If the DAF account owner pays the $100 portion and advises a gift from the DAF for the $900 charitable amount, the IRS said the DAF distribution would be subsidizing the owner's attendance or participation. This would be considered more than an incidental benefit under Code §4967.

Pledges

DAFs are often asked to make distributions to organizations where the account owner has made a pledge. It places an undue burden on sponsors of DAFs to determine whether a pledge is binding under local law or is simply an expression of the account owner's charitable intent. The satisfaction of a legal obligation of a disqualified person constitutes self-dealing under Reg. §53.4941(d)-2(f)(1).

The IRS said that a distribution from a DAF to a charity where the account owner has an outstanding pledge will not be considered to result in more than an incidental benefit, provided: (1) the DAF makes no reference to the existence of a pledge when making the distribution, (2) the account owner receives, directly or indirectly, no more than an incidental benefit as a result of the DAF distribution and (3) the account owner does not attempt to claim a charitable deduction under Code §170(a), even if the charity erroneously sends a letter that conforms with the requirements for a contemporaneous written acknowledgment under Code §170(f)(8). **Notice 2017-73**

MODIFICATION DOESN'T MAKE GIFTS DEDUCTIBLE

Under Code §642(c)(1), a trust is entitled to an unlimited deduction from gross income for any amount passing to charity pursuant to the terms of the governing instrument. A trustee received judicial approval to modify a trust to allow an individual to exercise powers of appointment in favor of two foundations. Initially, the trust did not authorize charitable distributions during the lifetimes of the beneficiaries.

The IRS said that a settlement agreement arising from a will contest qualifies as a governing instrument [Rev. Rul. 59-15], but that a modification will not be considered the governing instrument where it is not the result of a conflict. The IRS said the modification to this trust changed the terms of the governing instrument beyond its original intent.

The IRS added that it was not claiming that the modification order was invalid or that it was not binding on the parties. However, the judicial modification only determines the rights of the parties under state law, not the federal tax consequences of the modification. **CCA 201747005**

HELPING YOUR CLIENT THROUGH THE NEW TAX ENVIRONMENT

With or without a charitable deduction, Americans contribute and bequeath billions every year to charity. There's no reason to think that generosity will change under the new tax law. Giving has always been driven by a desire to support a charity's mission, not simply to get a tax break. The Salvation Army is available to help you and your clients navigate the charitable landscape and suggest ideas for using charitable vehicles to address a variety of personal and family issues. We provide this service at no cost or obligation. Please feel free to contact our office to learn more.