IN THIS ISSUE

Trust UPDATE

CITIZENS BANK
A Bank Built For You

October 2020

Year-end tax planning, 2020 edition

Start early this year on understanding your choices

The conventional rule of thumb for year-end tax planning has been to defer income and accelerate deductions. The 2017 tax reform hit that thinking with a one-two-three punch, doubling the standard deduction while cancelling some itemized deductions and capping the deduction for state and local taxes at $10,000. The result was that the number of taxpayers who itemize deductions fell by almost two-thirds from 2017 to 2018, according to a recent analysis. Nearly 90% of taxpayers now claim the standard deduction. See page 3 for more on this topic.

However, there are still choices that taxpayers may make, especially in the above-the-line area of the Form 1040, before they get to adjusted gross income.

Charitable gifts

For those who are near the boundary of the standard deduction, one strategy to consider is making large charitable gifts every other year. In the year without a gift, the standard deduction takes over. In this way, a maximum tax benefit may be secured for all of one's charitable gifts.

The CARES Act, enacted in response to the coronavirus pandemic, made two important changes to the tax treatment of charitable gifts this year.

No itemizing required for small gifts. Up to $300 in cash charitable gifts may be taken as an adjustment to gross income by taxpayers who do not itemize. Charities would like to make this rule permanent, with a higher cap, but that is a story for another day.

Higher ceiling for large gifts. The normal rule after 2017 has been that the deduction for charitable giving is limited to 60% of adjusted gross income. The limit has been boosted to 100% for cash gifts this year.

Special rule for older taxpayers. Another important rule for those who are 70½ and older is that they may make direct charitable gifts from their IRAs, up to $100,000. This rule was not affected by the CARES Act. Such gifts satisfy the required minimum distribution rules (those are suspended for 2020). The important takeaway is that charitable gifts from an IRA are not included in

A capsule guide to our services for investors

Our services are, in essence, powerful financial planning tools built upon important investment management components. One of the great strengths of trust planning is the ability to tailor the plan to respond flexibly to current and future financial needs.

Portfolio supervision. Serious investing is a full-time job. Our investment advisory and investment management services put experienced investment professionals on your side. The officer assigned to your account will work with you to establish an investment strategy suited to your personal goals and circumstances. Asset allocation planning will be employed to optimize your portfolio, reducing investment risk through a process of disciplined diversification.

Lifetime financial management. The next step in comprehensive financial protection employs a *revocable living trust*. We begin by developing an investment policy for the trust based upon your requirements. We will implement that plan, providing continuous portfolio supervision and distributing or reinvesting trust income as directed. As trustee, we can move beyond the investment sphere, arranging to pay household bills and taxes on your behalf. A revocable trust provides financial protection in the event of incapacity, and it has important estate planning advantages as well.

IRA rollovers. Anyone who will receive a lump sum distribution from an employer's retirement plan would be well advised to take a careful look at an IRA rollover for the funds. A rollover preserves valuable tax privileges and can enhance your retirement capital. Taxable withdrawals may begin without penalty at age 59½, and a program of minimum withdrawals must begin at age 72. With their tax-deferred nature, IRA rollovers present somewhat unusual investment issues, which should be resolved in the context of a full review of financial resources.

income, and the taxpayer is still entitled to the full standard deduction.

Portfolio review

2020 has been a roller coaster ride for investors, and not the good kind.

Many investors moved from stocks to cash as the pandemic got underway. Such prudent moves for protecting assets carry potential tax consequences, especially for long-term holdings.

At the same time, the recovery in stock prices has not been uniformly distributed across all industries. If there are portfolio holdings in the loss category, harvesting those losses to offset realized capital gains may be the sensible course. Capital gains and losses are netted to reach the final taxable amount for Form 1040.

Retirement savings

Another important adjustment to income is a contribution to a traditional IRA. Up to $6,000 may be set aside ($7,000 for those 50 and older). If your income is too high to permit a deduction for a traditional IRA, the Roth IRA may be a good alternative. No current tax savings are created, but there is a potential for tax-free income in retirement.

If the coronavirus pandemic has put you into a lower tax bracket than usual, this may be a good year to consider a conversion of your traditional IRAs to Roth IRAs. The conversion will be a taxable event this tax year, but the tax-free income in future years may be most welcome, especially if tax rates go higher so as to pay for the government deficits being run up in response to the pandemic.

See your tax advisors before making any final decisions on this year's tax strategies. ☐

Estate planning angles

If you haven't reviewed your will and estate plans for several years, this would be a good time to take a look at them. Changing family circumstances (births, deaths, divorces, retirements) are occasions for such evaluations. If major assets mentioned in the will have been sold, such as real estate or business interests, that's another good reason to make an appointment with the estate planning advisor.

Annual exclusion gifts. The first $15,000 in annual gifts to one person are free of gift tax. For married couples, one of them may give $30,000 and "split" the gift with the other, doubling the tax protection.

Gifts of appreciated securities to children or grandchildren carry an income tax bonus. The children may be in the 0% bracket for capital gains, and so may harvest that appreciation tax free.

Results from the 2017 tax reform

The Tax Cuts and Jobs Act (TCJA) of 2017 was primarily a reform of corporate taxes. The USA had the highest tax rate on corporate income of any developed nation, and that rate was dramatically reduced.

A secondary goal was simplifying the tax reporting for most taxpayers. To that end, the standard deduction was roughly doubled, so that more taxpayers could skip the paperwork of itemizing their deductions. Many deductions were eliminated, and one of the most important, the deduction for state and local taxes (SALT), was capped at $10,000 per tax return. That limit made it even more likely that a taxpayer's itemized deductions would be less than the standard deduction.

The goal of slashing the number of itemizers was achieved, according to a new analysis of the IRS' "Statistics of Income" by Martin Sullivan, published in *Tax Notes* in September. Before the TCJA, nearly 31% of taxpayers were itemizing. In 2018, just 11.4% took the trouble to document all their deductions. The phenomenon was most pronounced for those whose income was less than $500,000. At the top income levels above $10 million, 92% still itemized, down from 97.1%.

The dollar value of all itemized deductions, expressed as a percentage of adjusted gross income (AGI), fell from 12.2% to 5.6% in 2018. As one might expect, in percentage terms the greater declines were in the lower income brackets (See Figure One), but they were fairly represented across all the brackets. As most of the highest-income taxpayers still itemized, their total deductions declined less. The author attributed most of that to the cap on the SALT deduction.

Charities were very afraid that the loss of a strong tax reward for giving would result in a drop of philanthropic support. The data for 2018 do show a decline in claims for the charitable deduction, but it is far less than the decline is generally (see Figure Two). The larger decline is at the lower income levels where the standard deduction is much more likely to be the better choice for the taxpayer, masking the actual level of charitable support. For the top income levels, charitable donations as a percentage of adjusted gross income were almost unchanged.

The largest change in the itemized deduction matrix was for the SALT deduction, which fell from 5.7% of AGI to 1.3%. Top taxpayers had been reducing their AGI by 7.4% for the SALT deduction, roughly the same as their charitable contributions. In 2018, their SALT deduction fell to 0.5% of AGI. ☐

FIGURE ONE

Value of itemized deductions as a percentage of AGI (Thousands of dollars)

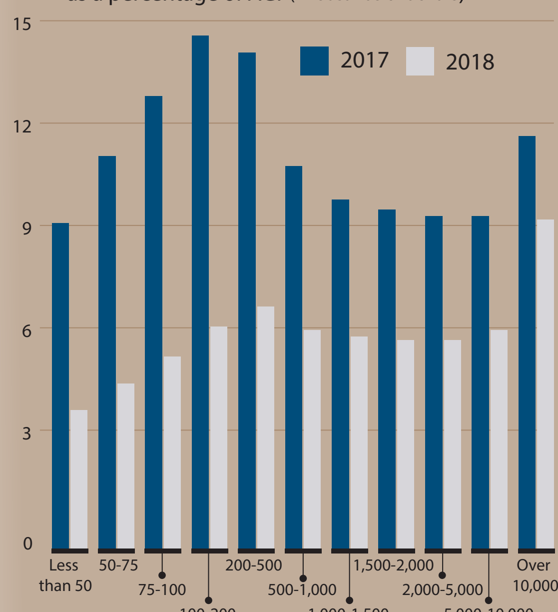
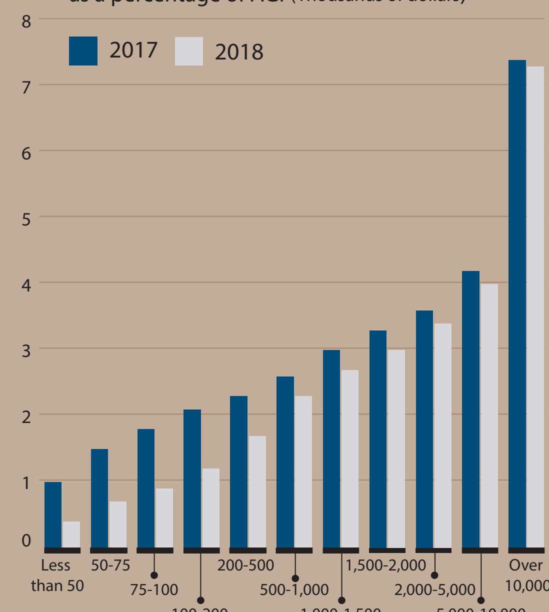


FIGURE TWO

Value of itemized charitable deductions as a percentage of AGI (Thousands of dollars)



Source: Tax Notes, TCJA Downsized Deductions Dramatically, September 11, 2020

"Giving While Living"

Before there was The Giving Pledge established by Bill Gates and Warren Buffett, there was Chuck Feeney. Both Gates and Buffett claim Feeney as the inspiration for their commitment to give half of their wealth to charity, and their drive to have all wealthy persons make a similar pledge. Feeney is a philanthropist who few have heard of, because he hates publicity.

Chuck Feeney was born in New Jersey in 1931 during the Great Depression. He served in the Air Force during the Korean War and used the GI Bill to attend the Cornell School of Hotel Administration. He and fellow Cornell alum Robert Miller founded the Duty Free Shoppers (DFS) Group in 1960 to sell liquor, tobacco, and other luxury goods to tourists and American servicemen.

The idea was a great success. According to a *Forbes* article, in 1967 the DFS Group paid dividends to Feeney of $12,000. Ten years later, the annual payout had grown to $12 million.

But Feeney did not want all the money for himself. In 1984 he founded the Atlantic Philanthropies and transferred to it his entire stake in the DFS Group. He conducted his charity anonymously. Rather than put his name on buildings, Feeney would leverage his donations, getting other wealthy people to join in a project or get matching funds from a government.

His philanthropy continued substantially in secret and under the radar until the DFS Group was sold in 1996. The share going to Atlantic Philanthropies was $1.63 billion.

> ***"People used to ask me how I got my jollies, and I guess I'm happy when what I'm doing is helping people and unhappy when what I'm doing isn't helping people."***
>
> ***—Chuck Feeney, as quoted in*** **Forbes**

Feeney's great plan was to give essentially all of his money away during his life, not just 50%. To that end, Atlantic Philanthropies had a termination date in 2020, by which time all of its funds needed to be expended. That day came this past September, and the foundation has now closed. Over the years Feeney gave $8 billion to charity. However, he is not entirely without resources; he did reserve some retirement money for himself and his wife.

How is The Giving Pledge coming along? As of 2020, there are 211 pledgers in 24 countries who have promised that half of their wealth will go to charity. Mr. Feeney recommends they not limit their giving to 50%, and that they make their gifts during life, not after death. Only in that way can they get the satisfaction of seeing the good that their money has achieved. ☐