To donate or not to donate?

Surprise! Charitable giving is NOT curtailed by the new tax law

As I've made the rounds of the various boards I serve on — or even cocktail parties — I've heard a groundswell of incorrect opinion, an urban legend, if you will, that the American Taxpayer Relief Act of 2012 lowers the benefit of charitable donations. NOT!

In fact, in certain situations for high-income taxpayers, the new law actually increases the benefit for giving to charity. While the budget deal did not create a specific limitation on deducting charitable contributions, the general limitation on itemized deductions (the Pease limitation) was brought back and made permanent.

Keeping the Pease

The Pease limitation reduces itemized deductions by 3 percent of adjusted gross income (AGI) above $300,000 for married couples filing jointly, $250,000 for a single taxpayer and $150,000 for married couples filing separately. The limitation does not apply to deductions for medical expenses, investment interest, casualty and theft losses, or gambling losses. Key point: Your limitation is based on your AGI, not your deductions. So increasing your deductions will not change your limitation if there is no change to your AGI.

Practical limitations

Let's say your AGI is $600,000 and your itemized deductions are $45,000 (taxes, mortgage interest and charity). In this situation, your itemized deductions will be limited by 3 percent of your AGI above $300,000 (married filing joint), or $9,000. Whether you donate an additional $1,000 or $15,000 to charity, your itemized deductions will still be reduced by the same $9,000 as before. By choosing to donate the additional amount to charity, there will not be any additional limitation to your deduction.

To take this one step further, let's say your AGI is $600,000 in both 2012 and 2013. In 2012, your maximum tax rate was 35 percent and in 2013 your maximum tax rate has increased to 39.6 percent. Now the additional charitable donation is worth an additional 4.6 percent tax benefit.

Key considerations

As you consider your charitable contributions for 2013, your decision should not be based on misguided tax advice. Also, know that the above examples only reference federal income tax. If you live in a state with an income tax, you are also impacting the state rate by the amount of the federal charitable deduction. Obviously, each state is different as to rates and what is deductible, but the impact on the state income taxes should not be forgotten when it is time to make the decision "to donate or not to donate."

Another key consideration is that the new tax law extended the charitable IRA rollover provision through Dec. 31, 2013. This provision allows up to $100,000 in tax-free distributions to certain charities directly from an IRA account held by individuals age 70 ½ or older.

So, charitable giving remains a matter of personal choice. But contrary to what you might have heard, the new tax law, if anything, may make it more tax advantageous for you to give. So, with apologies to Shakespeare, a decreased tax benefit to giving is NOT the question. ●

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