Charitable Giving 101

What you need to know about tax deductions, trusts, DAFs and QCDs

When social interaction was limited during the pandemic, many found a meaningful connection through charitable giving. In 2020, U.S. charitable giving increased by 5%, reaching a record $471.44 billion, including contributions from individuals and foundations.[1] Then, last year, it increased again by an additional 2.7%.[2]

Historically, charitable giving practices have been tied to one's desire to make an impact or leave a positive legacy on a community. The ways in which individuals typically give to charitable causes can be summed up with the three Ts: treasure, time and talent.

The majority of "treasure" donations come in the form of currency, checks and credit card payments, but personal property, marketable securities, business interest units and real estate also fall under this category. These alternative gifts are often focused specifically on the charitable organization's mission or need.

Some individuals choose to contribute their time and talent, more commonly referred to as volunteering. While not necessarily tax deductible, this can be very valuable to organizations who need assistance running charitable activities.

New donors and those who increased their charitable giving during the first two years of the pandemic reversed a decade long trend of fewer U.S households donating money. Here are a few key considerations for individuals looking to start or increase giving in 2022 and beyond.

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Charitable gifts: tax benefits and considerations

With such a wide array of charitable giving options, it's important to understand how each gift could affect your annual deductions. Here's a quick guide to tax deductions, out-of-pocket deductions and required substantiation:

Tax deductions

A charitable gift in the form of cash or hard assets like real estate can be deducted from your taxes, whether you are an individual or an organization. But there are limits to a taxpayer's current year deductions. While the type of gift plays a large part in determining the magnitude of the deduction, so does the receiving entity and the giver's taxable adjusted gross income (AGI).

TIPS:

- Through 2025, giving all gifts in cash to public charities, including Donor Advised Funds (DAF), during the calendar year increases your allowed deduction from 50% AGI to 60%.
- If you are giving to private foundations, you will be limited to 30% AGI.
- Public charity gifts in the form of long-term marketable securities are also limited to 30% AGI, and even less at 20% if to a private foundation.
- Other long-term intangible gifts like business interests and notes may be deductible on an income tax return.

Deductible out-of-pocket costs

While volunteering does not often include writing a check to the organization, regular volunteers can incur expenses. For example, a university board member who travels to meetings pays for meals, flights and other necessities while volunteering. These out-of-pocket expenses are eligible for a charitable contribution deduction.

TIPS:

It's important to note that the IRS only allows volunteers to claim a charitable contribution deduction for travel expenses if most of the time is dedicated to the charitable activity. To take this deduction, track volunteer hours and expenses, document activities and save receipts.

Substantiation required

The IRS will want to see that you're taking the appropriate deduction based on the fair market value (FMV) with a receipt from the charity that received the gift. The threshold for required substantiation is $250 for cash gifts. Similar requirements exist for non-cash gifts over $500; however, large non-cash gifts require more substantiation to verify their value. A qualified appraisal may be required for non-cash gifts more than $5,000, such as high-value artwork or real estate.

You must have the required substantiation by the earlier of the date you file your tax return or the due date of the return, including extensions.

TIPS:

Keep all receipts for gifts given during the calendar year. If the gift is over $5,000, acknowledgment and a qualified appraisal is required to verify the value of the gift. Form 8283 must be filled out by the charitable organization and appraiser if over $5,000.

Alternate options for giving beyond direct gifts

For those looking to go beyond the standard financial donation to an organization, there are a few alternate options. Each of these methods is impacted by the tax considerations previously discussed.

Trusts

The most common type of trust you can create for charitable giving is a charitable remainder trust (CRT), which is an irrevocable trust for the benefit of the charity and the individual. This means it's a split interest gift.

Let's say you give $1 million to a CRT. In the first year the gift is donated, you will receive a tax deduction for the fair market value of the trust remainder interest. Every year of the CRT's term, as the gifter you'll receive a payment, which may be a set amount or a percentage of the trust value, depending on the type of CRT. At the end of the term, the charity takes the money that is left.

Alternatively, a charitable lead trust (CLT), while still a split-interest gift, provides the reverse experience, providing an income stream to the charity through yearly returns and an individual beneficiary at the end of the term.

Donor Advised Fund (DAF)

Less complex and more common than a trust, a DAF is a giving account established at a public charity that allows donors to recommend grants over time. The donor decides the timing of the donation, the charity that benefits from the donation and the size of the donation made from the fund. The donor also claims the tax deductions upon funding the DAF.

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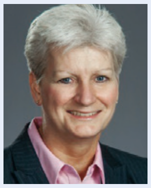

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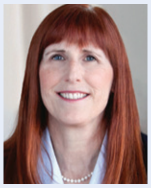

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One way to think about DAFs is as if you are creating your own public charity that allows for higher tax deduction limitations and the ability to defer the actual gift giving to a later year to align with your gifting strategies and commitments. DAFs may function like private foundations, without the 5% annual distribution rule, as multiple family generations can work together for grant making.

IRA Qualified Charitable Distributions (QCD)

An option only for donors over 70.5 years old, QCDs allow individuals to give up to $100,000 annually to charitable organizations directly from their IRA. The benefit: while the donor can't claim a charitable deduction for the gift, QCDs will never count towards the donor's taxable income.

While the amount and type of donation is a personal decision for families, charitable giving is a part of American culture and many family legacies. Understand the tax benefits and considerations before making donations, whether by means of cash, assets or even when donating your time. The impact on your community and family can be life changing.

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[1] Philanthropy Network Greater Philadelphia "Giving USA 2021: In a year of unprecedented events and challenges, charitable giving reached a record $471.44 billion in 2020," June 15, 2021.

[2] Association of Fundraising Professionals (AFP) "Charitable Giving in 2021 Increased 2.7% over Unprecedented 2020 Levels," April 7, 2022.