



ASK PAUL HOOD

March 2022

Greetings in the Lord!!! I always find Lent, which too many believe to be an austere, somewhat somber experience, as a wonderful time to reflect on what's truly important. Like Eternal Salvation. I've always welcomed Lent as a time to reflect, refocus and recharge.

Our questions today provide an excellent opportunity to address several different common questions.

If I was leaving my estate to my family, but I wanted to make a gift to a charity like the Sisters of St. Frances of Sylvania OH in my estate plan, which is better to give to charity vs. my family, a life insurance policy or my 401(k) plan, if they are the same value? Please use \$100,000 as an example.

Well, it depends in part on whether or not your estate is subject to the federal estate tax. However, given the amount that every citizen can pass free of the federal estate tax in 2022 is \$12,060,000, very few (0.4%) have enough wealth to worry about the federal estate tax, so I'll assume that you (like me) don't have to worry about the federal estate tax. But the income tax? That's an entirely different kettle of fish!

Suppose that your options for a \$100,000 charitable gift are a transfer out of your 401(k) or regular IRA or a life insurance policy. All other things being equal, if you're thinking about making a sizable estate gift to a worthy charity like our dear Sisters of St. Frances of Sylvania OH, **always** make it out of an **income taxable account**, like your 401(k) or a regular IRA, before using something like **income tax exempt property** like life insurance or other property (because inheritances are exempt from income tax).

Why? If you give your \$100,000 life insurance proceeds to your family, they'll get the **whole** \$100,000 because, with a few exceptions not relevant here, life insurance proceeds are **exempt** from income tax when the policy beneficiary(ies) receives them, which is the **exact same answer** if you gave those insurance proceeds to the Sisters of St. Francis of Sylvania OH, because the Sisters are income tax exempt. So both your family and the Sisters will **pay zero income tax** on receipt of the life insurance proceeds.

However, if you leave your 401(k) or a regular IRA to your **family**, they're going to have to pay income tax at their marginal income tax rates, so if their marginal tax rate is 25% on \$100,000, **\$25,000 is going to Uncle Sam** (and probably some extra for state income tax too), so **the family recipients will only net \$75,000**. But if you give \$100,000 out of your 401(k) or a regular IRA to the Sisters of St. Francis of Sylvania OH, they'll get and be able to use the **entire \$100,000**. Why, because the Sisters of St. Francis of Sylvania OH are **exempt** from income tax as a qualified IRC Sec. 501(c)(3) public charity.

So, to summarize, if you give your life insurance to your family, they'll get the **whole \$100,000**, but if you gave your 401(k) or regular IRA to your family, they'll **only net \$75,000**. However, you can ensure that **both** \$100,000 transfers go **free of income tax** by giving the life insurance to your family and your 401(k) or regular IRA to the Sisters. So **each set of recipients** get the whole \$100,000 apiece.

What is the best way to keep track of in-kind gifts to charity?

I interpret your reference to "in-kind gifts to charity" to mean all gifts to charity **except** for gifts of cash.

To be honest, just about all in-kind gifts to charity of tangible personal property like clothes and books generate paper receipts (which really are required by the IRS to substantiate charitable gifts, and, in fact, see the next paragraph about the IRS rules, which I took verbatim from the IRS website). Unfortunately, unless you're one of those fastidious and efficient souls (and I'm not one) who diligently and consistently scans and properly files the receipt for quick availability at tax time, how do you keep up with all of the receipts for charitable gifts made during a taxable year?

I learned a system intended for use during the research and information-gathering phase of writing a book called the "Pile-It" system years ago from the late Dan Poynter, who was perhaps the nation's leading expert on self-publishing. Basically, it's a common sense, low-tech system where the first step is to carve out a particular place, whether it's a file folder, binder, box, etc. for all material pertaining to your book, and then requires you simply consistently and contemporaneously – ie, immediately – 'pile-it' in there.

I later applied the "Pile-It" system to my charitable giving one year when I had made a bunch of in-kind gifts to charity and had a lot of receipts from the charities. From these, I was able to pull the substantiation necessary to prove a charitable deduction for charitable gifts of \$250 or more (and taxpayers bear the burden of proving entitlement to any deduction), what follows comes directly from the IRS.gov website:

The written acknowledgment required to substantiate a charitable contribution of \$250 or more must contain the following information:

- *Name of the organization;*
- *Amount of cash contribution;*
- *Description (but not value) of non-cash contribution;*
- *Statement that no goods or services were provided by the organization, if that is the case;*
- *Description and good faith estimate of the value of goods or services, if any, that organization provided in return for the contribution; and*

- *Statement that goods or services, if any, that the organization provided in return for the contribution consisted entirely of intangible religious benefits, if that was the case.*

In addition, a donor may claim a deduction for contributions of cash, check, or other monetary gifts only if the donor maintains certain written records.

Clearly, the more organized you are, you'll be better off and less stressed later on. But, if you're as busy as I am, the organizational system **must** be **simple** and **easy**. Frankly, with inexpensive scanners today and computers, smartphones and tablets, there's just no excuse for not maintaining the receipts (including all deductible items, i.e., not just those substantiating charitable deductions) electronically. But if you're not ready to take the electronic leap of faith, the "Pile-It" method can be very effective if you actually follow it.

Q 4. As we see inflation continue to rise in 2022, how is giving to charity still very important?

Wow. Great question. Unfortunately, the space allotted to my column is woefully insufficient to give a complete and proper answer to this question, so a few bullet points are going to have to suffice for now.

For starters, until about a year ago, according to official government statistics, we'd been in an extended period of time (just about back to the beginning of 1980) of so-called low inflation. However, during the last year, inflation has taken off rampantly (according to www.ycharts.com, the current United States inflation rate in January 2022 is 7.48%) versus where it'd been for most of the past 40 years. In part, this rapid increase in the inflation rate gave rise to the 5.9% cost-of-living-adjustment (COLA) to Social Security benefits at the end of 2021, which was the largest COLA since 1982-40 years ago and exceeded the sum of the COLAs for the three preceding years.

I purposely didn't quote an "official government source" for inflation. Why? Because about the only thing I really learned during my one year of graduate school before going to law school was the following adage that I've believed with every fiber of my being ever since I first heard it, and I've used it in just about every aspect of my legal and consulting career: ***If you torture the numbers long enough, they'll confess to whatever you want them to say.***

I have long believed that the official government statistics **understated** the actual inflation rates because the public perceives that things are much better during periods of **low inflation** than during periods of **high inflation**, so I have long suspected that elected officials have gently pressured the Federal Reserve and other government agencies that promulgate official inflation statistics to minimize and possibly understate the official inflation statistics, in an application of the above-quoted adage that I learned in graduate school.

Having been raised in a common sense way in a small town, I tend to more trust my gut and measure the economy in general and inflation in particular by what things actually are costing **me** in real time, instead of simply buying the government line about inflation. And in my opinion, actual inflation has been **higher** than the official government reports of inflation for a very long time.

Unfortunately, while the 2022 COLA was no doubt welcome news to Social Security recipients, many of whom are on fixed incomes that too often are limited to their Social Security benefits, a quick comparison of the January 2022 www.ycharts.com inflation rate (7.48%) to the 2022 COLA (5.9) quickly indicates that Social Security recipients are **losing ground**, i.e., prices are increasing at a greater rate than their Social Security benefits. This is bad news for charitable giving for those people, simply because there's less excess money available.

Despite the spike in inflation that occurred during 2021, the stock market, though more erratic and volatile than it'd been for a long time, still showed significant gains and remains in all-time high rarefied territory. But acceptable Price-to-Earnings Ratios (P/E Ratios) for publicly traded stocks continue to increase, which is troubling and surely can't continue. If actual inflation continues at the current rate, will the stock market continue to increase in value? At some point, real return must include some regular periodic distribution of earnings, i.e., dividends, so that your total return isn't merely appreciation in stock value. However, for those who have marketable securities portfolios while values continue to increase, inflation actually enhance the value of the charitable gift of appreciated securities.

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If you have any questions about estate planning that you'd like me to answer here or want to talk about how you might use your time, talent, or treasure to benefit the Sisters of St. Francis of Sylvania OH, e-mail Eileen M. Kerner, Director of Congregational Advancement, at ekerner@sistersosf.org or call Eileen at 419.824.3625.