KNOWING A PLANNED GIVER WHEN YOU SEE ONE

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Presented by:

Jeff Lydenberg
Vice President
PG Calc
129 Mt. Auburn Street
Cambridge, MA 02138
617-497-4997
jeff@pgcalc.com
www.pgcalc.com

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Introduction

Including a non-profit in a donor's estate plans is unusual behavior. Very few of the living donors with whom a fundraiser comes in contact will make provisions for a planned gift to benefit charity. While not common, bequest and other planned gift donors account for billions of dollars each year in gifts to charity. Giving USA 2013 reported bequests totaling $27.73 billion in 2013. The IRS reports that about $4 billion a year from charitable remainder and lead trusts is distributed to charities each year.

Being able to recognize those few who are likely to engage in planned gift behavior is critical to the success of deferred giving programs. Knowing the planned giver when you see one is partly science and partly art. The lessons from science help us recognize those things that typically characterize the planned giver. The art of planned giving is knowing when the time is right to have the planned gift discussion.

I. Bequest Giving Behavior

a. Estate taxes and bequest giving

Bequests to charity from a donor's will or living trust is the largest single source of planned gift dollars. Of the $335.17 billion donated to charity in 2013, bequest giving accounted for about 8% of total giving that year. (Giving USA 2014) This amounted to $27.73 billion in 2013. Some of this data comes from estates reporting estate tax charitable deductions and some comes from estimates of the amounts from non-taxable estates. The source of much of this money comes from estates that aren't subject to Federal estate tax because the estate tax is applicable to so few Americans.

The Federal estate tax is sometimes cited as the reason donors make gifts to charity at their deaths. However, the Federal gift and estate tax structure has experienced significant changes since 2001. In 2000, estates valued at more than $675,000 were subject to estate tax rates of up to 55%. Beginning in 2001 the exemption amounts began to increase and the estate tax brackets began to decrease. The estate tax was actually eliminated in 2010, but returned in 2011 with a $5,000,000 exemption and 35% top estate tax bracket.

In January 2013 the American Taxpayer Relief Act (ATRA) was passed. This law indexed the federal estate tax exemption for inflation and increased the top estate tax rate to 40%. The federal estate tax exemption in 2014 is $5,340,000. ATRA also introduced portability of the estate tax exemption between married couples, which means that with no special estate planning a married couple can pass to their heirs twice the exemption amount free from federal estate taxes. That means that married couples with estates of less than $10,680,000 are not subject to federal estate tax at all. How has this decrease in the federal estate tax influenced bequest giving?

The Bank of America High Net Worth Philanthropy Study last published in 2012 reported that high net worth households would leave the same amount to charity if they received no estate tax deduction for charitable bequests. The percentage of households agreeing with this statement rose from 48 percent in 2009 to 58 percent in 2011. Across the years, between 18 percent and 26 percent of high net worth households reported that they would somewhat increase their estate gifts and between 12 percent and 17 percent would dramatically increase their estate gifts if the

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estate tax deduction were eliminated. Between 2005 and 2011, two to eight percent of high net worth households reported that they would somewhat decrease their estate gifts under this provision. Across the years, the lowest percentages of high net worth households indicated they would dramatically decrease their estate gifts (between one and two percent) if the estate tax deduction were eliminated. How have the reductions in estate tax rates and the increases in estate tax exemptions affected charitable bequests?

The impact of the changes in the estate tax scheme have reduced the number of estates that must file estate tax returns. Between 2001 and 2012 the number of taxable estates declined by 90%. (Giving USA 2014) The amount claimed for estate tax deductions for charitable bequests declined by 25.4% for the same period. (Giving USA 2014) Fewer estates filing estate tax returns and fewer reportable charitable deductions does not necessarily mean the Bank of America data was wrong. Giving USA reported that the amount of giving by bequest actually increased by 7.2 percent from 2012 to 2013. It appears that bequest giving is not strongly influenced by the Federal estate tax.

b. Charitable Bequest Trends

Dr. Russell James of Texas Tech University has become widely-acknowledged as the leading academic studying charitable giving behavior. His research is critical to testing the validity of long held beliefs often based on anecdotal evidence. Some of his findings confirm the popular wisdom, some of his work exposes the myths that planned giving development offices have taken as gospel.

His report *American Charitable Bequest Demographics (1992-2012)* analyzed data from the Census Department's Health and Retirement Study (HRS). The primary purpose of the study was to understand the behavior of older Americans. The study included questions relating to charitable bequest giving. It offered a rich source of information about what Americans are actually doing about charitable estate planning without being filtered through the lens of the gift planner.

The study found three critical factors affecting charitable gift planning. First, the bequest donor must have trust in the organization that will benefit from the bequest. Second, the presence or absence of heirs may be the single most important variable to help identify the bequest donor. Third, the greater the net worth, the more likely a person is to leave a charitable bequest.

The study showed that of those surveyed, only 5.7% had made provisions for charity in their will or trust. Keep in mind that the participants in the HRS survey were not screened for charitable affiliation or net worth. Therefore, one could conclude that a very small percentage of Americans have made provisions for charity in their long term plans. Is it safe to conclude then that 5.7% of an organization's supporters will have included that organization in their plans? In other words, if an organization has 30,000 donor records, will 5.7% or 1,710 of those donors have included the charity in their estate plans? Not necessarily.

The HRS study was of Americans age 50 or older. So does that mean 5.7% of the 30,000 donors age 50 or older have included the organization in their plans? Once again, not necessarily.

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The study went on to ask of those who make charitable gifts of $500 per year or more during life, what percentage have included charity in their estate plans. The percentage increased to 9.4% of those surveyed. The take away is that 9.4% of those 50 and over who make charitable gifts of $500 a year to charity are likely to make a bequest gift to charity, as well. It comes as no surprise that planned giving should focus on the oldest donors in an organization's data base.

The rest of what Dr. James' research found is something that veteran planned giving professionals have observed for years. Among those over 50 who make charitable gifts of $500 or more a year, the lack of offspring is the single most important variable that predicts charitable estate plans. 50% of those who make charitable gifts of $500 or more a year and have no children will include charity in their estate plans. That percentage drops to 17.1% when donors have children and dwindles to only 9.8% when the donors have grandchildren. Research from Australia indicates that those with wills and no children are 10 times more likely to include charity in their estate plans.

Does this mean those with children and grandchildren will not establish planned gifts? Absolutely not. Look at completed estate gifts at your own organization. Many of these gifts come from those with children and grandchildren. But it is likely that some of the largest gifts come from those with no children. There is good news to the importance of childlessness and bequest giving. Demographic trends show that the number of people choosing not to have children is increasing. The number of respondents to the HRS survey who did not have children increased by 22.1% from 1996 to 2006.

II. Gift Annuity and Charitable Remainder Trust Donor Behavior

Those experienced in working with gift annuities and charitable remainder trusts know that prospects for life income gifts tend to be more transactional than donors making gifts through their estates. Part of this transactional approach follows naturally from experiences of these donors in their professional and personal investment activities. That being said, the life income gift is not and should not be presented as comparable to a commercial investment. These are gifts, not investments.

Non-profits need to meet their donors where they live. That means that the language of contracts, investments, and the marketplace are familiar to those with the means to make substantial charitable contributions. The challenge is to bridge the gap between the transaction and the relationship with your organization.

Life income gift donors share a transactional orientation to their philanthropy, but the various gift vehicles have features that make them appealing to a diverse group of donors. Gift annuity donors are typically your oldest life income donors. The average age at first annuity reported in the 2013 ACGA survey was 79, the majority of those annuitants are women, and most were single. Gift annuitants are cautious financial decision makers, may have limited investment experience, and are concerned about outliving their resources.

Charitable remainder trust donors look quite different from gift annuity donors. Donors who create these trusts are much more comfortable with financial risk and are usually experienced investors. Their ages can vary widely. It is not uncommon for charitable remainder trusts to

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benefit multiple organizations while gift annuities may only benefit the charity that issues the annuity.

Tag lines like "Make a gift and help yourself" can help hook prospects who either can't or won't make outright lifetime prospects. Once the prospect is interested, it's time to move away from the language of the marketplace. The act of charitable giving, whether during life or at death, is a social act. That means the making of a gift to charity is satisfying to the donor, but in a larger sense, the giver receives the satisfaction of being part of the organization almost like being part of an artificial family.

One of the ways to bridge the gap between the transaction/marketplace communications to the relationship/family language is to avoid technical talk. Many planned giving professionals come from the law, accounting or finance. The tendency is to talk about the various vehicles in a way that is as accurate as possible. Research suggests using softer, less formal language can engage the life income donor more effectively. (James 2013)

Simply substituting layman's language for technically accurate terms can increase interest in making a gift. Describing a gift annuity as "Make a gift and receive payments for life" is much more positively received than "Enter into a contract, transfer property to the charity, and receive a guaranteed lifetime income." The benefits of establishing the annuity are still described in the less formal language. Instead of technical talk of "contracts" and "property" the donor is asked to "make a gift" and receive payments.

III. How to "know" the Planned Giver

a. Broaden the Database

Planned giving fundraisers have used certain methodologies for years to identify their most likely planned giving suspects. These techniques usually involve looking first at those who have already given to your organization. The current research certainly suggests that philanthropic decisions are driven in large measure by those with a connection to your organization. That "connection" is most often defined as giving behavior. Focusing exclusively on those who have already given is a good place to start if resources are limited. Donors of assets other than cash also are more likely to make planned gifts.

The connections to a particular charity besides donations will vary depending on the mission of the organization. Universities have alumni but they also have members of their community who value the way the university enriches the quality of life where they live. Hospitals have grateful patients, volunteers, and those who value the service the hospital provides to their community. The arts have those who subscribe to a museum, a performance series or act as volunteers. These are just a few examples, but many of these people may have never made a gift and therefore are not captured in the charity's database. Yet each of them may consider themselves part of the "family" of supporters of their particular cause. Each of them also might consider including their charity in their long term plans.

If your database is limited to donors, meaning only those who have made gifts, a large audience of potential planned givers is missing. Develop a system to upload membership, volunteer,

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subscriber, patient and event attendees to the database. Code these records so that their connection to the organization is clear. Consider direct mail and social media campaigns targeting these "family" members to convert them to outright gift donors. Likewise, include this population in planned giving awareness marketing. The majority of charitable bequests are not known prior to being realized. While most bequest donors have made some, albeit frequently small lifetime gifts, a certain percentage will have never been in the "donor" database. A broad outreach to the community of those who support your mission can plant the seed that leads to the surprise planned gift.

b. Basic Field Identification

Those who are passionate about bird watching and bird identification look for what are known as "field marks." The basic field marks to a birder are size and shape, color pattern, behavior and habitat. Most birds can be quickly identified after noting its field marks. That's because these indicators quickly narrow down the possible species to a relatively few choices.

Likewise, the planned giving donor has certain field marks permitting quick assessment of the donor's interest in deferred giving and the vehicles most appropriate for each donor. The planned giving professional's field marks are: 1. Age; 2. Giving history or other attachment to the charity; 3. Presence or absence of heirs; 4. Educational level; 5. Life events. Armed with just these five pieces of information supporters can be screened for who is a promising planned gift prospect and a short list of the vehicles likely to be of interest can be compiled for each one who is.

i. Age

Planned giving donors are typically the oldest group of supporters to any organization. There is no single age at which a planned giving donor can be identified. However, research suggests that the age at which charity is <u>first</u> added to an estate plan is late 40's to late 50's. Younger potential planned givers typically receive the least attention, but some of the factors below can move them up the list.

The older the donor, the more risk averse she is likely to be and the greater the concern she is likely to have about outliving resources. The younger donor is typically more risk tolerant but has greater concerns about income and keeping pace with inflation. All ages are concerned about health care costs and long term care.

ii. Giving and/or involvement

Planned giving veterans almost always have stories of significant bequests from donors with extremely small lifetime giving histories or perhaps no giving history whatsoever. These stories are like the bad penny. Because these cases are unusual, they capture your attention. Research suggests that the number one indicator of the likelihood of a planned gift is a long giving history. (<u>Identification, Death and Bequest Giving</u>, Sargeant, Sheng (2008). If the frequent giver also makes larger than average gifts, usually annually, the likelihood of a planned gift goes up. A long history of giving at higher than average amounts marks these donors as more likely to include charity in their estate plans. (James 2008)

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iii. Presence or absence of heirs

Since giving is a social act, the inclusion of a charity in one's estate plans raises the charity to the status of a surrogate family. Think of your organization as one of your planned gift donor's children. If a donor has human children, the challenge of elevating your charity to the status of an alternate child is daunting.

Do donors with children still include charity in their estate plans? Certainly. To achieve that status, the charity must have a close emotional connection to the donor, the kind of connection is driven by how closely the donor associates their success, health, values, or religious faith with the charity.

As with all families, the more children, the smaller the fraction of the estate to be passed to each child. A donor with children will have to make hard choices about whether, how much, when and how to make the gift to charity, their stand-in child.

Experience tells us that some donors with children still include charity in their estate plans. We've already established that research shows that donors without children are more likely to include charity in their estate plans. Take a donor with children who has a long, generous giving history, volunteer service, and a deep connection to the charity. Compare this donor to a person with no children who has never made a gift to the charity, never volunteered, and has only a modest connection to the charity. The person with no children and a tenuous charitable engagement is far more likely to leave a bequest to charity than the engaged donor with children.

The implications of this research are far reaching. Every donor database has a way to record information about the donor's children, probably even their grandchildren as well. But few if any databases make any provision for recording those with no children. If you are not recording this data currently, ask your database manager to help implement a system that allows recording donors with no heirs. The next time you are prioritizing who to see first, call on the childless first.

The importance of the lack of heirs bodes well for the future of planned giving. Demographic trends point to an increasing number of individuals choosing not to have children. . (Childlessness up among All Women; Down among Women with Advanced Degrees http://www.pewsocialtrends.org/) The pool of those highly likely to include charity in their estate plans is growing.

iv. Educational Level

There is a strong correlation between educational achievement and the likelihood to include charity in one's estate plans. . (The growth of charitable estate planning among Americans nearing retirement, James, Lauderdale, and Robb 2009) The likelihood of a bequest increases if a donor has an undergraduate degree versus only a high school diploma. The likelihood increases even more if the donor has a graduate degree.

The importance of educational accomplishment to estate giving has similar implications as knowing a prospect has no children. When prioritizing prospects for qualification and cultivation, initials such as M.D., J.D., PhD., MS or even BA should push these prospects up the list.

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v. Life Events

Planned gifts are frequently influenced by events in a donor's life. Events that disrupt the donor's routine or force focusing on unexpected or upsetting life changes can trigger the planned gift discussion. These disruptions need not be negative things. The birth of a child or grandchild, the sale of a business, a promotion, or retirement can trigger reexamination of estate plans and how charity fits in.

Negative events like the death of a spouse, a diagnosis of cancer or a heart condition, divorce or losing a job can also force the donor to contemplate her mortality and consider her charitable priorities.

Watch for life events that can signal an opportunity to discuss including charity in a donor's plans. Keep in mind that some of these disruptive episodes in a donor's life can cut both ways. We've already seen that the birth of a child or grandchild can materially reduce the likelihood of a donor making a charitable bequest. Cash events such as a promotion, receiving a large bequest, or selling a business will increase the likelihood of a donor making a charitable bequest.

The challenge of using life events as a field mark of a planned giver is that life events are not easily known by the fundraiser. Not all of a charity's supporters will have a life changing diagnosis at the same time. It's not possible to predict who in the database will experience a cash infusion. Therefore the importance of life events on donor decision making is managed on the retail level (one on one between donor and fundraiser) rather than on the wholesale level (mass communication through direct mail or social media.)

vi. What about capacity?

One of the most common requests that fundraisers make of prospect research is, how much is this prospect worth? A donor's capacity is just like why Willie Sutton said he robbed banks: that's where the money is. If capacity were all that matters, fundraising would consist of just talking to Warren Buffet, Bill Gates and the Walton family. Capacity is not necessarily one of the field marks that distinguishes the planned giver.

A person must have some assets at their death to make a bequest. That much is obvious. The mere fact that a person has significant assets does not mean they are necessarily interested in a planned gift. If the field marks discussed above are present, however, capacity becomes important.

We've already established that those who see their wealth increase suddenly are more likely to consider a planned gift after such an event. The wealth in those cases is associated with an experience that changed the donor's life circumstance. The existence of wealth by itself, does not increase a donor's propensity to make a planned gift.

While wealth standing alone is not a field mark of a planned giver, it provides a useful framework for prioritizing which prospects to contact first. Given the presence of the five field marks mentioned above, those with the greatest capacity deserve priority attention.

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IV. Talking to prospects and motivating them to action

a. Starting the conversation

Planned givers share certain field marks, characteristics they have in common, but once identified, a prospect must be matched with the planned gift vehicle appropriate for the prospect. In order to do this you need to build trust with the donor, encourage them to share their philanthropic and financial goals, and learn how planned giving can help them.

It is the tendency of planned giving professionals, particularly those with legal or financial backgrounds, to immediately engage the planned giving prospect in a discussion to determine the vehicle most appropriate for the prospect. As we've seen, the technical aspects of the gift discussion are the last part of the conversation. These gifts are driven by emotions that engage the donor's passion.

The place to start is uncovering the source of the passion that will drive the gift decision. An effective way to reveal a donor's motivation is to let them tell their story. Certainly no later than the qualification phase of engaging a prospect, ask them why they support or otherwise engage in your organization's mission. Ask open ended questions, sit back, and let them tell their story.

Consider opening with questions like:

- What inspired you to make your first gift to our charity?
- How did you become involved with us?
- Of all the things our organization does, which ones do you consider most important? Why?
- There are other organizations with missions similar to ours. Why did you choose to become involved with us?

It is likely someone who has already provided financial support for your organization will feel particularly engaged with an aspect of your mission. Food bank donors may be passionate about child nourishment, but less concerned with job skills training the charity may offer. An academic medical center may conduct research in many areas of concern, but the donor is passionate about early detection of breast cancer.

The stronger the engagement with the donor's passion, the more likely the donor is to consider a planned gift. The challenge for all fundraisers, not just planned giving specialists, is the pressure to raise unrestricted dollars. The problem of encouraging unrestricted giving is particularly acute in the case of planned gifts. If including charity in long term plans raises that charity to the status of family, a broad request for general support is hardly likely to tap into the emotions that drive planned gifts. The donor must feel that support for a charity will fulfill an important need in their life. Only then will the donor be motivated to take action to include charity in her plans.

b. Overcoming inertia

Engaging in the process of planning one's estate forces a person to confront an array of unpleasant topics. Estate planning requires contemplating the things we don't want to focus on. The primary issue is confronting one's own mortality. The process can also shine a light on dysfunctional family issues, favoritism for certain family members, trust in one's family, friends and advisors, not to mention that it can be expensive.

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The emotional and financial barriers are probably why so many people die without a will or estate planning of any kind. It's easier to avoid the topic altogether. Therefore, inertia resulting from avoidance is a major obstacle to getting a donor to take action even if she is passionate about your mission.

One way to overcome inertia is to offer easy ways to make planned gifts. Beneficiary designations on retirement accounts, life insurance, commercial annuities, and other financial accounts is an easier and less stressful way to encourage the potential planned giver to take action. A relatively simple beneficiary designation form is all that is needed to leave a gift to charity. While every planned giver should be encouraged to consult a professional advisor, even when changing a beneficiary designation, the reality is that most donors won't see advice. The cost and the time required to engage the assistance of an attorney or accountant is one of the barriers to overcoming donor inertia. Even though the donor should consult an advisor before making changes to beneficiary designations, many donors will make changes without seeking advice.

Another way to overcome donor inertia, particularly with beneficiary designations, is to suggest that the donor consider making charity a beneficiary of only a portion of the financial account. Acknowledging that the donor has multiple personal and philanthropic priorities increases the fundraisers credibility as being genuinely focused on the donor's goals.

Some charities have had success with creating a sense of urgency to encourage donors (and fundraisers) to focus on planned giving. A national disease charity set a goal to acquire 100 new legacy society commitments in a seven month period. Every commitment to include the charity in one's estate plan would result in an immediate matching gift of $1,000 to support current disease research. The current gifts were provided by planned gift donors who were passionate about encouraging others to consider including the charity in their estate plans. The challenge generated 128 new notifications of estate commitments. This represented an 83 percent increase in commitments over the prior fiscal year.

The challenge created an urgency on the part of planned gift donors to overcome the obstacles holding them back from engaging in the charitable planning. Some would argue that many of these gifts may have already been in place. The challenge merely motivated the donor to disclose planning that was completed before the challenge happened. Certainly that may have been the case for some of these newly identified commitments. There are likely others for whom the challenge was the tipping point to get them to finally take action. Why does it make a difference if these are mostly notifications of planning already in place? The charity now has 128 new planned givers to engage in its mission and steward so the charity stays in the estate plan.

V. Knowing a planned giver from what he or she owns

Knowing what kind of assets a donor holds can help determine what planned gift vehicles are appropriate for her. Virtually all assets can be used to fund planned gifts. However, some assets lend themselves better than others to planned giving purposes.

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Remember that your priority is to get the donor excited about philanthropic opportunities, not to be their financial planner or attorney. Gain their trust; don't feel like you need to know all the answers.

Listed below is a description of assets a donor is likely to hold and the planned gift vehicle that is most appropriate for that asset. If the donor shares that they own these types of assets, you can match up that asset with the most appropriate planned gift vehicle.

A. Character of Assets:

1. **Illiquid assets**; these are assets that are not readily convertible to cash. Examples include real estate, collectibles, and closely held business assets. The vehicle of choice for illiquid assets is the flip unitrust. The net income provision of the flip unitrust allows the trustee time to sell the asset. After the sale, the trust can flip to a regular unitrust and begin making payments. Gift annuities also can be funded with illiquid assets, but the need to make fixed payments can present challenges for the charitable organization.
2. **Appreciated assets**; assets that have appreciated in value since the donor purchased them will generate capital gain income on sale. All planned and outright gifts of appreciated assets to charity offer opportunities to avoid, defer, or reduce capital gain income. The best way to avoid capital gain is to make an outright gift to charity.
3. **Non-income producing assets;** assets that may have experienced significant increase in value may not produce corresponding income. Growth stocks may have appreciated greatly but may pay little or no dividend. Non-commercial real estate may be extremely valuable, but since it is not rented produces no income. Life income gifts funded with non-income producing assets are the best way to convert a stagnant asset into a source of income.
4. **"Income in respect of a decedent" ("IRD") assets**; IRAs, savings bonds, and commercial annuities are assets upon which the donor has never paid income tax. At death, these assets are included in the donor's estate for estate tax purposes and also in the donor's income on the final income tax return. The tax burden on these assets can run as high as 70%, leaving little for the donor's heirs. IRD assets are ideal to leave to charity at the donor's death. The tax burden is relieved through the estate tax deduction and the avoidance of income tax.

B. Types of Assets

1. **Real Estate**
    i. **Personal Residence:** For many donors the most valuable asset in their estate is their personal residence. The residence represents a tremendous source of wealth for making charitable gifts. If the donor wants to continue to live in the residence, the retained life estate is the only realistic option. This gift plan allows donors to make a gift of the remainder interest in their home. They continue to live there the rest of their lives, and the home passes to charity upon their death.

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ii. **Vacation home:** Vacation homes can be an attractive funding source for planned gifts. If the donor wants to continue to use the vacation home, the retained life estate is the best option. However, the property could fund a flip unitrust to provide income to the donor.

iii. **Rental/Commercial real estate:** Donors may own apartment buildings or other commercial real estate that is providing an income stream. Many older people are tired of the work required to maintain rental real estate. These properties can fund a flip unitrust and provide lifetime income to the donor. The trust would continue to pay the donor the same net rental income he is already receiving. After selling the property, the trust could flip to a regular unitrust paying the unitrust amount for the donor's life.

2. **Retirement Plans:** Qualified retirement plans are an example of IRD assets mentioned earlier. These plans are funded with pre-tax dollars and grow tax free inside the retirement plan.

   i. Generally speaking, retirement plan assets are a poor choice to use to make current gifts to charity. These assets have never been subject to tax so withdrawals are taxed as ordinary income. If used to fund a planned gift, the charitable income tax deduction will be insufficient to offset the taxes due on the withdrawal from the plan. Even if used to make an outright gift, high income individuals may find that their deduction does not offset the taxes due on the withdrawal from the plan.

   ii. These assets are ideal to transfer to charity at death, however, because of the heavy tax burden if paid to non-charitable beneficiaries. The controlling document for disposition of these assets at death is not the donor's will or living trust. It is the beneficiary designation card that the donor files with the retirement plan administrator that determines who receives the donor's retirement plan. Retirement plan assets are an easy asset to give to charity and because of the tax burden on retirement assets, they can be given to charity as estate gifts with very little cost to the non-charitable beneficiaries of the estate.

3. **Securities**

   i. **Publicly traded**
   These securities are the most flexible appreciated asset. The donor can freely transfer publicly traded securities to fund any type of planned gift. Valuation is easy and the securities can be easily converted into cash.

   ii. **Closely held**
   These are securities that are not traded on a public exchange. One or a small group of persons or families may hold all of the shares of these types of business. Closely held securities are a type of illiquid asset

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that is not easily converted to cash. Therefore, the flip unitrust is the best vehicle for this type of asset.

4. **Closely held business assets** Many individuals are unable to make major charitable gifts with cash or publicly-traded securities, but some could do so with shares in a closely held company or with other business interests. Indeed, family business owners and other entrepreneurs have often been among the largest contributors to capital campaigns.

   i. **Corporations**

      1. C Corporations
         A C corporation is a business form that insulates its shareholders from liabilities incurred by the corporation. C corporation shareholders are subject to taxation both at the corporate and shareholder level. A charity, a charitable remainder trust, and a charitable lead trust can all own C stock in a closely held corporation. These shares also can be given in exchange for a charitable gift annuity. Converting closely held stock to cash is one of the biggest challenges of this type of asset for a charity.

      2. S Corporations
         An S corporation is exempt from federal income tax. Instead, the S corporation's shareholders include their share of the corporation's income on their personal income tax returns. A charity can be an eligible S corporation shareholder, but charitable remainder trusts cannot own S Corporation stock. If a charity holds S corporation stock, any dividends, interest, and rents on the stock are taxable to the charity, and even gain on the sale of the S Corporation stock is taxable.

   ii. **Partnerships**
       Some partnership interests generate positive cash flow, have good appreciation potential, and may be marketable. They can be valuable gifts to charity or to fund planned gifts. Others are virtually worthless and may saddle the charity with liabilities. Charities should carefully undertake due diligence before accepting partnership interests. Whether these assets are appropriate for funding a planned gift will vary depending on the facts of the particular case.

5. **Life Insurance**

   i. Transfer Ownership of Paid-Up Policy A gift of a paid-up policy is equivalent to an outright gift of cash, for the charity can, if it chooses, immediately surrender the policy for cash.

   ii. Transfer Ownership of an Existing Policy on Which Premiums are Still Owing If the policy is whole-life and has been in force for two or more years, it will likely have some cash value that is accessible to the charity. Assuming the donor continues to pay the premiums, the cash

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value will increase each year, and the charity will eventually collect the death benefit if it retains the policy.

iii. Purchase a New Policy, Initially Naming the Charity as Owner
Although the policy has no initial cash value, whole life or universal life policies will accumulate cash value, and all policies will pay a death benefit if the insured dies while the policy is in force.

iv. Name the Charity as Primary Beneficiary of a Policy
Provided the owner keeps the policy in force and does not change the beneficiary, the charity will eventually receive the death benefit. Beneficiary designations, like bequests, can be changed. The charity will receive nothing if the owner substitutes another beneficiary.

VI. Case Studies of the most Common Planned Gifts

As you can see from the material covered so far, the universe of planned gift types is quite large. However, in practice certain planned gifts occur more frequently. Bequests are typically responsible for the largest amount of deferred gift revenue. This is understandable since the end of life gift will be the largest for most people.

1. The Bequest Donor

a. A bequest donor case study

This is a true story. It didn’t happen to any of my clients, but a friend in the planned giving industry related the story. A Midwestern children’s hospital received notification that they were the beneficiary of an estate gift that will be in the low six figures once probate is completed. Development staff looked up the decedent’s record and learned that she lived in California but had been making small ($50 to $100) annual gifts since the 1990’s. The donor might have made gifts prior to that, but the development office did a database conversion and records prior to that transition were unreliable.

No development officer had ever visited the donor. There was no notation in the database that she had been a patient. Despite the geographical disconnect, database analytics rated her highly as a planned giving prospect and she was included in the planned giving department’s direct mail program. Because of her regular annual giving, she also was solicited by mail annually and received hospital publications and marketing. There was no record of requests for information or any contact other than regular informational mailings and the annual fund solicitation.

The director of planned giving was curious why a person with no discernable connection to the hospital would have such a long history of annual giving, let alone why did she leave such a large bequest to the hospital. The director of planned giving inquired of the donor’s executor if she knew why the gift had happened.

The executor was a longtime friend of the donor. They had been friends since school. The donor was born in New York, but when she was a young girl her father took a job in California. The family traveled to California by car. When they got to this Midwestern city, their little girl was very sick. They were panicked. They inquired as to the nearest hospital and were directed

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to the emergency room of the children's hospital. Her parents credited the hospital with saving her life. The donor had only the vaguest memory of the event. She was very young at the time. But it became a part of family lore that her life had been saved at that far away hospital.

The donor grew up, started a career, married, but never had children. She had been widowed for some time at the time of her death. Her gratitude for that treatment so many years ago prompted her gift.

b. Lessons learned

Stories like this donor's frequently prompt comments like "you just never know" and "many planned gifts are over the transom, no one did anything." In this case, there were institutional barriers to targeting this donor before she died. Patient data was not being captured in the development database at the time she was treated. The lesson: capture data indicative of how a donor is connected to your charity. Membership histories, baptism records, alumni data obviously. Event attendance and volunteering, if correlated with this donor's giving history, would have raised her visibility. Transitions to new donor databases often leave in the dustbin giving histories that are pure gold to the planned giving department. If it is possible to resurrect these old records, get it done. Geography was another barrier. It's hard to make the case to visit a $100 annual gift donor 2,000 miles away.

Despite the barriers, the gift got done. Donor analytics looked at factors including age and giving history and targeted her for planned giving mailings. The materials from both annual giving and planned giving showcased how the hospital continues to care for children when they need it most. The planned giving materials suggested ways to include the hospital in the donor's plan. She made use of those suggestions to give full expression to her gratitude.

2. The Gift Annuity Donor

a. A gift annuity case study

Mrs. Sylvester, age 75, has been a long time donor to her alma mater. Her annual gifts are modest but regular as clock work. She attends her alumni events regularly and lives near the campus. Ms. Sylvester's husband died recently. Her income is from Social Security and a small pension. Her husband left her his IRA, which was rolled over and from which she takes the minimum required distribution each year. She has a modest investment portfolio, but because she is worried about outliving her resources, her investments are primarily Government Treasury Securities and CDs. A 10-year Treasury Note is currently yielding 2.59%. The best she can find on a 5-year Certificate of Deposit is 2.3%.
Because she is close to campus and is closely involved in activities at the college, she gets regular visits from the planned giving office. Mrs. Sylvester is a member of the legacy society by virtue of an unspecified bequest intention.

The planned giving officer assigned to Mrs. Sylvester is getting pressure from her boss to get something irrevocable or better yet, current dollars from her (and quit wasting time stewarding a gift that may never come in.)

The planned giving officer finally works up the courage to ask Mrs. Sylvester to consider a $10,000 gift to partner with the College's new Center for Peace and Justice. Mrs. Sylvester blanches at the amount. She couldn't possibly afford to make such a gift. The planned giving

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officer goes to plan B. Would Mrs. Sylvester consider a gift to the College that secures her future as well? Mrs. Sylvester cautiously agrees to look at a proposal.

Unknown to the College, Mrs. Sylvester has a $50,000 CD that is coming due in a few months. She's learned that the best she can do is a 2.3% rate on a five year CD. That means that before tax she would receive $1,150. Her income is low enough that she is not subject to the 3.8% tax on net investment income. But her combined federal and state income tax bracket is 29.6%. That means she will only have $811 left after paying $339 of tax on her CD income.

The planned giving officer presents Mrs. Sylvester with a proposal for a gift annuity funded with $50,000 cash. She is entitled to a 5.8% annuity rate based on her age. That is $2,900 before tax and a substantial portion of that payment is tax-free. Assuming the same 29.5% tax rate as above, she would have $2,698 of after-tax income from the gift annuity. What's more, she would have a substantial charitable deduction that would save her income taxes in the year of the gift. Despite the tax and payment benefits, Mrs. Sylvester balks at the gift annuity proposal.

b. Lessons learned

The first lesson from this case is that the fundraiser has to put herself in the mind of her donor. The recent recession invoked memories Mrs. Sylvester has of stories of the Great Depression her parents and grandparents told. The talk shows and news programs she hears are filled with warnings of a crushing federal deficit and the possibility of runaway inflation.

The planned giving officer tries to allay her fears by noting that the Dow is at all-time highs, 3 million new jobs have been created since 2008, and interest rates and inflation are at all-time lows. Mrs. Sylvester is unmoved. Ultimately, if she needs to get her $50,000 back from her CD, she may pay a small penalty but she has access to her principal. If she does a gift annuity, she has no access to principal. All she has is an income stream.

3. The Charitable Remainder Trust Donor

a. A CRT Case Study

Michael and Elaine Sullivan, ages 76 and 74 met as undergraduates at an Ivy League school. Michael received his MD from the same school and Elaine got her JD. They both had long successful careers. Because of their busy careers, they had only one child. They credit much of their success to the educations they received. Despite that, the couple are intermittent annual fund donors to their alma mater. Because of Dr. and Mrs. Sullivan's success, they have been solicited throughout the years for capital and endowment campaigns. The Sullivan's have supported these campaigns through the years with gifts totaling $25,000.

Dr. Sullivan is solicited for his class gift for his 50th reunion for a gift of $250,000. The couple balk at the gift amount. They are grateful for the education and invaluable networking their college has provided, but the gift amount seems awfully high.

The major gift officer assigned to Dr. Sullivan's reunion class feels like she has hit a brick wall. The Sullivan's have offered to make a gift of $150,000. While generous, the gift officer is trying to get them to commit at the $250,000 level and asks her planned giving colleague for help.

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The planned giving officer reviews the research and estimates the Sullivan's are probably worth around $5,000,000. They can probably afford a $250,000 gift. There is also information that the couple enjoys managing their investment portfolio and probably owns a fair amount of highly appreciated stock.

The Sullivans are presented with a proposal for a gift of $250,000 to a 5% charitable remainder unitrust. They will be entitled to an income tax charitable deduction of $122,835 in the year of the gift. In the first year that the trust is in existence, it will distribute $12,500 in payments. Assuming a modest investment return of 6% a year on the trusts principal, their income will increase to $13,671 in the tenth year of the trust. The college is projected to receive nearly $300,000 if the trust terminates 16 years following its creation, which is the joint life expectancy of the Sullivans.

b. Lessons Learned

The Sullivans enthusiastically agree to fund the charitable remainder unitrust. They decide to establish the trust with the private wealth manager at their bank. The Sullivans will act as initial trustee; the bank will take over trusteeship if the Sullivan's ever choose to resign as trustee. The appeal to the donors in this case is two-fold. Being able to manage the investments in the trust is appealing to this couple. Plus, receiving a financial benefit from making the gift is attractive.

But this gift is not without its problems. The class agent for the reunion is concerned about issues of equity with classmates who make outright gifts. The Sullivan's agree to make the designation of the beneficiary to the college irrevocable, but the present value of the principal of the trust still is not equivalent to a cash gift. The projected $300,000 remainder is based on pure speculation that the trust will appreciate in value. One solution is to have the Sullivan's add a provision to their will that will provide an additional gift if the remainder in the CRT does not equal an amount agreed upon with the college to make the gift equivalent to those making outright gifts during the reunion year.

The idea of self-trusteeing a charitable trust is appealing to some donors. The donors may be successful and experienced investors and feel they can expertly make investment decisions for the trust. It is important to note that investing for one's own account is not the same as acting as a fiduciary where the interests of the trust are split between the beneficiaries and charitable remainderman. The good news in this case is that the bank will manage the accounting and tax preparation for the trust. Few donors want to take on this additional burden. Their private wealth advisor can also connect them with resources to help make investment decisions in a situation where there are competing interests. Finally, if the trust management is too burdensome, the Sullivan's can resign as trustee and the bank will take over.

VII. CONCLUDING COMMENTS

We have discussed the demographics and behaviors that drive deferred giving behavior. We've learned how to know the planned giver by their field marks. Based on their demographics, assets and behavior, we can narrow the potential gift vehicles to those most likely to appeal to a particular planned giving prospect. Finally we looked at the most common planned gifts, the things that can be controlled, the things that can't and the lessons learned from those situations. Apply these techniques and planned givers will start to appear on your radar and your efforts can be focused where they are most likely to be successful.

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APPENDIX 1

I. MATCHING THE PLANNED GIVER WITH THE RIGHT VEHICLE

a. BEQUESTS, LIVING TRUSTS AND BENEFICIARY DESIGNATIONS

i. The bequest landscape

Planned giving is associated with large well-established charities typically in existence for 50 years or more. But every non-profit has a planned giving program, although they might not know it. Anyone could make a charity the beneficiary of their estate plans. The charity might not know about it until after the donor dies. In fact, even in robust planned giving programs, only about 30% of bequests are known in advance of the donor's death. While every charity conceivably could benefit from an estate gift, for the reasons described above, it is unlikely that small organizations without a track record of success will receive bequests.

Giving USA has reported that in 2013, $22.73 billion of the $335.17 billion donated to charity was in the form of a bequest. (It is interesting to note as well that total individual gifts of $240.6 billion, when combined with bequest giving, represented over 80% of all giving. Foundation and corporate giving accounted for only 20% of total giving.)

The $22.73 billion in bequests came primarily from wills and living trusts that directed the donor's assets to the causes they hold dear. A small percentage of these gifts are likely attributable to beneficiary designations, but there is no data to indicate the exact composition of these gifts.

ii. The appeal of the bequest

Bequests are appealing because of the absolute flexibility that these gifts offer the donor. The donor doesn't know when they are going to die and how much they will be worth when they die. The amount of the bequest can be for a percentage of the donor's estate. This allows for adjustment of the charitable gift depending on the value of the donor's assets at death.

Bequests can be contingent on events that influence whether, how much, and when a donor wants to make a bequest. A bequest could lapse if the donor's spouse outlives the donor. A bequest can be contingent on a certain amount of assets being left in the donor's estate before the bequest is made.

Best of all, from the donor's perspective, the bequest is revocable. The right to revoke allows the donor to increase or decrease the charitable bequest or remove it altogether. While revocability may be a major concern of your manager, once a charity is in the will, it is rare for a donor to remove a charity. Also, the earlier a charity is in the will, the larger the charity's share is likely to be at death.

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b. LIFE INCOME VEHICLES

There are 3 broad categories of life income arrangements, charitable gift annuities, charitable remainder trusts, and pooled income funds. Each of these vehicles has characteristics that make it attractive depending on the donor's age, risk tolerance and income needs.

1. Charitable gift annuities

A gift annuity is a contract under which a charity, in return for a transfer of cash or other property, agrees to pay a fixed sum of money for a period measured by one or two lives. A person who receives payments is called an "annuitant" or "beneficiary." The contributed property becomes part of the charity's assets, and the payments are a general obligation of the charity. The annuity is backed by all of the charity's assets, not just by the property contributed.

The charity may spend a portion of the contribution immediately, provided it retains sufficient reserves to satisfy the requirements of applicable states in which gift annuities are regulated. Most charities, however, keep the entire contribution (increased by earnings and decreased by annuity payments and expenses) segregated in some way until the sole or surviving annuitant dies. The remaining portion of the contribution is called the "residuum."

Uniform gift annuity rates are published by the American Council on Gift Annuities (ACGA.) The older the annuitant, the higher is the annuity rate. The rates effective as of the date of this webinar, adopted by the ACGA on January 1, 2012, assume the following:

2. The Council's long-standing residuum target of 50%, with an additional requirement that the present value of the residuum be at least 20% of the gift amount;
3. The results of a recent study on charitable gift annuitant mortality conducted by the ACGA's actuarial consultants, the Hay Group; and
4. An investment return assumption of 4.25% on a model portfolio and a 1% expense assumption, for a net investment return of 3.25%.

2. Charitable remainder trusts

Charitable remainder trusts are distinct from gift annuities in that a remainder trust is a legal entity separate and independent from the donor and the charity. The trust holds and invests the contributed assets, makes the specified payments and only on the conclusion of the trust term may the remaining trust assets be applied for charitable purposes.

All charitable remainder trusts share certain characteristics:

- The trust donor is entitled to a charitable income tax deduction for the present value of the charitable remainder.
- The trust must be irrevocable and create a valid trust under local law.

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- The trust must make payments at least annually to at least one non-charitable beneficiary.
- The trust may make payments for the life of the designated beneficiaries or a term not to exceed 20 years.
- The trust annual payment may be no less than 5% and no more than 50%.
- The trust's income tax charitable deduction must be equal to or greater than 10% of the trust funding amount.
- The remainder trust charitable income tax deduction must be equal to or greater than 10% of the donated principal.
- The payout to the trust beneficiary may be in the form of an annuity or unitrust amount.

i. Charitable Remainder Annuity Trusts

A charitable remainder annuity trust must make a fixed payment of a specified dollar amount to the designated income beneficiary. The fixed payment must be no less than 5% and no more than 50% of the initial value of the assets transferred to the trust. The annuity trust's annual payment is based on the initial funding amount of the trust and remains constant throughout its term. Subsequent additions to the annuity trust are prohibited. It is not possible to defer payments from an annuity trust.

Charitable remainder annuity trusts are subject to the 5% probability test is described in Revenue Ruling 77-374 that requires all remainder annuity trusts that will make payments for one or more lifetimes to have less than a 5% chance of principal exhaustion. If a CRAT fails the 5% test, no deduction is allowed. It is also questionable whether the trust will qualify as a charitable remainder trust. In 2011, 15,862 charitable remainder annuity trust tax returns were filed with the IRS.

ii. Charitable Remainder Unitrusts

A charitable remainder unitrust must make payments of a fixed percentage of the trust value as revalued annually to the designated income beneficiary. The payment each year is based on the then current value of the assets held by the trust. The unitrust's annual payment fluctuates from year to year based on the value of the trust each year. Subsequent additions to a unitrust trust are permitted.

If the unitrust's value goes up from one year to the next, its payout increases proportionately. Likewise, if the unitrust's value goes down, the amount it distributes also goes down. For this reason, it may be advantageous to choose a relatively low payout percentage so that the unitrust assets can grow, which in turn will allow the unitrust's yearly payments to grow. In 2011, 93,828 charitable remainder unitrust tax returns were filed with the IRS.

Unitrust Types

Regular

A regular unitrust is the standard type of charitable remainder unitrust: it pays out a fixed percentage of its fair market value, as re-valued annually.

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If necessary, principal must be invaded to fulfill the trust's payment obligation.

Net Income/ Net Income with Makeup (also known as an income exception unitrust)
The net income unitrust makes income payments each year equal to the lesser of the unitrust percentage of the trust's fair market value and the trust's total income for the year. If the trust earns less income than is necessary to meet its percentage obligation, it is required to distribute only its earned income. The trust never invades principal to make a distribution.

The net income with makeup unitrust is similar to a net income remainder unitrust with one crucial difference. If the unitrust ever generates insufficient income to pay its unitrust percentage for the year, the shortfall is added to any previous shortfalls as payments to be made up. If, in a later year, the unitrust earns more income than necessary to meet its percentage obligation, it will pay out the accumulated "makeup" to the extent that the trust has earned excess income or until the makeup accumulation has been exhausted.

Flip/ Flip with makeup
The flip unitrust starts out as a net income unitrust, then changes into a regular unitrust in the year after a designated triggering event occurs. Once the unitrust makes the flip, it cannot flip back to a net income unitrust. Allowable triggering events are 1) a specific date, 2) the sale of specific unmarketable assets, or 3) the occurrence of an event outside the control of the trustee and anyone else, including the birth, death, marriage, or divorce of a specific person.

A flip unitrust with makeup starts out as a net income unitrust with makeup provision, then changes into a regular unitrust in the year after a designated triggering event occurs. Any makeup balance remaining at the end of the year in which the flip occurs cannot be distributed later.

3. **Pooled income funds**
A pooled income fund is a trust arrangement maintained by the sponsoring charity. The donor contributes property to the trust and receives a proportionate share of the trust’s future earnings for life. The pooled fund donor is entitled to a charitable income tax deduction for the present value of the charitable remainder. Fund participants are assigned units proportionate to their contribution and the total value of the fund. Income distributed to each participant is determined by the total income earned by the trust and allocated per unit held by each participant.

A pooled income fund is similar to a charitable remainder unitrust in that the amount of income distributed varies with investment performance. Unlike a Unitrust, however, there is no maximum amount that can be distributed each year.

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A pooled fund's annual payments are not fixed and depend exclusively on its net earned income.

Upon the death of the income beneficiary, an amount equal to the then current fund value attributable to the participant's units is severed from the fund and contributed to the charity maintaining the pooled fund. In 2011, there were 1,402 pooled income funds.

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