Charitable Planning and Gifting in the Biden Era

Warren H. Krueger
Foster Swift Trust & Estates Law News
January 30, 2021

AUTHORS/ CONTRIBUTORS
Warren H. Krueger, III

PRACTICE AREAS
Estate Planning
Tax Law
Trusts & Estates

With the election of Joe Biden, a number of changes to the U.S. tax laws may be on the horizon. If changes proposed by Biden are passed, estate and income tax planning for many taxpayers would be significantly impacted. Perhaps the most notable proposed change is a reduction of the federal estate tax and gift tax Exclusion Amounts.

As discussed in the above article, one proposal would see the federal estate tax Exclusion Amount reduced to $3.5 million, and the estate tax rate increased to 45%. Under those changes, the estate of an unmarried individual who died with a gross estate valued at $5 million dollars would be subject to a federal estate tax bill of $675,000 (($5M – $3.5M) x .45).

Biden's proposal would also increase the marginal tax rate for high net worth individuals, and increase the tax on capital gains for those with an income exceeding $1 million per year. In addition, Biden's proposal would limit the charitable deduction for charitable giving to 28% for those in a higher income tax bracket.

For those who may find themselves subject to estate taxes under the proposed changes, it is worth gaining a rudimentary understanding of tools available to reduce the estate tax burden. This article focuses on charitable giving – one of those tools.

Charitable giving has long been a staple of estate planning for "wealthy individuals" which, for purposes of this article, refers to individuals with taxable estates. There are many benefits to charitable giving. First, charitable giving may reduce the estate tax burden in two ways:

> (i) lifetime charitable giving can reduce the value of an individual's estate that will be subject to estate tax at death, and
> (ii) charitable giving as part of an estate plan may be a deduction to any estate tax owed at death since testamentary charitable bequests enjoy an unlimited charitable deduction.

Second, charitable giving provides financial support for charities or causes that are meaningful to the individual. Third, charitable giving may defer or eliminate capital gains tax on appreciated property, and reduce income tax liability.

As noted, wealthy individuals may face an increased income tax burden under Biden's proposed tax plan. In addition to reducing the value of an individual's estate, a properly planned charitable gift may reduce income or capital gains taxes while still providing the individual with some financial benefit from the gifted asset.

A commonly used instrument to achieve the dual goals of charitable giving and tax reduction planning is the charitable remainder trust ("CRT"). In essence, a CRT is a trust that is funded by an individual ("donor") during life.

The CRT makes distributions to a non-charitable beneficiary, which can include the donor, for up to 20 years.

After 20 years, any remaining property passes to one or more charities. The benefit of a CRT is that a donor who is charitably inclined may fund a CRT with assets that have increased in value and defer capital gains taxes. The CRT would provide an income stream to the donor for up to 20 years, and the assets will ultimately pass to the charity of the donor's choosing.

Determining the proper structure and terms of the CRT can be complicated. However, the tax benefit to an individual with a taxable estate, and who is charitably inclined, should not be overlooked.

Although there is no proposal to eliminate the tax benefits of utilizing a properly structured CRT, Biden's proposed plan would impose a 28% limit on charitable deductions for taxpayers making over $400,000 per year in income.

For example, a high-income earner can make a $100,000 charitable gift and write off $37,000 in income taxes (100,000 x .37 (the highest marginal tax rate)). But under Biden's plan, the same charitable gift would be limited to a $28,000 income tax write off (100,000 x .28 (the proposed limit for high-income earners)).

Admittedly, there is a long road between a proposed tax law and enactment of that law, particularly in the current political environment. However, there is no better time to understand the benefits of charitable giving and how it can be incorporated into a well-designed estate plan.