

Principal  
Event  
Sponsor



BNY MELLON  
WEALTH MANAGEMENT

# **Jammin' for Success:**

## **Gift Annuities, Gift Planning and All That Jazz!**



# **Conference Proceedings**

---

29<sup>th</sup> Conference on Gift Annuities

---

**April 28-30, 2010 • Sheraton New Orleans Hotel**

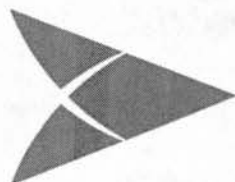
---

Presented by the American Council on Gift Annuities



The American Council on Gift Annuities

thanks



**BNY MELLON**  
**WEALTH MANAGEMENT**

**Principal Event Sponsor of the  
29th Conference on Gift Annuities**

**To Our Participants:**

Please refer to the conference program for a complete agenda, including room assignments. The program also includes a diagram of the exhibit hall with a list of exhibitors.

The views expressed in the papers presented in this publication are those of the authors and do not necessarily reflect the opinions of ACGA, its staff, or its board members. ACGA does not guarantee the accuracy of the authors' comments, and none of the material in these proceedings should be construed as legal advice. Readers are urged to consult their own legal counsel regarding any information found herein. Permission to reprint an individual paper must be secured from the author of that paper.

Neither ACGA nor the Sheraton New Orleans Hotel are responsible for lost or stolen conference proceedings. Replacement cost for the conference proceedings is \$60.

**Gift Annuities, Gift Planning & All That Jazz!**



## Jammin' for Success...

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010

**W**elcome to New Orleans and the 29th Conference on Gift Annuities! We appreciate the effort you have made to join us. Since 1927, the Conference on Gift Annuities has been a quality educational and networking event. Our Conference allows representatives from charities and consulting organizations the opportunity to gather together, share expertise, and enjoy the camaraderie.

The 29th Conference Committee, with Dan Garrett as its Chair, has been hard at work for two years to plan all the details of this conference. The Conference Committee has developed the

education program that will serve the needs of each of you. The committee has spent countless hours recruiting an outstanding faculty of the nation's most well-recognized speakers. They have been a hands-on, working committee from start to finish.

Our conference staff has carried out the plans of the conference committee with exemplary professionalism. From faculty communications and registration procedures through publication design and menu planning, the conference staff has worked with the committee, the faculty and the hotel staff to make this the best experience possible for you, our valued attendees.

While in New Orleans, you will find the ACGA Board at work monitoring educational sessions, taking meal tickets, and greeting our guests. Please take a moment to introduce yourself to any member of the board. We are eager to meet you and to learn about your needs as ACGA moves forward.

Most importantly, each of you has contributed to the success of this conference. We know that you have sacrificed precious time and professional development dollars to join us. We appreciate your confidence in us, and thank you for joining us. Please let any member of the conference team - committee, staff, board and hotel staff - know how we may better serve you.

*Lindsay L. Lapole*

ACGA President and Chairman of the Board



**Dan Garrett, Chair**

**Lynn Archer**

**Ronald A. Brown**

**Robert L. Coffman**

**Cam Kelly**

**David A. Libengood**

**Rebecca Locke**

**Edith E. Matulka**

**Laure W. Valentine**



**Gloria Kermeen, ACGA Director of Administration**

**Shana Dreher**

**Kay Ramsey**

**Katie Swisher**



# Table of Contents

## General Information

Message from Lindsay Lapole, ACGA President . . . . .	ii	Exhibit Hall Diagram . . . . .	xii
ACGA Conference Committee . . . . .	ii	Exhibitors . . . . .	xiii
ACGA Conference Staff . . . . .	ii	Sponsors . . . . .	xiii
ACGA Board of Directors . . . . .	iv	Conference Faculty Biographies . . . . .	xiv
Education Agenda . . . . .	v	Model Standards of Practice for the Charitable Gift Planner . . .	xxi

## Symposia

Transferring Values and Valuables . . . . .	3	Marketing Planned Gifts . . . . .	13
Presented by: Perry Cochell		Panelists: Douglas Page, Steven A. Rosenblum, Angela Woo Sosdian	
		Moderator: David Libengood	

## Thursday Morning Sessions

Understanding Gift Annuities . . . . .	25	Best Practices in Charitable Gift Annuity Programs . . . . .	89
Presented by: Elizabeth Brown		Presented by: Charles Gordy	
State Regulations Panel . . . . .	63	Investing CRT Assets . . . . .	97
Panelists: Timothy Costello, Kristofer Graap, Carol Harmon		Presented by: David G. Ely	
Moderator: Kristen Schultz		The Facts of Life (Estates):	
Gift Packages: Mix and Match to Maximize . . . . .	71	Remainder Interests in Residences and Farms . . . . .	109
Presented by: Grant Whitney		Presented by: David Wheeler Newman	
Gift Annuities During the Great Recession:		Gift Planning with Real Estate . . . . .	131
2009 ACGA Survey Results		Presented by: Philip M. Purcell	
Presented by: Ronald A. Brown			
(This presentation will be provided as a separate document and is not included in these proceedings)			

## Thursday Afternoon Sessions

Charitable Remainder Trust Basics . . . . .	161	Dead Men Do Tell Tales: Integrating Bequest Administration with Your Planned Giving Program . . . . .	231
Presented by: Joseph O. Bull		Presented by: Andrew Fussner	
What is the Financial Justification for your Gift Planning Program? . . . . .	183	Retirement Plan Gifts: Better Now or Later? . . . . .	241
Presented by: Kristen Dugdale & Richard W. Lawrence		Presented by: Timothy J. Prosser	
Would You Hire Actors Without a Script? Exploring the Role of eMarketing in a Strategic Marketing Plan . . . . .	193	Investing Charitable Gift Annuity Pool Assets . . . . .	255
Presented by: Ann McPherson & Gary Pforzheimer		Presented by: Damon L. Whelchel	
Non-Traditional Gift, Financial & Estate Planning . . . . .	219		
Presented by: Cindy Sterling			

**Friday Morning Sessions**

<b>Reform Roulette: Recent and Upcoming Changes in the Legal and Legislative Landscape</b> .....269 Presented by: Robert Harding	<b>Managing Risk in CGA Programs</b> .....325 Presented by: Bryan Clontz Note: This is a two-part session
<b>Maximizing Your Potential: Are You OK?</b> Presented by: Jack Beatty Note: This is a two-part session	<b>Charitable Lead Trusts</b> .....337 Presented by: Jeremiah Doyle
<b>Stewardship = Marketing</b> .....301 Presented by: Rachel F. Moore	<b>New Decade Gift Annuities</b> .....391 Presented by: A. Charles Schultz
<b>The Ethics of Philanthropy</b> .....311 Presented by: Gary Morris	<b>Evaluating Gift Annuity Programs</b> .....401 Presented by: Frank Minton

**2010 Board of Directors**

**Lindsay L. Lapole, President and Chairman of the Board**

Territorial Planned Giving Director  
The Salvation Army, USA Southern Territory

**Cam Kelly, Vice Chair**

Asst. Vice President for Principal Gifts Programs  
Duke University

**Laurie W. Valentine, Secretary**

Trust Counsel & Chief Operating Officer  
Kentucky Baptist Foundation

**Susan Gutchess, Treasurer**

Director of Gift Strategy and Administration  
The Nature Conservancy

**Robert L. Coffman, At-Large Executive Committee Member**

Vice President for Advancement  
Anderson University

**David Wheeler Newman, At-Large Executive Committee Member**

Chair, Charitable Sector Practice Group  
Mitchell Silberberg & Knupp

**Lynn Archer**

Vice President, Planned Giving  
American Heart Association

**Dianne Armstrong**

National Director of Gift Planning  
Planned Parenthood Federation of America, Inc.

**Ronald A. Brown**

Director of Gift Planning  
Princeton University

**David G. Ely**

Vice President  
State Street Global Advisors

**Karen Gallardo**

Senior Director of Gift Planning & Major Gifts  
AARP Foundation

**Dan T. Garrett**

President  
Abilene Christian University Foundation

**Charles B. Gordy**

Director, Planned Giving  
Harvard Law School

**Cynthia J. Halverson**

Executive for Development Services and  
President of the ELCA Foundation  
Evangelical Lutheran Church in America

**Carol J. Kersten**

Director of Planned Giving  
Stanford University Medical Center

**David A. Libengood**

Director, Relationship Management  
Kaspick & Company

**Rebecca Locke**

Senior Director, Gift Planning  
American Red Cross

**Edith E. Matulka**

Senior Consultant  
PG Calc

**Kristen Schultz**

Senior Vice President  
Crescendo Interactive

**Terry L. Simmons**

Senior Partner  
Thompson & Knight, L.L.P.

**James C. Soft**

President  
Yellowstone Boys & Girls Ranch Foundation

**Jeffrey K. Wilson**

Director, Planned Giving & Trust Services  
General Conference of Seventh-day Adventists

**Laird G. Yock**

Senior Philanthropic Advisor  
Colby College

**Counsel**

**Conrad Teitell**

**Actuary**

**Michael Mudry**



# Education Agenda

## Wednesday, April 28

- 8:00 am – 8:00 pm Registration Open
- 9:00 am – 3:00 pm Conference Primer – Fundamentals of Planned Giving (separate registration and fee required)
- 1:30 pm – 3:00 pm Symposium 1: Transferring Values with Valuables
- 3:30 pm – 5:00 pm Symposium 2: Marketing Planned Gifts
- 5:30 pm – 6:30 pm Grand Opening Reception
- 6:30 pm – 8:30 pm Opening Dinner/Keynote Address

### The Fundamentals of Planned Giving: Everything You Could Ask About Making Your Planned Giving Program Successful and Proactive

(separate registration and fee required)

9:00 am - 3:00 pm, Wednesday, April 28,

Presented by:

**Pamela Jones Davidson** • President • Davidson Gift Design • Bloomington, IN

**James E. Gillespie** • President & CEO • Commonwealth • Indianapolis, IN

This is the best investment of time you'll spend if you want essential information on virtually any aspect of establishing, running or refreshing a successful planned giving program. The presenters will address how to start a planned giving program, and how to assess if your organization is ready, plus what you may need to first remedy. They will offer a primer on the concepts (not all technical) behind top vehicles you should use, many involving little or no administration at your organization. They will also cover why donors consider gift plans, highlighting donor benefits from popular current uses, both lifetime and testamentary, of charitable gift options. The presenters will also cover smart enlistment strategies for board and committees, and policies and procedures for your program. The session will include marketing, how to introduce and educate your constituency about attractive gift options that can further individual planning goals, and will also address ethics in gift planning. You'll walk away with a lot of practical ideas you can use, and have fun too. These presenters are well known for their pragmatic yet dynamic style, sharing lots of illustrative donor stories and useable ideas to jumpstart and then sustain your proactive, ongoing planned giving effort.

### Symposium: Transferring Values and Valuables

(included in full conference registration fee)

1:30 - 3:00 pm, Wednesday, April 28

Presented by:

**Perry Cochell** • Senior Philanthropic Advisor • Boy Scouts of America • Irving, TX

This presentation explores the Heritage Process™ that incorporates clients' values, faith, family traditions, and work ethic with traditional tax and estate planning strategies. When parents leave their children financial assets but not the values, faith, traditions, and work ethic that built those assets, there is little chance the family fortune will survive into future generations. Recognizing this, values-based planning uses a "family first, fortune second" planning process that takes families beyond traditional tax and estate strategies. Through this process, families are guided in the construction of living plans that will benefit their heirs for generations to come. This six step process covers, the Initial Presentation, Guided Discovery Process™, Vision Statement, Implementing the Vision, Initial Family Retreat, and the Ongoing Family Councils.

### Symposium: Marketing Planned Gifts (included in full conference registration fee)

3:30 - 5:00 pm, Wednesday, April 28

Panelists:

**Douglas Page** • Senior Director, Gift Planning • Pacific Lutheran University • Tacoma, WA

**Steven A. Rosenblum** • Director of Planned Gifts • Saint Louis Zoo • St. Louis, MO

**Angela Woo Sosdian** • Director of Philanthropy for the Campaign and for Gift Planning • The Nature Conservancy • Arlington, VA

Moderator:

**David Libengood** • Relationship Manager • Kaspick & Company, LLC • Boston, MA

A panel discussion with three individuals responsible for marketing planned gifts at their charitable institutions. We will examine the various elements of marketing strategy, what has been working (or not), and what adjustments charities are making as a result of the difficult environment of the past two years.

## Education Agenda (continued)

### Opening Dinner Keynote Address: Economic Address (included in full conference registration fee)

6:30 – 8:30 pm, Wednesday, April 28

Presented by:

**Richard B. Hoey** • Chief Economist • The Bank of New York Mellon Corporation • New York, NY

The subject of this presentation is the outlook for economic policy and the world and U.S. economies. Key issues include monetary policy, fiscal policy, tax policy, energy policy, trade policy and the debate about how to deal with the demographic challenges of Social Security and Medicare. For the world economy, the main topics are real growth, oil prices, inflation and interest rates. Next is a discussion of the currency outlook, keyed to the prospects for the dollar, euro, yen and RMB. For the U.S. economy, the main topics are real growth, inflation, productivity, the budget outlook and profits. The bond market outlook includes a discussion of short-term rates, long-term rates, real yields and credit spreads.

## Thursday, April 29

7:30 am – 4:30 pm	Registration Open
7:30 am – 8:30 am	Continental Breakfast in Exhibit Hall
8:30 am – 9:45 am	Morning Breakouts
9:45 am – 10:15 am	Refreshment Break in Exhibit Hall
10:15 am – 11:30 am	Morning Breakouts Repeated
11:45 am – 1:15 pm	Rates Luncheon
1:30 pm – 2:45 pm	Afternoon Breakouts
2:45 pm – 3:15 pm	Refreshment Break in Exhibit Hall
3:15 pm – 4:30 pm	Afternoon Breakouts Repeated
4:30 pm – 5:45 pm	All That Jazz Reception
5:45 pm	Free evening

## Thursday, April 29 Morning Sessions

### Understanding Gift Annuities

Track: I

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Borgne – 3rd Floor

Presented by:

**Elizabeth Brown** • Assistant General Counsel • Moody Bible Institute of Chicago • Chicago, IL

This session will cover the basics of gift annuities, explaining the various types of annuity contracts, how the rates are established, the income, estate and gift tax implications, administration of a gift annuity program, and investing the annuity pool. The goal is to provide an overview and general understanding of all aspects of a gift annuity program.

### State Regulations Panel

Track: I & II

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Bayside A – 4th Floor

Panelists:

**Edie Matulka** • Senior Consultant • PG Calc • Seattle, WA

**Timothy C. Costello** • Chief of Valuation Bureau & Chairman of Life & Health Admissions Committee • New Jersey Department of Banking & Insurance • Trenton, NJ

**Kristofer Graap** • Auxiliary Lines Specialist, Company Supervision Division • Washington Office of the Insurance Commissioner • Olympia, WA

**Carol Harmon** • Senior Staff Counsel • California Department of Insurance • San Francisco, CA

Moderator:

**Kristen Schultz** • Sr. Vice President • Crescendo Interactive, Inc. • Camarillo, CA

This year's state regulations session is aimed at educating charities on the ongoing compliance requirements relating to state gift annuity registrations. Several individuals from state insurance departments will speak on a panel regarding regulatory issues relevant to their states. The goal is to educate charities on ways to comply with state law in issuing and administering gift annuities, with particular emphasis placed on meeting annual reporting requirements. The panel will be moderated and there will be time for Q&A from the audience.



### Gift Packages: Mix & Match to Maximize

Track: I & II

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Bayside B-C

Presented by:

**Grant H. Whitney** • Sr. Associate Director of Gift Planning • Harvard University • Cambridge, MA

In today's economy, current use gifts are at a premium. The gift planner who makes a "Double" or "Triple Ask" and can respond to immediate, near-term and long-term needs in one composite plan or gift package adds real value to both charity and donor. This presentation will highlight several such packages. Through case studies, attendees - regardless of shop size or time spent on gift planning - will come away with practical ideas to use back home.

### Gift Annuities During the Great Recession: 2009 ACGA Survey Results

Track: I, II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Rhythms Ballroom - 2nd Floor

Presented by:

**Ronald A. Brown** • Director of Gift Planning • Princeton University • Princeton, NJ

How has the economic crisis affected the number and value of annuity gifts? Are charities and their donors concerned about the funding levels for annuity reserves? Are charities continuing to follow the ACGA rate table of recommended maximum annuity rates? Who is making annuity gifts? The answers to these and many other critical questions will be reported publicly for the first time at this presentation.

### Best Practices in Charitable Gift Annuity Programs

Track: I, II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Waterbury Ballroom - 2nd Floor

Presented by:

**Charles B. Gordy** • Director of Planned Giving • Harvard Law School • Cambridge, MA

Many charities run successful charitable gift annuity programs that are invested appropriately, administered smoothly, and in compliance with Federal and State regulations. They may differ in how they get there and this paper presents what ACGA considers to be best practices in those programs. Additionally, in recent years gift annuities have come under increased scrutiny from

State regulatory agencies as abusive because of real or perceived illegalities engaged in by organizations offering gift annuities. Complying with gift annuity best practices should avoid this characterization and help ensure the continued success of gift annuities as a viable gift option for charitable organizations and their donors.

### Investing CRT Assets

Track: II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Maurepas - 3rd Floor

Presented by:

**David G. Ely** • Vice President, Charitable Asset Management • State Street Global Advisors • Boston, MA

This session will look at investing charitable remainder trusts. We will start with the basics of asset allocation and examine important considerations such as time horizon, percentage payout and risk tolerance. We will explore best practices used by organizations to implement asset allocation in remainder trusts. We will also examine the importance of timing in today's volatile marketplace

### The Facts of Life (Estates): Remainder Interests in Residences and Farms

Track: II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Nottoway - 4th Floor

Presented by:

**David Wheeler Newman** • Chair, Charitable Sector Practice • Mitchell Silberberg & Knupp LLP • Los Angeles, CA

This presentation will begin by identifying the situations in which a gift of a residence or farm, with retained life estate, may be the best philanthropic planning solution for a donor. We will next review the legal and tax requirements for these gifts, and the sometimes imaginative ways in which planners have run afoul of those requirements. Finally, we will look at selected planning opportunities to illustrate ways in which this gift vehicle may be effectively deployed in a variety of situations.

### Gift Planning with Real Estate

Track: II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Thursday, April 29

Location: Oak Alley – 4th Floor

Presented by:

**Philip M. Purcell** • Vice President for Planned Giving and Endowment Resources • Ball State University Foundation • Muncie, IN

This session will review the basics and beyond of gift planning with real estate, including outright gifts, bargain sales, remainder interests, gift annuities, charitable remainder trusts, lead trusts, conservation easements and more. Special attention will be given to important policies and procedures, such as environmental audits, title review, institutional approval, etc.

### Thursday, April 29 Afternoon Sessions

#### Charitable Remainder Trust Basics

Track: I

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Bayside B-C – 4th Floor

Presented by:

**Joseph O. Bull** • Senior Vice President for Community Engagement • Columbus Zoo and Aquarium • Powell, OH

The Charitable Remainder Trust is simultaneously the most versatile and the most complex of all charitable gift planning vehicles. Attendees will leave this session with an understanding of how CRTs work, the components of a CRT that most appeals to donors, and what questions to ask of legal counsel (both the donor's and your organization's).

#### What is the Financial Justification for Your Gift Planning Program?

Track: I & II

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Borgne – 3rd Floor

Presented by:

**Richard W. Lawrence** • Executive VP and Chief Operation Officer • University of Colorado Foundation • Boulder, CO

**Kristen Dugdale** • Vice President, Gift Planning • University of Colorado Foundation • Boulder, CO

In this session, the presenters will discuss their analysis to determine the cost to raise a planned gift dollar at the University of Colorado Foundation. This presentation will describe a methodology for quantitatively evaluating the power of a planned giving program, including; comparing the economic efficiency of planned giving versus major giving initiatives, a review of resource allocation decisions made by the Foundation and a review of actual outcomes compared to the projections in the model.

#### Would You Hire Actors Without a Script? Exploring the Role of eMarketing in a Strategic Marketing Plan

Track: I & II

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Nottoway – 4th Floor

Presented by:

**Ann McPherson** • Marketing Consultant • PG Calc • Cambridge, MA

**Gary Pforzheimer** • President • PG Calc • Cambridge, MA

If your Inbox looks like our presenters', you receive daily invitations to learn how various elements of eMarketing can "transform" your organization's fundraising capabilities. With social media added to the mix there's more eMarketing hype now than ever. So where do you start when the opportunity is seemingly endless? First, you must be clear about your strategic marketing goals in order to separate the buzz from the substance and determine what makes sense for you. We will discuss how and when to use eMarketing tactics, how they complement other media channels, and how eMarketing can help you achieve your overall marketing goals.

#### Non-Traditional Gift, Financial & Estate Planning

Track: I & II

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Oak Alley – 4th Floor

Presented by:

**Cindy Sterling** • Senior Associate • Washburn & McGoldrick, Inc. • New York, NY

Unmarried couples confront unique challenges when arranging their financial, estate and gift plans. For a variety of reasons, these individuals can be some of our best planned giving prospects. This talk will discuss several significant issues facing these prospects and help you better understand how to be a resource for them.

**Dead Men Do Tell Tales: Integrating Bequest Administration with Your Planned Giving Program**

Track: II & III

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Waterbury Ballroom – 2nd Floor

Presented by:

**Andrew Fussner** • VP - Estate Settlement • American Heart Association • St. Petersburg, FL

Bequest administration is usually the last step in the planned giving process - but it doesn't have to be. This session will cover ten tips for "completing the circle" between bequest administration and planned giving. A well-run bequest administration program should not only provide data to use for planned giving marketing, but actual planned giving leads as well.

**ACGA Rates: An Interactive Discussion**

Track: II & III

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Bayside A – 4th Floor

Panelists:

**David G. Ely** • Vice President, Charitable Asset Management • State Street Global Advisors

**Susan Gutchess** • Director of Gift Planning Administration • The Nature Conservancy • Arlington, VA

**Michael Mudry** • ACGA Actuary • St. Davids, PA

Moderator:

**Cam Kelly** • Assistant Vice President for Principal Gifts Programs • Duke University • Durham, NC

If you are curious how the ACGA Rates Committee conducts its work, join us for this in-depth panel discussion about the methodology, the assumptions, and other considerations.

**Retirement Plan Gifts: Better Now or Later?**

Track: II & III

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Rhythms Ballroom – 2nd Floor

Presented by:

**Timothy J. Prosser** • Vice President, Institutional Trust Consulting • TIAA-CREF Trust Co., FSB • St. Louis, MO

Retirement plan accumulations account for nearly one-third of U.S. household financial assets. Increased contribution limits and longer tax-deferral periods have fueled the growth of these accounts, making them a great potential source of charitable gifts. This session will help you understand the mechanics, as well as the pros and cons, of lifetime and testamentary retirement plan gifts. The session will also help you take advantage of Roth IRA conversions to spur donor conversations and benefit from continuation (and possible expansion) of IRA charitable rollover legislation.

**Investing Charitable Gift Annuity Pool Assets**

Track: II & III

1:30 - 2:45pm & 3:15 - 4:30 pm, Thursday, April 29

Location: Maurepas – 3rd Floor

Presented by:

**Damon L. Whelchel** • Associate Director of Investments • Kaspick & Company • Redwood Shores, CA

Charitable gift annuities have investment objectives, regulatory constraints, and risk profiles that are different from charitable remainder trusts or endowment funds. As a result, the investment and risk management processes for a gift annuity pool can differ from traditional portfolio management practices. This session will examine the risks of issuing gift annuities and the impact of the regulatory environment on portfolio design and account structure. It will also review how the risk profile of a gift annuity pool can change over time and in different market environments. Finally, it will address policy implications and how charities can better manage the liabilities associated with gift annuities today and in the future.

## Friday, April 30

- 7:30 am – 1:30 pm Registration Open
- 7:30 am – 8:30 am Continental Breakfast in Exhibit Hall
- 8:30 am – 9:45 am Breakout Sessions
- 9:45 am – 10:15 am Refreshment Break in Exhibit Hall
- 10:15 am – 11:30 am Breakout Sessions Repeated
- 11:45 am – 1:30 pm Closing Luncheon: Conrad Teitell

### Reform Roulette: Recent and Upcoming Changes in the Legal and Legislative Landscape

Track: I & II

8:30 - 9:45 am & 10:15 - 11:30 am, Friday, April 30

Location: Waterbury Ballroom – 2nd Floor

Presented by:

**Robert Harding** • Principal • Gray, Plant, Mooty, Mooty & Bennett, P.A. • Minneapolis, MN

Will Congress cancel the estate tax vacation? Will the lawmakers scale back the charitable deduction to help pay for health care reform? In the face of mounting deficits, will the IRA Rollover be extended? Place your bets now. We'll discuss the winners and losers in April. While Congress deliberates, the IRS and courts have not been idle. Abuse of the charitable deduction has moved up on the IRS hit list, and the Service has identified new scams involving CRTs. Treasury has promulgated more regulations on CRTs, substantiation of income tax charitable deductions, and CLT payments. "Charitable lid" estate tax planning with hard-to-value assets has come before the U.S. Tax Court. In an alarming trend, more donors and their families are asking state courts to grant them standing to sue charities for misusing their gifts. We will also cover anything else of interest that comes up between now and April.

### Maximizing Your Potential: Are You Okay?

Track: I & II

Two-part session: Part 1, 8:30 – 9:45 am, Friday, April 30  
Part 2, 10:15 – 11:30 am, Friday, April 30

Location: Nottoway – 4th Floor

Presented by:

**Jack Beatty** • President • C.O.R.E. Group USA • Scottsdale, AZ

If donors don't know they're "okay," then what happens to their gift giving? How will you provide value to your donors by helping them know if they're "okay?" This session will help you clarify for yourself where it is that you are today, where you want to go and how to get there. Learn more about how to create relationships through discovery, what to focus on to achieve success and how to be more self-aware of your own behavior.

### Stewardship = Marketing

Track: I & II

8:30 - 9:45 am & 10:15 - 11:30 am, Friday, April 30

Location: Bayside B-C – 4th Floor

Presented by:

**Rachel F. Moore** • Director, Campaign Initiatives & Leadership Support • Smith College • Northampton, MA

Your current donors are your best prospects. If you effectively steward planned giving donors you will be cultivating them to make additional gifts - planned, testamentary and outright. This session will offer some tried and true stewardship techniques, suggestions for getting your major gifts colleagues on board and some new ways of thinking about your planned giving marketing.

### The Ethics of Philanthropy

Track: I & II

8:30 - 9:45 am & 10:15 - 11:30 am, Friday, April 30

Location: Maurepas – 3rd Floor

Presented by:

**Gary Morris** • President • Morris Capital Corporation • Dallas, TX

This program explores the philosophical and psychological background of ethics; it provides an understanding of the application of the ethical standards of fairness, honesty, integrity and openness toward your service to prospective and existing donors and their beneficiaries. The program will review the development of an organizational and personal code built upon your professional Model Standards of Practice.

### Managing Risks in CGA Programs

Track: II & III

Two-part session: Part 1, 8:30 – 9:45 am, Friday, April 30  
Part 2, 10:15 – 11:30 am, Friday, April 30

Location: Borgen – 3rd Floor

Presented by:

**Bryan Clontz** • President • Charitable Solutions LLC •  
Jacksonville, FL

When the stock market is horrible, donors love gift annuities and charities hate them. This highly interactive session will cover many practical risk management best practices as well as some of the most recent research on the topic. Attendees will leave with much more confidence about their existing program as well as for new gift annuities going forward.

### Charitable Lead Trusts

Track: II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Friday, April 30

Location: Oak Alley – 4th Floor

Presented by:

**Jeremiah Doyle** • Senior Vice President • BNY Mellon Wealth  
Management • Boston, MA

This session will discuss the use of a charitable lead trust as a planned giving vehicle. The session will introduce the concept of charitable lead trusts and explain in general terms how they benefit both charity and the donor's family. Next, the session will outline the income, estate, gift and generation skipping tax consequences of using a charitable lead trust as a planned giving vehicle. Finally, the session will review the various situations in which a charitable lead trust may be useful to both the donor and charity.

### New Decade Gift Annuities

Track: II & III

8:30 - 9:45 am & 10:15 - 11:30 am, Friday, April 30

Location: Rhythms Ballroom – 2nd Floor

Presented by:

**A. Charles Schultz** • President • Crescendo Interactive, Inc. •  
Camarillo, CA

With the new decade, what will be prospects for gift annuities? Coming trends include more seniors, a quest for security and greater interest by professional advisors. Hear predictions about "New Decade Gift Annuitants," and share your feedback.

### Evaluating Gift Annuity Programs

Track: III

8:30 - 9:45 am & 10:15 - 11:30 am, Friday, April 30

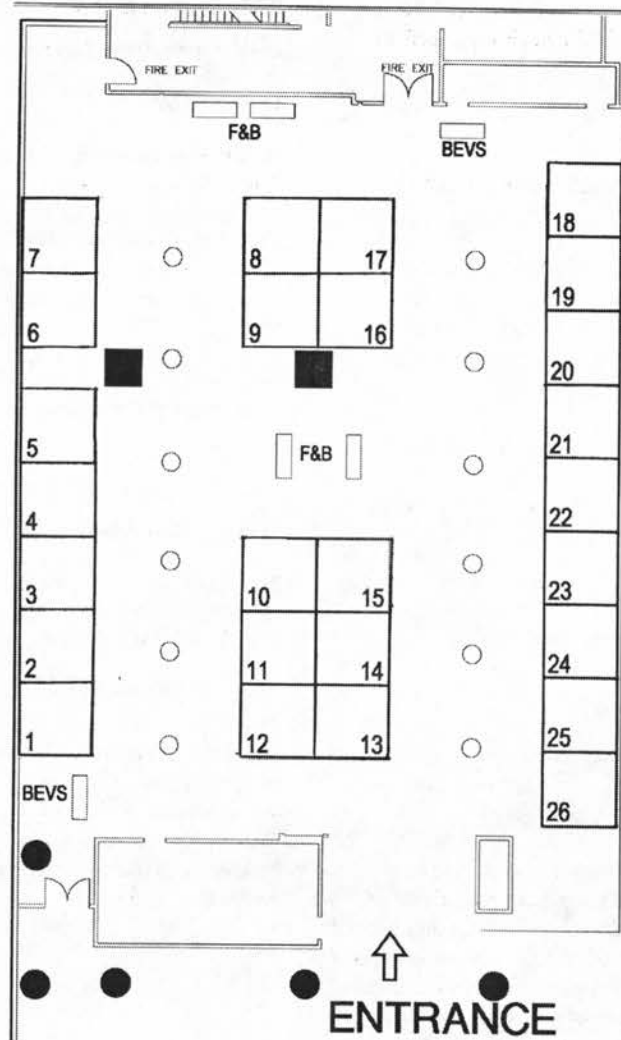
Location: Bayside A – 4th Floor

Presented by:

**Frank D. Minton** • Senior Advisor • PG Calc • Seattle, WA

Are your gift annuity reserves adequate to meet payment obligations? What residua are you likely to realize from existing annuities? Have you taken steps to control risk? Is your overall program profitable? These are the kinds of questions addressed in this session, which will discuss the methodology for auditing a gift annuity program, the information an audit should reveal, and how you can use this information to make the program more profitable.

# Exhibit Hall Diagram



Note: Exhibit Hall is Located on the Third Floor

## Exhibitors Listing by Booth Number

Booth	Exhibitor
1	Planned Giving Today/Mary Ann Liebert, Inc.
2	PNC Bank, N.A.
3	RuffaloCODY
4	The Stelter Company
5	eTapestry
6	Partnership for Philanthropic Planning
7	Endowment Development Services
8	The Charitable Capital Design Center
9	The Sharpe Group
10	Northern Trust
11	PG Calc
12	BNY Mellon Wealth Management
13	Crescendo Interactive, Inc.
14	Crescendo Interactive, Inc.
15	Pentera, Inc.
16	State Street Global Advisors
17	Wells Fargo Bank
18	MetLife
19	Cornerstone Planned Giving Services
20	R&R Newkirk
21	HWA International, Inc.
22	Kaspick & Company
23	Mutual of Omaha
24	BIPS LLC
25	The Six Bridges at Morgan Stanley Smith Barney
26	Charitable Solutions, LLC



# Exhibitors

Exhibitor .....	Booth	Exhibitor .....	Booth
BIPS LLC.....	24	Partnership for Philanthropic Planning .....	6
BNY Mellon Wealth Management .....	12	Pentera, Inc. ....	15
The Charitable Capital Design Center .....	8	PG Calc .....	11
Charitable Solutions, LLC .....	26	Planned Giving Today/Mary Ann Liebert, Inc.....	1
Cornerstone Planned Giving Services.....	19	PNC Bank, N.A. ....	2
Crescendo Interactive, Inc. ....	13 & 14	R&R Newkirk.....	20
eTapestry .....	5	RuffaloCODY.....	3
Endowment Development Services.....	7	The Sharpe Group.....	9
HWA International, Inc.....	21	The Six Bridges at Morgan Stanley Smith Barney.....	25
Kaspick & Company.....	22	State Street Global Advisors .....	16
MetLife .....	18	The Stelter Company.....	4
Mutual of Omaha .....	23	Wells Fargo Bank.....	17
Northern Trust.....	10		



# Sponsors

The American Council on Gift Annuities would like to extend a special thank you to our event and amenity sponsors!

## **BNY Mellon Wealth Management**

Principal Conference Sponsor

## **Crescendo Interactive**

Name Badge Holder Sponsor

## **Kaspick & Company**

Rates Luncheon Sponsor

## **Northern Trust**

All That Jazz Reception Sponsor

## **PG Calc**

Luggage Tag Sponsor

## **Mitchell Silberberg & Knupp**

General Conference Sponsor



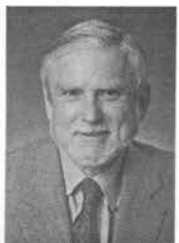
# Conference Faculty

## Conference Chair



**Dan Garrett** has worked for the past 35 years in the arena of fund development for not-for-profit organizations. He spent eleven years on the development staff of Abilene Christian University, where he personally directed major campaign efforts in both Annual Giving and Estate Planning. In 1984, Garrett joined the Baylor University Medical Center Foundation where he served as Vice President until October 1, 1994 when he formed the Garrett Group, a development and planned giving consulting firm. In addition to serving as president of the Garrett Group, he was appointed vice-chancellor of Abilene Christian University in 1995. In 1998 he was named the first ever President of The ACU Foundation. His professional experience has included face-to-face work with donors, as well as extensive contact and consultation with financial planning professionals. Garrett has consulted with professionals and individuals on estate plans of all sizes, securing avenues for more efficient transfer of assets and personal possessions.

## Keynote Address



**Richard B. Hoey** is chief economist of The Bank of New York Mellon Corporation, as well as chief economist of The Dreyfus Corporation. He is responsible for monitoring all aspects of the economic environment for The Bank of New York Mellon Corporation and Dreyfus including the U.S. economy, the global economy and currencies. He works closely with the heads of various specialized equity and fixed income teams at The Bank of New York Mellon Corporation and Dreyfus. Previously, Hoey spent nearly two decades as a chief economist, portfolio strategist and a member of both the investment policy and stock selection committees of a number of leading investment firms, including Prudential-Bache, A.G. Becker and Drexel Burnham Lambert.

## Plenary Sessions



**Lindsay L. Lapole** serves as Territorial Planned Giving Director for The Salvation Army-USA Southern Territory. In that role since 1986, Lindsay oversees the work of a professional staff of 34 serving donors in the 15 southeastern United States and District of Columbia. With over 30 years of planned giving experience, he provides training, marketing, and gift development expertise as well as quality control for the program. He has served on the Boards of

Directors of the Georgia Chapter of AFP, and Georgia Planned Giving Council where he served a President in 1996. Elected to the Board of Directors of the American Council on Gift Annuities in 1999, Lindsay served as Conference Chair, State Regulations Chair and Secretary before being elected President and Chairman of the Board of Directors in 2008.



**Cam Kelly** joined the University Development Office at Duke as assistant vice president for principal gifts programs in October 2008. She held advancement positions at her alma mater, Smith College, for seventeen years before coming to Duke; her most recent position was director of campaign & gift planning. She also served as special assistant to the president for strategic plan implementation in 2007 and 2008. Kelly held the position of director of planned gifts & bequests at Smith beginning in 1991, and assumed responsibility for the major gifts unit in 2005 and for campaign planning in 2007. Prior to joining Smith's advancement office she was an investment advisor and portfolio manager with an investment management firm in Boston. Kelly has served on the board of the American Council on Gift Annuities since 1994. She currently chairs its Rates Committee and serves as Vice Chair for the organization. She is a member of the Editorial Advisory Board of Planned Giving Today.



**Conrad Teitell** has lectured in all 50 states and on PBS television on taxes, estate planning and philanthropy. He is a commentator on NPR's Marketplace. He is a principal in the law firm of Cummings & Lockwood in Stamford, Connecticut, and chairs the firm's Charitable Planning Group. He is an adjunct visiting professor at the University of Miami School of Law. In addition to lecturing on taxes and estate planning, he writes extensively on those topics. Among his tax articles are columns in *Trusts & Estates* magazine and the *New York Law Journal*. He is the author of the five-volume treatise, *Philanthropy and Taxation* and writes in the monthly newsletter *Taxwise Giving*. His column, *Speaking and Writing*, has appeared in *The American Bar Association's Journal* and in *TRIAL*, the magazine of *The American Association for Justice*. Teitell is the recipient of ACGA's Lifetime Achievement Award, the Partnership for Philanthropic Planning's Distinguished Service to Philanthropy Award and the American Law Institute/American Bar Association's Harrison Tweek Award for Special Merit in Continuing Legal Education.



## Symposia



**Perry L. Cochell** was appointed to the position of National Senior Endowment Counsel, National Boy Scouts of America Foundation in 2006. In this position he works closely with the foundation director, related national and regional staff, and the foundation advisory committee to secure major gifts to the BSA, BSA-Foundation and/or local councils. Cochell began his career with the Boy Scouts of

America in September 1994 in the position of associate regional director/senior endowment counsel, Western Region. In this capacity, he has supported council professionals and volunteers in the development and implementation of endowment programs. He has provided technical expertise in all areas of tax for current and deferred gifts to councils. Cochell has practiced in the areas of Business, Benefits, and Trusts and Estates Tax Law. In addition to private law, Perry also was employed as Professor at the Scottsdale University of Law in Arizona.



**David Libengood** is a relationship manager at Kaspick & Company, LLC in Boston, Massachusetts. He consults with the firm's clients on a wide variety of gift planning, administration, investment, and program management issues. He has over 20 years of experience in the planned giving profession, has spoken at regional and national conferences, and serves as a member of the Board of

Directors of the American Council on Gift Annuities (ACGA). Prior to joining Kaspick & Company in 2001, he was responsible for gift planning and administration, bequest monitoring, and the investment of life income gifts for a large planned giving program at The First Church of Christ, Scientist in Boston. Libengood is a Certified Trust and Financial Advisor (CTFA), and is a past President of the Planned Giving Group of New England.



**Douglas Page** is in his 11th year as the Senior Development Director for Gift Planning at Pacific Lutheran University in Tacoma, Washington. With over 23 years of fundraising experience, Page is responsible for raising current and deferred gifts in support of the mission of PLU. His previous experience include serving as the director of planned giving at the University of Puget Sound in Tacoma,

Washington, Saddleback Memorial Foundation in Laguna Hills, California, and at his alma mater, California Lutheran University in Thousand Oaks. Page serves on the board of directors for Mt. Rainier Lutheran High School in Tacoma; and is President of the Association of Lutheran Development Executives (ALDE).



**Steven Rosenblum** has been the Director of Planned Gifts at the Saint Louis Zoo in Saint Louis, Missouri since 2005. He brings a wealth of knowledge in the areas of charitable gifts and estate planning from his seven years at Washington University and his work with the St. Louis Planned Giving Council Board and Leave A Legacy program where he serves as co-chair. Steven is also the co-chair of the Legacy Awards Dinner and serves on the planning committee for the "Will to Give" program.



**Angela Woo Sosdian** is director of philanthropy for the campaign and for gift planning at The Nature Conservancy in Arlington, Virginia. She manages the Conservancy's planned giving program, which includes 17,000+ Legacy Club members and \$120+ million in annual estate distributions. Sosdian also oversees the organization's \$1.6 billion Campaign for a Sustainable Planet, which also has an additional \$1 billion deferred gift goal. In 2005, she received the Conservancy's Lifetime Achievement Award for professional excellence. Sosdian has served as an officer and board member of the National Committee on Planned Giving (now the Partnership for Philanthropic Planning), served on the Conference Committee for the 1st National Conference on Philanthropic Planning, the 15th National Conference on Planned Giving, was a member of the NCPG Gift Valuation Task Force, and is an Editorial Advisory Committee member of the Journal of Gift Planning. She is a past board member of the National Capital Gift Planning Council, and in 2006 received that organization's Distinguished Service Award.

## Planned Giving Fundamentals



**Pamela Jones Davidson** has been a nationally recognized speaker in charitable gift planning for over 24 years. She is President of Davidson Gift Design in Bloomington, Indiana, a consulting firm specializing in gift planning, planned giving program design and implementation, and training. From 1985 through 1996, she was with Indiana University Foundation as its Executive Director of Planned Giving and Associate

Counsel. She has been an examiner in the Estate and Gift Tax Division of the Internal Revenue Service, and practiced law with an Indianapolis law firm before joining the nonprofit sector in 1985. Davidson was the 1999 President (now, Chair) of the National Committee on Planned Giving (now, Partnership for Philanthropic Planning, PPP) after serving on its board in various capacities for six years. As a past president, she is a past member and chair of its Ethics Committee. She serves on the Editorial Board of the Planned Giving Design Center. Ms. Davidson is a past board member and treasurer of the Indiana Chapter of the National Society of Fund Raising Executives (now, Association of Fundraising

## Conference Faculty (continued)

Professionals,AFP), and a past board member and president of the Planned Giving Group of Indiana. She serves on the Community Advisory Boards of both of her local public radio and television stations, and is, among other local boards, on the Board and past president of Middle Way House, her community's nationally recognized women's shelter.



**Jim Gillespie** is president of CommonWealth, a firm that, since 1995, has been providing comprehensive counsel in the area of planned and major gift development, annual funds and capital campaigns, and specializes in training, mentoring and professional development. He was chief operating officer of the consulting division of Renaissance Inc. for six years and was a professional development officer for almost 30 years. Gillespie served Junior Achievement and Tri-County Mental Health Foundation in Indianapolis, and was later recruited to the Indianapolis Symphony Orchestra as Chief Development Officer. He served Riley Children's Foundation, the fund raising arm of Riley Hospital for Children, as Interim Vice President for Development. Gillespie consults with a variety of charitable organizations, providing expertise in the design and implementation of capital and planned giving programs; developing a charitable infrastructure for planned giving; training and mentoring staff and volunteers. Gillespie is a contributing author and creator of the past three editions of "Planned Giving: Getting The Proper Start," published by a unit of Indiana University's Center on Philanthropy. He recently wrote a segment for Dr. Lilya Wagner's award-winning book, "Careers in Fundraising," published by John Wiley & Sons. Gillespie is a lead faculty member of The Fund Raising School, a unit of Indiana University's Center on Philanthropy. He has served as a member of the Center on Philanthropy's Research Committee.

## Breakout Sessions



**Jack C. Beatty** founded C.O.R.E. Group USA Inc., a firm that provides financial services firms and advisors strategies, tools and methods, enabling them to create and fulfill their High Priority Life Balance and maximize their potential. Having been in the financial services industry over 35 years, it was clear to Beatty that changes must be made to provide the kind of advice clients want from financial advisors. Through 11 years of process creation and testing, the C.O.R.E. program evolved, providing a platform for advisors to fulfill client expectations. Beatty is a faculty member of The Heritage Institute, which provides members a proven, credible process by which the individuals, families and organizations with whom they work can pass both their values and their valuables to the people they love and the causes they support.



**Elizabeth A. S. Brown** is an attorney and Certified Public Accountant, and serves as Assistant General Counsel of The Moody Bible Institute of Chicago. Prior to joining Moody in 1983, she was an Associate Attorney with McDermott, Will & Emery in Chicago. Brown recently retired from full time employment, but continues on a part time basis to assist donors with estate planning matters, and otherwise provide legal support for Moody's planned giving function. Throughout her 26 years of full time service at Moody, she has also carried general legal and management responsibilities, including oversight of investment and financial matters. Brown served on the Board of the American Council on Gift Annuities for over 20 years.



**Ron Brown** is Director of Gift Planning at Princeton University in Princeton, New Jersey. He is a Certified Financial Planner (CFP) with 30 years of experience in working with high-net-worth individuals and their professional advisors. Brown is currently a board member and Chair of the Research Committee for the American Council on Gift Annuities (ACGA). He has served as a board member of the Partnership for Philanthropic Planning (formerly National Committee on Planned Giving), president of the New Jersey Gift Planning Council, founding chair of LEAVE A LEGACY® New Jersey, and President of the CANARAS Planned Giving Council. Prior to joining Princeton in 1996, he served as Director of Planned Giving at United Way of America and the National Wildlife Federation. He has been a member of the board of Planned Giving Today and is a frequent speaker at professional conferences.



**Joseph O. Bull** joined the Columbus Zoo and Aquarium on February 9, 2009 as Senior Vice President for Community Engagement, leading the Zoo's philanthropy, marketing, membership and communications functions. Prior to this appointment, he was affiliated with the Worldwide Office of The Nature Conservancy as Interim Director of Philanthropy for Strategic Gifts and as Senior Philanthropy Officer for Global Priorities. Bull also provided 16 years of service to his alma mater, The Ohio State University. For 13 of those years, he served as the university's Director of Planned Giving. With 24 years of experience in the philanthropic arena, he began his career at Duke University and North Carolina State University. He was the 2005 Chair of the Board of the Partnership for Philanthropic Planning, having served two terms on the Partnership's Board of Directors. Additionally, he serves as a member of the Editorial Advisory Board for the national newsletter Planned Giving Today, the Editorial Board of the web-based Planned Giving Design Center and as a faculty member for The Academy of Gift Planning. Bull is a former member of the Boards of Directors of the American Council on Gift Annuities and Charitable Accord, as well as a past President of the Central Ohio and North Carolina Planned Giving Councils. He was co-chair of COPGC's Leave A

Legacy initiative, which became the model for the Partnership's national initiative of the same name. He is admitted to the Ohio and North Carolina bars.



**Bryan Clontz** is the president and co-founder of Charitable Solutions, LLC. Over the last 15 years, he has served as the director of planned giving for the United Way of Metropolitan Atlanta, director of planned giving at the national office of Boys & Girls Clubs of America and as vice president of advancement at The Community Foundation for Greater Atlanta. From 2000-2005, he served as a part-time

graduate instructor teaching personal financial planning in the Department of Risk Management and Insurance in Georgia State University's J. Mack Robinson School of Business. In addition to writing more than a dozen articles for financial services and planned-giving journals, he authored a planned giving manual entitled *Just Add Water*, which has sold more than 2,000 copies. Clontz serves on the Partnership for Philanthropic Planning Board of Directors (2007-2010), editorial board of the *Planned Giving Design Center*, the Rate Recommendation and the Research Committee of the American Council on Gift Annuities, and on the Advisory Board of the American College Chartered Advisor in Philanthropy (CAP) designation program.



**Timothy Costello** has served as Chief of the Valuation Bureau at the New Jersey Department of Banking & Insurance since 2007 and served as Assistant Chief from 1996 until his promotion to Chief. As Chief of the Valuation Bureau, he oversees the admission of charities seeking Special Permits to issue charitable gift annuities in New Jersey and the checking of the actuarial reserves of Special

Permit holders. Costello also sits on four State of New Jersey retirement program boards: the New Jersey State Employees Deferred Compensation Plan; the Supplemental Annuity Collective Trust of New Jersey; the New Jersey Defined Contribution Retirement Program; and the Pension Provider Selection Board.



**Jeremiah Doyle** is an estate planning strategist for BNY Mellon's Private Wealth Management group and a Senior Vice President of Bank of New York Mellon. He has been with the firm since 1981. Doyle provides high net worth individuals and families throughout the country with integrated wealth management advice on how to hold, manage and transfer their wealth in a tax efficient manner. He is the editor and

co-author of the of *Preparing Fiduciary Income Tax Returns*, a contributing author of *Preparing Estate Tax Returns*, a contributing author of *Understanding and Using Trusts*, a contributing author of *Drafting Irrevocable Trusts in Massachusetts* all published by Massachusetts Continuing Legal Education and a reviewing editor of the *1041 Deskbook* published by Practitioner's Publishing Company. Doyle served as president of the Boston Estate Planning

Council and a member of its Executive Committee and was a 20-year member of the Executive Committee of the Essex County Bar Association. He was named as the "Estate Planner of the Year" in 2009 by the Boston Estate Planning Council.



**Kristen L. Dugdale** is the Vice President for Gift Planning at the University of Colorado Foundation. She first began working in Gift Planning in 1998. She has also practiced law with the Denver law firm of Holmes, Roberts & Owens, LLP, and was the General Counsel of Sovereign Financial Services, a former private equity investment consulting firm. Kristen

received both her undergraduate & law degree from the University of Wyoming. She has spoken twice at the NCPG National Conference.



**David Ely** is a Vice President of State Street Global Advisors and a Portfolio Manager and Investment Team Leader in the firm's Charitable Asset Management Group (CAM). He is responsible for setting asset allocation strategy and managing charitable gift portfolios for all CAM customers. Prior to joining State Street in 1999, Ely worked for Salomon Smith Barney's Private Client Group. He has earned

the Chartered Financial Analyst Designation and is a member of the Boston Security Analysts Society, as well as the CFA Institute. David is also a Board member of the American Council on Gift Annuities and serves on the CAM Investment and Annual Account Review Committees.



**Andrew Fussner** serves as the national vice president of estate settlement for the American Heart Association (AHA) and oversees the administration of nearly \$100 million in bequest assets annually for the organization. He is based in St. Petersburg, Florida. Previously he served as the vice president of planned giving for the AHA's Florida Affiliate and as the AHA's Director of Planned Giving for the west coast

of Florida. Prior to joining the AHA, Fussner was an attorney with the Tampa office of the national law firm of Foley & Lardner. He specialized in estate planning, probate/trust administration and tax



**Charles B. Gordy** is the Director of Planned Giving at Harvard Law School. Prior to joining Harvard Law School, he managed planned giving services for The Bank of New York, and was the Director of Planned Giving at Yale University and at Tufts University. He is on the board of the American Council on Gift Annuities, chairs its Scholarship Committee, and sits on its Rates Committee and State Regulations Committee.

Gordy has recently joined the editorial advisory board of *Planned Giving Today*. He has served on the boards of the National Committee on Planned Giving, the Planned Giving Group of

## Conference Faculty (continued)

Greater New York, and the Planned Giving Group of New England. He is a frequent speaker nationally and regionally on topics related to planned giving.



**Kristofer Graap** has been with the Washington Office of the Insurance Commissioner since 1995, and has spent the last nine years working with auxiliary line entities such as CGA-issuing charities. Prior to a brief stint at Safeco Insurance, he spent ten years teaching math to junior and senior high school students. Outside of the office, Kris presently serves as corporate secretary

for the Scottish Rite Foundation of Washington, which annually provides over a quarter-million dollars of graduate fellowships and undergraduate scholarships to Washington residents.



**Susan Gutches** has had considerable experience in planned giving and the preservation of both historic properties and the environment. She is currently the Director of Gift Administration and Stewardship at The Nature Conservancy. She also serves as Treasurer of the American Council on Gift Annuities (ACGA), where she is a member of the Rates Committee. Previously, Gutches

she worked for many years at the National Trust for Historic Preservation where she was the Director of Planned Giving. She directed the team that originally established the Gifts of Heritage program, the Trust's unique program for the donation and protection of historic houses.



**Robert E. Harding** joined the Gray Plant Mooty law firm in 1983 and has been a principal since 1989. For most of his 26 years of practice he has focused exclusively on charitable gift matters and related tax-exempt organization issues. He represents colleges, universities, healthcare systems and other nonprofit organizations, primarily in the upper midwest. He speaks regularly at regional and

national conferences on charitable gift planning, and publishes an e-newsletter on charitable giving called *What Gives?*



**Carol Harmon** has practiced law in California since 1978. An Illinois native, she practiced civil litigation in San Francisco for 12 years before joining, in 1992, the California Department of Insurance at the San Francisco headquarters of its Legal Division. While she deals with virtually all matters filed by insurance companies with the Corporate Affairs Bureau, including Certificate of

Authority applications, mergers and acquisitions, and stock permits, she has a special affinity for non-profit licensees of charitable gift annuities. In the past several years, she has licensed hundreds of additional "Grants and Annuities Societies"

in California, and has recently revised the Application Forms and Instructions packet for prospective licensees and seen it added to the Department's award winning website.



**Richard W. Lawrence** is the executive vicepresident and chief operating officer at the University of Colorado Foundation in Boulder, Colorado. Previously, he served as the university's senior vice president, administration and chief financial officer. Before entering the nonprofit sector, Lawrence spent more than 25 years in the banking field, having served as executive vice president of Vectra Bank Colorado.



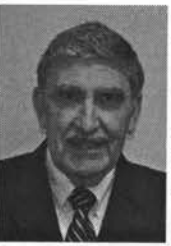
**Edie Matulka** is a senior consultant in the Seattle, Washington office of PG Calc. She has assisted charities in complying with state regulations for issuance of gift annuities since 1997. In addition to the practice of law, Edie's background includes work in government, public, and nonprofit settings. She is the primary author of certain chapters of *Charitable Gift Annuities: The Complete Resource Manual*, and

has spoken on gift annuities and state regulation at a number of conferences. She currently serves on ACGA's State Regulations Committee.



**Ann McPherson** joined PG Calc in 2001 as Vice President of Business and Strategic Development. In that role, she focused on corporate strategy, identifying and pursuing new business opportunities, and establishing strategic partnerships. Her move into a Marketing Consultant role was a logical result of the industry's need for strong marketing experience and expertise and her own extensive marketing

background in Internet marketing, business development, and brand management. Prior to PG Calc, McPherson held senior management positions in the Internet divisions of Inc. Magazine, Hill Holiday Advertising, and Lotus Development Corporation.



**Frank Minton** founded Planned Giving Services, a consulting firm that built an exceptional national reputation and was acquired by PG Calc in August 2005. Before entering consulting in January 1991, he spent ten and one-half years with the University of Washington, where he served as Director of Planned Giving and Executive Director of Development. Minton has played a critical role in shaping the planned giving

industry as we know it today. He has served both as conference chair and board chair of the National Committee on Planned Giving, (now the Partnership for Philanthropic Planning). In 1992 he received its Distinguished Service Award. He is an extensively recognized expert on gift annuities and has served as Chair of the American Council on Gift Annuities. He has also received a CASE (Council for the Advancement and Support of Education)

Distinguished Service Award, the David Donaldson Distinguished Service Award from the Planned Giving Group of New England, and was the first recipient of the Outstanding Development Officer Award from the Northwest Development Officers Association. He is the principal author of *Charitable Gift Annuities: The Complete Resource Manual* and is co-author of *Planned Giving for Canadians* (Second Edition, 1997). A number of his presentations have been to Canadian audiences, and in 1997, he received the "Friend of the Canadian Association of Gift Planners" award. He is on the advisory board of *Planned Giving Today*, and is a member of the Seattle Estate Planning Council and the Washington Planned Giving Council.



**Rachel Moore** is Director of Campaign Initiatives and Leadership Support at Smith College in Northampton, Massachusetts. Prior to stepping into this position one year ago she was Director of Gift Planning at Williams College in Williamstown, Massachusetts for six years, and for ten years before that she was a major and planned gifts officer at Smith. She is the immediate past president of the Planned Giving Group of New England and is a member of CANARAS. She currently serves on the board of Community Involved in Sustaining Agriculture, pioneers of the "Be a Local Hero - Buy Locally Grown" campaign.



**Gary Morris** established an individual investment advisor practice in December 1991. He previously served as president of a Dallas-based investment advisory firm. Morris is a registered investment adviser with the Securities and Exchange Commission. He serves as vice president of the Estate Planning Council of North Texas and serves on the board of directors of the North Texas Chapter of the Partnership for Philanthropic Planning.



**Michael Mudry** is a retired actuary, having worked for the Hay Group in Philadelphia, Pennsylvania. For many years Mudry has been a member of and consultant to the ACGA board, offering his actuarial talents to the Rates Committee. He has made presentations on gift annuity rates at many ACGA conferences.



**David Wheeler Newman** chairs the Charitable Sector Practice Group at the Los Angeles law firm of Mitchell Silberberg & Knupp LLP. For what seems to him like forever he has advised families and individuals concerning their foundations and other philanthropy, as well as charitable organizations and their donors on the legal and tax aspects of planned giving. David is a former member of the Board of the

National Committee on Planned Giving, where he served as an officer and member of its executive committee, and is currently

on the Board of Directors of the American Council on Gift Annuities. He is a founder and President Emeritus of New Roads School in Santa Monica and a member of the Professional Advisors Council of the Los Angeles Chamber Orchestra.



**Gary Pforzheimer** has directed all aspects of PG Calc since its inception in 1985. A leader in the fundraising community, Pforzheimer has spoken on planned gift development, marketing, administration, and technology-related topics to numerous groups, including planned giving councils across the country, The American Council on Gift Annuities (ACGA), and the National Committee on Planned Giving (NCPG). Gary is the Board Chair of NCPG's successor organization, the Partnership for Philanthropic Planning (PPP), and has received the David Donaldson Distinguished Service award from the Planned Giving Group of New England (PGGNE).



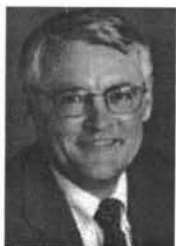
**Timothy J. Prosser** joined TIAA-CREF Trust Company in April 2000. He directs the delivery of planned giving technical consulting services to the Company's institutional clients. Prior to joining TIAA-CREF, Prosser practiced law in St. Louis with the firms of Sonnenschein Nath & Rosenthal and Armstrong Teasdale Schlafly & Davis, focusing his practice on estate planning, trust and estate administration and complex litigation in state and federal courts. Prosser is a board member of the Partnership for Philanthropic Planning (formerly National Committee on Planned Giving), a board member and past president of the Saint Louis Planned Giving Council, a past chair of Leave a Legacy® St. Louis and a member of several professional organizations, including the Missouri Bar, the Bar Association of Metropolitan St. Louis and the Estate Planning Council of St. Louis. He speaks widely on charitable planning topics and serves on the planned giving advisory councils of several not-for-profit organizations in the St. Louis area.



**Philip M. Purcell** is vice president of planned giving and endowment stewardship for the Ball State University Foundation in Muncie, IN, where he oversees a planned giving and endowment stewardship program with a staff of six, providing planned and endowment giving technical support service to twelve major gift officers. He has been involved in planned giving for over twenty years. He is a member and past president of the Planned Giving Group of Indiana and formerly served on the Partnership for Philanthropic Planning Board of Directors. Purcell currently serves as a volunteer on the Tax Exempt Organization Advisory Council for the Internal Revenue Service (Great Lakes States region). He teaches courses on Law and Philanthropy, Nonprofit Organization Law and Planned Giving as adjunct faculty for the Indiana University School of Law (Bloomington) and Indiana University Center on Philanthropy and Fundraising School (Indianapolis). He has

## Conference Faculty (continued)

consulted on behalf of all types of charitable organizations, including the Lilly Endowment's GIFT program serving community foundations throughout Indiana.



**A. Charles Schultz** is a California attorney who specializes in charitable giving and estate planning. He is President of Crescendo Interactive, Inc. and is the principal author of the Crescendo Planned Giving Software and the GiftLegacy Pro eMarketing System. Each year he is producer and moderator for the popular GiftLaw teleconferences. In addition, he is editor for the GiftLaw.com charitable tax planning

web site, the GiftLaw Pro charitable tax service and also edits the weekly GiftLaw and GiftLegacy eNewsletters. Schultz writes, speaks and publishes extensively. He teaches over 30 planned giving seminars per year and is the creator of GiftCollege.com, an Internet education program for gift planners and professional advisors. Charles assists a select group of business owners/trustees of major charities in charitable estate planning. Schultz is Chair of the Board of the Christian Foundation of the West.



**Kristen Schultz** is Senior Vice President for Crescendo Interactive, Inc. She is responsible for tax planning support, client education, and consultation for Crescendo's software and Internet services. Schultz has experience working with non-profits, colleges and universities in both the private and government sectors. Previously, she served as Counsel to the Assistant Secretary of Education in

Washington, D.C. Prior to that, she was Oversight Counsel to the Committee on the Judiciary of the U.S. House of Representatives. Schultz serves as a member of the ACGA State Regulations and Communications Committees, the Editorial Advisory Board of Planned Giving Today, and the Ventura County Planned Giving Council.



**Cindy Sterling** is a senior associate with Washburn McGoldrick, Inc. in New York City. She brings nearly 20 years of gift planning and major gifts experience to the organization. Previously, she served as director of gift planning at Vassar College in Poughkeepsie, New York. Sterling is a well-known authority on women's philanthropy, having written articles and given numerous talks on "Women's

Philanthropy: Gender Differences in Planned Giving." She was awarded the Steuben Apple Award from CASE for speaking excellence.



**Damon Whelchel** is associate director of investments at Kaspick & Company, a member of the TIAA-CREF family of companies. Kaspick & Company specializes in investing and administering charitable remainder trusts, gift annuity pools, and endowments for charities nationwide. Mr. Whelchel joined Kaspick & Company in 1997 with responsibilities that include portfolio design and analysis, manager

selection and oversight, and trading. His prior experience includes economic and financial market research for Wells Fargo Bank and Treasury debt market analysis for MMS International/Standard and Poor's.



**Grant Whitney** is the Senior Associate Director of Gift Planning for the Faculty of Arts and Sciences (FAS) at Harvard University in Cambridge, Massachusetts. He has over twelve years of major gift and gift planning experience. In addition to day-to-day gift planning work, Whitney manages the John Harvard Society, the FAS stewardship and recognition society for donors who make life income gifts and/or notify

the institution of a bequest intention. Before coming to Harvard, he started the planned giving program at Lesley University, also in Cambridge. He led the program through Lesley's first-ever comprehensive capital campaign. Whitney is a past president and of the Planned Giving Group of New England.



# Model Standards of Practice for the Charitable Gift Planner

## **Preamble**

The purpose of this statement is to encourage responsible gift planning by urging the adoption of the following Standards of Practice by all individuals who work in the charitable gift planning process, gift planning officers, fund raising consultants, attorneys, accountants, financial planners, life insurance agents and other financial services professionals (collectively referred to hereafter as "Gift Planners"), and by the institutions that these persons represent.

This statement recognizes that the solicitation, planning and administration of a charitable gift is a complex process involving philanthropic, personal, financial, and tax considerations, and often involves professionals from various disciplines whose goals should include working together to structure a gift that achieves a fair and proper balance between the interests of the donor and the purposes of the charitable institution.

## **I. Primacy of Philanthropic Motivation**

The principal basis for making a charitable gift should be a desire on the part of the donor to support the work of charitable institutions.

## **II. Explanation of Tax Implications**

Congress has provided tax incentives for charitable giving, and the emphasis in this statement on philanthropic motivation in no way minimizes the necessity and appropriateness of a full and accurate explanation by the Gift Planner of those incentives and their implications.

## **III. Full Disclosure**

It is essential to the gift planning process that the role and relationships of all parties involved, including how and by whom each is compensated, be fully disclosed to the donor. A Gift Planner shall not act or purport to act as a representative of any charity without the express knowledge and approval of the charity, and shall not, while employed by the charity, act or purport to act as a representative of the donor, without the express consent of both the charity and the donor.

## **IV. Compensation**

Compensation paid to Gift Planners shall be reasonable and proportionate to the services provided. Payment of finder's fees, commissions or other fees by a donee organization to an independent Gift Planner as a condition for the delivery of a gift is never appropriate. Such payments lead to abusive practices and may violate certain state and federal regulations. Likewise, commission-based compensation for Gift Planners who are employed by a charitable institution is never appropriate.

## **V. Competence and Professionalism**

The Gift Planner should strive to achieve and maintain a high degree of competence in his or her chosen area, and shall advise donors only in areas in which he or she is professionally qualified. It is a hallmark of professionalism for Gift Planners that they realize when they have reached the limits of their knowledge and expertise, and as a result, should include other professionals in the process. Such relationships should be characterized by courtesy, tact and mutual respect.

## **VI. Consultation with Independent Advisers**

A Gift Planner acting on behalf of a charity shall in all cases strongly encourage the donor to discuss the proposed gift with competent independent legal and tax advisers of the donor's choice.

## **VII. Consultation with Charities**

Although Gift Planners frequently and properly counsel donors concerning specific charitable gifts without the prior knowledge or approval of the donee organization, the Gift Planner, in order to insure that the gift will accomplish the donor's objectives, should encourage the donor early in the gift planning process, to discuss the proposed gift with the charity to whom the gift is to be made. In cases where the donor desires anonymity, the Gift Planner shall endeavor, on behalf of the undisclosed donor, to obtain the charity's input in the gift planning process.

## **VIII. Description and Representation of Gift**

The Gift Planner shall make every effort to assure that the donor receives a full description and an accurate representation of all aspects of any proposed charitable gift plan. The consequences for the charity, the donor and, where applicable, the donor's family, should be apparent, and the assumptions underlying any financial illustrations should be realistic.

## **IX. Full Compliance**

A Gift Planner shall fully comply with and shall encourage other parties in the gift planning process to fully comply with both the letter and spirit of all applicable federal and state laws and regulations.

## **X. Public Trust**

Gift Planners shall, in all dealings with donors, institutions and other professionals, act with fairness, honesty, integrity and openness. Except for compensation received for services, the terms of which have been disclosed to the donor, they shall have no vested interest that could result in personal gain.

*Adopted and subscribed to by the National Committee on Planned Giving (now the Partnership for Philanthropic Planning) and the American Council on Gift Annuities, May 7, 1991. Revised April 1999. Reprinted with permission*



**Notes:**

Two columns of blank musical staves for writing notes.



# Investing in a better tomorrow.

Our Charitable Gift Services group offers comprehensive administrative and investment management services to planned giving programs across the country. We are proud to serve clients who support our communities and strive to make them a better place, now and in the future.

For more information, please contact:  
**Douglas Cook** 617 722 7649



**BNY MELLON**  
WEALTH MANAGEMENT

Charitable Gift Services • Investment Management  
Asset Servicing • Gift Management  
[bnymellonwealthmanagement.com](http://bnymellonwealthmanagement.com)



## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



## **Symposium: Transferring Values and Valuables**

Presented by:

**Perry Cochell  
Senior Philanthropic Advisor  
Boy Scouts of America  
1325 W. Walnut Hill Lane  
Suite 327  
Irving, TX 75038  
972-580-2135  
pcochell@netbsa.org**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## TRANSFERRING VALUES WITH VALUABLES

PRESENTER:  
PERRY L. COCHELL, J.D., C.W.C.  
DIRECTOR/OFFICE OF PHILANTHROPY  
BOY SCOUTS OF AMERICA



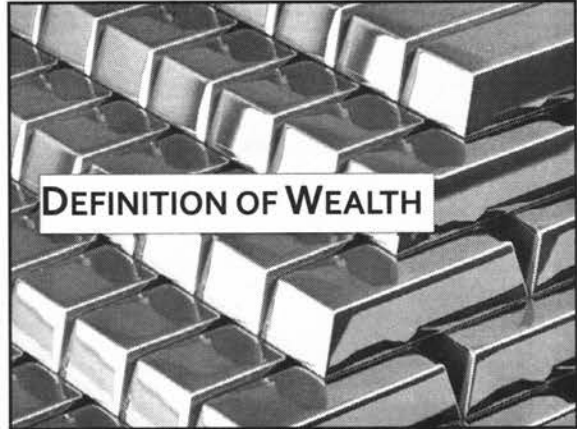
## LEGACY PLANNING FOCUS



## FOUR THINGS



## DEFINITION OF WEALTH



## AFFLUENZA OR SUDDEN WEALTH SYNDROME

**WARNING:** Receipt of this inheritance may be hazardous to your health. Upon receipt of this inheritance you may develop Affluenza Disorder. The symptoms of Affluenza Disorder include: Overspending, hoarding, using money to control others, using money to gain approval, and an inability to receive money.



## TRUE INHERITANCE:

"A transfer of values that provide sufficient judgment and wisdom for the inheritors to use economic inheritance as a tool versus Affluenza."

- Perry L. Cochell



# THE HERITAGE PROCESS™

ESTATE PLANNING

## THREE STEP GUIDE TO THE HERITAGE PROCESS™

1. Guide client(s) to understand what they value most.
2. Guide client(s) thru a process of inter-generationally passing of their values.
3. Guide client(s) to understand and accept their role in identifying, planning and implementing values into their estate plan.

ESTATE PLANNING

## STEP I

Guide client(s) to understand what they value most:

1. Story
2. Definition
3. Concept Map

ESTATE PLANNING

## STORY

ESTATE PLANNING

## DEFINITION OF WEALTH

The definition of wealth remains, as always, the means by which we fulfill our desires. As the saying goes, you are wealthy if you want no more than what you have, whether you grasp for fame, fortune, friends, or followers. In economic terms, this translates into material possessions and the means to attain them. In social and political terms, it translates into greater freedoms, and the means to attain them.

Stan Davis & Christopher Meye  
– *Future of Wealth*

ESTATE PLANNING

## CONCEPT MAP



ESTATE PLANNING

## HISTORY OF INTER-FAMILY WEALTH TRANSFERS

100 YEARS OF SCOUTING

## GROWTH IN MATERIAL WEALTH ACROSS CENTURIES, 1000-PRESENT



Copyright (c) 2004 Heritage Intellectual Resources, LLC. All Rights Reserved.

100 YEARS OF SCOUTING

## STEP II

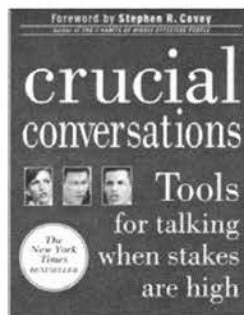
Guide client(s) thru a process of inter-generationally passing on their values.

1. Communication
2. Pre-Inheritance Experience
3. Pre-Charitable Inheritance Experience

100 YEARS OF SCOUTING

## COMMUNICATION

100 YEARS OF SCOUTING



Kerry Patterson  
Joseph Grenny  
Ron McMillan  
Al Switzler

100 YEARS OF SCOUTING

## PRE-INHERITANCE EXPERIENCE



100 YEARS OF SCOUTING

## PRE-CHARITABLE INHERITANCE EXPERIENCE

## STEP III

Guide client(s) in defining their role in identifying, planning and implementing values into their estate plan:

Vision Statement

## CONCEPT MAP

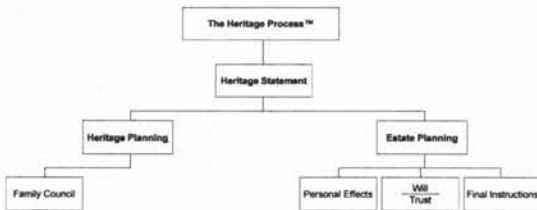


## HERITAGE STATEMENT:

A meaningful and compelling vision of the family's dynamic and long lasting pursuit of unity and of shared values, coupled with a clear focus on each family member's personal responsibility to leave an Estate of both self and wealth to the society wherein each lives.

- Perry L. Cochell

## CONCEPT MAP



## FAMILY COUNCIL



## CONCEPT MAP



## FAMILY BANK

## CONCEPT MAP

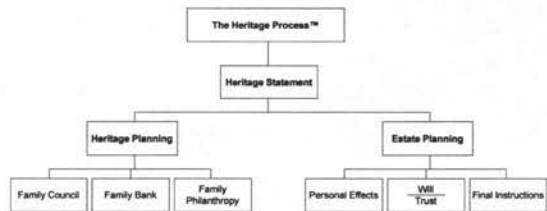


## FAMILY PHILANTHROPY



## OUTRIGHT INHERITANCE VS. CHARITABLE INHERITANCE

## CONCEPT MAP



## QUESTIONS & ANSWERS

THE UNIVERSITY OF NOTTINGHAM

## Your focus:

Securing support  
for your mission

## Our focus:

Providing high quality  
planned giving services

## Together:

Achieving your program goals

Our comprehensive services are designed to address the full range of challenges encountered by gift planning programs. We provide sophisticated asset management, high quality gift administration, expert program and policy consulting, and informative client and beneficiary reporting. Please contact us to learn more about how our services can make a difference.



**KASPICK & COMPANY**

*A member of the TIAA-CREF group of companies*

[www.kaspick.com](http://www.kaspick.com) • [inquiries@kaspick.com](mailto:inquiries@kaspick.com) • (650) 585-4100  
Redwood Shores, California • St. Louis, Missouri • Boston, Massachusetts

Copyright © 2010 by KASPICK & COMPANY, LLC, a member of the TIAA-CREF group of companies. C47217



## Jammin' for Success...

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## Symposium: Marketing Planned Gifts

### Panelists:

Douglas Page  
Senior Director, Gift Planning  
Pacific Lutheran University  
Office of Development  
Tacoma, WA 98447  
253-535-8377  
page@plu.edu

Steven A. Rosenblum  
Director of Planned Gifts  
Saint Louis Zoo  
One Government Drive  
St. Louis, MO 63110  
314-646-4509  
rosenblum@stlzoo.org

Angela Woo Sosdian  
Director of Philanthropy for the Campaign and for Gift Planning  
The Nature Conservancy  
4245 N. Fairfax Drive, Suite 100  
Arlington, VA 22203  
(703) 841-8790  
asosdian@tnc.org

### Moderated by:

David Libengood  
Director, Relationship Management  
Kaspick & Company, LLC  
One Beacon Street, 8th Floor  
Boston, MA 02108-3107  
617-788-5875  
dlibengood@kaspick.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 www.acga-web.org acga@acga-web.org



**29<sup>th</sup> Conference on Gift Annuities  
April 28, 2010**

**Marketing Symposium**

**Panelists**

Steven Rosenblum, The Saint Louis Zoo  
Douglas Page, Pacific Lutheran University  
Angela Sosdian, The Nature Conservancy  
David Libengood, Kaspick & Company (moderator)

**CONTEXT**

- a) Environment
  - Difficult economic and investment markets over the past two years
  - Mission activities remain crucial
  - Fundraising needs as great as ever
  - Most institutions are facing tighter budgets
  - Marketing strategy is therefore critically important
  
- b) Session objectives
  - Consider briefly a framework for thinking strategically about marketing
  - Share some approaches taken by actual non-profit practitioners responsible for marketing at their institutions
  - Provide some ideas you can apply at your institutions
  
- c) Panelists were selected to provide diversity in
  - Mission of the institution
  - Geographic location
  - Size of overall development effort
  - Size of the planned giving program
  - Stage in evolution of strategic marketing
  - Role played by the panelist

**AN APPROACH TO STRATEGIC MARKETING**

- a) What can we learn from the for-profit approach to marketing?
  
- b) Importance of comprehensive approach. If one of the elements is missing or weak, the outcome of the strategy will be suboptimal

## Strategic Marketing: The For-Profit Model

<b>Situation Analysis</b> <i>The Foundation</i>	<b>Marketing Strategy</b> <i>The Path</i>	<b>Marketing Mix</b> <i>The Elements</i>	<b>Implementation</b> <i>The Framework</i>
<ul style="list-style-type: none"> <li>▪ Perform SWOT analysis</li> <li>▪ Set broad goals</li> </ul>	<ul style="list-style-type: none"> <li>▪ Define and segment the market</li> <li>▪ Identify your target market</li> <li>▪ Position your product or service</li> <li>▪ Articulate the value proposition</li> </ul>	<ul style="list-style-type: none"> <li>▪ Define the product</li> <li>▪ Determine its price</li> <li>▪ Develop your promotional plan (branding, messaging, media)</li> <li>▪ Define place (sales and distribution channel)</li> </ul>	<ul style="list-style-type: none"> <li>▪ Establish metrics</li> <li>▪ Develop and allocate budget</li> <li>▪ Document your plan</li> <li>▪ Execute and make adjustments</li> </ul>

## Applying Strategic Marketing to Gift Planning Efforts

<b>Situation Analysis</b> <i>The Foundation</i>	<b>Marketing Strategy</b> <i>The Path</i>	<b>Marketing Mix</b> <i>The Elements</i>	<b>Implementation</b> <i>The Framework</i>
<ul style="list-style-type: none"> <li>▪ Perform SWOT analysis</li> <li>▪ Define broad institutional fundraising goals</li> </ul>	<ul style="list-style-type: none"> <li>▪ Define your prospect universe</li> <li>▪ Research, segment, and target the prospect base</li> <li>▪ Position the gift or service</li> <li>▪ Develop the case (value proposition)</li> </ul>	<ul style="list-style-type: none"> <li>▪ Tailor giving opportunities and messaging to segments</li> <li>▪ Identify and develop promotional materials</li> <li>▪ Train and incent fundraisers</li> </ul>	<ul style="list-style-type: none"> <li>▪ Define success (metrics)</li> <li>▪ Secure and allocate resources</li> <li>▪ Document the plan</li> <li>▪ Execute and make adjustments</li> </ul>



- c) Areas of overall marketing strategy we will focus on today
  - Segmentation and messaging
  - Promotional methods
  - Cultivation and solicitation (sales)
  - Managing execution and measuring success

## **SEGMENTATION AND MESSAGING**

Segmentation involves dividing your prospect universe into groups that are:

- Identifiable—the differentiating attributes must be measurable
- Accessible—reachable through communication channels
- Substantial—sufficiently large to justify the resources used to target it
- Unique—the individuals in the group must respond differently enough to the messaging to justify the distinct approaches
- Durable—the segment should be relatively stable through time

Typical segmentation approaches include:

- Geographic
- Demographic (age, wealth, etc.)
- Psychographic (personality, lifestyle, values)
- Behavioral (drivers of decision-making)

- a) When Steven began working for the Saint Louis Zoo, he made some changes in how prospect segmentation was done.

- b) Doug works at a university, and as one would expect, uses traditional segmentation methods of age (graduating class) and giving history. The messaging Doug uses varies by segment as he addresses gift planning broadly and in particular bequests.

- c) The Nature Conservancy uses a similar segmentation approach that has required some fine tuning over time. Angie and her team have also gone a step further to tailor messaging for its Legacy Club members.
  
- d) The world changed substantially for most donors beginning in the fall of 2008. Doug, Angie, and Steven will address how marketing messaging at their institutions has addressed this changed environment.

### **PROMOTIONAL METHODS**

There are many promotional methods charities use to reach the desired segments with appropriate messaging:

- Donor seminars or events
- Direct mail
- Ads in institutional or other publications
- Ads in broadcast media
- Email blasts
- Websites
- Social media marketing

These methods vary significantly in terms of cost, personalization and detail of the message, response rates, etc. It can sometimes be difficult to determine how to allocate scarce budget resources to the various activities.

- a) Steven has come to feel it is very important to use multiple methods because of the differing ways that individuals access information. The zoo has also made substantial use of “lunch at the zoo” seminars to build community relationships and educate constituencies about giving opportunities.

- b) Experience has convinced Angie that both consistency of approach and experimentation are important. The Nature Conservancy has also developed a unique way of combining broad and targeted messages in the same promotional method—wraps for Nature Conservancy Magazine.
  
- c) Doug's experience at Pacific Lutheran contrasts in some respects from the seminars at the zoo and the direct mail efforts of The Nature Conservancy. This illustrates the need for tailoring the elements of the marketing mix to the unique aspects of each charity—its mission, and its constituencies. Doug recently embarked on a significant shift in promotional resources toward electronic marketing.
  
- d) The Nature Conservancy recently made a shift in the way it allocated its promotional budget—a shift that was the source of some internal debate
  
- e) Steven has discovered that gifts/premiums for donors, when done creatively, has proven very successful for the zoo







*"For over 18 years, Crescendo Interactive has been a major influence on my success as a gift planner. Texas A&M is a very special place; Aggies are a special family; they give well and have created a wave of planned giving success. The Texas A&M Foundation Office of Gift Planning uses every service offered by Crescendo. We receive 25,000 page views on our planned giving website per month. We send out 75,000 GiftLegacy emails and over 300 Giftlaw emails per month. GiftLegacy has increased our eMarketing reach to over 100,000 eContacts per month, assisting in bringing in \$60 Million in new planned gifts last year alone!"*



Glenn Pittsford '72 CGPA, CFRE  
Assistant Vice President for Gift Planning  
Texas A&M Foundation

## **Expand Your Reach. Increase Your Gifts.**

The GiftLegacy eMarketing system by Crescendo Interactive, Inc. provides continuous fresh website content, 24/7 branding, an online wills guide and wills program, and an online professional tax reference. All the tools you need to reach more donors and close more gifts.

Call or click to start your **FREE 90-day trial** of the GiftLegacy system, software and marketing tools.

## **Crescendo**

*Total Planned Giving Solutions*

[www.CrescendoInteractive.com](http://www.CrescendoInteractive.com)

800.858.9154





## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



# Understanding Gift Annuities

Presented by:

**Elizabeth Brown**  
**Assistant General Counsel**  
**Moody Bible Institute of Chicago**  
**820 N. LaSalle Blvd.**  
**Chicago, IL 60610**  
**(312) 329-4141**  
**ebrown@moody.edu**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



I. What is a Gift Annuity?

A. Contract

B. Donor gives a certain amount of money; Charity agrees to pay fixed income for life.

C. General obligation of the Charity

1. Not dependent on charity's earnings.

2. All assets of Charity could be used to pay annuity obligation, not just the "annuity fund" or the amount of the gift.

3. What happens if Charity goes bankrupt? Conflicting authority.

a. Annuity Fund protected from general creditors?

b. Annuitants treated like other unsecured creditors?

D. Not a trust

1. There is no separate pool of assets supporting an individual annuity contract, or the annuity contracts in general.

2. Is Annuity fund protected from general creditors?

E. Gift

1. Emphasize gift rather than investment aspects.

See: Warfield v. Bestgen, No. 07-15586; D.C. No. CV-03-02390-JAT (9<sup>th</sup> Cir., June 24, 2009)

2. Must have donative intent.

3. Commercial annuity rates are higher.

II. Types of Annuity Contracts

A. Single life – pays a fixed amount for one person's life.

B. Two-life – pays a fixed amount for two people's lives.

1. Joint – pays income simultaneously to the two annuitants, either jointly or in equal shares. After first death, full amount is paid to the other annuitant.

2. Successor – pays all of the income to one annuitant until his death, then to the other annuitant.
- C. Immediate – begins to pay the annuity immediately.
  - D. Deferred – payments begin at a specified later date.
  - E. Flexible Deferred Annuity. Although typically the payout date is established at the time the gift is made, there is flexibility regarding changing the starting date at a later time. See P.L.R. 9743054, where the contract allowed the annuitant to elect the commencement date of the payments at any time after the annuitant reaches age 55. The deduction was based upon the earliest possible start date. Also see PLR 200449033.
  - F. Cannot have a charitable gift annuity for more than two lives.

### III. Annuity Rates (Effective 2/1/2009)

- A. Suggested rates established by the ACGA, based on assumptions regarding:
  1. Mortality – Annuity 2000 Mortality Tables for female lives w/ 2-year setback in ages
  2. Rate of return – 5.25%
  3. Expense load – 1%
  4. Residuum. Since 1939, this assumption has been 50%. This means that, if Charity's earnings exactly meet assumptions, and the person dies when the actuarial tables say they're supposed to, and the expense assumption is also accurate, then at the annuitant's death the Charity will have 50% of the original gift left. In fact, many charities experience a much higher residuum than 50%. A 2004 survey of charities observed a mean residuum of 85.5% and a median residuum of 65.6%.<sup>1</sup> Both of these figures represent a reduction from average residuums reported in 1999. A new survey is in process at this writing.
- B. Most charities follow ACGA rates. 97.1% of charities surveyed say that they either always or usually follow the ACGA rates.<sup>2</sup>

---

<sup>1</sup> Report and Comments on the American Council of Gift Annuities 2004 Survey of Charitable Gift Annuities.

<sup>2</sup> Ibid.

- C. State regulation may affect rates.
- D. IRS requires a minimum 10% gift. On occasion, the ACGA rates may not qualify.
- E. Charity individuation. May use higher or lower rates. May have age limits. But there are several reasons for a charity NOT to exceed the ACGA rates:
  - 1. Risk is minimized.
  - 2. More money will remain for charitable work.
  - 3. Charity does not need to hire an actuary and develop its own rate schedule.
  - 4. ACGA rates have credibility with state insurance departments.
  - 5. Focus on the “gift” rather than the “investment” aspects of the annuity.
- F. Ongoing study of methodology for calculation of rates.

#### IV. Tax effects of gift annuities.

##### A. Income Tax

- 1. Charitable deduction. Reg. §1.170A-1(d)(1): “In the case of an annuity...purchased from an organization described in section 170(c), there shall be allowed as a deduction the excess of the amount paid over the value at the time of purchase of the annuity...purchased.”
- 2. Value of the annuity. Reg. §1.170A-1(d)(2); Reg. §1.101-2(e)(1)(iii)(b)(2); Reg. §20.2031-7.
- 3. Taxation of annuity payments – IRC §72.
  - a. Exclusion Ratio – ratio of the “investment in the contract” to the “expected return.” IRC §72(b); Reg. §1.72-4.
  - b. Expected Return – Reg. §1.72-5.
    - (1). Single life – calculated by multiplying the annual annuity payment by the multiple shown in Table V

of Reg. §1.72-9 (Called the “expected return multiple.”)

- (2). Two-life – calculated by multiplying the annual annuity payment by the multiple shown in Table VI of Reg. §1.72-9. (Called the “expected return multiple.”)
- (3). Adjustments required if payments are to be made less frequently than monthly, or if first payment will cover a partial period. See Reg. §1.72-5(a)(2)(i).
- (4). Note that different tables apply to pre-1986 contracts.

c. Investment in the Contract

- (1). General rule of Reg. §1.72-6. Investment in the contract is the aggregate amount of premiums or other consideration paid, reduced by any return of premiums or any other amounts received which were excludable from income.
- (2). However, in the case of a gift annuity, the “value of the annuity” (see above) is the investment in the contract. The amount deductible as a charitable contribution is not part of the investment in the contract. See Rev. Rul. 62-137, 1962-2 CB 28, which provides older valuation rules for charitable annuities, and states, “The values prescribed herein will apply for the purpose of determining the aggregate amount of consideration paid for the contract (investment in the contract) for purposes of section 72 of the Internal Revenue Code of 1954.” Also see Rev. Rul. 70-15, 1970-1 CB 20, which states, “The amount in excess of the fair market value of an annuity contract purchased from an organization described in section 170(c) of the Code may not be treated as an ‘investment in the contract’; such amount may be deducted as a charitable contribution.”

d. Exclusion limited to investment; unrecovered investment.

- (1). The total exclusion over the life of the contract cannot exceed the total investment in the contract.

Thus, if the annuitant has recovered the entire investment in the contract, thereafter, his annuity payments are fully includible.

- (2). Conversely, if the annuitant dies before the investment in the contract is fully recovered, the unrecovered investment is allowed as a deduction on his final income tax return.
- (3). These rules do not apply to any annuities with a start date before 1986. For those contracts, the exclusion ratio remains the same for the life of the contract.

e. Example: Donor is 72 years old, gives \$50,000 for a single-life gift annuity.

(1).	Annuity Rate:	5.9%	
(2).	Annual Annuity:	\$2,950	
(3).	Charitable Deduction	\$21,282	
(4).	Investment in the Contract	\$28,718	
(5).	Expected life of the annuity	14.5 years	
(6).	Expected return = \$2,950 X 14.5 =	\$42,775	
(7).	Exclusion Ratio:		
	<u>\$28,718</u>		
	\$42,775		
(8).	Tax-free portion of each payment:		
	<u>\$28,718</u> X	\$2,950=	\$1,980
	\$42,775		

#### 4. Capital Gains implications

- a. Exchange of property for an annuity is considered a bargain sale. See Reg. § 1.170A-1(d)(3) and Reg. § 1.1011-2(a)(4)(i).
- b. The “consideration” received in the bargain sale is the “value of the annuity” (determined in accordance with §2031 and the regulations thereunder.) The “basis” in the property sold is determined by multiplying the donor’s basis in the property exchanged by a fraction whose numerator is the value of the annuity and whose denominator is the face value of the annuity.
- c. Example: Donor, age 72, transfers appreciated securities to charity in exchange for an annuity that pays \$2,950 per

year per life. The fair market value of the securities transferred (and the face amount of the annuity) is \$50,000. The donor's basis in the property transferred is \$5,000. The value of the annuity is \$28,718, per IRS tables, and the charitable contribution is \$21,282. (\$50,000 minus \$28,718). The donor's basis in the portion of the property "sold" is calculated as follows:

$$\$5,000 \quad \times \quad \frac{\$28,718}{\$50,000} \quad = \quad \$2,872$$

- d. The consideration received for the portion "sold" is \$28,715, and so the gain which must be recognized is \$25,846 (\$28,718 minus \$2,872).
- e. If the annuity is nonassignable, the gain is reported ratably over the period of years measured by the "expected return multiple", which is equal to the donor's life expectancy, in our example, 14.5 years. \$1,782 of gain must be reported each year.
- f. Only the donor's life expectancy is considered. The survivor annuitant's life expectancy is not considered.
- g. The maximum capital gain reportable in any year cannot exceed the amount treated as return of investment each year – in other words, the excludible amount.
- h. Upon the death of the annuitant, no further gain must be reported. However, if there is a survivor annuitant, the unreported gain will continue to be reported on the same basis by the survivor annuitant.
- i. In case of two-life annuity funded with joint property, gain is reported over the joint life expectancy.

## B. Estate and Gift Tax

- 1. *Single life annuity established by the donor during his lifetime.* There is nothing to include in the donor's taxable estate, since his right to income terminates with death, and there is no remaining value in the contract.
- 2. *Annuity established by donor during life with a survivor annuitant.* The value of the survivor's interest is included in the donor's gross estate. IRC §2039. If the survivor is the donor's spouse, the



marital deduction is available. IRC §2056(b)(7)(c). With non-spouse survivor annuitant, there may be tax due. Tax would likely be payable out of residuary estate.

3. *Annuity established at death for another beneficiary.* If a testator provides in his will or trust that an annuity should be established for someone else, e.g., a child, niece, etc., the entire amount of the annuity is included in his gross estate, and a charitable deduction is available for the charitable portion (same computation as for income tax.)
  - a. If spouse is the only annuitant, marital deduction is available.
  - b. Beware of two-life annuity established testamentarily for spouse and another beneficiary, e.g., wife, then daughter. There is no marital deduction available for the spouse's interest. Charitable deduction is still available, however.
4. Where donor establishes annuity for another beneficiary inter vivos, there are potential gift tax issues.
  - a. If a donor establishes a single life annuity for another beneficiary, e.g., a sister, daughter, niece, etc., a taxable gift has been made. The gift does qualify for the annual exclusion (\$13,000), as it is a "present interest". Face amount of annuity may be more than \$13,000. Compare the non-charitable portion ("value of the annuity") with the exclusion amount.
  - b. If a donor establishes a two-life annuity for himself and a survivor beneficiary, e.g., to donor during his lifetime and then to his daughter, he has made a completed taxable gift to his daughter, and this gift does not qualify for the annual exclusion, because it is not a present interest. Gift tax return would need to be filed, and donor would either pay tax or claim part of his unified credit. Problem can be avoided if donor retains the right to revoke the survivor's interest. Then a completed gift has not occurred, and there is no taxable event for gift tax purposes. However, the survivor's interest will be included in the donor's gross estate at death (see discussion above.)
  - c. Note that gift tax is still an issue, even in 2010 and following.

5. Beware of an income tax issue when annuities are established out of a decedent's estate or a testamentary trust. If the donor's will or trust provides that "10% of my residual estate shall be paid to ABC Charity to establish a single life gift annuity for the benefit of my niece, Susie," then 10% of the income earned by the estate during the period of administration will add to the face value of the annuity. However, someone has to pay the income tax on this income earned during administration. I believe there are three possible results:

- a. If the annuity can be set up immediately (within one month of death?) possibly income can be avoided by back dating the annuity to the date of death.
- b. If the annuity can be established immediately after the close of the estate's or trust's tax year, the estate or trust could report and pay tax on the income earned in the prior year, withholding the amount of tax due from the share used to establish the annuity. A charitable income tax deduction is available for that portion of the income which represents the charitable portion of the annuity.
- c. If the annuity is established mid-year, the only possible result seems to be that the beneficiary will have to receive a Form 1041-K-1 for the non-charitable portion of the income which is added to the annuity, even though she does not actually receive the income. This is the least desirable result, as Susie will not understand why she has taxable income to report when she has not yet begun to receive the income from the annuity.
- d. None of these issues exist if the bequest is stated as a specific dollar amount, as specific bequests generally do not benefit from income earned during administration. However, fairness would require setting up the annuity as soon as possible so that the beneficiary begins receiving income as the decedent intended.

6. Future of the Estate Tax

- a. Exemption equivalent is \$3.5 million for 2009.
- b. What will happen in 2010, 2011?
- c. Gift tax - \$1 million exemption, but tax stays in place.

7. Possible development for the future – IRA “rollover” into charitable gift annuity. Several proposals have been put forth over the last several years. This is not the law today, but it may be an opportunity for the future.

## V. Managing the Annuity Fund

### A. Segregation of assets

1. There is no general overriding requirement that annuity assets be segregated from the general assets of the charity. The obligation to pay the annuity is a contractual obligation backed by all of the charity’s assets, not just the annuity fund.
2. State law may require that there be a segregated fund, and may dictate how much must be in the fund. California requires a trust be set up.
3. Prudence requires that the charity maintain a separate fund, at least in an accounting sense, designated the “annuity fund.” This should be done for the following reasons:
  - a. This may provide greater protection to annuitants, as in some states there may be an argument that these assets are unavailable to general creditors if the charity goes bankrupt. This argument would be based on constructive trust or a similar theory. Although the ultimate success of these arguments is unknown, bargaining position vis a vis other creditors in a reorganization might be improved. Surely, if the assets are not segregated, they will be gobbled up by general creditors.
  - b. A separate fund facilitates accounting and tracking of performance.
  - c. Charity may wish to employ a different investment strategy with annuity assets than for the general fund or the endowment fund, or it may be required to do so by state regulations. Charity may wish to have the fund, or part of it, professionally managed, or may wish to hire a different investment manager than for its other funds.
4. In some cases, further segregation within the annuity fund may be desirable. For example, it may be desirable to create a separate sub-fund for California annuities, since that state has rigid

investment restrictions. The charity would then be free to invest the remaining annuity funds as it wishes.

- B. A key issue is what assumptions are used to calculate the reserves.
1. There is one set of actuarial assumptions that are implicit in the IRS tables used to calculate the charitable deduction. These assumptions are not likely to be the ones used for the charity's reserve calculations. In the example above, a \$50,000 annuity for 72-year-old donor produced a charitable deduction of \$19,175. This does not mean that the charity can immediately take \$19,175 out of the annuity fund.
  2. There is another set of actuarial assumptions that determine the annuity rates. These assumptions may or may not be the ones the charity wishes to use in its reserve calculations.
  3. State regulations may dictate a set of assumptions that must be used. (E.g., California.) In that case, the charity must use assumptions which are at least as conservative as the state regulation requires, at least for that portion of the fund. Keep in mind that the charity may choose to use assumptions which are more conservative than state regulation requires.
  4. It is always best to be conservative in your assumptions, considering the long term of the obligations incurred. However, the assumptions must be reasonable, or the accountants may object.
- C. How much should be in the annuity fund? Stated another way, when may the charity take its share (the "gift") out of the fund and spend the money for its charitable programs? There are two basic approaches:
1. At a minimum, the charity should keep the required reserves in the annuity fund. This is the amount that, actuarially, will enable it to meet the obligations which it has incurred for all of its annuity contracts.
    - a. If this approach is taken, the charity will likely take some of the face value of the annuity out up front, and will invest only a portion of the funds received from the donor.
    - b. On a periodic basis, (at least annually), the charity will recalculate the required reserve based on the annuity contracts then in effect. If the annuity fund exceeds this amount, the charity can withdraw funds and add them to its

general fund. If the fund is insufficient to meet the required reserves, the charity will have to add money to the annuity fund out of its general fund.

- c. Under this approach, the death of an annuitant will not result directly in funds being made available to the charity. However, the termination of the contract will affect the reserve calculation at the end of the year (or whenever it is done). Stated differently, if the gift portion is taken out up front, there will be no "50% residuum". In effect, the charity has taken out the present value of the residuum at the beginning, and the residuum at the end should be zero.
2. The other approach is to account for each annuity contract individually.
    - a. Under this approach, the entire face amount of the annuity is invested.
    - b. Income earned in the fund is allocated to each contract, and payments are deducted from that contract.
    - c. When an annuitant dies, the amount remaining in that contract is transferred to the general fund.
    - d. In some instances, the contract may even be individually invested, e.g., a \$100,000 Treasury Bond may be purchased to support a \$100,000 annuity. But this strategy has become much trickier with the elimination of the 30-year Treasury, and with our current low-interest environment. There is probably no safe bond that will produce enough income to pay any gift annuity. Thus, some portion of the fund will need to be invested in equities, and/or principal will need to be paid out to meet the annuity payment. Furthermore, if interest rates rise and the value of the bond drops, the reserves may be insufficient.
  3. Which approach is right for your charity?
    - a. ACGA recommends investing the entire principal amount of the annuity contract. In other words, Charity does not spend any of the annuity until the annuitant is deceased.
    - b. ACGA rates are based on the assumption that entire amount will be invested.

- c. How large is your fund? Are you constantly growing the fund through new contracts?
- d. Is your actuarial risk diversified?
- e. How confident are you in your investment performance? Do you regularly beat the assumptions underlying the annuity rates? (Keep in mind that the rates under older annuities were determined under different assumptions.)
- f. How conservative is your organization?
- g. What would be the implications if you had to add money to your annuity fund? Would your board and financial officer be able to accept this as a natural consequence of taking the less conservative approach?
- h. Does your organization have reserve funds that could be used to fund a deficit in the annuity fund?
- i. Consider hybrid approach. Segregate funds withdrawn from the annuity fund in a separate board-restricted (quasi-endowment) fund up to a certain percentage of the annuity fund. These funds are then available to replenish the annuity fund if needed.

#### D. Investing the Annuity Fund

##### 1. Objectives

- a. Meet or beat the return assumption which determines the rates. All things being equal, if you beat the assumption, your residuum will be greater than 50%, and if you do not meet the assumption, it will be less than 50%.
  - (1). The key figure is total return, including growth. It is not necessary to produce income equal to the return assumption, and certainly it is not necessary to produce income equal to the payout rate.
  - (2). Return is looked at on an average, multi-year basis. There may be years in which the assumption is not met. However, if, in any year, you do not meet your own assumption used to calculate the reserve, you may be forced to add money to the annuity fund.

b. Maintain sufficient liquidity to meet annuity payment obligations. In theory, the current income from the fund will not be sufficient to meet the annuity payment obligations, for two reasons:

- (1). Investment focus is on total return, not income.
- (2). Annuity rates contemplate dipping into principal, with only 50% remaining at termination of contract. If you have already withdrawn part or all of the excess over required reserves, then principal invasion is even more likely.

c. Another approach – asset/liability matching.

## 2. Specific investments

a. Stocks – acceptable within state regulation guidelines, and sufficient diversification. Stocks historically have produced better returns than bonds in the long run, but are not likely to produce large amounts of current income, so liquidity needs must be met elsewhere in the portfolio.

b. Bonds – generally produce better income than stocks. But value of bonds may vary greatly with swings in interest rates. This could affect your reserve calculation. Long-term bonds more susceptible to value fluctuation.

c. Real estate – In some cases, real estate could be an appropriate investment for the annuity fund. It probably should be income producing, such as a triple net leased commercial property, or apartment building. This may produce a good long-term return, but there are different risks associated with real estate. And there are management issues, as well. Consider obtaining real estate exposure through REITs as an alternative.

d. Mortgages and land contracts may also be held in the annuity fund. Again, consider unique risks – default, foreclosure, etc.

e. Alternative investments, aka “Absolute return strategies”, aka Hedge Funds. Understand the risks.

3. Investment Principles to consider
  - a. Asset allocation. Determine an asset allocation that is likely to produce the return that you need with a level of risk that you (and your board) are comfortable with.
  - b. Diversification – among asset classes, and within each asset class.
  - c. Discipline. Keep with your strategy for the long term, rebalance periodically.
4. Should you have professional investment management?
  - a. In-house expertise?
  - b. Size of portfolio
  - c. Portfolio mix – equities v. fixed income
  - d. Cost
  - e. Use of mutual funds.
  - f. Consider passive investment strategy.
  - g. Charity is still liable to make annuity payments if professional managers do not perform to expectations.
5. Investment issues are far more difficult in the early years of the fund. It is much easier to achieve diversification in a larger fund, and the actuarial risk is less the larger the number of annuitants in the pool. Liquidity is also harder to achieve in a small fund, because generally, the more liquid, the smaller the return. Consider these issues when deciding whether to take excess out of the fund.
6. Reinsurance
  - a. Possibly a way to manage actuarial risk, particularly on a very large contract or when the fund is just starting out.
  - b. May be prohibited in some states.



- c. Charity is still liable if insurance company goes under.
  - (1). Check company's rating.
  - (2). Use more than one company?

E. State Regulation

- 1. Do you need to register in your state?
- 2. Do you need to register in other states where your annuitants reside?
- 3. Reserve requirements.
- 4. Investment restrictions.

F. Administrative issues

- 1. Making timely payments. Need a method to produce checks and keep records.
  - a. Checks
  - b. Direct deposit
  - c. ACH
  - d. How do we find out when annuitants die?
- 2. Calculation of charitable deductions, capital gains, etc. Need to inform donor regarding tax matters.
- 3. Calculation of reserves.
  - a. Required by state regulation
  - b. For accounting purposes.
- 4. Tax reporting.
  - a. Annual 1099-R to all annuitants. Magnetic tape to IRS.
  - b. Calculate includible/ excludible portions, and keep track of when the investment in the contract is recovered.

- c. Capital gains.
    - 5. Software.
  - G. Decisions for your annuity program.
    - 1. Minimum annuity contract.
    - 2. Frequency of payment, or minimum payment allowed.
    - 3. What types of assets will you accept in exchange for an annuity?
      - a. Publicly traded assets are obviously OK.
      - b. What about real estate?
      - c. Subchapter S stock – UBI upon sale.
    - 4. Do you want any age limits?
    - 5. Outsourcing.
  - H. Marketing – Note that ACGA’s expense assumption does not include marketing costs.
- VI. Comparing the annuity to other charitable giving vehicles.
- A. Pooled Income Fund
    - 1. PIF has a fluctuating (growing?) income stream.
    - 2. All income is taxable.
    - 3. Capital gains totally avoided on gifts of appreciated property, even if the income recipient is not the donor.
    - 4. Assets are protected from the general creditors of the charity, but there is no guarantee of payments. Charity is only obligated to pay income earned in the trust.
    - 5. Can create PIF for more than two lives.
    - 6. Not subject to the 10% rule

B. Charitable remainder unitrust

1. Separately invested. Larger amount required to create a CRUT than a gift annuity.
2. Fluctuating income and valuation. In an income-only unitrust, beneficiary receives only income earned in the trust, up to the limitation. In standard unitrust, beneficiary receives a percentage of the fair market value of the trust assets, valued annually. Payment can go up or down.
3. Generally, all payments received are taxable income. There may be distributions of principal which are not taxed in a straight unitrust. Also, a unitrust may invest in tax-exempt securities (but watch out for accumulated capital gains.)
4. Assets in trust protected from general creditors of the charity. Income obligation is not backed by charity's general assets.
5. Complete elimination of capital gains (unless the tier system of income payouts dips into the capital gains layer.)
6. Can create for more than two lives (provided 10% rule is satisfied), or for a term of years up to 20.
7. Can provide for contingent income beneficiaries, or a class of income beneficiaries in a term of years trust.
8. Better vehicle for gift of Real estate – use FLIP trust.

C. Charitable remainder annuity trust

1. Separately managed trust. Requires larger amount to set up.
2. Annual payment is a fixed amount which does not vary.
3. Initially, complete elimination of capital gains. However, if principal is distributed, capital gains could be carried out under tier system.
4. Payment is not guaranteed by general assets of charity. If trust runs out of money, payments cease.
5. Assets protected from the charity's general creditors.
6. Can create for more than two lives, or for a term of years.

- D. In general, gift annuity, PIF, and charitable remainder trusts all provide similar, albeit not identical, tax benefits, namely income tax deductions when established inter vivos, estate tax deductions at death, and some shielding from capital gains when funded with appreciated property.

Comparison of Life Income Gifts

	Gift Annuity	Pooled Income Fund	Charitable Remainder Unitrust	Charitable Remainder Annuity Trust
<b>Fixed or variable payment</b>	Fixed	Variable	Variable	Fixed
<b>Growth in income payout?</b>	No	Likely	Possibly, depending on payout rate	No
<b>Payment guaranteed by charity's assets?</b>	Yes	No	No	No
<b>Assets in fund/ trust protected from Charity's general creditors?</b>	No	Yes	Yes	Yes
<b>Tax deduction on funding</b>	Yes	Yes	Yes	Yes
<b>Capital gains on funding with appreciated property</b>	Partial avoidance. Deferral of remaining gain if donor is the annuitant	Completely avoided	Completely avoided (But may be paid out in "tier" system)	Completely avoided (But may be paid out in "tier" system)
<b>Taxation of income payments</b>	Partially taxable; partially excluded	Fully taxable	Generally taxable. Some portion may be tax-free return of principal or capital gain	Some portion may be tax-free return of principal or capital gain.
<b>More than two lives?</b>	No	Yes	Possibly, but must meet 10% rule	Possibly, but must meet 10% rule.
<b>Term of years?</b>	No	No	Yes, up to 20	Yes, up to 20
<b>Separately managed?</b>	No	No	Yes	Yes
<b>Minimum to create</b>	\$1,000 or more	\$5,000 or more	\$50,000 or more	\$50,000 or more
<b>Payout rate</b>	Suggested by ACGA rates	Actual income earned in trust	Determined by donor and charity when trust established	Determined by donor and charity when trust established.
<b>Fund with real estate?</b>	Probably not	Probably not	Yes	Only if income-producing or readily marketable
<b>Fund with tax-exempt securities?</b>	Yes	No	Yes, but be careful of capital gains	Yes, but be careful of capital gains



## Understanding Gift Annuities



Elizabeth A. S. Brown  
Assistant General Counsel  
Moody Bible Institute of Chicago

## What is a Gift Annuity?

### Gift Annuity is a Contract

- Donor gives money
- Charity agrees (promises) to pay fixed income for life



### Gift annuity is NOT a trust

- No separate pool of assets
  - Reserve fund?
- Annuity Fund is part of the Charity's assets
- Is Annuity Fund protected from general creditors?

### Annuity Contract is a General Obligation of the Charity

- Obligation to pay does not depend on earnings
- All of the charity's assets stand behind its promise
- Annuitants' standing in the event of charity bankruptcy
  - Unsecured creditor?

### Gift Annuity is a GIFT

- Emphasize GIFT, not investment
- Donative intent
- Compare commercial annuity rates



**Gift Annuity rates vs. Commercial rates  
(Male, single life) (7/1/08)**

Age	ACGA rate	Sample Commercial rate
65	5.7%	8.09%
70	6.1%	9.14%
75	6.7%	10.64%
80	7.6%	12.75%
85	8.9%	15.74%
90	10.5%	20.08%

**Types of Annuity Contracts**

**Single-life vs. Two-life**

- Single-life – pays fixed annuity for one person’s life



**Two-life Annuity**



- Pays income for the lives of 2 people
  - Joint – pays jointly, or in equal shares
  - Successor – pays first to one annuitant, then to the other
- Two is the maximum number of lives
  - More than 2 – consider PIF or CRUT

**Immediate vs. Deferred**

- Immediate – begins payments immediately
- Deferred
  - Payments begin at specified later date
  - Some flexibility available

**Annuity Rates**

----- SINGLE LIFE ANNUITY RATES -----

Age	Rate	Age	Rate
65	5.7%	75	6.7%
70	6.1%	80	7.6%
75	6.7%	85	8.9%
80	7.6%	90	10.5%



## ACGA Rate Assumptions

- Mortality
  - Annuity 2000 Mortality Table for female lives w/ 2 year setback in ages
- Rate of return
  - Presently 5.25%
  - Portfolio makeup – 40% equities, 55% 10-yr Treasury bonds, 5% cash
- Expense load – 1%/year
- Residuum – 50%
- Ongoing study of methodology

## Other factors affecting rates

- State regulation
- 10% requirement
  - ACGA rates may not qualify in certain instances

## Why is it important to use ACGA rates?

- Minimize risk
- Assure that money will remain for charitable work
- No need to hire an actuary and develop rate schedule
- ACGA rates have credibility with state insurance departments
- Focus on the “gift”

## Tax Effects of Gift Annuities



## Income Tax

## Charitable Deduction

$$\begin{array}{r}
 \text{Amount paid for the Annuity} \\
 \textit{Minus} \quad \underline{\hspace{2cm}} \quad \text{Value of the Annuity} \\
 \textit{Equals} \quad \text{Charitable Deduction}
 \end{array}$$

## Taxation of Annuity Payments

$$\text{Exclusion Ratio} = \frac{\text{Investment in the Contract}}{\text{Expected Return}}$$

$$\text{Investment in the Contract} = \text{Value of the annuity}$$

$$\text{Expected Return} = \text{Annual Annuity Payment} \times \text{Expected Return Multiple}$$

**Exclusion is limited to Investment in the Contract.**

**Example: Donor, 72 yrs old, \$50,000 single-life annuity**

Annuity Rate	5.9%
Annual Payment	\$2,950
Charitable Deduction	\$21,282
Investment in the Contract	\$28,718
Expected life of the Annuity	14.5 years
Expected return	\$2,950 X 14.5 = \$42,775
Exclusion Ratio	\$28,718 / \$42,775
Tax free portion of each payment	\$28,718 X \$2,950 = \$1,980
	\$42,775

## Capital Gains

- Bargain Sale – part sale, part gift
- Gain on “sale portion” is taxable
  - Consideration = Value of the Annuity

– Basis (in sale portion) =

$$\text{Basis} \times \frac{\text{Value of Annuity}}{\text{Annuity Face Amt}}$$

**Example: \$50,000 annuity, funded w/ appreciated property; Cost basis \$5,000**

Charitable Deduction	\$21,282
Value of the Annuity	\$28,718
Cost Basis	\$28,718 / \$50,000 X \$5,000 = \$2,872
Taxable Gain	\$28,718 - \$2,872 = \$25,846

## Capital Gains

- Gain reported ratably over life expectancy.
- Donor's life only – Do not include survivor annuitant
- Two-life funded w/ joint property – use both lives
- Maximum annual reportable gain = excludible amount
- Upon death, no more reportable gain, except that survivor annuitant will continue to report

## Estate and Gift Tax

## Status of the Law

- Gift tax – 35% rate, \$1 MM exemption
- Estate tax – repealed (so far) for 2010
- 2011 - ???

### Single-life annuity established by donor during lifetime

- Right to income terminates at death
- Nothing to include in taxable estate

### Annuity established during life with a survivor annuitant

- Value of survivor's interest IS included in donor's taxable estate
- Marital deduction available if spouse is survivor beneficiary

### Testamentary Annuity

- Entire face amount included in gross estate
- Charitable deduction for the charitable portion
- If Spouse is ONLY annuitant, marital deduction is available
- Trap for the unwary: 2-life testamentary annuity for spouse and another beneficiary. NO MARITAL DEDUCTION

### Inter vivos annuity for another beneficiary – single-life

- Completed gift
- Amount of gift = "value of the annuity"
- File gift tax return, possibly taxable
- Exception:
  - Annual exclusion (\$13,000)
  - Annual exclusion not available for deferred annuity (Not a "present interest")

### Inter vivos annuity for another beneficiary – two-life

- Donor + survivor beneficiary
- Amount of gift = value of the survivor's interest
  - Compare “value of the annuity” w/ value of a single-life on donor's life only
- File gift tax return, possibly taxable

### Inter vivos annuity for another beneficiary – two-life

- Gift tax annual exclusion is NOT available
  - Survivor's interest is not a present interest
- Donor should retain right to revoke survivor's interest by Will – no completed gift

### Testamentary annuity can create income tax issue

- “I leave 10% of my estate to Charity to establish gift annuity for my niece”
- Who pays income tax on the earnings during the period of administration, before the annuity is set up?

### Managing the Annuity Fund



### Segregation of Assets

- Is it required?
  - Generally, no
  - BUT see state law
- Why segregate?
  - Possible protection to annuitants
  - Accounting, tracking performance
  - Customized investment strategy
- Segregate sub-funds, e.g., California

### How much should be in the Annuity Fund?

When may the charity benefit from the gift?

### Two approaches

1. Keep required reserves in Annuity Fund; Transfer excess to General Fund
2. Invest entire face amount of the Annuity; Transfer excess only after death of annuitant.

### Required Reserves

- Amount necessary to meet all outstanding annuity obligations
- Actuarial calculation
- Assumptions
  - Mortality
  - Earnings

### Varying assumptions for different purposes

- IRS tables – to determine charitable deduction
- ACGA assumptions – to determine rates
  - 50% residuum
- State regulations
- Accounting/ FASB

**Use conservative assumptions to calculate reserve if you are transferring excess to general fund.**



### Two approaches

1. Keep required reserves in Annuity Fund; Transfer excess to General Fund
2. Invest entire face amount of the Annuity; Transfer excess only after death of annuitant.

### Mechanics of Approach #1

- Some portion of annuity's face value is taken out up front.
- Periodically, required reserve of entire fund is recalculated.
- Excess transferred to General Fund when reserve recalculated.
- OR – transfer from General Fund to Annuity Fund if reserves exceed fund balance.

### Mechanics of Approach #1

- Death of an annuitant does not result in transfer to General Fund.
- Under Approach #1, "residuum" is really zero, because funds are spent ahead of time.

### Two approaches

1. Keep required reserves in Annuity Fund; Transfer excess to General Fund
2. Invest entire face amount of the Annuity; Transfer excess only after death of annuitant.

### Mechanics of Approach #2

- Entire gift invested.
- Income allocated to each contract.
- At annuitant's death, the actual "residuum" is transferred to General Fund.
- Individually invest each gift?
- Reserve calculation is still necessary.

### Which Approach is Right?

- ACGA assumptions and "model portfolio" assume 100% of the gift invested.
- How large is your fund?
- Is fund growing through new contracts?
- Actuarial risk adequately diversified?
- Investment performance?

### Which Approach is Right?

- How conservative is your organization?
- What if you had to add money to Annuity Fund from the General Fund?
- Does the organization have "rainy day" funds to fund an Annuity Fund deficit?



### Which Approach is Right?

- Accounting issue – GAAP may require recognition of the excess over required reserves
- Consider hybrid approach – use some of the excess to fund a special rainy day fund.

## Investing the Annuity Fund



## Investment Objectives

- Meet or beat return assumption that determines rates.
  - But some annuities in your pool were issued at different rates
  - Look at total return, not just income.
  - Look at average annual returns.

## Investment Objectives

- Meet or beat return assumption that determines rates.
- Liquidity
  - Income will not be sufficient to meet payments.
  - Rates contemplate dipping into principal.

## What types of investments can be used?

- Equities (stocks)
  - Historically, better return than fixed income
  - State regulation may limit stocks in portfolio
  - Liquidity issues – low income
  - Diversification
- Bonds
  - Produce more income
  - Subject to value fluctuation

## What types of investments can be used?

- Real Estate
  - Unique risks
  - Management issues
  - Consider triple net leased or REIT
- Mortgages, notes, land contracts
  - Unique risks – default, foreclosure
- Alternative investments

## Key investment principles

- Asset allocation
- Diversification
  - Among asset classes
  - Within each asset class
- Discipline

## Professional Investment Management

- Size of portfolio
- Cost
- Do you have in-house expertise?
- Use of mutual funds
- Passive investment strategy
- Consultant, Manager of managers

## Professional Investment Management

Remember:

Charity is still liable for annuity payments if professional managers do not perform to expectations!

## Reinsurance

- Possible way to manage actuarial risk
  - Large contract
  - Young fund
- May be prohibited in some states
- Charity is still liable to make the payments if insurance company goes under

## State Regulation

## Registration Issues

- Do you need to register in your own state?
- Do you need to register in other states?

## Other state regulation issues

- Reserve requirements
- Investment restrictions



## Administrative Issues



## Payments and Record-keeping

- Checks
- Direct Deposit
- ACH
- Verifying that annuitants are still alive

## Calculations

- Proposals for Marketing
- Assistance to Donors
  - Calculate charitable deduction
  - Capital gains implications
- Reserve calculations
  - State Regulation
  - Accounting/ FASB



## Tax Reporting

- Annual 1099-R to annuitants
- Magnetic tape to IRS
- Includible/ excludable
- When is "Investment in the Contract" recovered?
- Capital Gains



## Policy Decisions

- Minimum annuity contract
- Frequency of payment, or minimum payment
- Age limits?
- What types of assets to accept?
  - Real estate
  - Closely held stock
  - Sub-S stock

## There is help on the way!

- Software
- Consultants
- Outsourcing
- ACGA
- Visit the vendors

## Marketing

- Marketing costs NOT included in ACGA expense assumption
- Unique issues in the new annuity program

## Comparing the Gift Annuity to other Planned Gifts

Pooled Income Fund  
Charitable Remainder Trust

## Similarities: CRUT, CRAT, PIF and Annuity

- All have private income beneficiaries, remainder to charity
- Income tax deductions when established inter vivos
- Estate tax deductions at death
- Some CG avoidance
- Irrevocable

## Pooled Income Fund v. Annuity

- |   |   |
|---|---|
| ■ Fluctuating income stream; payments not guaranteed  | ■ Fixed payout; guaranteed by charity's assets                            |
| ■ All income taxable                                  | ■ Part excludible   |
| ■ CG totally avoided even if donor is not beneficiary | ■ CG partially avoided, spread over life of annuity IF donor is annuitant |
| ■ Assets protected from general creditors             | ■ Assets probably not protected from general creditors                    |
| ■ More than 2 lives OK                                | ■ Maximum 2 lives   |

## Charitable Remainder Unitrust v. Annuity

- |  |   |
|--|---|
| ■ Separately managed trust.                            | ■ Contractual obligation.                     |
| ■ Fluctuating income                                   | ■ Fixed income                                |
| ■ Distributions usually taxable                        | ■ Payments partially excludible               |
| ■ Trust assets protected from general creditors        | ■ Probably not protected                      |
| ■ Payment obligation not backed up by charity's assets | ■ Payments backed up by all assets of charity |

## Charitable Remainder Unitrust v. Annuity

- |   |                               |
|---|-------------------------------|
| ■ Complete avoidance of CG (subj to tier system)                          | ■ Partial CG avoidance        |
| ■ More than 2 lives OK (subj. to 10% rule)                                | ■ No more than 2 lives        |
| ■ Term of years option  | ■ No term of years option     |
| ■ Provide for contingent beneficiaries or class in a term of years trust. | ■ No contingent beneficiaries |

**Charitable Remainder  
Annuity Trust**

- Separately managed trust.
- Fixed payment
- Trust assets protected from general creditors
- Payment obligation not backed up by charity's assets
- More than 2 lives or term of years

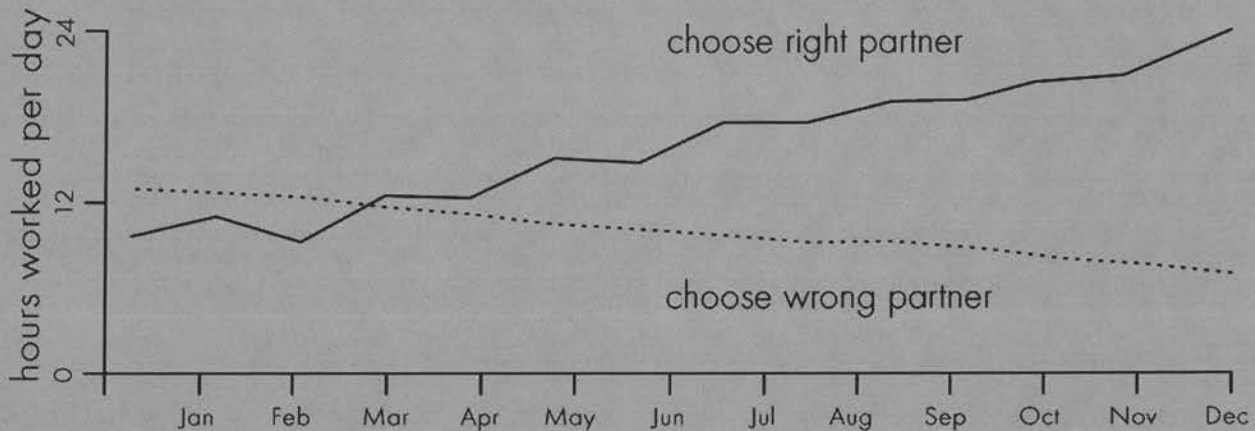
**v. Annuity**

- Contractual obligation.
- Fixed payment
- Probably not protected
- Payments backed up by all assets of charity
- Maximum 2 lives; no term of years



# RELATIONSHIP SATISFACTION

in Planned Giving



There's one Planned Giving provider that can give you what you want out of a relationship. Commitment. Communication. Creativity. Capability. With a thorough understanding of the donor community, Northern Trust takes the time to get to know you, your objectives and how they best can be achieved. A relationship with Northern Trust offers you not only gift administration, investment management and tax compliance, but also access to our specialists in non-financial assets. Our comprehensive approach to Planned Giving administration will deliver customized solutions that leave you wondering what life was like before we met. Call Marc Cosentino at 312-630-0730 or visit [northerntrust.com](http://northerntrust.com).



**Northern Trust**

Tax Compliance, Gift Administration, Custody, Investment and Specialty Services



## Jammin' for Success...

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## State Regulations Panel

### Panelists:

Timothy C. Costello  
Chief of Valuation Bureau & Chairman  
of Life & Health Admissions Committee  
New Jersey Department of Banking &  
Insurance  
PO Box 325  
Trenton, NJ 08625-0325  
609-292-5427 x 50313  
timothy.costello@dobi.state.nj.us

Kristofer Graap  
Auxiliary Lines Specialist, Company  
Supervision Division  
Washington Office of the Insurance  
Commissioner  
PO Box 40259  
Olympia, WA 98504-0259  
360-725-7206  
Krisg@oic.wa.gov

Carol Harmon  
Senior Staff Counsel  
California Department of Insurance  
45 Fremont Street, 24th Floor  
San Francisco, CA 94105  
415-538-4420  
harmonc@insurance.ca.gov

Edie Matulka  
Senior Consultant  
PG Calc  
115 NE 100th St., Ste. 300  
Seattle, WA 98125  
206-329-8144  
ematulka@pgcalc.com

### Moderated by:

Kristen Schultz  
Sr. Vice President  
Crescendo Interactive, Inc.  
110 Camino Ruiz  
Camarillo, CA 93012  
(800) 858-9154  
kristen@cresmail.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 www.acga-web.org acga@acga-web.org





## State Regulations Panel

### I. Introduction to the Session

This year, the ACGA State Regulations Subcommittee invited regulators from key states to speak on a panel regarding regulatory issues relevant to their states, with commentary to be provided on unrepresented states as applicable. The goal of this session is to educate charities on ways to comply with state law in issuing and administering gift annuities, with emphasis placed on meeting annual reporting requirements.

The panelists are Carol Harmon of the California Department of Insurance, Timothy Costello of the New Jersey Department of Banking and Insurance, Kristofer Graap from the Washington State Office of the Insurance Commissioner and Edie Matulka, Senior Consultant of PG Calc Incorporated. Ms. Harmon, Mr. Costello and Mr. Graap will answer questions regarding regulation of gift annuities in their respective states and Ms. Matulka will answer questions as they apply to other applicable state regulations. The panel will be moderated by Kristen Schultz, Senior Vice President of Crescendo Interactive, Inc.

### II. Panel Questions

The moderator will begin the discussion with general questions regarding the state registration process, annual filings, reserve requirements, penalties and changes in future law. Time will be allotted for specific questions directed to the state regulators. This handout has been designed with space for attendees to take notes after each question below.

#### A. General Questions:

1. Registration: What are your state reviewers specifically looking for when reviewing a charity's application to issue gift annuities in your state? What issues prompt the most concern? What steps can a charity take to ensure a successful review process?
2. Annual Filing: What information are you looking for in the annual report, and for what purpose is it requested? Must a charity report on a fiscal or calendar year basis or is there flexibility to choose either option? Do you permit electronic filing or have any plans to streamline the filing process?
3. Reserves: What are the reserve requirements in your state? Can you provide some background into the purpose of certain requirements (calculation methodology, surplus requirements, need for an actuary, investment restrictions)?

4. Reinsurance: What is the view in your state regarding reinsurance of annuity contracts? If a charity reinsures 100% of their gift annuities, are they still required to maintain a reserve fund? How does this change annual filing requirements if at all?

5. Winding Down: If an organization wishes to no longer issue CGAs in your state and to turn back its permit/certificate, what are the formal steps, if any, the organization needs to take with the State?

#### B. State Specific Questions:

##### California

What is the purpose behind requiring completion of Individual Affidavits? Who looks at this information, and how is it protected from public access?

Why is it necessary to provide back reports on the California reserves at the time of application, when a separate CA-only reserve fund did not exist?

What are the issues/circumstances that the Commissioner looks for in evaluating a charity's request under Sec. 11521.2(b), for special written consent of the Commissioner to invest the segregated California annuity fund in any other investments (such as real property)?

##### New Jersey

Why is an annual statement needed as part of the application process?

What is the link between registration as a foreign corporation and registration for issuance of gift annuities – why is proof of the former required as part of the latter?

Once a Special Permit is granted, New Jersey requires annual filings be continually submitted to the Insurance Department within 120 days of the end of each calendar year (or fiscal year if the charity has obtained permission to file on that basis). What is the process for requesting a fiscal as opposed to calendar year filing?

##### Washington

Minimum asset requirement: How does the OIC look to determine compliance with the minimum asset requirement? How can a charity with consolidated financial statements address this issue?

What factors are considered to assessing penalties (suspension, fines, revocation) when a charity is not in compliance with Washington law? To what extent do a

charity's individual circumstances determine the penalty? What, if any, penalties are fixed?

### III. Audience Questions

If you wish to ask a question of one or more of the panelists, please fill out the Panel Question Form available at your seat and pass it to the aisle during the session. Following the panelists' responses to the prepared questions, the moderator will read questions from the audience as time permits.

### IV. Conclusion

We hope this panel discussion provides you with an opportunity to learn more about the gift annuity state regulatory process and ask the questions you may have regarding compliance. If you have further questions about gift annuity regulation, the ACGA web site contains detailed information on the regulatory requirements of each state. Please consult the gift annuity state regulation pages at [www.acga-web.org](http://www.acga-web.org).



**Successful planned giving programs  
have a number of things in common.  
A compelling mission is only the first.**



*Consulting  
Marketing  
Calculations & Proposals  
Education  
Gift Administration*

  
**PG Calc**  
*Invested in your mission*

 888-497-4970

 [www.pgcalc.com](http://www.pgcalc.com)

 [info@pgcalc.com](mailto:info@pgcalc.com)



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## **Gift Packages: Mix & Match to Maximize**

Presented by:

Grant H. Whitney  
Sr. Associate Director of Gift Planning  
Harvard University  
124 Mount Auburn Street, 3rd Floor  
Cambridge, MA 01772  
(617) 496-6248  
grant\_whitney@harvard.edu

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)





**Gift Packages: Mix and Match to Maximize**  
**or**  
**10 Ways to Address Your Charity's Funding Needs in Today's Environment**

- 1) Annual gift in perpetuity. Donor in retirement has given \$1,000 annually for 15 consecutive years. Appeals to raise sights to higher giving club levels have been unsuccessful. Who is this person in the eyes of your advancement staff?
  - a) Approaching the conversation
    - i) Assess motivation
      - (a) What explains your consistency and level of giving?
      - (b) Would you like to provide that commensurate level of giving after you are gone?
      - (c) Opportunity to learn more about the source of donor's wealth, type of assets and which in turn may suggest other estate giving beyond endowing the annual gift to support other organizational priorities.
    - ii) Mechanics
      - (a) Rule of 20. To maintain \$1,000 of direct programmatic support into the future, an endowment 20 times the size is needed. Presumes a 5% spending rate.
        - (i) Pros
          1. Immediate support continues.
          2. Future expectancy created.
        - (ii) Cons
          1. No incremental increase
          2. Is an endowment of that size worth the effort
    - b) Alternative Formulations:
      - (1) Is it more palatable to have the fund function as a quasi (board designated) endowment?
      - (2) Structure as a spend-down fund with discretion to invade only in extreme circumstances, recognizing nature of donor's intent.
  - 2) What about Donor Advised Funds? These are separately identified funds owned and controlled by a sponsoring charitable organization; in which the donor or someone the donor appoints has advisory rights to make charitable distributions as well as the underlying investment of the fund. (PPA 2006).

- 3) Endowment Donors: Established endowments
  - a) Faced with depressed market values.
  - b) Reduced distributions and/or reduction in original gift principal.
  - c) Charity may prefer a gift to endowment income.
  - d) Three possible asks:
    - i) Single Ask: ask for a gift to income of that endowment. The ask should be proportionate to typical distribution based on internal factors.
    - ii) Double Ask: In addition, ask for a gift to principal. In this way your donor is responding both to immediate need and demonstrates longer term commitment.
    - iii) Triple Ask: If donor is more confident about the future can you frame an ask to respond to include an estate commitment?
  
- 4) New Endowments: Donor's philanthropic ambition has been checked by the economy.
  - a) If Donor's ultimate charitable design is the top end of a menu of endowment options seed the minimum level endowment in the programmatic sleeve. Top it off with an increment equivalent to a distribution until the endowment itself has earnings (i.e. a year of investment).
  - b) Add a revocable testamentary component to bring the entire commitment up to the desired threshold.
    - i) Donor is making the total commitment desired but approach respects changed circumstances
    - ii) Donor sees generosity at work and is invested in approach
    - iii) But what happens if the endowment threshold changes by the time the donor passes on:
      - (1) Standard bequest language: "I give \_\_\_\_\_% or \$\_\_\_\_\_ of my estate to [Charity] to be added to the XYZ Endowment".
      - (2) Modified language: "I give to [Charity] the then current minimum necessary to convert the XYZ Endowment into a [desired endowment opportunity]"
  - c) Add an irrevocable testamentary component to bring the entire commitment up to the desired threshold.
    - i) Difference is made up by a binding pledge enforceable against the estate which allows the organization to put it on its books.
    - ii) The pledge basically gives the donor a lifetime or two to satisfy the pledge, and obligates the donor's estate to make up any shortfall should a balance exist upon donor's demise.

5) “Endowment Like”: Flexible/Virtual Endowment: Donor can not prudently give the necessary principal – 20 times the income flow – but could commit to an annual sum equal to the endowment distribution. This option necessarily requires close collaboration with your business office, gift policy committee etc.

a) Three possible asks:

i) The Virtual Income Ask: ask for a gift equal to the income distribution of a particularly sized endowment. Size of the ask should be proportionate to typical distribution based on internal factors.

ii) The Virtual Income + Principal Ask: In addition, ask for a gift to seed endowment.

(1) Donor makes a stretch gift to seed endowment at programmatic minimum up front or over a typical pledge period.

(2) Once endowment threshold is reached and has earnings, distributions begin. It in effect supplements the longer term income gift (inflation adjustment)

iii) The Virtual Blended Ask: Combines income and principal in an annual contribution that is in effect amortized over time.

(1) Set the annual gift amount to satisfy the both income needs and begin building principal.

(2) Once threshold endowment level reached, and distributions start, alter the ratio between income and principal (ala an amortization schedule).

b) Issues

i) Would your institution commit to this kind of structure?

ii) Who do you offer this too? Long term supporters only?

iii) What about financial reversals?

iv) What kinds of priorities?

6) Seed Endowment Gift + LIG: As before, Donor’s ultimate charitable design is the top end of a menu of endowment options. Seed the minimum level endowment in the programmatic sleeve and add a life income gift component.

a) Example: Seed Endowment + CGA. Curator ship is \$500,000 but a discretionary fund to support a curator’s work at the gallery can be funded with \$100,000.

i) Plan Benefits:

(1) Gives Donor some satisfaction of seeing their gift at work while living.

(2) Donor boosts income, may claim income tax charitable deduction.

(3) Charity addresses programmatic need at a reduced level with reasonable expectation that the “seeded” endowment will grow over time and receive a sizeable, back end gift.

(4) Donor, seeing the impact made may make additional gifts to endowment income, principal or look at other ways to achieve “full funding”.

- ii) Would your organization credit or “lock in” the total value of the endowment at today’s rates?
- b) Example: Seed Endowment + CRUT Same charitable goal but Donor’s assets are more diversified.
- i) Plan Benefits:
    - (1) Gives Donor some satisfaction of seeing their gift at work while living.
    - (2) Donor eligible for sizeable income tax savings, generates income with growth potential.
    - (3) Charity addresses programmatic need at a reduced level with reasonable expectation that ultimate endowment will have grown over time adjusted for inflation.
    - (4) Seeing impact Donor may make additional gifts to endowment income, principal or look at other ways to achieve “full funding”.
  - ii) Issues: Would your organization be more comfortable locking in today’s endowment minimum in this context?
- 7) Severing or assigning income from existing life-income gifts.
- a) Threshold Questions
    - i) Does your organization still have Pooled Income Funds?
    - ii) How many of you question why a particular donor established a LIG in the first place. Example: Donor with a known family foundation establishes a modest LIG
    - iii) How many LIG donors have said something like:
      - (1) “but I thought you would establish that conservation fund once I made the gift....” or
      - (2) “The income is useful but not necessary for us”
  - b) Assigning payment in any one year acts as an annual gift. Income tax deduction for amounts received by charity as a cash gift. Donor preserves full flexibility in use of payments in future years.
  - c) Severing a portion or all of the income interest. This involves giving up the right to future income permanently and contributing it as an additional charitable gift.
    - i) Income tax charitable deduction roughly equals the present value of those future payments. Your planned giving software can help you figure out the actual value of the severed interest.

- (1) Pooled Income Funds
  - (a) Full or partial severance possible (ex. certain # of units)
  - (b) Deduction equals Value of Income Interest on Date of Transfer
  - (c) Software will indicate an IRS Form 8283 required
  
- (2) Charitable Gift Annuities
  - (a) Deduction equals PV of Annuity Interest or
  - (b) Deduction equals Investment in K – (Capital Gain + Tax-free amount received by annuitant)
  
- (3) Charitable Remainder Unitrusts: assumes that the instrument and state law allow
  - (a) Deduction equals Value of Income Interest on Date of Transfer. It is deemed a gift of a capital asset PLR 2000127023 so many advisors suggest an appraisal.
  - (b) Form 8283 required since the income interest is something other than cash or publicly traded securities Treas. Reg. 1.170A-13(c)(3)
  - (c) Also qualifies for a charitable gift tax deduction Rev. Ruling 86-60
  - (d) Where Charity is both trustee and the remainder beneficiary and donor wants the trust to keep running.
    - (i) If assignment of  $\frac{1}{2}$  of the unitrust income payments there is merger of interest in that half; the trust value is less, therefore less income to income beneficiary but an outright gift is made immediately.
  
- ii) Seed Endowment + Gift Reprise
  
- iii) For actuarial splits between income beneficiary and charity resulting in both parties receiving cash see PLRs 200208039, 200304025, and 200324035 for CRTs.

## 8) CRUT Design

- a) Term of Years: How many of you working with trust donors have considered a term less than a life time?
  - i) Benefits to Donor
    - (1) Increased income tax deduction regardless of age at inception
    - (2) Capital Gains Tax Avoidance on asset transfer
    - (3) Income for predetermined period
    - (4) Potential for growth in trust principal
  
  - ii) Benefits for Charity
    - (1) Functions like a back loaded pledge with known end date.
    - (2) Potential for growth in trust principal
    - (3) Measure of certainty for internal planning
  
- b) Include Charity as an income beneficiary:

- i) Charitable remainder unitrusts must have a payout rate of at least 5%. See Regs. 1.664-3(a)(2).
  - ii) Charity is a permissible income beneficiary as long as there also is a non-charitable income beneficiary Regs. 1.664-3(a)(2)(3).
    - (1) Example. Trust with a 5% payout could provide 4% payable to the donor and 1% to your Charity.
      - (a) Instrument could provide a sprinkling power to more than one charity. In that case the instrument might also consider adding a special trustee for making that decision. See PLRs 200813023, 200813006.
  - iii) There is no additional income tax deduction for the recurring payout to Charity. Regs. 1.664-3(d).
    - (1) Possible uses:
      - (a) Donor wants to make annual gift on auto-pilot and share growth/loss in trust value with charity
      - (b) Trust is part of a gift package involving a new or preexisting endowment gift. The charitable share of the payout is added to income to boost immediate impact and/or added to principal.
- 9) CLT: Charitable Lead Trusts are attractive due to depressed asset values, current low discount rate environment and capped lifetime \$1 million gift tax exclusion (leaving aside estate tax question) as a way to provide immediate charitable support for a term of years and lock in/eliminate gift tax cost to pass assets to heirs.
- i) Annual payouts to charity for terms up to 20 years in most cases.
  - ii) Payout can replicate endowment payout in entirety or be allocated between income and principal to seed an endowment.
- 10) CLAT/CRUT Combo: Combines predictable annual payments to Charity generated by the Lead Trust and the endowment building element through the CRUT.
- a) CLAT serves as primary driver of annual income, functioning almost like a virtual endowment.
  - b) CRUT serves as the primary engine to build the endowment so that when the trust terminates a fund of sufficient size is ready to provide future income for the programmatic purpose.
    - i) Another opportunity to use the CRUT with Charity as income beneficiary structure.
  - c) Employing an amortization schedule to the above package allows Charity to determine how much of each CLT payment can be applied as income vs. principal over time and take into account the income being produced by the endowment once a threshold level has been reached.

11) Conclusion: I hope I have provided some ideas that attendees can apply back at the office to address immediate, near and long terms organizational needs while remaining sensitive to the financial realities our donors face. The ideas presented today are not exhaustive but are offered as models. What you create is limited only by your creativity, imagination and that of your donors.

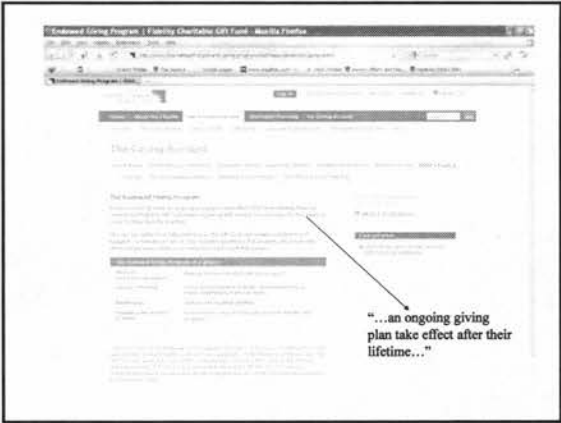
Grant H. Whitney  
Sr. Assoc. Director of Gift Planning  
Harvard University  
124 Mount Auburn St.  
Cambridge, MA 02138  
617.496.6248  
[grant\\_whitney@harvard.edu](mailto:grant_whitney@harvard.edu)



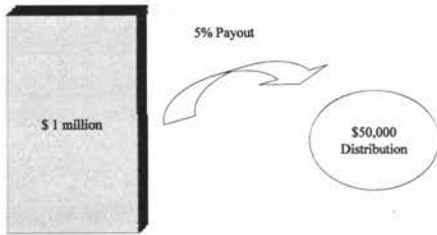


### The Annual Donor

- Donor in retirement gives \$1,000 annually for the last 15 years.
- Donor has resisted appeals to bump up to a higher giving club level.
- Who is this person in the eyes of your colleagues?



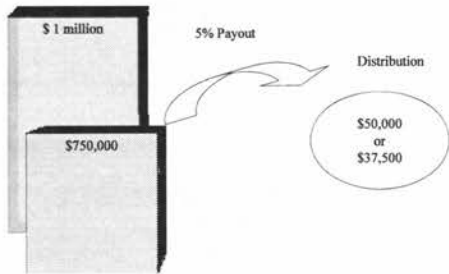
### Endowment in Practice



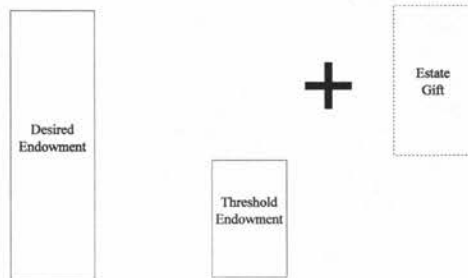
### The Capital Donor

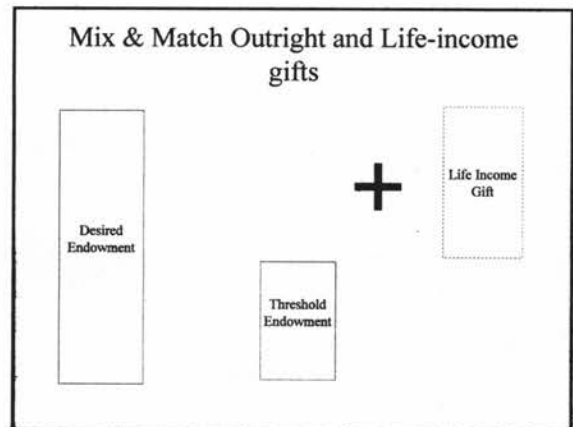
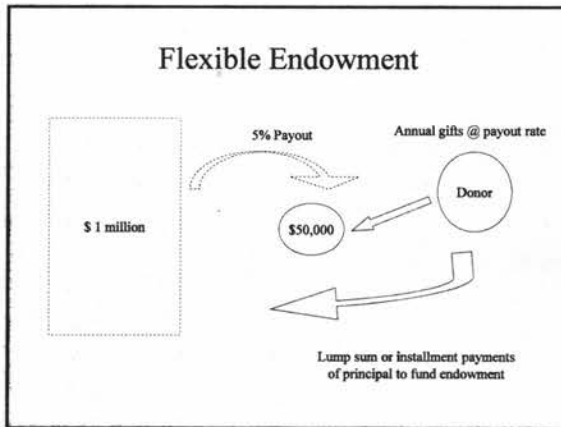
- Donor established endowment five years ago.
- Market value has dropped below original gift value.
- Distribution size?
- Possible Asks?

### New Reality

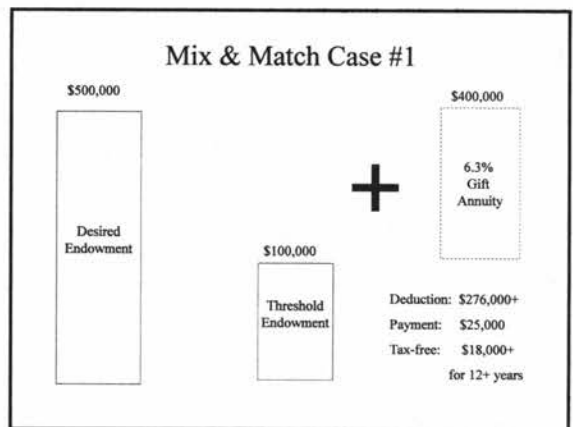


### Mix & Match: Outright and Estate

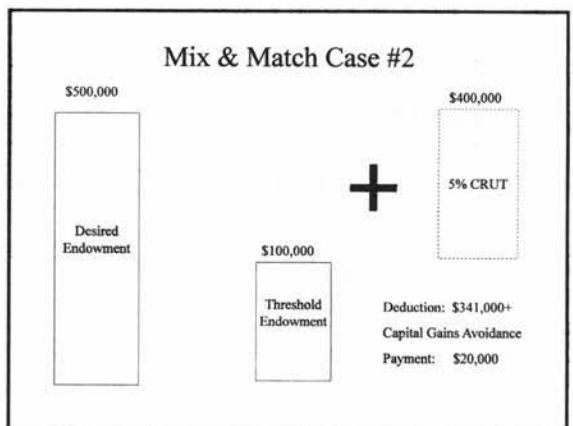




- ### Mix & Match Case #1
- 75 yr old Donor wants to fund a \$500,000 endowment but feels uncomfortable with the commitment size.
  - “Gateway” endowment is available at \$100,000.
  - She has a \$500,000 portfolio of bonds and CD’s maturing and despairs at the 3% reinvestment interest rate she’d receive.
  - What might you propose?

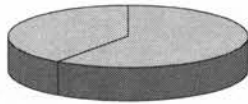


- ### Mix & Match Case #2
- Same facts
  - In addition to her income holdings she was bullish in the Fall of 2008 and went on a buying spree.
  - What might you propose?



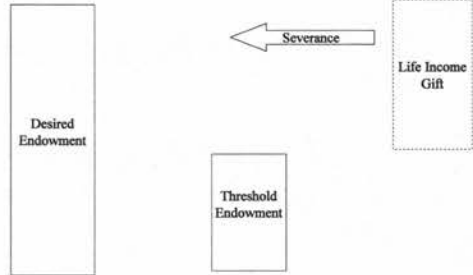
### Severing Life-Income Interest

Income Interest



Remainder Interest

### Outright and Severance



### Acceptable CRUTS?

- One-life CRUT for 88 year old
- One-Life CRUT for 82 year old
- One Life CRUT for 75 year old

### Acceptable CRUTS?

- One-life CRUT with a 5 year term
- One-Life CRUT with a 7 year term
- One Life CRUT with a 10 year term



THE PRIVATE BANK

WELLS  
FARGO



## Complete solutions, trusted partner

### Philanthropic Services from Wells Fargo Private Bank

As one of the oldest and largest trust and investment organizations in the country, Wells Fargo is uniquely positioned to serve the charitable community through our Philanthropic Services. Benefit from our depth of experience providing comprehensive management of Endowments, Charitable Trusts, Charitable Gift Annuities, Private Foundations and Donor Advised Funds.

To learn more about how we can partner with you, call us at (800) 930-4264, or contact one of our Regional Managers:

**Dominic Clemente**  
*Eastern Region, (215) 670-4070*

**Ty Smith**  
*Southeast Region, (404) 238-0440*

**John Libby**  
*Midwest Region, (312) 489-9512*

**Dan Harris**  
*Western Region, (720) 947-6775*

Investment Products: ▶ NOT FDIC Insured ▶ NO Bank Guarantee ▶ MAY Lose Value

Wells Fargo Private Bank provides financial products and services through Wells Fargo Bank, N.A. and its affiliates.  
©2008–2010 Wells Fargo Bank, N.A. Member FDIC.

Together we'll go far







# Satisfied Customers. HONEST RESULTS.

Does your gift planning marketing partner provide you...?

- a 900% average increase in Web visitors
- metrics for measuring your return on investment
- a 96% customer satisfaction rating
- annual investments in scientific market research
- an innovation team to develop and test data-driven ideas
- honest answers on what's working and what's not

 **STELTER**

*Getting to the heart of the matter*

**Gift Planning** Print • Web • E-Marketing • Training • Consulting • Donor Research

**800-331-6881**

**[www.stelter.com](http://www.stelter.com)**





## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# Best Practices in Charitable Gift Annuity Programs

Presented by:

Charles B. Gordy  
Director of Planned Giving  
Harvard Law School  
125 Mount Auburn Street  
Cambridge, MA 02138-5765  
(617) 496-9265  
cgordy@law.harvard.edu

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## Introduction

In 2004, The American Council on Gift Annuities (ACGA) conducted its third survey of charitable gift annuities and received responses from approximately 829 charities across the country.<sup>1</sup> Other information gathered during the survey indicates that over 4,000 organizations are offering gift annuities.<sup>2</sup> There are many more organizations offering charitable gift annuities than responded to the survey, so the gift annuity is an immensely popular way of making a gift to charity while retaining an income stream.

Most organizations offering charitable gift annuities are doing so in a responsible manner and to the great benefit of their donors and organizations, but gift annuities and the charities that offer them have faced a number of challenges in recent years. Between 2004 and 1999, which was when the last survey was conducted, the country experienced one of the worst bear markets in history.<sup>3</sup> This substantially decreased the value of many charities' gift annuity reserves and caused charities to focus on the financial risk they incur when issuing gift annuities. Not only was there risk in the financial markets, but a lawsuit in Texas that threatened to destroy the issuance of charitable gift annuities focused attention on the legal risks to institutions offering gift annuities.<sup>4</sup>

State regulators have increased their scrutiny of gift annuities and the organizations that issue them because of concerns over scams targeted at senior citizens by issuers more interested in financial gain than the charitable giving opportunity that gift annuities present. In 2002, The North American Securities Administrators Association (NASAA) issued a press release listing charitable gift annuities as one of its "Top Ten Scams, Schemes & Scandals" of the year.<sup>5</sup> The ACGA responded and it appears that NASAA has backed off from that assertion.<sup>6</sup> Gift annuities were also dropped from subsequent NASAA top ten lists. In 2002, The Arizona Commission Corporation's Security Division also identified gift annuities as one of its top ten scams.<sup>7</sup> Much of this regulatory activity in Arizona was a result of the conduct by Mid America Foundation, which amounted essentially to a \$54 million Ponzi scheme in which the principal used the donated funds to buy homes, to pay child support, and to support a lavish lifestyle.<sup>8</sup>

In 2003, The Securities Administrator in Maine issued a cease and desist order against a Maine insurance agent and the Tennessee based "New Life Corporation" for representing gift annuities as "guaranteed, no risk investments."<sup>9</sup> The insurance agents selling these gift annuities also received a 6% commission.<sup>10</sup> The Administrator's action prevented the sale of one annuity valued at over one \$1 million.<sup>11</sup> In the summer of 2003, Arizona State regulators secured judgments totaling \$4.3 million against an Arizona company and two insurance agents for fraudulently selling gift annuities, again representing them as secure investments.<sup>12</sup>

Despite these recent events, gift annuities remain a well respected and excellent way for many people to make gifts because the vast majority of organizations are acting responsibly and donors are satisfied with their gifts and the income they receive. The

responses to challenges and pro-active activity by ACGA, by NCPG, and by many charitable organizations have met the regulatory challenges head-on and for the most part have been successful in preserving gift annuities as a viable gift option and alleviating regulators' concerns. ACGA must continue to promote its mission to ensure future success; its mission is:

The American Council on Gift Annuities actively promotes responsible philanthropy through actuarially sound gift annuity rate recommendations, quality training opportunities, and the advocacy of appropriate consumer protections.

In furtherance of those efforts and ACGA's mission, ACGA recommends the following best practices and encourages charitable organizations to utilize as many of them as possible.

### Gift Annuity Best Practices

1. Make sure the donor understands the gift  
Proposal modeling  
It's irrevocable and not guaranteed  
Disclosure statement (required by law)  
Explain the contract in detail  
Meet with the donor in person if possible
2. Have the donor sign the contract  
Helps to insure donor understands the agreement  
Protects the institution  
Required by law in some states
3. Follow the ACGA Rates  
Risk is minimized  
Larger residuum (assuming the alternative is rates higher than ACGA rates)  
Don't need own actuarial work  
The focus is on the gift
4. Establish minimum amounts for a gift annuity  
\$10,000 is the most common in Higher Education; \$5,000 in religious and environmental – this ensures the charity will realize a minimum in exchange for the effort in setting up the gift and its stewardship
5. Establish minimum ages for immediate and deferred annuities  
The most common minimum age is between 60 and 65 years old; approximately 30% of institutions issuing gift annuities have a 55 age minimum; the average age

is 78. The younger the donor, the smaller the benefit to the donor of the arrangement because of the effects of inflation on the annuity distributions and the smaller the benefit to the charity because of the work required over a longer period of time to maintain and steward the gift

6. Develop a gift policy that specifies what assets will be accepted  
Cash, appreciated securities  
Other assets – real estate, tangible personal property, intangible property  
Process for making exceptions
  
7. Invest the entire face amount of the annuity  
Assumption built into the ACGA rates, if it's not done the investment return needed to reach the 50% residuum goes up  
Self insures against the liability, protects the institution  
Reduces risk  
Increases donor confidence
  
8. Invest the assets appropriately given the fact that the gift annuity assets back the issuing charity's obligation to make annuity payments  
Reserve assets should generally be invested more conservatively than general endowment and should remain more liquid than the general endowment  
It may be appropriate for institutions with larger endowments to invest more aggressively  
ACGA assumed returns are based on a conservative and relatively low risk portfolio  
Monitor the investment performance on a quarterly basis  
Formally rebalance annually, informally as you raise cash to make distributions
  
9. For purposes of the distribution to the charity from the annuity at the end of the income beneficiary's lifetime, establish a method for determining the balance of each gift annuity  
Will ensure that the donor's purpose is realized if specified in the contract  
Will enable your institution to determine which annuities are in the red and the extent of the risk of each annuity to the entire pool and to the issuing organization  
Use commercially available software, or in-house systems to track the value of each contract based on the annuity payments and the value of the pool  
For those institutions that do not use such software or another method of fund accounting, determine a method to track the value of each annuity contract
  
10. Develop a good working relationship with your finance and administrative staff  
Will ensure the program is administered in the best interests of the donor and the

of the institution

Will help the gift process go more smoothly  
When issues arise with payments or tax work, they will be easier to resolve  
Exceptions when you need them will be easier to obtain

11. Marketing Your Gift Annuity Program  
Emphasize the charitable nature of the gift in prospect meetings proposals, advertising, and direct mail  
Exercise caution when comparing gift annuity rates with returns from other financial instruments, e.g. “yield” or “rate of return”  
Do not use the phrase “guaranteed income”  
Use examples specific to your organization or develop your own generic examples  
Make sure you are not providing legal and financial advice in your materials  
Encourage donors to consult with their advisors before proceeding
12. Communicate regularly with your gift annuity income beneficiaries
13. Educate your colleagues about the benefits and liabilities of gift annuities

## Endnotes

<sup>1</sup> The “Report and Comments on the American Council on Gift Annuities 2004 Survey of Charitable Gift Annuities” is available at [www.acga-web.org/orderform06.pdf](http://www.acga-web.org/orderform06.pdf). If the past survey schedule is continued, the next survey would occur in 2009.

<sup>2</sup> *Supra*, See the ACGA 2004 Report’s Introduction

<sup>3</sup> *Supra*

<sup>4</sup> *Supra*, and Ozee, et al. v. The American Council on Gift Annuities, Inc., et al., [www.pgdc.com/usa/item/?itemID=30453](http://www.pgdc.com/usa/item/?itemID=30453)

<sup>5</sup> See Charitable Gift Annuities Make Regulator’s Top 10 Scam List, Planned Giving Design Center, September 19, 2002, [www.pgdc.com/usa/item/?itemID=54550](http://www.pgdc.com/usa/item/?itemID=54550).

<sup>6</sup> See comments by the ACGA at [www.acga-web.org/scams.rhtml](http://www.acga-web.org/scams.rhtml)

<sup>7</sup> See Commission News, [www.azcc.gov/divisions/securities/news\\_releases/2002/Apr01c-02.pdf](http://www.azcc.gov/divisions/securities/news_releases/2002/Apr01c-02.pdf)

<sup>8</sup> See Tax Analyst Summary on the Planned Giving Design Center’s website at [www.pgdc.com/usa/item/?itemID=54550](http://www.pgdc.com/usa/item/?itemID=54550)

<sup>9</sup> See Testimony of Christine A. Bruenn, NASAA President and Maine Securities Administrator, U.S. Senate Committee on Banking, Housing and Urban Affairs, May 7, 2003, [http://www.nasaa.org/Issues\\_\\_\\_Answers/Legislative\\_Activity/Testimony/555.cfm](http://www.nasaa.org/Issues___Answers/Legislative_Activity/Testimony/555.cfm)

<sup>10</sup> *Supra*

<sup>11</sup> *Supra*

<sup>12</sup> See, the press release by the North American Securities Administrators Association, September 4, 2003, “State Securities Cops: Senior Investors Facing a Perfect Storm for Investment Fraud” [http://www.nasaa.org/NASAA\\_Newsroom/News\\_Release\\_Archive/1552.cfm](http://www.nasaa.org/NASAA_Newsroom/News_Release_Archive/1552.cfm)

# WE ARE COMMITTED TO TWO THINGS:

## Our clients and our clients' donors.

STATE STREET GLOBAL ADVISORS | SSGA<sup>®</sup>

### Managing Gift Planning Programs

State Street Global Advisors is a leading provider of charitable trust services for nonprofit organizations. We provide our clients a full range of trust administration, investment management, tax services, and stewardship support.

We understand donor requirements and expectations and, through top-quality client service, we deliver:

- Diversified, tax efficient investment solutions
- Exceptional administration
- World class fiduciary support
- Timely, accurate tax work
- State-of-the-art technology and reporting

**To learn more, please contact:**

**Julie Hassel at 617.664.8754 or Hillary Repucci at 617.664.2069**

**[www.ssga.com](http://www.ssga.com) / [www.statestreet.com](http://www.statestreet.com)**





## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



## **Investing CRT Assets**

Presented by:

**David G. Ely**  
Vice President, Charitable Asset Management  
State Street Global Advisors  
1 Lincoln Street, 24th Floor  
Boston, MA 02111  
(617) 664-2357  
David\_Ely@ssga.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## American Council on Gift Annuities

April 29, 2010

David G. Ely, CFA

## Investment Charitable Trusts-Basics

### Customizing Life Income Portfolios — Factors to Consider

Institution	Planned Giving Vehicle	Donor/Beneficiary
<ul style="list-style-type: none"> <li>• Investment policy</li> <li>• Risk tolerance</li> <li>• Constituencies               <ul style="list-style-type: none"> <li>– Planned giving staff</li> <li>– Investment staff</li> <li>– Administrative staff</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Type:               <ul style="list-style-type: none"> <li>– Charitable Remainder Unitrust</li> <li>– Charitable Remainder Annuity Trust</li> <li>– Net Income Trust</li> </ul> </li> <li>• Payout Rate</li> <li>• Time Horizon</li> <li>• Tax characteristics</li> </ul>	<ul style="list-style-type: none"> <li>• Age</li> <li>• Income needs and expectations</li> <li>• Risk tolerance</li> <li>• Financial/estate planning issues</li> </ul>

STATE STREET GLOBAL ADVISORS | SSGA

### Planned Giving Programs vs. Endowments

	Planned Giving Program	Endowment
Tax Status	Taxable (usually)	Tax Exempt
Time Horizon	Donor's Life Expectancy	Unlimited
Risk Tolerance	Based on vehicle and balance of donor/institution	Institution-based
Payout Rate	Varies by vehicle/donor	Single rate/depending policy
Return Requirements	Based on vehicle/donor	Institution-based
Assets	Many smaller pools	One large pool
Unrelated Business Income	Potential Excise Tax	Limits on UBIT
Liquidity Requirements	Varies by vehicle/donor	Institution-based

STATE STREET GLOBAL ADVISORS | SSGA

### Fiduciary Responsibility

- **Fiduciary**
  - One that stands in a special relation of trust, confidence, or responsibility in certain obligations to others
  - Income beneficiary
  - Remainderman/charitable organization
- **Prudent Investor Rule**
  - Standard of prudence applies to total portfolio, rather than to individual investments (vs. Prudent Man)
  - Tradeoff between risk and return is central consideration
  - Can invest in anything that plays an appropriate role in portfolio
  - Diversifying investments integrated into the definition of prudent investing

STATE STREET GLOBAL ADVISORS | SSGA

### Risks

- **Inflation Risk**
  - The risk that investment will not keep pace with inflation, reducing purchasing power
- **Credit Risk**
  - The possibility a loan will not be fully repaid
- **Interest Rate Risk**
  - The risk that interest rates will increase—prices on existing bonds move in the opposite direction to interest rates
- **Price/Market Risk**
  - The risk that an investment will decline in absolute value

STATE STREET GLOBAL ADVISORS | SSGA

## Some Other Risks

- Rearview Mirror Risk
  - Basing long-term investment policy on recent investment events
- I Don't Care About Remainder Value Risk
  - Investing only in bonds to ensure stable or higher beneficiary payments

STATE STREET GLOBAL ADVISORS | SSGA

STATE STREET GLOBAL ADVISORS | SSGA

## Developing Investment Policy

## Investment Policy Statement Understanding Your Goals and Objectives

- Objectives
  - Return
  - Risk
- Constraints
  - Spending Rules
  - Tax Implications
  - Liquidity needs
  - Time horizon – Specific funding goals
  - Special circumstances – Social or environmental screens?

STATE STREET GLOBAL ADVISORS | SSGA

## Investment Policy Statement Understanding Your Goals and Objectives

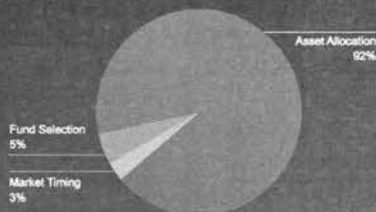
$$\sigma \neq \sum_n \text{fear}$$

- How organizations define risk
  - Losing money
  - The unknown... unfamiliar investments
  - Past experience... previous losses in familiar investments
  - Herd mentality... feel better following the crowd
  - Loss averse, not risk averse
- Level of Risk Aversion and Return Objectives changes with wealth

STATE STREET GLOBAL ADVISORS | SSGA

## Importance of the Right Mix

- The asset allocation decision is the most significant contributor to overall performance



The information contained herein is for illustrative purposes only.

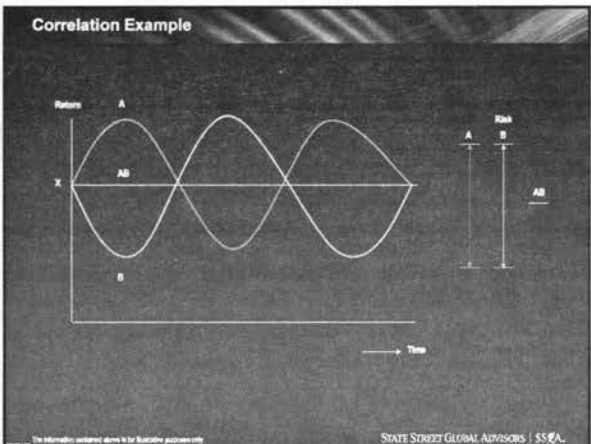
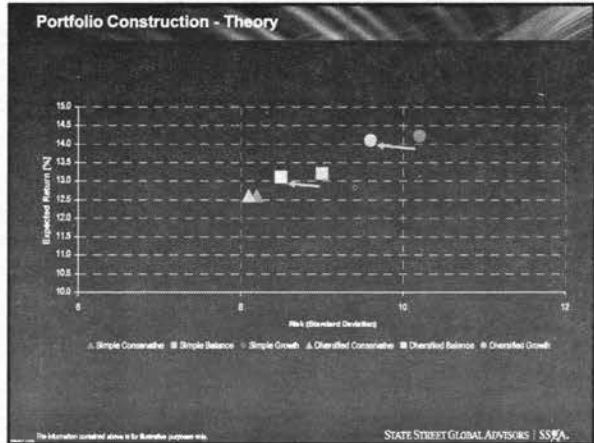
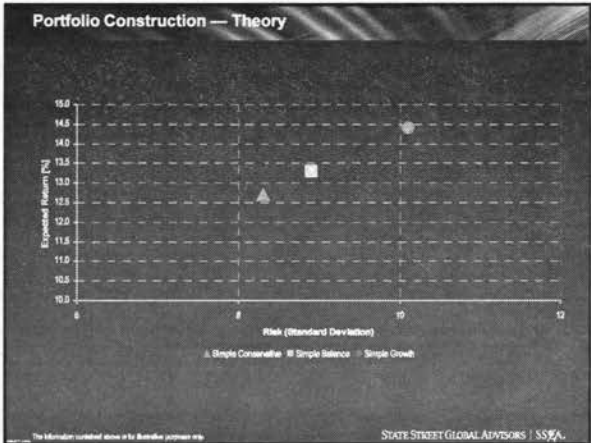
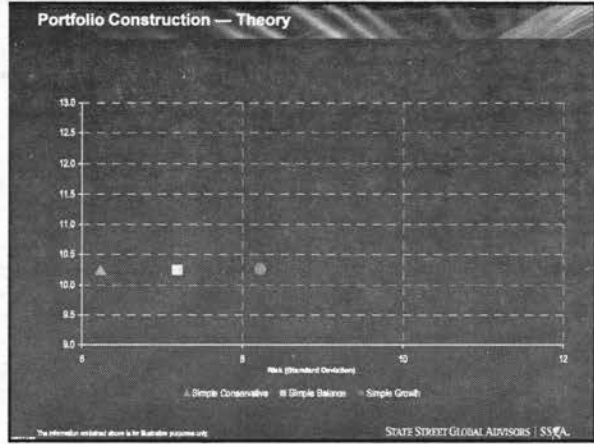
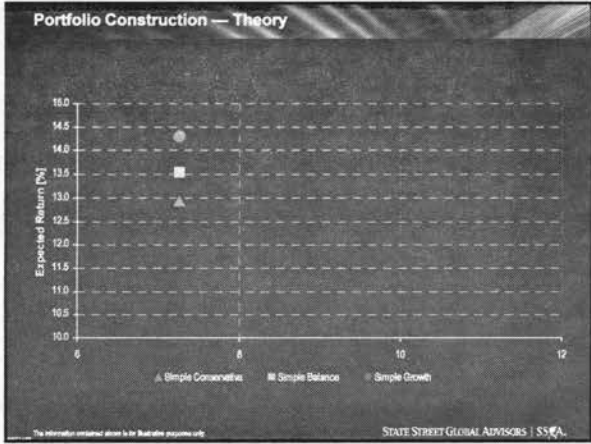
STATE STREET GLOBAL ADVISORS | SSGA

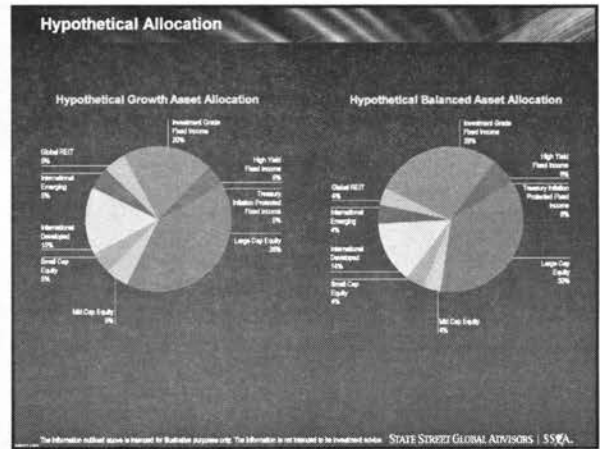
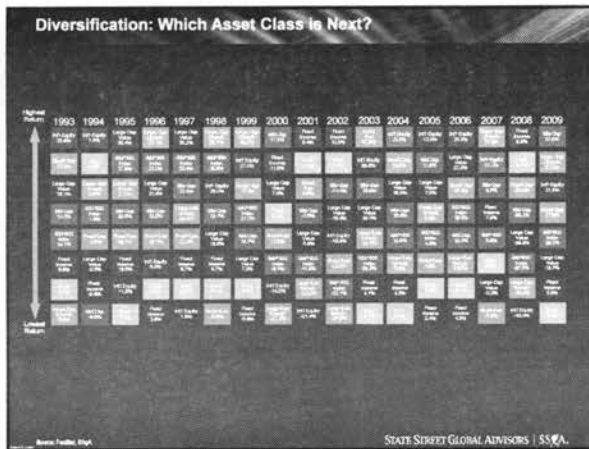
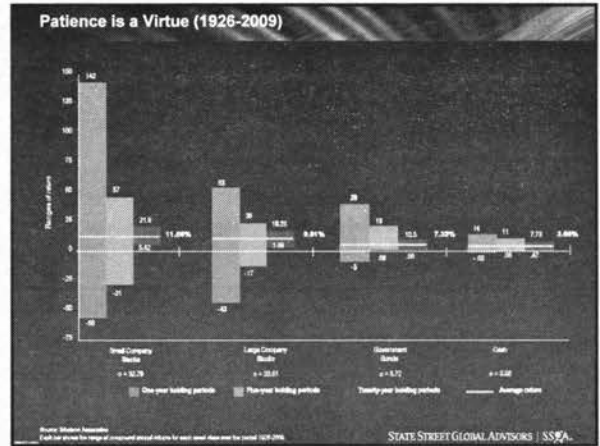
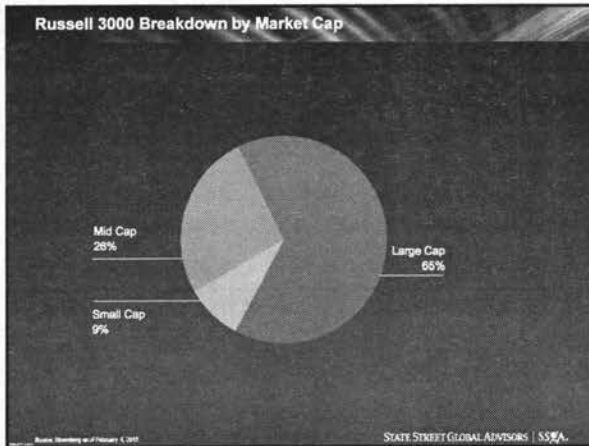
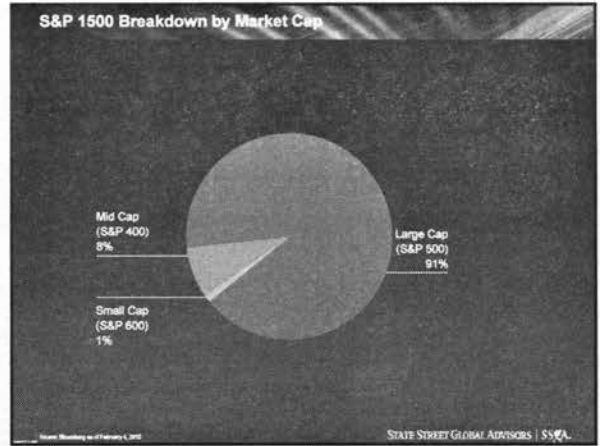
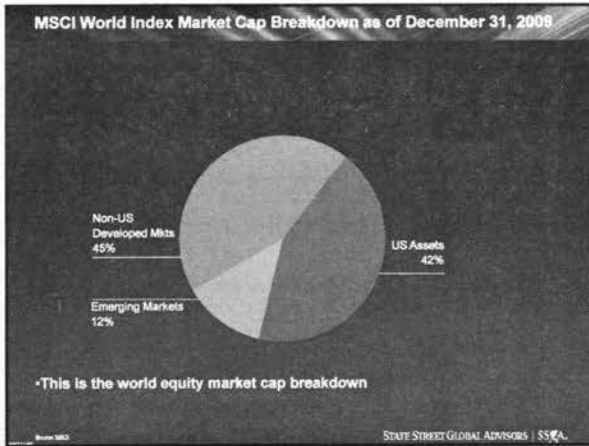
## What is Passive Management? Product of Historical Market Analysis

- Modern Portfolio Theory — Harry Markowitz (1952)
  - Investors are rational and make reasonable decisions over time
  - Investors make decisions based on an evaluation of risk and return potential
  - An optimal portfolio consists of a series of asset classes that offers the maximum possible expected return for a given level of risk, i.e., the "efficient frontier"
- Efficient Market Hypothesis — Eugene Fama (1965)
  - Impossible to beat the market
  - At any given time prices reflect all available information on a particular stock and/or market

Solution = Own the Market, i.e., Embrace Indexing

STATE STREET GLOBAL ADVISORS | SSGA





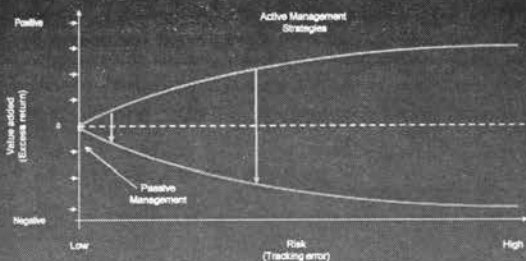
## Implementation

## Implementation Decisions

- How do you implement the asset allocation?
  - Passive/Indexing
  - Active management
  - Styles
  - Sector specialties
  - Funds versus individual securities
  - Pools under PPA
  - Mutual Funds and ETFs
  - PLR Options

## The Active Management Risk Spectrum

### Risk and Return Expectations



The information contained above is for illustrative purposes only.

## What is Active Management? Belief that Markets are Inefficient

- History and human behavior
  - Investors are not rational — motivated by fear and greed
  - Many examples of financial bubbles and historical anomalies (dot com boom/bust, real estate melt-down, etc.)
- Premise hinges on ability to identify winners and losers
  - Stock selection
  - Manager selection
  - Style/sector rotation
  - Market timing

Solution = Don't Own the Whole Market, Just Own the Most Attractive Companies Within the Market

## Advantages/Disadvantages of Active Management

- Advantages
  - Potential to beat the market
  - Protection in down markets
- Disadvantages
  - Relatively higher costs and fees
  - Risk and unpredictability

## The Key Question — How do you Effectively Utilize Both? Efficiency vs. Value Add

- Passive
  - Efficient asset classes
  - Broad market categories
  - Fee and tax sensitive
- Active
  - Less efficient asset classes
  - High value added generating categories
  - Risk-aware and absolute return

An Investors "Risk Budget" Determines the Appropriate Mixture

## Risk Budgeting —The Allocation of Risk

### What is risk budgeting?

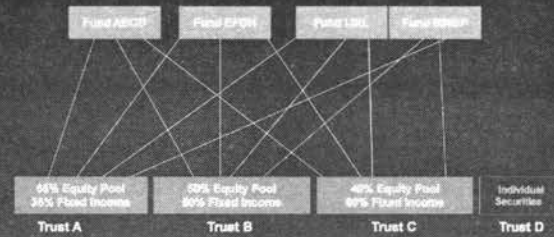
- A disciplined management process for allocating risk across asset classes based on the premise that active risk should be taken in areas that compensate for it

"You cannot manage outcomes, you can only manage risk."  
(Peter Bernstein)

STATE STREET GLOBAL ADVISORS | SSGA

## Sample Mutual Fund Structure

### Underlying Strategies



The information contained herein is for illustrative purposes only.

STATE STREET GLOBAL ADVISORS | SSGA

## Mutual Funds Held in Planned Giving Portfolios

### Advantages

- Daily Liquidity
- Transparency-donor knows exactly what is held in trust portfolio
- Consistent performance by account
- Lower out of pocket expense

### Disadvantages

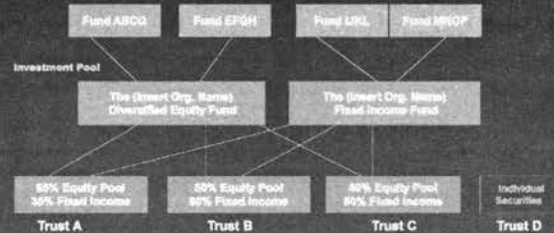
- Potential for "model creep"
- Potential for greater return dispersion
- Increased opportunity for error

STATE STREET GLOBAL ADVISORS | SSGA

## Sample Pooling Structure

### Equity and Fixed Income Pools

#### Underlying Strategies



The information contained herein is for illustrative purposes only.

STATE STREET GLOBAL ADVISORS | SSGA

## Investment Pools for Planned Giving Portfolios

### Advantages

- Streamlines tracking and reporting of trusts for the multiple parties
- Promotes consistent allocation and performance across trusts
- Strengthens marketing appeal to participate in a customized investment pool exclusively for the (Insert Org. Name)
- Consistent performance by asset class

### Disadvantages

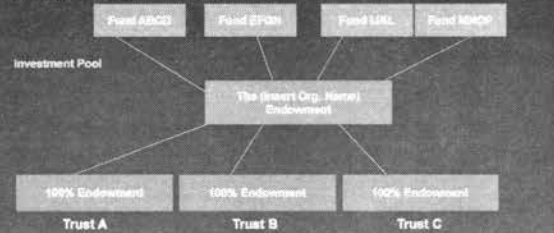
- Limited liquidity
- No Transparency
- Higher out of pocket expense

STATE STREET GLOBAL ADVISORS | SSGA

## Sample PLR Structure

### Equity and Fixed Income Pools

#### Underlying Strategies



The information contained herein is for illustrative purposes only.

STATE STREET GLOBAL ADVISORS | SSGA



### PLR Option for Planned Giving Portfolios

- **Advantages**
  - Streamlines tracking and reporting of trusts for the multiple parties
  - Promotes consistent allocation and performance across trusts
  - Strengthens marketing appeal to participate in the Endowment of (Insert Org. Name)
  - Consistent performance by asset class
- **Disadvantages**
  - Limited liquidity
  - No Transparency
  - Higher out of pocket expense
  - Adverse taxation to income beneficiaries

STATE STREET GLOBAL ADVISORS | SSGA

### Example: Core/Satellite Asset Allocation Strategy

- **Develop Core/Satellite Asset Allocation**
  - Establish diversified core investment with predictable asset behavior and low costs
  - Allocate risk budget to satellite segments with opportunities to add alpha



- **Result**
  - Mostly core passive/enhanced
    - Large Cap
    - Global Equity
    - Fixed Income
  - Find active managers with skill to add value
  - Use active in specialized segments (i.e. sectors & Hedge)
  - Avoid "boxing in" active managers search for return

STATE STREET GLOBAL ADVISORS | SSGA

### Benefits of Rebalancing

- Disciplined rebalancing ensures targets are kept on track
- Avoids drift in risk profile and unintended exposures
- **Typical Methods**
  - Calendar periods
  - Ranges
  - Combination of calendar and ranges

STATE STREET GLOBAL ADVISORS | SSGA

### Summary

- Understand the objectives and how they can change
- Diversification and solid portfolio construction is key
- Efficiently implement portfolio across approaches to ensure you get compensated for the additional risk

STATE STREET GLOBAL ADVISORS | SSGA

STATE STREET GLOBAL ADVISORS | SSGA

### Measuring Results

### Returns — Ways to Think About Performance

- Meeting a percentage of the original gift
  - Is 50% a good gift in real terms?
- Exceeding trust payouts
- Performance relative to benchmarks

STATE STREET GLOBAL ADVISORS | SSGA





# The Six Bridges Group

**Come visit us at Booth 25**

The Six Bridges Group is a network of select highly regarded professional consultants within Morgan Stanley Smith Barney

- ❖ **Customized strategies for complex investment issues**
- ❖ **Local, National, and International**
- ❖ **Concierge level of services**
- ❖ **Specialized Programs for Charitable Gift Annuities**
- ❖ **Specialized Programs for Scholarships Programs**
- ❖ **Specialized Programs for Trusts**

Contact: Dennis Berry  
Ben Robinson  
800-421-3028  
501-258-6562  
[www.fa.smithbarney.com/sixbridges](http://www.fa.smithbarney.com/sixbridges)

Morgan Stanley  
Smith Barney

Investment Products > NOT FDIC Insured > NO Bank Guarantee > May Lose Value



## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



# **The Facts of Life (Estates): Remainder Interests in Residences and Farms**

Presented by:

**David Wheeler Newman  
Chair, Charitable Sector Practice  
Mitchell Silberberg & Knupp LLP  
11377 West Olympic Blvd.  
Los Angeles, CA 90064  
(310) 312-3171  
dwn@msk.com**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



**The Facts of Life (Estates):  
Gifts of Remainder Interests in Residences and Farms**

**David Wheeler Newman**

**I. Partial Interest in Real Estate.**

A. General. No charitable deduction is allowed (for income, estate or gift tax purposes) for a charitable gift of less than the donor's entire interest in a piece of property. While there are exceptions to this general rule which form the basis for the field of planned giving, these exceptions are narrowly construed by the IRS and the courts.

B. Exceptions.

1. A contribution of the donor's entire interest in the property may be deducted, even if what the donor owns is a partial interest. IRC § 170(f)(3)(A).
2. A remainder interest in a charitable remainder trust or pooled income fund. IRC § 170(f)(2)(A).
3. The income interest in a charitable lead trust. Note that, while contributions to all qualified charitable lead trusts will qualify for the gift and estate tax deduction only contributions to those which are also grantor trusts will qualify for the income tax deduction. IRC § 170(f)(2)(B).
4. A remainder interest in a personal residence or farm. IRC § 170(f)(3)(B)(i).
5. An undivided portion (not in trust) of the donor's entire interest in the property. IRC § 170(f)(3)(B)(ii)
6. A qualified conservation contribution. IRC § 170(F)(3)(B)(iii).

C. Common Violations.

1. A gift of the right to use property without the transfer of ownership.
2. Retention by the donor of substantial rights to the property.

**II. Remainder Interest in Personal Residence.**

A. General. A charitable deduction is allowed for a contribution of a personal residence, subject to a life estate retained by the donor. This gift vehicle is very well suited to these situations:

1. A donor wishes to make a testamentary charitable gift of real property while enjoying a current income tax deduction;
2. A donor who is receiving income, for example from an IRA or from investments, but with no available tax deductions;
3. A donor who wants to make a substantial charitable gift now without losing any security;
4. A donor who is “house rich but cash poor”;
5. A donor who would like to plan her estate to avoid the probate process by making a non-probate transfer of a substantial asset.

Four main requirements must be met for this type of gift to qualify for income, estate and gift tax deductions.

- B. Personal Residence: To qualify, a personal residence does not need to be the donor’s *principal* residence. For example, a donor’s vacation home qualifies as a personal residence. Under IRS guidelines, all that is required for something to qualify as a personal residence is that it contain facilities for cooking, sleeping, and sanitation. Rev. Rul 74-241. The IRS has even ruled that a boat meeting these requirements qualifies as a personal residence. PLR 8015017. The regulations provide that a personal residence also includes stock owned by a donor in a co-op if the unit that the donor is entitled to occupy is used by the donor as a personal residence.
1. In PLR 8711038, a portion of the residence was rented by the donor to an unrelated tenant. The IRS nevertheless concluded that the property qualified as a personal residence for purposes of this provision. The Private Letter Ruling cited Revenue Ruling 78-303 in which a retired farmer, a portion of whose farm was leased to an unrelated third party, contributed the farm to charity subject to the farmer’s retained life estate. (Note that the same provision of the Code provides for gifts of both personal residences and farms, subject to a retained life estate). It seems that this logic should be extended to a duplex or triplex, so long as a portion of the property has been used by the donor as a residence.
- C. Farm. For these purposes, the term “Farm” means any land used by the donor *or his tenant* for the production of crops, fruits, or other agricultural products or for the sustenance of livestock. The term “livestock” includes cattle, hogs, horses, mules, donkeys, sheep, goats, captive fur-bearing animals, chickens, turkeys, pigeons, and other poultry.
- D. Not in Trust. The second requirement for the remainder interest to qualify is that the gift may not be made in trust. Note that this can be an issue for testamentary gifts of a remainder interest through a living trust.



1. *Example 1.* A mother provides in her living trust that, at her death, her residence will be held in trust for the ultimate benefit of her alma mater, retaining for her daughter the right to use this trust asset during the daughter's lifetime. The estate tax charitable deduction could be denied since the gift of the remainder interest to charity is made via the trust. Rev. Rul 76-357. This unfortunate result could have been avoided, and the estate tax deduction preserved, if the living trust instead provided that, at the mother's death, the trustee is to distribute the property to charity subject to the daughter's life estate.
- E. Irrevocable. The third requirement is that the remainder interest passing to charity must be irrevocable. In Revenue Ruling 85-23, the donor's will provided for a bequest of the family farm to Child A for life, with the remainder to charity. So far, so good. However, the will further provided that, if Child B survived Child A, the remainder will vest in Child B instead of the charity. The IRS ruled that this bequest to a charity was contingent, and the estate tax charitable deduction was denied.
1. *Example 2.* The donor retains the right to live in her house for the rest of her life and provides that, at her death, the property should go to charity, but only if her brother fails to survive the donor. If the brother is living at the death of the donor, the house goes to him instead. The IRS disallowed the charitable income tax deduction in this situation, ruling that if the probably exceeds 5% that the non-charitable beneficiary will receive the property, no deduction is allowed.
  2. *Example 3.* The gift of the residence to charity must be unrestricted (subject only to the retained life estate). For example, the donor provides for the transfer of his residence to charity, subject to his life estate, but further provides that, when the charity sells the house, 20% of the proceeds must be given to the donor's brother. In this situation, no charitable income tax deduction is allowed since the gift of charity is not unrestricted.
  3. Assume, instead, that the donor transferred the property 80% to the charity and 20% to the brother, with the interest of both co-tenants subject to the donor's life estate. In this way, when the charity and the brother join together to sell the residence following the death of the donor, the desired result will be achieved. In Revenue Ruling 87-37, the IRS determined that the donor was entitled to a charitable income tax deduction as to the 80%.
- F. Remainder in the Property Itself. A fourth requirement that the IRS takes quite seriously, but which has caused a surprising amount of confusion over the years, as demonstrated by a series of rulings, is that the charity must receive the remainder interest in the property itself, as opposed to the proceeds from a sale of the property. In Revenue Ruling 76-543, as amplified by Revenue Ruling 77-169, the IRS held that no charitable deduction is allowed for a remainder interest in a

decedent's personal residence bequeathed to charity under a will that provides that the property is to be sold upon the life tenant's death and the sale proceeds paid to charity. This is a painful result since the donor probably thought he was doing the charity a favor by making the executor of his estate, rather than the charity, responsible for selling the residence.

1. Even if the charity is given an irrevocable remainder interest in the personal residence, it might not be unreasonable for donor to want to retain the flexibility to convert a retained life estate into cash. Suppose that, in the life estate agreement, the charity agrees that, if the donor needs to move out of the residence due to poor health, the charity will join with the donor in selling the residence with the proceeds of the sale divided actuarially between them. The IRS held, in Revenue Ruling 77-305, that this created a chance that the charity would eventually receive something other than outright ownership of the residence – namely, the proceeds of sale of its remainder interest in the residence. The deduction was denied.
2. The desire of a donor to retain this flexibility is understandable, especially if the equity in the home is her largest asset. For example, she may require substantial assets in the future to move into an assisted living facility. However, the experience of several organizations with active residential remainder programs is that the same result is often achieved voluntarily with no legal right retained by the donor to compel this result, for a couple of reasons. First, one of the few drawbacks of a life estate arrangement, as with some other forms of planned gifts, is that the charity must wait to receive the cash proceeds from a gift. If the donor needing to convert her life estate in a residence into cash were to approach the charity with a proposed sale, many organizations would go along with the plan in order to accelerate the maturity of the gift. Moreover, since one of the core concepts of planned giving is for the charity to attempt to accommodate the legitimate interests of the donor, simple donor relations would make charities receptive to this proposal, even if the life tenant has no legal right to compel the result.

G. Steps for the Gift. Before the personal residence is accepted by the charity, the charity should investigate things that will affect its responsibilities as the owner of the property.

1. Obtain a title report to ensure a clear chain of title and consider obtaining title insurance.
2. Verify the existence of covenants, easements and other agreements affecting the property.
3. Confirm zoning compliance.
4. Verify building codes.

5. Inspect property for material defects.
6. Follow the charity's standard procedures regarding environmental hazards of real property.

H. Documentation Required. A deed is the form of documentation required to transfer the property from the donor to the charity. The deed should contain language reserving to the donor (or one or more other persons) the right to live in the residence for life or for a term of years. Requirements for the formalities of the deed vary from state to state. The deed should therefore be prepared or at least reviewed by an attorney admitted to practice in the state where the residence is located. Since under the deed the life tenant(s) and the charity will each own an interest in the property, there should be a written life tenancy gift agreement that clearly provides for the terms of the life estate. The life tenancy gift agreement should provide that the responsibilities of the life tenant include responsibility to maintain the property and pay property taxes. The life tenancy gift agreement should require the life tenant to carry insurance on the property naming the charity as one of the insured parties. The agreement should provide the charity with the right of access to the property at any time, after appropriate notice, for the purpose of inspecting the property. The document may allow the life tenant to lease the property to another person, but only if the charity consents to the lease.

1. A sample life tenancy gift agreement is attached as Appendix A.

I. Calculation of Deduction. To calculate the donor's income tax deduction, the planner must know the market value of the property, the allocation of that value between land and buildings, the useful life of the building on the property, the anticipated salvage value of that building, the term of the retained interest (typically for one or more lives, but maybe for term of years) and the applicable federal rate (AFR) for the month of the gift. The reason you need the useful life of the building and its salvage value is that Code Section 170(f)(4) directs that depreciation and depletion must be taken into account for purposes of determining the remainder value. Straight-line depreciation is used, which requires the useful life and salvage value of the building.

1. *Planning Tip:* The greater the value of land in relationship to the value of the building, the larger the deduction. This produces larger charitable deductions for residential remainder gifts in parts of the country with high residential property values.
2. The useful life is calculated beginning on the day of the gift. The allocation between land and building may be taken from the appraisal or possibly from the property tax bill. Once the portion of the property's value which is allocable to the structure has been determined, a typical calculation would assume that the structure will have an eventual salvage value of 20% of that amount following a forty-five-year useful life.

3. The AFR may be selected from the AFR from the current month or for the prior two months, whichever produces the largest charitable deduction.
4. *Example 4:* The donor, age 80, owns her home valued at \$1,000,000 without any mortgage or other encumbrance. When she contributes the home to her alma mater, subject to her retained life estate, she is entitled to an income tax deduction of approximately \$668,000. If, on the other hand, the same donor instead leaves the property to her alma mater in her will, subject to a life estate in her daughter, then age 50, the donor's estate will be entitled to a charitable tax deduction of about \$255,000. (The substantial difference in the deduction is attributable to the difference in ages of the life tenants.)

J. Planning Opportunities. Even though the IRS takes the basic requirements very seriously, this does not mean that this planned giving vehicle is completely inflexible. In fact, there are plenty of opportunities for planners to exercise their creativity.

1. The regulations specifically allow the charity's remainder interest to follow a term of years, rather than a life estate.

*Example 5:* The donor anticipates that he will not be using the cabin by the lake after his children are grown. He might give the residence to charity, subject to a retained right to use the property for, say, seven years. This will yield a substantially larger deduction for younger donors, as compared with a retained right to use the property for their entire lives.

2. Speaking of vacation homes, Revenue Ruling 75-420 involved a remainder interest in a personal residence combined with a current gift of a tenancy in common. (One of the other exceptions to the partial interest rules is for a gift of an undivided portion of the donor's entire interest in the property.)

*Example 6:* The donor only used the lake house during the summer. He transferred the property to his alma mater, retaining the right to use the property during his life only in the summer months. The college had the right to use the property the rest of the year (and the college in fact planned to use the property during the academic year for a study center and for events). The IRS allowed a double deduction – for the tenancy in common as to the exclusive right to use the property during the academic year, and a remainder interest and the right to possession of the personal residence in the summer.

K. Transfer Tax Issues. Gift or estate taxes will need to be considered if the donor transfers the right to use of the residence to a non-spouse beneficiary, such as a child, rather than retaining that right for herself.

1. If the transfer is made during the donor's life, a current gift tax arising from the life estate transferred to the non-charitable beneficiary may be avoided by the donor retaining the right to revoke that person's interest, either during life or through the donor's will.
2. *Example 7:* The donor may transfer the property to charity, subject to her right to remain in the property for her life followed by the right of her daughter to reside in the property for her life. If she has retained the right to revoke the daughter's interest, there will be no current gift tax arising from the gift to the daughter. However, if the donor dies without exercising the right to revoke, the actuarial value of the daughter's life estate in the residence, determined at the death of the donor, will be included in the donor's estate for estate tax purposes.

L. Exclusion of Gain.

Code Section 121 provides that gross income does not include gain from the sale of a residence if during the five-year period ending on the date of the sale the property has been used by the taxpayer as his or her *principal* residence for a period aggregating two years or more. The exclusion is gain of up to \$250,000 (or \$500,000 for taxpayers filing a joint return).

1. There is a specific provision allowing the exclusion of gain under Section 121 if the interest disposed of is not the principal residence itself but a remainder interest in the principal residence. Since the funding of a gift annuity with a remainder interest in the residence is treated for tax purposes as a bargain sale of that remainder interest, this provision of Section 121 allows gain resulting from that bargain sale to be excluded from gross income.
2. So long as the donor is an annuitant, capital gain recognized from the transfer of appreciative property in exchange for an annuity is recognized over the life expectancy of the donor/annuitant. This means that of each annuity payment received, a portion as ordinary income, a portion will be tax free recovery of the donor's basis in the property and the remainder will be capital gain recognized. If the donor otherwise meets the requirements for exclusion of gain under Section 121, the capital gain portion may be excluded from gross income up to the entire amount allowable (\$250,000, or \$500,000 if filing jointly).

- M. Combination With Gift Annuity. This is a popular variation on the bargain sale transaction. The actuarial value of the annuity received is treated as the amount realized by the donor in connection with the transfer. The amount of any liabilities to which the property is subject is also treated as part of the amount realized.

1. The allocation of basis to the property transferred, and the resulting capital gain, is determined in a manner similar to the allocation in bargain sales transactions. If a discharge of liabilities occurs, the basis must be allocated among the retained life estate, the annuity portion, the discharge of liability portion and the gift portion of the property transferred.
2. Gain attributable to the discharge of the liability is recognized by the donor in the year of transfer, but gain attributable to the value of the annuity is spread ratably over the life expectancy of the annuitants if the annuity is nonassignable.

*Example 8:* Donor age 75 would like to fund a gift annuity with her residence within a market value of \$300,000 and a basis of \$50,000. Since the potential gain from selling the residence does not exceed the available Section 121 gain exclusion of \$250,000, the gift planner may treat the annuity as funded with cash for purposes of calculating the taxation of annuity payments.

Value of remainder	\$176,100
Annuity 6.3%	\$11,094
Ordinary income	\$3,261
Tax free	\$7,833

*Example 9:* Assume instead that this donor's home is worth \$1,000,000 with a basis of \$50,000. Since the potential gain of \$950,000 exceeds the Section 121 exclusion amount, we will need to perform the following calculation to determine what, if any, portion of her annuity payment will be recognized as capital gains.

Value of remainder	\$591,535
Annuity 6.3%	\$37,267

### Gain Recognition

Allocate basis to remainder	
$591,535/1,000,000 \times 50,000$	29,577
Present value of annuity	326,060
Bargain sale basis	
$326,060/591,535 \times 29,577$	16,303
Gain <sup>1</sup>	309,757
Life expectancy of annuitant	12.4

<sup>1</sup> There is no IRS guidance on how the Section 121 exclusion amount should be applied in this context. One approach is to add the exclusion to the bargain sale basis, effectively applying the exclusion over the life expectancy of the annuitant. The second approach is to apply the exclusion as quickly as possible to the capital gain as it is recognized. These examples adopt the second approach.

### Taxation of Annuity

Tax-free portion	1,316
Capital gain	24,995
Ordinary income	10,956

Applying the Section 121 exclusion, no capital gain will be recognized for the first ten years, with the result that, during that period, the annuity will consist of a tax-free portion of \$26,311 and ordinary income of \$10,956.

*Example 10.* Assume the donor (age 75) owns her home worth \$1,250,000, subject to a mortgage of \$200,000, in which she has a basis of \$300,000, which she would like to use to fund a gift annuity.

### Calculation of Annuity

Equity in property (\$1,250,00 - 200,000)	\$1,050,000
Value of (net) remainder (59.2%)	621,600
Annuity 6.3%	39,161

### Gain Recognition

Liability allocated to remainder (59.2%)	118,400
Present value of annuity	342,632
Total amount realized	461,032
Basis allocated to remainder (59.2%)	177,600
Bargain sale basis	
$461,032/790,000 \times 177,600$	103,645
Total gain $461,032 - 103,645$	357,387
Gain allocable to liability	
$118,000/461,032 \times 357,387$	91,472
Use this amount as Section 121 exclusion	(91,472)
Gain taxable this year	0
Remaining gain	265,915

### Taxation of Annuity

Tax-free portion	6,636
Capital Gain	21,012
Ordinary Income	11,513

Applying the remaining Section 121 exclusion of \$158,528 (\$250,000 minus \$91,472), this means that no capital gain will be recognized for the first seven years. During this period, the annuity will consist of ordinary income of \$11,513 with the remaining annuity payment entirely tax-free.

- N. Risk Management. A charity issuing a gift annuity in exchange for or remainder interest in residence is assuming risks associated with that remainder, including the risks that the property may not sell for its appraised value when the life estate terminates, and that the property may take an extended period of time to sell, meaning that the charity will have maintenance, taxes, insurance and other carrying costs pending the sale. At the same time, the charity is incurring the substantial obligation of the annuity. To mitigate the risks inherent in this gift funding vehicle, the issuing charity may apply a discount to the amount of the annuity it is willing to pay in exchange for the remainder interest in the residence. For example, rather than the 6.3% annuity otherwise payable to a 75-year-old in the preceding 3 illustrations, the charity might offer a reduced amount of, say, 5.0%.

### III. Appraisal Requirements and Valuation Issues.

- A. In General. Donors must obtain qualified appraisals for charitable contributions of certain property, including real estate, if the claimed value of the property is greater than \$5,000. These rules were strengthened by the American Jobs Creation Act (2004) and the Pension Protection Act (2006).
- B. IRS Form 8283. The donor must attach this form to his tax return for the year in which the deduction for the gift is claimed.
1. The appraisal must be made not earlier than 60 days before the date of the contribution, and before the filing of the tax return on which the deduction is first claimed.
  2. The appraisal must be performed by a qualified appraiser who is an individual with verifiable education and experience in valuing the relevant type of property for which the appraisal is performed. Under regulations proposed by the IRS, an individual has verifiable education and experience if the individual has successfully completed professional- or college-level coursework in valuing the relevant type of property and has two or more years' experience in valuing that type of property. In addition, because significant education and experience are required to obtain a designation from a recognized professional appraisal organization, appraisers with these designations are deemed to have demonstrated sufficient verifiable education and experience.
  3. The appraisal must include:
    - a) Description of the property
    - b) Date of gift
    - c) Terms of any agreement relating to use of the property
    - d) Name, address, etc., of the qualified appraiser



- e) The appraiser's qualifications
  - f) The specific standard of valuation used (e.g., replacement cost, capitalization of income of sales of comparable property)
4. If the deduction claimed is more than \$500,000, the complete appraisal (not just the Form 8283) must be attached to the tax return on which the appraisal is claimed.
- C. Timing. The appraisal must be made no earlier than 60 days before the gift. It must be received before the due date (including extensions) of the return on which a deduction for the gift is first claimed.
- D. Valuation Adjustments. The same discounts that work to the taxpayer's benefit for gift and estate tax purposes -- e.g., discounts for lack of control and marketability that affect the value of a partial interest in real estate or an interest in a family limited partnership -- must also be taken into account when determining the amount of the charitable deduction.
- E. Disclosure by Charity. If the charity disposes of the contributed property within 3 years of the gift, it must notify the IRS of the sales price using Form 8282.

#### IV. Environmental Hazards.

Charity as owner (in the case of an outright gift), or as trustee (in the case of a gift in trust) may be exposed to liability for the expense of cleaning up hazardous waste.

- A. Environmental Review Policies. Many charities have adopted a policy that the organization may not accept a gift of real property without first evaluating the environmental risks.
- 1. An evaluation can uncover problems and help quantify the costs of correcting them.
  - 2. The evaluation may also protect the charity against problems that are discovered later, since the organization has exercised due diligence in investigating the property, even if problems which later come to light are not discovered in the evaluation.
  - 3. If the evaluation uncovers a hazardous waste problem, the person arranging for the evaluation must notify eventual purchaser of material problems.

#### V. Practical Issues.

- A. Property Management. Among other considerations, the charitable organization must determine if it has adequate administrative resources to act as a property manager of real property on the assumption that the property will be held and operated for some time prior to sale.

- B. Negative Cash Flow. Similarly, the organization must analyze the operating income (if any) and expense arising from the property to determine the likelihood and extent of any negative cash flow. It is a financial decision to determine whether the organization is willing to fund any negative cash flow associated with real property received from donors.

The Charitable Sector Practice  
at  
Mitchell Silberberg & Knupp LLP

Celebrating 100 Years of Service

Contact David Wheeler Newman  
(310) 312-3171 ▪ [dwn@msk.com](mailto:dwn@msk.com)

APRIL 30, 2008

CHARITY  
Director of Planned Giving  
123 Elm Street  
Los Angeles, California 90064

Re: Gift of Personal Residence to  
CHARITY

Ladies and Gentlemen:

This letter will confirm my desire to make a charitable contribution to CHARITY ("CHARITY"), in the form of a gift of a remainder interest in my personal residence located in BUTTON WILLOW, CALIFORNIA, and will set forth my understanding of the terms of the gift.

I have agreed to execute a Grant Deed, granting to CHARITY my entire interest in my personal residence in BUTTON WILLOW, CALIFORNIA, as more fully described in Exhibit "A" attached hereto. This transfer is subject to my right to reside in the residence during my lifetime.

My right to reside in the residence may be terminated at any time prior to my death if either I, the person holding a duly executed Power of Attorney authorizing him or her to act on my behalf or a conservator or guardian appointed to administer my estate gives written notice to CHARITY of the voluntary termination of my right to occupy the residence. A form of Notice of Termination is attached hereto as Exhibit "1."

It is my understanding that CHARITY will record in the Office of the County Recorder the Grant Deed which I execute.

I will maintain the residence in a condition as good as it is today, except for normal wear and tear, and agree to make all necessary repairs. I will make all mortgage payments, if any, in a timely manner. I understand that by accepting this gift, CHARITY assumes no responsibility to pay taxes, insurance premiums, maintenance or repair charges, mortgage payments, assessment or management fees ("Assessments") which relate to the period during which I reside in the residence. Rather, I have agreed to pay in a timely fashion all Assessments for so long as I live in my residence.

I will not make any structural changes or improvements to the residence, nor will I make major changes in the use of the residence, including rental, without the prior written consent of CHARITY.

The insurance coverage I provide will be sufficient to cover the full replacement value of the residence, and shall name CHARITY as an additional insured. In the event of a loss covered by insurance, at my election, available insurance proceeds may be used to repair and replace any damage to the residence. I agree that if I do not so elect, the proceeds of such insurance shall be divided between CHARITY and myself in proportion to our respective interests in the residence at the time such proceeds are received.

**APPENDIX A**

If, prior to my death, I give notice to CHARITY disclaiming my right to occupy the residence, I will pay all Assessments which relate to the period during which I occupy the residence of which I have been given written notice by CHARITY. CHARITY shall be responsible for paying any Assessments which relate to the period after the date on which I cease to occupy the residence.

CHARITY shall have the right, but not the obligation, to make payments I am obligated to pay, if I fail to pay them in a timely manner as provided above. If CHARITY makes any payments which I am obligated to pay pursuant to our agreement, I agree to reimburse CHARITY for these amounts. Until repayment by me, CHARITY shall have the right to set off any payments otherwise due to me from CHARITY, including without limitation my right to receive annuity payments from CHARITY. Any amounts I am obligated to repay to CHARITY which remain outstanding at my death shall be a liability of my estate.

I hereby give to CHARITY all personal property located in the residence (or on the property on which the residence is located), unless such personal property is removed from the residence by my personal representative within thirty days of my death pursuant to a provision in my Will or a trust to which my personal property has been transferred. I agree to provide CHARITY with the names and contact information for my personal representatives (executors and trustees) and copies of any provisions relating to this personal property contained in my estate planning documents. I understand that CHARITY assumes no responsibility for my personal care or welfare, and that CHARITY encourages me to nominate a conservator and to provide CHARITY with the name and contact information of my nominated conservator.

If the foregoing accurately represents your understanding of our agreement, please sign this letter where indicated below.

Very truly yours,

---

JANE SMITH

Enclosures

ACCEPTANCE

The transfer of the residence which you currently occupy, as described in Exhibit "A" attached hereto, is accepted by CHARITY upon the terms and conditions set forth above.

DATED: \_\_\_\_\_

CHARITY

By: \_\_\_\_\_  
VICTOR VEEPEE

RECORDING REQUESTED BY AND  
WHEN RECORDED MAIL TO:

CHARITY  
Director of Planned Giving  
123 Elm Street  
Los Angeles, California 90064

NOTICE OF VOLUNTARY TERMINATION

Pursuant to the terms of the reservation contained in that certain Grant Deed from JANE SMITH to CHARITY, granting real property in BUTTON WILLOW, CALIFORNIA, described in Exhibit "A," attached hereto, JANE SMITH hereby gives notice of voluntary termination of JANE SMITH's reserved right to the exclusive possession, use, and enjoyment of rents, issues and profits of said property.

Dated: \_\_\_\_\_

\_\_\_\_\_  
JANE SMITH

STATE OF CALIFORNIA            )  
  ) ss.  
COUNTY OF                            )

On \_\_\_\_\_ before me, \_\_\_\_\_ (here insert name and title of the officer), personally appeared JANE SMITH, personally known to me (or proved to me on the basis of satisfactory evidence) to be the person whose name is subscribed to the within instrument and acknowledged to me that he/she executed the same in his/her authorized capacity, and that by his/her signature on the instrument the person, or the entity upon behalf of which the person acted, executed the instrument.

WITNESS my hand and official seal.

[SEAL]

\_\_\_\_\_  
Notary Public Signature

APPENDIX A  
Exhibit 1

RECORDING REQUESTED BY AND  
WHEN RECORDED MAIL TO:

CHARITY  
Director of Planned Giving  
123 Elm Street  
Los Angeles, CA 90064

MAIL TAX STATEMENTS TO:  
JANE SMITH, 123 MAIN STREET, BUTTON WILLOW, CALIFORNIA

---

**GRANT DEED**

JANE SMITH hereby grants to CHARITY, the real property, commonly known as 123 MAIN STREET, BUTTON WILLOW, CALIFORNIA, described in Exhibit "A" attached hereto, reserving to the Grantor the exclusive possession, use, and enjoyment of rents, issues and profits of the above granted property for and during the lifetime of the Grantor. Such reservation shall be terminated prior to the death of the Grantor if written notice of voluntary termination of such reservation in recordable form is given to CHARITY by the Grantor, or by a person authorized by a duly executed Power of Attorney to give such notice on behalf of the Grantor, or by any conservator or guardian appointed by a court of competent jurisdiction to manage the Grantor's estate.

Dated: \_\_\_\_\_

\_\_\_\_\_  
JANE SMITH

STATE OF CALIFORNIA    )  
  ) ss.  
COUNTY OF                    )

On \_\_\_\_\_ before me, \_\_\_\_\_  
(here insert name and title of the officer), personally appeared JANE SMITH, personally known to me (or proved to me on the basis of satisfactory evidence) to be the person whose name is subscribed to the within instrument and acknowledged to me that he/she executed the same in his/her authorized capacity, and that by his/her signature on the instrument the person, or the entity upon behalf of which the person acted, executed the instrument.

WITNESS my hand and official seal.

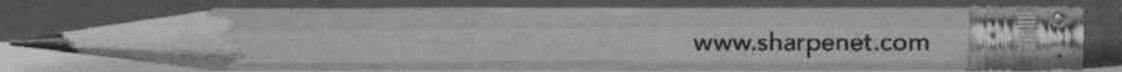
[SEAL]

\_\_\_\_\_  
Notary Public Signature



We've been sharpening our pencils...

# Maybe it's time to SHARPEn yours?



Here is how The Sharpe Group is taking steps to help you improve your results and/or stretch your budget:

- New Web services: see [webthatworks.aboutgiving.net](http://webthatworks.aboutgiving.net)
- New donor base file enhancement services
- Training webinars that eliminate travel costs
- Consulting based on 50 years of experience
- Reformatted booklet design with reduced cost
- Redesign and lower prices on many brochures
- Optional imprinting to save you more

We have taken serious steps to save you money and make your program more effective.

Now may be the time to see if we can help you make your training, gift marketing, consulting, and Web presence go further.

Contact us at 1-800-238-3253 or [www.sharpenet.com](http://www.sharpenet.com) for more information.

SHARPE  GROUP.





## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



## **Gift Planning with Real Estate**

Presented by:

**Philip M. Purcell**

**Vice President for Planned Giving and Endowment Resources**

**Ball State University Foundation**

**P.O. Box 672**

**Muncie, IN 47308-0675**

**765-730-4321**

**ppurcell@bsu.edu**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## *Gift Planning with Real Estate*

Philip M. Purcell, J.D.  
Vice-President for Planned Giving  
and Endowment Stewardship  
Ball State University Foundation  
ppurcell@bsu.edu  
Copyright 2010@ All rights reserved.

## *Why Gone With The Wind?*

Transforming Tara  
from Prospective  
Realty to Gift Reality

## *Why Gone with the Wind?*

- Prospective Realty
- Tara! Tara! Tara!
- Charitable Reconstruction
- Preventing Civil War
- Cultivating Fertile Tara
- Tara-ific Techniques



## **Intergenerational Wealth Transfer**



## **Intergenerational Wealth Transfer**

- Avery/Rendall (Cornell): \$10 trillion by 2040.
- Havens/Schervish (Boston College): \$40 to \$100+ trillion transfer by 2050.
- *Why The \$41 Trillion Wealth Transfer Estimate is Still Valid, The Journal of Gift Planning (2003).*
- *Wealth Transfer Has Yet to Materialize, The Chronicle of Philanthropy (April 6, 2006).*
- *Digest of Opinions, The Journal of Gift Planning (2006).*
- <http://www.bc.edu/research/cwp/>

## **Less than Anticipated Wealth Transfer?**

- Recent economic decline: reduced household income and reduced values of assets (stock, real estate, etc.).
- Focus on current (not deferred) giving.
- Mortality rates have declined since 1998.
- Giving USA data may underestimate bequest revenue due to conservative approach.

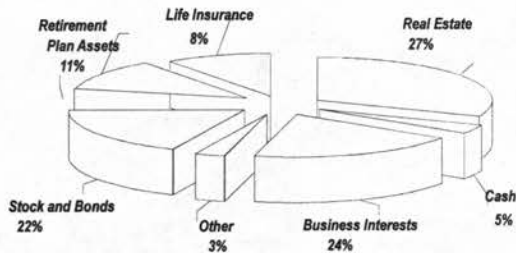
## Personal Wealth: Prospective Realty in the Wealth Transfer



## The Millionaire Next Door

- *The Millionaire Next Door* by Stanley and Danko (1996), Longstreet Press
- 46% of all gifts come from families worth more than \$1 million.
- 25% of all gifts from families worth \$200,000 to \$1 million.
- 1980: 700,000 millionaire families.
- 2001: 5 million millionaire families.
- 2005: 8.3 million millionaire families.
- 2005: 14 million affluent families of \$500,000+.
- 2010: Impact of economic decline?
- Additional Sources: Boston College Social Welfare.

## Portfolio of Assets (Households with \$1 million+)

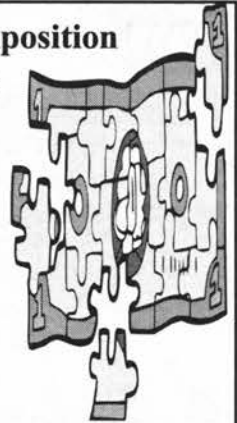


## Portfolio Composition

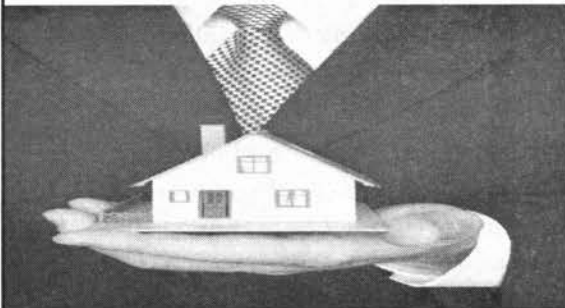
### Households with \$1 million+

- 27% - Real Estate
- 24% - Business Interests
- 22% - Stocks/Bonds
- 11% - Retirement Plan
- 8% - Life Insurance
- 5% - Cash
- 3% - Other

Source: Federal Reserve (2003)  
Compiled by Center for Wealth and  
Philanthropy, Boston College



## Real Estate for Real Opportunity!



## Current Challenges and Concerns for Our Donors

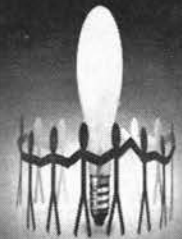
- Reduced values of stock portfolios.
- Reduced values of retirement plans.
- Reduced values of home or other real estate.
- Uncertainty of future.
- Need for dependable income.
- Concern for income for loved ones.
- Underperforming charitable remainder trusts.

## Current Challenges for Our Organizations

- Reduced budgets for salary and program expenses.
- Staff reduction or hiring freeze.
- Combined positions: major/planned gifts.
- Diminished values of endowments.
- Decreased values of charitable remainder trusts, lead trusts and pooled funds.
- Reduced value of gift annuity reserves.
- Fewer gifts of appreciated property.

## Real Opportunity!

- Needs continue – and increase!
- Deferred gifts are popular.
- Cash gifts and pledges are diminished – so promote asset gifts – including real estate.
- Use integrated gift plans: annual, major, planned.
- Secure planned gift commitments now – can increase outright gifts later as market improves.



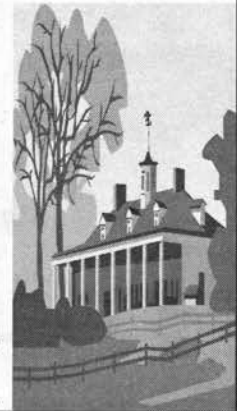
## Frankly, Scarlett....



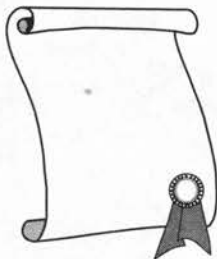
*Does your organization consider the potential of real estate gifts???*

## Tara!

- Real estate is land and generally what is erected on, growing on, or affixed to land. Personal property not affixed to land is separate. Reg. §170A-1(d)(2)(i)(b).
- Examples: personal residence, agricultural land, commercial or investment property, natural resources.



## Understanding Real Estate Interests



Donors may be unaware of their actual legal interest. A review of the documents will be necessary by the donor's and charity's legal counsel.

## Types of Real Estate Interests

### Whole Interests:

- Fee Simple Absolute
- Fee Simple Conditional
- Fee Simple Defeasible
- Fee Simple Determinable

### Partial Interests:

- Undivided Interest
- Partial Interest
- Life Estate
- Joint Tenancy
- Tenancy by Entirety
- Tenancy in Common
- Community Property





## Claim of Deduction

- IRS Form 8283: Non-Cash Gifts
- If deduction claimed exceeds \$5,000, appraiser signs form acknowledging value and charity signs acknowledging receipt.
- Donor is not required to file copy of the gift receipt or qualified appraisal with tax return unless the deduction claimed exceeds \$500,000.

**8283** Non-Cash Charitable Contributions

Form 8283 (2018)

Section 170(e)(2)(B) - If the total amount of non-cash contributions for the year exceeds \$500,000, the donor must file Form 8283 with the tax return.

Part I - Information on Donor

Part II - Information on Recipient

Part III - Description of Property

Part IV - Appraisal Information

Part V - Appraiser Information

Part VI - Donor's Acknowledgment

Part VII - Recipient's Acknowledgment

Part VIII - Signature of Donor

Part IX - Signature of Recipient

Part X - Signature of Appraiser

Part XI - Signature of Charity

**8282** Donor Acknowledgment for Charitable Contribution

Form 8282 (2018)

Section 170(e)(2)(B) - If the total amount of non-cash contributions for the year exceeds \$500,000, the donor must file Form 8283 with the tax return.

Part I - Information on Donor

Part II - Information on Recipient

Part III - Description of Property

Part IV - Appraisal Information

Part V - Appraiser Information

Part VI - Donor's Acknowledgment

Part VII - Recipient's Acknowledgment

Part VIII - Signature of Donor

Part IX - Signature of Recipient

Part X - Signature of Appraiser

Part XI - Signature of Charity

## Sale of Donated Property

- IRS Form 8282: Reporting proceeds of sale of donated property by charitable organization.
- Filed if property is sold within three years of date of gift.
- IRS audit "red flag" if value of claimed for charitable deduction significantly exceeds the charitable organization's sale value.

**8282** Donor Information Return

Form 8282 (2018)

Section 170(e)(2)(B) - If the total amount of non-cash contributions for the year exceeds \$500,000, the donor must file Form 8283 with the tax return.

Part I - Information on Donor

Part II - Information on Recipient

Part III - Description of Property

Part IV - Appraisal Information

Part V - Appraiser Information

Part VI - Donor's Acknowledgment

Part VII - Recipient's Acknowledgment

Part VIII - Signature of Donor

Part IX - Signature of Recipient

Part X - Signature of Appraiser

Part XI - Signature of Charity

**8282** Donor Information Return

Form 8282 (2018)

Section 170(e)(2)(B) - If the total amount of non-cash contributions for the year exceeds \$500,000, the donor must file Form 8283 with the tax return.

Part I - Information on Donor

Part II - Information on Recipient

Part III - Description of Property

Part IV - Appraisal Information

Part V - Appraiser Information

Part VI - Donor's Acknowledgment

Part VII - Recipient's Acknowledgment

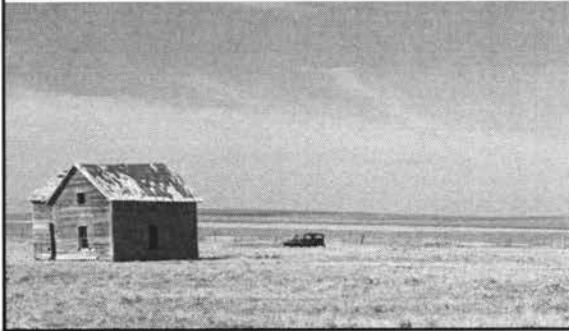
Part VIII - Signature of Donor

Part IX - Signature of Recipient

Part X - Signature of Appraiser

Part XI - Signature of Charity

## Outright Gifts of Real Estate



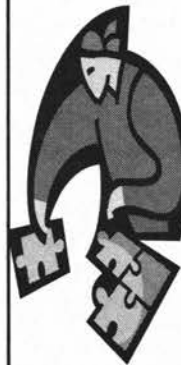
## Outright Gifts of Real Estate

- All outright gifts of real estate are “planned”.
- Income tax charitable deduction for full fair market value. Deduction limit: 30% of AGI if held more than one year (long-term).
- Alternative: Income tax charitable deduction for cost basis subject to 50% of AGI.
- Five years to carry-over excess deduction.
- Escape of potential capital gains tax.
- Removed from taxable estate.

## Completion of Gift

- Gift must be irrevocably completed.
- No tax deduction for a loan of property.
- **Date of Gift:** Signature on deed per state law. Rev. Rul. 69-93, 1969-1 CB 139.
- *Full Covenant and Warranty Deed* is preferred.
- *Grant Deed*. No warrant of full title.
- *Quit Claim Deed*. Only gives current rights – no warrant of full title.
- *Executors Deed*. For estate gift – no warrant.
- Title Review and Insurance to protect interests.

## Outright Gift of Undivided Interest



- A gift of a percentage of every right owned by donor.
- For entire term donor owns.
- May decrease FMV.
- Qualifies for income, gift/estate tax deductions and escape of capital gains tax. IRC § 170(f)(3)(B)(ii) and §2522(c)(2).
- Helpful where a gift of 100% would exceed deduction limit.

## Outright Gift of Ordinary Income Property

- Examples: inventory property (e.g., land developer), property held short-term (less than one year), commercial real property that has been depreciated under an accelerated method. See Reg. §170A-4(b)(1).
- Charitable deduction reduced by potential ordinary income earned if property is sold, i.e., limited to lesser of cost basis and cost of goods sold, subject to 50% AGI deduction.
- Consider gift of other assets or if inventory, converting to personal holdings prior to gift.

## Outright Gift of Natural Resources

- Oil, Gas, Timber, Water and Mineral Interests.
- State/federal laws: real or personal property (tangible or intangible).
- Consult attorney specialist.
- Beware violation of Partial Interest Rule (no charitable deduction) if donor give land but retains mineral interests. Rev. Rul. 76-331.



### Capital Gains Tax and Home Gifts

- \$250,000 (single)/\$500,000 (married filing jointly) capital gain exclusion on sale of primary residence.
- Owned for at least 2 of the 5 years before sale.
- Occupied as primary residence
- Cannot use more than every 2 years.
- Note: Not applicable to vacation home or other real estate.

### Special Consideration: Pre-Arranged Sales

- If charity is legally obligated to sell property to a third party by a contract between donor and the third party entered before the gift.
- Donor will receive an income tax charitable deduction but will owe capital gains tax.
- Distinguish from buyers “waiting in the wings”, unaccepted offers, etc.
- *Palmer v. Commissioner* and other legal rulings. See *How Far is Too Far?*, Planned Giving Design Center, Kallina and Temple, [www.pgdc.com](http://www.pgdc.com)

### Impact on Charitable Income Tax Deduction

- Retained right of first refusal: No deduction.
- Retained repurchase option: No deduction.
- Effect of debt on donated property: Deemed a bargain sale if charity assumes liability for any debt. No deduction for value of debt assumed by charity.
- Like-Kind Exchanges: May result in capital gains tax liability – and donor may consider a gift of cash or real estate to offset this liability with an income tax charitable deduction.

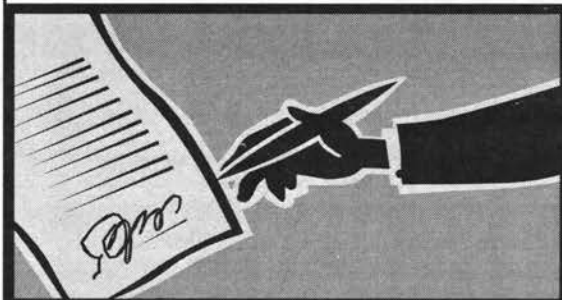
### Unrelated Business Income Tax (UBIT)

- Income from a trade or business (i.e., selling of goods or performing of services).
- Regularly carried on (i.e., with frequency and continuity).
- Not substantially related to charity’s exempt purpose or mission.
- IRS Form 990-T to report and pay the tax.
- IRS Publication 598 explains rules with specific examples.

### UBIT Examples

- UBI does not include investment income.
- UBI does not include rental income on real estate. Reg. §512(b)-1. However, UBI may exist on rental income if :
  1. Significant personal services are provided beyond normal (day care, housekeeping),
  2. More than incidental amount of personal property included,
  3. Commercial rents based on tenant’s income or profits, or
  4. Property subject to mortgage (in proportion to amount of debt) – IRC Sec 514.

### Charitable Bequests of Real Estate



## Charitable Bequests

- Most popular form of planned gift.
- Revocable.
- Simple.
- Included in will, codicil (will amendment) or revocable trust.
- Outright gifts or for life income plans
- Unrestricted, restricted, endowment.

## Due Diligence

1. Follow policies and procedures.
2. Consider sale by estate with acceptance of cash rather than in-kind acceptance.
3. Can disclaim.
4. Follow applicable state probate law.
5. Hire local counsel to assure appropriate title review and transfer.

## Types of Bequests

- Percentage of estate.
- Specific dollar amount.
- Specific property.
- Residual of estate.
- Contingent on other factors such as upon passing of loved ones.
- Transfer on Death Deed (TOD) - subject to state law.

## Split Interest Gifts

## Partial Interest Rule

- No charitable income tax deduction for a gift of less than the donor's entire interest.
- Note: A gift of an undivided interest in all that the donor owns – or a gift of a donor's entire interest that is a fractional or partial interest (e.g., time share), then a deduction is available so long as the valuation reflects the partial interest (e.g., lack of transferability and marketability, minority interest, etc.).
- Exceptions to partial interest rule allow tax benefits in narrowly defined techniques.

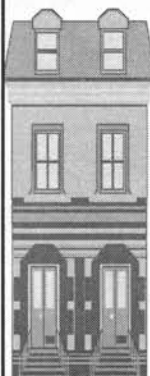
## Qualified Partial Interest Gifts

- Qualified Charitable Remainder Trust.
- Income Interest of a Charitable Remainder Trust.
- Qualified Charitable Lead Trust.
- Remainder Interest in Personal Residence/Farm.
- Qualified Pooled Income Fund.
- Undivided Portion of Entire Interest in Property.
- Qualified Conservation Easement.

## Gift of Remainder Interest with Retained Life Estate



## Remainder in Personal Residence or Farm



- Donor retains life estate and donates the remainder interest.
- Available for principal residence, vacation home, condo, co-op.
- Includes fixtures -not equipment, furnishings or crops.
- Remainder value is discounted to reflect depreciation and salvage value is factored.

## Planning Benefits

- Income tax charitable deduction for charitable remainder value. Reg. §1.170A-12.
- As Adjusted Federal Rate (AFR) decreases, the income tax charitable deduction value increases.
- Immediate gift to charity avoids estate tax and probate costs and delay.

## Remainder Interest Agreement

- Liability for property taxes. Verification to charity.
- Payment of property insurance. Verification to charity.
- Obligation for maintenance costs. Right of charity to inspect.
- Right of charity to review future leases, major changes to property that may diminish value and other considerations.
- Contingency plans if donor decides to move.

## If Donor Decides To Move

- Donate life estate and receive an additional income tax charitable deduction.
- Exchange life estate for a gift annuity.
- Lease life estate to third party with consent of charity per agreement.
- Sell life estate to third party per agreement.
- Joint sale of life estate and remainder interest with donor and charity splitting the proceeds.
- Note: These options must not be pre-planned. Be careful with pre-gift documentation.

## Income For Remainder Interest

- Gift annuity offered in exchange for irrevocable remainder interest gift.
- Income tax deduction reduced by income interest.
- Incentive for irrevocable gift of valuable property such as opportunity for future appreciation or strategic location for charity's mission and programs.
- Annuity may be funded by operating budget, endowment, reverse mortgage loan with bank.

## Gifts of Real Estate to Charitable Remainder Trusts



## Basics of CRTs

- Operated pursuant to a trust document that complies with state and federal law. IRC §664.
- Donor and/or others designated by donor receive income for life or a term of years not to exceed 20 years.
- Fixed income payout percentage between 5% and 50%.
- Established during life or at death.
- Remainder to charity is irrevocable. But donor may retain right to change the recipient charity(ies).

## Tax Benefits of a CRT

- Income tax charitable deduction for present value of charity's future interest.
- Income tax deduction value must be at least 10% of original value of donated cash or assets.
- Donated cash or assets removed from taxable estate.
- Assets donated to CRT are sold without capital gains tax liability since CRT is a tax-exempt trust.

## Types of CRTs

- Standard Unitrust (SCRUT).
- Net Income Unitrust (NICRUT).
- Net Income with Make-Up Unitrust (NIMCRUT).
- Flip CRT (begins as NICRUT or NIMCRUT and flips to a CRUT).
- Annuity Trust (CRAT).
- See model CRT template documents provided by IRS ([www.irs.gov](http://www.irs.gov)) to offer a "safe harbor" so long as substantially followed. Counsel can add state trust code powers of trustee, etc.

## Annuity Trust (CRAT)

- Pays fixed dollar amount determined by multiplication of fixed percentage (5% or more) by the value of assets donated to trust.
- No additional gifts allowed.
- Donated real estate must be sold – or use undivided interests - to fund annuity payment.
- 10% minimum deduction test as with all CRTs.
- Unique 5% probability test. The probability of trust depletion must not exceed 5%.

## Standard Unitrust (SCRUT)

- Pays fixed percentage (5% or more) of trust value as annually re-valued. Most popular form.
- Payments may be made from income and/or principal at discretion of trustee.
- Additional gifts allowed.
- Donated real estate may be sold to allow for payments or in-kind payments of undivided portions.
- Income/principal defined in trust document per state law, e.g., income may include realized gain.

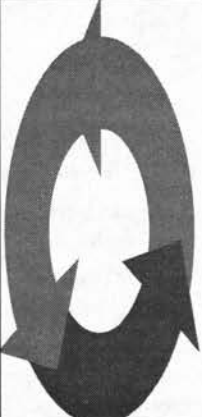
### Net Income CRUT (NICRUT)

- Pays fixed percentage (5% or more) of trust value as annually re-valued.
- Payment for percentage amount or net income, whichever is less.
- No payment from principal.
- Additional gifts allowed.
- Income and principal defined in trust document per state law.
- Income may include realized gain.

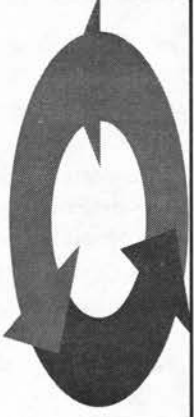
### Net Income with Make-Up (NIMCRUT)

- Pays fixed percentage (5% or more) of trust value as annually re-valued.
- Payment for percentage amount or net income, whichever is less.
- In pay periods when net income exceeds the percentage amount, extra payment allowed to make-up for pay periods when net income was less than percentage amount.
- No payment from principal. Additional gifts allowed.
- Income and principal defined in trust document per state law. Income may include realized gain.

### FLIP CRT

- 
- Flip from NICRUT to Regular CRUT. Treas. Reg. §1.664-3(a)(1)(i)(c).
  - Excellent vehicle to deal with real estate that may be slow to sell.
  - Get income tax deduction when property is donated to trust.
  - Pay income when asset is sold and proceeds reinvested and trust “flips”.

### FLIP CRT

- 
- Flip stated in trust document.
  - Triggered on a specific date or by an occurrence which is not discretionary or within the control of any person. The regulations provide specific examples. Treas. Reg. §1.664-3(a)(1)(i)(c).
  - After conversion, no make-up provision (loss of any make-up).

### Income Payments

- Beneficiaries pay income tax.
- Reported on K-1.
- Income taxation on a worst-in, first out (WIFO) basis in tiered system.
- Before any tax-free income is paid, all pre-gift capital appreciation is accounted for and taxed as income as paid to the beneficiaries.
- For excellent resource, see *Charitable Remainder Trusts*, Planned Giving Design Center, [www.pgdc.com](http://www.pgdc.com)

### Planning Opportunities

- Sale of appreciated assets – no capital gains tax.
- Transforms non-income producing property into income for retirement or for loved ones.
- As trust principal value grows, so does income with unitrusts.
- Removes worry of property management for older donors.
- Charities should be cautious about serving as trustee. Requires board approval.
- Donor may be trustee.
- Common minimum of at least \$100,000.

### Importance of Due Diligence

- **Concern:** Will real estate be sold, or generate income, for income payment obligation?
- *Martin v. Ohio State University*, 2000 Ohio App. Lexis 4824: Donor to flip CRT alleged not told that no income paid until real estate was sold.
- Document discussions.
- Assure independent counsel.
- Note: Recent economic downturn highlights importance of an annually reviewed investment policy statement for a CRT to assure prudent investment management.

### Self-Dealing Considerations

- CRTs are subject to private foundation rules and excise taxes for self-dealing.
- CRT property cannot be used, sold, rented or exchanged to a disqualified person: donor or donor's family (spouse, ancestor or lineal descendant or spouse of lineal descendant). IRC §4941(d)(1).
- Donate property to CRT prior to sale – i.e., no pre-arranged sale. Otherwise, capital gains tax is owed.

### Depreciable Property

- CRTs can invest in depreciable property. Reg. §167(h)-1(b).
- Depreciation deductions apportioned between income recipient and trustee on basis of income allocable to each.
- Governing trust instrument (or local law) may require a reserve for depreciation and a reserve is required for net income CRTs. See PLRs 8931019 and 8931020.

### Debt Encumbered Property

- | <u>Potential Problems:</u>              | <u>Solutions:</u>                                     |
|---|---|
| • Acquisition indebtedness.             | • Retire debt before gift.                            |
| • Unrelated Business Income Tax (UBIT). | • Sell portion of property to pay debt prior to gift. |
| • Act of self-dealing.                  | • Convert debt to personal debt prior to gift.        |
| • Bargain sale.                         | • Transfer debt to other property prior to gift.      |
| • Grantor trust rules.                  | • Use gift annuity instead.                           |
| • Prohibited payment.                   | • Debt reduces gift portion of transaction.           |
| • See PLRs 9533014 and 9015049.         |   |

### UBI and Debt Property

- CRT income from debt-financed property is UBI.
- Debt-financed property includes property that had *acquisition indebtedness* at anytime during the tax year or within 12-months of disposition of the property.
- "Acquisition indebtedness" is the principal indebtedness incurred prior, during, or after acquiring or improving the property.

### Five and Five Rule

- If mortgaged property is donated to CRT, the debt will not be treated as acquisition indebtedness during the ten years following the date of acquisition if:
  1. the mortgage was placed on the property more than five years prior to the gift, and
  2. the property was held by the trustor for more than five years prior to the gift.
- Inapplicable if the trust assumes any part of the debt secured by the mortgage. See Reg. §1.512(b)-1(c)(2)(ii)(b).



## Pooled Income Fund



## Basics of PIFs

- Operated by charity as trustee.
- All gifts “pooled” for investment purposes.
- May accept smaller gifts (e.g., \$5,000).
- All income from the PIF is paid ratably to all participants each year.
- Similar in approach to a mutual fund.
- See IRC §642(c).

## Current Environment

- PIFs not as popular now since they are inconvenient for long-term personalized investments as permitted with CRTs.
- Also, income paid from PIFs is not as attractive when compared to rates offered for gift annuities due to the current investment environment for bonds and other income-producing assets.

## PIFs and Real Estate Gifts

- **Concern:** Will property produce any or sufficient income such that fund’s unit value - or income flow to other beneficiaries - is not distorted?
- A new PIF could be established just for the purpose of attracting gifts to be used to build a building (e.g., college dorm with rental revenue) which may produce steady income.
- A depreciation reserve is required if real estate is donated to a PIF.

## Charitable Gift Annuity



## Charitable Gift Annuity

- Contract between donor and charity.
- Donor gives assets, charity provides fixed and guaranteed income for one or two lives.
- Rates of return: American Council on Gift Annuities
- Rate assumptions: life expectancy, market growth, costs.
- Current income tax charitable deduction.
- [www.acga-web.org](http://www.acga-web.org) for a wealth of information, including updates on state laws.

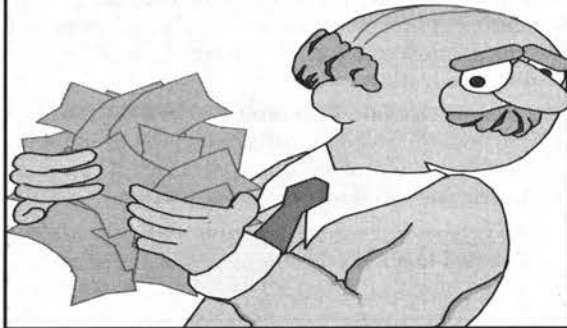
### Real Estate for Gift Annuity

- Income tax deduction subject to 30% limit (if long-term property).
- Capital gain is ratably spread over life expectancy if the donor is the annuitant. IRC §1011(b).
- If donor is not annuitant, a portion of the capital gains tax is owed immediately.

### Real Estate for Gift Annuity

- Key question: Must the donated real estate be sold to fund the annuity obligation?
- Other source of payments: endowment, operating budget.
- Possible to negotiate a lower rate to account for carrying costs, transfer expenses, etc.
- Annual or deferred payments may allow time to sell the donated property.
- Assure compliance with state registration laws, Prudent Investor Act standards and other applicable due diligence.

### Bargain Sale



### Bargain Sale

- Purchase of real estate by charitable organization for a bargain or discounted price. See IRC §1011.
- Useful to acquire property deemed important to charity's mission (e.g., contiguous land, building site) at a discounted price.
- Useful to purchase property with prospect of significant appreciation in value.

### Due Diligence and Tax Benefits

- Must document gift intention.
- Qualified appraisal necessary.
- Charitable tax deduction for gift portion of transaction. See IRC §1011.
- Cost Basis allocated proportionally between sale and gift portions of transaction.
- Escape capital gains tax on gift portion of the transaction.

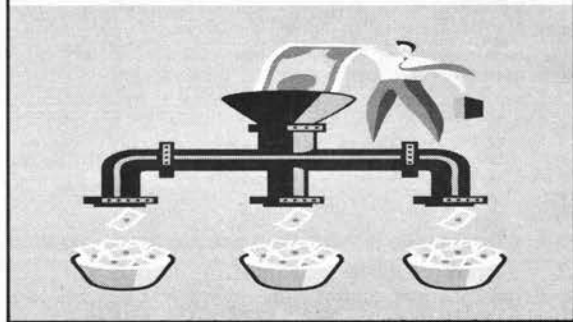
### Installment Bargain Sale

- Sale price paid in installments. Rev. Rul. 79-326.
- Interest and principal paid. Amortization schedule (like mortgage).
- A portion of principal includes tax-free return.
- Interest Rate: Consider mortgage rates with AFR as minimum.
- Capital gains tax spread over payment period.
- Possible UBIT if property is later sold by charity. Income from debt-financed property subject to acquisition indebtedness.

## A Flexible Gift Plan

- Term of years of installment bargain sale can be greater than 20 years unlike CRTs.
- Payments may be personalized, e.g.: deferred, single, fixed, variable, large up-front or balloon payment at end are all possible.
- Payments may be made to “disqualified” persons unlike CRTs.
- Payments may be made to more than two persons per contract unlike gift annuity contracts.

## Charitable Lead Trust



## What is a Lead Trust?

- Payments to charity: unitrust or annuity format.
- No required payout percentage unlike CRT.
- Any term of years unlike CRT.
- Remainder to donor (reversionary) or loved ones chosen by donor (nonreversionary).
- *Inter Vivos* (no step-up in basis for heirs) or Testamentary (step-up in basis).
- Qualified CLT allows for tax benefits.
- Nonqualified CLT offers no tax benefits.

## Grantor or Nongrantor CLTs

- Grantor CLT allows for income tax deduction – income of CLT taxed to grantor.
- Grantor CLT helpful to enhance deduction or to emphasize tax free investments.
- Nongrantor CLT allows for gift/estate tax deduction.
- Nongrantor CLT is income taxed as a complex trust. IRC §651(a); Reg. §651(a)-4.
- For nongrantor CLTs charitable deductions are available for payments to charity. IRC §642(c).

## Real Estate Gifts to Nongrantor CLT

- Property may produce income to satisfy payments to charity.
- Or property may be sold and reinvested to generate income.
- Future gifts to CLT are allowed for payments.
- Sale of real estate produces taxable gain to CLT.
- Income tax deduction to CLT for annual gifts.

## Passing Wealth at Reduced Tax Cost

- Nongrantor/nonreversionary CLT: gift tax paid now on remainder interest.
- As AFR decreases, gift/estate tax savings increases.
- Ideally, CLT principal appreciates in value, saving potential future gift/estate tax if nonreversionary.
- Passing specific real estate (farm, vacation land, etc.) or other assets to heirs at reduced gift and estate tax cost.

## Due Diligence and CLTs

- Private Foundation Rules - IRC §§4947(a)(2) and 508(e) :
  1. No self-dealing.
  2. No taxable expenditures.
  3. No excess business holdings.
  4. No jeopardizing investments.
- Acceptance of debt encumbered property: unrelated business income for recurring income and disposition.

## Conservation Easements



## What is a Conservation Easement?

- A permanent restriction on the use of the property pursuant to a qualified conservation purpose.
- Restriction defined in an easement agreement between the donor and a qualified charity.
- The charity owns a right to enforce and protect the qualified conservation purpose.
- The easement restriction passes to future owners of the property by sale, gift or other transfer.

## Application of State Law

- The law of the state in which the easement is donated dictates the form of the easement.
- Most states have legislation enabling conservation easements.
- Many states have adopted a version of the Uniform Conservation Easement Act.
- See Uniform Law Commissioners for a list of states adopting UCEA at [www.nccusl.org](http://www.nccusl.org)

## Requirements for Federal Tax Benefits

- Conservation easement must meet definition of “qualified conservation contribution” for federal income tax and estate tax benefits. IRC Sec. 170(h).
- A qualified real property interest ... donated to a qualified organization ...exclusively for conservation purposes.

## “Qualified Real Property Interest”

- A restriction granted in perpetuity on the use of the real property. IRC Sec. 170(h)(2)(c).
- An easement or similar interest in real property created under applicable state law: entire, remainder or restriction. Reg. 170A-14(b)(2)
- A gift in perpetuity does not mean violation of Rule Against Perpetuities. Conservation easements must “vest” in the easement holder upon recording of the easement. Reg. 1.170A-14(g)(6)(ii).

### “Qualified Organization”

- Must have a commitment to protect the conservation purposes of the donation and have the resources to enforce the restrictions. Reg. Sec. 1.170A-14(c).
- Local, state, federal governmental agencies.
- Charitable organizations qualified under 501(c)(3), including supporting organizations.
- Document must limit transfer to organizations that agree to conservation use.

### “Qualified Charitable Purpose”

- Preservation of land areas for outdoor recreation or education of general public;
- Protection of a relatively natural habitat for fish, wildlife or plants;
- Preservation of certain open space including farm land and forest land;
- Preservation of an historically important land area or certified historic structure.
- Reg. Sec. 1.170A-14(d)(1).

### Income Tax Benefits

- Income tax charitable deduction for value of easement: the difference between the value of the easement property before the donation and after the donation. Reg. 1.170A-14(h)(3)(ii).
- Exception to partial interest rule. Sec 170(f)(3).
- Annual deduction limit: If land is held > 1 year, then deemed long-term capital gain property and donor may elect deduction for full value limited to 30% of AGI or a cost basis deduction limited to 50% of AGI. Reg. 1.170A-8(d)(1) – (2).

### Income Tax Benefits

- If land is held < 1 year, then short-term gain property and deduction is limited to 50% of AGI or cost basis, whichever is less. Reg. 1.170A-8(b).
- Basis in property is reduced in proportion to the value of the easement relative to the total FMV. Reg. 1.170A-14(h)(3).
- Excess deduction may carry-over for five additional years. Reg. 1.170A-10(c)(1)(ii).
- *Gift Strategy*: Phase easement gifts in increments over time to spread total deduction.

### Enhanced Benefits

- If gift was on or before 12/31/09:
- 50% deduction limit with a 15 year carry-over.
- 100% deduction limit with a 15 year carry-over if easement gift is made by a farmer or rancher (i.e., 50% of income from the farm or ranch).
- For status on the possible extension or permanent ratification of these income tax benefits see Land Trust Alliance at [www.lta.org](http://www.lta.org).

### Reduction in Value of Estate

- Qualified easements reduce the value of the real property subject to the easements when this property is included in owner's estate for estate tax purposes.
- Other types of restrictions on real property are not taken into account when valuing the property for estate tax purposes. See Reg. 25.2703-1.

### Estate/Gift Tax Charitable Deduction and 40% Exclusion

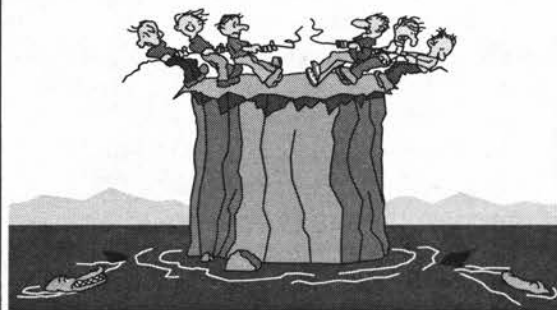
- Qualified easements are deductible for gift and tax purposes. IRC Sec. 2522(d); IRC Sec. 2055(f).
- IRC Sec. 2031(c): 40% of the *restricted* value of property subject to an easement is excluded from estate, i.e., the exclusion applies to the value of the land taking into account the restrictions of the easement.
- Easement must reduce land value by 30% for full exclusion. IRC 2031(c)(2).

### Preventing Civil War

#### Establishing Effective Policies and Procedures



### Create the Real Estate Gifts Team



### Policies and Procedures Manual

#### Initial Considerations:

- Accept real estate?
- What gift techniques?
- From what areas?

#### Process (is important!):

- Prepare draft(s) - input from all interested constituencies.
- Final draft for approval by Board of Directors.

### Policies and Procedures Manual

#### Advantages:

- Informed approval.
- Builds consensus.
- Educates constituents.
- Risk management – Use a Checklist
- The graceful “no”.
- Efficient disposition.
- Allows for exceptions and amendments.
- Stimulus for gifts!



6/23/07

DRAFT

BALL STATE UNIVERSITY  
FOUNDATION

Planned Giving and Endowment Stewardship Program  
Policies and Procedures

Approved by Ball State University Foundation  
Board of Directors



**BALL STATE UNIVERSITY FOUNDATION  
ESTATE ADMINISTRATION CHECKLIST**  
 Expected  
 Unexpected

Name of Estate: \_\_\_\_\_  
 Attorney Handling Estate: \_\_\_\_\_


Date: \_\_\_\_\_

Notify Advancement Services about Date of Death.  
 Notice of Administration received by Foundation.  
 Notify department or college, if appropriate.  
 Attorney contacted. Requested copy of will and inventory if completed which should be sent to the attention of the President of the Foundation.  
 Request biographical information and a picture (optional, if biographical information is not available).  
 Will received by Foundation.  
 Inventory received by Foundation. Copy to Vice President for Operations.  
 Taxable amount of distribution expected: \$ \_\_\_\_\_  
 Partial distribution possible? YES NO  
 If YES, date notice of distribution received.  
 Circulate to President, VP of Operations, VP for Planned Giving, and AVP for Planned Giving.  
 Notify BSU departments\* or other college of partial distribution received.  
 \*Notify Chairman or Dean of Department.  
 Notice of a hearing date received by the Foundation.  
 Preliminary accounting document received by the Foundation.  
 Approval of final accounting document received by the Foundation.  
 Final distribution received by the Foundation. Forward to the President of the Foundation who then gives it to the financial clerk for processing.  
 Type of distribution (cash, property, etc.): \_\_\_\_\_  
 Circulate final distribution to President, VP of Operations, VP for Planned Giving, and AVP for Planned Giving.  
 Notify BSU departments\* or other college of final distribution.  
 \*Notify Chairman or Dean of Department.

BSU Estate Checklist  
 Page 2

\_\_\_\_\_ Thank you letter sent to relative of donor or other appropriate person.  
 \_\_\_\_\_ Estate closed. Notify VP of Operations.  
 \_\_\_\_\_ Reviewed by AVP for Planned Giving to record on expectancy spreadsheet.  
 \_\_\_\_\_ Publicity (send note to Public Information Service).  
 \_\_\_\_\_ File copy of Public Information sheet in next benefice newsletter file for possible article.  
 Allocation of Fund Name: \_\_\_\_\_  
anyone@ballstate.edu

### Environmental Review



- **CERCLA: “joint and several” and “strict” liability.** State laws also apply.
- **Defenses: Act of God or war. “Gap” or Innocent (e.g., bequest) owner.**
- **ASTM: Initial Screen/Phase I, II by qualified professional.**
- **Homes: Inspection for asbestos, structure, lead paint.**

### Environmental Considerations

- **State assistance funds to remediate properties.**
- **Federal and state lists of properties subject to environment review by EPA and other agencies.**
- **Donors may be asked to sign disclosure and indemnification statements.**
- **Federal and state agencies may authorize releases.**
- **“Brownfields” developments allow authorized rehabilitation of property.**

### Organizational Considerations

- **Separate corporation, supporting organization, or LLC to hold property.**
- **PLR 200134025: If Charity sets up LLC for receipt of real estate gifts –**
  1. **Recognize limited liability under state law; no recognition under federal law.**
  2. **No 1023 application filed; No separate 990 annual report.**
  3. **No ruling on income tax deduction by donor.**

### Other Important Policies

- **Valuation and Inspection by Staff.**
- **Legal Counsel and Board approval.**
- **Receipts.**
- **Property with Debt.**
- **Marketability.**
- **Public Relations Issues (e.g., Charitable Family Limited Partnerships holding questionable property).**
- **Internal Reporting.**



## Other Important Policies

- Title Transfer, Review and Insurance.
- Survey.
- Governmental Regulation: Zoning, Tax Sales.
- Charitable Remainder Trusts. Trustee?
- Authorization for Gift Annuities.
- Authorization for Bargain Sale.
- Remainder Interest Agreement.
- Who negotiates?

## Who Pays?

- Each party may pay for that which protects its respective interest.
- Donor pays for: Appraisal to defend value claimed for deduction.
- Charity may pay for its own appraisal for audit and insurance purposes if it questions donor's appraisal.
- Charity pays for: Environmental Review, Title, Marketing Analysis.

## Cultivating Fertile Tara: Establishing Strategy for Marketing Real Estate Gifts



## NCPG Survey of Donors

(1993 - dated but instructive)

- Real Estate: 2nd most common non-cash gift (22.2%). Enough?
- Non-cash donors more likely to have income in top bracket. Target
- 59% say gift was own idea. Red Flag
- "Members" are most common affiliation of non-cash donors.
- Non-cash donors twice as likely to live near charity or to be trustees. Market close to home.
- 77.8% of gifts of land held >6 years. Appreciate appreciation; also donor knows defects
- 12.6% of non-cash donors had tried to sell first. Not a last resort!


## NCPG Survey of Donors

- 71% unsure of amount of capital gain. Of the other 29%, most said gain was more than 50%. Promote savings!
- 54% of noncash gifts - unrestricted. Great!!
- 36% said charity sold the gift, with 80% of those for more than deduction amount.
- Only 9% sold for less and none reported tax problems.
- One-third said they made non-cash gifts of >\$5,000 to more than one charity, being influenced by the needs of the specific charity.

## Appreciate Donor Motivations

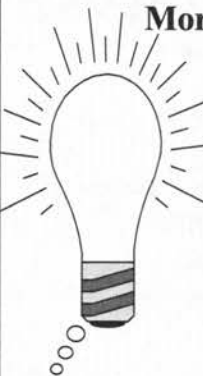
- Promote Mission: 92% support of charity was primary reason for gift.
- Specific Needs: 67% ultimate use motivated non-cash gift.
- Stress Capital Gains: 46% said such savings was important, especially for top bracket donors.
- Memorial Gifts: 36% , if over 70 - 50%
- Estate Planning: 30% cited long-range planning as motivator. 19% cited income needs.

## Marketing Motivators



- Be prepared! Must assure donors w/ confidence.
- Consider emotional ties to property and its value.
- Simplicity
- Consider repeat real estate gifts - or real estate from other planned or non-cash (stock) givers who are now familiar with gift procedures and benefits.

## More Bright Ideas



- Consider real estate gifts in areas of appreciation.
- Other motivators: eliminate burden of sale process, move (retire), extra income, pay off debt, 2nd home not needed, eliminate duties of investment property management, high capital appreciation, inherited property and not needed.

## Tara-ific Techniques!

### Successful Strategies for Marketing Your Real Estate Gifts Program

## Integration of Real Estate

- Educate and Involve Fellow Staff.
- Contact Reports.
- Coordinate Timing of all Mailings.
- Donor Recognition.
- Display of Brochures.
- Use of Volunteers, Class Agents, Planned Gift Agents.
- Integrated Policies and Procedures.
- Information on Pledge Cards, Surveys, Appeal Letters, etc.

**CONFIDENTIAL CONTACT REPORT**

DATE: \_\_\_\_\_ STAFF: \_\_\_\_\_

PROSPECT: \_\_\_\_\_

Home Address: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ Zip Code: \_\_\_\_\_

Telephone: ( ) \_\_\_\_\_

If Employment of Business, Company & Title: \_\_\_\_\_

Business Address: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ Zip Code: \_\_\_\_\_

Business Phone: ( ) \_\_\_\_\_ Fax: ( ) \_\_\_\_\_

ORIGIN OF CONTACT:	( ) Staff	( ) Satisfy	( ) Telephone
	( ) Volunteer	( ) S-Balance	( ) S-Balance
	( ) Write	( ) Meeting/Apple	( ) Other
	( ) Prospect		

PURPOSE OF CONTACT: \_\_\_\_\_

WHO, WHAT, WHEN, WHERE (in addition to above info.): \_\_\_\_\_

ASSESSMENT OF RESULTS OF INTERACTION: \_\_\_\_\_

INTERESTS, CHARACTER, BACKGROUND, CURRENT INFO., INFO. USEFUL FOR FUTURE: \_\_\_\_\_

NEXT STEP: \_\_\_\_\_

**Bell State University Foundation Gift Planning Opportunity Checklist**

Things you might have heard or noticed:

<input type="checkbox"/> Customer involved in estate planning	<input type="checkbox"/> Concerned about getting the best deal on their home?
<input type="checkbox"/> Customer making will, trust, etc.	<input type="checkbox"/> Have asked about "giving with appreciation"?
<input type="checkbox"/> Attorney advised financial planner's	<input type="checkbox"/> Have asked about "giving with appreciation"?
<input type="checkbox"/> "Need to be giving with appreciation"	<input type="checkbox"/> Have asked about "giving with appreciation"?

**Personal Assets/Income**

<input type="checkbox"/> How total or gross to sell a business?	<input type="checkbox"/> Gross highly appreciated securities or other real estate, assets?
<input type="checkbox"/> How high income?	<input type="checkbox"/> Gross highly appreciated stock?
<input type="checkbox"/> When will, mortgage, independence	<input type="checkbox"/> When will, mortgage, independence?
<input type="checkbox"/> Monthly received on inheritance	<input type="checkbox"/> Monthly received on inheritance?
<input type="checkbox"/> How much?	<input type="checkbox"/> How much?

**Tax Considerations**

<input type="checkbox"/> Concerned about capital gains tax	<input type="checkbox"/> Concerned about gift tax?
<input type="checkbox"/> Concerned about estate tax	<input type="checkbox"/> Concerned about estate tax?
<input type="checkbox"/> Concerned about inheritance tax	<input type="checkbox"/> Concerned about inheritance tax?

**Personal Information**

<input type="checkbox"/> Single	<input type="checkbox"/> Married or planning to marry soon
<input type="checkbox"/> Married or widowed	<input type="checkbox"/> Married or planning to marry soon
<input type="checkbox"/> Divorced	<input type="checkbox"/> Divorced
<input type="checkbox"/> Age	<input type="checkbox"/> Age

**Relationship to Bell State University Foundation**

<input type="checkbox"/> Employee of Bell State University	<input type="checkbox"/> Former employee of Bell State University
<input type="checkbox"/> Alumni	<input type="checkbox"/> Alumni
<input type="checkbox"/> Year? Age?	<input type="checkbox"/> Year? Age?
<input type="checkbox"/> How long associated with Bell State?	<input type="checkbox"/> How long associated with Bell State?

**Relationship Information**

<input type="checkbox"/> Married	<input type="checkbox"/> Married
<input type="checkbox"/> Divorced	<input type="checkbox"/> Divorced
<input type="checkbox"/> Single	<input type="checkbox"/> Single

## Personal Visits



- Cultivation
  - *Appreciate Motivations*
- Education
  - *About your charity*
  - *About real estate gifts*
- Solicitation
  - *Consider differences*

## Integrated Donor Proposals

- Blended proposals for annual, major and planned gifts.
- Easy-to-read illustrations personalized for the donor. Ideally incorporating educational information for the donor.
- Always encourage donors to share illustrations with their counsel.
- Usually illustrations are prepared once an excellent rapport is established.

## Recognition and Stewardship

- Personal Thank You
- Public Recognition
  - *Permission*
  - *Named Societies, Annual Report, Special Events, Photographs, Newsletters*
  - *Cumulative Gift Recognition*
- Separate Real Estate Donors Recognition



## Web Marketing



- Web Page with Real Estate Gift Information.
- Include in Gift Planning Options.
- Videos or Photographs and Stories with Testimonials.
- Blast E-Mails.

## Brochures

- Testimonials!
- Ebrochures.
- Easy-to-read (print, color, art, photos).
- Design coordinated with other materials.
- Use tax analysis with discretion.
- Include examples.
- State Bar Association brochures.
- Target mailings.
- Public display.
- Include reply device.
- Provide info on environmental audits, qualified appraisals, carrying costs, etc.
- Annual reports.

## Newsletters

- Testimonials!
- Easy-to-read (print, color, photos)
- More detail for tax info., updates, testimonials, recognition, etc.
- Mail regularly – or Email!
- 3-hole punch
- Use reply cards for follow-up letters, brochures, etc.
- Announcements
- Target mail.



## Bequest Programs

- Keep in mind that the bequest of real estate and other assets may be the largest gift a donor makes!
- Provide sample language.
- Carefully monitor estates in probate.
- Extend appreciation to surviving family.
- Honor donors or survivors with recognition if appropriate.

## Seminars



- Gift/Estate planning.
- Use professional advisors.
- With special events - or “on-the-road” with news from your charity.
- Offer private consultations.
- Provide brochures, etc.
- Testimonials possible.

## Taped Testimonials

- Excellent for testimonials from donors, advisors.
- Incorporate on website.
- Follow-up is crucial.
- Review videos from vendors prior to use.



## Advertisements

- May be used in your general publications.
- Paid media advertising may be considered.
- May use appropriate humor.
- Must have “eye appeal”.
- Quick to the point.
- Use professional artwork and design.

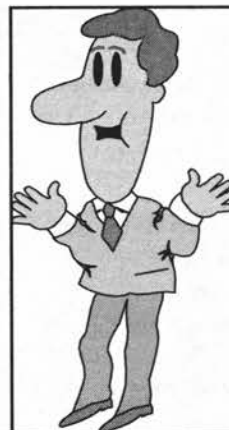
## Professional Advisors

- Communication is key in gift negotiations.
- Provide references to donors.
- Send newsletter or email educational materials.
- Educate about your charity.
- Advisory Committees.
- Continuing Education.
- Invite to PG /estate planning council meetings.

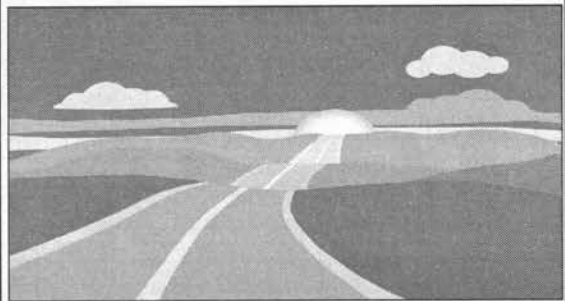


*So, frankly,  
Scarlett...*

*Is your  
organization  
considering the  
potential of gifts  
of real estate?!?*



*After all...  
tomorrow is another day!!*







Planned Giving ID

Marketing Audit

E-Strategy

Lifestage Annual Fund

Data Services

*"In my opinion, RuffaloCODY offers the premier Planned Giving calling program. The results have been outstanding. In the past three years, we've had more than 200 good leads from the programs together with RuffaloCODY."*

James Preston  
Senior Director of Planned and Major Gifts  
The University of Missouri

**Timothy Logan, ACFRE**  
Represents Clients in the Eastern United States  
12357 Brown Fox Way  
Reston, VA 20191-1648  
703.758.0970  
800.756.7483  
timothy.logan@ruffalocody.com

**Jeffrey Mielke, CSPG**  
Represents Clients in the Western United States  
18905 Pinon Park Road  
Peyton, CO 80831  
719.749.2772  
800.756.7483  
jeff.mielke@ruffalocody.com



**ASSOCIATION FOR  
HEALTHCARE  
PHILANTHROPY.**

*Connecting People • Enriching Lives*

RuffaloCODY is proud to be an Affiliate  
Member of the Association for Healthcare  
Philanthropy.



RuffaloCODY is proud to partner with CASE  
and its member institutions



RuffaloCODY staff are proud members of the  
Association of Fundraising Professionals

**w w w . r u f f a l o c o d y . c o m**





## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



# **Charitable Remainder Trust Basics**

Presented by:

**Joseph O. Bull**

**Senior Vice President for Community Engagement**

**Columbus Zoo and Aquarium**

**PO Box 400**

**Powell, OH 43065-0400**

**(614) 645-3545**

**joe.bull@columbuszoo.org**

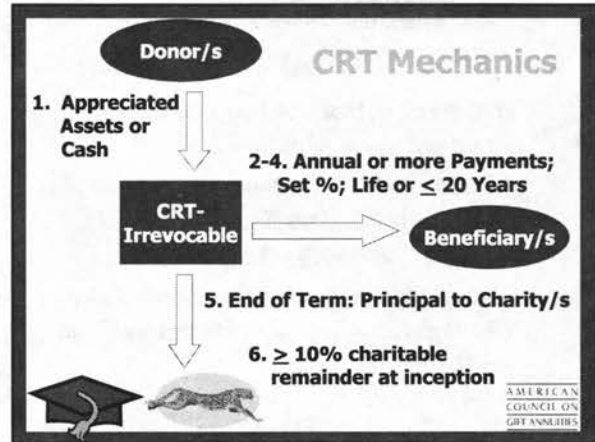
Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## What is a Trust ?

- Separate Legal Entity
  - Tax ID Number
  - Annual Tax Return
- Owns and Administers Property
- Governed by:
  - State Law
  - Trust Instrument
- *Inter Vivos* vs. Testamentary

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES



AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## Charitable Remainder Annuity Trust

- Pays “sum certain” at least annually
- $\geq 5\%$  of trust’s initial value...  $\leq 50\%$
- Fixed Income: \$\$ amount or %
- **NO** Additional Contributions
- a.k.a.: CRAT

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## Charitable Remainder Unitrust

- At least annual payments  $\geq 5\%$  ( $\leq 50\%$ ) of trust assets... *valued each year*
- Income can  $\uparrow$  or  $\downarrow$
- When are CRUT assets *valued*?
- Additional contributions can be made... *...IF...*
- a.k.a.: CRUT

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## Does Baskin-Robbins Sell CRUT’s ?

- Standard Unitrust
- Net Income Unitrust
- Net Income Unitrust with make-up
- Flip Unitrust

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## “Flipping” Over a CRUT

- Harsh realities of the NIMCRUT in low interest rate environment
- One Flip and One Flip Only !
- SCRUT status begins taxable year following triggering event
- Triggering Event
- Real Estate & Hard-to-value assets

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## CRT: Income Tax Issues

- Tax-exemption of the CRT
  - CRT no income or capital gains tax
  - Excess income accumulated without tax
- No Capital Gains Tax to Donor
  - Encourages transfer of appreciated assets
- Charitable Income Tax Deduction
  - Estimate of what Charity will receive
  - $\geq 10\%$  of trust's initial value
  - 5% Probability Test for CRAT's

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## Riding the Coaster with § 7520

- Prior to May, 1989 = 10.0% (fixed)
- May, 1989 = 11.6%
- May, 1994 = 7.8%
- May, 1999 = 6.2%
- May, 2004 = 3.8%
- May, 2009 = 2.4%
- All time low: February, 2009 = 2.0%
- Current: April, 2010 = 3.2%

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## CRAT vs. CRUT Deductions

Age	CRT %	CRT Type	Pmt. Freq.	AFMR \$7520	Charitable Deduction
72	5%	CRAT	Qtrly	3.2%	\$49,753
	5%	CRUT			\$55,620
	8%	CRAT			\$19,604*
	8%	CRUT			\$40,966

\* Fails 5% Probability Test...5.8% AFMR to pass

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## CRT: Gift & Estate Tax Issues

- *Inter Vivos* CRT's: gift & estate tax
- Testamentary CRT's: estate tax
- Unlimited spousal deduction
- Non-spousal income beneficiaries

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## Philanthropy Protection Act of 1995

- Background
- GP is about more than tax law
- PPA exempts charitable common funds from federal securities law
- Requires "disclosure" to donors

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## Trustee Selection

- Who *can* be the trustee?
  - Bank or Trust Company
  - Donor as Self-Trustee
  - The Charitable Organization
- Who *should* be the trustee?
  - Type of property funding the trust
  - Existing relationships
  - Fees
- Provision for Successor Trustee

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## **Practical CRT Applications**

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## **The Impatient Dean**

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## **Practical CRT Applications**

- **Crunch for CA\$H**
- **Charity as an income beneficiary**
- **Term of Years CRT**
- **Combos: not only for fast food**
- **Outright gift of CRT income and/or principal**

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES



### What is a Trust ?

- Separate Legal Entity
  - Tax ID Number
  - Annual Tax Return
- Owns and Administers Property
- Governed by:
  - State Law
  - Trust Instrument
- *Inter Vivos* vs. Testamentary

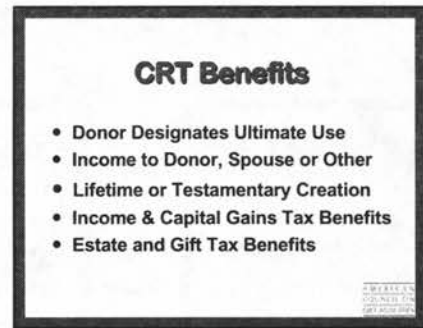
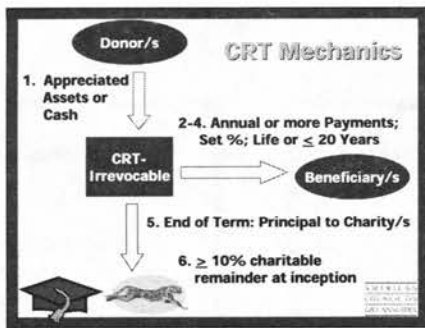
### A Trust is Not a Trust Until...

1. Grantor
2. Delivers Trust Property
3. With Intent of Creating a Trust
4. To Trustee
5. Trustee Manages Property for Beneficiaries
6. Trust is Operated for Lawful Purpose

### CRT Background

- Charitable Trust  
vs.  
Charitable Remainder Trust
- 1969: beginning of the modern era in Gift Planning

- A **Trust** is a separate legal entity. Examples of other legal entities include corporations and individuals.
- The purpose of a trust is to hold/own and administer property on behalf of someone.
- The person who creates the trust is known as the *grantor*. Occasionally, this person is referred to as the *settlor*.
- The person or corporate entity who administers the property within the trust is known as the *trustee*.
- The person or entity on whose behalf the trust is established and administered is known as the *beneficiary*.
- *Inter Vivos* trusts are created during the lifetime of the grantor. Testamentary trusts are created through the will of the grantor and do not take effect until the grantor's death.
- Trusts are governed by state law. The trust's grantor may choose the state whose law governs a particular trust. This designation is made in the trust document. There is no requirement that either the grantor or the beneficiary be a resident of the state whose law governs the trust.
- There are six distinct requirements for a trust to exist. Those requirements are listed in the middle slide above. These basic requirements were derived from English common law and are consistent from state to state.
- The Tax Reform Act of 1969 created the charitable remainder trust as we know it today. If the many provisions of the Internal Revenue Code are followed precisely, the charitable remainder trust will qualify for several favorable tax treatments (those provisions will be discussed in detail on the pages that follow). Such a trust is sometimes known as a qualified charitable remainder trust.
- If one or more of the provisions are not followed, the trust will still be a charitable remainder trust. However, it will not qualify for the favorable tax treatments and will be treated for federal tax purposes as any other trust.
- Charitable organizations can also receive funds from trusts that are not structured as charitable remainder trusts. These are known as charitable trusts. Specifics of these trusts are beyond the scope of this paper and presentation.



- Internal Revenue Code (IRC) Section 664 and Section 1.664-1(a)(1) of the Internal Revenue Regulations set forth the required provisions for a charitable remainder trust.
- Six basic requirements must be met:
  1. Grantor/Donor creates an irrevocable trust and contributes property to it.
    - From a practical perspective, the property contributed is generally an appreciated capital gain asset, with cash being the second most used asset.
  2. The trust sets forth a specified payment, made at least annually, to one or more beneficiaries, at least one of which is not a charity.
    - Generally, the beneficiaries are from a group which includes the donor, donor's spouse and donor's children. Other potential income beneficiaries are grandchildren, nieces/nephews, friends and employees.
    - While a charity may be an income beneficiary, that is not commonly done.
    - The ability to name beneficiaries from such a diverse pool provides a powerful planning tool for the charitable gift planner and the donor.
  3. The annual income payment is a set percentage of either the initial value of the assets placed in the trust (annuity trust) or the annual value of the trust's assets (unitrust).
    - This percentage is set at the trust's inception and cannot be changed.
  4. The annual income payments are made for a period of time measured by the life of the beneficiary (lives of the beneficiaries) or for a term of no more than 20 years.
    - Sophisticated planning can include a provision such as "income to my wife for her lifetime and then to my children for twenty years."
  5. At the end of the trust, all property remaining must be distributed to one or more charitable organizations.
  6. At the inception of the trust, the anticipated charitable remainder, as calculated by the IRS formulas, must be at least 10% of the value of the assets contributed to the trust.
- If all 6 requirements are met, then the CRT is qualified. As such, it is a tax-exempt entity (general trusts are taxable), and the donor can claim certain tax benefits.
- A CRT is a split-interest trust, meaning that multiple parties have an interest in the trust.
- The charitable gift planner must remember that the primary purpose of the CRT is to make a charitable contribution and must be sure that a potential donor understands that fact. While the CRT is a powerful tool in a donor's financial and estate planning, at its core, it is a gift. This gift will be utilized according to the donor's wishes.



## Charitable Remainder Annuity Trust

- Pays “sum certain” at least annually
- $\geq 5\%$  of trust’s initial value...  $\leq 50\%$
- Fixed Income: \$\$ amount or %
- **NO** Additional Contributions
- a.k.a.: CRAT

AMERICAN  
COUNCIL ON  
GRI ANGLERS

- IRC Section 664(d)(1) defines the CRAT.
- The income payment is a fixed percentage (not less than 5% nor greater than 50%) of the initial fair market value of the assets contributed to the trust. That amount never changes.
- The trust document can define the income payment as a set dollar amount or as a percentage of initial assets. Most commonly, the percentage is used.
- Income payment obligation is limited to the trust assets. In other words, if the payments are excessively higher than the investment returns of the trust over a period of time, the CRAT has no obligation to continue payments after the trust’s principal is exhausted.
- After the trust is established, no additional contributions may be made to it.
  - Care must be taken when a donor wants to fund a CRAT with several different assets.
  - For example, suppose a donor wishes to establish a CRAT and fund it with General Motors stock, some mutual fund shares and a small CD. It would be logistically difficult for all of those assets to arrive to the trustee on the same date. If the trust is established on Day 1 with the GM stock, the mutual fund shares and the CD cannot be added to the trust, even if the trustee obtains possession of them on Day 2. Day 2 would be considered an impermissible additional contribution.
  - In that scenario, the trustee would be well advised to create an escrow account to hold the assets as they arrive. Once all the assets are in the escrow, the trustee can transfer them to the CRAT from the escrow account.

## Charitable Remainder Unitrust

- At least annual payments  $\geq 5\%$  ( $\leq 50\%$ ) of trust assets... *valued each year*
- Income can  $\uparrow$  or  $\downarrow$
- When are CRUT assets valued?
- Additional contributions can be made...  
...*IF*...
- a.k.a.: CRUT

UNIT # 11-01  
ESTABLISHED 1988  
GRT 4050 01/01

- IRC Section 664(d)(2)-(3) defines the CRUT.
- The income payment is a fixed percentage (not less than 5% nor greater than 50%) of the fair market value of the assets as valued each year.
- That fixed percentage *never* changes; however the amount of income is likely to change each year as the trust's assets increase or decrease in value. It is important to inform prospect donors of the fact that trust income can go down as well as up.
- Trust assets are valued on the first business day of each year (January 2, 3 or 4).
- Additional contributions may be made to a CRUT.
  - Each additional contribution must meet the income tax deduction requirements discussed above.
  - At the time of the additional contribution, the anticipated charitable remainder of the additional contribution, as calculated by the IRS formulas, must be at least 10% of the value of the additional assets contributed to the trust.

## Does Baskin-Robbins Sell CRUT's ?

- Standard Unitrust
- Net Income Unitrust
- Net Income Unitrust with make-up
- Flip Unitrust

BASKIN-ROBBINS  
CORPORATION  
1975-1985

- IRC Section 664(d)(2)-(3), and the Regulations there under, define 4 CRUT varieties:
1. Standard Charitable Remainder Unitrust (Stan-CRUT)
    - Pays the stated percentage, no matter what
    - If trust principal must be invaded to make the payment, so be it.
    - Total Return investment philosophy works well with this type of CRUT.
  2. Net-Income Charitable Remainder Unitrust (NICRUT)
    - Net Income = *lesser* of the stated percentage or actual trust income
    - Income is defined by state law and is generally interest and dividends.
    - Capital appreciation is generally not considered distributable income; however, the trust document can contain a provision which includes capital appreciation in its definition of income.
  3. Net-Income with Make-up Charitable Remainder Unitrust (NIMCRUT)
    - Net Income = *lesser* of the stated percentage or actual trust income
    - Years where income paid by the trust is less than the stated percentage can be made up in years where income earned by the trust is greater than the stated percentage. This requires very sophisticated accounting by the trustee.
    - The investment environment over the past decade has made it very difficult for there to be any make-ups for past below-stated percentage payments.
    - Both NIMCRUTs and NICRUTS are excellent vehicles to which donors can contribute non-income-producing real estate or other difficult-to-value assets.
    - NIMCRUTs can be used as a "build-up" trust. Donors contribute annually to the NIMCRUT, and the trustee invests for low return and high growth. At some point in the future, generally retirement, the trustee switches investment philosophies to maximize returns. This higher return can then be distributed to the income beneficiaries.
  4. "Flip" CRUT
    - In 1998, the Regulations were amended to permit a NICRUT or a NIMCRUT to convert into a Stan-CRUT.

### **"Flipping" Over a CRUT**

- Harsh realities of the NIMCRUT in low interest rate environment
- One Flip and One Flip Only !
- SCRUT status begins taxable year following triggering event
- Triggering Event
- Real Estate & Hard-to-value assets

- Example: Don funded an 8% NIMCRUT with real estate. The trustee of Don's CRUT sold the real estate in year 2 and invested the proceeds in a balanced stock/bond portfolio. The NIMCRUT limits Don's payments to the lesser of actual income or the stated 8%, and income is defined as interest and dividends. In today's market, the income of the trust is only around 3%, far below Don's expectation of 8%.
- The Flip-CRUT would have been a much better option for Don.
- The Flip-CRUT begins as either a NICRUT or a NIMCRUT and "flips" to a Stan-CRUT upon the occurrence of a "triggering event."
  - Only one flip is permitted during the existence of the trust.
  - It becomes a Stan-CRUT on January 1 of the year following the triggering event.
  - Any make-up remaining in a NIMCRUT is forfeited at the time of the flip.
  - The stated pay-out percentage does not change with the flip.
- The triggering event must be stated in the trust instrument and must be either:
  - A specific date or
  - A single event whose occurrence is not discretionary with, or under the control of, the trustee or any other person
- 7 examples of permissible triggering events are listed in Reg. Sec. 1.664-3(a)(1)(i)(e):
  1. Sale of donor's former personal residence
  2. Sale of securities when there is no securities exemption permitting a public sale
  3. When the income recipient reaches a certain age
  4. When the donor gets married
  5. When the donor divorces
  6. When the income recipient's first child is born
  7. When the income recipient's father dies
- 3 examples of impermissible triggering events:
  1. Sale of publicly traded stock
  2. A request by the income recipient
  3. A determination by the income recipient's financial advisor
- Most common Flip-CRUT scenario: donor has an "unmarketable asset" (generally a parcel of real estate or another hard to value asset). The triggering event is the sale of that unmarketable asset.

### **CRT: Income Tax Issues**

- **Tax-exemption of the CRT**
  - CRT no income or capital gains tax
  - Excess income accumulated without tax
- **No Capital Gains Tax to Donor**
  - Encourages transfer of appreciated assets
- **Charitable Income Tax Deduction**
  - Estimate of what Charity will receive
  - $\geq 10\%$  of trust's initial value
  - 5% Probability Test for CRAT's

### **CRT: Income Tax Issues**

- **Factors in Determining the Charitable Income Tax Deduction**
  - Type of CRT
  - % Payout
  - Frequency of Payments
  - Length of Trust Term
  - § 7520 Rate

### **Riding the Coaster with § 7520**

- **Applicable Federal Mid-term Rate**
  - IRS earnings assumption
  - Average market yield of US Treasury Notes
  - 3-9 year maturity
  - § 7520 = 120% of AFMR
- **Donor can choose month of gift or either of prior 2 months**
- **Higher % = Higher Deduction**

- At the inception of the trust, the anticipated charitable remainder, as calculated by the IRS formulas, must be at least 10% of the value of the assets contributed to the trust. For example, a \$100,000 CRT must generate a charitable deduction of \$10,000 or more.
- The 5% Probability Test
  - Applies to CRAT's only, but not to CRAT's that exist for only a fixed term of years.
  - Articulated in Rev. Rul. 77-374.
  - CRAT must have less than a 5% chance of corpus exhaustion.
  - If the CRAT fails this test, no charitable deduction is allowed.
  - The major PG software packages automatically calculate this and warn you.
- Charitable Deduction Ceilings
  - The amount a donor can deduct on his/her Form 1040 depends on the type of asset contributed to the CRT.
  - If a donor reaches the deduction ceiling in the year of the gift, any unused deduction can be carried-forward and deducted within the next five years.
- 5 factors determine the amount of the charitable income tax deduction
  1. CRAT's and CRUT's produce different charitable deductions. Generally, a CRUT produces a higher deduction than a CRAT.
  2. The higher the trust payment rate, the lower the charitable deduction
  3. The more frequent the payments, the lower the charitable deduction. For example, quarterly payments produce a lower deduction than annual payments.
  4. The longer a trust lasts, the lower the charitable deduction. For example, a 20 year term of years CRT produces a lower deduction than a 15 year term of years. Likewise, a CRT payable over the life of a 65 year old produces a smaller deduction than a CRT payable over the life of a 75 year old, because the 65 year old is supposed to live longer according to actuarial tables.
  5. IRC § 7520 defines the interest rate to be used to determine the value of "any annuity, any interest for life or a term of years, or any remainder or reversionary interest..." Sometimes this rate is referred to as the Applicable Federal Rate. This rate is the annual rate of return that the IRS assumes the CRT assets will earn during the existence of the CRT. This rate changes monthly. The higher the 7520 rate, the higher the charitable deduction. The donor can select from the 7520 rate from the month of the gift or either of the previous two months in calculation his/her charitable deduction.

### Riding the Coaster with \$ 7520

- Prior to May, 1989 = 10.0% (fixed)
- May, 1989 = 11.6%
- May, 1994 = 7.8%
- May, 1999 = 6.2%
- May, 2004 = 3.8%
- May, 2009 = 2.4%
- All time low: February, 2009 = 2.0%
- Current: April, 2010 = 3.2%

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

### CRAT vs. CRUT Deductions

Age	CRT %	CRT Type	Pmt. Freq.	AFMR \$7520	Charitable Deduction
72	5%	CRAT	Qtrly	3.2%	\$49,753
		CRUT	Qtrly		\$55,620
		CRAT	Annual		\$50,343
		CRUT	Annual		\$55,973

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

### CRAT vs. CRUT Deductions

Age	CRT %	CRT Type	Pmt. Freq.	AFMR \$7520	Charitable Deduction
72	5%	CRAT	Qtrly	3.2%	\$49,753
		CRUT		3.2%	\$55,620
		CRAT		6.0%	\$59,137
		CRUT		6.0%	\$56,840

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

### CRAT vs. CRUT Deductions

Age	CRT %	CRT Type	Pmt. Freq.	AFMR \$7520	Charitable Deduction
72	5%	CRAT	Qtrly	3.2%	\$49,753
	5%	CRUT			\$55,620
	8%	CRAT			\$19,604*
	8%	CRUT			\$40,966

\* Fails 5% Probability Test...5.8% AFMR to pass

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

### CRAT vs. CRUT Deductions

Age	CRT %	CRT Type	Pmt. Freq.	AFMR \$7520	Charitable Deduction
72	5%	CRAT	Qtrly	3.2%	\$49,753
72		CRUT			\$55,620
80		CRAT			\$64,947
80		CRUT			\$67,925

72 = 14 years life expectancy ... 80 = 9 years

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

### CRAT vs. CRUT Deductions

Age	CRT %	CRT Type	Pmt. Freq.	AFMR \$7520	Charitable Deduction
72	5%	CRAT	Qtrly	3.2%	\$49,753
72		CRUT			\$55,620
72/72		CRAT			\$35,923
72/72		CRUT			\$44,472

72/72 = 18 years life expectancy...72 = 14 years

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

## **Philanthropy Protection Act of 1995**

- Background
- GP is about more than tax law
- PPA exempts charitable common funds from federal securities law
- Requires "disclosure" to donors

AMERICAN  
COUNCIL ON  
LIFE INSURANCE

- In the early 1990's, a class action lawsuit was brought against any charitable organization who issued charitable gift annuities using the ACGA's recommended rates. The cause of action alleged violation of the Sherman Anti-trust Act and the federal securities laws.
- The gift annuity/ACGA issues are beyond the scope of this presentation. However, the securities issues apply to any discussion of CRT's.
- The Philanthropy Protection Act of 1995, as well as the Charitable Gift Annuity Antitrust Relief Act of 1995, were the result of the charitable community coming together in response to the class action lawsuit. Terry Simmons, a retired partner of the Dallas law firm Thompson & Knight as well as a past board chair of the Partnership for Philanthropic Planning and a former ACGA board member, lead the charge in marshalling these two pieces of legislation through Congress.
- The purpose of the PPA is to protect both charities and donors. It exempts charitable common funds from the full requirements of the Investment Company Act of 1940. It protects donors by requiring that charities provide "to each donor to such fund, at the time of the donation...written information describing the material terms of the operation of such funds."
- If the charity serves as trustee of a CRT, and the charity commingles its CRT assets, it must provide the written disclosure.
- "Material terms" is not defined in the legislation.
  - It is clear that mutual-fund style disclosure is not necessary.
  - A good rule of thumb is to not have so much information that a 75 year old widow would be confused.
  - The Goldilocks Principal applies here: not too little, not too much, but just the right amount of information
  - Examples of disclosure statements are available from various PG vendors.



### Operation of the CRT

- Trustee Selection
- Trust Management
- Trust Administration
- Communication with the Charity

### Trustee Selection

- Who *can* be the trustee?
  - Bank or Trust Company
  - Donor as Self-Trustee
  - The Charitable Organization
- Who *should* be the trustee?
  - Type of property funding the trust
  - Existing relationships
  - Fees
- Provision for Successor Trustee

- Any time real estate or closely-held stock funds a CRT, the donor should **never** be sole trustee. It is very easy to run afoul of the self-dealing provisions of the Code and Regs.
- Self-dealing can disqualify the tax-exempt status of the CRT for the year of the self-dealing. Should that be the year of the gift, the income tax charitable deduction would not exist, and the donor would be required to recognize all the capital gain on the property donated to the trust.
- Charities should exercise great caution before embarking on a program of serving as trustee of CRT's. The accounting and investment infrastructure must be in place for success in this endeavor.
- Yield and Total Return are critical concepts to the effective management of a charitable remainder trust.
- Yield is the amount of cash generated by investments, while total return adds the amount of asset appreciation to the yield figure.
- The trustee has a duty to both the income beneficiary and the charitable beneficiary. Any investment strategy favoring one over the other is a breach of that duty.
- Many states have adopted the Uniform Prudent Investor standards as well as the Uniform Management of Institutional Funds Act. These statutes have great impact on the management of the trust.
- Trust administration is where a charity can provide excellent or slipshod customer service.
  - Be sure that income checks are mailed on time to the correct address
  - The income payments provide wonderful stewardship opportunities
  - Be sure to mail IRS forms on time

### Trust Management

- Investment of trust assets
  - When to sell the initial asset?
  - What is a prudent investment strategy?
- Split-interest trust means the trustee has a split-fiduciary duty
- Can a 5% trust actually be better for the donor than a 9% trust?
- Net-Income with Make-up Unitrust Trap

### Trust Administration

- Will the payments be made on time?
- Filing appropriate forms with the IRS and the income beneficiary
- Four-tiers of income must be reported to the income beneficiary

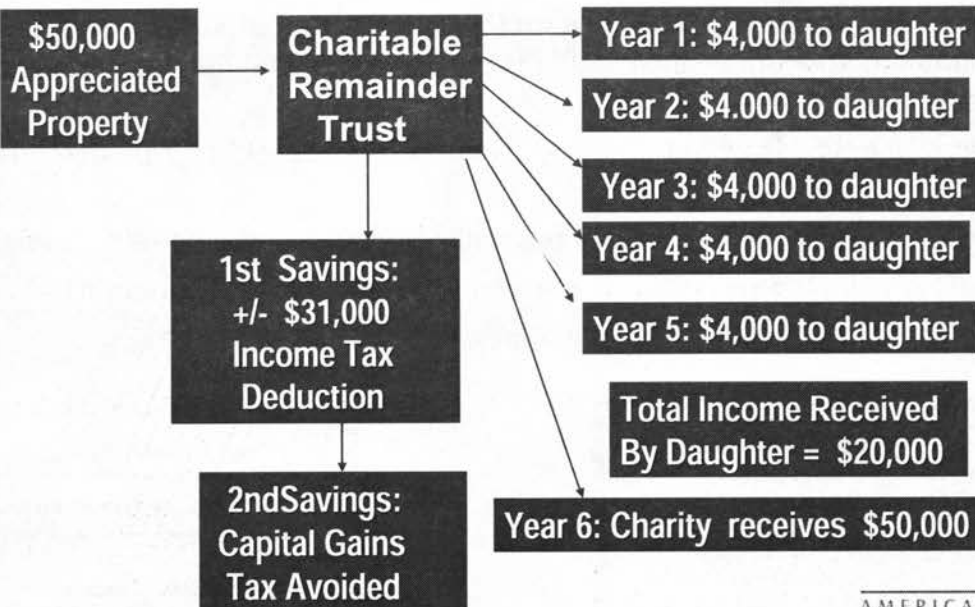
## Practical CRT Applications

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

**“I have children in college right now.”**

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

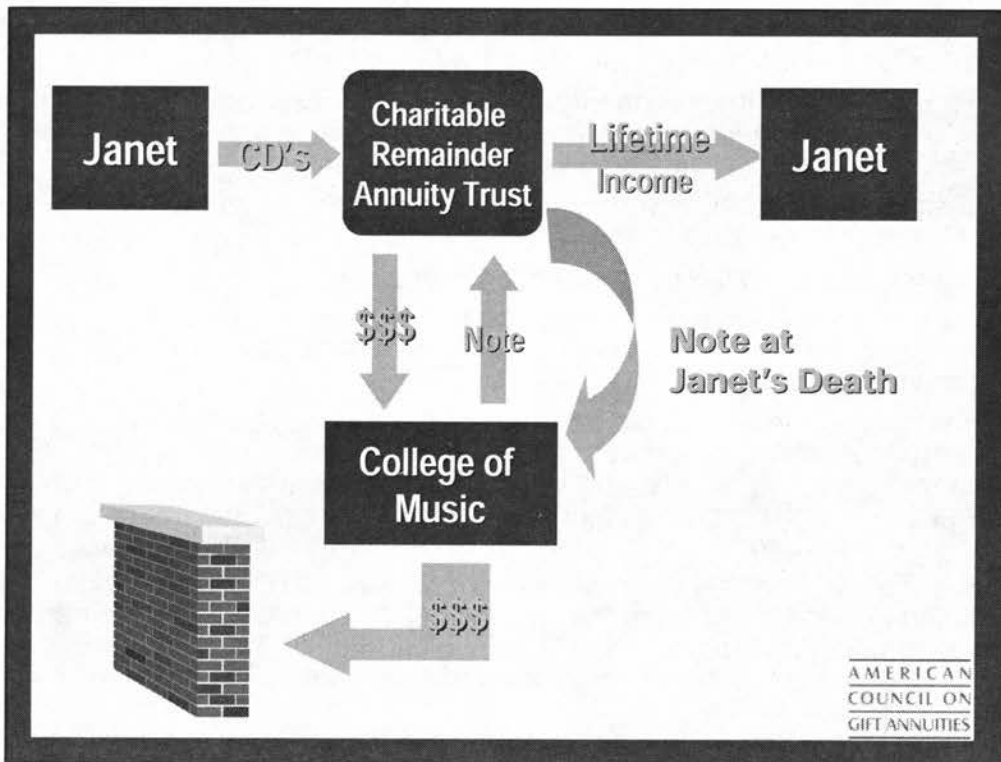
### COLLEGE EXPENSE TRUST



AMERICAN  
COUNCIL ON  
GIFT ANNUITIES

# The Impatient Dean

AMERICAN  
COUNCIL ON  
GIFT ANNUITIES




### Practical CRT Applications

- Crunch for CASH
- Charity as an income beneficiary
- Term of Years CRT
- Combos: not only for fast food
- Outright gift of CRT income and/or principal

- Charitable Organization as Income Beneficiary
  - Charitable organizations can be named as CRT income beneficiaries, provided that there is at least one non-charitable income beneficiary
  - IRS approved a CRUT, measured by Daughter's lifetime, that distributed its unitrust amount in the following manner: 50% to Daughter for life; 15% to charity for Daughter's life; 35% to charity for the initial 5 years of the CRUT, then to Daughter for her life beginning in the sixth year
- Term of Years CRT
  - CRT's may be established for a term of years, not in excess of 20 years
  - A short term CRT is a powerful tool to assist a donor in making a gift to a campaign.
  - It can also assist the donor in meeting other goals. For example, a 5, 6, 7 or 8 year CRT with income payments to donor's children to defray educational expenses is very attractive to many donors.
  - As most campaigns permit a 5 year pledge payment period, a 5 year CRT has the same net effect to the charity as the payment of the pledge over time with the only "loss" being interest income on the pledge as it was being paid.
- Negotiate a combined outright and planned gift
  - Part of every planned gift negotiation should be the discussion of an outright gift. It is possible to combine an outright gift with a planned gift.
  - This is especially true when a donor is contemplating payments to charity from a CRT. She/he should consider making an outright contribution of a portion of the funds being held for the CRT.
  - This combination often produces a higher income tax charitable deduction than the CRT standing alone.
- Request outright gift from CRT income beneficiaries
  - CRT donors have manifested their belief in the charity by naming it as a remainder beneficiary. It will not be a difficult "sell" to interest them in the current needs of the charity.
  - Donors with long-standing CRT's often find that they do not "need" the income from the trust. A donation of part or all of their income will involve them with the current happenings at the charity, and it will provide them with an income tax charitable deduction. It also provides them with flexibility should their circumstances change to the point where they need to use the CRT income for themselves.
  - Other donors find that they will never need their CRT income, or they become so excited about a program at the charity that they are willing to permanently forgo part or all of their income from the CRT to help fund this program. These donors can accelerate the charitable remainder portion of their CRT.

# ✓ r&r newkirk

for all your planned  
gift marketing,  
training and  
tax reference  
needs!

- 
- ✓ Mailing Programs
  - ✓ Web Content
  - ✓ Charitable Giving Tax Service
  - ✓ Seminars
  - ✓ More Donors

800-342-2375 • [www.rrnewkirk.com](http://www.rrnewkirk.com)

**r&r newkirk offers total planned gift marketing and support!**

- Planned gift mailing programs and targeted brochures for prospects, donors, doctors, and professional advisers
- Donor and Adviser Web Content • Electronic Publications
  - 5-Day and 3-Day Training Seminars
  - Web-Based Charitable Giving Tax Service
    - Federal Tax Pocket Guides
  - On-Site Seminars for Advisers or Donors



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# What is the Financial Justification for Your Gift Planning Program?

Presented by:

Kristen Dugdale  
Vice President, Gift Planning  
University of Colorado Foundation  
4740 Walnut Street  
Boulder, CO 80301  
(303) 541-1338  
kristen@davecolorado.com

Richard W. Lawrence  
Executive VP and Chief Operation Officer  
University of Colorado Foundation  
4740 Walnut Street  
Boulder, CO 80301  
303-541-1266  
rick.lawrence@cufund.org

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 www.acga-web.org acga@acga-web.org

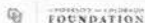




## What is the Financial Justification for Your Gift Planning Program?

Richard W. Lawrence  
Executive Vice President & Chief Operating Officer

Kristen L. Dugdale  
Vice President, Gift Planning



## Current Environment

- Budgets are tight and likely to remain so
- Pressure to raise current funds
- Deferred gift activities might be "deferred"
- Gift planning directors might have to defend program budget



## Gift Planning's Measurement Problem

- Hard to quantify means it is hard to manage
- Other development efforts are more quantifiable
- "Dollars in the door" seems more tangible—easier to measure
- Yet, significant dollars come from planned gifts, especially bequests



## What Might Leadership Be Thinking?

- How do I allocate development resources?
- How integral is the gift planning staff to the success of outright and campaign giving?
- What is the cost/benefit relationship of deferred gifts?
- If we cut X in annual giving or major gifts, we know the likely result. If we cut gift planning, there is no immediate loss, right?



## Director of Gift Planning Challenges

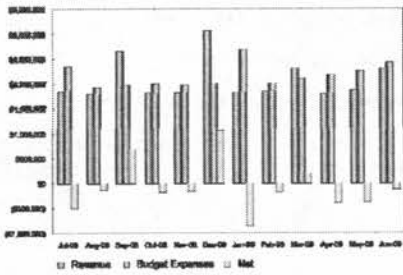
- You might be fortunate to have leadership that strongly supports gift planning
- Current environment will bring scrutiny
- How do you advocate to keep or to augment resources?
  - ✓ Qualitative case
  - ✓ Quantitative case
- Do you speak your leadership's "language"?



## Case Study University of Colorado Foundation

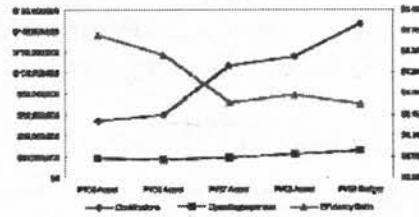


### A For-Profit Lens On a Non-Profit Activity



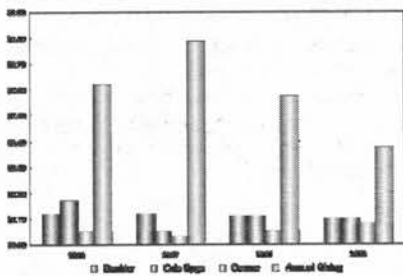
UNIVERSITY OF COLORADO FOUNDATION

### What Is Our Cost to Raise a Dollar?



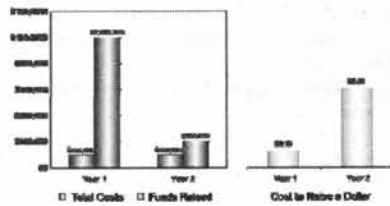
UNIVERSITY OF COLORADO FOUNDATION

### Efficiency of Various Business Units



UNIVERSITY OF COLORADO FOUNDATION

### Simple Formulas Don't Work for Gift Planning



UNIVERSITY OF COLORADO FOUNDATION

### The Planned Gift Measurement Problem

- Most planned gifts have an associated time deferral element
- Most planned gifts have undetermined gift value
- Many planned gifts are revocable

We gain the greatest insight by linking today's gift planning activities to some measure of the value that they create

UNIVERSITY OF COLORADO FOUNDATION

### Present Value Formula

$$P \left( \frac{1}{(1+r)^n} \right)$$

UNIVERSITY OF COLORADO FOUNDATION

### Present Value of \$100,000

Rate of Discount	In 5 Years	In 25 Years
5%	\$78,370	\$29,533
7%	\$71,327	\$18,426

### "Kristen, Why Invest in Gift Planning?"

#### Action Plan

- Identify the costs attributable to gift planning fundraising activities
- Identify the cash flows that will be associated with today's activities
- Identify the timing of those cash flows
- Calculate the present value of those cash flows
- Divide the cost of the fundraising activities by the present value
- Et voilà! Cost per present value dollar raised

### The Process

- Set the broad gift planning fundraising goal
- Divide the goal into gift types
- For each gift type, determine assumptions for horizon and investment return
- Calculate a future value for each type and discount it to present value
- Determine the costs associated with raising the gifts and divide them by the present values
- Et voilà!

### The Numerous Variables

- Goal
- Split of the Gift Types
- Horizon Assumptions
- Investment & Payout Assumptions
- Discount Rate

### Set the Goal

- Our gift planning goal for Fiscal Year 2008 was \$15.6 million in face value terms (revocable and irrevocable gifts)
- The goal was based generally on an average of the amounts raised over the previous 10 years
- The goal did not include realized bequest expectancies or life income gift maturities

### The Goal Categorized by Gift Type

- \$3.3 million in internally-managed CRTs
- \$3.3 million in gift annuities
- \$1.9 million in externally-managed CRTs
- \$0.9 million in outright gifts where gift planning was significantly involved
- \$6.2 million in revocable gifts (new bequest intentions, IRA beneficiary designations, etc.)
- The gift types were generally based on the split of deferred gift types in our previous campaign.

### Determine Average Horizons

Gift Type	Horizon
Internally-managed CRTs	20 years
Externally-managed CRTs	20 years
Gift Annuities	12 years
Specific Bequests	10 years
Residual Bequests	10 years

### Horizon assumptions predicated on facts

- Trust & Annuity horizon assumptions were determined by averaging the remaining horizons of every trust and/or annuity in our current program (15 years for trusts, 12 years for annuities).
- Is the horizon too short, as we did not look at original gift dates?
- Is the horizon too long, as we did not allow for the possibility of earlier than expected terminations?
- Because of these variables, we added 5 years to the assumption for trusts & 3 years to gift annuities
- Horizons = 20 Years for trusts; 15 years for annuities.
- In the case of gift annuities, we also considered the ACGA suggested rate for a 75 year-old.

### Horizon assumptions for bequests

- Made an assumption that specific & residual bequests would be split 50/50.
- Applied an annual total return to residual bequests of 3%.
- Compared the gift date of recorded bequests in our system to the realization date (if any), and averaged all for a period of 4 years.
- Conservatively added to that term by using 10 years.

### Chose not to discount bequests based on their revocability.

- NCPG's Survey of Donors conducted in 1992, and updated in 2000.
- 92% of donors did not take charity out of the will.
- 86% did not change the amount to charity.
- Of those who did change the amount, 1/10 did so to increase the amount.
- Only 1/100 decreased the amount & others made changes for "mechanical reasons".
- Results reaffirmed in 2000 survey.

### Determine Payout Rates and Projected Investment Returns

Gift Type	Payout Rate	Investment Return
Internally-managed CRTs	7%	9%
Externally-managed CRTs	7%	9%
Gift Annuities	7.1%	9%
Specific Bequests	n/a	n/a
Residual Bequests	n/a	3%

### Determine a Discount Rate

- Should we use the endowment rate of return to discount the value of a future gift to the university?
- Or use the Higher Education Price Index?
- Or pick a rate in the middle?

**We decided to use a 7% discount rate**

### Calculate the Present Value of Gifts

- Grow each gift type out to its estimated future value (net of payments and costs)
- Apply the discount rate to determine the net present value
- Add the net present values across gift types

$$\frac{\text{Costs}}{\text{PV of Gifts}} = \text{Cost per PV \$ Raised}$$

### How Will We Take Costs into Account?

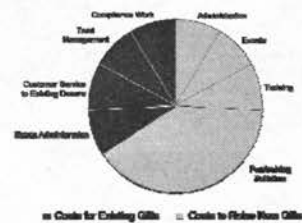
- Start with the department budget number
- Subtract the costs to manage existing life income gifts
- Subtract out estate administration and "customer service" costs

$$\frac{\text{Costs}}{\text{PV of Gifts}} = \text{Cost per PV \$ Raised}$$

### Gift Planning Budget Items

- Salaries and benefits
- Promotional activities and events
- Travel
- Gift management fees not charged to trusts
- Legal and compliance
- Professional development
- Overhead and other operating costs

### The Budget Items Are Allocated to Activities



### Et Voilà!

$$\frac{\text{Costs}}{\text{PV of Gifts}} = \$0.09$$

- We estimated our cost to raise a present value planned gift dollar to be nine cents
- Additionally, we decided to defray costs of administering certain existing and new gifts by charging expenses to the trusts

### Dollars Raised by Gift Type (Millions of Present Value Dollars)

	Fiscal Year '07		Fiscal Year '08		Fiscal Year '09		Fiscal Year '10	
	Plan	Actual	Plan	Actual	Plan	Actual	Plan	YTD
LIGs (internal)	\$2.8	\$0.5	\$2.8	\$14.8	\$2.8	\$0.1	\$2.8	\$0.02
LIGs (external)	0.6	0.1	0.6	0.1	0.6	0.8	0.6	0
Overight & B.A.	0.9	2.0	0.9	4.9	0.9	7.9	0.9	98
Reversible Intentional	3.7	7.0	3.7	1.7	3.7	1.3	3.7	7.9
<b>Total</b>	<b>\$8.0</b>	<b>\$9.6</b>	<b>\$8.0</b>	<b>\$21.4</b>	<b>\$8.0</b>	<b>\$11.8</b>	<b>\$8.0</b>	<b>\$9.0</b>

Cost per PV Raised      \$0.06                      \$0.03                      \$0.03                      \$0.06

### Some Observations

- Consistently exceeded goals
- Actual cost to raise a dollar beat estimates
- Different "winning" category every year
- Revocable category is understated
- Some assumptions were inaccurate
- Looking forward
  - ✓ If we add costs will we add revenue?
  - ✓ How can we get more cost-efficient?
  - ✓ Should we focus on older donors (higher PV)?

### Some Conclusions

- Gift planning makes logical sense from a business perspective
- "You have to know your business to know your business."
- Don't expect to reconcile cost per dollar raised data with announced fundraising totals
- Be careful of over-interpreting the analysis
- Think through your "product mix" carefully; focus where possible on the shortest and surest opportunities

### Other ways to measure a program

- Evaluate based on the effectiveness or charitable impact the charity makes
- Marginal costs/Diminishing Returns?

### Discussion

- What questions do you have?
- Has your VP of Development or your CFO asked you to justify the value of your gift planning program?
- How have you responded? Have you used other methods to make the case?

**The End**

Achieving your goals is quite an accomplishment.  
PNC can help you get there.



**The experienced professionals in Planned Giving at PNC can help.**

For over 30 years, PNC Institutional Investments has provided comprehensive Planned Giving solutions for some of the most successful non-profit organizations. Our dedicated staff of Planned Giving professionals can provide insight in the areas of life-income gift administration and investments for charitable gift annuities, charitable remainder trusts, and pooled income funds. Our specialists will work with you to create a specific administrative and investment program to meet your multifaceted needs. With our experience and your dedication, consider your goals met. **For more information, contact Chris McGurn at 410-237-5938 or email [christopher.mcgurn@pnc.com](mailto:christopher.mcgurn@pnc.com), or visit [pnc.com/plannedgiving](http://pnc.com/plannedgiving).**







## **Jammin' For Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities - April 28-30, 2010



# Would You Hire Actors Without a Script? Exploring the Role of eMarketing in a Strategic Marketing Plan

Presented by:

Ann McPherson  
Marketing Consultant  
PG Calc  
129 Mount Auburn Street  
Cambridge, MA 02138  
(617) 497-4970  
amcpherson@pgcalc.com

Gary Pforzheimer  
President  
PG Calc  
129 Mount Auburn Street  
Cambridge, MA 02138  
(617) 497-4970  
gary@pgcalc.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



# Table of Contents

## Part I: eMarketing Overview

Introduction

What is eMarketing?

Why eMarketing?

How eMarketing Works with Other Media Channels

## Part II: Case Study Examples

Case One Objective: Increase repeat giving of existing planned giving donors

Case Two Objective: Increase repeat giving of existing donors

Case Three Objective: Increase your bequest program

Case Four Objective: Donor retention and stewardship

## Part III: Resources

# Part I: eMarketing Overview

## Introduction

Every year, more gift planning prospects are comfortable on the Web, using it as a research tool, a source of information, and an interactive playground where they make connections with brands, organizations, and former acquaintances in ways they have never dreamed of. Gift planners who think a lot about the behaviors of their existing donors and prospects have steadily been recognizing over the last 10 years or more that there is a dual shift happening – advances in technology are changing the way all of us behave and as a result, the demographics, interests, and behaviors of their target audience have changed.

We see this dual shift every day. A grandmother who once waited for the mail to come for pictures of her grandchildren to arrive now logs into SnapFish or Facebook for the same reward. A mature alumna now goes to a university's website for information about her reunion instead of calling the Alumnae Office. A couple that likes to garden complements their gardening magazine subscriptions with subscriptions to one or two blogs that explore their specific interests in detail.

The *purpose* of this paper is to energize development professionals to capitalize on these changes and improve or at the very least begin their eMarketing of planned gifts. We understand and appreciate that to do this each person must work not only within their budget, but more importantly, within the framework of marketing at each individual organization. At some organizations, this means you'll have to be assertive. You may be limited by the culture and technology in use at your organization, and you might have to convince others of the value of eMarketing before you can be successful.

Before we delve in, let's review the concept of marketing. The objective of marketing is no different today than it was centuries ago when people first started trading. Marketing is about communicating value and convincing people that the value is relevant to them and that they should be willing to trade goods or, in today's world, currency for that value. While the purpose of marketing itself hasn't changed - it's still about communicating value - the technology infrastructure that facilitates communication is ever-changing. One of the primary reasons marketing today is very different than marketing 15-20 years ago is the Internet, and exploring the opportunities that the Internet provides as a platform is the *basis* of this paper.

## Establishing Goals

It's important to be strategic about your marketing efforts right from the beginning. That starts with thinking about what you are trying to accomplish and framing all your work in that context. You need to set goals and no marketing method should be considered until goals are established. Effective marketing plans have the following attributes in common:

- Documented, tangible, measurable goals in three categories: realistic, achievable, and stretch
- Documented goals that are less measurable
- Commitment to the goals of the program at all levels of the organization
- Transparency of priorities and goals to the organization's leadership and colleagues

## What is eMarketing?

eMarketing, also known as electronic marketing, Internet marketing, or online marketing, is the application of marketing principles and techniques via electronic media. In other words, eMarketing is the process of using the Internet to market your brand. It includes both direct and indirect marketing elements and uses a wide array of technologies to communicate with donors and prospects. While it's easy to understand the definition, it's harder to put it into effective practice.

Since eMarketing covers a broad range of media, we've identified the following elements of eMarketing that we think are particularly worthy of focus:

1. Websites
2. Email (including invitations, letters, newsletters, etc.)
3. Viral marketing
4. Social media – blogging, Facebook, Twitter (user content driven vs. org driven, interactive vs. static)
5. Search engine marketing and optimization

- 1. Websites.** PG Calc conducted a research project in late 2008 which reflects that most organizations are not satisfied with the results of their sites. (See Table 2 in the "How eMarketing Works with Other Media Channels" section.) This finding is in line with many recent articles about website effectiveness (See Part III: Resources at the end of this paper for some examples). Respondents in our study indicated that although they use websites in their planned giving marketing efforts more than any other technique listed (93%), only 7% of them feel their websites are "very effective." More telling, perhaps, is that over a quarter (27%) feel their websites are "not effective at all" for marketing planned gifts, a far greater percentage than for any of the other marketing tactics. These results should be a call-to-action to many organizations to gain a better understanding of what works for them on the Web.

Websites have various purposes and those purposes are unique to each organization. Clearly, there are some fundamentals and plenty of consultants have covered those in the past (include bequest language, planned giving staff contact information, etc.), but we encourage you to move past the basics if you haven't already and prioritize a fresh, simple design and updated, compelling content reflective of your mission. If you haven't changed the site's design in a number of years, this should be a priority to review and ensure it looks current from a design and copy perspective. So often we come across sites that are publicizing an event that happened months ago. However, there's more to it than that. Content is king and it's time to see your website as more than a source of information and include the most compelling stories you can find to promote your mission.

**Pros**

- *Websites have become the go-to medium to learn more about an organization*
- *Online usage including high-speed access continues to grow by the month*
- *Easy-to-track online activity with the right analytic tools*

**Cons**

- *Hard to measure effectiveness of content*
- *Takes effort to keep the site fresh, interesting, and attractive*
- *May not be the right medium to appeal to those people who are lacking in "web savvy"*

2. **Email.** The primary advantages to using email are its budget-friendliness, its simple-yet-effective technology, and its ease of sending to multiple recipients. But as with any target mailing you need to start with the right audience and good addresses. Most, if not all, of your recipients are overloaded with email so be cautious about how much of it you send. In particular, don't abuse your list of recipients with news that you think is important that they might not *or they will ask to unsubscribe.*

**Pros**

- *Inexpensive*
- *Easy to measure results if recipients are sent to a landing page or if you have the right technical tools*
- *Easy to coordinate and send*
- *Effective tool for lead retention and donor stewardship*

**Cons**

- *Many recipients are overloaded with email; sending too much to them can quickly become annoying*

- *Hard to measure if recipients are not sent to a landing page or if there is no follow-up action associated with the email(s)*
- *Email addresses tend to change more frequently than postal addresses*
- *Overall, response rates are even lower than they are with direct mail*
- *Should be used to communicate personal messages, not a mass message*

**3. Viral marketing.** At its most basic level, viral marketing is word-of-mouth marketing. This concept marries the connectedness of the Internet with the sharing characteristics of social networks to build brand awareness exponentially.

The reason some marketing efforts are known as “viral campaigns” is because of the similarities to many biological viruses: they don’t overtly show their true intentions and depend on the connection of people to spread.

Online is the perfect medium for people to pass on things of value because it’s essentially free. Anything that truly informs, entertains, or intrigues is certain to get the attention of many and is likely to be redistributed; think of chain letters, video clips, funny pictures, and sayings. A well orchestrated viral campaign harnesses this basic fact of human nature for the good of the brand. To intentionally execute a viral marketing effort, one must carefully plan. These campaigns are more sophisticated than they appear.

Many viral experiences that we are familiar with are the unplanned ones, such as the case of Susan Boyle. You didn’t have to be watching one fateful episode of the television show “Britain’s Got Talent” to recognize that name. The news of this rags-to-riches story of this unknown person who became an international sensation spread virally back and forth among blogs, YouTube, email, and more.

In contrast, an excellent example of a planned and relevant viral marketing campaign is the “Pink Glove Dance” video for breast cancer awareness from the Providence St. Vincent Medical Center in Portland Oregon, which has received almost 7 million views to date: <http://www.youtube.com/watch?v=OEdVfyt-mLw>

**4. Social media.** Social media – including Facebook, MySpace, Twitter, YouTube, Flickr, LinkedIn, Stumbleupon, Digg (to name a few), and blogging – is increasingly of interest to all marketers because of the enormous promise it seems to hold in terms of building communities and fostering stronger one-to-one relationships.

Social media is transformational because it takes advantage of true human nature and the fact that we care about what other people are doing and what they think

about products, services, and features. Word-of-mouth marketing is the essential appeal of social media, and word-of-mouth marketing is about placing trust in an objective source – getting the real breakdown on a product or feature from someone who is not a paid marketer or representative of a firm, such as an independent, objective blogger.

But discussions on social networks isn't yours to control, even if they are about your organization and your messages. That ceding of control is one component of engaging in social media – and the part that most managers find hardest to swallow. Keep in mind that for so long messaging has been about finding the right “spin.” This is where having organizational policies as they pertain to the people in your organization representing you is extremely important.

Social networks are vibrant ecosystems that haven't invited you in, so earning trust and building relationships is a necessary endeavor. Social networking as a platform for building and engaging communities isn't new, and what's more, building and engaging communities is a sweet spot for non-profits.

It is much more common for an organization to become a part of a social network than it is having the organization create its own. While we recommend engaging in social media, and whether you build your own community or join any of the many that exist, we encourage you to do it only when you are confident that you've lined up the human and technical resources to do it well.

### ***Pros***

- *Has the potential to produce huge viral results if done effectively*
- *Virtually free from a cost-of-media basis*
- *Effective for building community for your mission*
- *Enables you to form meaningful relationships with people who are passionate about your cause*
- *May increase the number of people who link to your site, improving search engine optimization*

### ***Cons***

- *Difficult to do effectively*
- *Requires creative and technical skills often not found within non-profit organizations*
- *Cannot implement independent of your organization; has to be integrated with the organization's marketing staff*
- *Execution tactics so new that ROI not clear yet*



5. **Search engine marketing (SEM).** SEM is divided into two categories, paid search and organic search. Paid search, known as pay per click (PPC) and organic search (SEO) together define SEM. While paid search may be something to consider, and some non-profits utilize this technology, the organic search is generally more relevant to most organizations.

SEO is about optimizing your website to achieve high rankings on search engines for certain key phrases and/or keywords. SEO involves making changes to the HTML code, content, and structure behind your website to make it more accessible for search engines. SEO is a continuous process, both to maintain rankings and improve rankings for other keywords that may bring in relevant traffic.

In SEO efforts, Google is your friend. Use it for free. It has easy, user friendly analytics and reporting. The report below demonstrates certain competitive relevance factors Google considers when ranking sites in its organic (unpaid) listings.

**Table 1: Competitive Relevance Factors**

Website	Page Rank	Inbound Links	Indexed Pages	Domain Age (Days)
www.1.com	5	33	1850	4871
www.2.com	5	23	150	3094
www.3.com	5	8	695	4681
www.4.com	6	510	137	3396

*Notes on this table:*

- *Page Rank is an indication of the # and quality of inbound links.*
- *Inbound links is the # of Google reported inbound links pointing to the site from other websites.*
- *Indexed pages is the # of pages Google has indexed on their servers.*
- *Domain age is also heavily factored into relevance. The older the domain name, the more relevant search engines think the site is.*

## Why eMarketing?

Why is eMarketing important? From a commercial standpoint, the return on investment (ROI) of eMarketing is one of the key reasons businesses are attracted to this medium. If executed correctly, eMarketing's ROI can far exceed traditional marketing strategies. The other primary reason is just pure visibility. You cannot dismiss the ability to reach millions of people. It has

redefined how businesses interact with their customers. These two reasons alone are sufficient for all non-profits to be exploring and eager to participate in this marketing technology.

Good marketing always has been about building a relationship with the customer. In many ways, eMarketing is the opportunity that marketers have dreamed of for decades: a chance to build relationships with a ready-made community of people who are open about who they are and what they like.

The main benefits of eMarketing over traditional marketing are: reach, immediacy, trackable results, and interactivity. eMarketing opens up new possibilities for small organizations on a small budget to reach more potential donors. But just as important, the Internet has transformed how people organize themselves and that has allowed organizations to reach niche markets in a way that hasn't been available in the past. And since marketing messages are most effective when delivered to the audience most likely to be interested in them, this capability becomes an important building block of any successful marketing program.

Consider the attributes mentioned above in the context of the recent fundraising efforts to rebuild Haiti. Reach was unprecedented. Immediacy was undeniable. Results were trackable in real-time. These attributes and more have compressed the length of time from awareness to action. The record-breaking donations to Haiti in the days following the catastrophic earthquake are evidence of this change. The result of this immediacy is the ability to measure, analyze, and adapt your message and or strategy in ways that were inconceivable before now.

eMarketing can present a huge opportunity for your program. We would caution you to recognize, however, that while eMarketing may not seem like a significant financial investment, it does require a commitment to a tremendous amount of ongoing work and substantial technical and creative resources to make it into something that has lasting and drawing power. Engagement in the social media space, for example, is a broad endeavor that goes well beyond simply building a page on a social site.

While traditional marketing is largely about mass communications and brand awareness, eMarketing facilitates conversations between organizations and their donors and prospects. eMarketing is now considered a two-way channel vs. a one-way channel, a difference that explains the social media craze. It is the missing link that has connected the other marketing technologies together, making it a much more powerful application.

## **How eMarketing Works with Other Media Channels**

It would be inappropriate, of course, to ignore the importance of ensuring that your eMarketing dovetails with your traditional marketing tactics. Note that the efforts for Haiti described above were reinforced by more traditional media – images in newspapers, benefits on television, and

telethon campaigns. Like that successful example, you need to make use of every available method that makes sense for your own marketing efforts, seeing the big picture of frequency, audience, message, and medium in communicating to your donors and prospects.

eMarketing complements traditional marketing, but in some cases it can serve as a substitute to traditional marketing, especially with a younger audience whose preference is only electronic or where an organization has minimal budget. Generally speaking, though, a marketing plan that is comprehensive and embraces all media types increases the chances for connecting with a prospect.

eMarketing is just like traditional marketing when developing a plan:

**Establish your goals.** Ensure you follow the process mentioned earlier in this paper when setting your goals.

**Identify your target audience.** What are its demographic characteristics – age, gender, education level, income level, and so on? What are its psychographic characteristics – are its members thoughtful and rational, or impulsive and emotional? What values are they governed by? Good marketers take all these factors into account as they seek to build a composite profile of their target audiences, thereby gaining a better understanding of the messaging they need to create in order to drive desired behavior.

**Define your budget.** The reality is that financial constraints usually dictate a specific budget to work within. What you spend on marketing needs to make sense in the context of your overall budget, and your ROI needs to make equal sense.

**Determine the marketing mix.** The important methods of marketing are often called the “Marketing Mix.” There is no magic formula as to what to use or when. The right methods to deliver your messages are a function of content, timing, constituency, and budget. A good marketing plan is neither exclusively electronic nor exclusively traditional. Your message will always benefit from a multi-media approach if you have the resources.

The table below shows some of the most popular marketing tactics, along with percentages given by our survey respondents (2008) as to their impression of their effectiveness. (NOTE: PG Calc did not use the survey as an opportunity to measure the effectiveness of social media tactics.)

**Table 2: Popular Marketing Tactics and Levels of Perceived Effectiveness**

	Very Effective	Reasonably Effective	Not Effective	We Don't Do This
Advertising	5%	40%	15%	40%
Direct Mail	11%	56%	17%	16%
Email	2%	23%	17%	58%
Website	7%	58%	27%	8%

**Measure your success.** This is where the difference between electronic and traditional marketing can be significant. There are primarily two aspects to defining success, at the aggregate level and on individual results. On the whole, a campaign could be considered successful if, for example, you decide to send an email invitation and 75% of the recipients opened your invitation and of that 75%, 50% went to your site for more information. These numbers are purely subjective and would be based on your own internal benchmarks (which should be set ahead of time!).

But that is only half of the picture; the other half is measuring the number of registrations you received. When evaluating the specific results, having a CRM tool to capture the electronic data is essential to measuring the success of your eMarketing program. With the ability to reach so many people and to monitor and measure results in real-time, feeding this information back into your system automatically is a necessity. Without that functionality your program will be limited in its effectiveness or worse you could get caught in a data management quagmire.

It's important to look at the entire picture when measuring your eMarketing programs. As with any technology, there will need to be changes made along the way in order for the end result to be successful.

### **Key uses of eMarketing**

Think of your eMarketing strategy in the following ways:

- Does it help you listen to your donors?
- Does it help you start a conversation?
- Does it let people share their ideas, concerns, and thoughts?
- Is your strategy integrated with the rest of your marketing program?

The goal of your eMarketing strategy is to be able to say “yes” to all of these questions and if there is a “no” then it's best to revisit why your strategy is not working as effectively as it could.

In order to determine if you are ready for eMarketing tactics, answer these questions:

- What percentage of my constituents is regularly online?
- How many of my constituents belong to other online communities? If the number is high, one of two things is true. They are saturated with online communities and will not join another one, or, more likely, they are engaged in online activities and will be susceptible to your online messaging.
- Do my constituents want to create relationships with each other? If you are simply seeking ways to let people access and create content, your website and a blog might be sufficient.
- Do I have the time? Online communities aren't a short term investment – it will take a significant amount of staff time to seed the community, get people engaged, and make sure conversation continues to flow.

Think of eMarketing as a second oven when you are preparing thanksgiving dinner for your family of twenty. That second oven is integral to the planning process starting with the menu. It's critical to the preparation and timing of the meal. It can be used to cook different dishes or more of the same dishes. It can be used for the main meal or for desserts. eMarketing complements your traditional marketing efforts and can be used as a:

- way to support and reinforce your traditional messaging
- follow up to your direct mail programs
- stand-alone campaign
- test to see if one medium produces different results than another
- vehicle for solicitation, donor acquisition, cultivation, supporting events, recruiting volunteers, and stewardship

### **Conclusion**

The true benefit of eMarketing is communication choice. It gives your prospects options – options for additional channels or preferred channels by which to connect with you. The more options you have to offer, the more choices they have and that can increase the likelihood of improving your relationship.

The methods described in this paper are channels you need to think about. eMarketing is not a question of “Should I”, but “How do I?”

When you know what you are trying to accomplish, when it is thoughtfully orchestrated using all of your available resources, and when you have defined when your goals have been reached, then you will not only have incorporated your eMarketing strategy effectively, but you will also have built a significant part of your marketing program's foundation.

# Part II: Case Study Examples

## Case One Objective: Increase repeat giving of existing planned giving donors

A healthcare provider feels its pool of existing planned giving donors is large enough to serve most effectively by targeted cultivation for a repeat gift. In this instance, the primary marketing goal of the organization is to grow its planned giving program by revisiting existing gift annuities donors to encourage additional gifts. This narrow scope is by definition somewhat limiting, but it's a piece of a larger development marketing plan. The additional gift could take the form of another gift annuity or possibly a bequest or beneficiary designation.

### Profile. Large Healthcare Provider

- Development Office: 98 people
  - Annual Fund: 10
  - Major Gift Officers: 34
  - Planned Gift Officers: 4
  - Corporate and Foundations 8
  - Special Events 8
  - Support Staff (Marketing, IT, Admin. Prospect Research): 34
- Planned Giving Program is 30 years old
- Endowment is \$650 million
- Annual Planned Giving Revenue: \$15 million (realized bequests plus life income gifts)

### Audience Segmentation.

- Existing planned giving donors

**Communication Matrix.**

<b>Media Channel</b>	<b>Type of Piece</b>	<b>Target Audience</b>	<b>Calendar</b>
Direct Mail	BatchCalcs mailing Follow up with call	Existing CGA donors	One-time
	Bequest mailing	Existing CGA donors	One-time
	Annual thank you that includes an update on what their gift has done for the organization	Existing CGA donors	One-time
	PG letters: annual thank you & update birthdays	PG donors	annually
PG Newsletter	Inspirational: PG donor stories, Educational: PG gift example	All legacy donors Major gift donors	2x per year Apr – Oct
<b><i>PG eNewsletter</i></b>	<b><i>Electronic version of printed one</i></b>	<b><i>Annual fund donors who give \$XX over a period of X years</i></b>	<b><i>2x per year Apr – Oct</i></b>
<b><i>PG Website Updates</i></b>	<b><i>Donor Stories:</i></b> - CGA - <i>Beneficiary designations</i> - <i>Bequest</i>	<b><i>Unknown</i></b>	<b><i>One-time</i></b>
<b><i>email</i></b>	<b><i>Short letters with custom intro depending upon the audience with a link to the new donor stories, which link to articles</i></b>	<b><i>All legacy donors Major gift donors Annual fund donors who give \$XX over a period of X years</i></b>	<b><i>One each month for three months</i></b>
	<b><i>Invitation to special events and lecture series</i></b>	<b><i>PG donors</i></b>	<b><i>Quarterly</i></b>

(***Bold, italics*** denotes eMarketing)

## Case Two Objective: Increase repeat giving of existing donors

A university wants to maximize all of its development efforts, integrating its marketing messages across all donors, where applicable. Its goal is to generate as much planned giving through all development channels, be it annual fund, major gifts, legacy society, etc.

### Profile. Large University

- Development Office: 53 people
  - Annual Fund: 15
  - Major Gift Officers: 25
  - Planned Gift Officers: 3
  - Support Staff (Marketing, IT, Admin. Prospect Research): 10
- Planned Giving Program is 25 years old
- Endowment is \$500 million
- Annual Planned Giving Revenue: \$10 million (realized bequests plus life income gifts)

### Audience Segmentation.

- Annual donors
- Major donors
- Alumni
- Faculty and staff
- Volunteers
- PG donors

Make sure email addresses are updated and accurate. Email will be an important channel for the older classes, where mobility is an issue, as well as for the younger classes. Both use email as a primary method of communication.

Segment 1: Class year 1960 and prior (70+ yrs.)

This is the market for repeat planned gifts, specifically gift annuities, trusts, and estate planning: wills, bequests, retirement plan assets, life insurance

Segment 2: Class year 1961-1975 (55-69 yrs.)

This class overlaps with the major gifts audience, so layered messaging for overall philanthropy is important. Key gift vehicles center on estate/legacy planning, which have to be tied into the overall messaging.

Segment 3: Class year 1976-1990 (40-54 yrs)

The most likely repeat gift would be an estate gift. Other planned giving vehicles are not likely in this age bracket.



## Communication Matrix.

Targeted messaging should be addressed to specific donor segments, namely by age group (class year).

Media Channel	Type of Piece	Target Audience	Calendar
Development Newsletter	Inspirational: donor stories, Reporting: update on philanthropic progress against goals Informative: upcoming events	Board, Faculty, Professional Advisors, Volunteers, Alumni – consecutive giving for 5+ years	Semi-annually Feb - August
Direct Mail	Annual Fund Solicitation Invitation – stewardship	Alumni Annual fund Major gifts PG donors Faculty & Staff Volunteers	Bimonthly
	Invitation to special events and lecture series	Major gifts PG donors Annual fund over \$XX	As required, but at minimum 2-3 times per year
	BatchCalcs letter	Existing CGA donors	
	PG letters: annual thank you & update birthdays	PG donors	annually
	PG Letter: educational	Faculty & Staff	annually
	PG Letter: educational	Volunteers	annually
PG Newsletter	Inspirational: PG donor stories, Educational: PG gift example	Major gifts PG donors Annual fund over \$XX	3x per year Mar – Jul - Oct
<b><i>PG eNewsletter</i></b>	<b><i>Electronic version of printed one</i></b>	<b><i>Major gifts PG donors Annual fund over \$XX</i></b>	<b><i>3x per year Mar – Jul - Oct</i></b>
<b><i>Development Website Updates</i></b>	<b><i>Donor stories</i></b>	<b><i>Unknown</i></b>	<b><i>Bimonthly</i></b>
	<b><i>Yearly goals and objectives funding is to accomplish</i></b>		<b><i>Semi-annually</i></b>
	<b><i>Philanthropic updates against plan</i></b>		
<b><i>email</i></b>	<b><i>Invitation to special events and lecture series</i></b>	<b><i>Alumni Annual Fund Major gifts PG donors</i></b>	<b><i>As required, but at minimum 2-3 times per year</i></b>

(***Bold, italics*** denotes eMarketing)

## Case Three: Increase your bequest program

This organization is a small social service organization that does not have a gift annuity program. It has limited resources, but the development officer is familiar with planned giving and realizes that bequests contribute the largest gifts over time. She doesn't want to lose any potential opportunities.

### **Profile.** Small Social Service Organization

- Development Office: 3 people
  - Annual Fund: 1
  - Major Gift Officers: 1
  - Planned Gift Officers: 0
  - Support Staff: 1
- A formal planned giving program doesn't exist yet
- Endowment is \$1 million
- Annual Planned Giving Revenue: \$100,000 (realized bequests)

### **Audience.**

- Grateful recipients
- Annual donors
- Major donors
- Volunteers
- Local Community

**Communication Matrix.**

Media Channel	Type of Piece	Target Audience	Calendar
Direct Mail	Bequest mailings: (letter w/ estate planning brochure)  email and selected phone follow up	Target two age groups - Age 40-50: creating a bequest - Age 65-70: preparing for retirement  Annual donors Major gift donors Grateful recipients	One-time
	Annual thank you that includes an update on what their gift has done for the organization  The letter should be customize to reflect the type of gift: major, annual, and introduce what a bequest could do for the organization	All donations over \$XXX	One-time
Development Newsletter	Inspirational: bequest donor stories Educational articles	All donations over \$XXX	annually
<b><i>Development eNewsletter</i></b>	<b><i>Electronic version only</i></b>	<b><i>Annual fund donors who give \$XX over a period of X years</i></b>	<b><i>annually</i></b>
<b><i>Development Website Updates</i></b>	<b><i>Annual, major, and PG donor stories:</i></b>  <b><i>PG focus is estate planning:</i></b> - <b><i>Bequest</i></b> - <b><i>Beneficiary designations</i></b>	<b><i>Unknown</i></b>	<b><i>quarterly</i></b>
<b><i>email</i></b>	<b><i>Short letters with custom intro depending upon the audience with a link to the new donor stories, which link to articles</i></b>	<b><i>All legacy donors</i></b> <b><i>Major gift donors</i></b> <b><i>Annual fund donors who give \$XX over a period of X years</i></b>	<b><i>quarterly</i></b>
	<b><i>Invitation to special events</i></b>	<b><i>All donations over \$XXX</i></b>	<b><i>annually</i></b>

(***Bold, italics*** denotes eMarketing)

## Case Four: Donor retention and stewardship

The planned giving program of this mid-size organization has been in existence for 8 years, but the program's growth has been decreasing over time. The director has determined that in addition to finding new prospects, the program has to do a better job of stewarding its existing donors.

### Profile. Mid-size Cultural Organization.

- Development Office: 15 people
  - Annual Fund: 5
  - Major Gift Officers: 4
  - Planned Gift Officers: 1
  - Support Staff (Marketing, IT, Admin. Prospect Research): 5
- Planned giving program is 8 years old
- Endowment is \$10 million
- Annual Planned Giving Revenue: \$100,000 (realized bequests)

### Audience.

- Grateful members
- Annual donors
- Major donors
- PG donors
- Volunteers

**Communication Matrix.**

Media Channel	Type of Piece	Target Audience	Calendar
Direct Mail	Thank you and celebration communications: Annual thank you letters which include an update on what their gifts have done for the organization	PG donors	annually
	birthday cards		
	anniversary of gift		
	recognition of other important events in the donors' life: hospital visits		
	Invitation to special events	PG donors	Quarterly
	Note from the president sharing non-public and relevant information.	PG donors	annually
PG Newsletter	Inspirational: PG donor stories Educational: PG gift example	PG donors	2x per year Apr – Oct
<b><i>PG Website Updates</i></b>	<b><i>Donor Stories:</i></b> - <b><i>CGA</i></b> - <b><i>Beneficiary designations</i></b> - <b><i>Bequest</i></b>		<b><i>One-time</i></b>
<b><i>email</i></b>	<b><i>Short letters with custom intro depending upon the audience with a link to the new donor stories, which link to articles</i></b>	<b><i>All PG donors Major gift donors Annual fund donors who give \$XX over a period of X years</i></b>	<b><i>One each month for three months</i></b>

(***Bold, italics*** denotes eMarketing)

## Part III: Resources

Beth Kantor Blog: How Nonprofit Organizations Can Use Social Media to Power Social Networks for Change

<http://beth.typepad.com/>

Social Media Policies Examples (for-profit) – Mashable.com

<http://inboundzombie.johnhaydon.com/wp-content/uploads/2009/10/3-Examples-of-a-Social-Media-Policy.pdf>

Social Networks Are Red Hot, Web Sites Are Diddlyquat – Non Profit Times

<http://www.nptimes.com/09May/news-090504-1.html>

The Future of Social Networks Lies in Shared Communities – eMarketingandCommerce.com

<http://www.emarketingandcommerce.com/story/future-social-networks-lies-shared-communities>

Social Net Fundraising - All Hype? – The Agitator

<http://www.theagitator.net/communications/social-net-fundraising-all-hype/>

Facebook Exodus – New York Times

<http://www.nytimes.com/2009/08/30/magazine/30FOB-medium-t.html>

To Nonprofits Seeking Cash, Facebook App Isn't So Green – Washington Post

<http://www.washingtonpost.com/wp-dyn/content/article/2009/04/21/AR2009042103786.html>

Four Reasons You're Not Using Social Media to Grow Your Business – Fast Company

<http://www.fastcompany.com/blog/rich-brooks/social-media-strategies-small-business/four-reasons-you-re-not-using-social-media-g>

Social Media Guide <http://mashable.com>

How To: Take Advantage of Social Media in Your E-mail Marketing

<http://mashable.com/2010/01/20/social-media-email-marketing/>

12 Common E-mail Marketing Mistakes – eMarketingandCommerce.com

<http://www.emarketingandcommerce.com/story/dirty-dozen>

E-newsletters don't work, says expert – Donor Power Blog

[http://www.donorpowerblog.com/donor\\_power\\_blog/2009/03/enewletters-dont-work-says-expert.html?utm\\_source=feedburner&utm\\_medium=feed&utm\\_campaign=Feed:+typepad/donor\\_power\\_blog+\(Donor+Power+Blog\)](http://www.donorpowerblog.com/donor_power_blog/2009/03/enewletters-dont-work-says-expert.html?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed:+typepad/donor_power_blog+(Donor+Power+Blog))

What the Web Changes about Fundraising – Donor Power Blog

[http://www.donorpowerblog.com/donor\\_power\\_blog/2009/08/what-the-web-changes-about-fundraising.html?utm\\_source=feedburner&utm\\_medium=feed&utm\\_campaign=Feed:+typepad/donor\\_power\\_blog+\(Donor+Power+Blog\)](http://www.donorpowerblog.com/donor_power_blog/2009/08/what-the-web-changes-about-fundraising.html?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed:+typepad/donor_power_blog+(Donor+Power+Blog))

10-Point Basic Website Checklist for Nonprofits—Non Profit Marketing Guide

<http://theraiser.blogspot.com/2008/04/10-point-basic-website-checklist-for.html>

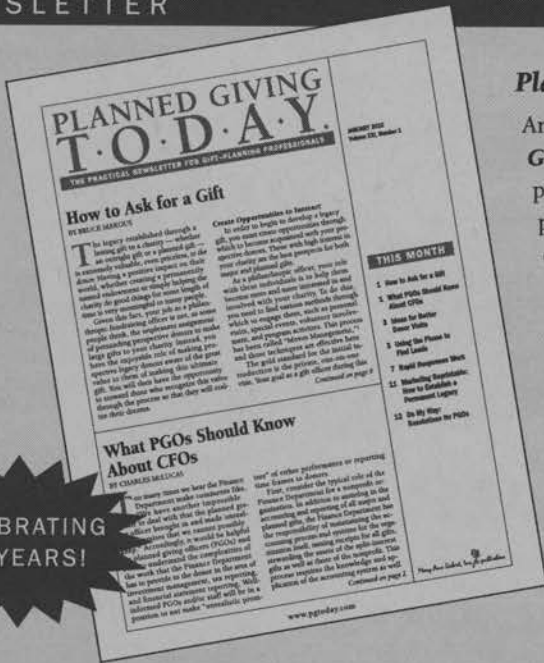
Why Social Media ROI Is A Compass And Not A Green Light

<http://johnhaydon.com/2009/02/social-media-roi-business-value/>





**NEWSLETTER**



**Planned Giving Today®**

An essential resource for gift-planning professionals, **Planned Giving Today** is the premier monthly publication serving the planned giving community, connecting readers to leading professionals in the field. This newsletter provides practical, educational information about key training events and resources, fresh marketing ideas, and valuable insights. Since 1990 **PGT** has served as a primary resource for those working in the gift-giving community and is read by more than 6,000 gift planners every month! Each issue contains a marketing "reprintable" readers can customize and print in their own publications. The distinguished editorial board includes five former presidents/chairs of National Committee on Planned Giving.

See newsletter samples at  
[www.pgtoday.com](http://www.pgtoday.com)

**REPRINTABLES**

We help gift planners enable others to give generously. Each CD is loaded with customizable reprintable marketing messages and tips designed to improve your gift-planning efforts and save you time — no royalties to pay, simply customize and use!



**PGT-MR Master Reprintables, EXPANDED!**

Updated and expanded this comprehensive CD includes the content of ALL 3 reprintable CDs plus more! PGT-MR is loaded with 220 articles, interactives, and display concepts, conveniently organized into seven categories: Gift Annuities (46); Assets (14); Bequests (47); Endowments (51); Miscellaneous (35); Planning (20); and Year-End Giving (7). The disk also includes over 100 marketing tips and nine sample response forms.



**PGT-BR Bequest Reprintables**

This CD helps gift-planners introduce one of the most popular gift vehicles: charitable bequests. It contains 40 bequest articles from PGT-MR, 19 tips on how to obtain more bequests, and a sample response form.



**PGT-AR Gift Annuities Reprintables – The NEWEST CD in our Reprintables line-up!**

This Gift Annuity CD contains 40 reprintables, including 36 marketing articles, 3 donor quizzes, and a sample letter. These brief and easy-to-read materials are geared to connect with your donor prospects and draw them toward an immediate or deferred charitable gift annuity with your organization. Simply drop in the name of your charity and use as is.



**PGT-ER Endowment Reprintables**

This CD contains 40 endowment articles that can be adapted and used, royalty-free, in your own publications. It contains 40 endowment articles from PGT-MR plus, you also receive 19 publishing tips, and a sample response form.

Visit [www.pgtoday.com](http://www.pgtoday.com) for complete information and to order Online!



## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



## **Non-Traditional Gift, Financial & Estate Planning**

Presented by:

**Cindy Sterling  
Senior Associate  
Washburn & McGoldrick, Inc.  
215 Park Avenue South, Suite 1402  
New York, NY 10003  
212-405-1616  
csterling@wash-mcg.com**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



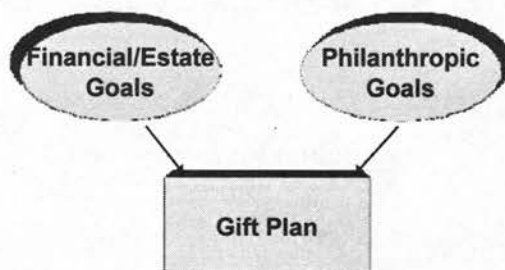
## Non-Traditional Gift, Financial and Estate Planning

**ACGA Conference  
April 29, 2010**

Cindy Sterling  
Washburn & McGoldrick, Inc.  
[csterling@wash-mcg.com](mailto:csterling@wash-mcg.com)  
212-405-1616

© Copyright by Cindy Sterling, 2010. Please do not reprint without permission.

## Planned Giving



## Definition of "Non-Traditional" Prospects

- Individuals who are not married, but create a family and share financial obligations

## Who Are Non-Traditional PG Prospects?

- Unmarried heterosexual couples
- Same-sex couples
- Non-romantic partnerships/families (sisters living together, etc.)

## Reasons Non-Traditional Prospects Are Important to PG

- Many may not have children
- Prospects without children are often our best planned giving prospects
- Focus is on bequests

## Working with Non-Traditional Prospects

- We need to be respectful of the prospect's relationship
- Be careful about making assumptions

### Financial Planning Concerns

- Income Taxes
- Estate Planning
- Retirement Planning

### Income Taxes

- Non-traditional couples can actually benefit, particularly if there is a difference in income
- A couple needs to be proactive and plan a strategy in advance

### Example: Income Requirements for Roth IRAs

- Non-traditional couples are viewed as single filers - Each qualifies if their income is less than \$120,000
- Married couples who file jointly - Qualify if their joint income is less than \$177,000

### Estate Planning is ESSENTIAL for Non-Traditional Couples

- Members **MUST have a will** to assure that their partner receives assets at their death
- Need other documents such as health care proxy, power of attorney, living will, etc.

### Estate and Gift Taxes

- Problematic areas
- No unlimited gifting between non-traditional partners – taxable event beyond annual gift tax exclusion
- No marital deduction

### 2010 Federal Estate Tax

- No Federal Estate Tax in 2010
  - ⇒ Speculation that the federal estate tax will be temporarily extended in 2010 for estates in excess \$3.5 million
  - ⇒ Under current law, federal estate tax will return in 2011 for estates larger than \$1 million with a top rate of 55%

### Estate Titling Concerns

- How a couple titles property is important
- IRS view about Joint Tenants with Right of Survivorship (JTWS)
- Need to keep track of how much each partner contributes to an asset

### Estate and Gift Tax Implications

- For wealthy individuals, plan for potential estate tax after death of the first partner
- No rollover option for surviving partner regarding retirement plans
- Life insurance is important to help pay for potential taxes

### Retirement Planning Concerns

- Non-traditional couples may not receive certain benefits a surviving spouse would
- No survivorship benefits w/social security
- Surviving partner may not receive partner's pension at death

### Retirement Plans

- Pension Protection Act
- Non-spouse beneficiary can transfer deceased owner's 401K to an IRA

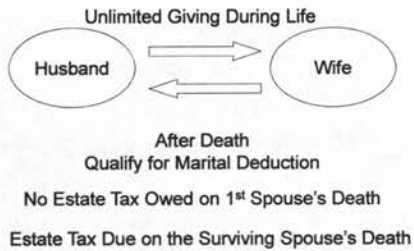
### Married Couple Example

- Sarah and Paul are both 60 and have a \$14 million joint estate. It is divided as follows:

	<u>Joint</u>	<u>Sarah</u>	<u>Paul</u>
House	\$1M		
Stock		\$5M	\$5M
Retire Plan		\$1M	\$1M
Artwork			\$1M

**Assume the Federal Estate Tax Exemption and Top Tax Bracket is the Same as 2009**

## Married Couple Benefits



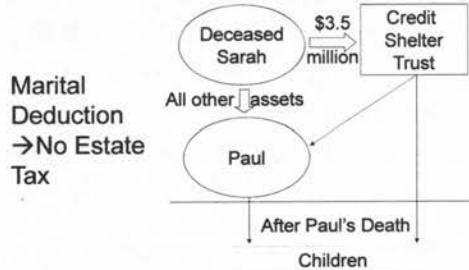
## Married Couple Example Cont.

- If Sarah dies first, her estate will be:

	<u>Joint</u>	<u>Sarah</u>
House	\$0.5	
Stock		\$5M
Retire Plan		\$1M
Total	\$0.5M	\$6M

Sarah's Total Estate Value =  
\$6.5 Million

## Possible Estate Plan for Married Couple: \$14M Joint Estate



## Married Couple Estate and Income Tax Results

- No estate tax after Sarah's death because of the Marital Deduction
- Paul can rollover Sarah's IRA to a rollover IRA.  
(He doesn't have to withdraw income until he is 70.5 years old)

## Non-Traditional Couple Example

- Sue and Sally are 60 and have a \$14 million joint estate. It is divided as follows:

	<u>Joint</u>	<u>Sue</u>	<u>Sally</u>
House (joint tenants with right of survivorship)	\$1M		
Stock		\$5M	\$5M
Retire Plan		\$1M	\$1M
Artwork			\$1M

## Non-Traditional Couple Example Cont.

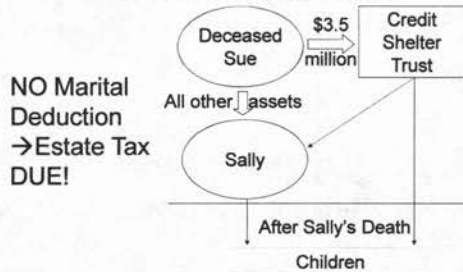
- If Sue dies first, her estate will be:

	<u>Joint</u>	<u>Sue</u>
House (JTWRS)	\$1M	
Stock		\$5M
Retire Plan		\$1M
Total	\$1M	\$6M

Sue's Total Estate = \$7M



**Possible Non-Traditional Estate Plan:  
\$14M Joint Estate**



**Non-Traditional Couple Results**

- Full value of house is included in Sue's estate unless Sally can prove she contributed to the house's purchase
- Estate tax at Sue's death – estimated at \$1,575,000 (2009 Federal Estate Tax)
- Sally cannot rollover the IRA. She will need to start withdrawing income and pay tax on the distribution.

**Non-Traditional Couple Federal Estate Tax Results**

- Various Levels of Federal Estate Tax

<u>Year</u>	<u>Estimated Tax</u>
2009	\$1,575,000
2010	\$ - 0 -
2011	\$3,145,000

**Comparison of Married and Unmarried Couples**

- Married - NO estate at Sarah's death. Paul can rollover Sarah's IRA and pay no immediate income tax. He can defer his withdrawal until he is 70.5 years old
- Non-traditional – At her death, Sue's estate faces the estate tax. Sally also incurs income tax when she receives income from the IRA.

**Charitable Gift Planning Options**



**Charitable Gift Annuity for Non-Traditional Couples**

- Warning: If a donor contributes to a CGA and names the partner as the income beneficiary ...
  - ⇒ Appreciated securities require donor to recognize capital gain
  - ⇒ Gift tax on the PV of the income stream if over \$13,000 (2010)
  - ⇒ Deferred Annuities do not qualify for annual exclusion

### Charitable Gift Planning for Non-Traditional Couples

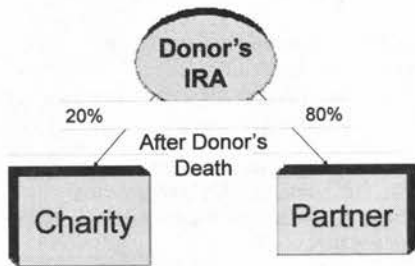
- Retirement & Estate Planning Concern – Provide income to the surviving partner and reduce taxes
- Want to provide for a charity
  - ⇒ Use retirement plans as an asset to give at death

### Most Tax Efficient Way to Make a Charitable Estate Gift

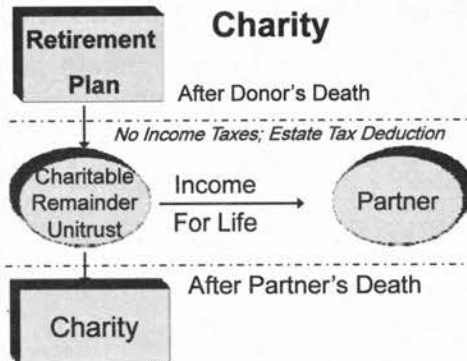
- Give the most highly taxed asset to charity –
- Give the least taxed asset to Family

**Highly Taxed Asset:  
Retirement Plans**

### Give IRA to Partner and Charity



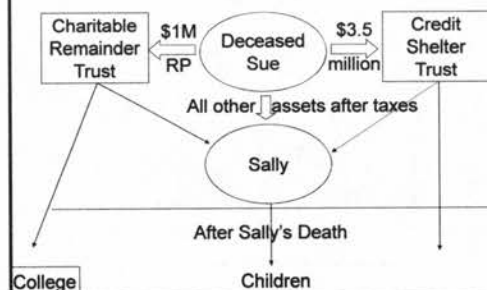
### Provide for Partner and Charity



### Sue and Sally's Estate Planning with a Charitable Gift

- Assume Sue wants to support her college alma mater and provide for Sally. She decides to name a CRT as the beneficiary of her retirement plan that will then pay income to Sally for life.

### Possible Estate Plan



### Sue's Estate Plan:

#### Give IRA to a 5% Charitable Remainder Unitrust\*

##### Financial Advantages

- Income is \$50,000 ( $\$1,000,000 \times 5\%$ ) in the first year
- Avoid immediate income tax
- Sue's estate receives \$383,410 charitable deduction\*

\* Assumes a 3.4% discount rate

### Things to Remember When Working with Non-Traditional Families

- Respect the relationship – do not make assumptions
- Non-traditional couples **NEED** to make estate plans to protect one another

### Things to Remember When Working with Non-Traditional Families Cont.

- Estate and retirement planning are more challenging
- Due to tax laws and demographics, testamentary gift arrangements may be the most attractive to non-traditional donors

### Resources: Websites

- [www.nolo.com](http://www.nolo.com)
- [www.agingwithdignity.org](http://www.agingwithdignity.org)
- [www.lambdalegal.com](http://www.lambdalegal.com)
- [www.unmarried.org](http://www.unmarried.org)
- [www.atmp.org](http://www.atmp.org)
- [www.prideplanners.org](http://www.prideplanners.org)

### Resources: Books

- *4 Steps to Financial Security for Lesbian & Gay Couples*, by Harold Lustig (Random House Publication Group)
- *Personal Financial Planning for Gays & Lesbians*, by Peter Berkery (Irwin Professional Publishing)
- *JK Lasser's Gay Finances in a Straight World*, by Peter Berkery (JK Lasser)
- *Money Without Matrimony: The Unmarried Couple's Guide to Financial Security*, by Sheryl Garrett & Debra Neiman (Dearborn)



Every channel. One vendor.



## Are you speaking your donors' language?

From eMarketing to younger donors to cultivating long-term loyalty with newsletters, postcards, and Web sites, our experienced marketing consultants will work with you to develop an integrated marketing communications strategy that will enable your direct mail and internet campaigns to work together to achieve a combined enhanced effect. Reach your donors at their mailboxes, their desktops, and everywhere in between with just one vendor: **Pentera**.

317-875-0910 | [www.pentera.com](http://www.pentera.com) | [info@pentera.com](mailto:info@pentera.com)



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# Dead Men Do Tell Tales: Integrating Bequest Administration with Your Planned Giving Program

Presented by:

Andrew Fussner  
VP - Estate Settlement  
American Heart Association  
AHA - National Bequest Center  
PO Box 22035  
St. Petersburg, FL 33742  
(727) 563-8050  
andrew.fussner@heart.org

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 www.acga-web.org acga@acga-web.org





## **Integrating Bequest Administration with Your PG Program: Dead Men Do Tell Tales**

### Introduction

We often think of the “planned giving process” as a linear progression. You identify a prospect. You cultivate the prospect. You assist the prospect in creating the planned gift. You then steward the donor until he or she passes away. Then the donor’s estate or trust is administered and once that is complete, the charity receives its ultimate distribution (as its just reward for your diligent work over the years with the donor). That’s the end of the story, because as we all know, dead men don’t tell tales. But what if they did?

What if our deceased donors “kept on giving” after death? Maybe they would provide us with future leads, tell us about the effectiveness of our planned giving efforts and point us in the direction of other donors. If you aren’t listening to what your bequest administration/estate settlement process is saying – you might be missing out on some opportunities to improve your PG program.

Bequest Administration or Estate Settlement is defined here as the business operations process of overseeing the handling and ultimate distribution of funds from a decedent’s estate, trust or other estate planning vehicle. Depending on the size of your organization, this function might be carried out by very different people – with very different goals in mind.

For smaller organizations, it is often the PG Director’s job not only to work with living donors to secure planned gift commitments, but also to handle the administration of bequests from the deceased. Because of this dual role, these folks are often best positioned to “complete the circle” between PG and Bequest Administration. However, they might also be so busy and crunched for time that they see right past what’s sitting directly in front of them.

For mid-size organizations, it is often someone in the Finance Department that handles bequest administration. These folks are good at collecting funds, but are they also collecting important information that PG Directors can use? Are your planned gifts dropping into the “black hole of accounting” once the donor is deceased – never to be heard from again? Finance staff may be sitting on some great information, but if PG and Finance staff don’t interact regularly, that information may stay hidden away forever.

Larger organizations may actually have a Bequest Administration Department or at least a person dedicated solely to bequest administration. These folks are the most likely to have gathered a wealth of information, but they still may be siloed from the PG Department depending on the reporting structure of the charity.

**The one thing charities of all size have in common is that information culled from Bequest Administration SHOULD be part of a feedback loop to staff in the PG Department. It’s just knowing what to ask for and setting up the mechanics of getting it that can muck up the process.**

This presentation will discuss ten ways that a charity's bequest administration should be integrating with its planned giving department. Your charity may already be doing many of these things – either formally or informally. None of these items are particularly earth-shattering or require a background in rocket science to implement.

Below you will find a list of ten integration ideas along with a few comments about each. We'll discuss each in more detail during the presentation – so I've left some space for notes or additional ideas/tweaks to these approaches.

### Ten Ideas for Integration

#### **1. Family/Friend Condolence Letters**

- Ask attorney/executor for name and address of proper parties to contact (keep in mind there may be situations where such a letter isn't appropriate). Keep an especially keen eye for surviving spouses and siblings.
- Should be sent as soon as the charity is informed of the bequest – don't wait until final distribution (as this could be years down the road).
- Don't reference actual dollar amount received in your letter – just say thanks for the bequest gift (and definitely don't ask for an additional donation).

#### **2. Attorney/Trustee Leads & Contacts**

- Look for attorneys that have handled multiple estates (maybe he/she is actually suggesting your charity to his/her clients or has some personal stake in your charity).
- Provide PG officers with contact information AFTER the estate has closed (this avoids confusion regarding to whom the attorney/trustee should be sending bequest-related information to).
- PG officer can thank attorney and provide suggested wording/information about the charity at the same time.

#### **3. Talking to Direct Mail – Removing the Dead**

- Obtain last known address of decedent (keep in mind the address on the death certificate may be a nursing home or some other final care facility) and have those donors removed from your direct mail lists and marked as deceased in any donor database.
- Match bequest gifts with direct mail donations to spot trends (age, gender, other types of gifts made, receiving PG mailing, etc.).

#### **4. Data Collection for PG Marketing**

- Determining who your bequest donors are (tracking date of last will, age at death, geographic location, gift restrictions, average gift size, etc.)
- Determining who your competition is (# of other charities in estate, does one charity turn up repeatedly? Maybe it's worth comparing notes with them or collaborating)
- Matching other organization contacts (direct mail gifts, special event gifts, volunteers, etc.) with matured bequests

#### **5. Stewarding split-interest trusts, perpetual trusts, and community foundation funds**

- Beneficiaries of these trusts might be good prospects in and of themselves. Plus, sometimes these beneficiaries don't "need" their distributions and might be willing to either terminate the trust early or use their distribution to fund a CGA or make an outright gift.
- Beneficiaries often have principal invasion powers, appointment powers or the power to change charitable beneficiaries (so you want to be in their good graces in order to maximize your charity's gift).
- Some trusts have granted discretionary powers for additional distributions to be made and/or a certain percentage of the annual distribution is at the trustee's discretion. Work to maximize your piece of the pie.

#### **6. PG Accountability**

- Matching known PG Commitments with matured bequests (determine how long it takes a typical donor commitment to come to fruition; are you collecting more or less than the commitment estimates; are donors who are stewarded leaving bigger bequests than non-stewarded decedents, etc.).
- Double checking on deceased PG Donors for bequests (determine if you've got PG Commitments that haven't turned into bequests and figure out why – insolvent estate, change of document, executor embezzlement; undue influence by individual, no gift to begin with, etc.).

#### **7. Listing Bequest in the Annual Report**

- Good way to recognize estate/trust. A listing or mention in an annual report might spur others to consider giving this way. Trusts with discretionary funds or surviving spouses are particularly important to recognize.
- Be sure to ask permission or have an opt out method

## **8. Special Recognition of Decedents**

- Marketing and media follow-up for matured bequests. This can be especially useful in smaller media markets or used in conjunction with cultivation pieces.
- Naming opportunities. Even if something isn't being named per se because of the bequest or was funded directly because of the bequest, the bequest can be used to promote your cause in a given geographic area (e.g. funding of research grant at local university example).
- Dedication moment at special events (such as galas or walks – again puts the idea of bequests in people's heads).
- Memory Book (donor stories and pictures; gives loved ones the opportunity to share the donor's story and/or ensures that their legacy is remembered).

## **9. Tying bequests in with memorial gifts**

- Enlarging endowments (explore the idea with family members to combine the bequest funds and memorial gifts in honor of the decedent [and maybe some additional funds from the family] to create a named endowment in honor of the deceased).
- Using memorial gifts as leads (look for spouses or siblings in particular or someone who may have done more than simply given).

## **10. Get to know your bequest administrator/finance person who handles bequests**

- Discuss how to handle suggested wording calls (this person is just as likely to have these types of calls directed to them as you – maybe more because he/she will be in the office more). Make sure this person is passing along leads and informing callers about your legacy society and you as a contact/reference.
- Talk about what you do as a planned giving officer. The more this person understands what you do, the more this person can help.
- Take bequest administrators on ride along donor visit to experience planned giving up close. The more you make this person feel a part of the "PG team," the more this person will end up helping you.

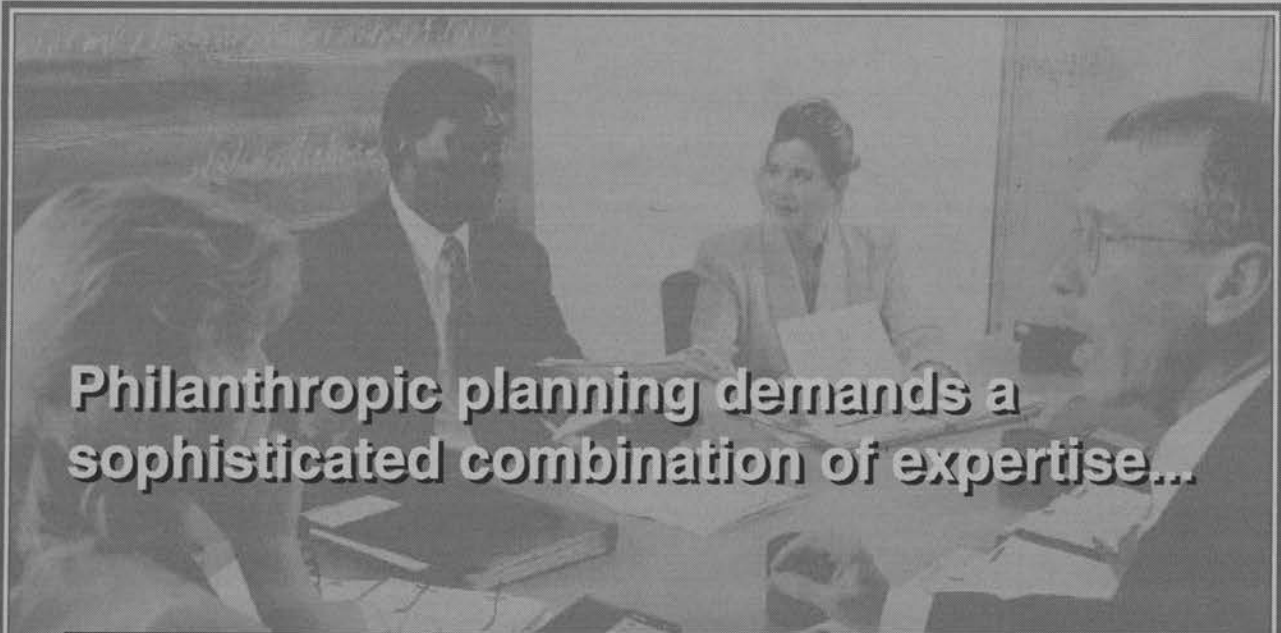
## Conclusion

No doubt you're probably doing some or many of the integration ideas listed above and most of these ideas aren't going to result in mountains of PG leads or future gift commitments. However, we all know it "only takes one big one" to make a big difference in planned giving and

you never know where it might come from. In a more and more competitive planned giving world, there's no reason not to be "completing the circle" and having your bequest administration process feed back into your planned giving program when and where it can.

**So, contrary to the famous saying – at least in planned giving –  
“Dead men DO tell tales.”**





**Philanthropic planning demands a sophisticated combination of expertise...**

- Estate Planning
- Retirement Planning
- Insurance Planning
- Investment Planning
- Tax Planning
- Elder Law and Aging Issues
- Business Succession Planning
- Family Values Discussions

When your donors need help to make wise philanthropic decisions, the Partnership for Philanthropic Planning is your resource for information and networking.

To learn more and become a member,  
visit [www.pppnet.org](http://www.pppnet.org).







## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# Retirement Plan Gifts: Better Now or Later?

Presented by:

Timothy J. Prosser  
Vice President, Institutional Trust Consulting  
TIAA-CREF Trust Co., FSB  
One Metropolitan Square, Suite 1000  
St. Louis, MO 63102  
314-244-5028  
tprosser@tiaa-cref.org

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)

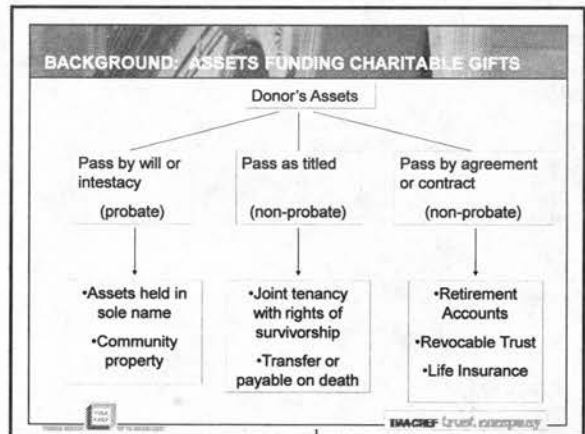


**TIAA-CREF trust company**

**Retirement Plan Gifts: Better Now or Later?**

29<sup>th</sup> Conference on Gift Annuities  
April 29, 2010  
New Orleans, Louisiana

Timothy J. Prosser  
Vice President -  
Institutional Trust Consulting  
TIAA-CREF Trust Company, FSB

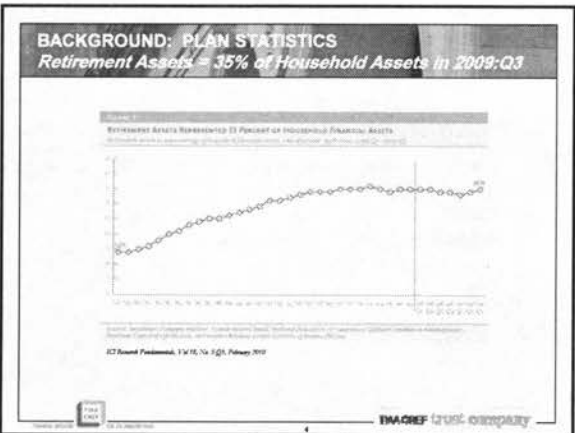


**BACKGROUND: IMPORTANCE OF RETIREMENT ASSETS AS GIFT SOURCE**

Recent statistics demonstrate continued growth of U.S. retirement plan assets:

- in dollars
- as a percentage of household assets

IRA assets continue to be a large portion of the retirement market



**BACKGROUND: PLAN STATISTICS**  
*Assets by Plan Type - 2009: Q3*

Plan Type	Trillions of Dollars
Annuities	1.5
Defined Contribution	3.9
Private Defined Benefit	2.1
Government Pension Plans	3.9
IRA	4.1
<b>Total</b>	<b>15.6</b>

IRA assets = 24.6% of U.S. retirement assets as of 2009: Q3

Investment Company Institute, February 2010

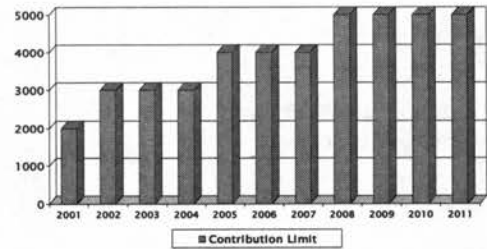
**BACKGROUND: RECENT LEGAL DEVELOPMENTS**

- . EGTRRA increases in plan funding limits
- . Required minimum distribution rules



THACHEF trust.comptax

**EGTRRA INCREASES IN PLAN FUNDING LIMITS**  
*Traditional IRAs*



THACHEF trust.comptax

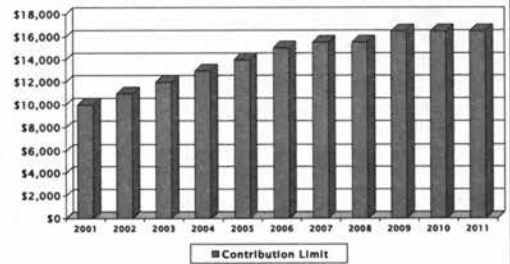
**EGTRRA INCREASES IN PLAN FUNDING LIMITS**  
*IRA Catch-up Provisions*

- . Available to taxpayers aged 50 and older
- . Accumulate greater amounts for retirement at an accelerated schedule
- . Contribute catch-up amounts in addition to the regular IRA contribution limits
  - \$500 (tax years 2002-2005)
  - \$1,000 (tax years 2006 and thereafter)



THACHEF trust.comptax

**EGTRRA INCREASES IN PLAN FUNDING LIMITS**  
*401(k), 403(b), and 457 Plan Limits*



THACHEF trust.comptax

**EGTRRA INCREASES IN PLAN FUNDING LIMITS**  
*401(k), 403(b), and 457 Catch-Up Limits*

- . 2002.....\$1,000
- . 2003.....\$2,000
- . 2004.....\$3,000
- . 2005.....\$4,000
- . 2006 & thereafter...\$5,000 indexed (\$5,500 for 2010)

*Available to taxpayers aged 50 and older*



THACHEF trust.comptax

**REQUIRED MINIMUM DISTRIBUTION RULES**

IRS regulations under Code 401(a)(9) for distributions from a retirement plan:

- . Lifetime distributions calculated under one Uniform Table for nearly everyone\*
- . "Designated beneficiary" determined as of September 30 of year following year of death (not RBD)
- . Charitable gifts of retirement assets at death made easier

\*RMD Holiday in 2009



THACHEF trust.comptax

## BACKGROUND – TESTAMENTARY vs. LIFETIME GIFTS

### Dichotomy of Testamentary vs. Lifetime Gifts

- Testamentary Gifts traditionally seen as:
  - Easy
  - Flexible
  - Tax-effective (income and estate taxes)
- Lifetime Gifts traditionally seen as:
  - Inconvenient
  - Irrevocable
  - Tax-ineffective (ordinary income and excise taxes)



11

TWACREP trust.competency

## BACKGROUND – TESTAMENTARY vs. LIFETIME GIFTS

### Rule of Thumb:

- Best charitable bequest gift is a retirement plan
  - Carries out taxable income, but charity is tax exempt
  - Estate tax charitable deduction
  - Easy gift to make (beneficiary designation)
  - Flexible for donor (retain control during life)
- Best lifetime charitable gift is appreciated stock or appreciated real estate
  - Fair market value IT deduction
  - Avoid capital gain



12

TWACREP trust.competency

## BACKGROUND – TESTAMENTARY vs. LIFETIME GIFTS

### Rule of Thumb (pt. 2):

- Lifetime gifts of retirement assets are not practical since withdrawal from qualified plan or IRA produces taxable income for the donor
  - Large gifts exceed AGI limits
  - Non-itemizers recognize income, but get no deduction
  - Increased AGI from withdrawals reduces other deductions
- No direct transfer from qualified retirement plan to charity possible under current law
- Limited directed transfer possible from IRA to charity . . .



13

TWACREP trust.competency

## TODAY'S DISCUSSION

- Lifetime gifts of retirement plan assets
  - Quick overview of IRA "Charitable Rollover"
- Testamentary gifts of retirement plan assets
  - Donor Considerations
    - Tax aspects of retirement plans and gifts to charity
    - Plan-specific issues
  - Planned giving techniques for retirement assets
    - New "income ordering" regs - a trap for the unwary?



14

TWACREP trust.competency

## EMERGENCY ECONOMIC STABILIZATION ACT *Extended Limited IRA Charitable Rollover thru 2009, Only*

IRA charitable rollover extended through 2009, only; ("Public Good IRA Rollover Act," S. 864 and H.R. 1250, would extend through 2010)

### Highlights:

Qualified Charitable Distributions (QCD) excluded from donor's taxable income

- IRA and Roth IRA accounts, only
- Up to \$100,000 per year per taxpayer
- Account owner age 70½ or older on the date of contribution
- Distribution directly from IRA account to charity



15

TWACREP trust.competency

## EMERGENCY ECONOMIC STABILIZATION ACT *Extended Limited IRA Charitable Rollover thru 2009, Only*

Qualified charitable distributions (QCD) excluded from donor's taxable income:

- To public charity or conduit foundation (§170(b)(1)(A))
  - not to donor-advised fund
  - not to private foundation (non-operating)
  - not to supporting organization
- Outright, fully charitable gift, only
  - no split-interest gift/no quid pro quo
  - donor must obtain written acknowledgement

QCD counts toward donor's Required Minimum Distribution from IRA Account



16

TWACREP trust.competency

## WHAT IS THE REQUIRED MINIMUM DISTRIBUTION?

Beginning the calendar year following the year in which the participant reaches 70½, must begin to withdraw required minimum distribution (RMD).

RMD = Account Balance divided by distribution period (life expectancy) associated with account holder's age



## WHAT IS THE REQUIRED MINIMUM DISTRIBUTION?

### Uniform Life Table (excerpt)

Applies to all unless sole beneficiary is a spouse who is more than 10 years younger.  
Treas. Regs. § 1.401(a)(9)-9 Q&A 2.

Account Owner's Age	Distribution Period	Account Owner's Age	Distribution Period	Account Owner's Age	Distribution Period
70	27.4	80	18.7	90	11.4
71	26.5	81	17.9	91	10.8
72	25.6	82	17.1	92	10.2
73	24.7	83	16.3	93	9.6
74	23.8	84	15.5	94	9.1
75	22.9	85	14.8	95	8.6
76	22	86	14.1	96	8.1
77	21.2	87	13.4	97	7.6
78	20.3	88	12.7	98	7.1
79	19.5	89	12	99	6.7



## WHAT IS THE REQUIRED MINIMUM DISTRIBUTION?

### Example #1:

Maria has \$500,000 in her IRA account on December 31, 2007. She will be 80 at the end of 2008. She must receive at least \$26,738 (\$500,000 divided by 18.7 year distribution period for an 80-year-old) during 2008.



## WHAT IS THE REQUIRED MINIMUM DISTRIBUTION?

### Example #2:

Maria has \$300,000 in her IRA account on December 31, 2009. She will be 82 at the end of 2010. She must receive at least \$17,543 (\$300,000 divided by 17.1 year distribution period for an 82-year-old) during 2010.



## WHICH DONORS BENEFIT THE MOST FROM IRA CHARITABLE ROLLOVER?

- Donors who do not itemize
- Donors subject to AGI limitations
- Donors who want to make large gifts and don't have other assets
- Donors who don't want / need RMD\*

\*CAVEAT: Reduced account values = reduced RMD



## TECHNICAL ISSUES – IRS GUIDANCE

Notice 2007-7; 2007-5 IRB 1 (January 10, 2007):

- Inherited IRAs are eligible for QCD, so long as beneficiary is age 70½
- QCD to satisfy *outstanding pledge* is not a prohibited transaction
- QCD is *not subject to withholding* (QCD request is deemed election not to withhold)

2006 Form 1040 Instructions:

- Custodian reports *all* IRA distributions on 1099 to donor & IRS
- Donor reports "QCD" and taxable IRA distributions on Form 1040



**PARTNERSHIP FOR PHILANTHROPIC PLANNING  
RESOURCES ON THE IRA CHARITABLE ROLLOVER**

"Charitable IRA Rollover Resource Center" ([www.pppnet.org](http://www.pppnet.org))

- Legislation
- IRS publications
- Commentary and analysis
- Survey of IRA Rollover Gifts to Charity



24

IMACREF trust, incapacity

**TESTAMENTARY CHARITABLE GIFTS OF  
RETIREMENT PLAN ASSETS**



25

IMACREF trust, incapacity

**TAX ON RETIREMENT PLAN ASSETS**

Retirement assets (IRAs, qualified plan accounts, tax-deferred annuities) are "Income in Respect of a Decedent" (IRD)

- IRD is taxable income to which the decedent was entitled at death but which was not included in any previous income tax return
- (Other IRD: wages, accounts receivable, untaxed interest on bonds, etc.)



26

IMACREF trust, incapacity

**TAX ON RETIREMENT PLAN ASSETS**

Retirement assets and other IRD are:

- Included in the decedent's taxable estate and
- Subject to income tax in the hands of the recipient

Double taxation can reduce assets to beneficiaries by nearly two-thirds (even greater if GST tax)



27

IMACREF trust, incapacity

**TAX ON RETIREMENT PLAN ASSETS**

Gift of retirement assets to charity can be a solution to double taxation

- Estate tax charitable deduction is unlimited
- Charity is income tax exempt
- (Uncle Sam pays 66¢ of every dollar to charity)



28

IMACREF trust, incapacity

**OUTRIGHT GIFT TO CHARITY AT DEATH**

Beneficiary Designation Form is mechanism for gift (non-probate)\*

**EXAMPLE #1:**

Primary Beneficiary = 100% Charity

- Charity receives immediate benefit
- No estate tax on gifted assets
- Charity pays no income tax on gifted assets

\* CAVEAT: Election to annuitize benefits can prevent testamentary gift



29

IMACREF trust, incapacity

**BENEFICIARY DESIGNATION FORM IS  
MECHANISM FOR GIFT**

**EXAMPLE #2:**

Primary Beneficiary = 50% Charity / 50% Individual

- Charity must be paid by 9/30 of year following decedent's death, then individual can stretch distributions over life expectancy
- No estate tax on portion of assets passing to charity
- Charity pays no income tax on gifted assets



**BENEFICIARY DESIGNATION FORM IS  
MECHANISM FOR GIFT**

**EXAMPLE #3:**

Primary Beneficiary = 100% Individual

Contingent Beneficiary = 100% Charity

- If individual survives account owner, charity receives nothing
- Charity takes if individual *predeceases* account owner (or disclaims)
  - No estate tax on portion of assets passing to charity
  - Charity pays no income tax on gifted assets



**BENEFICIARY DESIGNATION FORM IS  
MECHANISM FOR GIFT**

**EXAMPLE #4:**

Primary Beneficiary = 100% Spouse

Contingent Beneficiary = 100% Charity

- No estate tax on assets passing to spouse (marital deduction)
- Spouse can roll over to his/her own IRA, defer distributions until RBD, name own beneficiary (could be charity)
- Charity takes now if spouse *predeceases* account owner or disclaims
  - No estate tax on portion of assets passing to charity
  - Charity pays no income tax on gifted assets



**BENEFICIARY DESIGNATION FORM IS  
MECHANISM FOR GIFT**

**EXAMPLE #5:**

Primary Beneficiary = Estate (or Trust) 100%/Estate plan leaves all or part to charity

- Problem: IRA is taxable income to estate tax or trust (compressed rates)
- Question: How to pass IRA to charity and avoid income taxation at estate or trust level?
- Answer: Fiduciary income tax charitable deduction if:
  - (1) pay charitable bequest from "gross income," and
  - (2) do so "pursuant to terms of governing instrument" IRC §642(c)



**BENEFICIARY DESIGNATION FORM IS  
MECHANISM FOR GIFT**

**EXAMPLE #5 (continued):**

Fiduciary income tax charitable deduction if:

- (1) pay charitable bequest from "gross income," and
- (2) do so "pursuant to terms of governing instrument" IRC §642(c)

- Document states that retirement assets pass specifically to charity;  
OR
- Document leaves residue (or percentage of residue) to charity and states that:  
"to the extent possible, gifts to charitable organizations shall be satisfied by distribution of property constituting income in respect of a decedent as defined under §691(a) of the IRC"



**BENEFICIARY DESIGNATION FORM IS  
MECHANISM FOR GIFT**

**EXAMPLE #5 (continued):**

**WARNING:** New proposed Treasury regulations under §642(c) of the Code state that for such an income-ordering provision under an estate or trust to be effective for tax purposes, it must have "economic effect independent of income tax consequences."





## BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

### EXAMPLE #6 :

Primary Beneficiary = Charitable Remainder Trust

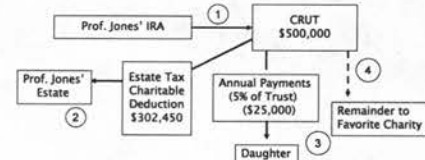
- Estate tax charitable deduction for remainder value of CRT
- CRT can provide for stream of annuity or unitrust payments to desired individual beneficiaries for life (subject to 10% minimum remainder interest rule)
- CRT payments are based on 100% of CRT value (no diminution for income tax)
- All income tax on assets are deferred until CRT payments are distributed



TIAA-CREF trust company

## EXAMPLE OF RETIREMENT ASSETS FUNDING CRT

Professor Jones names his CRUT as primary beneficiary of \$500,000 of retirement assets at his death. The CRUT provides for payments to his daughter for 10 years of 5% of the CRUT's market value, with the remainder to his favorite charity.



These amounts are calculated using 3.2% as the assumed applicable federal rate for purposes of calculating the value of the remainder interest



TIAA-CREF trust company

## RETIREMENT ASSETS TO A CRT

### Cautions:

- Is planner competent in relevant areas of the law? (*Estate tax, Income tax, ERISA, Retirement distributions, and CRTs*)
- No marital deduction if non-spouse income beneficiary
- No discretionary access to trust property (*Shouldn't be sole source of family support*)
- In large estate subject to estate tax, stretch IRA may produce better tax result (*691(c) deduction*)



TIAA-CREF trust company



## TIAA-CREF trust company

### Retirement Plan Gifts: Better Now or Later?

Timothy J. Proesser  
Vice President - Institutional Trust Consulting  
TIAA-CREF Trust Company, FSB

TIAA-CREF Trust Company, FSB provides trust services. Investment products are not insured by the FDIC, are not deposits or other obligations of TIAA-CREF Trust Company, FSB, and are not guaranteed by TIAA-CREF Trust Company, FSB, and are subject to investment risk, including possible loss of principal invested. Neither TIAA-CREF nor its affiliates provide legal or tax advice. This presentation is for educational purposes only and addresses a complex topic. Because it does not address many of the nuances of estate and tax law - both federal and state - and because these laws are continually being revised, we urge you to seek the advice of your own attorney, tax advisor, or accountant regarding your particular situation.  
©2009 TIAA-CREF Trust Company, FSB, One Metropolitan Square, 211 North Wackerley, St. Louis, Missouri 63102  
040602



TIAA-CREF trust company





## Keep Your Gift Annuity Program In Tune

Unpredictable investment returns and donor longevity can exhaust reserves and cause discord in a Charitable Gift Annuity program – especially if risk management isn't your specialty. A group annuity from United of Omaha Life Insurance Company can help restore harmony.

Learn how our *Solutions for Gift Annuity Programs* enable you to transfer both investment and longevity risk to us – a highly rated insurer with more than 45 years of annuity experience.

Julie Engel AAPA  
(800) 843-2455 ext. 5810  
[Julie.Engel@mutualofomaha.com](mailto:Julie.Engel@mutualofomaha.com)

THE POWER OF  
**Giving**

[mutualofomaha.com/giftannuity](http://mutualofomaha.com/giftannuity)

*United of Omaha Life Insurance Company, Mutual of Omaha Plaza, Omaha, NE 68175 is an affiliate of Mutual of Omaha Insurance Company. United of Omaha Life Insurance Company accepts full responsibility for all of United's contractual obligations under its group annuity contract (Form 504-GANC-03). No financial liability will be incurred by the parent or affiliate companies for business transacted by United of Omaha Life Insurance Company. Unless otherwise required by state law, United of Omaha's obligations under its contract are to the charity, as the owner of the contract, and not to individual donors. Charities are solely responsible for determining their reserve fund requirements in the state(s) in which they sell charitable gift annuities. Available for use in all states except NY and OR. MUGC9035*



**Mutual of Omaha**





*Lawyers for the 21st Century®* | [www.msk.com](http://www.msk.com)

MITCHELL SILBERBERG & KNUPP LLP

AND PARTNER

DAVID WHEELER NEWMAN  
CHAIR, MS&K CHARITABLE SECTOR PRACTICE

ARE PLEASED TO SUPPORT

THE ACGA CONFERENCE ON  
GIFT ANNUITIES

LOS ANGELES • NEW YORK • WASHINGTON, D.C.



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# Investing Charitable Gift Annuity Pool Assets

Presented by:

Damon L. Whelchel  
Associate Director of Investments  
Kaspick & Company  
203 Redwood Shores Parkway  
Suite 300  
Redwood Shores, CA 94065-1175  
650-585-4100  
dwhelchel@kaspick.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)





## Investing Charitable Gift Annuity Pool Assets

2010 ACGA  
29<sup>th</sup> Conference on Gift Annuities

Damon L. Whelchel, CFA  
Director, Investment Management

## Background

## Topics

- Background
  - Assumptions behind ACGA rates
  - Implications of regulatory environment for investment of gift annuity assets
- Risks of issuing annuities
- Risk review process
  - Assess the risk of your pool
  - Investment planning steps
  - Stress test your plan
  - Policy implications

## What is a Gift Annuity?

- A simple contract between the charity and the donor
- Assets belong to the charity (not a trust)
- Runs for one or two lives (never a term of years)
- Payments are fixed (they can be deferred) and are a general liability of the charity
- Taxation of the payments is determined at the outset
- Annuitant receives a 1099-R in January (not a K-1)
- Regulated in many states

## Not Topics

- State regulation of gift annuities (other than investment issues)
- Legal and regulatory risks
- Marketing gift annuities
- Administration and stewardship issues
- Reinsurance

## Gift Annuities: An Important Source of Funds

- The median percentage of all gifts received as gift annuities in 2008 was 72.1%; the highest reported value since we began tracking statistics (1998)
- In 2008 and 2009, our clients issued 31 gift annuities over \$500,000; 11 of these were \$1,000,000 or more

### Sample Gift Annuity Rates Effective February 1, 2009

Age(s)	One-Life	Two-Life
55/55	4.8%	4.1%
60/60	5.0	4.6
65/65	5.3	4.9
70/70	5.7	5.2
75/75	6.3	5.6
80/80	7.1	6.1
85/85	8.1	7.0
90/90	9.5	8.3

Page 6

Keefe & Connors

### State Investment Restrictions

State	Investment Restrictions
CA	Maximum 50% in equities (or mutual funds)
FL	Maximum 50% in common and preferred stocks
MD	Prudent Investor Rule
NJ	Prudent Investor Rule
NY	Prudent Investor Rule
TN	Prudent Investor Rule
WA	Prudent Investor Rule
WI	Prudent Investor Rule

Page 9

Keefe & Connors

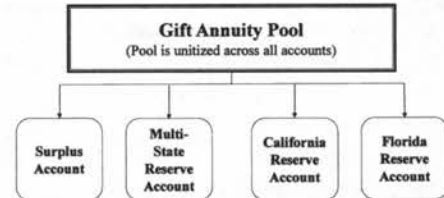
### Assumptions Behind the ACGA Gift Annuity Rate Tables

- Residuum: 50% of the gift in nominal dollars
  - Policy: Invest 100% of the gift
  - Total Return: 5.25% per year
  - Expenses: 1.0% per year
  - Mortality: Annuity 2000 Tables and all annuitants are assumed to be female and 2.0 years younger than their actual ages

Page 7

Keefe & Connors

### GAP Account Structure—Registered



Page 10

Keefe & Connors

### Historical Gift Annuity Rates 75 Year Old Donor

Year	ACGA Rate
1965	6.5%
1974	7.4
1980	7.9
1992	8.5
1999	8.2
2002	7.9
Today	7.3

Page 8

Keefe & Connors

### Example: What is the Maximum Amount You Can Invest in Equities?

Account	Equities		Fixed Income		Total
	(\$)	(%)	(\$)	(%)	(\$)
CA Reserve	\$913,826	50%	\$913,826	50%	\$1,827,652
FL Reserve	\$30,155	50%	\$30,155	50%	\$60,310
Multi-state Reserve	\$2,122,807	82%	\$475,133	12%	\$2,597,940
Surplus	\$466,260	95%	\$24,540	5%	\$490,800
<b>Total</b>	<b>\$3,533,048</b>	<b>71%</b>	<b>\$1,433,654</b>	<b>29%</b>	<b>\$4,976,702</b>

Page 11

Keefe & Connors

## Risks of Issuing Annuities

Page 12

Kemper & Company

## Risks *Within* the Charity's Control

- Issuing gift annuities at rates higher than ACGA rates
- Spending any portion of the gift before termination
- Accepting restricted gifts
- Accepting illiquid assets such as real estate without adequate review
- Writing very large gift annuities or many annuities for one annuitant
- Paying too much for related services

Page 13

Kemper & Company

## Negative Outcomes

- Annuity contract runs out of money and the charity must continue to make payments to the annuitant(s) from institutional funds
- The residuum is substantially below expectations and cannot fund the donor's objective, e.g., to fund a named scholarship

Page 13

Kemper & Company

## Risk Review Process

Page 16

Kemper & Company

## Risks *Outside* the Charity's Control

- Donors live longer than expected
- Market returns are below average
- Portfolio experiences a prolonged market downturn
- Investment manager produces poor results

Page 14

Kemper & Company

## Risk Review Process

Assess the risk of your gift annuity pool

Stress test your investment plan

Investment planning steps

Revisit your gift acceptance policies and practices

Page 17

Kemper & Company

## Risk Assessment

---

- What is the general health of the pool?
- Have any contracts run dry?
- Are there any individual contracts that look troubled and need further analysis?

Page 18

Korn & Chanoff

## Calculate the Effective Payout Rate (EPR)

---

$$\text{EPR} = \frac{\text{total annuity payments}}{\text{total market value of gift annuity pool}}$$

Page 21

Korn & Chanoff

## Collect Data About Each Contract

---

- Gift date
- Gift amount
- Current market value
- Payout % and annual payment (\$)
- If deferred, the date of the first payment
- Horizon
- Designation: restricted or unrestricted
- FASB liability

Page 19

Korn & Chanoff

## Example: Effective Payout Rate of 8.9%...

---

- The gift annuity pool has an effective payout rate of 8.9% and a weighted average horizon of 9.7 years
- A 9.7 year horizon equates to an 81 year old annuitant
- You would offer an 81 year old donor a gift annuity rate of 7.3%

This pool's effective payout rate is 1.6% higher than what a new donor would receive

Page 22

Korn & Chanoff

## Do Some Analysis — The Pool

---

1. Calculate the total market value of the pool and compare it to the pool's total gift value
2. Calculate the pool's effective payout rate and weighted-average horizon; identify the age associated with that horizon; determine the gift annuity rate for that age and compare it to your effective payout rate

Page 20

Korn & Chanoff

## Do Some Analysis — Contracts

---

1. Identify contracts that have already run dry

Page 23

Korn & Chanoff

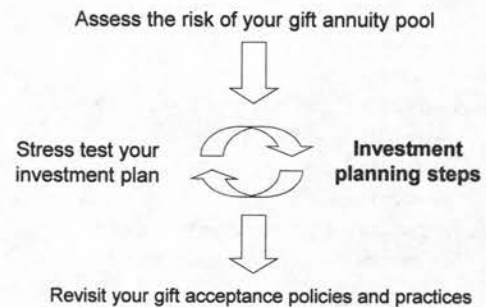
## Identify Contracts That Have Run Dry

- Determine what happened
  - Poor investment returns?
  - Very old annuitant?
  - Funding asset issue?
  - Contract written at a rate higher than the ACGA rate?

Page 24

KAPPA & COMPANY

## Risk Review Process



Page 27

KAPPA & COMPANY

## Do Some Analysis — Contracts

1. Identify contracts that have already run dry
2. Identify contracts for further analysis

Page 25

KAPPA & COMPANY

## Investment Planning Process

- Determine your return and risk objectives
- Choose an appropriate stock/bond mix
- Hedge against economic disasters
- Select diversifying asset classes
- Select managers/mutual funds
- Establish rebalance procedures
- Codify your investment policies

Page 28

KAPPA & COMPANY

## Identify Contracts for Further Analysis

- Contracts with future values that suggest they might run dry
- Largest contracts and largest concentrations
- Contracts established in 2007
- Contracts with liabilities that exceed their market values

Page 26

KAPPA & COMPANY

## Investment Objective: Return

Achieve your total return objective

- Earn an absolute return of 5.25%, net of fees
- Outperform your market benchmark, net of fees

Page 29

KAPPA & COMPANY

## Investment Objective: Risk

Reduce portfolio volatility and downside risk

- Hold some bonds
- Hedge against economic disasters
- Use commingled funds to diversify across:
  - asset classes
  - managers
  - securities
- Tilt the portfolio towards value stocks
- Rebalance the portfolio assiduously

Page 30

## Hold Some Stocks for Return, Some Bonds to Reduce Risk

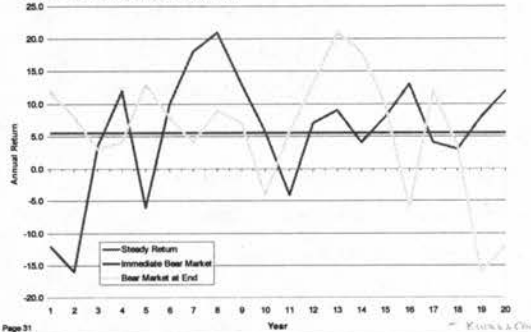
Stocks/ Bonds	AACR	Worst Year	Yrs. with a Loss	Std. Dev.
Stocks	9.8%	-43%	29%	20.5%
<b>60/40%</b>	<b>8.6</b>	<b>-27</b>	<b>23</b>	<b>12.6</b>
<b>40/60%</b>	<b>7.7</b>	<b>-19</b>	<b>19</b>	<b>9.1</b>
<b>30/70%</b>	<b>7.2</b>	<b>-15</b>	<b>14</b>	<b>7.7</b>
<b>Bonds</b>	<b>5.4</b>	<b>-6</b>	<b>13</b>	<b>6.4</b>

Note: 1926-2009, based on annual return.

Page 33

## Risk of a Down Market

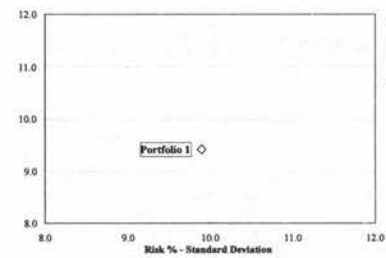
20 Year Annualized Returns of 5.25%



Page 31

## Building a Diversified Portfolio

Return % - AACR



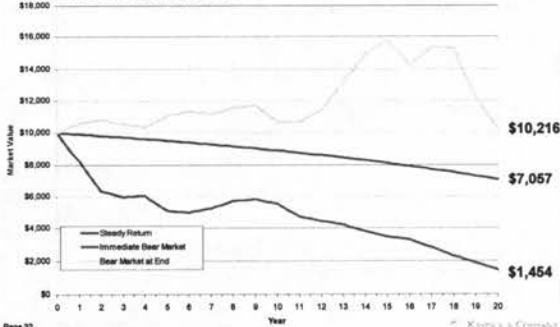
Note: 1972-2009, based on monthly returns. AACR is the average annual compound return.

Page 34

## Risk of a Down Market

20 Year 6.0% \$10,000 Gift Annuity

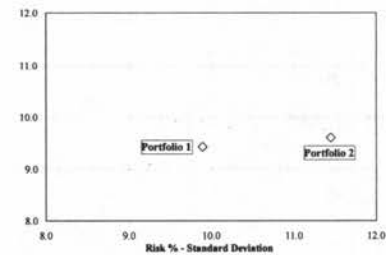
20 Year Annualized Returns of 5.25%



Page 32

## Building a Diversified Portfolio: Tilt Portfolio Towards Equities

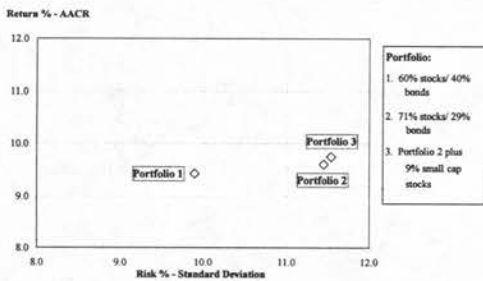
Return % - AACR



Note: 1972-2009, based on monthly returns. AACR is the average annual compound return.

Page 35

## Building a Diversified Portfolio: Add Small Cap Stocks



Note: 1972-2009, based on monthly returns. AACR is the average annual compound return.

Page 36

Kornel & Chinnici

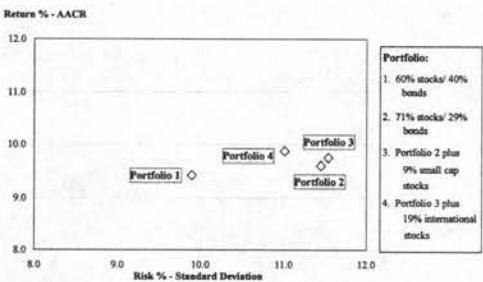
## Gift Annuity Pool Equity Allocations

- The combined commitment to equities in our CA clients' gift annuity pools:
  - Median: 63%
  - Minimum: 27%
  - Maximum: 80%

Page 39

Kornel & Chinnici

## Building a Diversified Portfolio: Add International Stocks



Note: 1972-2009, based on monthly returns. AACR is the average annual compound return.

Page 37

Kornel & Chinnici

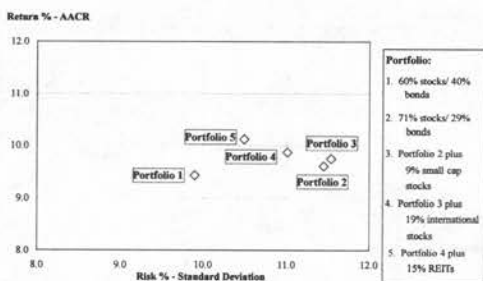
## Use Commingled Vehicles to Diversify

- Most gift annuity pools cannot meet the required minimums for separate accounts
- Diversify the gift annuity pool
  - By asset class
  - By manager
  - By security
- Access institutional managers
- Accomplish these goals by investing in funds

Page 40

Kornel & Chinnici

## Building a Diversified Portfolio: Add REITs



Note: 1972-2009, based on monthly returns. AACR is the average annual compound return.

Page 38

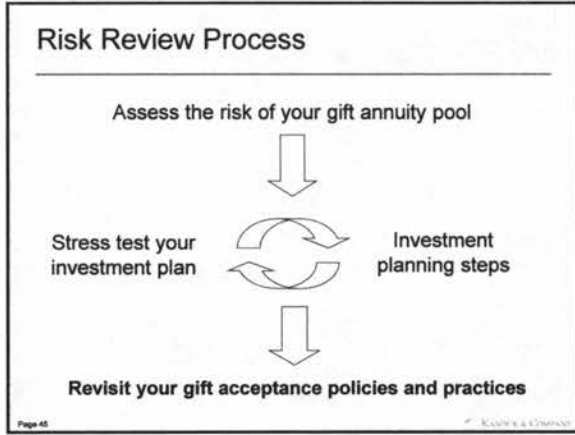
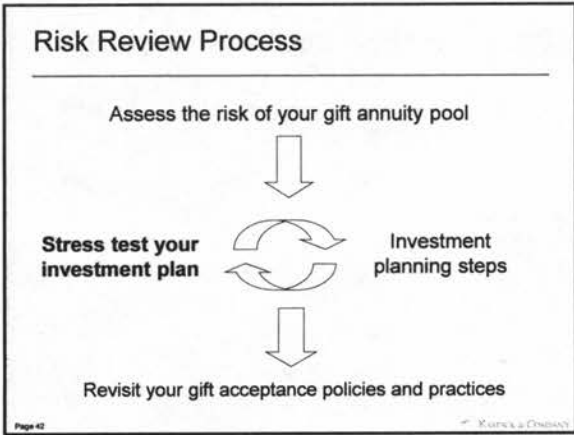
Kornel & Chinnici

## Some Investment Best Practices

- Unitize your gift annuity pool
- Promptly sell donated securities and reinvest
- Use commingled vehicles
- Closely manage cash
- Keep fees low/reasonable
- Be very disciplined about rebalancing
- Take the long view—avoid market timing
- (No credit cards)

Page 41

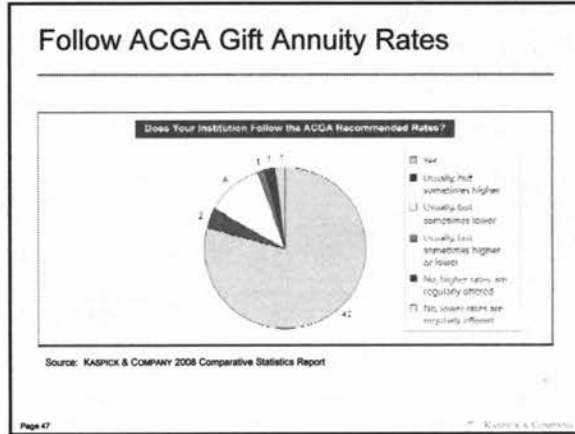
Kornel & Chinnici



- ### Run Stress Tests
- What happens to the terminal value of a contract if:
    - The contract earns your expected long-term return but the horizon is 3 years longer
    - The contract earns a constant 3% or 4% return
    - The contract experiences a down market followed by constant returns (use the performance of your stock/bond portfolio mix in 1973–1974 or 2000–2002)
- Page 43 KAPRICK & COMPANY

- ### Suggested Gift Annuity Policies
- Create a written policy statement
  - Review your policies with your Trustees and/or senior management
- Page 46 KAPRICK & COMPANY

- ### Run Stress Tests On...
- Contracts with future values that suggest they might run dry
  - Largest contracts and largest concentrations
  - Contracts established in 1998 and 1999
  - Contracts with liabilities that exceed their market values
- Page 44 KAPRICK & COMPANY





### Do Not Spend Any of the Surplus Assets Prior to Termination

- Pros for spending some now:
  - Provides current support to the charity
  - Creates an incentive to raise more gifts
- Cons for spending some now:
  - Significantly increases the risk of the pool
  - Donors might ask: Are my payments less secure?
  - Additional disclosure requirements
  - Dealing with restricted purpose annuities

Page 48

K&C Co. Advisors

### Set a Minimum Gift Amount

Minimum Amount	K&Co. Survey
\$ 5,000	9%
<b>\$10,000</b>	76
\$15,000	0
\$20,000	2
\$25,000	13

Page 51

K&C Co. Advisors

### Develop a Source for Funding Payments When Contracts Run Dry

- Other gift annuity pool assets
  - Raises the effective payout rate of the pool
  - Is it fair to the other annuitants?
- Operating funds and/or the endowment
  - Are the funds available?
  - What is the opportunity cost?
- An internal reserve fund
  - Terminating unrestricted contracts
  - "Tax" on all terminating contracts
  - "Tax" on all contracts annually

Page 49

K&C Co. Advisors

### Determine a Maximum Gift Amount

- Depends on many factors
  - Contract: rate and horizon
  - Annuitant: situation and relationship
- Size relative to the charity's
  - Gift annuity pool
  - Operating budget
  - Unrestricted endowment assets
- Large gift annuity contracts should be approved by senior management

Page 52

K&C Co. Advisors

### Set a Minimum Age

Minimum Age	K&Co. Survey
None / other	21%
50	19
55	9
60	26
<b>65</b>	23
70	2

Page 50

K&C Co. Advisors

### Determine Acceptable Funding Assets

- Cash
  - Publicly-traded securities
- } Automatically acceptable
- 
- Real estate
  - Tangible property
  - Other illiquid assets
  - Retained life estate
- } Review on a case-by-case basis

Page 53

K&C Co. Advisors

## KASPICK & COMPANY

---

Damon L. Whelchel, CFA  
Director, Investment Management

KASPICK & COMPANY  
203 Redwood Shores Parkway  
Suite 300  
Redwood Shores, CA 94065  
650-585-4100  
[www.kaspick.com](http://www.kaspick.com)

Page 54

KASPICK & COMPANY

## Resources

---

- **ACGA**  
Summary of CA Regulations  
<http://www.acga-web.org/regs/careg.html>
  
- **CA Department of Insurance**  
Home Page  
<http://www.insurance.ca.gov/>
  
- **Details on Insurance Code 11520-11524**  
<http://www.leginfo.ca.gov/cgi-bin/displaycode?section=ins&group=11001-12000&file=11520-11524>

Page 55

KASPICK & COMPANY

> Want to spend **less time worrying** about the risks and costs associated with your Charitable Gift Annuity program and **more time raising new donor gifts?**

FIND OUT HOW  
REINSURING  
YOUR GIFT ANNUITY  
PORTFOLIO  
MAY BE THE  
ANSWER.



VISIT THE METLIFE BOOTH  
IN THE EXHIBIT HALL FOR  
MORE INFORMATION ON OUR  
CHARITABLE GIFT SOLUTIONS.

**John B. Kvernland**  
Senior Sales Director  
(212) 578-4970  
[jbkvernland@metlife.com](mailto:jbkvernland@metlife.com)

**MetLife**

L0210088972[exp0211][All States][DC]



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# Reform Roulette: Recent and Upcoming Changes in the Legal and Legislative Landscape

Presented by:

Robert Harding  
Principal

Gray, Plant, Mooty, Mooty & Bennett, P.A.

500 IDS Center

80 South Eighth Street

Minneapolis, MN 55402-3796

(612) 632-3091

robert.harding@gpmlaw.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## REFORM ROULETTE:

### Recent and Upcoming Changes in the Legal and Legislative Landscape

#### I. Federal Tax Legislation

Three pieces of federal tax legislation that can have a major effect on charitable giving are currently in play: estate tax reform, the limit on the income tax charitable deduction included in President Obama's budget, and an extension of the IRA rollover statute. If Congress shocks us all and passes any of these bills before the ACGA Conference at the end of April, we will talk about the new laws and their implications. Otherwise, we will discuss how to be prepared when Congress acts, if it ever does. More important, we will explore ways to use this uncertainty as an opportunity to initiate and continue discussions with donors.

##### A. Estate Tax Repeal/Reform

###### 1. Current Law

The estate tax law currently on the books – part of the Tax Act of 2001 – will have three major effects if not superseded by new legislation:

- a. For an individual who dies during 2010, no estate tax will be imposed regardless of the size of the decedent's estate. (Oddly, the gift tax and the \$1 million gift tax exemption remain in effect for gifts made this year.)
- b. The assets of the decedent's estate will not receive a step-up in basis to their value at the date of the decedent's death. In other words, the beneficiaries of the decedent's estate take a carryover basis in the assets they receive.
- c. Beginning in 2011, the estate tax law in effect before 2001 will return:
  - i. The highest estate tax rate will go up from the 2009 rate of 45 percent to 55 percent.
  - ii. The estate tax exemption will drop from the 2009 exemption of \$3.5 million to \$1 million.

###### 2. Proposed Legislation

At last count there are at least five bills in Congress that address the fate of the federal estate tax. No major action is pending that would move any of them along. All are currently stuck in committee. They fall into three broad categories:

- a. Those that make “permanent” the 2009 top estate tax rate (45 percent) and the 2009 estate tax exemption (\$3.5 million). Some of these have additional but less important features, such as indexing of the exemption and “portability” of a decedent’s exemption so that the surviving spouse can use it.
- b. Those that would retain the estate tax but lower the top rate and increase the exemption.
- c. Those that would repeal the estate tax “permanently.”

### 3. Be Prepared

It is too soon to know how Congress will deal with the estate tax, but it is not too soon for donors to be curious and ask about the implications for charitable gifts. Therefore, it makes sense for development officers to be prepared to talk intelligently about philanthropy under each of the three alternatives: a return to the pre-2001 law, an estate tax law with current or higher exemption and current or lower top rate, and complete repeal.

- a. The return of the vampire (Tea Party jargon?)

If the pre-2001 law returns, the estate tax rate goes up, and the exemption goes down. As a result, charitable gifts that save estate tax and provide estate tax leverage will be especially attractive:

- i. Charitable lead annuity trusts: the AFR is still low, and so is the stock market. With a higher marginal rate and a lower exemption, CLATs will be even more attractive than they have been for the past couple of years.
- ii. Bequests: For a wealthy donor, more than half of every dollar in excess of the \$1 million estate tax exemption will go to the government in the form of estate tax. Thus, even for donors with medium-size estates, the cost to their children as a result of major charitable bequests will be modest.

- b. Some version of current law

The same logic holds as with pre-2001 law, but the top rate will be lower and the exemption larger, so the tax benefits of CLATs and charitable bequests will be appealing to a smaller class of donors.



c. Permanent repeal

This one is tougher.

- i. Depending on the donor's attitude toward wealth and taxes, a permanent repeal of the estate tax could make a major charitable bequest more appealing or less so. Take a look at Exhibit A.
- ii. Donors who live in states with an estate or inheritance tax still have a tax incentive to make charitable bequests. The highest state rate is typically quite a bit lower than the federal one has been, but the exemption is typically lower as well. Thus, although the tax incentive for charitable gifts will be more modest, it will still be there.
- iii. Implications of carryover basis (assuming it becomes part of permanent repeal). Testamentary CRTs will no longer be attractive from an estate tax perspective, but they will suddenly gain the same luster as lifetime CRTs for income tax purposes. A donor can leave low basis assets to a testamentary CRT, which can later sell them without immediate tax on the resulting gain.

4. Possible Conversations with Donors

Because no one yet knows what Congress will do about the estate tax, now is an ideal time for development officers to help donors explore their attitudes toward charitable giving. These discussions can be very productive, leading donors to decide to give more, not less.

a. How much is enough for the children?

- i. If Congress "permanently" repeals the federal estate tax, wealthy donors will be able to leave a much larger portion of their estates to their children, and for donors who live in states with no estate or inheritance tax, their **entire** estate. Thus, contemplating the possibility of permanent repeal leads naturally to the question, "How much is enough for the children?" As Exhibit A shows, the answer undoubtedly will be different for different donors.
- ii. Uncertainty about the estate tax also raises the question about "How much is enough for the children?" in a different way. If the estate tax continues, amounts left to the children in excess of the available exemption will go partly to the government. The "How much?" question then starts to focus on the size of the exemption. Donors may

ask themselves, “If roughly half of every dollar in excess of \$3.5 million that I leave to my children goes to the government, would I rather leave everything in excess of the exemption to charity?”

- b. How important are tax savings in motivating philanthropy?

As Exhibit A shows, without the estate tax some donors can leave more to children yet leave the same amount to charity. On the other hand, in that scenario the charitable gift “costs,” i.e., takes away from the children, more than if the estate tax were still in force.

- c. The value of discussion

Of course it is possible that this type of discussion will lead some donors to conclude that if the estate tax is repealed they wish to give less or give nothing to charity. Development officers should be discriminating in deciding when, and with which donors, a discussion of the uncertain estate tax situation will be beneficial.

## 5. A Practical Puzzle – Testamentary CRTs

Some commentators have speculated about the qualification of a testamentary CRT under the estate plan of a donor who dies while the estate tax is not in force. Suppose the Democrats decide to do nothing about the estate tax for 2010 as a negotiating strategy. Some of the wealthy individuals who die this year will have estate plans that create testamentary CRTs. Do those trusts qualify under Code Section 664? Even if they do, is there a concern about who gets the cookies when the trust ends?

- a. Will a testamentary CRT qualify under Section 664 if the donor dies while the estate tax is not in force? The Treasury Regulations define a CRT, in part, as a trust with respect to which an income, gift or estate tax deduction is allowed for the charitable remainder. With a testamentary CRT no income or gift tax deduction will be allowed, but if the estate tax is not in force at the donor’s death, an estate tax deduction won’t be allowed either. Does this mean that the trust does not qualify under Section 664 and therefore is not exempt from federal income tax? Arguably not.
  - i. The Internal Revenue Code, which trumps any Treasury Regulation, requires only that the remainder beneficiaries be described in Section 170(c), the income tax deduction section. Therefore, even if no estate tax is in effect when a donor dies, a properly drafted testamentary CRT meets this requirement.

- ii. It is hard to imagine that the IRS would cite its Regulation to disqualify a testamentary CRT of a donor who dies this year. With a properly drafted trust, there is no abuse. In addition, both Congress and the IRS are typically very conscientious about establishing transitional rules and technical corrections acts that address this type of situation and prevent a harsh result.
  - b. Prior to 2010, properly drafted testamentary CRTs have always required that the remainder beneficiary be described in Section 2055(a), the estate tax charitable deduction section. If the federal estate tax is not in effect when the donor dies, the named remainder beneficiary cannot be described in that section. The alternate remainder beneficiary clause will kick in, requiring that the remainder be distributed to another organization described in 2055(a). But there aren't any because Section 2055(a) is not in effect. Although it is unlikely that anybody will dispute the named beneficiary's right to the distribution, attorneys drafting testamentary CRTs this year may wish to include additional language that takes into account the possibility that the federal estate tax may not be in effect when the donor dies.
- 6. Another Conundrum – Zero Estate Tax Formula Clauses
  - a. A formula clause that zeros out the federal estate tax by means of the estate tax charitable deduction works this way. The estate plan of a single donor or a surviving spouse leaves the children the largest amount with respect to which there will be no federal estate tax, and leaves everything else to charity. Because of the combined effect of the estate tax exemption and the estate tax charitable deduction, no federal estate tax is imposed. If state estate or inheritance tax will also apply, the formula may have to be modified to take that into account, but if it is properly drafted, no estate tax will be due.
  - b. For donors with strong charitable tendencies, this type of estate plan has been popular, especially given the high federal estate tax exemption that has prevailed during the later years of the past decade. But how will this type of formula clause operate if the federal estate tax is not in effect when the donor dies? Because the entire estate can pass to the children without federal estate tax, the charitable residuary beneficiary would seem to get nothing. What, if anything, should charities do to address this possibility?
  - c. If a charity is aware of a living donor who has this type of estate plan in place, the charity can alert the donor to the problem and suggest that the donor have his or her attorney amend the formula

so that the charity gets the desired gift even if the estate tax is not in force. One possible solution would be an amendment to the effect that if the federal estate tax is not in effect at the donor's death, the formula is applied as if the federal estate tax law of 2009 *were* in effect. Some donors will be happy with this solution, but others may wish to give the charity less. Even so, less is better than nothing.

- d. Suppose the donor dies with this type of formula clause in place and the children are sympathetic to the donor's charitable goals. It may be possible for the charity to negotiate a settlement with the children.
- e. Suppose on the other hand that the children are unsympathetic to the donor's philanthropic plan. They may claim that the formula clause gives them everything. The courts of all states attempt to honor the intent of a decedent in disposing of his or her estate. The wording of the formula clause, the law in effect at the time it was drafted and executed, and perhaps the testimony of the drafting attorney may provide sufficient evidence of intent so that the state court will order a distribution to the charity equal to what it would have received had the estate tax been in effect at the donor's death. Charitable beneficiaries should be prepared to litigate this issue.

#### 7. State Response to Federal Uncertainty

Several state legislatures have introduced bills that address the interpretation of the estate planning documents of state residents who die while the federal estate tax is repealed. For the most part, these bills fall into two categories – the “Virginia approach” and the “Florida approach.”

- a. The Virginia approach creates a default rule for interpreting federal tax-related provisions in wills and trusts during 2010. For example, the Virginia bill, HB 775, provides that any reference in an estate planning document to the federal estate tax or the federal generation-skipping tax is deemed to refer to the relevant Code provisions in effect on December 31, 2009.
- b. The Florida approach authorizes a state court to construe the terms of an estate planning document in light of the decedent's intent and the repeal of the federal estate tax, but does not require that the interpretation assume that the decedent would have wished to follow the federal estate and GST tax laws in effect during 2009.
- c. Where a donor has died and there is no longer an opportunity to adjust the drafting to take estate tax repeal into account, a statute for the donor's state of residence that follows either approach will

go a long way toward resolving the two puzzles noted above – testamentary CRTs and zero estate tax formula clauses. The Virginia approach seems to resolve both problems conclusively. The Florida approach requires more work on the part of fiduciaries and beneficiaries to establish the decedent’s intent, but at least the Florida approach acknowledges that intent may be an issue because of the federal estate tax repeal.

## **B. President Obama’s Fiscal 2011 Budget**

The President’s budget proposal would limit the tax benefit of an income tax charitable deduction for high-income taxpayers (couples earning at least \$250,000 and individuals earning at least \$200,000). These high-end taxpayer would compute their tax savings by multiplying the charitable deduction by the 28 percent tax rate. This is drastic enough, but the President’s budget would also let the Bush-era reduction of the highest income tax rates expire, restoring the 36 percent and 39.6 percent brackets.

### **1. The Effect on Donors**

Some think tanks estimate that this reduction in the tax benefit of a charitable contribution will increase the cost of charitable gifts by about 10 percent for affected individuals.

### **2. The Odds of Passage**

A similar measure was defeated last year in Congress.

### **3. What To Do**

It is hard to find any silver lining here, in contrast to the case of the proposed permanent estate tax repeal (think back to Exhibit A).

- a. Emphasize donative intent over tax savings.
- b. Emphasize planned gifts that provide *other* income tax savings. The most obvious example is a CRUT funded with a highly appreciated asset. That plan can generate a charitable gift that costs the donor substantially less than an outright donation. Stated differently, the CRUT provides an opportunity for substantially greater tax leverage.

## **C. IRA Charitable Rollover**

### **1. Current Law**

Congress enacted the IRA charitable rollover statute as part of the Pension Protection Act of 2006. It applied to lifetime charitable gifts of \$100,000

or less of IRA assets during 2006 and 2007. Congress extended the law to apply in 2008 and 2009. It has now expired.

2. Another Extension?

On March 10, the Senate passed the American Workers, State and Business Relief Act of 2010 (HR 4210). This act includes a tax extender package that would extend the IRA charitable rollover through 2010.

3. The IRA Rollover Statute – A Summary

- a. A donor could make up to \$100,000 of “qualified charitable distributions” (“QCDs”) from an IRA to charities for each year during which the law was in effect.
- b. The donee had to be a public charity; the donee could not be a “supporting organization”; and the gift could not go to a donor advised fund.
- c. The donor had to be age 70½ or older.
- d. Transfers to fund CRTs, CGAs and PIFs did not qualify.
- e. The tax consequences:
  - i. QCDs were excluded from the donor’s federal gross income.
  - ii. The donor was allowed no income tax charitable contribution deduction.
  - iii. The QCD counted toward satisfaction of the donor’s minimum distribution requirement for the IRA.
  - iv. The QCD had no effect on phase-out of other tax benefits or on the taxable portion of the donor’s Social Security income.

4. What To Do While We Wait

- a. The uncertainty about another IRA charitable rollover extension gives development officers an opportunity to talk to donors about other ways to make charitable gifts with IRAs and qualified plans – ways that will be available whether or not Congress extends the IRA charitable rollover.

- b. Two charitable gift plans with retirement plan accounts have been perennially attractive and will continue to be so even if Congress does not extend the IRA rollover.
  - i. An outright gift of all or part of a retirement account at death. Because the retirement account constitutes income in respect of a decedent (“IRD”), children, but not a charity, would pay income tax on that IRD on receipt of the retirement account. Therefore, a charitable gift of a retirement account at death saves taxes that gifts of other assets do not. The potential tax leverage can be as high as 60 to 70 percent for individuals with estates subject to estate tax.
  - ii. Transfer of a retirement account to a testamentary CRT for a surviving spouse. This plan accomplishes two important goals. The donor uses the account to provide for the financial security of a surviving spouse and ultimately makes a charitable gift in a highly tax-leveraged way.

## II. Federal Case Law

The most interesting recent federal tax case related to charitable giving is *Christiansen v. Commissioner*, which is reviewed in detail below. This section also discusses several other cases worth noting.

### A. *Christiansen v. Commissioner*, AFTR2d 2009-7352 (8<sup>th</sup> Cir. 2009)

- 1. The Situation
  - a. Helen Christiansen’s will left her entire estate to her only child, a daughter.
  - b. The will provided that if the daughter disclaimed any portion of the gift, 75 percent of the disclaimed amount would go to a charitable lead annuity trust with the family foundation as the annuity beneficiary and the daughter as the remainder beneficiary. The other 25 percent of the disclaimed amount would go outright to the family foundation.
  - c. After Christiansen’s death, her daughter executed a partial disclaimer of a fraction of the estate. The disclaimer left the daughter with an outright gift of assets with a date-of-death value of \$6,350,000. The balance of the estate was allocated as described above to the CLAT and the family foundation. The daughter did not disclaim her remainder interest in the CLAT.

- d. The estate consisted primarily of limited partnerships that held farm assets and operated farms. On audit, the IRS substantially increased the value of the estate, and the parties stipulated to the IRS value.

## 2. Qualified Disclaimers in a Nutshell

For purposes of the *Christiansen* decision, three of the rules that govern qualified disclaimers are relevant.

- a. If a beneficiary of a decedent's estate makes a qualified disclaimer of certain property, that property is treated as passing, for federal tax purposes, as if the disclaimant had predeceased the decedent.
- b. For the disclaimer to be qualified for federal tax purposes, the disclaimant cannot receive any benefit from the disclaimed property (unless the disclaimant is the decedent's surviving spouse).
- c. A partial disclaimer, i.e., a disclaimer of only a partial interest in property, is permitted only in limited circumstances, which do not include a disclaimer of a portion of property that is not "severable" from the rest of the property.

## 3. The IRS Position

- a. The IRS asserted that the disclaimer in favor of the CLAT was not a qualified disclaimer because the daughter held a remainder interest in the CLAT and therefore received a benefit from the disclaimed property. The disclaimer was not a partial disclaimer of the charitable annuity interest because the annuity interest was not severable from the remainder interest. As a result, the IRS disallowed an estate tax charitable deduction for the value of the annuity interest in the CLAT.
- b. Because the value of the estate was increased on audit, the amount going outright to the family foundation as a result of the disclaimer increased in value as well. The IRS disallowed a corresponding increase in the estate tax charitable deduction on the grounds that this type of disclaimer was against public policy: it gave executors and trustees an incentive to undervalue non-liquid assets in hopes of underpaying estate tax on the amount passing to family members.



4. The Tax Court Decision

a. The disclaimer in favor of the CLAT

- i. The Tax Court held that the disclaimer in favor of the CLAT was not qualified because (i) the daughter received a remainder interest in the CLAT, (ii) the annuity and remainder interests in the CLAT were not “severable” from one another, and (iii) as a result, the daughter could not make a “partial disclaimer” that covered only the portion of the amount going to the CLAT equal to the value of the annuity. Therefore, the estate was allowed no estate tax charitable deduction for the present value of the annuity interest.
- ii. This is not a surprising result. It follows readily from provisions of the long-standing regulations on qualified disclaimers.

b. The disclaimer in favor of the family foundation

- i. The Tax Court acknowledged that this type of formula disclaimer decreased the incentive of the IRS to increase the value of an estate’s assets on audit. The Tax Court concluded, however, that the decreased incentive on that point did not *increase* a fiduciary’s incentive to undervalue assets because there were several disincentives for a fiduciary to do so:
  - a) A fiduciary has a legal duty to value assets correctly.
  - b) The directors of the charity that is the beneficiary of the disclaimer are also fiduciaries and have a duty to ensure that assets are correctly valued so that the charitable beneficiary receives the amount to which it is entitled.
  - c) The state attorney general polices activities of charities and gifts to charity.
  - d) If the IRS perceives that a charitable beneficiary is colluding with a fiduciary’s undervaluation of assets by not challenging it, the IRS has the power to revoke the charity’s Section 501(c)(3) status.

5. The Court of Appeals Decision

The estate did not appeal the Tax Court's ruling that the disclaimer in favor of the CLAT was not qualified and that no estate tax charitable deduction was allowable for the value of the CLAT's annuity interest. The only issue on appeal was the effectiveness of the disclaimer in favor of the family foundation. The Eighth Circuit Court of Appeals agreed with the Tax Court's reasoning on that point and affirmed its decision. In particular, the Eighth Circuit agreed that this type of formula clause may reduce the incentive of the IRS to adjust estate values upward on audit, but it does not encourage undervaluation of assets by fiduciaries and therefore is not against public policy.

6. What does *Christiansen* mean for charitable organizations, development officers and donors?

- a. Some commentators have suggested that *Christiansen* will help charities by encouraging charitable gifts made through this type of disclaimer (or through the same kind of formula clause included directly in an estate planning document). Certainly, development officers should be familiar with how the type of formula upheld in *Christiansen* works and be prepared to discuss it with donors where appropriate. Whether charities and development officers should actively promote the use of a *Christiansen*-type formula is another matter.
- b. One could argue that the Tax Court and the Eighth Circuit Court of Appeals ignored the practical realities surrounding these formula clauses. A charitable organization that is a beneficiary of this type of clause may actually have a **disincentive** to challenge a lowball valuation by the executor. Such a challenge could discourage charitable gifts to the beneficiary institution by members of the next generation, who stand to benefit by a low valuation. In addition, a reputation for challenging the executor's valuation in this type of situation could tarnish a charity's fundraising reputation and deter new gifts. Finally, state attorneys general and the IRS are overstretched and are unlikely to police this kind of gift carefully.
- c. Whether or not the *Christiansen* court underestimated the incentive for undervaluation that this type of formula clause creates, Congress could view a defined value formula clause as abusive when the estate consists primarily of hard-to-value assets. In the past, when Congress has perceived an abuse of the federal tax laws in the charitable planning area, it has often legislated too broadly, prohibiting legitimate charitable planning devices as well as abusive ones. Charitable gift planners with a sense of that history

know that Congress's draconian countermeasures often make it harder to structure legitimate planned gifts effectively.

**B. *Estate of Petter v. Commissioner*, T.C. Memo. 2009-280**

1. The Situation

- a. Ms. Petter contributed her UPS stock to a limited liability company. She then assigned her interest in the LLC to two irrevocable trusts for the benefit of her children and two charities.
- b. The assignment included a defined value formula that determined the portions of the assignment property to the various beneficiaries. That formula transferred to each irrevocable trust one-half of the maximum dollar amount that could pass free of federal gift tax, with any additional amount passing to two charities.
- c. The IRS challenged the value of the LLC units transferred to the trusts and argued that defined value formula clauses are contrary to public policy because they discourage the collection of gift tax. The parties agreed on a value for the LLC units but asked the Tax Court to determine whether the defined value formula clause was void and if not, in what amount a gift tax charitable deduction was allowable.

2. The Tax Court Decision

The Tax Court upheld the gift tax charitable deduction for the charitable gifts provided by the defined value formula. The court reviewed prior case law, including *Christiansen*, and determined that "savings clauses are void, but formula clauses are fine." Judge Holmes noted that the availability of formula clauses encouraged gifts to charity. The Court also determined that the gift was an assignment of a specific dollar amount as opposed to an open-ended amount exceeding a certain dollar value. Finally, the Court allowed the gift tax charitable deduction. This case provides additional support for the use of defined value formula gifts, but charitable organizations and development officers should consult counsel to ensure that the formula follows the roadmap provided by the Tax Court for this type of gift strategy.

**C. *Warfield v. Alaniz*, 569 F.3d 1015 (9<sup>th</sup> Cir. 2009)**

Generally, charitable gift annuities issued by a charitable organization are exempt from scrutiny under federal securities laws pursuant to the Philanthropy Protection Act. In *Warfield*, however, the Ninth Circuit determined that this exemption did not apply to CGAs that were issued as "investment contracts."

1. Marketing Materials

Mid-American Foundation marketed and issued CGAs through financial planners, insurance agents, and others. The Foundation's marketing materials focused on the value of the contract and put little emphasis on the charitable component. Through its promotions, the Foundation raised \$55 million from the sale of more than 400 CGAs.

2. The "Business Model"

The Foundation's CGA program was in fact a Ponzi scheme. Donor funds were used to make annuity payments, pay commissions, and pay the personal expenses of the Foundation managers. With a few minor exceptions, no charitable contributions were ever made. The scheme collapsed in 2001.

3. The Ninth Circuit's Decision

The Ninth Circuit determined that the CGAs offered by the Mid-American Foundation were "investment contracts" and therefore subject to the anti-fraud provisions of the federal securities laws. The court focused on the contents of the Foundation's marketing materials rather than the donors' intent. The Court also affirmed the lower court's finding that the Foundation's employees who were selling these gift annuity contracts were not exempt from the broker-dealer registration requirements because they were paid a commission (up to 8 percent) on the sale of each annuity. As a result, the individual agents (Foundation employees) were required to pay between \$31,900 and \$109,000 per agent in damages.

4. What It Means

- a. The federal securities laws will apply to a CGA that falls within the *Howey* test (*SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946)), i.e., if the CGA is an "(a) investment of money (2) in a common enterprise (3) with an expectation of profits produced by others." In *Warfield*, the Court focused on the expectation of profits by the donors, the target audience for the marketing materials, and the information included in the marketing materials. As a result, the Court found the CGAs constituted "investment contracts" and fell within the purview federal securities laws.
- b. The Philanthropy Protection act ("PPA") will not offer protection to employees of a charity who receive commissions on charitable gifts. When the PPA was enacted, Congress included a specific exemption for charitable organization employees. This exemption does not apply, however, unless a person "is either a volunteer or is engaged in the overall fundraising activities of a charitable organization and receives no commission or other special

compensation based on the number of donations collected for the fund.” Because the agents in *Warfield* received commissions, they fell outside the scope of the PPA’s protections.

**D. *Maddux v. Commissioner*, T.C. Summary Opinion 2009-30**

1. The Situation

Mr. and Mrs. Maddux were regular and generous contributors to their local church. They made substantial annual contributions, including a gift of \$122,214 in 2002. Because of the size of this gift, they had a charitable contribution carryover of \$61,150. Instead of amending their 2003 return (which had already been filed) to use part of this carryover, they applied the entire carryover on their 2004 and then 2005 returns.

2. Use It or Lose It

With respect to the 2005 return (which claimed a \$10,000 carryover charitable deduction) the IRS filed a notice of deficiency. The Service argued that in accordance with Treas. Reg. § 1.170A-10(b) the amount of charitable contribution carryover that could have been deducted on the 2003 return expired, whether or not Mr. and Mrs. Maddux claimed it for 2003. Therefore, that portion of the original carryover could not be applied to their 2005 return. Mr. and Mrs. Maddux disagreed and argued that they should be able to claim the carryover contribution in any of the five carryover years.

3. The Decision

In a summary opinion, the Tax Court agreed with the IRS and noted that although these rules are “intricate,” the contribution deductions may be claimed only as specifically provided by the Code. Therefore, Mr. and Mrs. Maddux had to claim the maximum allowable portion of their carryover deduction for 2003. Because they failed to do so, that amount could not be applied to their subsequent returns.

**E. *Estate of Tamulis*, 509 F.3d 343 (7th Cir. 2007)**

In *Tamulis*, the Seventh Circuit affirmed a Tax Court decision that disallowed an estate tax charitable deduction for a non-conforming charitable remainder unitrust. Father Tamulis, a Catholic priest, died leaving a \$3.4 million dollar estate. The majority of his assets passed to a trust that was to provide income to his brother and sister, benefits for other family members, and the remainder to a church. This trust did not have the structure or provisions required for a qualified charitable remainder unitrust under Section 664. The executor/trustee recognized that there was a problem, and he prepared a petition to reform the trust, but it was never filed. Instead, the trustee administered the trust as if it were a qualifying CRUT. Despite the trustee’s claims that he had “substantially complied” with the

unitrust requirements, the Court found that the executor/trustee “had no excuse for failing to bring the required judicial proceeding to reform the trust.” As a result, it was too late for a “qualified reformation” under § 2055(e)(3) of the Code. Thus, the Seventh Circuit denied an estate tax charitable deduction for the remainder interest.

### **III. IRS Rulings and Other Pronouncements**

Over the past two years, the IRS has issued a number of private letter rulings that have filled in the details of its position on several types of planned gift arrangements. The flurry of sample governing instruments that appeared from 2003 through 2007 has abated: the Service has promulgated no new sample split interest trust documents or explanations about them since its 2007 Revenue Procedure on charitable lead annuity trusts. The IRS has issued its annual “Won’t Rule” list for 2010, and its contents raise a few interesting issues.

#### **A. Early Termination of CRT**

For a number of years the IRS has issued private letter rulings (“PLRs”) that have allowed a CRT to terminate before the end of its specified term and distribute its assets to the income beneficiaries and the remainder beneficiary in proportion to the actuarial value of their respective interests. These PLRs specified conditions under which an early termination will be permitted (i.e., will not result in a prohibited act of self-dealing), and some of those rulings have also taken a position on the income tax consequences of the termination for the income beneficiaries.

##### **1. Prior IRS Position**

- a. No self-dealing will result if the beneficiaries and the trustee use normal IRS valuation procedures, the income beneficiaries represent that they have no medical condition that would cause them to have shorter than normal life expectancies for people of their age, and each beneficiary obtains a corroborating letter from a physician.
- b. If the CRT is one of the net income varieties of CRUT, the computation of the actuarial values of the various interests must use the applicable federal rate (“AFR”) for the month of the termination if that rate is lower than the payout percentage stated in the CRUT agreement.
- c. Each income beneficiary will realize long-term capital gain equal to the amount of the distribution he or she receives from the trust upon its early termination.

## 2. Shorter-Than-Normal Life Expectancy

In PLR 2009-12036, the IRS made an exception to its position that an early termination is permitted only if all of the income beneficiaries have normal life expectancies. The IRS rationale is eminently reasonable, and it expands the usefulness of this planning tool.

### a. The computation

In their ruling request, the income beneficiaries (there were four) represented that they would calculate the value of the income interests by ignoring the interest of the beneficiary who had a health condition. As a result, their distribution equaled the actuarial value of a three-life interest for three healthy beneficiaries in a CRUT of this size and payout. They also agreed among themselves that the value of the income interests would be distributed to one of the income beneficiaries. This feature clearly had gift tax consequences, but the beneficiaries and the IRS did not address them.

### b. The ruling

The IRS reasoned that this method of computing the distribution to the income beneficiaries did not inflate the value of the income interests to the detriment of the charitable remainder beneficiary. In fact, this method slightly understated the income interests, so the IRS was happy.

### c. Expanded planning opportunity

CRUT income beneficiaries typically become interested in an early termination when they need the cash, as opposed to the CRUT income stream, or when they believe the CRUT is underperforming. Whether an early termination will be attractive when the life expectancy of one of the income beneficiaries has to be ignored because of a health condition will depend on all the facts of the particular case. Development officers and other gift planners should keep this new possibility in mind when discussing early terminations with CRT donors and beneficiaries.

## 3. Early Termination in Settlement of a Litigated Dispute

In general, the IRS takes the position that distributions to the beneficiaries of a decedent's estate in settlement of litigation will determine the tax consequences. Two private letter rulings issued in 2008 follow this rule. PLRs 2008-02032, 2008-01033. In PLR 2008-02032, the decedent's estate plan left the bulk of the assets to a testamentary CRT for the decedent's only child. Litigation arose between the estate and the child.

To settle the litigation, the parties agreed that the decedent's assets would be divided between the child and the charitable remainder beneficiary of the CRT that would have been created. The IRS ruled that distributions according to the settlement agreement had no adverse tax consequences.

## **B. Reformations of CRTs**

The IRS has long taken the position that a reformation or amendment of a CRT that changes the interests of the noncharitable beneficiaries will typically cause the trust to be disqualified. On the other hand, the Service has been quite liberal in permitting reformations or amendments of CRTs where the drafting attorney, by mistake, inattention or miscommunication, drafted the wrong type of CRT, e.g., a NIMCRUT when the clients had asked for a standard CRUT. Recent PLRs continue this liberal tradition, and one of them gives some comfort about the reach of the *Atkinson* case.

### **1. Reformation to Allow Termination by Gift**

The donors wished to terminate their CRUT by transferring their unitrust interests to the remainder beneficiary, but state statute did not permit the termination without specific provisions that the trust agreement lacked. With the consent of the state attorney general, the donors and other CRUT beneficiaries amended the trust to add the necessary provisions. The IRS ruled that the amendment did not disqualify the trust. PLR 2008-02024.

### **2. Error by Drafting Attorney**

The IRS continues to issue PLRs that allow a reformation to correct an error by the drafting attorney, even when such a reformation changes the payout structure and therefore, in theory, changes the noncharitable interests. One of these is interesting in light of the *Atkinson* case, which held that failure to operate a trust as a CRT pursuant to its governing instrument cost disqualifies it. *Atkinson v. Commissioner*, 390 F.3d 1290 (11<sup>th</sup> Cir. 2002).

- a. The charitable remainder beneficiary's counsel drafted the trust as a NIMCRUT.
- b. The charity acted as trustee and administered the trust as a standard CRUT as the donors had intended.
- c. The IRS ruled that a judicial reformation to convert the trust to a standard CRUT was permissible. PLR 2008-11003.

## **C. Reinsurance of CGAs**

Over the past two years the IRS has issued three PLRs on the tax consequences when a charity reinsures a CGA by purchasing a commercial annuity contract.



PLRs 2008-47014, 2008-52037, 2008-52057. The facts presented in all three rulings were similar. Here is a summary of the situations and the rulings:

1. The Situations

- a. The CGA agreement complied with all of the requirements for a qualified charitable gift annuity under Section 514(c)(5).
- b. The CGA contract also included a provision that authorized but did not require the charity to reinsure the CGA by purchasing a commercial annuity contract. If the charity elected to do so, the excess of the donor's contribution over the cost of the commercial contract constituted funds available for the charity's immediate use.
- c. In all three rulings, the charity did in fact reinsure, and in some cases the commercial contract provided for a lump-sum payment to the charity if the annuitant died before the aggregate annuity payments equaled the premium on the contract.

2. Tax Consequences

- a. The donor would be allowed income and gift tax charitable deductions equal to the amount the donor contributed minus the present value of the CGA, computed in the usual way using the AFR and the IRS tables.
- b. None of the payments the charity received from the donor and from the insurer would constitute unrelated business taxable income.

**D. Flexible CGAs – No Constructive Receipt**

In a 2007 PLR, the IRS addressed for the first time the application of the doctrine of constructive receipt to a flexible CGA. PLR 2007-42010.

1. Because the annuitant of a flexible CGA has, within limits, the right to determine when annuity payments begin, there is a question as to whether the annuitant should be taxed on the payments as if he or she had elected the earliest date.
2. In general, the doctrine of constructive receipt and Code Section 451 require an individual to include an amount in gross income if that amount is available to the individual, even though the individual does not draw upon it.
3. For a variety of technical reasons having to do with the interaction of Section 72, which governs annuities, its legislative history, and Section

451, the IRS ruled that the doctrine of constructive receipt does not apply to flexible CGAs.

4. To the extent that this PLR represents a settled IRS position, it removes uncertainty about one tax consequence of flexible CGAs and is therefore very welcome.

#### **E. Investing in “Endowment Shares”**

Earlier in the decade, Harvard and several other institutions obtained favorable PLRs on a technique that allowed CRTs and CLTs to participate in the return on the institution’s endowment. Three recent PLRs indicate some changes to the IRS position. PLRs 2007-02036, 2007-35019, 2008-50048.

##### 1. “Endowment Shares”

- a. An endowment share is a right to participate in the investment performance of the institution’s endowment. In other words, the return on the endowment shares is tied to the return on the endowment itself.
- b. A holder of an endowment share receives an annual cash distribution based on the institution’s endowment spending policy.
- c. If the holder (e.g., a CRT) needs additional cash to satisfy its payout requirement, it can redeem some of its Endowment Shares.

##### 2. Prior IRS Rulings

The IRS issued favorable rulings with respect to Endowment Shares held by CRTs and CLTs.

- a. The shares did not constitute an ownership interest in the assets of the endowment. As a result, a holder of endowment shares did not have UBTI even if the endowment itself did.
- b. The annual cash distribution tied to the institution’s endowment spending policy constituted ordinary income.

##### 3. IRS Retrenchment

The IRS has announced that it is reconsidering whether a CLT’s investment in Endowment Shares will result in pass-through of UBTI from the institution’s underlying endowment.

4. Redemption of Endowment Shares by a CRT

A CRT that holds Endowment Shares has Tier 1 income when it receives the annual cash distribution tied to the endowment's spending policy. The IRS has now ruled that a CRT's redemption of Endowment Shares generates capital gain or loss that constitutes Tier 2 income for purposes of determining the character of the CRT payments in the hands of the beneficiary.

5. Endowment Shares Held by a Type III Supporting Organization

The IRS has ruled that a Type III supporting organization can invest in Endowment Shares issued by its "beneficiary organization." The SO does not have UBTI with respect to the shares, and the annual cash distribution counts toward its annual income distribution requirement.

**F. CRT – Broad Sprinkling Power**

A "grantor" trust under the federal income tax provisions of the Code cannot qualify as a CRT. Treas. Reg. § 1.664-3(a)(3)(ii). In general, a power of the trustee to allocate income or principal among a class of beneficiaries (a "sprinkling power") causes the trust to be a grantor trust. Under Section 674(c), an exception applies if the trustee is an "independent trustee."

1. PLR 2008-13006 – The Situation

- a. Husband and wife created a CRUT.
- b. Twenty-five percent of the annual payment would be distributed to them for their lives.
- c. The trustee had discretion to sprinkle the remaining 75 percent of each year's unitrust amount among husband, wife and any charitable organization selected by the trustee.
- d. The trustee qualified as an "independent trustee" under Section 674(c).

2. The Ruling

Because the sprinkling power fell within the Section 674(c) exception, the trust was not a grantor trust. Therefore, the trust qualified as a CRUT.

3. What It Means

This ruling is not surprising to anyone who knows the intricacies of the CRT regulations and the grantor trust rules of the Code. It is important, however, as a reminder that donors who seek unusual flexibility with a

CRT can often obtain it if their tax advisors fully understand the CRT regulations and related rules.

### **G. Donor Advised Fund – Closely Held Stock Gift**

Donor advised funds are subject to the private foundation prohibition against excess business holdings. The Code also strictly circumscribes permissible transactions between a DAF and the donor or a related party. Although this PLR did not answer all the questions one might wish to ask about this type of situation, it suggests a way to navigate these rules safely. PLR 2007-47001.

#### **1. The Situation**

- a. The creator of a donor advised fund was the owner of some of the stock of a closely held corporation (the ruling did not state how much of the stock the donor and members of his family owned).
- b. The donor proposed to transfer some of his stock to his DAF without any restrictions on a later sale of the stock.
- c. The donor was trustee of a trust for his wife. He proposed to cause the trust to make an offer to purchase the shares he had donated to his DAF.

#### **2. The Ruling**

The IRS ruled that this was not a “prearranged sale” and therefore would not be recharacterized as a sale of the stock from the donor to his wife’s trust followed by a contribution of the cash proceeds to his DAF. As a result, the donor avoided tax on the gain the DAF realized when it sold the shares to his wife’s trust.

#### **3. Unanswered Questions**

- a. Why wasn’t there an excess business holdings problem? There are two possible answers. Perhaps the donor and his family did not collectively own more than 20 percent of the stock of the company, so excess business holdings were not a problem. Perhaps the DAF divested itself of the stock within the five-year time period required by the “excess business holdings” rules.
- b. What about excess benefit transaction concerns? Certain transactions between a donor or a related entity on the one hand and the donor’s DAF on the other are automatically treated as excess benefit transactions regardless of whether those transactions are at fair market value. A sale, however, is not one of those transactions. Here the donor did not request a ruling that the sale from the DAF to the wife’s trust was not an excess benefit

transaction. Presumably, the donor was confident that the sale was at fair market value and that no excess benefit transaction resulted.

## **H. Residuary Bequest Funded with IRA**

The safest way for a donor to leave an IRA or other retirement account to a charity in a way that avoids tax on the income in respect of a decedent (“IRD”) is to name the charity in the account’s beneficiary designation. Two recent rulings show that there are other ways, in some cases, to arrive at the same result.

### **1. Disclaimed IRA**

In one situation a decedent’s IRA beneficiary designation named several individuals, all of whom disclaimed. As a result, the IRA passed to the decedent’s estate, and his will left the residuary estate to a charity. At the time of the disclaimer, all gifts other than the residuary bequest had been satisfied. The executor distributed the IRA to the charity, and the IRS ruled that the distribution would not cause the estate to be taxed on the IRD. This is an unsurprising result. Longstanding regulations provide that distribution of an IRD item in satisfaction of a residuary bequest causes the residuary beneficiary to take the IRD into gross income. Moreover, the only asset available to the estate at the time it satisfied the residuary bequest was the IRA. All other assets had been distributed to satisfy other gifts. PLR 2008-26051.

### **2. Discretionary Satisfaction of Residuary Gift with IRA**

Another ruling is perhaps more surprising and definitely more interesting. The named beneficiary of the decedent’s IRA predeceased the decedent so the IRA passed to the decedent’s estate by default. The estate was administered by a revocable trust, and the trustee proposed to fund the residuary gift, which was charitable, with the IRA. The trustee had enough assets to pay the specific legatees without using the IRA, but apparently had not yet done so. The trustee’s decision to satisfy the residuary bequest with the IRA did not trigger the IRD to the decedent’s revocable trust. PLR 2008-50004.

## **I. IRS “Won’t Rule” List**

For the most part, the IRS is willing to issue a private letter ruling on a prospective transaction, provided that the taxpayer who requests the ruling pays a hefty “user fee.” There are, however, some issues on which the IRS will not necessarily rule. Every year the IRS issues a Revenue Procedure that updates the list of topics on which: (i) it will not issue rulings, (ii) it will ordinarily not issue rulings, and (iii) it will not issue rulings because the issue is under extensive study.

## 1. The Significance of the “Won’t Rule” List

The “Won’t Rule” list can be useful to donors and charitable organizations in several ways.

- a. Some donors are unwilling to go forward with a major charitable gift transaction, especially one that has uncertain tax consequences, without the prior assurance of a favorable private letter ruling. The “Won’t Rule” list tells donors the issues on which such a ruling will not be forthcoming, so that they do not waste time and legal fees preparing a request.
- b. For donors who might wish to proceed with a gift transaction that has uncertain tax consequences, the list helps identify transactions with respect to which the IRS is apparently on the fence. As a result, such transactions may receive heightened scrutiny on audit. Unfortunately, the list does not tell what the IRS is thinking about these issues.
- c. In some cases the list is a reminder that no PLR is needed because sample documents promulgated by the IRS (e.g., sample CRT agreements) provide a safe harbor and assurance of favorable tax consequences if the donor’s attorney follows them when drafting the relevant document.

## 2. A New “Won’t Rule” Issue

This year’s list has one addition relevant to charitable gift planning. The Service will not rule on:

Whether the termination of a charitable remainder trust before the end of the trust term . . . in a transaction in which the beneficiaries receive their actuarial shares of the value of the trust assets, causes the trust to have ceased to qualify as a charitable remainder trust within the meaning of IRC § 664.

## 3. Other “Won’t Rule” Issues of Potential Interest

- a. Whether income, gift, and estate tax charitable deductions will be allowed for a transfer of a partnership or LLC interest to a charity.
- b. Whether a taxpayer who transfers property to a charity, then leases it back, may deduct the fair market value of the property for income tax purposes.
- c. Whether a trust that purports to be a NIMCRUT qualifies under Section 664 where certain parties can control the timing of the trust’s receipt of income from a partnership or deferred annuity

contract to take advantage of the difference between the definition of trust accounting income and the definition of federal tax income. This issue relates to the so-called “spigot trust.”

- d. Whether the termination of a CRT before the end of the defined term in a transaction that distributes their actuarial shares to the beneficiaries is treated as a sale or other disposition of the beneficiaries’ interests. This is a CRT early termination issue. A number of commentators disagree with the current IRS position that the income beneficiary realizes gain under Section 1001(e) equal to the amount he or she receives in the terminating distribution.

## **J. Donor Standing to Enforce a Restriction on a Charitable Gift**

The courts of most states that have addressed the issue of donor standing, i.e., the right to initiate a legal action, have held that neither a donor nor a member of a donor’s family has “standing” to enforce a restriction on a charitable gift. The only exception these cases make is the situation in which the donor has explicitly retained a reversionary interest, i.e., a right to get the gift back if the charity does not use the gift for the purpose the donor has specified. All of these cases hold that only the state attorney general has standing to enforce a restriction on a charitable gift. A recent Missouri Court of Appeals case followed the vast majority of states in holding that a deceased donor’s children did not have standing to enforce a gift. *Hardt v. Vitae Found., Inc.*, WD70525 (Mo. Ct. App. Nov. 10, 2009). The case is interesting because it is thorough, well reasoned, sheds light on the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”) and presents facts that would make a very sympathetic case for the court to have granted the donor standing.

### **1. The Situation**

- a. The decedent’s will gave her children, as her executors, the discretion to distribute roughly \$8 million of her estate to charities of their choice.
- b. The children decided to give all of the money to Vitae Foundation, a pro-life organization that focused on various ways, including mass media education, of promoting the pro-life cause.
- c. The gift agreement included detailed, specific agreements as to how the money would be used and how the organization would use parts of the gift as matching funds to solicit other contributions. Awhile after the gifts were made, the Vitae Foundation informed the donor’s children that the restrictions were not being followed.
- d. The children filed suit seeking restoration of the portion of the gift that had been misspent and an injunction preventing any additional

expenditures from the gift in a manner inconsistent with the gift instrument.

2. The Decision

- a. The court began by adopting the common-law rule in other states that a donor (and by implication, a donor's family) does not have standing to enforce a restriction on a charitable gift unless the donor has retained a reversionary interest. In *Hardt*, the parties acknowledged that the donor had not retained such an interest.
- b. Although the Missouri Uniform Trust Code gives standing to a donor of a charitable trust to enforce the trust in certain circumstances, the court held that the MUTC could not be expanded to include standing to enforce outright charitable gifts. Even though there was some Missouri case law that said outright charitable gifts should be treated like charitable trusts in some circumstances, the language of the MUTC was clear and did not extend to outright charitable gifts.
- c. Missouri had enacted a version of UPMIFA, and the Uniform Laws comments on UPMIFA strongly suggested that only the attorney general should have standing to enforce restrictions on outright charitable gifts.
- d. The Hardts argued that this was a sympathetic case and that the court should grant them standing on "public policy" grounds. The court declined to do so. It acknowledged that there might be situations in which the attorney general does not sufficiently represent a donor's interest, but that had not been shown in the Hardts' case. Moreover, the Missouri legislature's passage of UPMIFA meant that "it would not be appropriate for us [the court]" to grant the Hardts standing.



## EXHIBIT A

### Is the Bequest Half Full or Half Empty?

#### 1. The Situation

- Single donor
- Gross estate: \$15,000,000
- Estate Plan
  - \$5,000,000 charitable bequest
  - Balance after estate tax to children
- If estate tax is in force:
  - Rate: 50% (combined federal and state)
  - Exemption: \$5,000,000

#### 2. Effect of Charitable Bequest

	<u>With Estate Tax</u>	<u>Without</u>
● Net to charity	5,000,000	5,000,000
● Net to children		
○ Gross	10,000,000	10,000,000
○ Tax	2,500,000	- 0 -
○ Net	7,500,000	10,000,000
● Cost of charitable gift to children		
○ Gross to children without charitable gift	15,000,000	15,000,000
○ Tax	5,000,000	- 0 -
○ Net	10,000,000	15,000,000
○ Net with charitable bequest	7,500,000	10,000,000
○ Cost to children	2,500,000	5,000,000

#### 3. The Moral

- Without estate tax, there is \$2,500,000 more for the children after the charitable bequest than there would be if the estate tax were in force.
- With estate tax, half of the \$5,000,000 charitable bequest is paid out of what would otherwise go to the children, and half is paid by the federal government out of what would otherwise be tax dollars. Without estate tax, the entire charitable gift comes out of the children's pockets.

***This material is based on the relevant law in effect on the date it was completed: March 22, 2010. It is only a summary of the subject matter it addresses, and it is intended to provide information of a general nature only. It should not be construed as a comprehensive treatment or as legal advice or legal opinion on any specified facts or circumstances. Readers are urged to consult with an attorney concerning their own situations and any specific legal questions they may have. Because this material deals with recent legal and legislative changes, an update may be handed out at the conference.***

***Pursuant to the Rules of Professional Conduct set forth in Circular 230, as promulgated by the United States Department of the Treasury, nothing contained in this document was intended or written to be used by any taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer by the Internal Revenue Code of 1986 and it cannot be used by any taxpayer for such purpose. No one may use or refer to any portion of this document in promoting, marketing or recommending a partnership or other entity, investment plan or arrangement relating to any one or more taxpayers.***

GP:2733824 v1

# Fund and Trust Accounting Software

TRUSTprocessor is the next step in the evolution of fund and trust accounting software. The only General Ledger based, in-house trust system on the market, it remains a favorite within the non-profit community.

What is our secret? We have combined comprehensive functionality with versatility. We have added a variety of management tools and built it all with the power of a relational database. One look and you will see why this robust product is getting so much attention.

- Gift annuity processing
- Common fund or pooled fund accounting
- 4-Tier accounting
- Endowment accounting
- Internet access for your accounts
- General ledger based



**HWA**  
**INTERNATIONAL, INC.**  
Trust accounting software since 1977

8363 Wolf Lake Drive, Suite 101, Memphis, TN 38133 • 800-328-8661 • [www.hwainternational.com](http://www.hwainternational.com)



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## **Stewardship = Marketing**

Presented by:

Rachel F. Moore  
Director, Campaign Initiatives & Leadership Support  
Smith College  
33 Elm Street  
Northampton, MA 01063  
413-585-2068  
rfmoore@smith.edu

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## **Your Current Donors are Your Best Prospects**

How do you find new planned giving donors? You mail, you call, you e-mail, you advertise.... Still it seems like an awful lot of marketing dollars are going to waste. No matter how scientifically you segment your target audience and no matter what new technologies you employ, your brilliant words and appeals mostly fall into empty space.

Why beat the bushes for new customers when your best prospects are right in front of you?

The first place to look for new planned giving donors is within your current planned giving donor group. They are a captive and congenial audience and they represent a tremendous source of potential future gifts and bequests.

1. You know that these people like your organization's mission.
2. You know where they live.
3. You know they have resources.
4. You may even know how old they are.

By considering current planned giving donors as prospects you can dramatically increase the effectiveness of your marketing dollars and reap solid gains for your organization.

\*\*\*

Where to begin? Let's start with good, solid program administration – the back office stuff that is so critical to a good planned giving program. Unlike your major gifts and annual giving colleagues, you must watch over administration of donors' planned gift arrangements in a prudent, effective, conscientious manner, and you must communicate with the donors and income beneficiaries on a regular basis. You have built-in quarterly contacts as checks or statements go out. You send annual tax reports. And revaluation letters for CRUTs. Those are contact opportunities your major gifts colleagues can only dream of! Are you using them to full advantage?

Just like fast food restaurant chains and big box stores, we are talking about the most basic premise of good salesmanship and repeat business: customer service.

- ❖ Who do donors reach when they call the number on their quarterly (or annual) statement? The gift recording staff? The finance office? Your custodian bank? Be sure that they always reach the planned giving office. Don't lose opportunities to talk with your donors just because they can get transactional questions answered by capable accounting folks.

- ❖ As you well know, a planned gift is not a purely financial transaction – it’s a charitable donation. Keep your non-profit’s mission in front of your beneficiaries. Do the envelopes and checks/statements have your non-profit’s name and logo on them? Do they say “thank you for your philanthropic support of our organization’s mission” to remind them that they are part of something bigger than themselves (and more significant than the check they are depositing)?
- ❖ Remind donors that there are real people in the planned giving office who know who they are. Send Valentines to unmarried older ladies. Send birthday cards when people turn 80 or 90. Give them your name and number, send them your photo, make a personal connection.

Satisfied customers come back for more. Donors try you out with small gifts, and if they’re satisfied — with the experience, with the way the gift assets are managed, with the work your organization is accomplishing — they’ll come back with additional (often larger) gifts. Remember that nothing is more satisfying to donors than to know that their gifts are noticed and appreciated.

\*\*\*

Turning to more traditional fundraising techniques: get out and visit the donors! In planned giving it can seem particularly hard to get out from behind your desk some days. But you must. It not only reinvigorates you, but it also does more good for your program than any classic “marketing” effort can.

With any luck you have too many planned givers to be able to visit all of them! This is the best reason ever to establish a close working relationship with colleagues in other parts of your development office! Communicate regularly with the people who are in charge of stewardship or donor relations. There will definitely be opportunities to piggyback on their efforts. Even more important, you must educate your major gifts colleagues about the potential planned, testamentary and outright gifts that this donor pool represents. You need those folks helping you with the visits. You may need to advocate with the director of major gifts so that these “stewardship” calls are understood to be legitimate major gifts cultivation and prospecting visits. You may also need to advocate for internal gift officer evaluation methods that don’t pit one shop against another. Your best work will come in collaboration within the team, and your institution will benefit mightily if gift officers are supporting, not competing against, each other.

\*\*\*

Professionals in for-profit marketing may be surprised to hear planned giving experts declare that there’s no such thing as a form letter in our industry. If you have experience raising large gifts you know that, no matter how hard you try to streamline your promotional and donor relations work, one size does not fit all where major donors are concerned. And planned givers are, by definition, major donors. The essence of major gifts work is to help individual donors connect meaningfully with your organization’s mission, and that requires individualized communications.



Over the past decade planned giving programs have learned the value of segmenting their marketing efforts, targeting different groups with appropriate messages. We know that 40-year-olds aren't good candidates for gift annuities. For that matter, neither are 90 year-olds. We need to identify our audience and tailor our message accordingly. We need to segment as finely as our dwindling marketing budgets will allow.

Targeted stewardship is really just a modified major gifts cultivation program, custom tailoring messages to small groups of individuals. However, few planned giving shops have the personnel, time, or resources to develop and implement individualized stewardship plans for each and every donor. How can we prioritize?

Let's separate our planned giving donors into categories and look for marketing and cross-selling opportunities. Just as the gift vehicles are different, so are the characteristics and needs of the donors who choose them. There are stewardship and cross-selling opportunities galore. A few examples:

#### *Charitable Gift Annuities*

Often gift annuitants choose this type of gift because they like the security of fixed income. Communicate to them how your annuity assets are managed. Emphasize the financial stability of your organization. These donors are thinking about safety and reliability. Not every non-profit is as solid and well-run as yours! Let them know.

If you have long-time annuitants they may be surprised to learn that getting older has made them eligible for some relatively high rates. How will they know that if you don't tell them? Pointing it out in an informational way is likely to be perceived as looking out for their interests, rather than trying to sell them something.

#### *Deferred Payment Gift Annuities*

The very nature of these gift instruments means that you have an automatic stewardship problem. There is a built-in time delay between gift and first payout. What does the donor hear from you during that interim period? Probably nothing. That's a missed opportunity. Craft some kind of communication specifically for your deferred annuitants, so they know you remember them and you are grateful. They are wonderful potential repeat donors!

Deferred annuitants (especially those who have elected a flexible start date for payouts to start) are great candidates for renouncing their life income interest at some point down the road. They essentially have an additional "gift" right at their fingertips, with a tax deduction incentive to make it even more appealing. Let them know about that.

Ask your major gifts colleagues to prioritize deferred annuitants for visits. Coach them to consider deferred annuitants as "potential donors" rather than "closed gifts."

#### *Pooled Income Funds*

Although these gifts have fallen into disfavor at many institutions, they have an important place in the planned giving tool kit, and they will come back into vogue if tax rates and interest rates return to those of the 1980s. Pooled funds tend to see the highest volume of repeat donors. In fact, they are structured so as to encourage additions. Many institutions have a considerably lower dollar threshold for PIF additions than for initial gifts. For instance, if a \$5,000 gift is required to initially get into the pool, additions may be possible in increments of \$500 or \$1,000.

Do you provide pooled fund investment details to the donors each year? Your fund manager can help you with that. Remind donors how a pooled fund works, including the constraints that may result in relatively low payouts in these market conditions. Remind the donors that participation in a pooled income fund is a charitable gift, not an investment plan. Continually connect the donors to the mission of your organization, and reinforce that their donation will make a difference.

Yes, those PIF returns are pretty low.... You'll be surprised at how many donors will happily consider relinquishing their interests or directing their payouts straight to your annual fund.

Finally, use your PIF communications as a cross-selling opportunity. Many pooled fund donors went into the funds in the 1980s and '90s. They may not realize that, because they are older now, the payout rates of gift annuities are pretty appealing.

### *Charitable Remainder Trusts*

Each year you send revaluation letters to your CRUT donors and beneficiaries. That's a great opportunity for substantive contact. But what do your CRAT donors and beneficiaries receive?

How about outside-managed trusts, which you've booked as required by FASB? These generous donors don't receive anything from you! You thanked them when they informed you of their generosity – but what have they heard from you lately?

How about widows and widowers whose late spouses set up the trusts from which they receive payouts? Or children who receive payouts from trusts set up by parents who were connected with your organization? These income beneficiaries have second-hand relationships with your institution, and now the primary contact is gone. Perhaps these family members are worthy of special attention.

### *Bequest Intentions*

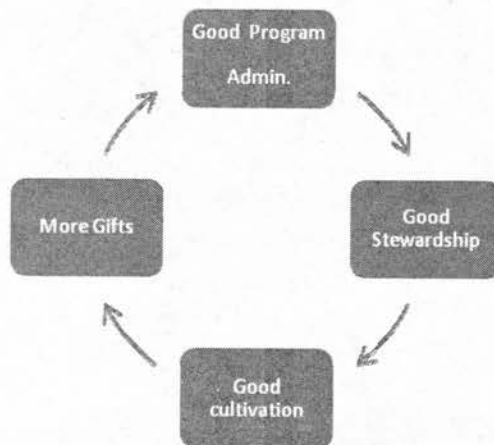
This type of planned gift is the most common and has the most promise as a potential source of new or accelerated gifts. A tried and true stewardship technique is a "bequest society," which recognizes individuals' generosity in including your organization in their estate plan. Regular contact with this group reinforces your institution's gratitude. It also makes it less likely that they will take you out of their estate plan! Once a donor has revealed the existence of a bequest intention (and has been acknowledged for it) it is extremely unlikely that he or she will ever remove that charity from the will.

Visiting these donors can be especially productive. Ask them to work with you to designate an eventual purpose to which their bequest will be directed. Get them connected with that part of your organization now. They may end up deciding to make a gift during their lifetime so they get the satisfaction of seeing the effect of their philanthropy. Sometimes donors are willing to make annual expendable gifts to accomplish an objective that their bequest will eventually endow.

Many people now understand the tax advantages of directing retirement plan assets to charities after their deaths. Make sure these folks are included in your bequest society. IRA beneficiary designation forms do not allow for any specificity of gift purpose. Encourage donors to sign a letter of intent that expresses their wishes for your institution's eventual use of their gift. Then start stewarding.

\*\*\*

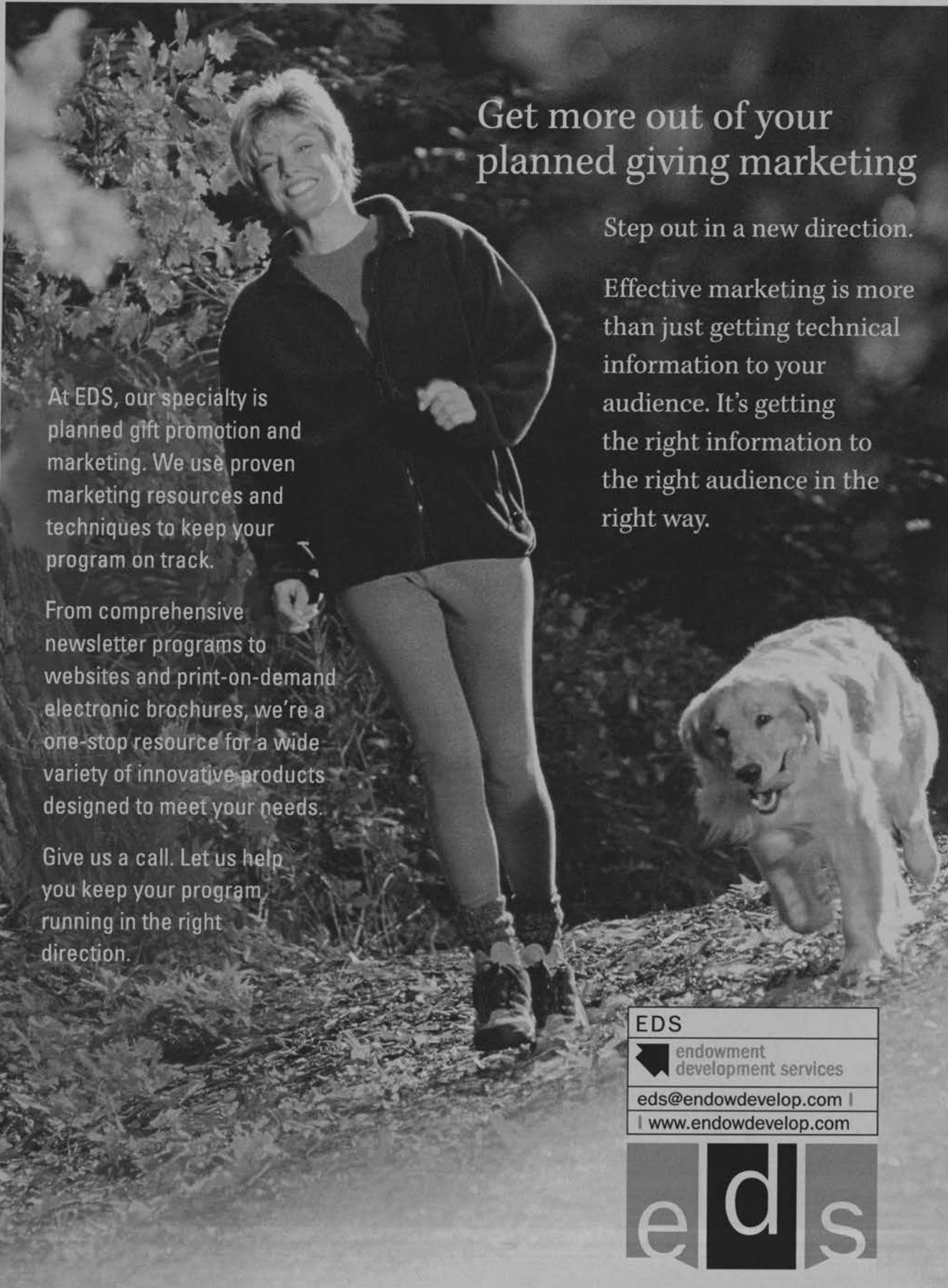
### Stewardship = Marketing



Rachel F. Moore  
Director of Campaign Initiatives & Leadership Support  
Smith College  
33 Elm Street  
Northampton, MA 01063  
(413) 585-2068  
[rfmoore@smith.edu](mailto:rfmoore@smith.edu)

Special thanks to ACGA board member Cam Morin Kelly, of Duke University, for her collaboration in developing the original version of this presentation.





## Get more out of your planned giving marketing

Step out in a new direction.

Effective marketing is more than just getting technical information to your audience. It's getting the right information to the right audience in the right way.

At EDS, our specialty is planned gift promotion and marketing. We use proven marketing resources and techniques to keep your program on track.

From comprehensive newsletter programs to websites and print-on-demand electronic brochures, we're a one-stop resource for a wide variety of innovative products designed to meet your needs.

Give us a call. Let us help you keep your program running in the right direction.

EDS

endowment  
development services

eds@endowdevelop.com |

| www.endowdevelop.com





## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## **The Ethics of Philanthropy**

Presented by:

**Gary Morris**

**President**

**Morris Capital Corporation**

**5310 Harvest Hill Road**

**Suite 192**

**Dallas, TX 75230**

**214-363-4949**

**[garyamorrisria@att.net](mailto:garyamorrisria@att.net)**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)





## THE ETHICS OF PHILANTHROPY

Journalism for Success...  
Gift Annuities, Gift Planning and All That Jazz!  
25th Conference on Gift Annuities • April 25-26, 2012



Sponsor and Exhibitor Invitation

Presenter:

Gary A. Morris, CFP®, CLU, AEP, CIMC®, AIF®

## Focus on Ethical Implications

for:

- YOU
- YOUR DONORS  
/CLIENTS
- YOUR ORGANIZATION



## GREEK “GIFTS”

- Ethos – The distinguishing character, sentiment, moral nature or guiding beliefs
- Aristotle – “Nicomachean Ethics” :  
Character =ethikos

## CORE ETHICAL VALUES

Josephson Institute – Six Pillars of Character

- Trustworthiness
- Respect
- Responsibility
- Fairness
- Caring
- Civic Virtue

## RESOLUTION THEORIES

-Rushworth Kidder:

- Ends-based Thinking  
Jeremy Bentham/John Stuart Mill  
Utilitarianism/ Consequentialism  
“greatest good for the greatest number”

## RESOLUTION THEORIES

-Rushworth Kidder:

- Rule-based Thinking  
Immanuel Kant  
Categorical Imperative

“If everyone ...followed the rule...that would create the greatest good..”

## RESOLUTION THEORIES

-Rushworth Kidder:

- Care-based Thinking  
Great Religious Leaders  
Reversibility

“ Do to others what you would like them to do to you”

## GOLDEN RULE

- Christianity: Matthew 7:12
- Judaism: Leviticus 19:18
- Buddhism: Udana-Varga 5:18
- Confucianism: Analects 15:23
- Hinduism: Mahabhartata 5:1517
- Islam: Sunnah

## Simple Ethical Standard FAIRNESS

- Treating Others as You Want  
to be Treated
- Viewing the Issues from All  
Stakeholders' Perspectives

## GREEK “GIFTS”

LOVE

- EROS – Sexual Passion
- AGAPE – God's benevolence toward  
people
- Phileo – Deep Devotion  
Philosophy – love of wisdom  
Philanthropy – love of promoting the  
happiness of others through gifts



## DEFINITIONS

- Charity – Directed to the “needy” and present situation. Criticized as being short term and dealing with the symptoms.
- Philanthropy – Directed toward society and the future; focused on long term solutions.
- Giving



## THE HERITAGE

-The “Contract”/ Obligatory Giving

Egypt/Greece/Rome/Hindu Culture

- “Stewardship” Giving

Judeo-Christian belief toward supporting the poor, widows and the orphans



## EIGHT STAGES OF TZEDAKAH

1. DONOR GIVES LOAN/ FORM PARTNERSHIP/FINDS WORK
2. NEITHER DONOR OR RECIPIENT KNOWS
3. DONOR KNOWS/RECIPIENT DOES NOT KNOW
4. DONOR DOES NOT KNOW/RECIPIENT KNOWS
5. DONOR GIVES DIRECTLY BEFORE BEING ASKED
6. DONOR GIVES DIRECTLY WHEN ASKED
7. DONOR GIVES LESS THAN APPROPRIATE IN A FRIENDLY MANNER
8. DONOR GIVES WITH A SCOWL

## THREE SCHOOLS OF PHILANTHROPY

- Social Calvinism
- Social Universalism
- Social Darwinism



### WHY GIVE ?

1905 John Mott, Student Volunteer Movement:

- Compassion for the Needy
- Self interest
- Community Spirit
- Reciprocity

2006 BoA/Center on Philanthropy Indiana U.

- Meet critical needs
- Giving back
- Reciprocity
- Desired intent

### GIVING PATTERNS

	USA	HNW
Religion	60%	22%
Basic Needs	11%	5%
United Ways	10%	22%
Health	5%	7%
Education	5%	20%
Arts	2%	10%
Disasters/Other		4%

### ETHICAL OBLIGATIONS TO DONORS /CLIENTS

- YOUR FULL DISCLOSURE
  - Philosophical/Religious Beliefs
  - Organizational Relations
- COMPREHENSIVE PROCESS
  - Determine Goals & Objectives
  - Review Data

### ETHICAL OBLIGATIONS TO DONORS/CLIENTS

- SPECIFIC CHARITABLE FOCUS
- DONATIVE INTENT**
  - Verbalized – Questions
  - Demonstrated- IRS Form1040 / Wills / Trusts





"Now this \$1-million contribution I made, was it a sincere gesture or just for tax purposes?"

### ETHICAL OBLIGATIONS TO DONORS/CLIENTS

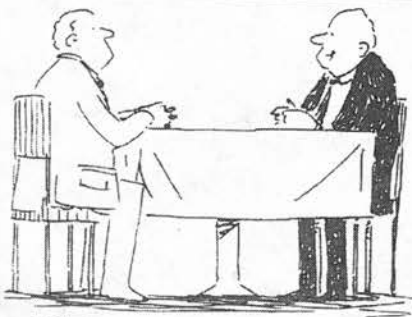
- CURRENT & PROJECTED CIRCUMSTANCE
  - Family    Risk Tolerance    Asset Basis
  - Asset Values    Cash Flow    Liabilities
  - Tax Status: Income/Gift/Estate



### ETHICAL OBLIGATIONS TO DONORS/CLIENTS

#### EVALUATION OF CHARITIES

- Congruence of Objectives
- Status
  - IRC 501 (C)(3)/ others
  - Corporate Non-profit
  - Trust



"Well, this is crazy. Every time we talk about likely donors for the project, it sounds like me."



### ETHICAL OBLIGATIONS TO CLIENTS

#### EVALUATION OF CHARITIES

- Directors/Staff
- Financial Condition
  - Grants
  - Overall Expenses
  - Fundraising Expenses
- "Trail Run"
  - Volunteerism

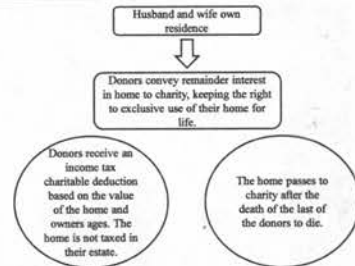
### ETHICAL OBLIGATIONS TO DONORS/CLIENTS

- DEVELOP SPECIFIC SOLUTIONS
  - COOPERATIVE EFFORT
    - Attorney Accountant Planned Giving Officer
- CRITERIA
  - Timing Cash Flow
  - Tax Impact Interest Rates

### ETHICAL OBLIGATIONS TO DONORS/CLIENTS

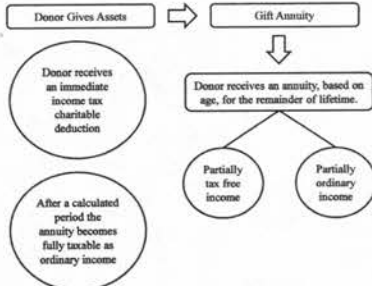
- CONSIDER ALTERNATIVE TECHNIQUES
  - Immediate Cash Gift
  - Immediate Property Gift
    - (Life Insurance, Real Estate, IRAs)
  - Deferred Property
    - (Home with Retained Life Interest)
  - Donor Advised Funds
  - Gift Annuities

#### Gift of Remainder Interest in Residence



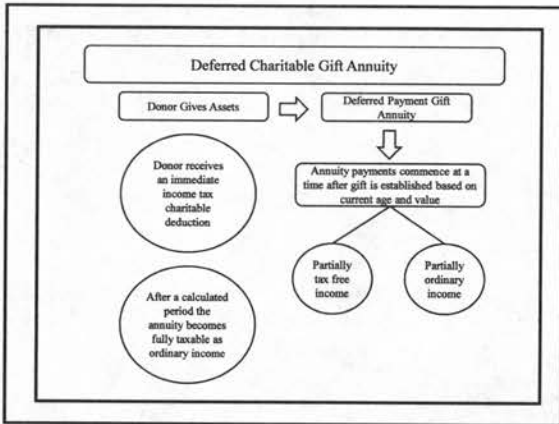
Additional Characteristics:  
 •Donors continue to live in their home, pay taxes and maintain the home.  
 •If a material change in the donors' circumstances occurs which necessitates selling the home, the donors will receive the income from sale proceeds for the remainder of their lives.

#### Charitable Gift Annuity



AGDA Gift Annuity Rates  
 Approved by AGCA Board December 28, 2004  
 Effective February 1, 2005 - June 30, 2009

Single Life Rates		Single Life Rates		Single Life Rates	
Age	Rate	Age	Rate	Age	Rate
18	2.5	26	3.7	52	1.4
19	2.7	27	3.8	53	1.4
20	2.7	28	3.9	54	1.5
21	2.7	29	4.0	55	1.5
22	2.7	30	4.1	56	1.5
23	2.7	31	4.2	57	1.5
24	2.7	32	4.3	58	1.5
25	2.7	33	4.4	59	1.5
26	2.7	34	4.4	60	1.5
27	2.7	35	4.5	61	1.5
28	2.7	36	4.5	62	1.5
29	2.7	37	4.5	63	1.5
30	2.7	38	4.5	64	1.5
31	2.7	39	4.5	65	1.5
32	2.7	40	4.5	66	1.5
33	2.7	41	4.5	67	1.5
34	2.7	42	4.5	68	1.5
35	2.7	43	4.5	69	1.5
36	2.7	44	4.5	70	1.5
37	2.7	45	4.5	71	1.5
38	2.7	46	4.5	72	1.5
39	2.7	47	4.5	73	1.5
40	2.7	48	4.5	74	1.5
41	2.7	49	4.5	75	1.5
42	2.7	50	4.5	76	1.5
43	2.7	51	4.5	77	1.5
44	2.7	52	4.5	78	1.5
45	2.7	53	4.5	79	1.5
46	2.7	54	4.5	80	1.5
47	2.7	55	4.5	81	1.5
48	2.7	56	4.5	82	1.5
49	2.7	57	4.5	83	1.5
50	2.7	58	4.5	84	1.5
51	2.7	59	4.5	85	1.5
52	2.7	60	4.5	86	1.5
53	2.7	61	4.5	87	1.5
54	2.7	62	4.5	88	1.5
55	2.7	63	4.5	89	1.5
56	2.7	64	4.5	90	1.5
57	2.7	65	4.5	91	1.5
58	2.7	66	4.5	92	1.5
59	2.7	67	4.5	93	1.5
60	2.7	68	4.5	94	1.5
61	2.7	69	4.5	95	1.5
62	2.7	70	4.5	96	1.5
63	2.7	71	4.5	97	1.5
64	2.7	72	4.5	98	1.5
65	2.7	73	4.5	99	1.5
66	2.7	74	4.5	100	1.5

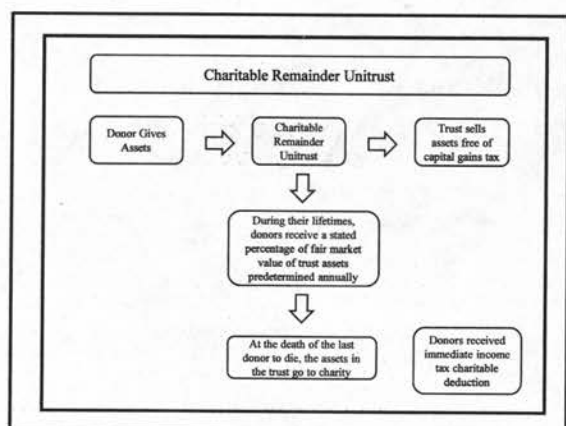
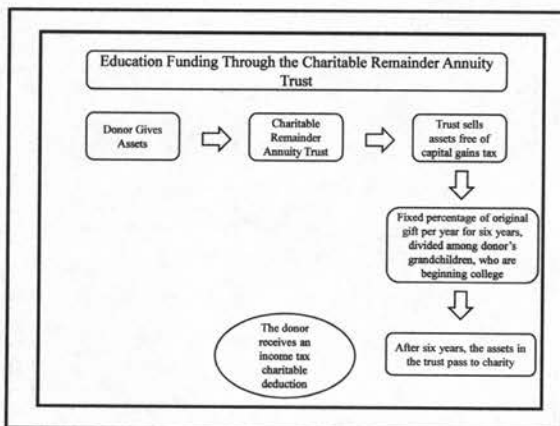
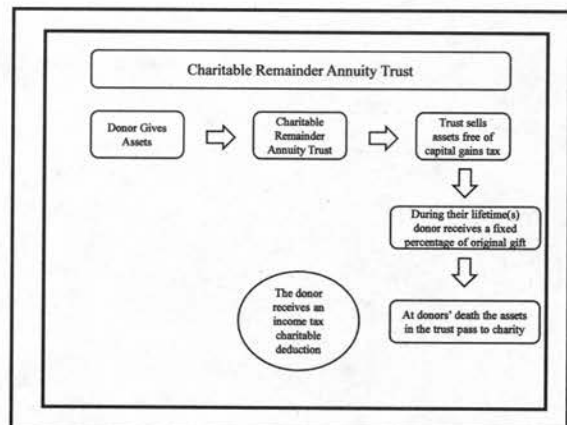
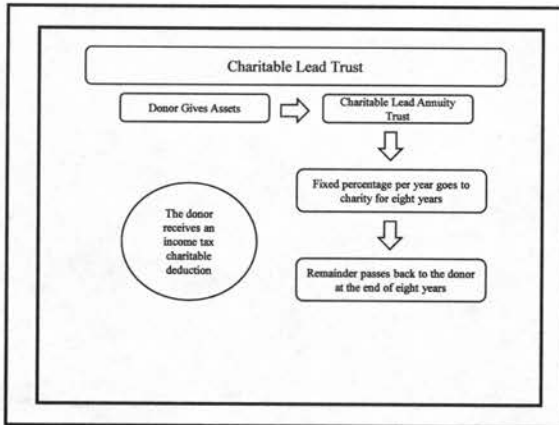


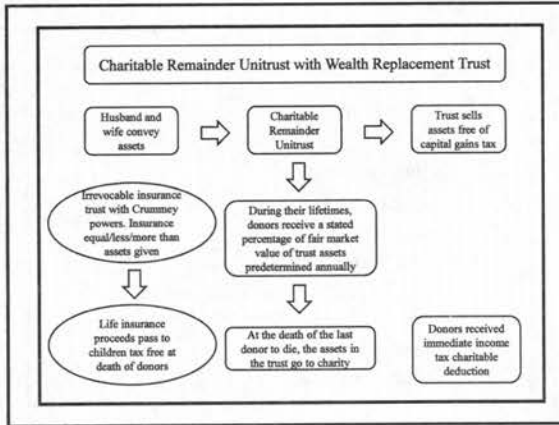
**ETHICAL OBLIGATIONS TO DONORS/CLIENTS**

**ALTERNATIVE TECHNIQUES**

Split Interest Gifts:  
 Charitable Lead Trusts (Annuity/Unitrust)  
 Charitable Remainder Trusts (NIMCRUTS/Wealth Replacement Trusts)

Foundations (Public/Private)





**ETHICAL OBLIGATIONS TO DONORS/CLIENTS**

**DECISION MAKING**  
 Specific Technique or Combination

Projected Benefits/Costs

Emotional Aspects:  
 Family Meetings  
 Thought  
 Meditation  
 Prayer



MODEL STANDARDS OF PRACTICE FOR THE CHARITABLE GIFT PLANNER

1. The Charitable Gift Planner shall act in the best interests of the donor and shall disclose to the donor all material facts concerning the proposed transaction, including the tax consequences and the risks of the transaction.

2. The Charitable Gift Planner shall consult with independent advisors, including a tax advisor, to ensure that the transaction is in the best interests of the donor and to ensure that the transaction is fully compliant with applicable law.

3. The Charitable Gift Planner shall describe and represent the gift to the donor in a clear and concise manner, including the nature of the gift, the value of the gift, and the tax consequences of the gift.

4. The Charitable Gift Planner shall ensure that the transaction is fully compliant with applicable law, including the requirements of the Internal Revenue Code and the Regulations thereunder.

5. The Charitable Gift Planner shall act in a public trust and shall not engage in any self-dealing or other transactions that may create a conflict of interest.

**MODEL STANDARDS OF PRACTICE**

**FOR THE CHARITABLE GIFT PLANNER**

- Philanthropic Motivation
- Tax Implications
- Full Disclosure
- Compensation
- Competence & Professionalism

**MODEL STANDARDS OF PRACTICE**

**FOR THE CHARITABLE GIFT PLANNER**

- Consultation with independent advisors
- Description and Representation of Gift
- Full Compliance
- Public Trust





**AFP CODE of ETHICAL PRINCIPLES and STANDARDS**

- Aspirations
- Ethical Standards
  - Member Obligations
  - Solicitation and Use of Philanthropic Funds
  - Presentation of Information
  - Compensation and Contracts

**EXPLORATION OF ETHICAL DILEMMAS:**

- Emotional/Financial Balance; Donor and Institution
- Publicity for Promotion
- Unfulfilled Pledges
- Charitable "Scams"
- Post Gift Donor/Beneficiary Behavior

**"PUBLIC" EXPECTATIONS**

- "Privilege" of Estate/Income Tax Status
- "Preferred" / Mandatory Beneficiaries
- Increased Giving
- Governance

**ETHICAL OBLIGATIONS TO YOURSELF**

- Professional Obligations: Law, Accounting, Insurance, Securities, etc.
- Fiduciary Duties
- Personal Codes/ Values/ Responsibilities
- Develop Your Skills

**ETHICAL OBLIGATIONS TO YOUR ORGANIZATION**

- Promote a Culture that Encourages Ethical Conduct
- Reinforce the Ethics Philanthropy Connection



QUESTIONS

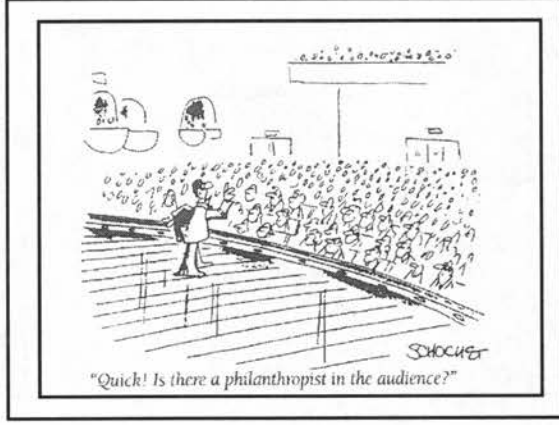
COMMENTS

**Acknowledgements:**

Doing Well and Doing Good: Money, Giving and Caring in a Free Society ; Os Guinness; Navpress; 2001

How Good People Make Tough Choices: Resolving the Dilemmas of Ethical Living: Rushworth M. Kidder; Free Press; 1995

Presentation Support : Taylor Nipp





**WHEN WE SAY YOU'RE LIKE A FRUIT BAT,  
WE MEAN IT IN THE BEST POSSIBLE WAY.**

*Symbiotic relationships. Fruit bats have one with fig trees, and your organization has one with eTapestry. Because you pay for our service instead of buying everything upfront, we have to keep earning your trust month after month. So when we say we're going to do everything we can to be your favorite fig tree, you can believe us.*

**WE'LL BE GOOD  
FOR EACH OTHER  
OR IT'S FREE.**

We're confident that you'll have a great relationship with eTapestry. In fact, we're willing to guarantee it. If you don't raise more money with our software than you were before, you get it free for a year. Call 888.739.3827 or visit [eTapestry.com](http://eTapestry.com)

*eTapestry is a Blackbaud Company*



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## **Managing Risks in CGA Programs**

Presented by:

**Bryan Clontz**

**President**

**Charitable Solutions LLC**

**3713 Pine St., Suite 165-109**

**Jacksonville, FL 32205**

**(404) 375-5495**

**bryan@charitableolutionsllc.com**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## Managing Risk in CGA Programs Part I

Bryan Clontz, CFP®  
President, Charitable Solutions, LLC  
www.charitableolutionsllc.com (404) 375-5496

## Agenda

- CGA Market Overview
- Risk Management 101
- CGA Risk Management: Worst Practices
- CGA Mortality Study
- 12 Dimensions of CGA Pool Risk
- Exhaustion Frequency and Severity
- Nasty Math of Negative Compounding
- Six Risk Management Strategies

## Charitable Gift Annuity Market Overview

- Estimated \$10-15 Billion in CGAs issued by 4,000 Charities
- Average Age 78
- Average Gift \$60,000 (Doubled Since 1999)
- Most Popular Form of Life-Income Gift
- Median Residuums  
76% (1994)  
96% (1999)  
65% (2004)

## Risk Management 101

- Actual Outcomes Worse Than Expected
- Event Frequency, Event Severity
- Risk Management Strategies
  - Retain Risk (Total Assumption/Deductible or Self-Insurance)
  - Reduce Risk (Stop Smoking or Reduce ACGA Rate)
  - Transfer Risk (Insurance or Contract)
  - Avoid Risk (Eliminate Activity)

### Three Rules to Remember:

Don't Risk a Lot to Gain a Little, Don't Risk More Than You Can Afford to Lose, Know the Odds

## CGA Risk Management

### Top Ten CGA Mistakes

1. Using Money Currently
2. Granting Rate Exceptions
3. Thinking a "Pool" is a Pool
4. Thinking FASB Liabilities are Reality
5. No Asset-Liability Matching on Investments
6. Relying on History to Project the Future
7. Self-Insuring Large Concentrated Risks
8. No Written Risk Management Plan Matching Risk Tolerance
9. No Periodic CGA Pool Review
10. No Pro-Activity on Known Issues – the "Ostrich Approach"

## CGA Mortality Research

### Clontz-Behan CGA Mortality Study for the Society of Actuaries

Sample Case: 77 Year-Old Female/\$100K 7.4% CGA/6% Discount Rate

1990 IRS Table	11.1 Years	\$55,828 Liability
Annuity 2000	12.7 Years	\$64,490 Liability
Clontz-Behan	14.8 Years	\$71,267 Liability

Income Tax Deduction Overstated by 38-40%  
Liability Understated by 27-30% over 1990 – 11-13% over 2000

Donors are living 1-5 years beyond Annuity 2000

### 12 Dimensions of CGA Pool Risk

1. Gender
2. Investment – Average Returns and Timing
3. Statistical
4. Restrictions
5. Charity's Risk Tolerance
6. Concentration
7. Gift Timing
8. Gift Flow
9. Rate
10. Asset-to-Liabilities
11. Exhaustion
12. Longevity

### Exhaustion Frequency and Severity

- 6-12% Exhaustion Probability for New CGAs
- Of the CGAs that Exhaust, the average "loss" on original gift is 10-15%
- Lowest Risk – Young Male with Deferred Annuity
- Highest Risk – 90 Year Old Female

### The Nasty Math of Negative Compounding

#### Case Facts:

65 year-old female \$100,000 CGA @ 6% issued on January 1, 2008 and assumes a 60% Equity-40% Bond allocation

1. Year 1: Loss of 25% dropping balance to \$75,000
2. Make payout of \$6,000 dropping balance to \$69,000
3. Remaining life expectancy is 24.3 years
4. Stock market return required in Year 2 to meet original ACGA expectations – 70-80% (or 51% blended return)

### Six CGA Risk Management Strategies

- Increase New CGA Flow!
- Revisit Pool Asset Allocation Given Pool and Charity Characteristics
- Offer/Encourage Reduced ACGA Rates
- Encourage Full/Partial/De-Facto Revocation of Life Interest
- Adopt Customized Risk Management Plan and Policies (Max Age, Max Size, Rate Approach, Investment Approach, Etc.)
- Selectively Use Reinsurance to Collar Concentrated Risks



## Managing Risk in CGA Programs Part II:

### CGA Reinsurance

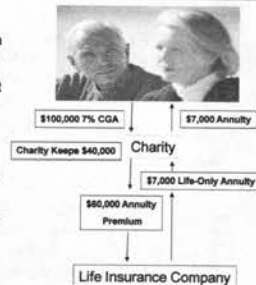
Bryan Clontz, CFP®  
President, Charitable Solutions, LLC  
www.charitablesolutionsllc.com (404) 375-5496

### Agenda

- CGA Reinsurance Defined
- What Risk is Transferred and What Risk Isn't?
- What are the Tax, Accounting and State Regulation Implications?
- Does Reinsurance Cost Too Much?
- Reinsurance vs. Self-Insurance Analysis
- Reinsurance vs. Fixed Income: An Alternative
- How Does the Insurance Company and the Agent/Broker Make Money?
- What Characteristics Make Reinsurance More Attractive or Less Attractive
- CGA Reinsurance: 10 Specialized Applications
- CGA Risk Management and Reinsurance Articles

### Reinsurance Defined

- Charitable gift annuity reinsurance is simply a financing technique whereby a charity chooses to purchase a commercial single premium immediate annuity as an asset to back its contractual life-income liability owed to the donor.
- The term "reinsurance" is both incorrect and unfortunate in that it has no resemblance to true reinsurance — where one insurance company cedes excess risk to another insurance company for a premium.



### What Risk is Transferred and What Risk Isn't?

- The longevity risk (the risk that donors will live past life expectancy) and the investment risk (the risk that average returns fail to meet assumptions or the timing of the returns generate early current losses) is transferred to the insurance company.
- If the life insurance company defaults, and another company does not take over its liabilities, and the state guaranty funds don't provide full coverage and the bankruptcy court and liquidation of assets does not make the liability whole, then the charity remains contractually liable to make the payments. This scenario has never occurred in our history, but certainly could in the future.

### What are the Tax, Accounting and State Regulation Implications of Reinsurance?

- If the charity does not require the purchase of reinsurance, then all of the tax implications from a charitable income tax perspective and a 1099 perspective are identical to a non-reinsured gift annuity.
- All FASB calculations are the same as well. Charities first calculate the FASB liability and then, since the commercial annuity is owned by the charity, they book an asset with a value that exactly matches the calculated liability.
- Every state allows for a reserve reduction for reinsured gift annuities so long as the charity uses a qualified reinsurance contract. States requiring customized contracts are WA, IL, WI, CA and NY.

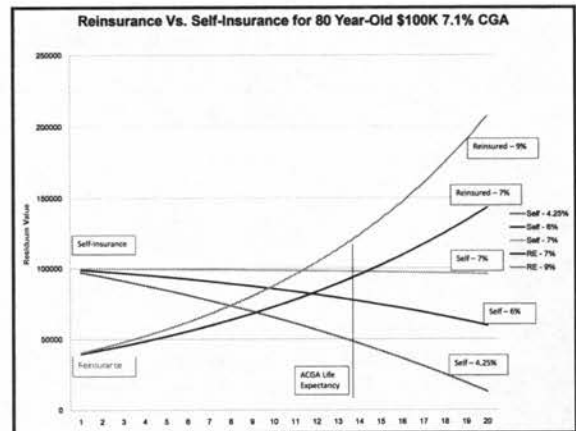
### Does Reinsurance Cost Too Much?

- Compared to what?: The state reserve liability calculation, the FASB liability calculation, the charitable income tax deduction reflecting the life-income present value?  
  
Each of these calculations may use completely different assumptions for discount rates and life expectancies.
- The benefit-cost analysis becomes – if we self-insure and model to life expectancy, what is the projected ending value vs. reinsurance?

### Future Value Calculations

Female Age	ACGA Life Expectancy (LE)/Present Value After Reinsurance (PV)	Future Value at 6%	Future Value at 7%	Future Value at 8%
65	LE= 27.55 PV= 21.28%	\$105,961	\$137,244	\$177,335
70	LE= 22.68 PV= 27.75%	\$104,039	\$128,732	\$158,969
75	LE= 18.07 PV= 34.28%	\$98,246	\$116,414	\$137,723
80	LE= 13.88 PV= 38.92%	\$87,381	\$99,545	\$113,264
85	LE= 10.28 PV= 43.81%	\$79,747	\$87,829	\$96,642
90	LE= 7.35 PV= 51.21%	\$78,587	\$84,202	\$90,161

-Assumes a \$100,000 CGA with the present value growing at a net constant rate of return to life expectancy. Note that the ACGA equity assumption is 9%.



### Reinsurance vs. Fixed Income: An Alternative

Internal Rate of Return (IRR) Estimated Calculations

Annuity 2003 Unisex Table	CGA Gender-Specific Life Expectancies		
	6.43% Net	6.51% Net	6.59% Net
Contract #623 - 14.1 years	18.47	18.47	8.91% Net
Contract #1178 - 23.2 years	20.03	20.03	7.24% Net
Contract #6111 - 3.8 years	6.16	6.16	15.80% Net
Contract #1911 - 5.9 years	7.87	7.87	12.47% Net
Contract #1218 - 23.2 years	20.03	20.03	7.85% Net
Contract #1482 - 7.6 years	8.97	8.97	10.76% Net
Contract #1318 - 7.6 years	10.88	10.88	11.80% Net
Contract #677 - 13.2 years	16.31	16.31	8.00% Net
Contract #638 - 13.8 years	18.90	18.90	8.79% Net
Contract #629 - 7.6 years	10.88	10.88	11.80% Net
Contract #1482 - 14.1 years	18.20	18.20	7.80% Net
Contract #1118 - 8.3 years	8.97	8.97	12.80% Net
Contract #1225 - 4.9 years	8.00	8.00	13.18% Net

- ### How Does the Insurance Company and Agent/Broker Make Money?
- The life insurance takes the premium and then buys institutional bonds to exactly match the future cash flows (asset-liability matching). It may earn 7% on the bonds and then credit the annuity with 6% so they make the spread. They have no longevity risk (law of large numbers).
  - The broker or agent usually earns a 3% commission, and the master broker/general agent usually earns 1% - so a total commission of 4%. Note that this would be the present value equivalent of a 36 bps (.36%) annual investment fee over 17 years.

### What Characteristics Make Reinsurance Attractive or Unattractive?

The donor and gift characteristics that make reinsurance the most attractive are: older donors, healthy donors, immediate annuity payments, female donors, large gifts relative to the pool, donor's who wish to see the money work immediately and/or restricted gifts (such as those governed by fund agreement).

The charity's characteristics that make reinsurance the most attractive are: new or smaller pools, large concentrated gift into existing pool, the charity's desire to use some money immediately, the charity desires the least amount of administration possible, the charity is organizationally risk averse, financial modeling that projects higher ending balances under reinsurance vs. self-insurance, charity wants to back out state reserve liabilities, there are no excess reserves or unrestricted money to draw upon if a CGA exhausts (*i.e.*, goes negative).

The converse of any these characteristics make reinsurance generally less attractive.

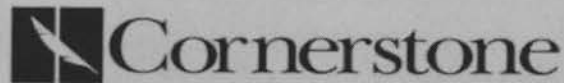
- ### CGA Reinsurance: 10 Specialized Applications
- Money Now! Total Reinsurance with Immediate Payout
  - "Under-Water" CGA Optimization: Solves for Longest Possible Payments
  - NY Reserve Requirement Mitigation: A Double-Kicker
  - Commercial Single Premium Immediate Annuity (SPIA): An Elegantly Simple Solution
  - Large CGA Risk Mitigation: Collaring the Outliers
  - Required Reinsurance to Maximize Charitable Income Tax Deduction: AFR and Immediate Annuity Rate Arbitrage
  - Options for Unhealthy Gift Annuitants
  - Isolating and Immunizing Longevity Risk: Chopping Off the Statistical Tail
  - Private Letter Rulings Clarify Reinsurance Rider Options and UBI Issues
  - The Stop-Loss Two-Step: Eating the Apple in Two Bites

## CGA Reinsurance/Risk Management Articles

- Newton, M. and Clontz, B. (1998) "An Analysis of Commercial Insurance as an Alternative Gift Annuity Financing Option." *Journal of Gift Planning*, National Committee on Planned Giving. <http://www.charitable-solutions.com/files/GiftAnnuity1.pdf>
- Clontz, B. and Behan, D. (2004). "Optimizing Charitable Gift Annuity Risk Management: Collaring The Bear and The Grim Reaper." *The Journal of Gift Planning*. [http://www.charitable-solutions.com/files/journal\\_of\\_gift\\_plan\\_1st\\_quart\\_2004.pdf](http://www.charitable-solutions.com/files/journal_of_gift_plan_1st_quart_2004.pdf)
- Clontz, B. (2004) "The Top Ten Charitable Gift Annuity Risks to Avoid: How Does Your Charity Stack Up?," *Planned Giving Today*, November. [http://www.charitable-solutions.com/files/top\\_10\\_cga\\_risks\\_to\\_avoid2.pdf](http://www.charitable-solutions.com/files/top_10_cga_risks_to_avoid2.pdf)
- Clontz, B. and Behan, D. (2005). "Optimizing Charitable Gift Annuity Risk Management Part II: Reinsurance Revisited." *The Journal of Gift Planning*, June 2005. [http://www.charitable-solutions.com/files/journal\\_of\\_gift\\_planning\\_2.pdf](http://www.charitable-solutions.com/files/journal_of_gift_planning_2.pdf)
- Behan, D. and Clontz, B. (2005). "Mortality of Beneficiaries of Charitable Gift Annuities." *Society of Actuaries* <http://www.soa.org/research/ife/research-mortality-beneficiaries.aspx>
- Clontz, B. and Atwood, G. (2006) – CGA Risk Management. Symposium speech at the ACGA conference.
- Clontz, B. (2007). "Charitable Gift Annuity Reinsurance: The Top Ten Most Frequently Asked Questions." *Planned Giving Design Center*. [www.pgdcc.com/usa/Item?ItemID=342815](http://www.pgdcc.com/usa/Item?ItemID=342815)
- Behan, D., Clontz, B. and Johnston, M. (2008). "Mortality of Charitable Remainder Trust Income Beneficiaries." Sponsored by SunTrust Bank and Renaissance Trust.
- Clontz, B. (2009). "Charitable Gift Annuity Reinsurance Part II: The Top 10 Unique Applications in a Turbulent Market." *Planned Giving Design Center*. <http://www.pgdcc.com/pads/charitable-gift-annuity-reinsurance-part-ii-the-top-10-creative-solutions-turbulent-times>

13





## Planned Giving Services

“We put the *Service* back into planned giving services”

### **Our Mission:**

Cornerstone Planned Giving Services was created under the principle that all institutions, no matter how large or small, deserve a comprehensive planned giving partner. We tailor our services and offerings to middle-market planned giving programs with assets between \$200,000 and \$5 million, offering a complete suite of fiduciary services usually reserved for large institutional programs. Cornerstone Planned Giving Services is a division of Cornerstone Advisors Asset Management, Inc., a SEC Registered Investment Advisor overseeing \$3.5 billion in client assets.

### **Our Services:**

Cornerstone provides complete administrative and investment advisory services for all forms of charitable trusts, gift annuities and pooled income funds. Our model is based upon flexibility, allowing us to engage our clients in a manner consistent with their needs, not ours. Our services are designed to provide a turnkey solution for all of your investment and administrative needs including asset management, private-labeled gift administration, donor and prospect support, trustee services and fiduciary tax preparation.

### **Our Partners:**

Cornerstone Planned Giving Services utilizes the services, knowledge and support of industry leaders PG Calc, Inc., Charles Schwab and Fiduciary Solutions, LLC. in order to deliver our turnkey planned giving solution to our clients. Our partnerships with these firms allow us to leverage our dedicated internal resources in order to deliver repeatable, high quality services at exceptionally competitive rates.

We believe we can offer your organization all of the services and resources you need to fulfill your mission and grow your planned giving program. For more information on how we can partner with you and your organization, please contact:

Thomas Aschoff  
Director, Cornerstone Planned Giving Services  
74 West Broad Street Bethlehem, PA 18018  
800-923-0900  
[taschoff@cornerstone-companies.com](mailto:taschoff@cornerstone-companies.com)

For information online, please visit [www.cornerstone-companies.com](http://www.cornerstone-companies.com).



# Charitable SOLUTIONS, LLC

*Leveraging Risk Management Knowledge*

## **Gift Annuity Risk Management Services:** ***Do You Know Where Your Gift Annuity Risks Are?***

- What if US equities don't return 9%-10% "in the long-term"? What will your CGAs look like then?
- What does your Programs' "long-term" actually look like?
- What are your return assumptions? What's the reasoning behind them?
- What is the probability of exhaustion for each CGA? For the Program overall?
- What are your expected cash flows & balances under different return environments?
- Where are your longevity risks?
- Where should reinsurance be used and where shouldn't it?

Our Life Income Risk Management Analytics Suite provides organizations with the most in-depth, comprehensive solution for understanding and managing the risks that are inherent in gift annuity programs. We have provided risk analysis on over \$1.5 billion in CGAs since 2003!

## **Investment & Outsourced Solutions:**

- Comprehensive Investment Management Services for small-to-medium sized CGA Programs.
- Dechomai Foundation can issue CGAs in 42 states: 100% of Residuum is granted back to charity.

## **Non-cash Donation Receipt & Liquidation Solutions:**

- We offer a complete, end-to-end proven process that allows non-profit organizations to accept non-cash assets without taking on the associated challenges or risks.
- Dechomai Foundation, Inc. is a national public donor advised fund in Atlanta, GA established with the sole purpose of accepting non-cash assets. After a fee of 1-3%, the entire net sales proceeds will be granted out within 31 days. See [www.dechomai.org](http://www.dechomai.org) for more information.

We have completed more than \$250 million in Non-Cash Contributions since 2003!

We also provide: CRT Trustee Services for non-cash assets and trusts under \$1 million as well as  
CGA Reinsurance Brokerage & Qualified Life Insurance Appraisals

**VISIT US AT BOOTH 26**

Charitable Solutions, LLC / 770-993-8501 / [info@charitablesolutionsllc.com](mailto:info@charitablesolutionsllc.com) / [www.charitablesolutionsllc.com](http://www.charitablesolutionsllc.com)  
Contacts: Bryan Clontz, CFP, CLU, ChFC, AEP, CAP (404-375-5496) and Mack Johnston, CFA (770-993-8501)





## **Jammin' for Success...**

**Gift Annuities, Gift Planning & All That Jazz!**

**29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010**



## **Charitable Lead Trusts**

Presented by:

**Jeremiah Doyle  
Senior Vice President  
BNY Mellon Wealth Management  
One Boston Place 024-0108  
Boston, MA 02108  
(617) 722-7420  
jere.doyle@bnymellon.com**

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



## Charitable Lead Trusts

Jeremiah W. Doyle IV  
BNYMellon Wealth Management  
One Boston Place  
Boston, MA 02108  
[Jere.doyle@bnymellon.com](mailto:Jere.doyle@bnymellon.com)

January, 2010

### I. Introduction and Background

- a. A charitable lead trust (CRT) is an irrevocable trust, created during life or at death, which provides for the upfront or “lead” interest being paid to charity in the form of a guaranteed annuity or unitrust payment and the remainder interest passing to or continuing in trust for non-charitable beneficiaries. It is a mirror image of a charitable remainder trust.
  - i. The term charitable lead trust is not used in the Internal Revenue Code. The rules relating to CLTs and describing the form of qualifying annuity and unitrust interests are contained in Internal Revenue Code §170(f)(2)(B), §2055(e)(2)(B) (estate tax) and §2522(c)(2)(B) (gift tax). The rules are set forth in further detail in Reg. 1.170A-6(c)(2)(i) and (ii), Reg. 20.2055-2(e)(2)(vi) and (vii) and Reg. 25.2522(c)-3(c)(2)(vi) and (vii).
- b. Two gifts are made by the donor at the time of the creation of a CLT: (1) a gift of the annuity or unitrust interest to charity and (2) a gift of the remainder interest to the non-charitable beneficiaries.
- c. CLTs can be either qualified or non-qualified. A qualified CLT provides for a payment at least annually to one or more qualified charitable organizations in the form of either an annuity (a fixed dollar amount) or a unitrust (a fixed percentage of the fair market value of the trust property, valued annually).<sup>1</sup> A qualified CLT creates a “lead” interest which qualifies for a gift or estate tax charitable deduction. A non-qualified CLT creates an annual payout to a charity which doesn’t meet the requirements of an annuity or unitrust interest and, as such, is not eligible for a gift or estate tax charitable deduction. Nonqualified lead trusts are not discussed in this outline.
  - i. A qualified CLT may be either created during the donor’s lifetime (inter vivos) or under the donor’s will (testamentary). An inter vivos CLT provides the donor with a gift tax charitable deduction

---

<sup>1</sup> Reg. 20.2055-2(e)(2)(vi); Reg. 25.2522(c)-3(c)(2)(vi). Unless otherwise noted, all references are to the Internal Revenue Code and the regulations thereunder.

in an amount equal to the present value of the annuity or unitrust interest payable to charity and may provide income tax benefits in certain cases. A testamentary CLT provides only an estate tax charitable deduction for the present value of the annuity or unitrust interest payable to charity. Depending on the term of the trust and the amount of the lead interest payable to charity, it is possible to produce a charitable gift or estate tax deduction that equals the amount transferred to the trust resulting in a gift and estate tax-free transfer.

- d. Generally, the donor is not entitled to an income tax charitable deduction for transfers made to a CLT. An income tax charitable deduction is only available if the CLT is structured as a grantor trust i.e. a trust in which the donor retains a power under §§673-677 that causes the income of the trust to be taxed to the donor.<sup>2</sup>
- e. The income taxation of a CLT depends on whether the CLT is treated as a grantor trust or a non-grantor trust. A grantor CLT is one in which the donor is treated as the owner for federal income tax purposes because the donor or parties related to the donor have retained certain powers over the trust under §§673-677. If the CLT is treated as a grantor trust, the donor is taxed on all the trust income during the charitable lead term. A non-grantor trust is one over which the donor has not retained any of the powers specified in §§673-677. If the CLT is treated as a non-grantor trust, the CLT is taxed under normal rules that apply to a complex trust meaning that the CLT is taxed on all its undistributed income and capital gains. A non-grantor charitable lead trust will receive a fiduciary income tax charitable deduction under §642(c) for distributions made to the charitable lead beneficiary. Unlike a CRT, a CLT is not exempt from income tax.
- f. A non-qualified CLT is one that doesn't have the requisite annuity or unitrust interest, does not entitle the donor to an income tax charitable deduction upon transfer of property to the CLT and is taxed under the normal rules of trust taxation.
- g. A CLT can benefit the charity, the donor and the donor's heirs. A CLT provides an immediate stream of payments to charity for the term of lead interest. The CLT also provides the donor with a gift or estate tax charitable deduction for the actuarial value of the lead interest payable to charity. If the CLT is structured as a grantor CLT it will provide an income tax charitable deduction to the donor in the year of funding for the

---

<sup>2</sup> §170(f)(2)(B).

actuarial value of the lead interest payable to charity.<sup>3</sup> If the assets in the CLT outperform the rate (the §7520 rate) used to value the lead interest, the donor's heirs (remaindermen) will receive the amount in excess of what the amount reported to the IRS as a taxable gift. The primary use of a CLT for gift and estate tax planning purposes is its potential to transfer wealth on a deferred basis to children or grandchildren at a significantly reduced or no gift or estate tax cost and at the same time further the donor's charitable goals. In a few case CLTs are used to reduce the income taxes of the person who creates the CLT.

## II. Basic Rules Applicable to CLTs

### a. The Various Participants

- i. Donor – There are no restrictions on who can be the donor of a CLT. A donor can fund a CLT either during his or her life (inter vivos) or at his or her death (testamentary).
- ii. Trustee – Any person or entity can serve as a trustee of a CLT. If the donor serves as the trustee he or she should avoid retaining the power to determine which charity is entitled to the lead interest or who is entitled to the remainder interest as these powers will cause the value of the CLT to be included in the donor's estate for federal estate tax purposes.<sup>4</sup>
- iii. Charitable Lead Beneficiaries
  1. The charitable lead beneficiaries must be one or more charitable organizations for which an estate tax charitable deduction is allowed under §2055 or a gift tax charitable deduction is allowed under §2522. Since §2055 (estate tax) and §2522 (gift tax) allow a charitable deduction for gifts to foreign charities and private foundations, a CLT's lead interest may be paid to a foreign charity or a private foundation. However, if the CLT is a grantor CLT, an income tax deduction for the lead interest will only be available if it is paid to a domestic charity because an

---

<sup>3</sup> The benefit of the income tax deduction may be offset by two factors. First, the donor of a grantor CLT is taxable on all the income of the CLT during the charitable term. Second, if the donor dies or the CLT otherwise ceases to be a grantor trust during the charitable term, the income tax deduction is "recaptured."

<sup>4</sup> §2036(a)(2); *Rifkind v. United States*, 5 Ct. Cl. 362 (1984). The inclusion of the CLT in the donor's estate can have catastrophic tax consequences especially if most of the term of the lead interest has expired. For example, if the lead interest lasts for 20 years and the donor dies in the 18<sup>th</sup> year, the entire value of the CLT as of the date of death will be included in the donor's estate but the estate will only get an estate tax charitable deduction for the actuarial value of the remaining 2 years left on the charity's lead term. Thus, more will be included in the donor's gross estate than will be excluded by an estate tax charitable deduction.

income tax deduction under §170(f)(2)(B) is allowed only for gifts to domestic charities. In order to obtain an income, estate and gift tax charitable deduction, the charitable lead beneficiaries should be described in §§170(c), 2055(a) and 2522(a) which specify organizations eligible to receive contributions deductible, respectively, for income, estate and gift tax purposes. In addition, if the lead interest of a grantor CLT is payable to a private foundation, the amount of the donor's income tax charitable deduction may be limited under the income tax rules applicable to gifts to private foundations.

2. There is no requirement that the charitable organization entitled to the lead interest be identified by name or that the amount paid to each charitable organization be specified in the trust instrument. The donor can either specify the charity or charities which will receive the lead interest from the trust or leave the selection up to the trustee or someone else each year. Thus, the trustees or other named individuals may be given the discretion to select the charitable beneficiaries.<sup>5</sup> Note that if the donor retains the ability to control the distribution of the lead interest, the donor will be deemed to have retained an interest which would subject the CLT to inclusion in his or her estate for federal estate tax purposes under §2036. For example, if the charity or charities are specified in the trust document, the donor should not have the power to decide about the use of the lead trust property paid to the charity or charities (for example, by being on the board of directors of the charity). If so, the CLT may be included in the donor's estate. In addition, retention by the donor of the ability to control the distribution of the lead interest will result in the lack of a completed gift.<sup>6</sup> If the trustee has the power to choose the charities entitled to payments of the lead interest, the donor should not serve as trustee of the CLT. This problem can be avoided (1) by the donor not retaining the power to control the distribution of the lead interest, (2) having a person other than the donor serve as trustee or (3) providing for an independent trustee to select the charitable lead beneficiary.<sup>7</sup>

---

<sup>5</sup> Rev. Rul. 78-101, 1978-1 C.B. 301; PLR 9331015

<sup>6</sup> Reg. 25-2511-2(b); Rev. Rul. 77-275, 1977-2 C.B. 346.

<sup>7</sup> PLR 9735012; PLR 9629009; PLR 8112039. The IRS held in PLR 9748009 that having the donor's child serve as co-trustee would not cause estate tax inclusion in the donor's estate. In PLR 9304020 the IRS held that language in the trust instrument requesting the trustee consult with the donor's children in selecting the charitable lead beneficiaries would not cause estate tax inclusion for the donor.

- a. The retained powers to avoid in order to prevent the value of the CLT from being included in the donor's gross estate are (1) the right to select, change or add new charitable beneficiaries,<sup>8</sup> (2) the right to apportion payments among the charitable beneficiaries and (3) the right to remove and replace the trustee with a subordinate or related person, including the donor, where the trustee has powers that, if held by the donor, would cause inclusion in the gross estate.
  - b. Note that estate tax inclusion may also result under §2036 where payments from a CLT are made to a private foundation whose directors or officers include the donor of the CLT and the donor has the power to direct the distributions of the private foundation.<sup>9</sup> The IRS has ruled that the CLT will not be includable in the estate of the donor even where the annuity or unitrust payments are made to a private foundation of which the donor is a director or trustee so long as the funds distributed from the CLT to the private foundation are isolated and the donor does not participate in decisions on how to distribute the funds of the private foundation.<sup>10</sup> Alternatively, the donor could resign his position as director or trustee prior to funding the CLT.<sup>11</sup>
3. The trust instrument should (1) name one or more alternative charities to which the lead interest will be paid in case the named charity fails to qualify or (2) authorize the trustee to select one of more charities as lead beneficiaries.
  4. Charitable lead trusts are permitted to include one or more noncharitable income beneficiaries. The portion of the lead interest payable to charity will qualify for a gift tax charitable deduction.<sup>12</sup> The trust instrument must provide that no preference is given to the distributions made to the noncharitable beneficiary. In addition, the trust assets held

---

<sup>8</sup> PLR 200328030; *James Estate*, 68 TC 249 (1977) aff'd 80-1 USTC ¶13327 (5<sup>th</sup> Cir.)

<sup>9</sup> *Rifkind v. U.S.*, 54 AFTR 2d 84-6453 (U.S. Claims Court 1984); Rev. Rul. 72-552, 1972-2 C.B. 525

<sup>10</sup> PLRs 9141017, 9317039, 9350033, 199908002 and 199903045

<sup>11</sup> PLRs 9822021, 9822019, 200138018

<sup>12</sup> Rev. Rul. 77-327, 1977-2 C.B. 353.

for the charitable beneficiaries must be segregated from the assets held for the noncharitable beneficiaries.

- iv. **Remainder Beneficiaries** - The remainder beneficiaries can be virtually any non-charity. Thus, the CLT remainder beneficiary can be the donor or his or her estate, members of the donor's family, a trust or and other non-charitable beneficiary. However, to avoid inclusion of the CLT in the donor's gross estate, the donor should not retain a reversion or the power to select, change or add new remainder beneficiaries.

b. **Types of CLT**

- i. §2055(e)(2) denies an estate tax charitable deduction and §2522(c)(2) denies a gift tax charitable deduction for gifts to trusts in which charity has only a partial interest unless the lead interest meets certain requirements. In order to get an estate tax or gift tax charitable deduction for the value of the lead interest, the lead interest must be in the form of an annuity (charitable lead annuity trust or CLAT) or in the form of a unitrust (charitable lead unitrust or CLUT).<sup>13</sup>

ii. **CLAT**

- 1. The annuity paid by a CLAT must be a fixed dollar amount based on the initial value of the trust payable at least annually. A fixed dollar amount need not be specified. The annuity can be established as a percentage of the assets initially contributed to the trust or by a formula as long as the amount of the annuity is ascertainable at the date of transfer<sup>14</sup> It is generally advisable to use a formula or percentage of the initial fair market value of the assets contributed as finally determined for tax purposes to define the amount of the annuity so that if the value of the gift is increased or decreased by the Internal Revenue Service, the value of the annuity will self adjust to avoid any adverse tax consequences.

- a. **Example:** In January, 2010 donor funds a 20 year CLAT with closely-held stock appraised at \$1,000,000 with an annuity of 6.72% of the value of the assets "as finally determined for federal gift tax purposes." The amount of the annual annuity payable to charity is \$67,200 and the gift tax

<sup>13</sup> §2055(e)(2)(B); §2522(c)(2)(B)

<sup>14</sup> Reg. 20.2055-2(e)(2)(vi) and Reg. 25.2522(c)-3(c)(2)(vi); Reg. 1.170A-6(c)(2)(i)(A).



charitable deduction would be \$999,768. The value of the remainder interest (and the amount of the taxable gift) based on a January, 2010 §7520 rate of 3% is \$232 (\$1,000,000 minus \$999,768). Assume the IRS doubled the value of the closely-held stock on audit to \$2,000,000. If the annuity amount were defined as \$67,200 per year rather than as a percentage of the assets “as finally determined for federal gift tax purposes,” the value of the remainder interest (and the amount of the taxable gift) would increase to \$500,116, possibly resulting in an unexpected federal gift tax. However, since the annuity is defined as a fixed percentage of the initial value of the trust assets “as finally determined for federal gift tax purposes,” the amount of the annuity payable to charity would self-adjust to \$134,400 ( $\$2,000,000 \times 6.72\%$ ) and the value of the remainder interest (and the amount of the taxable gift) would be \$464. In addition, the gift tax charitable deduction would likewise increase to \$1,999,536.

2. The amount of the annuity may fluctuate after the first year as long as the amounts to be paid are ascertainable on the date of the initial transfer to the trust.<sup>15</sup> An increasing annuity is permissible as is one which changes after a set period of years or upon the death of one of the measuring lives. However, an annuity formula that is tied to a fluctuating index (e.g. the Consumer Price Index) is not allowed.
  - a. Assuming the value of the CLAT assets appreciate over the life of the CLAT, the CLAT remainder beneficiaries will benefit if the payments of the lead interest are “back-loaded” i.e. increased over time. This is due to the fact that less is paid out of the CLAT in the earlier years, allowing more assets to stay invested in the CLAT.
  - b. Example: In January, 2010 donor funds a 20 year CLAT with closely-held stock appraised at \$1,000,000 with an annuity of 6.72% of the value of the assets initially transferred to the trust. The §7520 rate is 3%. If the CLAT assets earn 6% per year, \$735,144 passes to the remainder beneficiaries

---

<sup>15</sup> Reg. 20.2055-2(e)(2)(vi) and Reg. 25.2522(c)-3(c)(2)(vi)

at the end of the 20 year term. If the annuity payments are “back-loaded” (start at .84% and increase 20% each year for 20 years instead of a 20 year CLAT paying a 6.72% annuity) and the CLAT earns the same 6% per year, \$1,099,308 passes to the remainder beneficiaries. The “back-loaded CLAT passes \$364,164 (\$1,099,308 minus \$735,144) more to the remainder beneficiaries.

3. The annuity must be paid annually. The amount of the annuity cannot be tied to the income earned by the CLT.<sup>16</sup> If the income of the CLT is insufficient to pay the annuity, the trustee must invade principal to pay the annuity.
4. If the trust income exceeds the annuity amount, the governing instrument may permit the excess income may be paid to the charity<sup>17</sup> but the donor will not be entitled to an additional gift or estate tax deduction.<sup>18</sup>
5. There is no statutory or regulatory prohibition against the donor making additional contributions to the CLAT but it is assumed that a CLAT should not permit additional contributions.
  - a. PLR 8213127 held that additions to a CLAT should be prohibited because the annuity would not be paid from “the property transferred.” However, TAM 9506001 indicates that subsequent additions to a CLAT are allowed. An addition to a CLAT would not generate an additional tax deduction because the addition would not increase the size of the annuity payable to charity.<sup>19</sup>
6. Zeroing out the remainder interest. It is possible with a CLAT to cause the charitable deduction to equal the entire

---

<sup>16</sup> Reg. 20.2055-2(e)(2)(vi)(a) and Reg. 25.2522(c)-3(c)(2)(vi)(a)

<sup>17</sup> Reg. 20.2055-2(e)(2)(vi)(d) and Reg. 25.2522(c)-3(c)(2)(vi)(d)

<sup>18</sup> Increasing the annuity payment would violate the requirement that the annual annuity payment must be “determinable” at the creation of the CLAT. PLR 8034093. The additional contribution would not increase the annuity payable to charity but would instead increase the non-charitable remainder interest. Thus, no additional charitable deduction would arise and a gift would result to the non-charitable remainder beneficiaries.

<sup>19</sup> The annuity amount must be “determinable with certainty” at the time the CLAT is created to qualify for an income, gift or estate tax deduction. Reg. 1.170A-6(c)(2)(i); Reg. 20.2055-2(e)(2)(vi)(a); Reg. 25.2522(c)-3(c)(2)(vi)(a). An increased annuity amount resulting from an additional contribution would not be “determinable with certainty” at the creation of the CLAT. Thus, any additional contribution would not produce an additional income, gift, or estate tax charitable deduction. However, an additional contribution will not affect the deduction produced by the initial contribution.

value of the property transferred to the trust. In that case the taxable gift or bequest upon creation of the CLAT will be zero and no gift or estate tax will be payable. This result happens if the annuity payments are set for a sufficiently long period of time and at a sufficiently high rate (as a percentage of the initial value of the property transferred to the trust) given the relevant §7520 rate so that the value of the charitable interest is equal to the entire value of the property transferred to the trust.

- a. If the annuity payments are structured to end at the death of one or more individuals (as opposed to the end of a term certain), the IRS take the position that it is not possible to zero out the gift.<sup>20</sup>

### iii. CLUT

1. The unitrust paid by a CLUT is an amount equal to a fixed percentage of the net fair market value of the trust, determined and payable annually. If the CLUT increases in value, the unitrust payable to charity increases. If the CLUT decreases in value, the unitrust payable to charity decreases. The valuation of the CLUT may be on a set date (usually the first day of the year) or based on an annual average of several dates or according to any other consistent method provided in the trust instrument or selected by the trustee.<sup>21</sup>
  - a. Although multiple valuation dates may balance fluctuations in the payouts, they are impractical from an administrative perspective. Thus, most CLUTs use one valuation date and generally, the same valuation date or dates are used each year. The valuation date is usually the first business day of the calendar year.
  - b. If the annual valuation date is after the required payment date, the trustee will be required to estimate the future value of the trust assets to

---

<sup>20</sup> Rev. Rul. 77-454, 1977-2 C.B. 351 (if the lead interest lasts for the life of an individual and if the payment of the annuity would exhaust the trust prior to the expiration of the charitable term (assuming the trust earned a rate of return equal to the §7520 rate), the value of the annuity will be limited to an annuity for the shorter of the measuring life or the term of years over which the trust could be expected to make the annuity payments (assuming the trust earned a rate of return equal to the §7520 rate).

<sup>21</sup> Reg. 20.2055-2(e)(2)(vii) and Reg. 25.2522(c)-3(c)(2)(vii)

determine the unitrust amount. This is not recommended.

- c. If the governing instrument does not specify the valuation date or dates, the trustee must select the date or dates on the first tax return the trust is required to file.<sup>22</sup>
2. If the income of the CLUT is insufficient to pay the unitrust amount, the trustee must invade the principal to make the unitrust payment.
3. Unlike a charitable remainder unitrust, a CLUT cannot take the form of a net income only CLUT, a net income with make-up CLUT or a “flip” CLUT.<sup>23</sup>
4. If the trust income exceeds the unitrust amount, the governing instrument may permit the excess income may be paid to the charity but the donor will not be entitled to an additional gift or estate tax deduction.<sup>24</sup>
5. The CLT regulations do not discuss whether additions to a CLUT are permitted. In PLR 8043077 the IRS ruled that a CLUT that allowed additional contributions was qualified and the additional contributions qualified for gift tax purposes. The IRS sample CLUTs contain provisions governing the pro-ration of the unitrust distribution in the year of the addition although the regulations do not contain such a requirement.<sup>25</sup>
6. If a CLUT holds unmarketable or difficult to value assets, a third party qualified appraiser or an independent trustee should be used to value those assets.

#### c. Payout to the Charitable Lead Beneficiary

---

<sup>22</sup> Reg. 20.2055-2(e)(2)(vii); Reg. 25.2522(c)-3(c)(2)(vii).

<sup>23</sup> Rev. Rul. 77-300, 1977-2 C.B. 352; PLR 7918102; A net income option is not available because paying out the lower of the net income or the unitrust amount could reduce the lead payments to charity thereby overvaluing the present value of the income interest.

<sup>24</sup> Reg. 20.2055-2(e)(2)(vii)(d) and Reg. 25.2522(c)-3(c)(2)(vii)(d). Payment of excess income to charity will actually reduce the charitable deduction of a CLUT because the payment of the excess income to charity will reduce the base of assets upon which future year's unitrust payments will be computed. Rev. Rul. 78-183, 1978-1 C.B. 302.

<sup>25</sup> Prior to the issuance of IRS sample CLUT forms, PLRs 7938099 and 8043077 allowed CLUTs permitting additions where the governing instrument provided for calculating the additional charitable deduction as provided in the charitable remainder trust regulations.

- i. Distributions from the CLT must be made annually to the charitable lead beneficiaries. The payment may be made at either the beginning or end of the payment period. The frequency and timing of the distribution will affect the calculation of the charitable deduction.
- ii. There is no minimum or maximum payout from the CLT as there is with a CRT.
- iii. The regulations prohibit a CLT from making payments to a non-charitable beneficiary before the end of the lead term unless the non-charitable payments are made from trust assets that are segregated and administered exclusively for non-charitable purposes.<sup>26</sup>
- iv. If a CLT is created at death, the payment to the charity may be deferred until the end of the taxable year in which the CLT funding is completed. However, interest must be paid on the deferred payment presumably at the same rates that apply to deferred payments under testamentary CRTs.

d. Term of the Lead Interest

- i. A CLT must pay its annuity or unitrust interest for a fixed term of years (e.g. 20 years), or for the life or lives of one or more designated individuals in being when the trust is created (e.g. until the death of the donor and/or the donor's spouse). In addition, a term of years can be added after a measuring life.<sup>27</sup>
- ii. Unlike a CRT, the term of a CLT may extend beyond 20 years<sup>28</sup> limited only by the applicable rule against perpetuities.
- iii. The measuring lives must be one or more of the following individuals: the donor or donor's spouse, and an individual who, with respect to all remainder beneficiaries (other than charitable organizations described in section 170, 2055 or 2522) is either a lineal ancestor or the spouse of a lineal ancestor of those beneficiaries. A trust will satisfy the requirement that all noncharitable beneficiaries are lineal descendants of the individual who is the measuring life, or of that individual's spouse, if there is less than a 15% probability (as computed on the date of transfer to

<sup>26</sup> Reg. 20.2055-2(e)(2)(vi)(f), (vii)(e) and Reg. 25.2522(c)-3(c)(2)(vi)(f), (vii)(e)

<sup>27</sup> Reg. 1.170A-6(c)(2)(i)(A); Reg. 20.2055-2(e)(2)(vi)(a), (vii)(a) and Reg. 25.2522(c)-3(c)(2)(vi)(a), (vii)(a); Rev. Rul. 85-49, 1985-1 C.B. 330 (CLT with term of three lives plus a term of years)

<sup>28</sup> Rev. Rul. 85-49, 1985-1 C.B. 330

the trust) that individuals who are not lineal descendants will receive any trust corpus.<sup>29</sup>

1. Note that nieces and nephews are excluded as potential remainder beneficiaries.
2. Beware of “family disaster” clauses. A CLT may be disqualified if the trust provides that if the named remainder beneficiaries die the heirs at law become the remaindermen. The heirs at law may include collaterals (as opposed to lineal) heirs. The mere existence of such a clause may disqualify the CLT.
3. If the remainderman is a trust for the benefit of a lineal descendant, a lineal descendant should not have a testamentary power of appointment that would allow appointment to a non-lineal descendant.
4. An interest payable for a specified term of years can qualify as a guaranteed annuity or unitrust interest even if the CLT contains a savings clause intended to comply with the rule against perpetuities as long as the savings clause utilizes a vesting period of 21 years after the death of measuring lives who will maximize rather than limit the term of the trust.<sup>30</sup>
5. The IRS will not disallow the charitable deduction for a CLT whose measuring life does not comply with the above rule if the CLT is reformed into a lead interest payable for a specified term of years. Generally, the reformation must be made for an inter vivos CLT by October 15 of the year following the year in which the transfer is made or for a testamentary CLT by the date prescribed by §2055(e)(3)(C)(iii).

#### e. Private Foundation Restrictions

- i. A split interest trust, like a CLT, is subject to certain private foundation rules.<sup>31</sup>

---

<sup>29</sup> Reg. 1.170A-6(c)(2); Reg. 1.170-6(e); Reg. 20.2055-2(e)(2)(vi)(a), (vii)(a) and Reg. 25.2522(c)-3(c)(2)(vi)(a), (vii)(a). The rule limiting the individuals who may be used as measuring lives of a CLT was adopted to eliminate situations where a seriously ill (but not terminally ill) individual unrelated to the donor is used as the CLT measuring life. Using unrelated seriously ill individuals as the lead term measuring life artificially inflates the charitable deduction if the seriously ill individual dies before his life expectancy in the IRS actuarial tables.

<sup>30</sup> Reg. 20.2055-2(e)(2)(vi); Reg. 20.2522(c)-3(c)(2)(vi); PLR 8104213; PLR 9721006.

<sup>31</sup> §508(d)(2) and §4947(a)(2). Reg. 1.508-3(d) states that if state law imposes the private foundation rules on the trustees, the trust document need not impose those private foundation rules. However, it is probably

- ii. Under §4947(a)(2) the trust document must contain terms prohibiting the trust from engaging in acts of self dealing<sup>32</sup> and from making certain types of expenditures.<sup>33</sup> Absent such language the trust will not constitute a qualified CLT from which a charitable deduction is available.<sup>34</sup>
- iii. In addition, unless the deductible value of the lead interest is less than 60% of the fair market value of the trust assets and the entire income interest (and none of the CLT's remainder interest) is devoted to charitable purposes, the CLT is subject to the prohibitions against excess business holdings<sup>35</sup> and jeopardy investments.<sup>36</sup> In other words, the prohibitions relating to excess business holdings and jeopardy investments under §§4943 and 4944, respectively, need not be included in the CLT document if the present value of the charitable interest on the date of funding does not exceed 60% of the aggregate value of all amounts in the trust and no property is distributable to charity at the end of the charitable term.
  - 1. For a nongrantor CLT, the cost of avoiding the excess business holding rules requires subjecting at least 40% of the trust to the gift or estate tax.
  - 2. Reg. 20.2055-2(e)(2)(vi)(e) and Reg. 25.2522(c)-3(c)(2)(vi)(e) require the CLAT contain a provision

---

best to include the private foundation restrictions in the trust document to be sure that the trust is subject to those restrictions.

<sup>32</sup> §4941(d). Self-dealing is defined generally to mean certain transactions (e.g. certain sales, leases, loans furnishing of goods and services or use of trust property, payment of compensation) between a CLT and a "disqualified person." A disqualified person includes a substantial contributor (a person who contributes more than \$5,000 or a person who owns more than 20% of (1) the voting power of a corporation, (2) a profit interest of a partnership or (3) the beneficial interest in a trust or unincorporated organization, where the entity is a substantial contributor to the CLT), the donor, his spouse, descendants and their spouses, the donor's ancestors, the trustees of the CLT, and corporations, partnerships and trusts in which the donor and his family, or the trustee and his family hold, 35% or more of the voting power, profits interest or beneficial interest.

<sup>33</sup> §4945. This section prohibits the trust from making taxable expenditures, including transfers for non-charitable purposes and transfers to private foundations unless the CLT exercises expenditure responsibility over the payments.

<sup>34</sup> §508(d)(2)(A)

<sup>35</sup> §4947(b)(3) and §4943. A CLT will be deemed to have excess business holdings if the CLT, together with all of its disqualified persons, owns more than 20% of the voting stock of a corporation or an equivalent interest in a non-corporate entity engaged in a trade or business. A CLT with excess business holdings is granted five years to reduce the holdings (of the combination of the CLT and all disqualified persons) to no more than 2%.

<sup>36</sup> §4947(b)(3) and §4944

prohibiting both the purchase and retention of jeopardy investments.

3. The restriction against excess business holdings may require a donor funding a CLT with closely held stock to limit the deductible value of the lead interest if the donor or the donor's family owns 20% or more of the interests in a closely held business.

f. Forms.

- i. The IRS has issued sample CLAT trust documents in Rev. Proc. 2007-45, 2007-29 IRB 89 (June 22, 2007) and Rev. Proc. 2007-46, 2007-29 IRB 102 (June 22, 2007). In addition, the IRS has issued sample CLUT trust documents in Rev. Proc. 2008-45, 2008-30 IRB 224 (July 24, 2008) and Rev. Proc. 2008-46, 2008-30 IRB 238 (July 24, 2008). If the trust is substantially similar to the trust set forth in the sample trust form (or properly integrates one or more of the alternate provisions into a trust document that is substantially similar to the IRS sample trust form), and if valid under state law and property administered, the value of the charitable lead interest will be deductible under §2522(c)(2)(B) or §2055(e)(2)(B) and the payment of the annuity or unitrust amount to the charitable lead beneficiary will be deductible from the gross income of the CLT to the extent provided in §642(c)(1).
- ii. Sample CLAT documents. Rev. Proc. 2007-45 contains a sample trust document of an inter vivos nongrantor CLAT and inter vivos grantor CLAT. Rev. Proc. 2007-46 contains a sample trust document for a testamentary CLAT.
- iii. Sample CLUT documents. Rev. Proc. 2008-45 contains a sample trust document of an inter vivos nongrantor CLUT and inter vivos grantor CLUT. Rev. Proc. 2008-46 contains a sample trust document for a testamentary CLUT.
- iv. The revenue procedures specifically note that a CLT trust document that contains provisions in addition to those contained in the IRS sample trust form or omits any of the sample trust form provisions "will not necessarily be ineligible for the relevant charitable deduction(s), but neither will that trust (or contributions to it) be assured of qualification for the appropriate charitable deductions."

g. Reformation of Defective CLT



- i. A defective CLT may be reformed thereby qualifying the CLT for the gift tax or estate tax charitable deduction.<sup>37</sup>
- ii. Savings clause. To ensure that the document constitutes a qualified nongrantor CLT, the document should contain a savings clause such as the following language used for a CLAT:  
“Notwithstanding other provisions of this document, no powers granted herein may be exercised by the trustee if such exercise would in any way defeat the intent of the donor that the trust qualify as a charitable lead annuity trust so that the value of the annuity interest passing to the charitable beneficiaries hereunder is deductible as a charitable guaranteed annuity under §2055(e)(2)(B) and §2522(c)(2)(B) and that the payment of the annuity amounts to the charitable beneficiaries will be deductible from the gross income of the trust as provided under §642(c)(1).”

### III. Tax Consequences of CLT

#### a. To the Donor

##### i. Gift Tax

1. A donor who creates a CLT during life faces the potential of making a taxable gift in the amount of the present value of the remainder interest in the property transferred to the trust at the time the CLT is created i.e. the taxable gift will be equal to the value of the remainder interest which will pass to the non-charitable beneficiary after the charitable lead interest ends. The gift is a gift of a future interest and does not qualify for the §2503 gift tax annual exclusion.<sup>38</sup>
2. The donor may avoid a taxable gift if (1) the remainder reverts to the donor or the donor's estate or (2) the donor retains such powers over the remainder interest which prevents the transfer for being a completed gift. However, this will result in estate tax inclusion.
3. The donor is entitled to a gift tax charitable deduction for the actuarial value of the charity's lead interest assuming the transfer is a completed gift.<sup>39</sup>
  - a. For a CLAT, the value of the taxable gift is the value of the property transferred to the CLAT less

---

<sup>37</sup> §2055(e)(3) and §2522(c)(4)

<sup>38</sup> Reg. 25.2503-3(a)

<sup>39</sup> §2522(c)(2)(B); Reg. 25.2522(c)-(3)(c)(vi) and (vii).

the value of the charity's annuity. For a CLUT, the value of the taxable gift is determined by multiplying the unitrust factor by the value of the property transferred to the CLUT. The actuarial value depends on several factors, such as the length of the charitable interest, how frequently during the year the charitable payments will be made (e.g. monthly, quarterly, annually), the size of the annuity or unitrust payments and in the case of a CLAT, the §7520 rate used to value the annuity stream of payments. The §7520 rate is mostly unimportant for a CLUT.

- b. The valuation is determined by using the applicable §7520 rate<sup>40</sup>. The donor may choose to value the lead interests based on the §7520 rate for the month in which the trust created and funded or for either of the two preceding months.<sup>41</sup> The §7520 rate is redetermined monthly by the IRS and is published about the 20<sup>th</sup> or 21<sup>st</sup> day of the current month. Thus, as a practical matter, a donor has the ability to use the best of four possible rates – the rate for each of the two months preceding the date of transfer, the rate for current month or delay the transfer until the following month and use the rate for the following month.
- c. CLT for measuring life. The IRS actuarial tables must be used unless death of the measuring life is imminent. An individual who is known to have an incurable illness or other deteriorating physical condition is considered terminally ill if there is at least a 50% probability that the individual will die within 1 year. However, the individual will be presumed to have not been terminally ill at the time of the transaction if he survives for 18 months or longer after the date of the transaction unless the contrary is established by clear and convincing evidence.<sup>42</sup>
- d. Exhaustion test for term determined by a measuring life. If the annuity will not be payable for the entire

---

<sup>40</sup> The §7520 rate is equal to 120% of the Federal mid-term rate in effect under §1274(d)(1) (compounded semi-annually), rounded to the nearest 2/10 of 1%.

<sup>41</sup> §7520(a)

<sup>42</sup> Reg. 1.7520-3(b)(3); Reg. 20.7520-3(b)(3); Reg. 25.7520-3(b)(3).

period of the lead term if, using the applicable §7520 rate, the annuity is expected to exhaust the trust before the last annuity payment is paid in full, a special factor must then be used that takes into consideration the facts and circumstances that may exhaust the trust and the standard §7520 rate factor cannot be used.<sup>43</sup> The result is that the value of the annuity will be limited to an annuity for the shorter of the measuring life or the term of years over which the trust could be expected to make the annuity payments if the trust produced a rate of return equal to the assumed §7520 discount rate.<sup>44</sup>

- e. Affect of §7520 rate on the value of the annuity. The lower the §7520 rate, the higher the charitable deduction for the annuity interest. On the other hand, the higher the §7520 rate, the lower the charitable deduction for the annuity interest. The §7520 rate has little impact on the charitable deduction for a CLUT.
  - i. A CLAT has the potential for the maximum amount of assets to be passed to non-charitable beneficiaries if it is established in a low §7520 interest rate environment. Thus, in a low interest rate environment (like 2009 and 2010), the amount of the annuity payment to charity can be set at a much lower rate than in a high interest rate environment thereby increasing the chance that a greater amount of the trust will pass to the non-charitable remainder beneficiaries.
  - ii. CLUTS are not interest rate sensitive so a CLUT is a better choice in a high §7520 rate environment.
- f. A CLAT can be an effective gift leveraging device in a period of low interest rates. If the investment performance of the CLAT is higher than the §7520 rate, the amount earned in excess of the §7520 rate will pass to the remainder beneficiaries (e.g. donor's children) free of transfer tax.

---

<sup>43</sup> 25.7520-3(b)(2)(i); Rev. Rul. 77-454, 1977-2 C.B. 351.

<sup>44</sup> Rev. Rul. 77-454, 1977-2 C.B. 351. The Rev. Rul. 77-454 rules do not apply to CLUTs.

ii. Estate tax

1. If the CLT is established at death (e.g. a testamentary CLT) the same valuation rules apply as discussed above for gift tax purposes in determining the charitable deduction for the lead interest and the size of the taxable transfer (e.g. the value of the remainder interest). However, unlike the ability to use up to four §7520 rates, the valuation of the interest includible in the decedent's estate for estate tax purposes is calculated as of the date of the decedent's death or the alternate valuation date (e.g. six months after the date of death) if the election to use the alternate valuation date under §2032A is available.
2. CLATs provide the same leveraging ability at death as during life. A testamentary CLT can be structured to zero out or almost zero out the value of the taxable remainder interest. If there are assets in the estate which have a significant potential for post-death appreciation, a CLAT can achieve tremendous benefits for the donor's children.
3. The major problem with drafting a zeroed out testamentary CLAT is that the §7520 rate applicable at death will not be known at the time the CLAT is drafted. The rate will only become known at the donor's death. The solution to this problem is to draft the testamentary CLAT using a formula to determine the size of the annuity which will produce the desired remainder value. Such a technique has been approved by the IRS.<sup>45</sup>
  - a. Sample formula language to zero out the remainder interest of a testamentary CLAT: "The annuity amount shall be equal to that percentage of the initial net fair market value of all property passing to this trust, as finally determined for federal estate tax purposes, as shall produce a present value guaranteed charitable annuity interest and estate tax charitable deduction equal to (or as nearly equal as possible) 100% of the initial net fair market value of the entire trust fund, when applying the valuation principles of §7520 of the Internal Revenue Code, its regulations and applicable Internal Revenue Service and Treasury guidelines."

---

<sup>45</sup> PLR 9128051, 9118040, 9631021 and 9840036

4. Payment of estate tax. A CLT may be includable, in whole or in part, in the donor's gross estate if (1) the donor retains control over the distribution of the lead interest or (2) if the property in the trust reverts to the donor's estate at the end of a fixed term. In the case of a charitable remainder trust (CRT), the IRS has ruled that a CRT will not qualify for tax benefits unless any estate tax liability attributable to the CRT is paid from sources other than the CRT assets.<sup>46</sup> The annotations to the sample forms for both a testamentary CLAT and CLUT indicate that estate taxes may be paid from assets used to fund the CLT, stating that if "estate or other death taxes are paid from the assets used to fund a testamentary CLAT [or CLUT], the amount deductible under §2055 is the amount that passes to charity, reduced by the amount of estate and death taxes paid." The more estate or death taxes paid from the assets otherwise passing to a testamentary CLT, the less the estate tax charitable deduction and the greater the estate tax. A CLT should be drafted with language that obligates any estate tax liability attributable to the inclusion of the CLT in the donor's estate be paid from assets other than the assets in the CLT.<sup>47</sup>

iii. Generation skipping tax.

1. The generation skipping tax (GST) is an important issue if the remainder interest in the CLT is distributable, in whole or in part, to the donor's grandchildren or more remote descendants or any individuals who are two or more generations below the donor i.e. so called "skip persons."
2. The GST tax is imposed when the trust terminates in favor of a skip person (a "taxable termination") or when distributions are made to skip persons (a "taxable distribution"). The GST tax is not imposed at the time a CLT is established because the charity is assigned to the same generation as the donor.<sup>48</sup> Thus, a CLT is not subject to GST tax until the charitable lead interest expires.
3. The predeceased child exception. The predeceased child exemption allows a grandchild to be bumped up a generation to his or her parent's generation if the grandchild's parent died before the CLT is established. If the predeceased child exception applies and the grandchild

---

<sup>46</sup> Rev. Rul. 82-128, 1982-2 C.B. 71

<sup>47</sup> PLR 9348012 (example of governing instrument language regarding payment of the estate tax)

<sup>48</sup> §2651(f)(3)

is deemed to be bumped up into his or her parent's generation, any distribution of CLT assets to the grandchild will not result in a generation skipping tax because the child, being assigned to his or her parent's generation, is not a skip person. Note that the predeceased child exception only applies if the grandchild's parent has died prior to the funding of the CLT. If the donor's child is alive at the time the CLT is funded but dies before the CLT's lead interest terminates, a distribution to the grandchild will be a taxable termination or taxable distribution subject to the GST tax. The Tax Reform Act of 1997 extends the predeceased child exception to taxable terminations and taxable distributions as well as to direct skips. The 1997 Tax Reform Act also extended the predeceased child exception to non-lineal descendants provided that the descendants and the donor have a common ancestor and the donor has no living descendants of his or her own. For example, a donor who has no children or grandchildren can establish a CLT for the benefit of a deceased niece or nephew without creating a GST liability.

4. Allocation of the GST exemption. (Caution: This outline was prepared in January, 2010. As a result of EGTRRA of 2001 the estate and GST tax was repealed for one year as of January 1, 2010 and is scheduled to be re-instituted in 2011 with a maximum 55% rate and a \$1,000,000 exemption. There is a possibility that Congress will make changes to the estate and GST tax in 2010 and those changes may be retroactive to January 1, 2010. At this point, it is impossible to know what the estate tax and GST tax will look like going forward so for purposes of discussion this outline assumes the 2009 estate and GST tax rules apply i.e. a 45% estate and GST rate and a \$3,500,000 exemption.) The generation skipping tax provides an exemption from the GST. The amount of the exemption in 2009 was \$3.5 million. A donor can allocate his GST exemption to a CLT to eliminate or lessen the impact of any potential GST. The rules for allocating the GST exemption differs for CLUTs and CLATs.
  - a. Background of calculating the GST. The GST is imposed on the amount of the distribution as a taxable termination or a taxable distribution at a flat rate of 45% (for 2009). The GST rate is lowered or eliminated if the donor allocates some or all of his GST exemption to the trust.

- i. If GST exemption is allocated to the CLT, the CLT has an inclusion ratio of less than 1 for purposes of calculating the tax. If a trust's inclusion ratio is 1, GST is imposed at the full 45% rate on the property distributed. If the inclusion ratio is zero, no GST is imposed. If the inclusion ratio is between 0 and 1, the effective rate of GST is between 0% and 45%. The inclusion ratio is determined by deducting the applicable fraction from 1. The applicable fraction is a fraction, the numerator of which is the amount of GST exemption allocated to the trust and the denominator of which is the value of the property transferred to the trust, less (among other things) any charitable deduction allowed under §2055 or §2522 with respect to the trust.<sup>49</sup>
- b. Allocating GST exemption to a CLUT. The rules for allocating the GST exemption to a CLUT are much more straightforward than for the allocation of the GST exemption to a CLAT. If the donor allocates GST exemption at the time of funding the CLUT equal to the gift tax value of the remainder interest, the CLUT will be entirely exempt from GST tax regardless of the value of the CLUT at the termination of the charitable lead interest. The applicable fraction of a CLUT can be determined with certainty at the funding of the CLUT which is not the case with a CLAT. The applicable fraction of a CLUT is equal to the amount of the GST exemption allocated to the trust divided by the fair market value of the property transferred to the trust reduced by the deductible value of the charitable lead interest.<sup>50</sup>
  - i. If the GST tax exemption is allocated late, the fair market value of the trust on the date of the late allocation is used in the denominator of the inclusion ratio. As an alternative, the donor can use the fair market value of the trust assets on the first day of

---

<sup>49</sup> §2642(a)(2)

<sup>50</sup> Id.

the month during which a late allocation is made.

- c. Example: Donor establishes a \$1 million, 20 year term CLUT with remainder payable to his grandchildren. The §7520 rate for May, 2009 is 2.4%. The unitrust payout is 8%. The donor will get a charitable deduction of \$806,365. The donor allocates \$193,635 of his GST exemption at the time he establishes the CLUT. His GST inclusion ratio is  $1 - \frac{193,635}{1,000,000 - 806,365}$  or zero. At the termination of the trust the inclusion ratio of the CLUT is 0 regardless of the value of the trust at termination. Since the inclusion ratio is 0, no GST is payable when the property is distributed to the donor's grandchildren.
- d. Allocating GST exemption to a CLAT. The allocation of GST exemption to a CLAT is much more difficult and will not allow the donor to know the CLT's exposure to GST until the lead interest terminates. Allocating GST exemption to a CLAT involves a "wait and see" approach.<sup>51</sup> Even though the GST exemption may be allocated to the CLAT at the time the CLAT is funded, the inclusion ratio is not determined until the lead annuity interest terminates. The amount of GST exemption allocated to the CLAT is an "adjusted" GST exemption. The GST exemption allocated to the CLAT upon funding is adjusted or increased by assuming the GST exemption earned interest during the term of the lead interest in an amount of the §7520 rate used to calculate the charitable deduction for the value of the lead interest at the time of funding. In other words, during the CLAT term, the amount of the GST exemption allocated to the trust is annually compounded by the §7520 rate. More specifically, the applicable fraction is a fraction, the numerator of which is the *adjusted* GST exemption and the denominator of which is the value of all the property in the trust immediately after the termination of the charitable lead annuity. The adjusted GST exemption is an amount equal to the GST exemption allocated to the trust increased by the interest determined at the §7520 rate used in

---

<sup>51</sup> §2642(e); Reg. 26.2642-3



determining the deduction for the charitable lead annuity and for the actual period of the annuity.<sup>52</sup> In other words, the adjusted GST exemption is the amount of the exemption assigned to the CLAT compounded annually by the §7520 rate used to value the charitable lead interest over the duration of the lead interest.

- i. As a result, the donor will not know the applicable fraction and the potential exposure to GST until the lead annuity terminates. This drastically reduces the ability to leverage the GST exemption.
- ii. Allocation of the GST tax exemption can be made by formula i.e. the allocation may be stated as the amount necessary to produce an inclusion ratio of zero.
- iii. Bottom line regarding allocating GST exemption to a CLAT: If the value of the trust grows faster than the applicable §7520 rate at the time of funding, the GST exemption will not be sufficient to shield the CLAT from potential GST. On the other hand, if value of the trust grows slower than the applicable §7520 rate at the time of funding, GST exemption will be wasted. Only if the growth rate of the trust equals the applicable §7520 rate at the time of funding will the GST exemption exactly equal the value of the trust at the termination of the lead interest. Thus, caution must be exercised in establishing a CLAT with skip persons (e.g. grandchildren) as remainder beneficiaries.
- iv. Example: Donor establishes a \$1,000,000 20 year term CLAT with the remainder payable to his grandchildren. The May, 2009 §7520 rate is 2.4%. The annuity is 5%. The donor will get a charitable deduction \$786,870. The donor allocates \$213,130 of his GST exemption at the time of the transfer. The

---

<sup>52</sup> §2642(e)

exposure of the trust to the GST depends on the growth of the trust assets.

If the trust assets grow at a rate of 2.4% (the §7520 rate):

Value of trust at end of year 20:	342,484
Adjusted GST exemption (\$213,130 compounded annually at the initial 2.4% §7520 rate)	342,484

Inclusion ratio  $1 - 342,484/342,484 = 0$

If the trust assets grow at a rate of 6% (3.6% in excess of the §7520 rate);

Value of trust at end of year 20:	1,367,856
Adjusted GST exemption (\$213,130 compounded annually at the initial 2.4% §7520 rate)	342,484

Inclusion ratio  $1 - 342,484/1,367,856 = .74962$

In this situation when the trust terminates the GST tax payable is  $\$1,367,856 \times .74962 \times 45\% = \$461,417$ . The effective rate of tax is 33.73%. To prevent the imposition of the GST, the donor would have to have allocated \$851,219 of GST exemption when the trust was established – that is the amount of GST exemption which, when compounded annually at the §7520 rate of 2.4% will result in an adjusted GST exemption at the end of year 20 of \$1,367,856. Alternatively, if the donor were still alive at the end of the 20 year term and had enough GST exemption remaining, he could allocate \$1,025,372 of additional GST exemption to eliminate the GST tax liability.

- v. Conclusion. A CLUT provides certainty as to the GST consequences at termination but generally does not give the ability to leverage a gift. A CLAT results in uncertain

GST consequences but can yield significant gift and estate tax leveraging. The major disadvantage of a CLAT is that the trust will most likely have a fractional inclusion ratio at the expiration of the lead interest. As a result, the adverse GST consequences limit the usefulness of a CLAT if the remainder beneficiaries of the CLAT are skip persons i.e. the donor's grandchildren or more remote generations. Despite GST issues with a CLAT, some donors may elect to use a CLAT if *all* of the remainder beneficiaries are skip persons as opposed to having both skip (e.g. grandchildren) and non-skip (e.g. children) persons as CLAT remaindermen. If there was insufficient GST exemption allocated at the time the trust was originally funded and additional GST exemption cannot be made at the termination of the lead interest because the donor has used the balance of his GST exemption or died before the termination of the lead interest, a CLAT with all skip persons (e.g. grandchildren) will have the GST tax apply once at the termination of the lead interest (since all of the remaindermen are skip persons, it is taxed as a taxable termination at the termination of the lead interest) rather than being subject to the GST tax every time distributions are made to grandchildren and more remote beneficiaries.

Example: Donor establishes a \$1 million 20 year 5% CLAT. The May, 2009 §7520 rate is 2.4%. The value of the remainder interest and the amount of the gift is \$213,130. The donor allocates \$213,130 of his GST exemption to the CLAT. If the trust has an 8% rate of return, the trust will have a value of \$2,372,859 at the end of the 20 year term. The adjusted GST exemption is \$342,487. The trust has an inclusion ratio of .855665.

If the CLAT terminates in favor of a trust for the donor's grandchild (a skip person), there is a taxable termination at the end of the lead

term and a GST of \$913,668 ( $2,372,859 \times .855665 \times 45\%$ ), leaving a trust balance of \$1,459,191 ( $2,372,859 - 913,668$ ). All future distributions to the grandchild are free of GST tax and any other transfer tax.

If the CLAT terminates in favor of a trust for the donor's child (non-skip) and grandchild (skip person), no GST tax is due when the lead trust terminates because the donor's child (a non-skip person) has an interest in the trust. However, subsequent distributions to the grandchild during the donor's child's life will be subject to GST of 38.51% ( $.855665$  inclusion ration  $\times 45\%$  GST rate). When the donor's child dies there will also be a GST tax of 38.51% on the then entire value of the trust. Thereafter, no distributions to the grandchild will be subject to GST tax.

- e. The liability for payment of the GST tax as a result of a taxable termination is the responsibility of the trustee and is paid from the remainder interest prior to distribution to the remaindermen. §2603(a)(2).

#### iv. Income Tax - Donor.

##### 1. Non-grantor lead trust.

- a. The donor of an inter vivos non-grantor lead trust does not receive an income tax charitable deduction for the value of the lead interest.<sup>53</sup> Instead, the CLT gets an unlimited fiduciary income tax charitable deduction for the amount paid to the charitable lead beneficiary.
- b. The income earned by the CLT is not taxable to the donor. Instead the income is reported by the CLT.
- c. Since the income earned by the CLT is excluded from the donor's income tax return, a CLT may be an attractive income tax planning device for a donor who has reached his AGI deduction limits with respect to his or her charitable gifts.

---

<sup>53</sup> §170(f)(2)(B); Reg. 1.170A-6(c)

## 2. Grantor lead trust.

a. If the donor is treated as the owner of the deductible interest (not just the income interest) under the grantor trust rules and the trust otherwise meets the estate and gift tax requirements, the donor will receive a one-time income tax charitable deduction at the creation of the trust for the value of the lead interest.<sup>54</sup> The donor does not receive any deduction for the annual trust payments to charity.

i. If the lead interest is held by a public charity (normally subject to a 50% of AGI limit), the deduction is subject to the 30% AGI limitation (for cash gifts) as a gift “for the use of” the charity (because it is held in trust), with a five year carryover for any amount in excess of the AGI limit.<sup>55</sup>

ii. If the lead interest is held by a private nonoperating foundation (normally subject to a 30% of AGI limit), the deduction is subject to the 20% of AGI limit. PLR 8824039 held that the five year carryover is not available for a CLT benefiting a private foundation but that ruling appears to be wrong.

iii. The income earned by a grantor CLT is fully taxable to the donor during the term of the trust with no offsetting income tax charitable deduction for the annual payments from the trust to charity. This is so despite the fact that all or a significant portion of the income will be paid to charity and none of the income is paid to the donor. The net effect to the grantor is that his income tax is deferred via the upfront charitable deduction at the time the trust is funded rather than an elimination of the tax liability. The donor may find that the present value of the upfront income tax charitable deduction will be greater than the present value of the future tax burden on the trust income especially if

---

<sup>54</sup> §170(f)(2)(B) and §671, et. seq.

<sup>55</sup> §170(b)(1)(B)(i)

tax rates decline in the future. If the donor will be able to use the income tax deduction at a higher income tax rate than the rate at which he or she will be taxed on the trust income in later years, the donor may be better off structuring the CLT as a grantor trust for income tax purposes. For example, if lead trust is invested in municipal bonds (ignoring, for the moment, the trustee's fiduciary duty to diversify), the donor will not have an income tax liability as the municipal bond interest is nontaxable.

iv. Recapture of income tax charitable deduction if donor dies during the lead term of the trust. If the donor dies during the lead term of the trust (or otherwise ceases to be treated as the owner of the trust for income tax purposes), all or part of the income tax charitable deduction will be recaptured.<sup>56</sup> The donor must recognize as income an amount equal to the amount of the deduction the donor received when the trust was funded, reduced by the present value on the date of the trust's creation of all amounts that were required to be, and actually were, paid to the lead charitable beneficiaries before the donor's grantor trust status ceased.<sup>57</sup>

1. If the recapture occurs because of the donor's death, the income is included on the donor's final income tax return. It is not income in respect of a decedent under §691.
2. If the CLT ceases to be a grantor trust, the trust continues and is taxed as a complex trust.

v. How to structure a CLT as a grantor trust.

1. One way to make a CLT a grantor trust is to give the grantor or the

---

<sup>56</sup> §170(f)(2)(B); Reg. 1.170A-6(c)(4)

<sup>57</sup> §170(f)(2)(B); Reg. 1.170A-6(c)(4) and (5), Example 3.

grantor's spouse a reversion (right to get the trust property back at the end of the lead interest) having a value greater than 5% of the value of the trust at inception of the trust.

However, if the trust property reverts to the donor or his or her spouse, the CLT will be included in the donor's gross estate for estate tax purposes.

2. Another way to make the CLT a grantor trust but at the same time avoid estate tax inclusion is to have the remainder pass into a trust from which the trustee (someone other than the donor or his or her spouse) can pay the entire corpus to the spouse. The reversion to trust for the benefit of the spouse would be valued at more than 5% of the value of the trust because the maximum exercise in favor of the donor's spouse (or the donor) is presumed for purposes of determining if the present value of the interest of the spouse or the donor is more than 5%.<sup>58</sup>

3. Another way to make the CLT a grantor trust is to give the donor the power to substitute property of equivalent value<sup>59</sup> or a power to loan trust property to the donor without adequate interest or security.<sup>60</sup> However, giving the donor either of these powers would cause the trust to fail to be a qualified CLT because a CLT cannot engage in any act of self-dealing described in §4941.<sup>61</sup> An act of self dealing is any economic transaction between the trust and any person who is a

---

<sup>58</sup> §673(c)

<sup>59</sup> §675(4)(C)

<sup>60</sup> §675(2)

<sup>61</sup> §4947(a)(2)

“disqualified person” as defined in §4946. The exercise and probably the mere existence of these powers is most likely self-dealing.

4. A better option is to give someone other than the donor or another “disqualified person” the power in a non-fiduciary capacity to substitute property of equivalent value.
  - a. Sample language: “[Individual] other than the donor, the trustee or a disqualified person as defined in §4946(a)(1)] shall have the right, exercisable only in a nonfiduciary capacity and without the consent or approval of any person acting in a fiduciary capacity, to acquire any property held in the trust by substituting other property of equivalent value.”
  - b. A power to substitute property with property of equivalent value, even if held by the donor, will not cause estate tax inclusion. Rev. Rul. 2008-22, 2008-16 I.R.B. 796.

#### b. How the CLT is Taxed

##### i. Non-grantor lead trust.

1. A CLT is taxed as a complex trust under the normal rules applicable to trusts. Unlike a CRT, it is not exempt from income tax.<sup>62</sup>
2. The donor of a nongrantor CLT does not receive an income tax charitable deduction upon the funding of the trust or at any time thereafter but he is not required to recognize any of the taxable income earned by the trust.

---

<sup>62</sup> A special 100% excise tax applies if a CRT has any unrelated business taxable income. §664(c).



3. A CLT is entitled to an unlimited income tax charitable deduction for the amounts paid from the CLT to the charitable lead beneficiary<sup>63</sup> unless the CLT has any unrelated business taxable income.
  - a. To be entitled to an income tax charitable deduction under §642(c), the payments must be made (1) pursuant to the terms of the governing instrument and (2) paid out of gross income (in the tax sense).<sup>64</sup> If the lead payment is not made out of gross income, it is not deductible.
4. One of the benefits of a non-grantor CLT is the avoidance of the income tax charitable deduction limitations applicable to individuals. This is especially beneficial if the donor's charitable contributions are so large that the donor is not able to fully deduct those contributions for income tax purposes.
  - a. Although a nongrantor CLT is not exempt from income tax, it may ultimately be the equivalent of a tax-exempt entity due to the income tax charitable deduction available to the lead interest under §642(c)(1).
  - b. §681 generally disallows an income tax charitable deduction to the extent the payment to charity consists of unrelated business taxable income.<sup>65</sup> Despite the disallowance of the charitable deduction for unrelated business taxable income under §681, §512(b)(11) offers partial relief. Specifically, if the lead interest of a CLT is held by a domestic charity and the payment to charity consists of unrelated business taxable income for the year in question, the income tax charitable deduction for the amount of the unrelated business taxable income payable to charity is subject to the percentage limitations applicable to individuals.<sup>66</sup> The deductibility ceilings are applied against the unrelated business taxable income, not the trust's entire income.<sup>67</sup> If

---

<sup>63</sup> §642(c); Reg. 1.642(c)-1(a)(2). If the income of the CLT in one year is less than the amount required to be paid to satisfy the lead payout, the balance may not be carried forward to subsequent years.

<sup>64</sup> Rebecca K. Crown Income Charitable Fund, 8 F.3d 571 (7<sup>th</sup> Cir. 1993)

<sup>65</sup> Reg. 1.642(c)-3(d)

<sup>66</sup> §681(a); Reg. 1.681(a)-2(a).

<sup>67</sup> §512(b)(11)

the CLT has unrelated business taxable income the benefit of a CLT are diminished because the charitable deduction for the unrelated business taxable income is limited. Thus, the trust income (including the unrelated business taxable income) is paid to charity but to the extent the fiduciary income tax charitable deduction is denied for part of the unrelated business taxable income, the trust will be exposed to additional income tax on the non-deductible portion of the unrelated business taxable income paid to charity.

5. The CLT is taxable on undistributed income in excess of the amount required to satisfy the lead payout. The income tax rates for trusts are highly compressed. For 2010 a trust is taxed at the highest tax rate (35%) for income over \$11,200.
6. If a CLT distributes appreciated property to satisfy the lead payout, the distribution is treated as if the CLT sold the appreciated property and distributed cash.<sup>68</sup> This will trigger recognition of the gain by the CLT.<sup>69</sup> The gain, however, will be treated as having been paid to charity so that the CLT will be entitled to an income tax charitable deduction under §642(c).<sup>70</sup>
7. A trust may take an income tax charitable deduction for the current year as long as the amount is paid to the charity in the current year or before the last day of the subsequent year.<sup>71</sup> Thus, if the lead payment is paid after the close of the taxable year and before the last day of the following year, the trustee may elect to treat the charitable payments as being made in the preceding year.
  - a. The trustee makes the election by filing a statement with the return for the year in which the contribution is considered paid.
8. Unless the trust document specifically states otherwise, amounts paid from the trust to charity are deemed to consist of a proportionate amount of each class of income earned

---

<sup>68</sup> Rev. Rul. 83-75, 1983-1 C.B. 114; Kenan v. Comm., 114 F.2d 217 (2d Cir. 1940)

<sup>69</sup> PLR 200920031

<sup>70</sup> Rev. Rul. 83-75, 1983-1 C.B. 114.

<sup>71</sup> §642(c)(1); Reg. 1.642(c)-(1)(b).

by the trust.<sup>72</sup> The regulations state that the terms of the governing instrument control if trust document states the source of the amounts paid to charity. Thus, the charitable deduction can be maximized if the trust document requires the charitable payments to be made in the following order:

- a. From ordinary income, including short-term capital gains, but excluding unrelated business taxable income (this category represents income that, unless distributed, is taxable to the trust at ordinary income tax rates but, if distributed, can be fully deducted by the trust);
  - b. 50% of unrelated business taxable income (this category represents the portion of unrelated business taxable income that the trust may not deduct – since unrelated business taxable income is usually taxed as ordinary income, it is more tax efficient to distribute the nondeductible portion of unrelated business taxable income before distributing long-term capital gains);
  - c. Long-term capital gains<sup>73</sup>;
  - d. The balance of unrelated business taxable income (this category represents the portion of unrelated business taxable income that qualifies for a charitable deduction under §681);
  - e. Tax-exempt income; and
  - f. Principal
9. Despite the fact that the regulations specifically state that the terms of the trust documents govern the source of the amounts paid to charity, the IRS has repeatedly taken the position that an ordering provision stated in the trust document will be ignored in favor of a pro-rata allocation unless the allocation has economic effect independent of the tax consequences.<sup>74</sup> In June, 2008, the IRS issued proposed regulations that would codify the “independent

---

<sup>72</sup> Reg. 1.642(c)-3(b)(2)

<sup>73</sup> This category should have a further ordering requiring long-term capital gains taxed at higher rates (e.g. gain on collectibles taxed at 28%) deemed distributed prior to capital gains taxed at a lower (15%) rate.

<sup>74</sup> General Counsel Memorandum 39161 (September 30, 1983); PLR 8823022, 9750020 and 199947022. But see PLR 9716023 which permitted a deviation from the pro-rata allocation method.

economic effect” requirement for allocating particular-source income to charity for purposes of the fiduciary income tax charitable deduction.<sup>75</sup> Thus, planners must be aware that the IRS may not accept the ordering rules specified in the trust document (despite a current regulation<sup>76</sup> stating the opposite) unless the ordering rules have independent economic effect. The ordering rules should not affect the qualification of the trust as a valid CRT – it should only determine the type of income qualifying for the charitable deduction.

10. Depreciation and depletion. Unless the trust instrument specifically allocates the depreciation and depletion deduction to the trust, those deductions will be allocated to whoever receives the accounting income of the trust.<sup>77</sup> Thus, to ensure that the trust receives the benefit of the depreciation and depletion deduction, the trust instrument should specifically allocate those deductions to the trust.

## ii. Grantor Lead Trust

1. All the items of income, deductions and credits of a grantor CLT flow through and are taxed to the donor. The trust pays no tax – all items are taxed to the donor.
  - a. One advantage of a grantor CLT is that the donor pays the income tax on the income and gains accumulated for future distribution to the non-charitable remainder beneficiaries. The donor’s payment of the income tax on income earned by the CLT is, generally, not a taxable gift.<sup>78</sup>

## c. Taxation of remainder beneficiaries.

### i. Commutation of lead interest.

1. Income earned by a non-grantor lead trust that exceeds the amount needed to pay the lead interest is taxed to the CLT

---

<sup>75</sup> Prop. Reg. 1.642(c)-3(b)(2) and Prop. Reg. 1.643(a)-5(b).

<sup>76</sup> Reg. 1.642(c)-3(b)(2) provides that in determining whether income paid by a trust includes particular items not included in gross income, the trust document controls with respect to the source of the income if it “specifically provides as to the source out of which amounts are to be paid.” If the trust documents does not specifically provide the source of the payments, the amount paid to charity is deemed to come pro-rata from all of the income earned in the trust for the year in question. Reg. 1.642(c)-3(b)(2) does not contain any requirement that an allocation provision in the trust document have economic effect.

<sup>77</sup> §642(e); §167(d); §611(b)(3); Reg. 1.167(h)-1(b)

<sup>78</sup> Rev. Rul. 2004-64, 2004-27 IRB 7.

at the compressed fiduciary income tax rates. Thus, the accumulated income could be subject to higher tax rates than the rates applicable to the remainder beneficiaries.

2. One planning device that has been suggested is to use the excess income earned by the CLT and prepay or commute the lead interest of the charity if permitted by the terms of the trust document. Arguably, the trust would be entitled to an income tax deduction for the commutation payment under §642(c).
3. Although there are no statutory or regulatory prohibitions on commuting or prepaying charity's interest in a CLT, the IRS has ruled that the existence of a commutation provision disqualifies the lead interest for the gift or estate tax charitable deduction.<sup>79</sup>
4. The governing instrument should prohibit prepayment (commutation) of the lead interest to negate the trustee's ability to manipulate the value of the charity's lead interest if interest rates decline between the date the trust is funded and the date of prepayment.

ii. Accelerating the remainder interest

1. Rev. Rul. 75-307 addresses whether a grantor realizes gain or loss or income by transferring the rights to a remainder interest in a CLT to the holder of the charitable lead interest. The ruling held that the donation of the remainder interest to the charity holding the lead interest did not result in taxable income or realized gain to the donor because no economic benefit inured to the donor. In addition, the ruling held that when the donor assigns both his income and reversionary interest, the donor ceases to be treated as the owner of the income interest and, as a result, is not taxable on the income subsequently earned by the trust.

iii. Death taxes

1. The CLT should probably exempt the charitable interest from payment of any death taxes attributable to the CLT. Any death taxes payable from the charitable interest could jeopardize the payment of the annuity for a CLAT or reduce the size of the unitrust amount for a CLUT. While

---

<sup>79</sup> Rev. Rul. 88-27, 1988-1 C.B. 331; PLR 9734057; See Rebecca K. Crown Income Charitable Fund, 8 F3d 571 (7<sup>th</sup> Cir. 1993).

Rev. Rul. 82-128, 1982-2 C.B. 71 holds that a CRT must mandate that any death taxes be the paid by the noncharitable beneficiaries, there is no similar rule for a CLT.

#### IV. Funding and Investment Options.

- a. Funding with appreciated assets in generally not advisable. A CLT is not a tax-exempt trust. Therefore, funding a CLT with low basis assets which are later sold will result in a non-grantor CLT paying income tax on the amount of the gain to the extent the gains exceed the amount allowed as a deduction for the payment to the lead interest. This will reduce the tax leveraging affect of the CLT.
- b. CLTs are subject to the private foundation prohibitions against excess business holdings and jeopardy investments if the lead interest is worth 60% or more of the fair market value of the trust assets.
- c. A CLT must be careful to minimize or eliminate unrelated business taxable income. If a CLT has unrelated business taxable income, part of the non-grantor CLT's otherwise unlimited income tax charitable deduction is lost.

#### V. Uses for CLTs

- a. Accelerate deduction for charitable pledge. A grantor CLT is useful for donors who desire to make a multi-year charitable pledge and accelerate the charitable deduction into the year the CLT is funded. Absent the CLT, the charitable deduction would be taken over the pledge period. Note, however, that using a CLAT to satisfy a legally binding charitable pledge could have undesirable consequences.
- b. Leverage the GST Exemption. Donor has charitable intentions and wants to do some lifetime generation-skipping tax planning. The donor's grandchildren don't need money during his lifetime. Donor establishes a CLUT with a taxable remainder at the time the CLUT is established equal to the amount of his GST exemption. The CLUT will terminate at the donor's death (or at the end of a term equal to his anticipated life expectancy). The donor's grandchildren take the remainder free of transfer tax.
- c. Leverage and Discount Gift of Stock in Closely Held Business. Generally, if the investment performance of the CLAT is higher than the §7520 rate, the amount earned in excess of the §7520 rate will pass to the remainder beneficiaries (e.g. the donor's children) free of transfer tax (subject to any possible generation skipping tax if the remainder

beneficiaries are skip persons). If property transferred to a CLAT can be valued at a sufficient discount for transfer tax purposes, it may increase the possibility that the CLAT will experience growth in excess of the §7520 rate. For example, if the donor transfers stock in a closely-held business to a CLT and the transfer of the stock qualifies for a valuation discount for a minority interest and lack of marketability, the CLAT is off to a head start in beating the applicable §7520 rate.

- d. **Leveraging Against Life Expectancies.** If an individual's life expectancy is shorter than normal, it may be beneficial to create a CLT to make payments for the life of the individual. If the individual dies prematurely, the charity's interest may have been valued based on the IRS life expectancy tables but the charity may receive less (and the remaindermen more) than forecast under those tables. The IRS actuarial tables must be used unless death of the measuring life is imminent. An individual who is known to have an incurable illness or other deteriorating physical condition is considered terminally ill if there is at least a 50% probability that the individual will die within 1 year. However, the individual will be presumed to have not been terminally ill at the time of the transaction if he survives for 18 months or longer after the date of the transaction unless the contrary is established by clear and convincing evidence.<sup>80</sup> For example, assume the donor's actuarial life expectancy is 20 years but his is in poor health and likely to die sooner than expected. Donor could set up a CLUT for his life terminating in favor of a generation-skipping trust. Donor's family will likely have considerably more assets with this plan than without. Thus, to use this strategy, the individual's life expectancy must be shorter than normal but not so short as to preclude use of the IRS life expectancy tables.
- e. **Leveraging an Asset Ready to Pop.** Donor holds an asset whose value is likely to appreciate substantially in value in the near future. Donor is not interested in retaining any interest in the property. Donor establishes a lifetime CLAT with a high payout to charity designed to zero out the remainder interest. If the asset significantly appreciates in value after being transferred to the CLAT the donor's family (e.g. children) will most likely receive a substantial financial benefit at the end of the lead term at no transfer tax cost to the donor (subject to any possible generation skipping tax if the remainder beneficiaries are skip persons).
- f. **The Jackie O Scenario.** Donor has a substantial estate and wealthy children. Donor does not want to pay estate taxes and wants to provide significant charitable gifts at her death but doesn't want to cut out her family completely. Donor establishes a testamentary CLAT which zeros out the remainder interest and will distribute to her family 24 years after her death. If the CLAT assets grow at a faster rate than the §7520 rate, the

---

<sup>80</sup> Reg. 1.7520-3(b)(3); Reg. 20.7520-3(b)(3); Reg. 25.7520-3(b)(3)

excess will pass transfer tax free (subject to any possible generation skipping tax if the remainder beneficiaries are skip persons) to the noncharitable remainder beneficiaries.

- i. Example: Jackie O's will provided for the residue of her estate to pass to a 24 year 8% testamentary CLAT at her death in May, 1994 when the §7520 rate was 7.8%. The actuarial value of the stream of 8% payments for 24 years qualified almost 97% of the residue of her estate for a federal estate tax charitable deduction. Thus, only 3% of the residue of the estate was subject to federal estate tax. Any amount the CLAT earned in excess of the 7.8% §7520 rate would pass to the remaindermen free of transfer tax. Thus, if the remaindermen were willing to wait 24 years, only 3% of the residue of her estate would be subject to federal estate tax and the amount earned in excess of 7.8% would pass to the remaindermen free of federal estate tax.
- g. Funding a Private Foundation. Donor, whose other charitable deductions already exceed his income tax limits on deductibility, wants to fund his family foundation (of which he is not a trustee or director) during life. Donor establishes a CLT with the foundation as the lead beneficiary and the CLT receives an income tax deduction each year for its distributions to the foundation.
- h. Over the Deductibility Limits. A nongrantor CLT presents a planning opportunity for individuals who, because of their significant charitable giving, have exceeded their adjusted gross income limitation for charitable gifts. Since the income tax charitable deduction available for a CLAT is governed by §642(c)(1) instead of §170, the adjusted gross income limitations applicable to individuals under §170 are not applicable. Thus, a CLT is able to deduct 100% of the amounts that are distributed to charity. For example, a donor that makes charitable gifts in excess of her AGI limits but wants to make additional gifts but do so in a tax efficient manner could establish and fund a CLT. The income earned on the CLT's assets is not reported on the donor's income tax return and the CLT gets an unlimited fiduciary income tax charitable deduction for the amount of the lead payments to charity.
- i. The Double Decker. An individual may create a CRT to provide the donor or another beneficiary with benefits from the CRT for life. If the donor or the other beneficiary dies earlier than expected, there will be a significant reduction in the amount which they and their families were expecting. The donor could solve this problem by creating a CLT that terminates at the same time as the remainder interest in the CRT will be paid to charity. The CLT then serves as a hedge against the premature death of the individual beneficiaries of the CRT. Alternatively, the donor



may want to make contributions to charity both during his life and after his death but also benefit his children for their lives. The donor could establish a CRT for his life with his children as the lead beneficiaries and charity (or a private foundation) as the remainder beneficiary. In addition, donor could establish a CLT for his life paying the lead interest to charity and the remainder interest to his children. Donor has accomplished his goal of providing for his children during life via the charitable remainder trust and after his death via the CLT. He has also accomplished his goal of funding his charitable goals during life via the CLT and at death via the charitable remainder trust.

- j. Income tax advantage for spike in income. A grantor CLT may also be advantageous where a donor has a large spike in income. The CLT can be used to produce a large current income tax deduction to offset the current spike in income, thereby enabling the donor to shelter income otherwise subject to a high rate of tax. Note, however, that the donor's income tax charitable deduction will be limited to 30% of his adjusted gross income as the contributions to a CLT are considered "for the use of" rather than "to" a charity.<sup>81</sup> The donor would, of course, be taxed on the income earned by the grantor CLT during the lead term (for which no further income tax charitable deduction is available even though the trust will continue to make annual distributions of the lead interest to charity), the income that may be earned in the CLT may be taxed at a lower income tax rate in future years e.g. it may consist of 15% qualified dividends or long term capital gains, municipal bond interest exempt from income taxation or the donor may simply be in a lower income tax bracket at that time. In other words, while the income tax charitable deduction may shelter income taxed at the highest individual income tax rate, the donor's future income may be taxed at a much lower rate or not at all, depending on the investments of the CLT during the lead term.

## VI. Who should use a CLT

- a. Generally, the person who establishes a CLT should be someone who wants to benefit charity but at the same time be someone of significant wealth whose heirs (potential remainderman) can afford to wait to receive the remainder interest in the CLT.
- b. Due to legal and administrative complexities, CLTs tend to be used only by wealthy individuals. As a general rule, a CLT should have an initial funding of at least \$1 million.

---

<sup>81</sup> Reg. 1.107A-8(a)(2); PLR 8824039



## Charitable Lead Trusts

### American Council on Gift Annuities

Jeremiah W. Doyle IV  
Senior Vice President  
BNY Mellon Wealth Management  
Boston, MA  
April, 2010

1

BNY MELLON WEALTH MANAGEMENT

## Charitable Lead Annuity Trusts - Agenda

- Introduction
- Basics
  - Parties
    - Donor
    - Trustee
    - Lead Beneficiaries
    - Remainder Beneficiaries
  - Types of CLTs
    - CLAT
    - CLUT
  - Payout
  - Term
  - Private Foundation Restrictions
  - Forms

2

BNY MELLON WEALTH MANAGEMENT

## Charitable Lead Annuity Trusts - Agenda

- Tax Consequences
  - To the Donor
    - Gift Tax
    - Estate Tax
    - Generation Skipping Tax
    - Income Tax
      - Non-Grantor Lead Trust
      - Grantor Lead Trust
  - How the CLT is Taxed
    - Non-Grantor Lead Trust
    - Grantor Lead Trust

3

BNY MELLON WEALTH MANAGEMENT

## Charitable Lead Annuity Trusts - Agenda

- Funding and Investment Options
- Uses for CLT
  - Leverage and Discount Stock in Closely Held Business
  - Leverage Against Life Expectancies
  - Leverage an Asset Ready to "Pop"
  - The Jackie O Scenario
  - Funding a Private Foundation
  - Over the Deductibility Limits
  - The Double Decker
  - Income Tax Advantage for Spike in Income

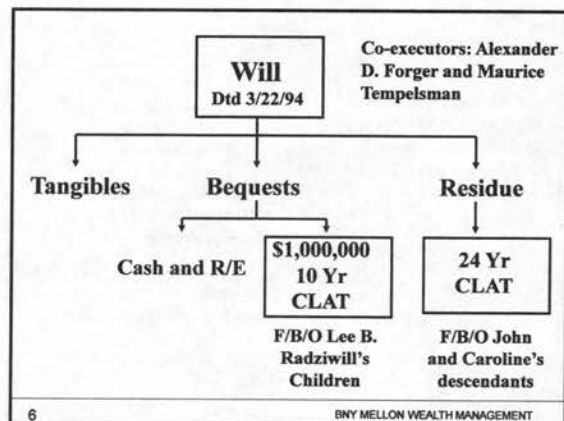
4

BNY MELLON WEALTH MANAGEMENT

## Last Will and Testament of Jacqueline Kennedy Onassis

5

BNY MELLON WEALTH MANAGEMENT



6

BNY MELLON WEALTH MANAGEMENT

### What is a Charitable Lead Annuity Trust?

- Irrevocable Trust
- Fixed percentage of trust is paid to a charity for life of donor or for a term of years
  - Qualifies for FET charitable deduction
- When trust terminates, balance goes to individuals named by donor
- If amount earned by trust exceeds the §7520 rate, individual beneficiaries win

7

BNY MELLON WEALTH MANAGEMENT

### What is a Charitable Lead Annuity Trust?

- Two gifts made at creation of CLT:
  - Gift of the annuity or unitrust interest to one or more charities
    - Qualifies for gift or estate tax charitable deduction
  - Gift of the remainder interest to non-charitable beneficiaries
    - Taxable for gift or estate tax purposes

8

BNY MELLON WEALTH MANAGEMENT

### What is a Charitable Lead Annuity Trust?

- Two types of CLT:
  - Grantor
    - Donor retains power that causes CLT income to be taxed to Donor
  - Non-grantor
    - Taxed as a complex trust

9

BNY MELLON WEALTH MANAGEMENT

### What is a Charitable Lead Annuity Trust?

- Income tax deduction for Donor
  - Donor gets a one-time up front income tax charitable deduction for transfer to grantor CLT
  - Donor does not get income tax charitable deduction for transfer to non-grantor CLT
- Lead interest qualifies for gift or estate tax charitable deduction
- Income taxation of CLT depends on status as grantor or non-grantor trust
  - Grantor CLT: donor taxed on all trust income during lead term
  - Non-Grantor CLT: CLT taxed as a complex trust and trust gets fiduciary income tax charitable deduction for distributions made to charity during lead term

10

BNY MELLON WEALTH MANAGEMENT

### Residue

Co-trustees: Caroline B. Kennedy, John F. Kennedy, Jr., Alexander Forger, Jr., and Maurice Tempelsman

24 Yr CLAT fbo John and Caroline's descendants

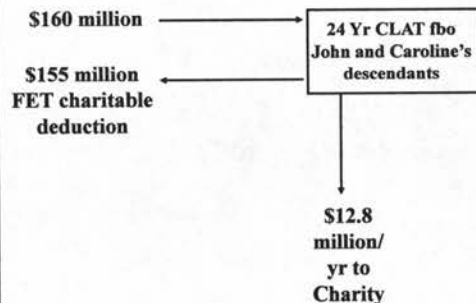
- Pay 8% of initial FMV to charities selected by independent trustees

- Upon termination, hold for ultimate distribution to John and Caroline's descendants

11

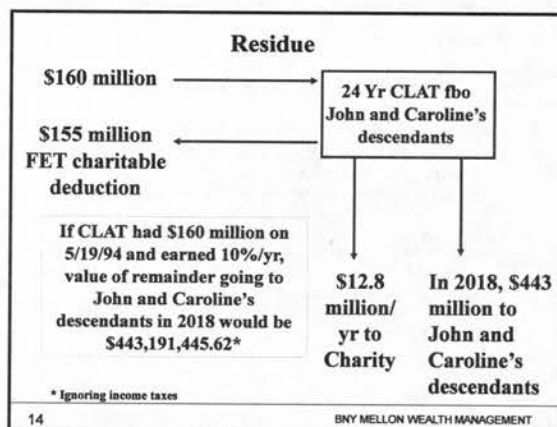
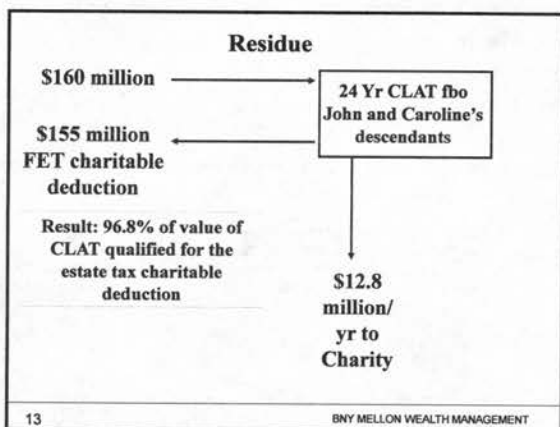
BNY MELLON WEALTH MANAGEMENT

### Residue



12

BNY MELLON WEALTH MANAGEMENT



- ### Basics - Parties
- Donor
    - No restrictions on who can be donor
    - Can be funded during life (inter vivos) or at death (testamentary)
  - Trustee
    - Any person or entity can be trustee
    - If donor serves as trustee, avoid retaining power to select charity entitled to lead interest or remainder interest
      - Retention causes estate tax inclusion
- 15 BNY MELLON WEALTH MANAGEMENT

- ### Basics - Parties
- Charitable Lead Beneficiary
    - Must be one or more charities eligible for estate (§2055) or gift tax (§2522) charitable deduction
    - Charity need not be identified by name or amount payable to each charity need not be specified
      - Donor can specify the charity to receive the lead interest or leave the selection up to the trustee or someone else each year
      - If Donor retains the power to select lead beneficiary, estate tax inclusion results
  - Remainder Beneficiaries
    - Can be any non-charity
- 16 BNY MELLON WEALTH MANAGEMENT

- ### Types of CLTs: CLAT and CLUT
- Charitable Lead Annuity Trust (CLAT)
    - Lead interest payable as a fixed dollar amount based on initial FMV of trust, payable annually
      - Annuity can be determined by formula
    - If trust income exceeds annuity amount, excess income may be paid to charity but donor will not receive additional gift or estate tax deduction
    - Possible to "zero out" value of remainder interest
      - Select annuity payments payable for a period of time and at a high enough rate given the §7520 rate that value of lead interest equals the value of the property transferred i.e. the value of the remainder interest is zero.
- 17 BNY MELLON WEALTH MANAGEMENT

- ### Types of CLTs: CLAT and CLUT
- Charitable Lead Unitrust (CLUT)
    - Lead interest payable as a fixed percentage of the FMV of the trust determined and payable annually
      - Amount of lead interest payable changes with FMV of CLUT
      - Valuation may be on a specific day each year or based on annual average of several dates
    - If trust income exceeds annuity amount, excess income may be paid to charity but donor will not receive additional gift or estate tax deduction
    - Additional contributions permitted
    - Possible to "zero out" value of remainder interest
      - Select annuity payments payable for a period of time and at a high enough rate given the §7520 rate that value of lead interest equals the value of the property transferred i.e. the value of the remainder interest is zero.
      - If CLUT holds unmarketable or hard to value assets, use third party appraiser or independent trustee
- 18 BNY MELLON WEALTH MANAGEMENT

## Payout

- Distributions must be made annually to charitable lead beneficiary
  - Payment may be made at beginning or end of the payment period
- No minimum or maximum payout as there is with a CRT
- No commutation of lead interest. Regs prohibit CLT from making payments to non-charitable beneficiary before the end of the lead term unless non-charitable payments made from assets segregated and administered exclusively for the non-charitable beneficiary
- If testamentary (created at death) CLT, payment to charity may be deferred until the end of the taxable year in which the CLT funding is completed
  - Interest is payable on deferred payment

19

BNY MELLON WEALTH MANAGEMENT

## Term

- CLT must pay annuity or unitrust interest for a fixed term of years (e.g. 20 years) or for the life or lives of one or more individuals (in being when the trust is created) e.g. until the death of the donor and/or the donor's spouse.
- A term of years can be added after a measuring life.
- Unlike a CRT, a CLT can extend over 20 years, limited only by the rule against perpetuities
- Measuring lives must be one or more of: donor, donor's spouse, individual who, with respect to all remainder beneficiaries (other than charity) is either a lineal ancestor or the spouse of a lineal ancestor of those beneficiaries.

20

BNY MELLON WEALTH MANAGEMENT

## Private Foundation Restrictions

- CLT, as a split interest trust, is subject to certain private foundation rules
- Trust document must prohibit the trust from engaging in acts of self-dealing and making certain types of expenditures
- Trust document must also contain prohibitions relating to excess business holdings and jeopardy investments if the present value of the charitable interest on the date of funding exceeds 60% of the aggregate value of all amount in the trust

21

BNY MELLON WEALTH MANAGEMENT

## Forms

- Sample CLAT forms
  - Rev. Proc. 2007-45
    - Inter vivos non-grantor CLAT and inter vivos grantor CLAT
  - Rev. Proc. 2007-46
    - Testamentary CLAT
- Sample CLUT forms
  - Rev. Proc. 2008-45
    - Inter vivos non-grantor CLUT and inter vivos grantor CLUT
  - Rev. Proc. 2008-46
    - Testamentary CLUT

22

BNY MELLON WEALTH MANAGEMENT

## Forms

- If trust is substantially similar to sample form (or properly integrates one or more of the alternative provisions into a trust document that is substantially similar to the sample form) and if valid under state law and properly administered:
  - Value of lead interest deductible for gift and estate tax purposes
  - Payment of annuity or unitrust amount to the lead beneficiary is deductible from gross income of the CLT i.e. qualifies for a fiduciary income tax charitable deduction
- A CLT that contains provisions in addition to those contained in the sample form or omits any of the sample form provisions "will not necessarily be ineligible for the relevant charitable deduction(s), but neither will that trust (or contributions to it) be assured of qualification for the appropriate charitable deductions."

23

BNY MELLON WEALTH MANAGEMENT

## Tax Consequences – Donor – Gift Tax

- CLT created during life
  - Donor makes gift in amount of present value of remainder interest to the non-charitable remainder beneficiaries at time property is transferred to CLT
  - Constitutes gift of future interest – doesn't qualify for gift tax annual exclusion
- Donor gets gift tax charitable deduction for actuarial value of charity's lead interest

24

BNY MELLON WEALTH MANAGEMENT

### Tax Consequences – Donor – Estate Tax

- CLT created at death
  - Donor taxed on amount of present value of remainder interest to the non-charitable remainder beneficiaries
- Donor gets estate tax charitable deduction for actuarial value of charity's lead interest
- Payment of estate tax
  - Annotations to sample forms indicate that estate taxes may be paid from assets used to fund the CLT but caution that the amount that qualifies for an estate tax charitable deduction is the amount that passes to charity reduced by the amount of estate taxes paid.
    - The more estate taxes paid from assets otherwise passing to a CLT, the less estate tax charitable deduction and the greater the estate tax.
    - Suggestion: draft CLT with language that obligates any estate tax liability due to the inclusion of the CLT in the Donor's estate be paid from assets other than assets in the CLT

25

BNY MELLON WEALTH MANAGEMENT

### Tax Consequences – Donor – GST

- Becomes an issue if remaindermen are "skip persons" e.g. Donor's grandchildren or more remote descendants or individuals who are two or more generations below the donor
- GST not imposed at time CLT is established (because charity is assigned to same generation as donor)
- GST imposed when the trust terminates in favor of a skip person (taxable termination) or when distributions are made to skip persons (taxable distributions)
- \$3,500,000 GST exemption

26

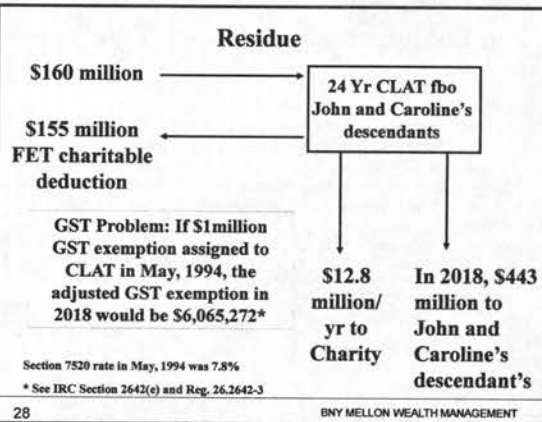
BNY MELLON WEALTH MANAGEMENT

### Tax Consequences – Donor – GST

- Allocation of GST exemption
  - CLUT
    - Easy to allocate GST exemption to CLUT
    - The "applicable fraction" of a CLUT can be determined with certainty at funding of a CLUT
  - CLAT
    - Involves a "wait and see" approach
    - The amount of the GST "inclusion ratio" not determined until the lead annuity interest terminates
    - Amount of GST exemption allocated to CLAT is adjusted
      - Amount of GST exemption allocated to CLAT is compounded annually by the §7520 rate used to value the charitable lead interest over the duration of the lead interest

27

BNY MELLON WEALTH MANAGEMENT



28

BNY MELLON WEALTH MANAGEMENT

### Tax Consequences – Donor – GST

- CLAT – Bottom Line
  - CLAT not advisable if "skip persons" (e.g. grandchildren) are the remainder beneficiaries
  - If value of trust grows faster than applicable §7520 rate at the time of funding, the GST exemption will not be sufficient to protect the CLAT from potential GST
  - If value of trust grows slower than applicable §7520 rate at time of funding, GST exemption will be wasted
  - Only if growth rate of trust equals §7520 rate at time of funding will GST exemption exactly equal the value of the trust at termination of the lead interest.

29

BNY MELLON WEALTH MANAGEMENT

### Tax Consequences – Donor – Income Tax

- Non-grantor lead trust
  - Donor does not receive an income tax charitable deduction for the value of the lead interest
  - Instead, the CLT gets an unlimited fiduciary income tax charitable deduction for the amount paid to the charitable lead beneficiary
  - The income earned by the CLT is not taxed to the Donor
  - Instead, the income earned by the CLT is reported by the CLT
    - If the taxable income (ordinary income plus capital gains) earned by the CLT equals the amount required to be paid to the charitable lead beneficiary, the CLT has no taxable income
    - If the income (ordinary income plus capital gains) earned by the CLT is more than the amount required to be paid to the charitable lead beneficiary, the CLT pays tax on the excess income at the compressed income tax rates applicable to trusts.

30

BNY MELLON WEALTH MANAGEMENT

## 2010 Fiduciary Income Tax Rates - §1(e)

<u>Over</u>	<u>Not Over</u>	
0	2,300	15%
2,300	5,350	25%
5,350	8,200	28%
8,200	11,200	33%
11,200		35%

31

BNY MELLON WEALTH MANAGEMENT

## Tax Consequences – Donor – Income Tax

- Grantor lead trust
  - Donor receives a one-time income tax charitable deduction at the creation of the CLT for the actuarial value of the charitable lead interest
    - Deduction subject to 30% of AGI limitation as a gift “for the use of” charity (because it is held in trust), with a 5 year carryover of the excess
  - The Donor does not receive any deduction for the annual trust payments to the charitable lead beneficiary
  - The Donor is fully taxable on income earned by the CLT during the term of the trust with no offsetting income tax charitable deduction for the annual payments

32

BNY MELLON WEALTH MANAGEMENT

## Tax Consequences – Donor – Income Tax

- Grantor lead trust – Net Effect
  - Grantor’s income tax is deferred via an upfront charitable deduction at the time the trust is funded rather than an elimination of the income tax liability
  - Present value of the up front income tax charitable deduction may be greater than the present value of the future income tax burden on the trust income especially if income tax rates decline in the future
    - If Donor is able to use income tax deduction at a higher income tax rate than the rate at which the Donor will be taxed on the trust income in later years, the Donor may be better structuring the CLT as a grantor trust for income tax purposes

33

BNY MELLON WEALTH MANAGEMENT

## Tax Consequences – Donor – Income Tax

- Grantor lead trust – Problem
  - Potential recapture of income tax charitable deduction
    - If Donor dies during the lead term of the trust (or otherwise ceases to be treated as the owner of the trust for income tax purposes), all or part of the income tax charitable deduction will be recaptured
    - Donor must recognize as income an amount equal to the amount of the deduction the Donor received when the CLT was funded, reduced by the discounted value of the amounts paid to the charitable lead beneficiaries before the Donor’s grantor trust status ceased.

34

BNY MELLON WEALTH MANAGEMENT

## Tax Consequences – CLT

- Non-Grantor lead trust
  - Taxed as a complex trust
    - Unlike a CRT, a CLT is not exempt from income tax
  - Entitled to an unlimited income tax charitable deduction for the amounts paid from the CLT to the charitable lead beneficiary
    - Exception: unrelated business taxable income
      - Income tax charitable deduction for UBTI payable to charity is subject to percentage limitations applicable to individuals
        - » The portion of the UBTI payable to charity for which an income tax charitable deduction is denied is subject to income tax in the CLT
  - CLT is taxable on undistributed income in excess of the amount paid to satisfy the payment to the charitable lead beneficiary
    - The tax rate for trusts is highly compressed. Taxable income over \$11,150 (for 2009) is subject to the 35% tax rate

35

BNY MELLON WEALTH MANAGEMENT

## Tax Consequences – CLT

- Non-Grantor lead trust
  - Distribution of appreciated property to satisfy payout to charitable lead beneficiary results in gain recognition to the CLT
    - The gain will be treated as payable to the charitable lead beneficiary so that the CLT will be entitled to a fiduciary income tax charitable deduction
  - The CLT may take a fiduciary income tax charitable for the current year as long as the amount is paid to the charity in the current year or before the last day of the subsequent year.

36

BNY MELLON WEALTH MANAGEMENT



### Tax Consequences – CLT

- Non-Grantor lead trust
  - Unless the trust document states otherwise, amounts paid from the trust to charity are deemed to consist of a proportionate amount of each class of income earned by the CLT
  - The trust can state the source of payments from the trust i.e. the trust can have an ordering rule\*
  - The charitable deduction can be maximized if the charitable payments are deemed made in the following order:
    - Ordinary income (including STCG but excluding UBTI)
    - 50% of UBTI (deductible portion)
    - LTCG
    - Balance of UBTI (non-deductible portion)
    - Tax-exempt income
    - Principal

\* Caution: Prop. Reg. 1.642(c)-3(b)(2) and Prop. Reg. 1.643(a)-5(b) would only recognize ordering rule if it has "independent economic effect"

### Tax Consequences – CLT

- Grantor lead trust
  - All items of income, deduction and credits flow through and are taxed to the Donor
    - The CLT pays no tax

	Grantor CLT	Nongrantor CLT
Exempt from income tax	No	No
Individual income tax charitable deduction	Yes – allowed at time of funding for actuarial value of lead interest	None allowed
Income taxation	All trust income, deductions, gains and credits reported by donor on his individual income tax return	Taxed as a complex trust
Annual distribution of lead interest to charity	No income tax deduction	Fiduciary income tax charitable deduction under §642(c)
Gift tax/Estate tax deduction	Deduction allowed for actuarial value of income interest	Deduction allowed for actuarial value of income interest

### Funding and Investment Options

- Funding with appreciated assets is not advisable
  - Non-grantor CLT subject to income tax on sale of appreciated assets
- CLTs subject to private foundation prohibitions against excess business holdings and jeopardy investments if the lead interest is worth 60% or more of the FMV of the trust assets
  - Must be careful with funding CLT with closely held stock
- CLT must be careful to minimize or eliminate UBTI
  - Otherwise, part of the fiduciary income tax charitable deduction is lost

### Uses for CLTs

- Leverage and Discount Gift of Stock in Closely Held Business
  - GR: if investment performance in CLAT exceeds the \$7520 rate applicable at the time the CLAT is funded, the excess amount will pass to remainder beneficiaries (e.g. Donor's children) free of transfer tax
  - If property transferred to CLAT can be valued at a discount for transfer tax purposes, it may increase the possibility that the CLAT will grow in excess of the \$7520 rate
    - The CLAT is off to a head start in beating the applicable \$7520 rate

### Uses for CLTs

- Leverage Against Life Expectancies
  - If individual's life expectancy is shorter than normal, may be beneficial to create CLT to make payment to charity for life of the individual
    - If individual dies prematurely, charity gets less (and the remaindermen get more) than the value of the lead interest valued under the valuation tables
      - Caution: IRS valuation tables cannot be used if individual is known at the time of transfer to have an incurable physical condition such that death is imminent and the prospects for survival for a year or more is so remote as to be negligible
      - To succeed, individual's life expectancy must be shorter than normal but not so short as to preclude used of IRS life expectancy tables

### Uses for CLTs

- Leveraging an Asset Ready to "Pop"
  - Donor holds asset ready to appreciate substantially
  - Donor establishes inter vivos CLAT with a high payout to the charitable lead beneficiary designed to "zero out" the remainder interest
  - If asset significantly appreciates in value after being transferred to the CLAT, Donor's family will most likely receive a substantial financial benefit at the end of the lead term without transfer tax cost

43

BNY MELLON WEALTH MANAGEMENT

### Uses for CLTs

- Jackie O Scenario
  - Donor has substantial estate and wealthy children
  - Donor doesn't want to pay estate taxes and wants to provide significant charitable gifts at her death but doesn't want to cut out family completely
  - Donor establishes testamentary CLAT which zeros out the remainder interest and will distribute to her family after the termination of the lead interest.
  - If CLAT grows in excess of the \$7520 rate, the excess passes to family free of transfer taxes (subject to any GST if the remaindermen are skip persons)

44

BNY MELLON WEALTH MANAGEMENT

### Uses for CLTs

- Funding a Private Foundation
  - Donor's charitable deductions already exceed his income tax limits on deductibility
  - Wants to fund a family foundation (of which he is not a trustee or director) during life
  - Donor establishes a CLT with the foundation as the lead beneficiary
  - CLT receives a fiduciary income tax charitable deduction each year for its distributions to the foundation

45

BNY MELLON WEALTH MANAGEMENT

### Uses for CLTs

- Over the Deductibility Limits
  - Donor has made charitable contributions exceeding his AGI limits
  - Donor wants to make additional charitable contributions
  - Creates and funds a non-grantor CLT
  - Non-grantor CLT gets unlimited fiduciary income tax charitable deduction for amounts paid to the charitable lead beneficiary
  - Income from non-grantor CLT not reported by Donor
    - Unlimited charitable deduction wipes out CLT income
  - Result: Donor makes charitable contributions in excess of his AGI limits in a tax efficient manner

46

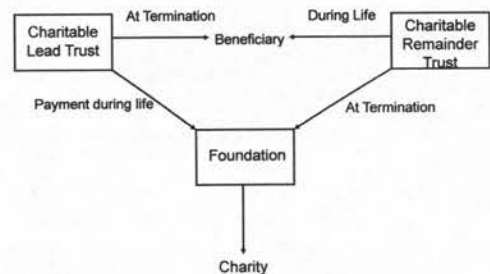
BNY MELLON WEALTH MANAGEMENT

### Uses for CLTs

- The Double Decker
  - Donor creates CRT to provide the Donor or another beneficiary with benefits from the CRT for life
  - Fear that CRT beneficiary will die earlier than expected and beneficiary and family will receive less than expected
  - Solve problem by creating CLT that terminates at same time as the CRT remainder will be paid to charity
  - CLT serves as hedge against premature death of CRT beneficiary
  - Alternatively, this strategy works for a Donor who wants to benefit charity both during his life and at death plus benefit his children for their lives
    - Establish CRT for his life with kids as beneficiary and charity (or a private foundation) as remainderman plus establish a CLT for his life paying lead interest to charity and remainder interest to his kids

47

BNY MELLON WEALTH MANAGEMENT



48

BNY MELLON WEALTH MANAGEMENT

## Uses for CLTs

- Income Tax Advantage for Spike in Income
  - Donor expects large spike in income for the current year
  - Donor creates and funds a grantor CLT
  - Donor receives a large one-time income tax charitable deduction upon funding the CLT
    - Charitable deduction limited to 30% of AGI as contributions to the CLT are "for the use of" rather than "to" a charity
  - Charitable deduction allows Donor to shelter income otherwise subject to a high rate of tax
  - Problem: Donor taxed on all income earned by CLT during the lead term and no further charitable deduction allowed for annual lead trust payments to charity
  - Solution: invest lead trust to produce income taxed at a lower rate e.g. qualified dividends and LTCG taxed at 15% or municipal bonds

49

BNY MELLON WEALTH MANAGEMENT

## What Apparently Happened\*

- Estate was worth far less than estimated at the time of her death
- Executors valued her estate at \$43.7 million
- Auction prices caused IRS to value the estate at \$73 million
- After distributing the property that John and Caroline decided to keep, making specific bequests and paying administration expenses, the estate had \$18 million but owed \$23 million in estate taxes
  - John and Caroline liable for the \$5 million shortfall
  - Due to the shortfall, there was no money to fund the residuary 24 year CLAT

\*New York Times 12/21/96

50

BNY MELLON WEALTH MANAGEMENT

## What Apparently Happened\*

- The tangibles were auctioned for \$34.5 million
- The executors had valued the tangibles at less than \$6 million
- IRS audited the Onassis estate tax return seeking to increase the value of the tangibles to the \$34.5 million auction proceeds rather than the executor's \$6 million value of the tangibles
  - Issue: what tax is owed on the \$28.5 million difference – the estate tax (55%) or capital gains tax (28%)

\*New York Times 12/21/96

51

BNY MELLON WEALTH MANAGEMENT

## Charitable Lead Annuity Trusts - Conclusion

- Basics
  - Parties
    - Donor
    - Trustee
    - Lead Beneficiaries
    - Remainder Beneficiaries
  - Types of CLTs
    - CLAT
    - CLUT
  - Payout
  - Term
  - Private Foundation Restrictions
  - Forms

52

BNY MELLON WEALTH MANAGEMENT

## Charitable Lead Annuity Trusts - Conclusion

- Tax Consequences
  - To the Donor
    - Gift Tax
    - Estate Tax
    - Generation Skipping Tax
    - Income Tax
      - Non-Grantor Lead Trust
      - Grantor Lead Trust
  - How the CLT is Taxed
    - Non-Grantor Lead Trust
    - Grantor Lead Trust

53

BNY MELLON WEALTH MANAGEMENT

## Charitable Lead Annuity Trusts - Conclusion

- Funding and Investment Options
- Uses for CLT
  - Leverage and Discount Stock in Closely Held Business
  - Leverage Against Life Expectancies
  - Leverage an Asset Ready to "Pop"
  - The Jackie O Scenario
  - Funding a Private Foundation
  - Over the Deductibility Limits
  - The Double Decker
  - Income Tax Advantage for Spike in Income

54

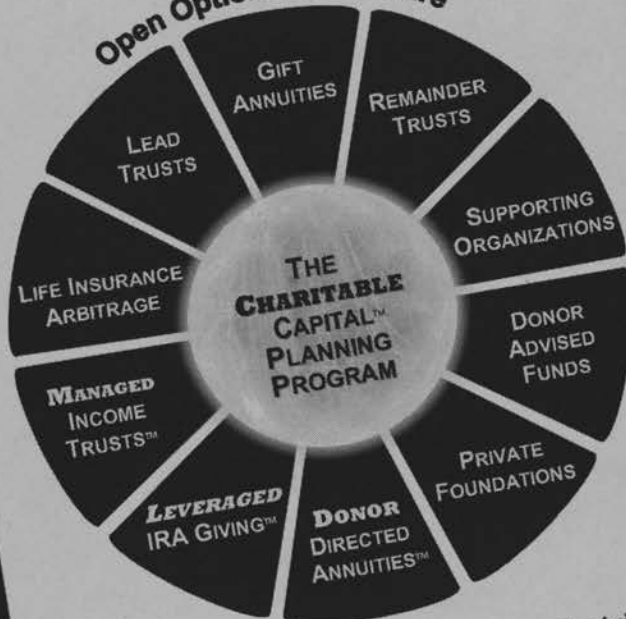
BNY MELLON WEALTH MANAGEMENT



**YOUR CHARITABLE CAPITAL™ DASHBOARD**  
**PLANNING**

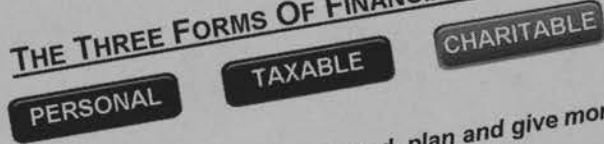
CREATING a HIGHER LEVEL of PLANNED GIVING

*Planned Giving Redefined*  
**Open Option Architecture**



Designing lifetimes of receiving through giving™

**THE THREE FORMS OF FINANCIAL CAPITAL**



Motivating donors to understand, plan and give more

Visit Booth Eight

**Offices**

- Atlanta
- Cincinnati
- Los Angeles
- Seattle
- Jacksonville
- Orlando
- Tampa Bay
- Phoenix
- Indianapolis
- San Diego
- Philadelphia
- New York
- Colorado Springs
- Houston
- Cleveland
- Kansas City
- Des Moines
- Las Vegas
- Boston
- Chicago
- St. Louis
- New Orleans

**THE CHARITABLE CAPITAL™ DESIGN CENTER, LLC**  
 A national intermediary for non-profits, donors and financial advisors  
 P.O. Box 249 Tarpon Springs, FL 34688

Phone: (727) 935-5815 • Fax: (727) 599-0539 • (888) 884-3332 • Website: [www.chcap.org](http://www.chcap.org) • E-mail: [info@chcap.org](mailto:info@chcap.org)



## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



## **New Decade Gift Annuities**

Presented by:

A. Charles Schultz  
President  
Crescendo Interactive, Inc.  
110 Camino Ruiz  
Camarillo, CA 93012  
(800) 858-9154  
crespro@cresmail.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)





# *The Future of Gift Annuities*

ACGA 2010 New Orleans By A. Charles Schultz

## Seven Gift Annuity Trends

1. Boomer Generation Flexible Annuities
2. Depression Babies Gift Annuity Campaigns
3. Higher Donor Expectations
4. Gift Annuities and Advisor Tax Planning
5. Gift Annuity Silver Surfers
6. CFOs Desire 90/10 Marketing
7. Gift Annuity Risk Reduction

### **1.**

#### Boomer Generation

- 74 million strong
- Trillions in assets
- Peak Income Years
- Flexible Deferred Annuities

### **1.**

#### Boomer Generation

- Persons age 45 – 65 seek to have greater flexibility
- 9/11, 2002 and 2008 downturns -- Boomers live with “new normal”

### **1.**

#### Flexible Deferred Annuities

- Desire Tax Savings
- Market Uncertainty
- Retirement Date?
- Fund Flexible Today
- Select Retirement Date Later
- Potential Future Gift of Annuity

### **2.**

#### Depression Babies

- Smaller group than Boomers (25 million)
- Lived through the Great Depression
- Looking for security and lifetime income

### **Gift Annuity Campaign**

eMarketing and Print Marketing  
Gift Annuity Campaign

- eNewsletters
- Donor stories
- Brochures
- Ads

### **New Decade Donors**

seeking security and  
will be interested in Gift Annuities

### **3.**

#### **Higher Donor Expectations**

- 1,000 new CGA charities
- Greater accuracy and transparency
- Increase response timeliness
- Full Disclosure

### **New Gift Annuity Donors**

Expect timely content and creative  
branding by their charities

### **4.**

#### **Advisors Encourage Gift Annuities**

- Top Federal/State rates 45% – 50%
- Capital Gains Rates = 20%
- Possible Value Added Tax

### **New Gift Annuity Donors**

interested in tax planning and  
charitable deductions

**5.**

**Gift Annuity Silver Surfers**

- Widespread Broadband
- Social Networking
- Online Banking
- Ms. Ivy Bean – Age ??
  - 5,000 Facebook Friends
  - 23,000 Twitter Followers

**New Gift Annuity Donors**

will want weekly eNewsletters  
with fresh content

**6.**

**CFOs Desire 90/10 Marketing**

- Trend to eMarketing
- Cost Savings
- Green Donors

**eMarketing Costs**

2,000 emails x 52 weeks = 104,000 emails  
2010 = 1 cent per eContact

**Print Costs**

2010 = 85¢ per mail contact  
2020 = \$1.50 per mail contact

**New Gift Annuity Donors**

will turn to charities who are “green”  
and use more eMarketing

## 6.

### CFOs Desire 90/10 Marketing

- 90% eContacts at 1 cent/contact
- 10% Print contacts at \$1.50/contact
- Cost Savings
- Green Donors

## 7.

### Gift Annuity Risk Reduction

- Charitable Gift
- Deferred Gift Annuity
- Prearranged  
“Unprearranged” Sale
- Reinsurance

### CGA & Debt Solution for the Land Developer

#### Bill and Betty Clark



### Clark B & B

- Bed and Breakfast
- FMV \$3,300,000
- Accelerated Depreciation \$165,000
- Debt \$1,000,000
- Adjusted Basis \$300,000



### Clark Goals

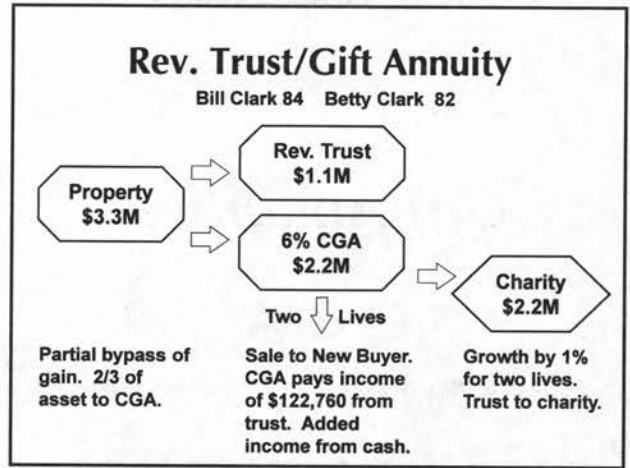
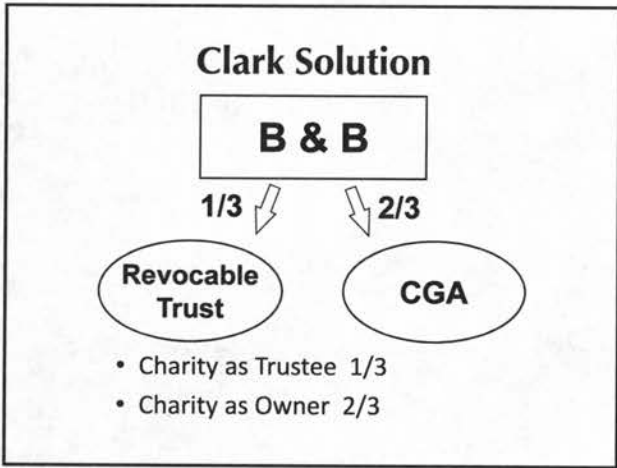
- Retirement Income
- Pay Debt
- No Net Tax



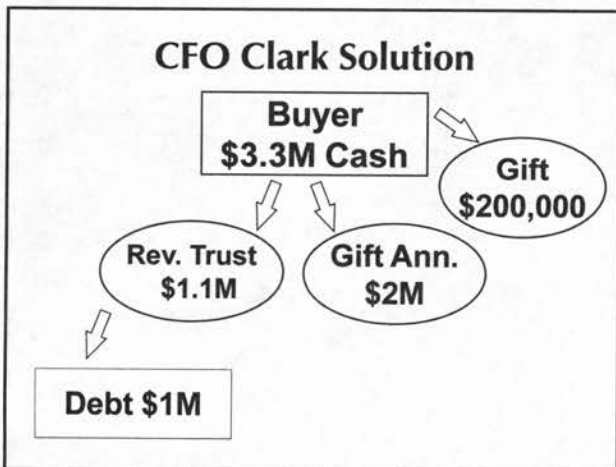
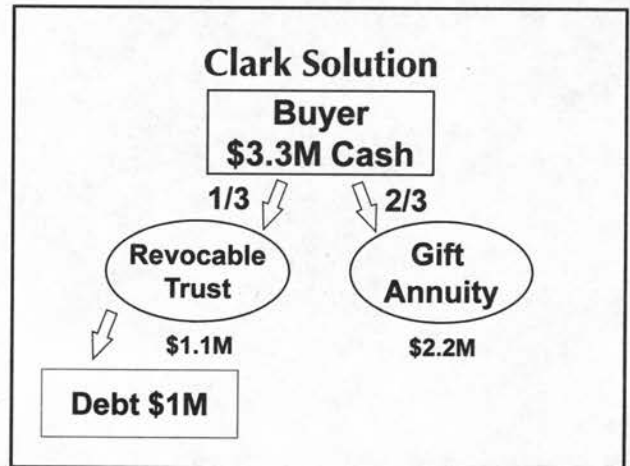
### Clark Solution

- Bridge Loan
  - Loan \$1M on Home
  - Pay Off Debt
- Deed 2/3 to CGA
- Deed 1/3 to Revocable Trust
- Buyer “Waiting in the Wings”





- ### Unprearranged "Prearranged" Sale
- Buyer and Charity Discuss CGA
  - Contingent Listing
  - Contingent Escrow
  - Transfer Before Closing For CGA at Sale Price
  - Close and Sell Property



- ### Reinsurance Risk Reduction
1. CGA Portfolio Size
  2. Life Expectancy – Plus 2 to 6 years
  3. Return Assumptions
  4. Self Insure vs. Reinsure

***The Future of  
Gift Annuities***

**Q & A**

ACGA 2010 New Orleans

By A. Charles Schultz



Bipster International LLC  
PO Box 3022  
Salem, MA 01970  
888-588-2477  
[www.bipster.com](http://www.bipster.com)

Finally a Planned Giving Software that counts and accounts for everything!

BIPSTER is the only program for administration of **all Planned Gifts, both future and realized**. BIPSTER proactively manages the entire process of Planned Giving from stewarding and projecting future planned gifts to collecting realized Planned Gifts easily in the only program designed specifically for Planned Giving.

**Track, Report and Steward future donors, with projections\*** of when the gifts will be received and what their current value is to your organization, using the same life expectancies as ACGA\*\*.

#### **INCREASE INCOME**

**See a 10-30% increase in cash in the door** in the first year of using our software by not letting gifts fall through the cracks or languish in probate.

**Produce over 500 sortable/modifiable reports totaling both future and realized bequest income** expected over any time period you select, such as weekly, monthly, semi annually,...compare 2008 to 2009, etc.

**Produce detailed cash flow analysis charts** to show what is in the pipeline and when it will come in for BOTH Future and Realized Bequests for any date range you want.

**Communicate almost automatically** with executors, attorneys and trust officers, using built-in template letters.

**Time your communications with estate professionals** so that you are proactive rather than reactive.

**Set Actions and Reminders** as well as use Auto Alerts to keep up to date on all administration and collections from estates.

**Simplify Accounting** by computing present values of future income to meet the new FASB (Financial Accounting Standards Board) and AICPA (American Institute of Certified Public Accountants) rules on reporting requirements.\*\* BIPSTER computes the present value **daily**, so you can pull a report any time with the correct present value.





## **Jammin' for Success...**

Gift Annuities, Gift Planning & All That Jazz!

29<sup>th</sup> Conference on Gift Annuities – April 28-30, 2010



# Evaluating Gift Annuity Programs

Presented by:

Frank D. Minton  
Senior Advisor  
PG Calc  
115 NE 100th St, Ste 300  
Seattle, WA 98125  
206-329-8144  
fminton@pgcalc.com

Presented by the American Council on Gift Annuities  
233 Mc Crea Street, Suite 400, Indianapolis, IN 46225  
317-269-6271 [www.acga-web.org](http://www.acga-web.org) [acga@acga-web.org](mailto:acga@acga-web.org)



# Introduction

During the past two years, comments such as the following are increasingly common:

Last year we had to move \$100,000 of general assets to our segregated reserve fund in order to meet state requirements.

Our charity has suspended the issuance of gift annuities.

Our charity had been planning to start a gift annuity program, but because of the risks involved our board is now having second thoughts.

It appears that the reserves for some of our annuities may be exhausted before the annuities terminate, and we are wondering whether we can use reserves from other annuities to continue payments.

We are wondering whether it would make sense for us to reinsure some or all of our annuities.

Is there a recommended asset allocation for the investment of gift annuity reserves?

Our volume of new annuities has decreased, and we don't know whether that's a common experience because of the economy, or whether we are not doing a good job marketing them.

Because of the concerns expressed in these comments, some charities are considering an audit of their gift annuity program. It might be a risk audit to identify problem annuities, project residua, and determine the profitability of the program; or it could be a comprehensive audit which also includes a review of policies and marketing strategy.

This paper is about the evaluation of gift annuity programs. It takes the reader through the process for assessing risk and determining profitability, and in so doing it describes practices that would help a charity minimize financial risk and improve the performance of the gift annuity program.

## 1. HOW DO YOU MEASURE THE PROFIT OF A GIFT ANNUITY PROGRAM?

The simplest formula for determining the profit of a gift annuity program is:

$P = D - E$ , where

P is profit,

D is the total of all distributions (also known as "residua") received from matured gift annuities and expected from existing gift annuities, and

E is total expenses other than those paid from gift annuity reserves.

If the charity has kept good records, past distributions are easily determinable. They would include transfers of residua when payment obligations terminated, any amounts expended for

charitable purposes at the time gift annuities were established, and withdrawals from the gift annuity reserve fund not associated with the termination of obligations. We will call the totality of all past distributions  $D_p$ .

It is, of course, impossible to know future distributions, but they can be approximated through the methodologies described below. We will refer to all future distributions as  $D_f$ .

Most charities charge the direct costs of investing reserves and administration of gift annuities to the gift annuity reserve fund. For example, if the charity outsources investment and management responsibilities to a vendor, the annual charge may be in the range of one percent of the market value of reserves. If this expense is deducted from gift annuity reserves, the net return on the investment of those reserves will be lower, and distributions for charitable purposes will consequently be reduced.

In determining the profit of the program, only expenses paid by the charity from funds other than gift annuity reserves would constitute "E" in the formula. There could be three categories of such expenses:

- First, the fees paid for state registrations, actuarial services, and filing annual state reports.
- Second, marketing expenses including collateral material and travel expenses in connection with donor visits.
- Third, indirect costs, which might be a percentage of salaries and office expenses of staff who spend time on the gift annuity program.

While definite numbers are available for the first category of expenses, the next two categories pose a challenge. Marketing materials and donor calls often deal with a variety of giving instruments, so it is difficult to isolate the portion that applies to gift annuities. The same is true of staff time. Also, the charity might employ the same number of gift planning staff even if it discontinued offering gift annuities.

Even though a considerable amount of subjectivity would be involved, it is possible to apportion some of the second and third category of expenses to the gift annuity program. However, in fairness, we should add to gift annuity distributions other types of gifts that have been stimulated by the gift annuity program. For instance, individuals who establish gift annuities sometimes develop a closer relationship with the charity, which results in increasing their annual giving and/or including the charity in their estate plan. Also, a visit with the intention of discussing a gift annuity with a person who responded to a gift annuity target mailing might morph into a discussion of a different, and perhaps larger, gift instrument such as a charitable remainder trust.

Because it is so difficult to quantify all of these things, and because it is known that a gift annuity program both carries a cost and has corollary benefits, we will assume that these added benefits are roughly equal to added institutional costs for marketing and overhead. Therefore, in calculating the profit of the program, we will factor into the formula only those direct administrative expenses that are not deducted from the gift annuity reserve fund.

Hence, the expanded formula would be:

$$P = (D_p + D_f) - E, \text{ where}$$

P is profit,

$D_p$  is the total of all past distributions,

$D_f$  is the total of projected future distributions, and

E is the total of direct administrative expenses, past and projected, paid from general institutional funds and not deducted from gift annuity reserves

## 2. HOW CAN YOU PROJECT DISTRIBUTIONS FROM EXISTING GIFT ANNUITIES?

As noted, the value of  $D_f$  (future distributions) cannot be known, but it can be approximated to the degree necessary to determine the likely profitability of the gift annuity program, not taking into consideration new gift annuities that may be established. There are two methodologies for projecting future distributions. One we will call the “constant-net-return model,” and the other the “Monte Carlo model,” and we will discuss each in turn.

### A. Constant-Net-Return Model

This model assumes that the charity earns a fixed constant net return on gift annuity reserves until the annuity terminates. It further assumes that every annuitant lives to the end of life expectancy, determined as of the date the analysis is done.

Let's assume that at the time the annuity was established, the annuitant's life expectancy was 14.0 years. Five years later the gift annuity program is audited, and at that time, per the mortality tables, the life expectancy of the annuitant is 10.1 years. The life expectancy used in the analysis would be 10.1 not 9.0 years (life expectancy at the time of the gift minus the 5.0 years the annuitant has already lived).

When doing the analysis, we must determine which mortality tables to use. One possibility is to use the Annuity 2000 tables. However, that may understate life expectancies. The ACGA, based on research it conducted a few years ago, concluded that life expectancies of gift annuitants are longer than those in the Annuity 2000 tables. That is why it makes adjustments to those tables by assuming all annuitants are female, setting their ages back two years and projecting for improved mortality since the tables were published. This procedure is very conservative – too conservative in the opinion of some. For purposes of demonstrating how the constant-net-return model works, we will use the Annuity 2000 tables without these adjustments.

It is also necessary to choose the assumed constant net returns for the calculations. We would recommend choosing at least three constant net returns for purposes of comparison, and the selection should take into consideration historical returns on a

portfolio such as the charity's and also current returns on such a portfolio. For example, the calculations might be done assuming constant net returns of four, five, and six percent. When choosing the assumed returns, keep in mind that the gross returns must be these net returns increased by whatever is being paid from gift annuity reserves for investment and administrative services. If the charity is outsourcing investment and administration to a vendor who charges one percent of the market value of gift annuity reserves, the gross returns would have to be five, six, and seven percent, respectively.

Because of the constraints of space, only two constant net returns – five percent and six percent – are used for the calculations in the chart below

Gift No.	Year of Gift	Gift Amount	Current FMV	Actuarial Age(s)	Gender	Annuity Amount	Projected Residua, Annuity 2000 Tables	
							5% Constant Net Return	6% Constant Net Return
1	1989	25,000.00	11,585.47	85	F	1,850.00	(1,469.92)	(794.59)
2	1991	25,429.38	10,701.46	80	F	1,805.49	(7,630.71)	(7,078.34)
3	1992	10,000.00	2,327.92	95/92	M,F	780.00	(2,785.94)	(2,736.16)
4	1994	10,000.00	3,600.70	95/92	M,F	730.00	(876.64)	(735.74)
5	1997	35,000.00	4,951.03	83	F	2,730.00	(20,712.56)	(20,654.10)
6	1999	51,879.98	5,949.04	84	M	4,150.40	(27,821.78)	(27,766.20)
7	1999	80,000.00	39,169.88	84	F	6,560.00	(11,569.40)	(9,523.76)
8	2000	100,000.00	23,409.56	86/88	M,F	7,700.00	(50,679.08)	(50,190.68)
9	2002	40,000.00	36,530.88	89/86	M,F	3,120.00	20,301.47	24,270.98
10	2003	100,000.00	82,671.48	74/73	M,F	6,000.00	20,649.68	43,987.42
11	2004	30,000.00	24,363.86	76/76	M,F	1,860.00	6,574.25	12,183.52
12	2004	30,000.00	23,960.79	69/66	M,F	1,650.00	1,380.89	11,626.11
13	2004	10,000.00	7,668.08	83/75	M,F	620.00	1,710.65	3,255.33
14	2005	10,000.00	7,530.82	76/68	M,F	570.00	(258.66)	2,112.97
15	2005	100,000.00	73,953.60	92/83	M,F	7,500.00	21,226.00	29,032.20
16	2005	10,000.00	6,203.80	94	M	1,130.00	1,993.14	2,223.60
17	2006	52,771.92	41,409.18	87/87	M,F	4,010.67	16,750.21	20,978.38
18	2006	10,000.00	7,071.64	84	F	830.00	1,772.04	2,345.28
19	2007	10,000.00	7,730.33	58/17	M,M	380.00	10,927.12	74,181.67
20	2007	100,000.00	74,775.25	80	F	7,400.00	19,615.30	28,157.50
21	2007	20,000.00	15,365.59	89/79	M,F	1,400.00	3,775.51	5,949.08
22	2007	10,000.00	7,443.04	69	M	630.00	417.68	1,934.75
23	2008	200,000.00	152,368.84	78/76	F,F	12,800.00	8,746.42	40,471.78
24	2008	100,000.00	82,428.80	76/68	M,F	5,900.00	10,804.30	38,670.30
25	2008	100,000.00	95,904.80	81	M	7,800.00	58,687.85	69,245.90
<b>Totals</b>		<b>1,270,081.28</b>	<b>849,075.84</b>			<b>89,906.56</b>	<b>81,527.82</b>	<b>291,147.20</b>

Let's assume that 10 of this charity's annuities have matured to date, that \$410,000 was contributed for these annuities, and that the distributions (residua) from these annuities totaled \$305,000. Let's further assume that the direct administrative costs paid from the

charity's general fund, both in the past and projected to be expended in the future, will total approximately \$40,000.

If the charity earns a five-percent constant net return on reserves and all annuitants live to life expectancy per the Annuity 2000 tables, then the charity's profit would be:

$$\$305,000 + 81,527.82 - 40,000 = \$346,527.82$$

If the constant net return on reserves is six percent, the charity's profit would be:

$$\$305,000 + 291,147.20 - 40,000 = \$556,147.20$$

### B. Problems with the Constant-Net-Return Model

There are three problems with the constant-net-return model.

- 1) The future average net return cannot be known. During the 1990s, it was not uncommon for a charity to realize average returns of nine or ten percent, especially if equities comprised a significant percentage of the portfolio. However, in recent years, average returns have often been four percent or less, and sometimes even negative.
- 2) Returns will not be constant, and the timing of returns affects outcomes. Imagine three annuities funded with identical amounts, each lasting 10 years, and each having an average return on reserves of six percent. The first annuity sustains investment losses the first two years followed by very good returns during the latter part of the period. The second has excellent returns in the early years but some losses late in the period. The third has constant returns. The first annuity will have the smallest residuum, the second annuity the largest, and the third will be between the others.
- 3) Some annuitants die before their actuarial life expectancy and some after.

Despite these inherent problems, the constant-net-return model does show outcomes if certain assumptions hold true. Thus, it is helpful in identifying problematic annuities and revealing to a charity the financial health and overall profitability of its gift annuity program.

### C. Monte Carlo Model

Instead of assuming a fixed return each year, a Monte Carlo program randomly generates returns to simulate performance under historically representative conditions, and it overlays these returns with randomly-generated life spans. For any given annuity, it may run a thousand trials, each having a different date of death and different return on the various classes of assets that comprise the portfolio of the gift annuity reserves. It is possible to enter into the program the percentages of the total portfolio consisting of different categories of equities and bonds as well as the percentage held in cash or cash equivalents. An expense percentage can also be entered.

The program will show the percentage probability that the residuum from a gift annuity will be “x” amount or higher. For example, it can be demonstrated that, based on the information entered, there will be a 25-percent chance that the residuum of an annuity will be \$90,000 or greater, a 50-percent chance that it will be \$70,000 or greater, and a 75-percent chance that it will be \$30,000 or greater, etc.

Following is a chart comparing residua projections, based on the constant-net-return model, with probability projections based on the Monte Carlo model. Certain pertinent information previously listed is not repeated.

**Comparison of Projected Residua Based on Constant-Net-Return and Monte Carlo Models**

Gift No.	Projected Residua, Annuity 2000 Tables		Residuum		
	5% Constant Net Return	6% Constant Net Return	25% Probability Residua this Amount or More	50% Probability Residua this Amount or More	75% Probability Residua this Amount or More
1	(1,469.92)	(794.59)	5,796.00	373.00	(8,030.00)
2	(7,630.71)	(7,078.34)	1,710.00	(6,790.00)	(17,692.00)
3	(2,785.94)	(2,736.16)	(1,450.00)	(3,652.00)	(6,621.00)
4	(876.64)	(735.74)	608.00	(1,230.00)	(3,643.00)
5	(20,712.56)	(20,654.10)	(11,127.00)	(24,373.00)	(42,757.00)
6	(27,821.78)	(27,766.20)	(15,258.00)	(35,636.00)	(61,668.00)
7	(11,569.40)	(9,523.76)	21,114.00	348.00	(33,840.00)
8	(50,679.08)	(50,190.68)	(32,580.00)	(64,196.00)	(106,876.00)
9	20,301.47	24,270.98	47,193.00	32,443.00	20,616.00
10	20,649.68	43,987.42	212,234.00	105,242.00	37,972.00
11	6,574.25	12,183.52	50,429.00	25,344.00	9,494.00
12	1,380.89	11,626.11	93,511.00	39,913.00	10,285.00
13	1,710.65	3,255.33	7,860.00	4,338.00	959.00
14	(258.66)	2,112.97	19,480.00	8,785.00	1,810.00
15	21,226.00	29,032.20	56,820.00	35,500.00	5,180.00
16	1,993.14	2,223.60	3,856.00	1,938.00	(1,036.00)
17	16,750.21	20,978.38	45,910.00	29,831.00	13,812.00
18	1,772.04	2,345.28	5,174.00	2,870.00	(817.00)
19	10,927.12	74,181.67	1,403,826.00	444,847.00	110,675.00
20	19,615.30	28,157.50	85,935.00	51,965.00	15,700.00
21	3,775.51	5,949.08	20,506.00	11,876.00	4,237.00
22	417.68	1,934.75	7,101.00	3,516.00	(1,162.00)
23	8,746.42	40,471.78	138,013.00	70,300.00	(19,694.00)
24	10,804.30	38,670.30	237,070.00	112,160.00	35,540.00
25	58,687.85	69,245.90	101,855.00	77,705.00	49,945.00
	<b>81,527.82</b>	<b>291,147.20</b>	<b>2,505,586.00</b>	<b>923,417.00</b>	<b>12,389.00</b>

Based on the Monte Carlo model, one could say the following regarding the profit of this charity’s gift annuity program.

There is a 25-percent probability that the profit will be:



$$\$305,000 + 2,505,586 - 40,000 = \$2,770,586$$

A 50-percent probability that the profit will be:

$$\$305,000 + 923,417 - 40,000 = \$1,188,417$$

A 75-percent probability that the profit will be:

$$\$305,000 + 12,389 - 40,000 = \$277,389$$

Gift number 19 skews the results because it has an annuitant only 17 years of age, and over the 70 or so years of payments before this annuity terminates, the performance could vary widely. For comparison purposes, it is probably better to delete this annuity. If it were deleted, there would be a 25-percent probability of residua totaling \$1,101,760 and a 50-percent probability of residua totaling \$478,570. Even if the high number for this annuity were realized, the present value would be relatively small because of the life expectancy of the successor annuitant.

#### D. Problems with the Monte Carlo Model

Like the constant-net-return model, the Monte Carlo model has problems and limitations.

1. The random returns built into the program might prove unrealistically high or low if financial markets over the next two or three decades perform below or above historic average.
2. The Monte Carlo model provides less precise information to charities who want to plan for future cash flow.

#### E. The Value of Using Both Models

To the extent the two models produce similar projections, a charity can evaluate its program and plan for the future with more assurance. It is interesting to note that in most cases where negative residua are projected by the constant-net-return model, the Monte Carlo program shows that there is a 50-percent probability of negative residua. This would be a powerful indicator that these annuities are at risk. For healthier annuities as well, it makes sense to compare outcomes and compute profitability both ways. The charity will have a better idea of whether the program is producing the desired results.

### 3. SHOULD A CHARITY EXPECT TO REALIZE A PROFIT EQUAL TO 50-PERCENT OF CONTRIBUTIONS?

This perception is based on the fact that one of the assumptions underlying the ACGA rates is that the residua will average 50 percent of contributions. Actually, for certain younger and

older ages, rates are suppressed, resulting in projected residua in excess of 50 percent. This does not mean that the residuum of every single annuity is expected to be half of the contribution. When annuitants die early, it will obviously be more, and when they live a long time it may be less. The 50 percent is an average.

Thus, it might be concluded that a gift annuity program producing a profit equal to 50 percent of contributions would be average, while one with a profit below 50 percent would sub-par, and one with a profit above 50 percent could be regarded as superior.

The fact that most ACGA rates assume a residuum of 50 percent does not reflect the average residuum charities are actually achieving. According to the 1994, 1999, and 2004 national gift annuity surveys, the residuum averaged well in excess of 50 percent. It was highest in 1999, which might expected because a bull market prevailed through most of the 1990s. By 2004, the average residuum had dropped, but it was still above 50 percent. The most recent survey, based on data collected in 2009, had not been published when this paper was being written. It is possible, that average residuum will have fallen even further because of recent declines in stock values and continuing low interest rates.

Even though a national benchmark is not available until the new survey results are published, we will assume that a 50-percent-of-contribution profit is normative and evaluate our hypothetical gift annuity program accordingly.

Contributions for matured annuities	\$410,000
Contributions for existing annuities	<u>1,270,081</u>
Total contributions	\$1,680,081
Distributions from matured annuities	\$305,000
Projected distributions from existing annuities (assuming five-percent constant net return)	<u>81,528</u>
Total received and projected distributions	\$386,528
Administrative expenses paid from general funds	<u>(40,000)</u>
Net distributions	\$346,528
Profit as a percentage of contributions	20.63%

Per a benchmark of a profit equal to 50 percent of contributions, this program is clearly not performing well. If we assume a future constant net return of six percent, the profit percentage rises to 33.1 percent but still remains well below the benchmark. Not only is the profit percentage low, but 36 percent of the annuities are at risk of exhaustion before the end of the annuitants' life expectancies, assuming a five-percent constant net return. Even with a six-percent return assumption, 32 percent are at risk.

#### 4. WHY DO GIFT ANNUITY PROGRAMS UNDERPERFORM?

Unfortunately, there are a number of gift annuity programs like our hypothetical one that underperform. Not only is their profit margin narrow, but they have numerous annuities at risk of exhaustion. That is, the reserves may be entirely consumed before the payment obligation terminates, and they may have to transfer unrestricted institutional funds to continue payments. One or more of the following factors could have caused this situation.

- A. The gift annuity rates offered by the charity were too high. Possibly the charity, in an effort to gain a competitive advantage, exceeded the rates suggested by the American Council on Gift Annuities (“ACGA”). In retrospect, possibly the ACGA rates themselves were a little higher than they should have been at certain times.
- B. The combined investment and administrative expenses charged to the gift annuity reserve fund(s) were higher than the assumed expenses on which the ACGA rates were based. For example, a charity might be paying a financial institution 90 basis points for investment and administration and also be debiting from the reserves another 100 basis points for internal costs in connection with gift annuities. An internal fee is more common among community foundations and national organizations that issue gift annuities for the benefit of affiliates. The ACGA rates assume expenses of 100 basis points per year, and if a charity’s total expenses charged to reserves total 190 basis points, its residua will average less than the ACGA target of 50 percent unless its total return exceeds the assumed return underlying the ACGA rates.
- C. The charity spent some portion of the contribution up front and invested the balance in the reserve fund. The residua of gift annuities will be less likely to average 50 percent unless the entire contribution is added to the reserves and nothing is withdrawn until the termination of the obligation.
- D. The gift annuity reserves sustained significant investment losses. This is, of course, the number one reason why so many gift annuities are now at risk. A significant percentage of reserves – perhaps as much as 60 or 70 percent – may have been invested in equities, causing the reserve fund to lose upwards of 25 to 35 percent of its value, first in the period 2001-2003, and especially in 2008 and early 2009.
- E. The annuitants of a particular charity lived well beyond the life expectancies on which the gift annuity rates were based. This is not likely unless the charity has a small number of annuities. Usually, a charity is far more affected by investment losses than by mortality variations.

### 5. HOW DO YOU DEAL WITH AT-RISK GIFT ANNUITIES?

This problem does not arise if a charity’s gift annuities are unrestricted as to purpose. In fact, if that is the case, the charity may not have set up a fund-accounting system to track the performance of each annuity. It will simply make payments from the gift annuity pool, and what matters is whether the pool as a whole is adequate to meet all annuity obligations.

However, if all or most of a charity's annuities are for designated purposes, and the reserves of a particular annuity run dry, it cannot tap the reserves of other annuities to continue payments on the exhausted one. For example, if the reserves for an annuity designated for a university's medical school are exhausted, it cannot use some of the reserve from an annuity designated for the university's business school to continue payments on the annuity established to benefit the medical school. This is true even if the business school annuity has surplus reserves.

The annuities of colleges and universities, community foundations, and national organizations that issue annuities for the benefit of affiliates typically have annuities that are restricted as to purpose. Even if their gift annuity program as a whole is financially sound, a particular annuity may run dry. Obviously, a charity could transfer some of its general funds to continue payments, but this will not be a popular solution when the administration has precious little discretionary money at its disposal. To prepare for this eventuality, the charity should build a fund that can be used to continue payments on any existing gift annuities that might exhaust their reserves in the future. Here are some possible ways to build the fund.

- Require that a certain percentage (for example, 10 percent) of all annuities be for the unrestricted purposes of the charity. At the termination of the obligation, 10 percent of the residuum would be added to the unrestricted contingency account. The problem with this option is that it will take a long time to build the contingency fund.
  - Have a stated policy, noted in the disclosure statement and marketing material that a certain percentage (for example, five percent) of the contributions will be immediately transferred to an unrestricted fund. The balance will be transferred to the gift annuity reserve fund, and the residuum used for the designated purpose upon termination of the payment obligation. The residuum available for the designated purpose will, of course, be smaller, but the size of the annuity payments will be unaffected because they are based on the amount contributed. The charity keeps these up-front assessments in a separate fund, or in an unrestricted account within the segregated reserve fund. The latter practice would help those charities that are having difficulty meeting state reserve requirements.
  - Assess a modest administrative fee (50 basis points, for example) and use fees to build a contingency fund. Of course, every additional fee reduces the residuum. The ACGA rates presuppose an annual fee equal to one percent of gift annuity reserves, so if external plus internal fees total 1.5 or 2.0 percent, the residuum may be less than 50 percent of the contribution. However, the total amount available to the charity will not be diminished, for internal fees, to the extent they are not needed to continue payments on exhausted annuities, can be used for general charitable purposes. All fees, whether front-end, back-end, or annual should be disclosed to donors.
- 6. WHAT IS A PRUDENT POLICY REGARDING EXPENDITURE OF GIFT ANNUITY FUNDS FOR CHARITABLE PURPOSES?**

According to the 2004 ACGA survey referenced above, 83 percent of charities place the entire contribution for a gift annuity in their reserve fund and, upon termination of the

annuity, use the residuum for charitable purposes. Only 17 percent spent some portion of the contribution immediately.

The latter is permissible so long as a charity maintains sufficient reserves to back outstanding annuities and meet state reserve requirements. However, it increases the risk that, during an economic downturn, the charity may have to move some of its general funds into the reserve fund. Some financially-strapped charities spent a significant portion of each contribution when it was received, intending to replace these “borrowed” funds when circumstances improved. They have been unable to replenish the reserves, which are now inadequate to fulfill future obligations.

To avoid ever finding itself in such a situation, a charity should adopt one of these spending policies:

- A. If it tracks individual annuities (i.e., does fund accounting), then it spends nothing until the annuity terminates and only at that point uses the residuum for charitable purposes – the policy of most charities as noted above.
- B. If its annuities are unrestricted and it does not track them individually, then it may periodically make a distribution from the reserve fund for charitable use, being careful at all times to maintain sufficient surplus reserves to meet state requirements. (New York requires a surplus of 26.5 percent.)
- C. Another option, if all annuities are unrestricted, is to withdraw an amount equal to the required reserve as of the death of the sole or surviving annuitant. This is a conservative policy and over time it will build surplus reserves, but at the expense of current expenditures for charitable purposes.
- D. If it chooses to spend some of the contribution immediately, then it should transfer to the reserve fund at least 125 percent of the present or actuarial value of the annuity obligation and spend only the balance. If the charity is registered in New York, that percentage should be larger. This practice is preferable to a policy of spending “x” percent of contributions and investing the balance because, when interest rates are low, the balance may be barely adequate to meet reserve requirements, let alone provide a cushion. (Note: spending “x” percent probably would not be a problem if the percent is small.) It should be remembered that the projected 50-percent residuum is based on the assumption that 100 percent of the contribution is invested in the reserve fund. If a portion is expended, the residuum will be less.

Some charities, whose gift annuity reserves have fallen short of state requirements, have been holding the residua of terminated annuities in the segregated reserve fund. This may be an acceptable temporary expedient, but the charity may not be keeping faith with donors, if it unreasonably delays expenditure of funds for the donors’ intended purposes.

### **7. HOW CAN A CHARITY CONTROL RISK AND INCREASE THE PROFITABILITY OF ITS GIFT ANNUITY PROGRAM?**

A number of strategies for limiting risk and increasing profitability have been implicit in the preceding discussion, but they are highlighted in the following list.

A. Invest Gift Annuity Reserves Prudently.

Many charities do not understand that the asset allocation they use for their endowment or for charitable remainder trusts is not appropriate for gift annuity reserves. When the equity exposure is too high and values plummet, as they did in 2002 and again in 2008, the charity may find that its annuities are under-reserved. It then has difficulty restoring reserves to an acceptable level because annuity payments, unlike distributions from an endowment, are not reduced when market values decrease.

At the opposite end of the spectrum are charities that are overly conservative, investing nearly all of their reserves in cash equivalents and short-term bonds, and seeing a steady erosion of reserves because the meager return is below the return on which ACGA rates are based.

The appropriate asset allocation depends, in part, on the financial situation of the charity, and the amount of gift annuity reserves. For example, a large university with significant surplus reserves could prudently invest more in equities than could a smaller charity with modest reserves. In general, though, fixed-income investments should comprise a higher percentage of gift annuity reserves than of endowed funds. Diversification, of course, is advised in both cases. Particularly in the case of annuities, expected cash flow should be taken into consideration.

B. Adopt Sensible Gift Annuity Acceptance Policies.

Some charities accept \$5,000, or even less for a gift annuity, and they may issue immediate gift annuities for people in their 50s. The cost of establishing and administering these gift annuities over their term very likely exceeds the present value of the residuum. To assure that a gift annuity is cost effective, there should be realistic policies regarding the minimum age of annuitants and the minimum contribution amount.

There should also be policies dealing with acceptable assets. Some charities accept only cash and securities that can be readily monetized. That is the safest course, but it could preclude some excellent, but admittedly more risky, gifts. Suffice it to say that assets such as real estate and closely-held stock should not be automatically rejected, but they should be very carefully screened and risk control measures taken.

C. Reinsure All or a Portion of Certain Gift Annuities

Some charities are hesitant to accept a very large contribution for a gift annuity, especially if the gift annuity pool is relatively small, for they would be at risk if the annuitant lives well beyond life expectancy. They might consider reinsuring a portion of the obligation. For example, if \$1,000,000 were contributed for an annuity paying \$70,000 per year, the charity might purchase one or more commercial annuities paying \$49,000 (70 percent of the obligation) and self-insure the remaining 30 percent of the obligation. If the reinsurance premium were \$510,000, the charity would realize \$190,000 plus earnings on the 70% of the \$1,000,000 contribution allocated to the reinsured portion of the gift annuity, along with 50 percent  $\pm$  of the \$300,000 (i.e., 30%

of \$1,000,000) allocated to the self-insured portion. Selective reinsurance of gift annuities, or reinsurance of all of them, is a way to offload risk.

- D. Consider Asking Certain Annuitants – Those Who Appear Not to Need Payments for Living Expenses – If They Would Be Willing to Assign Their Annuity Interests to the Charity.

They need not assign their entire annuity interest. For instance, they could assign an undivided 50-percent fractional portion of their annuity, which means that in the future payments would be only half of what they are now. This would reduce the charity's obligation, help it meet reserve requirements in regulated states, and preserve a larger amount for charitable purposes.

- E. Implement a Creative Marketing Plan.

As the volume of gift annuities increases, the mortality risk decreases. If a charity has just a few gift annuities, three-quarters of the annuitants might live beyond life expectancy, increasing financial risk. However, the mortality experience of several hundred annuitants is likely to approximate the tables. Obviously, the primary reason for marketing gift annuities is to increase dollars for charitable purposes, and this objective will be advanced when the mortality risk is lessened. Also, a larger pool may open investment opportunities not available for a small pool. While this paper does not address marketing, we do want to note that it would be included in an overall evaluation of a gift annuity program.

**8. IS REINSURANCE A GOOD WAY TO DEAL WITH PROBLEM ANNUITIES AND LIMIT FUTURE RISK?**

As commonly understood, reinsurance of a gift annuity means using a portion of the contribution to purchase from a commercial insurance company an annuity that makes payments equal to the payment promised in the gift annuity agreement. The charity would have effectively transferred the risk, though it would still be liable for payments if the insurance company became insolvent and the payment obligation exceeded the state guaranty limit. Generally, state laws do not require a charity to maintain reserves for any annuity that is reinsured. (It should be noted that in New York and California "reinsurance" has the more technical meaning of reinsuring the risk, and it is more difficult to arrange.)

- A. Reinsurance as a Solution for Problem Annuities.

When the reserves for a gift annuity have been depleted, they may be insufficient to cover the reinsurance premium. Consider this example:

A few years ago, a female donor, now age 75, contributed \$100,000 for an annuity that would pay her \$6,500 per year for life. Because of market losses, the reserves for this annuity are now \$61,200. To purchase from an insurance company a pure life annuity paying \$6,500 per year would require a premium of \$66,000. In order to reinsure this annuity, the charity would have to add \$4,800 of its unrestricted funds to existing

reserves. It might be willing to do this to prevent an even greater future cost, but it may have second thoughts about incurring a present expense and having to tell the donor that absolutely nothing will be available for the intended charitable purpose. Contrary to what charities may suppose, reinsurance is not necessarily a cost-free way to deal with annuities that are severely under-reserved.

B. Reinsurance as a General Practice to Limit Risk.

While reinsurance, as commonly understood, does not eliminate risk entirely, it does definitely limit it. Reinsurance is a way to substantially offload the risk inherent in gift annuities. That is why some charities, as a matter of policy, choose to reinsure all of their annuities. They might also choose reinsurance in order to free-up money (the difference between the contribution and the premium cost) for current needs. A small charity with modest assets on its balance sheet might conclude that reinsurance would be comforting to donors.

Instead of reinsuring all annuities, a charity might choose to reinsure just some of them. As noted above, to limit the amount of risk to which it is exposed, it could reinsure any annuity over a certain size. It might also choose to reinsure gift annuities when annuitants are either under or above a certain age.

The advantages of reinsurance must be weighed against the disadvantages. The charity will realize less money when annuitants die early, and if it can earn a reasonable return on gift annuity reserves, will probably realize less profit from the entire gift annuity program. Another disadvantage is that donors may be disappointed and confused when they learn that the charity retains only a fraction of the contribution.

C. Calculating Profit When Annuities Are Reinsured.

If a charity were to reinsure all of its existing gift annuities, it could determine the profit of the program up to this point by the formula:

$$P = D_p = (R - C) - E, \text{ when}$$

P is profit,

$D_p$  is the total of all past distributions,

R is the value of current reserves,

C is the cost of reinsuring existing annuities, and

E is the total direct administrative expenses paid from institutional funds and not deducted from gift annuity reserves.

To determine the advisability of reinsuring existing gift annuities, a charity should compare (1) profit realized if it reinsured with (2) profit projected if self-insured, using a conservative net return assumption for the latter calculation.

To compare reinsurance and self-insurance of a new annuity, follow these steps:



- Obtain a premium quotation for reinsuring the gift annuity.
- Subtract the premium from the amount contributed, and then compound that difference (the amount retained) for the life expectancy of the annuitant at a return rate the charity might realistically earn.
- Project the residuum the charity would realize from self insurance using the constant-net-return model.
- Compare the compounded amount (in the case of reinsurance) with the projected residuum (in the case of self-insurance).

To have a more complete comparison, you could do calculations with different dates of the annuitant's death, some before and some after actuarial life expectancy.

### 9. DOES IT MAKE SENSE TO CONTINUE OR TO ESTABLISH A GIFT ANNUITY PROGRAM?

#### A. Concerns about Financial Viability.

Business officers and governing boards are paying attention to gift annuity programs as they have never done before. Alarmed by the risk of losses on gift annuities, and surprised by having to transfer precious unrestricted funds to meet the requirements of state-mandated reserve funds, some have suspended gift annuity programs.

Some charities that intended to establish a new gift annuity program have put their plans on hold. Increasingly, people are asking whether a gift annuity program makes sense. Here are some of the concerns that are being expressed.

- 1) In the current economic environment we cannot earn as much as the gift annuity rates we are paying.
- 2) Life expectancies are continuing to increase, and we are committing payments for a period that could be much tougher than we anticipate.
- 3) Even if we don't incur an actual loss, the present value of the residuum we eventually receive is often too small to justify the effort. For example, the present value of the residuum of a \$10,000 contribution by a female, age 65, is only \$2,377, assuming we earn a constant net return of 4.25 percent and use the same percentage for computing present value. This, it would seem that time is better spend securing outright gifts and bequests. While the latter may be revocable, at least they don't subject us to risk.
- 4) Even if gift annuities can be beneficial to our charity, now is perhaps not the right time to offer them. Let's suspend the program and reconsider it when economic conditions improve.

#### B. Responses to These Concerns.

While we take all of these concerns seriously, we believe that it is possible to alleviate all of them and demonstrate that gift annuity programs still make sense.

- 1) Annuities, whether issued by insurance companies or charities, return part of the capital investment to the annuitants. It is expected that annuity rates, especially by older annuitants, will be higher than the return on investments. A charity that follows the ACGA rates needs a net return of only 4.25 percent for the average amount remaining for the charity to be 50 percent of the contribution.
- 2) The rates suggested by the ACGA are based on projected increases in life expectancy since the Annuity 2000 mortality tables were published. These rates, in fact, assume longer life expectancies than commercial rates do.
- 3) According to the 2004 ACGA national survey, the median value of a gift annuity was nearly \$30,000, and the average annuitant age at the time of the contribution was 78. Such an annuity would have a present value in the range of \$12,000. We certainly would welcome outright gifts of that size. We should also keep in mind that many gift annuity donors are unable to make outright gifts of this size. Often, they establish multiple annuities, so even if a single annuity is of modest size, cumulatively the present value is substantial. Furthermore, the annuity may foster a closer relationship with the charity and stimulate other types of gifts.
- 4) As a result of recent gift annuity rate reductions, new gift annuities are very likely to result in significant residua for the charity, even if returns are low. Moreover, the issuance of new annuities based on the current ACGA rates will result in the infusion of surplus reserves, and this will help a charity meet the reserve requirements of a state where it may be registered.

The immediately following chart shows projected residua, assuming (1) constant returns, (2) ACGA rates, (3) quarterly payments, and (4) female life expectancies per the Annuity 2000 tables with a two-year setback in ages.

**Projected Residua  
Hypothetical Annuities Established**

		<b>Projected Residua</b>		
	<b>Annuitant</b>	<b>2% Net</b>	<b>4% Net</b>	<b>6% Net</b>

Contribution	Age	Return	Return	Return
\$100,000	Male, 65	8,573	54,176	131,839
100,000	Female, 65	(5,618)	45,290	139,428
100,000	Male, 70	19,543	55,151	109,693
100,000	Female, 70	6,523	46,396	111,951
100,000	Male, 75	27,876	55,098	93,142
100,000	Female, 75	16,783	47,054	91,721
100,000	Male, 80	35,518	55,986	82,399
100,000	Female, 80	26,469	49,022	79,275
100,000	Male, 85	42,190	57,587	76,239
100,000	Female, 85	36,353	52,898	73,372
100,000	Male, 90	48,078	59,402	72,425
100,000	Female, 90	44,657	56,544	70,354

This chart demonstrates that, with current ACGA rates, gift annuities involve hardly any risk if XYZ charity simply invests contributions for new reserves in Treasuries. Of course, that may or may not be a wise investment, and residua could be considerably larger with a balanced portfolio. The point is that new gift annuities are very low risk unless the charity invests in a manner that exposes it to potentially significant investment losses.

The next two charts show the amount by which a contribution would exceed state-required reserves, taking into consideration that New York requires surplus reserves equal to 26.5 percent of actuarial reserves, and that certain other states require a 10-percent surplus.

**New York Reserves for New Gift Annuities  
ACGA Rates**

Donor	Contribution	Actuarial Reserves	NY Surplus 26.5%	Total NY Reserves	Excess
Male, 65	\$100,000	\$59,556.87	\$15,782.57	\$75,339.44	\$24,660.56
Female, 65	\$100,000	\$64,116.48	\$16,990.87	\$81,107.35	\$18,892.65
Male, 75	\$100,000	\$53,955.60	\$14,298.23	\$68,253.83	\$31,746.17
Female, 75	\$100,000	\$59,088.20	\$15,658.37	\$74,746.57	\$25,253.43
Male, 85	\$100,000	\$47,492.85	\$12,585.61	\$60,078.46	\$39,921.54
Female, 85	\$100,000	\$51,604.93	\$13,675.31	\$65,280.24	\$34,719.76

**Reserves for States Requiring 10% Surplus**

Donor	Contribution	Actuarial Reserves	Surplus 10%	Total Reserves	Excess
Male, 65	\$100,000	\$59,556.87	\$5,955.69	\$65,512.56	\$34,487.44

Female, 65	\$100,000	\$64,116.48	\$6,411.65	\$70,528.13	\$29,471.87
Male, 75	\$100,000	\$53,955.60	\$5,395.56	\$59,351.16	\$40,648.84
Female, 75	\$100,000	\$59,088.20	\$5,908.82	\$64,997.02	\$35,002.98
Male, 85	\$100,000	\$47,492.85	\$4,749.29	\$52,242.14	\$47,757.86
Female, 85	\$100,000	\$51,604.93	\$5,160.49	\$56,765.42	\$43,234.58

If a charity is having difficulty meeting state-required reserves for existing annuities, establishing new annuities will alleviate the situation and perhaps prevent the charity from having to transfer general funds to meet reserve requirements.

#### **10. SHOULD YOU CONDUCT AN EVALUATION OF YOUR GIFT ANNUITY PROGRAM?**

It is simply good business practice to determine whether your gift annuity program is making a profit and to consider how the profit margin can be improved. Most assuredly, if it is losing money, you should either take corrective action or terminate the program.

Many of the measurements described in this paper can be done internally, but you may need outside assistance with some, such as projections of outcomes using the constant-net-return and Monte Carlo models. Also, an external review may carry more weight with administrators and board members who are questioning the viability of the program.

If you do arrange for a formal evaluation of your program, it should do the following:

- A. Identify gift annuities at risk of exhausting their reserves before termination of the payment obligation.
- B. Determine the approximate residua expected from existing gift annuities.
- C. Project cash flow, taking into consideration expected distributions and institutional transfers for payments, if any.
- D. Based on the foregoing, calculate whether the program is making a profit, and whether it is performing below or above average.
- E. If reinsurance is under consideration, compare self-insurance and reinsurance of all or selected annuities.
- F. Examine distribution policies and see whether there is a place for continuing payments on exhausted annuities.
- G. Review policies regarding age of annuitants, minimum contribution levels, and acceptable assets to see whether they assure cost-effectiveness and limit risk.
- H. Consider whether the investment policy for gift annuity reserves is appropriate for the charity's situation. (In this regard, there could be modeling with different asset allocations.)

- I. If the evaluation is to be more than a “risk audit,” review the effectiveness of the marketing program and the stewardship of donors.

The evaluation analyzes risk and profitability for all annuities completed as of the date of the evaluation (those that have matured and those currently in force). New annuities will, of course, change the results. That is why an evaluation every few years is advisable. Then you can determine whether the program is improving with regard to risk and profitability.

An evaluation may confirm that the gift annuity program is profitable and performing well, which would be reassuring to the administration and board. Possibly, it may stimulate a course correction that will improve profitability. Either would be a positive outcome.





---

AMERICAN

---

COUNCIL ON

---

GIFT ANNUITIES

---

*Promoting Responsible Philanthropy*

American Council on Gift Annuities

233 McCrea Street, Suite 400 • Indianapolis, Indiana 46225

Phone: (317) 269-6271 • Fax (317) 269-6276

E-mail: [acga@acga-web.org](mailto:acga@acga-web.org) • Web: [www.acga-web.org](http://www.acga-web.org)