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Portfolio Rebalancing: A Tax-Efficient Opportunity for Charitable Giving

If you're a charitably inclined investor who uses an asset-allocation approach to your portfolio, the rebalancing process is a ripe opportunity to help increase your support to nonprofits while managing the overall health of your investments.

A periodic portfolio rebalancing helps keep your investments aligned with your risk tolerance and fine-tuned to your overall financial goals—but the associated tax consequences can be extensive. When you offload appreciated assets for a significant return, the capital gains realized could lead to a substantial tax bill.

A charitable strategy may reduce taxes

A charitable donation of long-term appreciated assets can be a great opportunity to reduce any increased tax liability accompanying a portfolio rebalancing. This efficient strategy can potentially eliminate taxes on capital gains while also enabling you to take a charitable income tax deduction in the amount of the fair market value of the assets.

Simplifying the rebalancing process

A charitable donation made to a donor-advised fund program at a public charity, such as a Giving Account® at Fidelity Charitable®, can be a powerful option if you are considering making a charitable gift to offset taxable income generated from rebalancing your portfolio.

With a donor-advised fund program, you make an irrevocable charitable contribution, become eligible to take an immediate tax deduction for the amount contributed, and support your favorite charities in a time frame that works best for your charitable causes. Additionally, you may contribute many types of assets to Fidelity Charitable and depend on us to handle the administrative details associated with your Giving Account—allowing you to focus on meeting your charitable goals.

Consider a hypothetical case:

Robert, age 54, and Judy, age 52, own a brokerage account that they would like to rebalance.

- The account has grown from $3.5M to $5.4M since 2008.
- The current asset allocation is 75% equities and 25% fixed income.
- Their target allocation is approximately 70% equities and 30% fixed income.

To reach their target allocation, they plan to shift $1M of equity investments with zero tax basis in the account to fixed income. Selling the equity investments will generate $1M of long-term capital gain.

Robert and Judy currently make charitable contributions of approximately $50,000 annually. After talking with their advisor, they decide to accelerate their giving and donate $250,000 of the appreciated securities to a donor-advised fund to minimize a prospective tax hit and to potentially fund their charitable contributions for several years.

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The charitable offset strategy

By making a qualified charitable contribution, Robert and Judy may reduce the tax cost of rebalancing $1M of their portfolio by $59,500.* In addition, they will be eligible for a charitable deduction of $250,000 on their income taxes worth $60,000 at a 24% rate.

Value of equities: $1,000,000

	Equities sold: $1,000,000 **Equities donated: $0**	**Equities sold: $750,000** **Equities donated: $250,000**
Sales proceeds subject to tax	$1,000,000	$750,000
Tax due	$238,000	$178,500

Tax savings: $59,500

With these rebalancing efforts, Robert and Judy now have an account of $4.4M with $3.05M in equities and $1.35M in fixed income. This creates an asset allocation of approximately 70/30 equities to fixed income. They have also donated $250,000 to charity and paid taxes associated with rebalancing. By donating a portion of their investments to charity, Robert and Judy have reduced the taxable consequences of rebalancing while continuing to support their favorite charities.

Call a Charitable Planning Specialist at **800-682-4438** or visit **FidelityCharitable.org** to learn more about our donor-advised fund program.

** As with any tax planning strategy, there may be additional considerations that pertain to your personal situation. Other strategies may provide more flexibility and similar savings. Please consult your tax advisor.*

Hypothetical tax amounts assume the following: a married couple filing jointly, using 2018 federal ordinary income tax rates,

$300,000 of taxable income, rebalancing of $1M of long-term capital gain from a $5.4M portfolio, $250,000 fully deductible charitable contribution, 20% capital gain rate, and 3.8% net investment income surtax. Other limitations, the federal alternative minimum tax and state and local taxes are not taken into account.

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