More Problem Solving with Planned Gifts

Date: July 30, 2015

Time: 1:00 – 2:30 Eastern Time

Presenter: Frank Minton
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Objective of Webinar

To demonstrate how creative adaptations and combinations of planned giving vehicles can solve donor problems.

Methodology

- Nine case studies, each beginning with a problem arising from a donor situation and then proposing a solution.
- Two Question and Answer periods.

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Case One

Example of Bill who owns a life insurance policy

Face value	$120,000
Cash surrender value	80,000
Total premium paid	60,000
Cost of insurance charges	12,000
Dividends paid and outstanding loans	0

Case One

If Bill surrenders the policy to the company for cash

Cash value	$80,000
Adjusted cost basis	60,000
Ordinary income	20,000

Case One

If Bill sells the policy to a third party for $88,000

Amount received	$88,000
Adjusted cost basis($60,000-12,000)	48,000
Ordinary income	20,000
Capital gain	20,000

Case One

If Bill contributes the policy to a charity

Benefit to charity (what an appraiser determines the value to be)	$86,000
Adjusted cost basis ($60,000-$12,000)	48,000
Portion of value that is ordinary income	20,000
Charitable deduction	66,000

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Things to Keep In Mind Regarding Gifts of Life Insurance

1. The value of a paid-up policy is the “replacement value;” the value of a policy on which premiums are still payable is the “interpolated terminal reserve value.”
2. An independent appraisal is required to determine the value if the charitable deduction will exceed $5,000.
3. Whether or not the policy is paid up, the deduction must be reduced by the amount that would be ordinary income if the policy were surrendered for cash.

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Case Two

Example of Stave and Wendy and their unusual CRT request

Objectives:

- Payments to Steve and Wendy, ages 73 and 72, for life
- Payments to daughter, age 49, if they don’t live very long, a concern since no family members have lived past 80
- Payments to grandson, age 23, if their daughter does not survive them

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Case Two

Beneficiary options that would not work or be advisable

- Payments to Steve and Wendy for life and then to their daughter for life
- Payments to Steve and Wendy for life, then to daughter for life, then to grandson for life
- Payments to Steve and Wendy for life and then to daughter or grandson for 20 years
- Payments for a 20-year period, first to Steve and Wendy, and if Steve and Wendy don’t live for 20 years, then to their daughter or grandson

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Solution

- Payments to Steve and Wendy for life
- If they don't live 20 years, then payments to daughter for rest of 20-year period beginning at establishment of the trust
- If neither Steve nor Wendy nor their daughter lives for 20 years following establishment of the trust, then payments to the grandson until the end of the 20-year period

Case Three

Example of Jim, who demands a high CRUT payout rate

Proposed Gift

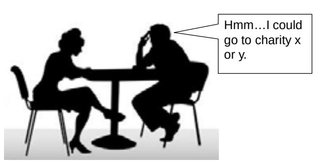
Donor: Jim, age 80

Amount of Gift: $2,000,000

- CRUT with an 8% payout rate
- Charity to be trustee and sole remainder beneficiary.
- Jim to travel and have no worries

Problem

- College has adopted a policy saying it will not serve as trustee of CRT with a payout rate higher than 6%
- Jim threatens to go to another charity if his alma mater will not budge on the payout rate



Case Three

If college adheres to current policy

Gift	Payout Value of Remainder	College would Serve as Trustee
$200,000 for a CRUT with a 5% payout rate	$135,564	Yes
$2,000,000 for a CRUT with an 8% payout rate	$1,099,760	No
$2,000,000 for a 10-year-term CRUT with a 10% payout rate.	$707,880	No

Solution

Change the policy!

Instead of a one-size-fits-all-maximum-payout rate, have a requirement that the present value of the remainder interest be a minimum dollar amount or a minimum percentage of the contribution, whichever is larger.

Case Four

Example of Ronald and Julia who want to name the new wing of a hospital

Proposed Funding Asset

Janet Smith Oncology Wing

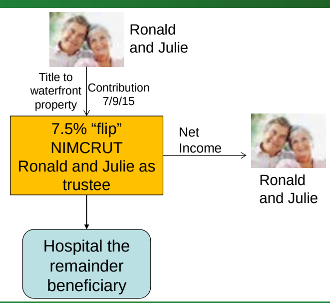
Naming Opportunity

The Situation

- Ages of Ronald and Julie — 75, 74
- Estimated value of property — $3.0-4.75 million
- Required naming gift — $1,500,000
- Portion of naming gift to be paid up-front — 75% or $1,125,000
- Portion that can be deferred — $375,000 (present value)

- Donors want to increase income and benefit charities in addition to hospital
- Because of potential issues with the property, hospital does not want to be an owner or trustee of a trust that owns it

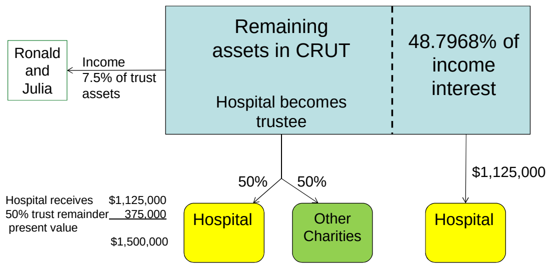
Proposed Solution



Proposed Solution: Step 2

- Trustee lists property for sale and sale closes 12/18/2015. Net proceeds are $3,700,000.
- Donors order an appraisal, and appraiser is instructed to value the property as of 7/9/15 based on information available at that time. The appraised value as of that date is $3,600,000, and the charitable deduction of $1,236,132 is based on that value.

Proposed Solution: Step 3



Questions

1. Why was the income interest contributed over one year after the establishment of the trust?
2. Why was the income interest contributed after the conversion of the trust from a NIMCRUT to a SCRUT?

Questions and Answers

- To ask a question:
  - Press **7#** on your telephone keypad or send a chat message.
- To remove yourself from the queue at anytime:
  - Press **7#** again on your telephone keypad.

Case Five

Example of David and Nancy who are asked for a $1 million campaign gift

Options presented to David and Nancy

- Contribute $1 million in a lump sum before the end of the year
- Contribute $200,000 per year for five years

They ask if they can pay $125,000 per year for eight years.

Case Five

Extending the pledge period raises these concerns

- Present value of gift diminished
- Long-term pledge might not be fulfilled
- Donors might die before pledge is fully paid, necessitating making it enforceable against their estate

Case Five

Long-term pledge has advantage and disadvantage to donors

- The advantage: They can retain capital for a longer period and potentially earn a high return on it.
- The disadvantage: Because of a spike in income, they could use a quite large charitable deduction this year.

Retain capital

Large deduction

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Solution

Grantor charitable lead annuity trust

Amount contributed	$1,000,000
Duration of trust	8 years
Annual payment (12.5%)	125,000
Total payments to charity	1,000,000
Charitable deduction (2.0% CMFR)	915,690
Income tax savings (39.6%)	362,613
After-tax earnings on tax savings	173,132
Amount paid to donors at trust termination	435,711
Estimated tax donors pay on income	160,000
Net cost of campaign gift **($1,000,000 + 160,000 – 435,711 – 362,613 – 173,132)**	**188,544**

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What if Lead Trust Funded with Municipal Bond Fund?

- No tax on income, possibly some tax on gain when bond fund shares liquidated to make trust payments
- Less returned to donor when trust terminates
- Whether investing trust assets in a tax-exempt bond fund is a better alternative depends on returns that would be earned, but probably it will be better to choose taxable investments with a higher total return potential

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Case Six

Example of Wanda who gets totally tax-free income and increases annual giving

- Wanda, age 76, makes outright gifts of $1,500 per year
- She has a maturing $50,000 CD, and interest on a new CD would be very low
- She is considering using the $50,000 to purchase shares in a municipal bond fund currently paying an interest rate of 3%
- She is subject to a 33% tax rate

Solution

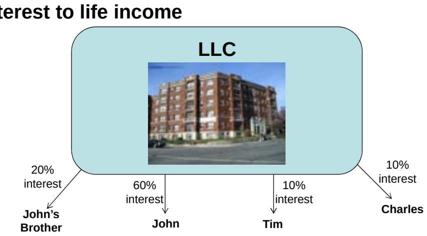
Contributes money from maturing CD for a gift annuity	$50,000
Annual annuity payment	3,000
Taxed as follows:	
Tax-free	2,298
Taxable	702
	3,000
Charitable deduction	22,869
Amount paid to Wanda tax-free each year	2,298
Additional annual contribution	702
Donation receipt	702

Summary

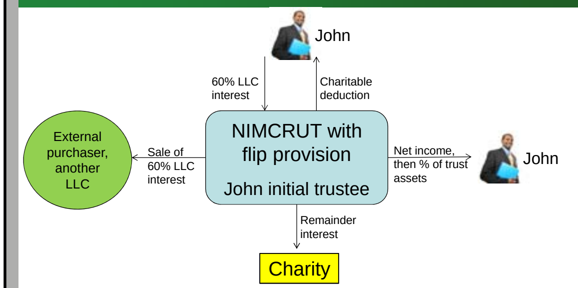
- Charity pays just the tax-free portion of the payments to Wanda
- This is 4.6% of her contribution. The interest from the municipal bond fund would be only 3.0% of her investment.
- She increases annual giving by $702
- Her deduction results in tax savings of $7,547

Case Seven

Example of John who wants to convert an LLC interest to life income



Solution

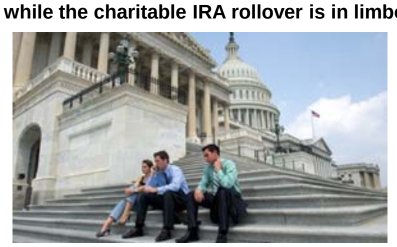


Questions

1. If the apartment building had been owned by an S corporation of which John was the principal shareholder, could he have contributed his share to the CRT?
2. Could he have made an outright gift of his S stock? Tax consequences?
3. Could the charitable remainder beneficiary serve as trustee of the CRT?

Case Eight

Example of Joe and Keith who wonder what to do while the charitable IRA rollover is in limbo



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Possible Legislative Outcomes Regarding the Charitable IRA Rollover

- Expanded and permanent Rollover, either as a stand-alone bill or part of Extenders bill, enacted
- One-year extension of Rollover for outright gifts once again included in Extenders bill and enacted
- The rollover is not approved for this year

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Should Donors Advise Their IRA Administrator to Make a Transfer Now?

Generally, yes.

- If the Rollover is approved retroactive to January 1, their transfer will be covered
- If it is not approved, the transfer will be included in taxable income, and a deduction for it will be allowed. In a few cases, the outcome will not be as favorable as the Rollover, but for most people it will be substantially the same.

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Retirement Fund Gifts Not Dependent on Fate of Charitable IRA Rollover

1. Combination of cash distribution and contribution of cash or appreciated securities
2. Roth conversion in tandem with major gift of cash or other property
3. Testamentary gift annuity funded with all or portion of remaining retirement funds
4. Testamentary CRT funded with all or a portion of remaining retirement funds
5. Charity outright beneficiary of some portion of remaining retirement funds

Note!

Unlike the Rollover, all five of the preceding gifts can be made from a 401(k), 403(B), or other defined contribution plan, as well as from an IRA.

Case Nine

Example of potential conflicts when a donor becomes personally attached to you

Situation

You change jobs from a university to a hospital foundation in the same city. One of your elderly donors at the university now wants to shift her bequest provision to your new employer. What should you do?

- Decline her request to visit her?
- Visit her, tell her to keep the bequest with the university, and tell your successor to see her?
- Suggest that she divide her bequest between the university and the hospital?
- Help her do what she wants to do?

The Larger Question

Is it okay to become friends with donors and socialize with them?

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"The world is but a canvas to the imagination."
- Henry David Thoreau

Most of the planned giving vehicles are not new, but they can be adapted and combined in novel ways to solve donor problems.

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Questions and Answers

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Still Have a Question?
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