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Sunset of Tax Cuts & Jobs Act and Effect on Charitable Giving

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Background

- 2024 Tax Cuts & Jobs Act (“TCJA”); mostly effective in 2018.
- Congress mostly made effective until 2026.
- Many provisions expire 12/31/2025.

Expiring Provisions (of Interest)

- Estate / gift tax exemption decreases from $13.6 M in 2024 to $7 M (estimated).
- Income tax rate on HNW taxpayers increases from 37% to 39.6%.
- Standard deduction decreases by about half from $29,200 in 2024 to $15,000 (estimate) for married taxpayers (single is $14,600 to $7,500, estimate).
- Annual limit for cash donations to public charities goes from 60% to 50% of adjusted gross income ("AGI").

Expiring Provisions (continued)

- State and Local Tax ("SALT") deduction will no longer be limited. $10,000 cap expires at 12/31/2025.
- Mortgage interest deduction increases from $750,000 of debt to $1M. Home equity loans also allowed to $100,000.
- Miscellaneous itemized deductions are deductible again. Expenses such as legal fees and investment advisory fees will be deductible if they exceed 2% of AGI.

Expiring Provisions (continued)

- Personal exemptions will be returned in 2026 ($2,000 per taxpayer and dependent, as adjusted).
- Alternative Minimum Tax ("AMT") reverts to pre-TCJA levels and more HNW taxpayers could pay AMT.
- 20% Qualified Business Income ("QBI") Deduction expires 12/31/2025. This will raise taxes on passthrough business owners of S corporations, partnerships and LLCs.

Non-Expiring Provision

- The Corporate Tax Rate remains the same at 21% (pre-TCJA level was top rate of 35%).

2026 Changes
Estate / Gift Tax Exemption Decreases and Income Tax Rates Increase

- If donors have less money due to taxes, they have less to donate to charity.
- Examples of 2026 Tax increases:
  - Income tax rates increase from 37% to 39.6% at highest level.
  - AMT taxes could increase.
  - 20% QBI deduction sunsets.
  - 20% QBI deduction disappearing.
  - Estate / Gift Tax Exemption cut in half.

2026 Tax Decreases

- Standard deduction cut and more can itemize.
- SALT deduction cap disappears.
- Mortgage interest deduction improves.
- Miscellaneous itemized deductions are more likely.
- Personal exemptions return to pre-TCJA levels.

Effects on Charitable Giving – Estate Tax

- Reduction of Estate / gift tax exemption ($13.6 M to $7 M for single taxpayers and $27.2 M to $13.6 M for married taxpayers).
- Strategies to Consider:
  - Substantial gifts to family and charity before 1/1/2026.
  - $18,000 annual exclusion gifts.
  - Gifts above annual exclusion which eat into exemption.
  - Consider creation of charitable reminder trusts, pooled income funds, and charitable gift annuities (with benefits retained by family).
  - Consider donations of capital gain assets to reduce estate size, and avoid federal income tax on appreciation.

Example 1

HNW Donor and spouse have federal estate of $50 M. If they gift $25 M in 2025 to their family, the exemption in 2026 is $14 M, and the exemption in 2025 is $28 M, they have moved an additional $11 M out of their estate. Savings at 40% is $4.4 M.

Example 2 - Effect Using a Charitable Gift Annuity ("CGA") Pre-2026

Sam transfers $1.5 M consisting of stock ($500K basis) to Grove City College for a gift annuity. In exchange for the $1.5 M contribution, a CGA is issued to Sam paying him $105,000 a year (7%) for life. Sam's income tax deduction is $697,500. Sam defers his capital gain, receives a charitable income tax deduction of $697,500, subjection to limitation, and reduces his taxable estate by $697,500.

Other Strategies

- Bunching – Rather than gifting $5,000 per year for 3 years, gift $15,000 in one year.
  - More likely to be able to deduct in pre-2026 years.
  - May not be as prevalent after 2025.

Other Strategies (continued)

- Gifts to private foundations or donor advised funds (DAFs) now, and decide later on charitable recipients.
  - Can be used in combination with bunching.

Other Strategies (continued)

- Consider converting an IRA to a Roth using pre-2026 lower rates.
- Can try to offset income tax with a charitable gift.

Donation of Capital Gain Assets

- Give appreciated stock to charity to avoid capital gains tax and reduce federal estate before 2026. See Example 2.
- Deductions could be more valuable in 2026 and later years.
- Still good to do pre-2026. Crunch the numbers!

Downsides to Pre-2026 Charitable Giving

- With higher income tax rates, charitable deductions may be better in 2026.
- In 2026, the standard deduction decreases, itemized deductions may be deductible as a result, and more taxpayers may be able to deduct charitable contributions.

Effects on Charitable Giving – Income Tax

- With 2026 rise in marginal tax rates, it may be best to defer charitable gifts until 2026 or later years. But watch AMT!
- With 60% AGI limit going back to 50% in 2026, it may be better to accelerate gifts into 2025.

Bottom Line – Consult Your Tax Advisor!

This is complicated.

Example 3 – Effect Using a Charitable Remainder Unitrust Pre-2026

Sam transfers $1.5 M, consisting of stock ($500K basis), to a CRUT with the remainder going to Grove City College. In exchange for the $1.5 M contribution, a yearly annuity of 5% is paid to him, with a first year payment of $75,000. The annuity payment of 5% will go up or down based on the CRUT's value. Sam's income tax deduction is $910,700, subject to limitation, and reduces his federal taxable estate by $910,700.

Election Effects – Democrats Win

- Biden's Green Book changes are more likely. TCJA sunsets.
- Green Book changes could include:
  - Required early distribution of retirement accounts over $10 M.
  - 25% minimum tax on taxpayers with wealth exceeding $100 M.
  - Increase top marginal tax rates and reduce joint filer benefits for high-income earners.
  - Loss of stepped-up basis at death.
  - Others?

Election Effects – GOP Wins

- TCJA tax cuts may be extended.
- Federal estate / gift tax exemption remains high.
- Others? More tax cuts?

Bottom Line:

- This is complicated and charities need help!
- Change cuts ways that help / hurt charitable giving.
- Crunch the numbers!
- Consult a tax accountant / tax advisor.

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