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Money Matters | Avoid these four charitable giving mistakes in the new tax reality

By JONATHAN HARRISON

Amazingly, the charitable deduction emerged almost completely unscathed from Washington's latest updates to the tax law. When the idea was floated last month to cap or eliminate the popular tax break, nonprofit leaders descended on Washington en masse to fight for it. Their voices were heard, and the deduction is mostly intact.

At the same time, changes in other areas of the tax code made the stakes even higher. Paychecks are decreasing due to the expiration of the payroll tax cut. Capital gains taxes are going up, and many now have an additional Medicare surcharge. Higher taxes mean people have less to give. In the face of this new tax reality, it's more important than ever to avoid these four common giving mistakes.

1. Not giving (or not giving enough). Many donors are going to feel pain over the coming months. With more going to the government, many people will feel like they have less to give away. But higher taxes also make giving more cost effective. The value of that deduction may actually be worth more now.

Giving is also important because of its effect on our psyche. Sociologists have shown that we are made happier not by how much money we make, but what we do with the money we have. Being generous can actually make a stretched checkbook more satisfying.

2. Giving cash. The vast majority of donations in the U.S. come in the form of a check. Donors with taxable investment portfolios have a significant opportunity to get a bigger advantage out of their giving. When individuals make gifts of appreciated assets like stock, they not only get a deduction for the gift, they also completely avoid the capital gains connected to that stock.

If you're in this camp, instead of reaching for the checkbook, donate appreciated stock or mutual funds you've held for over a year. Then take the cash you were going to give and buy back the stock for tax-free rebalancing. A tool like a donor advised fund is a great way to facilitate this type of giving, since many nonprofits aren't prepared to receive stock.

3. Not planning. Just like all other financial goals, thinking ahead can significantly maximize the impact of a charitable gift. But many Americans simply react to giving opportunities as they are made aware of them. This is the equivalent of spending a few dollars here and there on fast food instead of saving up for a night out at a nicer restaurant.

Instead, start setting aside a regular portion of your earnings for future gifts. My wife and I started doing this about a year before the earthquake in Haiti, and when tragedy struck, we had the opportunity to help an orphanage in dire need at ten times the level we would've been able to otherwise. A donor advised fund is a useful tool here too, because it creates a designated space for giving dollars. It also allows the giver to lock in the deduction when it's set aside, rather than the eventual distribution to charity.

4. Not keeping correct records for gifts. The IRS recently denied a taxpayer a charitable deduction for a $22,000 check he wrote to his church. The reason: he didn't have a correct receipt when he claimed the deduction.

It's not enough to make a gift to a qualified tax-exempt organization, givers must also make certain that they document the gift correctly. For gifts under $250, a cancelled check or bank statement is enough. Larger amounts must have a written receipt from the charity stating the date, amount, and whether any goods and services were given as a result of the gift. Noncash gifts have specific requirements depending on the type and size of the gift.

As the rhetoric from Washington increases, keep these blunders in mind and avoid them. Though very few donors give solely for the tax write-off, it's certainly a great benefit to maximize as long as it's available.

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