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Structuring Life-Income Gifts Using Retirement Plan Assets

Partnership for Philanthropic Planning
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EXTENSION OF IRA CHARITABLE ROLLOVER THRU 2011

SEC. 725. TAX-FREE DISTRIBUTIONS FROM INDIVIDUAL RETIREMENT PLANS FOR CHARITABLE PURPOSES.

(a) IN GENERAL.—Subparagraph (F) of section 408(d)(8) is amended by striking "December 31, 2009" and inserting "December 31, 2011".

(b) EFFECTIVE DATE; SPECIAL RULE.—

(1) EFFECTIVE DATE.—The amendment made by this section shall apply to distributions made in taxable years beginning after December 31, 2009.

(2) SPECIAL RULE.—For purposes of subsections (a)(6), (b)(3), and (d)(8) of section 408 of the Internal Revenue Code of 1986, at the election of the taxpayer (at such time and in such manner as prescribed by the Secretary of the Treasury) any qualified charitable distribution made after December 31, 2010, and before February 1, 2011, shall be deemed to have been made on December 31, 2010.

EXTENSION OF IRA CHARITABLE ROLLOVER THRU 2011

- Qualified charitable distributions *("QCD")* excluded from donor's taxable income
  - –IRA and Roth IRA accounts, only
  - –Up to $100,000 per year per taxpayer
  - –Account owner age 70½ or older on the date of contribution
  - –Distribution directly from IRA account to charity

EXTENSION OF IRA CHARITABLE ROLLOVER THRU 2011

- Qualified charitable distributions *("QCD")* excluded from donor's taxable income
  - –To public charity *(§170(b)(1)(A))*
    - not to donor-advised fund
    - not to private foundation *(non-operating)*
    - not to supporting organization
  - –Outright, fully charitable gift, only
    - no split-interest gift/no quid pro quo
    - donor must obtain written acknowledgement
- QCD counts toward donor's Required Minimum Distribution from IRA Account

WHICH DONORS BENEFIT THE MOST FROM PPA 2006?

- Donors who do not itemize
- Donors subject to AGI limitations
- Donors in states with no or limited charitable deduction
- Donors who want to make very large gifts and don't have other assets to give

TODAY'S DISCUSSION

- Importance of Retirement Plan Assets as a Source of Gifts
- Donor Considerations
  - Tax treatment of IRD assets
  - Plan-specific issues
  - Giving techniques

BACKGROUND: ASSETS FUNDING CHARITABLE GIFTS

Donor's Assets

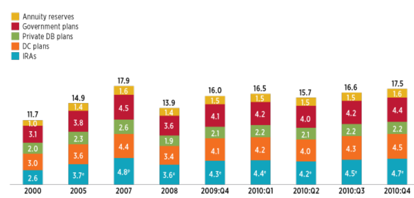
Pass by will or intestacy (probate)	Pass as titled (non-probate)	Pass by agreement or contract (non-probate)
•Assets held in sole name •Community property	•Joint tenancy with rights of survivorship •Transfer or payable on death	•Retirement Accounts •Revocable Trust •Life Insurance

IMPORTANCE OF RETIREMENT PLAN ASSETS AS A SOURCE OF CHARITABLE GIFTS

BACKGROUND: IMPORTANCE OF RETIREMENT ASSETS AS GIFT SOURCE

- Recent statistics demonstrate continued growth of U.S. retirement plan assets:
  - in dollars
  - as a percentage of household assets
- IRA assets continue to be a large portion of the retirement market

BACKGROUND: PLAN STATISTICS
$17.5 Trillion in U.S. Retirement Accounts Q4 '10



Retirement Assets = 37% of Household Assets in Q4 '10

ICI Research Fundamentals, Vol. 19, No. 3-Q2, October 2010

BACKGROUND: PLAN STATISTICS
Assets by Plan Type – Q4 2010

Plan Type	Trillions of Dollars
Annuities	1.6
Government Pension Plans	4.4
Private Defined Benefit	2.2
Defined Contribution	4.5
IRA	4.7
Total	**17.5**

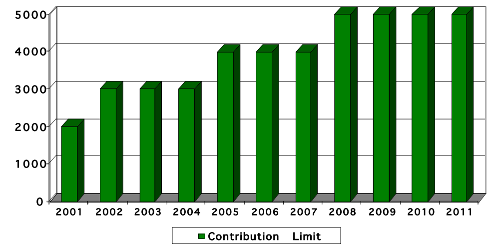
IRA assets = 27% of U.S. retirement assets as of Q4 2010

Investment Company Institute, October 2010

BACKGROUND: RECENT LEGAL DEVELOPMENTS

- EGTRRA increases in plan funding limits
- Required minimum distribution rules

EGTRRA INCREASES IN PLAN FUNDING LIMITS *Traditional IRAs*



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EGTRRA INCREASES IN PLAN FUNDING LIMITS *IRA Catch-up Provisions*

- Available to taxpayers aged 50 and older
- Accumulate greater amounts for retirement at an accelerated schedule
- Contribute catch-up amounts in addition to the regular IRA contribution limits
  - $500 (tax years 2002-2005)
  - $1,000 (tax years 2006 and thereafter)

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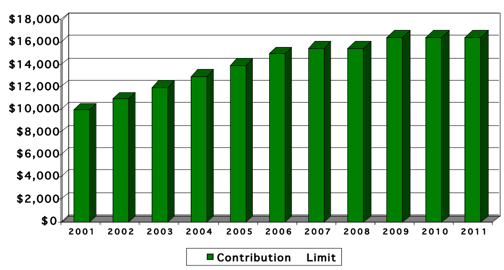
EGTRRA INCREASES IN PLAN FUNDING LIMITS *401(k), 403(b), and 457 Plan Limits*



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EGTRRA INCREASES IN PLAN FUNDING LIMITS *401(k), 403(b), and 457 Catch-Up Limits*

- 2002…………………$1,000
- 2003…………………$2,000
- 2004 ………………...$3,000
- 2005 ………………...$4,000
- 2006 & thereafter…$5,000 indexed ($5,500 for 2011)

Available to taxpayers aged 50 and older

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REQUIRED MINIMUM DISTRIBUTION RULES

IRS regulations under
Code §401(a)(9) for distributions from a retirement plan:

- Lifetime distributions calculated under one Uniform Table for nearly everyone
- “Designated beneficiary” determined as of September 30 of year following year of death (not RBD)
- Charitable gifts of retirement assets at death made easier

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BACKGROUND: IMPORTANCE OF RETIREMENT ASSETS AS GIFT SOURCE

Questions?

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DONOR CONSIDERATIONS FOR TESTAMENTARY CHARITABLE GIFTS OF IRD ASSETS

BACKGROUND – TESTAMENTARY vs. LIFETIME GIFTS

Dichotomy of Testamentary vs. Lifetime Gifts

Testamentary Gifts traditionally seen as:
- Easy
- Flexible
- Tax-effective (income and estate taxes)

Lifetime Gifts traditionally seen as:
- Inconvenient
- Irrevocable
- Tax-ineffective (ordinary income and excise taxes)

BACKGROUND – TESTAMENTARY vs. LIFETIME GIFTS

- Rule of Thumb:

  From a tax perspective, best charitable bequest gift is a retirement plan
  - Easy gift to make (beneficiary designation)
  - Flexible for donor (retain control during life)
  - Beneficial Tax Results

TAX ON RETIREMENT PLAN ASSETS

- Retirement assets (IRAs, qualified plan accounts, tax-deferred annuities) are "Income in Respect of a Decedent" (IRD)
  - IRD is taxable income to which the decedent was entitled at death but which was not included in any previous income tax return
  - (Other IRD: wages, accounts receivable, untaxed interest on bonds, etc.)

TAX ON RETIREMENT PLAN ASSETS

- Retirement assets and other IRD are:
  - Included in the decedent's taxable estate and
  - Subject to income tax in the hands of the recipient
- Double taxation can reduce assets to beneficiaries by nearly two-thirds (even greater if GST tax)

TAX ON RETIREMENT PLAN ASSETS

- Gift of retirement assets to charity can be a solution to double taxation
  - Estate tax charitable deduction is unlimited
  - Charity is income tax exempt
  - (Uncle Sam pays 66¢ of every dollar to charity)

PLAN–SPECIFIC ISSUES FOR DONORS

- Which plan should fund the gift?
  - ERISA vs. Non-ERISA
  - Plan document issues
  - Actions taken by account owner

PLAN-SPECIFIC ISSUES
Plan Type

- **ERISA**
  - –401(a) plans
  - –401(k) plans
  - –Some 403(b) plans
- **NON-ERISA**
  - –IRAs
  - –457 plans
  - –Some 403(b) plans

Waiver of spousal rights with ERISA plan

Creditor protection varies by plan & state law

PLAN-SPECIFIC ISSUES
Plan Document Restrictions?

- Does Plan permit a life-expectancy payout?
  - A “lump sum” payout may leave nothing for charity at owner’s death
- Does Plan require annuitized distribution?
  - A guarantee period may preserve something for charity

PLAN-SPECIFIC ISSUES
Participant Action?

- Election to annuitize (over life or lives) is irrevocable
  - May prevent designation of charity as beneficiary
- Participant may elect “guarantee period” for annuity payout
  - Death of annuitant(s) prior to expiration of guarantee may preserve something for charity (as contingent beneficiary)
  - Charity may take commuted value of remainder

DONOR CONSIDERATIONS

Questions?

TESTAMENTARY GIVING TECHNIQUES

OUTRIGHT GIFT TO CHARITY AT DEATH

Beneficiary Designation Form is mechanism for gift (non-probate)*

EXAMPLE #1:

Primary Beneficiary = 100% Charity

- Charity receives immediate benefit
- No estate tax on gifted assets
- Charity pays no income tax on gifted assets

* CAVEAT: Election to annuitize benefits can prevent testamentary gift

BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #2:

Primary Beneficiary = 50% Charity / 50% Individual

- Charity must be paid by 9/30 of year following decedent's death, then Individual can stretch distributions over life expectancy
- No estate tax on portion of assets passing to charity
- Charity pays no income tax on gifted assets

BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #3:

Primary Beneficiary = 100% Individual

Contingent Beneficiary = 100% Charity

- If individual survives account owner, charity receives nothing
- Charity takes if individual *predeceases* account owner (or disclaims)
  - No estate tax on portion of assets passing to charity
  - Charity pays no income tax on gifted assets

BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #4:

Primary Beneficiary = 100% Spouse

Contingent Beneficiary = 100% Charity

- No estate tax on assets passing to spouse (marital deduction)
- Spouse can roll over to his/her own IRA, defer distributions until RBD, name own beneficiary (could be charity)
- Charity takes now if spouse *predeceases* account owner or disclaims
  - No estate tax on portion of assets passing to charity
  - Charity pays no income tax on gifted assets

BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #5:

Primary Beneficiary = Estate (or Trust) 100% Estate plan leaves all or part to charity

- Problem: IRA is taxable income to estate tax or trust (compressed rates)
- Question: How to pass IRA to charity and avoid income taxation at estate or trust level?
- Answer: Fiduciary income tax charitable deduction if:
  (1) pay charitable bequest from "gross income," and
  (2) do so "pursuant to terms of governing instrument" - IRC §642(c)

BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #5 (continued):

Document states that retirement assets pass specifically to charity;

OR

Document leaves residue (or percentage of residue) to charity and states that:
"to the extent possible, gifts to charitable organizations shall be satisfied by distribution of property constituting income in respect of a decedent as defined under §691(a) of the IRC"

BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #5 (continued):

WARNING: Proposed Treasury regulations under §642(c) of the Code state that for such an income-ordering provision under an estate or trust to be effective for tax purposes, it must have "economic effect independent of income tax consequences."

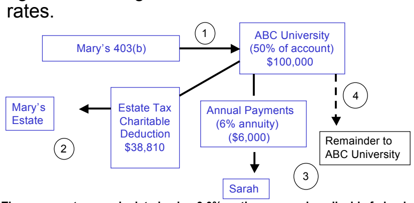
BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #6 :
Testamentary Gift Annuity

- CGA agreement between donor and charity:
  - CGA payments to annuitant for life if annuitant survives donor
  - CGA to be funded from donor's retirement account
- Primary Beneficiary = 100% charity
- Estate tax charitable deduction for remainder value of CGA
- Annuity payments are ordinary income (deferred until receipt)

EXAMPLE OF RETIREMENT ASSETS FUNDING CRT

- Mary Smith names ABC University as primary beneficiary of 50% of her 403(b) balance, to fund a charitable gift annuity to benefit Mary's best friend, Sarah (age 72). The CGA contract was signed years ago, referencing the account and ACGA recommended rates.



These amounts are calculated using 3.0% as the assumed applicable federal rate for purposes of calculating the value of the remainder interest

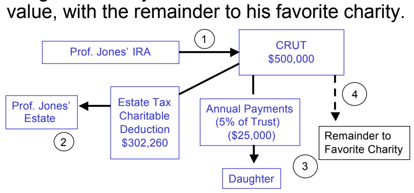
BENEFICIARY DESIGNATION FORM IS MECHANISM FOR GIFT

EXAMPLE #7 :
Primary Beneficiary = Charitable Remainder Trust

- Estate tax charitable deduction for remainder value of CRT
- CRT can provide for stream of annuity or unitrust payments to desired individual beneficiaries for life (subject to 10% minimum remainder interest rule)
- CRT payments are based on 100% of CRT value (no diminution for income tax)
- All income tax on assets are deferred until CRT payments are distributed

EXAMPLE OF RETIREMENT ASSETS FUNDING CRT

- Professor Jones names his CRUT as primary beneficiary of $500,000 of retirement assets at his death. The CRUT provides for payments to his daughter for 10 years of 5% of the CRUT's market value, with the remainder to his favorite charity.



These amounts are calculated using 3.0% as the assumed applicable federal rate for purposes of calculating the value of the remainder interest

RETIREMENT ASSETS TO A CRT

- Cautions:
  - Is planner competent in relevant areas of the law?
    (Estate tax, Income tax, ERISA, Retirement distributions, and CRTs)
  - No marital deduction if non-spouse income beneficiary
  - No discretionary access to trust property
    (Shouldn't be sole source of family support)
  - In large estate subject to estate tax, stretch IRA may produce better tax result
    (691(c) deduction)

TESTAMENTARY GIVING TECHNIQUES

Questions?

Gift Planning Case Studies

DISCUSSION QUESTIONS

- What are the primary issues you identify?
- What additional questions would you most like to ask?
- What gift options might you explore?
- What fundraising strategy issues or questions do you see?
- What institutional risk issues might arise?

CASE STUDY #1

DONOR WHOSE GIFT IS “ALREADY IN PLACE”

Retired university professor informs University’s planned giving office that she intends to fund a CRUT at her death using part of her 403(b) accumulation (currently $1 million).

The trust will benefit her children, then fund a scholarship in the professor’s name.

DONOR WHOSE GIFT IS “ALREADY IN PLACE” Additional Facts

On further inquiry, University’s PG officer learns that the professor’s attorney drafted the stand-alone trust instrument 10 years ago, which the donor then signed, naming University as trustee and remainder beneficiary. (The trust document has been kept in donor’s safe deposit box.)

Upon review, the document names the children (now ages 39 and 41) as joint and survivor beneficiaries of a 9% unitrust. The document recites funding with $10.00.

CASE STUDY #2

TESTAMENTARY GIFT ANNUITIES

In 2007, a board member informed Social Services Agency that she wanted to establish deferred gift annuities for her adult children, using IRA assets that would pass at her death.

TESTAMENTARY GIFT ANNUITIES
Additional Facts

Board member subsequently signed a codicil to her Will instructing her Executor to transfer the IRA accumulation to the Agency to fund the gift annuities.

Board member has recently passed away. Agency's planned giving office has discovered a copy of the Will and codicil in its files.

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