



NOT-FOR-PROFIT LEARNING SERIES:
**A Board Member's Guide to
Charitable Giving Strategies**



Presented by:

Louise Clayton-Kastenholz, CPA
Manager, PBMares

Certified Public Accountants & Consultants

What is Planned Giving?

- What it is not (just)
 - Making donations to church or pet charity each year
 - Naming a charitable beneficiary in your will
 - Dropping some money in a plate or jar
- What it is
 - Part of overall long term financial planning
 - An methodical strategy for support of specific causes
 - Thought through and implemented with care

Financial Planning in a Nutshell



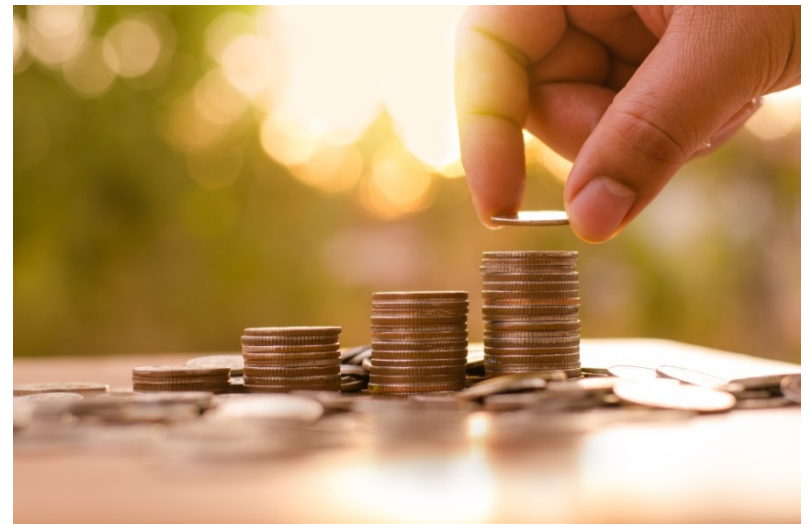
- How will I be prepared for life events?
 - Children and grandchildren
 - Home purchase
 - Education
 - Retirement or medical
 - Marriage or divorce
- Whom shall I support?
 - Family
 - Society



Financial Planning in a Nutshell



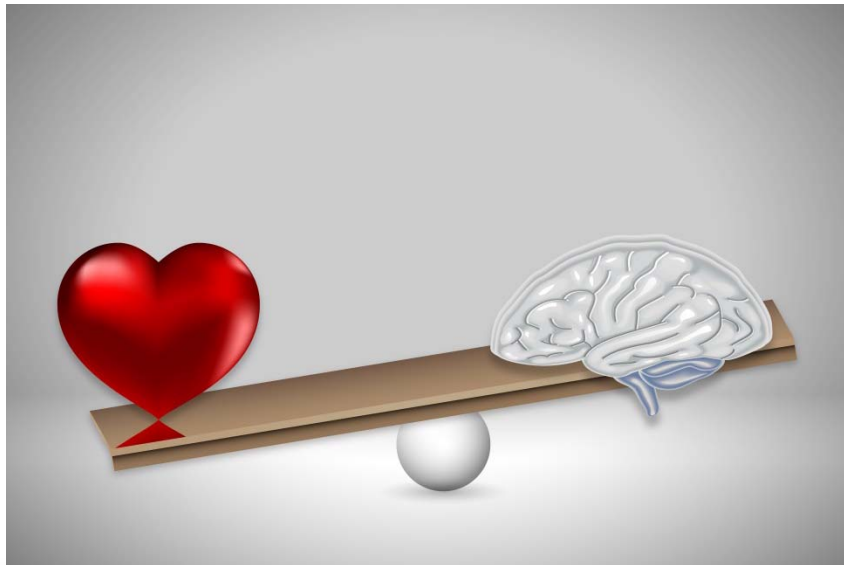
- How will I leave a legacy?
 - Provide for my immediate family
 - Provide an inheritance to future generations
- What resources do I have?
 - Income
 - Savings
 - Assets
 - Business



Financial Planning in a Nutshell



- Personal and Financial Planning are linked
 - All personal plans have financial aspects
 - All financial plans have personal aspects



Sometimes there is a
clear choice to be made
but.....

The relationship between
cost and satisfaction is
not linear.

Where Does Charity Fit In?

- Support
 - Ongoing year to year
 - Making a noticeable difference
- Provide for the future
 - Inheritance
 - Income stream
- Efficient use of resources
- Meeting estate goals
- Matching charitable goals with personal goals

Where Does Charity Fit In?



- The same considerations as other expenditures
 - Is this what I want?
 - Can I afford it?
 - Am I getting the best deal?
 - How should I structure the transaction?
- Plans change over time
 - Different goals and needs at different phases of life
 - Life throwing a curve ball
- Some things are “me” and some things are “us”

Donor Motivators

- General generosity
- Special circumstances
- Sense of obligation
- Something in return
- Tax reduction
- Self sufficient heirs
- Ability to leverage



Planned Giving Options

- Lifetime gifts of cash or property
- Charitable gift annuities
- Split-interest charitable trusts
- Charitable bequests
- Named charitable beneficiaries
- IRA income or assets
- Private foundations
- Donor advised funds

Lifetime Gifts of Cash or Property



- Advantages
 - Double tax advantage – income tax and estate tax
 - Donor can witness effect of gift
- Disadvantages
 - Loss of use of asset during lifetime
 - Loss of income from asset during lifetime
 - Not reversible once done

Lifetime Gifts of Cash or Property

- Types of assets to donate
 - Cash
 - Publicly traded stock
 - Closely held business interests
 - Real property
 - Tangible personal property
- Other considerations
 - Choice of specific asset
 - Timing of the gift



Lifetime Gifts of Cash

- Advantages
 - Easily quantifiable and valued
 - Current income tax deduction
 - 50% of AGI limit applies for most organizations
 - Cash is out of donor's estate
- Disadvantages
 - Not always readily available to be given away
 - Record-keeping requirements (true for all donations)
 - Must have acknowledgement from charity **before filing** tax return, or deduction could be disallowed (over \$250)
 - Need to keep acknowledgements at least three years

Lifetime Gifts of Cash or Property



- Publicly traded stock
 - Deduction for **Fair Market Value (FMV)** of stock if held over a year (long term capital gain property)
 - **No gain** is reported on the donor's tax return
 - No appraisal required for any size donation
 - Generally subject to 30% of AGI limitation (20% for PF)
 - Can elect to deduct basis instead of FMV to meet 50% deduction limit requirements
 - Easily sold by charity to raise cash
 - Charity has no tax effect from donation

Lifetime Gifts of Cash or Property



- Depreciated property
 - Deduction amounts for property are either FMV or lesser of FMV or basis
 - Better for donor to sell the property and deduct the loss on the tax return, then donate the proceeds
 - Some items that are suitable donations will be items for which a loss on sale cannot be deducted, in those cases the effect is the same as donating the item

Lifetime Gifts of Cash or Property



- Closely held business interests
 - Deduction limited to lesser of basis or FMV
 - Appraisal required and could be subject to challenge
 - **Adverse tax effect on charity**
 - Business income is Unrelated Business Taxable Income, may have excise tax due
 - Cash receipts may not accompany taxable income
 - Better option is to have the business donate assets
 - S Corp or Partnership passes deduction to owners
 - Does not create UBTI (unless debt-financed assets)

Lifetime Gifts of Cash or Property



- Real property
 - Can be all or an undivided fractional interest
 - Deduction is FMV if held over one year and investment or business property
 - Qualified appraisal required
 - Harder for the charity to sell if desired
 - Could potentially create liability for environmental or other problems



Lifetime Gifts of Cash or Property



- Bargain sale of real property
 - Sale of an asset for less than fair market value is a gift
 - Treated as both a sale and a gift to charity
 - Donation is difference between FMV and sale price
 - Less any ordinary or short-term gains
 - Long term holding needed to get benefit of FMV
 - Debt on property is treated as part of amount realized
 - Basis in property is prorated between sale and gift

Lifetime Gifts of Cash or Property



- Encumbered real property
 - Gift of debt encumbered property is subject to bargain sale rules (as if sold to charity below FMV)
 - Deemed proceeds equal to amount of debt
 - Charitable deduction is limited to FMV less debt less any ordinary income or short term gain portion of asset
 - Charity may or may not assume mortgage
 - Additional charitable gifts as mortgage paid by donor
 - **Mortgage could create UBTI for the charity**

Lifetime Gifts of Cash or Property



- Tangible personal property
 - Deduction is limited to lesser of basis or FMV
 - Deduction at FMV if used by charity for purpose related to its exempt purpose (includes furniture)
 - Can be recaptured if later sold by charity
 - A small portion of a donated collection can be sold
 - Charity can provide a written certification
 - Special rules apply to the donation of vehicles
 - Limitation on deduction amount
 - Reporting requirement for charity

Lifetime Gifts of Cash or Property



- Life Insurance
 - Leveraging premium costs against a lump sum benefit
 - Proceeds will pass outside of probate
 - Charity can use some of the attributes of a whole-life policy for flexibility instead of waiting
 - Tax effects to donor
 - Deduction disallowed under certain circumstances
 - Valuation is problematic
 - Possible inclusion in donor's estate

Remainder Interests in Property



- Deductibility

- Generally not deductible because not a completed gift
- Real property
 - Special rules for donation of home or farm
 - Special rules for donations for conservation purposes
- Tangible personal property
 - Special rules for donations where donor has given up possession and enjoyment of the asset
 - Example – donation of remainder interest in artwork to museum that has possession of the object for display

Remainder Interests in Property



- Advantages

- Donor retains use of asset for lifetime
- Current charitable contribution deduction of present value of remainder interest
- Charity has guarantee of asset, if not of timing

- Disadvantages

- Irrevocable transaction, no flexibility for future
- Donor can sell the life interest, but not the property
- Could be very long term depending on life expectancy

Charitable Gift Annuities



- Easy way for donor to receive income stream
- Organization sets up and administers
 - Organization has administrative costs involved
 - Advertised to donors, additional marketing effort
- Annuity rate dependent upon donor
- Income tax deduction for PV of remainder
- Donation does not need to be cash
- Appeals to the donor looking for a return

Split Interest Charitable Trusts



- Charity can receive either a lead (income) interest or a remainder interest
- Donor either retains other interest or gifts it to non-charitable beneficiary
- Term of years or lifetime term
- Irrevocable trusts, limited changes possible later
- Established by the donor, not the charity
- Income tax deductions depend on type of trust

Split Interest Charitable Trusts



- Charitable Lead Trusts – CLAT and CLUT
 - Charity gets annual contribution (annuity or unitrust)
 - Remainder to non-charitable beneficiary
 - Gift of present value of remainder interest
 - Trust can be grantor type or non-grantor
 - Charitable contribution deduction
 - taken by trust during the trust term (non-grantor trust)
 - taken by grantor at inception for present value of annuity or unitrust payments (grantor trust)
 - Good for donors who don't need the income stream

Split Interest Charitable Trusts



- Charitable Lead Trusts – CLAT and CLUT
 - Requirements to qualify
 - Fixed amount or fixed percentage to a charitable beneficiary at least annually
 - Term of years or specified individual's life
 - Donor, spouse or lineal ancestor of either
 - Remainder to one or more non-charitable beneficiaries
 - Must be lineal descendent of donor or donor's spouse
 - Trust document must contain certain prohibitions
 - Self dealing, Excess business holdings
 - Investments jeopardizing the trust's charitable purpose
 - Making certain taxable expenditures

Split Interest Charitable Trusts

- Charitable Lead Trusts

- Advantages

- Income tax deduction dependent upon type
 - Grantor type - present value of charity's interest, at outset
 - Non-grantor type – deducted at trust level as paid out
 - Estate and gift tax charitable deduction
 - Deduction on gift return filed for donation of lead interest
 - Non-grantor type – assets are out of the grantor's estate
 - Charity has guaranteed income stream
 - Terms not limited in the same way as CRTs
 - No minimum or maximum payout
 - No limit to duration (must be determinable at creation)

Split Interest Charitable Trusts

- Charitable Lead Trusts

- Disadvantages

- Trust is not a tax exempt entity
 - Grantor - must report income on his or her own individual return - **no contribution deduction as amounts are donated**
 - Non-grantor – taxed at trust level with contribution deduction
 - Tax filing requirements for trust – 1041 and 5227
 - Administrative costs as well as cost to create
 - Irrevocable – can only have minimal flexibility built in
 - Long term arrangement – term or lifetime
 - Restrictions against self dealing
 - Excise tax on UBTI at 100%

Split Interest Charitable Trusts



- Charitable Income Trusts – Non-qualifying Non-grantor CLT
 - All of net income is paid to charity
 - No fixed amount or fixed percentage to charity
 - No charitable income tax deduction at funding
 - Income tax deduction at trust level for charitable donations as made by trust
 - No reduction of principal during term of trust

Split Interest Charitable Trusts



- Charitable Remainder Trusts – CRAT and CRUT
 - Remainder to charitable beneficiary
 - Grantor or other non-charitable beneficiary gets annual payment (annuity or unitrust amount)
 - Income is taxed to beneficiary to extent of distributions, reported on K-1
 - Current charitable contribution deduction at time of funding for present value of remainder
 - Irrevocable, but can “roll-over” by essentially selling the income interest and creating an additional trust with the proceeds

Split Interest Charitable Trusts



- Charitable Remainder Trusts – CRAT and CRUT
 - Requirements to qualify
 - Fixed amount or fixed percentage to a non-charitable beneficiary at least annually
 - At least 5% and no more than 50% of the trust's value
 - A charity may also receive periodic payments
 - Term of beneficiary's life or no more than 20 years
 - Remainder to one or more qualifying charities
 - The value of the remainder interest must be at least 10% of the initial net FMV of the trust assets
 - Must have provisions prohibiting self dealing

Split Interest Charitable Trusts



- Charitable Remainder Trusts – CRAT and CRUT
 - Advantages
 - Large asset donation without loss of income stream
 - Assets are outside of estate at death
 - Deduction for present value of remainder interest
 - Trust is a tax exempt entity (except for UBTI)
 - Trust files only form 5227, no 1041 required
 - Non-charitable beneficiary is taxed on income
 - 4 Tiers for distributions of taxable income to beneficiary
 - Tier system stretches out tax effects of asset sales to bene

Split Interest Charitable Trusts



- Charitable Remainder Trusts – CRAT and CRUT
 - Disadvantages
 - Irrevocable – only have minimal flexibility built in
 - Long term arrangement – term or lifetime
 - Administrative costs as well as cost to create
 - Tax return reporting requirement
 - Form 5227 only, no 1041 required
 - 100% excise tax on UBTI
 - Certain items of income (such as partnership income) could be UBTI and subject to the excise tax

CRTs – NICRUT & NIMCRUT



- NICRUT – Net Income CRUT
 - Unitrust payment is limited to current year income
 - Does not reduce principal in low income years
 - Can adjust income level by choice of investment
- NIMCRUT – Net Income with Makeup Provisions
 - Unitrust amounts over income are made up when income increases over unitrust amount later
 - Makeup can allow for “retirement planning” use
 - Low income during working years
 - High income during retirement years

Estate Planning in a Nutshell



- Goals
 - Provide for spouse, children, other family
 - Leave a legacy for descendants
 - Make a difference for a special cause
 - Smooth administration for family
 - Minimize estate taxes
 - Minimize probate taxes
 - Minimize public record reporting requirements
 - Reduce income tax burden on beneficiaries

Estate Planning in a Nutshell

- Tools
 - Estate Planning Documents
 - Will
 - Revocable Trust Agreements
 - POA and Medical directive
 - Titling of Assets
 - Beneficiary Designations
 - Gifting Plan
 - Life Insurance
 - Irrevocable Trusts



Estate Planning in a Nutshell



- Probate vs non-probate assets
 - Probate
 - Owned in decedent's name
 - Pass by will only
 - Owned by the estate after death
 - Non-probate
 - Title passes automatically after death
 - Will does NOT affect disposition of asset
 - Part of estate for estate tax & basis step up
 - Not owned by the estate



Estate Planning in a Nutshell



- Probate assets
 - Owned solely by decedent
 - Tenant in common
 - Estate as named beneficiary
 - Predeceased primary bene & no contingent benes
 - Assets with no named beneficiary
- Testamentary trusts
 - Will be funded from probate assets
 - Will be under the supervision of the courts

Estate Planning in a Nutshell



- Non-probate assets
 - Joint tenants with right of survivorship
 - Tenants by the entirety
 - Assets with beneficiary designations
 - Transfer on death accounts
 - Pay on death accounts
 - Pensions and annuities
 - IRA accounts
 - Life insurance

Charitable Bequests

- Leaving something to charity in one's will
 - Specific asset
 - Specified sum of money
 - Portion of residuary
- Determined in reference to probate assets
- Also includes assets passing through a Living Trust or Revocable Trust (RLT)
 - Disposition upon death works in same way as will (without probate)
 - Usually pour over will leaves residuary to trust



Named Charitable Beneficiaries



- Assets pass outside of probate
 - Avoids expense for probate tax
 - Avoids reporting requirements of probate
 - Avoids public record aspect of probate
 - Not affected by will
- Transferred upon notification and documentation of death
- Reduces administrative expenses and effort
- Part of taxable estate - with charitable deduction

IRA Income or Assets

- Giving IRA income to charity
 - For IRA account holders who do not need the income
 - Charitable Rollovers
 - Special rule for over 70 ½ year old IRA account holders
 - Must be direct transfer from IRA trustee to charity
 - Not included in income, no charitable deduction
 - More beneficial than taking distribution then donating
 - Reduces AGI
 - No phase out
 - Limited to \$100,000 per year
 - Charitable rollovers count toward RMD

IRA Income or Assets



- Leaving IRA assets to charity
 - Use IRA bene designation form, not will
 - Very important because IRA income is IRD
 - IRD is taxed to beneficiary or estate at ordinary rates
 - Spouse has to sign off on the beneficiary form
 - Both charitable and non-charitable beneficiaries
 - the charitable beneficiary should be paid right away to allow other beneficiaries to use their life expectancies
 - Included in taxable estate
 - Estate tax charitable deduction applies

Using an IRA Instead of a Trust



- For donors who are concerned about the irrevocability of a charitable trust
- No administrative costs associated with trusts
- Can be used to simulate the effects of a
 - CLT by donating the distributions to charity
 - CRT by designating a charity as beneficiary
- Flexible based upon needs of the donor
- No guarantees for the charity

Using an IRA Instead of a Trust



- Simulating the effects of a CLT
 - Take distributions and donate or direct trustee to transfer directly to charity
 - Subject to regular income tax (but not NIIT)
 - Charitable income tax deduction taken
 - Net effect is same as trust without administration costs
 - Over age 70 ½ use charitable rollover to donate RMD
 - Under age 59 ½ use substantially equal payments
 - Funds remain in donor's hands if needed
 - Donor can switch charities each year if desired

Using an IRA Instead of a Trust



- Simulating the effects of a CRT
 - Designate charity as IRA beneficiary
 - Use IRA bene designation form, not will
 - Avoids generating IRD taxed to estate at ordinary rates
 - Estate tax deduction for charitable portion
 - Donor takes RMD, effectively a unitrust amount
- Funds remain in donor's hands if needed
- Donor can switch charities up to date of death

Private Foundations

- Charitable organization supported by a single source (often controlled by the donor also)
- Larger creation costs and effort than a trust
 - Drafting documents
 - IRS application for exempt status
- Administration costs
- Tax filing requirements – 990-PF
- 5% distribution requirement to maintain status
- Can be operating or non-operating

Private Foundations

- Taxes applicable to private foundations
 - Excise tax on net investment income
 - All private foundations are subject to this
 - Only tax a well-administered foundation should pay
 - Special rate if distribution ratio meets test
 - Penalty tax for failure to make distributions (non-operating only)
 - Tax is 30% of distribution shortfall
 - Distributions must be to qualified recipients
 - Tax on unrelated business taxable income (UBTI)
 - Excise taxes on certain prohibited activities

Donor Advised Funds

- Accounts offered by charitable organizations that allow donors to advise, but not dictate, how the funds will be invested or used
- Community foundation is an example
- Charitable organization has possession and control of the assets
- Deduction at time of donation to the fund
- Special reporting requirements for charity operating the donor advised funds

Closing Thoughts

- Planned charitable giving is an integral part of financial and estate planning
- Many plans can be of benefit to donor as well
- The same thought processes apply to charitable giving as to all financial plans
 - Determining goals and how they can best be met
 - Different plans for different time horizons and needs
- Charitable giving plans like other financial plans are personal as well as financial

Questions?



Please use the
Chat Pane
to submit your
questions.

Contact



Louise Clayton-Kastenholz, CPA
Manager, Estate and Trust Taxation

PBMares, LLP
434 McLaws Circle, Suite 201
Williamsburg, VA 23185
Phone: (757) 229-7180, x6242
LClayton-Kastenholz@pbmares.com

Mark Your Calendars



Join PB Mares for the last of our three-part
Not-For-Profit Learning Series!

#3: A Board Member's Guide to FASB Changes
November 2, 2016, 10 – 11:00 am EST

Visit www.pbmares.com/events to register!