5 Mistakes to Avoid When You Give to Charity

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Charitable giving provides benefits for you and the non-profit organization receiving the gift.

How do you know if you're currently giving in the most beneficial way?

Avoid these 5 mistakes so you can give more and make a greater impact on the organizations and causes you support.

1. Not Keeping Accurate Records for Gifts

In 2012 the Tax Court upheld a decision by the IRS to deny a taxpayer's charitable deduction for $22,517 in contributions made to his church. The reason was that he did not receive the proper acknowledgement for his contributions in a timely manner.

Having voided checks or a simple receipt may not be sufficient to support your charitable deduction. For gifts under $250, a cancelled check or bank statement is enough. For larger gifts, the charity must provide a contemporaneous written receipt or letter that states the name of the organization, the date, donation amount, and whether goods or services were given to you as a result of the gift.

In the court case mentioned above, the taxpayer went back to his church to obtain the proper acknowledgement of his contributions. However, the court would not accept the second acknowledgement because it did not meet the contemporaneous written acknowledgement requirement. The IRS defines contemporaneous as the earlier of the date of filing or the extended due date, including extensions of the tax return. If you have not filed your tax return for last year you still have time to obtain a proper written acknowledgement for contributions you made to a charity.

2. Giving Cash vs. Appreciated Investments

When you receive a donation request in the mail or over the telephone, do you pull out your checkbook, credit card, or debit card to make a contribution? By doing this you could be giving up an additional tax benefit. Instead of writing a check, you could donate an appreciated stock, mutual fund or other appreciated asset and receive two tax benefits with a single gift. When you donate an appreciated investment you not only receive a deduction for the gift, but you also avoid the capital gains taxes you would have paid by selling the investment.

For example, if you donate $10,000 in cash to your favorite charity you potentially receive a charitable deduction for $10,000. However, by donating a stock valued at $10,000 that was originally purchased for $7,000, you receive a charitable deduction for the $10,000 full market value of the stock and also avoid capital gains tax on the $3,000 that the stock appreciated since purchase. This could save you up to 20% of the capital gain.

Why not save on both income and capital gains taxes with the same gift?

What if you don't want to donate the stock because you like how it has performed and you plan on owning it for a long time? In this case, it still makes sense to donate the stock and use the cash allotted for the donation to re-purchase the stock. This way you avoid the current capital gain on the stock and establish a higher cost basis for it, thus reducing your future capital gain.

3. Donating an Investment Held Less Than One Year, or With a Loss

As we stated in mistake #2, donating an appreciated investment, such as a stock or mutual funds, can be a great way to save twice on your taxes with just one gift. However, you must have held the investment for a full year in order to deduct the fair market value. If you have not held the investment for a year, you can only deduct what you paid for it. In the previous example where you purchased a stock for $7,000 and donated it when it was worth $10,000, if you had owned the stock for less than a year, you would only get a charitable tax deduction of $7,000.

It's also a mistake to donate an investment that has lost value. If you initially paid $12,000 for a stock that's now valued at $10,000, you'll only receive a tax deduction for the fair market value. In this situation you're better off selling the stock, realizing the capital loss for your taxes and then using the proceeds to make the charitable donation.

4. Not Using the IRA Charitable Rollover

The IRA Charitable Rollover is for individuals over the age of 70½. After nearly a decade of expirations and renewals, the IRA charitable rollover was made permanent in December 2015 as part of the Protecting Americans from Tax Hikes (PATH) Act.

If you meet this age requirement, you can make tax-free distributions of up to $100,000 from an Individual Retirement Arrangement (IRA) directly to a nonprofit organization without recognizing the distributions as taxable income. In addition, the distributions count towards your required minimum distribution for the year. Due to the fact that the rollover distributions are pre-tax dollars and are not recognized as taxable income, you do not receive a charitable tax deduction.

Making a rollover can potentially provide a number of benefits. First, by the IRA distribution to a nonprofit being excluded from taxable income, you may realize additional tax savings by avoiding or reducing the potential phase-out of your tax deductions. In addition, by having a lower federal taxable income you may save more on your taxes if you live in a state with income taxes. Lastly, if you file a simplified tax return and only use the standard deduction, you do not get a tax deduction for the amount you donate to nonprofits. However, the IRA Charitable Rollover allows you to reap the benefit of a lower taxable income, even if you do not itemize your deductions.

5. Failing to Focus Your Donations

Diversifying your investment portfolio can be a good thing, but diversifying your charitable giving can lead to unfocused donations that create little impact. When you give to support an organization or cause, you hope to make a difference. While a number of small donations can add up, have you considered what type of difference you want to make?

Rather than dividing your charitable donations to a variety of nonprofits, think about the type of change you are passionate about and focus your donations on a single or a few charitable organizations. For example, if you care deeply about children, you may want to change lives by supporting a child in need somewhere in the world, give a child the gift of reading by aiding a children's literacy program, or give to your local children's hospital.

Instead of giving money here, there and everywhere, take time to think and plan—and then give. You'll make a greater impact on the organizations or causes you support and receive more satisfaction from the change you're making in our world.

Start Mapping Out Your Charitable Giving Strategy

Meet with a Hammond Iles Wealth Advisor to help you achieve your charitable vision. Contact (800) 416-1655, or clientcare@hammondiles.com today!