Tax reform and charitable giving

The Tax Cuts and Jobs Act, a widely anticipated overhaul to the tax code, was signed into law in December 2017. While the charitable tax deduction remains intact, other changes may influence when and how much Americans give to charity. People, of course, will continue to be motivated by the desire to make a positive impact on causes that they are passionate about. However, the tax reform law makes it more important than ever to make savvy financial decisions about charitable giving.

What's Inside

FIDELITY Charitable℠
Make more of a difference

White Paper

Tax legislation related to charitable giving

The Tax Cuts and Jobs Act overhauled the tax system, and you may be left wondering how it could affect your giving. Outlined below are the main tax rules that impact charitable giving. We recommend you talk with a tax advisor for how this may affect your specific situation.

Maintained charitable deduction

Taxpayers who itemize their deductions will still be able to deduct donations to qualified charitable organizations.

Impact on charitable giving: *Congress continues to value the charitable deduction and supports the tax incentives associated with giving.*

Maintained carry forward rules

The carry forward rules pertain to the limit on charitable contributions that can be deducted in a single year. The carry forward rules allow donors who contribute more than the prescribed charitable deduction limits in a single year—60% of AGI for cash, 30% for appreciated securities—to carry forward the excess deduction in the following five tax years.

Impact on charitable giving: *These rules allow you to deduct charitable contributions that exceed contribution limits in a given year and provide opportunities for tax planning.*

Maintained the capital gains tax rate

The long-term capital gains rates remain in place in the new tax law. Capital gains are a form of income reported on the 1040 and factored into a taxpayer's AGI. Taxpayers are subject to capital gains tax when selling appreciated securities held for over a year. The capital gains tax rate ranges from 0–20%, depending on the individual's income tax bracket. The Medicare surtax rate of 3.8% also remains, resulting in a capital gains tax of up to 23.8%.

Impact on charitable giving: *When donors contribute long-term appreciated assets to charity, they minimize the capital gains tax, enabling them to give up to 23.8% more. They will also continue to be able to take a fair market value[1] tax deduction.*

Increased the standard deduction

The standard deduction will increase to $12,000 for individuals and $24,000 for married couples filing jointly. This nearly doubles the standard deduction, which in 2017 was $6,350 for individuals and $12,700 for married couples filing jointly.

Impact on charitable giving: *Overall, fewer people will itemize deductions on their tax return. High-income taxpayers will continue to do so, but more middle-class families may not. If you stop itemizing your deductions, you will not receive a specific tax benefit for charitable giving.*

Increased limitation for cash charitable contributions

Through 2017, you could deduct the full amount of your cash contributions to charity as long as the deduction did not exceed 50% of your adjusted gross income (AGI). The new tax law increases the AGI limit on cash donations to 60%.

Rules limiting the amount of donated appreciated securities to 30% of AGI remain in place. Any contributions exceeding the AGI limits can be carried forward and applied over the next five years.

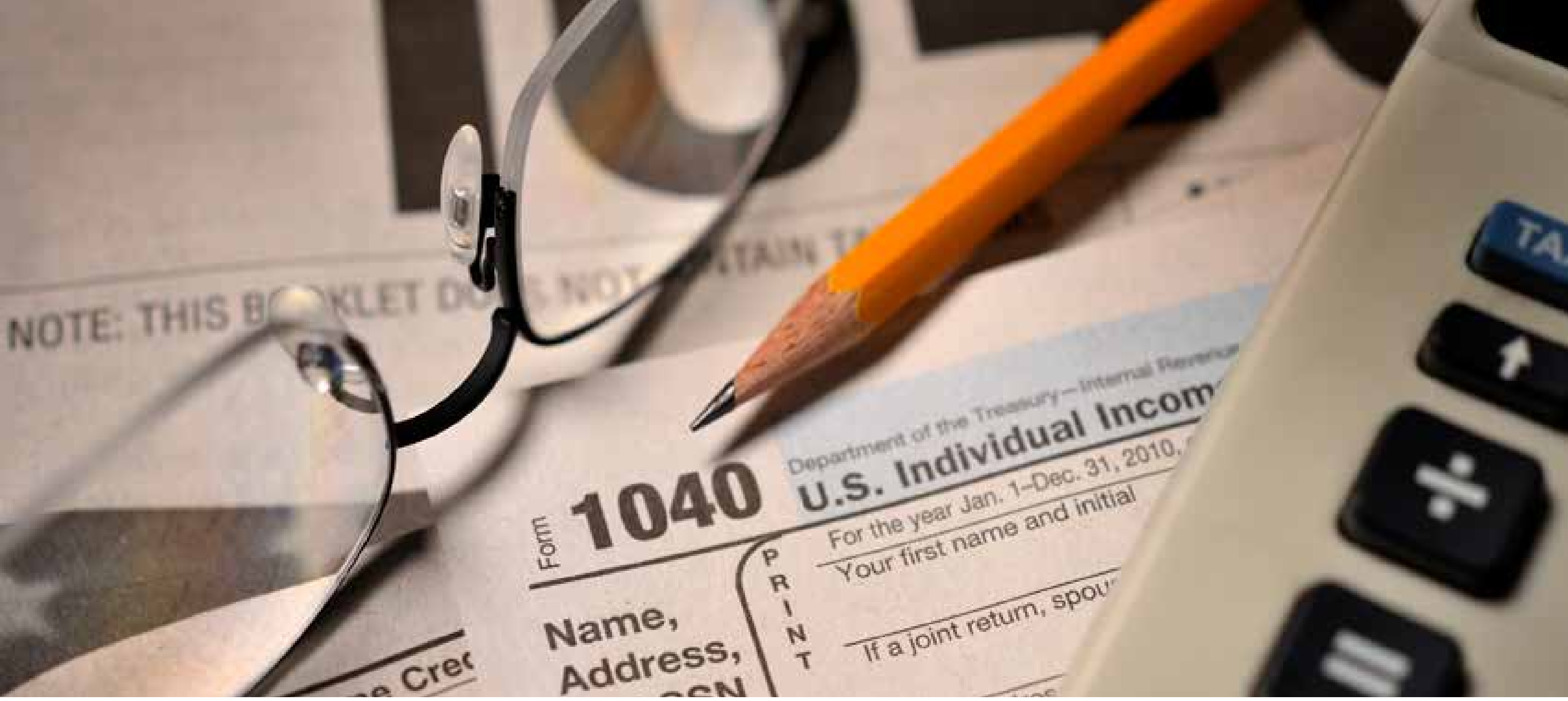
Impact on charitable giving: *This could have a positive effect, allowing for a higher tax deduction as a percent of AGI.*

Increased federal estate tax threshold

The law doubled the federal estate and gift tax threshold to $11M for individuals and $22M for married couples filing jointly. Until 2018, estates were subject to a tax when gross assets surpassed $5.49M for individuals and $10.98M for married couples filing jointly. The increased threshold means that fewer families will be subject to an estate tax.

Impact on charitable giving: *Charitable donations remain exempt from estate tax, and many high-net worth individuals offset estate taxes with charitable contributions. These strategies will be less frequently used as fewer people are subject to estate taxes.*

[1] *For contributions of complex or non-publicly traded assets, generally fair market value is determined by a qualified appraiser in compliance with the IRS.*



Reduced tax rates

The new tax law maintains seven tax brackets, but tweaks the income thresholds and lowers rates for most brackets.

Impact on charitable giving: *If you take a charitable tax deduction, this could mean a lower overall deduction for a similar contribution made in 2017. However, lower tax rates may also give you more discretionary income for charitable giving.*

Cut corporate tax rate

The law lowered the corporate tax rate from 35% to 21% beginning in 2018.

Impact on charitable giving: *For corporations taking a charitable tax deduction, this could mean a lower overall deduction for the same contribution. However, lower tax rates may also mean more discretionary income for charitable giving.*

Repealed the Pease limitation

The new law removed the Pease limitation from the tax code. The Pease limitation was an overall reduction on itemized deductions for higher-income taxpayers. The rule reduced the value of a taxpayer's itemized deductions by 3% of AGI over a certain threshold. The 3% reduction continued until it phased out 80% of the value of the taxpayer's itemized deductions.

Impact on charitable giving: *This has a positive impact on donors itemizing charitable contributions by allowing them to deduct more.*

Limited state and local tax (SALT) deductions

Up until 2017, taxpayers were able to claim state and local income, sales, and property taxes as a deduction on their federal returns. The new tax law maintains this deduction, but caps it at $10,000 and aggregates all of the individual taxes.

Impact on charitable giving: *In the past, the deduction of SALT in addition to charitable contributions allowed many people to exceed the standard deduction threshold. Limiting these deductions will make it more difficult to meet the newly increased thresholds.*

Trends and strategies to watch for charitable giving

As a significant tax overhaul, the Tax Cuts and Jobs Act could influence the way taxpayers give to charity. With such significant changes, it is a good time to reflect on your charitable giving and tax planning strategy. Below we offer a few of the trends you may see in 2018 and strategies to get the most out of your charitable giving.

1. Bunching charitable contributions to meet increased hurdle for itemization

With the standard deduction doubled and many popular deductions eliminated, you may find that it doesn't make sense to itemize your tax deductions in 2018 and beyond. But how can you still receive a tax benefit for charitable giving?

One strategy to consider is called "bunching." To take advantage of this strategy, you contribute multiple years' worth of your charitable giving in one year to surpass the itemization threshold. In off-years, you could take the standard deduction.

Consider this example. John, who files as single, donates $10,000 each year to his alma mater. In the past, his $10,000 donation put him easily over the threshold to itemize, and he has deducted the amount from his income as a charitable tax deduction.

Starting in 2018, his charitable donation alone will no longer surpass the standard deduction threshold, which is now set at $12,000 for single filers. However, if he "bunches" two years of donations into one year, he will be able to itemize every other year and receive the full tax benefit of his charitable giving.

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
	Pre-Tax Reform Strategy					
Donation	$10,000	$10,000	$10,000	$10,000	$10,000	$10,000
Deduction	Itemize	Itemize	Itemize	Itemize	Itemize	Itemize
	Post-Tax Reform Strategy					
Donation	$20,000	$0	$20,000	$0	$20,000	$0
Deduction	Itemize	Standard	Itemize	Standard	Itemize	Standard

2. Taking advantage of increased AGI limit in high-income year

While you may find that "bunching" is a tax-savvy strategy for your current situation, adjusting the cadence of your giving can also be useful if you find yourself experiencing a particularly high-income year.

In years when income is high or you receive a windfall, charitable giving can help you manage the associated tax burden. The new tax law increases the AGI limit on cash charitable contributions from 50% to 60% and repeals the Pease limitation. These changes mean you can receive a greater deduction for greater giving. And accelerating your giving can help you save even more on taxes.

For example, Mary typically donates $10,000 to charity each year. The chart below shows her tax savings if she donates 10 years' worth of her contributions in her high-income year. Strategies #2 and #3 show her tax savings if she continues donating $10,000 annually, whether she itemizes her deductions moving forward or doesn't, respectively. Donating the lump sum could save her thousands of dollars in taxes, while providing the same level of support to her favorite charities.

		Giving Strategies		
		1	2	3
	Income Tax Rate	Accelerated	Annual with itemization	Annual without itemization
Year 1 (high-income year)	37%	$100,000	$10,000	$10,000
Year 2	24%	-	$10,000	$10,000
Year 3	24%	-	$10,000	$10,000
Year 4	24%	-	$10,000	$10,000
Year 5	24%	-	$10,000	$10,000
Year 6	24%	-	$10,000	$10,000
Year 7	24%	-	$10,000	$10,000
Year 8	24%	-	$10,000	$10,000
Year 9	24%	-	$10,000	$10,000
Year 10	24%	-	$10,000	$10,000
Total Donation		**$100,000**	**$100,000**	**$100,000**
Tax Savings		**$37,000**	**$25,300**	**$0**

3. Growth in donating appreciated securities amid market gains

Donating appreciated securities to charity will reduce income tax liability and eliminate capital gains tax on the assets. Capital gains taxes are eliminated when you contribute long-term appreciated assets directly to a charity, like Fidelity Charitable, instead of selling the assets yourself and donating the after-tax proceeds. When you assume 20% for federal long-term capital gains taxes, plus a 3.8% Medicare surtax, this leads to a potential increase of 23.8% of both your tax deduction and your charitable contribution.

In addition, while the tax law increases the AGI limit on cash contributions, it maintains the rule that 30% of AGI can be contributed in securities. Maxing out the 30% limit in securities before contributing cash is a very tax-efficient method of charitable giving.

Outlined below is a hypothetical example showing the advantages of donating a long-term appreciated security as compared to selling the asset and donating the cash proceeds. In this scenario, the donors, Matt and Veronica:

- Are in the 37% federal income tax bracket.
- Have an asset that has a FMV of $450,000 that includes unrealized gains of $150,000, which could be subject to a 20% capital gains and 3.8% Medicare surtax.

Selling Matt and Veronica's Securities vs. Donating

Value of securities[1]

$450,000

Original cost of securities: $300,000[2]
Federal long-term capital gains rate: 23.8%[3]

Sell the securities Donate the proceeds	vs.	Donate the securities
$35,700	Long-term capital gains tax paid	$0
$414,300	Charitable contribution	$450,000

Reduced their tax obligation by: **$13,209[4]**

Additional amount dedicated to charity: **$35,700**

Bonus tip: Strong M&A markets driving giving

Current market conditions and the newly reduced corporate tax rate could create an active mergers and acquisitions environment in 2018, which can expose investors to capital gains even if they are not selling stock. Tax-smart investors will watch for potential M&A activity in their portfolios and act before they accrue forced capital gains. Charitably inclined investors may choose to donate their appreciated securities as a smart solution for eliminating capital gains tax.

[1] Amount of the proposed donation is the fair market value of the appreciated securities held more than one year that you are considering to donate.

[2] Total Cost Basis of Shares is generally the amount of money you have invested in the shares of a particular fund or individual security. It represents the basic dollar amount that, when compared to the price at which you sell your shares, tells you how much of a capital gain or loss you have realized.

[3] This assumes all realized gains are subject to the maximum federal long-term capital gain tax rate of 20% and the Medicare surtax of 3.8%. This does not take into account state or local taxes, if any.

[4] Assumes no unrelated business taxable income (UBIT), and top ordinary income tax rate of 37% for valuing charitable deduction. $13,209 reduced tax obligation calculated by comparing the tax benefit of a deduction of $450,000 at 37% versus a deduction of $414,300 at 37%. It does not account for any state and local taxes or alternative minimum tax.

How a donor-advised fund can help maximize giving

A donor-advised fund is an ideal vehicle for tax-savvy charitable giving. By making a charitable contribution to a donor-advised fund such as a Fidelity Charitable Giving Account®, you become eligible to take an immediate tax deduction for the amount contributed. Your contributions are invested so they have the potential to grow tax-free and generate more money for the charities you care about. You can then support your favorite charities in a time frame that works for you.

All of the tax planning strategies discussed in this paper can be supported and enhanced by using a donor-advised fund. Donor-advised funds make it easy to contribute appreciated securities directly to charity. And if you choose to accelerate your giving in a high-income year or via the "bunching" strategy, a donor-advised fund can hold your cache of charitable dollars—allowing you to maintain support of your favorite charities for years to come. A donor-advised fund can enable smart, tax-efficient charitable giving, and they are quickly becoming a go-to solution for Americans to manage their charitable giving.

FIDELITY Charitable℠

Make more of a difference