PBS Episode 139 Charitable Giving with John Nersesian of PIMCO

Patti Brennan: Hi, everybody. Welcome to "The Patti Brennan Show."

Whether you have $20 or $20 million, this show is for those of you who want to protect, grow, and use your assets to live your very best lives. Maybe even improve the lives of people or charities that you care about.

Joining me today is John Nersesian. John is a very dear friend of the firm. He's incredibly smart. He is head of advisor education at PIMCO. If you were listening to the prior podcast, we talked about year-end planning strategies. Stop this episode right away. Go back to that one. It was packed with great ideas.

As we were talking, we were talking about the aspect of charitable giving. Many people are already giving to charity. What John's idea is, his approach is, "Let's do what you're doing already and really add some bang for the buck."

John, welcome to the show.

John Nersesian: Thanks so much, Patti. I love being here and love this topic, so thanks for putting the two together.

Patti: Giving is really an interesting topic because, what a lot of people don't realize is, there's a lot of it going on, isn't there?

John: Gosh, the numbers last year were record-breaking. $499 billion, to be exact, was given to charity. That's just here in the US. There are several reasons behind that.

Number one, we all feel wealthier. Our homes have gone up in value, our portfolios have been rising over a couple of years. We want to share that success with those who are less fortunate.

Another reason that charitable giving continues to be of interest to families across the US, is this idea that a charitable gift is one of the few itemized deductions that are still available in the tax code.

So, part of it is doing well, obviously, for those that we care about. Part of it is maybe deriving a personal benefit as well.

Patti: One hundred percent.

Ultimately, when you think about the tax system, it is a form of charity. It's just you're giving the money to the government, and then they're doling it out.

John: [laughs] Yeah, right.

Patti: The way that the code works is you get to choose who's going to receive your money, rather than leave it to Uncle Sam. That's an interesting incentive and the motivations that go behind the giving.

I love your guide. PIMCO has a great guide. We're going to put it on our website because it's that good.

John: Thanks.

Patti: It's got lots of tidbits, people don't really know these things. If you don't know about it, you may be trying to take deductions that you're probably not allowed to take.

John: Listen, the intent is all great. I get it. We're all philanthropic, we all care about others. We're all trying to do well for those things that we care about or that are meaningful to us. It's not necessarily about giving away more money, it's about making the giving that we're already doing more impactful.

There's a term that I love to use -- I hope you might agree with this -- it's the idea that many of us give reactively. One of our relatives calls us up and says, "I'm doing this fundraiser for a noble cause. Will you support me?" Of course, we do.

What I'm addressing is this idea of giving intentionally, as opposed to reactively. Have I thought about how much I want to give away this year? Who I want to give it to? What purposes do I want to support? When do I want to give it? What amounts do I want to give? Let's be a little bit more intentional with the giving that we're doing as opposed to reactive.

Patti: I love that, because, again, we're all so busy, I would probably be on the reactive side.

John: Oh, we all are.

Patti: I get a lot of phone calls. I get a lot of this, "Donate to this, donate to that." "Get these T-shirts," whatever the case may be.

To be much more selective and understanding, who do we want to give to? Why are we giving it? What do we want to support? What are the values? Things of that nature it's important.

As we were talking about this, John, and laying out the outline for this podcast, we talked about it within the framework of, what do you give? How do you give? When do you give? The intentional versus the reactive, and what are the tools?

John: Yeah, I love it.

Patti: Let's talk tactical. Let's start at the top. What do you give?

John: The easiest way for us to give, I get convenience matters, is to write a check. There's a charity I want to support. I either put cash into the plate or I write a check to whatever the intended charity is. Once again, beneficial, we're supporting this organization that we want to receive or benefit from our philanthropy. It may not be the best way to give.

Keep in mind, Patti, something that'll be surprising to many of your viewers. We automatically assume that charitable giving is automatically a deductible, tax-saving activity. It's not. We only get a tax benefit when we itemize our deductions.

If I'm giving to charity, whether it's property, cash, or any other form, I don't get a tax benefit, I don't derive one unless I'm itemizing my deductions. Maybe a better way to give is not to give cash but to give appreciated property.

When I give the 100 shares of Apple stock that's way up in value, or I give my second home to a charity, or the automobile, or whatever the asset might be, giving property allows me to bunch my deductions in a single calendar year for maximum benefit and to avoid the capital gain that I would otherwise pay if and when I sold the asset.

Charity benefits either way. They benefit to a greater degree, and I derive a greater benefit if I give in that manner.

Patti: I love it when we were talking about this over the phone, you asked me a question. How would you like to be able to increase your deduction by 53 percent for the same amount of money you're giving to the charity? I'm like, "Wait a minute, John. Where are you going with this thing?"

John: [laughs]

Patti: It was awesome.

John: It sounded like a trick, didn't it?

Patti: It did. When we looked at the math that you provided for us, it was exactly that. Let's walk people through that example. I'll put it on the podcast.

John: I love it. I'll describe it conceptually. It ties into the concept that we were just talking about. I decided that I want to make a $100,000 pledge to my favorite charity. They approach me. They solicit me. It's a cause that I believe in. I want to support them.

My initial inclination might be to write them a check or maybe, over the next four years, I give them $25,000 a year. I fulfilled the pledge. They benefit. I benefit as well. In giving sporadically like that, a smaller amount each year, what happens is I get a deduction for that giving but only to the extent that it exceeds my standard deduction.

The standard deduction today is $27,700. If the gift that I've made inclusive of my SOL tax deduction and any other that I get, if that exceeds it, I'm going to take the larger number on my tax return. In this hypothetical example, it does.

The total deduction available to the client was about $140,000 by giving a smaller amount each year with regularity. What if I got the great advice of my great financial advisor?

I said, "Look, give the same $100,000 to the same charity that you want to support, but let's give it in a different manner. Let's bunch our deductions by giving the full $100,000 in one year.

You can either give the money upfront to the charity or maybe you deposit it in your donor-advised fund to get that full deduction upfront and dole the money out from there over the next four years."

In doing so, in year number one, I get a huge deduction for the charitable gift that I've made. In the following three years, I now relied upon the standard deduction, which is a little bit higher.

The total deduction in that example, Patti, is $193,000. The difference between the two, the same $100,000 given to the same charity by the same individual, produced an incremental deduction of $53,000. That's a win-win in my book.

Patti: That's real money. That is real money.

John: Yeah, I think so.

Patti: It's fantastic. The charity still benefited. You got your deduction upfront, and you took advantage of the tax code as it is written. This is all legit. It's all legal. It's how and when you give.

John: It's funny. You said something during one of our earlier calls or podcasts that impressed me which is, "John, so many of our clients come to us for help and guidance that they need at a certain point in their lives. They're making a substantial charitable gift. They're retiring. They're educating a kid. They're doing something.

"It's the first time through for that family. So, they want and need help. What they need to realize is that you've had these conversations with so many clients over the years. You've seen this before. You know how it works. You understand the tax code. You understand financial planning, and you can help these people navigate their way through the complexities of money." It's good stuff.

Patti: It is important. They get to do it once. If they continue the current strategy, they're going along. It's one of those things, John, I tell clients all the time. If you don't know about this stuff, you're not going to do it. Uncle Sam is not going to knock on your door and say, "Oh, by the way, John, here's another $53,000 in deductions."

John: "You overpaid me because you were unaware of the rules."

Patti: Right, and everybody's going to be different in terms of what rules apply to them.

Let's understand what's important to you, including the charities that are important, whether that's part of your values. It may not even be now; it may be later. We talked earlier about the idea of using required minimum distributions. That's later in life. Someone 73, 75 years old.

John: I love it.

Patti: You got to take money out of the IRA or the 401(k). Why not just, if you're already charitably inclined, go ahead and send some of that money over to the charity of your choice.

John: It's combining two separate activities into one that produces a greater benefit.

To your point Patti, I'm 75 years old and I am forced to take RMDs from my retirement account. The government requires me to do that, and I must pay tax on those distributions. I may be turning around at other points in the year and writing a check to charity, separately, for which I'm not receiving a deduction.

If I took Patti's advice and I put the two together, don't take the income, pay tax on it, and write a check to charity. What if I used that direct distribution to my charity? I avoid income tax recognition and satisfy my RMD in the process. Really smart idea.

Patti: And you still get your standard deduction.

John: Of course, I still get the 27-7 if I file a joint tax return.

Patti: It's a real multiplier effect. This is what we want to do. Understanding how to use the rules as they are today.

John: By the way, one of the things you haven't mentioned yet which is great, you're not trying to convince me to give away more money. You're saying, "John you've already figured out the charities or the causes that are most important to you. Let's help you produce a greater outcome from the charitable giving that you're already engaged in." I like that.

Patti: Right, 100 percent.

We were talking about this, and it was interesting because we talked about the things to give and the things that are deductible. What a lot of people don't realize is there are some things that people might be deducting that really aren't legit.

John: You mean my country club dues are not a charitable gift?

Patti: Sorry, John.

John: [laughs] Oh gosh, I'm going to have to redo my tax return.

Patti: OK, it still might not be a non-profit.

John: They're not making any money if that matters. Every year I get another bill saying, "Wait a minute, we fell short this year, will you provide additional income?" I get your point.

Patti: What about the table? You go to a fundraiser; you buy a table. A lot of people think that's tax deductible.

John: The charity derives a benefit, which is nice, I don't know what they're paying the organization, maybe it's being donated by the sponsoring entity or venue where it's being held. I love it that the charity's deriving some benefit, but I must be careful. I don't necessarily derive a personal tax deduction because I'm receiving something of value.

A true charitable gift is one that we are making with intent to support the charity, not to derive any personal benefit. If I buy an auction item at a charitable fundraiser, I don't get a deduction for that purchase. If I buy a table that me and my friends go to and we enjoy a meal of a certain economic value, I don't get anything for that. There's no deduction provided.

Patti: Those Phillies tickets are not deductible, John?

John: Unfortunately, not.

Patti: Bummer.

John: Why would you want to go see the Phillies? Are they doing any good this year? Are they in the playoffs?

Patti: Are you kidding me, John? We are going to the World Series my friend.

John: All right.

Patti: You just wait and see.

John: October 10th, that's the date. I'll come back in November. The Phillies do look pretty good this year.

Patti: They do look good.

John: I'm a Cubs fan, I'm from Chicago.

Patti: Yeah, you and Bernadette. "You and da Bears," as Bernadette would say.

All right, so back to this. In terms of other types of things, you mentioned cars. I thought that was interesting because how often do we trade stuff in?

John: The appeal of giving a car, or boat, or a home, or something like that, a larger personal item, it's a convenience factor. I can write a check which is very convenient, but I know that the benefits are not maybe as large as others I may derive.

I know that giving appreciated property is, in many instances, the best way for me to fulfill my charitable giving. "I'm going to give $100,000 to my church or synagogue." Giving away $100,000 of stock that I paid $80,000 for, I avoid the capital gain, so the charity gets the benefit and I derive a benefit from it as well.

Giving away things like cars and automobiles is a convenience factor. "I don't want to take this thing into an auto dealer and get appraised on it, or them clean the car and sell it to a private buyer who maybe shows up at my house or maybe doesn't." There's a convenience factor.

Of course, my gift is going to be limited to the depreciated value of the item that I'm giving to charity, so maybe there's a benefit there.

Patti: What about these other tools that are out there, charitable remainder trusts, charitable lead trusts, some of those other things, unit trust, things of that nature. This is advanced, and yet many people who listen to this podcast are interested in advanced planning tools.

Why would we do one versus the other versus what we talked about already, doing the donor-advised fund, keeping it simple?

John: To put this in order. You know me, I like to start first with the most fundamental, see if that solves the purpose. If not, then I'll move on to something a little more complex.

Patti: Good.

John: I love the idea of direct giving. I give either cash or property to a charity that I want to support. If that doesn't get me to where I want to be, I love the donor-advised fund for the benefits that we discussed a little bit earlier. It allows me to bunch my deductions. I'm making a larger substantial gift in the year in which I benefit from it.

Patti, think about this, "I'm 65 years old. If I hypothetically retire next year, what's going to happen to my income? It's going to go down, and so any charitable giving I do in the future is going to be less advantageous because my marginal bracket is lower."

You would most likely encourage me, "John, over the next 20 years you're going to give $10,000 a year to your favorite charity. Let's put the $200,000 into your donor-advised fund today to enjoy the benefit while it's of greater value to you now, in a higher marginal bracket. Then, distribute the money later on."

Patti: With a caveat.

John: What's the caveat?

Patti: The caveat is, "Let's make sure that you don't look back and say, 'I wish I hadn't.'"

John: Patti if I need that money, I'm calling you, you do realize that I've got your cell phone number.

Patti: Oh man, everybody's got my cell phone number, my address, they're going to come and...

John: Exactly. "Patti, I gave that money away. I'm coming to live in your guest bedroom."

Patti: That's where modeling is so important. Run the numbers. Make sure that under the direst...that we go into another lost decade, rights of returns with three...Whatever the case may be, make sure you're still going to be OK.

John: I want to be OK financially knowing that these are dollars that I'm comfortable giving irrevocably.

Even just as importantly, Patti, when you encourage me or help me to embrace giving, you want to do it because it makes me feel good, there's a psychological benefit that I derive from it. I don't want to give with any sort of remorse or regret.

That's not the kind of giving that I want to be involved with. I want to give because it feels good to do so. I support the cause, it's meaningful to me, and I feel great about the support I'm providing.

Patti: By doing it and running the numbers, you do it without any certainty. We can't guarantee anything in life. You can run the numbers in such a way, look at the worst-case scenario, and see you'd still be fine. "John, you're good. Go ahead and do whatever it is that speaks to your heart."

John: I suspect each of your clients, and the number will be different for each of them, but each of your clients have a number. There is within their overall budget a component for philanthropy. A component to provide this benefit that we all derive from knowing that we've helped others.

There's a benefit of getting a better return on my portfolio. There's a benefit of lowering my taxes through some of the smart things that you encourage your clients to do. There's a benefit that I derive by providing support to others that I care about.

Everybody's got a different number. I suspect with some appropriate planning; you can help them figure that out.

Patti: 100 percent. Let's think about some of the other tools.

John: Sure.

Patti: We do the annual stuff. We do the bunching, donor-advised fund. What else?

John: All right. We can talk about split-interest vehicles, the charitable remainder trust. If your client owns a family business or your client owns some real estate properties that are highly appreciated. An asset that they want to diversify away from, but they want to avoid the capital gain tax of selling it. The charitable remainder trust is a win-win.

I put in the appreciated property. I get an upfront deduction for the money that goes in. The trust sells the asset. I have no current Income tax capital gain to report. I derive an income stream from it during the remainder of my life and my surviving spouse. Then only after I'm gone does the money ultimately go to charity.

Those characteristics may be attractive to certain types of individuals who want to derive those benefits of the tax deduction, the income stream, the avoidance of the capital gain, and some philanthropic benefit as well.

Patti: The income stream, you think about that, John. We've run some numbers, etc. Let's say that you get a five percent payout.

John: Sure.

Patti: Right? You've got this money that's in this charitable remainder trust. You're getting the five percent. Hopefully, the money's invested because it's been diversified, etc. You're going to go through up years and down years, right? That five percent is based on the market value each year.

John: Correct.

Patti: That's got to be included as part of your planning. It's good news and it's bad news, right? It's one thing. It's not a pension per se. It is an interesting way of deriving income from your generosity.

John: That's why they call them split-interest vehicles, because there are two benefits that are being split or divided. There's the remainder that goes to charity, but it goes after my demise.

Then there's the income stream that I benefit from while I'm still alive. That seems to fit many financial situations. Particularly, those of us who are getting up in years, maybe we're retired. We need some income replacement vehicle because we're no longer working and drawing a salary.

Patti: The amount of the upfront tax deduction is formula-based.

John: It is. It's not 100 percent of what I put in, and you probably can guess why. The charity doesn't get the money right now. If I give a direct gift to by writing a check to my church or favorite charity, I'm going to get an immediate deduction for the fair market value because the charity is deriving the benefit today.

In this instance, the charity doesn't get the benefit for many years to come. Therefore, I'm not getting full value for that charitable deduction. It's limited or reduced by a certain degree.

Patti: There are limitations in terms of your adjusted gross income.

John: There are.

Patti: We could get into the weeds on this...

John: We're not going to. [laughs]

Patti: ...but it's a powerful, powerful tool. Now, how does the remainder trust compare to the lead trust?

John: The lead trust works a little bit differently. Let's say I want to start a scholarship program to support caddies at my local golf club, or underprivileged children in the inner cities of Chicago, and I want to provide scholarship dollars for them. What I have now is a need not to provide a remainderman later to the charity, but a current income stream to support the charitable cause.

Maybe I've endowed a church in Armenia, and I need a $100,000 a year to run the thing. That's where the CLT comes in. It's the same premise of splitting the benefits, the income benefit, and the remainder benefit, but it works in the opposite fashion.

The charity gets the income during the term of the trust, and then the individual's heirs receive the remainderman beneficiary upon their demise. I create this charitable lead trust, my church or my favorite charity gets the income along the way, and then my kids get the remaindermen that's left over when I'm no longer around.

Patti: When they receive it, it is not part of your taxable estate.

John: That's correct.

Patti: That's a win-win-win, I would think, right?

John: I love the fact that you're looking at charitable giving as not just a tool to achieve our philanthropic objectives or produce an income tax benefit today, but it's part of the estate planning process.

As you pointed out, "Look, when I'm gone, there are three places I can leave my money." I can leave it to the government -- Uncle Sam can get a big chunk of it -- maybe I don't want that to happen. I can leave it to my children, I certainly want to take advantage of the tools that allow me to maybe direct more of the money that way. I can leave it to the charities that I care about.

We should think about what we're going to leave behind, how we're going to be remembered, the impact that we can have on others, both while we're alive or when we're not. Be a little bit more conscious of where those resources go. Maybe a little bit more selective in that process to achieve the objectives that are important to each of us individually.

Patti: It's not just math, right, John? I mean, in all the textbooks that your program provides and other programs provide. The role of thumb is when interest rates are high, remainder trusts are the better option when they're low. Lead trusts are fantastic.

To your point, what are the objectives here? What's important to us? That's really got to guide the ultimate choice.

John: I love starting with the questions, Patti, because there is math. We can certainly get to the execution and the tools. The first step in the process is let me understand what the client's really trying to accomplish.

"How important is philanthropy to you and your family? How do you decide where you give your money? What are the primary motivations behind the giving that you're doing? Are you giving regularly or are you giving sporadically? Are you itemizing your deductions as the tax advantage?" A key ingredient in this charitable giving process.

These are some of the questions that can help us determine whether charitable giving is an important issue for the client.

Patti: Fantastic. So many important points, John. I really appreciate this discussion. There's so much to talk about. We're not going to get into all the weeds. I've got 10 questions that entered my brain while we were talking. I'm like, "OK, I can't get into that question. Don't want to get into the weeds there."

John: [laughs] Sorry. I can only give you nine, Patti. I'm awfully sorry. Our time is limited.

Patti: Oh, my goodness. What a privilege it is having you here in our studio.

John: Oh gosh. It's a privilege.

Patti: John, you're incredible.

John: It's a privilege to be here.

Patti: It's also a privilege to have you watching and listening to these podcasts week after week. I mentioned it on another podcast. John, you probably already know this.

Did you know that 99.7 percent of podcasts do not go beyond their 10th episode?

John: Wow. That means that people are not watching it. The person producing it has decided to quit because it's too much energy or...

Patti: They just quit. It's a lot of energy. It's a lot of work. It's a lot of people to pull this together to get great people like you, John.

John: All right. Tell me, what number are we at?

Patti: What do you think?

Patti: We are at 135. That's really a lot certainly in our profession, but just generally. I was surprised at one of the top podcasts. Programs that's on iTunes and all the same ones that we are as well.

John: Sure.

Patti: They're at less than a thousand.

John: Wow.

Patti: Which I thought they'd been doing, and they have been doing it for 10 years.

John: Right.

Patti: I thank you for coming. Again and again, you always say yes, John. I'm so grateful to you for that.

John: My pleasure. Sure. Thanks for the invite.

Patti: It's such a privilege to have you here. PIMCO as well.

John: Thanks.

Patti: Dan. The whole crew. We learned so much from all of you.

John: Love it. Let's continue. Let's do more.

Patti: All right, sounds good. We already have a couple of other subjects.

John: OK.

Patti: Thanks to you again for tuning in. You make all this worthwhile for us. Thank you for going to our website. You know the drill. It's www.keyfinancialinc.com.

It's a brand-new website. There's a lot of good stuff there. We've organized the information to make it even more relevant for you. Thank you for going to the website. Ask us your questions. Give us a call. If there's anything that you want to learn more about, let us know.

Many of the topics we talk about are because of people writing in. Thank you for that. In the meantime, I'm Patti Brennan. We're Key Financial, Wealth Management with wisdom and care.