Kim Laughton: What are the biggest changes in the new tax law?

Hayden Adams: One of the biggest changes is the tax rates and brackets. Some rates have gone down and the tax brackets themselves have shifted, so more income is going to be taxed at lower rates.

In addition, the standard deduction has been significantly increased to $12,000 from $6,350 for single filers and to $24,000 from $12,700 for married filers. Because of this change it’s estimated that about 90% of taxpayers will end up taking the standard deduction. The increased standard deduction combined with the new lower tax rates should lower the tax bills of the majority of these households.

Unfortunately, some itemized deductions have been limited or eliminated. This could negatively impact higher net worth taxpayers in areas with high taxes states; however with some planning some of the adverse effects may be mitigated.

Kim Laughton: You mentioned some itemized deductions have been limited or eliminated. Are there any changes to the popular charitable deduction?

Hayden Adams: Luckily, the charitable deduction remains unchanged and is a relative bright spot under the new tax law. Of all the itemized deductions, the charitable deduction is the one that taxpayers have the most control over.

The new tax law also preserves the tax benefits of donating appreciated investments or assets. Donating appreciate assets is a great way to maximize your charitable impact, because charities don’t pay capital gains on the sale of donated assets, which enables donors to give up to 20% more than they could if they sold the asset first, paid capital gains taxes owed and donated the proceeds.

Other popular itemized deductions have been eliminated or capped. For example, the deduction for property, real estate, local, and state taxes have been capped at $10,000. Also, the mortgage interest deduction has been capped at $750,000 of indebtedness. Taxpayers who continue to itemize will find the charitable deduction a relatively more powerful planning tool.

Kim Laughton: For those who continue to itemize their deductions, are there any changes in the tax bill that are going to impact them and their ability to maximize the tax benefits of charitable giving?

Hayden Adams: Yes. Prior to tax reform, there was a 3% overall limitation on itemized deductions—known as the Pease Limitation—that could potentially phase out a lot of the value that people would receive from itemizing. That limitation was removed. Also, the alternative minimum tax (AMT) deduction and phase-out has significantly increased, which means far fewer people will have their itemized deductions limited.

In addition, donors are now allowed to deduct cash contributions to public charities and donor-advised funds of up to 60% of their adjusted gross income (AGI), an increase of 10%. The limitation for asset contributions remains 30% of AGI.
Kim Laughton: That’s terrific news. Now let’s talk about the people who may have itemized their deductions in the past, but will most likely take the standard deduction in the future. How does this new tax law affect them and are there any strategies they can use to give more tax efficiently?

Hayden Adams: There are definitely some strategies that can be implemented for individuals who are right at the margin between itemizing or taking the standard deduction.

For example, let’s say there’s a married couple filing jointly who traditionally has had $23,000 of itemized deductions each year. Because their itemized deductions are less than the new $24,000 standard deduction, they would be better off taking the standard deduction going forward.

But let’s say $13,000 of their deductions are related to state taxes and mortgage interest, while $10,000 is related to charitable donations. In that case, the couple may want to consider concentrating or “bunching” multiple years of charitable contributions into a single year. That way in one year, they could double their charitable giving and itemize $20,000 worth of donations plus $13,000 of their other normal itemized deductions, which gives them $33,000 of total itemized deductions. This puts them above the standard deduction.

The next year, they can skip donating and take the $24,000 standard deduction. The net result would be a lower tax bill over that two-year period.

Kim Laughton: We are definitely seeing a number of our donors use their Schwab Charitable accounts to execute a bunching strategy and enjoy the best of both worlds. The years that they take the standard deduction, they get the benefit of that higher standard deduction, but every few years if they itemize and make bigger gifts, they receive the full tax benefit of those charitable gifts.

Hayden Adams: It’s definitely something that people should consider. It’s very tax efficient to concentrate giving in that manner and one of the simplest and most flexible methods to do so is to use a donor-advised fund. Individuals can contribute a large amount into a donor-advised fund account in one year and then they can grant it out to various charities over time.

Kim Laughton: For people who are philanthropically minded, is it good to discuss their charitable giving strategy with their tax and financial advisor?

Hayden Adams: Definitely. In addition to maximizing their deductions in any given year, people should also look at tax planning strategies for those years when they may have high income. Those with a big personal windfall in a single year have an opportunity to make large contributions to a donor-advised fund or a charity offsetting a portion of the income that would otherwise be taxed at a higher rate.

Kim Laughton: That’s excellent advice. Thank you so much for being with us and for helping us to decipher the complexities of the tax law and its impact.

Schwab Charitable will continue to provide convenient tools and knowledgeable support so donors can focus on maximizing their impact on the charities and causes that are most important to them.

Visit www.schwabcharitable.org to learn more
For more information, call us at 800-746-6216

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