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What if you could have more money for your retirement and your heirs by giving money to charity?

By Gabor A. Nagy

I am blessed to have so many people in my life who are genuinely nice and want to help others. It's in our nature to want to help those who are suffering or less fortunate than us. And in my practice, I have many clients who have been giving to their favorite causes for years and often I hear them say: *"I wish I could give more, I wish I could have a greater impact. But my concern is there would not be enough for my family."*

Conventional wisdom suggests that planning for your retirement and leaving wealth to your heirs or giving money to the causes that are near and dear to your heart is an either / or proposition. If I want to have more retirement income, then I have to give less to charity and vice versa. But it doesn't have to be that way. By combining charitable and retirement planning strategies, we can create more money for your retirement, your heirs, and your favorite charities.

There are three components I typically see in a conventional retirement / estate plan:

1 Try to create more income
2 Try to transfer more to heirs
3 Ignore the part you can't keep

With the increase to the estate tax exemption several years ago, the 'part' in #3 is typically the income taxes that we have to pay on our 401k's / IRA's and the long-term capital gains on appreciated non-retirement assets. I do not often see discussed in the financial media any strategies or attempts to offset or eliminate taxes on these retirement plans and appreciated assets. The prevailing attitude regarding retirement plans is: we received a tax break on the contribution, the account grew without a tax bite, and we have to pay the piper at some point. Or we are told to continue to defer taking any money out of these plans for as long as possible so we don't have to pay the tax. Keep in mind that as our account balance grows, so does the embedded tax. For example, if family has a $1 million IRA at age 60 and our tax rate is 40%, that is a $400k income tax lien. If we let that grow for 30 years (minus our RMD's of course) at 8%, our tax lien is now $4 million! On appreciated assets, it's a similar problem: we were fortunate to have assets that appreciated over time, now we need to diversify them to decrease risk and generate income, so we'll just have to pay the capital gains tax and move on. But what if we didn't? More on that in a moment.

One thing that you will see hotly debated in the retirement plan arena is whether you should contribute to a traditional IRA / 401k or a ROTH IRA / 401k. A ROTH IRA / 401k is not taxed on its distributions, but what you give up is the tax deduction on the contribution. A strategy I have seen presented to clients, which very few end up executing on, is the ROTH conversion. This is a great way to alleviate the tax burden on your retirement plan distributions. But there is one major caveat.

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In the year you do the conversion you will owe taxes on the entire amount converted! Again, there is never a discussion on how to offset these taxes. Oh well, say most, we just have to pay the piper.

Switching gears, a common charitable planning tool is the **Charitable Remainder Trust** (CRT). It is most often presented to clients as a tax-planning tool rather than a retirement-planning tool. A CRT is a split-interest gift because there are two beneficiaries: the income beneficiary and the remainder beneficiary. The person making the contribution to the trust (the grantor) can choose to receive a lifetime income, with the remainder at their death going to the named charity(ies). When the grantor contributes highly appreciated assets to the trust and subsequently sells them to create a more diversified/balanced portfolio to provide income, there are no capital gains taxes generated. The grantor will also receive a large tax deduction for contributing assets to the trust, the percentage being based on their age and the published federal mid-term rate. Now what to do with that tax deduction...

Aha! What if we converted our traditional IRA / 401k (or a portion thereof) to a ROTH in the same year we contribute to our CRT? We can even calculate the expected deduction before-hand and match it up with how much we will owe on taxes on the conversion (there are other factors that determine how much of a charitable deduction you can take in a given year which you should review with your accountant or tax advisor before doing this). The end result is that we not only save the taxes on our retirement plans, we preserve that tax savings in the tax-free safe haven that is our ROTH for as long as we want. In our example of the embedded tax of $400k above, if we decide to let this grow in our ROTH for the next 30 years at 8% (and now there's no RMD's!), that $4 million is now on our side of the ledger and can be passed down to our heirs, instead of a tax bill. If we live to life expectancy, we have accomplished our goal of having more for our retirement, and our heirs, and our charities. In order to ensure this strategy works, even if we don't, we can incorporate a life insurance policy to replace what was contributed to the CRT.

By adding a well-known charitable planning strategy to our overall approach to retirement planning, we have accomplished what we set out to in the title of this article, and also added a component that is missing from most conventional retirement/estate plans. We have changed #3 above from 'Ignore the part you can't keep' to 'Stewardship: Control the part you can't keep'. We have moved this part of our client's estate out of the realm of government-directed capital into the realm of self-directed (or social) capital. Paul Brooks of Renaissance, a leader in charitable trust administration, defined social capital as: that portion of a person's assets that must be re-distributed to the community for the common good. And who better to partner with in your Stewardship endeavor than the **Community Foundation of New Jersey**? You can even name them as the beneficiary of your CRT and have your family carry on your vision of giving and stewardship after you have passed on.

One final note. The concept I've outlined here is simple, but the execution of it is quite sophisticated. There are many different variations and applications of this approach, and many variables to consider when doing this sort of planning. It should only be done with a well-coordinated team of advisors, who have expertise & experience in putting this together. And above all, their focus should be to make your dreams come alive, to help you have an even greater impact than you thought possible. If you don't currently have that team in place or don't know if you do, the Community Foundation can be a valuable resource to help. As the late, great Arthur Ashe once said: *"Start where you are, use what you have, do what you can".*

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Gabor A. Nagy is Principal at Mendham Wealth Partners, LLC. He holds the Chartered Life Underwriter® (CLU®), Chartered Financial Consultant® (ChFC®), and Chartered Advisor in Philanthropy® (CAP®) designations from The American College. He obtained his Certified Financial Planner™ certification in 2000. Gabor is a member of the Community Foundation of New Jersey's Legal, Wealth, and Tax Advisory Committee, the GIVE™ Alliance, the Million Dollar Round Table (MDRT), and the National Association of Insurance & Financial Advisors (NAIFA).

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