Optimizing Charitable Contributions: Find the Most Effective Giving Strategy

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In navigating the landscape of charitable giving, individuals often find themselves contemplating the most efficient and impactful means of supporting causes that resonate with them. Determining the optimal way to donate is not just about the amount contributed but also about the effectiveness of the contribution. Factors such as administrative costs, transparency, and the direct impact on beneficiaries are crucial in deciding how best to channel one's philanthropic efforts. There's no universal strategy; understanding the most efficient giving method depends on one's personal financial plan and goals.

Direct Gifts

Donations of cash, checks, or other assets to public 501(c)(3) charities are the quickest and most straightforward way to contribute. This is a good option for those who itemize their deductions and want to make a one-time contribution but don't have long-term charitable goals. Appreciated long-term capital gain property is typically more advantageous to gift than cash. For example, you can gift shares of low-cost basis stock without selling it nor realizing the capital gain. Charitable organizations do not pay taxes on selling the securities once they are gifted, so make sure to identify the correct assets to donate to maximize your contribution.

1. Advantages
   a. **Simplicity:** These contributions are quick and require no set-up or administrative costs.
   b. **Tax Deduction**: For those who itemize deductions, donations qualify for a deduction of up to 60% of adjusted gross income (AGI) for cash and 30% of AGI for long-term capital gain property.

2. Disadvantages
   a. **Growth Potential:** With one-time gifts the cash or assets donated does not have the opportunity to appreciate and increase the impact of the contribution over time.
   b. **Privacy**: Gifts made are not anonymous.

Donor Advised Funds (DAFs)

These vehicles are well suited for those who want to make ongoing gifts to public 501(c)(3) charities, have low-cost basis assets to donate, and want to set up multi-generational giving. It is a straightforward, turn-key process that allows individuals to open accounts with a custodian, contribute cash or other assets, invest the donated funds, and then grant funds to charities as they so choose.

1. Advantages
   a. **Tax Deduction:** Taxpayers receive an immediate tax deduction. Donations can be bunched into specific tax years to maximize deductions and offset other taxable events, and then donated over multiple years. Individuals can donate a variety of liquid and illiquid assets, including cash, stocks and bonds, real estate, private investments, and artwork, among others.
   b. **Flexibility:** Minimums for donations and grants are low, making it accessible for many to get started. At Schwab Charitable, there are no account or contribution

minimums, and the minimum grant starts at $50. No required amount must be donated in any given year, so account holders can parcel out gifts as they see fit. Donations can also be automated for ongoing contributions. Many institutions now offer DAFs, so individuals have many options to choose from.
   c. **Multi-Generational Gifting:** Family members and loved ones can be added as successor account holders to continue the legacy of gifting.
   d. **Ease of Administration:** These are typically much less expensive to operate than private foundations and other trusts. Custodians also handle reporting and recordkeeping requirements.
   e. **Privacy:** Gifts made from DAFs can be kept anonymous.

2. Disadvantages
   a. **Administrative Fees:** While DAFs are cheaper than private foundations, they are still more expensive than contributing directly to a charity. At Schwab, there is an administrative fee starting at 0.60% for the first $500,000 of assets and tiering down from there, plus expense ratios associated with available investment options.
   b. **Limited investment options:** Most programs offer a limited menu of options that include mutual funds and ETFs. They do not have the same investment options as private foundations and trusts. At Schwab, DAFs with balances above $100,000 can be invested with a professional manager.

Private Foundations

These are charitable organizations typically set up by individuals or families to support ongoing philanthropic activities, overseen by a board of directors. These vehicles are good fits for those who want to maintain a level of control over the entity, set up a multi-generational legacy, and are comfortable with the time and financial commitment to keep them running.

1. Advantages
   a. **Flexibility of Grants**: Foundations allow donors to make grants to non-501(c)(3) organizations. This can include programs for specific individuals and scholarships.
   b. **Tax Deduction:** Allows up to 30% of AGI for cash gifts and 20% for long-term capital gain assets. A variety of assets can be accepted as donations.
   c. **Long-Term Legacy**: These are great tools for those who want to maximize their impact over many years.
   d. **Investment flexibility:** Funds can be professionally managed and generally can utilize a wide universe of stocks, bonds, mutual funds, or ETFs.

2. Disadvantages
   a. **Administrative Costs:** There is a lot of upfront and ongoing work associated with foundations, including fees for tax advisors and lawyers, and potentially employing staff.
   b. **Distribution Requirements:** Generally, foundations must distribute 5% of funds annually. Failure to do so may result in an excise tax payment of 30% on the undistributed amount.
   c. **Investment Income Excise Tax:** Foundations are exempt from federal income tax, but investment income is subject to an excise tax of 1.39%.
   d. **Deduction Limitations:** Non-publically traded assets do not receive a deduction based on current fair market value but are limited to the owner’s cost basis.

Charitable Trusts

These are irrevocable trusts and are best for those who have large estates and would like to designate a portion to charity. There are a variety of options for the structures of these trusts, with the main categories being either Charitable Remainder Trusts or Charitable Lead Trusts.

Remainder trusts are best for those who want to generate income. The grantor donates to the trust and while they can no longer access the principal, they can access a certain percentage or unit of interest that is determined upon creation of the trust. There are two types of these trusts, charitable remainder annuity trusts (CRATs), which distribute a fixed annuity amount, while charitable remainder unitrusts pay out a fixed percentage of assets that is revalued annually. Trust assets can be invested in and continue to grow. Upon the end of the dissolution of the trust, which is typically for the lifetime of the donor but not exceeding 20 years, the assets flow through to 501(c)(3) charities or a DAF.

Lead trusts are the inverse of remainder trusts, providing ongoing income to a public charity over a set period with the remainder being distributed to non-charitable beneficiaries. These are not subject to the 20-year time limit. In many cases a DAF can be named as a charitable organization, providing greater flexibility on where the ongoing income is granted.

1. Advantages
    a. **Tax Deduction:** An itemized deduction is incurred for remainder trusts. A variety of assets can be accepted for donation. Lead trusts do not get an immediate deduction but receive an estate or gift tax charitable deduction. The lead trust will receive ongoing charitable deductions for the amount gifted to charity.
    b. **Reduce Taxable Estate:** This is an efficient way to reduce estate taxes while retaining either income or principal for beneficiaries.
    c. **Investment Flexibility**: Funds within the trusts can be professionally managed at most custodians and can utilize a wide universe of investment options.
    d. **Flexibility**: Donors can act as trustees and may have the ability to change charitable beneficiaries during the term of the trust.

2. Disadvantages
    a. **Administration:** There are initial attorney and CPA fees to set up the trust, as well as ongoing annual tax returns.
    b. **Market and Inflation Risk:** Income taken by the lifetime beneficiaries may eat into the principal, reducing what is left to the remainder beneficiaries. Also, income may not keep up with inflation, specifically for Charitable Remainder Annuity Trusts, which specify a specific amount to be distributed annually.

Qualified Charitable Distributions

If you are over 70 ½ and have a tax-deferred IRA, you can gift up to $105,000 in 2024 (indexed for inflation) directly from the account to a public charity. Money is sent directly from the account to the receiving charity. This approach is well suited for those who do not need all or a portion of funds from their retirement accounts and do not itemize deductions.

1. Advantages
    a. **Above-The-Line Deduction**: Individuals can reduce taxable income without having to itemize deductions. This is especially useful for those with large required minimum

distributions (RMDs) as it is a dollar-for-dollar reduction in AGI.

   b. **Low Cost:** There are no administrative fees or setup costs, you can generally write a check directly from your existing retirement account.

2. Disadvantages
   a. **Timing:** Checks must be cashed by the receiving charity before 12/31 to count as a deduction for the tax year, so if you are making donations close to year-end there is a chance the transaction may not be completed. We recommend donations are made 3-4 weeks before year-end and to confirm with the receiving charity.
   b. **Privacy**: These gifts are not anonymous.
   c. **IRA Only:** Donations can only be made from IRAs and not other tax-deferred retirement accounts such as 403(b)s and 401(k)s.

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