Charitable Giving: A Win-Win Estate Planning Strategy

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Charitable giving is a win-win estate planning strategy for charities and donors alike. In addition to the altruistic benefit, many charitable gifts bring tax relief for the donor. This article explores opportunities to make charitable giving part of any estate plan.

1. Outright Gifts

The simplest strategy is an outright gift to charity. Outright gifts give the donor, or the donor's estate if the gift is made after death, a tax deduction. Lifetime cash gifts have the additional benefit of removing the asset from the donor's estate, which may lower estate taxes. Lifetime gifts of highly appreciated assets like stock or real estate are particularly effective because the donor may avoid capital gains taxes on the asset. Donors who depend on the assets for their livelihood may not be in a position to make an outright gift during their lifetimes, but they can arrange for a specific percentage or dollar gift to a charity through a will or trust.

2. Charitable Remainder Trusts

A charitable remainder trust (CRT) is a remarkable estate planning strategy because it provides tax benefits similar to an outright gift as well as a lifetime income stream for the donor. A CRT is an irrevocable, tax-exempt trust created when a donor transfers assets (irrevocably) to the trust. The trustee then invests the trust funds and pays the donor an income stream for a designated period of time, which is often the lifetime of the donor and possibly also the donor's spouse. At the end of the specified term, the charity keeps the remaining trust assets. A CRT either is an annuity trust or a unitrust; both allow flexibility in payment options but have important differences that should be explored further by each donor.

The tax benefits of a CRT may include an immediate income tax deduction for the value of the remainder that passes to charity, avoidance of capital gains taxes when highly-appreciated assets are contributed to the trust, and reduction of estate taxes since the asset is removed from the donor's estate.

3. Charitable Lead Trust

A charitable lead trust (CLT) gives income to the charity for a period of years, after which the remainder passes to the donor's heirs. Thus, a CLT is the reverse of a CRT. A CLT also allows the donor an income tax deduction for the charitable gift, which is the income stream that goes to charity, and again, the donor may avoid capital gains taxes on the assets transferred to the trust. While the donor must consider a discounted gift tax when transferring assets to the trust, the donor's heirs ultimately receive any remaining trust assets free of estate taxes.

4. Other Strategies

For gifts that do not justify the planning required for a private trust, donors may still take advantage of other charitable strategies. Some strategies provide income streams like a CRT but without the complexity. A charitable gift annuity allows donors to receive a lifetime income stream and immediate tax deduction, but the costs typically are less than a trust since the annuity is purchased directly from the charity. Similarly, donors may make gifts to a pooled income fund, which combines the contributions of many donors to leverage investment returns to the donors. Another strategy is a donor advised fund, which does not provide an income stream but, like a pooled income fund, does allow the donor to make contributions to many different charities. These alternatives also offer the donor a tax deduction and the possible avoidance of capital gains taxes.

5. Retirement Benefits

Finally, retirement benefits are an ideal asset to gift to charity for donors of any net worth. Donors may simply name the charity as the designated beneficiary with the plan administrator or IRA custodian. This strategy is simple and leverages what the donor's heirs receive from the estate. Retirement assets may be burdened with up to four taxes: both federal and state income taxes, and both federal and state death taxes. A charitable beneficiary is exempt from these taxes and can thus receive 100% of the gross retirement asset. This allows the heirs to receive non-retirement assets that do not bear the same income tax burden as retirement assets. Also, the heirs may receive a step up in the basis of non-retirement assets, which will further reduce the tax burden.

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There are many strategies to making charitable giving part of any estate plan. These strategies offer not just the altruistic benefit that comes from helping others, but they also provide significant tax advantages in a manner that makes charitable giving a win-win for donors and charities alike. This article is not legal advice and every donor should consult professional advisors for personal advice.

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