Strategies for Planned Giving

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Planned Giving Considerations

What to Give

- Cash
- Publicly Traded Stock
- Real Estate
- Tangible Personal Property

When to Give

- Lifetime or Testamentary Gift
- Timing to maximize income tax deduction
- Based on when the charity needs the funds

How Much to Give

- Amount of income willing and able to donate
- Amount of wealth willing and able to donate during lifetime
- Amount of residuary estate to leave to charity

Who to Give to

- Public Charity
- Private Foundation
- Donor-Advised Fund

Planned Giving Techniques

Low Complexity

- Direct Cash Gift
- Bequest in Will
- Beneficiary Designation on Life Insurance Policy or Retirement Plan

Moderate Complexity

- Donor-Advised Fund
- Gift of Appreciated Stock or Tangible Personal Property
- Qualified Charitable Distributions

High Complexity

- Private Foundation
- Charitable Lead Trust
- Charitable Remainder Trust

Appreciated Stock

Overview

- Rather than selling stock and donating cash to a charity, a donor may contribute the stock directly to the charity.
- The donor avoids paying capital gains taxes on the growth of the stock, and the charity receives a greater benefit (since the gift would have otherwise been reduced by the amount of taxes paid). The charity can then sell the stock without being subject to taxes.

Donor Benefits

- Avoids capital gains tax (up to 20%) on appreciation of stock held more than one year
- Receives charitable deduction for full fair market value (FMV) of stock on date of contribution
- Maximizes amount contributed to charity

Donor Drawbacks

- May be unwilling to part with a specific security and prefer to donate cash

Donor Profile

- Corporate Executives (or Retired Corporate Executives)
- Potentially anyone who owns appreciated securities

Appreciated Stock Example

Donor Scenario

- Jen is a corporate executive at Apple. Over the course of her career, she has received numerous stock grants and benefited from the growth in the stock price. She recently made a $100,000 pledge to her alma mater, which she decides to fulfill by gifting shares of her Apple stock that has a basis of $25,000.

Impact to Donor

- Jen receives a charitable income tax deduction of $100,000 (the full FMV of the stock, subject to AGI limits).
- Jen saves $15,000 in capital gains taxes (assuming a 20% capital gains rate).

Impact to Charity

- Jen's alma mater receives $100,000 worth of Apple stock, which it can then sell without being subject to capital gains taxes, as a tax-exempt organization.
- Had Jen first sold the stock and then donated cash, her school would have only received $85,000. In order to fulfill her pledge, she would have had to sell $117,647 worth of shares (assuming a proportionate cost basis) to net $100,000 in cash.

Life Insurance

Overview

- Individual may name charity as beneficiary of a life insurance policy.
- Alternatively, an individual may make an outright gift of an existing life insurance policy to a charity or purchase a new policy and irrevocably name a charity as the owner and beneficiary.

Donor Benefits

- Naming a charity as beneficiary is as simple as updating the beneficiary designation form and can be changed at any time.
- An outright donation or purchase of a new policy produces an income tax deduction, generally at the time of the transfer, as well as upon each premium payment.
- Ability to make a substantial gift to charity at a relatively low out-of-pocket cost

Donor Drawbacks

- No income tax deduction is available for naming charity as beneficiary.
- Certain states prohibit charities from owning a life insurance policy because they do not have an insurable interest on that individual's life.

Donor Profile

- Owns life insurance policy but has outgrown the original intent and no longer needs the proceeds
- Desire to fulfill charitable intentions, while preserving assets for family members

Life Insurance Example

Donor Scenario

- Karen owns a $500,000 life insurance policy that she took out when she was raising her children as a single parent. Her kids are now grown and financially independent, so she no longer needs the policy. Instead of surrendering the policy, Karen decides to make an outright gift to her church, naming it the owner and beneficiary of the policy.

Impact to Donor

- If Karen has paid $40,000 in premiums and the policy has a cash surrender value of $60,000, she could deduct $40,000 (subject to AGI limits). If she continues to pay the premiums, either directly to the insurance company or by donating cash to the church, she could deduct those as well.
- Had Karen simply named the church as beneficiary, she would not receive any income tax deduction.

Impact to Charity

- Upon Karen's death, the church will receive the $500,000 death benefit tax-free.
- Had Karen simply named the church as beneficiary, she would maintain the right to change the beneficiary at any time.

Retirement Plans

Overview

- Individual may name charity as beneficiary of a retirement plan.
- Retirement accounts may also be used to fulfill testamentary charitable bequests.

Donor Benefits

- Naming a charity as beneficiary is as simple as updating the beneficiary designation form and can be changed at any time.
- Retirement accounts are ideal assets to leave to charity because they are not subject to estate or gift tax and are deductible for income tax purposes. If left to heirs, these assets would be subject to both income and estate tax. Heirs would also pay income tax on the distributions and do not receive a step-up in basis on the assets.

Donor Drawbacks

- Retirement plan assets used to fulfill pecuniary (fixed dollar) bequests will be subject to Income in Respect of a Descendant (IRD) tax. This situation can be avoided by simply naming the charity as beneficiary.

Donor Profile

- Owns sufficient assets outside of retirement plans to satisfy family legacy desires
- Retirement accounts are not Roth accounts

Retirement Plan Example

Donor Scenario

- George has a 401(k) with a balance of $2,000,000. His wife, Martha, is the primary beneficiary, and MD Anderson is the contingent beneficiary. Martha predeceases George, but he does not update the beneficiary designations. When he passes away, the account balance will be distributed to MD Anderson.
- George also has cash of $2,000,000 and two homes, each valued at $1,000,000. George plans to leave these assets to his two children.

Impact to Donor

- Each of George's children will receive $1,000,000 cash and a home valued at $1,000,000.
- Had George named his children as contingent beneficiaries of his 401(k), the $2,000,000 balance would be treated as IRD. If the children were in the 37% tax bracket, they would each receive only $630,000 of their $1,000,000 share of the account.

Impact to Charity

- MD Anderson receives the full $2,000,000 balance.
- Had George not listed a contingent beneficiary, the 401(k) would have become part of his gross estate. Assuming that his Will included a $2,000,000 bequest to MD Anderson, using the 401(k) to fund such bequest would force the estate to recognize IRD income.

Qualified Charitable Distributions

Overview

- Individuals age 70 ½ and older are subject to Required Minimum Distributions (RMDs) from retirement accounts.
- Up to $100,000 of the annual RMD from an Individual Retirement Account (IRA) may be transferred directly to a tax-exempt charity and fulfill the required distribution.
- Applies exclusively to individual IRAs. Employer-sponsored retirement plans are ineligible.

Donor Benefits

- Distribution is not subject to federal income tax. Equivalent to 100% above-the-line deduction. Unlike most forms of charitable giving, this provides an income tax benefit to those who do not itemize deductions.
- If donor is married, each spouse can contribute up to $100,000 annually from his or her IRA.

Donor Drawbacks

- Distribution is not eligible for the charitable deduction.
- Individuals with employer-sponsored plans (i.e. 401(k) or 403(b)) must first rollover plan assets to an IRA to take advantage of this strategy.

Donor Profile

- Age 70 ½ or older
- Sufficient assets and income to maintain lifestyle without drawing RMDs

Qualified Charitable Distribution Example

Donor Scenario

- Bill turned 70 ½ this year and is required to take a distribution of $100,000 from his IRA. Bill has sufficient income from his consulting practice to maintain his lifestyle, so he decided that he would give these funds to his alma mater instead.
- Bill instructs his advisor to issue a $100,000 check from his IRA payable to his alma mater, which will qualify as his required distribution for the year.

Impact to Donor

- Bill reduces his taxable income by $100,000 and fulfills his charitable giving desires.
- Had Bill taken an IRA distribution and then donated cash, he would need to distribute $158,730 in order to net $100,000 to give to the school (assuming a 37% tax bracket).

Impact to Charity

- Bill's alma mater receives $100,000.
- Had Bill first taken the distribution into his taxable income, the charitable contribution may have only been $63,000 (assuming Bill is in the 37% tax bracket). The contribution could be reduced even further if Bill is subject to state income taxes.

Charitable Lead Trust

Overview

- A Charitable Lead Trust (CLT) is a type of split-interest charitable trust, in which the charity is the lead beneficiary and the noncharitable beneficiary (typically the donor's heirs) are the remainder beneficiaries.
- Trust makes distributions to charity for a set term. Distributions may be a fixed dollar amount (Charitable Lead Annuity Trust) or a fixed percentage of the FMV of the assets (Charitable Lead Unitrust).
- At the end of the term, the remaining trust assets are distributed to the noncharitable beneficiary free of federal gift tax.

Donor Benefits

- Satisfies charitable intent, while allowing asset to remain in the family
- May reduce federal gift/estate taxes

Donor Drawbacks

- Charitable payment required annually, regardless of income, so best to fund with an income-producing asset
- No charitable deduction if income is taxed to the trust, rather than the donor

Donor Profile

- Sufficient income outside of trust assets to maintain lifestyle
- Owns an asset with high future appreciation potential (i.e. business or real estate)
- Heirs are too young to take control of assets today or financially secure enough to defer inheritance

Charitable Lead Trust Example

Donor Scenario

- Eric and Kathryn own rental real estate valued at $1,000,000 that is expected appreciate significantly over time. They do not need the income from the property to maintain their current lifestyle. They would like to support their University Catholic Center during their lifetimes but ultimately want the real estate to pass to their children, who are too young to manage the property today.
- Eric and Kathryn establish a Charitable Lead Annuity Trust, and fund it with the $1,000,000 property. The trust pays a 6% annuity to the University Catholic Center for a period of 20 years. At the end of the 20 years, the trust property passes to their children.

Impact to Donor

- Assuming the 6% payout to charity and a 7520 rate of 2.40%, the value of the remainder interest to their children is $55,756. This is treated as a taxable gift but can be sheltered by their applicable credit amounts.
- Assuming the trust assets actually grow at 8%, the value of the property transferred to their children at the end of the 20 year term is $1,915,239, so the growth of $1,859,483 is transferred free of any gift or estate taxes (assuming they had a taxable estate).

Impact to Charity

- The University Catholic Center receives an annual annuity payment of $60,000 for a period of 20 years.

Charitable Remainder Trust

Overview

- A Charitable Remainder Trust (CRT) is a type of split-interest charitable trust, in which the noncharitable beneficiary (typically the donor) is the lead beneficiary and the charity is the remainder beneficiary.
- Trust makes distributions to the noncharitable beneficiary for either a set time period or for their lifetime. Distributions may be a fixed dollar amount (Charitable Remainder Annuity Trust) or a fixed percentage of the FMV of the assets (Charitable Remainder Unitrust).
- At the end of the term, the remaining trust assets are distributed to the charity.

Donor Benefits

- Provides continued income stream
- Enables deferral of capital gain on assets transferred to trust
- Charitable deduction received in year of contribution for the present value of the remainder interest

Donor Drawbacks

- If someone besides the donor is the income beneficiary, there may be gift tax consequences to the donor.
- Donor pays capital gains tax over time as income is received from trust.
- Not a recommended vehicle for donors wishing to contribute encumbered real estate or tangible personal property.

Donor Profile

- Needs income from trust assets to maintain lifestyle
- Owns a highly appreciated asset and has a desire to defer capital gain
- Appreciated asset is low-yield. May be sold inside trust to create a diversified portfolio to increase cash flow.

Charitable Remainder Trust Example

Donor Scenario

- John (age 70) purchased land 10 years ago for $250,000 that is now valued at $1,000,000. John is reluctant to sell the property and pay the capital gains taxes but needs to convert the land into an income-producing asset. John does not have any children and would like to leave his remaining assets to his alma mater.
- John establishes a Charitable Remainder Annuity Trust, and funds it with the $1,000,000 property. The trust sells the land and invests in a diversified portfolio. The trust pays John a 5% annuity for his lifetime, and the balance is paid to his alma mater.

Impact to Donor

- John defers capital gains taxes on the $750,000 gain in the property.
- John receives an annual annuity payment of $50,000 for the rest of his life.
- Assuming the trust assets grow at 6% and a 7520 rate of 2.60%, John receives a charitable deduction of $436,305.

Impact to Charity

- John's alma mater receives the remaining trust assets upon his death. Assuming a life expectancy of 84, at the end of the 14 years of payments to John, the charity would receive $1,210,150.

Donor-Advised Fund

Overview

- A Donor-Advised Fund (DAF) is a qualified public charity offered through many financial institutions and community foundations. A donor establishes a separate fund through the sponsoring organization and retains the right to make recommendations for distributions.
- Contributions to the DAF are tax-deductible immediately, even though they may not be distributed to individual charities until a later date.

Donor Benefits

- Ability to claim tax deduction in high income year and recommend charitable recipients in future years
- Lower minimum contributions, set-up costs, and administrative requirements than private foundations
- May reduce capital gains, gift, and/or estate taxes

Donor Drawbacks

- Contributions are irrevocable
- Recommendations are typically honored by sponsoring organization but are non-binding

Donor Profile

- High-income taxpayer, particularly in a year of unusually high income (i.e. sale of a business or immediately prior to retirement)
- Intent to make annual charitable gifts and/or gifts to various public charities
- Desire for simplicity and minimization of tax, legal, and administrative costs

Private Foundation

Overview

- A Private Foundation is a separate legal entity, organized either as a nonprofit corporation or as a trust, formed as a charitable organization but that is not a public charity. A non-operating foundation does not directly provide charitable services but instead makes grants to charities.
- Contributions to a private foundation are tax-deductible immediately, even though they may not be distributed to individual charities until a later date.

Donor Benefits

- Ability to claim tax deduction in high income year and make charitable contributions in future years
- May reduce capital gains, gift, and/or estate taxes
- Retains control over investments and distributions

Donor Drawbacks

- Substantial initial and ongoing tax and legal expenses
- Mandatory annual 5% payout
- Numerous IRS limitations and reporting requirements; severe penalties for violation

Donor Profile

- High net worth individuals who plan to make contributions large enough to substantiate the costs
- Desire to involve family members in pursuing long-term philanthropic objectives

Questions?

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