GRACE
LUTHERAN
CHURCH
& SCHOOL

Win-Win Giving

Tax-advantaged Charitable Contributions

Introduction

How would you like to be able to increase your charitable contributions while decreasing your income taxes? Here are three tax-advantaged ways to donate:

1. Using a donor-advised fund to "bunch" contributions
2. Contributing appreciated securities (e.g., stock)
3. Contributing required minimum distributions (RMDs) from a retirement account

Increase your charitable contributions while decreasing your income taxes.

These techniques have become more advantageous since 2018, when the rules changed to significantly limit itemized deductions and significantly increase the standard deduction. For many taxpayers, these changes eliminated the ability to take a tax deduction for charitable contributions.

All three of these techniques are highly publicized and are becoming more widely used as people become more aware of the benefits. For you and the charities, these techniques are WIN-WIN propositions.

This brochure presents simplified examples, meant only to show how each technique has potential financial and tax advantages. Actual income tax savings will depend on your filing status, deduction limitations, other itemized deductions, and tax brackets, among other things.

We hope you will apply these techniques to your Grace giving, but they apply equally to all of your charitable giving.

Bunching Using a Donor-Advised Fund (DAF)

If you typically make charitable contributions each year, but still don't have enough other itemized deductions to exceed the standard deduction, then a bunched deposit into a DAF will be advantageous. A DAF allows you to lump more than one year's charitable contributions into a single year. The technique of aggregating multiple years' of charitable contributions into one year is often referred to as "bunching".

The advantage of a DAF is that a deposit into the fund qualifies as a charitable contribution in the year of the deposit. Then, you can still spread smaller distributions to charities over multiple years. Distributions from a DAF account to charities do not qualify as charitable contributions, because your deposit into the DAF did qualify.

A DAF is similar to other personal investment funds, except distributions from a DAF can be made <u>only</u> to charitable organizations. DAFs are common and you can set one up with familiar brokers, such as Fidelity, Schwab, and Vanguard.

In addition, you can elect to invest the amount in your DAF, conservatively or more aggressively. Any investment income is not taxed and increases the amount available to distribute to charities.

Disclaimer: This brochure is not authoritative tax advice. It provides basic examples using generic assumptions to illustrate hypothetical possibilities. You should conduct your own research, consult with a financial advisor, or consult with a tax advisor to see whether and how these techniques could apply to your personal tax situation.

However, using a DAF necessitates being able to afford the large bunched deposit. One source for the large deposit can be stock. The tax advantages of donating stock are described in the next section.

Example of bunching using a donor-advised fund

Here is an example for a couple filing a joint income tax return, who typically make about $10,000 of charitable contributions each year and have other itemized deductions totaling $13,000. Their itemized deductions total $23,000 ($10,000+$13,000), but the standard deduction is larger at $24,800. Consequently, their charitable contributions have no tax benefit.

Instead of making $10,000 of deductible charitable contributions each year, they could bunch three years together and make one $30,000 DAF deposit. They can still make the $10,000 of annual distributions to charities from the DAF. Their itemized deductions in year one are now $43,000 ($30,000+$13,000), which is larger than the $24,800 standard deduction. Their itemized deductions in the next two years drop to $13,000 ($0+$13,000), but they will still be able to take the higher standard deduction in those two years. Bunching saves them $4,004 of income taxes. For you and the charities, bunching is a WIN-WIN proposition.

Lump more than one year's charitable contributions into a single year.

Bunching three years is just an example. Bunching more or fewer years could be just as, or more, effective depending on the level of your charitable contributions and the amounts of your other itemized deductions.

Bunching Using a Donor-Advised Fund

Without bunching, total taxes $62,832:	**2020**	**2021**	**2022**	**Total**
Income	$ 120,000	$ 120,000	$ 120,000	
Standard deduction:	*$ 24,800*	*$ 24,800*	*$ 24,800*	
Itemized deductions:	*$ 23,000*	*$ 23,000*	*$ 23,000*	
Larger of standard or itemized deductions	($ 24,800)	($ 24,800)	($ 24,800)	
Taxable income	$ 95,200	$ 95,200	$ 95,200	
Income tax @22%	$ 20,944	$ 20,944	$ 20,944	**$ 62,832**
With bunching, total taxes $58,828:				
Income	$ 120,000	$ 120,000	$ 120,000	
Standard deduction:	*$ 24,800*	*$ 24,800*	*$ 24,800*	
Itemized deductions:	*$ 43,000*	*$ 13,000*	*$ 13,000*	
Larger of standard or itemized deductions	($ 43,000)	($ 24,800)	($ 24,800)	
Taxable income	$ 77,000	$ 95,200	$ 95,200	
Income tax @22%	$ 16,940	$ 20,944	$ 20,944	**$ 58,828**
Tax savings:				**$ 4,004**

Contributing Appreciated Stock

Usually, if you sell stock for more than you paid for the stock, you will pay income taxes on the difference between the sales proceeds and your cost (i.e., the gain). However, if you donate stock to charity instead of selling the stock, then you don't owe any income taxes because you don't create a gain. Plus, the amount of your deductible charitable contribution for income tax purposes is equal to the appreciated value of the donated stock, not your cost.

If you donate stock to charity instead of selling the stock, then you don't owe any income taxes because you don't create a gain.

You can contribute stock directly to charities or you can contribute stock to a donor-advised fund. As explained above, a donor-advised fund is a means by which you can bunch your charitable contributions for income tax purposes.

Example of contributing appreciated stock

Assume a couple has stock with a value of $30,000 they can use to make charitable contributions, which they bought for $9,000 a few years ago. If they sell the stock, they will receive the $30,000 of sales proceeds, but will have to pay $3,150 of income taxes on the gain of $21,000, leaving only $26,850 to donate to charities or to a donor-advised fund. Using the facts from the bunching example, their itemized deductions will total $39,850 ($26,850+$13,000) in the year they sell the stock, assuming they contribute all of the net proceeds to charities or to a donor-advised fund.

On the other hand, if they donate the $30,000 of stock to charities or a donor-advised fund instead of selling it, their deduct-

Contributing Appreciated Stock

2020	Sell Stock	Contribute Stock	Tax Savings	Additional Donation
Market value of stock	$ 30,000	$ 30,000		
Cost basis	$ 9,000	n/a		
Taxable gain on sale	$ 21,000	$ 0		
Tax paid on $21,000 gain @15%	($ 3,150)	$ 0	**$ 3,150**	
Income	$ 120,000	$ 120,000		
Standard deduction:	*$ 24,800*			
Itemized deductions:	*$ 39,850*	*$ 43,000*		
Larger of standard or itemized deductions	($ 39,850)	($ 43,000)		
Taxable income	$ 80,150	$ 77,000		
Income tax @22%	($ 17,633)	($ 16,940)	**$ 693**	
Amount available for charitable contributions	**$ 26,850**	**$ 30,000**		**$ 3,150**
Total tax savings			**$ 3,843**	

ible charitable contribution is $30,000 and their itemized deductions will total $43,000 ($30,000+$13,000). As calculated below, their total taxes are $3,843 lower ($3,150 saved by avoiding the gain and $693 saved by the higher itemized deductions), and the charities receive $3,150 more, to boot.

For you and the charities, using appreciated stock is a WIN-WIN proposition.

Contributing Required Minimum Distributions (RMDs)

If you are over age 70½ and if you don't have enough deductions to itemize (a common situation under the new tax law), you can still enjoy a tax benefit from making charitable contributions. You can opt to make your charitable contributions using your RMDs. RMDs made to charities are called qualified charitable distributions (QCDs). QCDs are excluded from your income, thereby reducing your income and your taxes.

The rules do not allow a QCD to a donor-advised fund. All QCDs must go directly to a charity. So, you cannot use QCDs to accomplish bunching. However, a QCD reduces your income rather than increasing your itemized deductions, so the concept of maximizing your itemized deductions is a moot point.

Example of making qualified charitable distributions (QCD)

Assume $10,000 of a couple's income comes from RMDs and the couple uses that income to make their charitable contributions. The $10,000 of RMD income creates $2,200 of taxes (22%), leaving only $7,800 to contribute to charities.

Make your charitable contributions using your RMDs.

Contributing Required Minimum Distributions

	RMDs to You	QCDs to Charities	Tax Savings	Additional Donation
Non-RMD income	$ 110,000	$ 110,000		
Required minimum distribution income	$ 10,000	$ 0		
Total income	$ 120,000	$ 110,000		
Standard deduction:	*$ 27,400*	*$ 27,400*		
Itemized deductions:	*$ 17,800*	*$ 10,000*		
Larger of standard or itemized deductions	($ 27,400)	($ 27,400)		
Taxable income	$ 92,600	$ 82,600		
Income tax @22%	($ 20,372)	($ 18,172)	**$ 2,200**	
Required minimum distribution	$ 10,000	$ 10,000		
Amount needed to pay taxes on $10,000 RMD	($ 2,200)	$ 0		
Amount available for charitable contributions	**$ 7,800**	**$ 10,000**		**$ 2,200**

Assuming the couple has $10,000 of other itemized deductions, their total itemized deductions will be $17,800 ($7,800 + $10,000), which is less than their standard deduction of $27,400 (including $2,600 for being over age 65). Because their itemized deductions are smaller than the standard deduction, their $7,800 of charitable contributions have no tax benefit.

However, if they opt to send their $10,000 of RMDs directly to charities, then those QCDs are excluded from their income. Their itemized deductions drop to $10,000 ($0 + $10,000), but that doesn't matter because they will still take the standard deduction.

By sending the $10,000 directly to charities as QCDs, they avoid $2,200 in taxes and the charities receive $2,200 more. There is also the possibility their reduced income will lower their Medicare premiums. Using QCDs is a WIN-WIN-WIN proposition.

A plug for employer-matching programs

Another way of making larger charitable contributions, unrelated to the techniques described above, is through employer contribution matching programs. We have had good experience with religious organizations and private schools being eligible under these programs. Please look into whether your employer has a matching program and whether Grace would be an eligible recipient for the match.

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Request notification

We hope you make use of donor-advised funds, stock donations, and qualified charitable distributions. If you do, it is always good practice to let the Business Office know something is in the pipeline.

Donations from donor-advised funds and qualified charitable distributions come to Grace in the form of a check. Sometimes the check does not provide enough information to determine the source of the donation. Similarly, donations of stock into Grace's brokerage account come with even less information about the source of the donation.

A heads-up will help insure the donation gets into your account promptly.

Your results will be different

Everyone's personal financial and income tax situation will be different from the simple examples presented in this brochure. Please research these techniques or discuss them with your tax/financial advisor to determine how and whether they can be most advantageous to you.

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