FOUNDATION**SOURCE**

Philanthropy in Transition

NAVIGATING THE SHIFTING TAX LANDSCAPE

In September 2021, we sat down with leading experts in tax exempt organizations and philanthropy to have a timely conversation about pending tax proposals and the impact they may have on private foundations and donor-advised funds (DAFs). We discussed three tax proposals, including two pieces of legislation, put forth that have the potential to reshape the philanthropic landscape:

- **The Biden Plan**, known as the Green Book and the potential impact on charitable giving
- **The House Ways and Means Proposal** with estate tax, income tax and IRA changes
- **The Accelerating Charitable Efforts (ACE) Act** and what it means for foundations and DAFs

Here's a summary of the three proposals. For more information, watch the replay of *Philanthropy in Transition: Navigating the Shifting Tax Landscape.*

1 The Biden Plan, Known as the Green Book

- Increased income tax rates
  - Individuals to 39.6% (ordinary) and long-term capital gains (LTCG) and dividends for taxpayers with adjusted gross income (AGI) of more than $1 million
  - Increase in corporate tax rate from 21% to 28%
- Gifts, bequests, trust distributions as capital gains realization events
  - Loss of capital gains "step-up"
  - Gifts and certain trust distributions as realization events
  - 90-year trust realization event
  - $1 million exclusion

THE POTENTIAL IMPACT ON CHARITABLE GIVING

- The top marginal individual income tax rate would increase from 37% to 39.6% for taxable income in excess of the top bracket threshold—as tax rates rise, the value of itemized deductions also rises.
- For taxpayers with AGI of more than $1 million, long-term capital gains and qualified dividends tax rate would increase to match the proposed ordinary income tax rate. For a taxpayer with income in excess of $1 million, rates would jump from 20% (or really 23.8%, including the net investment income tax) to 39.6% (or really 43.4%, including the net investment income tax).

2 The House Ways and Means Proposal

- Return of proposed estate tax changes instead of capital gains tax
  - Accelerate "sunset" of current estate tax levels (effectively dropping in half from $11.7 million to about $5.5 million)
  - No mention of loss of "step-up" or gifts/distributions as realization events
- Income tax changes
  - Highest personal rate to 39.6%; capital gains rate to 25%
  - 3% surcharge for income over $5 million
  - Corporate rate to 26.5%
  - Changes to certain cross-border tax rates and rules
- Changes to grantor trusts (pulled into taxable estate)
- IRA changes
  - Increased required minimum distribution for high-income taxpayers with large balances ($10 million plus, and can never stay over $20 million)
- In terms of charitable giving, like with the Green Book proposals, higher taxes lead to a more valuable deduction
- Estate taxes
  - Brings a lot more people into the estate tax net
  - Eliminates a lot of common planning for reducing estates (e.g. grantor trust planning)
  - Eliminates valuation discounts
  - Makes gifts to charity and certain charitable lead trusts far more valuable

3 The ACE Act

Co-sponsored by Senators Angus King (I-ME) and Chuck Grassley (R-IA)

- Private foundations would no longer be allowed to count grants to DAFs towards meeting the annual minimum distribution of income requirement (MDR) if the private foundation retains advisory privileges.
  - **Note:** This is not a concern for a terminating foundation or for a foundation that grants to a DAF account over which the foundation has not retained advisory privileges.
- Private foundations would no longer be able to count administrative expenses (for example, payroll, travel, and other similar expenses) of certain insiders towards meeting the MDR.
  - **Note:** This limitation is targeted only at insiders who are family members of a foundation's substantial contributors. The payroll and expenses of non-family members would still count towards satisfying the MDR.
  - **Note:** This rule would still allow foundations to pay salary to and cover the expenses of the targeted insiders—these expenditures would not be taxable expenditures. However, such expenditures would not count towards satisfying the MDR.
- Private foundations that choose to sunset within 25 years would pay no excise tax. However, if such a foundation makes prohibited grants to related foundations, or it opts not to sunset at the point in the future when it is required to do so (after not paying excise taxes for 25 years), the foundation would have to pay the IRS any taxes it saved because of this tax break.
- Private foundations would pay no excise tax in any year in which it satisfies a voluntary 7% payout requirement determined by reference to the value of the foundation's assets on the first day of the tax year.
- A private foundation that uses DAFs to avoid "tipping" of the public charity status of a donee may no longer be able to do so, as distributions from DAFs will be treated effectively as distributions from the private foundation.

THE POTENTIAL IMPACT ON DAFS

- For non-community foundation DAFs, generally, the legislation would allow a current charitable deduction for cash or marketable security gifts to a DAF only if such gifts are distributed by the DAF to charities within 15 years of the first contribution to the fund and all advisory privileges terminate.
- There are narrow exceptions to these rules for DAFs that are set up at community foundations, but the exceptions apply only for amounts donated up to $1 million or there is a 5% MDR on the individual qualifying community foundation donor-advised fund.

HAVE A QUESTION?

Call 800.839.0054 or send us an email at info@foundationsource.com.

www.foundationsource.com

©2023 Foundation Source Philanthropic Services Inc.
All rights reserved. v0123

The information provided in this document is for general information purposes only, and does not constitute legal, tax or investment advice.

FOUNDATIONSOURCE