



Intermediate Taxation for Gift Planners



Date: November 16, 2017

Time: 1:00 – 2:30 Eastern Time

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Agenda

- Provisions related to the charitable deduction
- Provisions related to income tax
- Provisions related to transfer tax
- Provisions in House and Senate tax bills



Charitable Deduction: Pease Limitation

- Reduces itemized deductions by 3% of amount by which donor's AGI exceeds threshold amount
- Cannot reduce deductions more than 80%
- Threshold in 2017: \$313,800 for MFJ, \$261,500 for SF
- Most taxpayers subject to Pease limitation itemize enough non-charitable deductions that their charitable deductions are fully deductible



Charitable Deduction: Pease Limitation

Example: Harold and Jane

- \$400,000 AGI
- Deductions: \$20,000 charitable gifts, \$25,000 state and local taxes, \$10,000 mortgage interest
- Pease reduction: $3\% \times \$86,200 = \$2,586$
- Giving \$20,000 still saves $33\% \times \$20,000 = \$6,667$
- Pease limitation has no effect on tax savings from H and J gifts



Charitable Deduction: Deduction Carryforward Rules

Deductibility by Type of Organization

Type of Organization	Examples	Type of Property	Deductibility
Public charities and private operating foundations. Sometimes called "50% Charities."	Educational institutions, churches, tax-exempt hospitals, governmental units, publicly supported organizations such as the American Red Cross or a symphony orchestra, along with private operating foundations.	Cash and Ordinary Income Property	50% of AGI
		Long-term Capital Gain Property	30% of AGI
Private non-operating foundations. Sometimes called "30% Charities."	Strictly "grant making" foundations.	Cash and Ordinary Income Property	30% of AGI
		Long-term Capital Gain Property	20% of AGI



Charitable Deduction: Deduction Carryforward Rules

Example 1: Ben and Sarah

- AGI = \$125,000
- Charitable contributions = \$75,000 cash
- Can use \$62,500 of deduction in year of gift ($\$125,000 \times 50\%$)
- Carry forward \$12,500 of deduction, will be subject to 50% limit

Example 2: Ben and Sarah

- AGI = \$125,000
- Charitable contributions = \$75,000 in appreciated securities
- Can use \$37,500 of deduction in year of gift ($\$125,000 \times 30\%$)
- Carry forward \$37,500 of deduction, will be subject to 30% limit



Charitable Deduction: Deduction Carryforward Rules

Order of Priority of Deductions from IRS publication 526:

1. Current contributions of cash and non-appreciated property to “50% charities.”
2. Carryover contributions of cash and non-appreciated property to “50% charities.”
3. Current contributions of long-term capital gain property to “50% charities.”
4. Carryover contributions of long-term capital gain property to “50% charities.”
5. Current contributions of cash and non-appreciated property to “30% charities” as well as contributions of such property “for the use of” “50% charities.”
6. Carryover contributions of cash and non-appreciated property to “30% charities” as well as contributions of such property “for the use of” “50% charities.”
7. Current contributions of long-term capital gain property to “30% charities” as well as contributions of such property “for the use of” “50% charities.”
8. Carryover contributions of long-term capital gain property to “30% charities” as well as contributions of such property “for the use of” “50% charities.”



Charitable Deduction: 50% Special Election

Deduction limitations:

- Gifts of cash to public charity: 50% of AGI
- Gifts of long term gain property to public charity: 30% of AGI
- 30% limit applied within 50% limit
- Can carry forward deduction up to 5 additional years
- Donor can elect to treat ALL current and carried forward long term gain property gifts as 50% gifts



Charitable Deduction: 50% Special Election

May make sense for donor to make 50% election when:

- Cost basis of gift property is high relative to its FMV
- Can't use all of deduction if limited to 30% of AGI
- Expects to be in higher income tax bracket in year of gift than in subsequent years



Charitable Deduction: 50% Special Election

Example: Sam

- \$100,000 AGI
- Gives \$250,000 stock he inherited with \$240,000 basis
- If 30% limit: deduct $\$30,000/\text{yr} \times 6 \text{ yrs} = \$180,000$
- If 50% limit: deduct $(\$50,000/\text{yr} \times 4\text{yrs}) + \$40,000 = \$240,000$



Charitable Deduction: IRS Discount Rate Election

Summary of Benefits for 5.4% Charitable Gift Annuity
Date of Gift: 6/15/2017 Cash Donated: \$10,000.00
Annuitant age 72

CHOICE OF BENEFITS:	April 2017 IRS Discount Rate 2.6%	May 2017 IRS Discount Rate 2.4%	June 2017 IRS Discount Rate 2.4%
Charitable Deduction:	\$4,326	\$4,240	\$4,240
Annual Payout	\$540	\$540	\$540
Tax-free Portion (for 14.5 yrs)	\$391	\$397	\$397
Ordinary Income Portion*	\$149	\$143	\$143

*Once all tax-free portions have been distributed, the entire annuity will become ordinary income.



Charitable Deduction: IRS Discount Rate Election

Requirements (see Reg. Sec. 301.9100-8(a)(1)):

- A statement that an election under section 7520(a) is being made
- The transferor's name and taxpayer identification number as they appear on the return
- A description of the interest being valued
- The recipients, beneficiaries, or donees of the transferred interest
- The date of the transfer
- The Applicable Federal Midterm rate that is used to value the transferred interest and the month to which the rate pertains



Charitable Deduction: IRS Discount Rate Election

Example of IRS Discount Rate Election Statement:

Applicable Mid-Term Rate Election Charitable Gift Annuity

Donor Name: John Smith
Taxpayer ID: 999-88-7777

According to Reg. Sec. 301.9100-8(a)(1), I, John Smith, am making an election as provided under Section 7520(a) of the Internal Revenue Code.

The interest being valued is a charitable gift annuity agreement with THE CHARITY made on June 15, 2017. The payout rate of the gift is 5.4%, payable for the lifetime benefit of an individual, age 72.

To value the transferred interest, I elect to use the 2.6% rate under Section 7520 for April, 2017 (120% of the Applicable Mid-Term Federal Interest Rate compounded annually and rounded to the nearest two-tenths of one percent).



Charitable Deduction: Form 8283

Form 8283:

- Must be filed by donor when total non-cash donations for year exceed \$500 (deductible amount without respect to % AGI limits)
- Complete Section A for each item or group of similar items (e.g. coin collection) that produces deduction \leq \$5,000 and for publicly-traded securities of any value
- Complete Section B for each item or group of items that yields deduction $>$ \$5,000 (other than publicly-traded securities)
- Attach 8283 to 1040. Attach multiple 8283s, as needed
- Make donor aware when Form 8283 must be filed!



Charitable Deduction: Form 8283

Section A: deduction $<$ or $=$ \$5,000

- Part I: describe items / groups of items
 - Donee organization, date of contribution, FMV
 - If securities, company name and # of shares; if $>$ \$500, also date acquired, how acquired, cost basis
- Part II: complete if gift of partial interest or restricted use
 - Most planned gifts are gifts of a partial interest
 - Enter amount or deduction being claimed
 - If tangible property, identify where it is
 - Indicate if use is restricted



Charitable Deduction: Form 8283

Section B: deduction > \$5,000

- Part I: describe items / groups of items
 - Date of gift, deduction claimed
 - Appraised FMV, date acquired, how acquired, cost basis
- Part II: identify items in Part 1 valued at \$500 or less
 - Donor attests to value of items in Part 1 with signature



Charitable Deduction: Form 8283

Section B: deduction > \$5,000

- Part III: filled in by qualified appraiser
 - Attests to value of items in Part 1
 - Includes items in Part 1 with deduction > \$5,000, > \$10,000 if closely-held stock
 - Require written signed appraisal: art worth > \$20,000, clothing / household items not in good used condition, easement on buildings in historic districts, deduction > \$500,000
- Part IV: Authorized officer of charity signs acknowledging receipt of property described in Part 1, then returns form to donor



Income Tax Provisions: Medicare Surtax

- The first part is an extra .9% tax on wages and self-employment income above the thresholds.
- The second part is a 3.8% surtax called the Net Investment Income Tax or NIIT. This surtax is imposed on the lesser of:
 - net investment income or
 - the amount by which a taxpayer's modified MAGI exceeds the applicable threshold (\$250K for MFJ).
- The 3.8% surtax cannot be reduced by charitable deductions and applies to life income gift payments



Income Tax Provisions: Medicare Surtax

Example: Mark and Helen

- Wage income = \$100,000 (puts them in 25% bracket)
- Capital gain income (stock sale) = \$200,000 (taxed at 15%)
- Excess MAGI = \$50,000 ($\$300,000 - \$250,000$); NIIT = \$200,000
- Pay NIIT on \$50,000, the lesser of excess MAGI and NIIT.

Surtax effectively raises their marginal capital gains tax rate from 15% to 18.8% on last \$50,000 of capital gain, which makes giving appreciated property to charity more attractive.



Income Tax Provisions: Alternative Minimum Tax

- Alternative Minimum Tax (AMT) is computed in parallel with standard federal income tax
- Taxpayer pays whichever tax is greater
- Most deductions disallowed under AMT
- AMT meant to assure that taxpayers with a lot of deductions pay at least a minimum amount of tax
- About 5.2 million taxpayers expected to pay AMT in 2017



Income Tax Provisions: Alternative Minimum Tax

- Two rates
 - 26% on income below applicable threshold (\$187,800 for MFJ)
 - 28% on income above applicable threshold
- Exemption (\$84,500 for MFJ)
- Exemption phase-out above applicable threshold (\$160,900 for MFJ)
- Effective AMT rate during most of phase-out is 35% (\$187,800 - \$525,800 for MFJ)
- Deduction allowed for charitable contributions (and mortgage interest)
- For donor with income in AMT phase-out range, tax savings from gifts could be higher under AMT; otherwise likely to be lower



Income Tax Provisions: The 8 Tiers of Trust Taxation

Ordinary Income		Capital Gain				Tax-free Income	Return of Principal
Interest, rents, royalties, and ordinary dividends	Qualified dividends	Short-term capital gain	Long-term capital gain from sale of collectibles	Long-term capital gain from sale of assets involving depreciation recapture	Long-term capital gain from sale of other investments	Interest earned on tax-exempt securities	Distributions of trust corpus
Taxed up to 39.6%	Taxed at 15% or 20%	Taxed up to 39.6%	Taxed from 10% to 28%	Taxed from 10% to 25%	Taxed from 0% to 20%	Not taxed	Not taxed



Income Tax Provisions: The 8 Tiers of Trust Taxation

IRS Form 5227 for 2017

Form 5227 (2017) Page **7**
 Full name of trust Employer identification number

NOT Open To Public Inspection

Schedule A—Distributions, Assets, and Donor Information

Part I-A Accumulation Schedule (Section 664 trust only) (see the instructions)

Accumulations		(a) Ordinary income		(b) Capital gain (loss)		(c) Nontaxable income	
		Excluded Income	Accumulated NII	Excluded Income	Accumulated NII	Excluded Income	Accumulated NII
Net Investment Income (NII) Classification							
1	Total distributable income. Enter the amount from line 29						
2a	Total distributions for 2017:						
b	2017 distributions from income						
3	Undistributed income at end of tax year. Subtract line 2b from line 1						

Part I-B Simplified Net Investment Income Calculation

	(a) Accumulated NII	(b) Current Year NII	(c) Distributions	(d) Ending NII
4				

Part II-A Current Distributions Schedule (Section 664 trust only) (see the instructions)

	(a) Name of recipient		(b) Identifying number		(c) Percentage of total unitrust amount payable (if applicable)		
4a					%		
b					%		
c					%		
	(d) Ordinary Income	Capital gains		(g) Nontaxable Income	(h) Corpus	(i) Total (add cols. (d) through (h))	(j) Net investment income
		(e) Short-term	(f) Long-term				
4a							
b							
c							
Total							

If Part II-A, Total, column (i) does not agree with line 61b of Form 5227 for a CRAT or line 68 of Form 5227 for a CRUT, check here and attach an explanation.



Transfer Tax Provisions: Gift Tax

- Unlimited charitable deduction (but gift tax return may still need to be filed)
- Unlimited marital deduction (if spouse U.S. citizen)
- Annual exclusion per donor: \$14,000*
- Each spouse can give \$14,000 to any person each year, so parents of a family of three children can transfer \$84,000 ($2 \times 3 \times \$14,000$) to the next generation each year free of tax

*** Annual exclusion goes up to \$15,000 in 2018**



Transfer Tax Provisions: Gift Tax

Example: Mabel gives \$50,000 to each of her 5 nieces and nephews in 2017. She has given \$100,000 to each of her 3 siblings in previous years. The resulting gift tax would be computed as follows:

Prior years' potentially taxable transfers:	\$300,000
Current year's potentially taxable transfers:	+ <u>\$250,000</u>
Lifetime cumulative potentially taxable transfers:	\$550,000
Tentative gift tax on first \$500,000:	\$155,800
Tentative gift tax on next \$50,000:	+ <u>\$18,500</u>
Total tentative gift tax:	\$174,300
Lifetime gift tax credit :	\$2,141,800
<i>(equivalent to transfers of \$5,490,000)</i>	
Net gift tax due for 2017:	\$0



Transfer Tax Provisions: Generation Skipping Transfer Tax

- Assessed on transfers to “skip” person made during life or at death
- Devised to assure that each generation of a family pays transfer tax on substantial transfers
- Lifetime exemption of \$5,490,000 in 2017 (\$5,600,000 in 2018); no portability
- A skip person is:
 - Lineal descendant 2 or more generations below transferor
 - Non-lineal descendant 37.5+ years younger than transferor
- GSTT assessed at highest gift / estate tax rate (currently 40%)



Transfer Tax Provisions: Generation Skipping Transfer Tax

- Direct skip (e.g. bequest in will): transferor (donor or donor's estate) pays tax
- Taxable distribution (e.g. CRT payment): recipient pays tax
- Taxable termination (e.g. CLT distribution to heirs): trust pays tax
 - CLAT: fraction of distribution subject to GST (inclusion ratio) determined at end of trust; CAN'T allocate exemption exactly
 - CLUT: fraction of distribution subject to GST (inclusion ratio) determined when trust funded; CAN allocate exemption exactly



Tax Reform: Where Are We in the Process?

- House Bill
 - Out of committee and being debate on floor
 - Amendments still being considered
 - Expect vote before Thanksgiving
- Senate Bill
 - Chairman's mark reported out of committee
 - Amendments still being considered by Finance Committee
 - A little behind House in the process; vote may be after Thanksgiving
- Goal is to send tax bill to President to sign before Christmas



Tax Reform: Income Tax Rates

House Bill

- Reduces current 7 brackets to 4; rate lower at most income levels
- Top rate still 39.6%, but starts at \$1 million vs. \$480,000 for MFJ
- Effective rate of 45.6% while 12% bracket phased out (\$1.2 million threshold for MFJ, otherwise \$1 million threshold); takes \$1.1 million excess to fully phase out
- MFJ with \$260,000 - \$425,000 taxable income go from 33% to 35%
- 30% of pass-through income taxable can count as business income taxable at 25%
- Eliminates AMT



Tax Reform: Income Tax Rates

Senate Bill

- Maintains 7 brackets; rate lower at most income levels
- Highest bracket is 38.5%, which starts at \$1 million vs. \$480,000 for 39.6% MFJ
- 17.4% deduction for non-wage pass-through income taxable
- Eliminates AMT



Tax Reform: Income Tax Rates

Effect on charitable giving

- Donors will generally pay less tax on last dollar of income, so donors who itemize will save less taxes than now
- Modestly reduced tax incentive to give: modest negative effect, if any



Tax Reform: Itemized Deductions

- Both Bills eliminate most itemized deductions
- No deduction for state and local taxes, except House Bill allows up to \$10,000 deduction for property taxes
- Mortgage interest deduction preserved: House Bill limits to interest on \$500,000 loan, \$1 million limit in Senate Bill (which is current limit)

The good news in both bills:

- Charitable deduction preserved without a cap
- 50% AGI limit on deductions for cash gifts increased to 60%
- Pease limitation repealed



Tax Reform: Standard Deduction

Taxpayers can take standard deduction when total itemized deductions are less than standard deduction.

- House Bill and Senate Bill would roughly double standard deduction
- Both bills increase SD to \$24,000 for MFJ, \$12,000 for SF
- Under current law, SD in 2018 will be \$13,000 for MFJ, \$6,500 for SF



Tax Reform: Standard Deduction

Effect on charitable giving

- 69% of taxpayers expected to take SD in 2017
- 5% of taxpayers estimated to take SD if increased as proposed
- Donors who take SD (don't itemize) will get **NO** tax benefit from charitable deduction
- Likely to have significant negative impact on giving: IU Lilly Family School of Philanthropy Study predicts 1.7% - 4.6% decrease.



Tax Reform: Standard Deduction

CGP pushing for Universal Charitable Deduction

- Above-the-line deduction that would benefit all donors
- H.R. 3988 introduced, limits deduction to 1/3 standard deduction
- Amendment #9 to Senate Bill, 60% MAGI limit, Pease-like reductions
- Same IU Study estimates up to \$4.7 billion increase in giving in context of changes to SD, itemized deductions, and income tax rates



Tax Reform: Transfer Taxes

House Bill

- Double exemption from gift, estate, and GST tax to \$11.2 million (\$22.4 million per couple) in 2018
- Eliminate estate and GST taxes starting in 2024
- Reduce top gift tax rate from 40% to 35% in 2024

Senate Bill

- Like House Bill, double exemption from gift, estate, and GST tax to \$11.2 million (\$22.4 million per couple) in 2018
- Does not eliminate transfer taxes in future
- Does not change transfer tax rates in future



Tax Reform: Transfer Taxes

Effect of changes on charitable giving

- 99.8% of estates won't pay any federal estate tax (FET) in 2017
- Even tinier slice wouldn't pay FET in 2018 and after, but these are the largest estates which can make the largest gifts
- If FET eliminated, no incentive to give to avoid FET
- Fewer CLTs
- Maybe fewer bequests from large estates, too, but maybe just as many since no tax to reduce estate size



Summary

- Charitable deduction appears here to stay
- Context for charitable deduction could change dramatically
- Unless universal charitable deduction makes it into final bill – a long shot – changes will reduce tax benefits of giving
- Between now and end of 2017 is an opportunity to receive known tax benefits, and likely greater ones
- **Donors give because they believe in your mission; tax benefits are nice, but usually not essential. Focus on mission and other non-tax benefits and donors will continue to give and generously.**



Questions and Answers





Still Have a Question?

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