



# Planned Giving

## Opportunities to Structure a Gift that Benefits Charity, the Donor, and the Donor's Family—All at Once

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What do we mean by “planned giving”? We mean gifts that require more than writing a check to a charity during its annual fund drive. Donors are attracted to planned giving because it allows them to structure gift vehicles that achieve financial and other philanthropic objectives in a tax-efficient way. Planned gifts are attractive to charities because they provide gifts from donors who may not be in a position to make current gifts of cash.

Planned gifts can take a variety of forms. Most forms depend on the federal income tax charitable deduction rules discussed below. When a donor asks a planner about planned giving, the planner usually recommends vehicles based on the type of asset the donor wishes to give because different forms work better for different assets. This article describes the “tool box” of planned-giving vehicles.

### Planned Giving Vehicles

Because we are talking about planned giving, we will ignore the subject of current cash gifts. Other planned gifts can be separated into structures that are created by the donor and structures that are created by the charity, and they range from simple to complex.

#### Appreciated Property

One often-missed opportunity to plan for an outright gift is to make a gift of appreciated property rather than cash. Because donated assets such as stocks, bonds, mutual funds, or real estate held for more than one year provide a federal

income tax deduction based on fair market value, making a gift of the property eliminates all capital gains tax and can result in a larger gift for a lower out-of-pocket cost to the donor than selling the property and giving the proceeds.

#### Bequests

One of the simplest ways to make a planned gift is by a bequest of money or property through the donor's will or revocable trust. Such a bequest can be of a particular asset, a set dollar amount, or a percentage of the estate.

#### Life Insurance

A donor can name a charity as beneficiary of a life insurance policy, or the donor can transfer ownership of a life insurance policy to a charity. If the policy is transferred, the deduction is the replacement value or cash value depending on what the charity does with the policy, and the donor may receive an income tax deduction for future premiums paid. If the charity is named as beneficiary but the policy is not transferred, there is a deduction for federal estate tax purposes when the insured dies, but there is no immediate income tax deduction. Other arrangements with life insurance can be quite complex and are beyond the scope of this article.

#### Individual Retirement Accounts (IRAs)

IRAs are particularly good assets for planned giving. Naming a charity as beneficiary can produce an estate tax deduction upon the death of the owner as well as eliminate the income tax on the receipt of the IRA assets by the ben-

eficiary at the owner's death. Naming a charity as beneficiary of a dollar amount or percentage of an IRA is fairly simply accomplished on a form provided by the IRA trustee.

#### Charitable IRA Rollover

Congress has extended a charitable IRA rollover opportunity for a lifetime gift. Through 2011, an individual who has reached age 70½ may transfer up to \$100,000 from an IRA directly to charity. The transfer is not deductible as a charitable gift, but the amount transferred is not subject to income tax for the owner and can count toward the required minimum distribution for the year. The transfer, however, cannot be made to most private foundations, donor-advised funds, or their supporting organizations.

#### Conservation Easements

Conservation easements provide a powerful tool to preserve real property that is important to a donor while netting the donor a charitable deduction. Such an easement permanently restricts the use of the real property and must be enforceable by a qualified charity. Valuation of the easement can be an expensive process and often is subject to Internal Revenue Service (IRS) scrutiny, but for the donor with the right kind of property such a planned gift is worth exploring.

#### Remainder Interest in Donor's Personal Residence

Another planned gift involving real estate is the irrevocable transfer of a remainder interest in the donor's personal residence subject to the donor's right



to use the residence during the donor's lifetime. A donor who lives next door to a church or school would be a great candidate. After the donor signs the deed giving the remainder interest to the charity, state law or an agreement between the donor and the charity can determine the responsibility for maintenance, repairs, and other costs during the donor's lifetime. Although nothing passes to the charity until the donor dies, the donor can take an income tax deduction for the current value of the remainder that will pass to the charity using prescribed actuarial assumptions. The value of the remainder also will not be subject to estate tax.

**Split-Interest Trusts**

Several types of split-interest trusts can be created by a donor:

**Charitable remainder trusts (CRTs)** make annual payments to one or more individual beneficiaries for a term of up to 20 years or for the lives of the beneficiaries. At the end of the term, the remaining assets are distributed to one or more charities, which may include a family foundation. A CRT may be created by a will or during a lifetime. The value that passes to charity at the death of the income beneficiaries is not subject to estate tax either way. The value of the trust is included in the estate, but it is offset by the charitable deduction for the remainder passing to charity. So if a successor income beneficiary is not the donor's spouse, there could be a sliver of the trust that is subject to estate tax. The current value of the remainder that will pass to charity, calculated at the time of the gift for a lifetime CRT, is not subject to gift tax and may provide an income tax deduction as well.

A CRT allows a donor to make a commitment to a charity but keep income from the donated assets. When a CRT sells appreciated assets, the capital gains tax is deferred, so a CRT is particularly useful for a donor whose goal is to derive an income

stream from highly appreciated assets for the donor or other beneficiaries. As each distribution is made to the noncharitable beneficiary, a portion is capital gain that may be reported by the beneficiary depending upon the character of the amounts included in the distribution pursuant to IRS ordering rules. It is often misstated that a CRT eliminates the gain, when in fact the gain is just deferred. By the same token, a CRT does allow the entire proceeds from a sale by the CRT of an appreciated asset to be invested and grow rather than having to pay capital gains tax all in the year of the sale.

**Charitable remainder annuity trusts (CRATs) and charitable remainder unitrusts (CRUTs)** are specific CRT structures. CRATs allow for annual or more-frequent

distribution of a set dollar amount; CRUTs allow for distributions measured as a percentage of the fair market value of the assets at the time of the distribution.<sup>1</sup>

Tables 1 and 2 show the cash flow and remainder of a lifetime charitable remainder annuity trust (CRAT) and a charitable remainder unitrust (CRUT), respectively, each with a payout rate of 5 percent, each for a 20-year term, and each funded with a gift of \$1 million and assuming a 6.5-percent investment return<sup>2</sup> using the January 2011 Section 7520 rate<sup>3</sup> of 2.4 percent. The CRAT produces a current income tax deduction for the donor of \$213,130 and the CRUT deduction is \$367,495.

**Charitable lead trusts (CLTs)** basically are the inverse of CRTs. A

TABLE 1: \$1-MILLION, 20-YEAR, 5-PERCENT CHARITABLE REMAINDER ANNUITY TRUST (CRAT)				
Year	Beginning Principal	6.50% Growth	Payment	Remainder
1	\$1,000,000.00	\$65,000.00	\$50,000.00	\$1,015,000.00
2	\$1,015,000.00	\$65,975.00	\$50,000.00	\$1,030,975.00
3	\$1,030,975.00	\$67,013.38	\$50,000.00	\$1,047,988.38
4	\$1,047,988.38	\$68,119.24	\$50,000.00	\$1,066,107.62
5	\$1,066,107.62	\$69,297.00	\$50,000.00	\$1,085,404.62
6	\$1,085,404.62	\$70,551.30	\$50,000.00	\$1,105,955.92
7	\$1,105,955.92	\$71,887.13	\$50,000.00	\$1,127,843.05
8	\$1,127,843.05	\$73,309.80	\$50,000.00	\$1,151,152.85
9	\$1,151,152.85	\$74,824.94	\$50,000.00	\$1,175,977.79
10	\$1,175,977.79	\$76,438.56	\$50,000.00	\$1,202,416.35
11	\$1,202,416.35	\$78,157.06	\$50,000.00	\$1,230,573.41
12	\$1,230,573.41	\$79,987.27	\$50,000.00	\$1,260,560.68
13	\$1,260,560.68	\$81,936.44	\$50,000.00	\$1,292,497.12
14	\$1,292,497.12	\$84,012.31	\$50,000.00	\$1,326,509.43
15	\$1,326,509.43	\$86,223.11	\$50,000.00	\$1,362,732.54
16	\$1,362,732.54	\$88,577.62	\$50,000.00	\$1,401,310.16
17	\$1,401,310.16	\$91,085.16	\$50,000.00	\$1,442,395.32
18	\$1,442,395.32	\$93,755.70	\$50,000.00	\$1,486,151.02
19	\$1,486,151.02	\$96,599.82	\$50,000.00	\$1,532,750.84
20	\$1,532,750.84	\$99,628.80	\$50,000.00	\$1,582,379.64
Summary	\$1,000,000.00	\$1,582,379.64	\$1,000,000.00	\$1,582,379.64


**TABLE 2: \$1-MILLION, 20-YEAR, 5-PERCENT CHARITABLE REMAINDER UNITRUST (CRUT)**

Year	Beginning Principal	6.50% Growth	Payment	Remainder
1	\$1,000,000.00	\$65,000.00	\$50,000.00	\$1,015,000.00
2	\$1,015,000.00	\$65,975.00	\$50,750.00	\$1,030,225.00
3	\$1,030,225.00	\$66,964.62	\$51,511.25	\$1,045,678.37
4	\$1,045,678.37	\$67,969.09	\$52,283.92	\$1,061,363.54
5	\$1,061,363.54	\$68,988.63	\$53,068.18	\$1,077,283.99
6	\$1,077,283.99	\$70,023.46	\$53,864.20	\$1,093,443.25
7	\$1,093,443.25	\$71,073.81	\$54,672.16	\$1,109,844.90
8	\$1,109,844.90	\$72,139.92	\$55,492.25	\$1,126,492.57
9	\$1,126,492.57	\$73,222.02	\$56,324.63	\$1,143,389.96
10	\$1,143,389.96	\$74,320.35	\$57,169.50	\$1,160,540.81
11	\$1,160,540.81	\$75,435.15	\$58,027.04	\$1,177,948.92
12	\$1,177,948.92	\$76,566.68	\$58,897.45	\$1,195,618.15
13	\$1,195,618.15	\$77,715.18	\$59,780.91	\$1,213,552.42
14	\$1,213,552.42	\$78,880.91	\$60,677.62	\$1,231,755.71
15	\$1,231,755.71	\$80,064.12	\$61,587.79	\$1,250,232.04
16	\$1,250,232.04	\$81,265.08	\$62,511.60	\$1,268,985.52
17	\$1,268,985.52	\$82,484.06	\$63,449.28	\$1,288,020.30
18	\$1,288,020.30	\$83,721.32	\$64,401.02	\$1,307,340.60
19	\$1,307,340.60	\$84,977.14	\$65,367.03	\$1,326,950.71
20	\$1,326,950.71	\$86,251.80	\$66,347.54	\$1,346,854.97
Summary	\$1,000,000.00	\$1,503,038.34	\$1,156,183.37	\$1,346,854.97

CLT provides an annual payment to one or more charitable beneficiaries for a period of time, with the remainder interest going to family members. The value of the income or lead interest, determined using the IRS valuation rate, reduces the value and therefore the gift tax cost of the transfer of the remainder to the family. Using a CLT permits the transfer of appreciation in excess of the IRS benchmark rate<sup>4</sup> to a family, free of estate and generation-skipping transfer tax (GSTT). They are particularly attractive in the current low interest rate environment. CLTs may be structured in different ways to take advantage of income tax deductions or to leverage the GSTT.

Tables 3 and 4 show the cash flow and remainder of grantor and nongrantor CLATs, respectively,

each initially funded with \$1 million, assuming a 6.5-percent rate of return, and using the January 2011 2.4-percent Section 7520 rate, first for a 20-year term then a 10-year term, and with the annuity payout remaining the same or increasing each year by 20 percent. The grantor CLAT permits the grantor to take the charitable income tax deduction but requires the grantor to pay tax annually on the trust income. With a nongrantor CLAT, the trust pays the income tax and benefits from the charitable deduction.

For both the grantor and the nongrantor CLATs, the stream of annuity payments<sup>5</sup> are the same as shown in table 5, so it is the CLAT's structure as a grantor or nongrantor trust that changes the amount of the remainder passing to family.

### Pooled Income Funds

Planned giving opportunities sometimes are structured by the charity for the convenience of donors. One such vehicle is a pooled income fund or PIF. A PIF benefits the donor in much the same way as a CRT but is administered by the public charity. Individual donors make contributions in exchange for units of participation. A contribution to a PIF results in a charitable income tax deduction for the actuarial value of the remainder interest that will pass to the charity.

### Charitable Gift Annuities

Many charities also offer charitable gift annuities. The donor transfers assets in exchange for an annuity that provides a fixed payment for the life of the donor and up to one additional individual. The net amount remaining at the annuitant's death passes to the charity. A current charitable income tax deduction is available for the actuarial value of the remainder interest that will pass to charity. So a charitable gift annuity operates much like a unitrust between the donor and the charity, except that the donor's gift is not preserved in a separate trust. Charitable annuity rates are set by an outside organization and often are higher than the return on other kinds of investments. The donor does not recognize gain immediately if it is funded with appreciated property; instead, the gain is spread out as the annuity payments are received. Most organizations have a minimum size for a charitable gift annuity and many limit the minimum age of the individual donor.

### Private Foundations

On the more complex end of the spectrum, a donor can create a private foundation. Structured either as a corporation or as a trust managed by its officers or trustees, a typical private foundation makes grants to public charities. Through such a foundation, the donor/founder can maintain some control over the management and disposition of the assets as well as

**TABLE 3: \$1-MILLION GRANTOR CHARITABLE LEAD ANNUITY TRUSTS (GRANTOR CLAT) WITH LEVEL AND INCREASING ANNUITY PAYMENTS, 6.5% RETURN, AND 2.4% SECTION 7520 RATE**

Initial funding amount	\$1,000,000	\$1,000,000	\$1,000,000	\$1,000,000
Initial CLAT funding begins in:	2011	2011	2011	2011
Term (in years)	20	20	10	10
Increasing annuity (annually) payout percentage	20%	0%	20%	0%
7520 interest rate used in this illustration	2.40%	2.40%	2.40%	2.40%
Total rate of return	6.50%	6.50%	6.50%	6.50%
Initial payout rate (percentage)	0.77%	6.35%	4.53%	11.37%
Payout to remainder interests at the end of the grantor CLAT term	\$1,537,995	\$1,056,572	\$429,058	\$343,245

**TABLE 4: \$1-MILLION NONGRANTOR CHARITABLE LEAD ANNUITY TRUSTS (NONGRANTOR CLATS) WITH LEVEL AND INCREASING ANNUITY PAYMENTS, 6.5% RETURN, AND 2.4% SECTION 7520 RATE**

Initial funding amount	\$1,000,000	\$1,000,000	\$1,000,000	\$1,000,000
Initial CLAT funding begins in:	2011	2011	2011	2011
Term (in years)	20	20	10	10
Increasing annuity (annually) payout percentage	20%	0%	20%	0%
7520 interest rate used in this illustration	2.40%	2.40%	2.40%	2.40%
Total rate of return	6.50%	6.50%	6.50%	6.50%
Initial payout rate (percentage)	0.77%	6.35%	4.53%	11.37%
Payout to remainder interests at the end of the grantor CLAT term	\$1,336,701	\$1,046,539	\$422,777	\$343,245

the foundation's mission and purpose. In the family context, this structure allows the founder's legacy to live on for future generations and can provide a tool to unite family, practice good family governance and communication, and teach younger generations. Obviously this more-complex structure is more expensive to create and maintain. Numerous restrictions and regulations apply to private foundations and great care must be taken to avoid inadvertent violations of those rules and restrictions, all of which are designed to assure that the foundation is used to further charitable rather than private purposes.

**Donor-Advised Funds (DAFs)**

Some benefits of a private foundation can be achieved by establishing a donor-advised fund (DAF) through a sponsoring organization that offers DAFs, such as a community foundation. Because DAFs are simpler and

**TABLE 5: CLAT ANNUITY STREAM**

Year	20-Year Increasing Annuity Payment	20-Year Level Annuity Payment	10-Year Increasing Annuity Payment	10-Year Level Annuity Payment
2012	\$7,700	\$63,543	\$45,309	\$113,669
2013	\$9,240	\$63,543	\$54,371	\$113,669
2014	\$11,088	\$63,543	\$65,245	\$113,669
2015	\$13,305	\$63,543	\$78,294	\$113,669
2016	\$15,966	\$63,543	\$93,953	\$113,669
2017	\$19,160	\$63,543	\$112,744	\$113,669
2018	\$22,992	\$63,543	\$135,292	\$113,669
2019	\$27,590	\$63,543	\$162,351	\$113,669
2020	\$33,108	\$63,543	\$194,821	\$113,669
2021	\$39,730	\$63,543	\$233,785	\$113,669
2022	\$47,676	\$63,543		
2023	\$57,211	\$63,543		
2024	\$68,653	\$63,543		
2025	\$82,383	\$63,543		
2026	\$98,860	\$63,543		
2027	\$118,632	\$63,543		
2028	\$142,358	\$63,543		
2029	\$170,830	\$63,543		
2030	\$204,996	\$63,543		
2031	\$245,995	\$63,543		



**TABLE 6: PERMITTED DEDUCTIBLE CHARITABLE CONTRIBUTIONS FOR FEDERAL INCOME TAX PURPOSES**

Charitable Gift Categories	Adjusted Gross Income*
Gifts of Cash to Public Charities and Certain Foundations Colleges, universities, museums, hospitals, United Way-type organizations Donor-Advised Funds Supporting Organizations Conduit Foundations Operating Foundations	50%
Gifts of Long-Term Capital Gain Property (including appreciated stock) to Public Charities and Certain Foundations	30%
Gifts of Cash to Private Foundations	30%
Gifts of Long-Term Capital Gain Property to Private Foundations	20%

\* **Additional Limitations:** Full fair market value deduction permitted only for gifts of qualified appreciated stock, which is stock traded on an established securities market. **Adjusted gross income** does not include income exempt from federal income tax, does not address phase-out of deductions for higher income taxpayers, and does not address alternative minimum tax. **Qualified appreciated stock** is limited to 10 percent of the outstanding stock of a corporation, including all prior gifts made by the donor and family members to any private foundations.

less expensive to establish than private foundations, they are a good option for smaller donations. By law, donors may recommend uses for the donated funds, but in most cases sponsoring organizations follow those recommendations. Most DAFs have restrictions about the types of grants they will approve and DAF durations. Some DAFs allow donors to use their own investment advisors to invest the funds.

**Charitable Tax Deductions**


When arranging a gift for which the donor expects a tax deduction, it's vital for the advisor to understand the general rules for charitable tax deductions.<sup>6</sup> Table 6 summarizes these general rules.

Federal tax law limits allowable deductions based on the type of charitable organization, the kind of property donated, and the donor's adjusted gross income. Types of tax-exempt charities include public charities (religious organizations, schools, colleges, hospitals, and United Way-type charities, all of which receive a substantial portion of their revenues from the general public), and supporting organizations and private foundations (both of which receive most or all of their revenues from a small number of sources). Furthermore, an individual may not offset all of his or her income tax during any one tax year; the deduction is limited to a

percentage of the individual's adjusted gross income, with the ability to carry over the excess for five more years. That limitation further depends on the type of charity to which the contribution is made, with generally stricter limits on gifts to private foundations.

The deduction also may be limited based on the type of property donated. Deductions for gifts of property are limited by how they would be treated if they were sold: long-term capital gain, ordinary income, or short-term capital gain. Substantiation and valuation requirements also must be met to take the deduction.

**Conclusion**

Obviously planned giving involves much more than writing a check, yet it provides many benefits for donors and charities alike. Whether working for donors or charities, advisors are best positioned to help all parties fully access all the benefits by having a good understanding of the many different tools available for crafting planned giving programs. 

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**Endnotes**

- 1 A CRAT is required to pay an annual fixed amount to the income beneficiaries. A CRUT is required to pay an annual fixed percentage of its net fair market value, revalued each year, to the noncharitable beneficiaries. In both cases, the payment must equal at least 5 percent but not exceed 50 percent of the net fair market value of the assets contributed to the trust valued at the date of the initial transfer. The actuarial present value of the remainder interest projected to pass to the charitable remainder beneficiaries must be at least 10 percent of the initial fair market value of the contributed assets.
- 2 The rate of return assumptions used in this calculation are for illustration only. Rates





of return are not derived from Wilmington Trust's Capital Market Forecast. This illustration does not represent tax advice and is presented to demonstrate a gift and estate planning technique. Please consult your tax advisor.

- 3 The Applicable Federal Rate (AFR) is set monthly by the IRS and tends to follow market interest rates. AFRs are set for short-term loans (up to three years), mid-term loans (three to nine years), and long-term loans (more than nine years). The Section 7520 rate is used to value the remainder interest of a CRAT or CRUT and the annuity interest in a CLAT. The 7520 rate follows the AFR; it is set at 120-percent of

the mid-term AFR. Both of these rates are at or near historic low levels.

- 4 The section 7520 rate is the hurdle that an investment in a CLAT must outperform to pass the appreciation tax-free to family.
- 5 The annuity payments are calculated specifically to produce zero or nearly zero federal gift tax liability upon trust creation.
- 6 All references are to the Internal Revenue Code and federal tax law. State law differences are ignored for purposes of this article.

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