TRUSTS & ESTATES

It's a Good Time to Make Charitable Gifts

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Giving to charity is always fulfilling, but now there are extra benefits for philanthropic donors courtesy of the Coronavirus Aid, Relief, and Economic Security (CARES) Act.

Expanded Tax Benefits

If you take the standard income-tax deduction, starting in the 2020 tax year you'll be able to deduct up to $300 in cash donations to charity "above the line" ($600 for married couples filing jointly). It will come off your gross income in calculating your adjusted gross income (AGI), a significant benefit.

If you itemize in the 2020 tax year, the limit on deductible cash contributions to public charities has been raised from 60% to 100% of AGI. Deductions not fully usable in the 2020 tax year can still be carried forward for five years, albeit at the old 60% limit. Corporate donors giving cash can now deduct up to 25% of taxable income, an increase from the 10% limit.

The rules for donating property are complicated, depending on the property type—it's often good to give highly appreciated stock, and avoid a potentially burdensome capital-gains tax bill later—and the structure of the charity (a donor-advised fund, for example, a pooled income fund, or a foundation).

Is a CLAT Right for You?

Let's say you've decided to give to charity, and you want to address other goals too. One popular choice, to benefit not only charity but a family member, perhaps— typically a child— or even yourself, is a charitable lead annuity trust, or CLAT, which can be set up to start paying out while you're alive.

They're called "charitable lead" because with a CLAT the charity gets paid first, and then your other beneficiaries. You can also do it the other way: pay your non-charitable beneficiaries first and then the charity with a charitable remainder trust. CLATs distribute an "annuity" because you establish a percentage of your donation's initial value to be paid to the charity in a stream of fixed yearly payments. You pick the annuity's term—often 10 or 20 years, though it can be for your lifetime or someone else's (usually your spouse's). Or you can elect to use a charitable lead unitrust, a CLUT, which pays a fixed percentage of the value of the trust as it changes each year. Once the term of a charitable lead trust has been reached, your children, your spouse—whoever you've named—is entitled to the remainder. CLATs are "trusts," special legal vehicles that hold assets and that are subject to special tax rules.

And with a CLAT, you are entitled to an income-tax deduction based on the amount passing to the charity; the amount and the timing of the deduction will depend on the terms of the trust, the amount funding the trust, the discount rate set by the government, and your individual tax circumstances.

CLATs Like Low Interest Rates

Typically, when a CLAT is established, the donor allocates a portion of his or her transfer-tax exemption to the portion of the trust not passing to the charity. If the donor survives the term of the CLAT, the property remaining at the termination of the trust passes transfer-tax-free to the remaindermen.

The Section 7520 Rate (from a section number in the IRS Tax Code) governs the CLAT's assumed discount rate and is set when the trust is created. If the return on the assets in the CLAT exceeds the Section 7520 Rate, the CLAT's non-charitable beneficiaries receive more than the government estimates that they would. Likewise, the additional amount avoids transfer taxes.

With today's low interest rates, the chances of "success" for a CLAT are about as high as they ever get. This May, the Section 7520 rate was 0.8%; by way of comparison, in May 1989 it was 11.6%. Further, while the federal exemption from estate and gift taxes is now at an extremely high level, it's scheduled to revert to a lower amount in 2026 unless Congress intervenes, and it often doesn't apply in states that levy their own transfer taxes.

Don't Do It Alone

Like all trusts, CLATs are complicated, and they require that grantors make a set of decisions up front. And if the trust is established to pay out benefits while you're alive, it's irrevocable, so you need to be careful in setting it up. You'll need the counsel of a trusts-and-estates professional and your financial advisor to help you determine whether a CLAT is a good option for you.

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