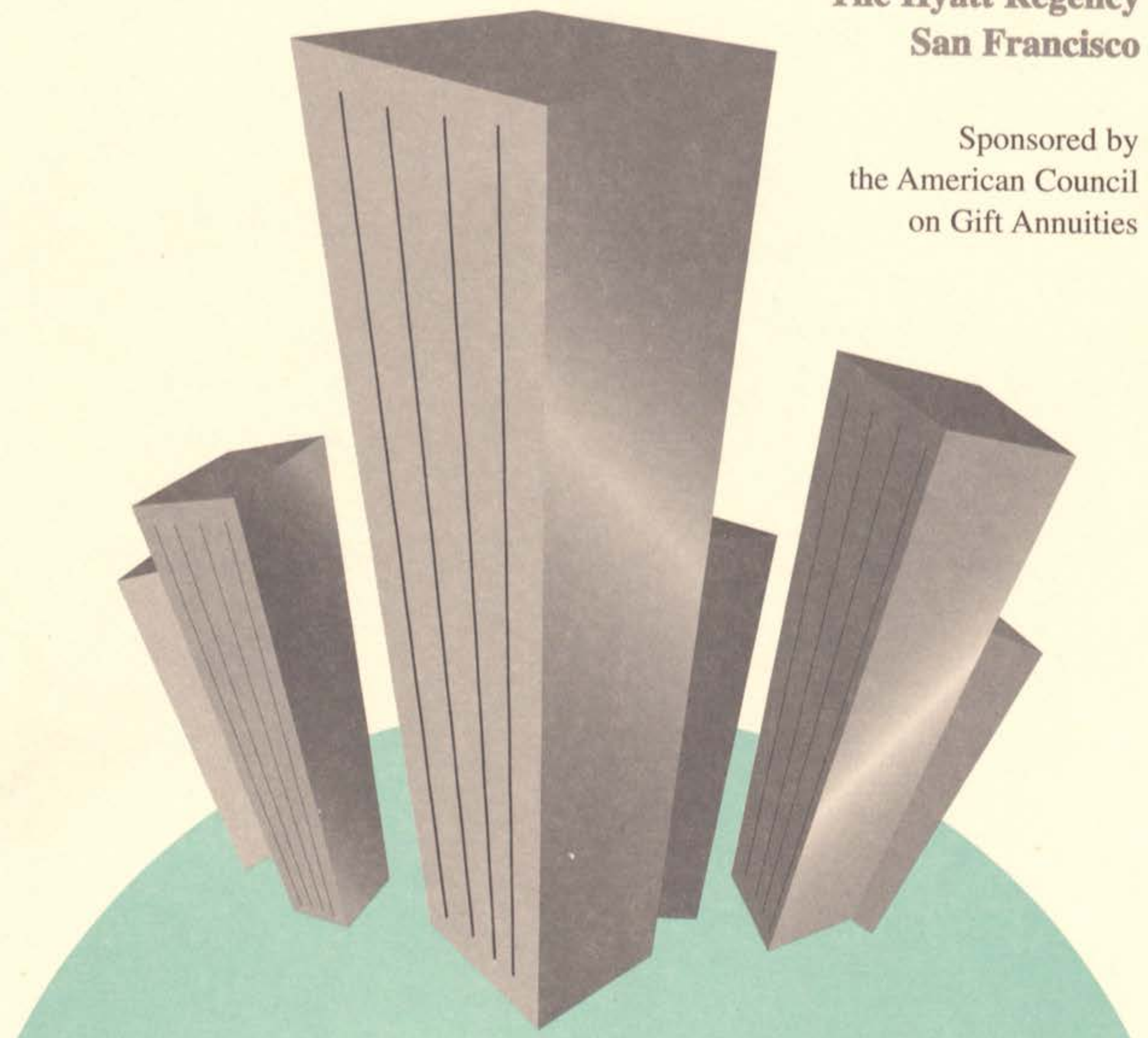
Golden Opportunities

22ND CONFERENCE ON GIFT ANNUITIES

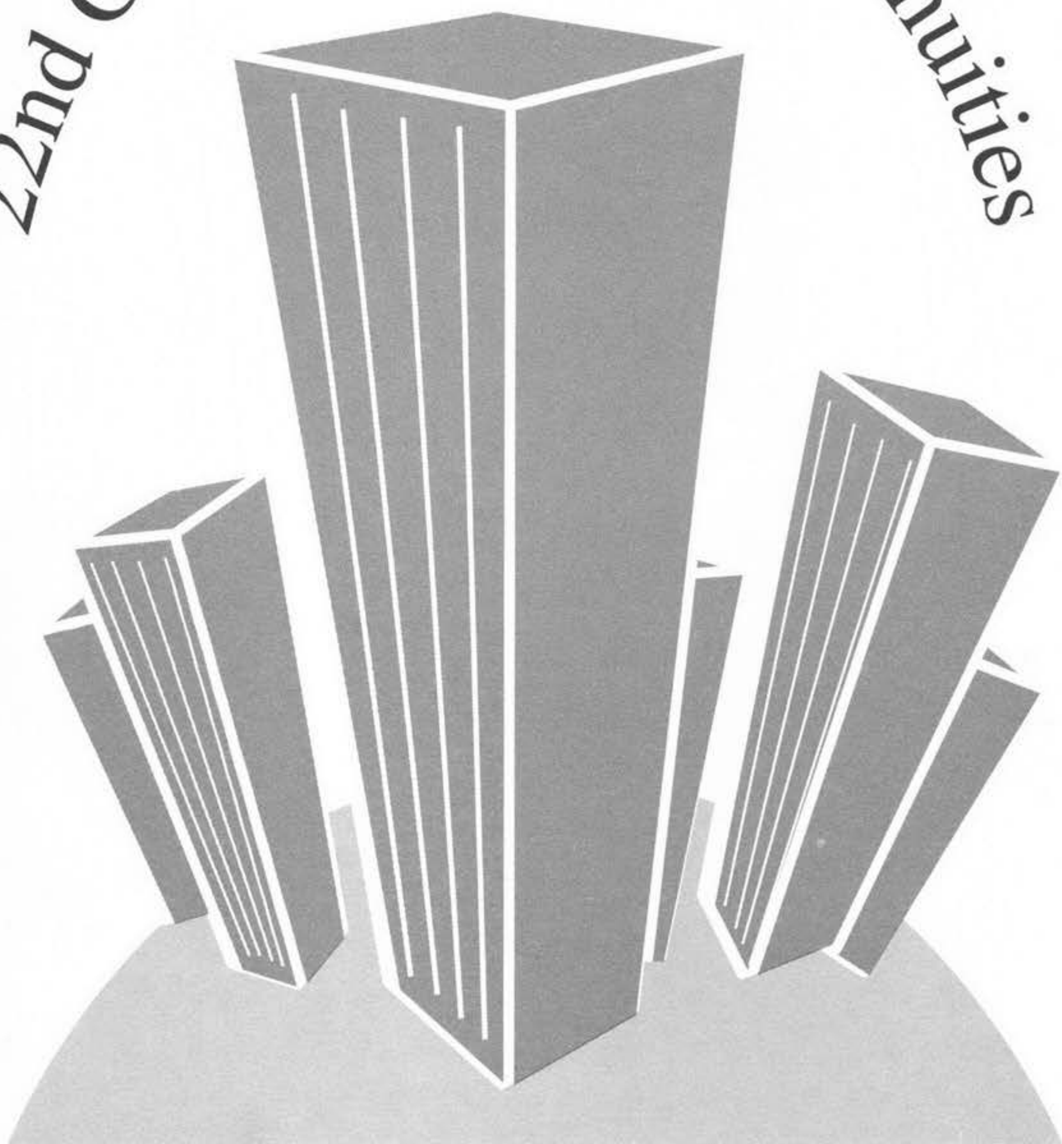
May 3-5, 1995

The Hyatt Regency
San Francisco

Sponsored by
the American Council
on Gift Annuities



22nd Conference on Gift Annuities



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the American Council on Gift Annuities

May 3-5, 1995

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The American Council on Gift Annuities

✱ **CHAIRMAN**
Tal Roberts, *Executive Vice President, Baptist Foundation of Texas*

✱ **VICE CHAIRMAN**
Clinton A. Schroeder, *Principal, Gray, Plant, Mooty, Mooty & Bennett*

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Frank D. Minton, *President, Planned Giving Services*

John D. Ordway, *Executive Vice President, The Pension Boards, United Church of Christ*

Eugene L. Wilson, *Director of Program Finance, American Leprosy Missions, Inc.*

✱ **ADVISORY MEMBERS**

A. Gordon Nelson, *Canadian Association on Charitable Gift Annuities*

James B. Potter, *President, Planned Giving Resources*

✱ **ACTUARY**
Michael Mudry, *Hay/Huggins Company Inc.*

✱ **COUNSEL**
Conrad Teitell, *Prerau & Teitell*

✱ **HONORARY MEMBERS**

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William E. Jarvis, *American Baptist Foreign Missionary Society*

David E. Johnson, *St. Olaf College*

Roland C. Matthies, *Wittenberg University*

Darold H. Morgan, *Annuity Board, Southern Baptist Convention*

Chester A. Myrom, *Evangelical Lutheran Church in America*

CONFERENCE AGENDA

❖ *Wednesday, May 3*

Noon - 6:00 p.m.	**Registration** • MARKET STREET FOYER
3:00 p.m.	**Exhibits Open** • GRAND BALLROM FOYER
5:15 - 6:00 p.m.	**Orientation for Newcomers** • BAYVIEW A & B
6:00 p.m.	**Dinner** • GRAND BALLROOM
8:00 - 9:00 p.m.	**PLENARY SESSION** • PACIFIC CONCOURSE *Trends in Planned Giving* -- **Robert F. Sharpe, Jr.**

❖ *Thursday, May 4*

	Breakfast on your own *Express Breakfast Available* • ATRIUM LEVEL
8:30 - 10:00 a.m.	**PLENARY SESSION** • GRAND BALLROOM *Welcome and Invocation* -- Tal Roberts *Keynote Address* -- Robert T. Parry *Update on State Regulation of Gift Annuities* -- James B. Potter
10:00 - 10:30 a.m.	**Break in Exhibit Area** • GRAND BALLROOM FOYER
10:30 - 11:45 a.m.	**BREAKOUT SESSIONS** *Charitable Gift Annuities* • W. Earl Taylor • BAYVIEW A *Charitable Remainder Trusts* • Robert L. Coffman • MARINA *Investment of Gift Annuity Funds* • Lindsay L. Lapole • BAYVIEW B *Investment of CRT, CLT and PIF Fund Assets* • J. Scott Kaspick • SEACLIFF C *Management of Real Estate Gifts* • Lynda S. Moerschbaecher • REGENCY A&B *Identifying Donors of Planned Gifts* • Jonathan R. Heintzelman • PACIFIC CONCOURSE L&M *Materials and Techniques That Appeal to Your Donors* • Ronald E. Sapp • PACIFIC CONCOURSE N&O *Contribution of Retirement Funds* • Robert E. Harding • GARDEN A&B *Creative Applications of Net Income Unitrusts* • Jonathan G. Tidd • SEACLIFF B *Gift Options with Personal Residences* • André R. Donikian • SEACLIFF A *Filing and Reporting Requirements in States that Regulate Gift Annuities* • James B. Potter and Clinton A. Schroeder • SEACLIFF D
Noon - 1:30 p.m.	**Lunch** • GRAND BALLROOM

1:30 - 2:45 p.m.	**BREAKOUT SESSIONS (10:30 a.m. topics repeated)** • SAME ROOMS AS 10:30 A.M.
2:45 - 3:15 p.m.	**Break in Exhibit Area** • GRAND BALLROOM FOYER
3:15 - 4:30 p.m.	**PLENARY SESSION** • GRAND BALLROOM *Reports --* Frank Minton Michael Mudry
4:30 p.m.	**Dinner on your own**
7:30 - 8:30 p.m.	**OPTIONAL SESSION** • GARDEN A&B *Update on Canada* -- Gordon Nelson

❖ *Friday, May 5*

	Breakfast on your own *Express Breakfast Available* • ATRIUM LEVEL
8:30 - 9:15 a.m.	**PLENARY SESSION** • GRAND BALLROOM *Announcements and Resolutions*
9:30 - 10:45 a.m.	**BREAKOUT SESSIONS** *Pooled Income Funds* • Marc Carmichael • SEACLIFF B *Charitable Lead Trusts* • Carolyn C. Clark • SEACLIFF C *Bequests and Other Revocable Gifts* • Ellen G. Estes • BAYVIEW B *Recording, Reporting and Substantiating Planned Gifts* • Tim A. Jones • PACIFIC CONCOURSE L&M *Fiduciary Issues for Charitable Organizations* • David W. Newman • BAYVIEW A *Practicing Good Stewardship* • Stewart J. Crook • SEACLIFF A *The Roles of Gift Planners and Professional Advisors -- Who Does What?* • David M. Benson • PACIFIC CONCOURSE N&O *Gifts of Closely Held Stock and Other Business Interests* • Terry L. Simmons • GARDEN A&B *Gifts of Personal Property, Mineral Rights, Crops, Royalties* • Carolyn M. Osteen • SEACLIFF D *Filing and Reporting Requirements in States that Regulate Gift Annuities* • James B. Potter and Clinton A. Schroeder • MARINA
10:45 - 11:15 a.m.	**Break in Exhibit Area** • GRAND BALLROOM FOYER
11:15 a.m. - 12:30 p.m.	**BREAKOUT SESSIONS (9:30 a.m. topics repeated)** • SAME ROOMS AS 9:30 A.M.
12:30 - 2:15 p.m.	**Closing Lunch** • GRAND BALLROOM *Address by* Conrad Teitell
2:15 p.m.	**Adjournment**

BREAKOUT SESSIONS

Learning tracks geared to your personal needs

◆ TRACK 1 -- Types of Planned Gifts

Charitable Gift Annuities ◆ W. Earl Taylor
Pooled Income Funds ◆ Marc Carmichael
Charitable Remainder Trusts ◆ Robert L. Coffman
Charitable Lead Trusts ◆ Carolyn C. Clark
Bequests and Other Revocable Gifts ◆ Ellen G. Estes

◆ TRACK 2 -- Administration of Planned Gifts

(New--especially for business officers)

Investment of Gift Annuity Funds ◆ Lindsay L. Lapole
Investment of Charitable Remainder, Lead Trust, and Pooled Income Fund Assets ◆ J. Scott Kaspick
Recording, Reporting and Substantiating Planned Gifts ◆ Tim A. Jones
Management of Real Estate Gifts ◆ Lynda S. Moerschbaecher
Fiduciary Issues of Charitable Organizations ◆ David W. Newman

◆ TRACK 3 -- Donor Relations

Identifying Donors of Planned Gifts ◆ Jonathan R. Heintzelman
Materials and Techniques That Appeal to Your Donors ◆ Ronald E. Sapp
Practicing Good Stewardship ◆ Stewart J. Crook
The Roles of Gift Planners and Professional Advisors--Who Does What? ◆ David M. Benson

◆ TRACK 4 -- Gift Planning

Contribution of Retirement Funds ◆ Robert E. Harding
Gifts of Closely Held Stock and Other Business Interests ◆ Terry L. Simmons
Gifts of Personal Property, Mineral Rights, Crops, Royalties ◆ Carolyn M. Osteen
Creative Applications of Net Income Unitrusts ◆ Jonathan G. Tidd
Gift Options with Personal Residences ◆ André R. Donikian

◆ SPECIAL TRACK -- State Regulations

Filing and Reporting Requirements in States that Regulate Gift Annuities ◆ James B. Potter and Clinton A. Schroeder

CONFERENCE SPEAKERS

K. Baerwald

D. Benson

M. Carmichael

C. Clark

KATHRYN E. BAERWALD

In 1988, Ms. Baerwald accepted her current position of Vice President and Associate General Counsel for the United Way of America. Prior to this, she served for six years as General Secretary for the American Lutheran Church. She is a member of the Virginia Bar, District of Columbia Bar and American Bar Associations. Ms. Baerwald is serving on the Board of Directors for the Lutheran World Federation, located in Switzerland.

DAVID M. BENSON

Mr. Benson is the President of David Benson and Associates which specializes in matters of estate planning and philanthropy. Mr. Benson previously served as Director of Development at Concordia College in Moorhead, Minnesota, and as a private consultant with various non-profit groups. Mr. Benson is a member of many professional organizations, including the National Society of Fundraising Executives and the National Committee on Planned Giving. He has presented numerous seminars and workshops on estate planning and deferred charitable giving.

MARC CARMICHAEL

Marc Carmichael has been Director of Seminars for the Chicago area R&R Newkirk Company since 1976. R&R Newkirk provides planned gift training and promotional literature to colleges, health organizations, and other institutions. Mr. Carmichael is a member of the Indiana State Bar Association, the Chicago Planned Giving Council, and the Board of Directors of the National Committee on Planned Giving. He has written extensively on the tax aspects of charitable giving and often makes presentations.

CAROLYN C. CLARK

Ms. Clark is a partner with the New York law firm of Milbank, Tweed, Hadley & McCloy where she heads the firm's Nonprofit Organization Practice Group. For twenty-six years, she has specialized in estate planning, trust and estate administration and in advising charitable organizations. She is a member of the American Law Institute and the New York and American Bar Foundation, and is a Fellow of the American College of Trust and Estate Counsel. She is a frequent speaker on legal issues of importance to non-profits.

CONFERENCE SPEAKERS

R. Coffman

S. Crook

A. Donikian

E. Estes

ROBERT L. COFFMAN
Robert Coffman has been with Anderson University for a total of fifteen years. Since 1987, he has served as Executive Director and Counsel for Development. Mr. Coffman previously served as Assistant Vice President of Pentera, Inc., a national planned giving consulting firm. He is a board member of the American Council on Gift Annuities and was a founding member of the Planned Giving Group of Indiana.

STEWART J. CROOK
Mr. Crook is the Director of Trust Services for the Southern Union Conference of Seventh-day Adventists, an administrative arm of the church which serves eight southeastern states. In this role he supervises continuing education and consults on development, charitable giving, and estate planning. He lectures at numerous seminars on the subjects of stewardship, charitable giving and estate planning. He is past President of the Georgia Planned Giving Council and serves on the Board of Directors of the National Council on Planned Giving.

ANDRÉ R. DONIKIAN
Founder and President of Pentera, Inc. in Indiana, Mr. Donikian manages a full-service planned giving consulting firm. In this role, he has served as an advisor to more than 300 charities and educational institutions throughout the United States. An attorney and member of the New York Bar, he also serves on the Board of Directors of the Planned Giving Group of Indiana.

ELLEN G. ESTES
Ms. Estes founded the firm of Estes Associates to provide fund raising consulting services to non-profit organizations nationwide. She has worked as a tax attorney and has experience in estate planning as well as non-profit development. In addition to consulting, She specializes in presenting seminars designed to provide the basics on how to establish, market and administer successful planned giving programs.

CONFERENCE SPEAKERS

R. Harding

J. Heintzelman

T. Jones

J. S. Kaspick

ROBERT E. HARDING

Since 1989, Mr. Harding has been a Principal at Gray, Plant, Mooty law firm. Over the last twelve years of practice, he has focused exclusively on charitable gift planning. As a balance to his legal practice, he trains for cross country ski racing and writes poetry.

JONATHAN R. HEINTZELMAN

Mr. Heintzelman serves as Assistant Vice President for University Development and Director of Planned and Major Gifts at Northwestern University. Before joining Northwestern, he spent several years in private law practice in the area of estate planning and administration. In 1993, he was recognized as the "Planned Giving Professional of the Year" by *Planned Giving Today* magazine and was elected to the Board of Directors of the American Council on Gift Annuities in 1994. He is a frequent speaker at conferences and has written several articles on marketing planned gifts.

TIMOTHY A. JONES

A licensed CPA, Mr. Jones serves as Treasurer and Assistant Vice President of the University of Colorado Foundation, Inc. Before joining the Foundation in 1989, he was Assistant Treasurer at the Kansas University Endowment Association. He also worked in public accounting for Deloitte, Haskins and Sells.

J. SCOTT KASPICK

As Managing Director of Kaspick & Company, J. Scott Kaspick has ten years of experience in managing endowment assets and various forms of income funds. From 1983-1989, he held the position of Associate Treasurer at Stanford University. In this role, he developed and implemented systems for managing the University's $150 million life income fund program. Mr. Kaspick has been a frequent speaker at conferences addressing financial issues related to planned gifts.

CONFERENCE SPEAKERS


L. Lapole


B. Mangone


F. Minton


L. Moerschbaecher

LINDSAY L. LAPOLE
Mr. Lapole has served in charitable fundraising work for over twenty-five years. Since August of 1986, he has served as the Territorial Planned Giving Director of The Salvation Army, southern territory, and is responsible for the management of the Army's Planned Giving Program in the fifteen southeastern states. He is a frequent speaker and lecturer on topics related to planned giving and fundraising management. He serves as Chairman of the National Planned Giving Consultants Committee of the Salvation Army.

BETSY A. MANGONE
Ms. Mangone is a Vice President of the University of Colorado Foundation, and previously served as Vice President of the Office of Gift and Estate Planning for the University's Foundation. She also serves as a board member for the American Council on Gift Annuities and is a past President of the National Committee on Planned Giving. She assists several non-profit organizations across the country as a trainer and consultant and is a frequent speaker at seminars.

FRANK MINTON
Mr. Minton is President of Planned Giving Services, Inc (Seattle, Washington) a planned giving consulting firm serving clients in the United States and Canada. He has also served as Senior Estate Planner in Northwestern University's planned giving program and as Director of Planned Giving for the University of Washington. Mr. Minton is a past President and Conference Chair of the National Committee on Planned Giving (NCPG) and is a past recipient of NCPG's Distinguished Service Award. Mr. Minton is the co-author of *Planned Giving for Canadians*.

LYNDA S. MOERSCHBAECHER
A well-known consultant and lawyer in San Francisco, Ms. Moerschbaecher speaks and writes frequently on estate planning and charitable gifts. She is past President of the San Francisco Estate Planning Council, has served with various financial and law related groups and is a publisher of *Charitable Gift Planning News*. She is also a member of several aviation organizations.

CONFERENCE SPEAKERS

M. Mudry

G. Nelson

D. W. Newman

C. Osteen

MICHAEL MUDRY
Mr. Mudry is the consulting actuary and Senior Vice President at Hay/Huggins Company, Inc. He specializes in the benefit plans of religious denominations and various forms of deferred charitable giving. He is a Fellow of the Society of Actuaries and the Conference of Consulting Actuaries and is actuary and ex officio Director for the American Council on Gift Annuities.

GORDON NELSON
Mr. Nelson is the current Director of Planned Giving at the Christian Blind Mission International in Canada. He is the past Chairman of the Canadian Association on Charitable Gift Annuities and continues to serve on the Association's Executive Committee. He currently serves on the American Council on Gift Annuities Board as a Canadian representative. Over the last fifteen years, he worked for two charitable organizations that aid developing nations.

DAVID WHEELER NEWMAN
In 1981, Mr. Newman joined Mitchell, Silberberg & Knupp and has since been made partner in the Tax Department. In his practice he works primarily with tax-exempt organizations on charitable giving with a special emphasis on fundraising programs. Through speaking and writing for charitable sector groups, he has become well known in California for his expertise in this area. He makes frequent presentations to the board members, staff and support groups of various organizations.

CAROLYN M. OSTEEN
Mrs. Osteen is a partner of the Boston law firm of Ropes & Gray and is a member of its Tax Department. She works primarily with tax exempt organizations, including universities and hospitals. She is immediate past Chair of the Exempt Organizations Committee of the Boston Bar Association and has served with other professional organizations. She speaks regularly on issues of charitable giving and tax issues. She works in a volunteer capacity with various non-profit organizations.

CONFERENCE SPEAKERS

R. Parry

J. Potter

R. Sapp

C. Schroeder

ROBERT T. PARRY
In February, 1986, Mr. Parry took office as the tenth Chief Executive of the Twelfth District Federal Reserve Bank at San Francisco. He is currently in his second term. In 1994, he served as a voting member of the Federal Open Market Committee. Mr. Parry previously held the position of Executive Vice President and Chief Economist of Security Pacific Corporation and its principal subsidiary, Security Pacific National Bank. He is a past President of the National Association of Business Economists and has served on various boards including the Boy Scouts of America and the United Way.

JAMES B. POTTER
After twenty-one years as a planned giving officer for the United Presbyterian Church Foundation and the American Lung Association, Mr. Potter went into full time planned giving consulting in 1991. He now serves over forty charities nationwide, helping to develop and administer planned gifts. He serves on the Board of the American Council on Gift Annuities where he presently chairs the State Regulations Committee.

RONALD E. SAPP
Mr. Sapp began working at Johns Hopkins University in 1967 with a background in corporate pension and annuity systems. In 1982, he assumed his present position as Director of Planned Giving. Mr. Sapp served as the National Committee on Planned Giving President in 1994. In 1992, he was selected "Planned Giving Professional of the Year" by the Editorial Advisory Board of *Planned Giving Today*. He is a founding member and past President of the Chesapeake Planned Giving Council.

CLINTON A. SCHROEDER
Mr. Schroeder is a principal in the law firm of Gray, Plant, Mooty & Mooty & Bennett in Minneapolis. He is former President of the Minnesota State Bar Association and is a Fellow of the American Bar Foundation. He is also a member and Vice Chair of the American Council on Gift Annuities. Mr. Schroeder is a regular lecturer at seminars regarding taxation and charitable gifts sponsored by various non-profit organizations.

CONFERENCE SPEAKERS

R. Sharpe, Jr.

T. Simmons

W.E. Taylor

C. Teitell

ROBERT F. SHARPE, JR.
Mr. Sharpe is President of Robert F. Sharpe & Company, Inc., located in Memphis, Tennessee. He previously practiced law, specializing in income, estate and gift taxation. He writes and speaks widely on estate and gift planning topics.

TERRY L. SIMMONS
Mr. Simmons is Vice President and General Counsel of the Baptist Foundation of Texas where he heads the Trust and Legal Division. The Baptist Foundation currently administers over $918 million in endowment and trust assets. Mr. Simmons was named the "1994 Planned Giving Professional of the Year" by *Planned Giving Today*. He is past President of the National Committee on Planned Giving and has spoken internationally on planned giving.

W. EARL TAYLOR
Mr. Taylor is currently Executive Director of the Omaha Community Foundation. He has over thirty years of fundraising experience and a strong background in the non-profit world. He is President of the Planned Giving Officers of Nebraska.

CONRAD TEITELL
Mr. Teitell is a partner in Prerau & Teitell in White Plains, New York and Of Counsel to the West Coast and Washington D.C. law firm, Perkins Coie. He is an adjunct visiting professor at the University of Miami Law School. Mr. Teitell lectures and writes on taxes, estate planning and philanthropy. He is author of the five-volume set *Philanthropy and Taxation* and is editor of *Taxwise Giving*. Mr. Teitell is a recipient of the National Committee on Planned Giving's Distinguished Service Award.

JONATHAN G. TIDD
Mr. Tidd has his own law practice in Connecticut and works with charitable organizations in the area of gift planning. Formerly, he was Director of Planned Giving for New York University. His articles on charitable gift planning have appeared in numerous professional publications including: *The Journal of Taxation, Estate Planning,* and *TAXES*.

22nd Conference

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- Kaspick & Company
  Boston, Massachusetts
  MORNING REFRESHMENT BREAK
  THURSDAY, MAY 4

- Loomis Sayles & Company L.P.
  Boston, Massachusetts
  MORNING REFRESHMENT BREAK
  FRIDAY, MAY 5

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BOOTH 7

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Oakland, California
BOOTH 11 & 12

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Roanoke, Virginia
BOOTH 10

22nd Conference on Gift Annuities
Golden Opportunities
May 3-5, 1995

Acknowledgements

ACGA Chairman

* CHAIRMAN- Tal Roberts

Mr. Roberts serves as the Executive Vice President and Chief Operating Officer of the Baptist Foundation of Texas where he has worked for the Baptist Foundation since 1969. Previous to that, he worked for three years as a special agent for the Federal Bureau of Investigation. He holds both B.B.A. and L.L.B degrees from Baylor University, and is a member of the State Bar of Texas and the American Bar Association.

Appreciation is expressed to Tal for his excellent leadership of the ACGA.

ACGA Program Committee

* CHAIR- Frank Minton

* COMMITTEE MEMBERS-
  Kathryn Baerwald
  Robert Coffman
  Betsy Mangone
  Clinton Schroeder
  Tal Roberts- Ex Officio

ACGA Arrangements Committee

* CHAIR- Gerry Gunnin

Dr. Gunnin is the President of Children's Medical Foundation of Texas, the fundraising and fund-management affiliate of Children's Medical Center of Dallas. He is active in the Association for Healthcare Philanthropy. Prior to serving at Children's, he was a university professor and administrator for fifteen years. He earned baccalaureate and masters degrees at Baylor University and a Ph. D. at the University of Chicago.

* COMMITTEE MEMBERS-
  John Jacobs
  Richard James

Other

* CONFERENCE MANAGER-
  Beverly Judge,
  New York, NY

* CONFERENCE PREPARATIONS-
  Ileen Bray, Secretary
  American Council on Gift Annuities,
  Dallas, TX

* CONFERENCE PROCEEDINGS BOOK-
  Prepared by Laura Peters, Communications Specialist
  Planned Giving Services,
  Seattle, WA

Notes

(Eight pages of notes were provided in the workbook version of this publication distributed at the conference. These have been deleted in this version.)

The American Council on Gift Annuities

Conference

Speaker Papers

THE VIEWS EXPRESSED BY THE SPEAKER ARE THEIR PERSONAL OPINIONS AND DO NOT NECESSARILY REFLECT THE OPINIONS OF THE AMERICAN COUNCIL ON GIFT ANNUITIES.

THE ROLE OF GIFT PLANNERS AND PROFESSIONAL ADVISORS: WHO DOES WHAT?

Presented by David M. Benson
David Benson and Associates

Introduction —This presentation is made from the perspective of a gift planner. Gift planning is generally learned through trial and error. Most of the technical details, for example sections of the IRS code dealing with charitable gifts are well documented, but the process of working with the prospective donors and the allied professionals is not as readily available. This presentation is designed to help eliminate some of the common mistakes that are made, by discussing both the participants and the process. It explores not only areas of cooperation but also areas of prospective conflict that may arise within the framework of these working relationships. It is based upon personal experience in the field and should provide information that will be useful to novice and experienced gift planners and allied professionals.

WHAT'S IT ALL ABOUT?

Reason for Giving — The gift planner's primary responsibility is to discover and help develop a reason for giving. This may seem obvious but its importance is often overlooked. Many people are philanthropic and have a desire to give. It is important to understand how the gift celebrates the donor's charitable intent as well as their life. Individuals look at their philanthropic responsibility in the context of a wish to see that the charitable organization will be successful in its mission. They may hope to have an impact on society. For some, it is an opportunity to perpetuate a family name, for others, an opportunity to repay a debt or simply to create an opportunity to be recognized.

Gift planning provides a method of transforming "public social capital" (taxes) into "private social capital" (charitable contributions). People realize that a charitable gift reduces their tax liability. Within this context, it is important to identify both the intangible benefits and tax benefits. However, one must assume that inside every individual is the desire to generate a major gift, and the role of a gift planner is to unlock that desire--by showing the prospective donor how their gift can make a difference. The gift planner is in a position to provide an opportunity for the prospective donor to express his or her philanthropy and, in turn, provide a service to assist them and their advisors in making an informed decision. What most allied professionals fail to realize is that the desire to make the gift is a much more powerful motivating factor than the numbers. The numbers may create excitement, but the ability to accomplish a dream with a gift truly motivates implementation. That is why so few allied professionals are able to influence prospective donors to make gifts: they miss the point. It is a vision of what the future holds that often motivates the prospective donor. It involves the heart as well as the head. In order to be successful in securing a commitment from prospective donors, it is important to emphasize the philanthropic decision over the business decision. We must learn how to communicate in "human speak" and not "financial speak."

Worthiness to Receive Gift Support — The second major responsibility for the gift planner is to determine how their charitable organization exhibits (through mission and activities) its worthiness to receive gifts. Prospective donors have "needs" and charitable organizations have "opportunities" to help the prospective donors meet those needs. In the process of matching the charitable organization with the prospective donor, it is important to do the best job possible in matching the prospective donor's interest to the charitable organization's missions and goals. This also involves explaining donor motivations and goals to colleagues and other individuals involved. One must establish and maintain well-defined relationships within a charitable organization that will support the commitment of the donors. At the same time, the gift planner also needs to recognize the limitations and avoid any impropriety.

Relationships with Donors — There are several relationships that are important to develop and maintain. The first involves the relationship between gift planner and prospective donor. There needs to be a clear determination to avoid any undue pressure and influence. Anonymity must be respected and genuine assurances of confidentiality must be provided which correctly represents the charitable organization's positions, goals and limitations. The gift planner must work closely with allied professionals the prospective donor chooses to involve. A successful relationship is found in the long-term perspective and finding appropriate solutions to meet the prospective donor's needs. As a member of a team, the gift planner can provide the prospective donor with adequate information so that an informed decision might be made. It is very important that, at the time of presentation, the gift planner is included. The prospective donor is often willing to allow conversation with their allied professionals (even by appointment) because most prospective donors are interested in taking advantage of every opportunity. The relationship between the gift planner, the charitable organization, and the prospective donor is strengthened as the prospective donor begins to view the relationship as a mutually-beneficial partnership.

Relationship with Allied Professionals — Some of the specific concerns for the gift planner and the allied professions involve respecting each of the advisor's roles, involving appropriate advisors and recognizing when to call in specialized advisors. A major concern comes with the handling of inept advisors who are without adequate experience or knowledge. One also needs to ask whether or not to recommend advisors to a prospective donor and how to help them narrow the field. When making recommendations, it is helpful to suggest several names so that the prospective donor has an opportunity to choose.

A team approach that uses specific expertise is needed to implement planned gifts. While each allied professional may have an area of specialty, a team approach to gift planning is essential. It is important that the allied professionals get to know the purpose and personality of the charitable organization. They should become acquainted with its leaders and learn their concerns. It is best to work with experienced allied professionals who have established a reputation for expertise in the area. Chances for success are greatest when the allied professionals are truly committed to the prospective donor's needs and goals. Mutual respect grows as professionals working together discover one another's expertise and the special role they can play in assisting prospective donors with the gift planning process. They must distinguish between sharing of general information and the giving of specific advice to donors.

It is also important for the gift planner to look closely at how these allied professionals make their living. Disclosure of possible conflicts of interest and compensation issues is critical if the prospective donor is to make an informed decision. The allied professionals must remain actively involved with his or her client. In doing this, the gift planner will earn the advisor's respect. If the team is working well, creative problem-solving techniques can be developed to keep everyone happy. It produces a most gratifying result.

Nothing turns prospective donors off faster than a hard sell, and too many allied professionals do not know when to stop. The aggressiveness that brings them success with some clients may inhibit their success with the prospective donor. Allied professionals need to look at the gift planning area as one of special significance and real meaning. Some will find more satisfaction in working for a greater good.

Relationship with Heirs — Another area of concentration is the relationship between the gift planner and the prospective donor's heirs. While one must respect the prospective donor's wishes to involve or disregard children and others in their gift discussion, the process must be treated "globally" (i.e. take the time to consider the impact on the heirs as well as on the prospective donor and/or spouse). You need to be particularly careful when working with prospective donors who are ill, near death or possibly incompetent.

Percentage Giving and Multiple Charities — It is often helpful to discuss the possibility of apportioning an estate between both charity and family. For example, a prospective donor might ask: "Is it possible to give 10 percent of my estate to charity and the remaining 90 percent to my children? Is there a way to preserve or enlarge my family's portion of the estate by funding the charitable gift using dollars that would normally be used to pay the estate taxes?"

Gift planners must also recognize a prospective donor's wish to support multiple charities and be both an advocate and facilitator for such an eventuality. These actions will generate greater prospective donor interest and encourage flexibility and cooperation among all parties.

The Charitable Option — Presenting the charitable options is another of the gift planner's responsibilities. In a team approach on gift planning, the gift planner is central and often participates at every level of the process. (Remember, his or her most important asset is the ability to discover and develop.) It makes sense to build relationships with allied professionals who understand how to implement planned gifts and know the value of keeping the gift planner in the center of the process. One might liken the gift planner's role to the conductor of the symphony: though not an expert at every instrument, a good conductor knows every musician and precisely when to call upon each instrument in order to produce a harmonious result.

Gift planners should be generalists and understand income tax planning; estate tax planning; differences between a simple will, a living trust and numerous trust provisions; gift tax laws, current marketing trends; and investment policies; life insurance; and, most importantly, the needs, wants, goals and desires of the potential prospective donor. They need to understand how making a gift will impact the prospective donor's overall financial and estate plan.

Life Issues — Common life issues which concern many prospective donors involve education for children or grandchildren; retirement planning, including the psychological factors of retirement as well as the investment strategies during retirement; the disposition of unwanted real estate; health care planning, including Medicare, Medicaid, long-term care insurance, nursing home costs; planning for incapacitation which might involve revocable trusts or standby trusts, directives for powers of attorney to accommodate property management, health care, and living will provisions.

Family problems including divorce, multiple marriages, blended families, aged parents, long-term care needs, the concern for an impaired dependent child and children not competent to manage must be considered. There may also be concern regarding the transfer of wealth in terms of timing, taxes and amount. Some financial concerns that must be addressed include: income generation, asset management, management planning, education planning, financial and estate planning, and tax issues.

New life issues often present new opportunities to re-examine charitable options that might be available in the planning process.

MEMBERS OF THE TEAM

Accountant — The primary focus is taxes. These professionals focus on tax and financial planning and business issues. Concerns will involve "available" versus "allowable" deductions; the payer and the source of the tax; recapture and accelerated gain; and reporting responsibilities. Unstated concerns may involve the loss of management responsibilities, inexperience with compliance requirements or lack of familiarity with tax benefits. They are compensated on an hourly basis.

The accountant often enjoys the greatest level of client confidence. This may be attributable to a combination of long-term relationship and frequent meetings. Often, advice to consider new tax-planning strategies originates with the CPA. The accountant provides the tax perspective for the gift. They are responsible for preparation of the annual tax returns. They appreciate complete, timely documentation as well as projections for the future income potential from any deferred gifts. In most cases, they will want to see a complete analysis showing all the computations that were used to determine the charitable gift value, the basis on which the income projections are made and information regarding the types of income that will be received. The accountant may also have the least personal economic gain or loss from a charitable gift agreement, so they are potentially the most unbiased.

Attorney — The primary focus is to protect the prospective donor's interest and to prepare documents. Prospective donors frequently have different attorneys for different aspects of their personal and professional lives. The prospective donors may have a general family attorney who also acts as a liaison with the other attorneys who may specialize on estate planning or business and professional issues. They are compensated usually on an hourly basis and/or fees for documents drafted.

The attorney's role might include preparing the legal documents for an individual making a planned gift or it might involve reviewing documents prepared by a charitable organization's counsel. Estate planning attorneys specialize in the distribution of family wealth during the client's lifetime and at death. Some unstated issues include the attorney's concern for the loss of control, loss of professional revenue or professional exposure due to practicing in an unfamiliar area.

Each charitable organization should have its own attorney prepare documents or review documents drawn by the donor's counsel. Some prospective donors do not have attorneys, nor do they wish to, but simply depend upon the counsel of the institution to provide information. This is a very dangerous situation and, in rare instances, where one is unable to convince the donor to secure their own counsel, there should be a dual representation agreement signed by the prospective donor acknowledging that the attorney serves both as counsel for the institution as well as to the prospective donor.

Financial Planner — The primary focus is on product sales. The financial planner is interested in assisting the client by repositioning and investing assets. Their concern is for diversification, risk management, minimization of income taxes, inflation and cash flow. These professionals are paid through commissions, fees, or sometimes both. Charitable gift planning is a method, but not a goal, for most planners. It requires that the charitable alternative be considered in a comparative analysis to more traditional planning techniques.

A financial planner generally has a very broad knowledge of the client's assets and goals and, in most instances, has developed a close working relationship. Financial planners are attaining more prominence as more individuals seek one-stop planning and coordination for family needs. A financial planner will advise clients on planning to meet future family expenses, retirement income and making estate and gift transfers in the most cost-effective manner.

Commission-based financial planners usually do not want to "lose assets." Fee-based financial planners are generally more open to recommending charitable gift options as part of an overall plan.

Gift Planner — This professional's primary focus is to secure financial support for the charitable organizations they represent. The goal of a gift planner is to secure immediate and deferred gifts for their charitable organizations. The key to this process is to discover and develop the reasons and motivation for the gift. They must balance the prospective donor's personal and economic situation with the charitable organization's needs and priorities. The gift planner will not, in all cases, be aware of the full scope of the prospective donor's circumstances or the non-charitable planning techniques that have been or might be utilized. They are compensated by a salary from charitable organizations.

Gift planning will be affected by the charitable organization's willingness or ability to utilize specific gift techniques. Conflicts of interest may exist because of the gift planner's disclosure or undisclosed responsibilities to the prospective donor and the charitable organization. It is the role of the gift planner to outline the charitable options that might be appropriate and available. They are oftentimes an advocate for specific options or programs.

It is the gift planner's responsibility to see that the donor has independent counsel that will review the recommendations and options and protect their interests. The gift planner often works with the prospective donor to identify the key professionals and to see that they are involved appropriately.

Often the questions of who is advising the donor and in what capacity is raised. Is the agreement formal (by contractual agreement) or informal. When do these allied professionals enter the gift planning process? How are they brought into the process? What are the credentials of the allied professionals? What is the prospective donor's relationship with the allied professionals, and what is the prospective donor's expectation of both the allied professionals and the gift planner's involvement.

Life Underwriter — The primary focus is also on product sales. The life underwriter addresses liquidity requirements of the client and the heirs or beneficiaries of the client that may be required because of the client's death, disability, retirement or other change of circumstances. The favored solution is life insurance. The problem often is finding the cash flow to fund the premiums for the insurance. Like the financial planner, charitable gift planning is a method, not a goal, for most life underwriters. It requires that charitable alternatives be considered in a comparative analysis to more traditional planning techniques. They are compensated by commissions on the sale of products.

The life underwriter has the more personal, complete and, oftentimes, more consistent relationship with the client than many of the other allied professionals. The life underwriter is often involved with wealth replacement issues and has generally been involved in family protection, estate planning liquidity, small business transfer and, in many instances, may have been in the advisor's role for the greatest span of time.

The gift planner will find involvement with the life underwriter in (a) beneficiary changes naming the charitable organization as beneficiary, (b) gifting an existing policy making the charitable organization, the owner and beneficiary, (c) writing a new policy where the charitable organization becomes the owner and beneficiary, (d) writing wealth replacement policies, and (e) often the insurance professional is involved with other investment opportunities and will be interested in reinvestment issues as well.

Philanthropic Consultant — The primary focus is on assisting charities to maximize their planned gift potential. A consultant's compensation is often based on a flat fee for service and he or she may be directly involved with the gift planner in securing the gift. The consultant should not only have good technical knowledge, but will likely have the best perspective on the task of coordinating the team of allied professionals. A consultant will also have a perspective on the task of coordinating the gift planning effort through the use of volunteers.

Realtor — The primary focus is on the sale of real estate. The realtor is in an excellent position to identify potential donors and also suggest methods for making gifts. Working with a gift planner may be an effective way for a realtor to move forward the sale of a highly-appreciated piece of property using a charitable gift for part or all of the property.

They are compensated by commissions. In most instances, a transfer of a piece of real estate into a charitable trust allows the trustee to engage the realtor to sell the property on behalf of the trust.

Stockbroker — The primary focus is on the sale of stocks and bonds. The stockbroker is usually considered a professional wealth management advisor. A broad-based stockbroker is often focused on retirement issues and also on investment diversification to control taxable income. A number of the major brokerage houses now have trust units. They are involved in trust management as well as the reinvestment issues related to the transfer of highly-appreciated assets into charitable trusts. They are compensated by commissions based on the transactions related to financial products.

Trust Officer — The primary focus is principal under management. Professional trustees have dual responsibilities for administration and investment management. They are compensated based on the size of the trust under management as well as certain transactional fees, compliance, investment fees and commissions. Since business development requires new and increased trust principal, the primary focus is establishing irrevocable and revocable trusts. This may affect the recommendations for non-trust planning including gift annuities and outright gifts or bequests. It may also affect the recommendations related to self-trusteeship, trusteeship by the client's own professional advisors or trusteeship by the nonprofits.

The trust officer often has a generational relationship with the donor and is closely tied to concerns related to family wealth preservation and transfer. The trust officer often has a long-term relationship with the prospective donor and may provide advice beyond that of basic administration.

AREAS OF COOPERATION

Planning — Each discipline has a professional interest in discussing and analyzing charitable gift techniques as part of sound business, tax and estate planning. Charitable gift planning frequently requires an understanding of and sensitivity to multiple generations: grandparent, parent and child. A gift planner may avoid discussions with younger generations who may feel deprived of their inheritance; however, the gift planner is in a good position to address parental concerns about values, excessive wealth and work ethics. Attorneys often speak of dynasty planning or generation-skipping transfers through multiple generation trusts. Life underwriters work with the younger generation since they will be the natural beneficiaries of the liquidity planning but do not necessarily address parental concerns for passing wealth to younger generations. Accountants focusing on estate planning may share the same concerns of the attorney but do not spend much time or effort on the issues facing the younger generation.

Marketing — Professional groups will find joint marketing to be beneficial through third-party endorsements, cross-referrals, cost-sharing, shared expertise and an expanded prospect identification. Marketing through the network involves being a participant in seminars and helping to provide articles and copy for publications and other media. Marketing to the network involves participation in planned giving councils, speaking for professional education seminars and providing technical support.

Individual Gift Design — The gift planner and the allied professions are often involved in drafting and designing proposals. On some occasions, the allied professional may review and analyze the proposals submitted by others. At other times, they may be involved in closing the gift with the donor.

Implementation and Operation of a Gift Plan — Attorneys are involved in either drafting documents or in reviewing documents drafted by others. Independent trust departments or brokerage houses with trust divisions may be involved in the administration of planned gifts. A number of the allied professions would like to be involved with investment management.

AREAS OF CONFLICT

The Prospect — Whose prospect is it: the gift planner or the allied professional? Who has access to the prospective donor and who will be entitled to see the personal, family, and financial information regarding the prospective donor? Whose responsibility it is to follow-up and cultivate the prospective donor?

Investments — Conflicts often arise because of the economic motivation of the referral source. Some prospective donors have serious reservations about giving up control. Others can be coerced into retaining control because it might be in the best interest of the referral source. Some charitable organizations perceive that investment control also protects the donor relationship. On occasions where the investment control is dictated by the referral source, the trustee is often denied their fiduciary responsibility which can create additional problems.

Compensation — The code of ethics for gift planners suggests that finders fees and commission-based fundraising is unethical and raises both moral and economic questions. Differences in the method or amount of compensation can lead to jealousy, competitiveness and greed. Methods of compensation for the various parties must be understood. In virtually all cases, the gift planner is in a salaried position; whereas most of the other allied professions derive their income on a fee-basis or a commission. To be able to work together and to allow the allied professional to continue involvement with the donor and receive reasonable compensation is the ultimate goal.

Control of Assets — Will the allied professionals lose control or influence over the prospective donor's wealth? Is the allied professional focused on the benefits to the prospective donors, the heirs or to the charitable organization?

Understanding Planned Giving — The marketing strategy provides the prospective donor with an opportunity to become aware of the charitable options. The solicitation process itself may require more time than the allied professional normally experiences. The failure to secure the gift for a charitable cause is discounted, assuming that the decision will ultimately be made on financial basis primarily. The steps necessary to establish, execute and implement a planned gift are time-consuming but worth it. The only acceptable goal is to create a win-win-win situation: good for the donors, good for the family and good for the recipient charity.

MARKETING

Prospective Donor Seminars — Choose topics that appeal to the target audience. A gift planner may wish to conduct a program that focuses on charitable planning techniques while the allied professionals may wish to expand discussion to traditional planning concepts. If the program is marketed as a financial planning seminar but addresses only charitable trusts and wealth replacement, then the audience may be disappointed. It is important that one's objectives be clear and that the agenda is appropriate.

Look for speakers with recognized experience in the field with public-speaking ability. Complement this with someone who admirably represents the goals of the charitable organization. Implied endorsement by the charitable organization makes a speaking engagement attractive to allied professionals but also carries a risk to the charitable organization if the speaker is unqualified, poorly prepared or fails to perform as promoted.

Know the audience and make the seminar specific to them. Having a general seminar that tries to appeal to everyone, seldom will meet the needs of a majority of the participants. If most of the audience shares some common concerns, it will encourage the participants to ask questions that they might otherwise be reluctant to ask.

It is always preferable to specifically invite an individual to a particular event. If possible, professionals or key volunteers should do a phone follow-up or personally invite selected individuals to be their guest for the seminar.

Sponsorship suggests endorsement of the participants. It also controls or influences the content of the program and the selection of speakers. Financial underwriting may be provided by the allied professions and can help spread the cost between several organizations that could benefit from the marketing. But also has the tendency to dilute the control over the speakers and their content.

Follow-up is a key to success in all marketing programs. Who has access to the list of attendees and who is responsible for initiating follow-up are key issues that must be resolved prior to the program.

Professional Education Seminars — The purpose of these programs is to enhance the education and training of the allied professionals. Because of the need to maintain proficiency in the field, such programs are widely attended.

The problem is to determine the content of the seminars. Some seminars may be designed for the inexperienced and will introduce new ideas; others may be very advanced, even for experienced allied professionals. Each objective has its own merits, but objectives must be clear. Allied professionals will not be interested in introductory courses. On the other hand, many of the allied professionals do not have experience or expertise in charitable gift planning and need the basic introductory information. It is also well to note that the gift planner might be most interested in marketing, whereas the allied professionals could be more interested in technical tax issues, drafting problems or operational and compliance considerations.

Technical Support — The gift planner often has more technical expertise and substantially more experience than many members of the allied professions. This shared experience can support an expanded market; however, it may raise some ethical, legal and financial concerns. Does the gift planner's charitable organization expect to participate in the ultimate gift, even if the prospective donor has little or no interest in the charitable organization? Will the gift planner be compensated for services provided to the allied professions? If so, is it independent of the gift planner's employment and is the gift planner clear with both his or her charitable organization and the prospective donors? What is the exposure of the charitable organization if the advice rendered by the gift planner is incorrect, inaccurate or incomplete? The gift planner is often requested to provide a plan before ever meeting the prospective donor. The prospective donor's goals and circumstances may be different than what was presented by the prospective donor's advisor. Planning should be done only after careful consideration and consultation with all of the parties involved.

THE ART OF GIFT PLANNING

Prospective Donor Identification — Prospective donors will come from a variety of sources. They may develop through an effort of the gift planner or as a result of discussion with one of the prospective donor's professional advisors. The prospective donor could also self-identify based on information received from a public seminar sponsored by a combination of charitable organizations and/or allied professionals.

Education — The initial responsibility is to educate both the prospective donor and the allied professional on the concepts that would allow for a deferred gift as part of an overall estate plan. The first step usually involves sharing some of the basic concepts with the prospective donor to try and determine which of the charitable options might be of interest to them. One of the key steps in developing the concept is the ability to listen. Most all of those involved in the gift planning process are there because of their ability to communicate; however, their ability to listen to the prospective donor is often a more critical skill. Listening carefully to questions and comments from prospective donors can be very helpful in developing the proper gift vehicle to accomplish the goals of the prospective donor. The next step may require gathering individual information and preparing a more detailed analysis.

The gift planner or the allied professional may use one of the deferred giving software programs to develop a model that outlines the concept being considered. If the concept is of interest to the donor, the model can be modified with actual figures for the basis and fair market value of the assets. This may be the time to prepare a more complete proposal. Some of the software programs also have provisions for a more detailed explanation that would be valuable to the allied professionals. In the case of some of the more complex gifts, it may be helpful to model on one page the plans under consideration and how they would relate to the overall estate plan as it currently exists. At this point you wish to inform the prospective donors of the options available, how they work, and the benefits to themselves, their families and to the charitable organizations. This will enable the allied professionals to begin evaluating and/or executing the desired programs more efficiently.

Designing the Plan — Proposals to be considered may be designed by several of the allied professionals. Whomever designs the plan will be influenced by his or her technical expertise, how they are compensated and the objectives of the prospective donor. If the plan is originated by the gift planner, it will more than likely be based on the charitable organization's preferred or authorized gift program. However, from the donor's perspective, there may be a better plan requiring an alternate trustee to handle the gift. Most of the allied professions that are involved in trust administration would prefer that the trust be administered by them. Most charitable organizations that are in a position to serve as trustees would normally recommend themselves to serve as trustee. Ultimately, the donor decides whether they wish to have a self-directed trust, a trust administered by the charitable organization or one administered by an institutional trustee.

If the prospective donor is comfortable with the value of the assets being considered for gifting, then it becomes appropriate to draw up a sample document along with a memorandum of explanation. This document may be developed by the attorneys for the institution or they may come from the prospective donor's attorney. If the document is prepared by the charitable organization's attorney, copies should be provided for the prospective donor so that they might discuss it with their own legal counsel and other allied professionals as appropriate. This may also be an excellent opportunity for the prospective donor to discuss the plan with their family. The prospective donor should have sufficient information to consult with their normal allied professionals to have them review the recommendation. The allied professionals should then be able to advise them on an appropriate course of action. If there are wealth replacement objectives as part of the overall plan, the life underwriter or financial planner should be involved to determine that the program will ultimately provide the wealth replacement assets. If the charitable trust is to be administered by a bank or trust department, they should also have the opportunity to review the documents, seeing to it that the conditions and provisions of the instrument are acceptable.

Drafting the Documents — Many charitable organizations have prepared "sample" instruments to be shared with prospective donors. Other institutions have their own counsel who prepare customized documents for each situation. If the charitable organizations have "sample" instruments, the question is whether or not the draft is legally sufficient to meet both state and federal requirements. A more basic question is whether or not that instrument is properly designed for the immediate and long-term needs of the donor. In some cases, the local attorneys will resent the "free" legal work offered by the charitable organization when they are capable of providing technical support to their professional colleagues and clients. Referrals to other professionals provide a benefit to the institution, assuming those who will do the drafting are knowledgeable and experienced. They may protect the charitable organization from exposure if a "sample" document proves to be ineffective or inappropriate.

Once all parties have had a chance to review and make recommendations for revisions, final documents should be drawn and executed. Asset may then be transferred to fund the trust. Drawing or reviewing the documents will involve the prospective donor's attorney. The transfer of assets will involve the appropriate allied professional depending upon the assets to be transferred. This process is often unfamiliar to the donor and sometimes also to the allied professionals.

Through this process, there are responsibilities to the prospective donor. The first responsibility is to disclose any conflicts of interest. If the allied professionals involved are representing anyone other than the prospective donor, that should be noted. They should, for example, disclose prospective conflicts with other charitable organizations, financial planning firms, accounting firms, banks or trust companies. The allied professionals may have a dual role as a member of the charitable organization's board or development committee. In the situation where an allied professional is a paid consultant to the charitable organization, is there an agreed-upon compensation agreement if the gift is completed? Likewise, if an attorney represents both the institution and the donor, there should be a disclosure statement signed acknowledging the dual representation. The prospect should also be aware of any compensation issues, including how the allied professional will be paid and by whom. With the philanthropic consultant, there are questions regarding relationships with more than one charity. Will those affiliations affect the gift plan or the selection of the charitable beneficiaries?

Confidentiality — A second responsibility to the prospect is the respect for confidentiality. The donor has rights of privacy and the process must protect all confidential information that is revealed during the relationship. The prospect must be aware of and give permission for the dissemination of any information. It is particularly sensitive where there are professional rules of conduct such as the attorney/client relationship.

There are four opportunities to rescind a gift before it becomes irrevocable: 1) after reviewing the concept, 2) after the value is determined for the assets to be transferred, 3) after the sample document has been prepared, and 4) after the document has been signed but before the assets have actually been transferred into the trust. Once the documents have been signed and the assets transferred, an irrevocable gift is in place.

A related issue is disclosure of a planned gift. If the gift has been generated by the gift planner, the institution is made aware of what is taking place. However, if the gift was initiated by one of the allied professions and is being trusteed by either the donor or an independent trustee, then the gift is made known to the charity at the discretion of the donor. Oftentimes, such notification is withheld, particularly if the donor has retained the right to change charitable beneficiaries as part of the instrument.

Any fees related to the gift planner are generally paid by those who are receiving the service. The charitable organization pays its advisors to provide service. The prospective donor, on the other hand, pays the fees for its allied professionals to draft or review the documents and for any evaluation or recommendations that result from the review. Generally speaking, the real estate or stockbroker's commissions are paid by the trust as a part of the disposition of the property.

Administration — The administration of planned gifts will be carried out by the respective trustee. They will take responsibility for issuing a receipt, seeing to it that the final documents are signed by the trustee, that a gift calculation is prepared showing the remainder value and, in the case of appraisals, that a signed form 8283 is returned to the donor. Most institutions will also develop an accountant's package which contains the information necessary to prepare the tax return for the year. This is usually a copy of the original information that is provided to the donor at time the gift is consummated.

There are regulations requiring the trustee to report periodically, at least annually, to the income beneficiary. The institution needs to remember that the charitable trust is still an asset of the individual, and regular, timely trust activity reports are essential. There is currently no federal law that mandates the independent trustee to make a similar report to the charitable institution, although some state laws may require it.

Along with a year-end report, there should also be a projection as to what the donor might expect to receive in income from that asset during the upcoming year. This will help the donor to plan, and the financial planner or accountant to more accurately project income for the year.

If the gift is intended for a designated program within the charitable organization, documents should be drawn that specify the ultimate use of the funds once they are received. It would be wise for those documents to be reviewed by the donor's counsel as well.

Investment opportunities will result when assets are sold and reinvested. It is best to have a policy in place regarding reinvestment with the referral advisors so that the trustee is consistent. The trustee needs to establish investment criteria and takes into account the needs of the income beneficiary, the objectives of the trust instrument and the interests of the ultimate beneficiary.

The success of every planned gift is measured over time with achievements of the original objectives and continued benefit to the donor and to the income beneficiary. Trustees and allied professionals should be encouraged to meet with their clients to review the status of a completed gift. Gift planners should schedule annual reviews with the donors and invite the allied professionals to participate in this process. The best future prospective donor is last year's donor. The best new referral source is a happy previous referral source.

Recognition — Charitable organizations will often recognize donors for their past, current or future gift to the organization. That recognition should not be made without the concurrence of the donor. If the donor wishes to remain anonymous, that wish should be respected. The allied professional is generally not recognized in the same public fashion, but is often recognized in other ways by the charitable organization.

SUMMARY

Discovering and developing reasons for giving is one of the major responsibilities of the gift planner. It is often easier for them to do than for the allied professionals because they are more closely associated with the ultimate beneficiary of the donor's interest.

It is important to understand that this is a team approach. Each professional brings a specific area of expertise. Not all members are involved in all transactions, but all appropriate individuals must be involved in each gift planning process.

There are no shortcuts. Always maintain healthy relationships with the allied professionals and go through each step in order until the final decision has been made and the goals have been achieved.

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POOLED INCOME FUNDS: THE ESSENTIALS

Presented by Marc Carmichael, JD
R&R Newkirk Company

I. WHAT IS THE BASIC NATURE OF A POOLED INCOME FUND?

A. A donor irrevocably contributes money, securities and/or real property to a charitable organization's separately maintained pooled income fund where it is invested and commingled with gifts made by other contributors to the fund.

B. The donor (or other designated beneficiary) receives each year his share of the pooled income fund's current earnings which may be more or less than the current earnings of the separate assets he or she contributed to the fund. This income interest may not be transferred other than to the charity.

C. On death of donor (or death of other designated beneficiary) payments terminate and the charitable organization removes the donor's gift from the pooled fund and uses it for prior designated purposes or those established by Board of Directors.

D. A contribution deduction is available based on the age(s) of the income beneficiaries and the highest annual payout rate during the fund's previous three years. A "deemed" rate is used for funds with less than three years' experience.

II. WHAT ARE THE MECHANICS OF A POOLED INCOME FUND?

A. A donor contributing to the Fund is given units of participation. In determining the number of units awarded to a donor the value of a unit at the time of the gift must be calculated and that unit value divided into the amount of the gift.

Example: A pooled income fund has issued 500 units in prior years and has a value of $140,000. Thus, each unit has a value of $280. If Peter Smith makes a gift of $20,000 he will be awarded 71.4 units.

B. The income of the fund is divided among donors according to the number of units owned by each donor.

C. At the death of a beneficiary, the amount of principal represented by the units owned by that beneficiary is distributed to the charity maintaining the fund.

Example: Years later, when Smith dies, the value of the trust is $840,000 and there are 2,000 units outstanding. Since the value of each unit is $420 and because Smith owned 71.4 units, the amount of $29,988 is paid to the charity.

III. WHAT ARE BASIC CHARACTERISTICS OF A POOLED INCOME FUND?

A. Consists of property transferred by each donor commingled with property transferred by other donors who have made similar transfers.

B. Pooled funds cannot receive contributions or have investments in securities that are tax-exempt.

C. More than one pooled income fund may be established by a charitable organization.

D. The pooled income fund assets may be jointly invested with the charity's endowment fund but the endowment may not be part of the pooled income fund. Careful thought must be given to this course of action.

E. The pooled income fund must be maintained by a public charity.

F. An independent trustee (such as a bank) may serve as trustee of pooled income funds set up by different charities, but a donor may not act as trustee.

G. Local chapters of national organizations can be named as remaindermen.

H. Qualified pooled income funds will not be subject to SEC regulation or registration so long as charities provide donors and prospects with a prospectus and gift solicitors are not compensated on a commission basis. Pooled income funds may be subject, however, to state securities laws, which differ from state to state. Several states specifically exempt funds from registration requirements. Check with local counsel on state and local regulation.

IV. HOW IS THE CHARITABLE DEDUCTION COMPUTED FOR A GIFT TO A POOLED INCOME FUND?

A. A charitable deduction is allowed for the fair market value of the transferred property less the value of the income interest.

The value of the income interest, solely for this purpose, is determined on the basis of mortality factors published by the IRS and an assumed rate of income. The assumed rate of income is the highest rate of return for the three taxable years immediately preceding the taxable year of the fund in which the transfer is made. This highest rate of return must be computed in accordance with Treas. Reg. Sec. 1.643(c)-6(c).

For funds that do not have three years' experience, a "deemed" rate is assigned. That rate is one percent less than the highest annual average "Applicable Federal Rate" (120% of midterm rate) for the three calendar years immediately preceding the calendar year in which the transfer to the pooled income fund is made (See IRC Sec. 7520). An important 1994 change in tax regulations now requires that the "deemed rate" for new funds be recomputed each calendar year [Reg. Sec. 1.642(c)-6(e)(3)]. For pooled income funds created in 1993 through 1995, the assumed rate is 6.8% for gifts made in 1995.

A donor's charitable contribution deduction from a 1995 gift to a "new" fund is particularly advantageous if the fund is paying 8% or 9% [IRC Sec. 642(c)(5)].

B. To calculate the deduction, Tables S and R(2) [IRS Pub. 1457] are used to determine charity's interest in each dollar contributed to the fund. As a practical matter, most charities now compute deductions with the assistance of computer software. Here are some examples of contribution deductions for donors making gifts to "new" funds in 1995 (employing a "deemed" rate of 6.8%):

Age(s)	Gift Amount	Deduction
65	$10,000	$3,966
75	10,000	5,471
65/65	10,000	2,733

C. Gifts of property (stock) of more than $500 require submission of Form 8283.

V. OTHER TAX CONSEQUENCES OF A GIFT TO A POOLED INCOME FUND

A. Taxation of Fund

The pooled income fund is taxed like an ordinary trust except that it is not taxed on long-term capital gains that are added to principal. Thus, if the fund distributes all its ordinary income and has no short-term capital gains, it will not incur any income tax liability.

B. Tax Reporting

Trustee must file the following returns each year: Forms 1041, 1041-A, 5227 and 1041K-1 (to each beneficiary).

C. Capital Gains Tax Implication

There is no capital gains tax on the transfer of appreciated property pursuant to a pooled income fund agreement so long as it is not subject to any indebtedness. Nor is there capital gains tax to a donor if the pooled income fund sells appreciated securities transferred to it by him.

D. Federal Income Tax of Income Beneficiary

All income received by a beneficiary under a pooled income fund agreement is reportable as ordinary income each year for Federal Income Tax purposes. There are no exceptions to this rule.

E. Federal Gift Tax Implications

When the donor is the sole beneficiary and the remainder interest in a pooled income fund agreement is given to the charitable organization, no gift tax liability is incurred by the donor but IRS regulations state that a return is required.

On the other hand, if the agreement provides for the payment of life income to a person other than the donor, or to a surviving beneficiary, gift tax liability may be incurred by the donor on the present worth of the "life interest," or "future interest" thereby given to or created for such beneficiary.

Gift tax implications can often be avoided by the donor retaining the right, exercisable by will only, to revoke the income beneficiary's right to life income.

An unlimited gift tax marital deduction shelters gifts to spouses, so long as a "QTIP" (qualified terminable interest property) election is made on a gift tax return. A spouse's interest in a pooled income fund was not covered in Code Sec. 1056(b)(8) and 2523(g), which specifically provides that a spouse's interest in a charitable remainder trust would qualify for the gift and estate tax marital deductions. The Technical Corrections Act of 1982 changed the law, however, so that pooled income fund gifts can be "QTIPs."

Where a life interest in a pooled income fund does qualify for the gift tax marital deduction, "revocation by will" clauses are unnecessary unless there is another life beneficiary in addition to a spouse.

F. Federal Estate Tax Implications

If the donor is the sole beneficiary of the pooled income fund, his or her estate can claim an estate tax charitable deduction for the full value of the units in the fund at death.

Does a spouse's interest in a pooled income fund qualify for the unlimited estate tax marital deduction? The answer if yes, so long as there are no other beneficiaries (such as children).

At the surviving spouse's death, the value of the units will either not be included in the estate or wash out as an estate tax charitable deduction, depending on whether the spouse was a contributor.

Important: Executors must make a **QTIP election** on the estate tax return when the first spouse dies or the marital deduction will be lost. The marital deduction is not automatic for pooled income fund interests -- it must be elected.

VI. WHAT ARE THE PRACTICAL ADVANTAGES OF A POOLED INCOME FUND?

A. Small gifts are possible. Generally, the minimum gift is $5,000, or even as low as $1,000.

B. Repeat gifts are permitted and should be anticipated.

C. Capital gains are erased. Investors can transfer highly appreciated but low-income stocks to a pooled income fund, avoid all capital gains tax at the time of transfer, and perhaps receive a higher income from the fund -- plus a charitable deduction.

Note that capital gains taxes are wholly avoided even when a person other than the donor is named as income beneficiary. Gift annuities funded with appreciated stock, on the other hand, result in partial capital gain reporting by the donor and if the donor names some other person to receive annuity payments, the capital gain must be reported by the donor entirely in the year of the gift.

D. Volunteers can solicit gifts to the fund because it is so rigid and absolute. It is almost as easy as soliciting outright gifts.

E. Fast results are probable because a gift to the fund does not generally involve extensive estate planning or extensive cultivation.

F. Gifts can be made without the drafting of documents by the donor's attorney. A straightforward agreement, prepared by the charity, is the only needed legal instrument.

G. An aggressive pooled fund program can lead to an effective broad-based planned gift program.

H. The probability of appreciation in value of corpus eventually passing to charity is excellent. Corpus cannot be depleted by distribution to income beneficiaries.

VII. WHAT ARE THE DISADVANTAGES?

A. Inability to pay tax-exempt income is a serious disadvantage for the high-income donor.

B. Inability to receive gifts of real property (permitted but generally impractical) limits the appeal of the fund.

C. Administrative costs are relatively high (1/2 of 1% of value of trust per year).

D. Charity must make an up-front investment to create the trust, prepare prospectus, organize procedures, etc., unless it can tag on to the fund of an "umbrella organization" (for example, the Association for Healthcare Philanthropy Pooled Income Fund welcomes participation by individual hospitals).

VIII. HOW TO START A POOLED FUND

A. Gain approval of governing board.

B. Draft trust using IRS "safe harbor" forms published in Rev. Rul. 88-53, 1988 C.B. 384 (no requirement to submit to IRS for approval).

C. Select trustee or investment procedures.

D. Write and publish a strong, convincing prospectus.

E. Prepare promotional material -- generally publications or slide presentation.

F. Establish core list of prospects.

G. Recruit and train volunteer solicitors.

H. Prepare a visionary case statement for future of institution.

I. Establish dollar goals and time frames.

J. Solicit core prospects in aggressive campaign using capital campaign approach.

K. Suggested solicitation approach:

1. Explain need of institution and nature of fund to small group of prospects.

2. Seek personal appointment with all prospects in a group.

3. Obtain basic information about prospect's income, property that could be given, and restrictions that prospect would impose on use of gift.

4. Show prospect the exact financial results of a particular gift including deduction, taxes saved from deduction, capital gain avoided, income projection, effective yield, and estate tax advantages.

5. Close the gift.

6. Provide effective service after gift; timely checks, periodic investment reports, tax information, progress of institution, etc.

7. Find additional prospects through direct mail program.

IX. PLANNING IDEAS

A. Window of opportunity in 1995 for "new" funds.

The year 1995 represents an unusual opportunity for gifts to "new" pooled income funds. The assumed rate of 6.8% may be substantially less than the actual payout rate of the fund, resulting in both large deductions and attractive payments for participants. Charities might consider creating and marketing new funds quickly before the "window" closes on December 31, 1995. (High applicable federal rates in 1995 likely will mean less attractive deductions for gifts to "new" funds in 1996).

B. Naming charity as partial income beneficiary.

One charity asks donors to name the organization to receive 10% of their pooled income fund payments made to named beneficiaries. Donors receive no additional income tax charitable deductions, but have the satisfaction of providing a **current** benefit to the charitable remainderman. Furthermore, this charity has been able to eliminate minimum age restrictions for beneficiaries (the organization is happy to receive 10% of a beneficiary's income for life, no matter how young that beneficiary may be).

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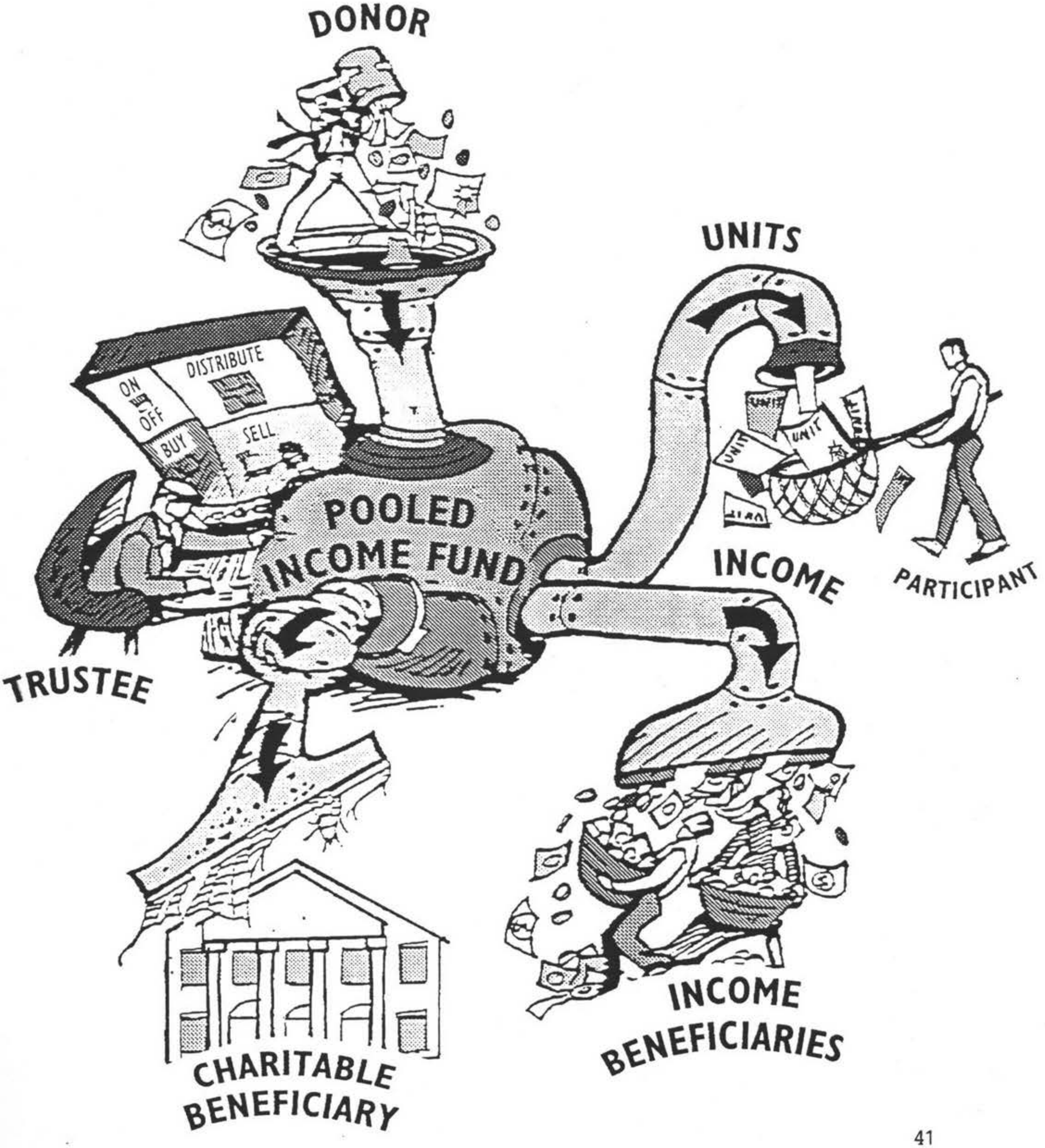
POOLED INCOME FUND



CHARITABLE LEAD TRUSTS

Presented by Carolyn C. Clark
Milbank, Tweed, Hadley & McCloy

Celebrity Vehicle. What do Jacqueline Kennedy Onassis, Averell Harriman, and Annie Laurie Aiken (the mother of Sunny Von Bulow) have in common? Each used a charitable lead trust in his or her Will to benefit charity and to provide benefits for young family members. What is a charitable lead trust and why is it so popular?

Charitable Lead Trust-The Basics. The primary function of a charitable lead trust is to help a donor provide immediate funds for charity and at the same time reduce the cost of transferring assets to members of the donor's family who can afford to wait until they receive funds. When the donor transfers property to the trust, a transfer tax is paid only on the value of the remainder interest, since the income, or, "lead" interest is transferred to charity.

Terms of the Trust. Typically, a charitable lead trust agreement provides that the Trustee must make annual payments to one or more qualified charitable organizations during a term of years or the life or lives of one or more individuals. At the end of the trust term, the property remaining in the trust will go to designated members of the donor's family.

The charitable interest can be an annuity (a specific dollar amount) or a unitrust interest (a fixed percentage of the value of the trust, valued annually). In contrast to a charitable remainder trust, the amount of the charitable lead interest may be less than 5% and the term of the trust may be longer than twenty years.[1] Special features which are important for planning purposes:

- The lead trust during its term of administration is a taxable trust. All income and realized capital gains above the charitable payout will be subject to income tax within the trust. Capital gains in a lead trust are subject to tax so unlike a charitable remainder trust or a pooled income fund, it is not a good vehicle for tax-free diversification. Significantly, the lead trust qualifies for an unlimited income tax charitable deduction under Code Sec 642(C), except to the extent it has unrelated business taxable income ("UBIT"). Therefore, it can be a useful vehicle to help the donor avoid the income tax charitable deduction limitations imposed on individuals.

- The family members or heirs take a carryover basis.

- A charity, bank, individual, child, or donor can be Trustee or co-Trustee.

- A charitable lead trust during its term of administration is subject to certain of the private foundation rules, as will be discussed in more detail later in this outline.

© Carolyn C. Clark heads the Nonprofit Organization Team at Milbank, Tweed, Hadley & McCloy, New York, New York where she advises charitable organizations and individual philanthropists. She is the Chairmen of the Committee on Charitable Planning and Exempt Organizations of the American College of Trust and Estate Counsel.

Special Limitations. The primary function of the charitable lead trust is to reduce the cost of the gift of property to the donor's family. The donor rarely gets an income tax deduction for the value of the charitable lead interest. In order to qualify for an income tax deduction, it is necessary for the income of the trust to be taxable to the donor under the grantor trust rules. Any available income tax deduction is limited to 30% of the donor's contribution base, because the gift is "for the use of", rather than "to", the donee charity. Because of these limitations, a charitable lead trust is only rarely used to obtain a current income tax deduction. It might be useful in a year when, for example, a donor has an unusually high income which raises her tax bracket or if income tax rates are scheduled to decrease in the tax year following the gift.

Variations. The donor can either specify the charity or charities which will receive payments from the trust or leave the selection up to the trustee or an advisory committee. However, the donor should not retain the right to select or change the charities, since that retained power could cause the entire trust to be includable in her gross estate.[2]

Unitrust or Annuity Trust?

- An annuity is a fixed sum payable annually. This stream of payment has to be paid each year during the term of the trust whether the market value of the trust increases or decreases in value.

    Advantages
    - fixed annual payments to charity
    - valuation required only once
    - can zero out value of the remainder

    Disadvantages
    - if principal declines in value, may be nothing left for family

- A unitrust payment is an annual payment equal to a fixed percentage (such as 5%) of the changing annual market value of the trust. When the market value increases, the unitrust amount increases; when the market value decreases, the unitrust amount decreases.

    Advantages
    - payment to charity reflects market changes in underlying asset value
    - family's interest cannot be eliminated by failure of investments to cover fixed payments

    Disadvantages
    - valuation required periodically
    - cannot reduce value of remainder to zero
    - amount payable to charity fluctuates

Effect of Changing IRS Valuation Rates. The value of the charitable deduction for the charitable annuity trust or unitrust depends upon a number of factors, including, the size of the payout, the length of the term of the trust, when, and how frequently payments are made, and, in the case of the annuity trust, the assumed IRS interest rate. I.R.C. Code Sec. 7520. (This last factor is largely unimportant for valuing a charitable lead unitrust interest.)[3] The donor may choose to value the trust based on the Sec. 7520 rate for the month of the transfer, or either of the preceding two months. As a general rule, it will be best to choose the lowest of those three monthly rates when valuing an charitable lead annuity trust. In March, 1995, the rate was 9.4%. For the two preceding months, it was 9.6%. Compare the comprehensive charts showing deductible amounts based on a 9.4% and 9.6% discount rate, which are attached to the end of this outline.

To illustrate, there would be no transfer tax (gift or estate tax) on $1 million left in a charitable lead annuity trust for 15 years paying an annuity of 12% or $120,000 per year. As long as the trust property could generate sufficient income to pay the annuity, at the end of the 15 year period, the principal of the trust could pass free of gift or estate tax to the children. In addition, any appreciation in the value of the fund and any accumulations added to principal would also pass free of transfer tax.

The attached chart shows that the payout rate necessary to obtain a 100% charitable deduction under the 9.4 and 9.6 discount rates is high. The payout rate, obviously, can be reduced by creating a charitable lead trust which will receive less than the 100% charitable deduction. There is still the possibility of incurring no transfer tax, if the donor has available his or her federal exemption equivalent to shelter the value of the remainder interest in the charitable lead trust which would not be offset by the charitable deduction.

Two major objectives in creating a charitable lead trust are to achieve an annuity amount which can be paid without consuming significant amounts of principal and a charitable term which will not be unduly prolonged.

<u>Use as or in Conjunction with Family Foundation</u>. Additional benefits to the donor's family can be secured by providing that the charitable lead trust pays part or all of its charitable interest to a family foundation. While the transfer tax benefits are the same, the family secures the additional benefit of retaining control of the disposition of the charitable funds. This technique has been greatly facilitated by a recent case. <u>See</u>, <u>Estate of Ann Jackson</u>, 15 F.3d 917 (1994). In this case, the Grantor had transferred $5,000,000 to charitable lead trust which distributed $350,000 a year for a 20-year term to the family foundation. At the end of the term, the remaining assets were to be distributed to the Grantor's heirs. It was hoped that the foundation would accumulate the bulk of the annual distribution and would have sufficient assets at the end of the trust term to continue as a viable family foundation. The success of this technique turns on whether the minimum distribution required from the foundation each year includes only the amount retained in the principal of the foundation, or also includes the corpus of the charitable trust. The Regulations define a distributable amount in such a case as 5% of the fair market value of the foundation's assets plus any amounts received from a charitable lead or other split interest trust. See Treas. Regs. Section 53-4942(a)(2)(b)(2). If this Regulation was effective, it would require the family foundation to give away all of the sums it receives from a lead trust and would prevent the accumulation of assets for distribution.

In the <u>Jackson case</u>, the Ninth Circuit affirmed the Tax Court's decision that distributions from a charitable lead trust are not includible in the distributable amount and that the regulation in question was invalid because it was inconsistent with the minimum investment return provision of Section 4942(e).

This decision allows a donor to obtain significant advantages from a charitable lead trust while maintaining control over the charitable trust distributions through a family foundation.[4]

<u>Charitable Lead Trusts and Private Foundation Rules</u>. Charitable lead trusts and the donor, his or her family and the trustees are subject to certain of the private foundation rules.[5]

- The Grantor, his or her family and the trustee would be subject to tax if they entered into any transaction with the charitable lead trust which did not fit into the limited exceptions

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to acts of self-dealing. An act of self-dealing would include, for example, a sale of property by a disqualified person to the trust or vice versa. However, the charitable lead trust can pay a disqualified person "reasonable compensation". IRC §4941.

- If the value of the charitable interest at the time the lead trust is created exceeds 60% of the value of the trust, the lead trust is subject to the excess business holdings rule of Code §4943 and the jeopardy investment rule of Code §4944. The potential application of the excess business holdings rule may inhibit the use of a charitable lead trust as a mechanism to transfer interest in a business if the donor and his or her family own 20% or more of the business. Similarly, it may be inappropriate to consider a charitable lead trust if the charitable lead trust interest will exceed 60% and it is anticipated that the trust would acquire jeopardy investments.

Short life expectancy. If there is reason to believe that a donor's life expectancy is shorter than normal, a charitable lead trust may be extremely beneficial in terms of sheltering transfers to family. The lead trust would be created to make payments to charity for the life of that individual. If the individual does die prematurely, although charities interest may have been valued based on standard IRS longevity tables, charity may receive less (and the remaindermen may receive more) than forecast under those tables. However, the standard IRS longevity tables cannot be used if the individual is known to be afflicted, at the time of the transfer, with an incurable physical condition that is in such an advanced state that death is both clearly "imminent" and the prospects for survival for a year or more are so remote as to be negligible. See Rev. Rul. 80-80, 1980-1, C.B. 194. See, e.g., Estate of McLendon v. Commissioner, T.C. memo 1993-459. In effect, to use this strategy, the individual's life expectancy must be shorter than normal, but not so short that use of the standard tables would be precluded. See, also, proposed Reg. §25.7520-3 which provides that standard mortality tables cannot be used unless there is at least a 50% chance of survival for one year or more.[6]

Reducing the taxable portion to zero. With a charitable lead annuity trust, it is possible, by adjusting the term of the trust and the payout rate to cause the charitable deduction to equal the entire value of the property transferred to the trust. In such a case, no gift or estate tax would be payable upon the remainder which the donor hopes will be available to provide for his or her family. What that length of time and annuity payment must be depend, primarily, on what rate of interest is used by the IRS to determine the value of the charitable interest in the trust. For example, if the discount rate is 6%, and if the trust provides for charity to be paid an annuity, at the end of each year, for 24 years, equal to 8% of the initial fair-market value of the property transferred to the trust, the charitable deduction will equal the entire value of the property transferred to the trust. Thus, the value of the noncharitable remainder will be zero, resulting in no gift or estate tax being due. If, however, the discount rate is 9.6%, the charitable deduction on the same facts would be reduced to approximately 61%.

If you desire to have the benefit of the zero out feature, it is better for the lead trust term to be based upon a term of years and not the life or lives of one or more individuals. See, Rev. Rul. 77-454, 1977-2 C.B.351. This ruling suggests that the value of an annuity stream may be less than the entire value of the trust if the annuity payments are structured to end when one or more individuals die.

Effect of property valuation on utility of charitable lead annuity trusts. A charitable lead trust is the most beneficial to the donor's family if it is expected that the trust will experience growth at a rate in excess of the IRS discount rate. One way this can be achieved is if the property transferred to the lead trust can be valued at a discounted rate. In fact, if the property transferred to a charitable lead annuity trust can be valued at a sufficient discount for tax purposes (for example, for a minority interest and/or non-marketability), it may increase the possibility of the charitable lead annuity trust experiencing growth in excess of the IRS discount rate. Moreover, if the property transferred to or held in a lead trust is valued at a discount, but the property distributed by the trust to charity in satisfaction of the annuity or unitrust payments is not, the benefits to the remaindermen may be even greater. One circumstance where the trust property as a whole may have a lower relative value is if a discounted interest in a family holding company will be contributed to the lead trust, and cash or marketable securities will be distributed to the charity in payment of the annuity or unitrust amount.[7]

Substituting lead trust payments for annual contributions. If an individual who otherwise would make annual charitable contributions during lifetime "substitutes" annual payments from a charitable lead trust, there may be an opportunity ultimately to increase the amount of property which the donor's family will receive. For example, a donor intends to make contributions to charity for the next ten years of $25,000 each year. The individual could create a ten year charitable lead annuity trust to pay charity $25,000 each year funding the trust with an amount such that no taxable gift is made (e.g., transfer $188,000 to the lead trust at a time when the discount rate is 6%). Any property left in the trust after the ten year charitable term would pass to or be held in further trust for family. The trust may be exhausted by reason of the charitable annuity payments by the end of the ten years. Nevertheless, if the trust follows the same investment pattern which the grantor would have followed had the grantor retained the assets transferred to the lead trust, no adverse effect of creating the trust would actually have occurred. If some property remains in the trust after the ten year term, that property will have been transferred to family members free of transfer tax.

Donors most likely to benefit from charitable lead trusts. Only a donor who has an independent desire to benefit charity should consider using the charitable lead trust. While, it is possible, in certain limited situations, for a charitable lead trust to result in more funds being available to the donor's family, generally, it does not. Moreover, a charitable lead trust will delay the receipt of property by the donor's family. Accordingly, only those individuals who can reasonably afford to postpone the receipt of funds by surviving family members would be interested in a charitable lead trust. The donor also runs a risk that, if the investment performance of the trust is disappointing, less will be available in the trust at the end of the term for his or her family. Accordingly, the charitable lead trust is primarily a vehicle for the rich and famous. The advantage of an inter-vivos charitable lead trust when compared with a similar testamentary trust is that the charitable term commences immediately, thereby advancing the date when the fund can pass to the family.

Generation-Skipping Tax Planning

- If the trust passes at the end of the charitable period to the donor's grandchildren, a generation-skipping tax may be payable. This tax can be reduced or eliminated by allocating the donor's (and in some cases the donor's spouse's) $1 million "GST exemption" to the trust.

- For a charitable lead unitrust, the exemption is applied to the initial value of the trust, reduced by the value of the charitable interest, in fixing the trust's "inclusion ratio" (taxability). This makes planning easier.

- A less predictable result occurs for a charitable lead annuity trust. The GST exemption allocated to the trust is increased for the charitable term of the trust at the IRS discount rate applicable to the gift. The increased GST exemption is then applied to the value of the trust at the end of the charitable period.

- Thus the charitable lead unitrust, and to a lesser extent the charitable lead annuity trust, may be good ways to use a donor's GST exemption.

Charitable Gift Tax Deductions

LEAD ANNUITY TRUST

	Years			
	10	15	20	25
5%	34.4	43.0	48.5	52
6%	41.3	51.6	58.2	62.4
7%	48.2	60.2	67.9	72.8
8%	55.1	68.9	77.6	83.2
9%	62.0	77.5	87.3	93.6
10%	68.9	86.1	97.0	100+
11%	75.8	94.7	100+	100+
12%	82.7	100+	100+	100+

LEAD UNITRUST

	Years			
	10	15	20	25
5%	40.1	53.6	64.1	72.2
6%	46.1	60.4	70.9	78.7
7%	51.6	66.3	76.5	83.7
8%	56.5	71.3	81.1	87.5
9%	61.0	75.6	84.8	90.5
10%	65	79.4	87.8	92.8
11%	68.8	82.5	90.2	94.5
12%	72.1	85.3	92.2	95.9

Discount Rate 9.4%

March 1, 1995

Charitable Gift Tax Deductions

LEAD ANNUITY TRUST

	Years 10	15	20	25
5%	34.2	42.6	47.9	51.3
6%	41.1	51.1	57.5	61.5
7%	47.9	59.7	67.1	71.8
8%	54.8	68.2	76.7	82.1
9%	61.6	76.7	86.3	92.3
10%	68.5	85.3	95.9	100.00
11%	75.3	93.8	100.00	100.00
12%	82.2	100.00	100.00	100.00

LEAD UNITRUST

	Years 10	15	20	25
5%	40.1	53.6	64.1	72.2
6.%	46.1	60.4	70.9	78.7
7%	51.6	66.3	76.5	83.7
8%	56.5	71.3	81.1	87.5
9%	61.0	75.6	84.8	90.5
10%	65.1	79.4	87.8	92.8
11%	68.8	82.5	90.2	94.5
12%	72.1	85.3	92.2	95.9

Discount Rate 9.6%

March 1, 1995

ENDNOTES

1 The primary rules are set forth in IRC §170(f)(2)(B) and Treas. Reg. §1.170A-6(c)(2)(f) and (ii).

2 See, e.g., Revson v. United States, 5 Ct. Cl. 362 (1984). This result is undesirable because the term for which charity will be receiving payments will be reduced which reduces the available charitable deduction and increases the amount subject to tax.

3 See, Blattmachr & Hastings, "Valuing Certain Split Interests", 122 Trusts & Estates 27 (June 1983).

4 See, Kalter and Newman, "The Value of the Family Foundation Charitable Lead Trust", Trusts and Estates Magazine, 37 (December 1994).

5 Chapter 42 of the Code; IRC §4947(a)(2)(B)(3).

6 Blattmachr, a Primer on Charitable Lead Trusts, to be published in a future edition of Trusts and Estate magazine.[1]

7 Blattmachr, ID.

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FORTUNE

PERSONAL INVESTING

By Susan E. Kuhn

LESSONS FROM THE WILL OF JACQUELINE KENNEDY ONASSIS

■To Maurice Tempelsman, her friend and companion of some 15 years and an executor of her will, she left a Greek alabaster head of a woman. To her children, Caroline and John, she left $250,000 apiece in cash, the Fifth Avenue apartment and other property and personal effects, and money in a trust that she inherited from her first husband. Jacqueline Kennedy Onassis left gifts to many people in her last will and testament dated March 22, 1994, two months before her death on May 19. But in leaving so many details of her estate in a will available to the public in room 504 of the Surrogate Court building in New York City, she left behind as much or more to the rest of us in the form of a model of smart estate planning.

In a world where supposedly nothing is inevitable except death and taxes, a good will and a sound estate plan are valuable gifts. Since the days of James Madison, when our forefathers considered outlawing the inheritance of wealth because it went against the American spirit of each person making his own money by working, the government has sought to take a taxing advantage of our passage from this world. Today, Uncle Sam can gobble up as much as 55% of the value of an estate over $600,000, and the states may grab their share too. If you think $600,000 is a high hurdle, consider: The figure has been fixed since 1987 and has not been adjusted for inflation. If you've got a family business or a pension plan, life insurance, a primary residence, and vacation home, you could hit that target more easily than you think.

Good thing that Jackie O., with the aid of her attorneys at the New York law firm Milbank Tweed Hadley & McCloy, planned wisely. Though not all of us may have her estimated $200 million in wealth, we can still learn from the expertise that guided her. At a very basic level, the fact that she had a will and devoted 36 pages to the distribution of her estate may be the most important lesson of all. A surprising number of smart people don't make a will, and that opens the door for the government to have a field day while potential heirs hassle with the probate courts or among themselves.

On a more sophisticated level, the Onassis will makes smart use of estate-planning vehicles like trusts to pass money on to heirs and charities while reducing the bite from estate taxes. Louis Hamel, chairman of the trusts and estates department at Hale & Dorr, a Boston law firm, plans to use the Onassis will as a case study for partners and associates. "It is an interesting will," says he. "It is a rare look at how a good estate plan is done."

In the beginning of the will, Jackie makes specific bequests. Valuable items with a probable sentimental attachment for particular people are duly assigned, such as a copy of John F. Kennedy's inaugural address signed by Robert Frost, to her lawyer, Alexander Forger. Personal friends, maids, and the butler get cash gifts ranging from $250,000 to $25,000. Property goes to those who might want it most. The kids get the New York apartment, for example, but Hammersmith Farm, the Newport, Rhode Island, property she inherited from her mother, Janet Lee Auchincloss, goes to her stepbrother Hugh Auchincloss Jr.

These line-by-line bequests reflect one universal estate-planning truth: Money is easier to divvy up than property, so spare the heirs from arguing and lay out who gets the goods of value. There is also a clause that recognizes another truth: Uncle Sam taxes everything, so if you want your maid to truly have $50,000, then designate that the taxes on the gift will be paid by your estate, which Jackie did. That saves the beneficiary from having to sell assets to pay the taxes owed.

ELEGANT ESTATE PLANNING

Activity	What Jackie did	Why it was smart
Giving gifts	Left gifts of cash to friends, and specified that the applicable taxes be paid out of the rest of her estate.	If the will does not direct the taxes to be paid from the estate, the value of a gift could be cut in half by the tax due.
Leaving property	Specified exactly who would inherit each of her real estate properties.	Homes are laden with emotion and should be disposed of directly, not lumped into total assets.
Creating trusts	Put the bulk of her estate into a charitable lead trust. The trust gives money to charities for 24 years, then the rest goes to her grandkids.	A charitable lead trust is a good way to give money to heirs who don't need income immediately. The donations to charity reduce the estate's taxes.
Making personal requests	Gave her personal property and letters to her children and requested that they respect her wish for privacy.	When giving gifts of valuable personal property, make your wishes known but allow the beneficiaries some flexibility.

Be careful with such provisions, though, warns Kenneth Brier, an estateplanning attorney with Sherburne Powers & Needham in Boston. If you give one heir valuable property and another the residue of the estate nominally worth as much, and the latter pays all the taxes, he or she may feel shortchanged. If you designate that taxes on gifts be paid from the estate, remember that this will shrink the value of the residual estate. So if you're planning to bequeath the residual estate to someone, adjust that beneficiary's gift accordingly.

After all the bequests are made, Jackie leaves the remainder of her estate to the C&J Foundation, a charitable lead trust established in the will and designed to last for 24 years. In a charitable lead trust, a set amount of money is distributed to charities each year and, at the end of its term, the remaining assets are passed on to a named beneficiary. Jackie's will names Caroline, John, MauriceTempelsman, and Alexander Forger as trustees and directs them to give an annual amount equal to 8% of the initial net fair market value of the assets to charities, preferably those "committed to making a difference in the cultural or social betterment of mankind or the relief of human suffering." Twenty-four years hence, the assets pass to her grandchildren, the oldest of whom, Rose Kennedy Schlossberg, is now 6 years old.

Charitable lead trusts are a great way to give money to family members and charities and save on estate taxes, provided your heirs don't need income right away. Assume you put $1 million into a 24-year charitable lead trust, says Hamel of Hale & Dorr. You can set the payout rate to charities as high or as low as you wish, but to maximize the tax benefits on a trust of this size, a 4% rate is about right. If you choose to give the charities $40,000 per year, the present value of that gift, discounted at a current federal rate of 8.4%, is $407,000. Your taxable estate is reduced by this amount to $593,000, or just below the $600,000 exemption, so your taxes are zero. If you gave $1 million to an heir outright, on the other hand, the estate taxes owed would be $153,000. If this gift was for your grandkids, and it was over $1 million, it would suffer yet another blow from the generation-skipping tax, which reduces the sum by 55%.

Although charitable lead trusts have existed for years, they haven't been widely used. But today such a trust makes sense for a lot of folks, including those who want to pass on a family business without being forced to sell it to pay the taxes on the appraised value. The family business will have to generate money to give to charity every year, which may take some discipline, says Hamel. Also, the trust can't give away more than 60% of the initial value of the business, otherwise the Internal Revenue Service will force the trust to liquidate. But putting the firm in a trust that will ultimately be paid to a relative is one way to keep it all in the family.

One nice thing about writing a will and thinking about your estate: It is a chance to leave a final word in black and white. Jackie's voice comes through when she asks, for example, that her children respect her desire to keep her papers private. Done right, such wishes can mean almost as much as legal safeguards. Says Marshall Gunn, a CPA and estate planner in Jacksonville, Florida: "The will made a real impression. She wasn't just saying, 'Here are my assets.' She said why she gave them. She made plain her intent for social good in describing the charities. She passed power on to her children as trustees. You could see the thought beyond the legal verbiage, and that's what a last will and testament should ultimately reflect."

CHARITABLE REMAINDER TRUSTS: FUNCTION AND USES

Presented by Robert L. Coffman
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I. *Introduction.* Charitable remainder trusts are planning vehicles that offer significant flexibility to taxpayers to provide for the income needs of themselves or other non-charitable beneficiaries and, at the same time, to address major charitable goals. Referred to as "split-interest" trusts, charitable remainder trusts are structured to direct a payment stream to a non-charitable beneficiary (or beneficiaries) for the lifetime of the beneficiary (or beneficiaries) or for a predetermined period of time not to exceed 20 years. When the income beneficiary's interest in the trust ends, the remaining trust assets will pass to a designated charity or charities, or will continue to be held in trust for the benefit of the charitable remainderman.

II. *Types of Charitable Remainder Trusts.* Regulations provide for two different types of charitable remainder trusts to meet different planning needs.

A. *Charitable Remainder Annuity Trust.* A charitable remainder annuity trust makes a *fixed* payment to the income beneficiary. The payment is based on a fixed percentage of the trust's initial value and remains constant throughout the term of the trust.

B. *Charitable Remainder Unitrust.* A unitrust provides for a *variable* payment to the income beneficiary. The annual payment is based on a fixed percentage of the trust's value as it is revalued on the annual valuation date. For example, the first year's payment is based on a fixed percentage of the initial value of the trust. If the value of the trust principal increased the next year's payment will be greater; if it decreases, the payment will decrease. There are several variations of the unitrust.

1. *"Straight" Unitrust.* A "straight" unitrust pays a fixed percentage of the trust's annual value regardless of the investment results of the trust.

2. *Income-Only Unitrust.* A unitrust can be drafted so that the payment will be made to the income beneficiary only to the extent that the trust has accounting income. Generally, "income" means dividends and interest but in some cases may be defined differently by the grantor of the trust (see below).

3. *Income-Only Unitrust with Make-up Provisions.* A further variation of the income-only unitrust can provide that any deficiencies in income in any given year essentially will go into a "credit" account for the beneficiary. In subsequent years the beneficiary will be entitled to any excess income generated by the trust beyond what is needed to pay that year's unitrust amount to the extent of any deficiencies from prior years.

4. *Additional Contributions.* Unlike annuity trusts, unitrust may permit future additional contributions. [Reg. Sec. 1.664-3(b)]

III. *Trust Provisions.* In order to be considered qualified, a trust must comply with very specific requirements. For some trust provisions the donor may be able to choose between alternatives, and some provisions are optional.

A. *Term of the Trust.* A qualified charitable remainder trust must be drafted to last for the life (or lives) of a named beneficiary (or beneficiaries), or must be for a specified term of years not to exceed 20 years. [Reg. Sec. 1.664-2(a)(5)(i); 1.664-3(a)(5)(i)]

1. Individuals may be named or they may be referred to by class but they must be lives in being at the time the trust is created.

2. It is possible to combine term of years and lifetime designations if there is no way that the trust will continue beyond 20 years or lives in being.

3. The trust may terminate on the occurrence of a *"qualified contingency."*

B. *Income Beneficiary.* The stated annuity trust amount or unitrust amount shall be payable to a named beneficiary or beneficiaries, at least one of whom is not a charitable organization described in Internal Revenue Code Sec. 170(c). [Reg. Sec. 1.664-2(a)(3)(i); 1.664-3(a)(3)(i)]

C. *Remainder Beneficiary.* The remainder interest in the trust must be irrevocably designated to pass to, or for the use of, a qualified charitable organization at the end of the trust term from the time the trust is created.

1. *"To or for the use of."* Typically, the remaining trust assets will pass directly to the designated charitable remainderman. It is permissible, though, for the trust to continue for the benefit of the charitable remainderman. In such cases, the trust most likely would be characterized as a private foundation.

2. *Qualified Charity.* A charity must be an organization described in IRC Sec. 170(c) to be a qualified remainderman of charitable remainder trust for income tax purposes. It also must meet the requirements of IRC Sec. 2522(a) in order for the value of the charitable remainder to be deductible for gift tax purposes, and Sec. 2055(a) for estate tax purposes.

3. *Not Necessary to Specifically Name Charity.* As long as the remainder is irrevocably designated to pass to or for the use of a qualified charitable organization, it is not necessary to specifically name the charity at the time the trust is created. The trust may set out a method for a qualified charity to be selected (e.g., by the trustee) or may reserve the power in the grantor to name a specific remainderman later.

4. *Alternate Remainderman.* The trust instrument must name or provide a method of selecting an alternate qualified remainderman if the initial charity should not be qualified when the trust terminates. [Reg. Sec. 1.664-2(a)(6)(iv); 1.664-3(a)(6)(iv)]

5. *Multiple Remaindermen.* The trust may designate multiple remaindermen as long as each is qualified.

6. *Changing the Remainderman.* The grantor may retain the power to change the remainder beneficiary. As long as the power to change is limited to qualified charities, this is permissible.

D. *Payment of Annuity or Unitrust Amount*

1. *Annuity Trusts.*

a. The amount reserved as the annuity trust amount must be at least 5% of the trust's initial value.

b. Payments must be made at least annually.

c. *5% Probability Test.* If there is greater than a 5% probability that the entire trust corpus will be exhausted by payments to the non-charitable income beneficiary (or beneficiaries), no income tax deduction is available to the donor. (Rev. Rul. 77-374)

2. *Unitrusts.*

a. The unitrust amount must be at least 5% of the trust value as recalculated annually.

b. *No 5% Probability Test.* The 5% probability test does not apply to unitrusts. *Reason:* by definition, a unitrust pays only a stated percentage of its annual value. It is, therefore, impossible to totally deplete the trust corpus through payments to the non-charitable income beneficiary (or beneficiaries).

3. *In General.*

a. No other payments are permitted during the trust term other than the payment of the annuity or unitrust amount. [Reg. Sec. 1.664-2(a)(4)(i); 1.664-3(a)(4)(i)]

b. *Payments in Kind.* Regulations permit the trustee of a charitable remainder trust to make payments in kind. [Reg. Sec. 1.664-1(d)(5)]

E. *Trustee.* The trust document appoints the person or entity to serve as trustee of a charitable remainder trust.

1. *Donor as Trustee.* Absent certain complicating circumstances it generally is possible for the donor to serve as trustee, although it may not be advisable.

2. *Charitable Remainderman as Trustee.* A common arrangement is for the charitable remainderman to serve as trustee. The ability of the charity to serve in this capacity is a matter of state law.

3. *Professional Fiduciary.* Many banks and trust companies serve as trustees of charitable remainder trusts.

4. *Multiple Trustees.* It may be necessary to appoint multiple trustees. For example, a donor generally could not serve as trustee for the purpose of valuing hard to value trust property such as real estate or closely held stock.

F. *Irrevocability.* A qualified charitable remainder trust must be expressly irrevocable.

G. *Amendment of Trust.* It is not possible to amend a trust, even to correct defective provisions, except within very limited circumstances.

H. *Specimen Trust Documents.* The Internal Revenue Service has released specimen trust documents. The IRS guarantees that a trust document will be qualified as long as it substantially follows the specimen language. (Rev. Proc. 89-19, 89-20, 89-21, 90-30, 90-31, 90-32)

1. *Basic Documents.* These forms meet the minimal requirements for qualification. They do not address issues unique to any particular situation, such as specific property used to fund the trust, powers of trustees, etc.

2. Many desirable provisions must be added by the drafter of the document.

I. *Prohibitions on Activities Subjecting Trust to Private Foundation Excise Taxes.* [Reg. Sec. 1.664-1(b); 1.508-2(b)(1)(vi)]

IV. *Charitable Income Tax Deduction.* The donor generally is entitled to a charitable income tax deduction equal to the present value of the charitable remainder interest.

A. *Actuarial Tables.* Typically, the deduction must be calculated according to actuarial tables set out in the regulations and in IRS tables.

1. Requests can be made for actuarial factors for situations not covered in the tables.

2. Exceptions are possible if the beneficiary is terminally ill. [Note: See Proposed Regulation Sec. 1.7520(3)(b)(3).]

3. *Discount Rate.* The exact amount of the deduction depends on the applicable federal discount rate in effect for the date on which the gift is made. The rate changes monthly. The donor may choose to use the rate for the month of the gift or for either of the two months immediately preceding the date of the gift. [IRC Sec. 7520(a)]

B. *Deduction Limits: General Rules.* Gifts to public charities are deductible to the extent of 50% of the donor's contribution base [generally adjusted gross income (AGI)] for gifts of cash and 30% for gifts of long-term appreciated capital gain property. Gifts to private foundations are deductible to the extent of 30% of AGI for cash and 20% for long-term appreciated property (limited to basis).

1. *50% Election.* A donor to a public charity can elect to utilize the deduction produced by a gift of long-term appreciated capital gain property to the extent of 50% of adjusted gross income by limiting his or her deduction to the extent of his or her basis attributable to the gift portion of the transaction.

2. Basis is allocated proportionally between the deductible and non-deductible portions of the transaction.

3. Excess deductions generally can be carried forward for an additional five years beyond the year of the gift.

C. *Type of Charitable Beneficiaries.* Qualified charitable remaindermen must meet the description of a charitable organization set out in IRC Sec. 170(c). This definition is broad and encompasses both private foundations and public charities. Deductions will be limited to those available for gifts to private foundations unless the trust also requires the remainderman to meet the description of a public charity set out in Sec. 170(b)(1)(A).

D. *Representative Income Tax Deductions.* The following charts show the charitable income tax deduction generated by a $100,000 charitable remainder trust. Deductions are shown both for annuity trusts and unitrust, for one life or two, and for terms of years (based on quarterly payments and 9.4% discount rate).

$100,000 CHARITABLE REMAINDER ANNUITY TRUST

(One Life)

Payout Rate

Age	**5%**	**6%**	**7%**	**8%**
55	$55,306	$46,367	$37,428	$28,489
60	$58,274	$49,928	$41,583	$33,238
65	$61,714	$54,056	$46,399	$38,742
70	$65,679	$58,814	$51,950	$45,086
75	$70,061	$64,074	$58,086	$52,098

(Two Lives)

Payout Rate

Ages	**5%**	**6%**	**7%**	**8%**
55-55	$50,042	$40,051	$30,059	$20,067
60-60	$52,158	$42,590	$33,022	$23,453
65-65	$54,908	$45,890	$36,872	$27,854
70-70	$58,398	$50,078	$41,758	$33,437
75-75	$62,636	$55,153	$47,690	$40,217

(Term of Years)

Payout Rate

Term	**5%**	**6%**	**7%**	**8%**
5 years	$80,086	$76,103	$72,120	$68,138
10 years	$67,378	$60,854	$54,329	$47,805
15 years	$59,269	$51,122	$42,976	$34,830
20 years	$54,094	$44,913	$35,731	$26,550

$100,000 CHARITABLE REMAINDER UNITRUST

(One Life)

Payout Rate

Age	5%	6%	7%	8%
55	$36,212	$30,397	$25,759	$22,032
60	$42,479	$36,596	$31,760	$27,762
65	$49,114	$43,324	$38,425	$34,262
70	$56,082	$50,566	$45,770	$41,587
75	$63,138	$58,070	$53,551	$49,511

(Two Lives)
Payout Rate

Ages	5%	6%	7%	8%
55-55	$25,502	$19,698	$15,303	$11,961
60-60	$31,158	$24,997	$20,150	$16,325
65-65	$37,575	$31,222	$26,041	$21,805
70-70	$44,725	$38,390	$33,047	$28,531
75-75	$52,413	$46,340	$41,055	$36,448

(Term of Years)

Payout Rate

Term	5%	6%	7%	8%
5 years	$78,490	$74,671	$71,002	$67,479
10 years	$61,607	$55,758	$50,413	$45,534
15 years	$48,356	$41,635	$35,795	$30,726
20 years	$37,954	$31,089	$25,415	$20,734

V. *Taxation of Payments.* Funds distributed to a beneficiary from a charitable remainder trust retain the same character those funds had in the hands of the trust.

A. *Four-Tier System.* There is a hierarchy for distribution of funds that divides distributable funds into four tiers [Reg. Sec. 1.664-1(d)]. All current and accumulated funds in each tier must be exhausted before funds of the next tier are distributed. Funds are distributed in the following order.

1. *Ordinary Income.* The first type of funds to be distributed are current and accumulated ordinary income. These funds would be taxed at the highest rates under present tax laws.

2. *Capital Gain.*

3. *All Other Income.* This would primarily consist of tax-exempt income.

4. *Return of Principal.*

B. *Allocation of Items to Principal or Income.* Generally, income consists of dividends and interest. Capital gains typically are allocated to principal. This becomes especially important to determine what should be distributed from an income-only unitrust.

1. Absent qualifying language, "income" is considered to be defined by the trust instrument and applicable state law [IRC Sec. 643(b)]. Most state laws give the grantor fairly broad discretion in defining income.

2. A recent Private Letter Ruling approved the classification of certain long-term capital gains as income *(Ltr. Rul. 9442017).*

VI. *Funding the Trust.* The choice of the asset with which to fund a charitable remainder trust is one of the most important decisions the donor will make. The donor can realize a wide range of potential benefits depending on the asset selected. The choice can affect considerations such as the percentage limitation for the resulting deduction, the avoidance of capital gains tax, or even the delay or unavailability of an income tax charitable deduction, among other things.

A. *Cash.* A gift of cash is a very straight-forward and uncomplicated way of funding a charitable remainder trust. If the irrevocable charitable remainderman is a public charity and is described as such in the trust document, the donor will be able to use the resulting income tax charitable deduction to the extent of 50% of his or her adjusted gross income (30% if the remainderman is a private foundation).

B. *Long-Term Appreciated Capital Gain Property.* Long-term appreciated capital gain securities or real estate are wonderful assets to use to fund a charitable remainder trust. Generally, for gifts to public charities, the donor gets a deduction based on the full fair market value of the property but does not have to recognize any of the paper gain. Because a charitable remainder trust is tax-exempt, it does not have to pay tax on the gain if the property is sold. This means that the full value of the property can be preserved for reinvestment in the trust.

1. Such gifts generate an income tax charitable deduction that may be used to the extent of 30% of AGI (20% for gifts to private foundations).

2. *Tangible Personal Property.* If the trust is funded with long-term appreciated tangible personal property no deduction is available to the donor as long as the donor or a closely related party has an interest in the property.

a. Traditionally this has been assumed to mean that no deduction is available as long as the disqualified person has an interest in the trust.

b. A recent Private Letter Ruling indicates that a deduction is available when the trust disposes of the tangible personal property *(Ltr. Rul. 9452026).* However, the letter ruling also indicates that the disposition by the trust would make the gift a non-related use gift which would limit the available deduction to the donor's basis in the gift portion of the transaction.

c. A donor of tangible appreciated property still would avoid recognition of any long-term capital gain upon transferring the property to the trust.

3. *Conversion of Appreciated Property to Tax-Exempt Securities.* At first blush it might appear that an excellent way to convert highly appreciated property to tax exempt income would be to transfer the property to a charitable remainder trust, have the trustee sell the property and invest in tax-exempt securities.

a. *"Pomona College Plan."* This plan became popularly known as the Pomona College plan. The IRS has ruled that if there is an express or implied arrangement to sell and reinvest in tax exempt securities, the gain will be taxed to the donor (Rev. Rul. 60-370)

b. Even if the gain is not taxed to the donor, this plan would not result in tax-exempt income being passed to the beneficiary until, under the four-tier distribution system, all of the capital gain realized by the trust is passed on to the beneficiary.

C. *Encumbered Property.* Except in very limited circumstances it is not practical to use encumbered property to fund a charitable remainder trust. The use of such property can cause a variety of problems, including causing the trust not to be qualified, causing the trust to lose its tax exemption, and imposition of penalty taxes for self-dealing.

VII. *Gift Tax Considerations.* The gift tax consequences of creating an inter vivos charitable remainder trust depend on many variables. If the donor gives any part of the income interest to any other person the transaction may generate a gift tax, depending on the relationship of the beneficiary to the donor, when the income interest takes effect, and whether or not the transfer of the interest is complete.

A. *Multiple Gifts.* Whenever a donor creates a charitable remainder trust and gives an income interest to a non-donor and a remainder interest to charity he or she has made gifts to each. The remainder gift will qualify for the gift tax charitable deduction as long as the charity is described in IRC Sec. 2522(a).

B. *Immediate Interests.* If the income interest given is to begin immediately the gift is one of a present interest and qualifies for the $10,000 gift tax annual exclusion.

C. *Future Interests.* If the interest begins after an intervening period (such as the life of a primary beneficiary) the gift is one of a future interest and will not qualify for the annual exclusion.

D. *Gifts to a Spouse.* In most cases, income interests in charitable remainder trusts will qualify for the gift tax marital deduction.

1. Generally, the income interest must be only for the spouse or the donor and the spouse to obtain marital deduction.
2. Gift qualifies even though it is a terminable interest under exceptions created by the Economic Recovery Tax Act of 1981 (ERTA) [IRC Sec. 2523(g)(1)].

3. If the spouse and a non-spouse are given income interests in the same trust, the spouse's interest will not qualify for the marital deduction.

E. *Gifts to a Non-Spouse.* Generally, the value of income interests passing to non-spouses will be taxable gifts. If they are gifts of present interests, the annual exclusion will apply.

F. *Power to Revoke.* A donor may retain the power to revoke the interest of a beneficiary, exercisable only by will. Such a reservation keeps a gift from being complete and can avoid any current transfer tax liability.

1. The value of a survivorship interest would not be ascertained until the donor dies without revoking the interest. At that time, the value of the survivorship interest would be included in the donor's estate.

2. Donor can reserve the right to revoke the interest of a primary beneficiary by will, but such a reservation may raise questions about improperly measuring the interest of the beneficiary by the life of another.

G. *Relationship to Estate Tax.* The taxable value of any transfers for gift tax purposes will be added back to the donor's estate for purposes of calculating the estate tax. Credit will be given for any gift tax actually paid. If donor dies within three years of making the gift, the gift tax paid also will be added back to the estate.

VIII. *Estate Tax Considerations.*

A. *Inter Vivos Trusts.*

1. *Donor Retains No Interest.* If the donor retains no interest in the trust or does not retain the right to revoke the beneficiary's interest, the value of the beneficiary's interest will be a taxable gift. That value, less any applicable exclusion or deduction, will be added back to the donor's estate at death. Credit is given for any gift tax actually paid.

2. *Donor Retains Interest.* If the donor retains an annuity or unitrust interest, or the power to revoke the interest of a beneficiary, the value of the trust can be brought back into his or her estate at death.

a. The value of any interest passing to the charitable remainderman will qualify for the estate tax charitable deduction.

b. The value of any continuing annuity or unitrust interest in non-charitable beneficiaries will potentially be taxable. This may be offset by the unlimited estate tax marital deduction for the value of a spouse's interest.

3. *Requirement for Beneficiary to Pay Death Taxes.* If there is any possibility of the trust becoming liable to pay federal estate taxes or state death taxes, the trust will not be a qualified charitable remainder trust (Rev. Rul. 82-128). The donor must include language requiring a beneficiary to provide funds to pay any such taxes attributable to the inclusion of his other interest in the estate of the donor or forfeit the interest.

B. *Testamentary Trusts.*

1. *Spouse's Interest.* A surviving spouse's income interest in a charitable remainder trust generally will qualify for the estate tax marital deduction if the spouse is the only income beneficiary. This is an exception to the terminable interest rules under ERTA [IRC Sec. 2056(b)(8)].

2. *Non-Spouse Interest.* The full value of the income interest of a non-spouse generally will be taxable for estate tax purposes.

IX. *Sample Gift Planning Strategies.*

A. *Escape from Locked-in Position in Securities*

EXAMPLE - Art J., age 70, has been a very successful investor. He owns one block of stock that is now worth $250,000 which he bought several years ago for $50,000. The stock pays no dividends.

Now that he is retired, Art would like to increase his spendable income and has been considering liquidating the stock investment so he can reinvest the sales proceeds for added income. He is deterred from doing so, though, because of the $200,000 capital gain he would generate. The tax on that gain would eat up $56,000, leaving just $194,000 to reinvest. Assuming he could get a 7% return, Art would end up with $13,580 additional income.

Art also has been looking for a way to make a substantial gift to his favorite charity, but he feels he needs all the income his property can generate. After learning about charitable remainder trusts, Art concludes that a trust may meet all his objectives.

He transfers the stock to a charitable remainder annuity trust that will pay him 7% of its initial value -- or $17,500 -- each year for the rest of his life. He realizes no gain upon transferring the stock to trust and the trust can sell it and reinvest the entire proceeds without paying any tax.

In addition, Art's gift produces an income tax charitable deduction of $129,875. In his 39.6% federal income tax bracket, this gift saves Art $51,430. If the tax savings are invested at 7%, Art will have additional income of $3,600 each year for a total income of $21,100 --an increase of more than 55% over the income he would generate by selling the stock, paying the tax on the gain and investing the net proceeds.

B. *Planning for Retirement.*

EXAMPLE - Dr. Margaret M., age 50, has a very successful practice. She tries to make maximum use of all qualified tax deductible retirement planning options available to her but she still would like to be able to do more to increase her security when her career ends. She plans to practice until she is 65. Margaret also is interested in finding a creative way to make a significant gift to her favorite charity.

Several years ago, the doctor bought some undeveloped real estate as an investment. The path of progress seems to be moving toward her property and, even though the value has doubled to $100,000, she still believes there is major upside potential.

Dr. M. decides to use her land to fund an income only unitrust with make-up provisions. She reserves a 5% interest for herself in the trust. Because she is in her peak earning years, she really doesn't even want any current income. Her hope is that the land will be retained in the trust, that it will appreciate substantially and that it will be sold when she retires and reinvested for maximum income.

Since the land produces no income, Margaret's cash flow will not be negatively affected by the gift. In fact, the $30,497 income tax charitable deduction the trust generates will actually give her more spendable cash.

Assuming the land appreciates at 10% per year it will be worth $417,725 when she retires. If the land is sold and reinvested for 8% income, Margaret will be entitled to the entire $33,418 annual income it produces -- even though it exceeds by more than $12,000 her 5% payout rate -- until her accumulated deficit of more than $158,000 is made up.

C. *Providing Expenses for Education.*

EXAMPLE - Don and Carol J. are proud of their grandson Bill, who is about to graduate from high school. They have been planning for some time to help Bill with his education, and have invested over the years for that purpose.

Don and Carol would like to give Bill $15,000 a year for the four years he will be in school. They have stock worth $75,000 they plan to use for this purpose. The value of the stock has grown nicely from the $15,000 they invested initially. The down side of their plan is that they face a tax of $16,800 on the gain if they liquidate the investment to generate cash to give to Bill, leaving just $58,200 net proceeds.

They also believe their desire to help Bill will cause their plans to make a significant gift to their favorite charity to be put on hold. But, a charitable remainder trust may enable them to address both objectives at the same time. Don and Carol can use the stock to fund an annuity trust that will pay Bill $15,000 each of the next four years and then pass to the charity.

Bill will get $15,000 for college expenses each year. In his low tax bracket he will pay less than $2,000 tax each year on the income. Don and Carol will generate an income tax charitable deduction of $25,161 and will avoid any tax on the gain. The deduction saves them $9,058 in their 36% tax bracket --more than enough to make up the difference to Bill for what was lost to income tax on his payments.

Assuming the trust earns 7% income during the four-year term, a total of $31,711 ultimately will pass to the charity. On the other hand, if Don and Carol sell the stock, pay tax on the gain, invest the net proceeds at 7% and give annual distributions of $15,000 to Bill, they will have less than $8,300 left to fund their charitable goals.

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PRACTICING GOOD STEWARDSHIP

Presented by Stewart J. Crook
Southern Union Conference of Seventh-day Adventists

INTRODUCTION: What is a steward? Words which come readily to mind are: manager, trustee, and fiduciary. They connote responsibility, trustworthiness, and obligation. Black's Law Dictionary indicates that a steward is "...a man appointed in the place or stead of another." It further relates (historically) that a steward was "....an important officer who had the general management of all forensic matters connected with the manor."

For relationships with donors the definition for steward may be expanded to include the concept of service. Thus, a working definition of a steward might be: a manager, trustee, fiduciary, and servant. Stewardship is not a matter to be taken lightly and the practice of it demands integrity, concern for the well-being of others, and attention to details relating to business matters, the law, and the care of properties. This concept of stewardship includes a service relationship beginning with or before the first contact with the donor which may continue throughout or beyond his or her lifetime. Therefore, for the purposes of this discussion, a steward is considered as a person who stands by the side of or in the place of another and is charged with assisting in or actively directing the management of the affairs of that person. He or she may be held responsible for all actions committed or omitted while acting as the steward.

The balance of this paper will address the practice of stewardship in light of the above definitions and expand upon the concept as it relates to various duties concerned with donors and charitable organizations. It should be noted that this paper is not all inclusive in its treatment of the practice of good stewardship and the reader may find it to be too broad or too narrow in concept when relating to specific situations.

I. THE INITIAL CONTACT. Once your organization has received notice of a donor's interest, response should be immediate. To delay could result in a lessening of interest by the donor and the resultant loss of a potential gift. Response can be made by one or more methods as listed below:

A. TELEPHONE. A brief contact may be made by telephone to indicate receipt of the interest, notify of mailings, and establish a date and time for visitation. This type of contact may be less than satisfactory when a donor is handicapped by hearing loss or some other physical or mental impairment.

B. VISITS. Visits should be made as frequently as desirable or necessary to establish rapport with the donor, assist in the accomplishment of objectives, and to complete the gifting process. During these visits it is desirable to:

1. Listen, listen, listen.
2. Answer questions.
3. Determine the objectives of the donor.
4. Determine the needs of the donor.
5. Determine the donor's level of sophistication with regards to the gifting process.
6. Gather necessary data.
7. Review existing documents and financial records as requested by the donor.
8. Give receipts for documents, monies, or personal items entrusted to your care.
9. Inform and educate the donor as necessary and/or desirable concerning various plans for gifting, tax avoidance, etc. In this regard, it is desirable to move at the donor's rate of understanding and to be careful about being too technical or verbose.

II. IN YOUR OFFICE - AFTER THE INITIAL VISIT. A careful assessment of the objectives and needs of the donor should be made soon after the initial visit. Research may need to be undertaken and preliminary efforts begun for selection of the gift-planning team. At this time the following action may be taken:

1. Secure any monies, documents, or personal items entrusted to your care.
2. Obtain information from other sources as authorized by the donor.
3. Organize the data (set up file).
4. Prepare computations and illustrations for the donor and his or her advisors and accompany them with explanations of the material. Be careful not to overwhelm the donor.
5. Re-establish contact by telephone and/or mail and schedule the date, time, and place for the next visit.

III. ASSEMBLING THE TEAM. It is usually desirable and often necessary to assemble a team of professionals to assist in the gift planning process. Permission should be obtained from the donor, and his or her professional advisors should be included as team members if such is desirable and advantageous to the planning process. These professionals may include:

1. <u>You or the person from your organization</u> who is to act as the team leader.
2. <u>Attorneys representing the donor and your organization</u>. If the donor does not have an attorney or his attorney has a different specialty, the donor may request that you supply the attorney. If such is the case, it is desirable to proceed with caution making certain that a statement outlining potential conflicts of interest is disclosed in writing and signed by the donor. The donor should also request (in writing) the services of this attorney.
3. <u>The Donor's Accountant</u>. The accountant may have served the donor for many years and will likely be able to supply much information necessary for gift planning in addition to providing advice relating to tax matters.
4. <u>Insurance Advisor</u>. A knowledgeable insurance professional can be of great assistance in the gift planning process. This is particularly true when there is a need for, or the gift is to be made with, an insurance product.
5. <u>Brokers</u>. If securities are to be gifted, the donor's broker(s) may need to be involved. You may need to make certain that the broker understands the process and any implications or restrictions, e. g. timing of transfers.
6. <u>Trust Officer</u>. The trust officer of the bank or trust company utilized or chosen by the donor may need to be involved as a member of the planning team. This is particularly true if: a) he or she is already involved with the donor's financial interests, or b) his or her institution is to act as fiduciary.
7. <u>Financial Planner</u>. Many persons use the services of a financial planner. If a planner has already been retained by the donor, he or she may have reasonably adequate knowledge of the assets as well as the plans and objectives of the donor
8. <u>Appraiser(s)</u>. Appraisals may be required for valuation and/or substantiation of certain types of gifts. A qualified appraiser can be a valuable addition to the team.

You or the person representing your organization may assemble the gift-planning team and coordinate the activities of the team while acting as liaison between the professionals and the donor. It is desirable that certain precautions be observed:

1. Be knowledgeable about gifts and the gifting process.
2. Be sociable. Know how to "win friends and influence people." Sociability should be accompanied by honesty and concern. The use of tact and diplomacy is critical.
3. Be a leader. A leader involves others and does not attempt to do and be "all things to all people." It is desirable to recognize and use the talents and expertise of other members of the team.
4. Make the donor's welfare a priority. Become genuinely interested in the donor's welfare and objectives and attempt to accomplish that which is best for him or her.
5. Keep the donor informed. Do not assume that the donor understands or is in full agreement with all details of the gifting process. It is wise to maintain an open channel of communication with the donor.
6. Avoid undue influence. There may be opportunities to influence the donor. This may be particularly true when the donor is unsophisticated or of advanced age. It may be necessary to be candid and forthright with the donor or to withdraw to an "arms-length-distance" if such situations should arise.
7. Avoid the unauthorized practice of law. Occasions may present themselves wherein you are asked to advise or when you are tempted to offer advice. Sharing of information about the gifting process and the resultant affect upon the estate is helpful and desirable, but beware of practicing law unless you are licensed to act in that capacity.

IV. DOCUMENTS. Drafting documents may not appear to be a functin of stewardship. However, assuring that documents are drafted to meet the donor's objectives is a primary role of the steward. You will need to attend to the following:

1. Determine who should draft the document(s) - the donor's attorney, or the attorney who represents your organization?
2. Make sure the attorney is knowledgeable about charitable gifting
3. Proof-read the documents. Unfortunately, mistakes do appear -- sometimes typographical and sometimes of a more material nature.
4. Submit a draft to the donor for review. His or her reading of the documents may reveal a need for changes. It may also be necessary to provide explanations for legal terms and unfamiliar phraseology.
5. When the final draft is completed, proof-read it once again, and confirm that it indeed reflects the donor's intent.

V. EXECUTION OF THE DOCUMENTS. It is preferable that documents be executed under the supervision of the donor's attorney. There are instances, however, when the attorney is not present for this important part of the gifting process. When such is the case, it is desirable that all applicable safeguards be employed. At all times execution of documents should be in accordance with the laws of the jurisdiction.

VI. RETENTION OF DOCUMENTS. Documents must be kept somewhere. Will they be retained by the donor; the attorney, in a safe-deposit box; or in the vault of the charitable organization? It is wise to obtain and follow legal advice in this regard along with consideration of the donor's desires.

VII. OLD DOCUMENTS. It is not unusual for the donor to have in his or her possession a collection of old documents. He or she may have several wills, one or more trust documents, powers of attorney, insurance policies, and other documents of various kinds. Documents may be valid or they may be invalid in whole or in part. They may be in force or revoked. The donor may not be aware of problems which may exist. As a steward you may need to encourage the donor to have the documents reviewed by his or her attorney.

VIII. PAYMENT OF COSTS. Certain costs (often substantial) will be attendant to the gift planning process. These may include:

1. Consultation fees.
2. Appraisals.
3. Title searches.
4. Title insurance.
5. Environmental inspections and possible clean-up costs.
6. Documents.
7. Recording fees.
8. Taxes.
9. Insurance.
10. Management.
11. Accounting.
12. Investment fees or commissions.
13. Repairs and maintenance.

Who is responsible for payment of these and other costs? A good steward will make sure that responsibility for these costs is understood by all parties in advance of the gift.

IX. MANAGEMENT. Certain types of gifts require expert management on a continual basis. Who should undertake this responsibility? Should it be the donor, the charitable organization, or a professional fiduciary? Is the donor knowledgeable or otherwise capable? Will the donor's management taint the transaction from a tax standpoint? Can or should the charitable organization be involved? These questions must be answered and the case for management should be taken seriously. Management may include: investing, tax reporting, buying, selling, renting, and other activities. Improper or incomplete actions as a fiduciary may result in financial losses, tax penalties, civil and/or criminal actions, poor relationships, loss of friendship and trust, change to other fiduciaries, revocation of documents, and loss of charitable motive.

X. NURTURING. Stewardship is an ongoing process. After the gift has been made, it is desirable to maintain contact with the donor. This relationship may be called nurturing. It is characterized by a caring attitude which manifests itself in exhibiting a continued interest in the donor's welfare. It sometimes results in acts of kindness or service by the steward. It is not the intent of the writer to enumerate these acts or to express approval or disapproval of them. It should be noted, however, that the practice of good stewardship must include an awareness of situations which might provoke charges of undue influence or other infractions of the law.

Nurturing may help to cement relationships between the donor and your organization and may lead to additional gifting. An important aspect of this type of contact with the donor is communication which helps to eliminate misunderstandings and keeps the donor informed.

XI. POSTMORTEM ACTIVITIES. The stewardship process may continue past the death of the donor. It may be necessary for the steward to be involved in the settling of the donor's estate. This paper will not address the duties involved with estate administration. However, the practice of good stewardship in this regard may lead to good relationships with other family members or friends of the donor and may result in their desiring to establish a gifting relationship with your organization.

CONCLUSION: The practice of good stewardship is a thread which runs throughout the fabric of donor relationships. It begins with the first contact and may continue during and beyond the lifetime of the donor. It may take the form of a friendly visit or it may require attention to the details of management and fiduciary responsibilities. All donors cannot be forced into the same mold and the steward will find that the duties of stewardship require the ability to adapt as circumstances or needs may dictate. Those who practice good stewardship will experience the joy which comes from working with satisfied donors. They will realize the personal satisfaction of knowing that they have been of service to others, and great benefits may accrue to the organizations which they represent.

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GIFT OPTIONS WITH PERSONAL RESIDENCES

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Gift Options with Personal Residences

Why Gifts of Personal Residences?

Historically, real estate has proved to be one of the best long-term investments. Most experts quickly agree that despite the recent soft market in some areas of the country, a single-family residence is still one of the best investments available to the average individual, and it is one of the most widely held assets.

Assets of All U.S. Families

Principal Residence	32.2%
Other Real Estate	15.1
Financial (Stocks, bonds, bank accounts, etc .)	27.7
Business Ownership	17.8
Other	7.2
Total	100.0

Potential Pool of Donors

- 75% of Americans over sixty own their own homes
- 83% of this group own their homes with no debt
- By the year 2000, there will be 18 million Americans over sixty-five

Reasons Older Americans Move

- Present housing costs excessive
- Difficult to maintain
- House is too large
- Yard requires too much upkeep
- Inconvenience
- Weather severe—keeps me inside
- Too far from shopping centers, recreational facilities, places of worship, doctors' offices
- Children and friends have moved

Growth in value is certainly good news to those fortunate enough to have channeled part of their earnings and capital into real estate. Significant appreciation, however, also accentuates the potential tax problems associated with real-estate ownership when the time comes to dispose of it, whether during life or from an estate.

The Problem of Liquidity

Among the various pitfalls inherent to home ownership, probably none casts a darker shadow than the problem of liquidity. Simply stated: How quickly can a residence be converted to cash? A corollary problem to be considered is whether the seller realizes a fair price in the event of a quick disposition of the property.

Disposing of listed securities involves no greater effort than a call to your broker. The transaction is consummated within minutes and for a price that reflects the fair-market value of the securities on that day. On the other hand, disposing of a residence or other real estate—even a prime parcel—takes time, and when it is urgent to sell quickly, this could be a costly predicament. In the event of a forced sale, seldom will the seller receive what the property is really worth.

Certainly, the nonliquid nature of real estate can be troublesome and, in some instances, costly for its owner while he or she is alive. But it's at the death of an individual that the full force of the ***liquidity crunch makes itself felt***.

Sheltering the Appreciation

Most residential real estate has appreciated dramatically during the past several years. More of this appreciation can be preserved for investment because of the liberalized rule regarding taxation of the gain on the sale of a personal residence. An individual who is 55 or older may ***exclude from gross income up to $125,000*** of gain from the sale of his or her personal residence.

This exclusion is available on a ***one-time elective basis***. To qualify, an individual must have owned and occupied the property as his or her personal residence for at least three of the five years ending on the date of the sale. If the residence is jointly owned between spouses, only one of them must be 55 years old.

A married couple cannot make separate elections or double-up the exclusion. Furthermore, once a person participates in making the election, he or she is prevented from participating again, even if married to a new spouse who has not previously participated.

Note: There is no carryover for any part of the $125,000 exclusion that is not used. For example, Mr. Miller, 58, sells for $130,000 his residence, which he had purchased for $75,000. He elects to exclude his $55,000 gain. Mr. Miller cannot make this election again, and the remaining portion ($70,000) of the unused exclusion is lost to him forever.

Planning Opportunities with Charitable Gifts

Planned gifts to qualified charitable organizations can play a key role in mitigating the harsh effects of the liquidity crunch, as well as satisfying personal philanthropic objectives. A personal residence—because of its nonliquid nature—may be a particularly suitable asset to fund a planned gift. And there is a variety of ways in which a person can arrange a gift of a personal residence without jeopardizing his or her family's financial security.

The chart below shows possible options to consider. As you can see, each has certain benefits, depending on your personal and financial priorities.

RESULTS OF

TYPE OF TRANSACTION	TAXES	INCOME	CASH	RETAINED CONTROL
OUTRIGHT GIFT	****	—	—	—
GIFT THROUGH WILL	(*)	—	—	****
LIFE ESTATE	**	—	—	***
PROPERTY SUBDIVISION	***	*	*	***
UNITRUST FOR FAIR-MARKET VALUE	***	***	—	—
BARGAIN SALE (PART SALE/ PART GIFT)	***	—	**	—
INSTALLMENT BARGAIN SALE	**	**	**	—
GIFT OF UNDIVIDED PARTIAL INTEREST	***	—	—	***

Benefit Key: **** *Maximum* *** *Good*
** *Medium* * *Minor* (*) *Varies* — *None*

Outright Gift

Maximum tax benefits are, of course, realized through an outright contribution of a personal residence. First, the donor does not realize any taxable capital gain on the built-in gain.

An additional and equally important benefit is that the full fair-market value of such a gift is deductible for income-tax purposes up to 30% of an individual's adjusted gross income. Any contribution amount that exceeds the 30% limitation may be carried over for up to five years. These dual tax benefits combine to substantially reduce the cost of such charitable gifts.

Example: Mrs. Brown, who is in the 36% income-tax bracket, owns a personal residence worth $250,000 with a basis of $50,000.

If Mrs. Brown were to sell

FMV	$250,000
Basis	50,000
Capital gain	$200,000
Capital-gain tax 28%	$ 56,000
Real value of personal residence ($250,000 less $56,000)	$194,000
A gift of the personal residence would produce a charitable deduction of	$250,000
Income-tax savings in 36% bracket	$ 90,000
Cost of gift ($250,000 less $56,000 less $90,000)	$104,000
Potential estate-tax savings 55% of ($250,000 less $90,000)	$ 88,000

In many instances, family considerations preclude making an outright gift of a donor's entire interest in his or her real estate. However, there are several options available that allow a donor to transfer an undivided partial interest in the property ***or*** to defer the transfer until some time in the future.

Gift of personal residence subject to mortgage. When property subject to mortgage is gifted to a charity, the transaction is treated as a bargain sale for the amount of the debt, regardless of whether or not the charity assumes or agrees to pay the debt [Regs. Sec. 1.1011-2(a)(3)].

1. ***Example:*** Mr. Watson contributes a home worth $200,000 to charity. There is a $100,000 mortgage on the property. The transaction is treated as a bargain sale of the home for the balance of the mortgage debt ($100,000). Mr. Watson has made a gift equal to the difference between the fair-market value of the home ($200,000) and the balance of the mortgage debt ($100,000). In this case that difference is $100,000.

$$\text{Reportable Capital Gain} = \frac{\text{Mortgage x Gain}}{\text{FMV}}$$

2. If the donor continues to make payments on the debt, he or she is entitled to an income-tax charitable deduction for such payments as they are made.

Installment Bargain Sale

The amount of the "sale" in bargain sale can be paid in installments over a period of time. This spreads out the donor's return of the bargain-sale price and creates a source of income for the length of the installment agreement.

Example: Mr. Rich owns a personal residence worth $400,000.

He decides to make a bargain sale of the home to charity for $200,000 (his basis in the home). The purchase price will be paid to him in ten annual installments of $20,000, plus adequate interest. With this plan, Mr. Rich has accomplished his objective of making a substantial gift to charity and creating a source of income for himself.

Comparable to Gift Annuity. An installment bargain sale is comparable to a charitable gift annuity in many respects. The charity pays income to a designated beneficiary and the transaction generally qualifies for an income-tax charitable deduction; however, while Treasury Regulations only provide for gift annuities for the life of one or two beneficiaries, installment bargain sales can be created for any length of time agreeable to the donor and the charity.

Reporting gain on an installment bargain sale. When appreciated property is sold on an installment sale, long-term capital gain may be reported over the life of the contract rather than recognizing all of the gain up front. Under the installment sale provisions of IRC Sec. 453 a portion of each payment of the contract price is treated as a proportional payment of long-term capital gain. It is important to note that amounts that are recognized as ordinary income must be reported immediately in the year of the sale and may be spread over the life of the contract.

The portion of each payment that is recognized as gain is determined by dividing the total gain by the contract price. In the example of Mr. Rich above, the total gain attributable to the sale is $100,000 (or $200,000 times $200,000 over $400,000), and the bargain-sale price is $200,000.

Consequently, the ratio for the recognition of gain would be:

$100,000/$200,000 = 50%

This means that 50% of each payment of the principal amount of $20,000 due under the contract will be recognized as long-term capital gain.

Imputed Interest. If adequate interest is not stated in an installment sale contract, interest will be imputed [IRC Sec. 483(b)].

1. The "total unstated interest" will be the amount by which the total payments due under the contract exceed the present value of such payments.
2. In determining present value, a discount rate equal to the applicable Federal rate determined under IRC Sec. 1274(d) will be imputed. The specific rate depends on the term of the contract.
   a. Not over 3 years: Federal short-term rate.
   b. Over 3 years but not over 9 years: Federal mid-term rate.
   c. Over 9 years: Federal long-term rate.
3. There are several exceptions to the imputed interest rules provided for under IRC Sec. 1274(c)(3), including:
   a. Sale of personal residence.
   b. Sale involving total payments of $250,000 or less.

Gift of Undivided Partial Interest

While a donor may wish to make a charitable contribution of a parcel of real estate, the donor may also be reluctant to part with complete control over the property. There is a method under which a donor may be able to make a charitable contribution; secure an immediate income-tax deduction; and, at the same time, retain partial control over the property.

Generally, an income-tax charitable deduction is not allowed for a contribution (*not in trust*) of an interest in property that consists of less than the donor's entire interest in the property. ***However, there is an exception to this partial-interest rule.*** The exception specifies that a deduction is allowed for the value of an undivided portion of a donor's entire interest in the property. An undivided portion must consist of a fraction or percentage of each and every substantial interest or right owned by the donor in such property and must extend over the entire term of the donor's interest in the property.

Example: Mr. Walls wants to make a special gift to a charity whose work is meaningful to him. He owns a vacation home and had considered contributing the property. However, he uses the home for three months and does not wish to give up complete control over the property.

Mr. Walls decides to give the charity the right, as tenant in common, to possession and control over the property for a 25% portion of each year. Thus, Mr. Walls is able to use the home himself during part of the year, while making a charitable contribution and obtaining a valuable current tax deduction.

Note: The rules are quite specific with respect to what constitutes a completed gift of an undivided partial interest. Had Mr. Walls simply given the right to use the property for a portion of the year, no deduction would be allowed.

Bargain Sale

A donor who wants to recover a portion of the value of a personal residence that he or she wishes to contribute to charity may consider entering into a bargain-sale transaction with the charity. In effect, a bargain sale is a sale of property to charity for less than its fair-market value. The bargain sale price may be any amount mutually acceptable to the charity and the donor. Some donors are willing to sell the property for an amount equal to their cost basis. Then they recover their investment and get a deduction for the appreciation element. The tax law states, however, that the recovered portion cannot be treated wholly as basis, but rather as part basis and part reportable capital gain [Regs. Sec. 170-4(c)(2)(ii)].

There must be an intention on the part of the donor to make a gift to the charity.

Example: Mrs. Brown owns a personal residence appraised at $120,000, which she inherited from her parents. Her basis in the property is $40,000, and she offers to sell it to a charitable organization for that amount. As a result:

- Mrs. Brown receives $40,000 from the charity;
- she can deduct the contributed portion of $80,000 for income-tax purposes; however,
- she must also report a capital gain of $26,667. (The reportable capital gain is arrived at by dividing the sale price of $40,000 by the fair-market value of the property—$120,000—and multiplying the result by the gain—$80,000.)

$$\text{Reportable capital gain} = \frac{\text{Gain x Selling Price}}{\text{FMV}}$$

Qualified Appraisals. Generally it is necessary for a donor to file IRS Form 8283 when claiming an income-tax deduction in excess of $500 for non-cash gifts. If the deduction exceeds $5,000 (in most cases), the donors also must obtain a qualified appraisal to support and substantiate the deduction, and the appraiser must sign an appraisal summary statement on Form 8283.

If the property for which a donee charity has been presented an appraisal summary is sold by the donee charity within two years of receipt, the charity must file IRS Form 8282 disclosing the price for which the property was sold. A copy of this form must be furnished to the donor.

Unrelated Business Taxable Income. IRC Sec. 511 imposes a tax on a charitable organization's unrelated business taxable income. The Code defines this as any income derived from any unrelated trade or business regularly carried on by the charity [IRC Sec. 512(a)]. Included in the calculation of UBTI are income and deductions arising from certain debt-financed property.

1. Whether or not acquisition and disposition of the property by installment bargain sale constitutes an activity "regularly carried on" typically would be a question of fact. A number of factors, including the number and frequency of such transactions and the use to which the property acquired was put, would have an impact on the determination.

   a. IRC Sec. 512(b)(5) excludes gain from the sale, exchange, or other disposition of property from UBTI.

   b. The exception does not apply if property is held primarily for sale in the regular course of business.

2. Acquisition indebtedness, either in the form of acquiring property subject to debt or incurring a debt to the seller for the purchase price, could give rise to debt-financed income.

   a. There is specific exception for real property acquired by a qualified organization [IRC Sec. 514(c)(9)].

   b. There also will not be debt-financed income for purposes of UBTI upon the acquisition of property substantially all the use of which is substantially related to the exempt purposes of the organization [IRC Sec. 514(b)(1)(A)].

Hazardous Substances. The Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA) imposes liability for clean up of hazardous substances on owners of real estate regardless of whether or not the current owner actually caused the problem. There are few defenses to this liability. It is imperative that a charitable organization take adequate steps to determine if real property it may acquire by gift is contaminated. There are a number of firms that conduct environmental audits for this purpose.

Marketing Appeal of Installment Bargain Sale

Creation of a source of income. An installment bargain sale allows the donor to turn an asset into a source of income. Depending on the donor's goals and the nature of the asset, the installment bargain sale may offer significant advantages over other types of retained-income gifts.

Term certain. The installment bargain sale allows the donor to know exactly how long payment will be made and in what amount. This degree of certainty generally is not available with charitable gift annuities in which payments terminate at the death of the beneficiaries.

THE TEN PLAN

Courtesy of Anderson University
Anderson, Indiana

Bob Coffman owns a residence valued at $100,000 which he is interested in transferring to charity in exchange for a life-income plan. The gift annuity approach appeals to him. But not being in the best of health, he would like to see the payments continue to his beneficiaries for a reasonable period of time after his death.

THE TEN PLAN TO THE RESCUE

- Guaranteed source of income, $10,000 a year over 10 years
- Guaranteed recovery of entire FMV of property, $100,000 after 10 years
- Tax savings, $34,217 charitable deduction for year of gift plus carryover years
- Satisfaction of making significant gift to charity.

BENEFITS TO DONOR

- Donors can use their real estate assets to make a significant contribution.
- TenPlan offers a guaranteed sales price, gift deduction, and income for ten years.
- Donors control the sales process by selecting closing and move out dates.
- TenPlan pays all closing costs and brokerage commissions.
- The transaction is simple, convenient, and hassle free. Donors don't need to:
    - ► compare and select brokers
    - ► prepare their home for marketing
    - ► interrupt lifestyle by showing property
    - ► negotiate commission or sales price
    - ► attend closing

EXAMPLE

If the owner were to sell house for		$100,000
Real estate commission & expenses		<10,000>
Net proceeds		$ 90,000
TenPlan payments present value	$65,783	
In 36% bracket, charitable deduction of $34,217 produces tax savings	12,318	
Total benefits		$ 78,100
Out-of-pocket cost of gift		$ 11,900

MECHANICS OF TENPLAN

1. Charity has the house professionally appraised at no cost to donor. For purposes of this example, assume that the property was appraised at $100,000.
2. A closing date of donor's choice can be established once donor and charity agree on the appraisal.
3. Charity agrees to make payments totaling $100,000 or 100% of the appraised value of the property over ten years.
4. Donor receives installment payments of $2,500 a quarter (1/40 of $100,000). Donor may also specify monthly, semiannual, or annual payments.
5. The installments are guaranteed to donor or donor's beneficiaries.
6. All closing costs are paid by charity.
7. The installment contract typically creates a deductible gift to charity of approximately 34% (in our example, $34,000).
8. Over the life of the contract, approximately 66% of all installment payments are tax-exempt return of principal (in our example, $66,000). The balance is interest taxable as ordinary income.
9. Many donors over 55 pay no capital-gain tax by using the one-time exclusion. Other donors can reduce their gain tax and pay it over the life of the contract.
10. A significant gift is created for charity's benefit.

RESULTS

Anderson University received approximately $3,000,000 worth of property under this program.

RESALE EXPERIENCE—Average resale price of properties sold is over 101% of the value at which they were taken into the program.

- This is extremely important!! You must have accurate realistic valuations of the property coming into the program, and you must have a realistic assessment of your ability to resell the property in a reasonable time frame.

- Anderson University has sold many of the properties on its own without having to pay real estate commissions. Some properties have been resold within a few days of receiving them.

- Very few properties have been on the market an inordinantly long period of time.

SURVEY OF THE TENPLAN DONORS
(Rationale for Selecting the TenPlan)

- Simplicity
- Convenience
- Guaranteed Payments
- Beneficence
- Privacy
- Personal Attention
- Timing
- Recognition
- Tax Advantages

Gift of a Remainder Interest in a Residence or Farm

The owner of a personal residence or farm may give the property to a charitable organization while retaining the right to occupy the residence or operate the farm for life or a term of years {Regs. Sec. 1.170A-7(b)(3)].

Such a gift of a remainder interest provides an income-tax charitable deduction for the present value of the remainder interest that frees up tax dollars into spendable income without causing any disruption in the donor's lifestyle. In addition, this plan permits the donor to escape any potential capital-gain tax on the built-in appreciation [Regs. Sec. 1.170A-7(c)].

The term ***personal residence is broadly defined*** in the Regulations to include any property used by the taxpayer as a personal residence even though it is not used as the donor's principal residence. A single-family dwelling, condominium, vacation home, or stock owned by the donor as a tenant-stockholder in a cooperative housing corporation qualifies as a personal residence if used each year by the donor. The term farm includes any land used by the donor or the donor's tenant for the production of agricultural products or for the sustenance of livestock [IRC §170(f)(3)(B)(i)].

Example of a Gift of Remainder Interest

Mrs. Hanson, 75, a widow, has lived in her present home for many years and has no plans to move. She has included a provision in her will that leaves her home to a charity, but that arrangement results in no current income-tax savings. To obtain present tax relief without altering her lifestyle, Mrs. Hanson gives the home to charity, while retaining the right to live in the home for life.

At the time of the gift, the residence is appraised at $500,000 (the land is valued at $100,000; the structure is worth $400,000). Her basis in the residence is $200,000.

Charitable income-tax deduction*	$204,810
Income-tax savings in 40% bracket	$81,924
Potential capital-gain tax avoided (28% of $300,000)	$84,000
Potential estate tax avoided (55% of $500,000)	$275,000

**Estimated useful life 45 years, salvage value $83,335.*

In the event she decides to move in the future, she has several options: rent the property and collect the rents, give her life interest in the home to the charity in exchange for a life income, or simply give her life interest outright and receive another deduction.

Variations on a Gift of a Remainder Interest in a Residence

a. ***Exchange value of remainder interest for a gift annuity*** (not permissible in all states)—see Letter Rulings 8806042 and 8120089—Mrs. Hanson is interested in additional income to offset increase in the costs of maintaining her home.

Under proper circumstances and where permissible, charity may agree to exchange the value of the remainder interest represented by the amount of the charitable deduction. To protect its interest, charity may offer say a 7% rate, lower than the 7.7% recommended rate. ***As a result—***

Mrs. Hanson, age 75

Principal Donated	$204,810.00
Cost Basis—40% (*$200,000 over $500,000*)	$81,924.00
Annuity Rate, quarterly at end of period	7%

BENEFITS:

• Charitable Deduction (*9.4% discount rate*)	$118,965.94
• Annuity	$14,336.70
Tax-free Portion	$2,769.85
Capital-Gain Income	$4,154.78
Ordinary Income	$7,412.07

Total reportable capital gain of $51,506.44 must be reported in equal installments of $4,154.78 over 12.4 years (*the expected lifetime of the donor age 75*).

After 12.4 years, when the investment in contract has been fully recovered, the entire annuity becomes ordinary income.

- The right to live in and enjoy her home for life.

b. ***Bargain sale of remainder interest to charity***—Such a transaction was approved by IRS in Letter Ruling 8134106. Tax results are as discussed earlier in bargain-sale section.

c. In *five years* Mrs. Hanson, now 80, decides it's ***time to move***. The home is now valued at ***$600,000***. The following options are available.

1. **Gift of life estate to charity—**

Mrs. Hanson is now entitled to an income-tax deduction for the value of the life estate computed on the FMV of the home at $600,000 and her age of 80.

structure $470,000, land $130,000, salvage value $117,500, 45 years

Value of remainder	$301,697
Value of life estate	$298,303
Income-tax savings in 40% bracket	$119,321

Charity is now sole owner of residence.

2. **Sale of life estate to charity—**

Mrs. Hanson would receive	$298,303
Realized capital gain 2/3	$198,869

Can apply $125,000 exclusion if available.

(*See* Rev. Rul. 84-43, IRB 1984-13,5)

3. **Joint sale of residence by Mrs. Hanson and charity—**

Charity would receive value of remainder	$301,697
Mrs. Hanson would receive value of life estate	$298,303

Can apply $125,000 exclusion if available.

(*But see* Rev. Rul. 77-305, 1977-2 CB 72)

4. **Exchange of life estate for a gift annuity—**

Basically what you have at the end of this arrangement is a ***gift annuity in exchange for the entire residence***. (Again, this is not permissible in all states.)

Mrs. Hanson, age 80

Principal Donated	$298,303.00
Cost Basis	$49,717.00
Annuity Rate, quarterly at end of period	*8.8%*

BENEFITS:

• Charitable Deduction (*9.4% discount rate*	$166,456.06
• Annuity	$26,250.66
Tax-free Portion	$2,336.30
Capital-Gain Income	$11,681.55
Ordinary Income	$12,232.81

Total reportable capital gain of $109,872.53 must be reported in equal installments of $11,681.55 over 9.4 years (*the expected lifetime of the donor age 80*).

After 9.4 years, when the investment in contract has been fully recovered, the entire annuity becomes ordinary income.

See Revenue Ruling 84-83 as to availability of $125,000 annual exclusion.

5. **Transfer of life estate to a unitrust**—This option is most appropriate when

   - donor's gain exceeds the $125,000 exclusion sufficiently to create a tax problem,

   - donor has used the exclusion, or

   - donor lives in a state (e.g. New York) that does not permit exchange for a gift annuity.

   If donor has exclusion available, it may be preferable to sell life estate or jointly sell residence with charity and contribute cash. This would also allow donor to go under 50% ceiling.

6. **Rent the personal residence**—Mrs. Hanson can rent her home and collect the rent for the remainder of her life. Charity could continue rental after Mrs. Hanson dies.

Odds and Ends:

1. Donor gives remainder interest in her residence to her husband under her will. She directs that at death of husband residence to be sold, proceeds distributed to charity. Does gift qualify for estate-tax charitable deduction? See Rev. Rul. 83-158, 1983-2 CB 159; **Est. of Blackford,** 77 TC 1246 (1981).

2. Donor owns a residence on 200 acres. He contributes 75 acres that include residence, pool, gym, garages, and kennel to charity reserving life estate. Rest of property pastures and woods. Is deduction allowed? Letter Ruling 8202137.

3. Donor reserves life estate in residence. Remainder 90% to charity, 10% to individuals. Deductible? Rev. Rul. 76-544, 1976-2 CB 288 and Letter Ruling 8341009; reversed in Rev. Rul. 87-37, 1987-1 CB 295.

4. Donor places residence in trust, receives life estate in trust. Is charitable deduction allowed? See **Est. of Cassidy**, 49TCM580 (1985).

5. Is deduction allowed for a retained interest in a residence including fixtures, household furniture, and other tangible property? Rev. Rul. 76-165, 1976-1 CB 279.

6. Gift of remainder interest in partially leased residence, is a deduction allowed? See Letter Ruling 8711038.

7. Life tenant has power to sell residence, remainder or proceeds to charity. Deductible? Letter Ruling 8810004.

8. Does gift of remainder interest in a residence outside U.S. qualify for charitable deduction? Letter Ruling 8411059.

9. In Letter Ruling 9329017, donor gifts remainder interest in farm.

FMV	$110,000
Mortgage	80,000

- Deduction in remainder interest value of $30,000
- Future payments of principal on the mortgage treated as additional gifts of remainder interest.
- The **full** amount of the mortgage ($80,000) has to be taken into account in computing reportable capital gain.

$$\text{Capital Gain} = \frac{\text{Mortgage x Appreciation}}{\text{FMV}}$$

Charitable Remainder Trusts and Pooled Income Funds

The **charitable remainder trust** (CRT) is similar to other types of trusts except that the amount distributed at its termination (***the remainder*** in legal parlance) is paid to a charitable beneficiary. A donor transfers property irrevocably to a trust and specifies: •the amount of income to be distributed, •to whom it is to be paid, •the duration of payments (a period of years or the beneficiary's lifetime), and •the charity that will receive the remainder.

A similar plan is the **pooled income fund** established by a charitable organization. The fund pools the irrevocable gifts of many donors who name the beneficiaries to receive income throughout their lifetimes. ***The pooled income fund is seldom, if ever, a suitable vehicle for a personal residence.***

These plans may become effective through outright transfers during the donor's lifetime or through transfers at death under the owner's will. To qualify for the charitable deductions available under federal tax law, a transfer of a residence in trust must conform to the requirements of a CRT.

An important feature common to all these arrangements is that they offer an escape from the age-old investment dilemma of the "locked-in" position: a donor may want to dispose of a personal residence for various reasons (*e.g.*, ***to protect a profit or to reinvest for a higher yield***) but is inhibited from acting because of the potential capital-gain tax on the appreciation.

Funding a charitable remainder trust with a personal residence can augment the available tax benefits because the grantor can avoid the potential capital-gain tax that would result from an outright sale of the property. Avoidance of capital-gain tax coupled with a current charitable income-tax deduction can substantially reduce the cost of such a transfer.

The larger the amount of appreciation in excess of the $125,000 exclusion (assuming it is available), the more attractive are the tax benefits of funding a CRT with a personal residence.

If the exclusion covers the appreciation, then the donor is better off selling the residence and funding the trust with cash. Of course, this option ignores the effect of the costs of selling that would be shifted from the trust to the donor.

When may a CRT be an appropriate choice for a personal residence?

- State law prohibits accepting a personal residence in exchange for a gift annuity.
- Charity unwilling to accept risks of disposing of assets.
- Donor has used $125,000 exclusion.
- There is substantial appreciation in value over $125,000 exclusion.
- The donor no longer wishes to occupy residence.
- It is a second or even third personal residence, and a "younger" donor wishes to use it to fund a retirement plan.

Clearly, the CRT of choice is the income-only unitrust with make-up because it provides the trustee with the luxury of time to dispose of the personal residence.

Odds and Ends

1. When is a regular unitrust appropriate?

2. How can trustee pay insurance costs, property taxes, and other expenses if trust does not generate income? Can it borrow funds?

3. Can NIMCRUT switch to regular unitrust after personal residence is sold? See Letter Ruling 9506015.

4. Can the trustee of a NIMCRUT be authorized to allocate realized capital gain of unproductive assets to income? See Letter Ruling 9442017.

5. Can the trustee of a CRT locate a buyer and negotiate terms of sale of personal residence in anticipation of receiving the gift?

6. Can donor continue to live in a residence and pay fair-market value rent after it goes into CRT? Reg. Sec. 53.4941(d)(2)(b).

7. What if personal residence has mortgage on it? See Letter Ruling 9015049.

8. Can donor be trustee of CRT funded with personal residence?

Procedural Requirements

1. ***Qualified appraisal.*** Each transaction requires the donor to obtain a qualified appraisal of the real estate. As a practical matter, the charity usually works with donors in locating qualified appraisers and in helping the appraiser understand the requirements of a qualified appraisal for the purpose of substantiating an income-tax charitable deduction.

2. ***Form 8283.*** The donor must file IRS Form 8283 to substantiate the deduction claimed as a result of the transaction, and the appraiser must sign the appraisal summary portion of the form.

3. ***Form 8282.*** If property is sold within two years of the date of the gift, the charity must file IRS Form 8282 indicating the price for which the property is sold. A copy of the form must be sent to the donor.

BEQUESTS AND OTHER REVOCABLE GIFTS

Presented by Ellen G. Estes

I. Background

A. Why might a donor prefer to make a gift that is revocable?

1. Fear of irrevocably parting with assets that may be needed later on -
   (a) Fear of outliving resources needed to provide for self or family
   (b) Fear of the unknown - possible expensive last illness or other disaster that would require access to funds

2. Donor does not need a current charitable deduction. Either donor does not itemize, or donor has made all of the charitable gifts that he or she will be allowed to deduct currently.

3. Donor has concerns about the organization itself: Is the charity viable in the long run? Will the donor's gift be used prudently and properly by the charity in furtherance of its mission? The donor may wish to see how the charity behaves over time before making an irrevocable commitment.

4. Donor wants the luxury of being able to "change my mind" if circumstances change.

B. Why should your organization promote revocable gifts?

1. This is often the only way a donor can make a major gift. For example, a bequest will often be the largest gift a donor will ever be able to make. However, the donor may be able to make that commitment comfortably only if the gift can be revoked should circumstances change during his or her lifetime.

2. Discussing revocable gifts with donors can begin a continuing relationship between the donor and the charity that will lead to irrevocable gifts later on. These discussions are part of the cultivation process that will encourage your donors to become more involved and interested in your organization and its mission.

3. With the highly-touted potential transfer of wealth from parents to baby boomers (estimated to be somewhere between $8 and $10 trillion by the year 2020), it will be important for non-profit organizations to tap into this financial resource. In many cases, the only gifts that the recipients of this wealth will be prepared to make will be gifts that are revocable.

II. Bequests - The Most Important Planned Gift of All

A. What they are and how they work

1. A bequest is a gift under a person's Will.

2. In preparing a Will an individual decides how he or she would like to distribute assets upon death, and works with an attorney to draft a Will that will fulfill his or her family, financial, and charitable objectives. The assets can go to individuals, charitable organizations, or a combination of both.

3. If a person dies intestate (without a Will) the laws of that person's home state will determine who gets his or her assets, and that statutory distribution may have no relationship to the donor's wishes, desires, or plans. Therefore, it is important for everyone to have a Will. And, you will be doing your constituents a service to remind them about the importance of Wills, whether or not you are named as a beneficiary.

B. Charitable Bequests can take several forms:

1. *Outright* - an unconditional outright gift. (For example, "I give and bequeath $25,000 to the ABC charity, located at 123 Main Street, Anywhere, USA, to be used for its general purposes.")

2. *Residuary* - A gift of all or a portion of the residuary estate (the assets that remain after specific bequests to others, taxes, etc. have been paid). (For example, "All the rest, residue and remainder of my estate I give as follows: 1/2 to my wife, Alma, and 1/2 to the XYZ School, located in Learningsville, PA., to be used for scholarship purposes.")

3. *Contingent* - A bequest that will come to your organization only if a contingency occurs. (For example, "I give $10,000 to my cousin Susie, but if Susie predeceases me, I give that amount to the Get Well Hospital Foundation, located in Feel Good, CT, to be used for its arthritis unit.")

4. *Bequest to Endow the Donor's Annual Gift* - A donor can make a bequest that is 20 times his or her annual gift. The charity will then invest the gift as part of its endowment, and will credit the income each year to the annual fund in the donor's name. If the endowment earns at least 5% annually, this bequest will generate an amount equal to the donor's regular annual gift each year. The bequest, will, in effect, "endow" the donor's annual gift, and make it live on --- in perpetuity.

5. *Bequest of a Remainder Interest* - A donor can set up a Charitable Remainder Trust or make a gift to a Pooled Income Fund by Will, providing income to a named individual for life, remainder to your organization.

6. *Bequest of an Income Interest* - A donor can set up a Charitable Lead Trust by Will, providing income to your organization for a specified period of time, with the remainder to family members. (For example, Jackie Onassis set up a Lead Trust under her Will, providing "an annuity amount" equal to "eight percent (8%) of the initial net fair market value of the assets" to charities for 24 years, with the remainder going to family members.)

7. *Bequests in conjunction with lifetime gifts* - For example, a donor can set up a Charitable Remainder Trust during her lifetime, the remainder of which is to be used to fund a professorship upon her death. The balance of the professorship can be funded through a bequest in the donor's Will. Both gifts will become effective at the same time --- and fully fund the professorship upon the donor's death.

C. Key Features. Bequests are -

1. Easy to understand. Most people are familiar with the concept of Wills.

2. Easy to promote. You can use simple materials and talk with prospects of any age about any kind of assets and any form of gift.

3. Not affected by changes in the economy. People do estate planning even in difficult economic times, to preserve and protect themselves and their families now, and in the future.

4. Non-threatening. Donors do not have to part with anything during lifetime.

5. Inexpensive for your organization to promote. There are minimal pre-transfer stewardship and management costs. However, make sure to continue to cultivate and communicate with all donors who tell you that they have included your organization in their estate plans.

6. Often the largest gift an individual can make - *the ultimate gift*.

D. Benefits for the Donor

1. Most personal form of charitable giving. During the estate planning process the donor has time to reflect on what is important and meaningful, and can consider ways to preserve and protect what is important for the family and for favorite charities.

2. Charitable bequests enjoy unlimited Federal estate tax deductibility. No percentage limits as under the income tax.

3. The donor can bequeath any asset to any charity. No "related vs. unrelated" issues to deal with.

4. A Will preserves confidentiality. No one need know what is in a Will during the donor's lifetime.

5. A Will provides simplicity. There are no complicated tax rules to apply.

6. Minimal cost to the donor. Putting in bequests to favorite charities is just one element of the estate planning process, and does not add much to the overall cost of making a Will.

7. Can provide contingency protection. If a family member predeceases the donor, that person's bequest can go to a favorite charity or charities.

8. Revocable. The donor has the comfort of knowing that he or she can always change the Will if circumstances should change.

E. Benefits to your Organization

1. Bequests are easy to understand and easy to promote.

2. Starting a bequest program will enable you to begin a long-term cultivation of your donors and prospects that will lead to larger (and often irrevocable) gifts later on.

3. Starting a bequest program NOW will ultimately provide an on-going source of funding to endow your organization's future.

III. <u>Revocable Charitable Remainder Trusts</u>

A. What they are and how they work

1. Revocable charitable remainder trusts are trusts that pay income to a donor (and another person, if appropriate) for life. The donor retains the right to receive all of the trust's net

income, to invade principal, and to terminate the trust at any time. After the lifetime of the donor, if the trust has not been revoked, the trust assets will go to the charity or charities named in the trust agreement. Revocable charitable remainder trusts can often be an attractive supplement to a Will.

2. To establish the trust the donor transfers assets to a Trustee who will manage and invest those assets and make payments to the donor (and another named by the donor, if appropriate) for life. The donor (and/or other income beneficiary) can receive the entire net income from the trust for life. The trust agreement will also specify that the donor reserves the right to invade principal and to revoke the trust at any time. Upon the death of the donor, if the trust is still in existence, the trust becomes irrevocable, and, after the expiration of any other life income interests, the assets go to the charity(ies) named in the trust agreement.

B. Key Features

1. The income beneficiary(ies) can receive all (or part of) the net income earned by the trust for life.

2. Additional contributions can be made to the trust at any time.

3. Unlimited withdrawals can be made from the trust at any time.

4. Since the trust can be revoked, the donor does not get an income tax deduction for setting it up, nor will the donor avoid capital gains taxes if appreciated assets are transferred to the trust.

5. The donor can make the trust irrevocable at any time, by amending the trust agreement so that the trust qualifies as a charitable remainder unitrust or a charitable remainder annuity trust. Once this is done, the donor will be entitled to the tax and other benefits related to irrevocable charitable remainder trusts.

6. If the trust is still in existence when the donor dies, the assets will go to the charity(ies) named by the donor in the trust agreement. The donor's estate will then be entitled to a Federal estate tax deduction for the charitable gift.

C. Benefits for the Donor

1. The donor (or other income beneficiary) can receive all of the net income earned by the trust.

2. The revocable trust provides maximum flexibility. If the donor's circumstances should change and the donor needs the assets, he or she can revoke the trust and re-acquire the assets. The donor can also invade principal at any time, providing protection against future unknown contingencies.

3. The donor can act as trustee of the trust, and manage and invest the trust assets, if desired. On the other hand, the donor may prefer to choose a corporate trustee to provide professional management of the trust assets, thereby relieving the donor of these responsibilities.

4. There is no income tax deduction for this gift, since the trust can be revoked at any time. However, if the trust is in existence at the time of the donor's death, the assets will

go to charity, and the donor's estate will be entitled to a Federal estate tax deduction for the charitable gift.

5. The donor can make the trust irrevocable at any time by amending the trust agreement so that the trust qualified as a charitable remainder unitrust or a charitable remainder annuity trust. If the donor does this, he or she will be entitled to all of the tax and other advantages of irrevocable charitable remainder trusts.

6. The trust assets will not have to go through probate.

D. Benefits to your Organization

1. A way to encourage your donors and prospects who cannot part with income or assets now to make a gift for the future benefit of your organization. This revocable trust arrangement can often provide large gifts that would not otherwise be received.

2. A good cultivation tool. Talking with donors about revocable trusts can get them thinking about your organization's long-range future, and can help to build the relationship.

3. May lead your donors to make other irrevocable gifts during lifetime, as well as to consider making the "ultimate gift" later on.

4. Promoting revocable trusts as a gift option can help provide endowment gifts later on, to preserve and protect your organization's future.

E. <u>Example</u>

<u>THE REVOCABLE TRUST</u>

<u>SITUATION</u>

Mr. Black, a widower in his 70's, is a retired investment banker. One of his greatest pleasures is following the stock and bond markets closely and overseeing his considerable portfolio of investments. Mr. Black has also been a strong supporter of several charities over the years. He would like to make a significant gift to a favorite charity, but is concerned about irrevocably parting with assets now that he is getting older and may face the possibility of long-term medical care and expenses later on.

<u>SUGGESTION</u>

Have Mr. Black set up a trust now which he can revoke at any time. The trust will pay income to him as he needs it, and he can invade principal, if he so desires. Mr. Black can be the Trustee of his trust, thereby enabling him to continue to manage and invest his portfolio. After his lifetime, the trust assets will be distributed to the charity.

<u>BENEFITS</u> - By establishing the trust during his lifetime the donor can -

- Maintain complete control over the management and investment of his assets.

- Revoke the trust at any time and re-acquire the assets, thereby providing maximum flexibility and security during his retirement years.

- Choose a successor Trustee to step in and continue to manage the trust for the benefit of the donor in the event of an accident or illness - providing an effective plan for continuing the management of his financial affairs.

- Avoid probate of the trust assets. If the trust is still in existence when the donor dies, the assets will be distributed to the charity in accordance with the terms of the trust agreement - and will not have to go through probate.

- Save estate taxes. If the trust is in existence when the donor dies, the assets will go to the charity, and the donor's estate will be entitled to a charitable deduction.

- Make a major gift to his favorite charity.

IV. Interest-free Loans - Repayable on Demand

A. What they are and how they work

1. A generous individual can benefit a favorite charity by making an interest-free loan to the organization, repayable on demand.

2. So long as the loan amount to any given charity does not exceed $250,000, and the purpose of the loan is to benefit the charity (not for tax-avoidance motives), the donor will have no adverse tax consequences because of the arrangement. (If the loan amount exceeds $250,000, or the transaction is deemed to have been made to avoid taxes, the donor will have adverse tax consequences: the donor must include "phantom interest" in his or her taxable income, based on a statutory rate of interest, reflecting what should have been charged on the loan if it had been made in an arm's length transaction. See IRC Section 7872.)

3. Later on, the donor can "forgive" the loan, and the charity will then get to keep the "loaned" amount. If the donor does this, the donor will be entitled to a Federal income tax deduction for making a gift at that time.

4. During the period that the loan is outstanding, the charity will receive all of the income generated by the loaned amount. The donor will avoid paying taxes on that income.

B. Key Features

1. Donor lends a significant amount of cash, interest free, to a favorite charity, to help the organization meet current expenses, etc.

2. Donor reserves the right to call the loan on demand.

3. The charity can use the income generated by the loaned amount for its exempt purposes.

4. The donor can always call the loan and get the principal back if he or she needs the money for personal use, or if circumstances otherwise change.

5. The donor does not get an income tax deduction for making the interest-free loan to charity. However, since the donor has parted with the loaned assets (usually cash), the donor will not be taxed on the income generated by those assets.

6. If the donor later "forgives" the loan, he or she will be entitled to an income tax deduction for the "gift" at that time.

C. Benefits for the Donor

1. Satisfaction of providing financial assistance to a favorite charity - at least for a short time.

2. Since the loan is payable on demand, the donor can always regain the principal if he or she needs the money for personal use.

3. Donor will avoid paying tax on the income generated by the loaned amount.

4. Donor could use this arrangement as a way to "endow" his or her annual gift.

5. This is an appropriate option for donors who do not itemize deductions, or for donors who cannot use additional charitable deductions currently.

D. Benefits to your Organization

1. A way to increase your financial security immediately.

2. A way to cultivate donors and help build the relationship, hopefully leading to additional irrevocable gifts later on.

3. A way to encourage donors to endow their annual gifts, simply and easily.

E. Example

AN INTEREST-FREE LOAN - REPAYABLE ON DEMAND

SITUATION:

Mr. and Mrs. Smith, both in their 70's, have been making gifts of $500 per year to their church. They would like to continue supporting the church, now and in the future, but are concerned about making an irrevocable commitment at this time.

SUGGESTION:

Make an interest-free loan to the church, repayable on demand, in the amount of $10,000 (20 times their annual gift of $500). If the church can invest the cash for a return or at least 5%, the loan will produce $500 each year for the church, to be added to the annual fund in the donors' names, relieving them of the necessity of writing out a contribution check each year. In the event of an emergency or other change in their circumstances, the donors can call the loan and get the $10,000 back. They can also provide that the loan is to be canceled upon the death of the survivor of them, and at that time, the $10,000 is to be added to the church's endowment, to endow their annual gift in perpetuity.

BENEFITS:

1. Donors do not have to write checks to the church each year, since their annual gift is now covered by the income generated by the loan. Donors will continue to get full credit as $500 annual donors to the church.

2. Donors can call the loan at any time, in the event that their circumstances should change and they need to get the $10,000 back.

3. Donors may also enjoy some tax savings as a result of the loan. Let us assume that the donors had been receiving interest of $500 per year on their $10,000 savings account balance, paying tax on that $500 (in the amount of $140 in their 28% bracket), and then making a gift of that $500 to the church each year. Let us further assume that the donors do not itemize deductions on their income tax return, so that they do not get any tax benefit from their annual gift to the church. If the donors now take that $10,000 and use it to make an interest-free loan to the church, they will no longer be taxed on the $500 income, so that they will enjoy some tax savings as a result of the loan.

4. Donors can provide that if the loan is still outstanding at the time of the death of the survivor of them, the loan will be forgiven, thereby creating a permanent gift that will "endow" their annual gift to the church in perpetuity.

5. Here, the donors are able to make a major financial commitment to their church, benefiting the church during their lifetimes, as well as benefiting the church in the future when the loan is forgiven.

V. Life Insurance

A. How this gift can work

1. A donor may wish to name your organization as the primary beneficiary of his or her life insurance policy, reserving the right to change beneficiaries at any time.

2. Alternatively, a donor may wish to name your organization as a contingent beneficiary of his or her life insurance policy, to receive the insurance proceeds if the primary beneficiary should predecease the donor.

3. The donor is not entitled to an income tax deduction for these revocable/contingent designations. However, if the life insurance proceeds actually do go to charity at the donor's death, the donor's estate will be entitled to a charitable deduction for the gift.

B. Benefits for the Donor

1. Donor retains maximum flexibility, since he or she can always change the beneficiary, as circumstances dictate.

2. Donor may be able to make a major gift to a favorite charity, simply and easily.

C. Benefits to your Organization

1. It is a non-threatening way to encourage donors and prospects to think about making a significant gift to your organization.

2. It is a good cultivation tool. Can bring the donor closer to your organization, and may lead to irrevocable gifts later on.

VI. Qualified Retirement Plan Assets

A. How this gift can work

1. Please note that the tax rules governing qualified retirement plans are extremely complicated. While we will not go into details here, you should remember that there may be a substantial potential income tax burden for heirs who inherit moneys from qualified plans. Therefore, it is often much better, from a tax standpoint, to give these plan assets to charity, and to give other assets to heirs. (For an excellent in-depth discussion of the rules regarding gifts of retirement plan assets, please refer to the presentation made by David Wheeler Newman and Reynolds T. Cafferata at the 1994 National Conference on Planned Giving, printed in the 1994 NCPG Conference Manual, page 215.)

2. Therefore, a donor may wish to give retirement plan assets to charity under his or her Will. This must be done very carefully, to comply with all of the tax rules. The attorney/estate planner must be an expert on all of these rules in order for the gift to work.

3. Alternatively, when the qualified plan permits it, a donor may be able to name a charity as beneficiary under the plan itself.

4. Another option may be to set up a charitable remainder unitrust by Will, funded by plan assets. Again, this must be done carefully so as to comply with all of the rules.

B. Benefits for the Donor

1. If gift is structured properly, donor's heirs may be able to avoid income taxes because of the gift.

2. Donor may be able to make a substantial gift to a favorite charity at a very low cost to heirs.

C. Benefits to your Organization

1. It is a non-threatening way to encourage donors and prospects to think about making a significant gift to your organization.

2. It is a good cultivation tool. Can bring the donor closer to your organization, and may lead to other kinds of irrevocable gifts later on.

VII. Charitable Lead Trust - a "Temporary" Gift

A. What they are and how they work

1. The charitable lead trust is the mirror image of a charitable remainder trust. The lead trust pays *income to charity* for a specified period of time (either for a specified number of years, or for the lifetime of an individual). When the trust ends, the trust assets go to the individual(s) (usually family members) named by the donor.

2. There are several different kinds of Lead Trusts. However, the *non-grantor lead trust* is the one we will focus on here.

3. Although the lead trust must be irrevocable in order to produce the important tax benefits for the donor's family, the gift to charity is temporary, and the trust assets later go to the donor's heirs, often at substantial savings in gift and estate taxes.

B. Key Features

1. The donor transfers assets to a trustee that will manage and invest those assets and make payments at least annually to one or more qualified charitable organizations named by the donor.

2. The annual payment to the charity must be either an annuity amount (Charitable Lead Annuity Trust) or a unitrust amount (Charitable Lead Unitrust.)

3. When the trust ends (either at the end of a specified number of years, or upon the death of a named individual), the remaining assets go the donor's family. Because charity has benefited up front, the trust assets can often go to the donor's heirs later at substantial savings in Federal gift and estate taxes.

4. There is no Federal income tax deduction for the donor who establishes a non-grantor charitable lead trust. However, the donor does receive an income tax "benefit", since the income generated by the non-grantor lead trust is not considered to be "income" to the donor, and, therefore, is not taxed to the donor.

5. The non-grantor lead trust is often used as a way to transfer assets from the donor to his or her children and/or grandchildren at a much lower transfer tax cost. This gift option is most appropriate for the donor who estate is valued in excess of $3 million.

6. Charitable lead trusts can be established by a donor during lifetime or by Will.

C. Benefits for the Donor

1. The donor can make a major gift to charity and still preserve assets for his or her heirs.

2. The lead trust may enable a donor to transfer specific assets (such as stock in a family-owned business or income-producing real estate) to heirs with little or no transfer taxes. Can be an important estate planning tool.

3. The lead trust gift may result in a substantial reduction in gift and estate taxes --- allowing the donor, ultimately, to transfer more assets to the family and less to the IRS.

4. If the lead trust is created during the donor's lifetime, the trust assets will not have to go through probate.

D. Benefits to your Organization

1. This is an immediate gift for the charity, since lead trust payments begin when the trust is created.

2. An interesting option to discuss with your wealthy donors who have concerns about paying huge estate taxes. May provide an important service to them.

3. May be an appropriate planned gift opportunity to use in a capital campaign.

E. Example

THE CHARITABLE LEAD TRUST

SITUATION:

Mr. and Mrs. Jones, both in their sixties, would like to make a major gift to their favorite charity. Because they have a large estate (approximately $5 million) they are also quite concerned about transferring as much of their assets as possible to their children --- at the lowest possible tax cost. (If they do no estate planning, the estate will ultimately be subject to a 55% marginal tax rate --- and what is left will go to their children.)

SUGGESTION:

In talking with their attorney about their estate plan the Jones' discover that they can set up a Trust that will pay income to their favorite charity for a period of time, and then the Trust assets will go to family members. Because the charity will benefit up front, the Trust assets will go to the family later on at substantial savings in gift and estate taxes. Here is how the gift can work:

Donors transfer $500,000 -------------> **LEAD TRUST** -------------> Trust pays $30,000 per year to charity for specified time

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Later, the Trust ends, and all Trust assets go to donors' children

BENEFITS:

1. Because the charity receives income from the Trust first, the tax cost of giving the trust assets to the donors' children later is *substantially reduced.*

   a. Let's assume that the Trust will pay $30,000 per year to charity for 20 years, and then all of the Trust assets go to their children. Here the donors are deemed to have made a gift to charity of $322,842, and a taxable gift to their children of $177,158.

   b. Let's also assume that the total return of the Trust (income plus growth of principal) is more than sufficient to make the annual payment to the charity, and that the Trust assets appreciate to $1 million at the end of the Trust term (when the assets are paid to the children).

   c. When the children receive the $1 million from the Trust, the $500,000 in growth passes to them completely free of gift or estate taxes.

2. Here, donors are able to transfer $1 million to their children at substantial savings in Federal gift and estate taxes. They are also able to make a significant gift to their favorite charity.

VIII. The Revocable Savings Account Trust --- An interesting option offered by organizations such as the Arthritis Foundation and the Salvation Army.

   A. How these arrangements work

1. Donor transfers cash to a charity who will invest it, and pay the entire net income from the gift to the donor for life. The donor also reserves the right to invade principal and/or revoke the gift at any time.

2. Upon the death of the donor, if the gift fund remains in existence, all of the assets in the fund go the charity.

B. Key Features

1. The donor receives all of the net income earned by the fund for life.

2. Additional contributions can be made to the fund at any time.

3. Unlimited withdrawals can be made from the fund at any time.

4. Since the donor can revoke the gift at any time, and get the assets back, the donor does not get an income tax deduction for the gift.

5. The donor can make the gift irrevocable at any time, by putting the assets into a Pooled Income Fund, Charitable Remainder Trust, or Charitable Gift Annuity. If this is done, the donor will be entitled to an income tax deduction for the remainder value of the gift.

6. If the Savings Account Trust fund is in existence when the donor dies, the assets will go to the charity maintaining the fund. The donor's estate will then be entitled to a Federal estate tax deduction for the charitable gift.

C. Benefits for the Donor

1. The donor can receive all of the net income earned by the fund.

2. This arrangement provides flexibility for the donor. If the donor's circumstances should change and the donor needs the assets, he or she can revoke the gift and get the assets back. The donor can also invade principal at any time.

3. There is no income tax deduction for this gift, since the gift can be revoked at any time. However, if the gift fund is in existence at the time of the donor's death, the assets will go to the charity, and the donor's estate will be entitled to a Federal estate tax charitable deduction for the gift.

4. The donor can make the gift irrevocable at any time by transferring the assets to a Pooled Income Fund, Charitable Remainder Trust, or Charitable Gift Annuity. If the donor does this, he or she will be entitled to an income tax deduction for the then remainder value of the gift.

D. Benefits to your Organization

1. A way to encourage your donors and prospects who cannot part with income or assets now to make a gift for the future benefit of your organization. This kind of arrangement may provide large gifts that would otherwise not be received.

2. Can be a good cultivation tool, to get your donors thinking about your organization in long-range terms, possibly leading to irrevocable gifts later on.

IX. The Totten Trust --- Another interesting option, available in states (like New York) which permit this kind of arrangement.

A. How Totten Trusts work

1. Donor deposits cash in a bank account, naming himself or herself as trustee for the benefit of a favorite charity.

2. The donor reserves the right to cancel the account at any time.

3. Upon the death of the donor, if the account is still open, the cash in the account goes to the charity.

B. Key Features

1. The donor uses the account as his or her own, during lifetime.

2. The donor can add to the account, withdraw from the account, or cancel the account at any time.

3. The donor does not get an income tax deduction for setting up the account, since it can be revoked at any time.

4. The donor can make the gift irrevocable at any time by making an unequivocal, irrevocable gift to the charity. If this is done, the donor will be entitled to an income tax deduction for the gift.

5. If the Totten Trust account is in existence when the donor dies, the assets in the account will go to the named charity, and the donor's estate will be entitled to a Federal estate tax deduction for the gift.

C. Benefits for the Donor

1. Donor can use the account for his or her own purposes during lifetime.

2. This arrangement provides flexibility for the donor. He or she can always cancel the account and take the money back, if circumstances change.

3. The donor gets no income tax deduction for setting up the Totten Trust. However, if the account is in existence at the time of the donor's death, the money will go to the named charity, and the donor's estate will be entitled to a Federal estate tax deduction for the gift.

D. Benefits to your Organization

1. A way to encourage your donors and prospects who cannot part with income or assets now to make a gift for the future benefit of your organization. This kind of arrangement may provide large gifts that would otherwise not be received.

2. Can be a good cultivation tool, to get your donors thinking about your organization in long-range terms, possibly leading to irrevocable gifts later on.

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RETIREMENT PLAN ASSETS

Charitable Donation or Family Gift?

Presented by Robert E. Harding

I. Tax Aspects of Retirement Plans - a Brief Overview

A. Types of plans

1. Plans described in IRC § 401 ("qualified plans") (including pension plans, profit sharing plans, Keogh plans, 401(k) plans, 403(b) annuities).

2. Individual Retirement Accounts described in Section 408 ("IRAs").

3. *Not discussed here*: nonqualified plans, e.g., "Rabbi trusts," Section 457 unfunded plans.

B. Federal tax attributes and distribution rules during plan participant's lifetime

1. Generally funded with pre-tax dollars (untaxed compensation).

2. Retirement plan account itself is exempt from federal income tax. IRC § 501(a).

3. Entire amount of any withdrawal during lifetime is generally subject to federal income tax. IRC § 402(a).

4. Withdrawals prior to age 59-1/2 are generally subject to a 10 percent early withdrawal penalty. IRC § 72(t).

5. Participant *must* begin withdrawals by age 70-1/2 at a specified minimum rate. IRC § 401(a)(9).

a. If beneficiary of plan balance at participant's death is an individual, the "minimum distribution rules" permit distributions to be spread over joint lives of participant and beneficiary. IRC § 401(a)(9)(A)(ii).

b. If beneficiary of plan is not an individual (e.g., a trust), distributions must, in some cases, be made more rapidly--ratably over life of participant, e.g., in the case where the beneficiary is a trust and at least one beneficiary of that trust is not an individual (e.g., a charitable organization). Prop. Treas. Reg. § 1.401(a)(9)-1, Q & A D-2A.

6. Excise tax is imposed at rate of 15 percent on annual withdrawals exceeding an amount defined by formula. IRC § 4980A(a).

C. Tax attributes and distribution rules at and following participant's death

1. Plan assets are potentially subject to a *triple tax*: estate tax, income tax, and 15 percent excise tax on "excess accumulations."

2. Estate tax

a. Estate tax rules have shifted from taxing plan assets more favorably than other assets to taxing them more adversely. As the rules have changed, the beneficiary designation which will produce the best tax result has also changed. Therefore, beneficiary designations made under prior estate tax laws should be reviewed, and may have to be revised.

b. Entire value of plan assets at participant's death is included in his or her federal gross estate. Deduction is allowed for any excise tax on excess accumulations. *See* C.4 below.

c. Marital deduction can shelter plan assets in some situations. IRC § 2056.

i. Outright distribution to spouse.

ii. Marital gift using plan assets can be structured as QTIP. Rev. Rul. 89-89, 1989-2 C.B. 231. However, it may be difficult both to satisfy "all income" requirement of QTIP and to structure installment payments in a way which is permitted by plan.

3. Income tax

a. In general, entire plan balance is "income in respect of a decedent" ("IRD") under Section 691. Therefore, IRD is includable in gross income of ultimate recipient when received. A federal income tax deduction is allowable for the *federal* estate tax paid on the IRD item.

b. If plan assets are distributed to spouse, he or she can generally roll that amount over to his or her IRA tax-free. IRC § 402(c)(9). Amounts are taxed to surviving spouse only as he or she makes withdrawals from IRA.

4. Excise tax on "excess accumulations"

a. Threshold is defined by formula: that amount which would be just sufficient to purchase an annuity which would pay the maximum annual amount which would not be subject to excise tax on excess withdrawals during life. IRC § 4980A(d).

b. Threshold amount is generally somewhere between $750,000 and $1,500,000, depending upon the decedent's age at death and the prevailing interest rates.

5. Distribution Rules

a. Death prior to commencement of benefits. Sec. 401(a)(9)(B)

i. If distributions have not begun, then entire balance must be distributed within 5 years of death of plan participant, *i.e.*, by December 31 of fifth calendar year following death.

ii. Exception to 5-year rule: Distributions may be made over life expectancy of a "designated beneficiary" if begun not later than 1 year after death of participant, *i.e.*, December 31 of calendar year following death.

iii. If surviving spouse is the designated beneficiary, then payment of benefits may be delayed until the date the participant would have reached age 70-1/2.

iv. Multiple methods may be used for multiple beneficiaries.

b. Death after commencement of benefits.

i. Remaining portion must be distributed at least as rapidly as before.

ii. Beneficiary designations control disposition.

II. <u>Difficulties Encountered in Noncharitable Estate Planning with Retirement Plan Assets</u>

A. <u>Outright lump sum marital gift</u>

The simplest solution to the spectre of the triple tax.

1. Sheltered from estate tax by marital deduction.

2. Income tax can be deferred by rollover to surviving spouse's IRA. IRC § 402(c)(9).

3. Excise tax on excess accumulations, if otherwise applicable, can be deferred if the surviving spouse so elects. IRC § 4980A(d)(5).

B. <u>Disadvantages of outright lump sum marital gift</u>

1. If plan assets comprise the bulk of the participant/decedent's estate, credit trust may be underfunded, with the result that part of unified credit will be wasted.

2. Participant/decedent has no control over use of plan assets during surviving spouse's lifetime or after surviving spouse's death.

3. If surviving spouse remarries, his or her new spouse may have marital claims on plan assets.

C. <u>Structuring the transfer as a QTIP is a partial solution</u>

1. Does nothing to address underfunding of credit trust.

2. May solve problems of control and marital claims of new spouse but at what may be a substantial cost:

a. Rev. Rul. 89-89 requires that the annual payment from the QTIP trust to the surviving spouse include all income earned by the trust *and* all income earned by the retirement plan (in the case at issue, an IRA) for the year.

b. Most pension and profit sharing plans do not provide for installment distributions calculated this way. Thus, using a QTIP may not be feasible unless plan assets are first rolled over to an IRA.

c. "All income" requirement may create a larger payout than desired.

III. Outright Lifetime Charitable Gift of Retirement Plan Assets - Pros and Cons

A. Tax consequences

1. Treated as a withdrawal of the assets by the plan participant, followed by outright transfer of those assets by participant to charitable donee.

2. Entire amount is included in participant's federal gross income for the year of the withdrawal/gift. IRC § 402(a).

3. Charitable contribution is deductible by participant/donor for year of gift, subject to applicable annual deduction limit for charitable contributions imposed by IRC § 170(b)(1).

a. Gift will presumably consist of cash or securities held short term.

b. Deduction limit for such a gift to a "public charity" is 50% of donor's "contribution base" for the year of the gift (Federal adjusted gross income computed without regard to net operating loss carry back to the taxable year under IRC § 172). IRC § 170(b)(1)(A).

4. Withdrawal/gift before age 59-1/2 will be subject to 10 percent early withdrawal penalty. IRC § 72(t).

5. Gift qualifies in full for gift tax charitable deduction. IRC § 2522(a).

6. Donated property is excluded from donor's federal gross estate and therefore escapes federal estate.

B. Comparison with outright lifetime charitable gift of highly appreciated stock held long term - which gift is "better"? (Charitable gifts under both plans are assumed to be to "public charities.")

1. The two plans.

a. *Plan A*: Plan assets donated to charity during donor's lifetime, stock retained and passed to children at death.

b. *Plan B*: Appreciated stock donated to charity during donor's lifetime, plan assets retained and passed to children at death.

2. Tax benefits during donor's lifetime.

a. *Plan A*: Gross income to participant generated by withdrawal of assets from plan will be exactly offset by charitable deduction, *assuming* annual deduction limit is not exceeded. No *net* tax benefit.

b. *Plan B*: Lifetime charitable gift of stock is deductible at fair market value (subject to 30% annual deduction limit). Gift generates no gross income to participant, so entire deduction is available to offset other income.

3. Tax benefits for family at/after donor's death.

a. *Plan A*: Estate tax on value of stock. Family receives stock with stepped-up basis, IRC § 1014.

b. *Plan B*: Estate tax on value of plan assets. Full value of plan assets included in federal gross income of recipient/family member. Federal income tax deduction is allowed for federal (but *not* state) estate tax paid on plan assets.

IV. Outright Testamentary Charitable Gift of Retirement Plan Assets

A. The "cost" of an outright testamentary charitable gift of a particular asset: the total amount family members would receive under the decedent's estate plan if that asset were transferred to them *minus* the total amount they would receive under the estate plan if the asset is distributed to charity.

B. Other things being equal, a donor should make an outright testamentary charitable gift with the asset which is least "costly." Same reasoning applies in the case of a transfer to a testamentary charitable remainder trust. *See* Section V below.

C. In a typical case, an outright testamentary charitable gift of retirement plan assets costs the family 25 percent to 30 percent of the value of the gift to the charity! *See* Exhibit A.

D. Mechanics of Beneficiary Designations for Qualified Plans and IRAs

1. The beneficiary designation is the only document that the plan administrator will consult when paying death benefits. The participant's will and other estate planning documents do not control the disposition of the plan benefits (unless the beneficiary designation designates the participant's estate or revocable trust).

2. Qualified plans - spousal consent: Without a legally effective beneficiary designation, the entire benefit is payable to the participant's spouse at the participant's death. IRC §§ 401(a)(11)(B), 417 (a)(2).

a. A married participant must obtain spousal consent in order to designate a charity as a beneficiary of qualified plan benefits. A spouse's signature on the form is not sufficient unless the spouse's consent (i) acknowledges the effect of the designation (and the waiver of the annuity benefit, if applicable. *See* b. below) *and* (ii) is witnessed by a plan representative or a notary public. IRC §§ 401(a)(11)(B), 417(a)(2).

b. Some plans are required to provide a survivor annuity to the spouse unless the spouse specifically consents to waive the annuity benefit. For those plans, the spouse's consent to the designation should mention both the waiver of the survivor annuity and the designation of the charity as a beneficiary. The spouse must receive an explanation of the survivor annuity benefit from the plan sponsor before giving consent to the beneficiary designation. IRC § 417(a)(3).

c. Federal law permits two types of spousal consent to a beneficiary designation.

i. The consent may be specific with respect to the beneficiaries named on the form, such that no change in the designation may be made without again obtaining the spouse's consent.

ii. With the second type of consent, the spouse consents to the designation of any other beneficiaries, thus allowing the participant to modify the designation of beneficiaries at a later date without notice to or consent by the spouse.

The beneficiary designation form should be clear as to which type of consent is being given by the spouse. If the second type of consent is desired, the spouse's consent must acknowledge that he or she has the right to limit the consent to the beneficiaries named on the form but agrees voluntarily to waive that right. IRC § 417(a)(2)(A)(ii).

d. A spousal consent may not be revoked by the consenting spouse, although the participant may always change the designation back to the spouse.

3. If the death benefit will be shared between a charitable organization and family members or other individuals, the designation must be clear as to what happens to the portion left to individuals who do not survive the participant. Many beneficiary designation forms, without adding special language, would cause the deceased beneficiary's share to go to the charity as the "surviving" primary beneficiary.

4. The charity's share of the death benefit should be described as a fractional share rather than as a fixed or formula dollar amount. (*See* V.D below).

V. <u>Testamentary Transfer of Plan Assets to a Charitable Remainder Trust -- the "Testamentary Charitable Rollover"</u>

A. An alternative for the charitably minded plan participant who does not wish to make an outright charitable gift of plan assets at death.

1. The charitable remainder trust ("CRT") can use plan assets to provide for a surviving spouse or surviving child, with ultimate distribution to charity.

2. IRS has now ruled favorably on two arrangements:

a. Priv. Ltr. Rul. 92-53-038--transfer of profit sharing plan assets to CRT for spouse.

b. Priv. Ltr. Rul. 92-37-020--transfer of IRA assets to CRT for child.

B. Those rulings concluded that these testamentary transfers of retirement plan assets to CRT have same tax consequences as any normal testamentary transfer to CRT.

1. Trust qualifies, or continues to qualify, as CRT under IRC § 664.

2. Present value of charitable remainder interest created by the transfer qualifies for estate tax charitable deduction. IRC §§ 2055(a), 2055(e)(2)(A).

3. If participant's spouse is the *only* noncharitable beneficiary, spouse's interest qualifies for estate tax marital deduction. IRC § 2056(b)(8).

4. Distributions to noncharitable beneficiary will be taxed to beneficiary under usual "four-tier" system of Treas. Reg. 1.664-1(d).

5. *Most important*: CRT will be exempt from federal income tax for any year in which it receives no unrelated business taxable income ("UBTI"). IRC § 664(c); Treas. Reg. § 1.664-1(a)(1). Thus, IRS implicitly recognized that transfer of plan assets, if properly structured (*See* D below), should not trigger immediate income tax on full value of plan assets.

C. A new tool for estate planning for retirement plan assets

The testamentary charitable rollover for a surviving spouse provides a way of avoiding the immediate double bite of estate tax and income tax but without some of the disadvantages described above for an outright gift of assets to a surviving spouse:

1. Participant/decedent specifies how plan assets will be used during surviving spouse's lifetime and at surviving spouse's death.

2. New spouse should not have claims on CRT corpus.

3. Note that the testamentary charitable rollover, like the outright testamentary charitable gift of retirement plan assets, does *not* avoid the 15 percent excise tax (if otherwise applicable) on excess accumulations. However, as explained at VI.B and C below, if the testamentary charitable rollover is combined with a "wealth replacement" insurance trust, the wealth replacement trust can be funded by means of lifetime withdrawals from the retirement plan by the participant. Such withdrawals will reduce the potential exposure of the plan to the excess accumulations tax at the participant's death.

D. IRD considerations

1. Generally, full value of assets transferred from retirement plan to CRT will be IRD.

   a. As IRD, value of plan assets will be reportable as gross income of CRT in year received by CRT. IRC § 691(a)(1)(B).

   b. However, if CRT has no UBTI in year it receives plan assets, it is tax-exempt, and therefore pays no income tax on such gross income. IRC § 664(c).

2. *Caveat*: the portion of the plan assets to be transferred to CRT must be defined so as not to trigger IRD inadvertently. Defining CRT's portion as a "fractional share" should avoid this result, whereas a distribution defined as a fixed dollar amount or a "formula pecuniary amount" may not. *Cf.* IRC § 691(a)(2); Treas. Reg. § 1.691(a)-4.

VI. Combination of testamentary charitable rollover and "wealth replacement trust"

A. Testamentary charitable rollover for surviving spouse provides no direct benefit to children.

B. One solution: a "wealth replacement trust," i.e., an irrevocable trust with Crummey powers funded with cash which trustee uses to purchase second-to-die life insurance. Such insurance can often be purchased at a modest cost.

1. Charitable remainder trust ("CRT") component of a wealth replacement plan.

a. Lifetime funding: (Can be, but need not be, combined with testamentary rollover of retirement plan assets if unitrust is used. Annuity trust cannot receive more than one contribution). Highly appreciated assets, otherwise includible in donor's estate at death, are transferred to charitable remainder trust.

i. Lifetime income to donor and spouse.

ii. No realization of gain on transfer to trust.

iii. Income tax charitable deduction based on present value of remainder interest. Tax savings can be used to help fund wealth replacement trust.

iv. Trust property included in donor's estate but sheltered by estate tax marital and charitable deductions. IRC §§ 2056(b)(8), 2055(e)(2)(A).

b. Testamentary funding: CRT can be funded at death with retirement plan assets. (*See* V.B above for tax consequences.)

2. Wealth replacement trust component.

a. Options for funding.

i. Annual payments from lifetime CRT, or tax savings from income tax deduction for lifetime funding of CRT.

ii. If plan document permits, insurance trust can be funded with distributions from the retirement plan during the last 7 to 10 years before retirement. If made after participant reaches age 59-1/2, or after age 55 if employment has terminated, these distributions will be subject to income tax but not the 10 percent early withdrawal penalty. If the plan assets are potentially exposed to the excess accumulations tax, these distributions will reduce that exposure.

b. Insurance is often available in short-term payment alternative - premiums fully paid ("vanish") after 6-9 years.

c. Each contribution by donor to wealth replacement trust is gift, for gift tax purposes, to individuals who are the beneficiaries of that trust.

i. Must structure contributions as gifts of present interests qualifying, up to annual limit, for present interest gift tax exclusion.

ii. Thus, trust beneficiaries must have present right to withdraw contribution each year ("Crummey Power").

d. Insurance proceeds not includable in donor's estate if all incidents of ownership in insurance policy are held by irrevocable trust, and donor never had any incidents of ownership in insurance policy. IRC § 2035(d).

e. Proceeds available, without being subject to income tax or estate tax, for children, grandchildren, or other relatives.

C. Benefits of combining the wealth replacement trust with the testamentary charitable rollover for a surviving spouse

1. Lifetime income is provided for the surviving spouse.

2. No estate tax is imposed on the "rolled over" plan assets at the death of either spouse.

3. No income tax is payable when the plan benefits are paid to the CRT.

4. Only amounts actually distributed to the surviving spouse from the CRT are subject to income tax.

5. At the death of the surviving spouse, the balance in the CRT is distributed to the charity without ever having been diminished by income or estate tax.

6. At the same time as the CRT ends, the insurance proceeds are paid to the wealth replacement trust and are available for the benefit of later generations without being subject to income tax or estate tax.

7. If the wealth replacement trust is funded by means of withdrawals from the plan during the participant's lifetime, those withdrawals will reduce the potential exposure of the plan assets to the 15 percent excess accumulations tax at the participant's death.

VII. Planning a Testamentary Charitable Rollover

A. Is the Donor's retirement plan suited for funding a CRT at death?

1. Types of plans which permit lump sum distributions and which are permitted to pay survivor benefits to a trust are suited to the testamentary charitable rollover. The following types of plans generally have those characteristics:

a. Profit sharing plans

b. 401(k) plans

c. Money purchase pension plans

d. IRAs

2. Other types of retirement plans do not lend themselves to this type of gift because they offer only an annuity form of benefit. In such cases, not only is the transfer of assets out of the plan restricted, but the CRT may not even be a permissible beneficiary.

   a. Defined benefit plans and 403(b) annuity plans fall in this category.

   b. Participants in such plans may be able to elect a lump sum, but should consider whether the amount of the lump sum, which is computed by formula, is sufficient to justify foregoing the annuity.

   c. If some aspect of donor's retirement plan presents an obstacle to a testamentary charitable rollover, it may be possible to amend the plan document in a way which permits the transfer.

      i. Amending the plan's beneficiary designation rules should normally be possible, subject to the IRC spousal consent rules.

      ii. Expanding the available forms of distribution to include a lump sum may be more involved.

B. <u>Impact of the charitable rollover on the donor's other retirement planning and estate planning objectives</u>

1. Interaction of minimum distribution rules (which govern retirement plan distributions after the participant reaches 70-1/2) with the charitable rollover can affect rate at which distributions will be made from the plan.

   a. Naming a CRT rather than an individual as the beneficiary causes benefits to be paid out more quickly, over the donor's life expectancy, rather than over the joint life expectancies of the donor and an individual beneficiary. Prop. Treas. Reg. § 1.401(a)(9)-1, Q & A D-2A. This affects all assets in the same plan account, even if only a portion is designated to go to the CRT. Prop. Treas. Reg. § 1.401(a)(9)-1, Q & A E-5.

   b. If donor and beneficiaries have sufficient other assets to support themselves, they will probably wish to maximize the tax deferred growth of the plan account so as to provide as much as possible to their heirs.

   c. Thus, there is a potential conflict between planning for family (where slower distributions are preferred) and the charitable rollover (which results in faster distribution of all assets in the plan account from which the CRT is funded).

2. One solution: segregate the assets destined for the CRT in a separate IRA before donor reaches 70-1/2.

   a. Required distributions from other retirement accounts can then be determined without regard to designation of CRT as beneficiary of the separate IRA. Prop. Treas. Reg. § 1.401(a)(9)-1, Q & A H-2(b).

b. If the balance of the plan assets is transferred to another IRA, each year's aggregate required distributions can be made from either IRA. IRS Notice 88-38. This allows donor to regulate the amount in the IRA which is destined for the CRT, thus controlling the amount of the charitable rollover.

3. Timing of transfer to CRT

Retirement plan distribution rules dictate the period within which retirement plan assets must be paid to the CRT after the donor's death.

a. If death occurs before date on which post-age 70-1/2 distributions are required to begin, transfer must be completed by 12/31 of calendar year which contains fifth anniversary of donor's death. IRC § 401(a)(9)(B)(ii); Prop. Treas. Reg. § 1.401(a)(9)-1, Q & A C-2.

b. If required distributions have begun before donor's death, transfer of remaining benefits must occur at least as rapidly as under the distribution method being used by the donor at his or her death. IRC § 401(a)(9)(B)(i).

This outline and the attached exhibit are designed to provide information of a general nature only. They should not be construed as legal advice or legal opinion on any specified facts or circumstances.

Robert E. Harding
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EXHIBIT A

The Cost of an Outright Testamentary Charitable Gift
of Retirement Plan Assets

I. Summary

		Situation #1	Situation #2	Situation #3
Gross Estate		$ 3,500,000	$ 3,500,000	$ 2,000,000
Qualified Retirement Plan		1,000,000	1,000,000	1,000,000
Option 1: Charitable Gift				
a)	Charitable gift	500,000	250,000	150,000
b)	Excise tax on charitable gift	37,500	37,500	22,500
c)	Amount by which other property passing to children is reduced	37,500	37,500	22,500
Option 2: Gift to Children				
a)	Gross gift to children	500,000	250,000	150,000
b)	15% Excise Tax	37,500	37,500	22,500
c)	Estate Tax	273,250	137,500	67,500
d)	Income Tax	94,908	50,428	38,250
e)	Total Tax	405,658	225,428	128,250
f)	Net amount received by children	94,342	24,572	21,750
g)	Percentage of gross gift actually received by children	19%	10%	15%
Cost of Charitable Gift				
a)	Cost of charitable gift (1.c plus 2.f)[1]	131,842	62,072	44,250
b)	Cost of charitable gift as percentage of benefit to charity	26%	25%	30%

[1] The "cost" of an outright testamentary charitable gift of retirement plan assets is the amount by which the property passing to the donor's children is reduced by making the charitable gift. Thus, that cost is the difference between the total property the children will receive if the amount of plan assets in question is left to them, and the total they will receive if the same amount of plan assets is donated to charity instead.

II. Assumptions:

A. Situation #1

1. Donor survives her spouse and dies in 1994 at age 63.

2. Donor has federal gross estate (including value of plan) with a total value of $3,500,000.

3. Value of donor's retirement plan assets at her death is $1,000,000.

4. At donor's death, assets of her retirement plan in excess of $750,000 are subject to 15 percent excise tax on excess accumulations.

5. Donor is survived by her two children, to whom she will give everything she doesn't give to charity (or pay out in taxes).

6. Donor is a Minnesota resident. Minnesota has a "pick up" estate tax, i.e., state estate tax which equals maximum federal estate tax credit allowable for state estate tax.

7. Any retirement plan assets passing to the two children will be in the form of lump sum distributions with respect to which they will elect 5-year averaging treatment. (They are allowed to do so because the donor was born before 1936.)

8. Donor's estate has federal estate tax deductions, other than deduction for excise tax, of $50,000.

9. Donor is considering making an outright testamentary charitable gift of $500,000 of plan assets.

B. Situation #2

Same assumptions as situation #1, except that donor is considering an outright testamentary charitable gift of $250,000 of plan assets.

C. Situation #3

Same assumptions as situation #1, except that donor has federal gross estate (including value of plan) with a total value of $2,000,000 and is considering an outright testamentary charitable gift of $150,000 of plan assets.

III. The "cost" of a testamentary charitable gift of retirement plan assets

The "cost" of a testamentary charitable gift of retirement plan assets is the amount by which the property passing to the donor's children is reduced by the charitable gift. Thus, that cost is the difference between the total property the children will receive if the amount of plan assets in question is left to them, and the total they will receive if that amount of plan assets is donated to charity instead.

IV. How much does an outright testamentary charitable gift of $500,000 of plan assets "cost" in situation #1?

A. Option 1: gift of $500,000 of retirement plan assets to charity

1.	Gross gift to children:	- 0 -
2.	*Excise Tax*: The 15 percent excise tax will apply. If the $500,000 of plan assets is distributed to charity, the $37,500 of excise tax will be paid out of other assets of the donor's estate which would otherwise go to her children.	$ 37,500
3.	*Estate Tax*: The gift to charity will be offset by an estate tax charitable deduction and will therefore generate no estate tax.	- 0 -
4.	*Income Tax*: The $500,000 of plan assets will go to the charity, so neither the donor's estate, nor her children, nor the charity (which is tax-exempt) will pay income tax on that amount:	- 0 -
5.	*Total Tax* (amount by which value of other assets passing to children is reduced):	$ 37,500

B. Option 2: gift of $500,000 of retirement plan assets to children

1.	Gross gift to children:	$ 500,000
2.	*Excise tax*:	($ 37,500)
3.	*Estate tax*: federal $226,750 state $ 46,500	($ 273,250)
4.	*Income tax* on lump sum distributions to children:	($ 94,908)
5.	*Total tax*:	($ 405,658)
6.	Net amount received by children (roughly 19% of gross value of gift):	$ 94,342

C. Cost of the Charitable Gift:

1.	Amount by which other assets passing to children are reduced if $500,000 of plan assets are left to charity:	$ 37,500
2.	Net amount received by children if $500,000 of plan assets are left to them:	$ 94,342
3.	Cost of charitable gift to children (roughly 26% of value of charitable gift):	$ 131,842

V. <u>How much does an outright testamentary charitable gift of $250,000 of plan assets "cost" in situation #2?</u>

A. <u>Option 1: gift of $250,000 of retirement plan assets to charity</u>

1.	Gross gift to children:	- 0 -
2.	*Excise Tax*: The 15 percent excise tax will apply. If the $250,000 of plan assets is distributed to charity, the $37,500 of excise tax will be paid out of other assets of the donor's estate which would otherwise go to her children.	$ 37,500
3.	*Estate Tax*: The gift to charity will be offset by an estate tax charitable deduction and will therefore generate no estate tax.	- 0 -
4.	*Income Tax*: The $250,000 of plan assets will go to the charity, so neither the donor's estate, nor her children, nor the charity (which is tax-exempt) will pay income tax on that amount:	- 0 -
5.	*Total Tax* (amount by which value of other assets passing to children is reduced):	$ 37,500

B. <u>Option 2: gift of $250,000 of retirement plan assets to children</u>

1.	Gross gift to children:	$ 250,000
2.	*Excise tax*:	($ 37,500)
3.	*Estate tax*: federal $113,500 state $ 24,000	($ 137,500)
4.	*Income tax* on lump sum distributions to children:	($ 50,428)
5.	*Total tax*:	($ 225,428)
6.	Net amount received by children (roughly 10% of gross value of gift):	$ 24,572

C. <u>Cost of the Charitable Gift</u>:

1.	Amount by which other assets passing to children are reduced if $250,000 of plan assets are left to charity:	$ 37,500
2.	Net amount received by children if $250,000 of plan assets are left to them:	$ 24,572
3.	Cost of charitable gift to children (roughly 25% of value of charitable gift):	$ 62,072

VI. How much does an outright testamentary charitable gift of $150,000 of plan assets "cost" in situation #3?

A. Option 1: gift of $150,000 of retirement plan assets to charity

1.	Gross gift to children:	- 0 -
2.	*Excise Tax*: The 15 percent excise tax will apply. If the $150,000 of plan assets is distributed to charity, the $22,500 of excise tax will be paid out of other assets of the donor's estate which would otherwise go to her children.	$ 22,500
3.	*Estate Tax*: The gift to charity will be offset by an estate tax charitable deduction and will therefore generate no estate tax.	- 0 -
4.	*Income Tax*: The $150,000 of plan assets will go to the charity, so neither the donor's estate, nor her children, nor the charity (which is tax-exempt) will pay income tax on that amount:	- 0 -
5.	*Total Tax* (amount by which value of other assets passing to children is reduced):	$ 22,500

B. Option 2: gift of $150,000 of retirement plan assets to children

1.	Gross gift to children:	$ 150,000
2.	*Excise tax*:	($ 22,500)
3.	*Estate tax*: federal $56,700 state $10,800	($ 67,500)
4.	*Income tax* on lump sum distributions to children:	($ 38,250)
5.	*Total tax*:	($ 128,250)
6.	Net amount received by children (roughly 15% of gross value of gift):	$ 21,750

C. Cost of the Charitable Gift:

1.	Amount by which other assets passing to children are reduced if $150,000 of plan assets are left to charity:	$ 22,500
2.	Net amount received by children if $150,000 of plan assets are left to them:	$ 21,750
3.	Cost of charitable gift to children (roughly 30% of value of charitable gift):	$ 44,250

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IDENTIFYING DONORS OF PLANNED GIFTS

Presented by Jonathan Heintzelman

I. MARKET TRENDS

A. Aging of America -- impact on generations

- Depression / World War II (pre-1946)

  - focus on the "final plan" which includes having enough to live on and deciding what to do with what's left

  - either retired or thinking about retiring

- Boomers (1946-1965)

  - currently in high earnings but with high costs of mortgages, college, weddings, etc.

  - should be putting *maximum* amount into retirement but most aren't

  - first two-income generation with growing rate of women in personal estate decision-making

- Generation X (post-1965)

  - facing lower standard of living than parents

  - fewer opportunities

B. Increase in Personal Wealth

  - Whither the transfer?

  - Growing importance of gift and estate taxes

C. The New Congress and the "Contract"

  - Capital Gains Reduction

  - Flat Tax

  - Shrinking the Transfer Possibilities

    - taxing gain at death
    - capping the annual exclusion (e.g., $30,000 annually)
    - budget impact and the search for additional revenue

D. Economic Jitters

- Wall Street

  - Real Estate

  - Interest Rates

  - Growing *lack* of confidence about the future
    (witness the low expectations of the Social Security System)

E. Increased Competition

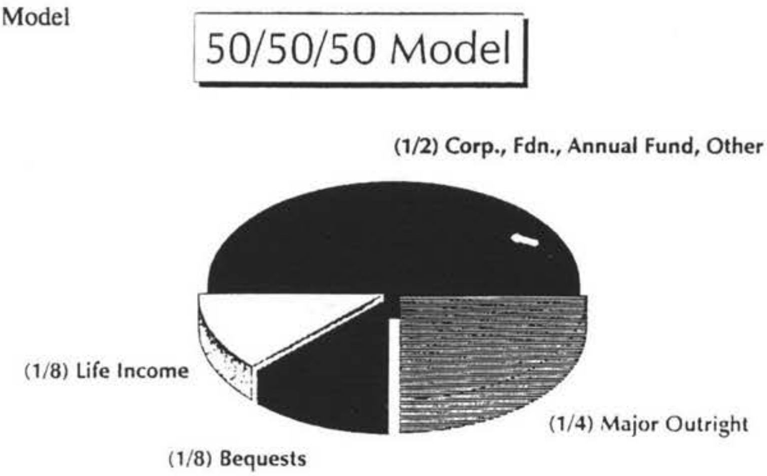
  - Not-for-Profits
    Have we peaked yet?

  - For Profits
    - trust management
    - investment management
    - donor advised funds

II. MARKET / PROSPECT ANALYSIS

A. Impact on Total Development

- The 50/50/50 Model



B. Irrevocables / Bequests

  - the 40% Barrier

C. Irrevocables et. al.

  - the "Big Two" and the rest

D. The Prospects

Planned Giving Prospects--Lions and Tigers and Bears

a. $1,000,000+ Analysis *(EXHIBIT 1)*

- Insignificant = occupation, location and alum status
- Significant = age and children
- Puzzling = past giving

b. $50,000 = Analysis *(EXHIBIT 2)*

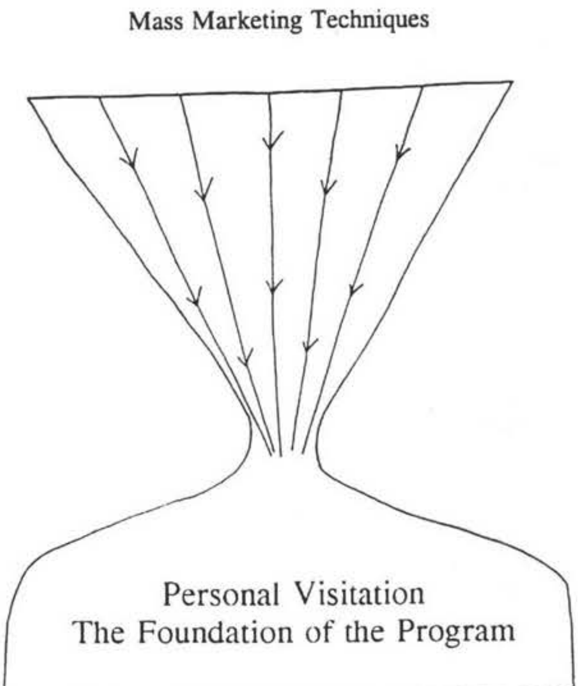
- 0% of Group A were "Never Givers"
- 45% of Donors (Groups B and C) = 66% of $$
- *Past Giving* decreases in importance as you move from outright to deferred (2/3 of bequests from never givers!)

Conclusions -- the Irony of it All!

- Planned Gifts are *larger* than Outright Gifts, but
- Planned Gift Prospects *do not self-identify* through past outright giving patterns
- Planned Gift Prospects do not fit traditional demographic profiles
- The Ratchet Effect of Irrevocables
  Once you go planned, you ***never*** go back to outright!

III. THE IDENTIFICATION PROCESS

A. Process Overview -- The "Funnel"



B. Techniques

1. Saturation

- Newsletter / Qualified Response *(EXHIBIT 3)*
- Advertising *(EXHIBIT 4)*
- Seminars
- Direct Mail
- 800 Number
- Signage

2. Segmentation

- See #1 above
- Bulletins *(EXHIBITS 5A and 5B)*

3. Other Identification

- Research
- Demographic Profiles
- Rating and Screening Programs

4. Recognition Society *(EXHIBIT 6)*

- Three Suggestions

  - make it *inclusive* re. type of planned gift and no minimum amount
  - make it *inclusive* re. documentation (but allow anonymity option)
  - make it *exclusive* re. identity (e.g., *not* heritage or legacy)

C. The Personal Visit

1. Goals

- Recognize the primary importance of the call

- The 120 standard
  really a minimum = average 10 calls per month can be divisible, e.g., if 50% of job is planned giving, the annual goal is 60 calls

- What about goals for other types of contacts such as letters and phone calls?

2. Key Factors on the Call / the Process of Discovery

- Affinity (v. Affiliation)
- Family / Friends
- Wealth (v. Income)

- Financial / Estate Plan
  (& documentation / implementation)

- Goals: Non-charitable
  Charitable

3. Next Step -- Discussion and Agreement

4. Follow-Up

   - immediate from visit
   - next contact - objective
   - long-term objective

IV. TARGETS OF OPPORTUNITY

A. The Case for CAPITAL CAMPAIGNS *(EXHIBIT 7)*

   - Planned gifts as:
     - percentage of total
     - lead gifts

B. Stock Portfolio Spin-Offs

   - Little "Chunks"

C. Real Property

   - Quick Sale Option

D. Testamentary Life Income Plans

E. Lead Trusts

   - Piggy-backed CRT

F. Inter-generational Planned Gifts

   - Term of Years CRTs
   - Two-Level CRTs
   - Testamentary Planning

G. Annuities - A Guaranteed Income in a Time of Economic Uncertainty

H. Bequests - First and Last Option

I. Concept of ENDOWMENTS

V. POSITIONING YOUR PROGRAM

A. Set a Goal for Personal Calls

B. Use a "Saturation" Newsletter with Qualified Response / Humanize!

C. Establish a Recognition Society

D. Focus on Bequests plus the "Big Two"

E. Trust Administration -- Do it Well or Farm it Out

F. Personnel: Don't Overdose on Planned Giving Experience -- Consider the Unconventional Candidate

G. The Capital Campaign Turbocharger

H. Hunting for Lions and Tigers and Bears

I. Continually Creative and Diverse Marketing Techniques

J. Build Endowment Opportunities into the Program

K. Patience, Consistency and a Long-Term Perspective

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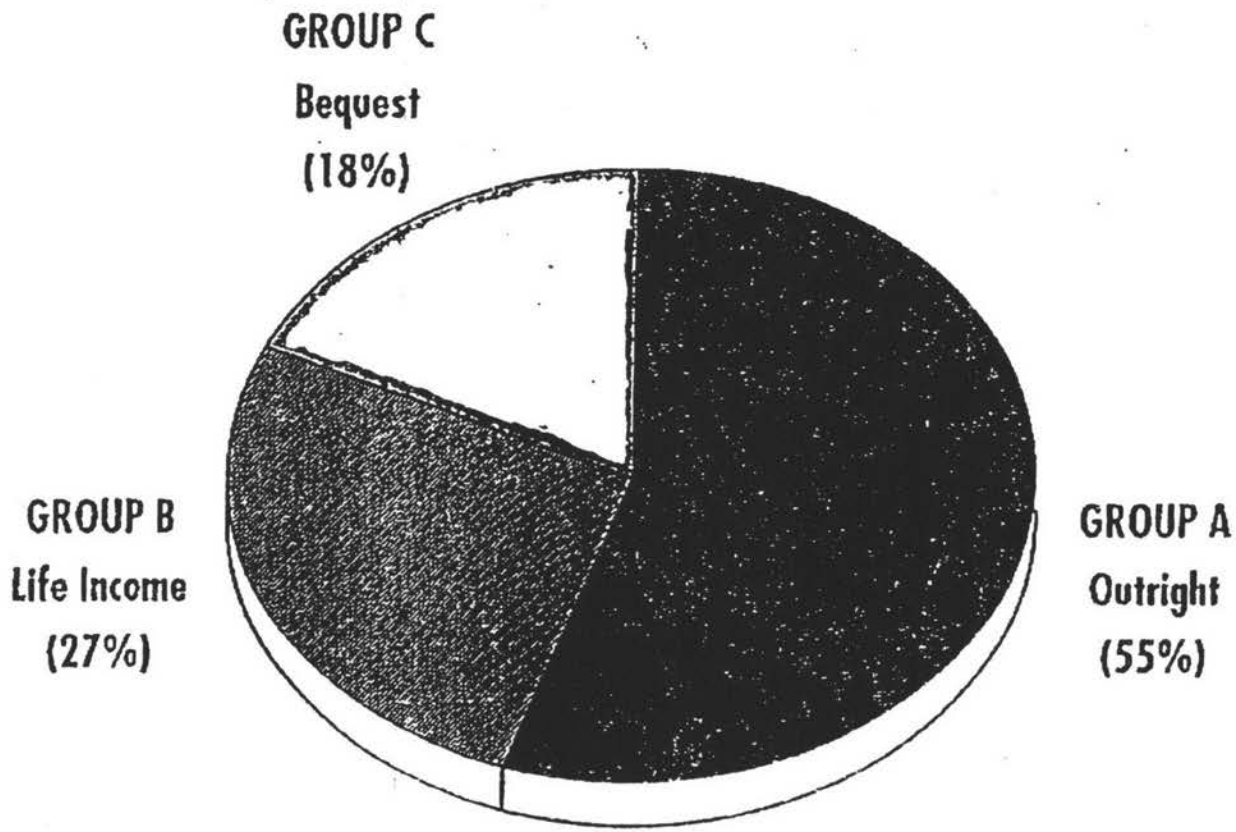
EXHIBIT 1: $1.0 M+ IRREVOCABLE GIFTS - 1980 to PRESENT

DONOR(S)	AGE(S)	OCCUPATION	LOCATION	ALUM	CHILDREN	TOTAL PAST GIVING
Dr./Mrs. A	86/75	Doctor/Teacher	California (metro)	No/Yes	No	$25
Misses B	77/75	Secretary/ Journalist	Chicago (city/suburb)	No/Yes	No	$1,104
Mrs. C	94	Teacher	Iowa (rural)	Yes	No	0
Mr. D	79	Unknown	Michigan (small city)	No	No	0
Mr. E	78	Construction	Indiana (rural)	No	Yes	0
Mr./Mrs. F	84/80	Advertising	California (metro)	Yes/No	No	0
Miss G	93	Advertising	Chicago (suburb)	No	No	$15,060
Misses H	78/74	Doctor/Secretary	Chicago (suburb)	No/Yes	No	0
Mr./Mrs. I	89/86	Manufacturer's Rep Pharmacist	Florida (city)	No/No	Yes	$280,196.38
Mr. J	78	Owner, Toothbrush Co.	Chicago (suburb)	No	Yes	0
Dr. K.	92	Dentist	Chicago (suburb)	Yes	Yes	$18,818.75
Mr. L/Miss L	deceased	Tool & Die Heir/Heiress	Chicago (city)	Yes	Yes	0
Dr./Mrs. M	76,75	VP Pharmaceutical Co	Chicago (suburb)	Yes/No	Yes	$650

EXHIBIT 2

165 Total Gifts From Individuals



2/3 Of Groups A & B Made A Gift Of $1,000+
1/3 Of Groups B & C Were Never Givers
None In Group A Were Never Givers

Planned Gifts = 45% of Total Number
Planned Gifts = 66% of Total Dollars

EXHIBIT 3

NO POSTAGE NECESSARY IF MAILED IN THE UNITED STATES

BUSINESS REPLY MAIL

FIRST CLASS MAIL PERMIT NO. 1092 EVANSTON, IL

POSTAGE WILL BE PAID BY ADDRESSEE

Jon Heintzelman, Director
Office of Planned and Major Gifts
Northwestern University
2020 Ridge Avenue
Evanston, Illinois 60201-2781

Northwestern University
Office of Planned and Major Gifts

We would be interested in any comments you have.

___

___

___

- ☐ I would like information about providing for myself and others through a life-income gift to Northwestern.
- ☐ I would like additional information about providing for the University through a will or living trust.
- ☐ I have provided for the University through my will.
- ☐ I would like information about Northwestern's Henry Wade Rogers Society for planned gifts.
- ☐ Please send a complimentary copy of Northwestern's new booklet, *Year-End Planning for Today and Tomorrow*

Home telephone ___ Office telephone ___

Business (optional) ___

EXHIBIT 4

Planned gifts with
Northwestern University
make good sense
for your retirement.
For information, call
1-800-826-6709
or 1-708-491-7392.

"George, did you realize at our age a Northwestern annuity pays 6.8%?"

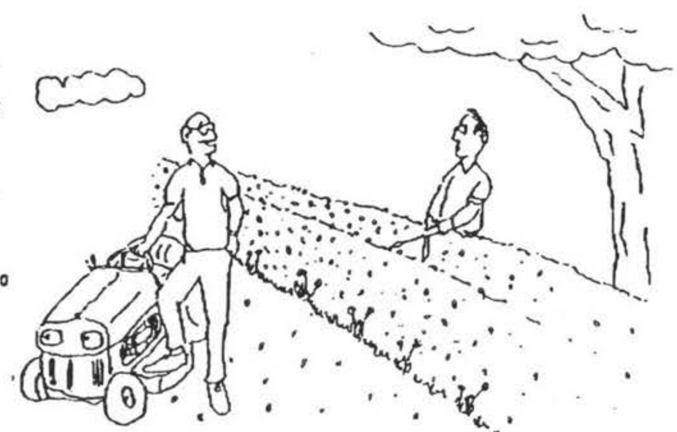
Planned gifts with
Northwestern University
make good sense for your
retirement. For information,
call 1-800-826-6709 or
1-708-491-7392, or write to
Jonathan Heintzelman,
Office of Planned and Major
Gifts, Northwestern University,
2020 Ridge Avenue,
Evanston IL 60208-4308.

We are thinking about adding a "Northwestern Plan" to our retirement package.

Planned gifts with
Northwestern University
make good sense
for your retirement.
For information, call
1-800-826-6709 or
1-708-491-7392
or write to
Jonathan Heintzelman,
Office of Planned
and Major Gifts,
Northwestern University,
2020 Ridge Avenue,
Evanston, IL 60208-4308.

George, maybe now would be a good time to update our wills!

Life income plans with
Northwestern University
create current charitable
deductions and yield
income. For information,
call 1-800-826-6709 or
1-708-491-7392, or write to
Jonathan Heintzelman,
Office of Planned and
Major Gifts,
Northwestern University,
2020 Ridge Avenue,
Evanston IL 60208-4308.



"Now, Martha and I get a check every quarter from Northwestern. We got this new mower with part of the last one"

Dealing in

EXHIBIT 5 A

F·U·T·U·R·E·S

Yours and Northwestern's

NORTHWESTERN UNIVERSITY ESTATE PLANNING FALL 1993

IMPORTANT GIFT ANNUITY RATE ANNOUNCEMENT

Annuity rates offered by Northwestern will be **reduced effective January 1, 1994,** in compliance with new lower rates set by the CGA.* Northwestern will continue to offer, through December 31, 1993, our current higher annuity rates. Therefore, **there is a window of opportunity for individuals to take advantage of the current rates through December 31.** If you have considered or are considering a gift annuity with Northwestern, you may want to take action now, **before the end of the year,** to take advantage of the higher rates. Please refer to the chart below for a comparison of rates.

Age	Current Rate	New Rate (1/1/94)	Age	Current Rate	New Rate (1/1/94)
55	6.7	5.9	75	8.5	7.7
60	7.0	6.1	80	9.6	8.8
65	7.3	6.5	85	10.9	10.0
70	7.8	6.9	90	12.0	11.0

For more information, call the Office of Planned and Major Gifts at our toll free number *1-800-826-6709* (Illinois residents may call *708-491-4945*).

*Founded in the 1920s, The Committee on Gift Annuities is a national association of 1,100 not-for-profit organizations and institutions, including colleges and universities, hospitals, churches, arts organizations and groups who do research on major diseases. The purpose of these rates is to ensure uniformity among the charitable organizations across the country.

These new lower rates are a result of the changing economic environment and the steady drop in interest rates since the last meeting of the Committee on Gift Annuities in April 1992. The Committee historically meets only once every three years; however, recent developments in the economy demanded prudent action to maintain the integrity of the Charitable Gift Annuity.

Dealing in

F·U·T·U·R·E·S

Yours and Northwestern's

NORTHWESTERN UNIVERSITY ESTATE PLANNING SPRING 1994

"Refinancing" Your Estate Plan

Many of us have refinanced home mortgages in the last year or so to take advantage of the lower interest rates. The lower rates also provide a window of opportunity to "refinance" the cost of transferring assets to heirs through a plan called the CHARITABLE LEAD TRUST.

Using the current low interest rates, the charitable lead trust is a useful tool for making significant a charitable contribution to Northwestern while transferring property to one's heirs at a reduced gift or estate tax cost. The lower rates increase the ability to shelter assets to be transferred to heirs from the potential gift and estate tax.

1993 Tax Act Rolls Back Gift and Estate Tax to Higher Rates

After 1993 changes in tax laws, the portion of an estate that exceeds the unified credit of $600,000 ($1,200,000 for couples) may be taxed at rates of up to 55%, with a 5% surcharge on estates exceeding $10 million. State inheritance taxes may be added to these federal taxes.

By establishing a charitable lead trust at Northwestern, you may be able to provide your heirs with a larger estate than would otherwise be possible.

For a personalized and confidential illustration on how a lead trust can benefit you and your heirs, please call us at:

800/826-6709

or drop us a line at:

Northwestern University
Office of Planned and Major Gifts
2020 Ridge Avenue
Evanston, IL 60208-4307

THE HENRY WADE ROGERS SOCIETY

EXHIBIT 6

☐ I accept membership in the Henry Wade Rogers Society and qualify on the following basis:

- ☐ I have included Northwestern in my will or living trust.
- ☐ I have established a life-income plan with Northwestern.
- ☐ I have an insurance policy naming Northwestern as beneficiary.
- ☐ I have made other estate provisions for Northwestern. (Please describe below)

____

____

____

I understand that upon joining the Henry Wade Rogers Society, I will receive a certificate. I would like my name to appear on the certificate as follows. (Please include spouse, if you wish.)

____

Name (Please Print)

____

Address (Please Print)

____

Signature

☐ I would be pleased to be included in Rogers Society membership lists appearing from time to time in University publications.

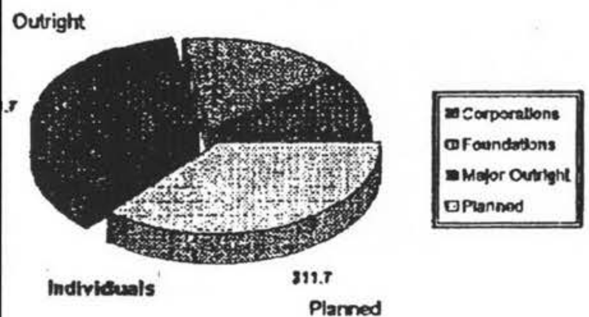
☐ I would prefer that my name not be included in Rogers Society membership lists appearing from time to time in University publications.

Northwestern University
Office of Estate Planning Services
2020 Ridge Avenue
Evanston, Illinois 60208

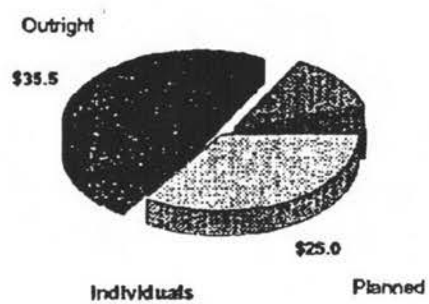
Major and Planned Gifts in Campaigns

EXHIBIT 7

Great Teachers Campaign
Total: $32.3M



Medical
TOTAL: $68M

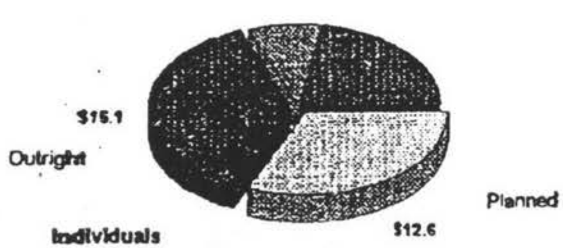


Dollars in Millions

Campaign	Total Gifts	Major Outright	Planned
Great Teachers	$32.3	$11.7	$11.7
Medical School	$68.0	$35.5	$25.0
Kellogg	$40.0	$15.1	$12.6
Law School	$27.0	$15.2	$7.6
Totals	$167.3	$77.5	$56.9
		46%	34%

80%

Kellogg Campaign
TOTAL: $40.0M



Law Campaign
TOTAL: $27.0M

RECORDING, REPORTING & SUBSTANTIATING PLANNED GIFTS

Presented by Timothy A. Jones
The University of Colorado Foundation, Inc.

For the purposes of this presentation, I will use the following definitions:

* **Recording** - accounting practices generally followed in entering and tracking planned gifts, principally split-interest gifts, on the financial statements of nonprofit organizations.

* **Reporting** - reports made to internal/external constituencies and donors/income beneficiaries concerning their planned gift's transactions, disbursements, investments, performance, valuation, etc.

* **Substantiating** - Methods to use in substantiating values used in the recording, transaction and valuation processes of planned gifts.

Recording

There are various sources of authoritative guidance on how to account for planned gifts. Some of these are as follows:

1. Financial Accounting Standards Board (FASB) statements

2. American Institute of CPA's (AICPA) audit guides and Statements of Position (SOP's)

3. Council for the Advancement and Support of Education (CASE), Council for Financial Aid to Education (CFAE) and National Association of College and University Business Officers (NACUBO) publications, among others.

In terms of a hierarchy, accounting principles described in FASB statements tend to carry the most weight, followed by AICPA guides and statements, followed by industry publications.

Recent and pending statements affecting accounting for planned gifts include the following:

1. FASB Statement #116 Accounting for Contributions Received and Contributions Made - issued and effective for fiscal years beginning after December 15, 1994. The statement does not specifically refer to split-interest gifts. The inference is drawn however.

2. FASB Statement #117 Financial Statements of Nor-for-Profit Organizations - issued and effective for fiscal years beginning after December 15, 1994. The statement does not specifically refer to split-interest gifts. The inference is drawn however.

3. AICPA Audit GuideTo provide guidance on FASB #116 & 117 and replace current audit guides for the following types of nonprofit organizations:

   A. Colleges and Universities
   B. Voluntary Health & Welfare Organizations

C. Hospitals
D. Certain Nonprofit Organizations

The draft of this new audit guide is projected to be available in March, 1995 and is expected to address split-interest gifts

Current General Accounting Practices (per AICPA Statement of Position 78-10):

1. Record asset only if the NFP is Trustee

2. Set up a liability for the present value of the life income interest - except for Pooled Income (Life Income) Funds

3. Record difference between assets and liability as "deferred revenue"

4. Record investment income as realized

5. Charge income distributions to the liability account

6. Periodically revalue the present value of the life income interest, adjusting the liability account balance through an expense account

7. At termination write off remaining liability account balance to deferred revenue

8. Reclassify deferred revenue as contribution income as restricted expenditures are incurred (if an expendable fund is created with the remainder) or as a capital addition (if an endowment fund is created with the remainder)

See the attached Chart #1 for further information

Potential New Accounting Practices (per draft proposal):

1. Record an asset whether or not the NFP is Trustee

2. If Trustee:

   A. Set up a liability for the present value of the life income interest - except for Pooled Income (Life Income) Funds

   B. Record difference between assets and liability as contribution income - either temporarily or permanently restricted

   C. Record investment income as an increase in the liability account

   D. Charge income distributions to the liability account

   E. Periodically revalue the present value of the life income interest, adjusting the liability account balance through an investment income account

   F. At termination, clear the liability account balance through an investment income account

See the attached Chart #2 for further information

Potential New Accounting Practices (per draft proposal - cont'd):

3. If Not Trustee

A. Set up an asset for the present value of the remainder interest

B. Record a contribution equal to the amount recorded in A above - either temporarily or permanently restricted

C. Periodically revalue the present value of the remainder interest, adjusting the asset account balance through an investment income account

D. At termination, clear the asset account balance through an investment income account

See the attached Chart #3 for further information

Reporting

In developing reports to provide to interested parties about an organization's planned gifts, the organization should consider the following:

1. What do the parties want? Consider a survey to determine needs. You may be surprised to find the simple information needs some, if not most, have.

2. Don't invite extended analysis. Extended analysis such as custom investment performance measurement reports and analysis of the economy takes a lot of time and expertise to prepare. With administrative staffs at NFP organizations tending to be "thin", excessive reporting demands may lead to undesired stress and turnover. Be ready to make a significant budget commitment if you choose to go down the sophisticated reporting path.

To help you in determining a minimum set of reports and information to provide to interested parties, principally donors and income beneficiaries, I offer the following list:

1. Annual Schedule K-1 or Form 1099R - see the attached Charts #4-5

2. Notices of Distributions - see the attached Chart #6

3. Year End Portfolio Report - see the attached Charts #7-9

4. Annual Formal Unitrust Valuations - see the attached Chart #10

   Note: If you are reporting on a pooled income fund or a pooled gift annuity program, you could offer a global report on the pool with a schedule showing the individual's interest in the pool. For a pooled gift annuity program, you might also consider including an actuary's report if one is obtained.

Optional additional reporting might include:

1. Investment Performance Reports - see the attached Charts #11-13

2. Reports on the Economy

3. Summary Program Reports - see the attached Chart #14-17

Substantiation

There are at least two critical values an organization needs to determine for planned gifts:

1. Fair Market Value - needed at inception to establish assets on the NFP's books and begin the remainder interest calculations. Needed during life of arrangements to revalue unitrusts, revalue the present value of income interests and mark assets to market if the NFP so elects, etc.

2. Remainder Interest - needed at inception to properly record the contribution portion of arrangements.

In determining fair market values, an organization has some flexibility in determining the source of valuation information. For cash and publicly traded securities the sources are obvious. For non-publicly traded securities and other hard to value assets consider the following:

1. Use of Donor's Experts:

   A. Creates agreement between the donor and donee.

   B. Beware though of the tendency to overvalue the asset(s).

   C. Could create a lasting problem with annuity arrangements via a permanently overstated income interest (example: $100,000 8% CRAT really worth $80,000 has an effective annuity rate of 10%).

   D. Donor will likely engage an expert to only value the asset(s) once - on date of gift. Thereafter it becomes the trustee's "problem".

2. Use of Donee's Experts:

   A. Objectivity of the value(s) is further assured.

   B. Who will pay the cost - NFP or trust? What if the trust has no cash?

   C. Could create a lack of consistency between the donor and donee resulting in potential conflict.

Suggestions:

1. Use the donor's expert at inception, being careful to negotiate a payout rate that may be impacted by an overstated value.

2. Thereafter, use a donee expert. Obviously, in most cases the objective is to sell the hard to value asset and invest the cash in easier to value assets. This may not be an option though and the NFP may find itself holding onto the hard to value asset. If so, consider using an expert within or connected to your organization. Examples would include a Board member or employee with skills such as: an art specialist, a real estate expert, a financial expert, CPA, attorney, etc. If no internal expert is available, consider engaging an outside expert with associated fees borne by the trust.

3. If the NFP is "well heeled", consider buying the asset out of the trust arrangement, replacing it with cash or a note.

With regard to determining charitable remainder interests, there remains flexibility also. This flexibility is provided because the donee is not bound to the same calculations as the donor (i.e. IRS regulations, etc.). Sources for remainder interest calculations would include:

1. Commercially available remainder interest calculator programs such as PG Calc, Crescendo, CCH, etc. These calculate the remainder interest in strict accordance to IRS regulations. Using numbers generated from these programs would create agreement between the donor and donee but may under/overstate the true contribution element.

2. Internal spreadsheet type analysis. For example, perhaps the donee does not want to discount an annuity at the "Adjusted Applicable Federal Mid Term Rate" (currently 9%+). A lower discount rate would result in a lower contribution recorded (alternatively, a higher present value income interest). The NFP's independent auditor might be interested in the reasoning behind using a different discount rate.

3. Beware of IRS receipting rules though. If the NFP customarily generates receipts in addition to the trust agreements themselves, the NFP's receipts should agree to the IRS calculated remainder interest.

Suggestions:

1. Make your life simple and use a commercially available remainder interest calculator. Soothe your fear of understating contribution income with the understanding that discount rates will fluctuate over time. The result should be that in some years contribution income will be understated, in other years overstated.

2. If you choose to calculate the remainder interest yourself, enlist the services of your finance and/or accounting office to perform the calculation. This will place the finance/accounting department in an educated position to explain the rationale to an interested independent auditor.

3. Consider making the trust agreement or gift annuity contract the one and only official receipt generated by the NFP organization. This will help avoid issuing conflicting numbers to the donors and should result in compliance with IRS receipting rules.

Timothy A. Jones, *Treasurer*
The University of Colorado Foundation, Inc.
P.O. Box 1140
Boulder, Colorado 80306
Voice: (303) 492-3616
Fax: (303) 492-5407
Internet: Jones_T@Cufund.Colorado.Edu

CERTAIN NONPROFIT ORGANIZATIONS (SOP 78–10)
Accounting for Split Interests

		Remainder Interests			Lead Interests
		Charitable Remainder Trusts	Charitable Gift Annuities	Life Income Funds	Charitable Lead Trusts
Donor's initial gift	Dr Cr Cr Cr Amount	Assets Annuities payable Support Deferred revenue *Assets at FMV* *Annuities payable at NPV* *The excess of assets over annuities payable is recorded as support to the extent that it may be used immediately, and as deferred revenue to the extent restricted for specific purposes.*	Assets Annuities payable Support Deferred revenue *Assets at FMV* *Annuities payable at NPV* *The excess of assets over annuities payable is recorded as support to the extent that it may be used immediately, and as deferred revenue to the extent restricted for specific purposes.*	Assets Deferred revenue *Assets at FMV*	N O T C O V E R E D
Investment income earned	Dr Cr Amount	NOT SPECIFIED			
Payments to life income beneficiary	Dr Cr Amount				
Periodic revaluations	Dr Cr Amount				
Termination of split interest	Dr Cr Amount	Deferred revenue–annuity fund Support *To reverse any amounts recorded as deferred support.* *Note: The disposition of any balance in annuities payable is not specified by SOP 78–10.*	Deferred revenue–annuity fund Support *To reverse any amounts recorded as deferred support.* *Note: The disposition of any balance in annuities payable is not specified by SOP 78–10.*	Deferred revenue Support	

** DRAFT PROPOSAL **

Accounting by Not–For–Profit Organizations for Split Interests

(When The Charity Acts As The Trustee)

		Remainder Interests			Lead Interests
		Charitable Remainder Trusts	Charitable Gift Annuities	Pooled (Life) Income Funds	Charitable Lead Trusts
Donor's initial gift	Dr Cr Cr Amount	Assets Annuities payable Contributions *Assets at FMV* *Annuities payable at the discounted NPV of the expected payment stream over the donor's life expectancy*	Assets Annuities payable Contributions *Assets at FMV; Liability at NPV; Contributions at the difference between assets and liability.*	Assets placed in trust Contributions *Assets at FMV*	Assets placed in trust Assets held for others Contributions *Discounted NPV of the expected income stream over the donor's life expectancy*
Investment income earned	Dr Cr Amount	Cash Annuities payable	Cash Investment income	Cash Income payable	Cash Assets held for others
Payments to life income beneficiary[1]	Dr Cr Amount	Annuities payable Cash	Investment income Cash	Income payable Cash	Assets held for others Investment income
Periodic revaluations	Dr Cr Amount	Investment income[2] Annuities payable[2] *NPV*	Investment income[2] Annuities payable[2] *NPV*	N/A	Assets held for others Investment income *NPV*
Termination of split interest	Dr Cr Amount	Annuities payable Investment income	Annuities payable Investment income *Balance remaining, if any, in annuities payable account.*	Net assets – PIF Net assets – other	Assets held for others Assets placed in trust

Notes

[1] The life income beneficiary of a Charitable Remainder Trust, Charitable Gift Annuity, and Pooled Income Fund is the donor or the donor's designee; the life income beneficiary of a Charitable Lead Trust is the not–for–profit organization.

[2] Or vice versa

** DRAFT PROPOSAL **

Accounting by Not–For–Profit Organizations for Split Interests

(Assuming The Charity Is Not The Trustee)

		Remainder Interests			Lead Interests
		Charitable Remainder Trusts	Charitable Gift Annuities	Pooled (Life) Income Funds	Charitable Lead Trusts
Donor'S Initial Gift	Dr Cr Ci Amount	Receivable from trust[1] Contributions *Discounted NPV of trust assets over the donor's life expectancy.*	Cash (or securities) Annuities payable Contributions *Assets at FMV; Liability at NPV; Contributions at the difference between assets and liability.*	N/A While the not–for–profit organization need not be the fund's trustee, it must control its management (for example, retain the power to remove the trustee). Therefore, even if the not–for–profit organization were not the trustee, it would account for the transactions as though it were the trustee.	Receivable from trust[1] Contributions *Discounted NPV of the expected income stream over the donor's life expectancy*
Investment Income earned	Dr Cr Amount	N/A	Cash Investment Income *GAAP*		N/A
Payments to life income beneficiary[3]	Dr Cr Amount	N/A	Annuities payable Cash *Payments to donor*		Cash Receivable from trust *Trust payments to NPO*
Periodic revaluations	Dr Cr Amount	Receivable from trust[1,2] Investment Income[2] *NPV*	Investment Income[2] Annuities payable[2] *NPV*		Receivable from trust[1,2] Investment Income[2] *NPV*
Termination of split Interest	Dr Cr Cr Amount	Cash Receivable from trust[1] Investment Income[2] *Cash = amount received; Receivable = balance*	Annuities payable Investment Income *Balance remaining, if any, in liability to donor account.*		Investment Income Receivable from trust[1] *Receivables are credited for any balance remaining*

Notes

[1] "Receivable from trust" represents the not–for–profit organization's economic beneficial interest in trust assets.

[2] Or vice versa

[3] The life income beneficiary of a Charitable Remainder Trust, Charitable Gift Annuity, and Pooled Income Fund is the donor or the donor's designee; the life income beneficiary of a Charitable Lead Trust is the not–for–profit organization.

SCHEDULE K-1 (Form 1041)

Department of the Treasury
Internal Revenue Service

Beneficiary's Share of Income, Deductions, Credits, etc.

for the calendar year 1994, or fiscal year

beginning ...., 1994, ending ...., 19 ....

▶ Complete a separate Schedule K-1 for each beneficiary.

OMB No. 1545-0092

1994

☐ Amended K-1
☐ Final K-1

Name of trust or decedent's estate
Sample CRUT U/A 7/27/92

Beneficiary's identifying number ▶ 123-45-6789

Estate's or trust's EIN ▶ 84-1234567

Beneficiary's name, address, and ZIP code
Beneficiary's Name
Street Address
City, State Zip

Fiduciary's name, address, and ZIP code
The University of Colorado Foundation, Inc
PO Box 1140, 1305 University Avenue
Boulder, CO 80306

	(a) Allocable share item		(b) Amount	(c) Calendar year 1994 Form 1040 filers enter the amounts in column (b) on:
1	Interest	1	0	Schedule B, Part I, line 1
2	Dividends	2	17,007	Schedule B, Part II, line 5
3a	Net short-term capital gain	3a	3,188	Schedule D, line 5, column (g)
b	Net long-term capital gain	3b	15,181	Schedule D, line13, column (g)
4a	Annuities, royalties, and other nonpassive income before directly apportioned deductions	4a		Schedule E, Part III, column (f)
b	Depreciation	4b		Include on the applicable line of the appropriate tax form
c	Depletion	4c		
d	Amortization	4d		
5a	Trade or business, rental real estate, and other rental income before directly aportioned deductions (see instructions)	5a		Schedule E, Part III
b	Depreciation	5b		Include on the applicable line of the appropriate tax form
c	Depletion	5c		
d	Amortization	5d		
6	Income for minimum tax purposes	6	35,376	
7	Income for regular tax purposes (add lines 1 through 3b, 4a, and 5a)	7	35,376	
8	Adjustment for minimum tax purposes (subtract line 7 from line 6)	8	0	Form 6251, line 12
9	Estate tax deduction (including certain generation-skipping transfer taxes)	9		Schedule A, line 28
10	Foreign taxes	10		Form 1116 or Schedule A (Form 1040), line 8
11	Adjustments and tax preference items (itemize):			
a	Accelerated depreciation	11a		Include on the applicable line of Form 6251
b	Depletion	11b		
c	Amortization	11c		
d	Exclusion items	11d		1995 Form 8801
12	Deductions in the final year of trust or decedent's estate:			
a	Excess deductions on termination (see instructions)	12a		Schedule A, line 22
b	Short-term capital loss carryover	12b		Schedule D, line 5, column (f)
c	Long-term capital loss carryover	12c		Schedule D, line 13, column (f)
d	Net operating loss (NOL) carryover for regular tax purposes	12d		Form 1040, line 21
e	NOL carryover for minimum tax purposes	12e		See the instructions for Form 6251, line 20
f	....	12f		Include on the applicable line of the appropriate tax form
g		12g		
13	Other (itemize):			
a	Payments of estimated taxes credited to you	13a		Form 1040, line 55
b	Tax-exempt interest	13b		Form 1040, line 8b
c	US Gov't Interest on Line 2	13c	4,528	Include on the applicable line of the appropriate tax form
d	....	13d		
e	....	13e		
f	....	13f		
g	....	13g		
h		13h		

For Paperwork Reduction Act Notice, see page 1 of the Instructions for Form 1041. Cat. No. 11380D **Schedule K-1 (Form 1041) 1994**
S388

Chart #4

9898 ☐ VOID ☐ CORRECTED

PAYER'S name, street address, city, state, and ZIP code

The University of Colorado
Foundation, Inc.
PO Box 1140
Boulder, CO 80306

1 Gross distribution
$ 2,500

2a Taxable amount
$ 888

OMB No. 1545-0119

1994

Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.

2b Taxable amount not determined ☐

Total distribution ☐

Copy A For Internal Revenue Service Center

File with Form 1096.

PAYER'S Federal identification number
84-6049811

RECIPIENT'S identification number

3 Capital gain (included in box 2a)
$ -0-

4 Federal income tax withheld
$ -0-

RECIPIENT'S name

5 Employee contributions or insurance premiums
$

6 Net unrealized appreciation in employer's securities
$

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, and W-2G.

Street address (including apt. no.)

7 Distribution code
7

IRA/SEP ☐

8 Other
$ %

City, state, and ZIP code

9 Your percentage of total distribution
%

Account number (optional)

10 State tax withheld
$ -0-
$

11 State/Payer's state no.

12 State distribution
$
$

13 Local tax withheld
$ -0-
$

14 Name of locality

15 Local distribution
$
$

Form 1099-R

Cat. No. 14436Q

Department of the Treasury - Internal Revenue Service

Chart #5

CO. FILE DEPT. CLOCK NUMBER
NGF 000134 0000000332 1

Earnings Statement

THE UNIVERSITY OF COLORADO FOUNDATION, INC.
1305 UNIVERSITY AVE. (303) 492-5016
BOULDER, CO 80306

Period Ending: 12/31/94
Pay Date: 12/30/94

Social Security Number
Taxable Marital Status:
Exemptions/Allowances:
Federal: 0,Tax Blocked
State: 0,Tax Blocked

Earnings	rate	hours	this period	year to date
Regular			8,843.99	
Gross Pay			$8,843.99	26,531.99
Net Pay			$8,843.99	

Important Notes

IF YOU HAVE QUESTIONS CALL AMY FORKER AT 303-492-0578.

THE FACE OF THIS DOCUMENT HAS A COLORED BACKGROUND ON WHITE PAPER. THE BACK OF THIS DOCUMENT CONTAINS AN ARTIFICIAL WATERMARK - HOLD AT AN ANGLE TO VIEW

THE UNIVERSITY OF COLORADO FOUNDATION, INC.

NGF 82-19/1070
Payroll check number: 00000332
Pay date: 12/30/94

VOID VOID

Pay to the order of:

This amount: EIGHT THOUSAND EIGHT HUNDRED FORTY THREE AND 99/100 DOLLARS $8843.99

BANK ONE, BOULDER, N.A.
BOULDER BANKING CENTER
BOULDER, CO 80302

VOID VOID VOID

AUTHORIZED SIGNATURE

⑈00000332⑈ ⑆107000194 Chart #6 340⑈

University of Colorado Foundation, Inc.

Foundation Center
1305 University Avenue
P.O. Box 1140
Boulder Colorado 80306
(303) 492-5016

March 31, 1994

2ADDRESS1?~
3ADDRESS2?~
4ADDRESS3?~
5ADDRESS4?~
6ADDRESS5?~
7CITY?~, 8ST?~ 9ZIP?~

Dear 10SALUTATION?~:

Enclosed please find a portfolio appraisal and formal unitrust valuation for tax year 1994. The March 31, 1994, distribution payment from your life income arrangement at The University of Colorado Foundation, Inc. is also enclosed.

The portfolio appraisal is included as an annual summary of the total asset cost, market value and current yield for your portfolio as of December 31, 1993. In addition, the unitrust valuation report is generated annually to compute the 1994 cash distribution amount based on the payout rate for your unitrust.

Thank you again for your support of the University and please do not hesitate to contact us if you have any questions regarding your life income arrangement here at the Foundation.

Sincerely,

Timothy A. Jones
Treasurer

TAJ/acf

cc: Betsy A. Mangone
Robert I. Spengler
Amy C. Forker

Chart #7

The University of Colorado Foundation, Inc.

PORTFOLIO APPRAISAL

Sample 6.0% Charitable Remainder Unitrust U/A 7/27/92

1-0-62345 Foundation Account

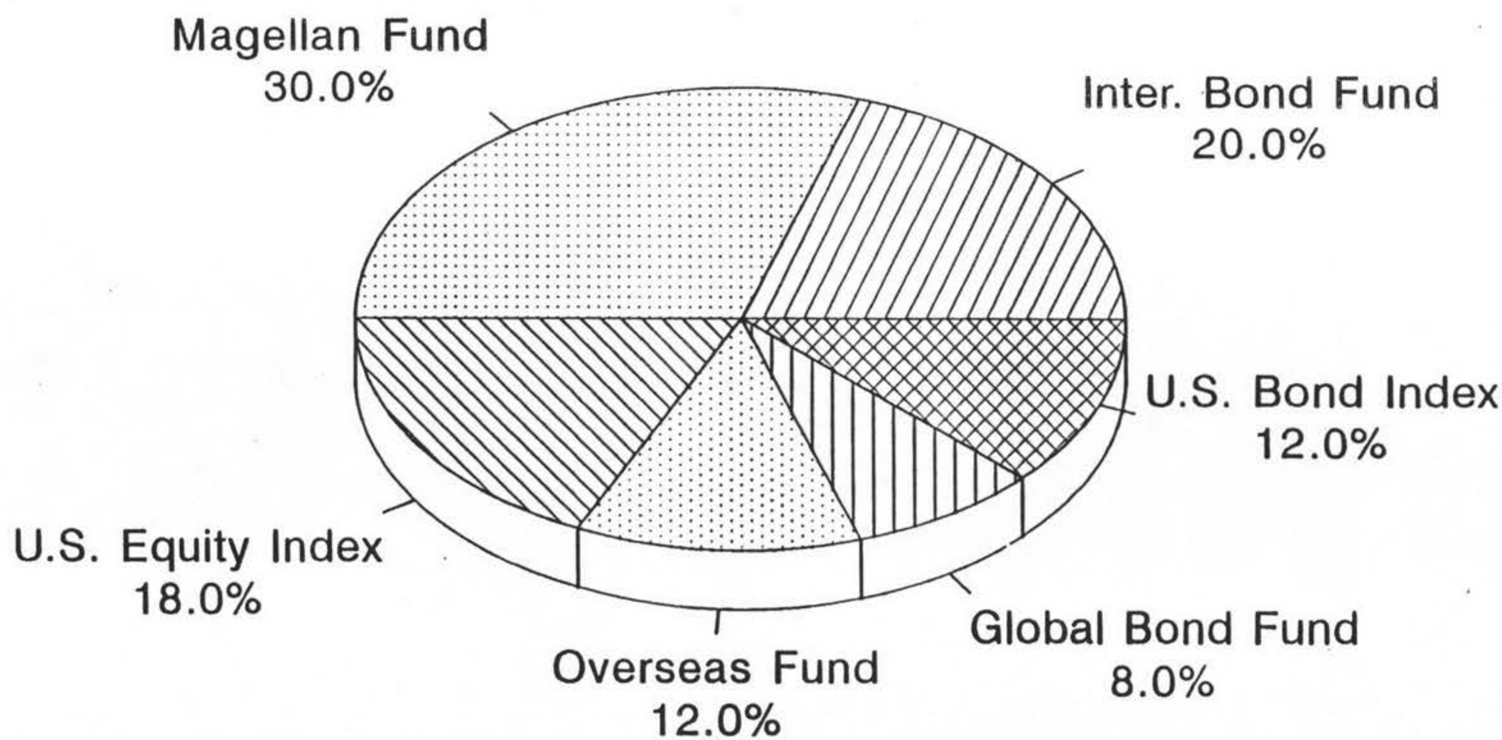
January 31, 1994

Quantity	Security	Unit Cost	Total Cost	Market Price	Market Value	Pct. Assets	Unit Income	Annual Income	Cur. Yield
EQUITY MUTUAL FUNDS									
Domestic Equities									
3,546.242	Fidelity Magellan Fund	64.37	228,275.83	73.65	261,180.72	44.3	0.130	461.01	0.2
3,731.254	Fidelity US Equity Index Portfolio	15.43	57,576.83	17.85	66,602.88	11.3	0.390	1,455.19	2.2
			285,852.66		327,783.61	55.6		1,916.20	0.6
Foreign Equities									
1,456.065	Fidelity Overseas Fund	22.07	32,140.37	29.38	42,779.19	7.3	0.000	0.00	0.0
			32,140.37		42,779.19	7.3		0.00	0.0
	EQUITY MUTUAL FUNDS Total		317,993.04		370,562.80	62.8		1,916.20	0.5
FIXED INCOME MUTUAL FUNDS									
Domestic Obligations									
14,036.361	Fidelity Intermediate Bond Fund	10.59	148,692.96	10.85	152,294.52	25.8	0.642	9,012.75	5.9
3,864.271	Fidelity US Bond Index Portfolio	11.07	42,785.97	11.08	42,816.12	7.3	0.742	2,867.68	6.7
			191,478.93		195,110.64	33.1		11,880.42	6.1
Foreign Obligations									
1,873.360	Fidelity Global Bond Fund	11.87	22,239.85	12.69	23,772.94	4.0	0.691	1,294.12	5.4
			22,239.85		23,772.94	4.0		1,294.12	5.4
	FIXED INCOME MUTUAL Total		213,718.78		218,883.58	37.1		13,174.54	6.0
CASH AND EQUIVALENTS									
	Fidelity US Govt Reserves		153.51		153.51	0.0	2.820	4.33	2.8
			153.51		153.51	0.0		4.33	2.8
TOTAL PORTFOLIO			531,865.32		589,599.88	100.0		15,095.07	2.6

Chart #8

Sample Portfolio - 6% Required Payment
60:40 Equity / Fixed-Income Mix

Diversified holdings in domestic and global equity and fixed-income mutual funds



Expected Total Return 9.52%
Expected Yield 3.71%

Chart #9

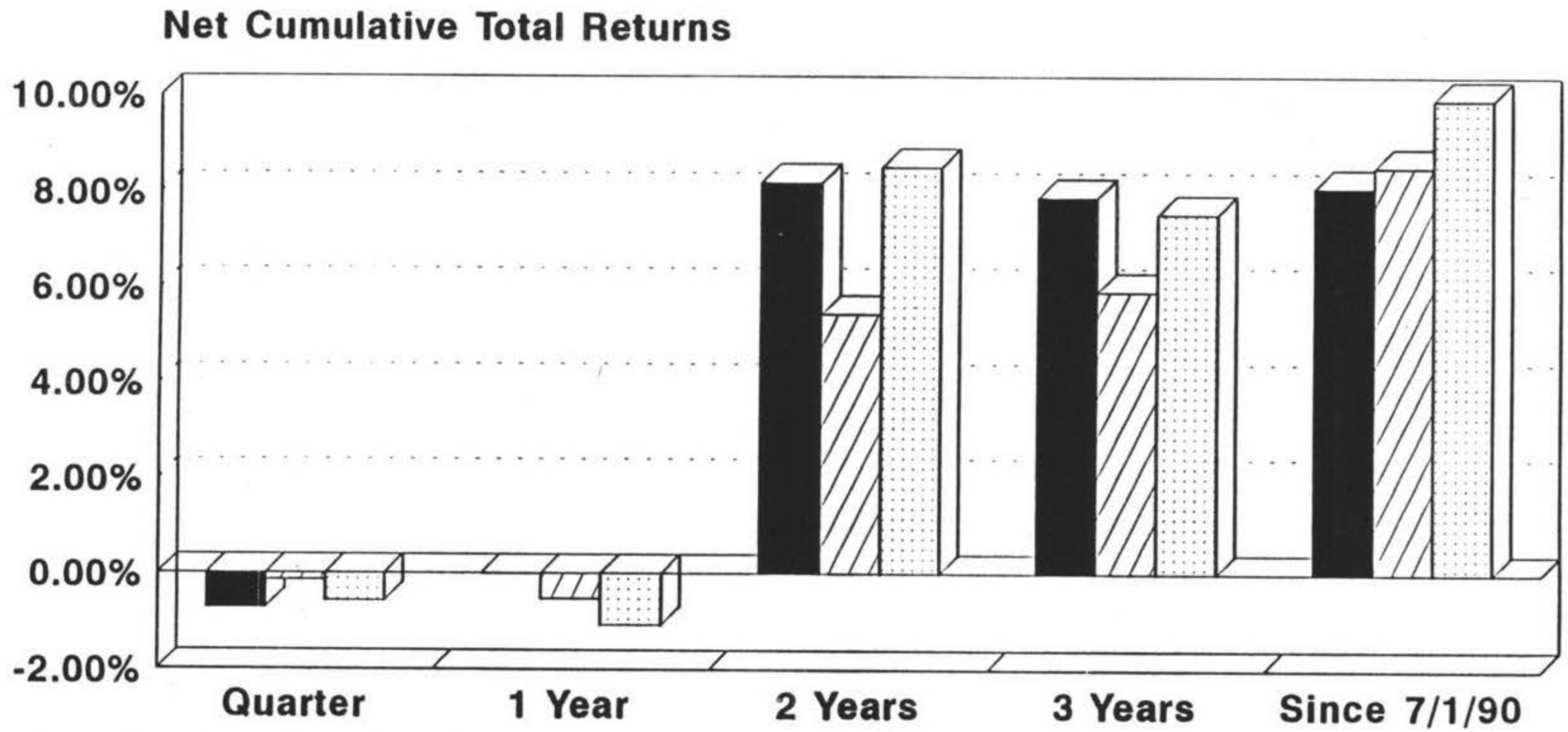
Sample CRUT
FRS #1-0-62345, Advent #1-0-62345
As of January 31, 1994
File: SAMPLE94

Asset Description	Shares or Par Value	Hi/Ask	Lo/Bid	Mean/ NAV	Market Value	Value Sourc
Fidelity Magellan Fund	3,546.242			73.65	261,180.72	Fidelit
Accrued Dividend						
Fidelity US Equity Index Fund	3,731.254			17.85	66,602.88	Fidelit
Accrued Dividend						
Fidelity Overseas Fund	1,456.065			29.38	42,779.19	Fidelit
Accrued Dividend						
Fidelity Intermediate Bond Fund	14,036.361			10.85	152,294.52	Fidelit
Accrued Dividend						
Fidelity US Bond Index Fund	3,864.271			11.08	42,816.12	Fidelit
Accrued Dividend						
Fidelity Global Bond Fund	1,873.360			12.69	23,772.94	Fidelit
Accrued Dividend						
Fidelity US Gov't Reserves	153.51			1.00	153.51	N/A
Accrued Dividend						

1/31/94 Value	589,599.88
Unitrust Rate	6.00%
1994 Unitrust Amount	35,375.99
1993 Unitrust Amount	31,274.88
% Increase (Decrease)	13.11%

Chart #10

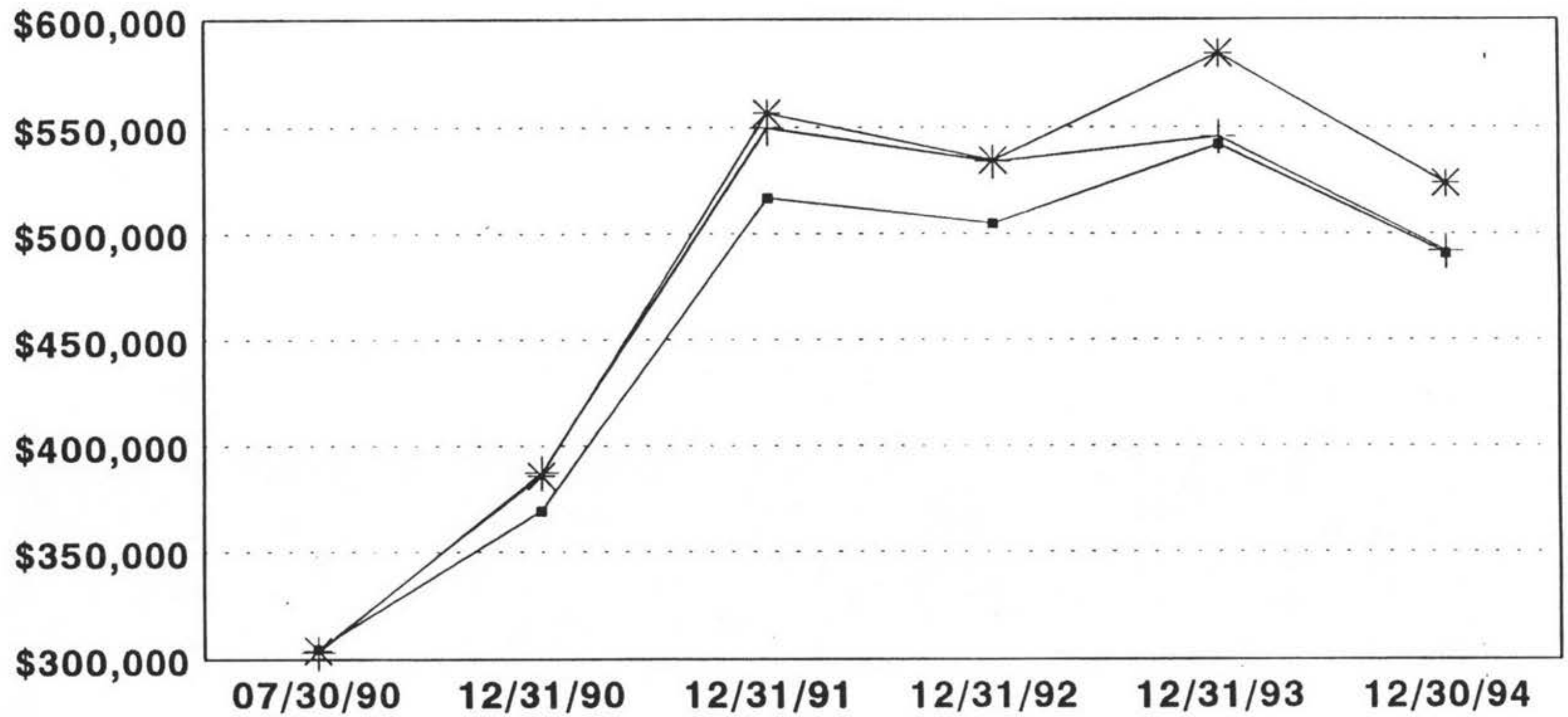
Sample 9.25% Charitable Remainder Unitrust
Total Trust Performance Versus Indexes
As of December 30, 1994



	Quarter	1 Year	2 Years	3 Years	Since 7/1/90
CRUT Actual	-0.72%	-0.01%	8.19%	7.88%	8.08%
Weighted Index	-0.14%	-0.53%	5.44%	5.91%	8.51%
Fidelity Std. Mix	-0.58%	-1.08%	8.50%	7.53%	9.91%

CRUT Actual | Weighted Index | Fidelity Std. Mix

Sample 9.25% Charitable Remainder Unitrust
Ending Fair Market Value Comparisons
As of December 30, 1994



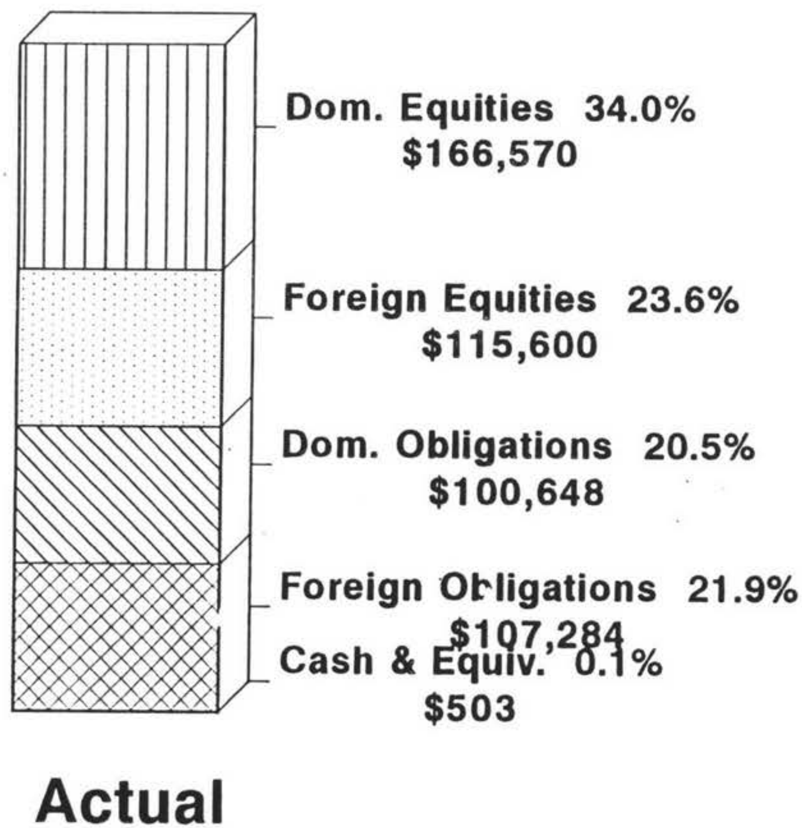
	07/30/90	12/31/90	12/31/91	12/31/92	12/31/93	12/30/94
CRUT Actual	$304,728	$369,344	$516,658	$504,722	$541,835	$490,605
Weighted Index	$303,118	$387,248	$549,574	$533,733	$545,577	$491,695
Fidelity Std. Mix	$304,028	$385,853	$556,588	$534,498	$584,359	$523,572

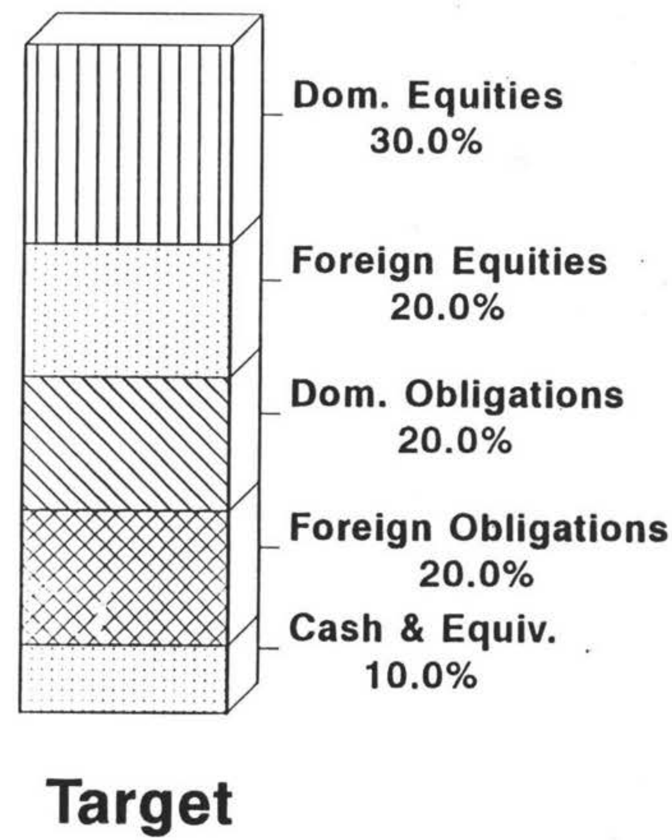
CRUT Actual + Weighted Index ✳ Fidelity Std. Mix

Sample 9.25% Charitable Remainder Unitrust

Actual vs. Target Asset Allocation

As of December 30, 1994





Ending Market Value $490,605

University of Colorado Foundation, Inc.
Growth in Number of Life Income Arrangements
As of December 30, 1994

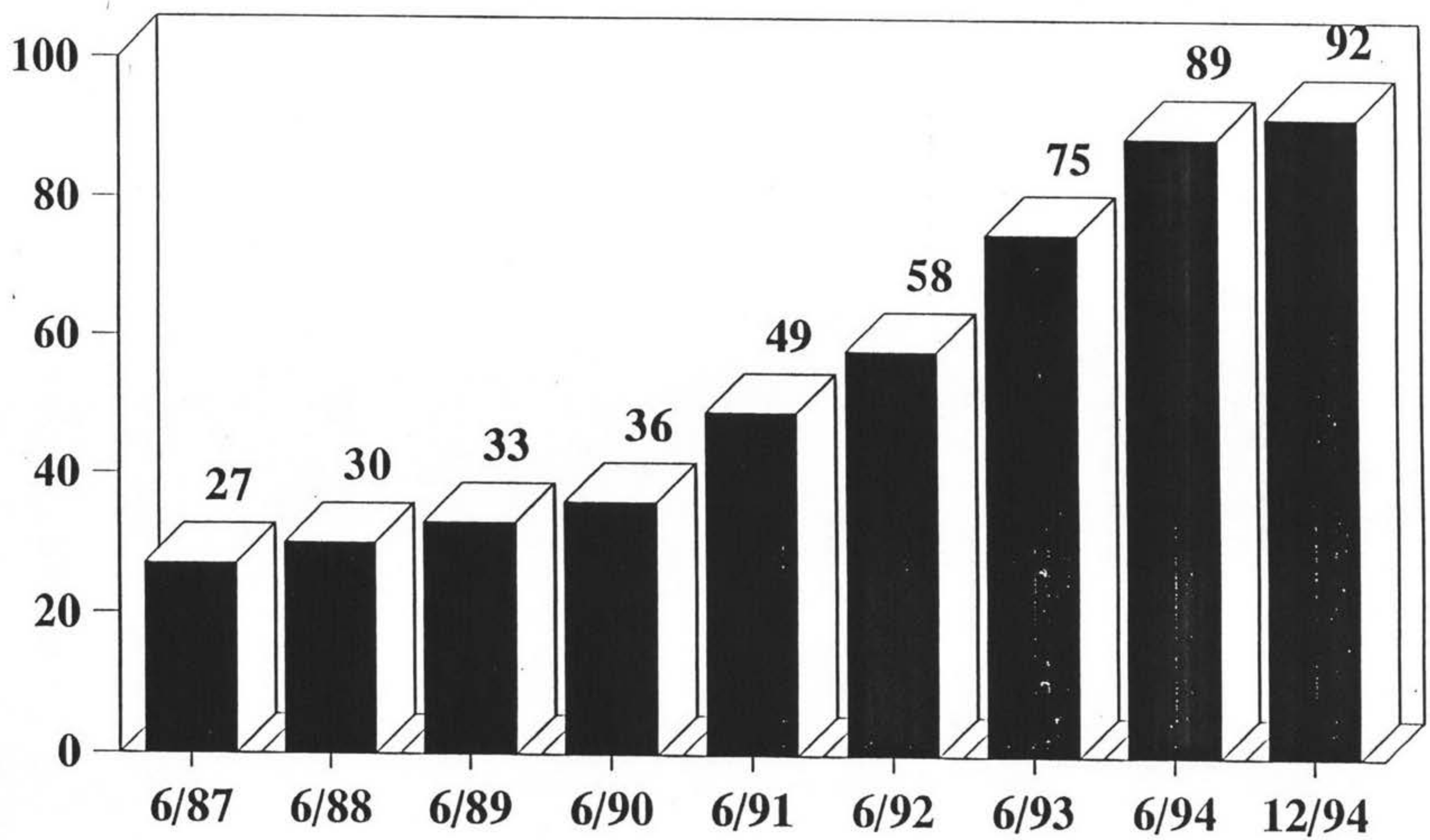


Chart #14

University of Colorado Foundation, Inc.
Growth in FMV of Life Income Arrangements
As of December 30, 1994

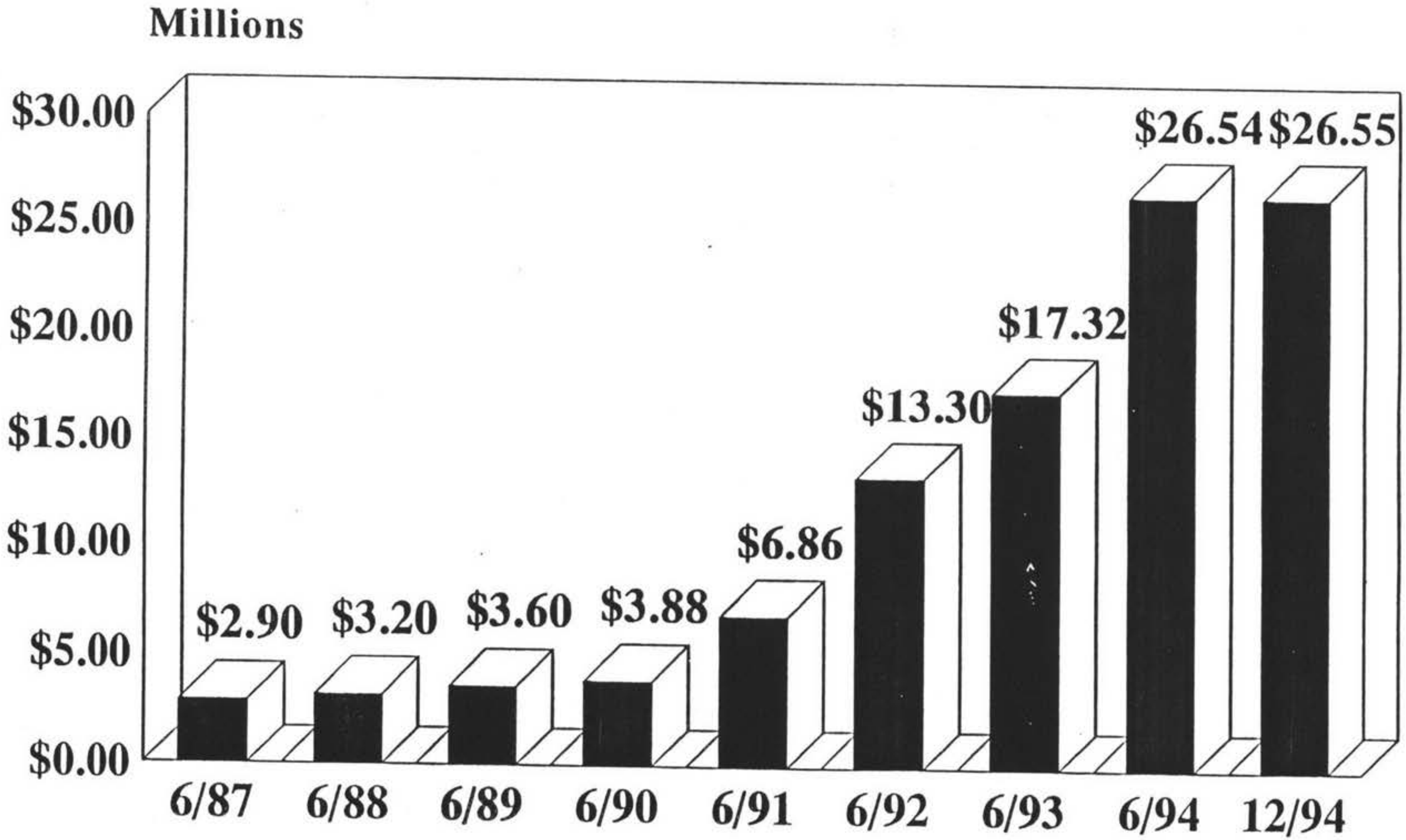
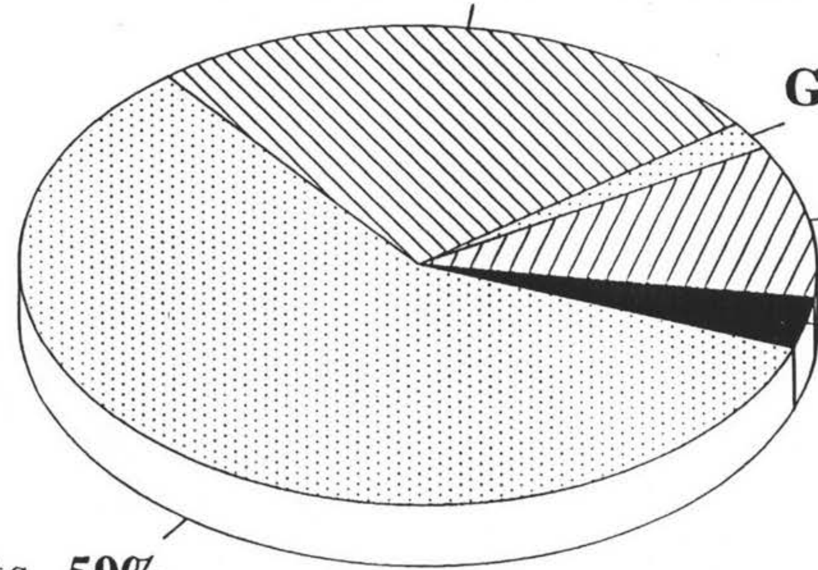


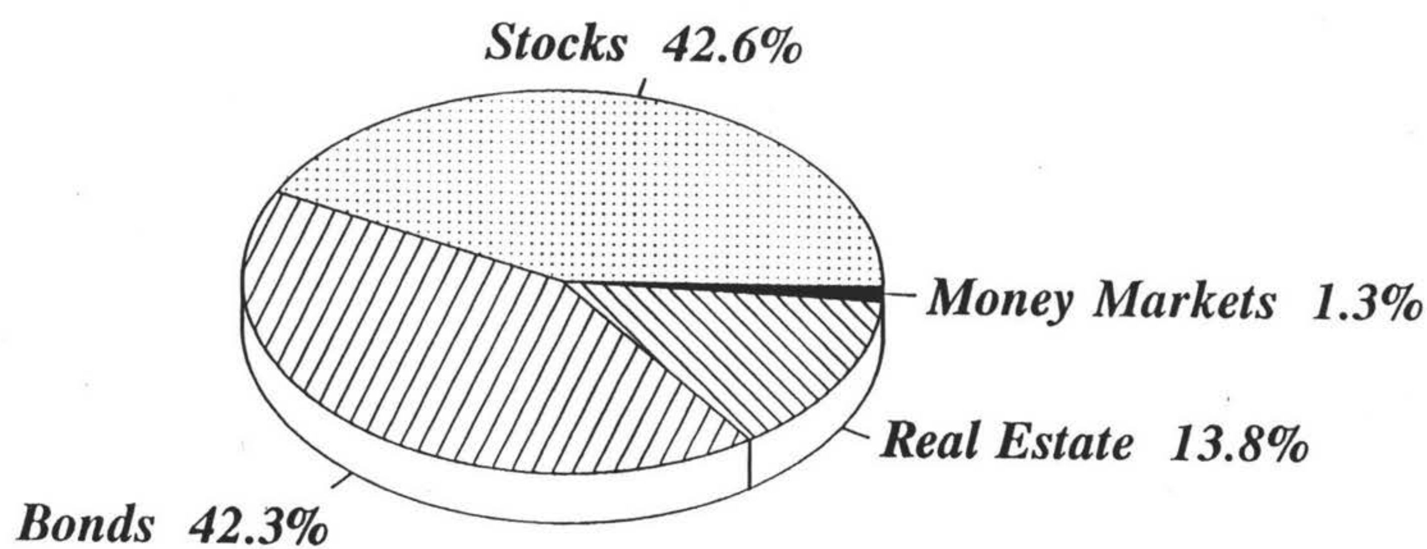
Chart #15

University of Colorado Foundation, Inc.
Types of Life Income Arrangements by FMV
As of December 30, 1994



Overall Fair Market Value = $26,550,591

Life Income Arrangements
Overall Asset Allocation
As of December 30, 1994



Overall Fair Market Value = $26,550,591

Chart #17

PLANNED GIVING SERVICES
22ND CONFERENCE ON GIFT ANNUITIES
PLANNED GIFTS DECISIONS: POTENTIAL RISKS & REWARDS

J. SCOTT KASPICK
MANAGING DIRECTOR, KASPICK & COMPANY

Planned giving professionals play a powerful role in helping donors arrive at decisions regarding trust vehicles and payout rates. These trust decisions along with the charity's policies determine the investment approach that will be used for each trust. The combination of trust decisions, policies, and investment approach when mixed with market uncertainties exposes the beneficiary and the charity to a set of potential risks and rewards. These risks and rewards can, however, be defined.

Planned giving professionals are often not aware of the set of potential risks and rewards they are helping to create. This lack of knowledge can cause substantial issues for the donor as well as for the charity. This presentation is designed to improve this awareness and provide the **planned giving professional** with:

1. A greater sensitivity to the importance of his or her role in the gift planning process.

2. The ability to provide more complete advice to the donor regarding the likely effects of choices regarding trust type and payout rate on both the beneficiary's and the charity's interests.

3. The ability to disclose a set of likely risks to the donor.

4. Some practical tools for identifying and evaluating alternatives and communicating them to donors.

KASPICK & COMPANY
PORTFOLIO MANAGEMENT

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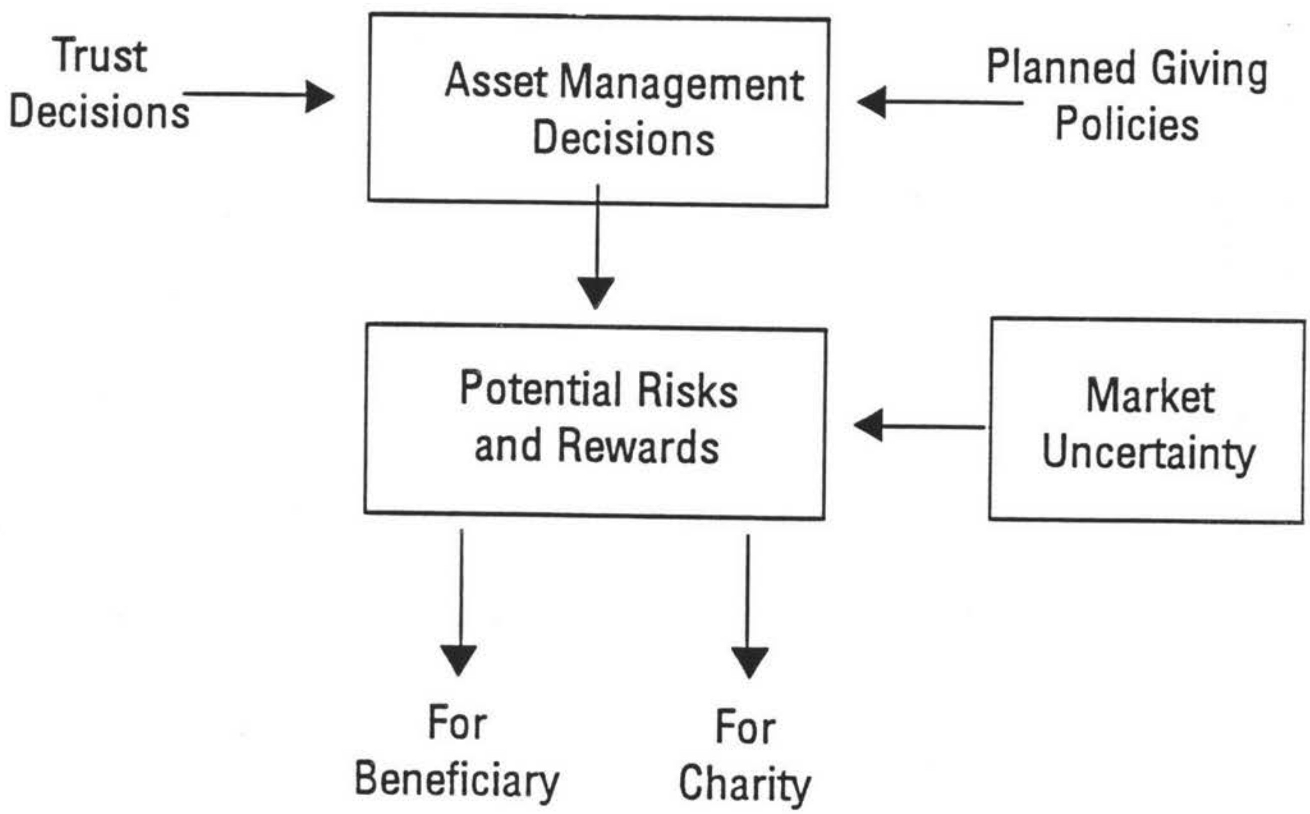
Planned Gifts Decision Environment



Which Gift Vehicle?

Questions to Ask:
What is expected trust life?
What are pros and cons of alternative trust vehicles?

Trust Type	Appropriate Trust Life	Good Qualities	Poor Qualities
Annuity Trust, Gift Annuity	Short ($\leq$10 years)	No income volatility	No income growth
Net Income Unitrust	Full range	Accomodates illiquid assets Allows change in income over time (spec. situations) Possible income growth	Income volatility Sensitive to market yields Can't use total return for payout
Pooled Income Fund	Full range	Pool small gifts Possible income growth	Income volatility Sensitive to market yields Can't use total return Deduction issue
Flat Unitrust	Full range	Possible income growth Use total return for payout	Income volatility Income can erode rapidly Can't adjust income over life

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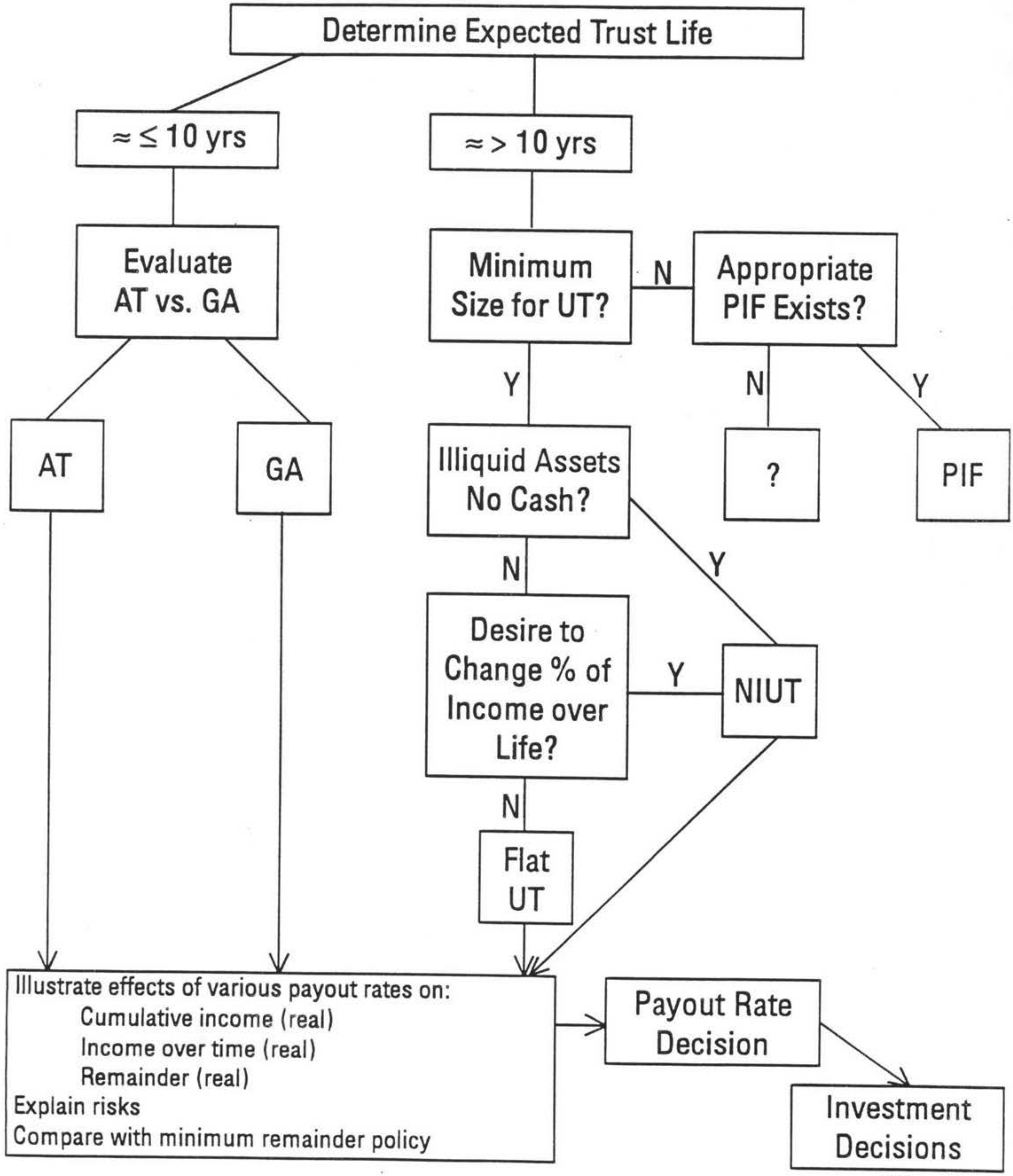
Portfolio Management

CHARITABLE TRUST DECISION TREE



Risks to Consider:

- Poor gift policies
- Poor choice of trust type or payout rate
- Poor investment approach / decisions
- Market volatility
- Changes in rate of inflation
- Changes in market yields (interest rates)

Trust Type	Typical Problems	Causes
Annuity Trust, Gift Annuity	Falling purchasing power of income	Fixed payment Trust life too long Inflation increases
	Trust assets depleted: Beneficiary loses income (AT) Charity must make up (GA)	Too high payout or too long life Costs too high Market losses grouped Poor investment decisions
Pooled Income Fund or Unitrust	Income erodes	Poor trust vehicle or payout choice Inflation rate rises Poor investment decisions
	Income falls Excessive income volatility	Market losses Poor investment decisions Market yields fall
	Remainder value erodes or falls	All of the above (except market yields fall)

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Portfolio Management

What Payout Rate?

Questions to Ask:
What is total benefit to donor/beneficiary?
How is income expected to change over time?
What is expected remainder value?

Trust Type	Payout Rate Affects:	Sensitivity to Payout Rate Decision
Annuity Trust or Gift Annuity	Total benefit, both cumulative and real (inflation-adjusted)	SENSITIVE: Total benefit to beneficiary is higher with higher payouts Charity's and donor's interests are divergent
	Change in real income over time	NOT SENSITIVE: Payment is fixed annuity Purchasing power erodes at rate of inflation
	Real remainder value	VERY SENSITIVE: Remainder value falls as payout rises *Important issues:* *Minimum gift policy* *Donative intent* *Investment approach*

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Portfolio Management

WHAT PAYOUT RATE? (CONT'D)

TRUST TYPE	PAYOUT RATE AFFECTS:	SENSITIVITY TO PAYOUT RATE DECISION
Pooled Income Fund or Unitrust	Total benefit, both cumulative and real (inflation-adjusted)	INSENSITIVE: 80s: Slight benefit with higher payout rate 70s: Negligible benefit with higher payout rate 60s: Reduced benefit with higher payout rate
	Change in real income over time	SENSITIVE: High payouts cause rapid erosion Mid-range payouts maintain real income Low payouts provide rising income *Effects greater for PIFs, NIUTs* *Effects increase as trust term increases* *Suggests disclosure*
	Real remainder value	VERY SENSITIVE: High payouts cause rapid erosion Mid-range payouts cause steady erosion Low payouts cause slow erosion *Effects greater for PIFs, NIUTs* *Effects increase as trust term increases* *Large opportunity cost for poor decisions* *Suggests minimum remainder policies*

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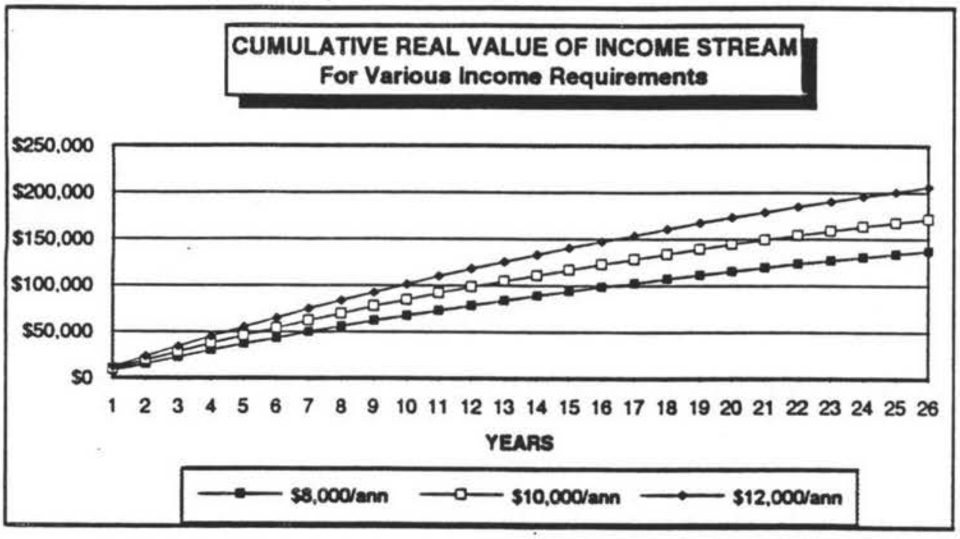
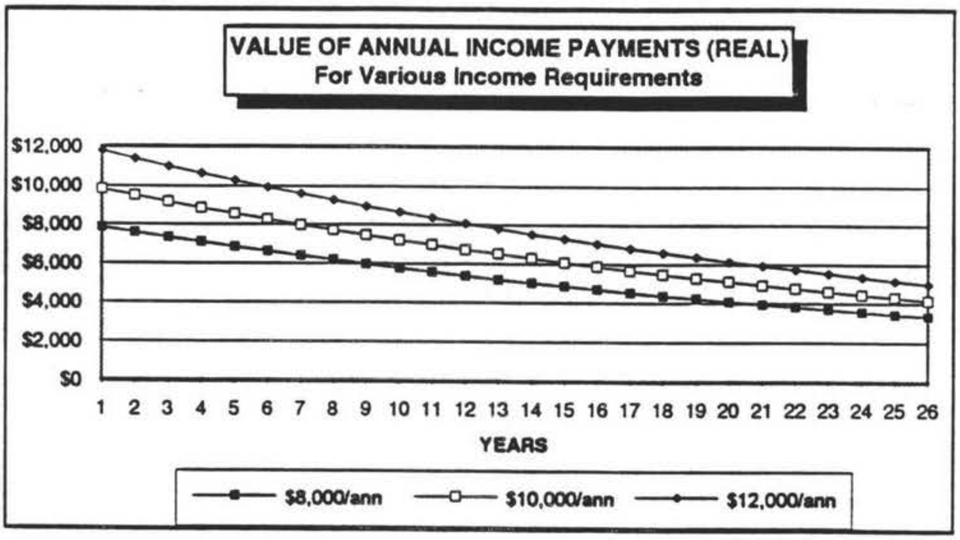
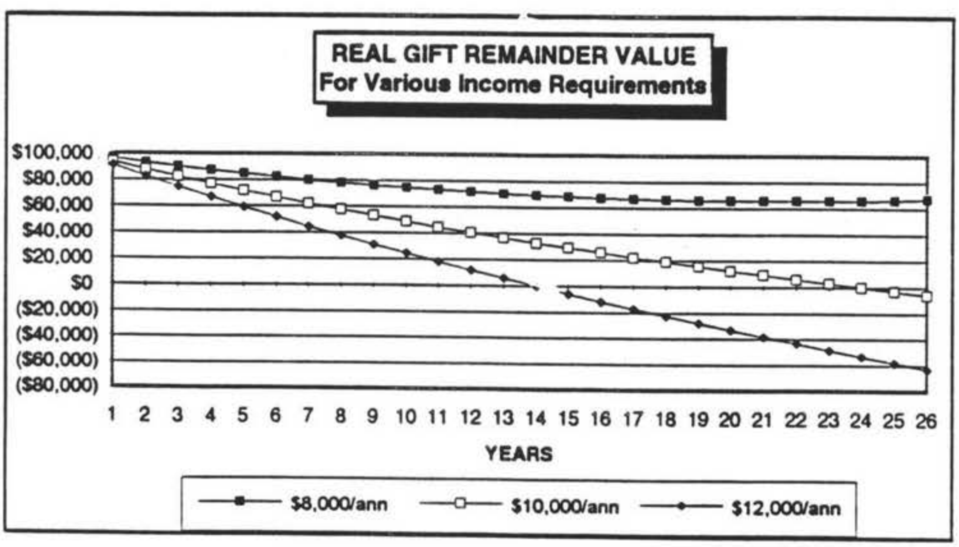
PORTFOLIO MANAGEMENT

Analysis of Typical Trust Flows

For High Payout Annuity Trust or Gift Annuity Pool



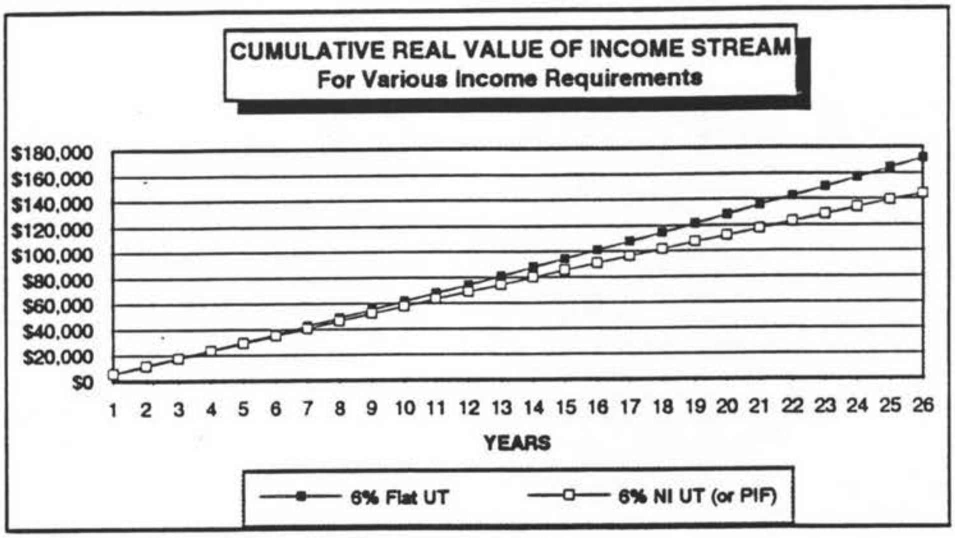


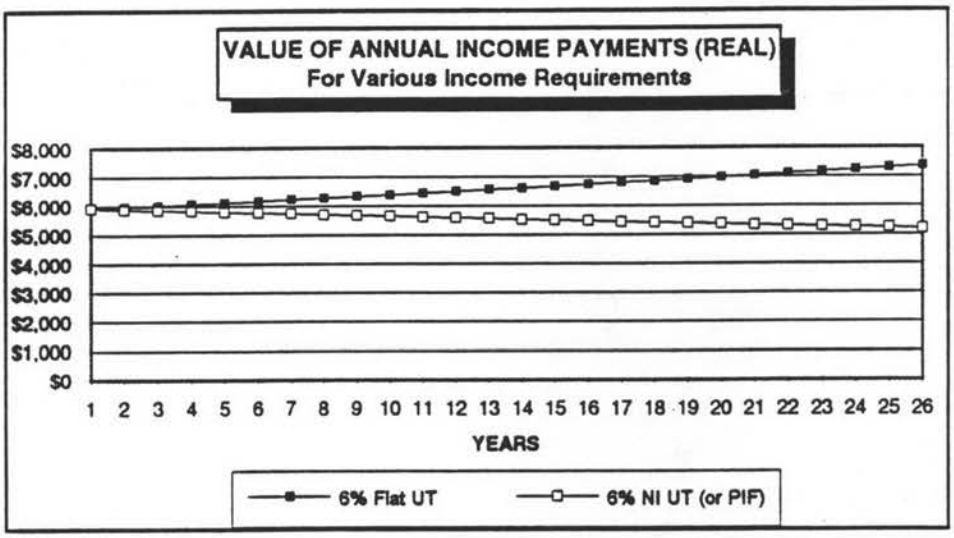


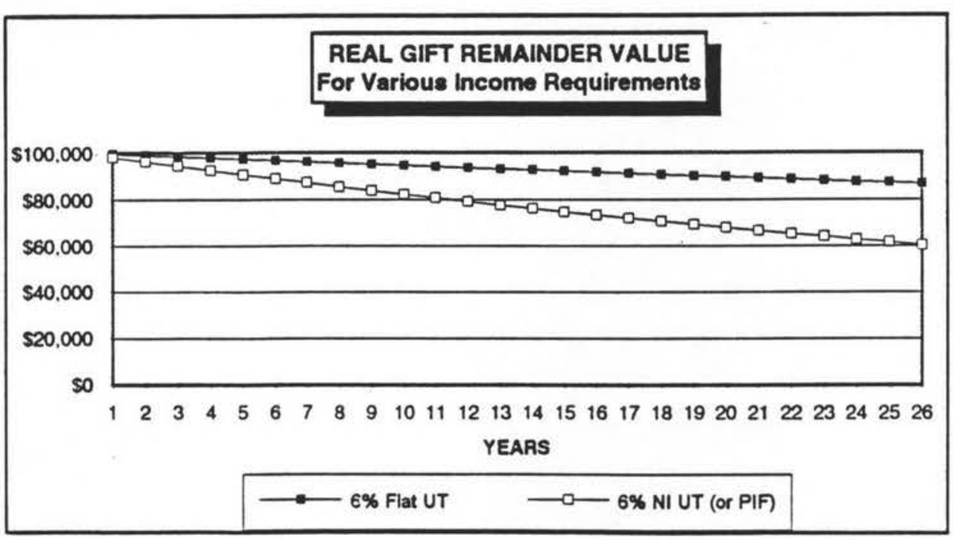
- Assumes $100,000 Annuity Trust or Gift Annuity Pool.
- Beneficiary flows discounted at an inflation rate of 3.5%; the charity flows are discounted at 5%.
- Total return assumptions are 9.40%, 8.64%, and 7.82%, respectively.

Analysis of Typical Trust Flows

For Flat Unitrust vs. Net Income Unitrust (or Pooled Income Fund)



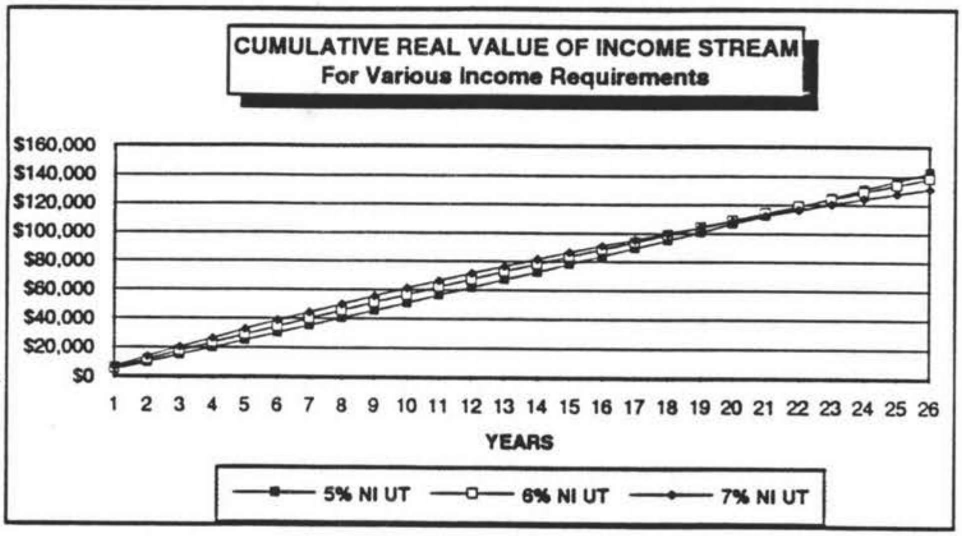


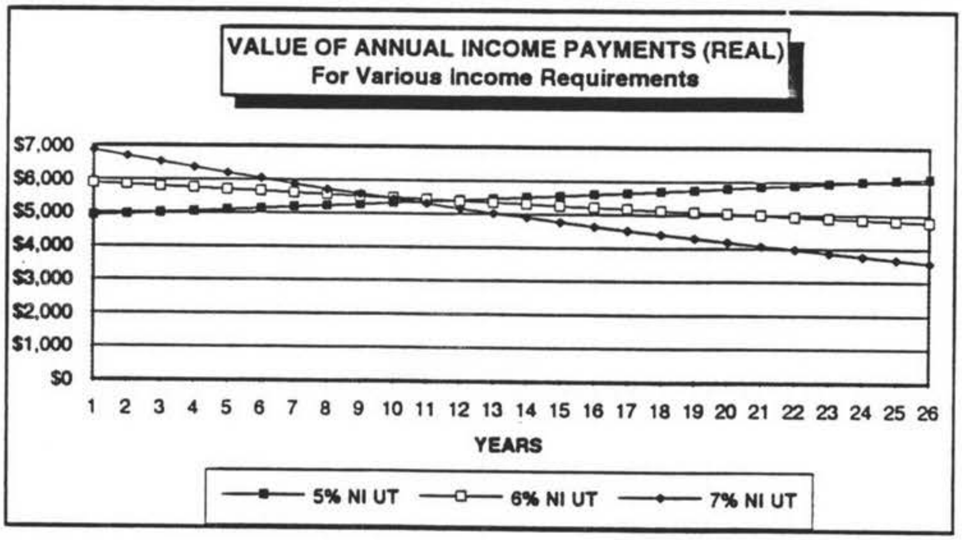


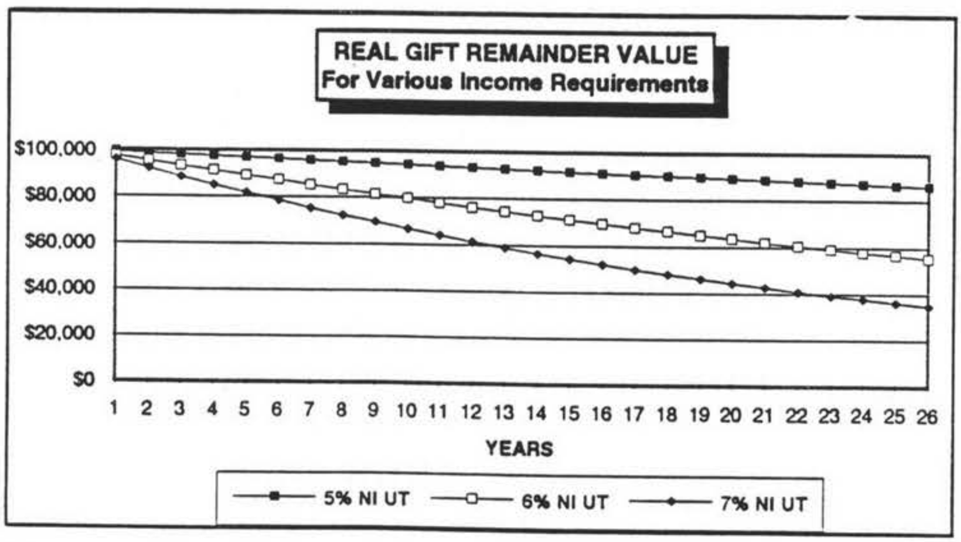
- Assumes $100,000 6% Flat Unitrust and 6% Net Income Unitrust (or Pooled Income Fund).
- Beneficiary flows discounted at inflation rate of 3.5%; the charity flows are at 5%.
- Total return assumptions are 10.43% and 8.98%.

Analysis of Typical Trust Flows

For Net Income Unitrust with Various Payout Rates



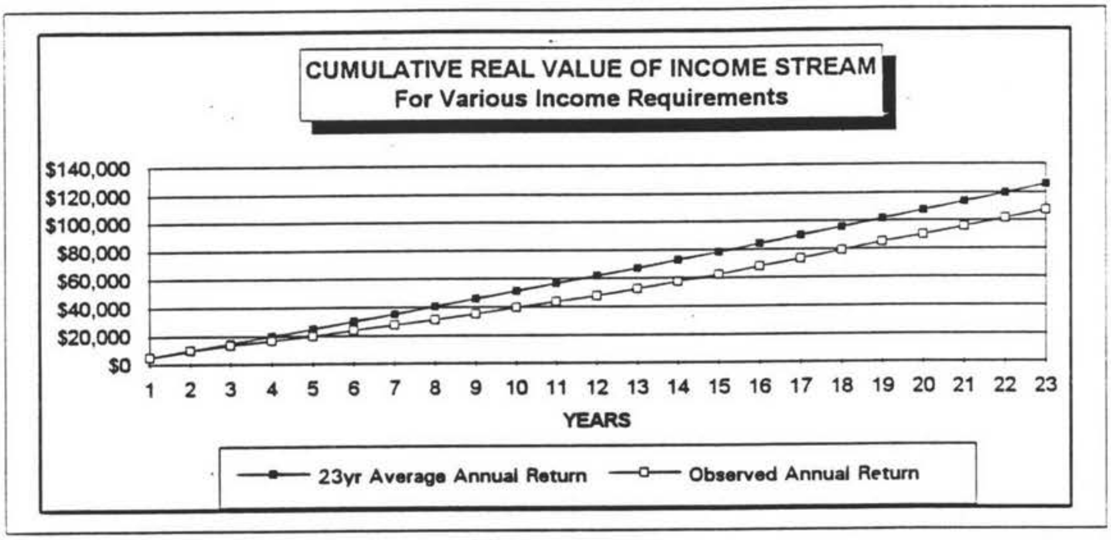


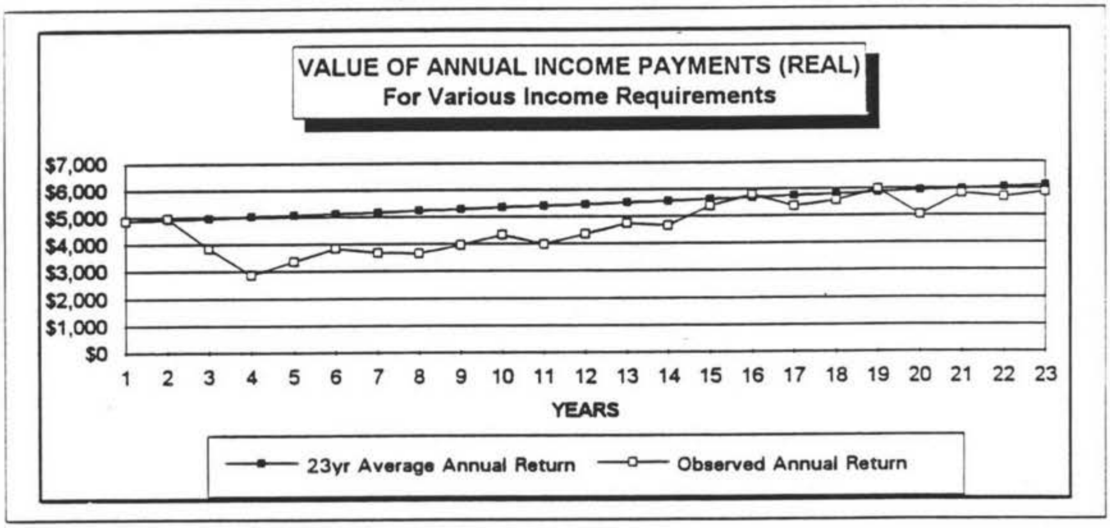


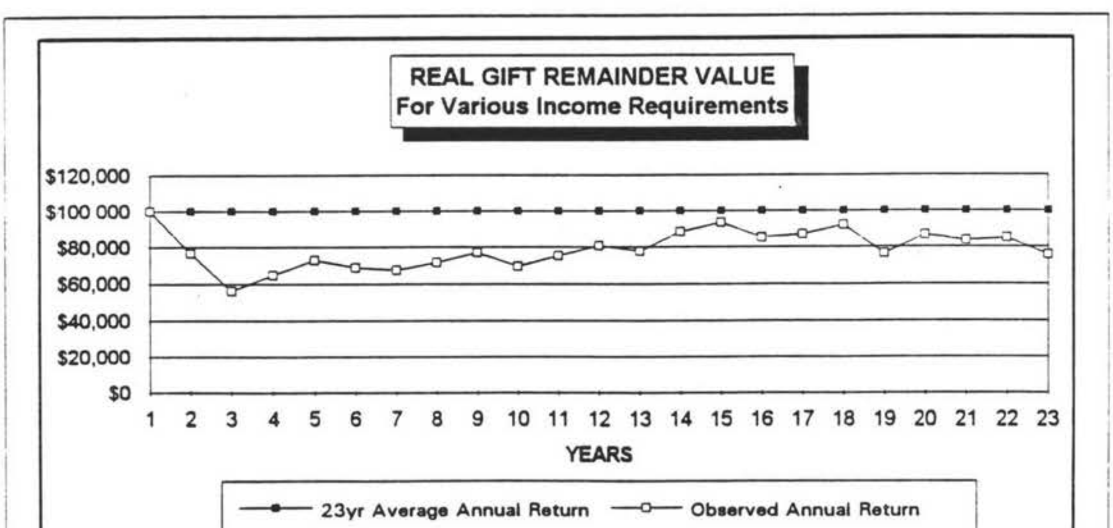
- Assumes $100,000 Net Income Unitrust with various payout rates.
- Beneficiary flows discounted at inflation rate of 3.5%; the charity flows are discounted at 5%.
- Total return assumptions are 9.40%, 8.64%, and 7.82%, respectively.

Illustration of Trust Portfolio Volatility

Average vs. Actual Returns (1972 - 1994)

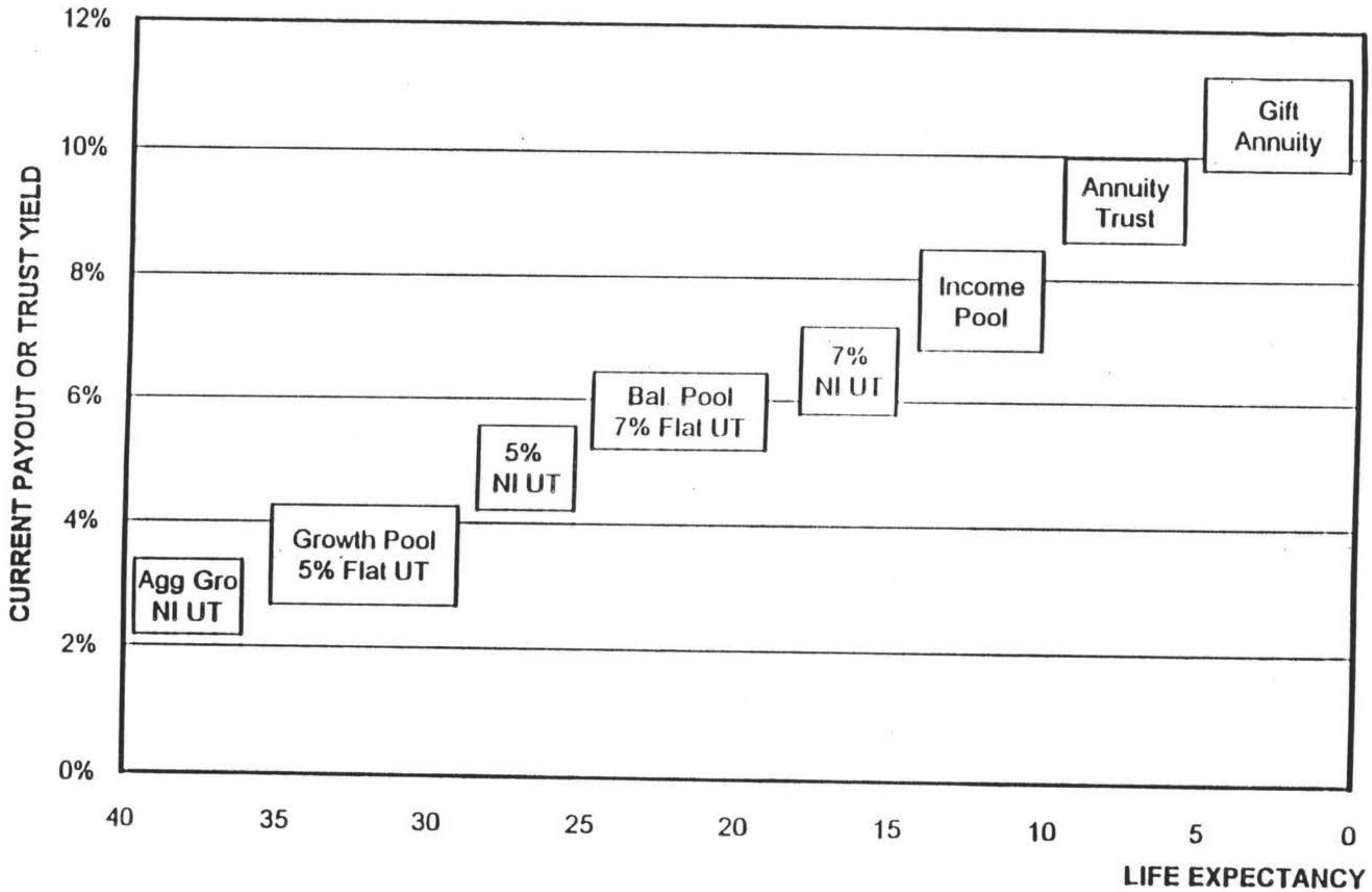






- Assumes $100,000 Flat Unitrust established January 1, 1972.
- Beneficiary flows discounted at inflation rate of 5.8%; the charity flows are discounted at 7.5%.
- Total return assumptions for this model are based on actual returns for various asset classes and our current long-run growth asset allocation back-tested over the 23 year period.

Charitable Trust Planning Matrix
Payout & Type vs. Life Expectancy



THE INVESTMENT OF GIFT ANNUITY FUNDS

Presented by Lindsay Lapole
The Salvation Army

I. INTRODUCTION

The investment of gift annuity reserves is a function of many factors. The purpose of this presentation is to identify those factors which have a significant impact on the investment process, and clarify the decision that must be made. We will also provide a basic framework for the selection and monitoring of investment consultants and their performance. Finally, we will provide an overview of investment vehicles and styles, that charities have available in the investment process.

Specific investments or investment styles will not be recommended. We will deal instead with the procedure of investing gift annuity assets. The information provided here must be reviewed by the charity's board of directors, legal counsel, and existing investment and financial advisors before any procedural or investment decisions are made. Every organization has different needs that affect their decision. They also must be mindful of the legal requirements of the state in which they are incorporated. Those areas that require specific decisions regarding these matters are presented below. A careful review of all these matters should be made before a charity proceeds with investing its segregated annuity reserve.

II. THE FUND TO BE INVESTED

The first factor that affects the investment of the segregated annuity reserve fund is the size of the corpus. The recent survey conducted by the American Council on Gift Annuities ("The Council") indicates that annuity reserves range in size from "24,999 and less" to "5,000,000 and more". A very different structure is required for the larger reserves than is required for the smaller ones. That is not to say that any less care and due diligence should be applied to the process for smaller funds. It is to say that the two extremes offer very different challenges.

Most knowledgeable investors agree that a small amount can cause even more challenges than a large amount when it comes to meeting long term investment objectives, controlling expenses, and providing diversification and protection against the impact of inflation. Therefore, the management of small annuity reserves requires special care and attention, just as the large reserves require.

The size of the fund is affected by the following factors:

1. Size and number of gifts generated.

2. Amount of each gift placed in the reserve.

3. Timing of withdrawals.

4. Age(s) of annuitant(s).

5. Effect of underlying interest assumptions in the:
   a. Calculation of the required residuum (reserve).
   b. Calculation of the terminated balance.

1. Size and Number of Gifts: The size and number of gifts your organization expects to receive on a regular basis has the most obvious impact on the investment structure needed by the organization. Over 76% of the charities reporting in the Council's survey indicated that total annuity gifts for calendar year 1993 was "$499,999 or less".

It should be obvious that the addition of one gift of $1,000 each year creates quite a different challenge for the investment manager than adding 200 individual gifts each year that may total $500,000. The simple solution for many is the use of mutual funds. However, the use of mutual funds requiring front-end loads can quickly diminish the value of the reserve position, and increase the administrative expense.

Without careful research, the fund could find itself with a 5%-6% loss in value before it makes the first payment to a beneficiary. Studies exist that would indicate that losses due to front-end loads are never recovered. It is important that independent research be done on behalf of the charity that will consider all the possible investment vehicles available for the size reserve fund being anticipated.

2. Amount of Each Gift Placed in the Fund: Over 85% of the charities responding to the survey conducted by the Council indicated that they place 100% of all gifts in their segregated annuity reserve. Another 6.5%, from "regulated states", reported they retained the "required reserve", and the other 7.9%, from "non-regulated" states, retained the "required" reserve even though they were not legally bound to do so. Therefore, all of the 737 charities responding retain either the "required" reserve, following the guidelines of regulated states, or 100% of the gift in the segregated annuity reserve. No charity reported retaining less than the "required" amount.

Actuarially, this assure the underlying health of the gift annuity program and increases the investment options available in the segregated annuity reserve. By retaining as much of the gift as possible in the reserve position, the charity is assuring both itself and its annuitants that the program is secure. It also provides the fund managers with maximum flexibility in producing positive investment results.

3. Timing of the Withdrawals: The timing of the withdrawals from the fund will have a significant impact on the investment of the reserve. We are aware that the income tax charitable contribution deduction is higher in those annuities that pay at the end of the annuity period instead of the beginning. The calculation assumes that the loss of use of the funds, by the income beneficiary, results in an overall reduction of "retained life interest". Because the beneficiary receives less benefit, the charity receives more, thus the higher deduction. Likewise, in the investment of the reserve fund, the timing of withdrawals from the fund will have a significant impact on its long-term performance and health. Removing money on a monthly or quarterly basis to make income payments will diminish the types of investment instruments that are available, and may adversely impact the charities ability to diversify the fund. Some charities are able to make all annuity income payments from their operating budget. A "required residuum" calculation is made annually with a reimbursement to the operating account for the income payments, and the annuity fund is balanced to the desired reserve position.

4. Age(s) of Annuitants: The age and number of annuitants impacts the segregated annuity from its very first day to the day the terminated balance is calculated. Every calculation related to the reserve includes the age(s) of the annuitant(s). Age is used as a primary factor in establishing the Annuity Rate. The level of the rate determines the rate of withdrawals from the fund, and establishes a level of investment performance that is required.

The impact of age will also be seen in the discussion of the calculation of the "required residuum". Each time the calculation is done, the age is used to recalculate the new life expectancy and thus the remaining annuity value. This individual calculation for each annuity becomes the aggregate calculation that establishes the residuum required. To state it clearly, the residuum calculation answers the question, "How much money must be invested at the assumed earning rate to assure the annuity payments to the charities' annuitants at their present ages?"

The lifetime of the annuitant, expressed in the form of the number of annuity payments actually paid, is the basis of the calculation of the terminated balance (that portion of the initial gift that is usable by the charity at the termination of the annuity payments). The annuity rates recommended by "the Council" in 1992 were based on the assumptions that they would provide a 50% remainder gift to the charity at termination if all funds were invested at a 6.5% earnings rate.

Subsequent economic factors made the 6.5% earnings assumption problematic, and thus the Council lowered its annuity rate recommendations effective January 1, 1994. Age is the one constant in the whole process. Once that factor is established as the known, all the other factors can be modified to meet the changing economic climate, Internal Revenue Regulations, State reserve requirements, and the needs of the charities to benefit from these gifts.

5. Effect of Underlying Interest Assumptions: Actuarial formulas are used in the calculation of the "required residuum" and the "terminated balance". Each of these calculations impacts the size of the reserve fund, and therefore the investment strategy and performance. Each formula requires the insertion of an assumed interest rate on the reserve fund in order to make the needed calculation.

In "regulated states", the regulating state agency may establish guidelines for the assumed rate of return. In "unregulated states" it will be up to the charity to determine what assumed rate it will use in making these calculations. We have previously states that in 1992 the Council used 6.5% in the recommendation of annuity rates. It is important that the assumed rate used in the calculations have some basis in reality. It is also helpful to have the assumptions tested by independent auditors at the time of the charities' outside audit.

Mr. Michael Mudry, Senior Vice President of Hay/Huggins Company, Incorporated, was our source for the formula and the explanation of its operation. There are some other actuarial firms that exist, however, who could also be of assistance in this matter.

III. ESTABLISH A WRITTEN STATEMENT OF INVESTMENT GUIDELINES

Write it Down: The establishment of written investment policies is essential to any fiduciary responsibility. It serves to protect and guide the charity, the investment staff and managers, and the income beneficiaries. It provides an established reference point to which all interested parties can return for information and correction.

Information to be Included: In the atmosphere in which we all function, charities must establish a written investment policy statement that would include the following:

1. Background information identifying the source of the funds and fiduciaries involved.

2. Organizational structure to identify line of authority in the investment decision making process.

3. Cash flow requirements on the funds.

4. Diversification requirements.

5. Performance objectives and guidelines.

6. The voting of proxies, trusteeships, and custodianships.

7. Guidelines stating when review meetings will take place, and how the minutes will be documented, reviewed, and approved.

8. Criteria for how performance will be reviewed.

Background Information: One of your internal procedures will be to require the maintenance of background information identifying the source of funds, and any fiduciary relationships that existed with those funds at the time they were transferred. This will assure that you are accepting moneys from a donor who has the legal right to make that transfer, and that claims against the charity, or its funds, will not be made by others who claim to have had control of property at the time the transfer was made. This is particularly important in transfers of jointly owned or community property, and in property being transferred from a trust.

Organizational Structure: Clear lines of authority and organizational structure must be established regarding the investment decision making process. Identify who will have the authority to make decision on a day-to-day basis, and the relationship between the internal financial officer, board of directors, and the investment manager. This includes a clear delineation of who has the authority to order the purchase and sale of assets, and whose signature must accompany those documents. The organization must protect itself by clearly delineating, for its own purposes, who within the organization has the authority and responsibility for the day-to-day decision making process, as well as the oversight supervisory responsibility.

Cashflow Requirements: The establishment of cash flow requirements will have an impact on the type of investments that can be made. If cash flow requirements are going to be on a fairly regular and short-term basis, then a significant part of the fund may have to be maintained in fixed-income investments. Should it be possible for those cash flow requirements to be spread over a broader time frequency, then fixed-income and equity investments can be balanced in a more traditional manager to give the opportunity for growth in the fund as well as income generation.

Diversification Requirements: "Diversification is the spreading of assets among a variety of securities, or among securities in a variety of markets, with a goal of reducing risks in the portfolio without reducing expecting return." IT should be noted that there are two major factors involved in diversification. The first is the reduction of risk in the portfolio, and the second is not reducing the expected return. [1] From the standpoint of unsystematic risk (that is risk that is not related to the overall market), it is diversified away after a fund has invested in approximately 20 positions within the market. Beyond that, unsystematic risk is not materially affected by extending the portfolio further.

The written investment policy statement generally would indicate those broad areas of investment vehicles in which the charity feels comfortable in investing: bonds, stocks, cash, commodities, real estate, and collectibles. In gift annuity reserves, we would not invest in commodities or collectibles simply because of their highly specialized and unique nature. The charity will also want to consider the appropriateness of investing segregated gift annuity reserves in real estate and other hard to value, or difficult to sell, assets in view of the long term requirements, and investment objectives of the reserve fund.

Diversification is a very full and comprehensive discussion. Two resources that the writer has used are "Managing Your Investment Manager" by Arthur Williams, III, published by Business One Irwin, and "Investments An Introduction" by Herbert B. Mayo, published by The Dryden Press, Harcourt Brace College Publishers.

Performance Objectives and Guidelines: The investment policy statement should outline those standards against which the performance of the fund will be judged. Generally, those will fall into one of four categories:

1. Comparison to an absolute goal.

2. Comparison to a recognized market index.

3. Comparison with other similar portfolios.

4. Comparison with a customary or "normal" portfolio.[2]

The most important factor in establishing performance objectives is that the objective must be realistic for the fund and the restrictions that have been placed upon it. It must also be subject to review and evaluation periodically to assure that the selected standard has not changed in some material way as to make it ineffective as a measuring tool.

The Voting of Proxies, Trusteeships, and Custodianships: Voting rights on those matters related to the underlying investments in the portfolio must be assigned to some individual, either the investment manager or the chief financial officer of the charitable organization.

Quality Guidelines: It may be that the charity will feel a need to limit the quality of investments to a certain predetermined level or to eliminated certain assets from the portfolio for various reasons. Notable reasons for elimination of specific assets would be "moral grounds" (i.e. tobacco, gambling, certain entertainment, publishing business), environmental concerns or limiting "foreign" investment. This matter can become very sensitive in an economic climate where many businesses are broadly diversified in their holdings. The charity will want to be very specific in the percentages of holdings that trigger the elimination of that asset as suitable for the charity.

One of the benefits of individual fund managers over the use of mutual funds is that the charity has much more control over this matter of quality control and limitation on the specific assets. The mutual funds busy assets that are most appropriate to establish a performance record, regardless of any other limitations placed on it by the various owners of that fund. A number of socially responsible mutual funds have developed over the last several years that charities may want to consider in the placing of there assets for investment.

Guidelines for Review Meetings: The policy statement should also establish a pattern of regular review meetings with provisions for minutes and documentation to be maintained, and an appropriate review of those minutes, and permanent filing. The review meeting should include a review of the performance of the annuity reserve fund, its performance against the pre-established criteria, any particular challenges that have arise since the previous review meeting, and recommendations by the investment consultant on how those challenges may be corrected.

IV. THE SELECTION OF AN INVESTMENT MANAGER

Management options: The size of the fund will determine the need for a particular type of investment management. Basic options would be the following:

1. The use of individual securities selected by a responsible person with the organization.

2. The use of mutual funds selected either by internal staff, or an external investment consultant.

3. The use of an investment consultant, and a combination of no-load mutual funds and individual fund managers.

The one recommendation in this presentation is that any charity holding invested funds needs a qualified investment consultant advising them on the management of those funds. The investment consultant should be offering their services on a fee-based arrangement. No charity should undertake a relationship that would be based on commissions or individual transaction fees. Any reputable investment consultant will be willing to provide their services on a totally fee-based arrangement.

It cannot be too strongly stated that whether your charity is holding $25,000 or $25,000,000 in reserve, you must exercise the same level of due diligence and accountability, and must be prepared to defend your investment decisions through a well established track of documentation and regular reporting.

<u>Criteria for selection:</u> Just as the prudent organization is submitting itself to outside audit, and has outside general counsel, the prudent organization will also have outside investment consultation in determining how to invest its own reserve assets as well as those moneys that are committed to providing life income to its beneficiaries. The criteria for selecting an investment consultant should include the following:

1. Professional credentials, training and experience.

2. Be well enough established that they are not going to go without a meal if they don't get your business.

3. Their willingness to become involved in understanding your organization and how it works administratively, politically, and mechanically.

4. Their willingness to accept the nuances of your organization's administrative structure.

5. The amount of information that they ask you for before making presentation to you.

6. Their willingness to continue to service your needs in a way that will make your overall organization more efficient and enhance your ability to provide better service to your beneficiaries.

<u>Professional credentials:</u> In seeking an investment consultant, you should begin with those individuals who have a proven track record and credentials in their own profession. They should be recognized by their professional peers as being competent, and recognized by the organization with who they work as one of the top level representatives of that company.

A part of the investment policy statement should direct that they person is recognized as a professional in their field of investment management. It is essential that the investment consultant be independent so as to make appropriate professional recommendations to the charity, and must not have other ties or connections with charity that would in any way influence those recommendations.

<u>Well established:</u> Your search should eliminate any aunts, uncles, cousins, nieces, nephews, brothers, sisters, and grandchildren of the key decision makers within your charitable organization. They should not present themselves as going to go hungry if they don't get your business. Be reluctant to consider those individuals who are making a presentation to your charity for the investment of your reserve funds, and this is the "second call" that they have made in their new career as a broker. Look for the well established advisor with experience and credibility. You may want this person to meet your donors. They should add credibility to your organization, not detract from it. An instantaneous clue would be that the prospective consultant arrives at the interview with their sales manager who does most of the talking. The investment of a segregated gift annuity account is not a good "new business account" for a beginning investment advisor.

<u>Their willingness to Become Involved:</u> Every organization has its own unique administrative style and structure. In addition to the structure as laid out on the organizational charity, it also has its own political and mechanical structure- those methods and mechanisms for making the organization move forward. The investment consultant, to be effective, must become familiar with the operations at all levels

of the organization, and determine the time frames necessary for decisions to be made and implemented. Much of this learning will take place before any funds are transferred to the investment manager so that both they, and the organization, have absolute confidence in the administrative operation of the system before any money is committed.

Willingness to work with the administrative nuances: Not only does the investment consultant need to understand the administration, but there must be a willingness to accept, and work within those nuances. If you have placed "moral" restrictions on investments, the investment consultant must be willing to accept those, and serve as the watchdog of your desires whether they agree with them or not. This is not to say that they don't have input on suggested modifications of administrative practices or the investment policy statement. It is to say that once a decision is made, the investment consultant becomes a gatekeeper on behalf of the charity to assure that all money managers within the structure adhere to those policies. Any deviation from that should be immediately reported by the investment consultant to the charity for appropriate action by the decision making group. Failure to do so should result in an immediate review of the investment consultant's relationship to the charity.

Information Requested: The successful investment consultant will spend a great deal of time collecting information from the charity before making any recommendations. This would include how you have been doing business and investing the funds historically, and discussions with the key business and decision making officers of the organization as well as the people who get the work done on a day-to-day basis. It would include a careful review of financial productivity, asset allocation, and historical performance. The wise investment consultant will then come with a presentation that fits your organization based on this exhaustive study.

The selection of an investment consultant should be made from a presentation that recognizes the administrative style and structure of your organization, consideration of its written investment policy statement, and an understanding of how well and completely that statement has been carried out in the past. It should include a thorough knowledge of the decision makers, and how they feel about the decision to be made.

Willingness to Continue to Service: Your investment should be continually (i.e. daily or weekly) suggesting ways in which they can improve their service to you and your income beneficiaries. This may be through suggestions for restructuring administrative procedures, streamlining where possible in the decision making process, providing you with a broader variety of investment products, arranging for direct computer access to your accounts, or whatever else may be appropriate to continue as an investment consultant with your organization. They should expect to continue that relationship with a significant amount of time and energy in caring for the charities' needs.

"Our Experience": As we went through this process recently with regard to our charitable trusts, we worked for almost four years developing and refining a structure that we though would work. One individual, through patience and endurance, worked with us every step of the way to help deal with those decision of procedure that needed to be dealt with in a major transfer of over 17 million dollars.

When it was time for the decision to be made, we requested proposals from five major brokerage firms under a "request for proposal" letter that outlined exactly what our requirements, limitations, and objectives were. A committee made up of the chief financial officer, the head of the department that would be administering the funds, and the key administrative personnel was formally appointed by the Board of Trustees to pursue the selection process. Each of the five firms was invited to make a formal presentation. Follow-up presentations were made personally by each of those firms as well.

In total, there were 14 formal interview periods lasting from two and a half to three hours each during a three month period of time in which a proposal, that had been developed over three years was reviewed with these companies and their staff. The story of those presentations was very interesting and revealing. We had the brokerage firm who we had been with for years answer our concerns with the basic response that we would stay with them because they are "the biggest and the best". We had the brand new broker, who only a year before had been dancing with the Cincinnati Ballet who came with her sales manager, and we had the companies who would place us in a prepackaged program based on no contact with use except the content of our letter to them with our request for a proposal. Needless to say, the process was exhaustive, but the outcome was predictable.

V. REVIEW OF INVESTMENT POSSIBILITIES

Investment Types: People can put their money in many different "investments"- antique automobiles, oil paintings, rare coins- but most of us do not have sufficient information to make any sizable investments in anything but stocks, bonds, or cash. In general, the following categories of investment are available:

1. *These investments are any debt vehicle (bond) in which a corporation or government borrows money for a predetermined period of time.* Remember the fair market value of bonds fluctuates while the income stream remains constant. We've just been through the worst bond market since 1927. The price of bonds moves in the opposite direction of the interest rates. When the Federal Reserve increased rates, the prices of bonds went down. However, bonds are still our most reliable source for fixed income. U.S. Government bonds are all AAA since they are backed by the full faith and credit of our government. Corporate bonds, however, are of lower quality, some even default. Generally, we use only A or better quality bonds.

2. *Equity investments:* Equities are shares of stock in corporations which reflect direct ownership, and your investment value will fluctuate in direct proportion to the success or failure of the company that you own. The objective is to own shares of stock in companies that appreciate in value, thus providing growth of your account in keeping with the overall economy. Stocks have outperformed bonds in every ten year period, and most always outperform inflation. Risk is reduced with diversification and the longevity of the portfolio.

3. *Commodities:* Commodities are the raw materials of manufacture and production. While these investments may not be appropriate for our purposes, commodities are very important to the stability of our basic food sources. If you required soybeans in the manufacture of your product, you certainly couldn't wait until the harvest came before you decided how you would price the product.

   It would be very helpful if you could buy soybeans for future delivery when you need them at your plant. If you could find a farmer who was willing to sell you his beans even though they had not been planted, and you agreed on a price, then you both have a successful transaction. The commodities markets includes everything from gold to chickens. Lambs, soy bean oil, tin, hogs, and cattle are among the diversified products available for trading. The "future markets" can include investments, S&P indexes, and various derivatives.

4. *Real Estate:* Real estate has been an attractive investment for a number of years as many of use have experienced from our individual home ownership. But, let us remember that the appreciated value is not a matter of having a unique piece of property, but more likely the result of inflation. As inflation is kept under control and it becomes easier and faster to build house in a more cost effective manner, real estate may not hold the attraction that it has over the past few years. We must consider the implications of real estate as an appropriate investment as a part of the gift annuity reserve. Generally, you will want to be cautious with depreciating and non-income producing assets in this fund.

5. *Cash:* Cash, of course, is sometimes better than any of the above. During times of market fluctuation and uncertainty, many money managers maintain cash as a significant proportion

of their portfolios. This allows them to adjust asset allocations without having to sell other desirable invested positions to create cash.

Investments Objectives and Types of Accounts:

1. *Fixed income accounts:* Fixed income accounts are primarily invested in bonds of various maturities, rates, and credit worthiness. Most Investment Policy Statements require an "A" or better rating for their bond investments and all United States Government bonds are "AAA". Most bond portfolios are structured so that they have staggered maturities (i.e. one, three, five and seven year maturities, etc.). This allows the manager to achieve some stability within the account and generate the required income.

2. Equity accounts: Equity accounts come in two forms. One form is the growth account, wherein the manager is primarily targeting an increase in the value of the account without income being a major consideration. Income accounts are more generally emphasizing conservation of principal with, stable but growing dividend income. Capital appreciation is not the major consideration in this style account and they are sometimes referred to as "income with growth" accounts.

3. Balanced accounts: Balanced accounts are structured using asset allocation techniques with a mixture of stocks and bonds to achieve the desired performance while lowering the risk. This will be discussed more later because there are many ways we can use a balanced account to meet the requirements of the gift annuity reserve.

Advantages of Balanced Accounts for Gift Annuity Reserves: Our main objective in the gift annuity reserve is to meet the income requirements to the annuitants and to preserve the remainder value for future use by the charity. Asset allocation is 90% of the reason for the performance of an account.

Therefore, when you have a balanced account and allow the manager the flexibility to change the ratios and the weighing between fixed income and equity investments, you are participating in asset allocation. This allows for participation in two major segments of the economy and maximizes the opportunity for success.

Stocks outperform bonds on 10 year rolling average in every case we find. However, there are cases in individual years when stocks do not outperform bonds. There may also be particular reasons at any given time when the asset allocation may need to be adjusted. Therefore, the opportunity to fine tune the investment portfolio for growth, income, risk tolerance and quality increases significantly as the size of the reserve account increases. One of the major points of impact on smaller reserve accounts is the inability to participate in the asset allocating process.

Importance of Manager Style: Investment managers subscribe to different theories of investing. There are many different financial management styles but the largest groupings are growth and value.

1. *Value style:* A value style is endorsed by a manager who is looking for value in the stock market. A company that is going to earn $10 a share normally sells for ten times the earnings, for $100. If it is currently selling at $90, it would be considered a value. Currently, Bethlehem steel is a good example of value stock. A growing economy is generally good for value style investing. Earnings are increased, and investors are looking for a "value".

2. *Growth style:* On the other side of the equation, you have a growth style investor. This manager feels that the best bargains in the market place are those companies who have the ability to grow their earnings. The growth investor is willing to pay a premium for a company whose earnings are growing at an above market rate. A current example would

be WalMart. When the people who buy stock for $90 find that the earnings are going to $8, instead of anticipated $10, they become disenchanted and look for companies whose earnings may not be as attractive on a ratio basis, but whose earnings nonetheless are growing. At that point, they move from the value style to the growth style. When the economy begins to slow and earning deteriorate, investors often turn their attention to those companies still managing an increase in revenues and earnings.

We note that historically the two styles, growth and value, swing like a pendulum over the years. For this reason, the charities' trustees/directors, charged with looking for stable growth in their gift annuity reserve, would select a combination of growth and value managers rather than ride the ups and downs of the changes in personality of the market.

Monitoring Performance: The most important aspect of investment management consulting is the monitoring process. With all due respect to the time we spend in formulating an investment policy and in searching for the proper manager to best work within the constraints of that investment policy, the monitoring process is the most important step in the entire process. Without monitoring there is no accountability and no meaningful way to determine compliance with the goals and objectives of the fund.

Determine a Benchmark Index: Determine a benchmark index that is readily available and best expresses the intent of the policy statement. If the index is to strictly conform to the market in general, the S&P 500 would be a proper selection. Should the goal be to have a balanced fund, then a 60/40 index (60% in the S&P 500, and 40% in the Lehman Brothers Government Corporate Index) would be selected. An appropriate index can either be identified or blended from several indexes that will very closely resemble the intent of the portfolio.

Risk Management: Another important function of the monitoring process is measuring the risk and volatility of the portfolio. The most common measure of volatility is standard deviation, the amount by which a given portfolio deviates from the index on a month-by-month or year-by-year basis. An elaborate mathematical formula is used to measure this force. The investment consultant will provide regular interpretations of the standard deviation of the portfolio.

Another monitoring function is determining the beta of the stock or portfolio, that is an average of all the stocks in the portfolio. And how does the individual issue compare to the performance of the market as a whole? That is, when the market moves 10%, does this issue move 15% (or a beta of 1.5)? A beta of 1.0 is equivalent to the market.

Alpha measures the amount of reward that is earned for the risk that is taken. An alpha of zero indicates that the risk versus the reward is that of the market itself. A positive alpha shows the portfolio has achieved higher returns for the risk level assumed, while a negative alpha means a lower return for the additional risk taken. The object of the investment consultant is to assist the charity in "keeping your betas low and your alphas high".

Reward Management: It is also important to measure the reward in keeping with the amount of risk that is taken by evaluating total return. When it is said that a portfolio has moved 10% in one direction or the other, it refers to a composite change in fair market value and earned income (total return).

An increase of 10% in total return may have come from a 5% increase in dividends and 5% from growth of the portfolio through appreciation in principal value. In the bond market, a bond that yields 8%, may fall in value by 10% in the year. Your total return would be a negative 2%. The value of the portfolio declines 10% while continuing to provide an income above 8%. That is total return.

To determine the value the manager is adding to our account, we use the Treynor Ratio. This ration measures the performance of the portfolio given the level of systematic risk that is taken. Systematic risk refers to those factors that are intrinsic to the nature of the economic market. When moneis invested in the stock market, it is subjected to risk. The monitoring process determines how much return was received for the amount of risk exposure encountered.

The Sharpe Ratio measures the portfolio as it is, minus a return on the risk free investments (t-bills) and divides it by standard deviation. It tells the charity how much additional risk they are taking in order to experience a given return.

Comparison with Peer Group Managers: Most investment committees are interested in how their managers do versus other managers in their peer group. By compiling, on a quarterly basis, the performance data from over 1,1100 investment managers, this comparison can be provided. There are 18,000 registered investment advisors in the United States. Of those, only about 1,500 are considered institutional quality, that is, those portfolio management companies (investment counselors) who do some outside research. Various software programs are available that allow investment consultants to monitor performance on 1,100 managers. It also allows the consultant to group these managers among their peers by investment style (i.e. value style, growth style, small capital, mid-cap, etc.)

Within six weeks of the end of the quarter, the performance of your manager can be compared to other managers in his peer group. This allows the investment committee and investment consultant to evaluated a comprehensive performance comparison and make appropriate adjustments in investment direction.

Blending Manager Styles for Best Results: The blending of a growth manager with a value manager will usually achieve the best long term results for the investment of most gift annuity reserves. In our quest for stable growth portfolios, it is sometimes advisable to add an international sector to the blend. By having thirty percent of the portfolio invested with an international manager, the stability of the account can be increased and the total return can be enhanced.

What Can We Expect?: The economist Harry S. Dent, Jr. in his book, "The Great Boom Ahead", suggests that the economy rises with the increase of buyers and falls with the decrease in buyers. And that just makes good sense. Mr. Dent's team did the research that tracked the buying habits of different age groups.

Their research shows that the baby boom began right after World War II and continued through the Korean War. By looking at the fifteen year period from 1946 through 1961, they tracked that group of babies until they became 43 years old. At that age they buy their largest house and when they become 49, they peak in spending. The S&P tracks very closely the number of 49 year olds in the country. So 49 plus 1946 equals 1995, the beginning of the greatest boom in 49 year olds that we have ever known. That will impact our economy, the market and, most assuredly, impact charitable giving. It is important that charities prepare themselves to meet the opportunities and challenges that lie ahead.

Conclusion: In the present legal, regulatory and economic climate, it is essential that charities maintain the highest possible standards of fiduciary responsibility. Charities no longer hold a special place of honor that exempts us from scrutiny by regulators, long-lost relatives, and their legal counsel. Unfortunately, some charities have contributed to the problem by their business and financial practices. We can no longer operate as "mom and pop" operations where financial decision are made by family, friends and self-proclaimed development experts.

The investment of the gift annuity reserve, and all the other assets of the charity, must follow well established guidelines. Specific goals and objectives must be established for each fund. Regular monitoring of fund performance should take place and written records and documentation of the process should become a part of the permanent records of the charity. The monitoring should measure performance against both the charities' state goals and objectives and well as industry recognized indices.

These steps can greatly enhance the opportunity for success in the investment of the gift annuity reserve fund. It will also place the charity on a firm fiduciary foundation should questions ever arise.

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Other Helpful Reading

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MANAGEMENT OF REAL ESTATE GIFTS

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Management of Real Estate Gifts

Never ask of money spent
Where the spender thinks it went
Nobody was ever meant
To remember or invent
What he did with every cent

—Robert Frost

I. Real estate transfers are by far the most complex of assets to receive as a contribution, whether the gift is made outright or in trust.

A. Scope of this outline and talk

1. The topic of how to manage real estate gifts is as large as the field of real estate itself. Any type of real estate that one can conceive of has been offered to and accepted by charities in their planned giving programs.

2. Because of the immense breadth of this topic, it is probably best in the short time available to help the participant or the reader to see the extent of the topic, as opposed to delving into one or a few minor points at length.

3. Nevertheless, once the manager of a real estate program knows the panoramic landscape this field offers, he or she will quickly learn that almost every point in this outline is a gray area. This means that every single point needs further study, analysis and conquering if you are to manage a real estate program well. *This is a daunting task. If you have no heart to learn volumes of information, you and your organization will pay the price in spades.*

B. My goal in this presentation and outline will therefore be to offer an analytical framework for you which will then serve first as your basis for creating the appropriate checklists and second as a reference for management policies and guidelines.

C. As a digression, there is a vast difference between policies and guidelines.

1. Policies are things that ought to be set or at least agreed to by your board. They are designed to limit the exposure of the entity as well as the individual board members. (See my pamphlet entitled, *What's Your Role In Planned Giving As A Board Member?)* Your board is after all the policy-making body for the entity.

2. Guidelines are rules that the entity and its staff and volunteers should abide by. They are sort of your bylaws of operating. They are not law; they can be bent in certain cases. They are there to give guidance and uniformity in gift giving situations.

II. **Intake** of real estate gifts

A. How can we break down the types of real estate gifts that are taken in by charities? Should we do that by type of real estate or by vehicle in which it is received, or both?

1. If your response is both, how can you acquire, organize and maintain the information you will need?

2. You must understand that there are various "vehicles" in planned giving and that real estate is not one of them. There are only three types of vehicles in planned giving: wills, contracts (including deeds and annuity contracts) and trusts.

3. On the other hand, there are a zillion types of assets that can be given. Well, perhaps not that many, but whatever a person owns, a person has considered getting rid of — including by way of gift. Real estate is an asset, not a gift vehicle.

4. As to the intake of real estate, let's try to break down the issues by the nature of the vehicle in which the gift arrives. Legal rules will vary according to the nature of the vehicle. Your intake procedures, therefore, will also vary with the nature of the vehicle that delivers it to you.

B. Intake chart of planned gifts of real estate

1. Outright gifts (by deed, i.e., by contract)

   a. Fee interest in 100%

   b. Fee interest in less than 100%

      (1) Undivided interest

      (2) Partial interest, but not an undivided interest in each and every ownership right in the property.

   c. Non-fee interest, such as a leasehold interest

      (1) Effect of state law on the determination of whether this is an item of property.

      (2) Specialty laws such as in Louisiana and Hawaii

   d. Bargain sales

      (1) Lump sum payment of less than fair market value

      (2) Installment bargain sale

         -Deferred payment contract terms
         -DFI issues (acquisition indebtedness)

2. In trust

   a. Mandatory payment charitable split-interest trusts

      (1) CRAT

      (2) SCRUT

      (3) CLAT

      (4) CLUT

b. Income-paying trusts

(1) Charitable, with cap on payments

- NIWOM

- NIMCRUT

- NIMCRUT with flip provisions

(2) Without cap on payment

- Charitable - PIF

- Noncharitable - RLT

3. Charitable gift annuities

a. Immediate payment

(1) States with mandated reserves

- Calculation of reserves

- Funding of reserves

- Does the state permit the reserve fund or trust to hold title to real estate

(2) States without mandated reserves

b. Deferred payment

(1) States with reserves

- Calculation of reserves

- Funding of reserves while not in possession of real estate to sell

(2) States without reserves

c. Is a sales contract necessary? Is disclosure similar to sales necessary?

4. Remainder interest gifts in residence or farm

   a. What is a residence?

   b. What is a farm?

   c. What is a remainder interest?

      (1) After a term of years

      (2) After a life estate

      (3) Combination of life plus term of years

   d. Gift of a partial interest in the remainder interest

   e. Remainder interest in exchange for a gift annuity

      (1) Immediate gift annuity for remainder interest

      (2) Deferred gift annuity in exchange for remainder interest

5. Other deed transfers

   a. Easements

      (1) Valuation

      (2) Mechanics of transfer

      (3) Nature of restrictions and drafting thereof

      (4) Determining if the easement qualifies as an exception to the partial interest rule

   b. Ground leases

   c. Tangible personal property

      (1) Is it really real estate?

      (2) Improvements, fixtures, manufactured homes, mobile homes, water rights, shares in cooperative housing

III. **Operational concerns** in working with real estate

A. Outright gifts

1. Retention by the donee.

a. Use in the exempt function of the donee

(1) Property tax exemption

(2) Costs

(3) Avoiding UBI issues - rental, debt

(4) Purpose for which it will be used and planning commission or zoning snags

b. Unrelated use (including sale)

(1) Property tax assessment

(2) Sale (see also below applicable to all real estate gifts, listing and selling concerns) at, below or above appraised value and 8282 reporting in relation to claimed value; possible assessment of penalties

c. Lease by donee

(1) Negotiation of terms and drafting of lease

(2) Avoiding UBI and DFI issues

(3) Ground leases vs. ground and structures

- Longer term of ground leases

- Changes in value of property over term of lease, change in neighborhood, cost of living adjustments

(4) Seeking competent professional help in leasing

B. Trust holdings of real estate

1. Valuation

   a. Initial or ongoing

   b. Need for appraisal or valuation?

   c. Corrections to value and repayments to or from trust

2. Sale price

   a. Offering price vs. accepting price

   b. Sale price vs. net sale price

   c. Relationship of sale price or net sale price to initial value of the real estate for the setting of the trust payout (other than for PIFs)

3. Interim between gift date and sale date

   a. Carrying costs while in trust — amount

   b. Who pays them?

   c. What if charitable remainderman pays them?

      - Keeping a clear distinction between assets owned by the trust entity and by the charitable remainderman

      - Potential for DFI with advances from the charitable remainderman (reasonably foreseeable, after the fact acquisition indebtedness)

4. Depreciation reserve requirement of the various vehicles

   a. SCRUT, CRAT, CLAT, CLUT— probably no federal tax requirement for depreciation reserve (possible state law or GAAP need, however)

   b. NIWOM, NIMCRUT— private letter rulings indicate depreciation reserve may be required

   c. PIF — Depreciation reserve required

5. Trust accounting for the entity itself

    a. Principal and income act provisions as to allocation of income and expenses

    b. If unproductive or underproductive property, possible reallocation of principal to income on sale

6. Beneficiary accounting

    a. Four-tier system does not always coordinate with Principal and Income law as to allocation of receipts and expenditures

    b. Effect on K-1s

D. Annuity gifts of real estate

1. Cost of carrying real estate and paying annuity, plus possible reserves, for either immediate or deferred annuities in progress

2. Rate at which donee will pay the annuity

3. Base on which the donee will pay

4. The "sole consideration" rule for issuing gift annuities

E. Remainder interests in residences and farms

1. Joint ownership problems

2. Insurance coverage for both donor and donee interests

3. Maintenance, repairs, rebuilding,

4. Inspection rights

5. Rental by donor

6. Vacating to convalescent home by tenant

7. Destruction, fire, flood, earthquake, etc.

8. Need for well-drafted tenancy agreement between co-owners (current and future estate holders)

E. Other deed transfers

1. Monitoring of easement

2. Release or modification of restrictions of easement

3. Sale of property subject to easements

III. Issues applicable to all transfers of real estate

A. Chronology of working with real transfers

B. Types of real property

1. Personal, whether or not primary residence

2. Investment rental

3. Business or industrial

4. Agricultural

5. Natural resources (oil, timber, minerals, etc.)

6. Conservation Easements

C. Valuation

1. Valuation vs. appraisal

2. Whose valuation is it?

3. When and how often is it done?

4. Who pays for it?

5. Who performs it?

6. Effect of the later sales price on it

7. Penalties for doing it wrong

D. Quality of title

1. Analysis of the property on paper

- type of property — personal, investment, commercial
- title holding — fee simple, partnership, trust interest, condo, co-op, lease
- if joint, joint tenancy, community property, tenancy by the entirety, tenants in common, life estate/remainder
- zoning, parcelability
- mortgage
- leases, tenants, occupancy, rent control
- environmental review
- site visit
- title policy or search
- liens, encumbrances (two different things)
- easements
- encroachments
- code, code violations
- property tax
- survey
- parcel map
- perc test
- conservation acts controlling/restrictions
- insurance needed, flood, earthquake, etc.
- contractor inspection
- FMV/valuation
- basis
- depreciation/method/recapture, if any
- carrying costs (including who will pay these during the sale pending)

2. Title searches, title policies and what they cover or more importantly what they exclude from coverage

E. Site inspection

1. Off site

a. Environmental review — trustee liability

(1) Determine level of review, Phase I, II, III

(2) Determine who bears the cost of review

(3) Establish preliminary review guidelines

- conversations with donor
- description of current uses
- donor's knowledge or prior uses
- date of donor's acquisition
- names of former owners
- any business or commercial use
- types of nearby businesses
- names of architects or engineers familiar with the property
- any permits requested
- any prior environmental testing
- location of rivers, lakes, streams nearby
- location of any known or potential nearby toxics

2. Site visit

- presence of oil, petroleum
- discoloration of land, pavement
- dead or dying plant life
- apparent subsurface storage tanks
- electrical transformers
- asbestos
- smoke, soot
- paint products
- waste from business
- wells
- septic systems
- ditches, drainage, marsh
- landfill, holes, sunken areas
- vehicle tracks
- state and type of construction
- trash

3. Nature of business or premises suspect

- cleaning, janitorial
- chemical plants
- dry cleaners
- paint stores, factories
- wood strippers, refinishes
- gas stations
- storage facilities
- sewage treatment
- fiberglass

- tanneries
- mines
- quarries
- oil
- plastic & rubber
- pesticides

4. Authorities to check with

   - local government listings re environmental hazards
   - state agencies
   - EPA
   - National Priorities List
   - outside consultants
   - title companies re history
   - holders of maps, photos, etc.
   - department of health, public works

5. Developing policies <u>before</u> the gift of real estate and adhering to those policies uniformly, even using them as a shield

F. Prearranged sale rules

   1. Donee ability to walk away, amend or finalize the deal

   2. Undoing donor's escrow and the problems it may bring

G. Mortgages

   1. Problem with CRTs and PIFs — grantor trust rules and their effect on the donor and the trust

   2. The 5-5-10 rule with respect to UBI and the lifetime gift

   3. The 10 year rule with respect to UBI and the bequest

   4. After the dog's first bite, self-dealing

H. Liens, encumbrances, charges such as LIDs and assessment districts' assessments

   1. UBI

   2. Payment or removal

I. Depreciation

1. As taken by the donor and its effect on the deduction or recapture on bargain sale

2. Effect on carryover basis to the donee if it is a trust, especially if the trust is not exempt, such as for the PIF or CLT

J. Transfers of undivided interests either outright or in trust

1. How to effect

2. Reaction of lender

3. Is it self-dealing to transfer an undivided into a trust

K. Partial interest rule

1. How a partial interest differs from an undivided interest

2. Transfers of partial interests— mechanics of the transfer

3. No matter which, concepts of jointly owning property with another party

a. Problems in the course of the relationship

b. Self-dealing problems

c. Private insurement problems

L. Knowing all the rules about 8283s and 8282s and the penalties for doing things wrong

M. UBI-DFI analysis

1. Operating a trade or business with real estate

2. Acting as a developer or dealer in real estate

3. Neighborhood land rule

N. Recordation, notarization and when the transfer is effective

O. Listing and selling

1. Selecting a broker

2. Negotiations

3. Selling

4. Net proceeds and reinvestment, or spending or creation of endowment

P. Status of donee and its effect on the transfer and operation of the real estate

1. Public charity

a. Educational organization

b. Not an educational organization

2. Private foundation

3. Trust

a. Tax-exempt trust, CRT

b. Taxable trust, PIF, CLT, RLT

4. Title holding companies

a. 501(c)(2)

b. 501(c)(25)

5. Self-dealing for #2 and 3 above

Q. Selecting a real estate administrator

1. Use of administrator as analogy to trustee or trust administrator

2. Entering a contract for administration

3. Utilizing their resources to pay mortgages and possible DFI consequences

ACTUARIAL REPORT
Presented by Michael Mudry, Actuary of the American Council on Gift Annuities

In my actuarial report this year, I plan to explain in some depth some of the factors considered by an actuary in making recommendations as to assumptions to be used in calculating a gift annuity rate of payout. A gift annuity rate represents the percentage payout that will be made annually on the amount initially paid to a charitable organization for the gift annuity. For example, if the annual gift annuity paid is 7.5% of the amount paid for the annuity, such 7.5% is the gift annuity rate. Thus, if a donor pays $10,000 for a gift annuity for herself or himself, the dollar amount of annual annuity she or he will receive for the rest of her or his life will equal the gift annuity rate of 7.5% times the $10,000 amount paid for the gift annuity, or $750. However, before a charitable organization decides to enter into a contract to pay a gift annuity for the life of one or more individuals, it must first determine the annuity rate it is willing to pay in exchange for the amount it receives from the donor for the annuity This amount can be determined in one of several ways. For example, the organization could decide that, since it might be able to invest the amount paid for the annuity in a 30-year U.S. Treasury bond with an annual rate of, say, 7%, it would simply pay the 7% as the annuity rate to the annuitant or annuitants. On this basis, the organization would basically be making provision to receive in the future a remainder or residuum at the death of the last annuitant of 100% of the amount paid for the annuity if any related administrative or investment expenses were to be ignored. Alternatively, if the organization determines through studies that its annual investment and administrative expenses related to gift annuities amount to, say, 1% of amounts paid for annuities, it could decide to pay an annuity rate equal to the 7% yield rate minus the 1% expense rate, or 6%, which would also leave a 100% residuum to the organization at the death of the annuitants after having covered the payment of both the annuity and expenses during the lifetimes of the annuitants. While such a simple approach toward calculating annuity rates of payout could have much to commend it where a 100% residuum is desired, charitable organizations became willing in the past to enter into gift annuity agreements under which a residuum of less than 100% was deemed acceptable. Although there were probably some rough rules of thumb that could be used to develop annuity payout rates which would make approximate provision for the desired percentage residuum, it was soon found that a mathematical actuarial calculation was the best means of developing accurate appropriate annuity payout rates.

Under an actuarial approach, the actuary generally makes assumptions as to the following five areas of future experience in connection with the calculation of immediate gift annuity rates:

1. the investment yield rate or, as often called, the interest rate to be earned while the gift annuity agreement remains in force on the amount paid to the charitable organization under such agreement,
2. the mortality rates of the annuitants in future years,
3. expenses to be paid in connection with the gift annuity agreement,
4. the frequency and timing of the annuity payouts under the agreement, and
5. the percentage residuum that is desired to be available to the charitable organization at the death of the last annuitant.

An actuary generally tries to adopt assumptions in these five areas that she or he considers reasonable by studying past experience in each applicable area. Such study of past experience serves to produce information not only as to the type of experience currently occurring, but also as to past trends which can aid the actuary to draw conclusions concerning future expectations.

Let me now explain some of the factors actuaries consider in connection with each of the five areas of assumptions in the order previously listed. First in line is the interest assumption.

One of the major considerations involved in arriving at an interest assumption is the type of securities in which the amount paid for the gift annuity will be invested. It has been shown repeatedly that, over lengthy investment periods, equities produce greater average yields than do investments in fixed income securities. Similarly, longer term fixed income securities have slightly outperformed those for shorter terms. For example, for the 67 years of 1926 through 1992, gross annual compound yield rates have averaged 10.05% for the Standard and Poors 500 stock index, 4.37% for long term government bonds and 3.95% for 3-month U.S. Treasury bills. Thus, for such period, the S&P average equity yields have annually exceeded yields on long term government bonds by 5.68 percentage points and of 3-month Treasury bills by more than 6 points.

It is of interest to note that the Consumer Price Index during that same 67-year period increased at an average annual compound rate of 3.19%. When this CPI rate of increase is subtracted from the gross yield rates just mentioned, the results represent what are generally considered real rates of return. Thus, the average annual compound real rates of return for the 67 years would be 6.86% for the S&P 500, 1.18% for long term government bonds and less than 1% (or .77%) for 3-month Treasury bills. If administrative and investment expenses are deducted from the real rate of return, there is little remaining real rate of return on governmental fixed income securities.

The choice of the organization as to the types of investment securities it will utilize may depend on several factors. For example, one factor is the degree of fluctuation in investment performance that the organization's executives or board of directors would be willing to tolerate. Equity values frequently move up or down much more significantly in the short term than do values of government bonds or Treasury bills. Even though a substantial dip in equity market values has eventually been reversed in the long run in the past, management may be unwilling to have to face current criticism for short term unfavorable results. On this basis, investments may either not be made in equities or may be kept to a small percentage of the total investment portfolio.

Another factor which may determine investment policy is investment restrictions which appear in the laws of those states which have laws relating to gift annuities either directly or indirectly. For example, if a state law restricts investments of required reserves held for gift annuities primarily to government bonds, it will not matter that equities should produce greater yields on average in the long run than such bonds because equity investments would either be prohibited or strictly limited. Therefore, even if management were willing to risk the fluctuations that occur in equity values, such investments simply might not be permitted or might be restricted. Some charitable organizations that do wish to invest to a greater degree in equities than allowed under state laws have limited the impact of such laws by establishing separate gift annuity pools for states that do restrict investments and those that do not. In this manner, the organizations can invest their assets in equities to the extent desired at least in connection with gift annuities related to the states without investment restrictions.

If each charitable organization bases its gift annuity rates on its own expected investment yield rate, it is obvious that those organizations which anticipate a higher yield rate and would reflect such rate in the computation of their gift annuity rates, would develop calculated gift annuity rates that are higher than those calculated by organizations with lower investment yield assumptions, all other assumptions being equal. If such different annuity rates were adopted, it might be expected that more annuities would be issued by the organizations providing higher gift annuity rates than by those with lower rates. It also may be, though, that other factors are involved in the decision-making process of individuals entering into gift annuity agreements. For example, when the gift annuity rate is increased, the resulting charitable deduction for Federal income tax purposes is decreased.

Probably a more important factor in the decision-making process of an individual entering into a gift annuity agreement is donative intent. Planned giving officers from several organizations have indicated to me that the goal of many of their annuitants was to benefit the specific organization, so it was immaterial that higher gift annuity rates were available elsewhere

An organization that considers that it will be able to earn a higher yield rate than another organization may for various reasons still prefer not to calculate and adopt higher gift annuity rates than those of other organizations. In such case, the residuum available to the organization anticipating higher investment yield rates would normally exceed the 50% residuum applicable for other organizations.

In deciding upon an assumed investment yield rate, there tend to be two main approaches used. Under the first approach, the assumption would be based on the yield rates at which the organization can invest any new monies it receives. Under the second approach, the assumption would reflect the current yield rate being presently received on the organization's gift annuity assets. For example, the interest rate being currently earned by an organization on its present gift annuity assets, all of which are invested in fixed income investments, might be 8%. This would likely reflect various bonds with differing coupon rates. However, for the investment of any new money received, the organization would have to invest at rates currently available, which could be higher or lower than the 8% rate. If current new money earnings rates are lower, they would in effect depress the average earnings rate in the future. This should be taken into account in making the interest assumption. I tend to favor basing the assumed investment yield rate on the first, or new money, approach.

It should be recognized that an interest assumption does not have to remain constant for all future years. Under new money interest assumptions, if an organization invests primarily in long term government bonds without a call feature, so that the bonds cannot be redeemed prior to maturity, it might be appropriate to adopt a level assumed rate of interest for the entire period of the annuity. However, if investments are made in bonds which may be called, the initial yield rate may not be available for the entire life of the gift annuity agreement because the bond may be called before the annuitants die and it would be necessary to reinvest the money received. If the reinvestment is at a lower yield rate than that under the original bond, losses could arise which could produce a lower residuum than originally assumed. Actually there is some, though smaller, reinvestment risk even under non-callable bonds because some annuitants should live beyond the maturity date of even a long term bond. For this reason, if current yield rates are high on new money investments, the interest assumption could reflect the higher yield for some period of years, but then grade into a lower assumed rate at some future date. This grading approach could also be appropriate in connection with interest assumptions based on average yields on present assets if investments are now being made at lower yield rates than such average.

I have spent a significant amount of time discussing the investment yield assumption because it is probably the most important assumption relating to the calculation of gift annuity rates. While much more could be said about this area, I have probably said enough, so let us now consider the second assumption involved in the calculation of gift annuity rates, which is the <u>mortality rates</u> of annuitants. In calculating recommended annuity rates presently in force, it was assumed that mortality would occur at the rates set forth in what is called the 1983 Individual Annuity Mortality Table for female lives with a one-year setback in ages.

A mortality rate represents the percentage of a given group of individuals that would be assumed to die within one year. It would of course be possible to study mortality among various categories of groups of individuals, including separations according to age, gender, race, occupation or any other criteria desired. In setting mortality assumptions for calculating recommended gift annuity rates, the only separation recognized is that of age. Thus, a separate mortality rate is assumed for groups arranged only according to age, with no difference in assumptions being made for males as compared to females, or for whites as compared to non-whites, or for race car drivers as compared to accountants, etc. Such distinctions have never been made in connection with the calculation of recommended gift annuity rates from the date of the first gift annuity rates developed in 1927. Thus, the gift annuity field was one of the first in the United States to have developed gender-neutral annuity payout rates which do not differ according to the gender of the annuitant. Of course, when a mortality study is made of a group of individuals of a given age, some of whom are females and some males, the resulting experience rate of mortality for that age represents a mortality rate which averages out the normally lower mortality rates of females and the higher rates of males.

The mortality table previously mentioned as being used to calculate the present gift annuity rates has been used for calculating all the gift annuity rates recommended in 1983 and later, which is a 12 year period. For this reason, it is becoming an increasingly inappropriate mortality assumption because it does not take into account decreases in mortality rates that have generally occurred during this period. An illustration of experience as to decreases in mortality rates is as follows:

Age	*Assumed Mortality Rates Use to Calculate Recommended Gift Annuity Rates in* 1927	1983	*Ratio of 1983 Rate to 1927 Rate*	*Average Annual Compound Percentage Decrease in Rates*
65	3.911%	0.663%	17.0%	3.1%
70	5.722	1.065	18.6	3.0
75	8.521	1.791	21.0	2.7
80	12.790	3.233	25.3	2.4

It can be seen from this illustration that, in 1927, it was assumed that 3.91% of a group of individuals who were age 65 would die in one year. In 1983, though, only 0.663% (or less than two-thirds of one percent) of 65 year olds were being assumed to die in one year, which is a rate only 17% of that assumed 56 years earlier. This represents 3.1% average annual compound rate of decrease in mortality rates at that age for the 56 year period. Based on this type of experience, I would recommend that the mortality assumption be used for calculating gift annuity rates currently reflect two changes from the present assumptions. First, in order to take into account the continuing decreases in mortality rates from 1983 to 1995, I would add a second year of setback in ages to the present one year setback. Second, I would introduce a new actuarial concept into the calculating which would make provision for future continuing reductions in mortality rates.

I would like to make some comments concerning the second change. In the past, actuaries have almost universally adopted what is called a static mortality table. Under such table, if a mortality rate at age 80 is 3.233%, the assumption being made is that such rate of 3.233% applies not only to the current group of 80-year old individuals, but also for the future year when an individual now less than age 80 attains that age. However, experience has now shown that when, for example, a person now age 65 reaches age 80, her or his mortality rate will have decreased. Therefore, the assumed mortality rate at age 80 under a static table of a person now age 65 would be overstated. Thus, in connect with annuities, it would be assumed that more people will have died than will actually have died. This understates the amounts of annuity payments that will be expected to be made, so it will have a financially detrimental effect.

The Society of Actuaries is now in the process of recommending that, at least for the purpose of calculating required annuity reserves, a specific assumption be made as to future rates of decrease in mortality rates among annuitants. On this basis, my recommendation would be that improvement rates set forth in what is called Protection G be utilized for purposes of developing future mortality rates among annuitants in connection with the calculation of gift annuity rates. The projection scale would use the same female assumption and two-year age setback applicable to the basic mortality rates. Thus, the recommended mortality assumptions would reflect the mortality rates and projection factors of the 1983 Individual Annuity Mortality Table with Protection G, both of which are for female lives with a two-year setback in ages.

It should be recognized that an acutal mortality study of gift annuity annuitants has not been made for a number of years. However, we believe that the recommendation does take into account the last actual mortality study, together with appropriate mortality rate decreases since the last study.

Let us now turn to the third assumption mentioned, which is *expenses*. Prior to 1955, no provision for expenses was incorporated in the calculation of gift annuity rates. Beginning in 1955, all calculations of recommended gift annuity rates assumed that 5% of the amount paid for a gift annuity would be needed, together with interest earnings thereon, to cover all future expenses associated with a gift annuity. Based on conversations with various individuals involved in the gift annuity field, I have been informed that it would be more appropriate in the expense area if it were assumed that expenses would be three quarters of 1% (i.e. 0.75%) of assets annually. Therefore, I would recommend such assumption in place of that presently being used in connection with expenses.

The expense assumption is intended to make provision for all expenses, including those relating both to investements and administration. Thus, it would cover expenses of items such as issuing the agreement, investing the money paid for the annuity, paying annuities, providing initial tax information, and filing reports with state insurance departments.

The fourth assumption listed in connection with the calculation of gift annuity rates relates to the *frequency and timing of annuity payments* under the agreement. In a sense, this is less an assumption than it is a statement of fact. However, in another sense, it is an assumption because the calculated recommended immediate gift annuity rates reflect the premise that all gift annuities are payable in semi-annual installments, with the first payment in six months. In reality, of course, payments are often instead payable monthly, quarterly or annually. It would greatly add to the number of tables of annuity rates that would have to be prepared if separate rates were developed for each type of frequency, which would add to the complexity of gift annuity operations. Moreover, the recognition of different frequencies in the calculation process would generally produce little or no change in a calculated gift annuity rate. For this reason, the continuation of this assumption seems reasonable.

The fifth and last assumption made in connection with the calculation of gift annuity rates relates to the percentage *residuum*. The percentage residuum represents the portion of the amount paid for the gift annuity that would still be left for use by the charitable organization at the death of the last annuitant. It assumes that the entire amount paid for the annuity would be (1) invested, (2) increased by earnings, and (3) decreased by the payout of the gift annuity and expenses until the last annuitant dies. Until 1939, provision was made for a 70% residuum. Form that point on, a 50% residuum has been assumed. Obviously, the less residuum assumed, the greater the annuity that can be paid.

It should be recognized that there is nothing in the gift annuity field which actually requires that the entire amount paid be held until the annuitants dies. As long as adequate reserves are held to cover the liability for annuity payouts, expenses and contingencies, the reaminder of the amount paid for the annuity can be released for use by the charitable organization, either immediately or at a later date prior to the death of the annuitants. Because such remainder would not be held until the annuitants die, its amount would normally be less than 50% of the amount paid for the gift annuity.

It should also be mentioned that, for deferred gift annuities, an interest assumption is also introduced in connection with the deferred period between the issue date of the deferrerd gift annuity and the date six months before the date of the first annuity payout. No mortality is taken into account during such deferred period for purposes of calculating deferred gift annuity rates. The main reasons for the interest and mortality approach used in connection with the deferred period appear to be first, that it would greatly expand the number of rate tables needed if a more typical actuarial approach were used, and sowould add significantly to administrative complexity, and second that relatively few deferred annuities are issued, so simplified assumptions are acceptable.

It is of course possible for each charitable organization to develop its own assumptions and calculate its own gift annuity rates. This is especially true when recognition is made of current computer capabilities that can eliminate much of the burdensome complexity that could be involved in calculating gift annuity rates in past years. On the other hand, and especially for organizations that issue few gift annuities, it may be more practical for the organization to adopt some standard rates in order to reduce the expenses involved with individual calculations by each organization.

In conclusion, let me simply say that I've given you what is really a brief summary of actuarial considerations in connection with the calculation of gift annuity rates, even though it may not have seemed brief to you. Make use of may comments as you wish!

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UPDATE ON CANADA

Presented by Gordon Nelson

PART I-- PLANNED GIVING -- THE GROWTH OF PLANNED GIVING IN CANADA

Abbreviated History:

Certain forms of planned giving have been available in Canada since early in the twentieth century. However, for a good many years, there was very little active promotion done with the exception of what was usually a low key encouragement of bequests and gift annuities by charities in the religious sector. These were typically based on the concept of "stewardship" of one's resources, and those involved in the area were often referred to as stewardship counsellors. A variety of trust arrangements and the use of life insurance began to gain popularity in the 1970's.

The last ten years (1985 through 1994) has seen an explosion of interest in gift planning in Canada as development officers of universities, hospitals and other charitable sectors have become aware of the vast potential to be found in the various forms of planned giving. The "gift planning officer" (often called the Director of Planned Giving) is becoming a vital part of many development departments.

Although the tax laws do not provide the same degree of incentive for giving as is found in the U.S., there is a move to expand the number and complexity of planned giving instruments so that Canadians may be able to express their donative intent in the most tax-effective manner possible.

Current Status:

(1) *Organizations*

(a) Canadian Association of Gift Planners

While this organization is only some three years old, it has had a great influence on gift planning in Canada. It has brought together gift planning officers, lawyers, accountants, insurance agents and other professionals through the combination of a national body and regional round-tables. Like the first conference a year earlier, it's second Annual Conference, held in Toronto in April, 1995, brought together a sell-out audience of people from all across the nation.

(b) Canadian Association on Charitable Gift Annuities

About 1979, a group of representatives of less than a dozen religious charities involved in the issuance of charitable gift annuities formed the Canadian Committee on Gift Annuities. Out of this (in 1988) grew a formal organization, the CACGA which now has over sixty members, including universities, hospitals, social agencies, etc. as well as religious charities.

The CACGA has set standards in the areas of contractual agreements, advertising and promotion (including a "disclosure" document), financial reserves and the protection of annuitants. Each organization is asked to complete a report annually, with a more detailed report every three years.

Like the American Council on Gift Annuities, the CACGA recommends maximum annuity rates to its members. Rates are more flexible in Canada; that is, they can be changed more easily for two reasons: (1) The members are provided sets of rates (on computer disks) which have varying pricing (interest earned) assumptions. It is therefore easy to change from one set of rates to another. (2) The Association's members have authorized the five-person Executive to make changes in the recommended rates between meetings of the membership, if warranted by major changes in the general interest rates on investments. Recently, the Association has also undertaken to advise recommended rates to those members who choose to re-insure their annuities with commercial carriers.

(c) Canadian Council of Christian Charities

While this organization, which has been in existence for over 20 years, is restricted in its educational influence to the "religious" sector and deals with much more than gift planning, it did have considerable sway on the development of deferred gifts in Canada, particularly in the 1970's when much of the activity was in that quarter.

Of interest is its recent formation of CCCC Trust Services, designed to help its members in the training of planned giving field representatives, preparation of agreements, investing of funds held for donors and related areas. Those charities which join CCCC Trust Services are offered an education program which, when combined with an internship period and the successful completion of a certification examination, leads to a designation of CSC (Certified Stewardship Counsellor) for the field representative.

(2) *Publications and Other Aids Available*

Planned Giving for Canadians - Frank Minton & Lorna Somers, published by Somersmith, Waterdown, On., 1994

Canadian Taxation of Charities and Donations - Arthur B. Drache, published by Carswell, Scarborough, On., 1990

Canadian Income Tax with Regulations - CCH Canadian Limited, North York, On, 1995

Canadian Estate Planning Guide - CCH Canadian Limited, North York, On, 1995

Canadian Estate Administration Guide - CCH Canadian Limited, North York, On, 1994

Canadian FundRaiser - Jim Hilborn et al - published by The Newsletter Group, Toronto, On (Newsletter - Several issues per year)

Front & Centre - published by the Canadian Centre for Philanthropy, Toronto, On (Newsletter - 6 to 8 issues per year)

CCCC Bulletin - published by the Canadian Council of Christian Charities, Elmira, On (Newsletter - 5 issues per year)

Course in Financial Planning -- Chartered Financial Planner - a course available through the Canadian Institute of Financial Planning, Toronto, Ontario. This course covers all aspects of financial planning and leads to the C.F.P. designation.

PART II -- PLANNED GIVING INSTRUMENTS IN CANADA AND THEIR TAX IMPLICATIONS

(1) *Gift Annuities (Self-Insured)*

(a) The Agreement

Not all charities in Canada are able to issue their own gift annuities. (Indeed foundations are forbidden to do so by law.) Those who do, issue an agreement promising to pay a level income for life to an annuitant (or to two co-annuitants in the case of joint and survivorship annuities) in exchange for a gift of capital. While some charities take an administration fee (up to 8%) off the top, most invest the entire contribution in a fund totally segregated from the normal moneys of the charity. Rates are generally based on a conservative investment earning (the "pricing" assumption) and are designed to produce a balance for the charity of a least 50% of the original gift if the annuitant (or last survivor in the case of a joint agreement) lives to the expected mortality date.

(b) Tax Implications

Under Revenue Canada's regulations, in accordance with mortality tables set out in Bulletin 111R, part of each annuity payment is considered to be a return of capital. Therefore, only a portion of the income received by the donor(s) is taxable. As the tax-free portion increases with the age of a donor at the time of the commencement of the agreement, those who take out annuities when they are older will have very little income they must declare or, possibly, none at all. If the government tables indicate that the donor is not expected to get back as much as was given, then the income is totally tax-free, and the donor will qualify for a charitable receipt for the amount by which the donation exceeds the anticipated return (that is, the difference between the contribution and the total annuity payments receivable). Unlike the situation in the United States, the tax-free portion of the annuity payments continues for life even if the donor lives well beyond the anticipated mortality date.

(2) *Gift and Annuities (Reinsured)*

(a) The Agreement

Under this plan, which is accessible to all charitable organizations, a commercial insurance company underwrites the annuity rather than the charity itself. When the gift is made, the donor signs an agreement which authorizes the charity to arrange for a commercial annuity which provides payments of a stipulated amount to the annuitant. The charity then pays the single premium for the annuity contract and keeps the difference between the gift amount and the premium as an immediate donation. If the annuity purchased is for a term certain or has a "guaranteed" period, and the donor does not survive to the end of the said term or guaranteed period, the charity may benefit further by receiving the annuity payments from the insurer to the end of the term.

(b) Tax Implications

If the annuity purchased is for a term certain, or is a life annuity with a guaranteed period of payment, the taxable portion of the annuity payments would be the same as though the donor had personally purchased the annuity from the insurance company. However, the donor is entitled to a receipt for tax purposes in the amount of the portion (usually 25% to 30%) of his/her original gift that was retained by the charity. The amount of this receipt can be used as a charitable contribution up to the normal limit (20% of income) allowed for all charitable donations and has the same carry-forward privileges that any other charitable donation has.

If the annuity purchased is simply payable for the life of the annuitant (or annuitants in the case of a joint and survivorship plan), the tax situation can be handled in one of two ways. If it is preferable, it can be dealt with in exactly the same manner as outlined in the previous paragraph: the donor can get a single receipt for the amount of the difference between the gift and the premium and be taxed on the same basis as any other "prescribed" commercial annuity. However, if it is to the donor's advantage, there is the option of treating the arrangement as a gift annuity under Income Tax Bulletin 111R, basing the tax-free portion on the entire amount transferred to the charity rather than just the amount the charity passes on the insurance carrier. Of course, the donor would then not qualify for a receipt for the difference between the gift and the premium, but would qualify for a gift receipt for the excess (if any) of the amount contributed over the total annuity payments to be paid during the life expectancy.

(3) *Life Insurance Policies*

(a) The Agreement

A donor can always name any charity as the beneficiary of any type of life insurance -- whether an individual policy or a certificate of insurance under a group policy, and no matter whether the insurance coverage is of a term, permanent life or endowment nature. Of course, the designation is always changeable during the lifetime of the insured. If the policy is still in force at the time of the donor's death, the insurance benefit is paid directly to the charity and does not form a part of the estate.

An irrevocable gift is made when the donor assigns title to an individual insurance policy (i.e. transfers the ownership of the contract) to a charity. This is preferable to the simple beneficiary designation as it assures the charity will receive some benefit and it brings certain tax advantages to the donor.

On occasion life insurance is purchased with a view to "wealth replacement" in connection with a direct donation of property or a charitable remainder trust. The tax savings received from the gift to the charity is used to purchase a policy payable either to the estate or directly to children. For the heirs, this replaces the value of the gift made to the charity.

(b) Tax Implications

Where the gift of insurance proceeds is effected simply by a beneficiary designation, there is no income-tax saving. There is one advantage to the donor's heirs in that the proceeds paid directly by the insurer to the charity do not become a part of the estate and are, therefore, excluded from the calculation of the probate fees charged by the courts. (Can be up to 1.5% of estate value depending upon province.)

Insurance policies which have their title assigned to a charity create two tax advantages. First, all premiums paid by the donor subsequent to the transfer of ownership are fully receiptable for tax purposes, whether those premiums are paid directly to the insurer or paid to the charity for forwarding to the insurer. Secondly, if the policy being transferred has a cash value (the net surrender value including any dividends left on deposit), the charity may issue a receipt for the said cash value at the time of transfer. Note that on older policies a taxable capital gain will be triggered if the cash value exceeds the donor's costs (net premiums paid.)

(4) *Charitable Remainder Trusts*

(a) The Agreement

A trust fund is created by the donor with an irrevocable gift of cash, bonds, shares of stock, or real estate. Charitable organizations (not foundations) often act as a corporate trustee (assuming it is authorized and able to so serve), but the trustee could equally be a person named by the donor or a trust company. The income from the trust is paid for the life of the donor and/or other beneficiaries named. Whatever remains in the trust upon the passing of the last beneficiary is the gift to the charity.

(b) Tax Implications

A donation receipt can be issued to the donor for the present value of the remainder (residual) interest. A donor is responsible for capital gains up to the time of the transfer. However, this can be reduced or eliminated by electing a donation value receipt for any amount between the cost base and the fair market value at the time of transfer. Choosing a lower than market value reduces both the capital gains to be declared and the tax credit donation receipt. Future gains accrue to the trust and are not attributable back to the donor for tax purposes. As the gift is no longer a part of the estate, there is a savings in probate fees.

(5) *Loan Agreements*

(a) The Agreement

Capital is loaned to the charity at either an extremely low rate of interest or none at all. The charity may then use this loan for capital needs or reinvestment at a higher rate, keeping in mind that most loan agreements provide for return of the capital on demand. Note: Canadian foundations cannot enter into this type of agreement.

(b) Tax Implications

Only interest paid to the donor is taxable. The excess interest earned by the charity is not attributed back to him/her. This plan is particularly useful to persons who wish to help a charity but cannot use a donation receipt as they are already exceeding the 20% maximum allowed.

(6) *Wills*

(a) The Agreement

In Canada, wills may be formally prepared with or without the help of a lawyer. (Using a lawyer is highly recommended.) To be effective, in addition to the signature of the testator and the date of that signature, two disinterested persons (of legal age) must sign as witnesses in the presence of the testator and each other. Holograph (handwritten) wills are also acceptable in all provinces. However, such a will must be completely written in the hand of the testator and contain the date of signature. No witness is necessary to make this will legal. When a will is witnessed, the signatures of the witness(es) must follow the date and signature of the testator and should be identified as being that of a witness.

Charitable bequests made through a will may be specific, residual or conditional in nature. Charitable trusts may be set up in a will. Care should be given to spell out the terms of such a trust as well as identify the person(s) who are to act as trustees.

(b) Tax Implications

A charitable receipt is issued to the estate of the deceased donor and may be used on any of the returns completed for the year of death. Any excess which is not usable may be carried back one year, that is, the return for the year-prior-to-death may be resubmitted, including the excess charitable contribution (up to the normal 20% limit for that year as well).

Where appreciated assets are bequeathed to a charity, the executor may elect to value the gift at (and receive a donation receipt for) any amount between the cost base and the fair market value of the asset to reduce the taxable capital gain.

PART III -- TAXES AND OTHER GOVERNMENTAL MATTERS

Federal Government:

(1) *Influences for Change*

Two opposing forces come very much into play in the arena of taxation relief for charitable gifts on the Canadian scene. On one hand, the large financial deficits faced yearly by the federal and provincial governments and the resultant mounting public debt places pressure on the legislators to prevent any growth in areas which would reduce the tax base. On the other hand (as pointed out to the governments by charitable groups such as those mentioned earlier in this paper) because the government must cut down on what is being spent on the social sector, hospitals, universities and other charities must have available as many tax incentives as possible so that they can attract more private donations. Obviously, if more funds are raised privately, there will be less need for government grants.

(2) *Income Tax Bulletin IIIR*

This bulletin, which deals with taxation of charitable gift annuities in Canada is currently under review. One of the major changes proposed is to update the mortality tables used by the government. This will result in a smaller tax advantage being made available to future annuitants. The CACGA has been consulted about the proposed new regulation and has responded with several suggestions.

(3) *On the Horizon*

Dialogue with Revenue Canada and other governmental departments is continuing on several fronts. It is anticipated that Pooled Income Funds will soon be approved as a charitable planned giving instrument in Canada. Other creative instruments are being suggested. It is hoped that at the next conference (1998) an update similar to this one will contain several other planned giving methods and instruments.

Provincial Governments:

(1) *Recent Events*

Negotiations are in progress with the Province of British Columbia regarding the registration of charities who wish to issue gift annuities and the licensing of their representatives. The Canadian Association on Charitable Gift Annuities is continuing to keep in contact with all the other provinces. Further reports/updates will be provided by the CACGA as they become available.

PART IV -- SOME CROSS-BORDER CONSIDERATIONS

(1) *Canadians Giving to Foreign Charities*

With some exceptions, Canadian who make a gift to a charity in the United States are not able to claim a donation credit on their tax returns. The following circumstances result in a tax credit being available. (1) The Canadian donor makes a gift to an American university which is listed in Schedule VIII of the Income Tax Regulations. (2) The Canadian lives near the border, commutes to a workplace in the United States and gives to a charity which issues receipts deductible on a U.S. return.
(3) The government of Canada has made a gift to the foreign charity in the same year or the year previous to the donor's gift. (4) The Canadian gives to a qualified American charity and although he is not employed in the United States, he/she has a U.S. source of income. (Allowable only up to 20% of the U.S. income.)

(2) *Canadians Donating American Property*

If real estate in the United States is donated by a Canadian to a Canadian charity, the donor will be taxed on the capital gain in both the United States and Canada. However, Canada will allow a tax credit for the amount of tax paid in the United States.

(3) *Other Matters*

There are specific regulations concerning several areas of cross-border gifts. Some of these apply to Americans and others to Canadians. If considering gift annuities, charitable remainder trusts, gifts of real estate or shares, reference should be made to the Canada-United States Tax Treaty (recently revised).

PART V -- GIFT ANNUITY RATES IN CANADA

History and Method of Change:

Although gift annuities have been issued in Canada for most of this century, the Canadian Committee on Gift Annuities (the predecessor of the Canadian Association on Charitable Gift Annuities) began less than twenty years ago. One of the first issues settled upon was the sharing of rate schedules. From the beginning it was emphasized that each charity should have a program which would both protect the financial interest of both the charity and the donors/annuitants. Keeping in mind that the payment rates should not only assure that the issuing charity would be able to continue payments for the lifetime of the annuitant(s), but that there should always be a "gift" portion of capital remaining upon the death of the annuitant(s). The members agreed to a schedule of rates which would represent the maximum that should be paid at each age.

The original "recommended" schedule was based on four factors: (1) a rather conservative actuarial mortality table, (2) the investment of the entire gift to provide an income stream, (3) a reasonable interest earning assumption (which any prudent investment plan could attain), and (4) an assumption that 50% of the original gift would remain and be available to the charity if the donor died on the anticipated mortality date. The actual experience has been that the charities have been ending up with much more that the anticipated 50%.

For many years the recommended maximum rates did not change, although they were reviewed by the members at least annually. However, with the advent of computerization and the provision of disks which contain several sets of rates to all issuing members, rates can now be adjusted more frequently. The Executive of the CACGA reviews rates every month and (based on a formula) can recommend a change between the semi-annual members meetings, any changes subject to ratification by the general membership at their next meeting. During the turbulent shifts in general interest rates the last three years, the recommended rate schedule has been adjusted five times. It must be remembered that although most charities use the recommended rate schedule, an individual charity may have reasons why it chooses not to do so. In fact, some charities consistently offer lower rates than the suggested maximums.

Current Rates Being Used:

The following schedule represents the maximum (unisex) rates being recommended by the CACGA to self issuers of gift annuities in Canada as of March, 1995. Rates for annuities on more than one life and a separate table of suggested rates for charities which reinsure with commercial carriers are available to members of the CACGA.

MALE	ANNUITY RATE (%)	% INCOME TAX FREE	FEMALE	ANNUITY RATE (%)	% INCOME TAX FREE
65	9.0%	64.60 %	65	9.0 %	55.05 %
66	9.1%	66.60 %	66	9.1 %	56.81 %
67	9.2%	68.79 %	67	9.2 %	58.70 %
68	9.3%	71.22 %	68	9.3 %	60.71 %
69	9.4%	73.87 %	69	9.4 %	62.87 %
70	9.5 %	76.27 %	70	9.5 %	65.19 %
71	9.7 %	78.70 %	71	9.7 %	67.71 %
72	9.8 %	81.63 %	72	9.8 %	70.44 %
73	9.9 %	84.88 %	73	9.9 %	72.91 %
74	10.1 %	87.62 %	74	10.1 %	75.59 %
75	10.3 %	90.74 %	75	10.3 %	79.15 %
76	10.5 %	94.30 %	76	10.5 %	82.44 %
77	10.7 %	97.36 %	77	10.7 %	85.31 %
78	10.9 %	100.0 %	78	10.9 %	89.32 %
79	11.1 %	100.0 %	79	11.1 %	92.90 %
80	11.3 %	100.0 %	80	11.3 %	96.90 %
81	11.6 %	100.0 %	81	11.6 %	100.00 %
82	11.9 %	100.0 %	82	11.9 %	100.0 %

MALE	ANNUITY RATE (%)	% INCOME TAX FREE	FEMALE	ANNUITY RATE (%)	% INCOME TAX FREE
83	12.0 %	100.0 %	83	12.0 %	100.0 %
84	12.0 %	100.0 %	84	12.0 %	100.0 %
85	12.0 %	100.0 %	85	12.0 %	100.0 %
86	12.0 %	100.0 %	86	12.0 %	100.0 %
87	12.0 %	100.0 %	87	12.0 %	100.0 %
88	12.0 %	100.0 %	88	12.0 %	100.0 %
89	12.0 %	100.0 %	89	12.0 %	100.0 %

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FIDUCIARY ISSUES FACED BY CHARITABLE ORGANIZATIONS

Presented by David Wheeler Newman
Mitchell, Silberberg & Knupp

I. **Should Your Charity Serve as Trustee?**

A. Our Natural Instincts. There is a tendency of development officers to prefer the charity serving as trustee of trusts established by their donors, as trusteeship is viewed as another opportunity for contact with the donor, hopefully in a positive situation.

B. Stop to Consider. To avoid making decisions based solely on this inclination, the development officer must consider:

1. The added contact will be positive for the donor (and therefore advantageous to the charity) only if the job is done right.

2. Does the charity now have, or is it likely to develop, the capability to manage trusts effectively?

3. If so, is the charity willing to accept the risks of liability that come with fiduciary responsibility?

C. Examine Your Infrastructure. Does the charity have the resources to devote to trust administration?

1. Administrative/bookkeeping.

2. Investment.

3. Tax returns.

4. Record keeping.

D. A Realistic Comparison of Alternatives. The comparison with a professional trustee cannot overlook the expense to the charity in maintaining this type of infrastructure. Do not assume that the comparison is between services that cost something and those that are free. "Why should we pay the bank a trustee fee when we can get the work done in our office for free?". If you are really performing the same services as the bank, it cannot be done for free. The charity is either:

1. Incurring additional overhead expense.

2. Diverting staff resources from other activities.

3. Relying on volunteers.

4. Not providing the same level of service.

E. Co-Trustee Alternative.

1. The charity may be able to structure a relationship with a bank or other institutional trustee to serve as co-trustee and to divide responsibility with the charity.

2. A typical division might be for the institutional trustee to act as custodian and to provide administrative services such as tax returns and accounting to beneficiaries, but investment services only within guidelines set by the charity co-trustee.

3. To make the trust document more "user friendly" to the donor, it is possible for the name of the bank or trust company to not even appear in the document, so long as the document gives the initial trustee -- the charity -- the right to appoint a co-trustee and to delegate certain authority and responsibility to the co-trustee. If this approach is used, you still need to have the document (or at least a prototype) reviewed in advance by the bank or trust company to make sure it will be prepared to accept the co-trusteeship under the terms of the document.

4. In negotiating this type of arrangement with the professional co-trustee, critical issues include the size of trusts that will be accepted and the fee schedule to be applied.

   a. Many trustees have a minimum size of trust they are willing to accept, and this minimum may be larger than at least some of the trusts typically generated by your organization. The trustee should reduce its "floor" to correspond with the planned giving policy statement of your organization, which, in turn, should have such a floor to take into account the costs of developing a gift in trust as compared with an outright gift. For example, the policy statement might provide that the minimum corpus of charitable remainder trust with which the charity is prepared to assist is $50,000, in which case the professional trustee should be prepared to accept trusts of this size for administration as co-trustee, perhaps with the additional understanding that there will be a minimum number of such trusts within the program.

   b. The fee schedule for most professional trustees is expressed as a percentage of the value of trust assets under management, and is a sliding scale with a higher percentage applied to smaller trusts, perhaps subject to a minimum fee, and a lower percentage applied to larger trusts. To negotiate the fee arrangement, consider the following:

      (i) Linked with the agreement of the trustee to accept the small trusts along with the big ones, as suggested above, the sliding scale fee may be applied by aggregating the corpus of all trusts. Note that many co-trustees will automatically apply the lowest fee on their schedule in this situation.

      (ii) The co-trustee may agree to waive the minimum fee for all trusts.

      (iii) Will the percentage fees apply to assets on which there is little, if any administration required, such as raw land or closely held stock, or will it apply only to the value of "investment assets" which the trustee is responsible for administering?

II. The Donor as Trustee

A. The Purpose to be Served. Donor trusteeship may eliminate some of the sources of misunderstandings regarding trust administration matters between trustee and beneficiary.

1. For example, in the sale by the trust of the appreciated asset used to fund the trust, it is important for the donor to feel comfortable that the highest reasonable price was obtained for the asset under the circumstances (especially if income distributions to the donor are affected!).

B. Successor Trustee. The charity's policy (or the arrangement with a specific donor) may anticipate that the donor will remain as trustee only until disposition of the assets used to fund the trust.

C. CERCLA Exposure. Donor trusteeship may also eliminate the risk of hazardous waste liability to the charity or institutional trustee.

D. Donor Preference. To realistically evaluate the alternative of donor trusteeship, keep in mind that the desire to rid oneself of the burden of responsibility for assets is often one of the motives behind a proposed gift in trust. Your donor may not be interested in being trustee, even for a little while.

III. Special Trustees

A. Purpose. As an alternative to co-trusteeship, consider preserving the flexibility of the trustee having the power to appoint a special trustee for a narrowly defined task.

B. Valuation. It may be inappropriate in certain circumstances for either the donor, as income beneficiary, or the charity, as remainder beneficiary, to value trust assets to determine the annual distribution from a charitable remainder unitrust, in which case the trust document should give the trustee the power to appoint a special trustee to value difficult assets.

C. Investment Advisor or Custodian. The trust document can give the trustee the power to appoint a special trustee with authority limited to custodianship and/or investment advice to the primary trustee, which will be especially helpful if the charity does not have in-house investment expertise.

IV. Responsibility of Trustees for Hazardous Waste

A. The Critical Issue. Is the trustee liable for hazardous waste cleanup expense of property held in a trust, and if so whether that liability is limited to assets of the trust or whether it may extend to other assets of the trustee.

B. The Conservative Assumption. Pending clarification, a trustee must assume that it will be liable for hazardous waste cleanup expense in the same manner as any other owner or operator of real property, and that it may be forced to satisfy that liability from its own assets, separate and apart from those of the trust.

V. Trustee Compensation

A. Legality. Check for possible restrictions on receipt of trustee's fees under state law. Some states do not allow corporations (including nonprofit corporations) to charge trustee fees unless they are licensed as trust companies.

B. Alternatives for Charities.

1. A charitable remainder trust can distribute a portion of the payout to the charity. Example: The donor wishes to fund a 6% net income charitable remainder trust, and has agreed that the charity should receive the economic equivalent of a trustee's fee equal to 1% of trust corpus. The trust could be written as a 7% net income unitrust, with 6% distributable to the income beneficiary and 1% distributable to the charity.

2. Even if no trustee fee is charged, the trustee is still entitled to recovery of reasonable expenses properly allocable to the trust. This makes it even more important for the charity, when acting as trustee, to have adequate administrative and bookkeeping capability to use cost accounting to attribute direct and indirect expenses to the trust for reimbursement.

VI. Trustee Powers

A. Trust Agreement. Statute(s) governing the administration of trusts may give the trustee adequate powers as a matter of state law, but it is always preferable to explicitly provide in the trust document for those powers that might be useful or necessary in the administration of the type of assets held in the trust.

1. Avoid boilerplate that may not apply to the specific type of trust or asset.

2. Note that the IRS prototype charitable remainder trust documents contain no trust powers.

B. Specific Powers. The trustee may find the following powers useful, in addition to standard trustee powers:

1. Sell or encumber real property.

2. Employ an appraiser or other independent advisor to value trust assets.

3. Make distributions to a conservator or other representative appointed to oversee the affairs of a legally disabled beneficiary.

4. Deal appropriately with hazardous waste issues.

5. The right to refuse additions to the trust.

6. The right to resign.

VII. Trust Accounting Rules

A. Charitable Remainder Trusts. A net income unitrust distributes the lesser of the unitrust amount or the net income of the trust determined under IRC Section 643(b), which is trust accounting income, determined under local law. Many states have adopted the Revised Uniform Principal and Income Act (subject to minor variations in some states), which provides "default" rules for allocating trust receipts and expenditures between income and principal in the absence of contrary provisions in the trust instrument.

1. This feature of the uniform act allows the trustee to write its own accounting rules for allocating items between principal and income, with some obvious (and some not-so-obvious) possibilities for custom-designing a net income unitrust.

2. Caveat: The regulations under Section 643(b) make it clear that there is a limit to how creative the draftsperson can be: "Trust provisions which depart fundamentally from concepts of local law in the determination of what constitutes income are not recognized for this purpose."

B. Other Trusts. Other situations where the trust accounting rules are important include a trust providing for distribution of income to one beneficiary, followed by the distribution of corpus to another.

C. Specific Provisions.

1. Accrued bond discount is income only in the year the bond matures or is sold by the trust.

2. Establish an adequate reserve for the depreciation of real property.

3. Trust has income from a partnership, insurance product, common trust fund or other investment vehicle only when it receives a distribution.

4. Optional allocation of realized capital gains to income, instead of the traditional allocation to principal, will be respected by the IRS for purposes of Section 643(b).

VIII. Investment Considerations

A. Income vs Growth. The trustee has a fiduciary obligation to not favor one beneficiary over another. This tension exists with a net income charitable remainder trust, since net income below the unitrust rate will favor the remainder beneficiary. The tension is exacerbated in the common situation where the charitable remainder beneficiary serves as trustee. One solution, to avoid the appearance of impropriety by trying to generate net income at least equal to the unitrust amount even if it means jeopardizing the remainder, may not resolve the tension if there are other charitable remainder beneficiaries of the trust.

B. Balancing Yield and Risk. The trustee will, at the very least, be held to the standard of the "prudent man rule." If the charity has represented itself as having special expertise in the making of investments, it may be held to the stricter standard of the "prudent investor rule." Note that such a representation may be easily inferred with hindsight.

1. The "prudent man rule" is that the trustee "is under a duty to the beneficiary in administering the trust to exercise such care and skill as a man of ordinary

prudence would exercise in dealing with his own property; and if the trustee has or procures his appointment as trustee by representing that he has greater skill than that of a man of ordinary prudence, he is under a duty to exercise such skill." Restatement, Second, Trusts Section 174.

C. <u>FDIC Insurance</u>. As a result of strain on the nation's deposit insurance system, the FDIC has become much stricter in applying limitations on FDIC insurance of bank deposits. This will usually not be a problem for a charitable remainder trust. As an irrevocable trust, it will be entitled to deposit insurance up to $100,000. However, with a revocable trust, the deposit of the trust might be aggregated with other deposits of the donor at the same financial institution with a single $100,000 limit applied to determine insurance coverage.

D. <u>Diversification</u>. Confirm whether diversification of trust assets is mandatory or permissive under the law of your state. A provision in the trust document can normally override this provision of state law. Subject to the preferences of your donor, it is generally preferable for the trust agreement to provide the trustee with discretionary power to diversify trust assets, making it clear that the trustee is not obligated to do so (permissive diversification).

1. The trust document may not restrict the trustee from investing trust assets in a manner intended to result in annual realization of a reasonable amount of trust income.

E. <u>Use of Investment Advisors</u>. Many charities serving as trustee determine that the most prudent approach to investing trust assets is to retain a reputable investment advisor.

F. <u>Experience and Expertise on Your Staff or Board</u>. Caveat: If you are depending on board members for investment expertise, keep in mind that these volunteers have their own businesses to run and that the priorities assigned to your account may be determined accordingly.

IX. Written Policy

A. <u>Incorporation of Trusteeship Issues</u>. As the number of trusts originated over time by your organization increases, it becomes critical that your written statement of policy for the planned giving program address trusteeship issues.

B. <u>Specific Policies</u>. In addition to specific policies of your organization covering the matters discussed above, the written policy might also address the following:

1. If your charity will act as trustee, is there a minimum irrevocable gift? Based on present value or future value?

2. Will the charity serve as trustee of a revocable trust?

3. Is the charity prepared to advance funds to a trust it administers?

4. Integration with gift acceptance policy.

5. Once a trust has been accepted for administration, authority to make all but the most major decisions should be delegated to one staff person, with the organization and its board prepared to stand behind the actions taken by that person.

X. **Staying Out of Trouble**

A. Follow Your Written Policy. The only thing worse than not having a written statement of policy governing trusteeship issues is having a policy which is not followed. It can be awkward if the trustee is called upon to explain its action or inaction in contravention of the trustee's own policy.

B. Recordkeeping. Remember that, no matter how diligent the trustee, things periodically go wrong in the administration of a trust. The beneficiaries (or the donor), armed with hindsight, will have a distinct advantage. The best defense for the trustee is a careful record documenting the decision-making process, including the collection of information, the seeking of advice from professionals and the various alternatives from which the eventual course of action was selected. This record will document the activities of a trustee which has acted prudently but which, at the very worst, made an error of judgment after exercising due care. The key to presenting this defense is maintaining good records of trust administration.

C. Communications. It may seem obvious that frequent and forthright communications with trust beneficiaries is an important key to avoiding fiduciary problems. It is surprising, however, how often those problems grow out of proportion simply because the trustee did not communicate the situation regularly to the trust beneficiaries. Written communications are part of the record of trust administration, and, performed regularly, may keep small problems from developing into large ones.

D. Centralized Trust Administration. Many charities divide trust administration responsibilities between the development office (communicating with the donor) and the finance office (asset management, recordkeeping and tax compliance). This is usually done with the understanding that there will be a clear-cut division of authority and responsibility which, of course, almost never happens in practice. It is more common when trust administration is divided between two departments for there to be a confusing overlap of authority or responsibility or for things to "fall between the cracks" between the two departments. These problems can be avoided if authority and responsibility is centralized in a single office.

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GIFTS OF TANGIBLE PERSONAP PROPERTY, CROPS, MINERAL RIGHTS AND OTHER INTANGIBLES

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I. *GIFTS OF TANGIBLE PERSONAL PROPERTY*

A gift of tangible personal property, such as work of art, a coin collection,[1] antique furniture or a yacht, is subject to special rules that are not applicable to gifts of cash, real estate or securities and other intangible property.

A. *Effect of Use by the Charity on Deduction for Income Tax Purposes.*

1. Use of Contributed Property in the Conduct of the charity's Exempt Functions.

A gift to a public charity[2] of tangible personal property that would generate long-term capital gain upon its sale is deductible to the extent of the full fair market value of the contributed property, only if it is "reasonable to anticipate" that the charity will use the property for some educational, charitable or scientific purpose (i.e., a use related to the charity's exempt purpose).[3] If the gift consists of a set or collection of items, the donor's deduction is not reduced if the charity sells or disposes of an insubstantial portion of the set or collection.[4] This "related use" rule applies for income tax purposes only; the gift and estate tax deduction is equal to the full fair market value irrespective of the use to which the property is put.

For example, a donor who gives a painting and a set of rare books to a college may deduct their full fair market value if donor can reasonably anticipate that the college will hang the painting in a college building and incorporate the books into a college library or collection.[5]

On the other hand, if the donor can reasonably anticipate that the charity will sell or lease the tangible personal property or a substantial portion of it, or otherwise put it to a use not related to the charity's exempt purpose[6],

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[1] Rev. Rul. 69-63, 1969-1 C.B. 63 (a coin collection is not currency but tangible personal property).

[2] Private foundations, described in IRC § 509(a), are subject to special rules with respect to the deduction for appreciated property. See IRC § 170(b)(1)(D).

[3] IRC § 170(e)(1)(B)(i) and Reg. § 1.170A-4(b)(3)(ii). The phrase "reasonable to anticipate" as used in the regulation provides some latitude in the application of the related use rule. For example, if the donor contributes property to a museum, and if the property is of a type normally retained by the museum for purposes, the regulations provide that unless the donor has actual knowledge to the contrary, it will be reasonable for the donor to anticipate that the property will not be put to an unrelated use whether or not the property is later sold or exchanged by the museum.

[4] Reg. § 1.170A-4(b)(3).

[5] Priv. Ltr. Rul. 7751044 (lithographs to art museum); Priv. Ltr. Rul. 8208059 (stamp collection to college for study by students); Priv. Ltr. Rul. 8145085 (porcelain objects given to retirement center); Priv. Ltr. Rul. 9147049 (violin to cultural organization which maintains bank of musical instruments; Priv. Ltr. Rul 9131052 (plant and livestock products to private school emphasizing plant and life science curriculum).

[6] See, e.g., Priv. Ltr. Rul. 8009027; A car given to a university and subsequently given to a professor for use as a family car was not used by the university to carry out its exempt purpose. The donor's deduction was therefore limited to the basis of the car.

the donor's income tax deduction must be reduced by the entire amount of the unrealized appreciation,[7] which, in effect, limits the deduction to the basis of the property.[8]

Example

In 1995 Mary Jones contributed a jade necklace to a charity. Mary acquired the necklace in 1970 for $1,000; at the date of the contribution the necklace was worth $5,000. The gift was made in anticipation that the necklace would be sold and the proceeds added to the endowment fund which Ms. Jones had earlier established. Ms. Jones' income tax deduction would have been $5,000 if she could have reasonably expected that the necklace would be used in the hospital's exempt functions; because it is highly unlikely that the hospital could use a necklace to carry out its exempt purpose, the deduction must be reduced by the unrealized appreciation ($4,000) to $1,000.

Since the burden of proving that the property is put to a related use (or that the donor can reasonably anticipate that it will be put to such a use) is on the donor,[9] it is advisable for any donor making a gift of tangible personal property to obtain a letter that indicates the use to which charity expects to put the property. To insure that the charity is not required to keep the property indefinitely, any such letter should permit the charity to sell the property if, in its judgment, it is no longer advisable to retain the property for educational, scientific or other exempt purposes. Such a later sale, occasioned by changed circumstances after the property has legitimately been used by the charity for its exempt purposes, should not affect the donor's deduction.

2. Income Tax Percentage Limitation.

A gift of appreciated long-term capital gain property is generally deductible subject to a limit of 30% of the individual donor's contribution base unless the donor makes an election to reduce the deduction by the unrealized appreciation, in which case the deduction limit is increased to 50% of the contribution base. In the event that the donor's gift is put to an unrelated use by the charitable donee, the deduction is automatically reduced by the appreciation, and the deduction, as reduced, is subject to the 50% limitation rather than the 30% limitation.

B. *Ordinary Income Property.*

1. General Rule.

The Code contains a special provision that requires a donor, for purposes of computing the charitable income tax deduction, to reduce the value of any property contributed to a public charity by any gain that would not be taxed as long-term capital gain if the property were sold.[10] This provision limits a dealer or a manufacturer seeking to make a contribution of inventory to a deduction equal to the basis of the property, notwithstanding the

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[7] Prior to the 1986 Act, the required reduction was only 40% of the appreciation (28/46ths in the case of a corporation) because only that amount would have been subject to tax had the property been sold. With the repeal of Section 1202 and elimination of the capital gain deduction, the entire appreciation has become nondeductible.

[8] This rule effectively puts the donor in the same position as he or she would have been in had the property been sold, the tax paid and the proceeds (unreduced by the tax) contributed to the charitable organization.

[9] Reg. § 1.170A-4(b)(3)(ii).

[10] IRC Sections 170(e)(1)(A) and 1221.

fact that the property may have a value to the charity that is greatly in excess of its basis.[11]

If the property contributed is not inventory but represents property received as income by the donor, e.g., books received by a book reviewer in the hope that he will review them, the donor may take a deduction for the fair market value of the property, but that deduction will be "offset" by the inclusion of the property in the donor's income. For example, if a book reviewer donates books that she has received in the hopes that she would review them, she may take a deduction for the value of the books, but will also have to include that value in her income.[12] Including the property in the income of the donor gives it a basis equal to the amount of the inclusion, and it is this basis that the donor is deducting.

2. Works of Art, etc., Created by the Donor.

Works of art, including manuscripts, books, letters and written material that are created by the donor, or acquired by gift (but not by inheritance) by the donor from the person who created them, are ordinary income assets in the hands of the donor. Any gain realized on sale of the property would be taxed to the donor as ordinary income rather than as capital gain.[13] Accordingly, a donor's deduction for a charitable gift of such property is limited to the basis, generally cost, unless the donor has already deducted the cost as a business expense, in which case no deduction is available.[14]

Because their work is treated as ordinary income property, writers and artists cannot deduct the fair market value of any of their work that they contribute to charity. The rationale for this treatment is that since other donors are not allowed to deduct a contribution of their services or the value (in excess of basis) of any inventory, artists and writers should be placed on the same footing; their work is the product of their efforts. While this result may be consistent with the basic rule regarding ordinary income property, it seriously inhibits the ability of museums and libraries to collect works of living artists and writers. Efforts to amend the tax law to permit artists to claim a fair market deduction for gifts of their own work have so far been unsuccessful.

If the artist dies, any such property that passes through his or her estate receives a stepped-up basis[15] and the ordinary income property taint will disappear. Thus, persons who inherit such property from a person whose

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11 See Greer v. Comm'r, 70 T.C. 294 (1978), aff'd, 634 F.2d 1044 (6th Cir. 1981) (donation of race horses to charity treated as gift of inventory on the ground that donor was a dealer in race horses); Holcombe v. Comm'r, 73 T.C. 104 (1979) (donation of eyeglasses to charity by optometrist limited to basis because they represented inventory in the hands of the optometrist). See. also, Williford v. Comm'r. 64 T.C.M. 422 (1992) (personal art collection of art dealer was not a capital asset).

12 IRC § 1221; Rev. Rul. 70-498, 1970-2 C.B. 6 (donation of books sent by publishers hoping for a review by book reviewer); Haverly v. U.S., 513 F.2d 224 (7th Cir. 1975) (donation of textbooks received as samples by high school principal).

13 IRC §§ 170(e)(1)(A) and 1221; Reg. § 1.170A-4(b)(1). See Maniscalco v. Comm'r, 37 T.C.M. 1174 (1978), aff'd, 632 F.2d (6th Cir. 1980) (painting); Sylvester v. Comm'r, 37 T.C.M. 1847-79 (1978) (manuscript); Forrer v. Comm'r, 42 T.C.M. 613 (1981) (royalty agreement); Glen v. Comm'r, 79 T.C. 208 (1982) (tape of interviews made for research); Morrison v. Comm'r, 71 T.C. 683, aff'd, 611 F.2d 98 (5th Cir. 1980) (donation of personal papers by congressman); Chronicle Publishing Co. v. Comm'r, 97 T.C. 445 (1991) (newspaper clipping library). See, also, Priv. Ltr. Rul. 9335017 (sports figure's own autographed photos not capital assets since product of personal services, but trophies and awards won during career are capital assets).

14 See Reg. § 1.170A-1(c)(4); Rev. Rul. 82-9, 1982-1 C.B. 39.

15 See IRC § 1014.

efforts have created it may claim a full fair market value deduction for a charitable gift of the property. The taint remains as to inter vivos gifts in the hands of a donee because the donor's basis is carried over to the donee.[16]

3. Inventions.

The treatment of artists and writers is not consistent with the treatment of inventors, whose patents are treated as capital gain property.[17] This treatment is designed to encourage the inventive spirit by giving the income produced favorable treatment. As a result, gifts of such inventions by an inventor (or a transferee) are treated like gifts of any other capital gain property and are deductible at the full fair market value. This disparity in the deductibility of the contributions is probably unintentional, but it does tend to imply that the tax law favors inventiveness over artistic talent.

C. *Appraisal and Valuation Problems.*

1. Valuation.

Fair market value is the price at which property would change hands between a willing seller and a willing buyer, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts.[18] Relevant factors to be considered in determining the value of property include the cost or selling price within a reasonable time of the gift, comparable sales, reproduction cost under some circumstances, opinion evidence and appraisals.

2. Substantiation Requirements.

The regulations now require any donor claiming a deduction of more than $5,000 for a gift of tangible personal property[19] to obtain a written appraisal from an independent qualified appraiser before the donor files the return on which the deduction is claimed. The donor must furnish the charity with a summary of the appraisal on a Form 8283, have that form acknowledged by the charity, and file a copy of the Form 8283 as acknowledged with his or her return.[20]

3. Gifts of Recently Acquired Property.

Prior to the 1984 Act, the IRS was confronted with rather questionable schemes in which taxpayers (usually at the urging of a promoter who emphasized the tax benefits) acquired a volume of items such as art books, lithographs, gems, bibles, etc., at a "wholesale" price, held the property for slightly more than the long-term holding period and then donated the items to charity, claiming a deduction for each item on the basis of its retail value. The IRS first attacked such schemes by treating the donor as a "dealer" (irrespective of the fact that the donor might never have made a sale) and thus limiting the deduction to the donor's basis.[21]

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[16] See IRC § 1015; IRC § 1221(3)(c).

[17] IRC § 1235.

[18] Reg. § 1.170A-1(c)(2).

[19] Or any property other than securities for which quotations are readily available.

[20] Reg. § 1.170A-13(c).

[21] See, Pasqualini v. Comm'r, 103 T.C. No. 1 (1994) in which the Tax Court held taxpayers were not dealers in greeting cards purchased at auction for purposes of a one-time contribution to charity; See, also, Rev. Rul. 79-419, 1979-2 C.B. 107; Rev Rul. 79-256, 1979-2 C.B. 105; Rev. Rul. 80-329, 1980-2

The dealer theory was a very questionable method to reach a result that was reasonably correct. A much better theory is found in a ruling in which the IRS was confronted with a contribution of an assortment of gems to a museum at a value three times the price at which they were purchased 13 months earlier. That ruling did not attempt to treat the taxpayer as a dealer. Instead, the ruling held that the taxpayer's original purchase price, not "some artificially calculated estimate of value contrary to the prices at which the very gems at issue change hands in the market place," provided the best evidence of fair market value.[22] In a similar ruling, the taxpayer's deduction for a gift of bibles was reduced to reflect the taxpayer's purchase price.[23]

While focussing on the donor's purchase price as the best evidence of value is defensible, it does not take into account the fact that the items may have actually appreciated in value. The Tax Court, supported by various Courts of Appeal, deals with the issue head on, valuing the group of items as a group in the market "in which it is most likely to be sold," normally the wholesale market in which the taxpayer purchased the items.[24]

4. Penalty Provisions.

The penalty provisions have been extensively and frequently revised in recent years. The penalty provisions adopted by the 1989 Act now impose a penalty of 20% of the understatement of tax due to a "substantial understatement" and 40% of the underpayment due to a "gross misstatement" of value.[25] In the context of a charitable contribution, there is a substantial understatement if the amount claimed as a deduction is more than 200 percent of the amount determined to be the correct amount; there is a gross misstatement if the value claimed is 400 percent of the amount determined to be correct.[26] The penalty may be waived only if the donor can show that he or she relied on a "qualified appraisal" and that he or she has made a "good faith investigation" of the value of the contributed property.[27] This provision is aimed at abusive schemes and should not inhibit legitimate donations of properly appraised property, provided the donor carefully selects the appraiser and reviews the appraisal for factual inaccuracies.

In addition, the Code subjects an appraiser who is found to have provided an appraisal knowing that the appraisal will result in an underpayment of tax (i.e., knowing that the valuation is too high) to the $1,000

C.B. 70. See also Sandler v. Comm'r, 52 T.C.M. 563 (1986), in which the Tax Court found that a taxpayer who was not actually in the business of selling gravesites could not be a dealer by virtue of his donations.

22 Rev. Rul. 80-69, 1980-1 C.B. 55.

23 Rev. Rul. 80-233, 1980-2 C.B. 69.

24 See e.g., Anselmo v. Comm'r, 80 T.C. 872 (1983), aff'd, 757 F.2d 1208 (11th Cir. 1985); Skripak v. Comm'r, 84 T.C. 285 (1985) (scholarly books); Chiu v. Comm'r, 84 T.C. 722 (1985) (gemstones and minerals); Lio v. Comm'r, 85 T.C. 56 (1985), aff'd sub nom. Orth v. Comm'r, 813 F.2d 837 (7th Cir. 1987) (lithographs); Ferman v. Comm'r. 68 T.C.M. 1063 (1994) (coins salvaged from shipwreck); Pasqualini v. Comm'r, 68 T.C.M. 89, 103 T.C. No. 1 (1994) (greeting cards). See, also, Klavan v. Comm'r, 66 T.C.M. 68 (1993) and Weiss v. Comm'r, 65 T.C.M. 2768 (1993) (gravesites valued at taxpayer's cost).

25 IRC § 6662.

26 IRC §§ 6662(b)(3), 6662(e), 6662(h).

27 IRC § 6664(c); Treas. Reg. § 1.6664-4(e).

penalty imposed on any person who aids or abets the understatement of tax liability of another.[28] The 1984 Act permits the Internal Revenue Service to ignore appraisals prepared by any appraiser who has been subjected to that penalty.[29]

The 1982 Act had given the Internal Revenue Service additional weapons directed at abusive tax shelters. A civil penalty may be imposed upon the organizers of any plan or arrangement who furnish a false or fraudulent statement with regard to any tax deduction, credit, exclusion or other tax benefit or who furnish a gross overvaluation statement, i.e., one that overstates the correct value of any property or services by 200% of the correct amount.[30] Thus, promoters or appraisers who substantially overstate the value of such items as gems, real estate or closely held stock to assist a donor in obtaining an excessive tax deduction risk penalties of the lesser of $1,000 or 100% of the income derived from the activity.

In addition, the manner of calculating interest on underpayments of tax was changed by the 1986 Act. Effective January 1, 1987, interest is compounded daily on the principál amount plus unpaid interest.[31] The rate is adjusted quarterly based on the average market yield on outstanding marketable obligations of the United States with remaining periods to maturity of three years or less (the "Federal short-term rate") which is then increased by three percentage points to determine the rate paid on underpayments.[32]

D. *Undivided Interests.*

An undivided portion of the donor's entire interest is one of the forms of deductible partial interest. The same basic rules apply to gifts of tangible personal property as to real estate. The charitable donee must have exclusive possession for a portion of each year representing its interest.[33] The donor must bear his or her share of the expense of maintenance but may retain partial enjoyment. Gifts of successive fractional interests may be a useful technique to extend the five-year carryforward period, but such fractional interests may have a value that is less than an allocable portion of the value of the entire property.[34]

E. *Remainder Interests in Tangible Personal Property.*

1. The Confusing Rule of Section 170(a)(3).

The basic rules restricting income, gift and estate tax deductions for gifts of partial interests apply to gifts of partial interests in tangible personal property. Thus, no income, gift or estate tax deductions are available for gifts of remainder interests in tangible personal property unless the remainder interest is in the form of a charitable remainder annuity trust, a charitable remainder unitrust or a pooled income fund.[35]

In addition to these restrictions, Section 170(a)(3) contains a special rule <u>for income tax purposes</u> that provides that no contribution of a future interest in tangible personal property will be considered to be made until the expiration of all intervening noncharitable interests or until all intervening noncharitable interests are no longer

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[28] IRC § 6701.

[29] 1984 Act Section 156.

[30] IRC § 6700, added by 1982 Act Section 320(a). Like the IRC § 6701 penalty, the IRC § 6700 penalty is imposed in addition to any other penalties that may be applicable.

[31] IRC § 6622, added by 1982 Act Section 344(a).

[32] IRC § 6621 and § 6601, amended by the 1986 Act.

[33] Reg. §§ 1.170A-5(a)(2), 1.170A-7(b)(1)(i); Priv. Ltr. Rul. 7728046.

[34] <u>But see</u> <u>William R. Knapp v. Comm'r</u>, 36 T.C.M. 1576 (1977).

[35] IRC §§ 170(f), 2055(e) and 2522(c).

held by the donor or a related person. Section 170(a)(3) was added to the Internal Revenue Code in 1963, well before the Tax Reform Act of 1969, and was intended to prevent donors from taking a deduction for a gift of a remainder interest in tangible personal property as long as the donor or a relative retained the right to possess and enjoy the property. Since the partial interest rules in Section 170(f), adopted by the 1969 Act, also prohibit a deduction for a gift of a remainder interest in tangible personal property (unless the remainder is in a charitable remainder trust or a pooled income fund), it is arguable that Section 170(a)(3) is excess baggage and should have been repealed; however, it was not and continues to create problems.

For example, if a donor contributes a remainder interest in a painting to charity subject to a reserved right to keep the painting for ten years, both Section 170(a)(3) and Section 170(f) prohibit an income tax deduction until the ten year period has expired or the donor relinquishes the right to keep the painting. Furthermore, since the Section 170(f) rules (but not the Section 170(a)(3) rule) are picked up by reference in the estate and gift tax provisions[36], the donor would be subject to gift tax on the value of the future interest contributed to charity because the reserved interest is not in a pooled income fund or charitable remainder trust. If the donor dies within the ten-year period without having relinquished the right to keep the painting, Section 170(f) (but not Section 170(a)(3)) would deny an estate tax deduction for the charity's remainder interest. This is obviously not a desirable form of gift from the donor's standpoint.

However, suppose the donor satisfies the requirements of Section 170(f) by contributing the painting to a charitable remainder trust. In this case, while Section 170(f) would permit an income tax deduction (and by reference, the estate and gift tax deduction), if the donor or a family member is a beneficiary of the trust (and thus, through the trust, holds an "interest in the property") Section 170(a)(3) <u>postpones</u> the income tax deduction until the donor and his family no longer hold any the intervening interest.[37]

Note that Section 170(a)(3), read carefully, does not deny, but merely postpones the deduction. If the trust sells the property to an unrelated person and invests the proceeds in securities, the sale terminates any interest that the beneficiaries of the trust might have in the property. To be sure, the donor or the relatives may, through the vehicle of the charitable remainder trust or pooled income fund, still have an intervening interest in the <u>proceeds</u> of sale of the property, but, as emphasized, the statute speaks in terms of an interest in <u>the property</u>, not the proceeds. Accordingly, the donor should be able to deduct the value of the remainder interest at the time the trust sells the property. This analysis has recently been confirmed in a 1994 private letter ruling which described a gift of a violin to a charitable remainder unitrust with a life income interest reserved by the donor. The donor was permitted to deduct the remainder value in the year in which the violin was sold. The donor's primary objective was the sale of the property by the trust free of tax and reinvestment of proceeds.[38]

When a donor makes a gift of a remainder interest in a personal residence or a farm, no income, gift or estate tax deduction is available for the remainder interest in the household furnishings because they are not considered to be part of the residence or farm and thus do not qualify under the partial interest rules of Section 170(f). Since the donor will continue to live in the residence and use the furnishings, Section 170(a)(3) would also deny the income tax deduction.

2. Charitable Remainder Trusts, Pooled Income Funds and the "Related Use" Rule.

As discussed above, when tangible personal property is given to charity, the deduction is limited to the basis of the property unless the donor can reasonably expect that the charity will use the property to carry out its exempt purpose; this rule is generally known as the "related use" rule. Although a charitable remainder trust is exempt

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[36] IRC §§ 2055(e)(2) and 2522(c)(2).

[37] Reg. § 1.170A-5(b), Example (6).

[38] Priv. Ltr. Rul. 9452026. Because of the related use rule discussed in the next section, the value will be based on the basis of the property.

from tax, it is exempt under Section 664, not Section 501(c)(3), and thus does not have an exempt purpose to which the use of the property can relate. A pooled income fund is not exempt from tax at all.[39] The regulations provide, somewhat cryptically, that the use by a trust of property contributed to the trust for the benefit of a charity is unrelated if the use to which the property is put by the trust is one that would have been unrelated if made by the charitable organization.[40] Since the only way in which a pooled income fund or charitable remainder trust can use property is to sell it, if tangible personal property is given to a charitable remainder trust or a pooled income fund, the deduction for the remainder interest (once the trust or fund sells the property) must be determined with reference to the basis of the property rather than the fair market value, for the trust or pooled income fund does not have an exempt purpose for purposes of applying the "related use" rule.[41]

Thus, even if a painting is given to a pooled income fund maintained by an art museum, since the pooled income fund does not have an exempt purpose, the deduction is limited to the remainder interest in the basis. Although the remainder interest in the painting is, through the mechanism of the pooled income fund, given to the museum, there is no way that the museum can use the painting to carry out its exempt purpose. The only way that the museum can get its hands on the painting (at least as long as the donor is alive) is to buy the painting from the pooled income fund for its full value.

3. Tangible Property and Pooled Income Funds.

Most pooled income funds do not accept gifts of tangible property and for good reason. Tangible personal property does not generally produce income and, since a pooled income fund must produce income for the benefit of all of its income beneficiaries, the property will have to be quickly sold and the proceeds reinvested in order to avoid a dilution of the income interests of the other beneficiaries.[42] Thus, a trustee of a pooled income fund should not accept tangible personal property until the trustee is reasonably sure that the property can be quickly sold for a fair price.

F. *Alternative Minimum Tax - 1991 Exception for Gifts of Tangible Personal Property.*

The 1993 Act repealed the alternative minimum tax preference item for charitable contributions of appreciated property. Prior to this repeal, effective for the period January 1, 1991 through June 30, 1992, gifts of appreciated tangible personal property were not subject to this rule. The 1993 repeal of the general rule was effective for all gifts of appreciated property made after December 31, 1992, but was made specially retroactive for gifts of tangible property after June 30, 1992, thus retroactively filling the gap in the effective dates of the special rule.

G. *Gift Annuity.*

Because the related use rule limits the deduction for a gift of tangible personal property to a charitable remainder trust or a pooled income fund to the value of the remainder interest in the basis of the property, a donor who wishes to fund a reserved income gift with tangible personal property and obtain a deduction based on the full

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[39] A pooled income fund is a fully taxable trust; as long as it does not realize short term gains it will pay no tax because it deducts the income paid out to the beneficiaries and is entitled to a special deduction for long term gains by reason of IRC § 642(c)(5).

[40] Reg. § 1.170A-4(b)(3)(i).

[41] See Reg. § 1.170A-5(b), Example (7). See, also, Priv. Ltr. Rul 9452026, n. 38 above (deduction reduced to basis in remainder interest in violin).

[42] This is less of a problem where the value of the property is small relative to the size of the pooled income fund, but even in this case the trustee of the pooled income fund has a fiduciary duty to sell and reinvest quickly.

fair market value of the property might consider a gift annuity. The special rule of Section 170(a)(3) limiting gifts of future interests does not apply to a gift annuity because the gift constitutes an outright gift of the contributed portion, i.e., a bargain sale. Since the gift element in the bargain sale represents a direct gift to the charity, as long as the charity uses the property to carry out its exempt purpose, the deduction will be based on the full fair market value of the property rather than its basis.

H. *Research and Other Scientific Equipment.*

Ordinarily, if a corporation donates equipment that it has manufactured, the property is treated as ordinary income property, and the deduction is limited to the cost basis of the property. However, under a provision added by the 1981 Act and modified by the 1986 Act,[43] a corporation (other than an S corporation) may claim a deduction for the cost basis plus 50% of the appreciation (but not more than twice the basis) for equipment donated to certain qualified organizations[44] for research or experimentation in the physical or biological sciences in the United States. Under certain circumstances, this provision may cover gifts of computers and related materials. A similar rule is applicable to property contributed by a corporation (other than an S corporation) if the property is used solely for the care of the ill, needy or infants.[45]

I. *Copyrights to Artworks.*

The 1981 Act added a provision that treats an original work of art and its related copyright as separate properties for purposes of the gift and estate tax charitable deductions.[46] Thus, a donor may give an original artwork to a charitable organization while retaining the copyright without subjecting the gift to gift tax (or estate tax where the transfer is made on death). However, no income tax deduction is available for such a gift because, for income tax purposes, it is considered a gift of a nondeductible partial interest.

J. *"Permanent" Loans.*

One method of making a gift of tangible personal property to a museum is to loan the property to the museum either on a "temporary" or "permanent" basis. A temporary loan runs for a definite period; a permanent loan is for an indefinite period. A permanent loan creates a bailment, and the owner of the property may claim it at any time; the statute of limitations does not begin to run against the donor until demand is made for the return of the property.[47] This creates a potential for great confusion in cases where the original donor has died, since it is often impossible to ascertain who the owner really is. To avoid this confusion, many museums have adopted a policy of terminating in the museum's favor all permanent loans that run for more than a set term (e.g., 15 years) unless such loans are renewed.

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[43] IRC § 170(e)(4), amended by 1986 Act Section 231(f).

[44] IRC § 41(e)(6). The list includes institutions of higher education and certain scientific research organizations.

[45] IRC § 170(e)(3). In Tech. Adv. Mem. 8732002, the National Office permitted a deduction under this section for a gift of books and educational material (held as inventory by the donor) to an exempt organization that made the books and materials available to prison inmates on the ground that the prison inmates came within the category of "ill and needy". See, also, Priv. Ltr. Rul. 9321057 in which the IRS approved a program under which a corporation did not give its medical products directly to the needy but to pharmacies who dispensed the products out of their normal stock to the needy who received vouchers from physicians or others identifying the needy.

[46] 1981 Act Section 423, adding IRC § 2055(e)(4) and IRC § 2522(c)(3).

[47] Estate of Therese Davis McCagg, 450 A.2d 414 (D.C. App. 1982) (paintings were loaned to museum in 1917 and the donor died in 1932; the donor's estate did not demand return until 1981).

Since a permanent loan is a gift of the use of the property, it is a partial interest in the property for which no income, gift or estate tax deduction is available.[48] If the permanent loan arrangement does not give the charity any legally enforceable rights vis-à-vis the property, it may be possible to argue that there is no gift of property at all[49] (so as to avoid a gift or estate tax). But that approach is highly questionable in view of the 1984 holding of the Supreme Court that an interest-free demand loan constituted a gift of property that was subject to the gift tax.[50]

II. *GIFTS OF CROPS*

A. *Outright Gifts*

Crops represent income and a charitable gift of growing crops represents an assignment of income. The income realized may be partially or entirely offset by the deduction for the gift. [51]

B. *Gift of Remainder Interest.*

1. Donor may transfer real estate subject to a crop-sharing agreement to a charitable remainder unitrust and the gift will be treated as the gift of a capital asset.[52]

2. Unrelated Business Income.

a. Section 664(c) makes all income of a charitable remainder trust taxable in any year in which it has $1 of unrelated business taxable income.[53]

b. Crop-sharing is a form of rental arrangement whereby the landlord receives payment based on a share of crop income net of allocable expenses. If a gift of land subject to a crop-sharing agreement is made to a charitable remainder trust and the recognition of crop-sharing income causes the trust to recognize UBTI, all income, including capital gain on sale of land, would be taxable at ordinary trust rates (39.6% when the income reaches $7,500).

c. After much litigation, the 7th Circuit has confirmed that a standard crop-sharing agreement is a source of rent, not partnership income and does not cause the exempt recipient to recognize UBTI because the owner does not actively participate in the business of farming.[54]

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48 IRC §§ 170(f), 2522(c) and 2055(e).

49 See Rev. Rul. 70-477, 1970-2 C.B. 62, holding that a gift of the use of property which was not legally enforceable did not constitute a gift of property subject to Section 170.

50 Dickman v. Comm'r, 465 U.S. 330 (1984), reh'g denied, 466 U.S. 945 (1984).

51 Tatum v. Commissioner, 68-2 USTC ¶ 9563 (5th Cir. 1968). Rev. Rul 75-11, 75-1 C.B. 27; G.C.M. 35374, June 22, 1973.

52 Priv. Ltr. Rul. 8415030.

53 See Newhall Unitrust, Wells Fargo Bank v. Commissioner, T.C. No. 10. Docket No. 10195-95 (1995).

54 Harlan E. Moore Charitable Trust v. U.S., 93-2 USTC ¶50, 601 (7th Cir. 1993). The IRS has acquiesced in this decision. 1994-13 I.R.B. 5.

III. *GIFTS OF MINERAL RIGHTS TO CHARITY.*

A. *General Considerations.*

Mineral rights, primarily oil and gas interests, come in many forms: they may be fee interests, leasehold interests, working interests, royalty interests, overriding royalty interests, net profits interests, production payments or any combination of the above. They may be owned directly or through a partnership. Consequently, a gift of an oil and gas interest to a charity involves special considerations.

1. Capital Asset.

In most cases the oil and gas interest will be a capital asset in the hands of the donor, even though (as in the case of an overriding royalty interest or a net profit interest) it may represent a right to the future income from the property. As long as the term of the interest is co-extensive with the underlying working interest, a gift of the interest is treated as a deductible gift of property interest in the oil and gas rather than an anticipatory assignment of income.[55] Where, however, the interest is not co-extensive with the working interest, as is the case with a production payment, a gift of the interest is treated as a nondeductible anticipatory assignment of income.[56] In such a case, the donor would not be entitled to a deduction when the gift was made, would have to include the production payments in income when made to the charity, and would presumably receive a charitable deduction at that time reflecting the fact that the production payment was made directly to the charity.

If the donor is in the oil and gas business, the oil and gas interest may not be a capital asset in his or her hands; if that is the case, a gift of the interest would give rise to a deduction equal to its basis rather than a deduction that is based on its fair market value.[57] Even if the donor is in the oil and gas business, if the interest can be characterized as real property used in a trade or business so as to qualify as Section 1231 property,[58] a gift of the interest may generate a deduction based on fair market value if the donor's Section 1231 gains exceed his or her Section 1231 losses.

2. Donor's Entire Interest.

No deduction is allowed for a gift of a partial interest unless it is an undivided portion of the donor's entire interest.[59] Accordingly, no deduction would be allowed if a fee owner grants a charity a leasehold interest in the oil and gas, if the holder of a leasehold interest grants a charity a working interest or if the holder of a working interest grants a charity an overriding royalty or net profits interest, because in each case the owner has not given the charity all of his or her rights.[60] If however, the donor owns an overriding royalty interest and gives a charity a one-half interest in that royalty interest, the gift is deductible because it represents an undivided fractional interest of all the rights possessed by the donor.

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55 Rev. Rul. 67-118, 1967-1 C.B. 163; Rev. Rul. 73-428, 1973-2 C.B. 303.

56 See G.C.M. 24849, 1946-1 C.B. 66, declared obsolete by Rev. Rul. 70-277, 1970-1 C.B. 280; Wiseman v. Barby, 390 U.S. 339 (1968); Eugene T. Flewellen, 32 T.C. 317 (1959).

57 IRC § 170(e)(1)(A).

58 Rev. Rul. 68-226, 1968-1 C.B. 362.

59 IRC § 170(f)(3).

60 Rev. Rul. 76-331, 1976-2 C.B. 52; Priv. Ltr. Rul. 7726004 (gift of fee interest with retention of mineral rights held to be a nondeductible gift of a partial interest).

3. Ordinary Income Property.

Even if the interest given is a capital asset in the hands of the donor and represents the donor's entire interest, in calculating the deduction the donor will be required to reduce the fair market value by the amount of any ordinary income that the donor would have realized had the interest been sold.[61] In the case of oil and gas properties, the most likely source of ordinary income is the recapture of intangible drilling costs deducted after December 31, 1975.[62] Thus, if on the sale of the interest, the donor would have to recapture the intangible drilling costs as ordinary income, he or she will have to reduce the charitable contribution deduction by the amount of the recapture.[63]

4. Bargain Sale.

A gift of property subject to an indebtedness is taxable as a bargain sale, even if the indebtedness is nonrecourse. The "at risk" rules[64] deny significant tax benefits for oil and gas interests that are financed with indebtedness and thus it is unlikely that an oil and gas interest will be subject to standard indebtedness unless the debtor has personal liability. However, "carved out production payments" are treated as a loan for tax purposes[65] and thus a gift of a working interest (or an overriding royalty interest) from which a production payment has been carved out may be treated as a bargain sale on the ground that the transfer relieves the donor of the liability for the carved out production payments.

5. Valuation.

In calculating the amount of the deduction, one first must determine the fair market value of the oil and gas interest. Since market quotations for such interests are not available, this will require an appraisal by a qualified expert. Assuming that the interest relates to property on which oil or gas has been found and that the property is producing revenue, the operator should be able to furnish the donor with a cash flow projection which indicates the expected cash flow from the property. This is usually a good starting place for evaluating the interest. The future cash flow is first discounted by an appropriate factor to determine its present value; then, depending on the nature of the property, a further discount may be applied to reflect the risk that the projected cash flow may not be realized. Where the interest represents a minority interest in a partnership, a further discount may be required to reflect the minority status, unless there is a mechanism that allows the charity to readily dispose of the donated interest. All charitable gifts in excess of $5,000 except gifts of cash of cash or publicly traded securities must be independently appraised, and the appraisal summary must be attached to the donor's federal income tax returns for the year of the gift.[66]

6. Partnership Interests.

Oil and gas interests are frequently held in the form of an interest in a limited partnership, and in such a case a gift of the interest will involve all of the special considerations with respect to the gift of partnership interests. There are two that deserve special mention:

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[61] IRC §§ 170(f)(3), 170(e)(1)(A).

[62] Rev. Rul. 76-331, 1976-2 C.B. 52; Priv. Ltr. Rul. 7726004 (gift of fee interest with retention of mineral rights held to be a nondeductible gift of a partial interest). IRC § 1254.

[63] Priv. Ltr. Rul. 8004142.

[64] IRC § 465.

[65] IRC § 636(a); Reg. § 1.636-1.

[66] Reg. § 1.170A-13(c).

a. Partnership Indebtedness.

A gift of a partnership interest in property that is subject to an indebtedness requires the partner to treat the gift as if he or she had sold the partnership interest for the amount of the indebtedness.[67] It makes no difference whether or not the partner is personally liable for the partnership liabilities; the rule applies irrespective of whether the indebtedness is nonrecourse.[68]

For example, if we assume a partnership interest with a gross value of $10,000 and a basis of $2,000 to which $4,000 of the partnership liabilities are attributable, a gift of the interest would be treated as though the partner had sold the interest for $4,000 (the amount of the liabilities). Under the bargain sale rules, the gain would be determined by allocating the donor's basis to the amount sold on the basis of the ratio of the "sales proceeds" to the fair market value of the interest as follows:

sales proceeds	$4,000
2,000 (basis) x 4,000/10,000	(800)
taxable gain	$3,200

In this example, the amount of the deduction would be $6,000, the difference between the donor's share of the partnership assets and the amount of his or her share of the partnership liabilities.

Because the "at risk" rules deny tax benefits for oil and gas interests funded with borrowed money,[69] partnership indebtedness is often not a problem in the case of a gift of an oil and gas interest, unless the property is subject to a carved out production payment.

b. Unrealized Receivables

Another factor that must be considered is whether the partnership assets contain any "unrealized receivables" (which includes depreciation and intangible drilling costs subject to recapture as ordinary income) or "substantially appreciated inventory items" which would generate ordinary income to the partner if he or she were to sell the interest. If this is the case, then the amount of the deduction must be reduced by the amount of such items attributable to the portion given.[70] If the gift is treated as a bargain sale (as a result of the existence of liabilities as discussed above), then a portion of the gain may be treated as ordinary income rather than capital gain.

7. Unrelated Business Income.

Before the charity accepts a gift of an oil and gas interest, it will want to determine what income (as opposed to cash flow) is projected for the partnership interest and whether that income will be taxable to the charity. The definition of unrelated business income excludes "all royalties (including overriding royalties) whether measured by production or by gross or taxable income from the property."[71] The regulations expand on the exemption for royalties by providing:

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[67] Crane v. Comm'r, 331 U.S. 1 (1947); IRC Sections 722 and 752.

[68] Rev. Rul. 75-194, 1975-1 C.B. 80.

[69] IRC §§ 465 and 47(d).

[70] IRC §§ 751, 170(e).

[71] IRC § 512(b)(2).

Mineral royalties shall be excluded whether measured by production or by gross or taxable income from the mineral property. However, where an organization owns a working interest in a mineral property, and is not relieved of its share of the development costs by the terms of any agreement with an operator, income received from such interest shall not be excluded.[72]

Accordingly, if the interest transferred to the charity constitutes a working interest in the mineral property, and if the charity is required to bear its share of the development costs by the terms of the agreement with the operator, the income received from the interest will be treated as unrelated business income.

Even if the interest is not a working interest (so that the royalty paid qualifies as a royalty for purposes of Section 512(b)), if the interest is subject to any liability, the income derived from that interest will be treated as "debt-financed income" to the extent of the liability, which means that portion of the income will be treated as unrelated business income.[73]

If the oil and gas interest is held by a mature tax shelter partnership which has "crossed over" so that it is throwing off considerably more income than cash, and if the income thrown off is taxable to the charity, it may not be desirable for the charity to accept the gift if there is a risk that the cash flow will not support the tax liability.

8. Effect of the Transfer on Percentage Depletion

If the oil and gas interest throws off unrelated business income to the charity, the charity may be entitled to a depletion allowance associated with the interest. The Code provides for two methods of calculating the depletion deduction on natural resource property. Cost depletion allows the taxpayer to recover the basis in the property during the productive life of the property.[74] Percentage depletion allows the taxpayer to deduct a percentage of gross income from the property for the taxable year, even if the total deductions taken in previous years exceed the taxpayer's basis.[75] The taxpayer must use whichever method of depletion results in the greater deduction for the taxable year.[76] However, the extent to which a taxpayer may use percentage depletion with respect to oil and gas wells is somewhat limited.[77] In general, percentage depletion is now allowed only for regulated natural gas, natural gas sold under a fixed contract in effect on February 1, 1975, and natural gas from geopressured brine from wells the drilling of which began after September 30, 1978 and before January 1, 1984.[78] Independent producers and royalty owners may also continue to use percentage depletion, to a limited extent. In the case of transfers after October 12, 1990, proven oil and gas property that is otherwise eligible for percentage depletion will not disqualify the property.[79]

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[72] Reg. § 1.512(b)-1(b).

[73] If the debt-financed asset is real estate held by a university pension trust or support organization affiliated with such an organization, Section 514(c)(9) may protect it from UBIT treatment.

[74] IRC § 612.

[75] IRC § 613.

[76] Id.

[77] IRC § 613A.

[78] IRC § 613A(b).

[79] P.L. 101-508, § 1152(a).

B. *Form of the Gift; Use of Oil and Gas Investments in Charitable Lead Trusts.*

In a depressed market for oil and gas interests, the discounts used in valuing an oil and gas interest may result in an appraised fair market value that is considerably below the economic value of the investment to an investor who has the patience and resources to hold the property for a number of years. As such, while the discounts may discourage outright or remainder gifts of oil and gas interests, the same factors may make oil and gas interests an interesting vehicle for a lead trust; where the oil and gas interest represents a sound producing interest with prospects for future growth, the discounts used in valuing the interest help to guarantee that the donor's gift to his or her heirs will grow in value.

1. Realization of Gain and Recapture.

As in the case of an outright gift, a transfer of an oil and gas interest to a lead trust will result in the realization of gain to the extent of any liabilities attributable to the interest. To the extent that there are any intangible drilling costs associated with the interest that are subject to recapture, the realized gain will be taxed as ordinary income. However, in a lead trust one is normally concerned only with a gift or an estate tax deduction, thus the fact that portion of the property given represents ordinary income property (which would cause a reduction of the income tax deduction[80]) is of no consequence.

2. Taxation of the Trust.

a. Jeopardy Investment.

A lead trust in which the value of the lead interest exceeds 60% of the fair market value of the assets transferred to the trust will be subject to all of the private foundation rules.[81] Therefore, an investment in the oil and gas partnership should be scrutinized to determine whether it is an investment that would jeopardize the ability of the trust to carry out its charitable purposes.[82] While the regulations specifically include a working interest in a mineral property as an investment that may jeopardize the charitable purpose of a private foundation, the fact that the interests involved are working interests in oil wells does not necessarily require a conclusion that the investment is one which would jeopardize the carrying out of the trust's charitable purpose.[83]

In determining whether the investment would jeopardize the trust's ability to meet the charitable purpose, the trustee should be entitled to take into account the fact that the partnership interest represents an unleveraged interest in a great number of wells in a very stable and profitable oil field that is not expected to require any further investment to continue the projected income stream. As long as the trustee can demonstrate that this is the sort of investment that would be made by a prudent business person, it would appear that the investment can be defended as one which does not jeopardize the ability of the trust to carry out its charitable purposes.[84]

b. Excess Business Holdings.

A charitable lead trust in which the value of the lead interest exceeds 60% of the fair market value of the

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[80] IRC § 170(e)(1)(A).

[81] IRC §§ 4947(a)(2) and 4947(b)(3).

[82] IRC Section 4944.

[83] Reg. § 53.4944-1(a)(2).

[84] Reg. § 53.4944-1(b)(2)(iii).

property transferred to the trust may not hold any investment that is an excess business holding.[85] An excess business holding is defined as any interest in a business enterprise that, when combined with the interest of the donor and his family (and any other "disqualified person"[86]), exceeds 20% of that enterprise.[87] Thus, if the interest of the lead trust in the oil and gas partnership, when combined with the interest of the donor and his family and any other disqualified person, exceeds 20% of the total partnership, the trust would be required to dispose of a sufficient portion of the interest so as to reduce the combined holdings of the disqualified persons and the trust to 20% of the total enterprise. The trust would have five years from the date of its creation to make the disposition of any such excess business holding that has been contributed to the trust.

c. Unrelated Business Income.

By contributing a partnership interest to a lead trust, the donor makes the trustee of the lead trust a partner in the partnership. As such, the trustee would be deemed to be engaged in the business of the partnership. If the partnership is throwing off income that would be unrelated business income if it were received directly by the charity, and if the unrelated taxable business income must be distributed to the charity to meet the annuity obligation, the ability of the lead trust to deduct a portion of the unrelated business taxable income is limited.[88] In effect, the Code disallows an unlimited charitable deduction for unrelated business income that is distributed by a nonexempt lead trust; as a result, a trust's ability to deduct a distribution is subject to the same limitations applicable to contributions made by individuals.[89] Assuming the distribution is made in cash, this means that no more than 50% of the unrelated business income may be deducted in any year, with a five-year carryforward of the excess deductions.

Since any income accumulated by the trust will be taxable under the rates applicable to trusts generally, the fact that the income generated by the oil and gas interests is considered as unrelated business taxable income is of no consequence to the extent that such income is, in fact, accumulated. The lead trust instrument set forth in the appendices contains a provision that attempts to guarantee that the last income to be distributed will be that portion of the unrelated taxable business income that cannot be deducted by the trust for just this reason.

The Chief Counsel's Office of the Internal Revenue Service believes that the regulations under Section 681 prevent the marshalling provisions from being effective and require that a distribution from a lead trust be deemed to carry out unrelated business income on a pro rata basis.[90] That interpretation of the regulations is questionable and has no support in the statute, so that until and unless the regulations are clarified, it is permissible for a trustee of a lead trust to continue to utilize such a marshalling provision. Thus, the extent to which the disallowance of a deduction for 50% of the unrelated business income (UBI) will cause a problem for the lead trust depends in large part on the amount of the unrelated business income in relation to the amount of the total income of the trust and the amount of the required annuity payments.

Example

Suppose the lead trust is funded with $5,000,000 of property as follows:

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[85] IRC § 4943.

[86] IRC § 4946.

[87] IRC § 4943(c).

[88] IRC § 681.

[89] Reg. § 1.681(a)-2.

[90] G.C.M. 39161 (September 30, 1983).

$1,500,000 oil and gas yielding	$150,000 (all UBI)
500,000 notes yielding	75,000
3,000,000 growth stocks yielding	105,000
total $5,000,000	$330,000

Suppose further that the annuity is set at $300,000. Under the marshalling provisions of the lead trust instrument in the appendices, the $300,000 distribution is deemed to be composed of the following amounts:

dividends	$105,000
interest	75,000
UBI	120,000
total	$300,000

The balance of the UBI ($30,000) will be accumulated by and taxed to the trust. The $105,000 of dividends and the $75,000 of interest distributed are fully deductible by the trust. However, the deduction for the $120,000 of UBI distributed to the charity is subject to a limitation of 50% of the total UBI ($150,000) earned by the trust. Thus, the deduction would be limited to $75,000 even though $120,000 was actually distributed. This means that the trust's taxable income will be $30,000 plus $45,000 or $75,000, rather than $30,000. The excess deduction ($45,000) may be carried forward and deducted in the succeeding five years subject to the same limitation.

If, in year two, the yield on the growth stocks rises to $140,000 while the other yields stay the same, the UBI problem will be ameliorated. In this case the total income of the trust will be:

oil and gas	$150,000
dividends	140,000
interest	75,000
Total	$365,000

The distribution will be deemed to be composed of:

dividends	$140,000
interest	75,000
UBI	85,000
total	$300,000

Here again, the deduction for the $85,000 of UBI is subject to the 50% limit so that the deductible amount is $75,000 with a $10,000 carryforward. (Since the amount that is currently deductible exceeded the 50% limit, none of the carryforward from year one is utilized.) The taxable income of the trust is, therefore, composed of the $65,000 of UBI accumulated by the trust plus the $10,000 of UBI distributed to the charity which cannot be deducted currently.

If, in year three, the growth stock dividends rise again to $175,000, the situation will be even better. Here the trust income will be:

oil & gas	$150,000
dividends	175,000
interest	75,000
total	$400,000

The distribution will be deemed to be composed of the following amounts:

dividends	$175,000
interest	75,000
UBI	50,000
total	$300,000

Here, the $50,000 of UBI distributed is less than 50% of the total UBI and is thus fully deductible. In addition, the trust will be entitled to use $25,000 of the $40,000 deduction carried over from year one as a deduction against its undistributed income, thereby reducing the taxable income from $100,000 to $75,000.

If, in following years, the dividends from the growth stocks stay at the same level (or continue to rise), the problem of limited deductions for the UBI will not recur and the carryforwards will be fully utilized.

Of course, if the dividends on the growth stock do not increase over the amount postulated for year one, or if the UBI increases, the UBI problem will continue year after year and the carryforwards may never be utilized.

d. Depreciation and Depletion.

The trust instrument should be drawn so that depletion and depreciation deductions are allocated to the trust; otherwise, all or a portion of such deductions will follow the income distributed to the charity and will, therefore, be wasted.[91]

[91] See Priv. Ltr. Rul. 8330107 for an interesting use of a common law lead trust funded with an oil and gas interest. In that ruling the taxpayer created a trust that was to last 10 years and one month. The trust instrument required the income to be paid out to charities selected by the taxpayer but required the trustee to maintain a reserve for depletion. The IRS ruled that the trust did not constitute a completed gift of the income interest because the taxpayer had reserved the right to select the charitable beneficiaries, citing Rev. Rul. 77-275, 1977-2 C.B. 346, but held that the trust would receive a deduction under § 642(c) for income paid out to the charities selected by the taxpayer. By requiring the trustee to maintain a reserve for depletion, the taxpayer in effect required the trustee to set aside a portion of the income each year equal to the depletion deduction and to add that to principal. Accordingly, the taxpayer was required to include that amount in income each year under § 677(a)(2) but was also entitled to an offsetting depletion deduction. Most importantly, even though the taxpayer was not deemed to be the owner of the trust under § 671-678, the transfer of the oil and gas property to the trust did not cause a loss of the depletion allowance under § 613A(c)(9) because the taxpayer was entitled to the depletion deduction before and after the transfer.

C. *Gifts of Oil and Gas Interests to Charitable Remainder Trusts.*

While it is technically possible to fund a charitable remainder trust with an oil or gas interest, it is not often done. The discount factors mentioned above, which depress the value of the interest, will also depress the deductible value of the remainder interest. Moreover, while unrelated business income can, with careful planning, be absorbed by a lead trust without undue difficulty, any unrelated business income received by a charitable remainder annuity trust or unitrust will destroy its qualification.[92] Thus, if an oil and gas interest is to be given to a remainder trust, the interest should be carefully analyzed to ensure that it does not involve unrelated business income.

IV. *GIFTS OF INTANGIBLES OTHER THAN STOCKS AND BONDS*

A. *Partnership Interests.*

A contribution of an interest in a partnership to a charity will give rise to a charitable deduction that is based on (but not necessarily equal to) the difference between (a) the donor's share of the fair market value of the assets owned by the partnership, and (b) the donor's share of the liabilities of the partnership (whether recourse or nonrecourse).

Example

> Five years ago Bill Monroe invested $50,000 for a 10% interest in a limited partnership. During the last five years the partnership has thrown off deductible losses to Bill of $35,000, thereby reducing Bill's basis to $15,000. At the present time, the assets of the partnership are worth $800,000 and are subject to nonrecourse debt of $200,000. Bill's 10% interest is, therefore, worth ($800,000 - $200,000) x 10% or $60,000, and, if he were to give the partnership interest to a charity, his deduction would be based on, but not necessarily equal to, that value.

Because a partnership is generally not considered to be an entity separate from the partners who comprise it, it is at least arguable that a partnership interest represents the direct ownership of a portion of each asset owned by the partnership. If this were the case a gift of a partnership interest would represent a gift of an interest in each asset owned by the partnership so that would be a mixed gift of tangible and intangible property. However, while the Internal Revenue Service has never ruled directly on the point,[93] it is generally assumed that a gift of a partnership interest represents a gift of intangible personal property that does not bring into play the special rules regarding gifts of tangible personal property discussed earlier. Nevertheless, charitable contributions of partnership interests present special problems from both a tax and a non-tax standpoint. These include:

1. Suitability.

Is the charity an acceptable partner to the other partners in the venture, and is the investment suitable for the charity? Although the Internal Revenue Service no longer takes the position that it is <u>per se</u> inconsistent with a

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[92] IRC § 664(c).

[93] Although the Service has not directly considered the question of whether a partnership interest is a tangible or intangible asset for charitable contribution purposes, for purposes of the like kind exchange rules in IRC Section 1031, partnership interests are intangible personal property and not eligible for IRC Section 1031 treatment. IRC § 1031(a)(2)(D). <u>See,</u> G.C.M. 39606 (February 27, 1987). Similarly, for IRC § 1033 purposes, investment of the proceeds from an involuntary conversion of real property in partnership interests is not qualified replacement property under IRC § 1033. "A partnership interest in general is a capital asset which is separate and distinct from the underlying firm assets." G.C.M. 39572 (November 18, 1986).

charity's tax exempt status for the charity to act as a general partner, gifts should normally be restricted to limited partnership interests.[94] Not only is it probably undesirable for the charity to assume the unlimited liability and responsibilities accompanying a general partnership interest, in most cases the other partners will not wish to have the charity as a general partner. However, this is not a problem if the partnership is simply a form of co-ownership of real estate, so that a general partnership interest is, in effect, only an undivided interest in real estate.

2. Transfer restrictions.

Does the partnership agreement permit the gift? There are frequently rights of first refusal or other restrictions on transferability that will have to be satisfied before the gift is effective. Some partnership agreements have special restrictions on transfers to tax exempt organizations.

3. Unrelated Business.

Is the partnership engaged in a business that is unrelated to the exempt purpose of the charity?[95] In a partnership situation, each partner is deemed to be engaged in the business conducted by the partnership, at least to the extent of characterizing the nature of the income received by the partner. Thus, if the business conducted by the partnership is unrelated to the exempt purpose of the charity and generates active business income that is not exempt from the unrelated business income tax,[96] the charity's share of the income of the partnership will be taxed as unrelated business income.[97] This is not necessarily a problem as long as the cash distributions from the partnership are sufficient to cover the charity's tax liability. However, if the partnership represents a tax shelter that has reached the "crossover" point where the taxable income is sufficiently greater than the cash distributions (so that the charity's ownership of the interest would require a net cash outlay), it may be inappropriate for the charity to accept the interest unless the underlying assets have a value that significantly exceeds the indebtedness and the charity can readily convert the interest to cash.

In addition, the income from an interest in a publicly traded partnership is treated as income derived from an unrelated trade or business notwithstanding any of the other unrelated business income tax exceptions.[98] Accordingly, in evaluating whether to accept a gift of a partnership interest the charity should determine whether the partnership interest is publicly traded to determine the unrelated business income tax consequences of such a gift.

4. Indebtedness.

Even if the partnership is throwing off passive investment income, does the partnership have indebtedness on its books that will create problems of "unrelated debt-financed income" for the charity? Note the exceptions to the definition of "acquisition indebtedness":[99]

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[94] Priv. Ltr. Ruls. 8342001, 8344099, 8344110.

[95] A general partnership participation by a charitable organization is consistent with its exempt status if the partnership is engaged in activities such as low-income housing or operation of a nursing home. See G.C.Ms. 39005 (June 28, 1983) and 39444 (November 13, 1985).

[96] IRC §512(b) exempts from the unrelated business income tax certain passive investment income such as dividends, interest, rent, royalties or capital gain.

[97] IRC §§511-514.

[98] IRC § 512(c)(2).

[99] IRC § 514(c)(2)(B).

a. For property acquired by bequest or devise on the death of a partner there is no "acquisition indebtedness" if the property is sold by the charity within 10 years.

b. For property acquired by gift there is no acquisition indebtedness if the mortgage has been in place for more than five years at time of gift, and if the donor has owned the contributed property for more than five years at time of gift.

These two exceptions are only applicable in the event that the charity does not assume and agree to pay the indebtedness secured by the mortgage, and if the charity makes no payment for the equity. Thus, if the property is acquired by gift and the donor (or partnership in which the donor is a partner) has increased the mortgage or other indebtedness within the previous five year period, the exception does apply. If, after the charity acquires the partnership interest, the partnership makes payments on the mortgage debt, those payments would be allocated among and attributed to the partners so that again, the exception would not provide protection.

In a rare case, it may be possible for the charity to pay off its share of the indebtedness, obtaining releases from the mortgagee and its co-owners, and avoid having acquisition indebtedness.[100]

Because of the exception for property acquired by bequest, the problem is less likely to arise where the gift is by bequest or devise. Even then, however, the charity will normally wish to sell the interest as quickly as practical, because any indebtedness incurred subsequent to the date of death is not protected.

In the event that the charity retains the partnership interest, it may transfer the interest to a title holding subsidiary to insulate its other assets from the potential partnership liabilities.

Even if the exceptions to the acquisition indebtedness rules do not apply, it may be possible to avoid unrelated business income under Section 514(c)(9). That section, which has been revised frequently since 1980, now permits educational organizations to invest in debt-financed real estate either directly or through controlled tax exempt subsidiaries.

5. Charitable Remainder Trusts.

As discussed earlier, the problem of unrelated business income can be fatal for a charitable remainder trust for if such a trust receives <u>any</u> unrelated business income during a year, <u>all the</u> income received by the trust during that year (including capital gains) is taxable to the trust.[101] This may not be a problem if the trust is paying out all of its income to the beneficiary, but if the income of the trust exceeds the payout, the trust's ownership of the partnership interest will generate unnecessary taxes to the trust. Accordingly, unless there are unusual benefits to be obtained, a partnership interest that throws off unrelated business income is generally not an appropriate asset to be held by a charitable remainder trust. Note that the receipt of unrelated business income by a charitable remainder trust affects its tax exemption only for the year in which the income is received. It has no effect on the donor's deduction for the value of the remainder interest, nor does it affect the tax-exempt status of the trust for any other year.

6. Unfavorable tax consequences.

Are there unexpected and unfavorable income tax consequences to the donor such as:

a. *Recognition of Income Under the Crane*[102] *Principle?* Where a partner's share of

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[100] Rev. Rul. 76-95, 1976-1 C.B. 172.

[101] IRC § 664(c).

[102] <u>Crane v. Comm'r</u>. 331 U.S. 1 (1947).

partnership liabilities exceeds the partner's tax basis in the partnership interest, a charitable gift of the partnership interest will result in a deemed distribution of cash to the donor to the extent of the donor's share of the partnership's liabilities;[103] this will cause a recognition of income, which may be ordinary income or capital gain. This is most likely to occur in real estate partnerships and "mature" tax shelters.

Example

Suppose that the donor in the example under IV. A. above had received $35,000 in deductible losses, thereby reducing his basis to $15,000. His share of the partnership liabilities is 10% of $200,000 or $20,000 so that a gift of his partnership interest would result in a deemed distribution of $5,000 (the excess of his share of the liabilities over his basis) to the donor. This would be taxed to him as ordinary income or capital gain, depending on whether the distribution is deemed to be a distribution of ordinary income or capital gain items.

b. *Unexpected Application of the "Bargain Sale" Rules?* The "bargain sale" rules, illustrated below, may be triggered where there are partnership liabilities. The gift of a partnership interest subject to liabilities creates a deemed distribution as noted in (a) above, and this also brings into play the special bargain sale basis allocation rules.[104] The application of these rules can result in the recognition of gain by the donor even where the special "negative basis" problems discussed in (a) do not exist; and even when the partnership liability is a nonrecourse liability.[105]

Example

If the donor in the example above makes a gift of his interest, he will be deemed to have "sold" his interest in the partnership for an amount equal to the partnership liabilities allocated to his share, i.e., $20,000. Under the bargain sale rules, his basis of $35,000 has to be allocated between the amount sold ($20,000) and the amount given ($60,000) on the basis of the ratio of each to the total fair market value ($80,000). Thus 20/80 of his $35,000 basis or $8,750 is allocated to the amount "sold" so that his bargain sale gain is $20,000 - $8,750 or $11,250. This may be taxed as capital gain or as ordinary income, depending on the nature of the partnership accounts (see (c) below).

c. *Reduction of the Charitable Contribution Deduction Under the "Ordinary Income Rule"?* If a partnership's assets include "unrealized receivables" or "substantially appreciated inventory," a portion of the gain to a partner on the sale of a partnership interest is characterized as ordinary income.[106] This will cause a reduction of any charitable contribution deduction for a gift of the interest under the rules of Section 170(e), which require that the fair market value of any property be reduced by any gain that would not be taxable as long term capital gain if the property were sold. This situation is frequently seen in real estate and tax shelter partnerships, because potential depreciation recapture is treated as an "unrealized receivable."

Example

Suppose that the assets owned by the partnership in the Example above were subject to depreciation recapture of $160,000, of which the donor's share would be 10% or $16,000. As noted in the example above, if the donor contributes his partnership interest to a charity, under

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103 Id.; IRC § 722.

104 IRC § 1011(b).

105 Rev. Rul. 75-194, 1975-1 C.B. 80.

106 IRC §§ 170(e)(1)(A) and 751.

the bargain sale rules the donor will be deemed to realize a gain of $11,250. The depreciation recapture, which is taxed as ordinary income, is allocated between the amount given ($60,000) and the amount realized ($20,000) on the basis of the relative values of each. Thus, 20/80 of the $16,000 depreciation recapture or $4,000 is allocated to the bargain sale so that $4,000 of the $11,250 gain is taxable as ordinary income; the balance is taxable as capital gain. The balance of the depreciation recapture ($16,000 - $4,000 or $12,000) is allocated to the amount contributed ($60,000). Any contribution must be reduced by the amount of ordinary income that would be realized had the property contributed been sold. This means that the $60,000 interest contributed must be reduced by the $12,000 ordinary income element, so that the donor's deductible amount is $48,000.

Note that the bargain sale rule comes into play only where there is a charitable deduction involved. If the recapture amount allocated to the donor in the foregoing example had been $80,000 so that a gift of the partnership interest would have produced no charitable deduction at all, the donor could have allocated all of his basis to the "amount realized," i.e., his share of the partnership liabilities, so that while he would receive no deduction, he at least would not have to recognize income.[107]

d. *Investment Credit Recapture?* If a partner's profit interest in the partnership is reduced below 2/3 of what it was in the year when qualifying property was placed in service, there is a "disposition" of the property by the partner. This may result in the recapture of a proportional amount of credit, if it takes place before the end of the useful life on the basis of which the credit was claimed.[108]

Example

Suppose that, in the year preceding the gift, the partnership had invested in equipment that was five-year recovery property and produced an investment credit of $5,000, of which the donor's share was $500. If the donor gives a charity his 10% interest after the equipment has been in service for a full year (but before it has been in service for two full years), the donor's interest in the partnership will have decreased by more than 2/3 and 80% of the $500 credit or $400 will be recaptured and added to the donor's income tax for the year of the gift.

Because most investment credits were repealed by the 1986 Act effective January 1, 1986, credit recapture will be less significant in the future than it has been. However, the Code still provides tax credits for qualified rehabilitation of buildings and these credits are subject to recapture.[109]

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107 See Estate of Bullard v. Comm'r 87 T.C. 261 (1986), in which the Tax Court invalidated Reg. § 1.170A-4(c) to the extent it seemed to require that in the context of a bargain sale the charitable contribution be reduced by the full amount of the appreciation rather than the portion of the gain allocated to the contributed property. The regulations have since been amended to correct the problem. T.D. 8176, 1988 CCH Federal Tax Reporter ¶ 6405; Federal Register February 24, 1988.

108 Prior to the 1990 Act, Section 47 and Reg. § 1.47-6 contained the recapture rules generally applicable to investment tax credit property dispositions. Recapture rules are now generally incorporated into new Section 50(a) effective for most property placed in service after 1990. The Revenue Reconciliation Act of 1990 changed those sections of the Code dealing with tax credits. Special rules dealing with credit recapture are now governed by IRC § 50 and the regulations thereunder for property placed in service after December 31, 1990. IRC § 47 and Reg. § 1.47-6 are still controlling for credit recapture with respect to property placed in service prior to January 1, 1991.

109 The Rehabilitation Tax Credit is governed by IRC § 47. IRC § 47 combines the relevant rules pertaining to certified historic structures or buildings placed in service prior to 1936 from old IRC § 46 and old IRC § 48. Twenty percent of the qualified rehabilitation expenditures is allowed as a tax credit for certified historic structures. Ten percent of the qualified rehabilitation expenditures is allowed for any qualified rehabilitated building other than a certified historic structure.

e. *Loss of Suspended Passive Losses?* To prevent taxpayers from using losses from passive investments (limited partnerships, S corporations and any other trade or business in which the taxpayer does not "materially" participate in the management), the 1986 Act requires that passive losses may be deducted only against passive income.[110] Passive losses in excess of passive income are suspended and carried forward to future years, where they may be used against passive income; the suspended passive loss relating to a particular activity such as a limited partnership may be offset against any gain realized when that activity is disposed of in a taxable transaction.[111] However, if the interest in the passive investment is given away, the suspended loss is added to the basis of the property in the hands of the donee and is therefore lost forever to the taxpayer.[112] Accordingly, if the donor owns a limited partnership interest with respect to which there is a suspended loss, it is probably inadvisable to give the interest to a charity because the suspended loss will be lost forever.

7. Transfer of the partnership interest to charity at death.

If the donor's share of partnership liabilities exceeds the donor's tax basis in the partnership interest, a charitable gift of a partnership interest to a charity during lifetime would result in a deemed distribution of cash to the donor to the extent of the donor's share of partnership liabilities and would then generate a taxable gain to the donor. On the other hand, a transfer at death will not generate a taxable gain because of the step up in basis that occurs on death.[113]

The basis of a partnership interest in the hands of the decedent's estate (and the decedent's heirs and legatees) is "stepped up" to the fair market value of the interest at the date of death. However, under Section 743 of the Code the basis of partnership property in the hands of the partnership is not automatically adjusted to fair market value as a result of the death of a partner. Thus, the estate or other transferee will generally have a high basis in the partnership interest (so-called "outside basis") that is different from its share of the adjusted basis of partnership assets ("inside basis").

To rectify this situation and equalize the transferee's basis in the partnership interest with the basis of the transferee's share of partnership assets, Sections 743(b) and 754 permit an election by the partnership to adjust inside basis so that it equals outside basis. Such an election is generally advantageous to the transferee; since outside basis will usually be greater than inside basis, an upward adjustment of inside basis will usually be made.

The partnership is not required to make this election and although it has nothing to lose, may find it burdensome from a record-keeping perspective. As long as the partnership is not producing any unrelated trade or business income, any difference between the inside and the outside basis is of no consequence to the charity. If unrelated trade or business income is involved, then assuming a timely election is made, the charity's tax basis for purposes of determining gain on a subsequent sale of partnership assets becomes the estate tax value of the partnership interest.[114] In the event that the partnership is unwilling to make the election or if the partnership assets, even though stepped-up in value, generate phantom income that is taxable though no actual cash is distributed, the charity must be able to dispose of the interest promptly. If the interest cannot quickly be converted into cash, the charity will consider disclaiming the interest if the cash drain of the taxes is not offset by the potential value of the interest.

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110 See generally IRC §469.

111 IRC § 469(g).

112 IRC § 469(j)(6).

113 See Willis, Pennell & Postlewaite, *Partnership Taxation* § 101.09 (3rd edition 1988).

114 See *Ownership of a Partnership Interest by an Estate or Trust: Tax and Other Consideration*. 38 Tax Lawyer No. 1, 33, at 96 (1984).

B. *Copyrights.*

When a gift of a copyright is made, the donor should be careful to ensure that all the rights with respect to the copyright are given to avoid problems with the partial interest rule.[115] Under the 1976 revision to the federal copyright law, the copyright is a property right that is separate and distinct from the work in which the copyright may be embodied.[116] Thus, a transfer of a manuscript or a painting does not constitute a transfer of the copyright in the work unless there is a specific written agreement making it clear that the transfer includes the copyright. Similarly, the transfer of the copyright does not in and of itself constitute a transfer of the work in which the copyright is embodied.

The 1981 Act modified the gift and estate tax law to permit a transfer of a copyright separate from the work of art (or vice versa) so that such transfers do not run afoul of the partial interest rule, but only for gift and estate tax purposes.[117] Thus, an artist can now give a lithograph to the Fogg Museum while retaining the copyright to the lithograph; the artist's retention of the copyright will not cause the gift of the lithograph to be treated as a gift of a partial interest that is subject to the gift tax.

However, the 1981 modification does not apply to the income tax deduction and the Internal Revenue Service takes the position that a gift of a work of art with the copyright retained is a gift of a partial interest that will not qualify for the income tax charitable deduction.[118] Of course, if the donor does not own the copyright, a gift of the artwork will constitute a gift of his or her entire interest, to which the partial interest rule is not applicable.

Conversely, if the donor makes a gift of the copyright but retains the work in which the copyright is embodied, this is a gift of a partial interest that will not generate an income tax deduction unless the material object (e.g., a manuscript) can be shown to have no significant intrinsic value.[119]

Federal copyright law creates a nonassignable right in the author (or a person who inherits the author's interest) to terminate the grant of a copyright[120] that apparently can be exercised even if the author has agreed that he or she will not exercise the right.[121] If the right to terminate the grant of the copyright is held to be an essential part of the copyright itself, so that a grant of the copyright without releasing the right to terminate it is treated as a gift of a partial interest by the Internal Revenue Service, it will be impossible to obtain an income or gift tax deduction for a gift of a copyright. The Internal Revenue Service does not yet appear to have faced this issue; if and when it does, one would hope that the Internal Revenue Service would not apply the partial interest rule, on the ground that the donor is powerless to give away the right to terminate. If the Internal Revenue Service does apply the partial interest rule and is upheld in court, corrective legislation is the only solution. A gift at death may be made free of the termination issue because the termination right disappears at death.

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115 See Smith v. Comm'r 42 T.C.M. 431 (1981).

116 17 U.S.C. § 202.

117 IRC §§ 2522(c)(3) and 2055(e)(4).

118 Reg. § 1.170A-7(b)(1).

119 Priv. Ltr. Rul. 7944030 permits a deduction for a copyright with respect to a book without dealing with the issue of whether the manuscript had to be given as well.

120 17 U.S.C. § 203.

121 17 U.S.C. § 203(a)(3) and (5).

C. *Royalties (Non-mineral).*

A royalty is a payment to the holder of a copyright for the right to use the copyright. To ensure that a gift of the royalty interest is effective to eliminate the royalty payments from the income of the donor, it is important that the donor assign the copyright from which the royalty flows as well as the royalty payments. Failure to do so will cause the transactions to be taxed as an ineffective attempt to assign income without also assigning the source of the income under the doctrine of Lucas v. Earl[122], which renders such assignments ineffective for tax purposes.[123] If the royalties are assigned without the copyright so that the royalties are taxed to the donor, the authors believe the donor should be entitled to an offsetting deduction as the royalties are paid to reflect the fact that the royalties are received by a charity.

D. *Patents.*

A patent may make an ideal subject for a gift to a charity; unlike a work of art or a copyright held by the artist or author, a patent is treated as a capital asset even in the hands of the inventor. As long as the donor disposes of his or her entire interest in the patent, any resulting gain is taxable as a long-term capital gain.[124] Thus, an inventor or other holder of a patent may contribute the patent to a charity and receive a deduction equal to the fair market value of the patent (which would normally be based on the expected royalty payments). Furthermore, the royalty payments would not be subject to tax in the charity's hands because they are specifically exempted from the unrelated business income tax, even if they are based on the income produced by the patent license.[125]

E. *Installment Sale Obligations.*

When property is sold in exchange for notes payable over a number of years, the seller may spread the recognition of gain over the payment period by using the "installment method" of recognizing the gain.[126] Under this method the seller recognizes a portion of the gain as each payment is made equal to the ratio of the payment to the total sales price. While a donor may be tempted to give notes arising from such an installment sale to a

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122 Lucas v. Earl, 281 U.S. 11 (1930).

123 Walter J. Moore v. Comm'r 27 T.C.M. 536 (1968) (author taxed on royalty payments assigned to children where author retained the underlying copyright).

124 IRC § 1235.

125 IRC § 512(b)(2). The taxation of unrelated business income has been under scrutiny by Congress. In September, 1986, House Ways and Means Committee Chairman Dan Rostenkowski asked Rep. J.J. Pickle, Chairman of Ways and Means Oversight Subcommittee, to conduct a review of federal tax treatment of income-producing activities of exempt organizations. The Subcommittee produced discussion options on March 31, 1988 following five days of hearings in 1987. The draft report which has never been endorsed by the Subcommittee would, among other changes, restrict the royalty exception to situations in which the royalty is based on gross income and to tax as unrelated business income any royalty income that is based on the net income of the licensee except with respect to exempt research activities and non-working mineral interests. See Statement by O. Donaldson Chapoton, Deputy Assistant Treasury Secretary for Tax Policy, before Ways and Means Oversight Subcommittee Hearing on the Unrelated Business Income Tax on Exempt Organizations, June 22, 1987, reprinted in the Bureau of National Affairs Daily Executive Report No. 119, June 23, 1987.

126 IRC § 453.

charity in order to avoid the unrecognized gain, such a gift would be treated as a "disposition" of the installment sale obligations that would trigger the immediate recognition of the deferred gain in the hands of the donor.[127]

Example

In 1982 Gretchen sold a parcel of real estate for $20,000 in cash plus a note calling for ten annual installments of $8,000 with annual interest at 10%, a total purchase price of $100,000. If Gretchen's basis is $20,000, the total gain is $80,000. Under the installment method, 20% of the gain (20/100) or $16,000 is recognized in the year of sale. As each payment of $8,000 is made, 8% (8/100) of the gain ($6,400) is recognized. If Gretchen were to give the note to a charity in 1990 when eight of the installments were yet to be paid, and after she had recognized $67,200 of the gain, Gretchen would be entitled to a deduction based on the then fair market value of the note. However, the gift of the note would trigger the immediate recognition of the balance of the gain, $12,800, which represents the gain element of the last two unpaid installments.

F. *Options*.

1. A charitable gift of an option is similar to a pledge, i.e., the donor gratuitously transfers a right or option to acquire an asset at a price substantially below market. The charity either exercises the option directly or sells the option to an independent third party who exercises it at a market price.

2. Rev. Rul 82-197, 1982-2 C.B. 72 stated that a charitable deduction would be allowable at the time the option was exercised, either by the charitable donee or a third party.

3. On exercise of the option, the donor reorganizes income to the extent of the bargain sale price and the charity has proceeds.

4. The option technique is extremely useful when the donor wants to transfer significant value in the form of real estate to a charity without the liability associated at times with a gift of real estate (perhaps having some environmental problem) or wants to transfer S corporation stock without causing loss of "S" status of the corporation the shares of which are contributed.

5. In Priv. Ltr. Rul. 9501004 the IRS held that a transfer of an option to purchase encumbered real estate to a charitable remainder trust would be considered a transfer of a non-qualifying partial interest for which no deduction is allowed for income or gift tax purposes, regardless of whether a charity or another third party exercised the option. The IRS also said that, since no tax deduction is available for the gift to the trust, the trust was merely "a means to take advantage of the exemption from current income tax on the gain from the sale of the property." Thus, the ruling concludes that the trust fails to qualify under Section 664 as a valid charitable remainder trust. This is a very troubling private letter ruling.

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[127] IRC § 453B; Rev. Rul. 55-157, 1955-1 C.B. 293 (gift of installment sale obligation to charity is a disposition that triggers recognition of gain). See also Legg v. Comm'r 496 F.2d 1179, 74-1 USTC ¶ 9464 (9th Cir. 1974), aff'g per curiam 57 T.C. 164 (1971); Rev. Rul. 76-530, 1976-2 C.B. 132 (transfer of installment sale obligation was a disposition that triggered recognition of gain).

FILING AND REPORTING REQUIREMENTS IN STATES THAT REGULATE GIFT ANNUITIES

As Reported by the State Regulations Committee, ACGA

Presented by James B. Potter and Clinton A. Schroeder

Recent Changes

The following listings reflect recent changes in the state regulation of charitable gift annuities (CGAs) as compiled by the State Regulations Committee of the American Council on Gift Annuities and reported to the 22nd Conference on Gift Annuities, May 3-5, 1995, in San Francisco, California.

Arkansas	CGAs now regulated by Insurance Dept. (1993). Permit issued to charities, which must agree to offer rates no higher than the suggested maximum rates of the American Council on Gift Annuities.
Hawaii	Section 431:1-204 of the Hawaii Insurance Law was amended in 1994 to allow certain 501(c)(3) tax exempt organizations to write CGAs if certain conditions are met. Prior to this, only the University of Hawaii qualified to write CGAs. Qualifying organizations must: 1) have conducted business in Hawaii for at least 10 years; 2) have assets in Hawaii of not less than $5 million; 3) maintain separate annuity fund with at least half of the value of the annuity, and 4) file an appropriate statement prescribed by the Department of Commerce and Consumer Affairs on an annual basis.
Indiana	Indiana state law exempts charities from regulation of CGAs as of March, 1994. Senate Bill #146 was signed by the Governor in May, 1994.
Iowa	The Iowa Insurance Commission views CGAs as "securities," but now permits charities to file for an exemption from the category of "securities." The process of filing for a regulatory "exempt status" is much like qualifying for a "permit" in other states.
Maryland	In February, 1994, new rules regulating CGAs were published in the State Register. A hearing was held in June, 1994, and the Maryland Insurance Commissioner requested the ChesaPeake Planned Giving Council to assign five persons to a task force to work with the Insurance Commissioner's staff to arrive at regulations that the non-profits could live with. Work was completed in February, 1995, and new, more non-profit-friendly regulations are due to be published in the State Register sometime before September, 1995. Special wording will be required in the Gift Annuity Agreements advising donors that the State Insurance Fund will not cover CGAs and that the Insurance Commissioner's office does not pass on the efficacy of the charity's gift annuity fund. The types of non-profits that can write CGAs are (continued) still tightly limited by the state insurance statute.
Ohio	Effective July 3, 1993, the Ohio Division of Securities ruled that CGAs are now exempt from registration as securities under Section 1707.20.
Oregon	In 1993, the state legislature expanded the list of qualified charities that can write charitable gift annuities. Section 731.704--7.31.724 expands that list to virtually all educational institutions, hospitals, religious organizations, museums and performing arts groups in business twenty years, and national voluntary health organizations.

Summary of Regulatory Categories

1. **CGAs are <u>regulated</u>. Permit issued/regulated by State Insurance Department (12):**

   AR CA FL HI ME* MD NJ NY ND OR WA WI

2. **State law <u>does not specifically address</u> gift annuities (25):**

   AK AZ CO* CT D.C. ID IL* KA MS MO MT NE NV NH NM NC OK PA RI SD TN TX* VT VA WY

3. **State insurance law specifically <u>exempts</u> CGAs from regulation (10):**

   DE IN KY LA MA MI OH SC UT WV

4. **State interprets CGAs as securities (4):**

   AL GA IA MN

Notes:

ME: Registration is required for institutions belonging to the University of Maine system. Other charities are not mentioned in the statute. The Insurance Department has indicated it will take no enforcement action against other charities issuing CGAs pending resolution by the state legislature.

CO: As of April, 1995, a new law exempting CGAs from regulation has passed the legislature and is awaiting the Governor's signature.

IL: Legislation exempting CGAs from regulation has been introduced to the Illinois legislature and is expected to pass in 1995. It has the support of the Insurance Department.

TX: Legislation exempting CGA's from regulation has been introduced and is expected to pass before the legislature recesses on May 29.

Except when issuing gift annuities in states that specifically exempt them from regulation, contact the appropriate state departments to determine the registration requirements, if any, and comply with those requirements before issuing gift annuities.

Contact Names for Information on Permits for Non-Profits to Issue Gift Annuities

Arkansas: Mr. John Shields, Director
Life and Health Division, Arkansas Insurance Dept.
400 University Tower Bldg., 1123 South University Ave., Little Rock, AR 72204
Tel: (501) 686-2900

California: Ms. Karen Miller, Legal Division
State of California Department of Insurance
45 Fremont Street, San Francisco, CA 94105
Tel: (415) 904-5688

Florida:	Ms. Jackie Marston, Insurance Specialist Florida Insurance Commission 200 East Gaines St., Tallahassee, FL 32399-0327 Tel: (904) 922-3153, ext. 2574
Hawaii	Mr. Gordon Ito, Legal Department, Insurance Division, Department of Commerce and Consumer Affairs P.O. Box 3614, Honolulu, HI 96811-3614 Tel: (808) 586-2790
Maine:	Mr. Thomas Record, Counsel Bureau of Insurance, State of Maine Tel: (207) 582-8702
Maryland:	Mr. Howard Max, Chief Administrator Life and Health Division, Maryland Department of Insurance 501 St. Paul Place, 7th Floor S., Baltimore, MD 21202-2272 Tel: (502) 564-4553 Fax: (502) 564-6090
New Jersey	Ms. Nancy Hritz Life and Health Division, New Jersey Department of Insurance 20 West State St. -- 11th floor -- CN 325, Trenton, NJ 08625 Tel: (609) 984-2420 Fax: (609) 777-0019
New York	Mr. Robert Ginnelly, Esq., Office of General Counsel New York State Dept. of Insurance Agency Building 1, Empire State Plaza, Albany, NY 12257 Tel: (518) 474-4553) Fax: (518) 473-4600
North Dakota	Mr. Glenn Pomeroy, Commissioner of Insurance State of North Dakota 600 East Boulevard, Bismarck, ND 58504-0255 Tel: (701) 224-2440
Oregon	Ms. Diane Koenig, Administrative Specialist Department of Insurance and Finance, Insurance Division 440-4 Labor and Industries Building, Salem, OR 97310 Tel: (503) 378-4271 Fax: (503) 378-4351
Washington	Mr. James E. Tomkins, Asst. Deputy Commissioner for Company Supervision Office of the State Insurance Commissioner P.O. Box 40255, Olympia, WA 98504-0255 Tel: (206) 664-8055
Wisconsin	Mr. Robert Walker, Senior Insurance Examiner Office of the Commissioner of Insurance 121 East Wilson Street, P.O.Box 7873, Madison, WI 53707 Tel: (608) 267-2239

STATE REGULATIONS COMMITTEE
of the American Council on Gift Annuities

East:	James B. Potter (Chair), Planned Giving Consultant Planned Giving Resources P.O. Box 6930 Falls Church, VA 22040-6930 Tel: (703) 533-0033 Fax: (703) 533-7446
South:	Col. Joseph B. Matthews The Salvation Army P.O. Box 269 Alexandria, VA 22313 Tel: (703) 684-5507 Fax: (703) 684-3478
Midwest:	Elizabeth A. S. Brown, Esq., Legal Counsel Moody Bible Institute 820 North LaSalle Drive Chicago, IL 60610 Tel: (312) 329-4000 Fax: (312) 329-4328
West:	Richard A. James, Esq., Legal Counsel Loma Linda University Loma Linda, CA 92354 Tel: (714) 824-4522

State Regulations Committee
Committee on Gift Annuities
2401 Cedar Springs
Dallas, TX 75201

Incomplete Listing Showing
Data Available as of 5-03-95

Summary Data for States that Regulate Charitable Gift Annuities *

Line	Column: / States:	(a) AR	(b) CA	(c) FL	(d) HI	(e) ME	(f) MD
1	No. of Years of Operations	5	10	5	10 *	5	10
2	Section of Insurance Code	23-63-201 (d)	11520- 11524	67.481	431:I-204		487
3	Must be Exempt Under 501(c)3	Yes	Yes	Yes	Yes	Yes	Yes
4	Segregated Fund	Yes	Yes	Yes	Yes	Yes	Yes
5	Annuity Issuing Organizations Restricted to						Education, Relig. Some Hospitals Located in state
6	Gifts Prohibited						
7	Minimum Reserve Required Fund	Yes	Yes	Yes	Yes	Yes	Yes
8	Special Wording Must be written into Agreement (Note Key below)	(1)	(1) (2) (3)	(1)	(1)	(1)	(1)
9	Charity Must File-- Rates:		Yes	Yes	Yes	Yes	Yes
	Form of Agmts:		Yes	Yes	Yes	Yes	Yes
10	File Annual Rpt	Yes	Yes	Yes	Yes	Yes	Yes
11	Permit Needed	Yes	Yes	Yes	Yes	Yes	Yes
12	State Issues "Certificate of"	Special Permit	Authority	Special Permit	Special Permit	"Authority"	Special Permit
13	Initial File Fee	None	$2,883	None	None	None	None
	Annual Fee	None	$ 58	None	None	None	None
	New Agmt Fee		$15 or less				
14	Mortality Table/Reserves Interest Rates	1983"a" Same as NY	1983"a" 6 % (6)	Rev. Ruling 72-438 + 25% (or) Same as NY	1983"a" Same as NY (or) 6%		1983"a" Same as NY (or 6%)
15	Reserves Reduced by Reinsurance	Yes	Yes	Yes		Yes	Yes
16	Effective Date:	07-93		10-01-93	1994	07-01-92	
	States:	AR	CA	FL	HI	KY	MD

Notes: * States that permit charitable gift annuities with annual reporting to State Insurance Commissioner.
(1) Value of property transferred; Amount of periodic payments; Manner & intervals of payment.
(2) Age of Annuitant(s) shown. (3) Commensurate/Reasonable Value of Annuity must be shown.
(4) Agreements must be numbered. (5) Corrective action required if age or sex is wrong.
(6) Effective with gifts made 1-1-92. (1950-1991 gifts use 1937 SAT @ 2.5%.)

 Please send updates to: James B. Potter, Planned Giving Resources, Box 6930, Falls Church, VA 22040

State Regulations Committee
Committee on Gift Annuities
2401 Cedar Springs
Dallas, TX 75201

Incomplete Listing Showing
Data Available as of 5-03-95

Summary Data for States that Regulate Charitable Gift Annuities *

Line	Column:	(g)	(h)	(i)	(j)	(k)	(l)
	States:	NJ	NY	ND	OR	WA	WI
1	No. of Years of Operations	10	10		20	3	10
2	Section of Insurance Code	17B:17-13.1	1110	26.1-34.1	731.704-731.724	48.38	615.03-615.15
3	Must be Exempt Under 501(c)3	Yes	Yes	Yes	Yes	Yes	Yes
4	Segregated Fund	Yes	Yes	Yes	Yes	Yes	Yes
5	Annuity Issuing Organizations Restricted to				Types of Charities List expanded in 1991		
6	Gifts Prohibited		Real Estate				
7	Minimum Reserve Required Fund	Yes	Yes	Yes	Yes	Yes	Yes
8	Special Wording Must be written into Agreement (Note Key below)	(1)	(1)	(1) (3)	(1) (2) (3)	(1) (2) (3) (4) (5)	(1)
9	Charity Must File-- Rates: / Form of Agmts:		Yes / Yes	Yes / Yes	Yes / Yes	Yes / Yes	Yes / Yes
10	File Annual Rpt	Yes	Yes	Yes	Yes	Yes	Yes
11	Permit Needed	Yes	Yes	Yes	Yes	Yes	Yes
12	State Issues "Certificate of"	Special Permit	Special Permit	Exemption	Authority	Exemption	Authority
13	Initial File Fee / Annual Fee / New Agmt Fee	None / None	None / None	$ 100	$ 250 / $ 50	$ 25 / $ 25 / $ 5	$ 200 / $ 50
14	Mortality Table/Reserves Interest Rates	1983"a" Same as NY (or) 6.0 %	1983"a" Changes annually		1937 SAT 2.5 %	1971 IAM 6.0 %	1971 IAM 7.5 %
15	Reserves Reduced by Reinsurance	Yes	Over $100,000 by "Treaty Agmt"				Yes
16	Effective Date:			07-01-91			
	States:	NJ	NY	ND	OR	WA	WI

Notes: * States that permit charitable gift annuities with annual reporting to State Insurance Commissioner.
(1) Value of property transferred; Amount of periodic payments; Manner & intervals of payment.
(2) Age of Annuitant(s) shown. (3) Commensurate/Reasonable Value of Annuity must be shown.
(4) Agreements must be numbered. (5) Corrective action required if age or sex is wrong.
(6) Effective with gifts made 1-1-92. (1950-1991 gifts use 1937 SAT @ 2.5%.)

 Please send updates to: James B. Potter, Planned Giving Resources, Box 6930, Falls Church, VA 22040

MATERIALS AND TECHNIQUES THAT APPEAL TO YOUR MARKETS

Presented by Ronald E. Sapp
The Johns Hopkins Institutions

The subject at hand is often part of the agenda for the conferences we attend because we all seek prospects. To have prospects we must put in place, sustain and continuously refresh a prospect development program. Prospects do not walk in the door of their own accord. We must make that happen.

The lifeblood of every successful business is prospecting and the same is true of fund raising. Without processes to develop prospects, a charity will not succeed in its quest for financial support. Successful prospecting requires a high level of priority, a considerable allocation of time and requires several marketing approaches. I plan to discuss two of these approaches in this presentation. They are directed at a typical constituency. Part of the constituency consists of future donors that are quite visible and you will plan your moves accordingly. The rest of the constituency is invisible so you need to develop ways to cause these prospects to reveal themselves. Today's discussion will focus on this invisible portion of the prospect pool made up of attractive "yet to be prospects". These are people you don't know but want to connect with.

One of our objectives today is to talk about "materials" and to do this I plan to review an array of materials developed over the past thirteen years. These materials take the form of direct mail as well as indirect mail. By that I mean information that is incorporated in on-going communications such as newsletters. These materials, used in a broad based manner, reaching out to an entire constituency, or key segments of it, are intended to cause an individual to self identify.

A second objective is to talk about "techniques" to reach our prospects. I plan to talk about a technique that I think is an essential part of marketing- working through others who can bring us new opportunities. These "centers of influence" as they are sometimes called, may be volunteers or colleagues in our own organization that we work with every day. They are people we can motivate and, more importantly, train to uncover new opportunities.

I. The Case for Training and Motivating Our Colleagues

A. What will it achieve?

1. More prospects resulting in more gifts from individuals.
2. Less time qualifying new suspects and prospects.

B. What will it require?

1. High priority status.
2. A considerable segment of available time.
3. Development of a variety of training materials.
4. A long term approach.

II. Who Should Be Trained?

A. Anyone who can help fundraising efforts, but primarily those persons in contact with potential donors.

1. Development staff
2. Executive officers
3. Trustees / Board members
4. Volunteers
5. Alumni Relations staff

B. Not to be overlooked:

1. Financial staff
2. Administrative staff
3. Personnel staff
4. Faculty
5. Library staff
6. Curators
7. Real estate officers

III. Development Professionals

A. Do they know what they are doing?

1. Generally, yes -- "People, People"
2. Good at what they do:
   a. Prospect identification
   b. Cultivation
   c. Follow-up
   d. Event planning
   e. Peer identification / networking
   f. Stewardship
3. Generally speaking:
   a. Effective at bringing prospects to a point of wanting to help -- establishing "charitable intent."
   b. They are "Move Managers."
4. Dilemma follows accomplishment of all the right moves.
   a. How can the prospect give?
   b. Many fundraisers lack the skills to recognize the ways of giving. What - when - how.
   c. Confidence in discussing financial things is often lacking. Caused by lack of financial knowledge.
   d. Fundraisers are out there to raise money, yet there is often a reluctance to talk "MONEY" (fear of the dreaded "M" word).

B. What do they know?

1. Often what they know (knowledge and skills) is based on some earlier career before fundraising.

   For example:

   - *Social Work*
   - *Advertising*
   - *College Admissions*
   - *Political Campaign staffer*
   - *Nurse*
   - *Homemaker/Volunteer*
   - *Military Career*
   - *Family Retailer*
   - *Industrial Sales*
   - *Public Relations*

2. Most fundraisers come into the profession without background or experience in finance or business. For this reason, a base of financial knowledge is often lacking among professionals in the fundraising business.

   a. Most fundraisers do not need the financial knowledge considered necessary to be a planned giving professional. What is needed is a level below -- a more basic level of knowledge.

   b. Often lacking is the basic level of knowledge that allows a fundraiser to comfortably and confidently take a prospect beyond the level of wanting to give and begin to discuss **how** to give.

   c. This void may often cause a fundraiser to miss or fail to recognize an opportunity.

IV. The Training Program

A. Preface to the program

1. Philanthropy First -- Wanting to give comes before how to give. Charitable gift planning deals with *how* gifts are made.
2. Financial knowledge
   a. Is of great personal value
   b. Is of great professional value
   c. Can be self taught
   d. Learning resources are abundant

B. The Keystone Concept

Components of every gift are: an asset, a method of transferring the asset, and a time frame which may differ for the donor and the donee.

V. The Building Blocks

A. Income tax form 1040

1. Adjusted gross income
2. Taxable income
3. Types of income

4. Schedule A deductions
5. Substantiating deductions, Form 8283
6. Tax rates

B. Financial jargon
1. Cost basis
2. Fair market value
3. Capital gain / loss
4. Dow Jones Industrial Average
5. Bull market
6. Bear market
7. Economic indicators

C. Contribution limits
1. Contribution base
2. 50% / 30% limits
3. Related use
4. Carry over

D. Exercises using tax tables, jargon and limits
1. Sale
2. Cash gifts -- outright
3. Securities / Real Estate / Personal Property (related use) / Personal Property (unrelated use)

E. More building blocks
1. Time value of money
2. Rule of 72 & 113

F. Life income gifts -- CONCEPTS
1. Gifts of securities -- Outright
2. Gifts of real estate -- Outright
3. Life income gift benefits -- Generic
4. Gifts of securities -- Life income
5. Gifts of real estate -- Life income

G. Life income gifts -- FEATURES
1. Pooled income funds
2. Charitable gift annuities
3. Remainder trusts

H. Handling securities
1. <u>Wall Street Journal</u>
2. Stock certificate

3. Stock transfer
4. Stock power
5. How to transfer
6. Marketing brochure
    a. Annual Fund
    b. Gift clubs
7. Closely held corporate stock
    a. Flow chart
        (1) Donor not corporation gift
        (2) Cash sources
    b. Effect on company ownership

I. Gifts of real estate
    1. Overview
        a. Outright
        b. Bargain sale
        c. Life income
        d. Life interest
        e. Life interest / Life income combined
        f. Undivided fractional interest
        g. Bequest
    2. Real estate gift examples
        a. Outright and life income
        b. Life interest -- Age factor
        c. Combination of life interest and gift annuity
        d. Partial interest -- Income property

J. Noncash gifts
    1. Substantiation procedures
    2. Form 8283 & Form 8282

K. Deed of gift
    1. Personal property
    2. Real estate -- Gift purpose
    3. Cash gifts

L. When is a gift a gift?
    1. Year end / date of gift
    2. Remainder trust transactions
    3. Securities
    4. Real estate
    5. Personal property
        a. Delivery

b. Registration

M. Wills
1. Terms and features defined
2. Types of bequests
3. Sample language
4. Estate taxes
   a. Estate tax rates
   b. Estate tax calculations
5. Contract to make a will

N. Trusts
1. Features and terms
2. Serving as trustee

O. Charitable remainder trusts
1. Trustee / remainderman, etc.
2. Taxation of income
3. Annuity trust
4. Unitrust / variations
5. Comparison
6. Instruments
7. Revenue Procedures

P. Pooled income funds
1. Instruments
2. Plain English description
3. Investment objectives
4. Case history -- performance
5. Revenue Procedures

Q. Gift annuities
1. The American Council on Gift Annuities
2. Instruments
3. Plain English description
4. Standardization
5. PG Calc examples
6. Deferred annuities
7. State requirements

R. Time value gifts
1. Zero coupon bonds
   a. Plain English description

b. Rates
c. Short term gift plans
2. Life insurance
a. A legacy gift
b. Insurance theory
c. Cash value
d. Policy types -- Value
e. High cash value examples
f. Wealth replacement

S. Lead trusts
1. Description -- Grantor and non-grantor
2. Benefits
3. Donor application

T. Tax Sheltered Retirement Funds
1. Required distributions at age 70½
2. Income in Respect of a Decedent (IRD)

U. Marketing Plan
1. Advertising
2. Indirect mail
3. Direct mail

This leads us to the second part of my presentation in which we will look at a collection of materials that were developed to attract the attention of our constituency. They include advertising and printed infomercials.

The objective of all of this material is to make people aware of the possibilities; to cause people to explore the ways planned giving could bring together their objectives, based on their circumstances. These materials are designed to create opportunities. You will see them in color and on screen. They were not all created at the beginning. They evolved over time. We made mistakes, corrected and learned as we went along. The message here is not that you should do as I have done. We must all work within our own resources and our own constituency. The lesson here is that we must communicate in a succinct and recognizable format over time, and, most importantly, we have to speak the language of our prospects.

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AN OUTRIGHT GIFT OF CASH

Tax Bracket	31%
Cash Gift	$10,000
Charitable Deduction	$10,000
Tax Saving (31%)	$ 3,100
Cost of $10,000 Gift	$6,900

Tax Bracket	36%
Cash Gift	$10,000
Tax Saving (36%)	$ 3,600
Cost of $10,000 Gift	$ 6,400

Tax Bracket	39.6%
Cash Gift	$10,000
Tax Saving (39.6%)	$ 3,960
Cost of $10,000 Gift	$ 6,040

Outright Gift of Appreciated Assets

	Securities	Real Estate
Current Value	10,000	100,000
Original Cost	2,000	20,000
Capital Gain	8,000	80,000
Income Tax Deduction	10,000	100,000
Tax Saving (31% Tax Rate)	3,100	31,000
Capital Gain Tax Avoided (28% Tax Rate)	2,240	22,400
Total Tax Savings	5,340	53,400
Cost of Gift	4,660	46,600
Benefit to Charity	10,000	100,000

Life Income Gift Plans

- Income for Life to the Donor and/or another Beneficiary

- Federal Income Tax Deduction for a Portion of the Gift Value

- Elimination or Reduction of Capital Gains Tax if the Gift is Made with Appreciated Securities or Real Estate

- Remainder of the Gift goes to Charity at the Death of the Last Beneficiary

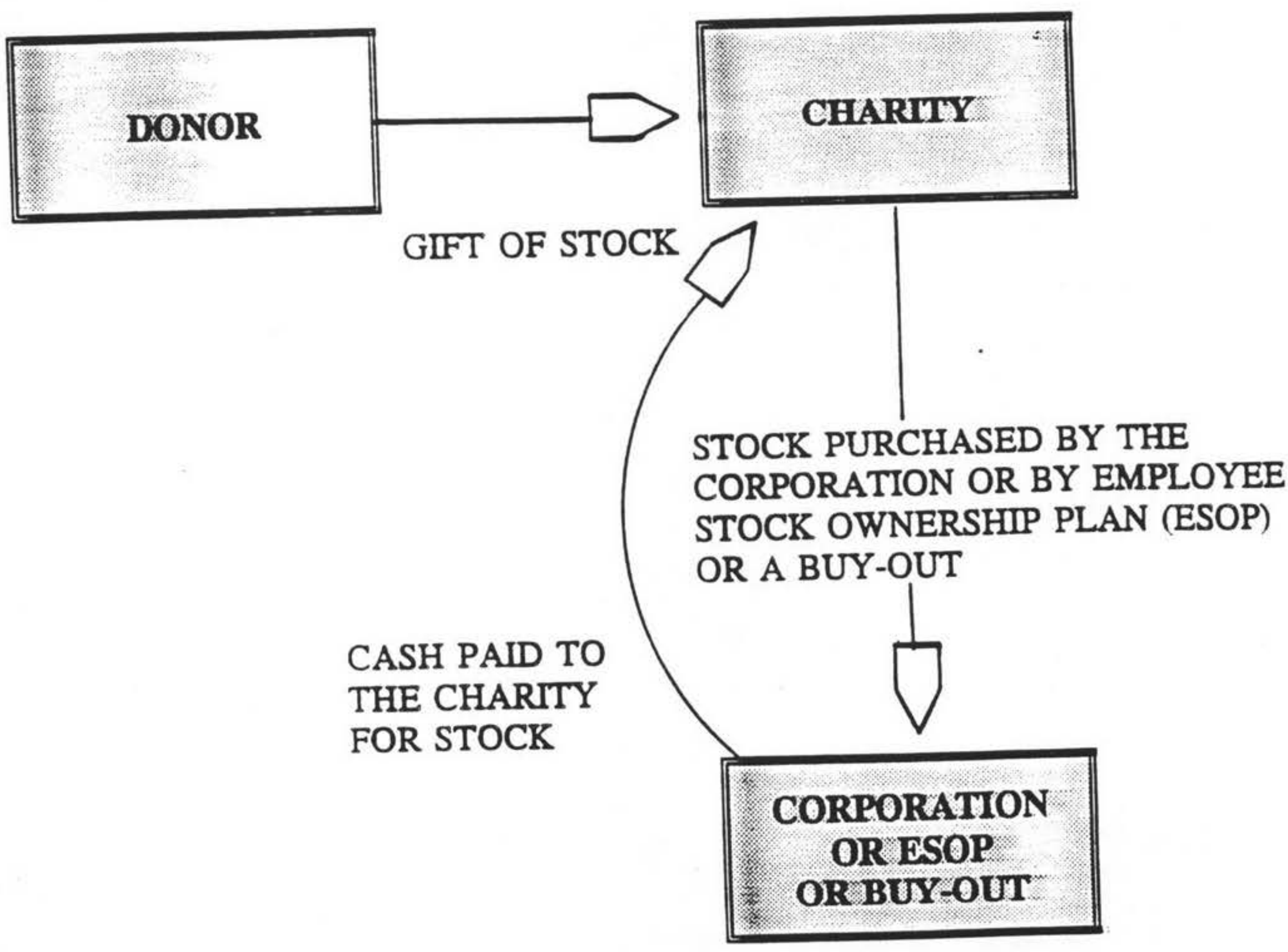
GIFT OF CLOSELY HELD C-CORPORATION STOCK

DESCRIPTION:

When a donor makes a gift to a charity of stock in a closely held C-Corporation, they are entitled to receive a charitable income tax deduction for the appraised value of the stock. The stock is held by the charity and can be subsequently redeemed for cash in one of three ways. One method is to sell the stock to the corporation in exchange for corporate cash. The stock is then retired. The second method is to sell the stock to the corporation's Employee Stock Ownership Plan (ESOP) if such a plan exists. The third method is to sell the stock at the time of a buy-out.

This type of gift arrangement is beneficial in several ways. It allows the donor to make a personal gift which provides a charitable income tax deduction without realizing capital gains tax on the appreciated value of the stock. It also allows the corporation to use a potentially taxable cash surplus for philanthropic purposes.

EXAMPLE:



REAL ESTATE PRELIMINARY INFORMATION FORM

DONOR INFORMATION:

NAME(S) ______________________ PHONE ______________________

ADDRESS ____

AFFILIATION ____

PROPERTY INFORMATION:

TYPE OF PROPERTY ____

ADDRESS OF PROPERTY ____

____

ACCESS INSTRUCTIONS ____

TITLE HELD BY ____

OWNER'S INTEREST __________ ENCUMBERED __________ DEBT AMOUNT __________

OWNER'S VALUE ______________ SOURCE ______________________

LAND VALUE ______________ IMPROVEMENT VALUE ______________ AGE __________

DATE ACQUIRED ______________ ADJUSTED COST BASIS ______________

SITE VISIT ______________ PHOTOS ______________________

IS PROPERTY FOR SALE OR BEEN FOR SALE RECENTLY? ______________________

REAL ESTATE AGENT ____

CURRENT PROPERTY EXPENSES: TAXES ______________ INSURANCE ______________

UTILITIES ______________ MAINTENANCE ______________ OTHER ______________

PAST USES: RESIDENTIAL __________ INDUSTRIAL __________ FARM ______________

IF RENTED, GROSS INCOME ______________ OPERATING EXPENSE ______________

RESTRICTIONS: WETLANDS __________ COVENANTS __________ ZONING ______________

ENVIRONMENT/BIOHAZARD CONDITIONS: CONTAMINATION ________ LEAD PAINT ________
ASBESTOS ________

METHOD OF GIFT:

OUTRIGHT ________ PARTIAL INTEREST ________ BARGAIN SALE ______________

LIFE ESTATE ________ TRUST ________ GIFT ANNUITY ________ OTHER ______________

BIRTH DATE OF BENEFICIARIES:

#1 ______________ #2 ______________ #3 ______________

DATE ______________

REAL ESTATE WORKSHEET

	A. SALE BY OWNER	B. LIFE INCOME PLAN	C. OUTRIGHT GIFT
1. Fair Market Value			
2. Selling Price			
3. Closing Costs (3%)			
4. Commissions (7%)			
5. Total Selling Costs			
6. Proceeds of Sale			
7. Cost Basis			
8. Capital Gain			
9. Tax on Capital Gain			
10. Net Proceeds			
11. Charitable Tax Deduction			
12. Tax Savings			
13. Income from Invested Net Proceeds (5%)			
14. Income from Invested Tax Savings (5%)			
15. Total Income			

UNIFIED GIFT AND ESTATE TAX RATE SCHEDULE				
Taxable Estate From:	To:	Tentative Tax	+ %	Of Excess Over
$ 0	$ 10,000	$ 0	18	$ 0
10,000	20,000	1,800	20	10,000
20,000	40,000	3,800	22	20,000
40,000	60,000	8,200	24	40,000
60,000	80,000	13,000	26	60,000
80,000	100,000	18,200	28	80,000
100,000	150,000	23,800	30	100,000
150,000	250,000	38,800	32	150,000
250,000	500,000	70,800	34	250,000
500,000	750,000	155,800	37	500,000
750,000	1,000,000	248,300	39	750,000
1,000,000	1,250,000	345,800	41	1,000,000
1,250,000	1,500,000	448,300	43	1,250,000
1,500,000	2,000,000	555,800	45	1,500,000
2,000,000	2,500,000	780,800	49	2,000,000
2,500,000 and over		1,025,800	55	2,500,000

60% Phantom Bracket

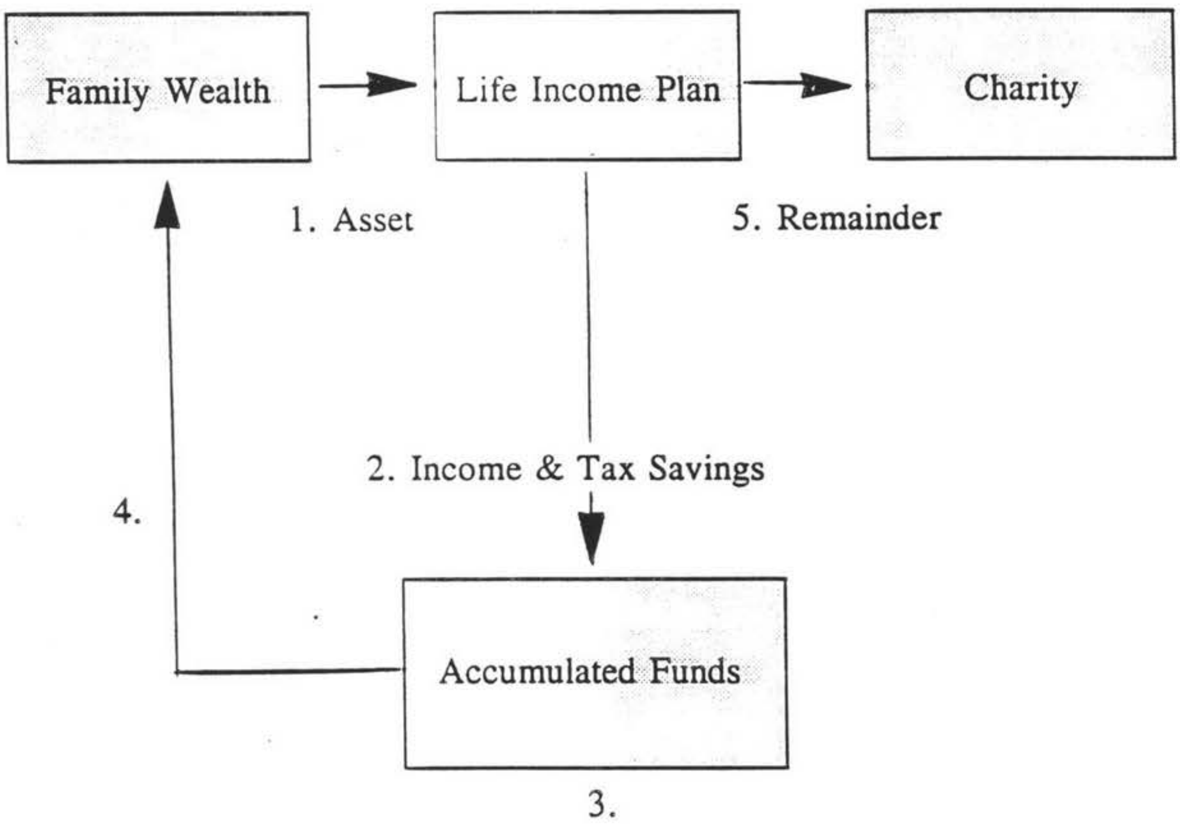
In addition to the above rates, there is a 5% surcharge that applies to taxable estates between $10 million and $21,040,000. The effect of the phantom bracket is to deny those estates the use of the graduated tax rates and the benefit of the $192,800 credit. By applying a 60% rate in the phaseout range, the effect is to hit estates valued at $21,040,000 and above at a flat 55%.

ESTATE TAX CALCULATION			
	Example 1	Example 2	Example 3
Gross Estate			
Less Probate and Settlement Costs			
Adjusted Gross Estate			
Less Estate Tax Marital Deduction			
Less Estate Charitable Deduction			
Taxable Estate			
Tentative Tax on Taxable Base			
Less: Unified Estate Tax Credit*			
Estate Tax			

*** The unified gift and estate tax credit is $192,800 which is equivalent to an exemption of $600,000 (portion of estate not subject to tax).**

WEALTH REPLACEMENT

Wealth replacement is a financial planning method which seeks to replace, within a donor's estate, the value of an asset contributed to charity. Income tax savings and/or life income payments provide funds which the donor accumulates through investment or the purchase of life insurance. The accumulated funds are passed to heirs at the time of the donor's death.



1. Asset donated to Life Income Plan.
2. Donor receive Income and Tax Savings.
3. Income and tax savings are accumulated
4. At death, heirs receive accumulated funds.
5. Charity receives remainder.

HELTER YOURSELF

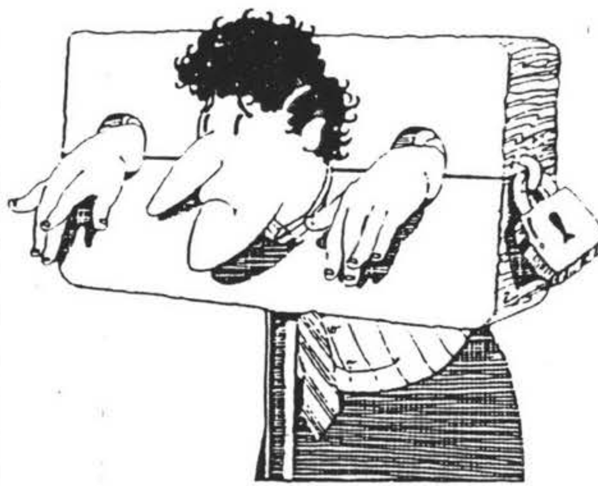
Tired of April tax showers?
helter yourself—give a gift to Johns Hopkins and njoy special tax benefits. You'll receive a charitable ncome tax deduction and in addition, you can enjoy ncome

- that is partially tax-free
- that you can receive now or defer until later
- that is designated for you or a loved one.

nterested? Please contact:

Ron Sapp, Director, or
Gary Owens, Associate Director
Office of Planned Giving
The Johns Hopkins Institutions
3400 North Charles Street
Baltimore, MD 21218
Baltimore: 338-7954
Elsewhere: 1-800-JHU-1268

LOCKED INTO YOUR STOCKS?



Are you locked into appreciated securities you can't afford to sell? We can help!

Put your appreciated stock in a Hopkins life income plan and enjoy

- income for life for you or someone else
- an immediate charitable income tax deduction
- avoidance of capital gains taxes
- probable reduction of estate taxes

Interested? Please contact:

Ron Sapp or John Kudless
Office of Planned Giving
The Johns Hopkins Institutions
Garland Hall
3400 North Charles Street
Baltimore, Maryland 21218
(301) 338-7954

THE ICING ON YOUR RETIREMENT CAKE

A recipe for enhancing your retirement income:

First, put the layers in place (pension plan, social security, IRA, etc.). Then, ice the cake with a Hopkins gift plan, which can give you income taxed at a favorable rate—income you can receive now or later. And, you get an immediate income tax charitable deduction as well!

Interested? Please contact:

Ron Sapp, Director, or
John Kudless, Associate Director
Office of Planned Giving
The Johns Hopkins Institutions
3400 North Charles Street
Baltimore, Maryland 21218
(301) 338-7954

TAKE THE BULL BY THE HORNS

Has a bullish market caught you on the horns of a dilemma? Do you have appreciated stock you can't afford to sell because of today's higher capital gains tax rate?

Take matters into your own hands. Put your stock into a Hopkins life income gift plan and enjoy:

- **income for life for you and/or someone else**
- **an immediate income tax deduction**
- **avoidance of capital gains taxes, and**
- **satisfaction, by providing for the future of Johns Hopkins**

Let us help you take hold of your financial future. Call or write:

Ron Sapp, Director, or
John Kudless, Associate Director
Office of Planned Giving
The Johns Hopkins Institutions
3400 North Charles Street
Baltimore, Maryland 21218
(301) 338-7954

IS YOUR FAMILY FISCALLY FIT?

You have watched your family grow and along the way your investments have grown as well. But they won't be worth much to your family if you haven't secured them in a will.

Even if you feel fiscally fit, a check-up may be in order. Draw up your will now. And after safeguarding your family's future, ask yourself:

- Does your will provide for charities you value?
- Do you need language that will help you provide for Johns Hopkins?

Interested? Please contact:

Ron Sapp, Director, or
Gary Owens, Associate Director
Office of Planned Giving
The Johns Hopkins Institutions
3400 North Charles Street
Baltimore, MD 21218
Baltimore: 338-7954
Elsewhere: 1-800-JHU-1268

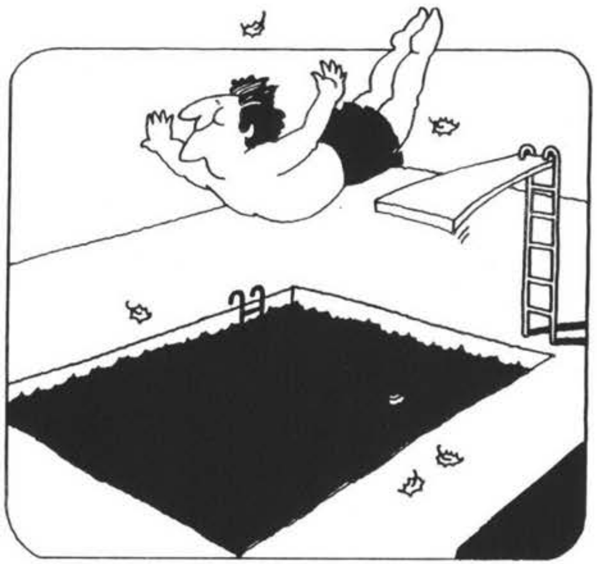
IS YOUR VACATION HOME ALL WORK AND NO PLAY?

Your vacation home can seem like more of a burden than a joy, what with the cost of up-keep, travel, repairs, and taxes.

Maybe it's time to consider an alternative that can help you and Johns Hopkins. Ask how you can donate real estate and get immediate tax savings, avoidance of capital gains tax and the option of income for you or someone you love. Please contact:

Ron Sapp, Director or
Gary Owens, Associate Director
Office of Planned Giving
The Johns Hopkins Institutions
3400 North Charles Street
Baltimore, Maryland 21218
(301) 338-7954

Pool Your Resources



Johns Hopkins Pooled Income Funds
Example of a Gift of $10,000

Life Income Beneficiaries	Income Tax Deduction	Capital Gains Tax	Approximate Rate of Return
One beneficiary, age 55			
Balanced	$ 2,500	-0-	6.0% / $600
High Yield	$ 2,080	-0-	8.0% / $800
Two beneficiaries, age 65 and age 62			
Balanced	$ 2,320	-0-	6.0%
High Yield	$ 1,860	-0-	8.0%
One beneficiary, age 75			
Balanced	$ 5,270	-0-	6.0%
High Yield	$ 4,810	-0-	8.0%

Savvy investors and donors like Dr. Beatrice Aitchison, profiled in this issue, have found the Johns Hopkins Pooled Income Funds a personally beneficial way to make a gift to the University.

Hopkins offers two Pooled Income Funds. The balanced fund benefits donors interested in both income and capital growth over the long term. It currently yields about 6%. The high yield fund is for donors more interested in an immediate high yield and currently pays about 8%.

Both Pooled Income Funds operate similarly to mutual funds. An irrevocable gift of at least $5,000 is combined with those of other donors in a common investment pool managed and operated by Johns Hopkins. Income earned by the fund is paid to the donors in proportion to their respective share of the pool's assets. Either fund pays the donor (and another beneficiary, if desired) a variable rate of income for life. Gifts to a pooled income fund provide an immediate income tax deduction for a portion of the value contributed.

Gifts to the Pooled Income Funds may be made using cash or appreciated securities. By giving appreciated securities, donors avoid paying the capital gains tax that would be due if they sold the property themselves.

The table depicts current expected yields of each of the Pooled Income Funds, based on gifts of $10,000, with varying numbers and ages of beneficiaries.

If you would like to find out more about giving to Johns Hopkins through its Pooled Income Funds or other life income arrangements, please call or write: Ron Sapp, Director of Planned Giving, 210 Garland Hall, The Johns Hopkins University, Baltimore MD 21218; (410) 516-7954 or 1-800-JHU-1268.

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Real Estate:
Turning It From A Burden Into A Source Of Income

When nursing alumna and former faculty member Ruth Dale Ogilby recently gave her one-acre waterfront home on the Chesapeake Bay to the School of Nursing, the primary motivation behind her gift was philanthropic. But making the gift has made life easier for her as well.

"The house was getting a little much for me," says Ogilby, who no longer has to worry about its upkeep. The charitable remainder trust she created will generate income that will help to cover her fees at a retirement community. The gift will also allow her to take an income tax charitable deduction and avoid tax on the capital gain.

You may discover, as Ruth Ogilby has, that a gift of real estate makes sense in a lot of ways, especially if you no longer need or use the property; maintenance costs have become burdensome; or you want to reduce your taxes and supplement your income.

Ruth Dale Ogilby (right) at a recent nursing alumni event with Nancy and Emory Bogardi.

An Example

A 65-year-old alumnus and his wife have a vacation home that is burdening them with the cost of upkeep and taxes. Since their children are not interested in the property, they donate it to Hopkins. The property is placed in trust with Johns Hopkins to be sold, and the proceeds invested to provide income to the donors for their lifetimes.

Assumptions	
Current Value	$150,000
Original Cost	$ 40,000
Annual Upkeep Expenses	$ 7,000
Age of Both Donors	65
Donors' Annual Income	$ 70,000
Donors' Tax Bracket	28%

Life Income Gift Plan Benefits	
Annual Income (6%)	$ 9,000
Capital Gains Tax Avoided (at 33% rate)	$ 36,300
Income Tax Deduction	$ 47,180
Tax Savings	$ 13,210

By making the gift, the donors eliminate $7,000 in annual expenses, increase their annual income by $9,000, receive tax savings of $13,210 and completely avoid capital gains tax of $36,300 at the time of transfer.

Almost any kind of real estate can make a valuable gift to

Johns Hopkins: a primary residence, vacation home, farm, commercial building, or an undeveloped parcel of land. There are many ways to give, depending upon your individual financial needs and philanthropic goals. The Johns Hopkins staff can help you determine the most appropriate method of giving real estate for you.

If you would like to discuss how your real estate can work for you and Johns Hopkins, please call Ron Sapp, Director, or Gary Owens, Associate Director, Office of Planned Giving, at (301) 338-7954, or 1-800-JHU-1268

The Hopkins Planner

A newsletter on financial, estate, and gift planning

I • N • S • I • D • E

YEAR-END PLANNING CUSTOM FIT FOR 1994

TAX RATES FOR 1994

PERENNIAL STRATEGIES

PLAN NOW FOR BEST RESULTS

PLANNING RETIREMENT DISTRIBUTIONS FROM QUALIFIED RETIREMENT PLANS AND IRAS

Planning—1994 and Beyond

All of us here at The Johns Hopkins Office of Planned Giving have frequent opportunities to talk with many of our readers about matters of mutual interest. In recent months we have noticed an increased interest in two subjects that we believe deserve attention in this newsletter. One is the impact of 1993 tax legislation on 1994 income and taxes. In response to questions and concerns that have come from readers on this subject, this issue provides information on year-end financial planning.

The second area of reader interest is fast becoming an important financial issue: contending with the IRS rules and requirements that apply to IRAs and other qualified retirement plans. In this issue we have reprinted information on this subject taken from a recent workshop conducted on campus as part of the education and training program for the Johns Hopkins development staff.

We hope you will find these two articles informative and useful. If you have questions, need information, or would like to discuss an idea, please feel welcome to write to us or call our toll-free number. We look forward to hearing from you.

Sincerely,

Ron Sapp

Ronald E. Sapp
Director
Office of Planned Giving

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TRENDS IN PLANNED GIVING

Presented by Robert F. Sharpe, Jr.

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Fax (901) 761-4268

TRENDS IN PLANNED GIVING

I. Introduction.

A. The "Golden Age" of planned giving.

1. Changes in society are resulting in unprecedented interest in planned giving.

a. Aging of America.

b. Changing political climate.

c. Changing family structures.

2. Planned giving is now the fastest growing source of income for many organizations.

3. Greater interest among "allied professionals."

4. Greater interest among regulators.

B. Greater emphasis on costs and benefits of planned giving.

1. More resources being directed toward planned giving.

2. Greater involvement of financial professionals and regulators.

3. Greater volatility in financial markets.

C. New ways of planning gifts.

1. New uses for old plans.

2. Emergence of "blended" gifts.

3. Working with nontraditional market segments.

D. Changes in way planned gift development efforts are managed.

1. A number of models are emerging.

2. One size does not fit all.

3. Different organizations doing planned giving in different ways.

4. Fewer independent "planned giving" programs.

5. Much more sophisticated and targeted marketing approaches.

II. Changes in the Environment Leading to Increased Role for Planned Giving.

A. Aging of America's population.

1. Donor population becoming older.

2. Younger persons not yet "taking up the slack" for most.

3. Greater awareness of coming wealth transfer.

a. Estimates growing like topsy.

b. Don't raise expectation levels too high.

c. Authors of study that projects $11 Trillion transfer also estimate it will be 115,000,000 bequests of $95,000 each over the next 45 years. "Fine print" reveals that the authors do not account for taxes and costs of dying.

B. Changes in structure of society.

1. Increased longevity means longer period of retirement.

2. Surviving spouses living longer.

3. More responsibility for eldercare among younger persons.

4. High divorce rates.

5. More childless couples.

6. More two earner families among baby boomers.

7. Increases in marriages with children from previous marriages.

8. Children dependent for longer periods of time.

C. Result is change in the way people approach estate and financial planning.

1. More emphasis on probate avoidance means fewer assets passed by will.

2. Marital deduction planning taking on a greater role for the wealthy.

3. Tax apportionment issues will be critical.

4. More planning revolving around retirement plan assets.

5. Greater emphasis on planning for long-term management of assets.

6. Parents will increasingly focus on their own economic security.

7. Charitable planning will assume greater role for many.

8. Irrevocable gift plans will become attractive for reasons other than tax planning.

D. Changing political attitudes.

1. Some are seeking a shift away from government responsibility for social services and cultural amenities.

2. Greater emphasis on self-reliance.

3. Re-emergence of respect for and dependence on entrepreneurs in our society.

4. Less support for high tax rates and offsetting deductions as a way to "centrally plan" economy. Marketing based on tax planning may be less effective in the future. A degree of certainty is necessary to motivate in this way.

5. Result may be greater role for the non-profit sector of economy.

E. Interest among financial professionals flows with capital.

1. Began with 1986 tax act.

2. "Last game in town" for tax avoidance.

3. Lower investment returns and proposed reductions in capital gains taxes may lead to waning and or suspension of interest.

   a. Economic trends now leading to proposals for trusts that may last for forty, fifty years or longer in order to make plans "work" most effectively for donors.

   b. Culture clash occurring when those in for profit sector don't understand the need for a "profit margin" of 70% or more when that is not the norm in their industries.

4. Allied professionals can move on to other planning tools if economics dictate this, while nonprofits can't afford to suspend their efforts.

   a. Even if interest among planners wanes somewhat, a great deal of residual knowledge will remain.

   b. Working with advisors will be easier for a generation of development professionals.

F. With more activity has come greater interest among regulators.

1. IRS beginning to give greater scrutiny to certain types of planned gifts.

2. Recent pronouncements have begun to move away from "laissez-faire" approach.

   a. IRS disallows "flip trusts" in PLR #9506016.

   b. IRS says no to funding trusts with options in PLR #9501004..

   c. In notice 94-78, IRS announces it will apply doctrine of substance over form where they deem it appropriate.

3. More states attempting to impose insurance regulations on gift annuities.

4. Securities regulators are paying closer attention to pooled income funds and gift annuities in some states.

5. State banking regulators question whether charities have trust powers.

6. Courts are being asked by plaintiffs to apply antitrust law to attempts to regulate gift annuity rates.

   a. But ACGA rates may be required as maximums by some states.

   b. Argument backfires as the rates are required to assure that a gift is made and that we are not marketing insurance.

7. Greater regulation may be natural result of a shift in focus by some planned giving programs and financial "fallout" from the 1980s.

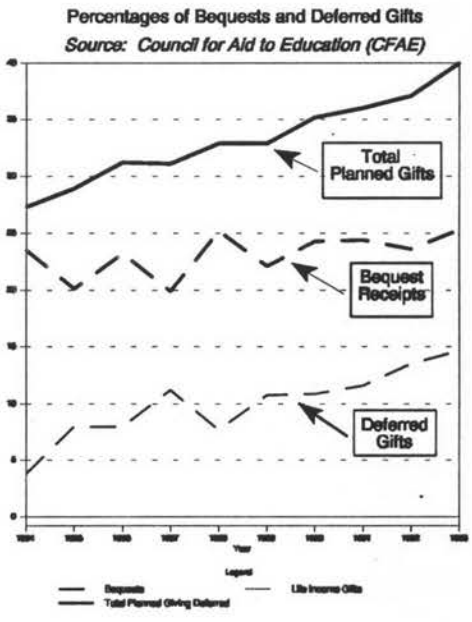
   a. Some programs have aggressively and publicly marketed planned gifts primarily as investment products with only tangential charitable benefits.

   b. Others have perhaps overemphasized the gift element and motivation at the expense of donor's personal concerns.

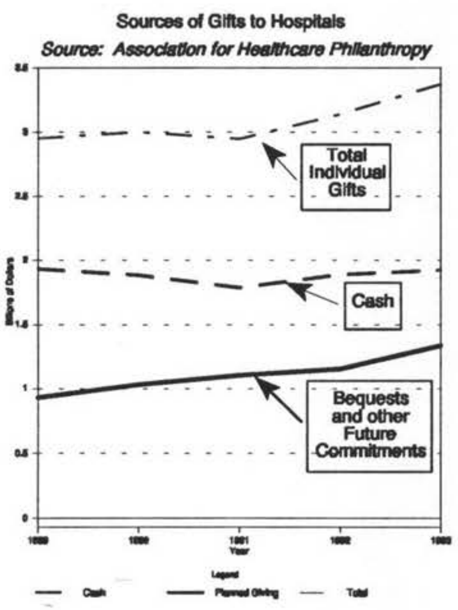
   c. One solution is to return the focus on the gift element of planned gifts while recognizing and giving proper place to the personal economic security of donors.

III. Charities Remain Interested Because of Unprecedented Income From Planned Gifts.

A. Trends in education.

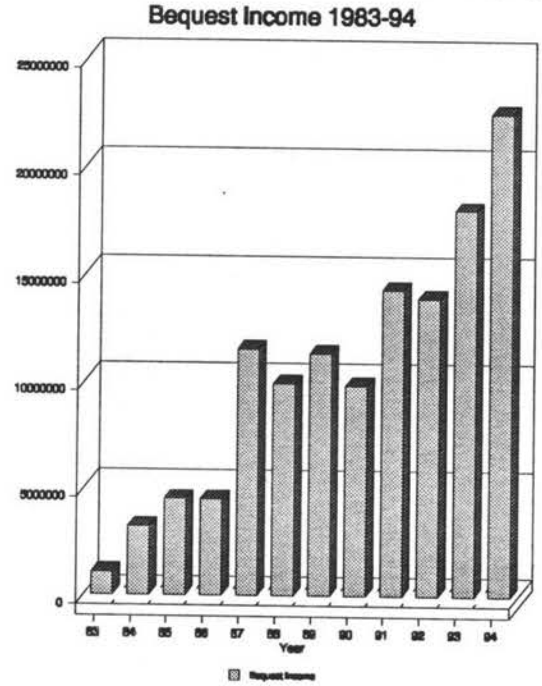


B. Trend in healthcare.

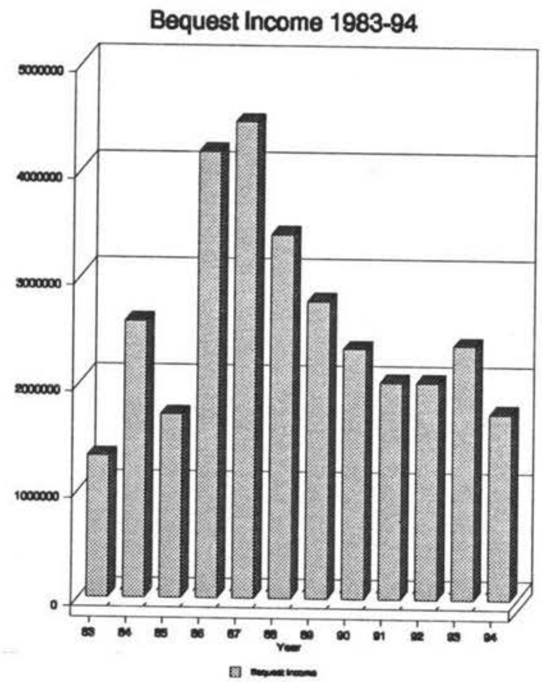


C. Positive results are not universal and some are now exploring reasons.

1. Some programs experiencing long-term double digit growth rates.



2. Others see income stagnating.



3. Result is greater scrutiny on programs thought not to be keeping pace.

D. Greater attention being paid to cost effectiveness of planned gift development efforts.

1. Focus on effectiveness of staff as most visible cost element.

a. Less tendency to add staff in anticipation of production.

(1) Increased salaries have made staff additions more costly.

(2) Many programs are adding staff only after growth occurs that "justifies" it.

b. Many successful programs have started programs with less labor intensive approaches until production justified expense of additional staff.

2. More emphasis on containing costs of program within an acceptable percentage of the expected value of gifts.

a. Economic volatility has had an impact.

(1) Fluctuation in interest rates have wreaked havoc on projections as higher returns result in lower present values of gifts.

(2) Relatively low growth in equity markets

(3) Some gifts are not "performing" as planned.

(a) "Buildup" not occurring.

(b) "Wealth" not "replacing."

b. More programs are putting policies in place that feature "firewalls" to protect against gifts based on over optimistic projections.

(1) Greater attention to minimum ages.

(2) Greater attention to minimum gift sizes.

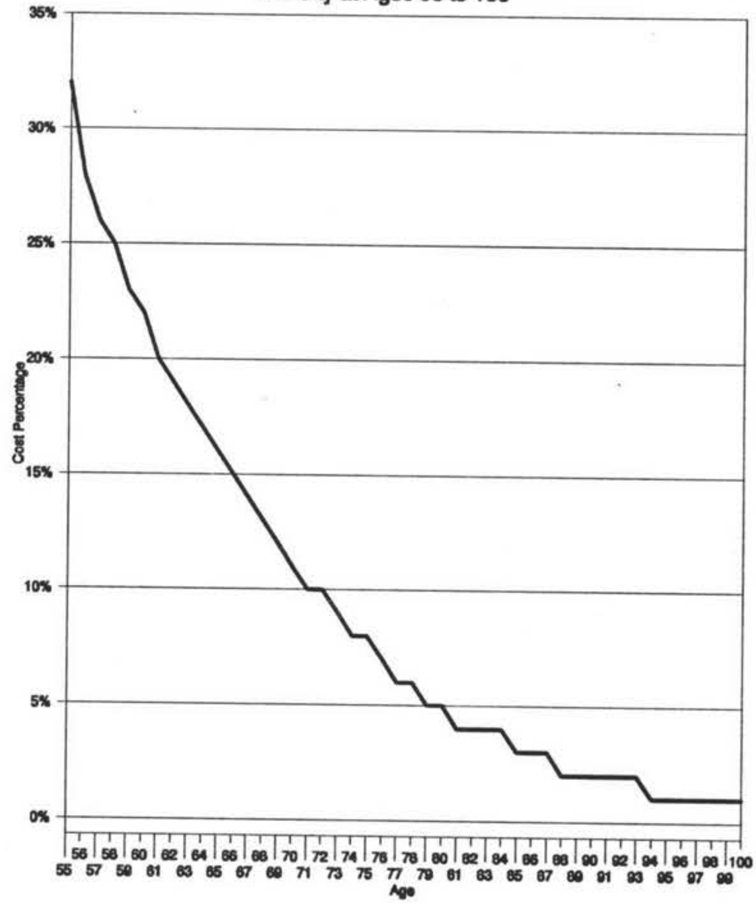
(3) Greater attention to maximum payout rates for various gifts.

3. Example:

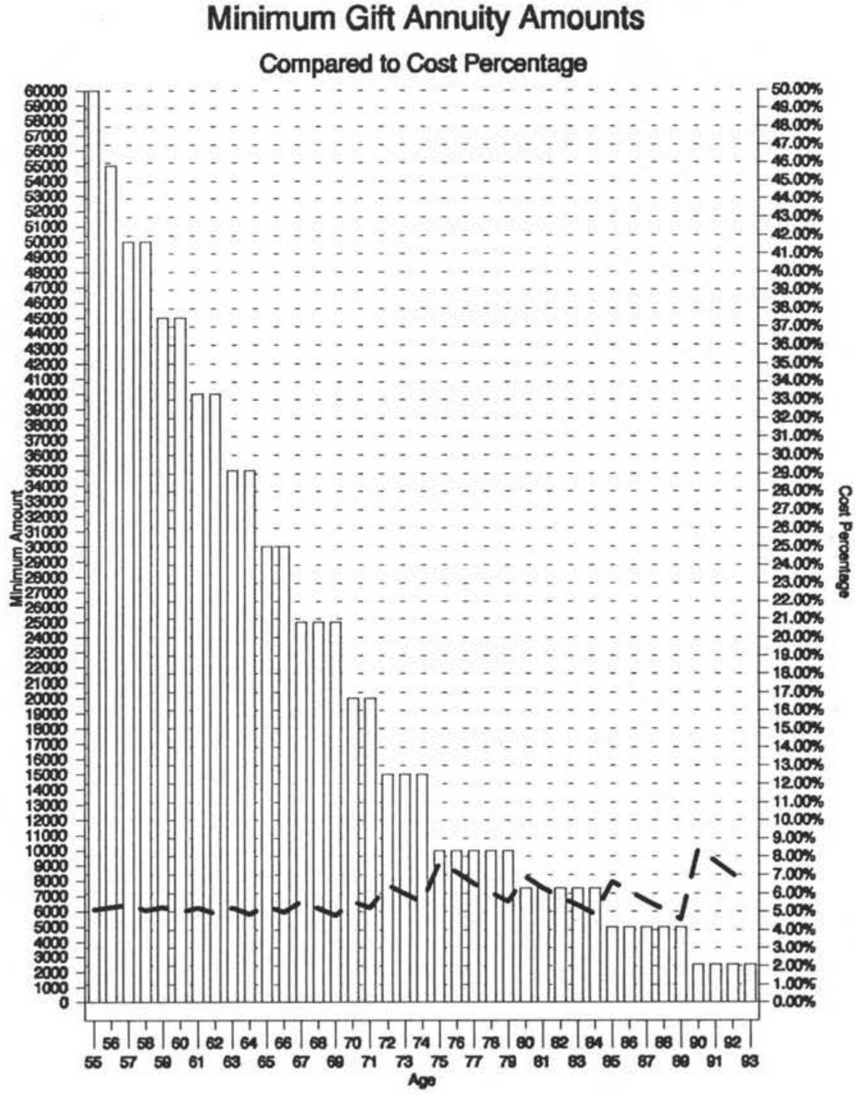
Some programs have set minimum gift annuity amounts based on what others may be doing and other factors not related to their individual cost structure. In doing so they may be experiencing costs far beyond what the ACGA rates anticipate.

Cost Percentages for $10,000 Gift

Annuity at Ages 55 to 100



When examining the costs based on expected number of years of payment and other factors, it may make sense to have a minimum amount that floats with age.



Looking at it from minimum age standpoint, if you have a minimum gift amount that is fixed, then it would seem necessary to have a minimum age based on the amount contributed.

4. All of this activity is healthy and will in all likelihood result in greater investment of resources in planned gift development efforts.

E. More pressure to account for gifts at present value.

1. Financial Accounting Standards Board (FASB) requires this.

a. Acquiring necessary information can be difficult to impossible.

b. Persons who wrote the rules not sensitive to realities of fund development and donor relations.

2. Council for Advancement and Support of Education (CASE) and National Association of College and University Business Officers (NACUBO) have promulgated guidelines for capital campaign gift crediting policies that require reporting at present value for certain reports.

3. This activity is additional internal regulation that must be dealt with.

F. Increasing interest in projecting results as compared to cost over the longer term.

1. Can be accomplished with fairly high degree of accuracy with irrevocable deferred gifts.

2. More challenging in the area of bequests and other revocable commitments.

IV. Successfully Adapting to Emerging Trends.

A. Return to focus on planned gift vehicles as ways to help motivated donors make gifts that would not otherwise be possible.

1. Less pressure on rates of payment for "donors" looking to make a "profit" on their "gift."

2. Fewer gifts offered from those that are "too young."

3. Much more convincing arguments can be made to regulators if we can show that plans are presented primarily as gifts.

4. Better relationships with internal peers will result.

B. Planned gifts are designed to make gifts possible through responding to natural objections from otherwise motivated persons that are rooted in the realities of life in today's world.

1. Need for self preservation.

2. Need to provide for loved ones.

3. Desire to give to multiple charitable interests.

C. Different types of institutions will adapt in different ways.

1. Local, regional and national models.

   a. Greater regulation may give advantage to local and regional based organizations.

   b. National programs will have to make very significant commitments to remain competitive.

      (1) Large programs will make the investment.

      (2) Smaller national programs will suffer most from increased regulation.

2. Organizational models will revolve around three or more models.

   a. Model One - no full time fundraiser.

      (1) Heavy role for consultants.

      (2) Volunteers may assume greater role.

      (3) Emphasis on basic gift plans.

   b. Model Two - at least one full time fundraiser.

      (1) No staff specialist in planned giving.

      (2) Need for outside support.

      (3) Broader range of plans offered.

c. Model Three - at least one full time planned gift specialist.

(1) Typically a broader offering of plans.

(2) Less reliance on outside consultants and volunteers.

(3) Some programs combine a "profit center" and "cost center."

d. Model Four - at least one full time major gifts officer, no planned gift specialist.

(1) Emerging trend to train those with donor access in basics of planned giving vehicles.

(2) Less emphasis on planning by nonprofit staff as awareness has grown among "allied professionals" in the community.

(3) Greater reliance on consultants for "quality control" and assistance in marketing mass oriented vehicles and structuring particular gifts.

e. Model Five - both a full time planned gift specialist and one or more major gift specialists.

(1) Planned gift specialist responsible for mass-oriented gifts such as bequests, gift annuities and pooled income funds as well as discovery of prospects for other gifts.

(2) Major gift officers cross trained to "prescribe" various gifts and bring in gift planning specialists where necessary to complete gifts.

(3) This model recognizes that most major gifts are current gifts but they must increasingly be made on a deferred basis.

(4) Key is to complete larger gifts in a cost effective manner that come to fruition within an acceptable period of time.

(5) This model occurs most frequently during and in the wake of a "comprehensive" capital campaign.

(6) Some smaller programs have tried to combine both functions in one person with mixed success.

f. More organizations, regardless of the model chosen, will take steps to assure that representatives are not moving over the line between helping to plan gifts and planning an entire estate.

D. Marketing efforts will become more focused along with greater access to technology and more sophisticated marketing techniques long employed in other sectors of the economy.

1. Focus will be on matching gift opportunities with those persons who are in the best position to take advantage of them.

2. Key will be to focus on the needs of various age and economic groups and not so much on the plans. We must stop putting the plan in front of the gift and the planner in front of the giver.

3. Less emphasis on size and timing of gifts in marketing and more focus on age and wealth of donors.

4. All plans find "a home" in one or more segments of constituency based on wealth and age.

AGE AND WEALTH-BASED MATRIX

	-55 YOUNGER	55-65 MIDDLE-AGED	65+ OLDER
WEALTHY	A1 Gifts of Cash Appreciated Property Charitable Lead Trusts Term of Years Trusts Lifelong CRT's for Others	B1 Gifts of Cash Appreciated Property Charitable Lead Trusts Term of Years Trusts Lifelong CRT's for Others	C1 Gifts of Cash Gifts of Appreciated Property Charitable Lead Trusts Term of Years Trusts Lifelong CRT's for Others Testamentary Lead Trusts CRT for Donor's Life Bequests Gift Annuities
MODERATE MEANS	A2 Gifts of Cash	B2 Gifts of Cash Appreciated Property Term of Years Trusts Charitable Trusts for Life Pooled Income Fund	C2 Gifts of Cash Appreciated Property Bequests Charitable Trusts for Life Term of Years Trusts Pooled Income Funds Gift Annuities Retirement Plans & Insurance
LIMITED MEANS	A3 Gifts of Cash	B3 Gifts of Cash	C3 Gifts of Cash Bequests Gift Annuities Retirement Plans & Insurance

5. Different plans require different levels of donative intent.

6. Plans like bequests, which require the greatest level of donative intent, typically produce the most income. Plans that require little or no donative intent typically make up a small part of activity of even the largest planned giving programs.

7. Pooled income funds may be the "sleeper" gift plan of the late 1990s.

   a. Recent indications that this plan has been mismarketed.

   b. Best prospects appear to be same persons who make gifts in the form of charitable remainder unitrusts but who lack means to fund an independent trust, rather than an alternative to gift annuities for younger persons.

8. Less emphasis on tax benefits in marketing efforts may be appropriate until tax picture stabilizes.

E. Gift acceptance policies rooted in economic considerations will increasingly drive marketing efforts to look for the correct "needles" in the right "haystack" depending on the particular gift plan.

1. The future will bring "blended" gifts.

   a. Combinations of current and deferred gifts.

   b. Emphasis on total value of gift transactions.

   c. Some portions of overall plan may be less valuable.

2. Key to planned gift success in first decades of 21st century will be working with the "winners" among the baby boomers.

   a. Childless people will make gifts in disproportionate amounts.

   b. More will give in quest for spiritual fulfillment.

   c. Great opportunities for those who are willing to take the time to educate this group and attract their assets through creative funding options that meet multiple legitimate needs as they age.

3. Asset management and tax savings will be less central to the decision making process than meeting personal planning challenges in a way that allows significant charitable gifts to be made.

   a. Providing for personal security in retirement years.

   b. Providing for children and other younger relatives.

   c. Providing for parents in later years.

V. Conclusion.

A. What is our ultimate mission.

1. Providing estate planning services in exchange for a gift?

2. Promoting planned gifts as financial "special events?"

3. Psychological counseling?

4. Resolving conflict between desire to give and desire for physical preservation?

5. Fulfilling the goals of capitalism?

6. Maximizing private initiative in a complex world with almost limitless need for funds to meet formidable challenges?

B. Planned giving is an integral part of our society.

1. Will be with us as long as there is private property.

a. Planned giving thrived in this country before there was an income or estate tax system.

b. Evidence that arrangements very similar to modern day planned gifts were popular in medieval times.

2. An integral part of our economic system.

3. Tools will change with time.

a. Use them.

b. Don't abuse them.

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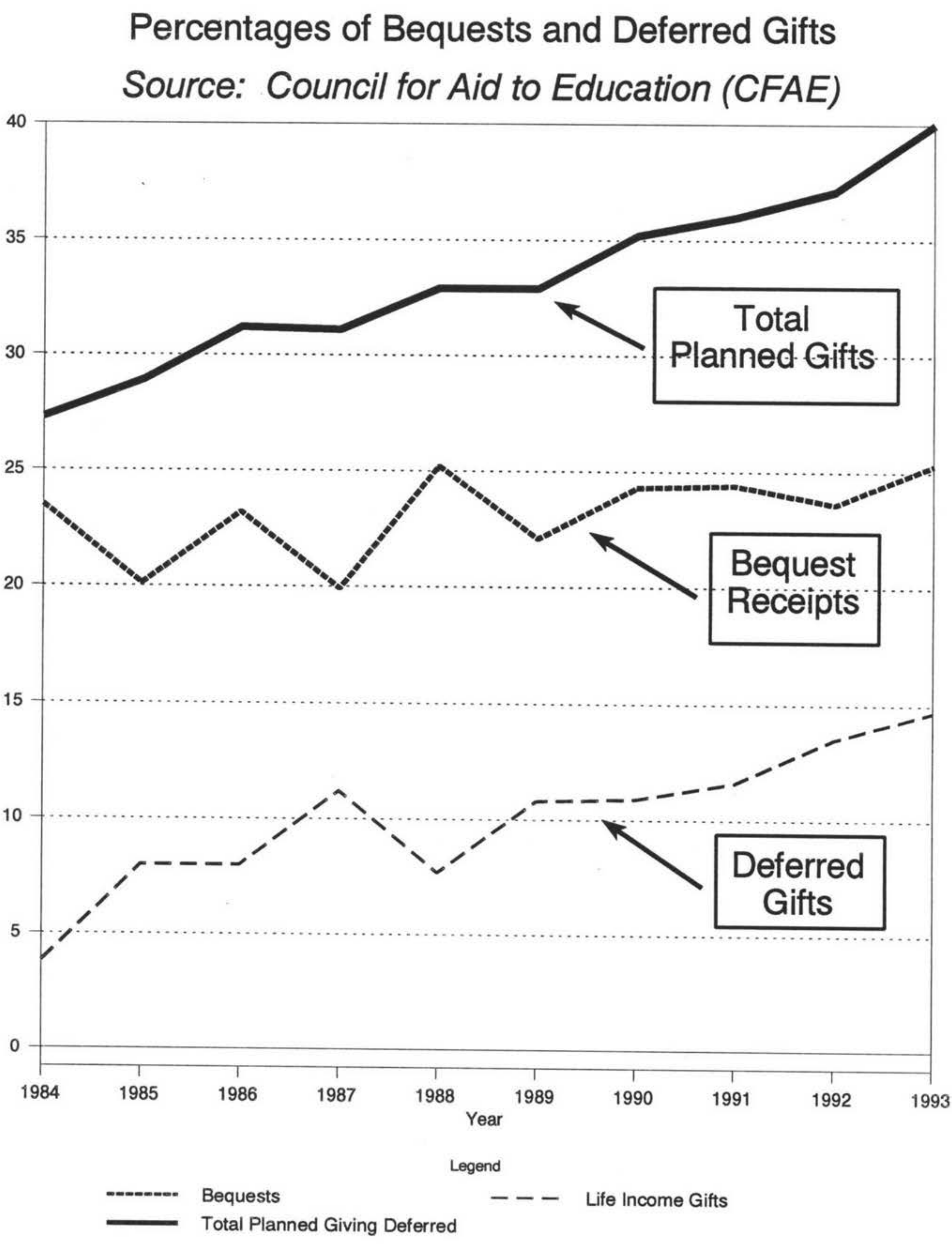
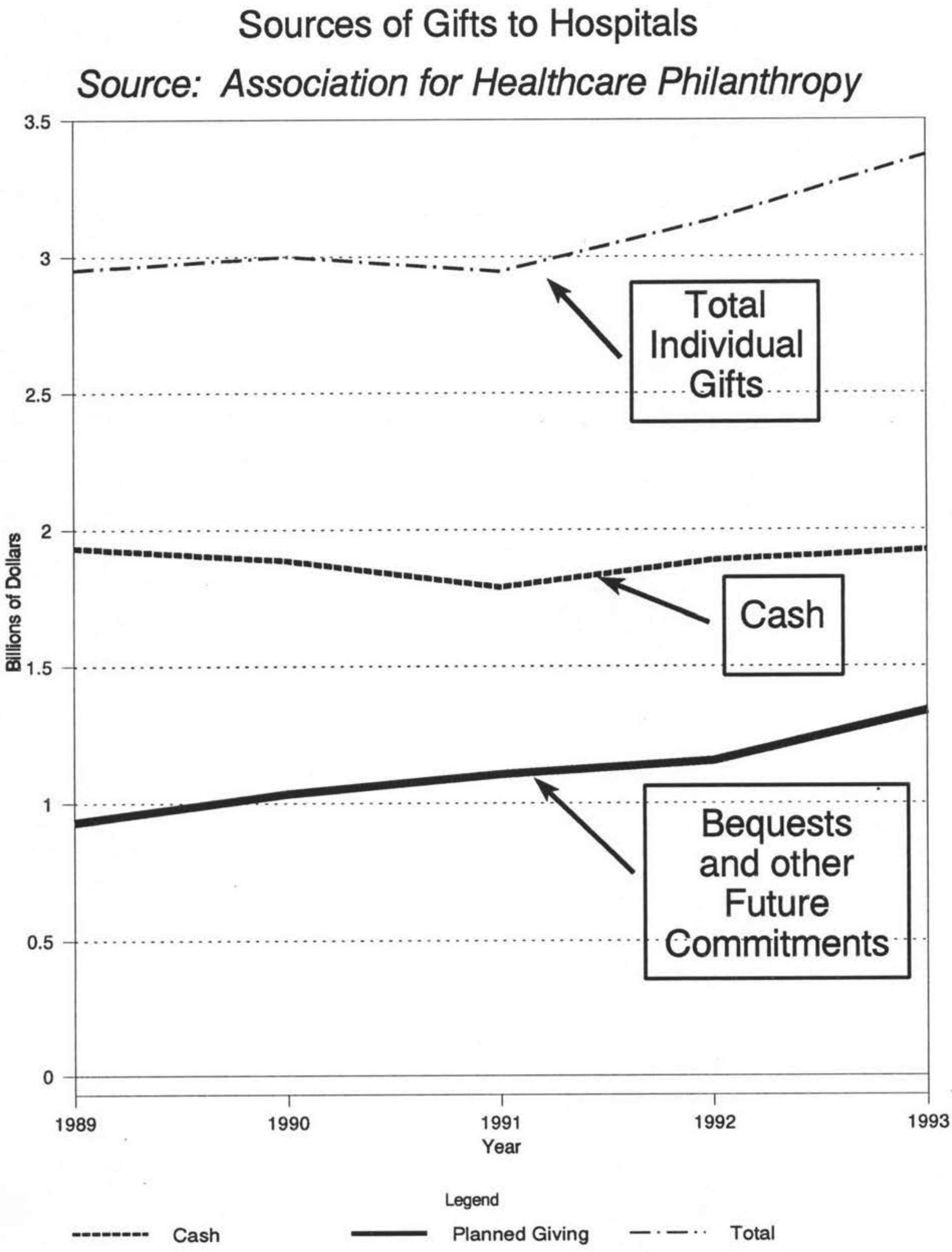
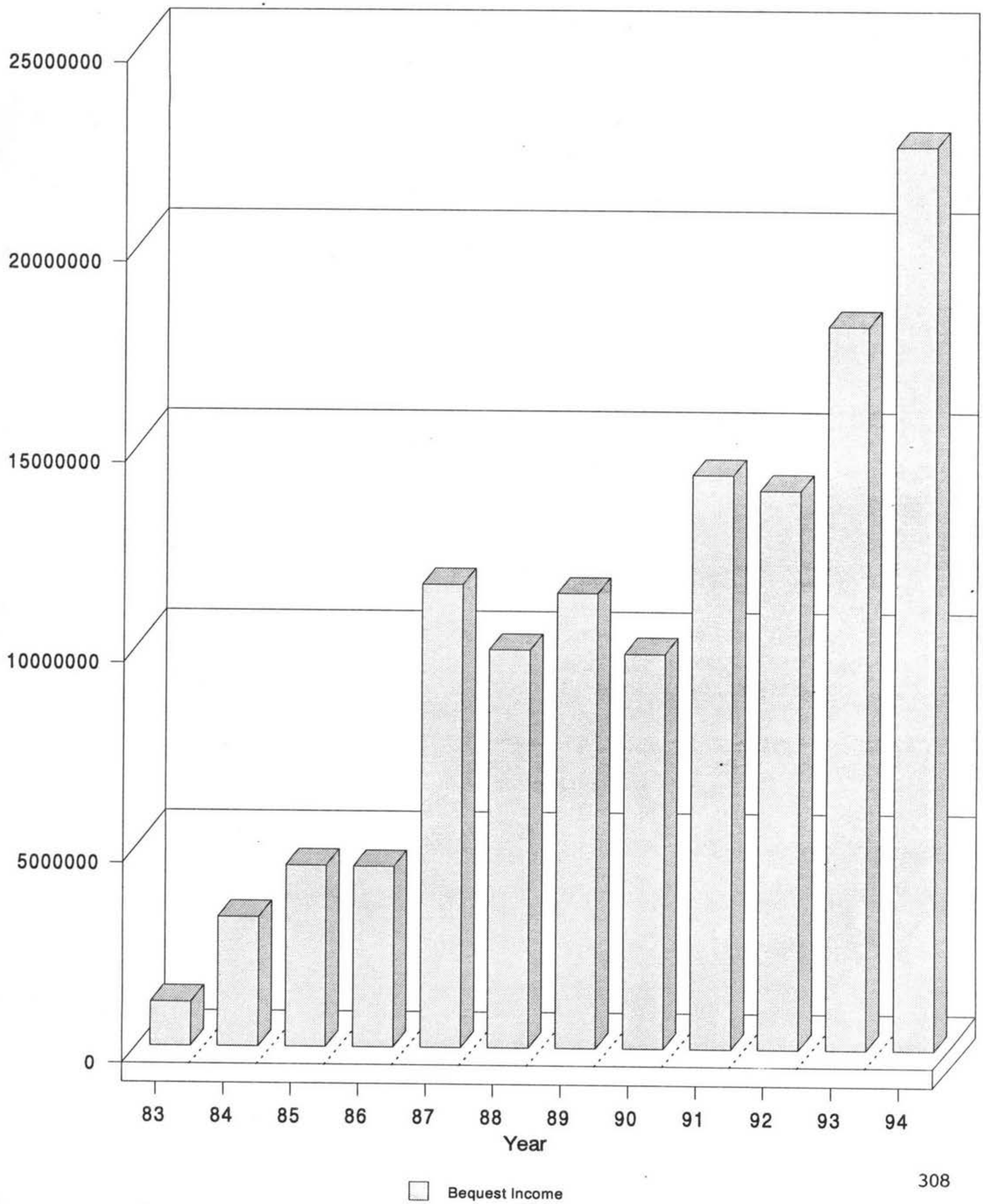
901/680-5300 fax 901/761-4268


Percentages of Bequests and Deferred Gifts
Source: Council for Aid to Education (CFAE)
40
35
30
25
20
15
10
5
0
Total Planned Gifts
Bequest Receipts
Deferred Gifts
1984
1985
1986
1987
1988
1989
1990
1991
1992
1993
Year
Legend
Bequests
Life Income Gifts
Total Planned Giving Deferred

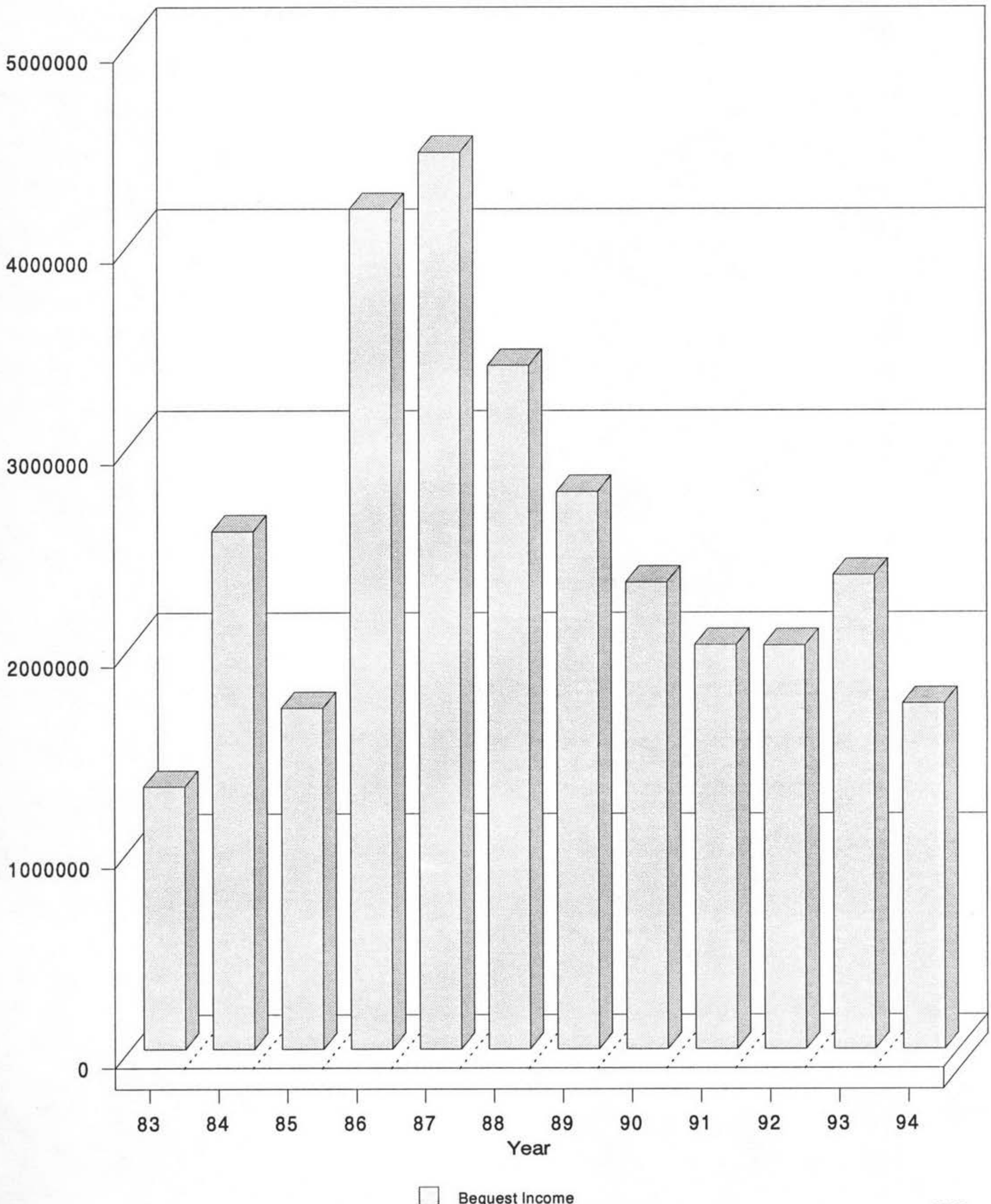


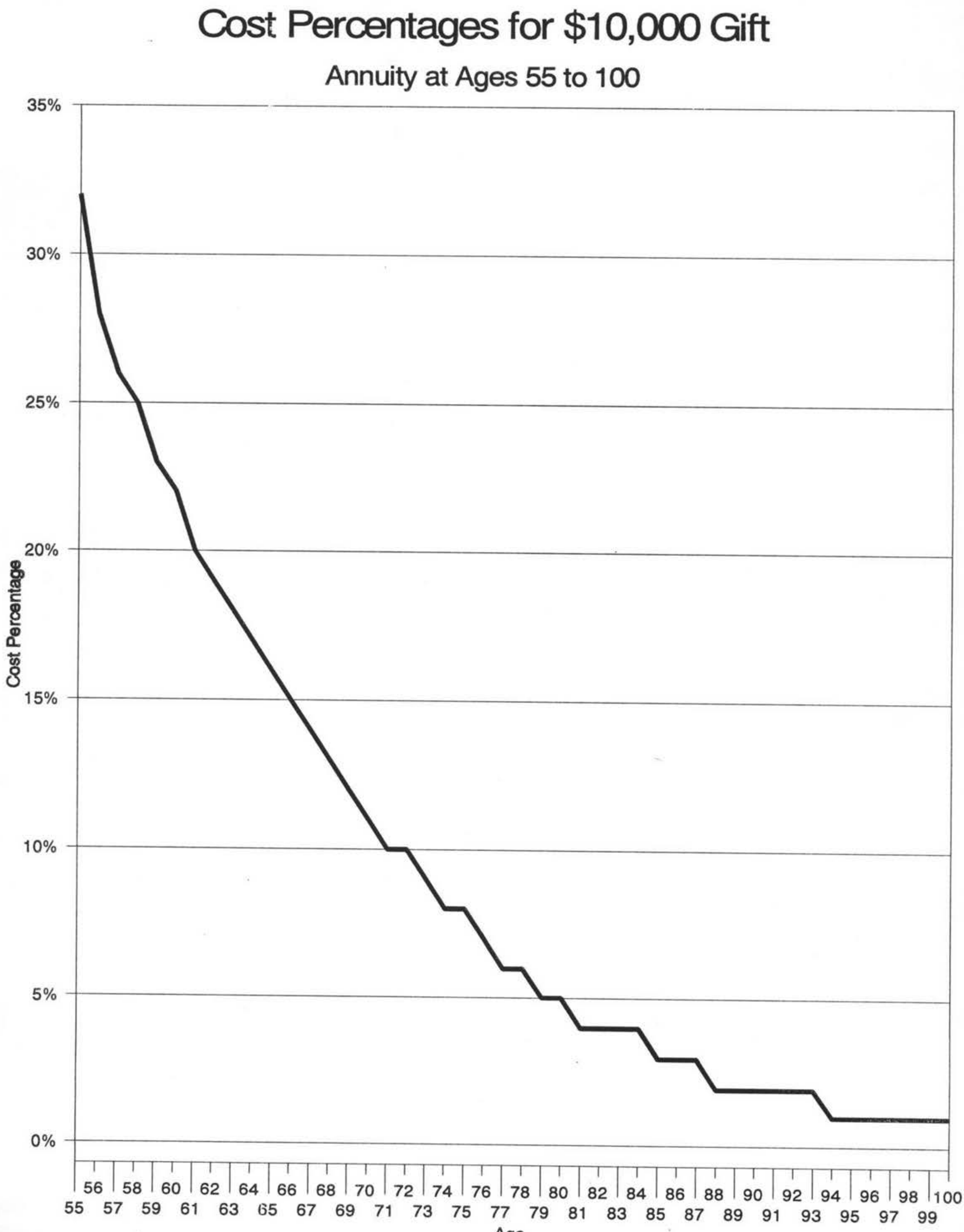
Sources of Gifts to Hospitals
Source: Association for Healthcare Philanthropy
3.5
3
2.5
2
1.5
1
0.5
0
Billions of Dollars
1989
1990
1991
1992
1993
Year
Total Individual Gifts
Cash
Bequests and other Future Commitments
Legend
Cash
Planned Giving
Total

Bequest Income 1983-94



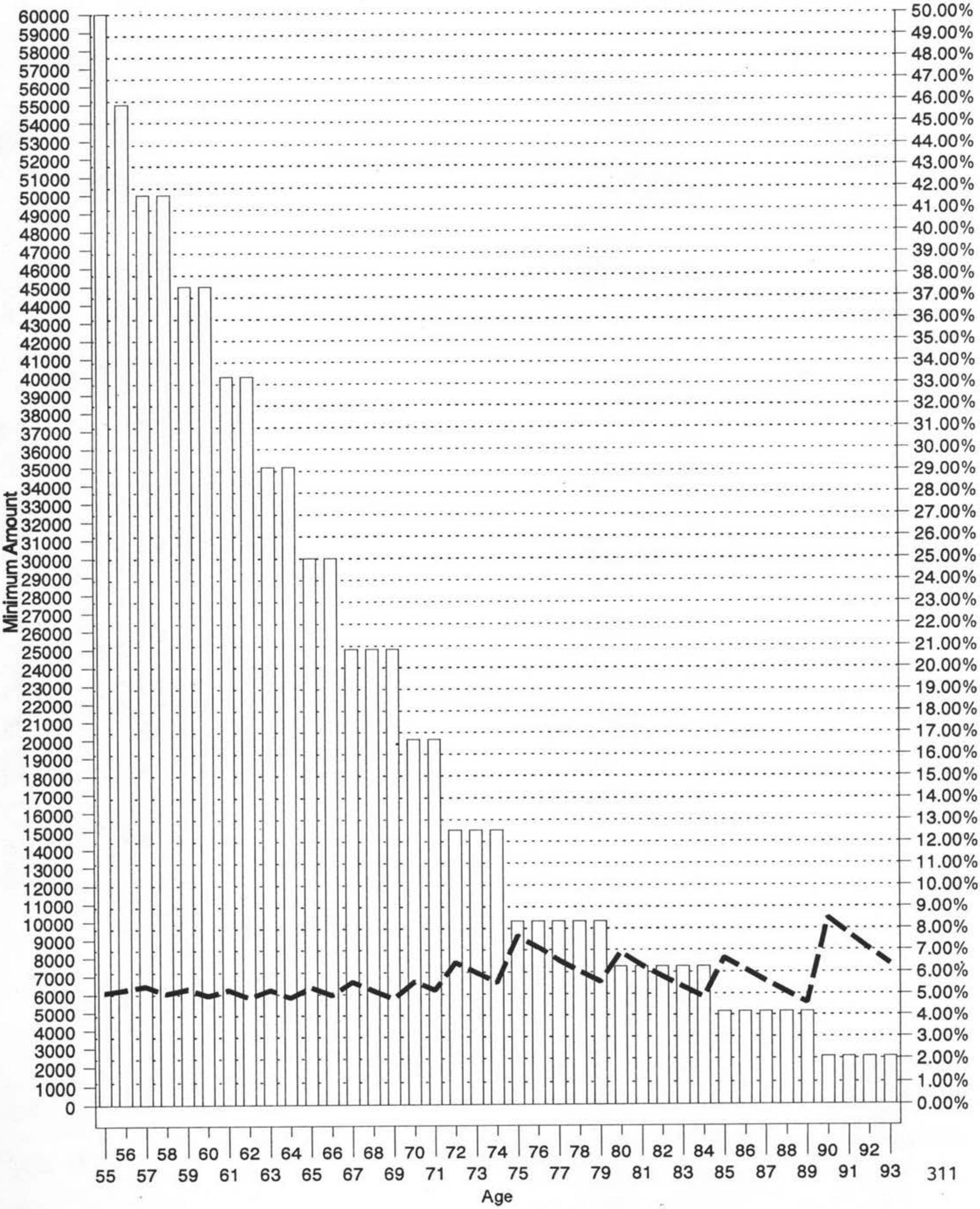
Bequest Income 1983-94




Cost Percentages for $10,000 Gift
Annuity at Ages 55 to 100
Cost Percentage
35%
30%
25%
20%
15%
10%
5%
0%
55 56 57 58 59 60 61 62 63 64 65 66 67 68 69 70 71 72 73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 100
Age

Minimum Gift Annuity Amounts

Compared to Cost Percentage



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22nd CONFERENCE ON GIFT ANNUITIES
Sponsored by
The American Council on Gift Annuities

The Hyatt Regency - San Francisco
May 3-5, 1995

Gifts of Closely-Held Stock and Other Business Interests

The Entrepreneur's Dilemma

One of the most promising areas of growth in charitable giving lies in gifts of stock in closely-held corporations. *Fortune Magazine* for the week of February 20, 1995, in its cover story, noted that the "best and brightest" are avoiding or fleeing from employment by major corporations to run their own businesses. Almost every charity's donor base includes entrepreneurs who have started businesses and built them, in corporate form, to successful and valuable enterprises. These companies often have substantial retained earnings and large cash holdings. Paying the cash out as dividends will result in this money, which has already been taxed once when earned by the corporation, being taxed a second time. Typically, salaries to the owners, deductible to the corporation, will already be at the maximum level that can withstand an IRS audit.

The result is a frustrated business owner with a highly-appreciated asset in the form of shares in a closely-held corporation that produces little or no current return. As retained earnings build, the risk that the corporation will be subjected to penalty taxes for excess retained earnings or as a personal holding company also increases. Through sophisticated planning utilizing outright charitable gifts, charitable remainder trusts and even charitable lead trusts, these frustrations can be addressed and significant tax benefits can be obtained for the philanthropically-minded entrepreneur.

The Charitable Alternative

Typically, a donor will give shares to a charity with the understanding that the shares will later be redeemed by the corporation in a transaction known as a "Palmer gift." Absent such an understanding, few people will be willing to give shares in their corporations to charity since by nature most entrepreneurs cast a dim view on the prospect of an "outsider" as a partner, even when the outsider is a favored charity. Fortunately, the typical charity is not interested in indefinitely holding an asset for which there is no ready market and which produces no current return. This atmosphere of enlightened self-interest produces an environment for very advantageous giving.

In a typical transaction, a donor who owns all of the shares in a corporation will give a portion of the shares to charity. These shares are typically highly-appreciated (in fact, the donor may have no significant basis in the shares at all) but produce a deduction for the full fair market value of the shares given. After the corporation redeems and then retires the shares, retained earnings are reduced and the cash is distributed out of the corporation to the charity with no additional tax on the distribution. Once the transaction is concluded, fewer shares in the corporation will be outstanding, but the donor will continue to own all of the outstanding shares. Consequently, ownership is unaffected.

Alternatively, a donor may have children who want to continue the business after their parent's death. These children may already own some shares in the corporation. In this scenario, a Palmer gift reduces the total number of outstanding shares by the number of shares gifted to the charity, but the entire reduction in outstanding shares occurs with the parent's holdings. After the redemption, the parent will own fewer shares while the number of shares owned by the children will be unaffected. The result is a transfer of equity interest in the corporation to the children from the parent without gift tax consequences so long as the corporation pays full fair market value in redemption of the shares.

Granted, these transactions reduce capital in the corporation. However, the income tax deduction creates capital in the hands of the business owner, and estate taxes in the absence of such planning can result in an even greater reduction in the family's capital resources of all kinds. The key, obviously, is to strike a proper balance between meeting philanthropic goals, saving income, gift and estate taxes and retaining sufficient capital in the corporation for current operations and future economic growth.

Later in this paper, planning opportunities and pitfalls involving charitable split-interest trusts and closely-held stock gifts will be considered. But before we can run, we must walk. So, the first portion of this paper will be given to an analysis of the origins of "Palmer gifts" and the current state of the law in this area as framed both by the courts and rulings issued by the IRS.

Palmer v. Commissioner: The Gift Gets a Name

The leading case in this area is Palmer v. Commissioner, 62 TC 684 (1974). Dr. Daniel D. Palmer, the taxpayer in this case, was the grandson of Daniel David Palmer, the founder of what the Court referred to as the "non-medical profession of chiropractic." The older Palmer established the first school of chiropractic located in Davenport, Iowa, known as the "Palmer College of Chiropractic." The for-profit status of the school made fund raising difficult, denied the school access to certain government funds, and violated the licensure requirements of at least one state.

For these reasons, Palmer (the taxpayer) created a nonprofit corporation known as the Palmer College Foundation which he controlled. At the time, approximately 70 percent of the for-profit corporation's shares were owned by a life income trust of which Palmer was both trustee and beneficiary, and the remainder of the shares were owned outright by Palmer. On August 31, 1966, the Foundation purchased all of the corporation's shares held by the trust. On the same day, Palmer contributed to the Foundation sufficient shares in the corporation to increase the Foundation's ownership in the corporation to approximately 80 percent.

On September 1, 1966, the board of directors and shareholders of the corporation met and agreed to redeem the shares of the corporation held by the Foundation in return for the assets of the College. The transaction was consummated as proposed. Palmer claimed an income tax charitable deduction for the full fair market of the shares he donated, and it was conceded that Palmer controlled both the Foundation and the corporation at all times relevant to the matters at issue.

The IRS asserted that in reality, Palmer had his shares redeemed by the corporation in a taxable transaction and had in effect contributed the proceeds of the redemption to the Foundation. In support of its position, the IRS argued that substance controlled over form in what it deemed to be a step transaction in that Palmer contemplated the entire transaction as it occurred before the series of transactions began and that he controlled all of the entities involved. Furthermore, the IRS argued that control gave Palmer the power to compel the redemption so that the transaction was merely an assignment by Palmer to the Foundation of the income realized on the redemption.

The Court recognized the principles of law espoused by the IRS, but found them inapplicable here, saying the validity and substance of the gift was unaffected by Palmer's anticipation of the redemption. Furthermore, Palmer's control of the Foundation was that of a fiduciary, and no breech of fiduciary duty had occurred, the redemption served the purpose of the Foundation, and the Foundation was neither a sham nor Palmer's alter ego.

The Foundation controlled the corporation at the time the redemption offer was made and could have blocked it but did not do so since the redemption was in the Foundation's best interest. Summarizing, the Court said Palmer "wished to have the College become a nonprofit organization, and there were two paths he could have taken--he could have had the stock redeemed and then made a contribution of the assets, or he could have contributed the stock and let the donee arrange for the redemption. The tax consequences to the donor turn on which path he chooses, and so long as there is substance in what he does, there is no requirement that he choose the more expensive way."

The IRS Goes Along

After some four years of consideration, the IRS acquiesced in Palmer in Rev. Rul. 78-197, 1978-1 C.B. 83. After briefly restating the facts and holdings of the Tax Court in Palmer, the IRS said it "will treat the proceeds of a redemption of stock under facts similar to those in Palmer as income to the donor only if the donee is legally bound, or can be compelled by the corporation, to surrender the shares for redemption."

Blake Muddies the Waters

The rules seemed clear until the case of Blake v. Commissioner, 697 F.2d 473 (CA-2, 1982). In 1972, Blake purchased the yacht "America," modeled after the original ship for which the America's Cup was named, for $500,000. For Blake, however, the America was nothing but trouble. Its maintenance expense was substantial, and it required a relatively large and expensive crew to operate it. Blake determined "to get rid of the America at all costs" because it "was taking too much time and concern."

Blake tried to donate the America to Mystic Seaport in Mystic, Connecticut, but Mystic declined the gift. Then Blake approached the Kings Point Fund, Inc., a charity associated with the U.S. Merchant Marine Academy at Kings Point, New York, about the possibility of the Academy using the America as a training vessel. The superintendent of the Academy indicated interest in the idea in a letter to Blake written in February, 1975. A key to the Fund's receiving the gift was the development of resources from Blake and others to meet the operation and maintenance expenses of the America. Apparently with this understanding, the Board of Directors of the Fund unanimously agreed to acquire the America in a resolution passed at a Board meeting on March 13, 1975.

At this point, however, the facts began to get interesting. Four days after the March 13 meeting, Blake donated $686,875 of stock in Friendly Ice Cream stock, a company Blake had founded, to the Kings Point Fund "to advance your training program of young cadets in a way that you see fit." At an April 18, 1975, meeting of the Fund Board of Directors, it was reported that Blake had contributed the stock to be used to acquire the America from Blake for $675,000 with the balance to be used to offset operational and maintenance expenses.

Whether the maintenance and operational expenses were greater than expected or for some other reason, the Board resolved as early as June 17, 1975, to sell the America. At a June 17, 1975 Board meeting it was announced that the America had been sold for $250,000 netting $200,000 for the Fund.

Later, Blake acknowledged that he probably would not have given the stock to the Kings Point Fund absent its agreement to use a portion of the proceeds of the sale of the stock to purchase the America from him. But he argued that his was a mere expectation and not an enforceable obligation.

The Court of Appeals said that the question to be resolved was "whether the taxpayer was entitled to treat the transfer of the first asset--corporate stock--as a contribution and treat the transfer of the second asset--a yacht, as a sale, or whether, as the Tax Court held, the transaction must be recharacterized as a sale of the stock followed by a contribution to the charity of the vessel."

The Court first addressed the question of whether the gift of the stock created an obligation on the part of the Fund to purchase the America. The Court said the gift of stock was conditioned on the Fund's agreement to purchase the America, and that the receipt of the stock by the Fund created an obligation to purchase the America under the doctrine of promissory estoppel.

More importantly, even if no legally enforceable obligation to purchase the America existed, the "understanding" of what was to occur was sufficient in this case to uphold the Tax Court's decision. The Appeals Court held that failure to follow through with its agreement to purchase the yacht in the face of Blake's strong "expectation" would have jeopardized future vessel donations, and that the Board of Directors was fully cognizant of that fact. The Court noted that Blake acknowledged that "there was almost no likelihood" that the Fund would fail to purchase the yacht as contemplated.

Under these facts, the Court held that whether the obligation to purchase the yacht was enforceable or not, the Tax Court's recharacterization of the transaction was correct.

The Court somewhat gratuitously discussed Palmer, and observed that the IRS, in Rev. Rul. 78-197, read too much into Palmer, saying, "Where there is, as here, an expectation on the part of the donor that is reasonable, with an advance understanding that the donee charity will purchase the asset with the proceeds of the donated stock, the transaction will be looked at as a unitary one. A wooden view that would require legal enforceability of an understanding or obligation to purchase the asset contemplated to be donated ab initio is not what the tax law contemplates. At least, this circuit will not take it to do so."

What Hath Blake Wrought?

Arguably, the facts of Blake were so blatant that the result reached was almost unavoidable. It should be noted that contrary to Palmer, the redemption transaction occurred not between the charity and a corporation whose shares had been donated, but rather between the charity and the donor himself. Furthermore, the redemption was not one of the company stock but rather was a redemption of a wholly different asset. Given these distinctions, how has the IRS reacted to Blake? Thankfully, very reasonably. In LR 8623007, the IRS reiterated its decision in Rev. Rul. 78-197. In that letter ruling, stock was transferred by a donor to charity. The donated stock was subject to restrictions prohibiting its transfer without the approval of the company's Board of Directors and gave the company the right of first refusal on any sale. Approximately five months after the gift, the company redeemed the shares from the charity at a price slightly in excess of the value of the shares as claimed by the donor on his tax return. The IRS approved this transaction under the Palmer rationale, saying that the restrictions did not alter the result since the company could not compel redemption from the charity and the charity was free to retain title to the shares indefinitely. The Service specifically distinguished this fact situation from Blake by noting that the donor received nothing of value from the charity.

Accordingly, then, it appears that so long as planners play by the rules, the advantages offered to the philanthropic entrepreneur by Palmer and Rev. Rul. 78-197 remain. But one word of caution should be offered. Palmer ordinarily works only with C Corporations, i.e., corporations which are taxable entities themselves. Since the Tax Reform Act of 1986, the maximum corporate rate of 34 percent exceeds the maximum individual rate, now 31 percent, for the first time. For this reason, many small business owners are choosing to do business as S Corporations, which are pass-through entities that allow items of income and loss to pass through to shareholders in a fashion similar to partnerships. Under Sec. 1361(c) and (d), only an individual, a grantor trust, an estate or a qualified Subchapter S trust defined in Sec. 1361(c)(2)(A) may hold S Corporation stock. The transfer of S Corporation stock to charity or to a charitable split-interest trust will break the donor's election to have his corporation taxed as an S Corporation, often with catastrophic tax consequences. Later, a planning alternative for S corporations will be discussed. Careful planning, nonetheless, with the donor's tax advisors is necessary, and caution is advised.

ESOPS and Palmer Gifts

While gifts of closely-held stock followed by redemption can be very attractive for the donor in that (1) he receives a full fair market value deduction for property in which he has little, if any, basis, and (2) he gets cash out of the corporation tax-free which is helpful if the corporation is in danger of being assessed a penalty tax as a personal holding company or as a corporation with excess retained earnings, the fact remains that the corporation is paying out dollars to a third party with no other tangible benefit. An alternative which does add benefit for the corporation is to have the corporation create an employee stock ownership plan (ESOP). The corporation can then contribute cash to the ESOP and receive a deduction for the cash on a dollar for dollar basis up to an amount equal to 15% of the total compensation of all employees participating in the plan (subject to Internal Revenue Code imposed ceilings). As long as the contribution amount for any given year does not exceed that 15% limitation, then in the transaction the corporation will receive a full deduction for any cash it adds to the ESOP, and instead of the corporation redeeming the stock from the donee, the ESOP will purchase the stock. If the 15% ceiling is exceeded in any given year, the excess may be carried over to future years and deducted by the corporation. Of course, the donor still receives a full fair market value deduction for the gift of stock to charity. To add even more octane to the arrangement, the ESOP can borrow money from a third party to purchase securities, and deductible contributions may be made to the ESOP by the corporation to enable the ESOP to repay its loans. Obviously, an ESOP, where it otherwise makes sense, can provide added benefit for the donor in a transaction geared to making a meaningful gift to charity. A gift of stock to a charitable remainder trust followed by a purchase of the trust's stock by the ESOP can make a gift even more attractive. A note of caution is in order, however. While ESOP and remainder trust combinations are often depicted in simplistic terms, expert counsel is essential to be sure that the combination produces both a qualified ESOP and a qualified remainder trust.

Gifts of Closely-Held Stock to Charitable Remainder Trusts

As a threshold matter, it should be noted that sec. 4947(a)(2) applies some of the private foundation penalty tax provisions to charitable remainder trusts as if those trusts were, themselves, private foundations. These taxes include self-dealing taxes (sec. 4941), the taxes on excess business holdings (sec. 4943), the taxes on jeopardizing investments (sec. 4944) and the taxes on taxable expenditures (sec. 4945). Fortunately, sec. 4947(b)(3)(B) also exempts charitable remainder trusts from the excess business holdings tax and the jeopardizing investments tax, so long as a prescribed tax deduction is allowed for the remainder interest.

Section 4946(a)(1)(E) provides, in effect, that if disqualified persons own in excess of 35% of the total combined voting power of a corporation, then the corporation itself will become a disqualified person. On the surface, this would indicate that a Palmer redemption transaction involving a charitable remainder trust would be a prohibited act of self-dealing with potentially disastrous application of the private foundation penalty taxes for self-dealing. However, sec. 4941(d)(2)(F) and Treas. Reg. sec. 53.4941(d)-3(d) specifically allows for a redemption of stock by a corporation, when even the corporation is a disqualified person, if the corporation offers to redeem all outstanding shares of stock of the same class as that owned by the remainder trust on the same terms, and so long as the purchase price is for full fair market value. When those conditions are met, the redemption transaction should be allowed to proceed unaffected by the self-dealing rules.

As a result, charitable remainder trusts can be an excellent vehicle for holding closely-held stock. The absence of the application of the excess business holdings provisions means that the remainder trust can continue to own all or any portion of the stock of the corporation indefinitely. In a unitrust with a net income provision, the unitrust can continue to own the shares for the life of the trust, absent some application of fiduciary rules which would require a diversification of the assets. Taking this transaction a step further, the trustee of the charitable remainder trust and the owner of the corporation could be one and the same person. In that situation, it would be necessary that the payments be fixed as to the beneficiaries, as opposed to allowing a sprinkling power for the unitrust percentage or the annuity amount, so as to avoid grantor trust treatment of the trust, thus resulting in its disqualification. Where the closely-held business owner does serve as the trustee, special care should be taken by the trustee, in conjunction with his tax advisors, to assure that his actions are not inappropriate as trustee and are in compliance with the regulations under sec. 664, and that all requirements applicable to the trustee as to management of the trust assets are followed scrupulously. Specifically, it may be necessary for a co-trustee to be named for the limited purpose of valuing the stock initially and annually thereafter. See H.R. Rept. No. 91-413 (Part 1) 91st Cong., 1st Sess. at p. 60 and S. Rept. No. 91-552, 91st Cong., 1st Sess. at p. 88.

Note, however, that an installment purchase of the stock by the corporation from the trust would constitute a prohibited act of self-dealing under Treas. Reg. sec. 53.4941(d)-2(c). As an alternative, the stock can be redeemed incrementally over time.

Closely-Held Stock Gifts and Charitable Lead Trusts

As with charitable remainder trusts, charitable lead trusts are also subject to the private foundation rules generally. However, sec. 4947(b)(3)(A) grants exemptions from sec. 4943 and sec. 4944, so long as the actuarial value of the charitable income interest does not exceed 60% of the aggregate fair market value of the trust. While appropriate planning can often be done while remaining within the 60% safe harbor, the fact remains that it is quite typical for a donor who is contemplating utilizing charitable lead trusts in his or her estate planning to want to obtain a larger deduction than 60%. In that case, all private foundation penalty taxes will apply, although sec. 4943(c)(6) allows a five-year grace period for disposition of the excess business holdings.

Often, however, the goal of passing the family corporation to the next generation will not be served by the application of this grace period, since the self-dealing rules will prevent the sale of the stock to the children or any entities controlled by the children. In that case, an interesting and helpful provision is found in Treas. Reg. sec. 53.4941(d)-1(b)(3) headed "Transactions during the administration of an estate or revocable trust." This section will allow the administrator of an estate to honor preexisting options regarding the property which are binding on the administrator of the estate, thus allowing a sale of the securities to whoever holds the right to purchase them.

Accordingly, an agreement can be entered into by a parent and his children which will be binding on the executor of the parent's estate at death. The executor, under his binding obligation, will sell the entire assets involved, (even in an extreme case, the entire estate) to the children. However, rather than selling it to the children for a lump sum, the executor will sell the stock at fair market value (this is essential) with the purchase price being paid out on an installment basis. Although at first blush, this would seem to be a prohibited transaction because Treas. Reg. sec. 53.4941(d)-2(c) entitled "Loans" specifically provides that loans between a private foundation (the lead trust) and disqualified persons (the children) will be a self-dealing transaction, this provision expressly excepts a loan resulting from a transaction described in Treas. Reg. sec. 53.4941(d)-1(b)(3) from self-dealing treatment. (This is the provision previously discussed entitled "Transactions during the administration of an estate or revocable trust.")

Here, two alternatives exist. The first alternative would be to have the children actually amortize the note over the period of the trust, e.g., fifteen years, twenty years or even twenty-five years. This would mean that the assets would be available for the children to utilize immediately, the lead trust would be funded with a note, and when the note is amortized and the trust terminates, the children would receive back any residue of the trust. The other alternative is to have the note be an interest-only obligation payable during the term of the lead trust, with the note coming due at some point past the expiration of the term of the lead trust. At the termination of the trust, the note funding the lead trust would pass to its new owners, the children who are the makers of the note, and merger would occur. Apparently, income in the form of debt relief is not an issue in this testamentary setting.

Obviously, this has been a very simplistic description of a very complicated process. It is described in more detail later.

Odds and Ends

In the first part of this paper, it was pointed out that the entire concept of Palmer Gifts works best with C Corporations. Whenever an S Corporation is involved, a gift of S Corporation stock to a charity or split-interest trust break the S election. This will not always have traumatic tax consequences for the donor, but often the consequences will be severe, and in any event, the donor's tax preparers must seriously consider the effect of breaking the S election in advance of the gift of S Corporation stock to a charity or to a split-interest trust.

Additionally, a contribution of appreciated securities in a closely-held corporation will result in a deduction for the full fair market value of the securities subject to the 30% of contribution base (basically adjusted gross income) limitation, with a five-year carryover. However, if the shares donated by the donor are sec. 306 stock, then the donor's deduction will be likely be limited to his or her basis in the stock, since the sale of sec. 306 stock would produce ordinary income to the extent the sales price exceeds basis. Under the general reduction rules under sec. 170(e), gifts of property producing only ordinary income are deductible only at basis, although the higher 50% deduction ceiling applies.

Likewise, gifts of stock in collapsible corporations, (sec. 341 stock) result in a deduction only to the extent of basis, since the sale of such stock results in ordinary income to the extent that the sales price exceeds basis.

As indicated at the outset of this paper, successful entrepreneurs are all around us. They come from all kinds of backgrounds, and wear blue collars as well as white collars. Where the common thread of philanthropic-motivation is present, a closely-held gift can work wonders for both the donor and the charity who is the beneficiary of the donor's generosity.

Having Your Cake and Eating it, Too, Through Charitable Lead Trusts: Setting the Stage

One of the continuing challenges for small business owners is transferring the business to the next generation at the minimum transfer tax cost. Over the years, private annuities, sales of remainder interests, GRITs, GRATs, GRUTs, corporate freezes and partnership freezes, among other approaches, have been used. Legislation, over time, has created some of these options and eliminated others.

For the charitably inclined business owner with an incorporated business, C corporation stock can be transferred in an advantageous fashion to the next generation through Palmer gifts. Another alternative that presents itself to the charitably inclined business owner utilizes charitable lead trusts to minimize transfer taxes. This portion of the paper considers this alternative, but to set the stage, a review of a few basic rules is in order.

The Self-Dealing Rules

First, as you will recall, charitable split-interest trusts are subject to the self-dealing provisions of Sec. 4941 and the accompanying regulations. Sales, leases, loans, exchanges and other specific transactions between private foundations (for our purposes, split-interest trusts) and disqualified persons as defined in Sec. 4946(a), no matter how advantageous to the split-interest trust, are strictly prohibited. However, certain exceptions exist. For example, compensation reasonable in amount for services that are necessary to the trust do not constitute self-dealing when the service provider is a disqualified person. Additional, more technical exceptions apply.

One of these technical exceptions lies in the area of indirect self-dealing. Specifically, Sec. 4946 makes entities controlled by or substantially responsive to a disqualified person a disqualified ~~person~~ as well. When a split-interest trust deals with one of these third party entities, indirect self-dealing can occur.

In Reg. Sec. 53.4941(d)-1(b), indirect self-dealing transactions are discussed. In (3) in that section, an exception to the self-dealing rules entitled "transactions during the administration of an estate or revocable trust" is set out. This exception is particularly helpful in testamentary settings. While a revocable trust becoming irrevocable at the grantor's death is covered by this section as well, we will discuss this exception in terms of a decedent's estate.

Under this provision of the regulations, a transaction involving a split-interest trust's interest or expectancy in property will not constitute self-dealing if several requirements are met. These requirements are:

(1) The administrator or executor of the estate must possess a power to sell the property, a power to reallocate the property to another beneficiary, or be required to sell the property under the terms of an option to which the property was subject at the time that the property was acquired by the estate.

(2) The transaction must be approved by the court having jurisdiction over the estate.

(3) The transaction must occur before the estate is closed or considered terminated under Reg. Sec. 1.641(b)-3 which provides for automatic termination of the administration of estates in which the administration is deemed unduly prolonged in the view of the IRS.

(4) The estate must receive an amount which equals or exceeds the fair market value of the trust's interest in the property at the time of the transaction. The fair market value has to be determined taking into account the terms of any option which applies to the property acquired by the estate. Furthermore, the trust must receive an interest at least as liquid as the one it gives up, the transaction must result in the trust receiving an asset related to the active carrying out of its exempt purposes, or the transaction must be required by the terms of an applicable option.

Enter Charitable Lead Trusts

That's a list of dry rules for sure, and the question is, "how does it help us as planners?" Assume that we have a husband and wife who operate a bakery business. Their two adult children both work in the business, and the business has a value of several million dollars. The children want to take over the business, which is a profitable one and which produces a significant annual cash flow. The parents are in the process of retiring from the business, and they are beginning the process of planning for the disposition of their estates. They are interested in supporting their local university, and want to give their business to their children.

After consulting with counsel, the couple grants an irrevocable option to their children allowing each of them the right to purchase an undivided one-half interest in the business from the estate of the last parent to die at fair market value at the time of the purchase. An appropriate provision for valuing the company at the time of purchase is included in the option agreement. The option further provides that the children will be able to purchase the business with 100% financing by the surviving parent's estate, with the interest rate being the long-term applicable federal rate for the month in which the sale is concluded. The note will be an interest only note for 20 years with all principal being due at the end of the 20 years.

The grantors provide in the will of the second to die, that a lead trust will be funded with the bakery business or with the proceeds of its sale. If the children exercise the option, then the note, which constitutes the proceeds of sale, will fund the lead trust.

The interest on the note will provide the cash flow for the lead trust to meet its annuity obligation. Depending upon the earnings expectations from the business, the payout rate from the lead trust can be high enough, in the case of a charitable lead annuity trust, to completely zero out the gift. Consequently, estate tax in the estate would be avoided (at least insofar as the business is concerned).

Having the Cake (and Eating it, Too)

After the death of the second spouse, assuming that the option is exercised, the children will take immediate possession of the business without having to wait for the termination of the lead trust. This is important not only for family reasons, but because the provisions of Sec. 4943 relating to excess business holdings would require that the lead trust divest itself of the business within five years from the date of funding since the charitable deduction exceeds 60% of the value of the property funding the trust.

For the term of the trust, the children would service the note. If we assume that the lead trust is an 18-year lead trust, then upon termination of the trust, the lead trust assets will pass to the children outright and free of tax.

What are the assets that the children receive? A note of which they are the makers. Since they now own that note, the doctrine of merger applies and the note is extinguished. On that basis, while it is not totally clear, it would seem that the doctrine of merger would avoid any income tax consequences in the form of cancellation of indebtedness.

In summary, the children will receive the business immediately upon the death of the last parent to die without payment of estate tax.

How the Numbers Add Up

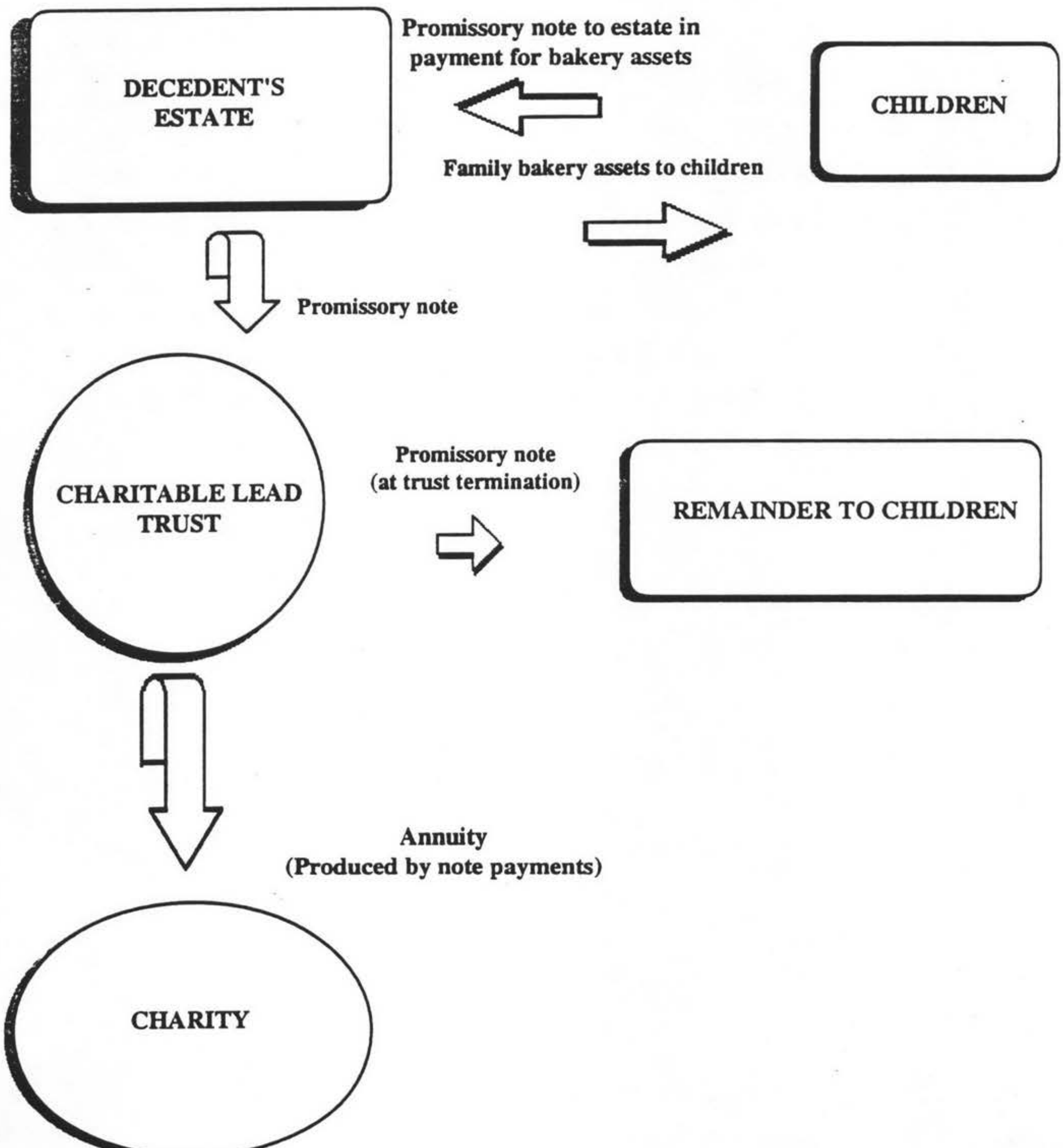
A numerical example would be helpful. Assume that the business has a value of $8 million and that the children exercise their purchase option. Assume further that the lead trust will run for a period of 18 years from its creation. Furthermore, we will assume that the discount rate is 8% (today, of course, it is much lower which would be much better for the donor).

Under our circumstances, an annuity of 10.37% paid quarterly for a period of 18 years produces a charitable deduction sufficient to completely eliminate the gift from estate taxation. Because the note will be indebtedness for purchasing a business, the interest should be deductible. Assuming that the children are in the new proposed maximum tax bracket of 36%, their net after-tax cost per year will be $530,944 ($824,600 interest payment reduced by tax savings of $298,656). On a present value basis assuming an 8% interest rate, the children will have paid $4,975,947 for the $8 million business. They will have paid only slightly more in note payments than the estate tax would have been on an outright gift of the business, but they will have, in effect, been able to pay it over time without interest. Furthermore, charity will have received almost $15 million over 18 years.

Obviously, implementing this transaction would be more complex than the skeleton description set out above. For one thing, all of the steps set out in the regulations would have to be followed (although for the most part, in a situation such as this, those steps would be mechanical). Nonetheless, this is one more planning alternative for the philanthropically-motivated client who wants to put specific assets in the hands of his or her children.

The following diagram generically depicts the transaction described in this portion of the paper:

HAVING YOUR CAKE AND EATING IT, TOO, THROUGH CHARITABLE LEAD TRUSTS

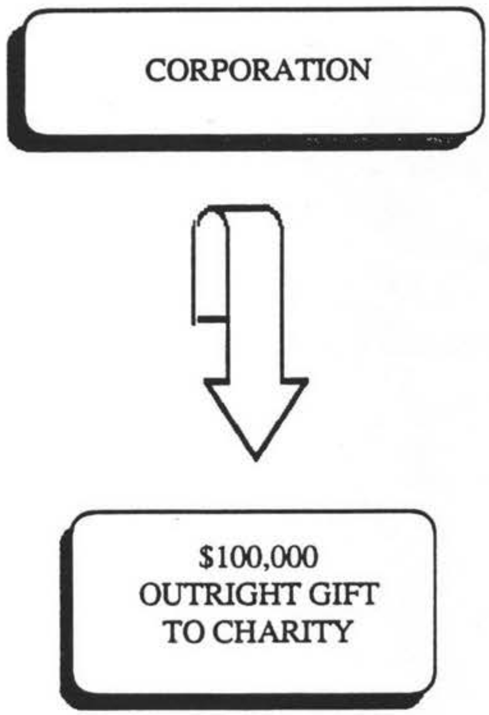


CASE STUDY

Andre' Preneur spent the first ten years of his career as a VCR repairman. However, during the last five years he has been developing and marketing a series of children's action characters known as "Tae-Kwon-Do Adolescent Ants." The individual characters are known as Bach, Beethoven, Brahms and Barney (what can I say -- there are only three "B's" and four ants).

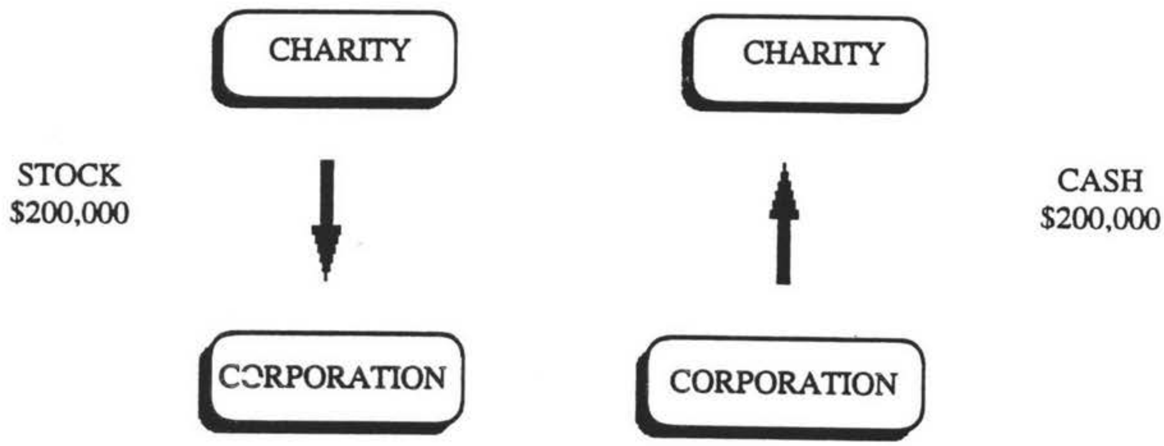
Sales are booming, there are spin-offs galore, and the Ants have just completed their "Coming out of their (Ant) Hill" Tour. The corporation that markets the products is solely owned by Andre' and his wife, Priddy Preneur, and is worth millions. Andre' and Priddy are thinking of taking the company public. They are 60 and 58 years old, respectively, and are interested in arts-related charities. What alternatives are available to them?

GIFT BY CORPORATION



*** THE CHARITABLE DEDUCTION FOR THE YEAR OF THE GIFT CANNOT EXCEED 10% OF THE CORPORATION'S TAXABLE INCOME. THE CORPORATION CAN CARRY EXCESS CHARITABLE DEDUCTION FORWARD FOR UP TO FIVE ADDITIONAL YEARS.**

CLOSELY-HELD CORPORATE STOCK GIFT

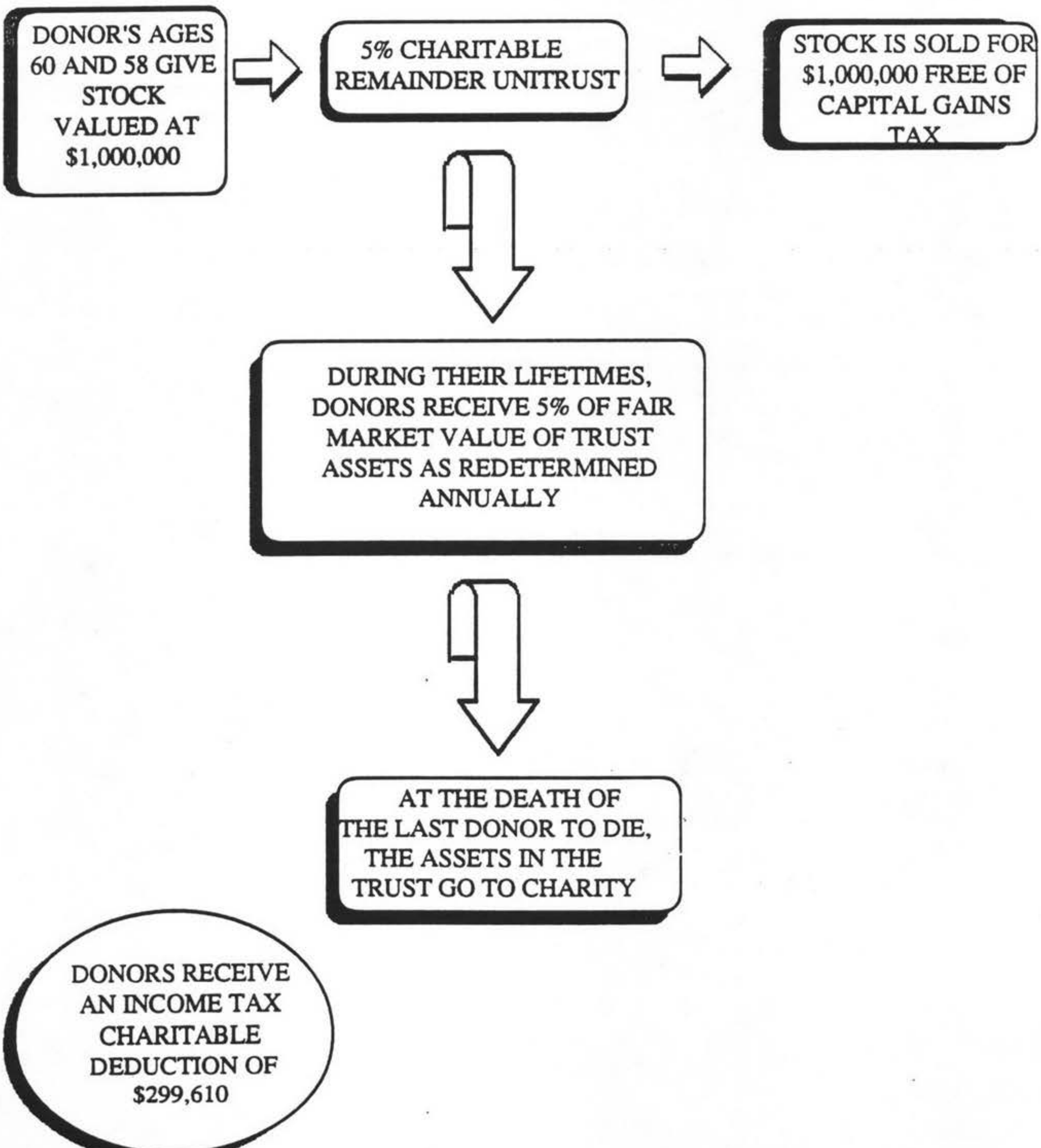


• **IF DONOR IS THE SOLE STOCKHOLDER, HE CONTINUES TO RETAIN FULL OWNERSHIP IN THE CORPORATION.**

• **IF DONOR AND HIS CHILDREN OWN SHARES IN CORPORATION, THIS GIFT WILL INCREASE OWNERSHIP OF CHILDREN IN THE CORPORATION AND WILL DECREASE OWNERSHIP OF DONOR IN CORPORATION WITHOUT GIFT TAX CONSEQUENCES.**

•• **THE DONOR HAS A $200,000 CHARITABLE DEDUCTION WHICH CAN BE USED TO OFFSET UP TO 30% OF HIS ADJUSTED GROSS INCOME IN THE YEAR OF THE GIFT.**

GIFT OF STOCK THROUGH CHARITABLE REMAINDER UNITRUST



LOCAL UNIVERSITY

Deduction Calculations
Actuarial Calculations

5% Charitable Unitrust

ASSUMPTIONS:

[1]	Beneficiary Ages	60 58
	Date of Gift	3/14/1995
[2]	Principal Donated	$1,000,000.00
[3]	Payout Rate	5%
[4]	Payment Schedule	quarterly 3 months to 1st payment
[5]	Discount Rate under IRC Section 7520(a) for 2/95	9.6%

CALCULATIONS:

[6]	Adjustment factor for payment schedule on [4] (Table F in IRS Publication 1458)	0.944628
[7]	Adjusted unitrust payout rate ([3] x [6]) (Reg. 1.664-4(b)(2))	4.7231%
[8]	Remainder factor for values on [1] and [7] (Table U(2) in IRS Publication 1458)	0.29961
[9]	CHARITABLE DEDUCTION ([2] x [8])	$299,610.00

Prepared for ANDRE' AND PRIDDY PRENEUR — March 14, 1995

LOCAL UNIVERSITY

Life Income Projections
Detailed Cash Flow Analysis

ASSUMPTIONS:
Projection begins in 1995 and runs for 30 years.
Measuring lives age 60, 58.
Original principal is $1,000,000. Cost basis is 100%.
Donor income tax bracket is 39.6%, 28% for capital gains.
Beneficiary income tax bracket is 39.6%, 28% for capital gains.

5% Charitable Unitrust

YR	Year-End Principal	Capital Apprec. (3%)	Income (6%)	Before-Tax Ben. Inc.	After-Tax Ben. Inc. (39.6%)
95	$1,000,000				
96	1,040,000	$30,000	$60,000	$50,000	$30,200
97	1,081,600	31,200	62,400	52,000	31,408
98	1,124,864	32,448	64,896	54,080	32,664
99	1,169,859	33,746	67,492	56,243	33,971
00	1,216,653	35,096	70,192	58,493	35,330
01	1,265,319	36,500	72,999	60,833	36,743
02	1,315,932	37,960	75,919	63,266	38,213
03	1,368,569	39,478	78,956	65,797	39,741
04	1,423,312	41,057	82,114	68,428	41,331
05	1,480,244	42,699	85,399	71,166	42,984
06	1,539,454	44,407	88,815	74,012	44,703
07	1,601,032	46,184	92,367	76,973	46,492
08	1,665,074	48,031	96,062	80,052	48,351
09	1,731,676	49,952	99,904	83,254	50,285
10	1,800,944	51,950	103,901	86,584	52,297
11	1,872,981	54,028	108,057	90,047	54,388
12	1,947,900	56,189	112,379	93,649	56,564
13	2,025,817	58,437	116,874	97,395	58,827
14	2,106,849	60,774	121,549	101,291	61,180
15	2,191,123	63,205	126,411	105,342	63,627
16	2,278,768	65,734	131,467	109,556	66,172
17	2,369,919	68,363	136,726	113,938	68,819
18	2,464,716	71,098	142,195	118,496	71,572
19	2,563,304	73,941	147,883	123,236	74,434
20	2,665,836	76,899	153,798	128,165	77,412
21	2,772,470	79,975	159,950	133,292	80,508
22	2,883,369	83,174	166,348	138,623	83,729
23	2,998,703	86,501	173,002	144,168	87,078
24	3,118,651	89,961	179,922	149,935	90,561
25	3,243,398	93,560	187,119	155,933	94,183
TOT	$3,243,398	$1,682,548	$3,365,096	$2,804,247	$1,693,765

LOCAL UNIVERSITY

Life Income Projections
Detailed Cash Flow Analysis

Page 2

Prepared for ANDRE' AND PRIDDY PRENEUR

March 14, 1995
Discount Rate for 2/95 is 9.6%

A Planning Opportunity for S Corporations

Recently, the IRS ruled that an S corporation can be a donor to a charitable remainder trust. The letter ruling, PLR 9340043, gives another alternative for the entrepreneurial giver.

LR 9340043. A subchapter S corporation contributed its 78% interest in a limited partnership to a charitable remainder unitrust of which the S corporation is the trustor. Immediately after the transfer, the limited partnership sold all of its assets. Under the terms of the trust instrument, the S corporation's sole shareholder is the trustee and his wife is successor trustee. The term of the trust is 20 years and the unitrust amount is payable to the S corporation. The unitrust amount is the lesser of the income of the trust for the taxable year as defined in sec. 643(b) of the Code or 5% of the net fair market value of the assets of the trust valued as of the first day of each taxable year of the trust. At the termination of the trust, the trustee will distribute the remainder of the trust assets to qualified charitable organizations and a private foundation created by the shareholder and his wife before their deaths, or if none, to other qualified charitable organizations.
The first issue was whether the S corporation could be a donor to a charitable remainder unitrust. The IRS ruled simply that there is nothing in sec. 664 of the Code or its regulations that would prohibit an S corporation from being a permissible donor to an otherwise qualified charitable remainder unitrust.

Second, the taxpayer sought a ruling that the trust qualified as a charitable remainder unitrust. First, to qualify, Sec. 664(d)(2)(A) requires that the unitrust amount must be paid "to one or more persons (at least one of which is not an organization described in section 170(c). . .)" for a term which "continues either for the life or lives of a named individual . . . or for a term of years not to exceed 20 years." Sec. 7701(a)(1) defines a "person" to include an individual, trust, estate, association, company, corporation, and partnership. Thus, the S corporation is a permissible recipient of the unitrust amount. The IRS found that the trust otherwise was qualified. The IRS notes that where a person other than an individual or a charity is a unitrust beneficiary, only a term of years trust may be used. See also LR 9205031 in the April/May 1992 CGPN.

Importantly, the IRS also ruled that the contribution by the S corporation of its partnership interest to the trust does not result in a constructive dividend to the shareholder. Further, the IRS computed the actuarial value of the remainder interest for the S corporation.

As for the charitable deduction, the IRS noted that to the extent that the S corporation is relieved of partnership liabilities by reason of the contribution, the transaction will be treated as part sale, part contribution and thus affected by the bargain sale rules. Moreover, the percentage limitations will apply as well as certain reductions.

Finally, the IRS ruled that the mere continued holding of its partnership interest after the partnership's assets have been transferred will not involve the trust in any income-producing activity which could be characterized as a trade or business and therefore will not result in the incurrence of any unrelated business income tax liability pursuant to sec. 512(c)(1). The IRS gave particular emphasis to the fact that the partnership assets were sold on the same day as the trust was created, implying that the brief holding period precluded the trust from having income (to the trust unrelated business income).

Note that the IRS also ruled that the unitrust document in this instance created a qualified charitable remainder trust. The IRS is willing to provide rulings of this nature in cases where no similar model form has been promulgated. In this case, no term of years forms have been published by the IRS.

The basic plan used in this ruling may have some helpful implications for gift planners. For example, a similar approach might be helpful as an alternative to a proposed gift of S corporation stock to a CRT. Having the corporation make the contribution might provide a solution for an otherwise-impossible gift.

A copy of PLR 9340043 is attached.

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PRIVATE RULING 9340043 printed in FULL format.

PRIVATE RULING 9340043

"This document may not be used or cited as precedent. Section 6110(j)(3) of the Internal Revenue Code."

SECTION 0170
Charitable, Etc. Contributions and Gifts

SECTION 0512
Unrelated Business Taxable Income (Taxable v. Not Taxable)

SECTION 0513
Unrelated v. Not Unrelated Trade or Business

SECTION 0664
Charitable Remainder Trusts
-- Definitions
-- Charitable Remainder Unitrust

SECTION 1366
Pass-Thru of Items to Shareholders

SECTION 1367
Adjustment to Basis of Stock of, and Indebtedness Owing Shareholders

0170-0000
0512-0000
0513-0000
0664-0302
1366-0000
1367-0000

PRIVATE RULING 9340043; 1993 PRL LEXIS 1620

DATE: July 8, 1993

REFER REPLY TO: [*1]

CC:P&SI:3/ TR-31-1326-92

* * *

This is in response to your letter dated July 10, 1992, and supplemental information concerning several ruling requests. Specifically, you have requested the following rulings: (1) that A is a permissible donor to the Trust; (2) that the Trust qualifies as a charitable remainder unitrust under section 664(d) of the Internal Revenue Code and that the Trust may pay the unitrust amount to A for a term of 20 years; (3) that the contribution by A of its general partnership interest in B to the Trust does not result in a constructive dividend to C; (4) that the actuarial value of the remainder interest and retained interest be computed; (5) that 12 percent of the actuarial value of the remainder interest shall be subject to the percentage limitations of section 170(b)(1)(A) and (C), and that 88 percent of the actuarial value of the remainder interest shall be subject to the percentage limitations of section 170(b)(1)(B) and (D); (6) that the general partner's pro rata share of the gain from the sale of B's assets to E will be allocated to the Trust; and (7) that for any year in which the Trust qualifies as a charitable remainder unitrust, the Trust will [*2] be exempt from taxes imposed by Subtitle A of the Code, unless it has any unrelated business taxable income as defined in section 512 of the Code and applicable regulations, and that no such income results from the transaction involved herein.

We will not issue a ruling on issue (6) because that determination is primarily one fact. See Section 4.02(1) of Rev. Proc. 93-3, 1993-1 I.R.B. 71.

Facts

The following facts have been represented.

A is a subchapter S corporation within the meaning of section 1361 of the code. C is A's sole shareholder. A is a general partner holding an approximately 78 percent partnership interest in B, a limited partnership (the partnership). A has been a partner in the partnership for approximately three years.

On October 21, 1992, A formed the Trust and transferred to the Trust its interest in the partnership. Prior to the transfer, the partnership distributed cash, accounts receivable, and any substantially appreciated inventory pro rata to the partners of B. Immediately after the transfer of the partnership interest to the Trust, B sold all its assets to E, a subsidiary of F.

Under the terms of the governing trust instrument, C is named [*3] trustee, and his wife, D, is designated the successor trustee if C is unable to serve. Also, under the terms of the governing instrument, A may at any time remove any presently acting or designated trustee or cotrustee or successor cotrustee and name a replacement or successor trustee or cotrustees.

The term of the trust is 20 years, and the unitrust amount is payable to A. The unitrust amount is the lesser of: (a) the income of the Trust for the taxable year as defined in section 643(b) of the Code; or (b) 5 percent of the net fair market value of the assets of the Trust valued as of the first day of each taxable year of the Trust.

At the end of the term of the Trust, the trustee will distribute not less than 12 percent of the remainder interest to organizations then described in section 170(b)(1)(A) of the Code. The trustee will distribute the remaining 88 percent of the remainder interest to a private foundation that will be created on or before the death of the last survivor of C and D. If, at the time the remainder interest is payable, the private foundation is not described in sections 170(c), 2055(a), and 2522(a), then the remainder interest will be distributed to organizations [*4] selected by the trustee that meet the requirement of those sections.

Qualification of A as a Permissible Donor

There is nothing in section 664 of the Code or the underlying regulations that would prohibit an S corporation from being a permissible donor to an otherwise qualified charitable remainder unitrust.

Qualification of the Trust as a Charitable Remainder Unitrust and the Term of the Trust

Section 664(d)(2) of the Code sets forth the requirements to be a charitable remainder unitrust. Section 664(d)(2)(A) provides that the unitrust amount must be paid "to one or more persons (at least one of which is not an organization described in section 170(c) and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals."

Section 1.664-3(a)(3)(i) of the Income Tax Regulations provides that the unitrust amount must be payable to or for the use of a named person or persons, at least one of which is not an organization described in section 170(c) of the Code. Section 1.664-3(a)(5)(i) provides that the period for which the unitrust [*5] amount is payable begins with the first year of the charitable remainder trust and continues either for the life or lives of a named individual or individuals or for a term of years not to exceed 20 years. Only an individual or an organization described in section 170(c) may receive an amount for the life of an individual.

Section 7701(a)(1) of the Code defines a "person" to include an individual, trust, estate, association, company, corporation, and partnership.

In the present situation, the Trust provides that the unitrust amount is payable for a term of 20 years. Because the term of the Trust is a term of years not to exceed 20 years, the recipient of the unitrust amount may be any person or persons, including a corporation, so long as at least one such person is not a charitable organization. Thus, A is a permissible recipient of the unitrust amount.

The governing instrument of the Trust as submitted contains provisions set forth in Rev. Rul. 72-395, 1972-2 C.B. 340, as modified by Rev. Rul. 80-123, 1980-1 C.B. 205, and Rev. Rul. 82-128, 1982-2 C.B. 71, and clarified by Rev. Rul. 82-165, 1982-2 C.B. 117.

Accordingly, the Trust will qualify as a charitable remainder [*6] unitrust, for federal income tax purposes, for any year in which it continues to meet the definition of and functions exclusively as a charitable remainder unitrust. For such year, the Trust will be exempt from taxes imposed by subtitle A of the Code unless it has any unrelated business taxable income as defined in section 512 and the applicable regulations.

Constructive Dividend to C

The contribution by A of its partnership interest in B to the Trust does not result in a constructive dividend to C.

Actuarial Value of the Remainder Interest

The value of the remainder interest is computed for the contribution made to the Trust on October 21, 1992. With interest at 7.8 percent, an adjusted payout rate of 5 percent times .954353 (equalling 4.772 percent), and with quarterly payments at the end of each quarter for which they are paid, the present worth of the remainder interest in a unitrust which falls in 20 years after the transfer is $ 0.376130 for each $ 1.00 of the initial trust corpus.

Limitations on Charitable Contribution

Section 1366(a)(1)(A) of the Code provides that a shareholder in a subchapter S corporation determines his tax liability by taking into account his [*7] pro rata share of the corporation's items of income, loss, deduction, or credit that if separately stated and given separate treatment on his individual income tax return could affect his tax liability. The flush language of section 1366(a)(1) provides that items referred to in section 1366(a)(1)(A) include amounts described in section 702(a)(4). Amounts described in section 702(a)(4) are charitable contributions as defined in section 170(c).

Section 1367(a)(2)(B) of the Code provides that the basis of each shareholder's stock in an S corporation shall be decreased by the items of loss and deduction described in section 1366(a)(1)(A) determined with respect to the shareholders.

In the present case, the amount of the charitable contribution may be affected by the bargain sale rules. To the extent that A is relieved of partnership liabilities by reason of the donation, the transaction will be treated as part sale, part contribution. See Rev. Rul. 75-194, 1975-1 C.B. 80. The rules for computing the sale and the contribution portions in such a case, and for applying the reduction provision in section 170(e)(1), are set forth in the Code and the regulations under sections 170 [*8] and 1011(b). See sections 1.170A-4(c)(2)(i); 1.1011-2(a)(3); 1.1011-2(b).

Provided there is no part gift, part sale under the bargain sale rules, the amount of the charitable contribution will be the fair market value of the remainder interest of A's interest in B, reduced in accordance with the applicable provisions of section 170(e) of the Code. C, as the sole shareholder of A, will take this charitable contribution into account pursuant to section 1366(a)(1)(A) and will reduce the basis of C's stock in A by this amount pursuant to section 1367(a)(2)(B). The limitations applicable to individuals set forth in section 170(b) apply in determining C's allowable deduction for the charitable contribution.

Section 170(f)(2)(A) of the Code provides that in the case of property transferred in trust, no deduction shall be allowed for the value of a contribution of a remainder interest unless the trust is a charitable remainder annuity trust or a charitable unitrust (described in section 664) or a pooled income trust (described in section 642(c)(5)).

Section 170(b) of the Code provides percentage limitations for the charitable contribution deductions of individuals. Generally, individuals [*9] may deduct contributions to organizations listed in section 170(b)(1)(A) to the extent that the aggregate of such contributions does not exceed 50-percent of the taxpayer's contribution base (generally, adjusted gross income) for the taxable year. Deductions for charitable contributions to organizations other than those listed in section 170(b)(1)(A) are generally limited to 30 percent of the taxpayer's contribution base for the taxable year.

Section 1.170A-8(b) of the regulations provides that to qualify for the 50-percent limit the contributions must be made "to," and not merely "for the use of," a section 170(b)(1)(A) organization.

Section 1.170A-8(a)(2) of the regulations provides that a contribution of a remainder interest in property, whether or not the contributed interest is transferred in trust, for which a deduction is allowed under section 170(f)(2)(A) or (3)(A) of the Code, is considered as made "to" the charitable organization except that, if the interest is transferred in trust and, pursuant to the terms of the trust instrument, the interest contributed is, upon termination of the predecessor estate, to be held in trust for the benefit of the organization, the contribution [*10] is considered as made "for the use of" the organization.

In Rev. Rul. 79-368, 1979-2 C.B. 109, a charitable organization described in section 170(b)(1)(A) of the Code is designated as the recipient of the remainder interest in a qualified charitable remainder unitrust. Under the terms of the trust, the grantor and surviving income beneficiaries have the power at any time to substitute for the named recipient any other charitable organization described in section 170(c). Thus, the grantor and the surviving beneficiaries have the power to change the recipient of the remainder interest in the trust from an organization that would qualify for the 50-percent limit on contributions under section 170(b)(1)(A) to an organization that would be subject to the lower limit on contributions set by section 170(b)(1)(B). The ruling holds that because of this power the charitable deduction is subject to the lower section 170(b)(1)(B) limit.

The general percentage limits under section 170(b) of the Code are modified, under sections 170(b)(1)(C) and 170(b)(1)(D), if the property contributed is capital gain property.

For this purpose, "capital gain property" is defined in section 170(b)(1)(C)(iv) [*11] of the Code as, with respect to any contribution, any capital asset the sale of which at its fair market value at the time of the contribution would have resulted in gain which would have been long-term capital gain. Section 1222(3) provides that the term "long-term capital gain" means gain from the sale or exchange of a capital asset held for more than 1 year, if and to the extent that the gain is taken into account in computing gross income

Section 741 of the Code provides that in the case of a sale or exchange of an interest in a partnership, gain or loss is recognized to the transferor partner. Such gain or loss is considered as gain or loss from the sale or exchange of a capital asset, except as otherwise provided in section 751 (relating to unrealized receivables and inventory items which have appreciated substantially in value). Section 751 provides that to the extent attributable to these items, the sale or exchange of a partnership interest results in ordinary income.

Generally, the amount of a charitable contribution of property, including a charitable remainder unitrust interest, is its fair market value, as reduced under section 170(e)(1) of the Code. Section [*12] 1.170A-1(c)(1) and section 1.170A-6(b)(2) of the regulations.

Under section 170(e)(1) of the Code, the amount of a contribution of property is reduced by the amount of gain which would not have been long-term capital gain if the property had been sold at its fair market value. Thus, the amount of a contribution of long-term capital gain property is generally the fair market value of that property. Under section 170(e)(1)(B), however, the amount of a contribution is reduced by the amount of gain which would have been long-term capital gain in two situations: (1) the property is tangible personal property whose use by the donee is unrelated to the donee's exempt purpose or function; or (2) the contribution is to or for the use of a private foundation not described in section 170(b)(1)(E).

With respect to contributions of long-term capital gain property (not described in section 170(e)(1)(B) of the Code) to organizations described in section 170(b)(1)(A), section 170(b)(1)(C)(i) provides generally that the total amount of contributions which may be deducted for any taxable year may not exceed 30 percent of the taxpayer's contribution base for the year. However, under section 170(b)(1)(C)(iii), [*13] a taxpayer may elect to have the 50-percent limit apply, if the amount of the contribution is reduced as provided in section 170(e)(1).

With respect to contributions of long-term capital gain property to organizations described in section 170(b)(1)(B) of the Code, section 170(b)(1)(D) provides that the total amount of contributions deductible for any taxable year may not exceed the lesser of (1) 20 percent of the taxpayer's contribution base for the taxable year or (2) the excess of 30 percent of the taxpayer's contribution base for the taxable year over the amount of the contributions of capital gain property to which section 170(b)(1)(C) applies.

Section 57(a)(6)(A) of the Code provides that an item of tax preference for alternative minimum tax purposes includes the amount by which the deduction allowable under section 170(f)(2)(A) would be reduced if all capital gain property were taken into account at its adjusted basis. Section 57(a)(6)(B) defines "capital gain property" the same as does section 170(b)(1)(C)(iv), but excludes any property to which an election under section 170(b)(1)(C)(iii) applies.

Since the Trust in this case qualifies as a charitable remainder unitrust [*14] as described in section 664 of the Code, a charitable contribution deduction will be allowed under section 170(f)(2)(A) for the value of the remainder interest, subject to certain reductions and percentage limitations.

In determining these percentage limits, the contribution of the remainder interest in the trust will be considered to have been made "to," rather than "for the use of," charitable organizations because, at the end of the charitable trust term, the remainder interest will be distributed to charitable organizations outright and not in trust. See section 1.170A-8(a)(2) of the regulations. Applying the rationale of Rev. Rul. 79-368, section 170(b)(1)(A) of the Code applies to 12 percent of the remainder interest, since a minimum of 12 percent of the remainder interest must be distributed to section 170(b)(1)(A) organizations. In this regard, the fact that the trustee has the discretion to determine the specific donee or donees within the class of section 170(b)(1)(A) organizations is not relevant. Because it is not possible to determine what portion, if any, of the remainder interest over 12 percent will be distributed to section 170(b)(1)(A) organizations, section [*15] 170(b)(1)(B) applies with respect to the other 88 percent of the remainder interest.

The contribution amounts and percentage limits are also affected by the rules of section 170(b)(1)(C) and (D) and section 170(e) of the Code. Under section 741, the contributed partnership interest will be a capital asset at the time of the contribution, and no part of the contributed interest will be attributable to section 751 items that would yield ordinary income had the partnership interest been sold. The partnership interest is long-term capital gain property, as defined in section 1223(3), because A has held the partnership interest for more than one year. Therefore, section 170(b)(1)(C)(i) applies to the 12-percent portion of the remainder interest contributed to section 170(b)(1)(A) organizations and decreases the percentage limit applicable to the charitable contribution of that portion to 30 percent. Section 170(b)(1)(D) applies to the other 88 percent of the remainder interest and reduces the applicable percentage limit for the charitable contribution of that portion of the remainder interest to 20 percent.

The amount of the charitable contribution of the 88-percent portion of [*16] the remainder interest will also be reduced under section 170(e)(1)(B)(ii) of the Code, since long-term capital gain property is being contributed to a private foundation. This assumes that the foundation that C and D create qualifies as a private foundation as defined in section 509(a) and is not a private foundation described in section 170(b)(1)(E). Section 170(e)(1)(B)(ii) reduces the amount of the charitable contribution by the amount of any long-term capital gain that would have resulted if the partnership interest had been sold.

For alternative minimum tax purposes, the 12-percent portion of the remainder interest that is being contributed to section 170(b)(1)(A) organizations is subject to the tax preference item under section 57(a)(6) of the Code, since the amount of the contribution of that portion of the remainder interest has not been reduced under section 170(e)(1). The amount of the tax preference item is the amount by which the deduction allowed under section 170 for the 12-percent portion of the remainder interest exceeds the adjusted basis of that portion of the remainder interest. However, if C elects under section 170(b)(1)(C)(iii) to reduce the amount of the [*17] contribution of the 12-percent portion under section 170(e)(1) in return for a 50-percent limit, then no tax preference item would exist. No tax preference item exists with respect to the other 88 percent of the remainder interest, assuming that the amount of the contribution is reduced under section 170(e)(1)(B) to the adjusted basis of the contributed property.

Unrelated Business Income

Section 664(c) of the Code states that a charitable remainder annuity trust and a charitable remainder unitrust shall, for any taxable year, not be subject to any tax imposed by this subtitle, unless such trust, for such year, has unrelated business taxable income (within the meaning of section 512, determined as if part III of subchapter F applied to such trust).

Section 1.664-1(a) of the regulations states that a trust created after July 31, 1969, which is a charitable remainder trust is exempt from all of the taxes imposed by subtitle A of the Code for any taxable year of the trust except a taxable year in which it has unrelated business taxable income.

Section 512(a)(1) of the Code states that the term "unrelated business taxable income" means the gross income derived by any organization [*18] from any unrelated trade or business (as defined in section 513) regularly carried on by it, less the deductions allowed by this chapter which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

Section 512(b)(5) of the Code excludes from the calculation of unrelated business taxable income all gains or losses from the sale, exchange, or other disposition of property other than stock in trade or other property of a kind which would properly be includible in inventory if on hand at the close of the taxable year, or property held primarily for sale to customers in the ordinary course of the trade or business.

Section 512(c)(1) of the Code states that if a trade or business regularly carried on by a partnership of which an organization is a member is an unrelated trade or business with respect to such organization, such organization in computing its unrelated business taxable income shall include its share of the gross income of the partnership (whether or not distributed).

Section 513 of the Code states that the term "unrelated trade or business" means any trade or business the conduct of which [*19] is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of the purpose or function constituting the basis for its exemption under section 501.

Section 1.513-1(b) of the regulations states that, for purposes of section 513 of the Code, the term "trade or business" has the same meaning it has in section 162, and generally includes any activity carried on for the production of income from the sale of goods or performance of services.

The sale of B's assets, effectuated by the Trust, as general partner, in the circumstances described, does not involve a sale of inventory or property held primarily for sale to customers in the ordinary course of the business of an investment management and advisory company. Therefore, under section 512(b)(5) of the Code, gain on the sale of B's assets will not produce unrelated business taxable income to the Trust.

Since the sale of the partnership assets occurred on October 21, 1992, the same day of the Trust's receipt of its interest in the partnership, the Trust was not the owner of a partnership interest in an unrelated [*20] trade or business, which would have produced unrelated business taxable income to the Trust. Therefore, the transaction will not result in the Trust's incurring any unrelated business income tax liability pursuant to section 512(c)(1) of the Code.

The mere continued holding of its partnership interest after the partnership's assets other than office furnishings and equipment have been transferred to the subsidiary of F will not involve the Trust in any income producing activity which could be characterized as trade or business. Therefore, the Trust's mere holding of such partnership interest after the transfer of assets to F's subsidiary, as described previously, will not result in the Trust's incurring any unrelated business income tax liability pursuant to section 512(c)(1) of the Code.

Accordingly, we have concluded that the Trust will not realize any income subject to unrelated business income tax as a result of the transactions described above.

No opinion is expressed as to any other provisions of the Trust. No opinion is expressed as to the federal tax consequences of the formation or operation of the Trust under the provisions of any other section of the Code.

A [*21] copy of this letter should be attached to the federal tax return for the tax year that the Trust is formed. A copy of this letter is enclosed for that purpose.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) of the Code provides that it may not be cited as precedent.

Sincerely yours,
Frances D. Schafer
Senior Technician Reviewer
Branch 3
Office of Assistant Chief Counsel
(Passthroughs and Special
Industries)
Enclosures (2)
One copy of this letter
Copy for section 6110 purposes

Charitable Gift Annuities -- Basic

W. Earl Taylor, C.F.R.E.
Executive Director, Omaha Community Foundation

The purpose of this workshop is to do what has been done 21 times before. Every Conference on Gift Annuities has scheduled time for a basic survey of the Charitable Gift Annuity. My challenge, in preparation for this 22nd time, was to revisit the basics while trying to refrain from blatant plagiarism of the work accomplished by those who came before. At the same time, I'm challenged to communicate anew with fund raising professionals who harbor a disdain for gift annuities because they've been told something like: "you will put at risk all the agency's assets," or, "you'll be promoting a program that will result in getting less money than the donor gave you in the first place."

Back in Omaha we are treated to periodic insights concerning the wit, lifestyle and thought patterns of a very successful investor. A reason for Warren Buffett's success is that he believes in keeping things simple. "If the restaurant serves a hamburger or steak you like, why search out a diner across town?"

When Buffett bought his first billion dollars worth of Coca Cola stock he exclaimed, "Coke is exactly the kind of company I like. I like products I can understand. I don't know what a transistor is, for example."

In contrast to a plethora of complex estate planning techniques, the gift annuity is something any of us can understand. As in the case of Warren Buffett's emulators, however, there are all to few gift annuity advocates who effectively subscribe to KISS -- so, today, lets make sure we really know the basic attributes of the simple gift annuity, and I'll try to remind myself to *Keep It Simple, Stupid*.

Let's start with the easiest definition I've come across: " 'The Charitable Gift Annuity is a contractual arrangement between a donor and a charitable institution whereby the donor makes a gift to the charity, and the charity agrees to pay a specified income to the donor for life.' "

Emphasis should be added to three parts of that definition. First, the CGA is a *contract* and not a trust as are most other deferred gift instruments. When face to face with a prospective annuitant I'm moved to suggest that "the proceeds from the sale of this desk will go to you before we fail to meet one of your annuity payments." Indeed, gift annuity payments are secured by the entire assets of any issuing agency and not just by the property contributed.

Second, the person makes a *gift* to the charity. This is the glue that has held this arrangement together a hundred years longer than any other type of planned gift outside of the charitable bequest. If there were no charitable motivation the person ought to buy a commercial annuity and receive a higher rate of return.

Third, is the *specified income* that your institution obligates itself to pay for life. Since 1927 it has been during this Conference, called every three years by the Committee on Gift Annuities--now the Council on Gift Annuities--that when recommended gift annuity rates have been announced. In October of 1993, the Board of Directors of the American Council on Gift Annuities made an interim rate adjustment between triennial Conferences. These rates have been provided as a service to charities offering gift annuities, and each charity has decided whether to follow these rates or a different set of rates.

Different, durable and eminently do-able as the corn flakes ad suggests, let's revisit the flavor of the basic 150 year old gift annuity as if you were tasting it for the first time.

Perhaps fund raising professionals too often start with the recommended rate guide as the beginning point in their mental workup before talking with a prospective donor, or in seeking Board approval to launch a gift annuity program.

Potentially, they would believe more in gift annuities if they better understood the implications of why rates change and how rates are carefully designed to make sure that ultimately there will be resources to carry out their agency's mission. A good understanding of the historical basis for gift annuities might be insightful and would help to frame dialogue with others, but it is really more important to stone cold know the five assumptions upon which the recommended rates are based.

The most recent rates recommended by the American Council on gift annuities are based on the following five assumptions, which can be remembered by the word "PRIME."

P **Payout** to annuitants will be made in installments at the end of each 6 months.

R **Residuum** (remaining amount) available to the charitable organization at the death of the last annuitant will be 50% of the amount paid for the gift annuity.

I **Interest** will be earned at the rate of 5.5% per year, compounded annually.

M **Mortality** will occur in accordance with the mortality rates of the 1983 Table "a" for female lives with ages set back one year.

E **Expenses**, both initial and future, are to come from 5% deducted immediately from the amount paid for the gift annuity and held in an invested reserve for administrative costs to be paid from such 5% and from interest thereon.

Payout assumption

Most annuities will probably have a payout frequency different from semi-annually. In picking an interval between quarterly and annually, this assumption is simply a mid point that results in minimal impact on the amount of the residuum.

Residuum assumption

A 50% residuum is the result when all assumptions are realized exactly. When managing an annuity investment pool, a logical extension of this concept is that only 50% of original gifts from early deaths should be released for the agency's use in order to also provide a 50% residuum for those who outlive their life expectancies. However, new standards of fiduciary duty may dictate to your trustees that greater flexibility be incorporated into managing risk than has been previously thought to be prudent.

Several annuity issuing institutions hire actuarial firms to assist in determining whether their annuity investment pools are properly funded or over funded. They do this to be assured they are adequately managing risk and with an objective of releasing funds for current operations. Such discussion is probably best left for other workshops. Suffice to say in our time together that any variance should never be pursued in ignorance of either these basic assumptions or individual state regulations.

Interest assumption

Interest and mortality estimates are the two assumptions most closely reviewed when changes in the recommended rates are anticipated. When it was possible to earn double digit returns on bank CD's just a few years ago, a 5.5% assumption would have appeared low. When projecting future interest earnings, however, a high degree of conservatism is prudent. Historically, the Committee's interest assumption has been lower than the prevailing 30-year treasury rate.

Frank Minton has published these observations on the financial risks of gift annuities:

- If the charity achieves a total return of only 5.5% on annuity assets, an annuitant (or two annuitants) would have to exceed life expectancy by 50-90% before the charity would lose money on a particular annuity.

- If the charity achieves a total return of 6.5% on annuity assets, an annuitant (or two annuitants) would have to live to age 100 or older before the charity would lose money on a particular annuity.

- If the charity achieves a total return of 7.5% on annuity assets, it is virtually impossible to exhaust reserves.

Mortality assumption

While commercial annuities often distinguish between males and females when setting rates, life expectancy input for gift annuities has always been based on a unisex assumption. Therefore, a gift annuity pool composed of only females should be viable given the basis of this assumption alone, but further safeguard is added with an age set back of one year. An annuity pool that includes male annuitants operates with an even more conservative return projection.

Expense assumption

Would you like both the principal and earnings from a $50,000 fund to help pay expenses for administering your gift annuity program? Well, 5% of a million dollars will get you there, and an 8% return on that would net $4,000 annually for operating.

If you don't take 5% off the top of every new annuity for expenses you will certainly further increase the conservancy of rate assumptions. Not covering institutional administrative expenses may also diminish staff zeal and their advocacy of gift annuities.

Personally, I like the incentives built into the gift annuity assumptions. Not only are we able to book a portion of the gift annuity as an immediate asset, we also get an immediate boost in our operating reserves.

Fundamental federal tax aspects of the CGA

A donor who is issued a gift annuity is entitled to a charitable deduction in the year of the gift equal to the amount of money or the fair market value of the property *less* the value of the life benefiary's interest or "actuarial value."

The "actuarial value" is determined by multiplying the annuity payments by the amount necessary to produce a dollar of income annually over the donor's life expectancy. IRS Tables R(1) for single lives & R(2) for joint lives are used to determine the actuarial value of gift annuities. *These tables are completely different from the Council's recommended rate tables that pertain to the size of the annual gift annuity payments.*

Annuity payments are taxed as ordinary income though a portion of each payment is excluded because it is a return of the principal initially gifted. The easiest way to grasp this concept is to expect that an annuity's earning power will diminish as payments are made, and that eventually the principal will be invaded to make payments. It is this estimated and prorated return to the donor of her own money that results in the tax-free portion of each annuity payment.

When the donor is an annuitant, and the donor's appreciated property was given for the annuity, capital gain is reportable over the life of the annuity. The advantage to the donor is that as each year passes and inflation takes its toll, the cost of paying the capital gain tax decreases.

Because these transactions are also treated as bargain sales, the donor additionally benefits from partially avoiding taxes on some of the capital gain. In other words, the portion of the gift that provided the "actuarial value" is viewed as having been sold by the donor and is subject to capital gain reporting though the gain can be prorated over life expectancy of the dnoor provided the donor is the annuitant. The other portion, that segment of the gift that resulted in determining the income tax deduction, also avoids capital gain reporting.

Once the capital gain is fully reported (the annuitant outlives her life expectancy), the entire annuity payment will be taxed as ordinary income. However, should the donor die before expected, another avoidance of capital gain tax is realized.

An estate tax deduction is available for annuities established at end of life.

While a donor is living, an annuity can be established to benefit another person and qualify for the annual $10,000 gift tax exclusion. When an annuity allows for payments to a successor following the donor's death, there is no longer a present interest and payments would be subject to gift tax consequences. However, if the same donor retained the right to revoke the successor interest by will, then no completed gift has been made and the gift tax is avoided.

How do you start an annuity program?

Perhaps the best advice I received before initiating my first annuity program in a hospital setting was -- just do it!

Though I, in turn, have urged scores of fund raisers to 'just do it' I know many fledgling efforts are bolstered by offers of help from those with experience in administering annuity programs, particularly within states that seek to regulate the issuance of gift annuities. Help can be extended through providing and interpreting gratuitous computer runs, by specifically answering questions, or by participating in assurance meetings with staff leaders and Board volunteers. Community foundations can extend the offer to manage annuities as part of an agency's endowment building efforts.

The American Council on Gift Annuities provides sample documents and worksheets. I began by using their forms to hand calculate annuities before buying our Foundation's handy software just last year.

Now I'm an advocate for you to at least once take the time to work up calculations by hand and then check your work against computer generated results. It will help you better understand how payment frequency and federal midterm rates alter the equation, how capital gain is partially avoided and what is meant by the "tax-free" portion of an annuity payment being a return of the donor's own money.

Whether for your own calculations or before asking for help using somebody else's software, it's good to have a checklist of general information items needed to fully process and calculate a CGA. Here's one list to get you started:

- Full name and birth date of all donors and beneficiaries. (Agreements are not written on more than two lives and ACGA recommended rates are quoted based on actuarial age which is the age to the nearest birthday.)
- Specifically identify those who are male and female beneficiaries.
- Full address and social security numbers for all of those above.
- The amounts and type of assets that will fund the CGA. Cash is easy, otherwise you'll need the basis of the asset, its present value and an indication of the actual owner. (Will your institution and the involved state allow you to accept the asset in exchange for a gift annuity?)
- Frequency of payment requested. (*Plan for payments to arrive on due dates*.)
- The date the gift will actually be delivered.
- Any additional information that may be helpful: I.e., clarification of who is donor who is beneficiary (If donor is not annuitant all capital gain is reported in year of gift and gift tax consequences may result when payments exceed the $10,000 annual exclusion); end restrictions agreed to should be detailed in a separate agreement that takes effect at the termination of the annuity, etc.

Three details -- in case no one else has told you

- You are obligated to provide 1099R Forms to all annuitants by January 31st of each year and report that information to IRS by February 28th on Form 1096.
- Should you be unaware of an annuitant's death and forward a payment, or if death occurs between the time you send a payment check and the actual payment due date, you are obligated to ask for a refund and are advised to document your efforts in seeking such a refund from the annuitant's estate. If an annuitant dies on the due date the payment belongs to the estate.
- Gift annuities are legally binding contracts. If a charity reinsures with a commercial firm that goes bust, payments from the charity are still due.

Who would you add to this list of best prospects for gift annuities?

- Devotees actively involved with accomplishing your agency's mission
- Supporters who have cash to contribute or those who want to turn collections or other tangible personal property into tax deductible life income gifts.
- Your oldest constituents -- often with the collaboration of relatives/heirs
- Younger donors who want to supplement their pension plans (Professionals in highly litigious areas or career paths may consider gift annuities because they are not vulnerable to legal confiscation. Others may plan for deferred gift annuity payments before their retirement funds become available.)

What do you tell your publics about your new/revitalized gift annuity program?

The Omaha Community Foundation's promotional flier touts gift annuities as our simplest plan for providing mature donors with a fixed life income from irrevocably gifted assets worth $10,000 or more. On the back panel is listed what a donor receives when they contract for an annuity with us:

- Satisfaction of making a gift.
- Annual payments you can't outlive -- regular, dependable, unchangeable.
- Tax benefits, such as the initial deduction, delayed capital gain taxation, annual payments that are partially tax-free, and reduction of possible estate taxes and expenses.
- Fewer worries about money management or investment matters.
- Payments that don't penalize age -- the older you are, the larger your payments.
- Flexibility -- amounts to fit your needs and means, and types of gift annuities that can help fulfill your responsibilities.
- A unique way to give while you are alive.

As a community foundation, we offer two additional incentives using special agreements that take effect at the end of the annuitant's life:

- With larger gifts you may add to or create an advised fund and involve heirs in annually advising as to charitable distribution of earnings.
- A managed permanent named fund ($25,000+) that through the years will help many agencies advance their missions.

Doing it ethically, does it make life all that much more difficult?

You have printed on various documents that donors are urged to consult their own advisor. Is it then "buyers beware" and OK to continue with executing any agreement?

Should prospects be counseled until the gift planner is comfortable that there'll be adequate cash flow to meet future needs? Who determines the donor's best interest?

Do gift planners have an ethical responsibility to point out to 'younger' prospective annuitants -- those in their 60's or 70's and who are in good health -- that CGA's produce fixed income that will buy less and less as time progresses?

If you or your institution does not like offering charitable remainder trusts but your handy software projects donors will get a better return from a 5% unitrust over their life expectancies, are you obligated to say anything in pursuit of a full and accurate explanation of all aspects of your proposed charitable gift annuity?

The Council's annuity rates are suggested maximum rates -- they are not mandatory. I've observed that virtually all institutions either adhere to the rates or negotiate rates with donors that are less than the Council's recommended maximums. But your institution can offer rates based on a different set of actuarial assumptions. It should probably hire an actuarial firm to make the computations.

A few closing observations and cautions:

Conservancy is, in theory, exercised by states seeking to regulate gift annuities.

New prudent man rules as promulgated by the Uniform Management of Institutional Funds Act suggest that managing risk is preferable to sitting on fixed income portfolios.

There are terms to avoid when promoting your gift annuity program.

Stay away from for-profit marketing ideas. Gift annuities are not sold, they are issued in support of your organization. Don't suggest you have "returns that are higher than banks pay" or even use "competitive with" examples. Emphasize that gifts are being made that benefit your institution and community.

You may invest the donor's gift but the donor is not "investing" with you. In the instance of gift annuities find another warm fuzzy way to explain how the donor is helping provide for the positive future envisioned for your institution. It follows that you will be sending annuity payments not "interest" payments.

Because of the nomenclature of local commercial annuity companies, we are currently working to eliminate "guarantee" from our foundation's annuity lexicon.

Several years ago I came away from a visit at Oberlin College in Ohio with this terminology: "While the College maintains a reserve fund to meet its gift annuity commitments, in a larger sense, the total assets of the College stand as your guarantee. -- There are very few safer investments available today."

While we might agree to change a couple of their words, I'm partial to the way they convey the extent of their commitment as embodied in their promotional text.

When the next conference rolls around will you be a have or a have not?

Haves will be those blessed with enough determination to wade into doing gift annuities with little or minimal help but knowing that help is there for the asking. Have nots will still be cowed by the prospect of running up against state regulations or board level conservatism.

Haves will be at work plussing inherited annuity programs or busy getting their arms around the details of a program that is finally up and running -- have nots will still be on the outside of those unexpected conversations with annuitants who now call you rather than avoid you.

Haves will be advocating that God intended for annuitants to do God's work -- have nots will probably still be viewing annuities as God-awful.

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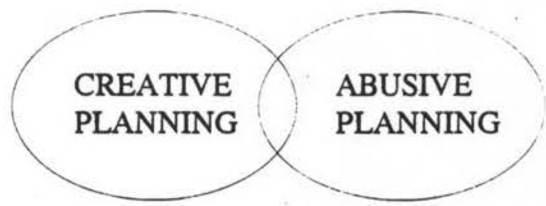
CREATIVE APPLICATIONS OF NET-INCOME UNITRUSTS

Presented by Jonathan G. Tidd

I. INTRODUCTION

A. Diagram



B. Key Questions

1. Does the proposed plan benefit (arguably) <u>both</u> the donor and the charitable remainder beneficiary?

2. Under the proposed plan, does the donor come off looking <u>greedy</u> (gluttonish, if you prefer)?

In <u>Notice 94-78</u>, which dealt with the 2-year, 80-percent payout straight unitrust, the benefit to charity was minimal, and the donor appeared to be excessively hoggish.

C. To What Extent Can You Rely on Private Letter Rulings?

1. IRS has ruled favorably, for example, on putting a zero-coupon bond in a net-income unitrust. <u>Letter Ruling 8604027</u>.

2. But you can't rely on someone else's private ruling.

3. And IRS, from time to time, does change its mind about previously issued private rulings.

A recent example is <u>Letter Ruling 9501004</u>, in which IRS pulls an earlier favorable ruling on using <u>options</u> to create a unitrust.

II. A FEW BASICS: WHAT <u>IS</u> A NET-INCOME UNITRUST?

A. Basic Definition

1. What we call a net-income unitrust (without a makeup provision) is a unitrust that pays out each year whichever is less:

a. the stated unitrust percentage amount, or

b. the trust income as defined in section 643(b) of the Internal Revenue Code.

2. "Income" under section 643(b) is trust accounting income -- which is not necessarily the same as income for federal income tax purposes. (Trust accounting income is net of expenses.)

> Example: Tax-exempt bond interest is income for trust accounting purposes but not federal income tax purposes.

3. The key question from a planning standpoint then becomes whether under the proposed gift plan, the trust will have accounting income.

B. How Is Trust Accounting Income Defined?

1. You look to:

a. applicable local law -- which typically is the old or new version of the Uniform Principal and Income Act (UPIA), and

b. the trust instrument.

2. Under the UPIA, the settlor of a trust has freedom to define income and principal as he or she pleases.

> The UPIA provides a "default" definition of accounting income and principal.

3. IRS, however, won't respect a trust provision that defines something that is fundamentally income (the regs use the example of ordinary dividends or interest) as principal. Income Tax Regulation section 1.643(b)-1.

III. PLANNING PROBLEM

A. Facts for Discussion

1. Donna, aged 72, wants to use some highly appreciated, undeveloped land to establish a 7-percent charitable remainder unitrust.

2. Donna's lawyer has advised her that a "flip trust" is not possible, in view of Letter Ruling 9506015. In this ruling, IRS takes the position that a unitrust instrument may not provide for a change in the method of computing the unitrust amount during the term of the trust.

3. Donna, however, is uncomfortable with the idea of a net-income unitrust, for fear that it won't earn 7 percent in terms of net income.

B. Question and Discussion

1. Would it all right for Donna to set up a net-income unitrust and define trust

accounting income to include realized capital gains?

This arrangement might not allay her fears entirely, but it would hedge to a degree against an environment in which interest rates were low and stock prices were high and rising.

2. Discussion

a. Under the UPIA, the settlor of a trust pretty clearly can define trust accounting income to include realized gains (which generally are allocated to principal).

b. But will IRS respect such a definition?

Realized gains are not as fundamentally in the nature of principal as dividends and interest are in the the nature of income.

For example, in some states (New York, for one), an under-productive property rule treats appreciation on trust assets as income to a certain extent if the trust has not produced a certain minimum amount of income.

Furthermore, IRS regulations do at one point acknowledge that trust accounting income may be defined to include realized gains. See Income Tax Regulation section 1.643(a)-3(a).

Finally, in Letter Ruling 9442017, IRS ruled it was OK for a unitrust trustee to allocate a reasonable portion of realized gains to trust income (this ruling involves Nebraska law).

3. Further discussion: Apart from the example we're considering, what are the pros and cons of setting up a net-income unitrust and defining trust accounting income to include realized gains?

¶ Investing for total return -

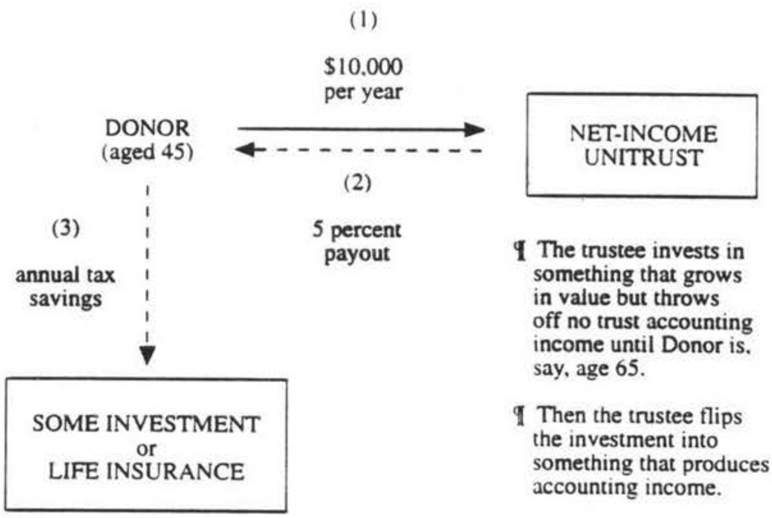
¶ Flexibility in timing distributions (but be careful of self-dealing) -

¶ Potential lack of flexibility, depending on market conditions -

¶ Potential problems if there is a make-up provision -

IV. THE "BUILD-UP" UNITRUST AS A WAY TO PROVIDE FOR FUTURE INCOME

A. The Basic Game Plan -- a Typical Illustration



B. Example

1. Donor, who is aged 45 contributes <u>$10,000 a year</u> to a <u>5-percent</u> net income unitrust, with a make-up provision, for the next <u>20 years</u>.

3. The trust is able to earn (in terms of capital appreciation or other non-trust-accounting-income earnings) <u>10 percent</u> a year.

4. In year 21, the trustee <u>flips</u> the trust investments into something that produces 10-percent income (an optimistic assumption in terms of today's economy).

5. The spreadsheets on the next 2 pages show, to a fairly good degree of approximation, how the numbers work out for the donor.

C. Investment Schemes

1. Zero-coupon tax-exempt bonds (bought at a discount)

   a. Is <u>the annual increase</u> in the value of the bonds due to the decreasing length of time to maturity <u>trust accounting income</u>?

      If so, the scheme <u>doesn't work</u>, because the trustee has to make an annual payout.

      Whether the annual increase is trust accounting income depends on <u>local law</u> and the <u>trust instrument</u>. See, e.g., <u>Letter Ruling 8604027</u>.

ASSUMPTIONS

Initial Age	45
Annual Contribution	10,000
Trust Payout Rate	0.05
"Life Expectancy"	40
Tax Bracket	0.36
Trust Investment	0.10
Discount Rate (PV)	0.06

Invest $10,000
per Year at 6%
for 20 Years
$114,699

Total Benefit
from Trust
$133,528

Present
Value
Comparison

Amount Eventually
Passing to Charity
$1,214,466

Present Value of
Charitable Benefit
$118,073

Year	Tax Savings	P.V. Savings	A-T Income	P.V. Income
1	867	867	0	0
2	900	849	0	0
3	934	831	0	0
4	969	813	0	0
5	1,003	795	0	0
6	1,039	777	0	0
7	1,075	758	0	0
8	1,114	741	0	0
9	1,151	722	0	0
10	1,190	705	0	0
11	1,230	687	0	0
12	1,270	669	0	0
13	1,311	652	0	0
14	1,353	634	0	0
15	1,395	617	0	0
16	1,438	600	0	0
17	1,482	583	0	0
18	1,525	566	0	0
19	1,569	550	0	0
20	1,613	533	0	0
21	0	0	40,322	11,861
22	0	0	40,322	11,189
23	0	0	40,322	10,556
24	0	0	40,322	9,959
25	0	0	40,322	9,395
26	0	0	40,322	8,863
27	0	0	40,322	8,361
28	0	0	30,404	5,948
29	0	0	20,657	3,812
30	0	0	21,690	3,776
31	0	0	22,774	3,741
32	0	0	23,913	3,705
33	0	0	25,108	3,670
34	0	0	26,364	3,636
35	0	0	27,682	3,602
36	0	0	29,066	3,568
37	0	0	30,519	3,534
38	0	0	32,045	3,501
39	0	0	33,648	3,468
40	0	0	35,330	3,435
	Totals	$13,948		$119,580

Present Value
Numbers

ASSUMPTIONS

Initial Age	45
Annual Contribution	10,000
Trust Payout Rate	0.05
"Life Expectancy"	40
Tax Bracket	0.36
Trust Investment	0.10
Discount Rate (PV)	0.08

Invest $10,000
per Year at 8%
for 20 Years
$114,699

Total Benefit
from Trust
$83,389

Present
Value
Comparison

Amount Eventually
Passing to Charity
$1,214,466

Present Value of
Charitable Benefit
$55,903

Year	Tax Savings	P.V. Savings	A-T Income	P.V. Income
1	867	867	0	0
2	900	833	0	0
3	934	800	0	0
4	969	769	0	0
5	1,003	737	0	0
6	1,039	707	0	0
7	1,075	678	0	0
8	1,114	650	0	0
9	1,151	622	0	0
10	1,190	595	0	0
11	1,230	570	0	0
12	1,270	545	0	0
13	1,311	521	0	0
14	1,353	497	0	0
15	1,395	475	0	0
16	1,438	453	0	0
17	1,482	433	0	0
18	1,525	412	0	0
19	1,569	393	0	0
20	1,613	374	0	0
21	0	0	40,322	8,010
22	0	0	40,322	7,417
23	0	0	40,322	6,867
24	0	0	40,322	6,359
25	0	0	40,322	5,888
26	0	0	40,322	5,452
27	0	0	40,322	5,048
28	0	0	30,404	3,524
29	0	0	20,657	2,217
30	0	0	21,690	2,155
31	0	0	22,774	2,096
32	0	0	23,913	2,037
33	0	0	25,108	1,981
34	0	0	26,364	1,926
35	0	0	27,682	1,872
36	0	0	29,066	1,820
37	0	0	30,519	1,770
38	0	0	32,045	1,721
39	0	0	33,648	1,673
40	0	0	35,330	1,626
	Totals	$11,931		$71,458

Present Value
Numbers

b. If the annual increase is not trust accounting income, the difference between the cost of the bonds and the amount paid for them upon maturity will be trust accounting income when the bonds mature.

What potential problem doyou see in this case if the trust contains a make-up provision?

c. Note that in Pennsylvania, the Attorney General takes the position that a CRT may not hold tax-exempt bonds. Feinstein Trust (Orphans' Court 1986).

2. Commercial deferred annuity -- the "spigot trust"

a. The trust invests in a commercial deferred annuity.

b. Trust accounting income is defined to exclude any build-up in the value of the annuity.

c. The trustee causes the trust to have income by taking withdrawals from the annuity (presumably, the annuity has been designed so that no early withdrawal penalties are imposed).

d. Does this "spigot trust" plan work?

IRS has issued one basically favorable ruling on the idea of using a commercial deferred annuity as the investment of a net-income unitrust. Letter Ruling 9009047.

But manipulating the trust (the "spigot" aspect) might be viewed by IRS as self-dealing, in the wake of Notice 94-78 and Letter Ruling 9506015.

Another concern is that by putting all its eggs in this one basket, the trustee might be violating its fiduciary duties under local law.

3. An imaginative, if abusive, variation

a. Donor sets up a net-income-with-make-up unitrust.

b. The trust is to run for the donor's life and then for
the donor's son's life
or 30 days, whichever is shorter.

c. The trust is managed (manipulated) so that a large "deficit" is built up during the donor's life.

d. During the 30 days following the donor's death, the trustee cashes in the annuity, causing the unitrust to have a lot of income for trust accounting purposes.

e. This income is paid out to the donor's son to make up for the large "deficit."

f. The large payout to the son is an "inheritance," but he gets it subject to income tax not higher estate tax rates.

> The scheme is based on the fact that the son's interest in the trust has a very small value for federal gift and estate tax purposes, because it will run no more than 30 days.

V. PLANNING PROBLEM -- A SITUATION FOR DISCUSSION

A. Facts

Hal wants to use some undeveloped land to establish a net-income with make-up unitrust for the benefit of ABC College.

ABC has agreed to act as trustee.

Both ABC and Hal anticipate that it will take 6 to 12 months for the unitrust to sell the land. In the meantime, the trust will have expenses of $10,000 to $12,000 in connection with the property (taxes, insurance, etc.).

Hal is reluctant, for his own reasons, to put cash into the trust or otherwise cover these expenses.

B. Questions

1. Suppose that ABC simply pays the expenses out of its general operating budget. Any potential problems?

> Note: A unitrust may accept additional contributions. But may an additional contribution to a unitrust be made by a 501(c)(3) organization? And is such a contribution consistent with 501(c)(3) status?

2. ABC might make an interest-bearing loan to the trust as a way to cover the expenses -- which is arguably OK. What is another way ABC might provide cash to the trust -- a way that is all right from a tax standpoint?

> Note that charitable organizations are excluded from the definition of "disqualified person" and therefore can engage in acts that otherwise would be self-dealing.

VI. ALTERNATIVES TO THE NET-INCOME UNITRUST

A. Situation for Discussion

Jane, aged 65, wants to use some undeveloped land to set up a 6-percent straight-payout unitrust. Jane is adamant that she does not want a net-income limitation.

Suppose Jane were to put about $6,000 of cash or marketable stock into a straight-payout trust along with the land.

Suppose further that the first year's payout to Jane were $6,000.

How would this $6,000 be taxed to Jane if the trust for the first year had:

ordinary income of	$200
realized gains of	$800

and no other income?

> Caution: Once again, one must bear in mind the recent IRS pronouncements against manipulating charitable remainder trusts for the donor's benefit.

B. Variation

Jane's cousin Val, aged 65, also wants to set up a 6-percent straight-payout unitrust using some negligible-dividend NASDAQ stock Val believes will increase tremendously in value over the next 5 to 10 years.

Like Jane, Val regards a net-income limitation as unacceptable.
Val, moreover, wants the trustee of her unitrust basically to hold onto the NASDAQ stock. Told that a corporate trustee might not be willing to do this, Val has volunteered to act as the trustee.

Question: From a tax standpoint, what are the potential risks and rewards of the plan Val has in mind?

VII. APPENDIX: TWO RECENT PRIVATE RULINGS ON NET-INCOME UNITRUSTS

A. Letter Ruling 9442017

1. 7-percent net-income-with-make-up unitrust

2. Initial trustee is the charitable remainder beneficiary. Donor reserves right to remove initial trustee and name a successor trustee, including himself or his wife.

3. Donor will serve, in a fiduciary capacity, as the "investment manager" of the trust.

4. An independent investment manager (meeting the requirements of an independent trustee) will value and direct the investment of any trust assets not having a readily ascertainable market value.

5. Trustee is authorized -- as permitted under local (Nebraska) law -- to make reasonable allocations between income and principal of any gains from the sale of unproductive assets.

6. Internal Revenue Code §674(b)(8): Permits this power to be held by any person with respect to a trust without causing the trust to be a "grantor trust":

> A power to allocate receipts and disbursements as between corpus and income, even though expressed in broad language.

7. IRS rules that the discretionary power to allocate capital gains to trust income is OK.

B. Letter Ruling 9506015

1. Donors, husband and wife, set up an 8-percent net-income-with-make-up unitrust using land.

2. After the land was sold, they went to court to get the unitrust agreement reformed (amended), so the trust would pay them a straight 8 percent.

3. They told IRS that a "flip" provision had been omitted from the trust agreement by mistake.

4. IRS said reforming the trust would disqualify it as a unitrust. It also said including a "flip" provision in the trust instrument in the first place would have disqualified the trust.

5. IRS said it was necessary to pick and stick with one of the 3 basic unitrust formats for the entire trust term "[t]o prevent possible manipulation of trust assets to the detriment of the charitable remainder interest...."

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APPENDICES

Twenty-Second Conference on Gift Annuities
May 3-5, 1995
Hyatt Regency San Francisco Hotel, San Francisco, California

Wednesday, May 3, 1995

Pre-Conference Session

A special session, "Orientation for Newcomers," was held in Bayview Rooms A and B at 5:15 p.m.

At 6:00 p.m. the delegates were treated to a San Francisco dinner in the Grand Ballroom.

First Plenary Session

The Conference was called to order at 8:00 p.m. in the Grand Ballroom by Chairman Tal Roberts. The invocation was delivered by Mr. Roberts.

Mr. Roberts introduced Robert F. Sharpe, Jr. who spoke about "Trends in Planned Giving."

Thursday, May 4, 1995

Second Plenary Session

The Conference was called to order at 8:30 a.m. in the Grand Ballroom by Chairman Roberts.

The invocation was delivered by Mr. Roberts.

The Chairman welcomed those present to the Conference and introduced Frank D. Minton, chairman of the Program Committee, and James B. Potter, chairman of the State Regulations Committee, who will speak later in the morning's program. He introduced the members of the Program Committee, Arrangements Committee, Council vice chairman and treasurer, and asked all of the directors to stand and be recognized. He announced that secretary and former long-time chairman of the Council, Charles W. Baas, was unable to attend the Conference, his second absence in 50 years, because of surgery yesterday.

Comments on the State of the Conference were made by Chairman Roberts. See "Chairman's Address to the 22nd Conference."

Dr. Minton introduced Robert T. Parry, chief executive of the Twelfth District Federal Reserve Bank at San Francisco. Mr. Parry explained the role of the Federal Reserve in the economy, gave an overview of the economic outlook and answered questions from the floor.

Dr. Minton introduced Mr. Potter who gave an update on state regulation of gift annuities." See "Filing and Reporting Requirements in States that Regulate Gift Annuities." Mr. Potter named the State Regulations Committee, listed in his report, and asked that the members be contacted with any information about state regulations. A task force on state regulation has been appointed consisting of nine persons representing the American Council on Gift Annuities, National Committee on Planned Giving (NCPG) and National Society of Fund Raising Executives (NSFRE).

Dr. Minton announced that Kaspick & Company and Loomis, Sayles & Company, L.P. sponsored the morning breaks today and tomorrow.

Dr. Minton recognized speakers, exhibitors, sponsors of breaks, Laura Peters and Ileen Bray for their work on the Conference.

The Chairman said that the results of the gift annuity survey and the actuarial report will be given at the 3:15 p.m. plenary session today.

The second plenary session was declared in recess at 10:00 a.m. for a break in the Exhibit Area until 10:30 a.m.

Breakout Sessions

The following breakout sessions convened at 10:30 a.m. and continued until 11:45 a.m.:

Charitable Gift Annuities
W. Earl Taylor

Charitable Remainder Trusts
Robert L. Coffman

Investment of Gift Annuity Funds
Lindsay L. Lapole

Investment of CRT, CLT and PIF Fund Assets
J. Scott Kaspick

Management of Real Estate Gifts
Lynda S. Moerschbaecher

Identifying Donors of Planned Gifts
Jonathan R. Heintzelman

Materials and Techniques That Appeal to Your Donors
Ronald E. Sapp

Contribution of Retirement Funds
Robert E. Harding

Creative Applications of Net Income Unitrusts
Jonathan G. Tidd

Gift Options with Personal Residences
Andre' R. Donikian

Filing and Reporting Requirements in States that Regulate Gift Annuities
James B. Potter
and
Clinton A. Schroeder

Luncheon Session

Lunch was served at 12:00 noon.

Breakout Sessions

The topics given at 10:30 a.m. were repeated from 1:30 to 2:45 p.m. At 2:45 p.m. a break in the Exhibit Area was held until 3:15 p.m.

Third Plenary Session

The Conference was called to order in the Grand Ballroom by Dr. Minton.

Dr. Minton said the directors approved a national survey in 1993 with the results to be provided at the 1995 Conference. The data was collected to 1994 so the gift totals largely apply to 1993 and 1994. The data comes from 841 surveys returned from about 2,100 mailed. Copies of the survey were provided to all attendees at registration.

Dr. Minton introduced Mr. Mudry, Senior Vice President, Hay/Huggins Company, Inc., for the actuarial report. See "Actuarial Report."

The Chairman announced that the next Conference will be held at the Atlanta Marriott Marquis in Atlanta, Georgia, April 15-17, 1998.

The Conference adjourned at 4:30 p.m. for dinner.

Optional Evening Session

The following optional session convened at 7:30 p.m.

Update on Canada

A. Gordon Nelson

Friday, May 5, 1995

Third Plenary Session

Chairman Roberts reconvened the Conference at 8:30 a.m. in the Grand Ballroom.

Mr. Roberts reiterated remarks from his chairman's address to the Conference on May 4 that any action on the suggested gift annuity rates was being deferred until a favorable court ruling in the lawsuit is obtained.

Mr. Roberts introduced Elizabeth Brown, chairman of the Resolutions Committee. Mrs. Brown presented the recommendations of the Resolutions Committee. See "Report of Resolutions Committee." Mrs. Brown moved the adoption of the Committee's report and it was seconded. Mr. Roberts added that it be resolved that greetings be sent to Dr. Baas and best wishes to him for a speedy recovery. He thanked Conrad Teitell in advance for his presentation and said no title was given to it because it is a closely guarded secret. He asked that approval of the resolutions be given by standing and voting with applause. Approval was unanimous.

Breakout Sessions

The Conference recessed at 9:30 a.m. for the following breakout sessions which continued until 10:45 a.m.:

Pooled Income Funds

Marc Carmichael

Charitable Lead Trusts

Carolyn C. Clark

Bequests and Other Revocable Gifts

Ellen G. Estes

Recording, Reporting and Substantiating Planned Gifts

Tim A. Jones

Fiduciary Issues for Charitable Organizations

David W. Newman

Practicing Good Stewardship

Stewart J. Crook

The Roles of Gift Planners and Professional Advisors --Who Does What?

David M. Benson

Gifts of Closely Held Stock and Other Business Interests
Terry L. Simmons
Gifts of Personal Property, Mineral Rights, Crops, Royalties
Carolyn M. Osteen
Filing and Reporting Requirements in States that Regulate Gift Annuities
James B. Potter
and
Clinton A. Schroeder

A break in the Exhibit Area was held at 10:45 a.m., after which the 9:30 a.m. breakout sessions were repeated from 11:15 a.m. to 12:30 p.m.

Luncheon Session

Lunch was served at 12:30 p.m. in the Grand Ballroom.

After lunch, Dr. Minton expressed appreciation to speakers, advertisers, exhibitors, hotel staff and Chairman Roberts.

Dr. Minton introduced the speaker for the final session of the Conference, Conrad Teitell, Esq., Partner, Prerau & Teitell, and Editor of Taxwise Giving. The presentation was an off off Broadway production of the Teitell Players who recreated a Ways and Means Committee hearing on tax reform. Mr. Teitell reviewed deduction losses for charitable contributions through the years, pinpointed pending legislation, and urged those present to contact their members of Congress.

The Conference adjourned at 2:15 p.m.

Respectfully submitted,
Ileen Bray, Acting Secretary

CHAIRMAN'S ADDRESS
TO THE
22ND CONFERENCE ON GIFT ANNUITIES
MAY 4, 1995

On behalf of the American Council on Gift Annuities, welcome to San Francisco and the 22nd Conference on Gift Annuities. You are part of a tradition that goes back almost seventy years when forty-seven people attended the first Conference on Gift Annuities in April of 1927 in New York City. Today you are part of a record gathering of almost a thousand people from every part of the country representing charities of every description.

These conferences, now held every three years, are the primary focus of the American Council on Gift Annuities. And before I go any further I want to take this opportunity to thank two people in particular without whose hard work this conference would not have happened. The first is Frank Minton who is Program Chairman for this conference and the second is Gerry Gunnin, Chairman of the Arrangements Committee. Both are members of the Board of Directors of the American Council and both have given countless hours in their volunteer capacity to insure that this conference will be for each of you both productive and enjoyable. Assisting Frank Minton on the Program Committee are Kathryn Baerwald, Bob Coffman, Betsy Mangone and Clint Schroeder. Serving on the Arrangements Committee with Gerry Gunnin are John Jacobs and Richard James.

I want to recognize also the other officers of the Council that give so unselfishly of their time—Clint Schroeder, Vice Chairman and Harold Richardson, Treasurer. Our Secretary and former longtime Chairman, Charley Baas, is absent today, missing only his second conference in fifty years. Charley had surgery yesterday in South Carolina and I am pleased to report that he is doing well.

The names of all the directors of the Council are listed in the program and I'd like to ask all of them to stand, if they're in the hall, and be recognized.

As we gather this morning to officially kick off the 22nd Conference , there is an important matter on which I must report to you, and that is the status of the lawsuit which was filed against the Council and its sponsors on December 30, 1994. As most of you know by now, the lawsuit originally had been filed in Texas state court alleging a private claim by a woman purporting to act under a power of attorney for her aunt against various Lutheran charities. The Plaintiff then abandoned her state court case and refiled in federal court to sue the Lutheran entities, to add the American Council on Gift Annuities, and to seek to have a class action certified to include countless donors and their beneficiaries and heirs on the Plaintiff side and perhaps more than a thousand charities in America involved in planned giving on the Defendant side. The Plaintiff asserts a number of theories, including an antitrust claim for alleged price-fixing against every charity using the American Council's annuity tables. The Plaintiff also alleges that charities, even those located outside the State of Texas, are violating the Texas Insurance Code, the Texas Trust Act, and the Texas Deceptive Trade Practices Act by issuing charitable gift annuities or acting as trustee of charitable trusts for residents of Texas. The relief sought is astronomical—a return of affected property by each charity and/or treble damages. In other words, the Plaintiff's lawyers may try to get back the money contributed by the class **plus** twice that amount from funds that unaffected donors contributed. One of the Plaintiff's lawyers has boasted, and I quote, "This will be a billion dollar lawsuit."

The Council believes that the positions taken in the lawsuit are without merit and that the basic premise on which the lawsuit is based is flawed in that it attempts to change an act of generosity into a crass commercial transaction in which the donor is characterized as trying to get all he can get. The Council immediately engaged the Dallas law firm of Thompson & Knight and began to defend the lawsuit vigorously.

In time, the American Council and the Lutheran entities filed a Motion to Dismiss, and in response the Plaintiff amended the original complaint to assert also a class action claim under the Investment Company Act of 1940. The judge has ruled that the case will not be dismissed at this early stage and has directed the parties to begin pretrial discovery, a process which has already begun.

The American Council and the other defendants have now filed their answer to the Plaintiff's complaint and have asserted numerous defenses to the allegations which have been raised.

Recently the Plaintiff filed a motion for Summary Judgment against the Lutheran Foundation on two state law issues in the case, namely, the issuance of gift annuities in Texas and serving as trustee of charitable trusts in Texas. Subsequent to that action, which is still pending, the Attorney General of the State of Texas filed a motion seeking to intervene in this case, and within the last few days the Salvation Army has filed a friend-of-the-court brief on behalf of the defendants.

At some point in the next few months the Court will determine whether or not a class action will be certified. If the class actions requested are certified (despite the American Council's belief that such certification is not justified), then the breathtaking reach of this lawsuit would take effect and charities from all over America would be brought into the lawsuit merely for having issued or managed gift annuities while a sponsor of the American Council.

In years past, changes to the suggested annuity rates were considered at the triennial Conference. That practice is not being followed this year because of the lawsuit. The Council's Board of Directors, which considers any suggested rate changes in the first instance, had hoped that we would have a court ruling in our favor by the time of this Conference, but that not having occurred, the Board has deferred action to allow more time for such a ruling to be obtained.

We have attempted to keep you advised since January of the pertinent developments in this matter and will continue to do so. As you might imagine the defense of an action such as this is very expensive and will far exceed the ability of the Council's treasury to fund. In the days and weeks ahead you may be asked to make contributions of time or resources to help with this cause. In the meantime we hope you will enjoy and benefit from this conference and when you return home, mark your calendars for April 15-17, 1998, when we will reconvene in Atlanta.

Again, welcome to the 22nd Conference on Gift Annuities.

Report of Resolutions Committee

22nd Conference on Gift Annuities
May 5, 1995
Hyatt Regency San Francisco

Actions taken by the Resolutions Committee:

1. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express its sincere appreciation to Robert T. Parry, Chief Executive, Twelfth District Federal Reserve Bank, for his timely and authoritative keynote address.

2. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express appreciation to Michael Mudry, Actuary, Senior Vice President of Hay/Huggins Company, Inc. for his actuarial report.

3. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express deep appreciation to those persons who made plenary session presentations on matters of continuing concern, namely:

   Robert F. Sharpe, Jr., Robert Sharpe and Co.
   "Trends in Planned Giving"

   James B. Potter, President, Planned Giving Resources
   "Update on State Regulation of Gift Annuities"

   Frank Minton, President, Planned Giving Services
   "Report and Comments on the ACGA's 1994 Survey of Charitable Gift Annuities"

   Conrad Teitell, Prerau & Teitell

4. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express gratitude to the leaders of the various breakout and optional sessions who graciously shared their knowledge and expertise during this Conference, namely the following:

   David M. Benson, President, David Benson & Associates
   Marc Carmichael, President, R & R Newkirk Company
   Carolyn C. Clark, Milbank, Tweed, Hadley & McCloy
   Robert L. Coffman, Executive Director & Counsel for Development, Anderson University
   Stuart Crook, Director of Trust Services, Southern Union Conference of Seventh-day Adventists
   Andre' Donikian, President, Pentera, Inc.

4. continued -

Ellen G. Estes, President, Estes Associates
Robert Harding, Gray, Plant, Mooty, Mooty & Bennett
Jonathan R. Heintzelman, Assistant Vice President for
University Development, Northwestern University
Tim Jones, Treasurer, University of Colorado Foundation, Inc.
J. Scott Kaspick, Managing Director, Kaspick & Company
Lindsay L. Lapole, Territorial Planned Giving Director,
The Salvation Army
Lynda S. Moerschbaecher, Moerschbaecher & Dryburgh
A. Gordon Nelson, Planned Giving Director, Christian Blind
Mission International
David W. Newman, Mitchell, Silberberg & Knupp
Carolyn Osteen, Ropes & Gray
James B. Potter, President, Planned Giving Resources
Ronald E. Sapp, Director, Office of Planned Giving,
The Johns Hopkins Institutions
Clinton A. Schroeder, Gray, Plant, Mooty, Mooty, & Bennett
Terry L. Simmons, Vice President and General Counsel,
Baptist Foundation of Texas
W. Earl Taylor, Executive Director, Omaha Community Foundation
Jonathan G. Tidd, attorney, editor and consultant.

5. BE IT RESOLVED, that the 22nd Conference on Gift Annuities recommend that religious, educational, health, and charitable groups be requested to send to the Chairman of the ACGA copies of new rulings by Federal or State authorities dealing with gift annuities or life income agreements.

6. BE IT RESOLVED, that the 22nd Conference on Gift Annuities send greetings to Charles L. Burrell, Jr., John M. Deschere, William E. Jarvis, David E. Johnson, Roland C. Matthies, Darold H. Morgan and Chester A. Myrom, Honorary Members.

7. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express its appreciation for the special helpfulness extended to Conference delegates in connection with all the arrangements for the Conference by the staff and management of Beverly Judge, Inc.; Miss Ileen Bray of the Annuity Board of the Southern Baptist Convention, and the Hyatt Regency San Francisco, Embarcadero Center.

8. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express its deep appreciation to the Annuity Board of the Southern Baptist Convention, host organization to the American Council on Gift Annuities, for its generous support through the provision of facilities and personnel which undergird the day-to-day operation of the Council.

9. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express its warm thanks and hearty commendation to Frank D. Minton, Chairman, Kathryn E. Baerwald, Robert L. Coffman, Betsy A. Mangone and Clinton A. Schroeder of the Conference Program Committee, and to Gerry C. Gunnin, Chairman, John B. Jacobs and Richard A. James of the Conference Arrangements Committee.

10. BE IT RESOLVED, that the 22nd Conference on Gift Annuities express its warmest greetings and best wishes for a speedy recovery to Charles Baas, our former long-time Chairman, who could not attend the conference because of recent surgery. This is only the second conference Charley has missed in fifty years.

Resolutions Committee
Elizabeth Brown, Chairman
Richard James
Tal Roberts, Ex Officio

Report and Comments on the

American Council on Gift Annuities

1994 Survey of Charitable Gift Annuities

PRESENTED BY:

Frank Minton, President
Planned Giving Services
Seattle, Washington

Introduction

Except for the bequest, the charitable gift annuity is the oldest planned gift. The first gift annuity is believed to have been written by the American Bible Society in 1843. By the 1920's a number of religious organizations were issuing gift annuities, and in the intervening sixty years all types of organizations, secular as well as religious, have found the gift annuity to be an effective means of securing contributions. The increasing interest in gift annuities was accompanied by growth in the number of sponsoring members of the Committee on Gift Annuities and in attendance at the triennial conferences sponsored by that organization. Effective January 1, 1994, that organization was incorporated, and the name was changed to the American Council on Gift Annuities (ACGA).

Although gift annuities have been around for more than a century and ever more charities appear to be offering them, we have had little hard data on what is actually happening. The only previous survey of which we are aware was conducted in 1955 by Charles Baas, who was then Chair of the Committee on Gift Annuities. That survey was primarily concerned with financial statistics regarding gift annuity funds.

Because of the lack of current data, the Committee on Gift Annuities, at a meeting of the Board of Directors in 1993, authorized a comprehensive survey, and Chairman Tal Roberts appointed me as Project Director.

In designing the questionnaire I greatly benefited from the constructive suggestions of Tal Roberts, Clinton Schroeder, Charles Baas, Michael Mudry, James Potter, Robert Coffman, and Elaine D'Amours, all of whom serve on the Board of Directors of the ACGA.

I would also like to express appreciation to Ileen Bray for all of her work in mailing the questionnaires, to Brost Data Systems for keying in the data from the questionnaires, to Gilmore Research, Inc. for tabulating and analyzing the data, and to my associates Paul Flucke and Laura Peters for the many hours they spent helping me produce the graphics and prepare the report.

This report displays the data that was collected and offers interpretive comments and personal observations on charitable gift annuities.

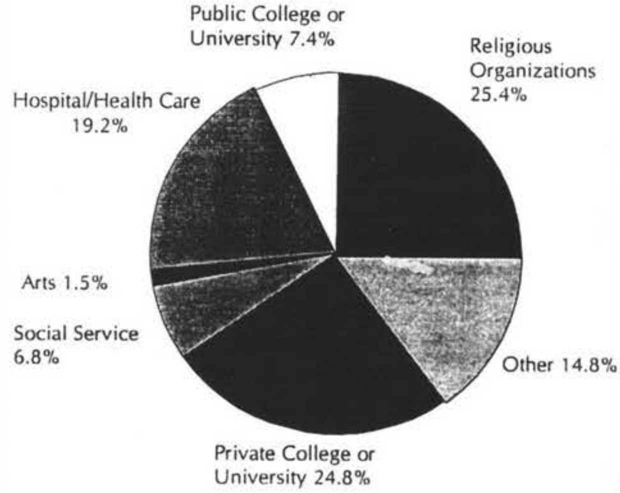
Frank Minton

Methodology

In the spring and summer of 1994 questionnaires designed to elicit information about charitable gift annuities were mailed to approximately 1,800 current and former ACGA sponsors and to approximately 300 other charitable institutions. Of the total 2,100 questionnaires sent, 841 were returned completed, representing a 40% response rate. This rate exceeded expectations, especially considering that four or more hours were required for many charities to collect and enter the data.

ACGA sponsors accounted for 94.8% of the responses, while 5.2% came from other charities. All 50 states were represented. Figure 1 depicts the percentages of total responses that came from various types of organizations.

Figure 1: *Type of Organization*



The questions were grouped under the following categories:

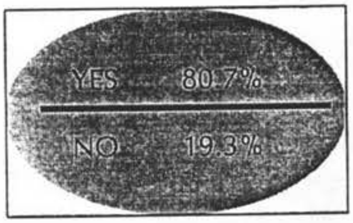
1. Type of organization
2. Number, volume, and other characteristics of completed gifts
3. Policies regarding issuance of gift annuities
4. Registration in states that regulate gift annuities
5. Investment of annuity assets
6. Responsibility and procedures for administering gift annuities
7. Amount of original contribution remaining at death of annuitants

It was possible to compare data by type of institution and to correlate answers to different questions. For example, total investment returns were correlated with portfolio allocation. Other cross-tabulations of significance are noted in the report.

The complete survey questionnaire appears in *Appendix A*.

Institutions Issuing Gift Annuities

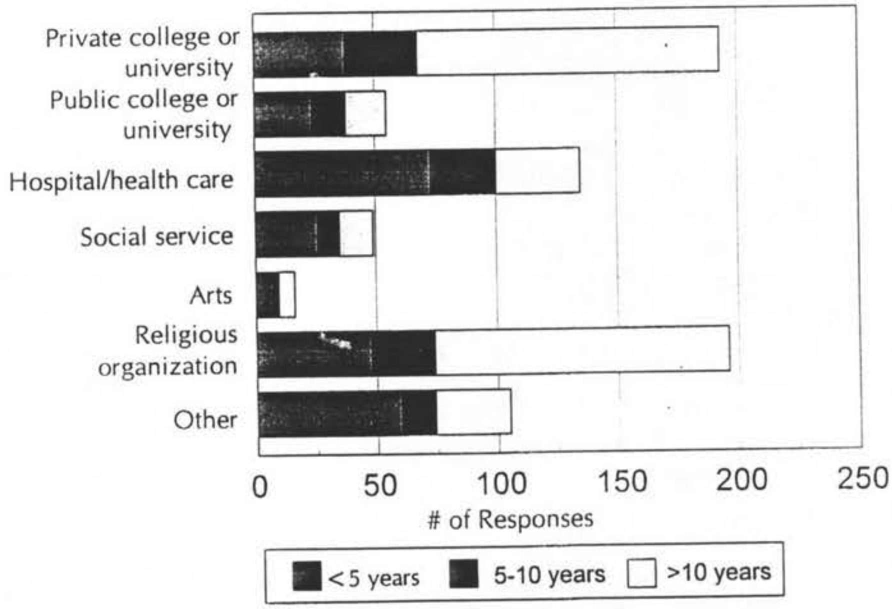
Asked whether their institution had issued any charitable gift annuities during calendar year 1993, respondents answered as follows:



The vast majority of those surveyed were sponsoring members of the American Council on Gift Annuities and were therefore more likely to have issued annuities than institutions in general. Thus, it should not be concluded that 80% of *all* charities issued annuities in 1993.

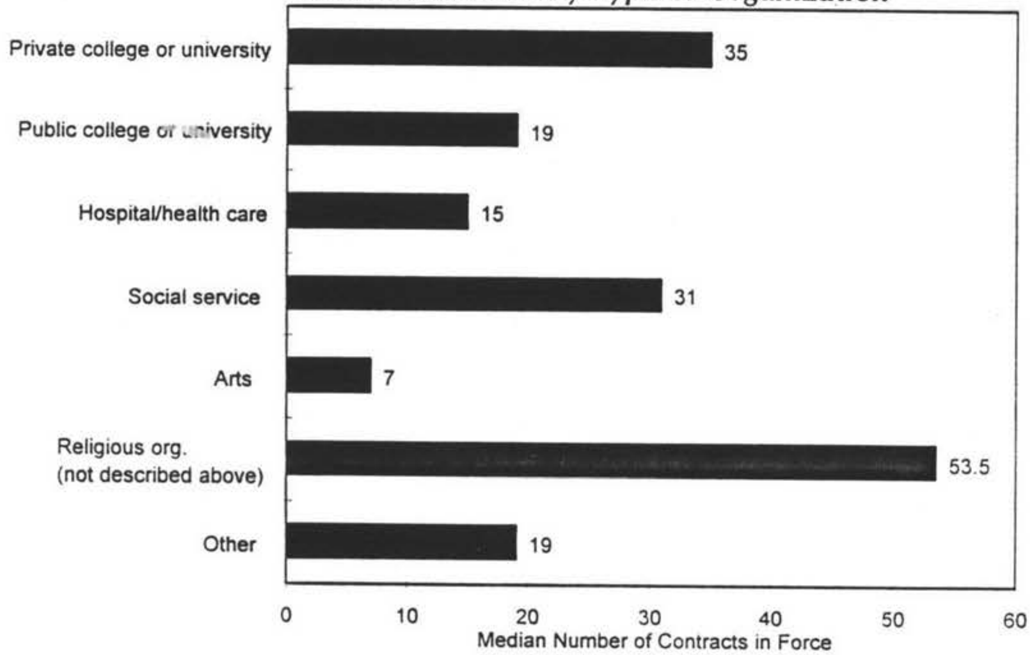
Of the organizations issuing gift annuities in 1993, nearly half (46.7%) said they had been offering annuities for more than ten years, and 16.3% said five to ten years. More than a third (37.1%) said they had been issuing annuities for less than five years. An analysis of responses to this question by organizational type indicates that institutions of higher education and religious organizations are the "old timers" in the gift annuity field while health, social service, and arts organizations are the "newcomers." This is not surprising since the founding members of the original Committee on Gift Annuities were religious bodies, and the next to join were colleges and universities.

Figure 2: ***How Long Organization Has Offered Annuities***



Each institution was asked to report its total number of annuity contracts in force. A total of 80,688 contracts were reported by 783 institutions, yielding an average (mean) of 103 contracts per institution. The median, however, was 20 contracts, meaning that half of the charities held fewer than that number and half held more. The disparity between the mean and median is due to the fact that a few national institutions reported very large numbers, thus elevating the average. See Figure 3 below for the median number of contracts in force by type of organization.

Figure 3: *Median Number of Annuity Contracts in Force by Type of Organization*

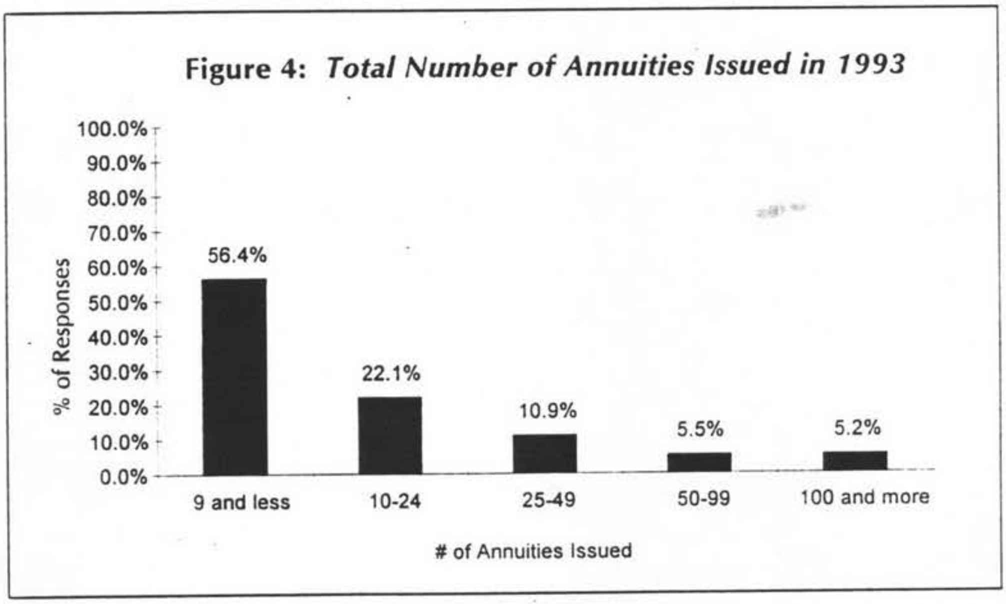


With one exception, the organizations that have been issuing annuities for the longest time have the most annuity contracts in force. That exception is social service charities. These are often national organizations with regional chapters. Gift annuities are administered from the national office, and totals reported are for the entire organization. This probably accounts for the fact that the number of annuities they have in force is higher than might be expected from relatively recent annuity programs.

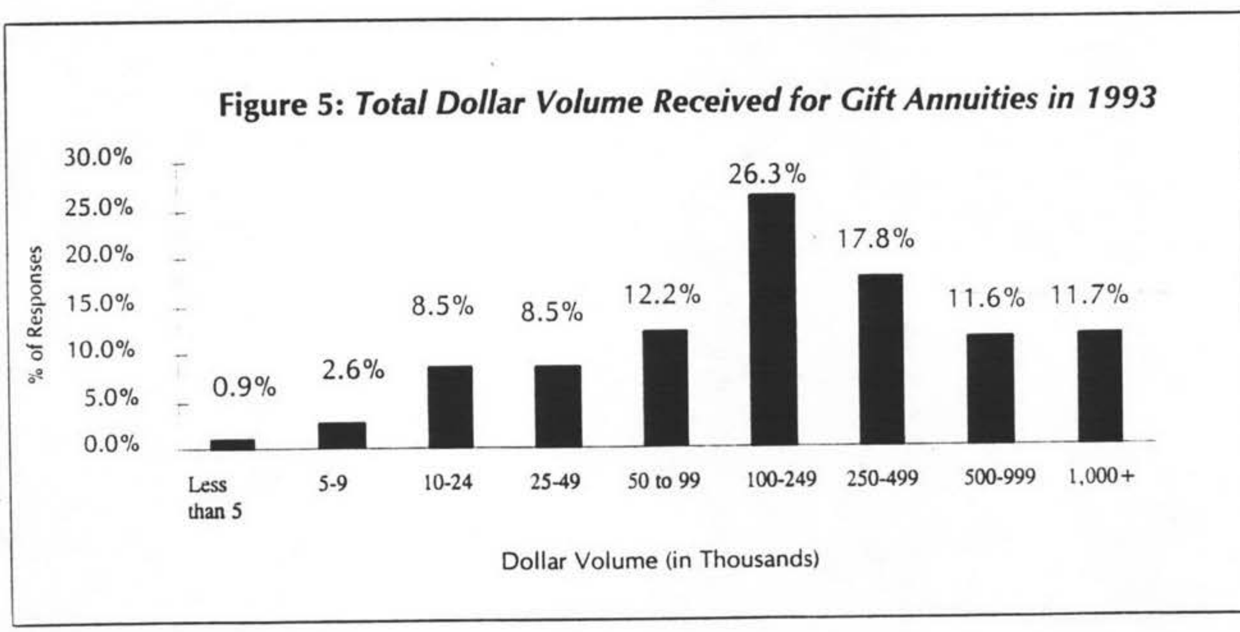
The average current market value of total annuity reserves--$1,681,654--is misleading for the same reason cited above. The largest institutions raised the average: 15.2% reported reserves of $2,000,000 or more. The median response was a much lower $480,000, with 17.7% of the respondents reporting reserves of less than $100,000, and 14.2% in the $100,000--$300,000 range.

Gift Annuity Activity in 1993

The total number of annuities issued by the responding charities in 1993 was 16,673. While this yields an average of more than 25 annuities per charity, over half of the respondents (56.4%) reported issuing nine or fewer annuities for the year, and only 21.6% issued 25 or more during the year.



The average total dollar volume of gift annuities issued in 1993 was $480,185 per institution. Here again, the average is elevated by the high volume reported by a comparatively small number of institutions. The median amount was a more modest $167,914.



Dividing the total dollar volume of annuities issued by responding institutions in 1993 ($315,962,233) by the total number of annuities issued by them (16,673) yields an average contribution of ***$18,950*** per contract. The average size varies considerably by type of organization. Religious and arts organizations receive, on average, the smallest contributions for annuities, while colleges and universities, particularly public universities, receive the highest.

Figure 6: ***Average Size of Annuity by Type of Organization***

Type of Organization	*Number of Annuities*	*Dollar Volume Received*	*Average Size*
Not indicated	972	$10,184,563	$10,478
Private College/University	2,794	82,220,133	29,427
Public College/University	565	28,689,143	50,777
Hospital/Health Care	1,441	32,812,257	22,770
Social Service	789	17,101,909	21,675
Arts	32	873,728	12,304
Religious Organizations	8,369	107,577,577	12,854
Other	1,711	36,502,923	21,334

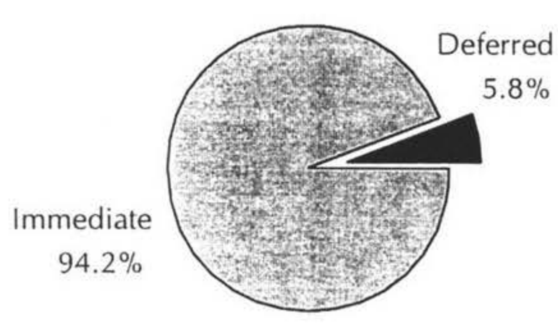
Immediate and Deferred Payment Gift Annuities

The overwhelming majority of gift annuities start making payments to annuitants immediately. Only a small percentage defer payments to some future time.

The gift annuity has not really caught on as a means to make a gift and simultaneously create a supplemental retirement plan.

One reason for the infrequent use of deferred payment gift annuities may be the growing popularity of an alternative--the net-income with make-up provision charitable remainder unitrust. The deferred payment gift annuity, however, does offer two advantages: a larger income tax charitable deduction and guaranteed payments of a certain amount. Deferred annuity rates are necessarily conservative because charities cannot be certain of the interest rates they can earn on annuity reserves in the distant future.

Figure 7: ***Immediate vs. Deferred Annuities***



Profile of Gift Annuity Donors

The survey confirmed that gift annuities appeal to the charity's oldest donor group. The average age of annuitants at the time immediate-payment gift annuities are funded is 77. The median age is virtually the same as the average age, and there is little variation by type of institution.

According to a National Committee on Planned Giving survey on charitable remainder trusts, based on data collected in 1992, the average age of beneficiaries of charitable remainder trusts at the time the trust is funded is 69. This number refers to trusts initiated by the charity. Beneficiaries of charitable remainder trusts initiated by financial advisors tend to be still younger. Thus, the average donor for a gift annuity is eight or more years older than donors to charitable remainder trusts. The security of guaranteed, fixed payments that will not fluctuate with the stock market or interest rates is very appealing to older individuals. Those in their fifties and sixties, who are able to make larger contributions, may opt for a charitable remainder unitrust because it offers a potential hedge against inflation.

Female annuitants outnumber male annuitants by 60% to 40%, with little variation by type of institution. It should be noted that at age 77 women in the United States outnumber men by almost exactly the same 60-40 ratio. Thus it appears that males and females have approximately equal interest in charitable gift annuities.

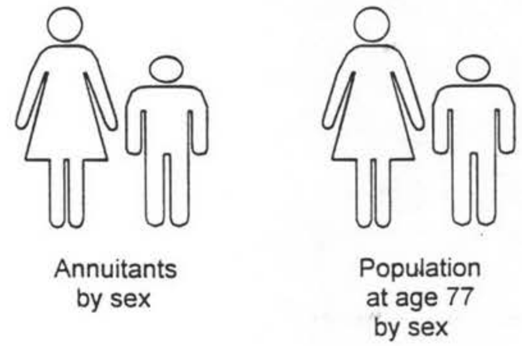
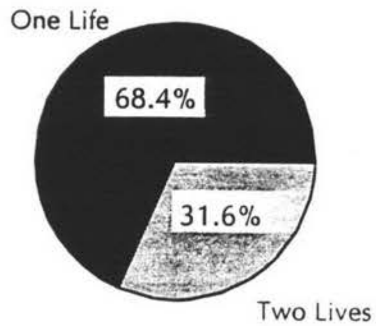


Figure 8: *Annuitants by Sex Vs. Population at 77 by Sex*

An interesting sidelight: Both the IRS mortality tables and the ACGA gift annuity tables are unisex. That is, they are identical for males and females of the same age. The IRS tables, for example, project a life expectancy of 11.2 years at age 77 regardless of sex. However, the "1983-a" mortality table, required by many states to calculate required annuity reserves, *does* distinguish between the sexes, setting age-77 life expectancies at 10.2 years for a male and 13.4 years for a female. Thus, if a man and a woman, both aged 77, contribute equal amounts for gift annuities, they will receive equal yearly payments for life and get the same income tax deduction. However, the man, on average, will live to collect only 76.12% (10.2÷13.4) of what the woman collects, and will leave proportionately more for the charity.

Charities were asked what percentage of the annuities they had issued in 1993 were for one life and what percentage were for two lives. Figure 9 shows the average (mean) response. More than two-thirds of annuities are issued for one life.

Figure 9:*One Life vs. Two Life Annuities*

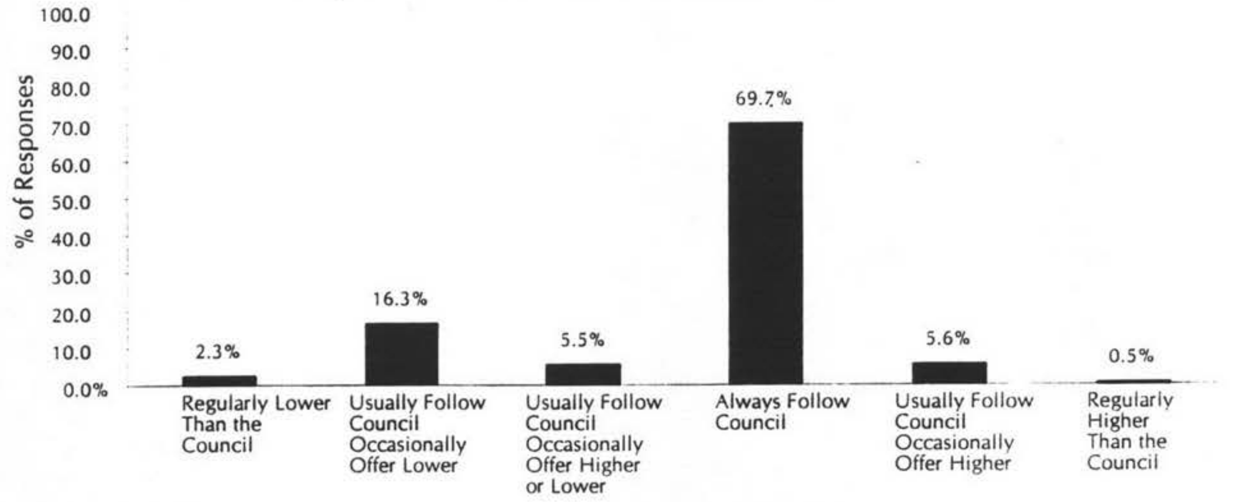


Gift Annuity Rates Offered by Charities

Since its founding in 1927, the ACGA (formerly the Committee on Gift Annuities) has periodically computed and distributed to sponsoring charities annuity rates which, based on certain assumptions, would produce an average residuum of 50% of the amount originally donated to the charity. The ACGA has never attempted to enforce these rates, nor even to monitor how many charities, in fact, followed them.

This survey sought to discover, among other things, how many charities were following the ACGA rates and how many were choosing to offer different rates, whether higher or lower. As the following graph indicates, the majority of charities (69.7%) said they *always* follow the ACGA rates, but a significant minority (30.3%) offer different rates, usually lower than the ACGA rates. Only 6.1% said they occasionally or always offer higher rates.

Figure 10: ***Maximum Gift Annuity Rates Policy Compared to ACGA Recommendations***



Asked whether, to their knowledge, at least one of their prospective donors had compared their annuity rates with those offered by other organizations, 65.3% of the respondents answered Yes. This does not mean, however, that any of the prospective donors were shopping for the charity with the highest rates. If that were true, many charities would probably exceed the ACGA rates in order to gain a competitive edge. But, in fact, most charities that depart from the ACGA rates choose lower rather than higher rates.

Many donors, having completed a gift annuity with one charity and being satisfied with it, decide to make similar gifts to other charities in which they are interested. Often donors have annuities with their college, their church, a hospital foundation, and perhaps a social service or arts organization as well. In those instances, it is natural for them to be aware of the rates offered by the various charities to whom they make such gifts. Sometimes they choose to establish an annuity with a charity that offers lower rates because they are devoted to the cause and the lower rate is still sufficient for their financial needs. If the cause were not important to donors, they undoubtedly would invest in a commercial annuity which pays higher rates than any charity.

In response to sharply declining interest rates in 1993, the ACGA rates were lowered, effective January 1, 1994. Recipients of the survey questionnaire were asked whether they approved of the rate reduction. Their responses:

Figure 11: *Response to ACGA Rate Reduction in 1994*

- 75% approved.
- 11.1% approved of a reduction but felt the rates were reduced too much.
- 7.1% felt the reduction should have been greater.
- 6.9% felt no reduction should have been made.

It should be noted that these responses were made before the increase in interest rates during the second half of 1994. Possibly the responses would be different if the same question were asked today.

Administrative Policies and Practices

The survey inquired about policies regarding minimum contributions for charitable gift annuities. For an immediate-payment annuity, responses ranged from $100 to $100,000, with the most common requirement being $5,000 (39.5% of the respondents), followed by $1,000 (30.5%) and $10,000 (16.2%). For deferred-payment annuities, the most common minimum amount was again $5,000 followed by $1,000 and $10,000.

For subsequent immediate-payment annuities by the same donor, 42.5% of the charities require a minimum of $1,000 and 32% require $5,000. The responses were similar for subsequent deferred-payment annuities. Unlike subsequent contributions to a charitable remainder unitrust and pooled income fund, which are simply additions to an existing trust, subsequent contributions for gift annuities entail preparing entirely new contracts. The paperwork is entirely the same as with the initial contribution. Nevertheless, charities require lower minimums for repeat donations. Perhaps charities are willing to lower the minimums for these gifts because they already have essential data about the donor in their files, and they can combine quarterly payments from multiple annuities into a single check.

In addition to policies regarding minimum annuity contributions, most charities also have policies regarding the minimum acceptable age for annuitants. The most popular minimum ages are listed below:

Figure 12: *Most Popular Minimum Ages*

Immediate-Payment Annuities		Deferred-Payment Annuities	
Age	*Percent*	*Age*	*Percent*
50	24.6	35	10.7
55	22.4	40	17.2
60	23.8	45	12.6
65	11.5	50	27.3
		55	10.7

The actual average ages are considerably higher than these minimums (77 for immediate-payment gift annuities and 57.4 for deferred-payment annuities.) The latter number is higher than might be expected because not all deferred annuities are completed by donors during their high-income working years. A significant number are actually executed by post-retirement donors who choose to delay payments a few years until they are more likely to be needed.

When it comes to administration of gift annuities, duties are likely to be divided between the charity's development and business offices. The standard procedure seems to be for the development office to close the gift and provide information about the deduction amount and taxation to the business office or outside administrator, which then assumes responsibility for investing, accounting, tax filing, and sending checks to annuitants.

Figure 13: *Annuity Processing Procedures*

Responsibility for Calculating Deduction	
Development Office	71%
Business Office	14.1%
Other	14.9%

Responsibility for Investing, Accounting, Checks, etc.	
Business Office	50.6%
Development Office	17.9%
Outside Administrator	16.3%
Combination of Above	15.2%

Investment of Annuity Assets

To ascertain how annuity reserves are invested, respondents were asked how their charity's reserves are allocated among several types of investments. The mean and median amounts invested in various assets are show in the following table.

Average (mean) percentages of investments in various categories of assets are shown below:

Figure 14:
Mean Percentages of Investments by Category

Invested In Cash	% of Respondents
0-24%	73.9%
25-49	9.8
50-74	5.1
75-100	11.2

Invested in Bonds	% of Respondents
0-24%	12.5%
25-49	35.9
50-74	29.4
75-100	22.2

Invested in Stocks	% of Respondents
0-24%	29.1%
25-49	31.7
50-74	34
75-100	5.2

Invested in Mortgages	% of Respondents
0-24%	87.6%
25-49	5.1
50-74	4.4
75-100	2.9

Invested in Real Estate	% of Respondents
0-24%	91.3%
25-49	4.3
50-74	1.4
75-100	2.9

Invested in Other Assets	% of Respondents
0-24%	72.3%
25-49	11.3
50-74	1.9
75-100	14.5

Very few charities invest in assets other than cash, bonds, and stocks. A few large ones, however, do invest in mortgages, real estate, and other property. Since so few charities invest in other assets, the median investments for all charities combined are:

Figure 15: ***Median Percentages of Investments***

Cash	10.0%
Bonds	50.0%
Stocks	40.0%

Total Return on Annuity Reserves

- During the ten-year period ending December 31, 1993, the interest rate underlying the ACGA rates was ***6.5%***. Over this same period, the average annual rate of return actually achieved by the responding charities was ***10.95%***. The median annual return was only slightly lower at 10.0%.

- Responding charities also exceeded the 6.5% assumption during the past five and one-year periods.

- Over the past ***five year period***, their average annual rate of return was ***9.84%***. The median was 9.1%.

- Over the past ***one-year period*** (calendar year 1993 for most respondents), the average annual rate of return was ***8.45%***, and the median was 7.5%. Though lower than for longer periods, they were still above the 6.5% assumption.

- It should be noted that the past ten years saw unusually high returns on both bonds and equities. In other periods, the yields may have been considerably lower.

Effect of Investment Allocation on Total Return

To determine how a charity's net total return on its annuity assets is affected by the mix of investment types, returns were computed for various allocations. The following results are significant:

- For each of the three time periods (past year, past five years, past ten years) the ***highest total yield*** was reported by charities who had 50-74% of their annuity assets invested in stocks. (Over the ten-year period, the average return from portfolios including 50-74% ***stocks*** was only slightly higher than from portfolios including 50-74% bonds.)

- For each of the three time periods, the ***lowest total yield*** was reported by charities having 75-100% of their annuity assets in ***cash or cash equivalents***.

Reinsurance of Gift Annuities

To the question whether the charity reinsures gift annuities, the responses were:

The cost of reinsuring fluctuates with interest rates and generally requires 60-80% of the contribution. Most charities apparently conclude that reinsuring is not cost effective.

Regulation of Gift Annuities

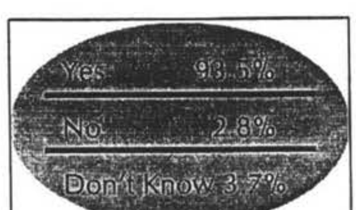
At the time of the survey, the insurance departments of the following eleven states were known to regulate gift annuities:

Arkansas
California
Florida
Maine (University of Maine system)
Maryland
New Jersey
New York
North Dakota
Oregon
Washington
Wisconsin

Certain other states were known to define gift annuities as securities and possibly to require some form of registration with the state securities department. Since the survey was completed, Hawaii and possibly other states have begun to require registration with their insurance departments while in other states legislation is being considered that would specifically exempt gift annuities from regulation. This survey isolated and analyzed data from the above eleven states known to regulate gift annuities through their insurance department. All of these state require a charity to obtain some form of permit to issue gift annuities, and all require the charity to submit an annual report. In this section, these eleven states are referred to as "the regulated states," and authority to issue gift annuities is referred to as "certification".

Certification in Regulated States

Responses were received from 214 charities domiciled in regulated states. To the question whether their state of domicile required certification to issue gift annuities, this group responded:



When this group was further limited to the 166 charities in regulated states that said they had, indeed, issued gift annuities in 1993, the level of awareness was slightly higher:

Yes	94.6%
No	3.0%
Don't Know	2.4%

After indicating whether their state of domicile required certification, respondents were asked whether their charity was, in fact, certified.

Figure 16: ***Percent of All Charities in Regulated States Declaring That They Are Certified in State of Domicile***

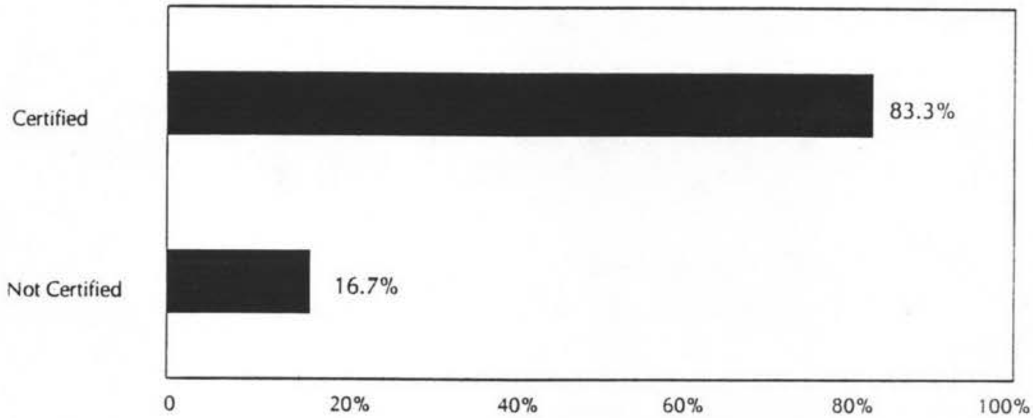
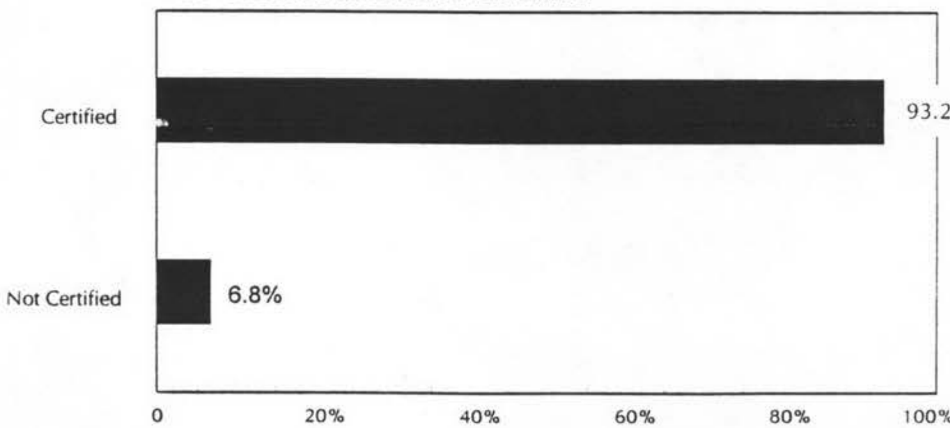
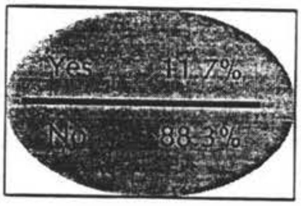


Figure 17: ***Percent of All Charities in Regulated States Actually Issuing Annuities in 1993 Declaring That They Are Certified in State of Domicile***



The results demonstrate that compliance is high with reference to obtaining certification in the state where the charity is located. Some of those not certified may be in the process of doing so or be in a state where certification is not required until a certain threshold amount of annuities have been issued. Respondents were also asked whether they were certified in any states other than their own. The responses from all charities, not just those in regulated states, were as follows:



Unfortunately, no definite conclusions about compliance with other states' certification requirements can be drawn from these numbers. Charities that do not issue annuities to donors outside of their own state naturally would have answered No. Also, charities issuing annuities outside their own state, but not necessarily in regulated states, would have answered No.

Retention of Gift Annuity Contributions in Reserve

Charities were asked to indicate their practice regarding the retention of gift annuity contributions in reserve. Overall, 85.6% answered that none of the contribution is used by the charity until the sole or surviving annuitant has died; 6.5% said that the legally required reserve is set aside and the excess is used by the charity; 7.9% said that, although not required, a reserve is set aside and the excess is used by the organization.

The responses to this question were then compared to the response to the question that asked whether the charity's home state required certification to issue gift annuities. The results were as follows:

Figure 18: ***Does Your State Require Certification to Issue Gift Annuities?***

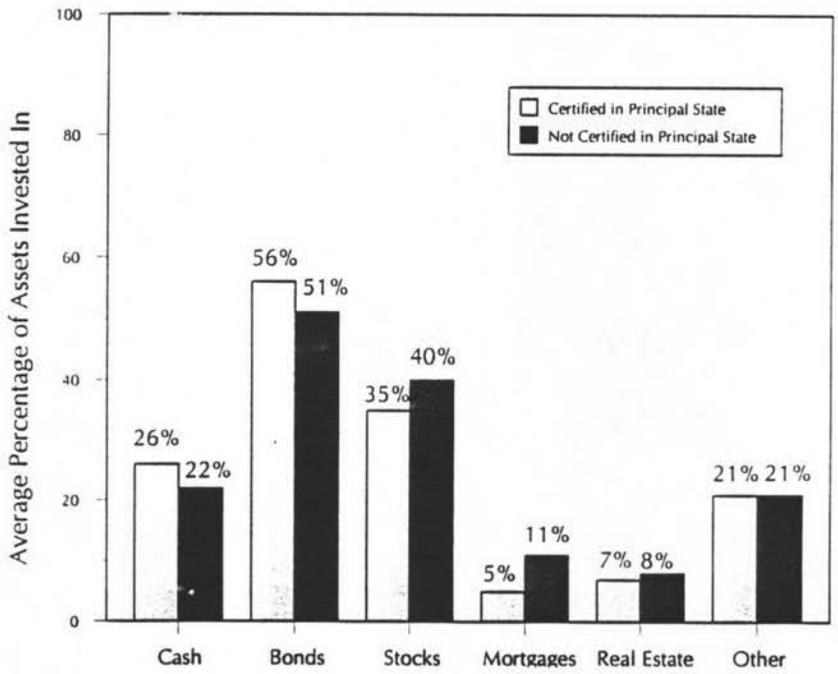
	YES	*NO*
■ Retain all of contribution in reserve	87.4%	84.9%
■ Retain required reserve, use excess	8.7%	5.4%
■ Retain a reserve, though not required, and use excess	4.0%	9.7%

Whether or not required by state law to maintain a legal reserve, most charities don't spend any of the contribution until the surviving annuitant dies.

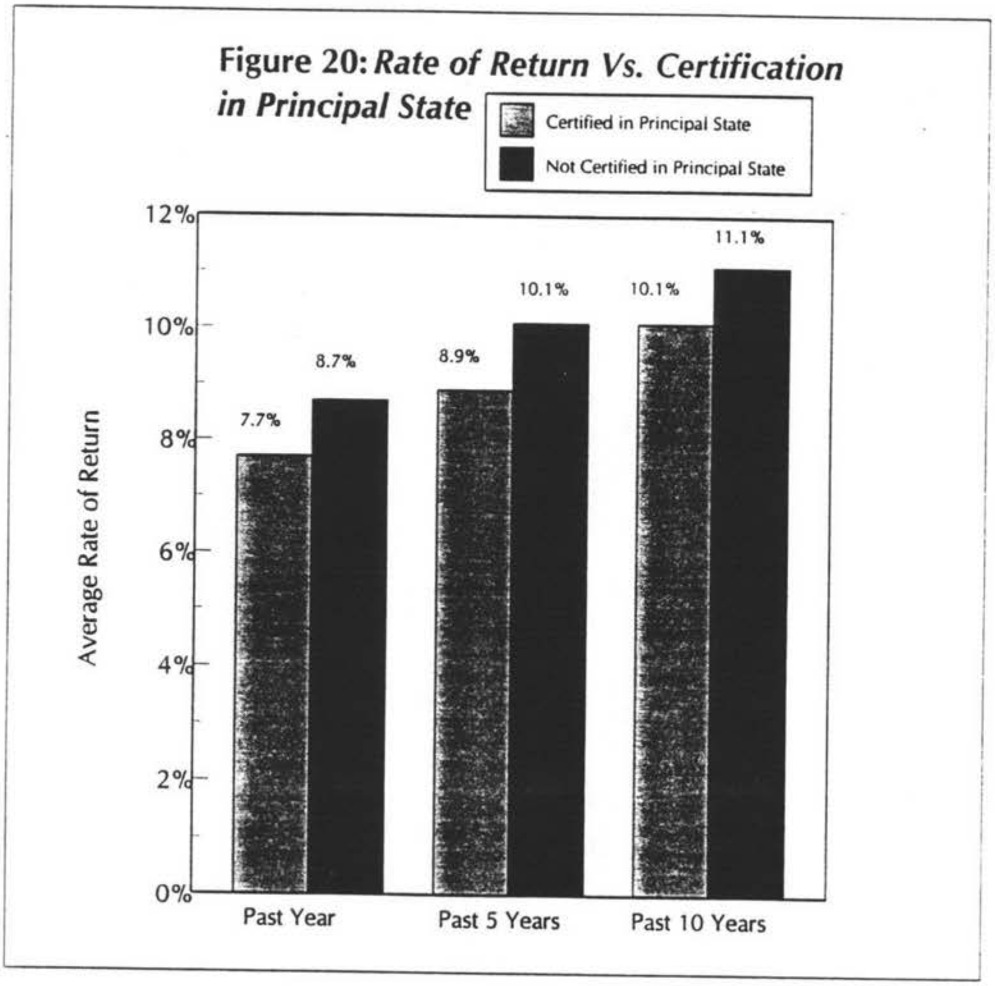
Effect of State Regulation on Investment Return

In order to ascertain how state regulation--or the absence thereof--affects the way charities invest their annuity reserves, the asset mix reported by charities located in regulated states was compared with that of charities in other states. Overall, the tabulation indicates that charities certified in their home states invest comparatively more of their reserves in cash and bonds, while charities not certified in their home states invest comparatively more in stocks.

Figure 19: ***Composition of Portfolio Vs. Certification in Principal State***



Not surprisingly, charities domiciled in regulated states show lower rates of return on their reserves. This is because state regulations restrict the amount of investments in equities which, historically, have shown higher returns than bonds and cash equivalents.



Residuum for the Charity

The "residuum" refers to the portion of the initial contributions for a gift annuity remaining for the charity at the death of the annuitant(s). The ACGA rates, based on certain assumptions about mortality, expenses, and investment earnings, are designed to result in a 50% residuum for the charity.

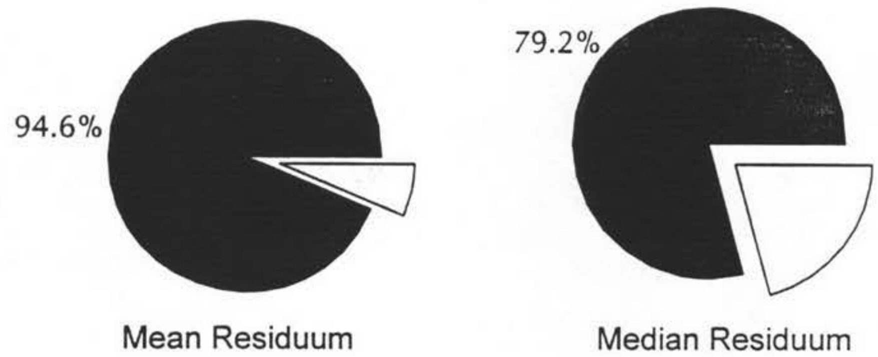
The survey sought to determine the actual residuum realized by charities. Useful data came from 175 charities, all of which have been issuing gift annuities for many years and all of which answered both of the following questions regarding gift annuity contracts that have terminated through the death of the sole or surviving annuitant:

- *What was the total amount received?*

- *What was the total amount left for the organization (residuum) when the contract was terminated?*

The results were most encouraging for charities. The average (mean) amount retained by charities was 94.6% of the original contribution. The median retention (midway point of the responses) was a somewhat more modest 79.2%, but still well above the 50% target residuum of the ACGA rates. Of course, we are comparing dollars originally contributed and dollars remaining for the charity without any present value or inflationary adjustments.

Figures 21 & 22: *Residuum for Charities*



Many of the terminated annuities were likely written in the 1960's and 1970's when charities offered lower annuity rates, in response to the lower interest rates that prevailed during much of that period. When total returns in the 1980's and early 1990's exceeded expectations, the residuum was correspondingly higher than had been projected. The reverse could happen if a prolonged period of lower-than-expected returns followed the issuance of annuities.

Recommended Residuum

Asked whether, for purposes of computing ACGA rates, the assumed residuum should remain at 50%, 78.8% of the respondents said Yes, 17.7% said it should be higher, and 3.5% said it should be lower. A large majority (79.3%) also thought that the 5% expense assumption was about right.

Are Annuitants at Risk?

The finding of the survey regarding the portion of annuity contributions being retained by the issuing charities makes it abundantly clear that the risk to annuitants is minimal. Survey respondents bore out that conclusion when asked whether they were aware of any institution that had defaulted on a charitable gift annuity. Only 2.0% had ever heard of a default. Had they been asked whether they had first-hand knowledge of a default, the percentage undoubtedly would have been lower.

The following factors revealed by the survey all provide security to annuitants:

1. Most charities, even though not required to do so, spend none of the contribution until the death of the sole or surviving annuitant.

2. When charities choose rates different from those provided by the ACGA, they are usually lower.

3. The residuum left for charities at the death of annuitants indicates that ample surplus reserves are being maintained.

These conservative practices not only assure an eventual gift for the charity but also should be reassuring to annuitants.

Conclusions

The following statements summarize the major findings of the 1994 Survey of Charitable Gift Annuities and point to their significance.

1. **Gift annuities are cost effective for charities.** Consider the present value of an annuity:

   - Funded with $18,950 (the 1993 average),
   - With one annuitant age 77 (the average age),
   - And an eventual residuum of 94.6% (the average retention).

   After 11.2 years (the age 77 unisex life expectancy), the charity would receive $17,908. The present value of this gift, discounted at 8%, is $7,563. Assuming the median residuum of 79.2%, rather than the 94.6% average, the charity would receive $15,008, and the present value would still be a respectable $6,338. To be sure, the charity will have incurred some administrative costs during the life of the annuity, but they would ordinarily be a fraction of the present value.

2. **A growing number of charities are issuing gift annuities.** Nearly half of the charities now issuing them started doing so within the past ten years.

3. **Religious organizations and private colleges and universities have been issuing gift annuities for longer than the health care, social services and arts organizations.** As might be expected, they have more annuities in force and complete a larger number of annuity gifts each year.

4. **Gift annuities appeal to a charity's oldest donor group.** On average, donors to charitable remainder unitrusts, charitable remainder annuity trusts, and pooled income funds are younger than gift annuity donors.

5. **Relatively few deferred gift annuities are written.** Gift annuities are not widely used for the purpose of creating a supplemental retirement plan while making a gift.

6. **More than two-thirds of gift annuities are for one life; less than a third are for two lives.**

7. **Males and females are equally inclined to contribute for a gift annuity.** Females make nearly 60 percent of annuity contributions, but in the age range when people are most likely to contribute for a gift annuity, they comprise about 60 percent of the population.

8. **The average size of gift annuities varies widely by type of organization.** Colleges and universities issue the largest annuities, religious and arts organizations the smallest.

9. **While a few of the reporting charities do a very high volume of gift annuities, more than half of them issued nine or less in 1993.** The number tends to increase the longer the institution has been encouraging this type of gift.

10. **Most of the reporting charities (69.7%) followed the ACGA rates. When they departed from those rates, they were more likely to offer lower rates.**

11. **The most common minimum amount required for an initial contribution for an immediate or deferred annuity is $5,000.** A significant number of organizations, however, have a $1,000 minimum. Considering that the costs of administering gift annuities are essentially the same, whatever the size, a $1,000 contribution may be marginally cost effective for the charity unless the organization can handle a high volume of gift annuities very efficiently.

12. **The minimum annuitant ages set by the charities are substantially below the actual ages of most annuity donors.**

13. **The charity's development office generally calculates the deduction, and the business office or outside administrator generally does the accounting and investing and issues the checks.**

14. **For at least ten years, the reporting charities have achieved a significantly higher total return on gift annuity reserves than the rate of return assumed in computing ACGA rates.**

15. **Stocks, bonds and cash equivalents constituted the entire portfolio of most reporting charities.** A relatively small number invested in other assets such as mortgages and real estate.

16. **Charities that have invested 50-74% of their reserves in stocks have achieved the highest total returns, though portfolios with 50-74% bonds have performed nearly as well over the ten-year period ending December 31, 1993.**

17. **Most charities located in states that regulate gift annuities comply with their own state's certification requirements.**

18. **Charities located in regulated states, complying with investment restrictions, invest relatively more of their annuity reserves in bonds and cash equivalents, and they achieve lower rates of return than charities in non-regulated states.**

19. **Most charities go beyond the minimum legal reserve required in regulated states and, in fact, keep the entire contribution in reserve until the death of the sole or surviving annuitant.** Also, charities are careful to explain to prospective donors that a gift annuity is first and foremost a **gift**, and to offer rates sufficiently conservative to assure the gift.

Clearly, the findings of the 1994 Survey of Charitable Gift Annuities reaffirm the popularity of the charitable gift annuity among donors/annuitants and a wide range of charities. The findings also underscore the security and practicality of this time-tested giving vehicle as a means by which donors may simultaneously realize both philanthropic and financial goals, and charities may attract vitally needed resources for their work.

A SURVEY OF CHARITABLE GIFT ANNUITIES

Person completing questionnaire:

Name______________________________ Title______________________________

Organization____

City/State______________________________ Telephone__________________

(If you prefer to remain anonymous, you may omit the above information.
In either case, the data you provide will be confidential.)

Type of Organization:

____ Private college or university
____ Public college or university
____ Hospital/health care
____ Social service
____ Arts
____ Religious organization (not described above)
____ Other

Regarding Completed Gifts:

1. During the calendar year 1993, did your organization issue any charitable gift annuities?
   _____Yes _____No

2. If the answer to Question 1 is "yes,"
   a. What was the total number of annuities issued in 1993? _____
   b. How many of these were deferred annuities? _____
   c. What was the total dollar volume received for gift annuities? $__________
   d. What percentage of annuities issues were for one life? ____% Two lives? ____%
   e. What percentage of the annuitants were male? _____% Female? _____%
   f. What was the average age of annuitants of immediate annuities? _____ yrs.
   Of deferred annuities? _____ yrs.

3. What is the total number of annuity contracts in force at your organization? _______

4. What is the current market value of your organization's total annuity reserves? Include the total amount in all of your annuity accounts, not just the reserves required by state law. $______________

5. For how many years has your organization been offering gift annuities?
   ____ a. Less than five years
   ____ b. Five to ten years
   ____ c. Over ten years

Regarding Policies:

6. Which of the following best describes your organization's practice regarding the maximum gift annuity rates recommended by the American Council on Gift Annuities (until January 1, 1994, known as the Committee on Gift Annuities)?

   ____ a. Always follow the Council rates.
   ____ b. Usually follow the Council rates, but in some instances offer lower rates.
   ____ c. Usually follow the Council rates, but in some instances offer higher rates.
   ____ d. Usually follow the Council rates, but in some instances offer either higher or lower rates.
   ____ e. Regularly offer rates lower than the Council rates.
   ____ f. Regularly offer rates higher than the Council rates.

7. Recently the Council recommended lower maximum rates effective January 1, 1994. Which of the following best describes your opinion of the rate adjustment?
   ____ a. Approve the adjustment and think it was the right amount.
   ____ b. Approved an adjustment but think rates were reduced too much.
   ____ c. Approved an adjustment but think rates should have been reduced still more.
   ____ d. Did not approve an adjustment at this time.

8. To your knowledge, have any of your prospects compared rates with those offered by other organizations?
   ____ Yes ____ No

9. What is the minimum amount your organization requires for a gift annuity?
   a. Initial contribution for an immediate annuity $__________
   b. Subsequent contributions from same donor for an immediate annuity $__________
   c. Initial contribution for a deferred annuity $__________
   d. Subsequent contributions from same donor for a deferred annuity $__________

10. What is the minimum acceptable age of the annuitants?
    a. For immediate annuities _____years
    b. For deferred annuities _____years

Regarding Registration:

11. Does your state require a charity to be registered or certified to offer gift annuities? ____Yes ____No____Don't know
12. Is your organization registered or certified to issue gift annuities in the state where it has its principal location? ____ Yes ____ No

13. Is it registered in any other states? ____Yes ____No

Regarding Investment of Gift Annuity Assets

14. Does your organization operate in a state that restricts the investment of gift annuity reserves? ____Yes ____No
15. Do you reinsure any of your gift annuities? ____Yes ____No

16. What is the practice of your organization regarding retention of contributions in reserve?

____ a. None of the contribution is used by the organization until the sole or surviving annuitant has died.

____ b. Required reserve is set aside and excess is used by the organization.

____ c. Though not required, a reserve is set aside and excess is used by the organization

17. Please indicate the percentages of gift annuity assets invested by your organization in each of the following:

a. Cash and cash equivalents ______%

b. Bonds ______%

c. Stocks ______%

d. Mortgages ______%

e. Real estate ______%

f. Other ______%

Comments: ____

18. What was the net total <u>annual</u> rate of return on the investment of annuity assets? (If most annuity funds are in an investment pool, such as the institution's endowment, state the returns on that pool.)

a. For the past year ______%

b. For the past five years ______%

c. For the past 10 years ______%

Regarding Administration:

19. Who is responsible for gift annuity administration (accounting, tax forms, checks to annuitants, etc.)?

____ a. Business office

____ b. Development office

____ c. Financial institution retained for that purpose

20. Who calculates the amount of the charitable deduction and taxation of payments and provides this information to donors?

____ a. Business office

____ b. Development office

____ c. Other. Explain: ____________________________________

21. By whom are annuity assets invested?

____ a. Internally, by trustees, officers or staff or the organization

____ b. Externally, by professional asset managers

____ c. Combination of a. and b.

22. The American Council on Gift Annuities assumes that the cumulative cost of administering an annuity over its entire duration will be 5% of the amount contributed by the donor. In your experience, is this assumption
____ a. About right
____ b. Too low
____ c. Too high
d. If you checked b. or c., what do you estimate your cost to be? ______%

23. One of the assumptions underlying the gift annuity rates is that the residuum for the charity at the death of the sole or surviving annuitant will be 50% of the original contribution. ("Residuum" refers to the actual amount left for the charity after making payments for the life of the annuitant/s. It is not the present value of the amount left.) Do you think the assumed residuum should
____ a. Remain at 50%
____ b. Be higher
____ c. Be lower
d. What residuum would you recommend? _____%

24. Are you aware of any institution that has defaulted on gift annuity contracts?
____ Yes ____ No

Optional Question:

Please answer to the extent you have available data. This information would be very helpful in evaluating the cost-effectiveness of gift annuities and recommending annuity rates.

25. For all gift annuity contracts that have terminated through the death of the sole or surviving annuitant,
a. What was the total original amount received? $______________
b. What was the total amount left for the organization (residuum) when the contracts terminated? Include in the residuum any portion used by your organization prior to the termination of the contract. $______________

REGISTRANTS FOR 22ND CONFERENCE ON GIFT ANNUITIES
May, 3-5, 1995 San Francisco

Name	Organization	City, State
Stanley J. Abrams, Esq.	United Jewish Appeal, Inc.	New York, N.Y.
Jonathan D. Ackerman, Esq.	Kallina & Ackerman, PC	Baltimore, Md.
Phillip Adcock	American Cancer Society	Atlanta, Ga.
James Y. Albertson	Seventh-day Adventists Georgia Cumberland Assoc.	Calhoun, Ga.
Faye S. Albright	Southern Baptist Foundation	Nashville, Tenn.
Robert A. Alder	Salvation Army, The	Tampa, Fla.
Karen Alexander	Inter-Varsity Christian Fellowship	Madison, Wis.
Roger Alexander	Church of the Nazarene	Kansas City, Mo.
Vernon L. Alger	Seventh-day Adventists Lake Union Conf.	Berrien Springs, Mich.
Sarah M. Alig	Christian Church Foundation, Inc.	Indianapolis, Ind.
Ed Allen, Jr.	National Benevolent Association, The	St. Louis, Mo.
Ralph Allen	Presbyterian Church (U.S.A.) Foundation	Jeffersonville, Ind.
David M. Allison	Emmaus Bible College	Dubuque, Iowa
Al Amaral	Cal Poly State University Foundation	San Luis Obispo, Calif.
Ed Ammon	Walla Walla College	College Place, Wash.
Richard Among	Seventh-day Adventists Hawaii Conference	Honolulu, Hawaii
Elaine Anderson	State Street Bank & Trust Co. of Calif., N.A.	San Francisco, Calif.
Lee F. Anderson	Upper Columbia Corporation	Spokane, Wash.
Michael W. Anderson	Rutgers University Foundation	New Brunswick, N.J.
Eric Andresen	PhilanthroTec, Inc.	Matthews, N.C.
Stuart Appelbaum	Minneapolis Foundation, The	Minneapolis, Minn.
Lynn Eugene Archer	Arthritis Foundation	Atlanta, Ga
Wayne W. Archer	University of Texas Foundation, Inc.	Tyler, Texas
Peggy M. Armstrong	Southern Baptist Foundation	Nashville, Tenn.
Selwyn L. Ash	Seventh-day Adventists Northeastern Conference	Jamaica, N.Y.
Debra Ashton	Boston College	Chestnut Hill, Mass.
John A. Ashworth, III	Salvation Army, The	Charlotte, N.C.
JoAnn L. Avery	Salvation Army, The	Atlanta, Ga.
Lyndon S. Back	American Friends Service Committee	Philadelphia, Pa.
Kathryn E. Baerwald	United Way of America	Alexandria, Va.
Edward F. Bailey	Salvation Army, The	Tampa, Fla.
Walter E. Bailey	Nebraska Methodist Hospital Foundation	Omaha, Neb.
Donna M. Bandelloni	Wells Fargo Bank	Mill Valley, Calif.
James Barber	Samaritan's Purse	Boone, N.C.
Ann Barden	California Pacific Medical Center Foundation	San Francisco, Calif.
Seth Bardu	Seventh-day Adventists South Central Conference	Nashville, Tenn.
Trevor D. Barnes	Seventh-day Adventists N. California Conf. Assn.	Oakland, Calif.
John H. Barney	Africa Inland Mission	Windsor, Conn.
James E. Barr	Ohio Presbyterian Retirement Serv. Found.	Kettering, Ohio
Wayne C. Barrett	United Methodist Foundation	Grand Rapids, Mich.
Anne Bartlome	Ohio State University	Columbus, Ohio
Keith W. Bartz	Carleton College	Northfield, Minn.
Merle Bascom	Andrews University	Berrien Springs, Mich.
Wayne L. Baskerville	Michigan State University	East Lansing, Mich.
Carla J. Bass	Seventh-day Adventists General Conference	Silver Spring, Md.
John R. Bass	Alzheimer's Association	Chicago, Ill.
Louis N. Basso	Catholic Diocese of Wichita	Wichita, Kan.
Ann Bayless	Baptist Memorial Hospital System Foundation	San Antonio, Texas
David L. Bearchell	Arthritis Foundation	Ringoes, N.J.
Don L. Beard	Salvation Army, The, KS/W. MO Div.	Kansas City, Mo.
Dale R. Beaulieu	Seventh-day Adventists Oregon Conference	Gladstone, Ore.
Marvin E. Beckman	Moody Bible Institute	Chicago, Ill.
Jerry Bedford	Heifer International Foundation	Little Rock, Ark.
Ardith Ann Beers	Seventh-day Adventists S. Union Conf.	Decatur, Ga
David R. Beers	Worcester Academy	Worcester, Mass.
Sharon Benner	American Cancer Society	Oakland, Calif.
Mike Bennett	Willamette University	Salem, Ore.
Vera L. Bennett	Peninsula Community Foundation	San Mateo, Calif.
David Benson	David Benson & Associates	Fargo, N.D.
Michael D. Benson	Planned Giving Systems	Cleveland, Ohio
Barry Bentley	Church of God Board of Church Extension	Anderson, Ind.
Barry Benton	Seventh-day Adventists S. Union Trust Services	Calhoun, Ga.
Sandy Benton	Seventh-day Adventists S. Union Trust Services	Calhoun, Ga.

Name	Organization	City, State
Beth Berger	Salvation Army, The	Jackson, Miss.
Brian P. Berrigan	Jesuit Seminary & Mission Bureau	New Orleans, La.
Robert Berube	ALSAC/St. Jude Hospital	Orange, Calif.
Jeffrey W. Billingslea	United Methodist Foundation, Balt.-Wash. Conf.	Baltimore, Md.
John B. Bingham	BancCorp Systems, Inc.	Amarillo, Texas
The Rev. Roger L. Bisson	Missionaries of Africa	Washington, D.C.
Debby Bither	Resource Development, Inc.	Springfield, Mo.
Ron Bitzer	Doheny Eye Institute	Los Angeles, Calif.
James C. Blackburn	American Bible Society	New York, N.Y.
Harold R. Blatt	Eastern Baptist Seminary	Wynnewood, Pa.
Tom Bledsoe	Seventh-day Adventists Arizona Conference	Scottsdale, Ariz.
Denise M. Blew	Lehigh University	Bethlehem, Pa.
Greg Bodine	Salvation Army, The	Glendale, Ariz.
John David Boggess	Seventh-day Adventists Florida Conf.	Winter Park, Fla.
John F. Bohner	Seventh-day Adventists General Conference	Lake Elsinore, Calif.
Jennifer Boland	PG Calc Incorporated	Cambridge, Mass.
Susan Bonne	Arthritis Foundation	Atlanta, Ga.
Harry G. Bonner	California Baptist Foundation	San Marcos, Calif.
Thomas P. Bonner	University of the South	Sewanee, Tenn.
Arthur C. Borden	American Bible Society	New York, N.Y.
James R. Borut	Society for the Propagation of the Faith, The	New York, N.Y.
Keith O. Boyd	Seventh-day Adventists W. Wash. Conf.	Bothell, Wash.
E. J. Brackett	Seventh-day Adventists N. California Conf. Assn.	Paradise, Calif.
Philip S. Brain, Jr.	Minnesota Masonic Home	Bloomington, Minn.
Elizabeth Outland Branner	Young-Preston Associates	Roanoke, Va
Jerry Brass	Adventist Media Center	Ryderwood, Wash.
Michael Brennan	Brennan Analytical	Wall, N.J.
Kara Brewer	University of the Pacific	Stockton, Calif.
Robert T. Bridges	Asbury Theological Seminary	Wilmore, Ky.
Eva M. Brightup	Friends University	Wichita, Kan.
Arthur M. Brink, Jr.	Fletche Allen Health Care	Burlington, Vt.
Warren Brock	Life Outreach International	Ft. Worth, Texas
Roy E. Brooks	Loma Linda University	Loma Linda, Calif.
Bro James P. Brown, SM	Marianist Mission	Dayton, Ohio
Elizabeth A. S. Brown	Moody Bible Institute	Chicago, Ill.
Gail A. Brown	Coral Ridge Ministries Media	Ft. Lauderdale, Fla.
Jim Brown	Seventh-day Adventists N. California Conf. Assn.	Pleasant Hill, Calif.
Linda J. Brown	Concordia College	Moorhead, Minn.
Ronald A. Brown, CFP	National Wildlife Federation	Washington, D.C.
Walter E. Brown, Jr.	Salvation Army, The	Pittsburgh, Pa.
Gene Brueland	David and Margaret Home, Inc.	La Verne, Calif.
Edward A. Brumley	United Methodist Village, Inc., The	Lawrenceville, Ill.
David C. Brunkow, CFRE	Gronlund Sayther Brunkow	Brandon, S.D.
Morris Brusett	Seventh-day Adventists Montana Conference	Helena, Mont.
Beeler Brush	University of the South	Sewanee, Tenn.
Marsha L. Bryan, CFRE	United Methodist Foundation of New England	Salem, N.H.
Steve Bryant	Lutheran Medical Center Foundation	Wheat Ridge, Colo.
Heidrun Buehner	Pranschke & Holderle, L.C.	St. Louis, Mo.
Joseph O. Bull	Ohio State University	Columbus, Ohio
Bill Burkey	California Baptist Foundation	Fresno, Calif.
Barbara Burley	First Church of Christ, Scientist	Boston, Mass.
Linda Burr	Care, Inc.	Oakland, Calif.
Janice H. Burrill	Loyola Marymount University	Los Angeles, Calif.
Jean Bursley	United Methodist Church Gen'l Bd. of Global Ministries	Half Moon Bay, Calif.
Barry Burton	Seventh-day Adventists Rocky Mountain Conference	Littleton, Colo.
Marite M. Butners	Sisters of Providence Health System	Seattle, Wash.
Harvey J. Byram	Seventh-day Adventists SW Union Conf.	Burleson, Texas
Carla Byrd	Oakwood College	Huntsville, Ala.
Douglas L. Byrd	United Methodist Foundation	Raleigh, N.C.
Stacy Caddey	Planned Giving Systems	Cleveland, Ohio
O. Richard Caldwell	Seventh-day Adventists General Conference	Silver Spring, Md.
Marcia J. Cammack	Presbyterian Church (U.S.A.) Foundation	Jeffersonville, Ind.
Eric Campbell	Arthritis Foundation	Chanhassen, Minn.

Name	Organization	City, State
Louis Canosa	Seventh-day Adventists Carolina Conference	Charlotte, N.C.
George Carambot	Seventh-day Adventists N. Pac. Union Conf.	Portland, Ore.
Ray M. Caraway	United Methodist Foundation of La.	Baton Rouge, La.
Arthur Carlson	Seventh-day Adventists Carolina Conference	Fletcher, N.C.
Phil Carman	Moody Bible Institute	Chicago, Ill.
Marc L. Carmichael	R&R Newkirk	Willow Springs, Ill.
Wilma Carmichael	R&R Newkirk	Willow Springs, Ill.
Richard G. Carnes	Kentucky Baptist Foundation	Louisville, Ky.
Joel Carroll	Salvation Army, The	Dallas, Texas
G. Tom Carter	Seventh-day Adventists General Conference	Silver Spring, Md.
Alvin I. Cassidy	Saint Meinrad Seminary	Saint Meinrad, Ind.
Howard B. Castle	Wesleyan Church Corporation	Indianapolis, Ind.
Brigidine M. Castro	Rutgers University Foundation	New Brunswick, N.J.
Gordon M. Caswell	Baylor Helath Care System Foundation	Dallas, Texas
Richard P. Center	Seventh-day Adventists S. Union Conf.	Decatur, Ga
Patricia Chanee	Mount Holyoke College	San Francisco, Calif.
Gerald A. Chapman	Seventh-day Adventists Illinois Assn.	Brookfield, Ill.
Kathleen Chase	Ohio State University	Los Angeles, Calif.
Carolyn A. Chassee	American Cancer Society	Kenner, La.
Dan Chegwidden	Michigan State University	East Lansing, Mich.
John Cherry	Casa Colina Foundation	Pomona, Calif.
John D. Cherry, III	Oral Roberts University	Tulsa, Okla.
Julie Cheshire	San Diego Museum of Art	San Diego, Calif.
R. Joseph Chickey	University of Illinois Foundation	Urbana, Ill.
Maggie Craig Chrisman	Habitat for Humanity International	Scottsdale, Ariz.
K. Gene Christian	St. Vincent Medical Foundation	Portland, Ore.
Kristine Christlieb	Southwestern University	Georgetown, Texas
Kathlene Chytil	Boys and Girls Town of Missouri	St. Louis, Mo.
Carolyn C. Clark	Milbank Tweed Hadley & McCloy	New York, N.Y.
Sannette Clark	Idaho Youth Ranch	Boise, Idaho
Patricia A. Cloninger	Loma Linda University	Grand Terrace, Calif.
Edwin S. Coates	N.C. Baptist Foundation, Inc.	Cary, N.C.
Robert Coffman	Anderson University	Anderson, Ind.
Carol A. Cole	Tufts University	Somerville, Mass.
Richard B. Cole	Whitworth Foundation	Millbrae, Calif.
David M. Coleman	Foreign Mission Board Southern Baptist Conv.	Richmond, Va.
Patricia A. Collins	State Street Bank & Trust Co. of Calif, Inc.	Kingwood, Texas
Laurie McGregor Connor	Ohio Wesleyan University	Delaware, Ohio
Phyllis Cook	Jewish Community Endowment Fund	San Francisco, Calif.
Rev. Thomas R. Cook	Augustinians	Villanova, Pa.
Leon Cornforth	Seventh-day Adventists Idaho Conference	Boise, Idaho
Roy Cortez	Seventh-day Adventists General Conference	Keene, Texas
Rev. William Couchenour	Olivet Nazarene University	Kankakee, Ill.
Richard W. Coughlin	Heritage Gift Planning, Inc.	Indianapolis, Ind.
Becky Cowlishaw	Wells Fargo Bank	San Diego, Calif.
Dewitt T. Cox	Georgia Baptist Foundation	Atlanta, Ga.
Kevin Crawford	Christian Homes	Lincoln, Ill.
John Crooch	Oklahoma United Methodist Foundation	Oklahoma City, Okla.
Stewart J. Crook	Seventh-day Adventists S. Union Conf.	Decatur, Ga
Clark Cropp	Kansas University Endowment	Lawrence, Kan.
Jim Cruthoff	Catholic Community Foundation Diocese of Phoenix	Phoenix, Ariz.
Larry Cruzen	Trinity Broadcasting Network	Tustin, Calif.
Tom Cullinan	University of Houston System	Houston, Texas
Charles P. Cushman	Gonser Gerber Tinker Stuhr	Naperville, Ill.
Charles W. Custer	Salvation Army, The	Tampa, Fla.
Max W. Custer, Jr.		Pawling, N.Y.
Pamela N. Czekanski	Loomis-Sayles & Company	Boston, Mass.
Laura D'Addato	Heath Village, Inc.	Hackettstown, N.J.
Elaine D'Amours	Mount Holyoke College	South Hadley, Mass.
Sherri Dalbom	Friends University	Wichita, Kan.
Michael S. Dalis	State Street Bank & Trust Co.	Boston, Mass.
W. Robert Daum	Seventh-day Adventists Pac. Union Assn.	Westlake Village, Calif.
Pamela J. Davidson	Indiana University Foundation	Bloomington, Ind.

Name	Organization	City, State
David M. Davies	Salvation Army, The	Omaha, Neb.
Daniel L. Davis	Seventh-day Adventists	Pine Forge, Pa.
Herman L. Davis, Sr.	Seventh-day Adventists SE Conf.	Altamonte Springs, Fla.
Larry L. Davis	Seventh-day Adventists S. Union Conf.	Decatur, Ga
Judith M. Dawson	Punahou School	Honolulu, Hawaii
Dennis R. Day	St. Norbert College	DePere, Wis.
Ethel M. Dean	Presbyterian Homes of N.J. Foundation, The	Princeton, N.J.
Paul M. DeBooy	Seventh-day Adventists General Conference Trust Services	Nice, Calif.
John Degnin	Mt. Angel Abbey & Seminary	St. Benedict, Ore.
Leo H. Dehler	Archdiocese of St. Paul and Minneapolis	St. Paul, Minn.
William P. DeMoranville	Arthritis Foundation	Land O'Lakes, Fla.
Rose Denman	Southwestern Ohio Seniors' Services, Inc.	Cincinnati, Ohio
Ken DeVries	Western Mich. University Foundation	Kalamazoo, Mich.
Michael B. Dey	SIM USA, Inc.	Charlotte, N.C.
Kent W. Dickinson	Seventh-day Adventists Nevada-Utah Conference	Reno, Nev.
Phil Dickinson	Salvation Army, The	Phoenix, Ariz.
John Dickson	American Heart Association	Los Angeles, Calif.
Barbara R. Diehl	American Bible Society	New York, N.Y.
Chris E. Dierkes	American Institute for Cancer Research	Washington, D.C.
Raymond Diesbourg	Missionaries of the Sacred Heart	Aurora, Ill.
Doris Dieter	American Foundation for the Blind	New York, N.Y.
Bernard DiFiore	Catholic Foundation, The	Dallas, Texas
John W. Dixon	Fiduciary Trust Co. International	New York, N.Y.
Pat Dixon	Crista Ministries	Seattle, Wash.
Ernest Dobkins	Seventh-day Adventists Rocky Mountain Conference	Denver, Colo.
Gary Dodge	Seventh-day Adventists Idaho Conference	Boise, Idaho
Lynwood Donald	Mercer University	Macon, Ga.
Stephen A. Donato, Esq.	American Lung Association	New York, N.Y.
Andre Donikian	Pentera, Inc.	Indianapolis, Ind.
Janet Doolin	National MS Society	Engelwood, Colo.
Karnik Doukmetzian	Seventh-day Adventists Ontario Conf. Corp.	Oshawa, Ontario, CANADA
Michael P. Dowell	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Rick Downey	Fred Hutchinson Cancer Research Fnd. Ctr.	Seattle, Wash.
Pamela G. Downing	Diocese of Brownsville	Brownsville, Texas
Peter V. K. Doyle	Wellesley College	Wellesley, Mass.
James Draznin	Portland State University	Portland, Ore.
Steacy Drew	St. Helena Hospital	Deer Park, Calif.
Phyllis H. Drickman, Esq.	Shriners Hospital for Crippled Children	Tampa, Fla.
Gabrielle Dudley	Children's Hospital Foundation	Seattle, Wash.
Lon P. Dufek	Crescendo Software	Camarillo, Calif.
Douglas Duke	People for the Ethical Treatment of Animals	Rockville, Md.
David R. Duncan	Seventh-day Adventists N. Pac. Union Conf.	Portland, Ore.
Dale E. Eazell	Casa Colina Foundation	Pomona, Calif.
Gregory W. Edwards	Nature Conservancy, The	Arlington, Va.
Trudi Edwards	Nat'l Assn. of Congregational Christian Churches	Oak Creek, Wis.
Bill Eichmeyer	Wycliffe Bible Translators	Huntington Beach, Calif.
Melvin K. Eisele	Seventh-day Adventists S. Union Conf.	Montgomery, Ala.
Gene A. Ekenstam	Huntington Library, The	San Marino, Calif.
Katherine V. Ekstrom	Glenwood School for Boys	Glenwood, Ill.
Don Elmore	South America Mission	Lake Worth, Fla.
Fred C. Ely	SIM USA, Inc.	Charlotte, N.C.
Ben H. Engbrecht	North American Baptist Seminary	Sioux Falls, S.D.
Ellen Estes	Estes Associates	Woodbridge, Conn.
G. Thomas Evans	Seventh-day Adventists Mid-America Union Conf.	Lincoln, Neb.
William W. Evans	Free Will Baptist Foundation	Antioch, Tenn.
Gary Faircloth	Starr Commonwealth	Albion, Mich.
Charles Fankhauser	Diocese of Brownsville	Brownsville, Texas
Martha Farrington	Riverside Community Hospital Foundation	Riverside, Calif.
Terry Farris	Seventh-day Adventists Pacific Union College	Angwin, Calif.
Kenneth C. Feinour, Jr.	Good Shepherd Home Foundation	Allentown, Pa.
James A. Felchlin	Van Deventor & Hoch	San Francisco, Calif.
John G. Fike, CFRE	Detroit Intitute of Arts	Detroit, Mich.
LeRoy Finck	Seventh-day Adventists Oregon Conference	Brush Prairie, Wash.

Name	Organization	City, State
Robert J. Finley	American Bible Society	Boiling Springs, Pa.
Linda M. Fischler	Fox Chase Cancer Center	Philadelphia, Pa.
Allan Fisher	Walla Walla College	College Place, Wash.
Ann M. Fisher	Trinity Missions	Silver Spring, Md.
Thomas Fitton	Accuracy in Media	Washington, D.C.
Kenneth Flanigan	Evangelical Alliance Mission, The	Wheaton, Ill.
Dr. Milton B. Fletcher	Abilene Christian University	Abilene, Texas
Carol Eid Fliss	Concordia College	Moorhead, Minn.
Paul Flucke	Planned Giving Services	Seattle, Wash.
John H. Fogel	Bowling Green State University	Bowling Green, Ohio
Bill W. Foil	Salvation Army, The	Dallas, Texas
Kathy Folkerts	Bremwood Lutheran Children's Home	Waverly, Iowa
Stanley J. Forkner	U. S. Trust Company	New York, N.Y.
Karen J. Forster, CFP	University of Dayton	Dayton, Ohio
Paula S. Fortunas	FSU Foundation, Inc.	Tallahassee, Fla.
David Fortune	Church of God Board of Church Extension	Anderson, Ind.
Colin T. Foster	Salvation Army, The	West Nyack, N.Y.
Charles A. Fowlie	Preachers' Aid Society of New England	Northboro, Mass.
James B. Fox	Clifford Associates, Inc.	Pasadena, Calif.
Jean Carlson Frailey	Salvation Army, The	Boston, Mass.
Jackie W. Franey	American Heart Association	Dallas, Texas
Ralph Franklin	Seventh-day Adventists So. Atlantic Conf. Assn.	Atlanta, Ga.
Gary Franz	General Conference Mennonite Church	Newton, Kan.
Vince Fraumeni	Chapman University	Orange, Calif.
Diane M. Freaney	Philadelphia Foundation	Philadelphia, Pa.
David D. Freedman	Seventh-day Adventists Alaska Conference	Anchorage, Alaska
Renelda Freeman-Wyles	St. Labre Indian School Ed. Assn.	Ashland, Mont.
Colin V. French	Boy Scouts of America	Irving, Texas
Harold G. Frentz	Nat'l Assn.of Congregational Christian Churches	Huntington Park, Calif.
Don Freymann	Loras College	Dubuque, Iowa
Jeanne Friedman	Peninsula Community Foundation	San Mateo, Calif.
Laura B. Froats	Community Foundation of Greater Flint	Flint, Mich.
Robert W. Frost	Loma Linda University	Loma Linda, Calif.
Susan Frost	Clarke School for the Deaf	Northampton, Mass.
Lynn F. Furr	Phoebe-Devitt Homes	Allentown, Pa.
David Gadberry	City of Hope	Los Angeles, Calif.
Barbara Gallo	Peale Center for Christian Living	Pawling, N.Y.
W. Wayne Gardner	Toccoa Falls College	Toccoa Falls, Ga.
Judy C. Garner	Southern Baptist Foundation	Nashville, Tenn.
Dave Garrett	Jews for Jesus	San Francisco, Calif.
Dan T. Garrett	Abilene Christian University	Mansfield, Texas
Patricia Gately	Oblate Missions	San Antonio, Texas
Susan Gathings	Loma Linda University	Loma Linda, Calif.
Leo E. Geier	University of Maryland System	Adelphi, Md.
Dianne Georgen	Catholic Church Extension Society of the U.S.A.	Chicago, Ill.
G. G. Gessele	Seventh-day Adventists Oregon Conference	Gaston, Ore.
D. Randall Gibson	Kentucky Baptist Foundation	Louisville, Ky.
Doris L. Gidney	United Methodist Church Gen'l Bd. of Global Ministries	Asheville, N.C.
Francis C. Gillette	Northwest College Foundation	Powell, Wyo.
Phillip H. Gillis	Flat Rock Homes	Flat Rock, Ohio
Marvin Glantz	Seventh-day Adventists W. Wash. Conf.	Bothell, Wash.
Cheryl Godwin	Colorado National Bank	Denver, Colo.
Bob Golberg, CFRE	Amherst H. Wilder Foundation	St. Paul, Minn.
Adolfo Gomez	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Mary J. Goodell	City of Hope	Los Angeles, Calif.
Kenneth E. Gooden	Salvation Army, The	New York, N.Y.
Chris Goodier	Salvation Army, The	Washington, D.C.
Gregory S. Goodrich	Hoag Hospital Foundation	Newport Beach, Calif.
Laura Goostree	American Bible Society	New York, N.Y.
Gordon Gordon	Carnegie Mellon University	Pittsburgh, Pa.
Charles Gordy	Tufts University	Somerville, Mass.
Robert S. Goss	Loyola University	New Orleans, La.
DeWitt S. Goulbourne	Seventh-day Adventists General Conference	Silver Spring, Md.

Name	Organization	City, State
David L. Gowan	American Bible Society	New York, N.Y.
Robert Grady	Seventh-day Adventists W. Wash. Conf.	Bothell, Wash.
Donald P. Grant	Peale Center for Christian Living	Pawling, N.Y.
Grayce N. Grant	Adventist Media Center	Newbury Park, Calif.
Susan Dame Greene	American Red Cross	Washington, D.C.
R. Bertram Greener	Fredrikson & Byron, P.A.	Minneapolis, Minn.
Doug Gregg	Seventh-day Adventists Indiana Assn.	Carmel, Ind.
Richard A. Gross	Camina Healthcare Foundation	Mountain View, Calif.
Allison K. Groves	Wellesley College	Wellesley, Mass.
Sister Rose Guercio	Maryknoll Sisters of St. Dominic, Inc.	Maryknoll, N.Y.
Gerry C. Gunnin	Children's Medical Foundation	Dallas, Texas
Richard G. Habenicht	Seventh-day Adventists Wisconsin Conference	Madison, Wis.
Arlind F. Hackett	Seventh-day Adventists Oregon Conference	Boring, Ore.
Ronalyn S. Hackleman	Seventh-day Adventists Indiana Assn.	Carmel, Ind.
Bill Haggstrom, CFRE	Salvation Army, The, Indiana Div.	Indianapolis, Ind.
Kathleen M. Hale	Evangelical Lutheran Church in America	Chicago, Ill.
Beth Hall	Casa Colina Foundation	Pomona, Calif.
Will J. Hancock	Hawaii Preparatory Academy	Kamuela, Hawaii
Robert Harding	Gray, Plant, Mooty, Mooty & Bennett	Minneapolis, Minn.
Paul Harkess	Prudential Real Estate Gifts	Houston, Texas
Catherine C. Harper	Principia Schools	St. Louis, Mo.
David J. Harris	United Methodist Foundation, California-Nevada	Santa Rosa, Calif.
Nancy Gunn Harsha	Whitworth Foundation	Spokane, Wash.
Kandy K. Hart	Cal Poly State University Foundation	San Luis Obispo, Calif.
Sid Hartman	Minneapolis Foundation, The	Minneapolis, Minn.
Robert D. Hastings	Seventh-day Adventists N. Pac. Union Conf.	Portland, Ore.
Lawrence Hawkins	Christian Record Services, Inc.	Lincoln, Neb.
B. Hay	Seventh-day Adventists Gulf States Conference	Montgomery, Ala.
Martin Hayter	University of California San Diego	La Jolla, Calif.
Cecil Hazzard	Seventh-day Adventists General Conference	Westlake Village, Calif.
Dwight Heaney	Curative Rehabilitation Services	Milwaukee, Wis.
Donald S. Hedrick	Eastern Mennonite University	Harrisonburg, Va.
David Heetland	Garrett-Evangelical Theological Seminary	Evanston, Ill.
Richard L. Heinrich	Salk Institute for Biological Studies, The	San Diego, Calif.
Roger W. Heinrich	Seventh-day Adventists Southeastern Calif. Assn.	Colton, Calif.
Jonathan Heintzelman	Northwestern University	Evanston, Ill.
Doris H. Heiser	Milwaukee Foundation	Milwaukee, Wis.
Richard L. Heiss	United Methodist Foundation	Chicago, Ill.
Phillip N. Helmuth	Eastern Mennonite University	Harrisonburg, Va.
The Rev. William F. Helwig	United Methodist Foundation Wisconsin	Sun Prairie, Wis.
Peter W. Hemmenway	Hemmenway & Reinhardt, Inc.	Swarthmore, Pa.
Art Hempel, Jr.	Seventh-day Adventists Central Calif. Assn.	Clovis, Calif.
Dwight Hendricks	College of St. Benedict	St. Joseph, Minn.
William L. Henry	Seventh-day Adventists General Conference	Roca, Neb.
Viveca N. Hernandez	Seventh-day Adventists, The Quiet Hour	Redlands, Calif.
A.J. Hess	Seventh-day Adventists Florida Conf.	Apopka, Fla.
Roger M. Hewett	University of Massachusetts	Amherst, Mass.
Peggy Hilden	Physicians Committee for Responsible Medicine	San Francisco, Calif.
Edwin R. Hill	Whitworth Foundation	Spokane, Wash.
Irving G. Hill	United Methodist Church Foundation	Syracuse, N.Y.
Douglas Hilliard	Seventh-day Adventists Kentucky/Tennessee Conference	Goodlettsville, Tenn.
Margaret F. Hillman	Colorado College, The	Colorado Springs, Colo.
David Himes	Salvation Army, The	Des Plaines, Ill.
Sharlene P. Hirsch	Glens Falls Hospital	Glens Falls, N.Y.
Larry Hitner	Louisville Presbyterian Theological Seminary	Louisville, Ky.
Thomas R. Hixson	Northwest Baptist Foundation	Portland, Ore.
Darl G. Hobson	United Methodist Foundation, Rocky Mountain Conf.	Denver, Colo.
Lee Hoffman	PhilanthroTec, Inc.	Matthews, N.C.
Michelle Holmes	American Baptist Seminary of the West	Berkeley, Calif.
Paul Holtan	Concordia College	Moorhead, Minn.
James R. Hoobler	Ohio State University	Columbus, Ohio
James Hoodman	Bremwood Lutheran Children's Home	Waverly, Iowa
Jim Horsley	World Vision, Inc.	Monrovia, Calif.

Name	Organization	City, State
Yvonne M. House	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Rodney L. Houts	Arizona State University	Tempe, Ariz.
Chris Howe	First Church of Christ, Scientist	Boston, Mass.
Jerry Howell	Haggai Institute	Atlanta, Ga.
Michael E. Howell	Whitman College	Walla Walla, Wash.
Eckhard Hubin	Andrews University	Berrien Springs, Mich.
Chase S. Hunt	Princeton Theological Seminary	Princeton, N.J.
James C. Huska	WELS Foundation, Inc.	Milwaukee, Wis.
Deborah M. Hyde	Music Center Foundation	Los Angeles, Calif.
Dr. Richard E. Ice	American Baptist Homes of the West	Oakland, Calif.
Albert D. Inglish	Seventh-day Adventists Indiana Assn.	Carmel, Ind.
David J. Iommarini	Lighthouse, The	New York, N.Y.
Davida Isaacson	Thirteen/WNET	New York, N.Y.
Allen J. Iseminger	Seventh-day Adventists Oregon Conference	Clackamas, Ore.
A. F. Iwen	Shodair Children's Hospital	Helena, Mont.
Jerald Jackson	United Methodist Foundation, NM Conf.	Albuquerque, N.M.
Sam Jackson	World Vision, Inc.	Monrovia, Calif.
John B. Jacobs	American Baptist Foundation	Valley Forge, Pa.
J. Lance Jacobson	Mayo Foundation for Medical Educ. & Res.	Rochester, Minn.
Richard A. James	Loma Linda University	Loma Linda, Calif.
Lloyd Janzen	Seventh-day Adventists Southeastern Calif. Assn.	Riverside, Calif.
Coy H. Jeans	N.C. Baptist Foundation, Inc.	Cary, N.C.
Nancy J. Jeffers	Robert F. Sharpe and Co., Inc.	Memphis, Tenn.
Reese Jenkins	Loma Linda University	Loma Linda, Calif.
Robert D. Jenkins	DePauw University	Greencastle, Ind.
Andrew G. Jensen	California Lutheran Homes	Alhambra, Calif.
Bill Jester	Resource Development, Inc.	Springfield, Mo.
Kenneth D. Johns	Braille Institute	Los Angeles, Calif.
James P. Johnson	Christian Church Foundation, Inc.	Indianapolis, Ind.
Leroy M. Johnson	Covenant Trust Co.	Chicago, Ill.
Michael A. Johnson, CFRE	Arthritis Foundation	Richmond, Ind.
Ray Johnson	Georgia Baptist Foundation	Atlanta, Ga.
Tanya Howe Johnson	National Committee on Planned Giving	Indianapolis, Ind.
David E. Johnston	Seventh-day Adventists General Conference	Silver Spring, Md.
Oliver L. Johnston	Seventh-day Adventists, The Quiet Hour	Redlands, Calif.
Donald W. Joiner	Planned Giving Resource Center	Nashville, Tenn.
Catherine S. Jones	American Baptist Churches M&M Benefit Board	New York, N.Y.
Don B. Jones	Oklahoma Baptist University	Shawnee, Okla.
Lynne Marie S. Jones	Salvation Army, The	Syracuse, N.Y.
Major Tom Jones	Salvation Army, The	Atlanta, Ga.
Timothy A. Jones	University of Colorado Foundation	Boulder, Colo.
William C. Jones	Oakwood College	Harvest, Ala.
Lisa Jordan	Salvation Army, The	Des Plaines, Ill.
Neil S. Jordheim	Heartland Trust Company	Fargo, N.D.
John Joslin	University of St. Thomas	St. Paul, Minn.
Bill Junk	Oklahoma United Methodist Foundation	Oklahoma City, Okla.
Molly Karnitz	Grand Rapids Foundation, The	Grand Rapids, Mich.
Rev. Peter Kaseta	Province of St. Mary of the Capuchin Order	New York, N.Y.
J. Scott Kaspick	Kaspick & Company	Menlo Park, Calif.
Glen Kauffman	Mennonite Foundation, Inc.	Harrisonburg, Va.
Lorri Kazlauskas	First Interstate Bank	Riverside, Calif.
D.C. Keith, Sr.	Oakwood College	Huntsville, Ala.
Phil Kell	California Baptist Foundation	Fresno, Calif.
Marvin L. Kelley	University of Cincinnati Foundation	Cincinnati, Ohio
Robert Kelley	Society of the Divine Word	Techny, Ill.
Stephen D. Kelley	Lutheran Social Services of the South, Inc.	Houston, Texas
Don Kellogg	Seventh-day Adventists Dakota Conf.	Pierre, S.D.
Cam Kelly	Smith College	Northampton, Mass.
Joan Kenna	Vassar College	Poughkeepsie, N.Y.
John F. Kennedy	Catholic Medical Mission Board, Inc.	New York, N.Y.
Leonard Kennedy	Central Association of the Miraculous Medal, The	Philadelphia, Pa.
Carol Kersten	Stanford University Medical Center	Stanford, Calif.
C. William Kimbell	Masonic Charity Foundation of Conn., The	Wallingford, Conn.

Name	Organization	City, State
Mary E. King	Cal Farley's Boys Ranch	Amarillo, Texas
Wayne A. King	OMS International, Inc.	Greenwood, Ind.
William R. Kinsella	UCLA Foundation, The	Los Angeles, Calif.
Joyce Kinson	Colorado College, The	Colorado Springs, Colo.
Luanne Kirwin	Brandeis University	Waltham, Mass.
Sandra L. Klasky	California State University Northridge	Northridge, Calif.
Linda Klebba	Seventh-day Adventists Southeastern Calif. Assn.	Riverside, Calif.
Brian B. Knecht	Dominicans - Province of St. Albert the Great	Chicago, Ill.
Robert Knehans	Lutheran Church-Missouri Synod Foundation	St. Louis, Mo.
Edward C. Knox, CFRE	Salvation Army, The	Hazelton, Pa.
Fr. Martin Kobos	Conventual Franciscan Friars	Ellicott City, Md.
Russell V. Kohr	Ravinia Festival Association	Highland Park, Ill.
Louise Kolar	Salvation Army, The	Des Plaines, Ill.
Floyd Koorenny	Loma Linda University	Loma Linda, Calif.
John Korb	Portland Adventist Medical Center	Portland, Ore.
C. Alan Korthals	First Church of Christ, Scientist	Boston, Mass.
Sister Anne Kraus	Sisters of Providence	St. Mary-of-the-Woods, Ind.
Kathy Kroeger	Ayn Rand Institute, The	Marina del Rey, Calif.
Dr. Charlotte Kroeker	Whitworth College	Spokane, Wash.
Alfred G. Kromminga	Seventh-day Adventists Southeastern Calif. Assn.	Riverside, Calif.
Walter Krovoza	Pilgrim Place	Claremont, Calif.
Gail Kurtz	Western Mich. University Foundation	Kalamazoo, Mich.
Silvana La Russa	Salvation Army, The	San Juan, Puerto Rico
Larry LaCross	St. Lawrence Seminary	Detroit, Mich.
Ken Ladd	Seventh-day Adventists Nevada-Utah Conference	Reno, Nev.
Karen J. LaMadrid	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Doug Lambert	Bible Literature International, Inc.	Columbus, Ohio
Jerry Lambert	Salvation Army, The	Tampa, Fla.
Lindsay L. Lapole, CFRE	Salvation Army, The	Atlanta, Ga.
William A. Lapole	Salvation Army, The	Charlotte, N.C.
Joseph L. Lapp	Eastern Mennonite University	Harrisonburg, Va.
Kenneth C. Larson	Wheaton College (Illinois)	Wheaton, Ill.
Bill Laskin	PG Calc Incorporated	Cambridge, Mass.
Carl J. Latona	Highfields, Inc.	Onondaga, Mich.
Rita Lawler	Father Flanagan's Boys Home	Boys Town, Neb.
Sara Lawrence	Colby-Sawyer College	New London, Conn.
Robert Lawson	Catholic Charities of St. Paul and Mpls.	Minneapolis, Minn.
Clair H. Leaman	Transport for Christ, Int'l.	Denver, Pa.
Nancy Leanues	Wheaton College	Norton, Mass.
Frederick H. Leasure	United Methodist Foundation, W. Pa. Conf.	Pittsburgh, Pa.
Maynard LeBrun	Seventh-day Adventists Pacific Union College	Angwin, Calif.
Anne Lee	Medical University of South Carolina	Charleston, S.C.
Bill Lee	Georgia Institute of Technology	Atlanta, Ga.
Maril Lee	HCJB World Radio	Colorado Springs, Colo.
Jose A. LeGrand	Seventh-day Adventists Florida Conf.	Winter Park, Fla.
Barry E. Leonard	Christian Appalachian Project	Lancaster, Ky.
Gary W. Leonhardt	Arizona State University	Tempe, Ariz.
Lennette Lesko	Seventh-day Adventists Southeastern Calif. Assn.	Riverside, Calif.
Richard J. Lesniak	Priests of the Sacred Heart	Hales Corner, Wis.
Charles T.E. Lester	Glenmary Home Missioners	Cincinnati, Ohio
H. Kenwood Lewis	Northwestern Memorial Foundation	Chicago, Ill.
David A. Libengood	First Church of Christ, Scientist	Boston, Mass.
John Lillie	Northern Illinois Medical Center Foundation	Woodside, Ill.
Steve Link	Lehigh University	Bethlehem, Pa.
John Lipscomb	Berry College	Rome, Ga.
Greg Lober	Resource Development, Inc.	Springfield, Mo.
Thomas R. Locke	Texas Methodist Foundation	Austin, Texas
Fred E. Loder	Nebraska United Methodist Foundation, The	Lincoln, Neb.
Christine Loew	Presbyterian Healthcare Foundation	Albuquerque, N.M.
Lee W. Logan	Erskine College	Due West, S.C.
Lorna Loram	Independent Institute, The	Oakland, Calif.
Jim Loscheider	Christian & Missionary Alliance, The	Colorado Springs, Colo.
Bruce Lott	Christian Church Homes of Ky., Inc., The	Louisville, Ky.

Name	Organization	City, State
Norm Lotz	Covenant House	New York, N.Y.
Gaye Lowenstein	Wells Fargo Bank	Los Angeles, Calif.
Daniel A. Luessenhop	Society of the Little Flower	Darien, Ill.
Robert Lumbrix	United Methodist Village, Inc., The	Lawrenceville, Ill.
Clifford H. Lura	American Heart Association	Martinez, Calif.
Daniel W. Luther	Mayer, Brown & Platt	Chicago, Ill.
Andrew E. Lutton	American Cancer Society	Tampa, Fla.
Jeffrey Lydenburg	Cleveland Clinic Foundation	Cleveland, Ohio
Elizabeth Dyrud Lyman	Children's Museum of Indianapolis, The	Indianapolis, Ind.
Barbara D. Mack	St. Jude League/Claretians, Inc.	Chicago, Ill.
Alexander Macnab	Covenant Trust of the Evangelical Covenant Church	Chicago, Ill.
Pat Madsen	Carle Development Foundation, The	Urbana, Ill.
Dennis J. Mahon	Seton Hall University	South Orange, N.J.
David Mahoney	Stelter Company, The	Des Moines, Iowa
James Mallery	Salvation Army, The	Anchorage, Alaska
Betsy Mangone	University of Colorado Foundation	Denver, Colo.
Linton G. Manier	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Barlow T. Mann	Robert F. Sharpe and Co., Inc.	Memphis, Tenn.
Nancy Maraldo	Pentera, Inc.	Indianapolis, Ind.
Ray L. Marchman	Salvation Army, The	Atlanta, Ga.
Jonathan Markham	Jews for Jesus	San Francisco, Calif.
Ray Markham	Jesuits of Missouri Province	St. Louis, Mo.
Myrna S. Marseille	Suomi College	Hancock, Mich.
Thomas W. Marston	United Methodist Foundation, Florida	Lakeland, Fla.
William Roger Martin	Upper Columbia Corporation	Spokane, Wash.
John L. Martinez	Tulane University	New Orleans, La.
Thomas A. Martz	Rockhurst College	Kansas City, Mo.
Leslie Mason-Bailey	ALSAC/St. Jude Hospital	Memphis, Tenn.
A. Ruth Matthews	Arthritis Foundation	Atlanta, Ga
Colonel J. B. Matthews	Salvation Army, The	Alexandria, Va.
Elizabeth E. Matthews	Seventh-day Adventists Pac. Union Assn.	Westlake Village, Calif.
Marty Matula	Morton Plant Hospital Foundation	Clearwater, Fla.
Dee May	Seventh-day Adventists Florida Conf.	Winter Park, Fla.
Larry Mayfield	Great American Life Insurance Company	Cincinnati, Ohio
Edward J. McBride	University of Idaho Foundation	Moscow, Idaho
Michael D. McCall	University of Colorado Foundation	Boulder, Colo.
William P. McCarthy	Kelly Ryan Financial	Sarasota, Fla.
Maureen McCawley	Province of Our Lady of Consolation, Inc.	Mt. St. Francis, Ind.
Nan McClaren	American Red Cross	Kansas City, Mo.
Blanche D. McCloskey	National Wildlife Federation	Washington, D.C.
Carolyn Pharis McCone	St. Vincent Development Foundation	Little Rock, Ark.
Michael S. McCormack	Pomona College, Annuity & Trust	Claremont, Calif.
Robert A. McCumber	Seventh-day Adventists Rocky Mountain Conf.	Denver, Colo.
Bo McElroy	Converse & Associates	Memphis, Tenn.
Monica M. McGinley	Medical Mission Sisters	Philadelphia, Pa.
Hetty N. McGinnis	Pittsburgh Foundation, The	Pittsburgh, Pa.
Frank H. McGrory	Massachusetts Institute of Technology	Cambridge, Mass.
Becky McGuire	Seventh-day Adventists General Conference	Winter Park, Fla.
Rev. Jerome McHugh	Province of St. Mary of the Capuchin Order	White Plains, N.Y.
Clif McIntire	Salvation Army, The	Atlanta, Ga.
C. Joe McIntosh	Southern Baptist Convention Annuity Bd.	Dallas, Texas
John S. McIntosh	Seventh-day Adventists N. California Conf. Assn.	Angwin, Calif.
Mary F. McIntyre	Jesuit Development Office	Baltimore, Md.
T. Joseph McKay, JD/CPA	Baylor College of Medicine	Houston, Texas
Dick McLaughlin	Rogue Valley Manor Foundation	Medford, Ore.
Michael J. McNamara	Mayo Foundation	Jacksonville, Fla.
Evelyn L. Meditz	Designs for Planned Giving Success	Joliet, Ill.
Glenn Meekman, Jr.	Seventh-day Adventists General Conference	Columbia, Md.
Carl I. Mehl	Planned Giving Foundation	San Jose, Calif.
Raymond L. Mehl	Evangelical Lutheran Good Samaritan Society	Sioux Falls, S.D.
Ben Mehringer, CPA	National Benevolent Association, The	St. Louis, Mo.
Ronald H. Meier	Wisconsin Lutheran High School	Milwaukee, Wis.
Todd Mekelburg	Seventh-day Adventists Rocky Mountain Conference	Denver, Colo.

Name	Organization	City, State
Philip E. Melberg	NRA Foundation, The	Fairfax, Va.
Julius Melton	Davidson College	Davidson, N.C.
T. Edward Mercer	University of Texas Foundation, Inc.	Edinbrug, Texas
Gene Meyer	Martin Luther Home Foundation	Lincoln, Neb.
Martha Meyer	Lucile Packard Children's Hospital	Palo Alto, Calif.
Darryl Mikami	Fidelity Investments	Boston, Mass.
Bob Millar	Seventh-day Adventists N. California Conf. Assn.	Chico, Calif.
David F. Miller	Eastern Mennonite University	Harrisonburg, Va.
Florence Miller	National Academy of Sciences	Washington, D.C.
Richard Mills	SEND International	Farmington, Mich.
Frank Minton	Planned Giving Services	Seattle, Wash.
Billy J. Mize	Children's Home of Lubbock	Lubbock, Texas
Lynda S. Moerschbaecher	LMNOP Seminars & Publications	San Francisco, Calif.
Delmar R. Mohler	Moody Bible Institute	Chicago, Ill.
Charles Molloy	Care, Inc.	Atlanta, Ga.
Amelia Montjoy	World Wildlife Fund	Washington, D.C.
David Moore	Seventh-day Adventists Arizona Conference	Scottsdale, Ariz.
Ed Moore	Sunny Glen Children's Home	San Benito, Texas
W. David Moore	Arkansas Baptist Foundation	Little Rock, Ark.
William M. Moran	St. Vincent Foundation of Alabama	Birmingham, Ala.
Ivan W. Morford	Seventh-day Adventists Central Calif. Assn.	Clovis, Calif.
Barbara Y. Morgan	Punahou School	Honolulu, Hawaii
Heather Morgan	American Institute for Cancer Research	Washington, D.C.
Laurie A. Moritz	Mellon Private Capital Management Group	Pittsburgh, Pa.
Haskell Morrison	BancCorp Systems, Inc.	Amarillo, Texas
Patricia N. Moulton	San Diego State University	San Diego, Calif.
Michael Mudry	Hay/Huggins Company, Inc.	Philadelphia, Pa.
Bill Muehlman	Boys and Girls Town of Missouri	St. Louis, Mo.
Dick Mulder	RACOM/Back to God Hour	Holland, Mich.
Karen Muldoon	Deborah Hospital Foundation	Brown Mills, N.J.
James A. Mullin	Catholic Community Foundation	St. Paul, Minn.
Ronald Munger	Nature Conservancy, The	San Francisco, Calif.
Wallace Munro	Actors' Fund of America, The	New York, N.Y.
Michael Murphey	Women's Missionary Union Foundation	Birmingham, Ala.
Dennis J. Murphy	Seeing Eye, Inc., The	Morristown, N.J.
Charles R. Murray	Seeing Eye, The	Morristown, N.J.
Derek A. Mustow	Seventh-day Adventists General Conference	Greenbrier, Tenn.
Emily P. Myers	Mercer University	Macon, Ga.
Gifford G. Myers	Northwestern College	St. Paul, Minn.
James H. Myers	California State University Northridge	Northridge, Calif.
G. Ted Nace	Peale Center for Christian Living	Pawling, N.Y.
William H. Nace	United Methodist Church Tenn. Conf. Foundation	Nashville, Tenn.
Virginia M. Natera	United Methodist Church Gen'l Bd. of Global Ministries	New York, N.Y.
Timothy R. Neal	Nebraska Children's Home Society	Omaha, Neb.
William A. Neill	Ripon College	Ripon, Wis.
Gordon Nelson	Canadian Association on Charitable Gift Annuities	Stouffville, Ontario, CANADA
Jeffrey Nelson	South Dakota State Univeristy Foundation	Brookings, S.D.
David Newman	Mitchell, Silverberg & Knupp	Los Angeles, Calif.
John B. Nickels	Bethesda Lutheran Homes and Services, Inc.	Watertown, Wis.
David Nienas	School of Theology at Claremont	Claremont, Calif.
Margaret W. Nikelly	Swarthmore College	Swarthmore, Pa.
Ellen C. Nixon	Seventh-day Adventists General Conference	Silver Spring, Md.
Jodie Nolan	Father Flanagan's Boys Home	Boys Town, Neb.
Ron Nordeen	Cal Poly State University Foundation	San Luis Obispo, Calif.
Bruce Nortell	North Central College	Naperville, Ill.
Mavis Northam	Seventh-day Adventists General Conference	Oshawa, Ontario, CANADA
Art Nunn	California Baptist Foundation	Fresno, Calif.
Sharon K. O'Brien	Arthritis Foundation	Irvine, Calif.
William O'Connor	Missionary Oblates	Belleville, Ill.
Michie S. O'Day	Paralyzed Veterans of America	Washington, D.C.
Thomas J. O'Donnell	Loomis-Sayles & Company	Boston, Mass.
Ronald G. O'Neel	Free Methodist Foundation, The	Bellevue, Wash.
Gary Oliver	Loma Linda University	Loma Linda, Calif.

Name	Organization	City, State
Bob Olson	Willamette University	Salem, Ore.
David H. Olson	Lee Bernard Co.	Palm Springs, Calif.
John D. Ordway	United Church of Christ Pension Boards	New York, N.Y.
Anita F. Orquia	Seventh-day Adventists General Conference	Winter Park, Fla.
Carolyn Osteen	Ropes & Gray	Boston, Mass.
Scarlett Powers Osterling	Children's Bureau of Southern California	Los Angeles, Calif.
Ed Ostermeyer	Arthritis Foundation	Los Angeles, Calif.
Bill Overby	N.C. Baptist Foundation, Inc.	Cary, N.C.
Dale A. Overholt	Capin Crouse	Rancho Cucamonga, Calif.
Ronald Ovitt	World Relief	Carol Stream, Ill.
Bob Owen	World Vision, Inc.	Monrovia, Calif.
Pat Owen	World Vision, Inc.	Monrovia, Calif.
C. Jim Owens	Seventh-day Adventists N. California Conf. Assn.	Pleasant Hill, Calif.
Triena Owens	ALSAC/St. Jude Hospital	Memphis, Tenn.
Glen Paden	California Baptist Foundation	Fresno, Calif.
Douglas Page	University of Puget Sound	Tacoma, Wash.
Philip Palmer	Seventh-day Adventists South Central Conference	Nashville, Tenn.
Debra Palmer-Seiler	Children's Hospital	Seattle, Wash.
C. Jeffry Paoletti	University of Utah Development Office	Salt Lake City, Utah
Melia Parchman	Girl Scouts of the U.S.A.	New York, N.Y.
David L. Parkhurst	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Barbara J. Parrott	Seventh-day Adventists Rocky Mountain Conference	Denver, Colo.
Robert T. Parry	Federal Reserve Bank of San Francisco	San Francisco, Calif.
Suzanne Pate	Wright State University Foundation	Dayton, Ohio
Calvin A. Patterson	WELS Foundation, Inc.	Milwaukee, Wis.
Robert Patterson	Seventh-day Adventists SE Conf.	Altamonte Springs, Fla.
Robert Patterson	Seventh-day Adventists North American Division	Columbia, Md.
Ronald W. Paulson	Trinity Western University Foundation, US	Lynden, Wash.
Robert S. Peach	Ashrae Foundation	Atlanta, Ga.
George Pearson	Seventh-day Adventists South Central Conference	Nashville, Tenn.
Frederick Peck	Good Samaritan Foundation	Portland, Ore.
Noelia Pena	Oblate Missions	San Antonio, Texas
Doloras Perrone	Shriners Hospital for Crippled Children	Tampa, Fla.
Ernest Peters	Abbott House	Mitchell, S.D.
Erik H. Petersen	Moral Re-Armament, Inc.	Fort Myers Beach, Fla.
John Peterson	Kevin Coleman Center	Kent, Ohio
Nancy Peterson	Sisters of Providence Health System	Seattle, Wash.
Robert Petmecky	In Touch Ministries, Inc.	Atlanta, Ga.
Karl Petzke	Lutherhaven	Coeur d'Alene, Idaho
E. Randall Phillips	Upper Columbia Corporation	Spokane, Wash.
John A. Phillips	Mercy Hospital Foundation	San Diego, Calif.
Kerry W. Phillips	Rochester Institute of Technology	Rochester, N.Y.
Nancy J. Pickell	Christian Church Foundation, Inc.	Indianapolis, Ind.
Howard Pierucki	Biblical Ministries Worldwide	Pittsboro, N.C.
Mark D. Pitman	Brethren Foundation, Inc.	Elgin, Ill.
Ed Plumier	Christian Homes	Lincoln, Ill.
Joan Pohas	Bentley College	Waltham, Mass.
Jack H. Pohl	Saint Paul Foundation, The	St. Paul, Minn.
Burt Pooley	Southern College of Seventh-day Adventists	Collegedale, Tenn.
Tari Popp	Andrews University	Berrien Springs, Mich.
Diane Portnoff	American Committtee for the Weizmann Inst. of Science	San Francisco, Calif
Fay Potter, V.P.	First Fidelity Bank, N.A.	Philadelphia, Pa.
James B. Potter	Planned Giving Resources	Falls Church, Va.
Norman Pottle	Seventh-day Adventists General Conference	Berrien Springs, Mich.
Anthony J. Powell	Westbury United Methodist Community	Meadville, Pa.
Floyd H. Powell	Seventh-day Adventists Florida Conf.	Winter Park, Fla.
Lin Powell	Seventh-day Adventists Kentucky/Tennessee Conference	Goodlettsville, Tenn.
John Power	Angen, Power & Twersky	Los Angeles, Calif.
Wayne R. Price	Lutheran Church-Missouri Synod Found.	St. Louis, Mo.
Daniel Pritchard	Mercy Home for Boys and Girls	Chicago, Ill.
Jack Quackenbush	Cal Farley's Boys Ranch	Amarillo, Texas
Rev. Raymond Quetchenbach	Society of the Divine Word	Techny, Ill.
Patrick Quinn	St. Jude League/Claretians, Inc.	Chicago, Ill.

Name	Organization	City, State
Katelyn Quynn	Massachusetts General Hospital	Boston, Mass.
Gary D. Ragnow	Oregon State University	Corvallis, Ore.
Richard E. Ralston	Ayn Rand Institute, The	Marina del Rey, Calif.
Susan M. Randall	Turning Point	Sioux Falls, S.D.
Mary Ann Ranta	Children's Hospital Foundation	Seattle, Wash.
Patricia A. Rawa	Catholic Church Extension Society of the U.S.A.	Chicago, Ill.
David Ray	Fidelity Investments	Boston, Mass.
Marla R. Ray	Pennsylvania State University	University Park, Pa.
John H. Reed	Salvation Army, The	Jackson, Miss.
Kenneth R. Reed	United Methodist Foundation of La.	Baton Rouge, La.
Steve Reed	Arkansas Children's Hospital Foundation	Little Rock, Ark.
Dean Rees	Holt International Children's Services Inc.	Eugene, Ore.
Douglas D. Reeves	Seventh-day Adventists General Conference	Vancouver, Wash.
Dale Regier	Mennonite Brethren Foundation	Hillsboro, Kan.
Kathleen M. Rehl	Capital University	Gahanna, Ohio
Rev. Thomas E. Rehl	Capital University	Columbus, Ohio
Marian Reiber	Adventist Media Center	Moorpark, Calif.
David Reid	Azusa Pacific University	Azusa, Calif.
Wayne C. Reinauer	International Bible Society	Colorado Springs, Colo.
Harold L. Reiner	Seventh-day Adventists Pacific Union Conference	Fountain Hills, Ariz.
Edith A. Reinhardt	Hemmenway & Reinhardt, Inc.	Swarthmore, Pa.
Robert L. Remington	Divinity School, Rochester, The	Rochester, N.Y.
Eugene Remmers	Seventh-day Adventists Georgia Cumberland Assoc.	Calhoun, Ga.
Susan Ressmeyer	Sharp HealthCare Foundation	San Diego, Calif.
Gary Reynolds	National Benevolent Association, The	Columbia, Mo.
Randee R. Reynolds	Seventh-day Adventists Carolina Conference	Charlotte, N.C.
Benjamin J. Rhodes	Illinois Wesleyan University	Bloomington, Ill.
James A. Rhodes	Pennsylvania State University	University Park, Pa.
Janet Ribble	Salvation Army, The	Des Plaines, Ill.
R. Jay Ribble	Arthritis Foundation	San Antonio, Texas
Louis W. Rice	University of Illinois Foundation	Urbana, Ill.
Lynette Davis Rice	United Methodist Church Gen'l Bd. of Global Ministries	Libertyville, Ill.
Harold D. Richardson	Southern Baptist Convention Annuity Bd.	Dallas, Texas
Steven D. Rick	Free Methodist Foundation, The	Spring Arbor, Mich.
Leroy F. Rieley	Seventh-day Adventists N. Pac. Union Conf.	Portland, Ore.
Jana L. Rittgers	Salvation Army, The	Boston, Mass.
Andrew W. Rivers	Society of the Little Flower	Darien, Ill.
Roy D. Roberts	Seventh-day Adventists Lake Union Conf.	Berrien Springs, Mich.
Donna Roberts	Seventh-day Adventists S. Union Conf.	Winter Park, Fla.
Tal Roberts	Baptist Foundation of Texas	Dallas, Texas
Sara Robertson	Pioneer Clubs	Wheaton, Ill.
Barbara K. Robinson	Mellon Private Capital Management Group	Pittsburgh, Pa.
Beverly S. Robinson	Oakwood College	Huntsville, Ala.
Randy Robinson	Seventh-day Adventists Illinois Assn.	Brookfield, Ill.
William B. Robinson	Reformed Theological Seminary	Jackson, Miss.
James A. Roehm	Northern Illinois Medical Center Foundation	McHenry, Ill.
Jennifer E. Rogers	National Wildlife Federation	Washington, D.C.
Glenn R. Rohrbach	Baptist Mid-Missions	Cleveland, Ohio
Linda A. Roiger	St. Olaf College	Northfield, Minn.
David R. Rood	MAF Foundation	Redlands, Calif.
Don Roth	Seventh-day Adventists Central Calif. Assn.	Clovis, Calif.
Ray Rotolo	Claremont McKenna College	Claremont, Calif.
Philard L. Rounds	First United Methodist Church	Tulsa, Okla.
Harold Roys	Young Life	Colorado Springs, Colo.
Luis Runde	Franciscan Charities	St. Louis, Mo.
Thomas B. Russell	Association of Graduates	West Point, N.Y.
Andrew Russo	Planned Giving Systems, Inc.	Cleveland, Ohio
Nancy Ryan	Sharp HealthCare Foundation	San Diego, Calif.
Constantino Salios	North American Baptist Conference	Oakbrook Terrace, Ill.
Howard F. Salmon, Jr.	University of Hawai'i Foundation	Honolulu, Hawai'i
Ron Salzman	North American Baptist Conference	Wheaton, Ill.
Ronald E. Sapp	Johns Hopkins Institutions, The	Baltimore, Md.
Ed Savage	Sacred Heart League	Walls, Miss.

Name	Organization	City, State
William E. Sawin, Jr.	Archdiocese of Los Angeles	Los Angeles, Calif.
Richard G. Sayther, CFRE	Gronlund Sayther Brunkow	Burnsville, Minn.
Suzanne Schaffner	Blackbaud, Inc.	Charleston, S.C.
Dale Schenewerk	Northeast Missouri State University	Kirksville, Mo.
Edward Scheresky	Seventh-day Adventists Idaho Conference	Boise, Idaho
Robert Schlesinger	PG Calc Incorporated	Cambridge, Mass.
Paul H. Schmitt	St. Olaf College	Northfield, Minn.
David W. Schneider	Twin Towers	Cincinnati, Ohio
G. Roger Schoenhals	Planned Giving Today	Seattle, Wash.
Edward T. Scholl	Passionist Monastery	Chicago, Ill.
Douglas H. Schroeder Scott	Walker Methodist Foundation	Minneapolis, Minn.
Grace H. Schroeder Scott	St. Olaf College	Northfield, Minn.
Clinton A. Schroeder	Gray, Plant, Mooty, Mooty & Bennett	Minneapolis, Minn.
Kim Schroeder	Seventh-day Adventists Oregon Conference	Sandy, Ore.
A. Charles Schultz	Crescendo Software	Camarillo, Calif.
Mark Schultz	Loma Linda University	Oak Glen, Calif.
Ryan Scott	Willamette University	Salem, Ore.
Wayne A. Searson	Upper Columbia Corporation	Spokane, Wash.
Catherine J. Sentz	SUNY Binghamton University Foundation	Binghamton, N.Y.
John G. Serbein	University of Redlands	Redlands, Calif.
Robert Shafis	Alzheimer's Association	Chicago, Ill.
Jack Shakely	California Community Foundation	Los Angeles, Calif.
Martin F. Shanahan, Jr.	Anti-Cruelty Society, The	Chicago, Ill.
Robert F. Sharpe, Jr.	Robert F. Sharpe and Co., Inc.	Memphis, Tenn.
H. John Shaw, III	Mercy Foundation	Rancho Cordova, Calif.
Milt Shaw	Prudential Real Estate Gifts	Houston, Texas
George L. Shearin		Dallas, Texas
Sidney J. Shearin	Shearin Consulting Services	Irvine, Calif.
Dennis E. Sheridan	Starr Commonwealth	Albion, Mich.
Wes Sherrick	Salvation Army, The	Oklahoma City, Okla.
Alan G. Sherwood	Good Samaritan Hospital Foundation	Kearney, Neb
Linda Shestock	California Community Foundation	Los Angeles, Calif.
Judy Shideler	Presbyterian Church (U.S.A.) Foundation	Portland, Ore.
Janice A. Shoen	Diocese of Ogdensburg	Ogdensburg, N.Y.
Phillip W. Shopbell	First Interstate Bank	Sacramento, Calif.
Craig Shopneck	KeyCorp	Cleveland, Ohio
Ellen O'Connor Shugart	Arthritis Foundation	Wethersfield, Conn.
Rev. Kenan Siegel	St. Lawrence Seminary	Mt. Calvary, Wis.
Kenneth Siegele	California Lutheran University	Thousand Oaks, Calif.
Liz Saladi	Radcliffe College	Cambridge, Mass.
Tom Simandl	Salvation Army, The	Des Plaines, Ill.
Ronald E. Simers	Billy Graham Evangelistic Assn.	Minneapolis, Minn.
Glenn O. Simmons	Utah Valley State College	Orem, Utah
Kay Simmons	Salvation Army, The	Dallas, Texas
Stephen E. Simmons	Boy Scouts of America, Northeast Region	Nassau, Del.
Terry Simmons	Thompson & Knight, PC	Dallas, Texas
Larry Simonson	Christian Homes	Lincoln, Ill.
Chuck Simpson	Seventh-day Adventists Illinois Assn.	Brookfield, Ill.
Bobby E. Sims	Ga. Baptist Children's Homes & Fam. Min.	Atlanta, Ga.
Clevridge R. Sinclair	Loma Linda University	Loma Linda, Calif.
Michael Skaggs	Northern Rockies Cancer Center	Billings, Mont.
Joseph W. Skehen	Oregon State University	Corvallis, Ore.
Mary Ann Sloan	N.C. Baptist Foundation, Inc.	Cary, N.C.
David M. Slover	Southern Methodist University	Dallas, Texas
Charles L. Smith, Jr.	Texas Methodist Foundation	Austin, Texas
Chris Smith	Starr Commonwealth	Albion, Mich.
Pamela A. Smith	Seventh-day Adventists General Conference	Berrien Springs, Mich.
Paul G. Smith, Jr.	Southern College of Seventh-day Adventists	Collegedale, Tenn.
Ronald M. Smith	Seventh-day Adventists Oregon Conference	Clackamas, Ore.
Scott D. Smith	Colby College	Waterville, Maine
Scott T. Smith	Hillsdale College	Hillsdale, Mich.
Sister Suzanne Smith	Sisters of Providence	St. Mary-of-the-Woods, Ind.
Thomas W. Smith	California Institute of Technology	Pasadena, Calif.

Name	Organization	City, State
Tom A. Smith	Church of God Board of Church Extension	Anderson, Ind.
Tom A. Smith	Thoms Rehabilitation Hospital	Asheville, N.C.
James C. Soft	Yellowstone Boys and Girls Ranch Foundation	Billings, Mont.
Ron Soloc	Salvation Army, The	Des Plaines, Ill.
William G. Solomon, IV	Mercer University	Macon, Ga.
Christine K. Solso	Carleton College	Northfield, Minn.
Edward Sommers	Middlebury College	Middlebury, Vt.
Vickie Soper	Seventh-day Adventists Florida Conf.	Winter Park, Fla.
John R. South	Salvation Army, The	Union, N.J.
Les Speer	Seventh-day Adventists Georgia Cumberland Assoc.	Calhoun, Ga.
Sterling K. Speirn	Peninsula Community Foundation	San Mateo, Calif.
Kathryn Sperlak	R&R Newkirk	Willow Springs, Ill.
Greg Sperry	Christian Ministries Foundation	St. Simons Isl., Ga.
Virginia G. Spradlin	Christian Church Foundation, Inc.	Indianapolis, Ind.
Pat Sprague	Actors' Fund of America, The	Los Angeles, Calif.
Ann Squires	United Methodist Foundation, California-Nevada	Santa Rosa, Calif.
Bill Squires	Lindsey Wilson College	Columbia, Ky.
Gary Stambaugh	Bible Literature International, Inc.	Columbus, Ohio
Thomas G. Staples	Seventh-day Adventists Southeastern Calif. Assn.	Riverside, Calif.
Kristina Starkey	American Lung Association	San Diego, Calif.
Barry Stater-West	Holt International Children's Services Inc.	Eugene, Ore.
Alfred N. Steele	Christian & Missionary Alliance, The	Colorado Springs, Colo.
Pamela Steele	Seventh-day Adventists W. Wash. Conf.	Bothell, Wash.
Jay Steenhuysen	World Vision, Inc.	Monrovia, Calif.
Larry P. Stelter	Stelter Company, The	Des Moines, Iowa
Steve Stelter	Stelter Company, The	Des Moines, Iowa
James R. Stephan	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Guy Stewart	Adventist Media Center	Newbury Park, Calif.
Peggy Still	Fuller Theological Seminary, The Fuller Foundation	Pasadena, Calif.
Elvin R. Stoltzfus	Philhaven Hospital	Mt. Gretna, Pa.
Rev. Donald G. Stoner	United Church of Christ	Cleveland, Ohio
Lowell V. Stortz	Leonard, Street and Deinard	Minneapolis, Minn.
Dale V. Story	Fifth Third Bank	Cincinnati, Ohio
Paul Strawhecker	Archdiocese of Omaha	Omaha, Neb.
Linda Stringer	Southern Poverty Law Center	Montgomery, Ala.
Robert O. Stuewig	American Baptist Homes of the West	Oakland, Calif.
Sister Danielle Sullivan	Sisters of Providence	St. Mary-of-the-Woods, Ind.
Gregory J. Sullwold	Salvation Army, The	West Nyack, N.Y.
Ada Swanson	Adventist Media Center	Newbury Park, Calif.
Byron L. Swanson	Back to the Bible	Lincoln, Neb.
William R. Swecker	Bridgewater College	Bridgewater, Va.
Kevin Sweeney	Holt International Children's Services INc.	Eugene, Ore.
Herb Swenson	Adventist Media Center	Newbury Park, Calif.
Roger E. Swenson	Anne Carlsen Center for Children	Jamestown, N.D.
Richard V. Swindle	Mercer University	Macon, Ga.
LaVand Syverson	MAF Foundation	Redlands, Calif.
Bill Tanner	John Muir Medical Center Foundation	Walnut Creek, Calif.
W. Earl Taylor	Omaha Community Foundation	Omaha, Neb.
Conrad Teitell	Prerau & Teitell	White Plains, N.Y.
Norman J. Tellier	Reformed Church in America	Schenectady, N.Y.
David A. Teune	Wheaton College (Illinois)	Wheaton, Ill.
Ronald J. Theberge	Oregon State University	Corvallis, Ore.
Calvin N. Thomas	Presbyterian (U.S.A.) Foundation	Petaluma, Calif.
Charles W. Thomas, Jr.	American Printing House for the Blind, The	Louisville, Ky.
Donal D. Thomas	Planned Giving Foundation	San Jose, Calif.
Peter D. Thomas	Oregon Shakespeare Festival	Ashland, Ore.
Philip G. Thomas	Back to the Bible	Lincoln, Neb.
Katherine B. Thurber	Providence Community Health Foundation	Medford, Ore.
Jonathan G. Tidd		West Simsbury, Conn.
John M. Tincher	Children's Hospital Foundation	Orange, Calif.
To Be Named	Salvation Army, The	Des Plaines, Ill.
Ronald Tollerud	Salvation Army, The	Washington, D.C.
Grace M. Tompos	College of Wooster	Wooster, Ohio

Name	Organization	City, State
J. D. Toms	Upper Columbia Corporation	Spokane, Wash.
J. Michael Touhey	Washington University in St. Louis	St. Louis, Mo.
Larry Townsend	Seventh-day Adventists N. California Conf. Assn.	Oakley, Calif.
Mike Tracey	College of Osteopathic Medicine of the Pacific	Pomona, Calif.
I-Ju Tracy	University of California, San Diego	LaJolla, Calif.
Greg Traucht	United Methodist Church West Ohio Conference	Columbus, Ohio
David Treadwell	Salvation Army, The, Md/W.Va. Div.	Baltimore, Md.
Robin Weeks Trozpek	Pomona College, Annuity & Trust	Claremont, Calif.
Jackie L. Tucker	Seventh-day Adventists, The Quiet Hour	Redlands, Calif.
Alden B. Tueller	Utah Valley State College	Orem, Utah
Robert Turner	Seattle Univ. - Planned Giving Office	Seattle, Wash.
Sharyl R. Turon	Seventh-day Adventists Illinois Assn.	Brookfield, Ill.
Ken Turpen	Seventh-day Adventists General Conference	Silver Spring, Md.
Robert M. Tuttle	Allegheny College	Meadville, Pa.
Ray Tyler	Cornerstone Management Inc.	Norcross, Ga.
Keith D. Ulery	Messiah Village	Mechanicsburg, Pa.
George Ulloa	Seventh-day Adventists Oregon Conference	Battle Ground, Wash.
Jeff Underwood	First Church of Christ, Scientist	Boston, Mass.
Theodore H. Uren	Seventh-day Adventists Hawaii Conference	Honolulu, Hawaii
Laurie W. Valentine	Kentucky Baptist Foundation	Louisville, Ky.
Jan Van Der Kley	Western Mich. University Foundation	Kalamazoo, Mich.
Dave Vander Ploeg	Barnabas Foundation	Orland Park, Ill.
Rev. Douglas Verdin	United Methodist Church NY/CT Foundation	White Plains, N.Y.
Leslie E. Vidra	Indiana University Foundation	Bloomington, Ind.
Anthony M. Vienna, Esq.	Argue Pearson Harbison & Myers	Los Angeles, Calif.
Richard Vorpe	University of California, Davis	Davis, Calif.
Jean Vukas	Saint Paul Foundation, The	St. Paul, Minn.
Terry R. Wade	Southern Baptist Convention Annuity Bd.	Dallas, Texas
Richard Wagenleitner	Seventh-day Adventists, The Quiet Hour	Redlands, Calif.
A. Graham Walker	American Bible Society	New York, N.Y.
Charles A. Walker	Muskingum College	New Concord, Ohio
John M. Wall	Salvation Army, The	Tampa, Fla.
Joel Wallace	Seventh-day Adventists SW Union Conf.	Burleson, Texas
Kathryn L. Ward	American Institute for Cancer Research	Washington, D.C.
Kim Warner	Texas Presbyterian Foundation, The	Dallas, Texas
Melinda Warren	Baptist Foundation of Oklahoma	Oklahoma City, Okla.
Patti Warren	Resource Development, Inc.	Springfield, Mo.
Susan Warsaw	Shawnee State University	Portsmouth, Ohio
Essil Washington	Arthritis Foundation	Atlanta, Ga.
Cecil W. Watson	Church of God Board of Church Extension	Anderson, Ind.
Ron Watson	Loma Linda University	Loma Linda, Calif.
Gary Wayman	Mercy Foundation, Inc.	Roseburg, Ore.
Douglas A. Weaver	Pentera, Inc.	Indianapolis, Ind.
Samuel G. Weaver	Eastern Mennonite University	Harrisonburg, Va.
Edward F. Weber, Esq.	Weber & Sterling	Maumee, Ohio
Greg Weber	Salvation Army, The	Dallas, Texas
Robert Weber	Scripps Health	LaJolla, Calif.
Albert C. Weidenbusch	Course Corrections, Inc.	Niceville, Fla.
Ross G. Weidman	Brethren Village	Lancaster, Pa.
Teresa Weintraub	University of Miami	Coral Gables, Fla.
Michael S. Welling	Arthritis Foundation	Antelope, Calif.
Malcolm Wernik	Presbyterian Homes of N.J. Foundation, The	Princeton, N.J.
Thomas E. Wetmore	Seventh-day Adventists General Conference	Silver Spring, Md.
Alan W. White	Seventh-day Adventists General Conference	Beltsville, Md.
Douglas White	Kaspick & Company	Boston, Mass.
Henry Whitney	David and Margaret Home, Inc.	La Verne, Calif.
William E. Whitsitt	Salvation Army, The	Tampa, Fla.
Dr. A. Julian Wigen	United Methodist Foundation Dakotas Conf.	Mitchell, S.D.
Don Wildman	Florida Hospital Foundation	Orlando, Fla.
S.S. Will	Seventh-day Adventists Carolina Conference	Hendersonville, N.C.
James S. Williams	College of Osteopathic Medicine of the Pacific	Pomona, Calif.
Paul Williams	Moody Bible Institute	Tempe, Ariz.
Lois K. Williamson	Bradley University	Peoria, Ill.

Name	Organization	City, State
Ed H. Williford	French Camp Academy	French Camp, Miss.
David Wills	Christian Ministries Foundation	St. Simons Is., Ga.
Eugene L. Wilson	American Leprosy Missions, Inc.	Greenville, S.C.
Jeffrey K. Wilson	Andrews University	Berrien Springs, Mich.
Stephan Wilson	Seventh-day Adventists Florida Conf.	Winter Park, Fla.
Jane L. Wilton	New York Community Trust, The	New York, N.Y.
Arvin W. Winkle	Seventh-day Adventists N. California Conf. Assn.	Ukiah, Calif.
Eunice E. Winston	Seventh-day Adventists Southern Calif. Assn.	Glendale, Calif.
Tom Witte	Inter-Varsity Christian Fellowship	Madison, Wis.
Gary Witz	Seventh-day Adventists N. California Conf. Assn.	Pleasant Hill, Calif.
Michelle S. Wolff	Prudential Resources Management	Valhalla, N.Y.
Larry Woodard	Arkansas Children's Hospital Fnd.	Little Rock, Ark.
George Woodruff	Seventh-day Adventists Kentucky/Tennessee Conference	Goodlettsville, Tenn.
Judi A. Wright	Seventh-day Adventists Central Calif. Assn.	Clovis, Calif.
Kenneth A. Wright, Jr.	Seventh-day Adventists Wisconsin Conference	Madison, Wis.
Roger E. Wyman	Florida International University	Miami, Fla.
Ronald E. Wyrick	Juniata College	Huntington, Pa.
Catherine Ann Yekenevicz, CPA	Cedar Campuses Foundation, Inc.	West Bend, Wis.
Charles Young	Seventh-day Adventists Georgia Cumberland Assoc.	Calhoun, Ga.
Kelly Young	Pepperdine University	Malibu, Calif.
W. Richard Young	Project Hope	Millwood, Va.
Paul J. Youngdale, Jr.	University of Texas Foundation, Inc.	Austin, Texas
Jeffrey M. Yussman	Stites & Harbison	Louisville, Ky.
Harold Zacharias	Seventh-day Adventists Carolina Conference	Charlotte, N.C.
Rebecca S. Zimmer	National Benevolent Association, The	St. Louis, Mo.
Al Zimmerman	Oregon Health Sciences Foundation	Portland, Ore.
Dick Zinser	University of Texas Foundation, Inc.	Galveston, Texas
Dale Zschoche	Michigan Tech Fund	Houghton, Mich.