

Client Uses Custom Core[®] to Increase Charitable Gifting, Reduce Tax Burden

CHALLENGE

A client usually funds charitable donations by selling stock—taking a large capital-gains hit in the process.

SOLUTION

Parametric recommended donating stock instead of cash, then repurchasing stock with an equivalent amount of newly deposited cash.

RESULTS

The client maintained her desired market exposure, increased her charitable contribution, and set herself up for a potentially lower future tax bill.

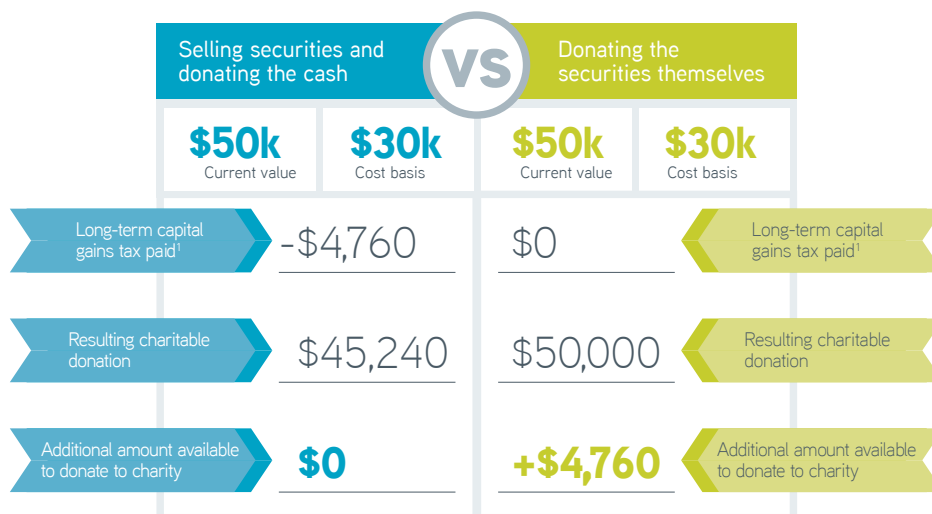
Challenge

A client makes an annual cash gift to her local food bank, funding her contribution by selling stock in her investment portfolio. While she appreciates the tax deduction for charitable giving, she's also paying taxes on capital gains incurred from selling the appreciated stock. She asks Parametric if there's a more tax-efficient way for her to make charitable donations in coordination with the tax management Parametric already performs on her Custom Core[®] account.

A welcome tax deduction for charitable giving meets an unwelcome tax on capital gains.

Parametric solution

Making charitable gifts in cash is a natural instinct for many people. After all, cash gifts may lessen an investor's current tax bill by reducing taxable income by the amount of the gift (subject to limitations, of course). But cash gifts aren't the only option. For example, when you donate stock to a charity, you get the added benefit of receiving a tax deduction for the full fair-market value. As the below example demonstrates, this approach also represents an increase of more than 10% in the size of the gift as opposed to selling the shares and then donating the cash, since you avoid the payment of capital gains tax incurred when selling the shares.



Added benefit:
The portfolio's tax alpha can increase by 1% to 2% depending on the size of the gift, how much cash is replenished, and the portfolio's overall appreciation.

Source: Parametric, 2020

¹ Assumes all realized gains are subject to the maximum federal long-term capital gains tax rate of 20% plus the 3.8% Medicare surtax, for a total rate of 23.8%. Does not take into account state and local sales tax, if any apply.

In the case of this client, Parametric suggested a two-step course of action. First, we identified suitably appreciated securities from the client's Custom Core portfolio, recommending a list of low-basis securities that, when donated, would maximize the capital gains transferred through the gifting process. Second, the client deposited cash equal to the value of stocks gifted. Parametric then used this cash to purchase stocks that allow the portfolio to maintain the client's chosen market exposure but that have a much higher cost basis than the gifted shares. This higher-basis investment increases the potential for tax-loss harvesting, which should help reduce future tax payments.

Gifted low-cost-basis securities helped the client avoid realizing capital gains.

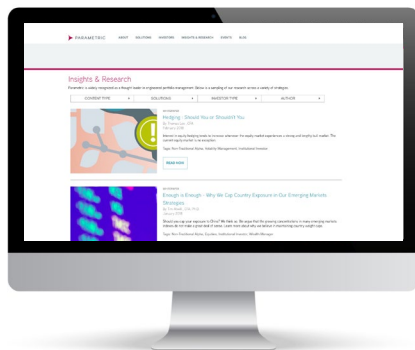
Results

By gifting appreciated securities from her Custom Core portfolio, the client was able to donate a higher dollar amount to her favorite charity, potentially increasing her charitable tax deduction in the process. By then investing an equivalent amount of cash back into her Custom Core portfolio, she was able to purchase a number of securities with higher basis, resulting in a portfolio with a higher potential for tax-loss harvesting and reduced tracking error.

The client was able to donate a higher dollar amount to her favorite charity.

At Parametric, we manage more than \$134 billion in assets in Custom Core accounts alone, with \$110 billion in client-specified tax mandates.* Charitable gifting—and how to optimize its impact—is a critical component of our comprehensive approach to tax management.

*As of 12/31/2020



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