


PG Calc YOUR PARTNER IN PLANNED GIVING SUCCESS



What to Use When: CGAs vs. CRATs and CRUTs

Date: May 25, 2023
 Time: 1:00 – 2:00 Eastern
 Presenter: Jeff Lydenberg
 Vice President, Consulting

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PG Calc YOUR PARTNER IN PLANNED GIVING SUCCESS **Agenda**

1. Characteristics of CGA and CRT donors
2. Features of CGAs, CRATs, and CRUTs
3. Comparison of a CGA and a CRAT
4. Charitable remainder unitrusts: variations on a theme
5. Deferred annuities and CRTs to supplement retirement
6. Funding life income gifts with illiquid assets/real estate

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PG Calc YOUR PARTNER IN PLANNED GIVING SUCCESS **Gift Annuity Donor Profile**

- Average age at first annuity is 79
- Charitable inclination to support nonprofit organizations
- Not comfortable with risk
- Interested in receiving fixed payments for life
- Aware of the tax advantages associated with CGAs
 - ✓ Transactional
- Frequently establish multiple annuities

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Charitable Remainder Trust Donor Profile

- Typically, retirement age but younger donors too
- Donors with significant assets
- Philanthropically inclined
- Looking for an income tax deduction and capital gains tax savings
- Interest in regular income during life or a specified period


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CGAs, Annuity Trusts, and Unitrusts

- Potentially hundreds of thousands of gift annuities
- 2012, 14,616 annuity trusts in existence
- 2012, 91,250 unitrusts in existence
- CRTs often initiated by donors' estate and financial planning professionals
- CGAs initiated by gift planning officers through their charity's marketing efforts




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Features of the Gift Annuity

- Low barrier to entry (\$10,000 min. common)
- Easy to establish and understand
- Annuities backed by all of charity's assets
- Subject to heavy regulation in some states
- Benefits the issuing charity
- One or two annuitants permissible



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The Prototype CGA

- Leah, 79 years old
 - ✓ \$50,000 CD paying 3%
 - ✓ After-tax income \$1,140 (24% bracket)
- Contributes \$50,000 cash for 7.4% CGA (ACGA 2023)
 - ✓ \$3,700 annual payment
 - ✓ \$2,501 tax-free for her 9.9-year life expectancy
 - ✓ \$1,199 taxed as ordinary income
 - ✓ \$3,412 of after-tax income

*All examples in this presentation based on a 5% discount rate and ACGA 2023 rates.

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The Prototype CGA

- Charitable deduction of \$25,540
- CGA is irrevocable
- Leah can't get contribution back
- She owns an income stream, not principal
- Not equivalent to an investment, it is a gift
- Does not keep pace with inflation
- Not subject to market fluctuation

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Rules Applicable to CRTs

- Separately managed trust managed by trustee
- Payout may not be lower than 5% or over 50%
- Deduction must be no less than 10% of gift
- Term can be lives, fixed term, or a combination
- Can name multiple charitable beneficiaries
 - ✓ Donor usually retains power to change charities

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    graph TD
      Donor[Donor] -- "1 Gift of property" --> Untrust[Untrust]
      Untrust -- "2 Income tax deduction  
Variable payments" --> Donor
      Untrust -- "3 Remainder to Charity" --> Charity[Charity]
  
```

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Rules Applicable to CRTs


- Can be created during life or at donor's death
- Unitrusts offer flexibility
 - ✓ Trust terms can more easily accomplish multi-generational benefits
 - ✓ Vehicle of choice for illiquid assets
 - ✓ Unitrust can keep pace with inflation if investments appreciate
 - ✓ Can make additions to a unitrust

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CRAT: The "Other" Fixed Income Gift



- Gift minimums much higher than CGAs
 - ✓ +\$250,000 is common
- Can benefit multiple charities
- Term can be combination of lives, fixed term, or combination of both
- May not be greater than 5% chance trust will exhaust
 - ✓ 5% probability test
 - ✓ Can avoid 5% probability test by requiring early termination if principal falls below 10% (Rev. Proc. 2016-42)

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CRAT: The "Other" Fixed Income Gift

- Liability for payments limited to assets in the annuity trust
- No risk to charity if named as beneficiary
- Charity acting as trustee fraught with peril
- Not subject to CGA regulations
- Payout negotiated between donor and trustee
 - ✓ No ACGA for trust rates!

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CRAT: The "Other" Fixed Income Gift

- George and Sally, both 75
- \$2M highly appreciated, low yielding stock
- Gift of stock to 5% annuity trust
 - ✓ Payments of \$100,000 for life
- Capital gain trapped inside annuity trust
- Income taxed at capital gain rates after reporting interest and dividend income


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Unitrust to Diversify and Increase Income

- George and Mary, 78 and 74 fund a 5% CRUT
 - ✓ \$2M principal, \$1M basis
 - ✓ Year 1, Before-tax income \$100,000
- Assume constant net return of 6%
 - ✓ 2% income, 4% capital appreciation
 - ✓ \$2M principal has grown to \$2,209,244 in year 10
 - ✓ Before-tax income has increased to \$109,369



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Security v. Growth Potential

- Charitable remainder unitrust payments subject to market performance
- Compare two 5% CRUTs invested as follows
 - ✓ Historical returns for 10-year period beginning 1/1/1990
 - ✓ Historical returns for 10-year period beginning 1/1/2000
- Compare to 6.5% annuity paying to 74-year-old


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The Flip Charitable Remainder Unitrust

- Operates as net-income trust until trigger event
 - Operates as straight payout after trigger
- Flip trigger may not be in discretion of donor, trustee, or any other person
- As a retirement vehicle
 - Invest for low income in pre-flip years
 - Invest for total return post-flip
- Flip occurs in year following flip trigger



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Life Income to Supplement Retirement

- Dr. and Mrs. Mahoney, both 55
- Retiring at age 70
- Gift of \$250,000 to CRUT that will flip in 2038
 - \$40,000 annual additions for 10 years
 - Flips at age 70

\$250,000 in year one, \$40,000 additions for 10 years	\$650,000
Trust fair market value at age 70 (6% constant returns)	\$1,034,526
Before-tax income at age 70 (Income in subsequent years will vary.)	\$39,789
Total income tax charitable deductions, based on 2% discount rate	\$167,520

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Deferred Payment Gift Annuity

- Annuity payments begin at least one year from date of gift
- ACGA rate compounded at 4.25% a year
 - Deferred offers higher annuity rate and larger deduction than immediate payment annuity
- Two flavors of deferred annuities
 - Donor picks a fixed future payment date at time of gift
 - Donor chooses a range of payment start dates (flexible)

ADMIT
 DEFER
 DENY

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Deferred Payment Gift Annuity

- Linda Sommers, 50
 - ✓ 4.2% if an immediate CGA in 2023
- Gift of \$50,000 in 2023
- Defers payments to age 65
 - ✓ Deferred annuity rate 10%
 - Annual annuity of \$5,000 for life
 - ✓ Income tax deduction of \$26,771 in year of gift

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Flexible Deferred Annuity

- Richard Runcey, 59
- Unsure when he might want CGA payment
- Funds flexible deferred annuity with \$100,000
- Retains right to begin payments between age 65 and 70
- Lowest deduction of all possible start dates, \$47,376

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Flexible Deferred Annuity

Elective Start Date	Age at Start Date	Annuity Rate	Tax-free Portion	Ordinary Income	Total Annuity
6/30/2029	65	6.9%	\$2,642.70	\$4,257.30	\$6,900.00
6/30/2030	66	7.3%	\$2,752.10	\$4,547.90	\$7,300.00
6/30/2031	67	7.8%	\$2,878.20	\$4,921.80	\$7,800.00
6/30/2032	68	8.2%	\$3,009.40	\$5,190.60	\$8,200.00
6/30/2033	69	8.7%	\$3,149.40	\$5,550.60	\$8,700.00
6/30/2034	70	9.3%	\$3,310.80	\$5,989.20	\$9,300.00

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The Right Gift Option with Illiquid Assets



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Illiquid Assets Funding a Flip CRUT

- A Flip CRUT pays its net income prior to the trigger event
 - ✓ Non-income producing asset, no income prior to flip, OR
 - ✓ Donors continue to receive net income until flip
- Sale of an "unmarketable asset" is a permissible trigger event
- Unmarketable means not easily converted to cash
 - ✓ Real estate, tangible personal property, business interests

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Illiquid Assets Funding a Flip CRUT

- Timing of trigger event matters!!
- Flip to straight payout occurs in year **following** trigger event
- Sale on January 1 vs. December 31?
 - ✓ If income producing asset sold early, net income could drop precipitously
 - ✓ Circumstances of income and sale require special attention

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Flip CRUT Funded with Apartment Building

James and Linda, 71 and 70

\$1.6M FMV
\$400,000 basis

Deduction
\$678,960

"Flip"
NIMCRUT

Net income until sale
5% of trust value after sale

James and Linda

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Flip CRUT Funded with Apartment Building

Year	Year-End Principal	Capital Appreciation (0%)	Income (3%)	Before-Tax Payments
Year of gift 1	\$1,600,000	\$0	\$48,000	\$48,000
Sale in year 2	\$1,600,000	0	\$48,000	\$48,000
		(4%)	(2%)	
Flip in year 3	\$1,616,000	\$64,000	\$32,000	\$80,000
4	\$1,632,160	\$64,640	\$32,320	\$80,800
5	\$1,648,482	\$65,286	\$32,643	\$81,608
6	\$1,664,966	\$65,939	\$32,970	\$82,424
7	\$1,681,616	\$66,599	\$33,299	\$83,248
8	\$1,698,432	\$67,265	\$33,632	\$84,081
9	\$1,715,417	\$67,937	\$33,969	\$84,922
10	\$1,732,571	\$68,617	\$34,308	\$85,771

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Summary

- One life income gift does not fit all
- Consider donor's profile and risk tolerance
- Consider donor's objective with life income
- Select the vehicle that suits donor **and** charity
- Use familiar vehicles in new ways
- Take advantage of flexibility of life income gifts

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