CHARITABLE GIVING OPPORTUNITIES IN 2025

With the start of the new year, it is an excellent time for gift planners, advisors and donors to consider tax planning opportunities for 2025. Two full tax years have elapsed since the passage of the SECURE 2.0 Act which created the opportunity to fund lifetime split-interest gifts with a qualified charitable distribution from an IRA. With the possible sunset this year of many major provisions in the Tax Cuts and Jobs Act (TCJA), taxpayers and their advisors recognize the utility of prudent charitable planning.

There are crucial areas that advisors should be aware of to maximize charitable giving. The new year represents a great time for donors to take advantage of tax-saving opportunities.

I. Individual Income Taxes

The top tax rate is scheduled to return to 39.6% in 2026, which would be an increase from the TCJA top tax bracket of 37%. In addition, the TCJA nearly doubled the standard deduction from 2018 through 2025. In 2025, the standard deduction will be $30,000 for couples filing jointly, $15,000 for single filers and $22,500 for head of households. The increase in the standard deduction reduced the number of itemizing taxpayers significantly. If lower standard deductions are returned in 2026, more taxpayers will resume itemizing their deductions, including charitable income tax deductions.

Donors may benefit from bundling charitable deductions by making a gift to a donor advised fund (DAF). A DAF permits a charitable deduction in the year of the gift, while the DAF can hold the funds and make charitable grants for many years in the future. This can simplify gifts in future years and permit the donor to make a gift large enough to itemize deductions in 2025. A good "bundling" method is to make gifts in January and December of alternate years.

II. State and Local Taxes

Prior to TCJA, state and local taxes (SALT) were deductible for federal income tax purposes, without a cap on the amount of taxes paid. However, the TCJA imposed a $10,000 limit on SALT deductions. The cap is set to expire in 2026. Taxpayers in high income tax states may experience some relief if this provision sunsets. In 2025, taxpayers may choose to make increased charitable deductions to offset the burden of the $10,000 cap on state and local taxes.

III. Estate and Gift Taxes

The estate tax lifetime exclusion amount increased from $13.61 million in 2024 to $13.99 million in 2025. A married couple in 2025 may have an estate of $27.98 million without incurring a transfer tax.

The annual gift exclusion will also increase in 2025 to $19,000. This exclusion applies on a per donor-per donee basis. An individual or couple with a large family may make substantial tax-free transfers each year using annual gift exclusions.

While the gift and estate exemption are $13.99 million in 2025, this increase is set to expire in 2026 and will be reduced to $5 million, plus adjustments for inflation. The inflation adjusted amount is expected to be approximately $7 million per individual. If the TCJA is not extended, the IRS final regulations in T.D. 9884 state that if a taxpayer has used his or her lifetime exemption at the current higher amount, there will not be a claw back of the excess exemption if the exemption is reduced in a future year. For example, a taxpayer can make gifts up to $13.99 million using his or her lifetime exemption in 2025, and if the lifetime exemption falls to $7.15 million in 2026 and the donor passes away that year, the gift amounts that were covered by the larger exemption would not be clawed back into the estate.

Advisors need to consider the implications of locking in gifts during 2025. It is uncertain if the larger exemption will be carried forward, so taxpayers should consult with competent counsel to make informed decisions before locking in the larger estate tax exemption.

IV. Charitable Deductions

The TCJA increased the charitable cash gift deduction limit to 60% of adjusted gross income (AGI). This charitable deduction limit, however, will revert to 50% of AGI in 2026. Both limits permit a five-year carryforward of excess charitable gift amounts. Donors may want to take advantage of cash giving to offset up to 60% of AGI in 2025. Tax professionals may want to prepare an estimated AGI to help donors optimize their cash giving.

Due to technical issues in the drafting of TCJA, tax professionals may apply a 50% AGI limit to combined gifts of cash and appreciated property. In December 2018, the Joint Committee on Taxation (JCT) published a "Bluebook" (JCS-1-18) on the Tax Cuts and Jobs Act. The JCT Bluebook explanation suggests that Sec. 170(b)(1)(G)(iii) was not intended to change the prior 50% and 30% ordering. On page 51, "Coordination with certain other percentage limits applicable to individuals," JCT stated, "It is intended that any contribution of cash by an individual to an organization described in section 170(b)(1)(A) (generally, public charities and certain private foundations that are not nonoperating private foundations) shall be allowed to the extent that the aggregate of such contributions for the taxable year does not exceed 60 percent of the taxpayer's contribution base, reduced by the aggregate amount of the contributions allowed under section 170(b)(1)(A) for the year. In other words, the 60-percent limit for cash contributions is intended to be applied after (and reduced by) the amount of noncash contributions to organizations described in section 170(b)(1)(A)." A technical correction bill has not been passed to clear up this error.

However, donors who make both appreciated property and cash gifts should consult their CPA to determine the 50% or 60% charitable deduction limit for their specific situations. Regardless of this technical difference, donors may want to take the opportunity to make cash gifts to maximize their charitable deductions.

V. IRA Charitable Rollover

An excellent way to fulfill an IRA required minimum distribution (RMD) is to give part or all of the IRA distribution to a qualified charity. Qualified charitable distributions (QCDs) for individuals over age 70½ may fulfill part or all an IRA owner’s RMD. The QCD is a transfer directly from the IRA custodian to a qualified charity and is not included in taxable income. The 2025 QCD limit will be $108,000 for gifts to charity. While there is no additional deduction, this may be a substantial tax-saver that helps prevent donors from being pushed into higher tax brackets.

January 1, 2025, will mark the two-year anniversary of the SECURE 2.0 Act's provision allowing a one-time election to a split-interest gift with a QCD. The 2025 limit for an IRA charitable split-interest gift rollover will be $54,000. The split-interest entity may be a charitable remainder annuity trust (CRAT) (Sec. 664(d)(1)), a standard charitable remainder unitrust (CRUT) (Sec. 664(d)(2)) or an immediate charitable gift annuity (CGA) (Sec.501(m)). The trust or annuity must be exclusively funded by a QCD. A gift annuity must have a minimum payment of 5% and is required to make the first payment within one year. All payments from the QCD-funded vehicle will be taxed as ordinary income.

If an IRA owner made the election to use a QCD to fund a life-income plan in a prior calendar year, the IRA owner is precluded from making an additional election in 2025 even though the limit increased to $54,000. While the one-time election is for a single tax year and can only be exercised once in a lifetime, the IRA owner can make multiple QCD gifts within the same tax year, up to the $54,000 limit in 2025. Advisors may need to track this for their clients to ensure they do not run afoul of this once-in-a-lifetime provision.

Donors who use the QCD are not subject to the charitable deduction limits because the gifts do not generate a charitable income tax deduction. If the custodian makes a transfer to charity, the IRA owner will receive IRS Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. The IRS Form 1040 for the tax year will require the IRA distribution to be reported on Line 4a. If the full distribution is a QCD, the taxpayer will enter "zero" on Line 4b of his or her tax return and write in "QCD" next to the line.

A charity must send the donor a written acknowledgment of the IRA contribution. This is not a receipt because the gift is not included in income and is not deductible. However, the written acknowledgment from the charity must state that "no goods or services were received" as a result of the IRA gift.

VI. Income Tax Strategies in 2025

Three basic strategies can help optimize charitable giving in 2025.

First, an upper-income person should maximize his or her IRA charitable rollover. The upper-income person may be subject to alternative minimum tax (AMT), even if there are large gifts to charity. High adjusted gross income will result in the phasing-out of the AMT exemption. Therefore, it is very important for individuals in the higher tax brackets to use the IRA charitable rollover to fulfill their RMD and avoid taking the IRA payout as taxable income. Reducing adjusted gross income may save substantial AMT for these taxpayers.

Second, because an appreciated gift of land or stock bypasses capital gain and produces a fair market value charitable deduction, these are considered "favored" gifts. A strategy for high-income taxpayers is to make appreciated property gifts up to the 30% limit each year. Some donors will invest in stock or land for the purpose of making appreciated property gifts in the future.

Third, donors often make additional cash gifts. Gifts of cash and appreciated property may be combined, provided that the total gifts do not exceed the deduction limits of the donor's AGI.

To maximize income tax savings, donors can combine strategies such as reducing AGI through IRA charitable rollover gifts, appreciated property gifts and cash gifts. The appreciated property and cash gifts may be made outright or through life income plans. If the donor is age 70½ or older and has not elected in prior years to fund a split-interest gift with a QCD, that may be considered as well.

VII. Life Income Planning in 2025

There are a few life income plans that will produce charitable deductions or reduce taxable income. These can be used quite effectively to maximize the tax savings through charitable planning.

Example 1 – QCD - Samantha is 80 years old and wishes to take advantage of using her IRA to fund a one-life CGA in 2025. Samantha decides to contribute the maximum limit of $54,000 in exchange for a CGA with her favorite charity. Samantha's total QCD gifts cannot exceed $108,000 in 2025. As such, Samantha will have a remaining available QCD limit of $54,000 that she can transfer tax-free outright to charity. She makes an additional outright gift to her favorite charity to maximize her QCD giving in 2025.

In future years, Samantha will only be able to make outright QCD gifts to her favorite charity because she has used her once-in-a-lifetime CGA funded with a QCD.

Example 2 – Appreciated Stock - Robert and Jewel bought stock in a technology company several years ago. It appreciated from $200,000 to $1 million in value. They are in the top 37% income tax bracket. If they were to sell the stock, there would be federal capital gains tax of $190,400.

By contributing the stock to a 5% charitable remainder unitrust, they bypass or avoid $190,400 in capital gains tax. In addition, they receive an income tax deduction of approximately $450,240. With deductions spread over three years under the 30% AGI limit, they will write off this amount and save over $166,000. In addition, they will receive lifetime payments from the trust of approximately $50,000 each year.

The unitrust is invested in a stock-bond portfolio with approximately 60% capital gain and dividends and 40% ordinary income. The annual income of $50,000 includes tax-favored payouts of capital gains and dividends, which also provide significant tax savings over their two lifetimes.

Example 3 – Unitrust and Sale - Brandon and Holly purchased development land for $400,000. It has grown in value to $2 million. If they were to sell the property, they would owe over $350,000 in capital gains tax.

Brandon would like to retain cash to make another similar investment but hopes to reach this goal with no capital gains tax payment. The chosen solution is to fund a charitable remainder unitrust with 80% of the property and retain 20% in a revocable trust. With their financial advisor as trustee for both trusts, sale of the property to a third party is negotiated. Because the trustee has title to 100% of the property, there are more favorable characteristics for both charitable tax deductions and sale of the property.

The buyer is willing to purchase the property at the fair market value of $2 million. Costs for the sale of the land are estimated to be $160,000 and will be allocated pro rata between the two trusts. The net cash received will be $368,000 and the unitrust funding will be $1,472,000.

The capital gain is bypassed on the unitrust. With the allocation of 20% of the basis to the revocable trust, potential gain on the cash portion is more than offset by the tax savings on the $819,216 unitrust charitable deduction. With their net tax savings over five years under the 30% guideline, Brandon and Holly enjoy a net cash benefit of $602,566.

The sale and unitrust achieved all objectives. Brandon has the cash necessary to make another investment and they receive generous income for two lifetimes from the trust. They reduced the net tax to zero and benefitted from additional tax savings.

Example Four – Tax Free Payouts - Susan has a large income and substantial estate. As a result, she is in the top 37% federal bracket. Susan has always been open to supporting her favorite charity and transfers $1 million in cash to fund a 6.8% gift annuity. The $1 million in cash had previously been invested in short-term corporate bonds with a 2% to 3% payout. In addition to subjecting her to a high tax rate, the return was relatively low.

Upon funding the charitable gift annuity with $1 million of cash, she has an income tax deduction of $376,161. Susan can offset up to 60% of her AGI and may save approximately $139,180. The charity that created the gift annuity ran the illustration with the lowest possible AFR of 4.4%. This slightly reduces the charitable deduction, but it maximized the tax-free payout. Susan was pleased because this tax-free payout was her number one objective.

Each year, the charity makes quarterly payments that total $68,000. The tax-free amount of $47,260 is 69.5% of the total payout. The balance of the payout is ordinary income. With her high tax bracket and the combination of income tax savings and tax-free payout, the 6.8% annuity has an effective annual rate of 11.1%. Susan considers this in effect a 6.8% payout with two tax benefits that dramatically increases her effective rate.

Conclusion With the combination of increased tax brackets and phase-outs of the increased standard deduction, upper-income Americans will be very interested in creative 2025 tax strategies. Since many of these individuals will not have substantial mortgage interest or medical expense deductions, their primary tax-saving opportunities will most likely be charitable. For those who are charitably inclined, the IRA charitable rollover, maximizing deductions and creative use of the life income charitable plans will create great benefits for both the donors and their favorite charities.

ABOUT JAMES E. CONNELL

James E. Connell FAHP, CSA of Connell & Associates, Pinehurst, North Carolina, is a respected gift planning consultation firm with over four decades of experience offering a broad range of charitable estate and gift planning services to non-profits throughout the country. He heads CONNELL & ASSOCIATES, Charitable Estate & Gift Planning Specialists in Pinehurst, North Carolina. Contact him to help your organization analyze the value CGAs may provide.

Contact James at 910-295-6800 or james@connellandassoc.com or fax him at 910-295-6866