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Satisfying Charitable Wishes


"It's not how much we give but how much love we put into giving."
~ Mother Teresa

Introduction

This month we're going to review charitable giving, including the process and the tools. We'll start by reviewing a decision process and then describe a few commonly discussed vehicles.

For many of us, giving is little more than a year-end chore. As the holidays and the year-end approach, we think about the importance of giving back and then we start writing checks or entering credit card numbers on charities' websites. Simply writing a check may fulfill an obligation, but it doesn't usually provide much satisfaction. It may be better to start earlier and make sure that the charities we give money to do indeed share our most important values.

There are over 1 million public charities in the U.S., so the task of deciding who is most deserving can be daunting. However, most of our clients know what's really important to them because they have well-developed values they would like to reinforce and spread. Those provide an excellent platform to start a giving process. Whether its education, health, the arts, or another from the myriad of other worthy causes, there's at least one that speaks to each of us.

A Process for Giving

How do we find that cause and organization, and how do we decide on the most appropriate method for giving? Here are some questions to help you get started:

1. What kind of organization do you want to support?

Whether you care about the arts, education or the environment, you'll face some similar options. Do you want to support a local group or a national/international one? A large and established group or a new and struggling one? Each alternative presents different psychological rewards. A large, international group may speak to your need to fuel global solutions, while a small local group may offer the sense of making a visible, tangible difference. You can use the web to do some of your research. Two popular websites that may be helpful are www.charitynavigator.org and www.guidestar.org.

2. What type of donor do you want to be?

Do you prefer to be hands-off, giving money to worthy organizations that are doing good work? Or do you want to be an active donor who takes a board position and works closely with the group's executives? Both approaches can be effective. Melinda and Bill Gates epitomize the active donor, spending tremendous amounts of time and money through their own foundation to fulfill their vision for improving the world. Warren Buffett, on the other hand, is a good example of a hands-off donor. He saw what the Gates were doing, liked it, and opted to give large sums to the Gates Foundation to use as it wished.

3. If you want to be active, how active?

Many nonprofits have been around for a long time, perhaps longer than you have been. They are often established organizations with their own internal policies and politics. Most organizations can be improved and nonprofits are certainly no exception, but be mindful of the fact that if they have survived for a long time, they're probably doing many things right. The role of a board member is very different from that of a CEO or manager: Good board members need to build consensus, provide oversight, and give strategic advice while avoiding the pitfalls of micromanagement.

4. How would you like your money used?

Major donors can often specify the use of their gift to support a particular program within a nonprofit, or construct a new building, or publicize the nonprofit's position on an issue, etc. Keep in mind that for most nonprofits, the most valuable gift is one that covers general operational costs. It's often not the most glamorous use, but it allows them to keep their doors open and perform their mission. One fruitful option is to use your gift as a challenge grant, inspiring others to give by promising to match their donations.

5. What does the charity expect from working with you?

Being on a board requires you to give generously of your time and loyalty. Beyond that, the charity will most likely have specific expectations of you. For example, if you are well-connected in the community, they may expect you to fundraise. If you have a legal background, they may expect you to review contracts or connect them with *pro bono* expertise.

6. What do you expect from working with the charity?

Do you want your name on a building or project, or are you more comfortable being anonymous? Who would you like to work with inside the charity? From years of acting on behalf of our clients, we've learned that negotiating with charities can be tedious and time-consuming. But as with any relationship, communication is the key to satisfying your charitable goals. Avoid surprises on both sides by being clear about your intentions and obligations before donating any of your time or money. Your interest and maybe even your passion will be obvious to the charity, so make sure that it is reciprocated. Don't move ahead if you feel you are being taken for granted. Philanthropy should be a rewarding experience – both for the charity and for you.

The Tools for Giving

Some charitable giving tools are designed for ease-of-use, some are designed to maximize the incentives provided in the tax law, and some are designed to be as flexible as possible.

We'll start with the most common tools and work up to the more complex. We'll discuss when each makes sense and why you might choose one over the other. To aid in your understanding, we'll also include a hypothetical example: Let's assume that you have low-basis stock that is now worth $1 million that you would like to donate. The total income on your tax return is $500,000 per year. Note that it is generally better to give appreciated property, such as stock, instead of cash.

Direct Giving to a Public Charity

These include large and small nonprofit organizations, everything from universities, food banks and arts groups to organizations like United Way that spread one donation among many different causes. In our hypothetical example, you would be allowed to deduct up to 30 percent of your income or $150,000 each year for stock contributions to public charities. If you give more than that, you create a carryforward that must be used within five years using the 30% limitation on each future years' income.

Note that there is a rule that allows you to make direct charitable contributions of up to $100,000 per year from an IRA without affecting your tax calculation.

Donor Advised Fund (DAF)

These funds are often housed within a community foundation such as the San Francisco Foundation, although some investment firms like Schwab and TD Ameritrade also offer donor advised funds through an affiliated public charity. You would typically make a large donation to the DAF at one time, and then direct distributions over the years to your favorite causes. Establishing a DAF can make sense if you have a large sum of taxable income in one year and aren't sure which charities you would like to support. Since the organizations that administer DAF's are public charities, they have the same rules about deductible contributions as in the example above. Typically, the public charity handles all tax filings.

Given the changes in last year's tax bill, DAFs could make more sense than they have in the past. The reason is that one way to minimize taxes in multi-year planning is by "bunching" deductions into certain years. We'd be happy to discuss this strategy with you in more detail.

Charitable Remainder Trust (CRT)

Most trusts are formed to provide for individual people. A CRT, however, is a trust you would form that eventually pays a charity and therefore pays no taxes. Until the final distribution is made, the CRT would typically pay you a quarterly distribution of either a fixed dollar amount or a fixed percentage of the trust's value.

The tax-free nature of the trust offers advantages: You can contribute property with a low tax-basis, then the CRT can sell it without paying capital gains taxes and its distributions to you would be computed on the full pre-tax value of the property. You would pay taxes, using special rules, on the distributions as you receive them.

The IRS publishes tables regulating the size of distributions you can receive from a CRT. In our example, you might use your $1 million to establish a ten-year trust that pays you $97,000 each year. You would receive a deduction of about $100,000 in the year that you establish the trust, and you would pay income taxes on a portion of each quarterly distribution you'd receive. Assuming a seven percent growth rate in the trust, the remainder of $584,000 would go to your charitable beneficiary at the end of the ten-year term.

Charitable Lead Trust (CLT)

This is the reverse of a CRT: a CLT pays periodic distributions to charity, and the final distribution or remainder goes to one or more individuals whom you designate. A CLT may make sense if you know that you'd like to donate a set amount to charity each year. In our example, a ten-year CLT might pay out $50,000 a year to your favorite charity. Again assuming a seven percent growth rate in the trust, the remainder of $1.25 million would be paid out to the non-charity beneficiaries of your choice after 10 years. Given the structure of a CLT, it can be an effective way of both fulfilling charity wishes and tax-efficiently providing gifts to family members.

Private Foundation

Creating a foundation can give you almost complete control over investments and charitable distributions. Private foundations are independent entities, subject to complex tax and reporting rules. We typically recommend that private foundations be funded at a level of at least $10 million in order to justify the annual tax and reporting paperwork.

Thanks

We hope this has piqued your interest in applying a process to your philanthropy (if you aren't doing that already). Please carefully consider any planning ideas we present and be sure to discuss them with us and your other advisors, especially tax professionals, before taking action.

As always, we look forward to hearing from you so please don't hesitate to contact us.

Thank you for your trust in Vista,

Your Vista Wealth Management Team

of reviewing/evaluating/revising our previous recommendations and/or services. Please also advise us if you have not been receiving monthly statements from the account custodian.