

# Charitable Deduction





## What is the charitable deduction?

The charitable deduction allows you to deduct the value of property you give to charity from your estate and may reduce any federal gift and estate tax that may be owed. Charitable gifting allows you to satisfy your personal philanthropic desires and fulfill your estate planning objectives.

You may wish to give to the charitable community out of devotion, moral obligation, altruism, generosity, or a sense of responsibility. Or you may want to give because you believe you will do a better job of distributing your wealth than Uncle Sam. Whatever your motivation, charitable giving should be gratifying.

Gifts to charity can also fulfill your estate planning objectives. There are no limits on the amount that you can pass to charity. It is possible to transfer your entire estate to charity, tax free. Gifts to charity allow you to:

- Distribute your property tax free
- Potentially put the amount subject to estate taxes into a lower tax bracket

**Caution:** *However, remember that property you give to charity is property that does not go to your heirs. Don't let your attempt to save taxes have the unintended effect of depriving your heirs.*

**Tip:** *Charitable gifts are also deductible for income tax purposes for taxpayers you itemize. However, there is a limit imposed on the amount that can be deducted, and other adjustments may be required.*



## How does a gift or bequest of property qualify for the charitable deduction?

Certain conditions and requirements must be met to qualify for this deduction:

- You must make the transfer, either during life or at death by will, rather than your executor or heirs

- The property must be transferred to a qualified charity for a charitable purpose. A qualified charity includes:
  1. The United States, any state, the District of Columbia, and any local government
  2. Certain religious, scientific, or charitable organizations
  3. Certain veterans organizations
  4. Certain fraternal organizations
  5. An employee stock ownership plan if the transfer is a qualified gratuitous transfer or qualified employer securities

**Caution:** Gifts or bequests to individuals, no matter how needy or worthy the individuals are, cannot qualify for the charitable deduction.

**Tip:** The IRS publishes a list of charitable organizations (the Cumulative List) to which gifts or bequests will qualify for this deduction. The IRS does not define what a qualifying charitable purpose is. However, it has issued Letter Rulings that discuss what has been allowed or disallowed, and it has privately ruled that charitable purpose means the same for gift tax and estate tax purposes as it does for income tax purposes. Generally, a charitable purpose means a public purpose, as opposed to a private purpose.



- Depending on the year in which you die, the gift or bequest must be included in your estate for estate tax purposes. The amount of the deduction is the value of the property transferred, but the amount cannot exceed the value of the property that is required to be included in your estate.

**Tip:** A charitable deduction is allowed for nonresidential noncitizens, but only certain types of charities qualify.

- Generally, the gift must be a present interest. A present interest means that the donee (the person or organization you give to) has the unrestricted right to the immediate use, possession, or enjoyment of the property, or the



**Technical Note:** “Future interests” is a legal term and includes reversions, remainders, and any other delayed interest that postpones the commencement of the use, possession, or enjoyment of the property, or income from the property.


**Tip:** Gifts of future interests may qualify for the deduction if the gift is structured as a partial interest gift. Partial interest gifts (property rights given to both charitable and noncharitable interests, e.g., a trust paying income to a charity, with the remainder going to noncharitable beneficiaries) may qualify for the deduction if the donated property is transferred to an IRS-approved form of charitable trust, such as a charitable lead trust, charitable remainder trust, or pooled income fund.

## How do you use the charitable deduction?

For lifetime gifts, the charitable deduction is allowed for the year in which the gift is made for federal gift tax purposes. You don’t need to file an annual gift tax return if all gifts made for a given year fully qualify for the charitable deduction.

## Special rules regarding the charitable deduction

The amount of the charitable deduction is limited to the amount of the transfer actually made. Special rules apply if the transfer to charity first must bear a portion of any estate taxes because of the calculation difficulties that arise. Estate taxes are a function of the charitable deduction and the charitable deduction is a function of the estate taxes.



Donations

**Tip:** *The interrelated computation can be avoided by providing a specific bequest to the charity, instead of a gift from the residuary estate.*



## An example of the use of the charitable deduction

**Example(s):** *Ron is a small-business owner in the town where he was born and raised. He is a well-liked and respected member of the community. Ron feels he should give back to his community and donates money every year to support the town's zoo, hospital, library, children's center, church, and other local charities.*

**Example(s):** *During the years 2018 through 2022, Ron gave \$500,000 in total to different charities. Each year, Ron filed a gift tax return but paid no gift tax because the gift tax charitable deduction offsets his taxable gifts. Each year, Ron also filed an income tax return, reducing his taxable income by the amount of income tax charitable deduction allowed. Say Ron dies in 2023 and that his will provides for a charitable bequest in the amount of \$100,000, with the residuary estate passing to his only nephew, James. Ron's executor reduces Ron's taxable estate by \$100,000 (allowed by the estate tax charitable deduction), which then reduces the estate tax owed. Ron's executor pays the estate tax owed and then distributes the residuary estate to James.*



## Charitable IRA rollover gifts

Donors over the age of 70 1/2 can make tax-free charitable distributions of up to \$100,000 directly from their IRAs each year.

**Tip:** *This provision for charitable IRA rollover gifts has been made permanent.*

Donors who have reached age 70 1/2 can direct amounts (subject to the aforementioned \$100,000 limit) to charity in satisfaction of their minimum required distribution as long as the following requirements are met:

- The donor is age 70 1/2 at the time the gift is made.

- The charitable gift is made directly from an IRA to the charity.
- An individual can give a maximum of \$100,000 per year. A spouse can give an equal amount from his/her IRA.
- Individuals can make as many gifts in any amount to as many charities as desired as long as the total does not exceed \$100,000 per year.
- The gift cannot be made in exchange for a charitable gift annuity or to a charitable remainder trust.
- The gift cannot be made to a private foundation, donor-advised fund, or supporting organization (as described in IRC Section 509(a)(3)).



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Tax laws are subject to change annually. Please consult a qualified tax professional prior to implementing any of the strategies discussed.