Lowe, Brockenbrough & Company

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Charitable Giving Today

As the second quarter of 2014 came to a close, domestic equity market indices were trading at or close to record highs. The strong market returns of the last several years have recently prompted conversations with a number of our clients about making annual charitable gifts or satisfying outstanding charitable pledges with their appreciated stock. With this in mind, we thought we would pass along some observations about charitable giving and the timeliness of making gifts, particularly at this point in the market cycle.

Why Give?

Numerous academic studies have been undertaken over the years to better understand the economic, sociological and psychological motivations behind philanthropic behavior. These motivations can be driven by self-interest or purely altruistic reasons, but in most cases the reasons for giving are some combination of both. In examining the most common reasons for giving, most studies cite several of the following:

1) Personal connection with a charity or cause
2) Personal relationship with the fundraiser
3) Desire to make a difference in the lives of others less fortunate
4) Desire to make a difference in the community
5) Family tradition
6) Religious reasons
7) Recognition for self or company
8) Take a stand on a particular issue or cause
9) Tax Benefits

Regardless of the reasons and motivations, most would acknowledge that the tangible and intrinsic benefits of philanthropy are significant, whether in local communities, at the national level or globally.

Why Now?

Charitable giving has recently been on the upswing. Our friend, Bobby Thalhimer of *The Community Foundation Serving Richmond and Central Virginia*, points out that according to Giving USA, charitable donations rose 4.4% in 2013, its best performance in a number of years. He believes this upward trend can be attributed to four primary factors:

1) The strong equity market of the past five years has produced outsized capital gains.
2) Tax rates have risen substantially.
3) Many wealthy donors provided for their families in 2012, prior to potential adverse changes in the estate tax law (which never occurred), allowing for more charitable intentions now.
4) Baby boomers are living longer, so that by the time they grow old their children are in many instances fully self-sufficient, again allowing them to pursue their charitable passions.

With the market having moved further ahead in 2014, all of these factors remain in place, likely prompting additional growth in charitable giving.

Avenues for Giving

While there are several reasons for the recent rise in philanthropy, one of the strongest motivations has been the change in tax law as a result of the American Taxpayer Relief Act of 2012 and the Affordable Care Act of 2013. Larry McKoy, Partner at Dixon Hughes Goodman in Richmond, commented that "having to write bigger checks for tax payments caught most taxpayers by surprise in 2013. Congress produced a 'perfect storm' of tax changes creating tax liabilities often 10-20% higher than in recent years. The new surtax on unearned income of 3.8% and the higher long-term capital gains tax rate of 20% have pushed the total effective federal tax rate for long-term capital gains to 23.8% (compared to 15% in 2012)." Combined with state tax, the effective tax rate on long-term capital gains is nearly 30% for high income taxpayers, making gifts of appreciated securities more tax efficient than gifts of cash.

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As mentioned at the outset of this piece, a number of our clients are using the strong appreciation in their equity portfolios to make charitable stock gifts and satisfy outstanding charitable pledges. By giving away appreciated securities, one can deduct the full market value of assets such as stocks and mutual funds held for more than one year. For the donor, there is no capital gains tax on the appreciation, and it can facilitate the re-balancing of investment portfolio allocations. The deduction for charitable donations of appreciated long-term securities is limited to 30% of Adjusted Gross Income, yet donations exceeding this limitation may be carried forward to future tax years. It is best to consult with a tax advisor regarding your specific tax situation.

In addition to satisfying existing charitable obligations with appreciated securities, donors also have available to them other strategies with which they can pursue charitable desires within their financial or estate plans, for all the reasons previously mentioned. These strategies may include setting up gift annuities, establishing charitable trusts or creating donor-advised funds. As with any trust and estate-related strategies, these issues require that the donor consult with their legal and financial advisors to determine the best strategy to achieve desired charitable and financial results.

Charitable Gift Annuity: A Charitable Gift Annuity is a contract between a donor and a charity, whereby the donor transfers cash or property to the charity in exchange for a partial tax deduction and a lifetime stream of annual income from the charity. When the donor dies, the charity keeps the gift. The amount of the income stream is determined by many factors, including the donor's age and the policy of the charity.

Charitable Remainder Trust (CRT): A CRT, which can be funded with appreciated assets or cash, provides a predetermined payment stream to the donor (or other beneficiary). In return, the donor receives an income tax deduction. The trust is irrevocable and must make payouts at least annually. The term of the trust can be for the life of the donor or for a specified time period. At the end of the term, the remaining assets are distributed to a designated charitable beneficiary. The CRT can be a useful vehicle for diversifying concentrated stock positions.

Charitable Lead Trust (CLT): A CLT is the inverse of a CRT. It provides a stream of payments to one or more charities during the lead period, which can stretch many years, after which the remaining assets are distributed to the donor's beneficiaries. It can be a good choice if the donor doesn't need lifetime income from a particular asset. A CLT can be useful in passing appreciated assets to heirs at a reduced valuation for gift and estate tax purposes. Like a CRT, a CLT is irrevocable and provides a tax deduction to the donor.

Donor-advised Fund: These accounts can be opened with a tax-deductible contribution of a variety of assets, including appreciated securities, real estate and cash. Once the fund is established, the donor serves as the advisor of the fund, selecting those public charities to receive grants that best fit the donor's charitable inclinations. In addition, the donor's children may serve as co-advisors, and grandchildren as successor advisors, thereby establishing or sustaining the donor's charitable legacy. Contributions to donor-advised funds can be made with relatively small amounts and avoid the legal costs of establishing a trust. Donor-advised funds are administered by various financial organizations and community foundations (including *The Community Foundation Serving Richmond and Central Virginia* mentioned above) that provide invaluable information on charitable organizations and philanthropic guidance to donors and their families.

In addition to the attractive tax benefits, philanthropy has deep tangible and intangible benefits for individuals, families, and communities. It can build a tremendous legacy for families and can inspire friends and others in the community to get involved. In turn, the organizations that receive donations are able to perpetuate and strengthen their community work, a vital part of any healthy community's fabric.

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