Introduction to Planned Giving Essentials

Chicago Council on Planned Giving
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Presented by
Marc Carmichael, J.D.
15524 Janas Drive
(708) 705-1246
marccarmichael@msn.com

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Planned Giving: The Answer to “I Wish I Could Do More”

I. Planned Giving Defined

A. Planned giving uses tax, financial and estate planning techniques to enable a donor to make a substantial gift commitment to your organization that provides significant tax and financial benefits for the donor.

B. Through the use of planned giving techniques, the gift is often greater than the donor may have previously considered because the benefits may dramatically reduce the net cost of the gift.

C. With benefits available to donors through planned giving, such a program will enhance the overall fund raising efforts of your organization.

D. Creative use of planned giving techniques can be tailored to meet the economic needs of the donor as well as your organization’s programs.

E. Donors’ personal satisfaction is increased because they can make a larger gift and “experience” the implication of their gift during their lifetime.

II. Forms of Planned Gifts

A. Outright Gifts

1. Cash – a frequently used asset for all forms of charitable gifts
2. Marketable securities – Gifts of highly appreciated securities may be given with substantially reduced after-tax cost.
3. Real estate – due to historically rapid escalation in values and the capital gain exposure, real property is frequently used to make charitable gifts.
4. Tangible personal property – special rules apply, and with the rapid appreciation in collectibles, they can be attractive for giving.
5. Life insurance – life insurance policies no longer needed for family
security can be a good source of charitable gifts.
6. Direct IRA gifts by donors over age 70½ may be retirees’ best resource.

B. Gifts with Retained Benefits for Donors/Families

1. Charitable gift annuity – individual(s) receives a fixed income for life. Institution receives gift principal immediately.
2. Charitable remainder annuity trust – individual(s) receives a fixed income from an irrevocable trust. Institution receives remainder.
3. Charitable remainder unitrust – individual(s) receives variable income from an irrevocable trust. Institution receives remainder.
4. Charitable lead trust – an irrevocable trust pays income to your organization; trust principal reverts to donors or their heirs.
5. Gift of residence or farm with retained life occupancy or use – donor transfers title to institution, but reserves the right to use property for life.

C. Gifts by Will

1. Outright bequests – donors of modest means, as well as the wealthy, can make gifts from their estates by will.
2. Bequests to a charitable trust or gift annuity – all of the forms of trusts and life-income gifts can be established by will.
3. Contingent bequests – donors with family members can make a gift by will should the family members no survive the donor.
4. Will substitutes: Life insurance, financial account beneficiary designations, revocable living trusts, IRA designations, etc., enable donors to make gifts without making or changing their wills.

D. Purpose of the Gift

1. Current operating expenses – may be the purpose for outright gifts, but generally not for gifts in trust and bequests.
2. Capital projects – because funds are received at indeterminate future date, life income gifts are often less suitable for “bricks and mortar.”
3. Endowment support – most frequent purpose for life income gifts and bequests.
4. Unrestricted – use of institution gifts may be for unrestricted purposes.
5. Restricted – life income gifts and bequests usually are for restricted purposes.

III. The Market for Planned Giving

A. Size of Estate Is Important

1. Impact of federal estate tax on estates may be a factor for some donors – but less than .1% of the adult population is affected.
2. Potential market for your organization should run 1-2% of constituency
depending upon relative wealth.

3. According to IRS statistics, 18% of estate tax returns in past years have included charitable bequests.

4. Planned giving techniques historically have been underused due to lack of knowledge by general public and their advisors.

5. Indication of lack of sophistication in estate planning: Estimates are that 80% of the population who are not college graduates do not have wills; of college graduates, 60% do not have wills.

6. Conclusion: tremendous opportunity exists to provide a service to your constituents and raise money for your organization through planned giving that raises awareness of the need for estate planning.

IV. Advantages of a Planned Giving Program

A. Provides a valuable service that strengthens your relationship with your donors.

B. The planned gift is often made from the estate of the donor and is not dependent on just the donor’s income.

C. The tax and other financial benefits of planned giving enable donors to make gift commitments many times greater than they thought possible.

D. The after-tax benefits of a planned gift enable donors to increase their annual gifts.

E. Even those of modest wealth can make meaningful gifts through bequests.

V. Challenges to Overcome in a Planned Giving Program

A. Relies on more direct cultivation and solicitation by staff. Less able to use volunteers effectively. A planned giving “anchor person” is needed on staff.

B. Emphasis on tax benefits can create imbalance at expense of donor’s emotional commitment to the institution.

C. Procrastination can develop from the long negotiation period, which is difficult to overcome.

D. The need for current funds can result in lack of focus and commitment to planned giving.

VI. Some Generalizations about Planned Giving

A. Solicitation calls are most effective when conducted by a trained staff person, as
opposed to a volunteer, because of the technical background required.

B. A planned gift solicitation may require several repeat calls over a period of many months.

C. Some knowledge of tax and estate planning is important to being a successful planned giving officer.

D. However, planned giving is analogous to the marketing and sale of a financial service. Success depends mostly upon persistence, follow-up and the ability to relate to people, especially those of older ages.

Who Are Planned Gift Prospects?

Who is a planned gift prospect? Conventional wisdom suggests that the best (but not the only) planned gift prospects are people who (1) will receive personal satisfaction from assisting your organization, (2) are retired or nearing retirement age, (3) have sufficient wealth to make a major gift and (4) are childless or otherwise without family financial obligations. It is estimated that the average planned gift takes more than two years to cultivate and negotiate. This is a considerable time investment. Planned giving is not a broad-based effort. You must eliminate the multitude of prospects by identifying and zeroing in on those with whom your efforts will be most productive. This requires considerable research to determine the age, family situation, past giving record, financial ability and mix of assets they own.

I. Donor Profile

A. Not all constituents are not good prospects for planned gifts.

B. Only a person whose situation contains a certain set of circumstances is likely to become interested in this form of giving.

II. Age – You will find that individuals age 60 and over are usually your best prospects.

A. They should be retired or about to retire and therefore have gone through the period in their lives when they have been concerned with accumulating assets and building their estate. This is the time in life when they will have the greatest amount of capital for making significant planned gifts.

B. They probably have passed the time of family responsibilities of raising and educating children. In fact, the best prospects are often childless.

C. The tax advantages of planned giving will be great at this age. If it is prior to retirement, they will have reached the highest level of earned income and
therefore have the greatest need for the deductions generated by planned gifts.

D. In retirement, they will need the increased income possible from planned giving and their rate of income tax will have diminished from their peak earning years.

E. The psychological benefits of planned giving can also be great. Planned giving enables donors to say: “I have truly made a difference for the good of humanity.”

F. Donors may appreciate having someone else manage part of their assets. Being past the time when they are active in their careers, poor health, approaching senility or just the desire to enjoy life may stimulate planned gifts for the freedom from management concern – especially when real estate and closely-held business interests can be converted into liquid investments through planned gifts.

G. The elderly may say: “I gave because you were the only one who visited me.”

H. You must seek gifts from these elderly prospects because they are current donors. You need to convert some of their assets into endowment gifts so you will have income to replace their current gifts when they are no longer here to make them.

I. The next best prospects are age 50-59. They should be included in your marketing program because they are in their peak earning years. Also, because planned giving success requires education over a period of time, prospects in their 50s will become aware of university programs and the benefits of planned giving when they do their serious estate planning. The 50s group should be encouraged to make bequests and beneficiary designations from retirement plans.

J. Putting too much effort into prospecting with individuals in their 40s may not be a wise investment of time and money. While there are exceptions, these people are in the process of building their estates, rearing and educating children, and are not in an estate planning frame of mind. Note: A recent PPP study indicated a surprising number of donors in their 40s and younger who said they had made a planned gift of some kind. So, while they won’t be your first marketing targets, bequests and other estate gifts by this group should be encouraged.

K. One exception may be the opportunity offered by the deferred payment gift annuity for prospects in their 50s and early 60s. Donors can make annual payments or a lump sum to fund a gift annuity and receive a significant income tax charitable deduction during high earning years to save taxes. They postpone the annuity payment until retirement when they need supplemental income: A satisfying add-on to a retirement account.

III. **Family Situation** – There are many exceptions to the following profiles, but generally
speaking they are better planned giving prospects.

A. Married couples with no children are excellent prospects.
B. So are married couples whose children have independent wealth.
C. Unmarried individuals who have no close family ties are good prospects, including men and women who have never married, widows and widowers.
D. Individuals who are helping to support older relatives.

IV. Past Giving Record

A. Long-term annual donors are probably the most likely prospects for planned gifts. They have already expressed their interest in our programs and are committed to your organization’s success.
B. You don’t have to start from scratch to get to know them and you may have already convinced them of the worthiness of your mission.
C. You need only communicate with them about another form of giving.
D. Research your donors over age 50 to find those with the capital assets to enable them to make significant gifts.
E. But do not neglect steady donors with consistent giving records. They can make more modest gifts that can be at the five-figure level. The Millionaire Next Door book illustrates that people who live modestly often have surprising wealth – albeit wealth that they are unwilling to part with until death.
F. And don’t neglect donors who have already made a gift in trust or a provision in their wills. Many previous donors increase and accelerate their commitments as family circumstances change and their desire to assist your organization grows.
G. Do not neglect families of deceased donors – especially those who have made planned gifts. These family members have a strong tie to your organization and have experienced the benefits of planned gifts as income beneficiaries and have seen the evidence of what charitable gifts can achieve.

V. Financial Ability

A. Individuals with significant capital assets and high levels of income are best able to make planned gifts and enjoy the tax benefits that they generate. Therefore, identifying those prospects is critical to success in planned giving. As noted earlier, the federal estate tax can be a motivating factor for individuals with taxable estates. Why? Because gifts can save both income taxes and “death taxes.” But federal estate taxes now affect only persons with estates above $11.4
million ($22.8 million for married couples), indexed for inflation.

B. Single individuals who are not affected by the federal estate tax remain worthwhile prospects for bequests and gift annuities. Millionaires in your constituency should be considered prime prospects. While the 2017 Tax Reform Act has limited federal estate tax liability to only a few thousand estates a year, some estates will still have to deal with state death taxes and income taxes on IRAs and qualified retirement plans.

VI. Special Situations

While all the above factors contribute to a profile of a worthwhile prospect, you should be mindful of some special situations that relate to the property owned by the individual.

A. Real estate is the source of considerable wealth. Some of the investment and tax considerations inherent in real property can make it especially attractive property for planned gifts. In some cases, the capital gains exposure and the recapture of depreciation deductions that result from a sale make planned giving the only economic way to convert a successful real estate investment when it has matured.

B. Owners of closely held businesses who are approaching retirement and may wish to sell their company or have family members step into management are very good prospects for planned gifts. Gifts of closely held stock to your organization, followed by a prearranged corporate redemption funded by corporate cash can be a very effective technique for charitable remainder trusts and may require the use
of the gift annuity for large gifts of closely held stock.

C. Washington University Profile of Typical Donors by type of gift.

Charitable Gift Annuity

42% are married couples; 39% are widowed; 13% single
55% have children
Average age is 78
64% of donors fund gifts with cash; 33% with appreciated securities
53% make repeat gifts
69% live out of town

Charitable Remainder Unitrust

66% are married couples, 19% are widowed; 11% single
60% have children
Average age is 76
70% of donors fund gifts with appreciated securities; 20% with cash
74% make repeat gifts
56% live out of town

VII. “Donor Sounds.” Here are some words and phrases that, if heard from someone with links to your organization, may identify them as a prime planned gift prospect:

“I’m getting ready to do some estate planning (or make my will);”
“We’re planning to sell our business this year;”
“The stock market is making me nervous – I’d like to bail out;”
“We’re moving to a retirement community;”
“My farm/house/investment real estate is up for sale;”
“I’m tired of the low returns I’m getting from my CDs;”
“My spouse (or other family member) died recently;”
“I wish I could stop worrying about managing my investments.”

“Supersizing” Lifetime Gifts

Most donors provide support for worthwhile organizations – their house of worship, college, service organizations and many others. And for the most part they simply write a check. But there are techniques to increase one’s support, often for little or no additional outlay – and there
are ways to truly be a “hero” to a worthwhile institution at remarkably low cost.

I. Advantages of Gifts of Cash.

Gifts of cash are simple, safe, easy to document for deduction purposes and can be put to immediate use by the institution. Tax savings are simple to calculate: Simply multiply the donor’s highest tax bracket times the amount of cash contributed. For example, a gift of $10,000 saves $2,400 for a person in the 24% tax bracket. Question: John, an unmarried donor, expects to have taxable income for 2019 of $220,000, which lands him in the 35% tax bracket. What will he save in taxes by mailing your organization a check for $10,000 on December 31?

II. Gifts of Securities.

Investors who own marketable securities – stocks and bonds — that have gone up in value have a tremendous opportunity to increase their support. By giving stocks instead of writing a check you can receive a charitable deduction based on the full fair market value of the stocks, not just what you paid for them. The stocks must have been held long-term (more than one year) in order to deduct the “paper profit.” For example:

Mollie gives $500 a year to your organization, and the gift qualifies her for membership in the “Wonderful Person Club.” Mollie would like to join the “Really Wonderful Person” donor club, which requires a $1,000 contribution.

Mollie happens to own securities worth $1,000 that she bought 15 years ago for only $200. If Mollie sells the stock she will have a capital gain to report of $800 and a capital gains tax to pay of $120 (15% x $800). So the stock is really worth only $880 to Mollie ($1,000 minus the $120 capital gains tax burden).

But if Mollie gives the stock to your organization, your organization will keep the entire $1,000 free of capital gains tax (as a tax-exempt organization). And Mollie will receive an income tax charitable contribution deduction for the full $1,000, which saves her taxes of $240 in her 24% tax bracket. It is fair to say that her $1,000 gift will actually cost her only $640 ($880 – $240 of taxes saved). And the director of development has promised not to tell any of the other members of the $1,000 gift club that Mollie actually sneaked in for only $640! Note: Even non-itemizers avoid capital gains taxes on stock gifts.

III. Stock in Closely-Held Companies.

Business owners have special opportunities when it comes to making charitable contributions. One attractive option is giving stock in a closely held corporation. Mom owns 90% of the stock in the Mom-and-Pop Corporation and decides to give a few shares of her stock – worth, say, $10,000 – to your organization. The gift of stock leaves her in full control of the business and does not deplete her checking account or personal investments. Yet she is entitled to a $10,000 charitable deduction on her personal tax
return, which would save her $3,700 in taxes in a 37% income tax bracket.

Your organization, which has no reason to keep the stock, turns the shares in to the corporation for redemption. The corporation gives your organization $10,000 cash to use for scholarships and retires the stock. The key to this arrangement is that while Mom has received a valuable benefit from her corporation (a charitable deduction) she will not be considered to have received a dividend from the corporation, according to an IRS ruling. (Your organization cannot be required, however, to turn the shares of stock back to the corporation).

IV. Gifts of Collectibles.

Gifts of tangible personal property such as antiques, coins, paintings, stamps, etc., may have the same favorable tax consequences as gifts of stock. A special rule, however, limits deductions for such gifts to the donor’s cost basis if the charity does not put the gift to some use related to its tax exempt purposes.

V. Gifts of Real Estate.

Same tax advantages as other gifts of appreciated property. Note that any noncash gifts other than marketable securities require qualified appraisals if the value is more than $5,000. Real estate gifts require scrutiny for hazardous waste liability.

VI. Gifts from One’s Business.

A donor’s corporation can make contributions to charity and take a charitable contribution deduction, just like an individual taxpayer. Owners should compare their individual tax rates with the corporation’s tax rates to determine which donor saves the most taxes from a gift: owner or the corporation. Keep in mind that a gift made by a donor’s corporation to a charity is not taxable income to the donor – and remember that appreciated securities are an excellent choice for corporate as well as individual giving.

VII. IRA Gifts by Persons over 70½

Congress in 2015 passed permanent legislation enabling IRA owners over 70½ to make nontaxable “qualified charitable distributions” up to $100,000. IRA gifts can count toward satisfying the required minimum distributions required of IRA owners over age 70½, which will reduce taxes for these donors – even those who do not itemize their
deductions (the case with many retired persons).

Summary

- Donors should give appreciated securities, if possible, instead of cash.
- Small business owners should give stock in their companies.
- Gifts of collectibles and real estate need special planning.
- Business owners should consider having their business make charitable gifts.
- Eligible donors should consider IRA gifts.

Gifts from Donors’ Wills and Estate Plans

I. Charitable Bequests

Bequests are a popular means of providing for charities and may be the most practical way for many individuals to satisfy charitable commitments. Indeed, conventional wisdom holds that 80% to 90% of all planned gifts are gifts by will. Advisers who are unfamiliar with other planned giving techniques sometimes are inclined to tell clients: “Just take care of the charity in your will,” but bequests require just as much planning and forethought as other planned gifts.

Property passing to charity from a donor generally will qualify for the federal estate tax charitable deduction and for a deduction or exemption from state inheritance taxes. For federal estate tax purposes the transfer must be to an organization described in Code Sec. 2055(a), and the property must (1) be included in the decedent’s gross estate, and (2) be considered “transferred by the decedent.” Charitable bequests are 100% deductible; there are no deduction “ceilings” such as the 30% and 50% of adjusted gross income limits on the income tax charitable deduction.

A. Selecting property to bequeath to charity.

**Tax-Burdened Assets.** Where possible, donors should bequeath to charity property that would cause tax problems to other beneficiaries. That generally means “income in respect of a decedent” (IRD) – items of income earned by a decedent before death but paid to his estate after death. Such income is includible both in the taxpayer’s gross estate and in the estate’s income.

Charities usually do not pay income taxes and therefore keep every dollar of such tax-burdened bequests. Furthermore, a bequest of IRD can create both an estate tax charitable deduction and an income tax charitable deduction for the estate.

It’s important, from a tax standpoint, for a donor’s will to make specific bequests of items of IRD to charity, or to have IRD assets pass to charity as a residuary
bequest. Alternatively, a donor can change the death beneficiary of a pension plan or IRA to a qualified charity. Satisfying pecuniary bequests to charity out of IRD items will generate an estate tax charitable deduction but the estate will have to include the IRD in its income. Examples of IRD items include:

1. Interest on U.S. savings bonds
2. Accounts receivable of a cash-basis individual
3. Renewal commissions of insurance agents
4. Deferred compensation, last salary check and bonuses
5. Accrued royalties under a patent license
6. A deceased partner’s distributive share of partnership income up to date of death
7. Payments on installment obligations.
8. Death benefits from IRAs and other retirement accounts

**Assets that have poor tax results if contributed during life.** Certain kinds of property have poor income tax results if contributed to charity during life. Bequests of such property, on the other hand, can be 100% deductible for estate tax purposes.

*Ordinary income property* – Several years ago an artist living in the southwest burned about $1 million worth of his paintings when he found they would be subject to federal estate tax. Had he given some thought to the matter, he might have found it better to bequeath the paintings to a museum, university or other charitable institution.

If the artist had given the paintings to charity during life his charitable contribution would have been limited under income tax law to his cost basis – what he paid for paint and canvas. Paintings in the hands of the artist are one kind of “ordinary income property,” defined as property the sale of which would produce any ordinary income or short-term capital gain. No such reduction applies in the estate tax charitable deduction; thus the artist’s estate would have been allowed a deduction for the full fair market value of the paintings had he bequeathed them to charity.

*“Collectibles”* – If an individual makes a lifetime gift to charity of tangible personal property (e.g., a painting, boat or a coin collection), and the charity puts the gift to an “unrelated use,” the donor’s contribution will be reduced by 100% of any long-term capital gain present in the property. No reduction occurs, however, with bequests of tangible personal property – another situation where bequests make more sense than lifetime gifts.

**B. Options in planning outright bequests**

An outright charitable bequest can be:

1. A specific dollar amount
2. A specified property (specific bequest) – “my 100 shares of stock in XYZ
Corporation, evidenced by share certificate number 3345729 – could be “adeemed by extinction” (eliminated)

3. A particular kind of property (general bequest) – “100 shares of stock in XYZ Corporation.” Executor could go out and purchase appropriate shares, if necessary. General bequests can be adeemed only by “satisfaction” – the estate owner makes an identical gift to the beneficiary during life with the intent to make the bequest inoperative.

4. A percentage of the net value of the estate
5. The residue of the estate
6. A percentage of the residue of the estate.

Estate tax charitable deductions are available only for amounts actually passing to charity. Death taxes and expenses recovered from a charitable bequest will reduce the amount charity receives and the available deduction. Furthermore, reductions in the estate tax deduction will increase the amount of tax due, further reducing charity’s share, and on and on – a vicious circle. Donors should direct that no death taxes or costs of administration will be payable from charitable bequests or distributions.

C. Alternative charitable bequests

In general, every will should contain one or more alternative charitable bequests. These bequests provide flexibility in carrying out an individual’s testamentary desires in the face of changing circumstances and unforeseen events.

1. Qualified disclaimer – If an individual makes a qualified disclaimer of a bequest and the bequest property passes under an alternative bequest to a qualified charity, the decedent’s estate will be allowed a deduction for the amount passing to charity.

This arrangement allows a family beneficiary who feels he or she does not need all that a testator has provided, to pass along all or part of a bequest to a worthwhile cause favored by the estate owner – and also provide tax savings to the estate.

2. Contingent bequests – Individuals sometimes provide that bequests shall pass to named charities if the primary beneficiary – a friend or family member – should predecease them.

Another use of alternative charitable bequest clauses is to cover the possibility that all intended beneficiaries predecease the estate owner, or the possibility that the estate owner and his or her intended beneficiaries are killed in a common disaster. The advantage of naming a charity as one’s “ultimate contingent beneficiary” is twofold:

(a) The estate owner avoids having his or her estate pass to distant
(perhaps unknown) relatives. In unusual cases, the estate could even escheat to the state. Instead, the estate owner has the satisfaction of knowing a worthwhile cause will be benefited.

(b) The estate will completely avoid federal estate taxes, and perhaps state death taxes, if everything passes to charity under an alternative bequest.

D. Life income bequests.

Estate owners can divide benefits of property ownership between charities and private beneficiaries in a variety of ways, with or without a trust. Cash or property can be bequeathed to charity conditioned on the charity’s promise to pay an annuity to a named beneficiary. Additionally, a farm or personal residence can be bequeathed to charity while reserving a life estate for, say, a surviving spouse. All these gifts provide estate tax deductions.

E. Bequests in trust

Charitable remainder trusts, charitable lead trusts and QTIP trusts. A charitable bequest can be postponed until the death of a beneficiary – that is, a family member can receive lifetime income from the bequest property, remainder to charity. This can be accomplished by means of a charitable remainder trust. Both techniques will produce estate tax charitable deductions.

A “deferred bequest” can be made through any form of trust if an estate tax charitable deduction is not important. A testamentary charitable lead trust can pay income to charity temporarily and ultimately pass all trust principal to family beneficiaries, with significant estate tax savings. A spouse’s interest in a testamentary charitable remainder trust or pooled income fund will qualify for the unlimited estate tax marital deduction, if properly planned.

A qualified terminable interest property (QTIP) trust with charity as remainderman can generate a 100% estate tax marital deduction when the first spouse dies and a 100% estate tax charitable deduction at the death of the surviving spouse. This is a simple, flexible arrangement that permits a person to provide for a spouse, yet ultimate pass part or even all of the estate to charity.

Among other things, QTIP trusts are required to pay all trust income, at least once a year, to a surviving spouse, and no other person can be an income beneficiary. Such a trust would not be a qualified charitable remainder trust, in which payments are made as “unitrust” or annuity payouts. But a charitable deduction would be unnecessary because the trust would qualify for the unlimited estate tax marital deduction. Would spouses ever want to establish testamentary qualified remainder trusts for a surviving spouse? The answer is yes – if there are to be income beneficiaries in addition to the surviving spouse. Such a trust would fail
as a QTIP trust, but could nonetheless generate an estate tax charitable deduction. A testamentary charitable remainder unitrust for a surviving spouse also might make sense if the survivor wanted to use the trust as a philanthropic vehicle. The spouse could make additional contributions to the unitrust, realize income tax and capital gains tax saving, and provide further benefit to the charitable remainderman.

**QTIP emptying into charitable remainder trust.** A private letter ruling permitted a spouse to bequeath property to a QTIP trust that pays the surviving spouse income for life, and then empties into a charitable remainder trust for children. The estate of the first spouse to die qualifies for the marital deduction, assuming the executor makes a timely QTIP election. The surviving spouse’s estate will include the value of the assets passing to the charitable remainder trust – but the estate will qualify for a charitable deduction equal to charity’s remainder interest. The same technique reasonably should apply to a charitable lead trust.

Rollover of retirement accounts into unitrust. The IRS has approved a testamentary transfer of funds from a retirement account to a charitable remainder unitrust for the benefit of a surviving spouse. The donor established the trust during his life, using other assets, and upon his death part or all of his retirement account will be transferred to the trust as an additional contribution. The Service ruled that the value of the spouse’s interest would qualify for the estate tax marital deduction and that his estate would be entitled to an estate tax charitable deduction for charity’s remainder interest. In another ruling, the IRS wrote that there would be no immediate income tax results from a charitable remainder unitrust funded with assets from an IRA. IRA amounts would be taxed as received by the income beneficiary.

### II. Life insurance and other beneficiary arrangements.

Donors may have assets that can be transferred to charity at death outside a will. Most arrangements that provide for death beneficiaries can be made payable to charity.

#### A. Life insurance

Life insurance can be both the subject of a charitable contribution and the means of facilitating other types of gifts through wealth replacement. Designating charity as beneficiary of a policy creates estate tax charitable deductions only. Charity can be a contingent beneficiary or a beneficiary of a fraction of the proceeds. Assignment of all ownership rights in existing policy produces income tax charitable deduction and estate tax deductions. Future premium payments are
Advantages of life insurance gifts:

(1) Privacy – the gift doesn’t go through probate.
(2) Larger gifts – premiums let donor give in installments
(3) Family isn’t deprived of other assets.
(4) “Surplus” policies are often easy items to contribute.
(5) Gifts are self-executing.

B. P.O.D. and T.O.D. accounts. P.O.D. (payable on death) accounts at banks, building and loan associations, industrial loan and investment companies, savings banks and credit unions allow depositors to indicate that their deposits will be “P.O.D.” to a particular individual or charity. The P.O.D. designation is wholly revocable and in no way affects a donor’s control over the deposit. T.O.D. accounts permit the same procedure with brokerage accounts.

C. Pension plans, 401(k) and IRA death benefits.

Death benefits payable to the beneficiary of a deceased plan participant often have income tax consequences for the beneficiary. Because charities are generally tax exempt, it may make sense – if family members have no need of the death benefits – to name charity as death beneficiary and bequeath other assets, not burdened with income tax, to private beneficiaries. Spousal consent typically will
be necessary if the participant is married.

“Life Income Gifts” – Charitable Gift Annuities

Charitable gift annuities are the most popular of all the “life income” gift techniques, and their popularity seems likely to grow as donors seek the security of fixed annual payments in an uncertain economy. Gift annuity donors are generally older (mid-70s) people who often make repeat gifts, once they experience the benefits of a gift annuity. Half of all immediate gift annuity donors are above age 77, according to an American Council on Gift Annuities survey.

Marketing gift annuities, obviously, should focus on retirees, especially current annuity holders, although deferred gift annuities offer benefits to donors in their 50s or even younger. Gift annuity prospects include middle-income people who can afford a $5,000 or $10,000 gift (common minimums). But gift annuities have been established for six- and seven-figure
I. Charitable Gift Annuity Basics

A charitable gift annuity is a simple contract in which a donor transfers cash or assets to a charity; charity promises to pay one or two individuals an annuity (fixed income) for life. The American Council on Gift Annuities (ACGA) recommends maximum payout rates that range from 4.7% at age 60 to 9.5% (ages 90 and over) for one-life arrangements. Rates were raised recently for gift annuities arranged after June 30, 2018:

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<td>84</td>
<td>8.1%</td>
</tr>
<tr>
<td>70</td>
<td>5.6%</td>
<td>86</td>
<td>8.5%</td>
</tr>
<tr>
<td>72</td>
<td>5.8%</td>
<td>88 and above</td>
<td>8.9%</td>
</tr>
<tr>
<td>74</td>
<td>6.1%</td>
<td>90 and above</td>
<td>9.0%</td>
</tr>
</tbody>
</table>

A. The amount transferred to charity will be more than the “investment in the contract” (the value of the annuitant’s right to receive payments for life, discounted to today’s dollars) and the difference is a charitable contribution (deductions are typically 25-50%).

B. A portion of each annuity payment is a tax-free return of the donor’s principal. The tax-free portion (currently 50-85%, depending on ages and interest rates) is figured based on the “exclusion ratio,” which equals the investment in the contract divided by the “expected return” to the annuitant (annuitant’s life expectancy, adjusted for frequency of payments, times the annual payment).

C. Unlike commercial annuities, gift annuities may be funded with appreciated securities or other property. The bargain sale rules apply and part of any long-term capital gain (the portion prorated to the investment in the contract) must be reported. If the annuity is nonassignable and the donor is an annuitant, any reportable capital gain may be reported annually over the donor’s life expectancy.

D. Deferred payment gift annuities are arrangements in which payments begin more than one year from the date of the annuity contract. Both the annuity payments and the charitable contribution deductions are larger for deferred annuities; tax-free payments are smaller, as a percentage of the annuity payment. The American Council on Gift Annuities recommends interest factors for computing deferred rates.
II. Planning Ideas for Gift Annuities

A. CD Rollovers. Payouts under the rates recommended by the American Council on Gift Annuities can be attractive to donors discontented with low CD rates, or who no longer have the intestinal fortitude for the stock market. Many CDs mature in the months of April and October, so it makes sense to market gift annuities so your message reaches donors in March and September.

B. Savings Bonds Alternative. The same donors who have CDs may own U.S. savings bonds that have stopped earning interest (an estimated $8 billion now fall in the “dead” category). These bonds should be cashed immediately; proceeds could be used to fund a gift annuity that provides lifetime income and a charitable deduction that may shelter the interest reported when the bonds are cashed. Deductions can be enlarged for this purpose if the donor takes a lower payout than recommended by the ACGA.

C. Stock Market Exit. Gift annuities offer a means for donors to bail out of the stock market with reduced exposure to capital gains taxes. “Buy-and-hold” investors may still own stock with significant paper profits and should consider using their securities to establish immediate payment or deferred payment charitable gift annuities. In general, up to half of a donor’s capital gain escapes capital gains tax completely. The remaining gain will be reported in small annual installments as part of the donor’s annuity payments – if the donor is also the annuitant. The reportable gain generally will be taxed at a 15% rate, but may be tax tax-free if the annuitant is in the 10% or 15% tax bracket.

D. Tax-Free Benefits. Low applicable federal rates (AFRs) mean reduced charitable deductions for gift annuities, but donors receive a higher percentage of tax-free income when interest rates are low. Some donors may need or prefer large tax-free income over the larger deduction (nonitemizers, for example, or those who have so many charitable deductions that they can’t deduct any more).

E. A “Charitable IRA.” Deferred payment charitable gift annuities provide a way for “baby boomers” to make a major charitable gift that cuts taxes and improves their retirement security. But what if the “baby boomer” says she doesn’t really know the year she wants payments to start? She may decide to work till 70 or 75 and won’t need the money earlier than that. Or she may fear the onset of poor health and want the ability to tap annuity payments early. A 1997 IRS ruling permitted a donor to postpone choosing the exact starting date for the annuity until years into the future. The donor could elect to have payments start in any year, upon giving charity three months’ notice. The donor’s deduction would be fixed at a “ballpark” starting date (age 65, for example), but he or she could qualify for larger payouts by delaying the start of payments according to a schedule incorporated in the annuity contract. The donor could start payments
earlier than the assumed start date by taking lower annual payments.

Charitable Remainder Trusts

People who have included, or plan to include, bequests to charities in their wills or living trusts may be better advised to “accelerate their bequests” through a charitable remainder unitrust that provides a gift at death, but additionally offers income tax deductions, capital gains tax benefits, the assistance of a skilled trustee, the satisfaction (and recognition) of making a lifetime gift, plus a variety of other potential benefits. Establishing lifetime unitrusts in many cases can be a solution to personal and family challenges. Indeed, donors may find that they truly can enjoy “better living through charitable giving” – particularly through creative application of techniques such as the charitable remainder unitrust. In recent years, unitrusts have been employed to supplement retirement savings, educate grandchildren, pay alimony, liquidate art collections, “rule from the grave,” sell businesses and support disabled family members – all in the context of invaluable assistance to worthwhile causes and institutions and tax-saving charitable deductions.

I. Potential Benefits of Charitable Remainder Unitrusts

Charitable remainder unitrusts have the ability to:

A. Increase a donor’s income (or that of a family member) by reinvesting low-yield or no-yield properties for a fixed or variable income (generally 5% to 7%);

B. Provide favorably-taxed income if careful attention is given to how the trust is funded and invested;

C. Avoid capital gains taxes when property is sold and reinvested by the trustee;

D. Supply income tax and transfer tax charitable deductions (generally 20% to 40% of the amount transferred, depending on beneficiaries’ ages or the length of the trust term);

E. Afford significant personal satisfaction and recognition, including memorializing the life of the donor, a friend or family member.

Consider the case of Mary Smith, a 61-year-old widow. Her two children, Tom and Jane, are professionals earning good incomes. They and their children were well provided for through a trust set up under the will of Mary’s husband, Robert. Mary’s sister, Amy, age 60, is not so well off. Amy’s husband has suffered a series of financial setbacks, and Amy has little income of her own. Mary would like to do something for Amy – and for her alma mater and the hospital that cared for her husband during his final illness. Mary owns various properties, including some highly appreciated, low-yield stock worth about $190,000 and some highly appreciated, undeveloped real estate worth about $120,000. She has contemplated leaving these assets to charity at death. A number of goals might be inferred from the foregoing description, many of which Mary can achieve through a
charitable remainder unitrust.

- Mary can fund a unitrust with the stocks and real estate and retain lifetime payments of 5%, 6% or higher – a significant increase in family income – which can be paid to someone in a low tax bracket, such as her sister Amy, and then to a survivor beneficiary (Mary, herself, for example), if desired. A trustee provides skilled investment and management services, which can be important for many families.

- The trustee can invest so that trust payments are taxed at low dividend or capital gains tax rates. Under current law, Amy’s payments could be totally tax free. Payments consisting of trust principal or tax exempt interest also escape taxation.

- No erosion from capital gains taxes occurs when the trustee sells Mary’s stocks and real estate, which leaves the full $310,000 available for reinvestment.

- Mary can deduct roughly $100,000 on her next tax return if the trust is to pay Amy 6% for life. Gift taxes can be minimized, with proper planning.

- Mary will name this arrangement “The Robert and Mary Smith Trust to Save Humanity” and be offered membership in the “Heritage Societies” of the organizations she selects as remainder beneficiaries.

II. Fundamentals of Charitable Remainder Trusts

Charitable remainder trusts are irrevocable trusts that donors establish for the benefit of designated income beneficiaries and one or more charitable remainder beneficiaries. The trusts last for the lifetimes of the income beneficiaries or for a term of years (20-year maximum) or sometimes a combination of the two. Income tax and estate tax charitable deductions (10% minimum) reduce the cost of benefitting charity and improve the donor’s tax situation. Deductions depend on the ages and number of the income beneficiaries (or the term of years the trust is to last), the amount of income retained for the beneficiaries and the applicable federal (midterm) rates (§7520 rates) in effect at the time the trust is established. Donors can choose the current monthly §7520 rate or either of the rates from the previous two months, whichever is most favorable for deduction purposes.

Charitable remainder trusts come in two varieties: annuity trusts and unitrusts. Only 20% of all CRTs are annuity trusts and the trend has been for donors to establish unitrusts. CRTs are commonly set up in amounts from $100,000 to $1 million, although $10 million trusts and larger have been established.

A. Annuity trusts pay an unchanging dollar amount. They resemble charitable gift annuities in that respect, but donors establish the terms of annuity trusts, subject to IRS rules. The payout is unaffected by fluctuations in trust income or changes in the value of trust assets [IRC §664(d)(1)]. Donors may not make additional
contributions to annuity trusts [Reg. §1.664-2(b)].

Annuity trusts, except for term-of-years trusts, must pass a “5% probability test” – that is, no charitable deductions are allowed if there is more than one chance in 20 that the trust assets will be exhausted when the trust ends. In addition to losing charitable deductions, the trust could not operate as a tax-exempt charitable remainder trust. However, a recent ruling allows annuity trusts that fail the 5% probability test to still qualify if they contain a “qualified contingency” clause that guarantees a minimum 10% distribution to charity.

Annuity trusts are less common than unitrusts, primarily because they lack the flexibility and planning options of unitrusts. Current low interest rates also heighten the chances of failing the 5% probability test.

B. Unitrusts (so called because trust principal and trust income generally are treated as a “unit” in calculating payouts) pay beneficiaries a percentage (minimum 5%, maximum 50%) of the value of the trust as revalued at least once a year. Payments will rise or decline according to the investment success of the trustee. This is commonly called the “standard” unitrust (STANCRUT). Additional contributions may be made to unitrusts, if the trust instrument so provides.

Payouts can be limited to the lesser of the trust’s net income or the unitrust percentage – a “net income” or “income exception” unitrust (NICRUT) – and provision also can be made for “make-up” or “catch-up” of deficiencies from years in which payouts were less than the payout percentage stated in the unitrust agreement (NIMCRUT) [Reg. §1.664-3(a)(1)(i)(b)]. The trustee may make up prior years’ deficiencies in payouts to the extent current income of the trust exceeds the specified unitrust amount.

CRTs are tax exempt; however if a trust has unrelated business taxable income, such income is taxed at a 100% tax rate (that is, forfeited). Rents and dividends from corporations generally are not considered unrelated business taxable income. Income beneficiaries are taxed on income under the “four-tier” system: (1) current and accumulated “ordinary income” of the trust is considered first, then (2) current and accumulated capital gains, (3) “other” (tax-exempt) income, and (4) corpus (also tax free).

IV. Selecting Assets to Fund Charitable Remainder Unitrusts

A donor desiring to create a charitable remainder trust should give careful thought to what kind of property to place in the trust. Transfers of debt-encumbered real estate will disqualify a charitable remainder trust, and donors should be aware that deductions for gifts of tangible personal property will be reduced and postponed until the item is sold from the trust. Transfer of S corporation stock to a charitable remainder trust will
terminate the company’s S status.

Real estate that is not subject to a mortgage can be excellent for funding a unitrust or annuity trust. Office buildings and apartments that have been depreciated can be sold and reinvested within the trust without loss to capital gains taxes as high as 25% on the depreciation recapture portion. A personal residence is suitable for transfer to a charitable remainder trust, but not if the donor wishes to continue living in the house. The prohibition against self-dealing would be violated if the donor continued using the house rent free, and probably would be violated even if a reasonable rent were charged, because the regulations forbid a lease of property by a charitable remainder trust to a disqualified person.

Publicly-traded securities that have appreciated in value are ideal for funding a charitable remainder trust. Unlike closely held stock, these shares are freely transferable and generally pose no problems under the private foundation rules. Donors do not realize capital gain upon the transfer to the trust because the transfer is not considered a “sale or exchange.” The trustee may sell the stock without causing the donor or the trust to incur current capital gains tax, enabling the trustee to construct a diversified portfolio, invest for higher yield or tax-favored income, such as qualified dividends. Income beneficiaries eventually may report capital gain income from the sale appreciated assets by the trust, under the four-tier system of trust taxation. But such gains typically are taxed at low rates. U.S. savings bonds can be used to fund CRTs, but generally result in taxable interest for the donor when cashed by the trustee (but charitable deductions may help).

Gifts of Remainder Interests in Farms and Residences

A donor can take a deduction for the contribution of a remainder interest in a farm or personal residence. A residence need not be the donor’s primary residence. So contributions of the remainder interest in a vacation home, condo, or stock in a cooperative housing corporation are deductible for income tax purposes. Donors who anticipate leaving a home or farm to charity should consider accomplishing the same result by deeding the property to charity during life while retaining a life estate. They will be entitled to an income tax charitable deduction for the value of charity’s remainder interest. In computing the present value of the remainder interest the improvements must be depreciated, on the straight-line method, for the life expectancy of the beneficiary.

Planned Giving in the Small Development Office

You may find yourself in the position of being the only person at your organization with planned giving responsibilities – and planned giving may be only a small part of your overall job description. Still, positive results are achievable if you can make planned giving a priority and
devote some time to it every week. Here are some simple ideas you can incorporate:

A. Become a one-person bequest solicitation program.

1. Get a basic wills brochure, with a bequest phrase for your organization, or start a wills mailing program, if you have the budget. Include bequest messages with every mailing — annual reports, thank-you letters, annual mailings, etc.
2. Start a wills society, with you and all board members as charter members.
3. Promote at every opportunity the fact that you are “in the business” of accepting bequests.
4. Change your stationery to include the tag line: “Have you included ______ in your will or living trust?”
5. Send out a survey card asking constituents if they (1) have included you in their wills or (2) will consider making a gift to you through their estate plans.

B. Include planned giving articles in your current publications (you can purchase “copy only” from publishers or perhaps find a volunteer professional to write for you).

C. Learn as much as you can about planned gift techniques; attend a comprehensive planned gift training seminar, then “keep your hand in” by attending at least one program a year that includes planned giving topics. Subscribe to a planned giving newsletter for fundraisers.

D. Touch base with the local Community Foundation. Excellent help often is available, especially if you place endowed funds with the Foundation.

E. Consider planned gift mailings, but only if you can follow up. Consultants can let you extend your follow-up capabilities and provide technical expertise.

F. Broaden the activities of your planned giving committee. Conduct “internal marketing” with staff and your board so they can provide planned gift referrals — and make gifts themselves.

G. Just because you can’t do everything you would like to do in planned giving, DO SOMETHING! Make it a priority.

MARC CARMICHAEL

Marc Carmichael, J.D., has worked in the field of charitable gift planning since 1976, and served as president of the R&R Newkirk Company, a leader in planned gift marketing, research and training, for 25 years. Marc has a bachelor’s degree in journalism from Indiana University and is a graduate of the Indiana University School of Law. He is a past president and board member
of the National Committee on Planned Giving (now the National Association of Gift Planners) and served on the board of directors of the Chicago Planned Giving Council. He has spoken at the national conferences of the National Association of Gift Planners, Association of Fundraising Professionals, National Catholic Development Council, American Council on Gift Annuities and the Association for Healthcare Philanthropy, and has chaired the National Conference on Planned Giving. He served for four years as chair of the editorial advisory committee of *The Journal of Gift Planning*. In 2005 he received the inaugural Russell V. Kohr Memorial award for excellence in gift planning from the Chicago Council on Planned Giving. Marc continues to write and speak on planned giving topics and appears frequently before donor and professional groups.

Marc Carmichael, J.D.
Attorney
15524 Janas Drive
Homer Glen, IL 60491
marccarmichael@msn.com
(708) 705-1246