MANAGEMENT & *TAX CONCEPTS*

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TAX-SMART CHARITABLE GIVING: 5 STRATEGIES TO CONSIDER IN 2019

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Tax-smart charitable giving: 5 strategies to consider in 2019

If charitable giving is important to you, you may be motivated by several goals. Perhaps you're supporting a cause you're passionate about, giving back to a school or other organization that contributed to your success, or honoring a loved one's memory. Typically, tax breaks for charitable donations are not, by themselves, the top motivating factor. But taxes are an important consideration, partly because they may affect how much you choose to give.

Here are five tax strategies for enhancing the tax benefits of your charitable gifts.

1. Make the most of itemized deductions. To deduct charitable gifts, you must itemize, but recent tax law changes reduced the number of people who will choose to itemize. The Tax Cuts and Jobs Act (TCJA) nearly doubled the standard deduction to $12,200 ($24,400 for joint filers). It also capped deductions for state and local income and property taxes at $10,000, and limited deductions for interest on certain mortgages and home equity debt. If your total itemized deductions are less than the $12,200 or $24,400 threshold, you'll likely claim the standard deduction and your charitable gifts will provide no tax benefits absent some additional planning.

For instance, one effective strategy for maximizing your deductions is to "bunch" your charitable

gifts into alternating years. Here's how that works: Suppose Donnie and Connie, a married couple filing jointly, have itemized deductions totaling $20,000 per year. The deductions consist of $10,000 in state income and property taxes and $10,000 in charitable donations. (Their mortgage is paid off, so they have no deductible interest expense.) Because the couple's itemized deductions are less than $24,400, they're better off taking the standard deduction.

Donnie and Connie can increase their deductions if, instead of donating $10,000 per year to charity, they donate $20,000 every other year. That way, they're able to claim $30,000 in itemized deductions one year and the $24,400 standard deduction the following year. Their expenses for the two-year period still total $40,000, but they increase their deductions for the period from $48,800 to $54,400.

2. Open a donor-advised fund. Bunching charitable donations can help you maximize your tax benefits, but the timing may not be ideal for the charities that receive them. One way around this problem is to use a donor-advised fund (DAF), a charitable investment account to which you make tax-deductible contributions. A properly structured DAF allows you to bunch your charitable deductions into alternating years while requesting the fund sponsor to distribute funds to your charitable beneficiaries evenly over time.

3. Donate cash. Even if you itemize, your charitable deductions are limited to a percentage of your "contribution base" — generally, your adjusted gross income (AGI). Cash gifts to public charities are currently deductible up to 60% of the contribution base, while noncash gifts are usually subject to a 30% limit. (Contributions more than those limits may be carried forward up to five years.) If income limits come into play, you may be able to maximize your deductions by donating cash.

4. Donate appreciated assets. Despite lower deduction limits, donating appreciated stock or other assets to charity may provide attractive tax benefits. For example, if you sell appreciated stock and donate the proceeds to charity, you'll owe capital gains taxes on your profits. But if you donate the stock directly to a charity, you'll avoid those taxes. Plus, you'll enjoy these savings even if you're unable to deduct the value of your gift (because you don't itemize, for example).

5. Do a charitable "rollover." If you're 70½ or older, consider a qualified charitable distribution (QCD) from your traditional IRA to charity. A QCD allows you to transfer up to $100,000 tax-free *directly* from an IRA to a qualified public charity and to apply it toward your required minimum distribution for the year. The advantage of a QCD is that the distribution is excluded from your AGI, allowing you to avoid the tax even if you don't itemize.

One effective strategy for maximizing your deductions is to "bunch" your charitable gifts into alternating years.

As you review your philanthropic plans, be sure to consider the tax implications of your charitable gifts and strategies for reducing those costs. Tax savings may not be the reason you give, but they can provide an incentive to give more. You have until December 31, 2019, to make a donation that could affect your 2019 tax year. •

Should you choose a traditional or a Roth IRA?

When introduced in 1975, Individual Retirement Accounts (IRAs) were the first government-sponsored, tax-advantaged tool designed to help people save for retirement. More than 40 years later, IRAs remain one of the most popular retirement savings tools in America.

While many people contribute to employer-sponsored 401(k) plans, IRAs can also be beneficial — especially for those who don't have access to an employer 401(k) or other retirement plan. You have until April 15, 2019, to make an IRA contribution for tax year 2018.

HORSES OF DIFFERENT COLORS

Should you choose a traditional IRA or a Roth IRA? It's important to understand the differences between them to make the best choice. Or you can opt to split

your contributions between the two IRA types. The maximum (presuming your earned income is no less than the amounts mentioned below) that can be contributed, in aggregate, is $5,500 for 2018 and $6,000 for 2019 — plus an additional $1,000 for those age 50 or older.

The original (or traditional) IRA can enable retirement savers to deduct annual contributions, thus lowering current taxable income. But withdrawals, which generally begin in retirement, are taxed at ordinary-income tax rates.

Some people, however, want to minimize their income tax liability later in life so they've more money to spend when retired. So, effective in 1998, the Roth IRA was introduced, allowing tax-free withdrawals of principal and earnings.

But there's a tradeoff: No tax deduction is allowed for Roth IRA contributions.

QUALIFICATION CRITERIA

As you weigh the traditional vs. Roth IRA decision, the first thing to determine is whether you qualify to contribute to a Roth IRA.

If you're single (or head of a household) and your modified adjusted gross income (MAGI) is greater than $137,000 (or $203,000 if you're married and file jointly), for 2019 you can't contribute to a Roth IRA. If you're single and your MAGI is between $122,000 and $137,000 (or $193,000 and $203,000 if you're married and file jointly), you can make a reduced Roth IRA contribution.

The next thing to determine is whether you qualify for a traditional IRA deduction. If you or your spouse is covered by a retirement plan at work, your deduction may be limited or eliminated, depending on your MAGI. If neither you nor your spouse is covered by a retirement plan at work, your deduction is generally allowed in full.

BENEFIT NOW OR LATER?

Assuming you're eligible for both, the decision about which type of IRA is better essentially comes down to which has more value for you: a tax deduction now or the ability to withdraw money tax-free later when you retire.

If you're in a lower tax bracket today than you might be in retirement, you may prefer to take advantage of the tax-free growth and income offered by a Roth IRA. On the other hand, if you're in a higher tax bracket today than you might be in retirement, you may prefer to take advantage of the current tax deduction offered by a traditional IRA.

The decision about which type of IRA is better essentially comes down to which has more value for you: a tax deduction now or the ability to withdraw money tax-free later when you retire.

The withdrawal rules for traditional and Roth IRAs could also affect your decision. With a few exceptions, distributions from traditional IRAs before age 59½ are included in gross income and subject to a 10% early withdrawal penalty. However, contributions (but not earnings) made to Roth IRAs can be withdrawn penalty- and tax-free at any age.

Also, you must begin taking required minimum distributions (RMDs) from traditional IRAs, with certain exceptions, when you turn 70½. But there are no RMDs with Roth IRAs that you've created. (Different rules apply for inherited IRAs.)

GET EXPERT ADVICE

There are a lot of nuances involved in making the traditional vs. Roth IRA decision. Be sure to consult with your financial and tax advisors for guidance in your situation. •

QOFs may defer and even minimize capital gains tax

If you're selling a business interest, real estate or other highly appreciated property, it's likely you'll be hit with a substantial capital gains tax bill. One way to soften the blow — if you're willing to tie up the funds long term — is to "roll over" the gain into a qualified opportunity fund (QOF). Under a new federal program, reinvesting in a QOF allows you to defer, and even reduce, the tax on your original gain and to avoid tax on future appreciation within the QOF.

WHAT IS A QOF?

A QOF is an investment fund, organized as a corporation or partnership, designed to invest in one or more Qualified Opportunity Zones (QOZs). A QOZ is a distressed area that meets certain low-income criteria, as designated by the U.S. Treasury Department. Currently, there are more than 9,000 QOZs in the United States and its territories. QOFs can be structured as multi-investor funds or as single-investor funds established by an individual or business.

To qualify for tax benefits, at least 90% of a QOF's funds must be "QOZ property," which includes:

QOZ business property. This is tangible property that's used by a trade or business within a QOZ and that meets certain other requirements.

QOZ stock or partnership interests. These are equity interests in corporations or partnerships substantially all of whose assets are QOZ property.

Note: Proposed regulations, which can be relied on pending final regulations, define "substantially all" to mean at least 70%.

WHAT ARE THE BENEFITS?

If you recognize capital gain by selling or exchanging property, and reinvest an amount up to the amount of gain in a QOF within 180 days, you'll enjoy the following tax benefits:

- Deferral of tax on the reinvested gain until the earlier of December 31, 2026, or the date you dispose of your QOF investment,
- Permanent reduction of the taxability of your gain by 10% if you hold the QOF investment for at least five years and an additional 5% if you hold it for at least seven years, and
- Tax-free capital gains attributable to appreciation of the QOF investment itself, if you hold it for at least 10 years.

The only way to obtain these benefits is to first sell or exchange a capital asset in a transaction that results in gain recognition. You then would reinvest some or all of that gain in a QOF. You can't simply invest cash in a QOF.

WHAT ABOUT THE DOWNSIDE?

QOFs can be attractive investment opportunities, but they're not without their drawbacks. For one thing, you'll need to hold the investment for a significant amount of time to enjoy the full benefits. Also, you or your heirs will eventually be liable for taxes on some or all of the original gain. So, it pays to consider other options that would allow you to avoid those taxes, such as holding the original property for life or doing a tax-free exchange.

ACT NOW

If you're interested in investing in a QOF, it's a good idea to start the process as soon as possible. As explained above, you can defer gain reinvested in a QOF until the end of 2026. But to enjoy a 15% gain reduction, you must hold the investment for seven years. In other words, to achieve the maximum benefit, you must invest in a QOF by the end of 2019.

Consult your financial advisor before investing in a QOF. The rules surrounding these investments are complex, and the proposed regulations may be modified before they're finalized. •

Borrowing alternatives for businesses

Your need for capital will color your financing choice

You may be ready to walk into your banker's office and apply for a loan to expand your business, buy equipment or just stay afloat. Or you may be considering an alternative to a bank loan. But exactly what type of financing should you pursue?

BANK LOAN TYPES VARY

Bank loans come in a variety of shapes and sizes, but most fall into one of several broad categories. *Lines of credit* are the most common small business loan, primarily because of their simplicity and flexibility. Once your business is approved for a line of credit, you can borrow up to your credit limit whenever you like without having to reapply. It's often a good idea to apply for a line of credit *before* you need capital. That way, you can easily tap your line when a need for capital arises.

As the name suggests, *term loans* are issued for a specific period of time. They're repaid with interest over a set number of years and used mainly to buy fixed assets like property, plant and equipment.

Commercial mortgages are a specific type of term loan used to buy new or existing commercial real estate. Examples include retail store space, industrial warehouses and office buildings.

Government loan programs are also used for raising capital. Among the most popular programs are the Small Business Administration (SBA) loan programs, such as the SBA 7(a), SBA 504 and SBA Express loan programs. The SBA guarantees a portion of these loans, enabling banks to lend to companies that might not ordinarily be able to use normal underwriting criteria.

It's important to know *why* you need capital so your banker can suggest the right type of loan to meet your financing needs. For example, if you need a capital infusion to meet periodic cash flow shortfalls or fund accounts receivable, a line of credit is probably the right source of capital. But you typically wouldn't use a line of credit to buy equipment or real estate — a term loan or commercial mortgage is the right type of loan for these capital needs.

> *It's often a good idea to apply for a line of credit before you need capital. That way, you can easily tap your line when a need for capital arises.*

OTHER PLACES TO LOOK

In addition to banks, some businesses today are seeking capital from alternative sources, such as commercial finance companies and peer-to-peer lenders. The former provides alternative financing solutions such as factoring. In this scenario, you receive an advance against uncollected receivables and asset-based and accounts receivable loans, in which real estate, equipment, inventory and receivables are pledged to secure capital.

Meanwhile, peer-to-peer lending is becoming popular as a way for businesses to access capital via the Internet. Sometimes referred to as "crowdfunding," it allows businesses to borrow money from individuals or Internet lenders that focus on lending to small businesses.

Finally, when it comes to acquiring equipment, *leasing* is often a better capital option than borrowing. This is especially true for equipment with built-in obsolescence like computers, because they can be replaced or upgraded when the lease is up. Equipment leasing is 100% financing, which frees up cash flow. And it also may offer tax benefits which would otherwise only be available when purchasing an asset.

YOUR DECISION

You may need capital because your company is going through a tough economic stretch. Or you may want it to grow your business, remodel or buy new equipment. Whatever the reason, you have a wide variety of lending sources to which you can turn. And it's usually smart to "shop around" before making a commitment. •

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