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Gifts of Appreciated Securities in Today's Economy

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We noted 2019's phenomenal stock market performance in the February 2020 edition of PG Calc's eRate newsletter. The S&P 500 Price index returned 33.07% in 2019 if you include dividend reinvestment. Stock in Axsome Therapeutics, the maker of the common anti-depressant Wellbutrin, gained an astounding 3,578%!

Headlines in the financial press range from "Heading for A Slowdown: 2020 U.S. Economic Outlook" to "U.S. Economy Heads Into 2020 With Steady Growth." In these uncertain times, both statements can be true. Forbes magazine concluded, "…whether or not we see a crash in 2020 is impossible to say, but there is a risk that market returns, especially for the U.S., are a lot less good for the next few years, than we've seen in recent history." Ultimately, it doesn't matter where any of us think the economy is heading, rather, we need to know what our donors think.

Why Should I Care how the Stock Market Performs?

While donors have watched their investments grow, if they sell these appreciated securities to lock in gains, they will trigger realization of capital gain, eroding their net investment returns. Transferring these appreciated securities directly to charity yields a double tax benefit. Donors avoid tax on the capital gain and receive an income tax charitable deduction for the fair market value of the stock. The tax savings can make such a gift easy and affordable. The full value of gifts of highly appreciated securities support your mission and make a tax-smart gift.

Besides the tax benefits of donating securities, making gifts of assets shifts the philanthropic discussion. Some say when you are asking for cash, you are asking small. When you are asking for assets, you are asking big. Academic research demonstrates that charities actively soliciting gifts of assets raise more money than charities that focus on gifts of cash. Why? There are several theories: Cash is fungible, one dollar is the same as any other dollar. Gifts of assets are more personal. Assets represent wealth accumulated over time with hard work. Another reason may be that the majority of a high net worth donor's wealth is in their assets (securities, real estate, business interests) not in cash. Assets may be perceived as more plentiful and easier to part with.

What Is Capital Gains Tax?

For basic review, let's say that Sue owns stock in Proctor and Gamble, the consumer products giant, worth $250,000. She paid $70,000 for her Proctor and Gamble stock. Therefore, her stock has grown in value by $180,000 over time. If she sells the stock now, she will have to report $180,000 in realized long-term capital gains income. ($250,000 - $70,000) How much tax is due on the $180,000 of capital gain income depends on the applicable capital gain rate. A taxpayer's filing status and level of income determine the applicable capital gain tax rate. The higher one's income, the higher the capital gains tax rate. The capital gain tax rate can be as little as 0% for low income taxpayers, 15%, 20%, or as much as 23.8% for the highest income earners. (The additional 3.8% tax is actually a Medicare surtax, but effectively increases the capital gains tax rate.)

Let's assume Sue has a high income and her filing status puts her in the 23.8% capital gains tax bracket. Assuming the facts above, on the sale of her Proctor and Gamble stock, she will report $180,000 of capital gains income on her Form 1040. She will owe a capital gain tax of $42,840 (23.8% of $180,000) from the sale. The stock was worth $250,000 at its sale, but Sue's after-tax net proceeds will be only $207,160. These calculations are based on Federal capital gain tax only. It doesn't include any tax on the realized gains by the state in which Sue resides. (AL, FL, NV, NH, SD, TN, TX, WA, and WY have no state income tax and therefore no state capital gain tax.) The table below summarizes the tax implications of the sale of Sue's stock.

	Sale of Sue's Stock
Cost basis	$70,000
Fair Market Value	$250,000
Capital gain realized ($250,000-$70,000)	$180,000
Capital gain tax due (23.8% of $180,000)	$42,840
Net left for Sue	$207,160

Why Should Sue Make a Gift of Securities to Charity?

Let's further assume Sue wants to make a gift to your charity using her highly appreciated stock portfolio. If Sue were to sell the securities valued at $250,000 described above, pay the tax, and donate her net proceeds to charity, her gift to charity would only be $207,160.

There's a tax efficient way to save Sue taxes and maximize the gift to charity. Sue could donate $250,000 of Proctor and Gamble stock to charity. Charity would immediately sell the stock and, because the charity is tax-exempt, owe nothing in tax and realize the full net proceeds of the sale. The gift of stock increases the charitable gift by the amount of capital gains tax that would otherwise be due.

Sue enjoys attractive tax benefits in this scenario as well. The gift of Proctor and Gamble stock immediately saves her $42,840 of capital gains tax that would otherwise be due. Sue is also entitled to an income tax charitable deduction for the fair market value of the donated stock. Assuming the $250,000 valuation, and if Sue is in the 37% tax bracket, she will enjoy income tax savings of $92,500 if her deduction is not subject to limitations.

The table below illustrates the income and capital gains tax savings of a gift of Sue's Proctor and Gamble stock to charity.

	Charitable Gift of Sue's Stock
Cost basis	$70,000
Fair Market Value	$250,000
Income Tax savings ($250,000*37%)	$92,500
Capital gain tax savings (23.8% * $180,000)	$42,840
Total Tax Savings	$135,340
Net Cost of $250,000 Gift ($250,000-$135,540)	$114,660

Conclusion

The stock market's record-setting highs make gifts of securities particularly attractive in early 2020. Donors tend to make larger gifts of assets like securities instead of cash. This is an opportune time to market these gifts, and to discuss the capital gains tax and income tax savings associated with gifts of appreciated securities. The crystal ball of the economy is opaque, but 2020 could be a prosperous year for non-profits from gifts of assets.