Craig Wruck - Wed, 1/13/2021 - 18:06

As of the writing of this article, the inauguration of Joseph R. Biden, Jr. as the 46th President of the United States is just days away. Although past changes in the balance of political power have had little impact on overall charitable giving, we know that when donors experience uncertainty they tend to postpone and delay their giving decisions. This is a natural reaction: charitable giving is optional and, faced with uncertainty, the rational choice is to slow down or defer giving until the future becomes clearer.

Changes in tax law can create new and different gift opportunities. Gift planners will need to watch carefully and be prepared to react strategically to changing circumstances. What concerns might surface among donors? Could potential changes affect donors’ gift plans? How might we anticipate and address them? In this article we begin with a review of some concerns that are likely to be on donors’ minds with respect to charitable giving followed by a discussion of some of the essential processes by which Washington works.

Donors' Concerns

Income Tax – Restoration of the previous 39.6% top tax rate or adjustments to tax brackets would increase income taxes for many taxpayers – especially those with higher incomes. Donors might be inclined to curtail their giving if they become concerned about an increase in their income tax bill. Conversely, higher income tax rates would have the positive effect of increasing the value of the charitable deduction and, therefore, reducing the donor's after-tax cost of giving. A careful explanation of the increased tax savings and lowered after-tax cost could encourage giving. But, as a potential complication, there has been discussion of capping the value of the charitable deduction, perhaps at 28% for high bracket taxpayers.

Capital Gains Tax – If long-term capital gains become more highly taxed, the advantages of a contribution of appreciated property will increase. Gifts of appreciated assets provide a double tax benefit: a charitable deduction for the fair market value of the asset and avoidance of the capital gain tax that would have been due if the asset had been sold. Suggesting contributions of highly appreciated assets and pointing out the tax advantages could help donors overcome reluctance to consider a contribution. Remember that even non-itemizers can avoid capital gains tax by contributing appreciated property.

Estate Tax – Changes to the estate tax seem inevitable. Lowering the estate tax exemption would expose many more donors to the estate tax, perhaps at a tax rate higher than the highest income tax rate. Reminding donors that there is an unlimited charitable deduction that reduces the estate tax and showing them the substantial income tax and estate tax benefits of testamentary contributions of qualified retirement plans would be in order. For certain select donors, a conversation about the gift and estate tax savings and other benefits of charitable lead trusts could be productive.

Qualified Charitable Distributions – For donors age 70½ or older, a qualified charitable distribution from an IRA remains a very tax-efficient way to give because it avoids income tax that would have been due on the amount withdrawn. Since there is no charitable deduction involved, the QCD is an incentive even for non-itemizers. The resumption of required minimum distributions for those over age 72 provides an additional incentive for donors to consider a qualified charitable distribution. Qualified charitable distributions are particularly attractive to charitable organizations because they provide current support.

Universal Charitable Deduction – For the past few years there has been growing momentum to allow all donors, not just those who itemize, to benefit from an income tax deduction for their charitable contributions. The CARES Act of 2020 introduced a modest $300 deduction for non-itemizers and temporarily increased the limit on the charitable deduction for cash contributions to 100% of AGI. Both of these incentives for charitable giving have been extended through 2021, and the deduction for non-itemizers has been increased to $600 for married filers by the Consolidated Appropriations Act, 2021.

Processes in Washington

Anticipating donor qualms, an understanding of the legislative and political processes that are likely to play out over the coming months may be useful. It is not possible in this short article to provide a comprehensive civics lesson, but a review of the fundamental structure of the Federal government and certain legislative processes can provide helpful background or perhaps fill in gaps in our own knowledge when navigating conversations with donors.

Executive Versus Legislative – The President heads the Executive Branch of the Federal government and is charged with carrying out the laws that are enacted by Congress, the Legislative Branch. The span of the Executive Branch is very broad, encompassing the departments and administrative functions of the Federal government, including the Treasury Department where the Internal Revenue Service resides, but the power of the executive is limited. With few exceptions (see Executive Orders below), the President cannot act unilaterally. Ultimately, the executive functions all report to the President, but their power is limited by the laws enacted by Congress. For instance, although the Internal Revenue Service issues regulations and other guidance interpreting and implementing the Federal tax laws, it is bound by the Internal Revenue Code, which is written by Congress.

The House and the Senate – Congress consists of 535 elected individuals divided into two bodies, the House of Representatives, and the Senate. The 435 members of the House of Representatives are apportioned based upon population with each House member representing about 750,000 people. House members serve for just two years before they must run for re-election. Two Senators represent each state, serving for six years with their terms staggered so that approximately one-third of the Senators stand for election every two years. Sometimes, for example in Georgia in 2020, both Senators stand for election at the same time due to vacancies and special elections.

117th Congress – A Congress lasts for two years. The 117th Congress began on January 3, 2021 and will conclude at the end of 2022. Each Congress starts with a blank agenda; nothing is carried forward from the previous Congress. Proposed legislation that is not acted upon before the end of the 117th Congress becomes void and will need to begin the process again in the next Congress.

Congressional Leadership – The Speaker of the House heads the House of Representatives and is elected by its members. On January 3, 2021, Representative Nancy Pelosi (D-CA) was elected Speaker of the House for the 117th Congress. The Vice President of the United States serves as the President of the Senate but casts a vote only in case of a tie and rarely attends Senate sessions. When the newly elected Senators from Georgia are seated, it is anticipated that Senator Charles Schumer (D-NY) will become Senate Majority Leader. The Speaker of the House and the Senate Majority Leader set the agendas and manage the affairs of their respective bodies, including, most importantly, determining if and when proposed legislation is considered by the body.

Congressional Committees – Much of the work of Congress is accomplished in its committees. Committee membership is assigned by the two parties, roughly equal to the balance of seats held by each party. The Democratic party has a narrow majority in the 117th Congress, so committee membership is likely to be more or less evenly balanced. Committee chairs are selected by the majority party. The Chair sets the committee agenda, which means the majority party wields significant power over the committees.

House and Senate Rules – During the first few days of the 117th Congress, each chamber will adopt its own rules governing how the body will operate, including how much time is allotted for debate before a vote must be taken (see Filibuster and Cloture below). Under certain circumstances a rule can be set aside or amended, usually by a super majority vote of the body.

Filibuster and Cloture – Although not a part of the Constitution, a “filibuster” is an attempt by a member to hold the floor in order to prevent a vote, thus blocking a legislative action. The filibuster is rare in the House because its rules impose limitations on the length of debate. Filibusters are more common in the Senate, where there are fewer limitations on debate, but a Senate filibuster can be halted if three-fifths (60) of the members vote in favor of a “cloture” motion to end debate. Senators rarely take to the floor and hold forth in a filibuster. Instead, when a Senator notifies leadership of the intention to filibuster, leadership moves on to other business, unless it is confident it can muster 60 votes in favor of cloture. The practical effect is that most legislation in the Senate requires a 60-vote margin. The Senate has changed its rules over the years (see Budget Reconciliation below), most recently in 2017 when the cloture threshold was reduced to a simple majority to end filibusters of Supreme Court nominees.

Budget Reconciliation Bill – Reconciliation is a rule that can be applied to prevent a filibuster of certain budgetary legislation. Reconciliation bills can involve spending, revenue, or the Federal debt limit, and there can be only one reconciliation bill for each of these subjects each year (a potential total of three reconciliation bills per year). The “Byrd Rule” prohibits reconciliation bills from including policy changes that are extraneous to the budget, increasing the Federal deficit after a ten-year period, or making changes to Social Security. Reconciliation bills have been used several times in recent years, including the Health Care and Education Reconciliation Act of 2010 and the Tax Cuts and Jobs Act of 2017, which allowed both of these landmark laws to pass with bare majorities on near party-line votes. Reconciliation could be used by Congress to enact some of the tax policy changes under discussion without the need for 60 votes in the Senate (see Filibuster above). Also note that the reason many of the provisions of the Tax Cuts and Jobs Act of 2017 expire at the end of 2025 is to comply with the ten-year budget-neutral requirement.

Making a Law – A bill must be drafted, introduced, debated, and passed in identical form by each chamber before it is sent to the President for signature. If the President refuses to sign the legislation, Congress can override the President's veto by a two-thirds majority vote in both chambers. In most cases, leadership refers a bill to a committee for review and recommendation. Committees may hold hearings, order studies, make changes to the proposed legislation, or simply do nothing. After a committee refers a bill to the body, leadership controls when or if the matter is brought to the floor for action. In most cases, members can propose amendments to the bill during debate on the floor.

Executive Orders – The President can issue Executive Orders covering many operations of the Federal government, but there are limitations. Although the Constitution gives the President broad executive and enforcement authority and Congress has delegated certain discretionary power to the President, an Executive Order is not a substitute for legislation. Executive Orders are subject to judicial review and can be overturned if the Court finds that the order lacks support by statute or the Constitution. Executive Orders remain in force until canceled. Typically, a new president reviews existing Executive Orders during the first few weeks in office. It is expected that President Biden will review and cancel some of the Executive Orders issued by President Trump.

Whatever the future may bring, we know that donors are motivated to give by their passion for the organization's mission. Even if political events and news about legislative initiatives discourages some donors, good gift planning can help maintain and even increase the quality and quantity of their giving.

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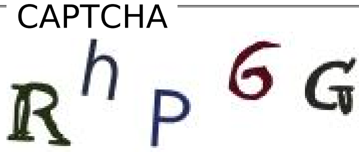

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