

INTRODUCTION

A common misconception about charitable giving is that it is only for retired or wealthy donors. But charitable giving is a powerful tool for individuals of all ages and income levels who want to make a philanthropic impact that is aligned with their current financial circumstances. Different gift models can provide benefits to prospective donors at any age, financial situation or life stage. These gifts can take many forms including outright gifts, bequests, charitable remainder trusts (CRTs), charitable gift annuities (CGAs), life insurance policies and more.

It is useful to examine different donor groups by age, income and financial asset values. Doing so will help nonprofits and advisors target the best giving options for charitable individuals of all ages. In this two-part series, we will explore the different strategies for charitable giving across different age groups. The first installment will review charitable gifts for younger generations (20s to 40s) and middle-aged individuals (40s to 60s). The second installment will discuss giving strategies for early retirees (60s to 70s) and seniors (70s and older). By understanding how charitable giving needs and goals evolve over a lifetime, nonprofits and their advisors can create a more personalized approach to philanthropy.

STRATEGIES FOR YOUNGER DONORS (20s to 40s)

Before diving into the specific needs and strategies for charitable giving among different age groups, it is important to understand what charitable giving is and why it is a significant consideration for potential donors. Whether it is a major gift or a planned gift, all charitable giving provides financial benefits to donors and fulfills philanthropic goals. Some giving options can provide immediate financial benefits to the donor, such as income tax deductions or increased income during retirement, while others offer long-term advantages. The benefits to the nonprofit can also vary depending on whether it is a current gift or a planned gift.

Younger donors can begin their charitable giving with smaller, manageable gifts. They are ideal candidates for making current gifts of cash, stock, insurance and unique assets such as cryptocurrency. These gifts allow younger donors to make an immediate impact without requiring a large financial outlay while receiving income tax deductions to offset current income. Another area of importance that is often overlooked with younger donors is encouraging them to create wills or trusts that include charitable bequests.

Outright Gifts

An outright gift is a transfer of the donor's entire interest in the property to a nonprofit. An outright gift provides benefits for the donor, including a fair market value charitable deduction for most assets and the removal of the property from the donor's estate for estate tax purposes. Assuming the property is a long-term capital asset, the donor also avoids capital gains tax on the portion of the property contributed to the nonprofit.

The most straightforward and common method of making an outright gift is through a cash donation. Many individuals in their 30s, whether they are salaried employees or entrepreneurs, allocate a percentage of their income to charitable giving. Cash donations offer immediate support to the nonprofit and are easy to manage.

In-kind donations, which are contributions of goods or services, are another valuable way for these donors to give. For those in their 30s who may not have a significant amount of disposable income, in-kind donations can be a valuable way to support a cause. Donating items like clothes, food, electronics or professional services (such as marketing expertise or web development) can make a substantial impact for nonprofit organizations. While a donation of services does not qualify for a charitable deduction, many younger donors still choose to donate their time as a way of directly helping a nonprofit and participating in the nonprofit's mission.

As individuals in their 30s begin to build their investment portfolios, gifting appreciated stocks or other investments can be a particularly advantageous way to give. Donating appreciated assets, such as stocks, bonds or mutual funds, can provide both the donor and the nonprofit with significant tax benefits. Some younger donors may own real estate or unique assets such as cryptocurrency that can be a good fit for an outright gift. If long-term capital gain property (property held for investment for more than one year) was sold, the entire gain would be subject to capital gains tax. By donating the property outright, the donor avoids capital gains tax at the maximum rate of 23.8% (20% plus the 3.8% surcharge for net investment income for high-income earners), which they would otherwise owe if they sold the asset instead. Additionally, the full market value of the asset is generally deductible from the donor's taxable income.

Donor Advised Funds

An increasingly popular option for outright gifts is contributing to a donor advised fund (DAF). According to recent surveys, younger donors are more likely than older donors to establish their generosity through a structured method like a DAF. A DAF allows individuals to make a tax-deductible donation into an account that can grow over time, and the funds can be directed to a nonprofit at a later date. While DAFs might seem like a tool for wealthier donors, DAFs can be used by individuals at any income level. DAFs are especially beneficial for those who are committed to supporting long-term causes but want flexibility in how and when they make those gifts. Many DAFs now also offer app-based interfaces and lower minimum deposits which appeal to the digital lifestyle of younger donors.

A DAF is an account that a donor establishes at a Sec. 501(c)(3) public charity, often a community foundation. When a donor makes a contribution to the DAF, the donor must give complete control of the donated funds to the public charity. The nonprofit's receipt must also state that no goods or services were provided in exchange for the gift and that the nonprofit has exclusive control of the gift assets. As a result, the donor gets an immediate income tax deduction for the full amount of the contribution to the DAF. Even though the donor relinquishes control over the donated funds, the unique aspect of a DAF is that the donor can remain involved by making non-binding recommendations to the sponsoring organization of the DAF as to investment policy and distributions. Although the DAF sponsor has final approval on distributions from the DAF, the donor can fulfill his or her philanthropic goals in a flexible, tax-favored and cost-effective way.

IRC Sec. 4966 creates a comprehensive set of rules for DAFs outlining key elements such as the definition of a DAF, rules for distributions and definitions of disqualified persons and deductible

donations. DAFs are generally not subject to minimum distribution requirements. To qualify as a DAF, the DAF must be: (i) separately identified by the donor, (ii) owned and controlled by the sponsoring nonprofit and (iii) the donor must have a reasonable expectation of advisory rights. IRC Sec. 4966(d)(2)(A). A DAF is also subject to various requirements and several prohibitions. DAFs are maintained by Sec. 501(c)(3) public charities, and gifts to DAFs are typically deductible to 60% of adjusted gross income (AGI) for cash and 30% of AGI for appreciated property for contributions to public charities. The gifts must also comply with substantiation requirements. IRC Sec. 170(f)(18)(B).

Bequests

It is important to start informing younger donors about the ease and benefits of making a bequest to a nonprofit in their will or trust. A bequest is a gift that can be made to support a nonprofit's mission through a will or living trust. Incorporating a bequest to a charitable organization in a will or trust is an excellent method to participate in philanthropy while deferring the transfer of assets. A bequest allows the donor to have continued lifetime use of the property that he or she will leave to the nonprofit. Upon death, the designated bequest passes to the nonprofit. A bequest allows the donor to keep control of assets during his or her lifetime but still make a lasting impact on the nonprofit's work after they are gone.

Bequests are flexible and can be tailored to specific needs. Bequests can be for a fixed amount, a percentage of the estate or the remainder estate after other distributions. Bequests can also involve making a gift of a specific asset such as real estate, a car or other property.

There are multiple ways to structure a charitable bequest in a will or trust. The first option is to designate a fixed dollar amount for the nonprofit. The benefit of this approach is that the donor knows exactly what the nonprofit will be receiving. However, the downside is that if an estate decreases in value, the other beneficiaries will receive less since the bequest to the nonprofit is unchanged by the value of the estate.

The second option is to provide for a percentage of the estate to go to a nonprofit. Because the amount going to the nonprofit is not fixed, this option ensures the other beneficiaries receive the proportion of the estate that the donor desires, and that proportion remains consistent regardless of any change in value of the estate.

It is also important to remind younger donors of the benefits of naming a nonprofit as a contingent beneficiary. A contingent beneficiary is the designated recipient of a bequest only if the person named as the primary beneficiary has died, cannot be located or refuses the bequest when the estate is settled. If a younger donor does not have a contingency plan, due to a limited number of heirs or other family members, their estate could be given to distant relatives after a lengthy probate proceeding. Naming the nonprofit as a contingent beneficiary is an effective backup plan that is easy to implement and maintains donor control while fulfilling a charitable purpose.

Beneficiary Designations

For younger donors without heirs, designating all or a portion of their retirement accounts, such as a 401(k) or IRA, to a nonprofit organization can be an effective philanthropic start. Younger individuals may already be contributing to retirement accounts. Including charitable giving as a component of retirement planning can have long-term benefits. For instance, they could designate a nonprofit as the beneficiary of their retirement account, thus reducing their taxable estate.

Younger donors may also consider a gift of life insurance as a planned giving strategy. Life insurance policies allow donors to contribute a relatively small amount upfront, which can translate into a much larger gift to a nonprofit in the future. By naming a charitable organization as the life insurance beneficiary, the policyholder can leave a substantial contribution to a cause he or she believes in.

STRATEGIES FOR MIDDLE-AGED DONORS (40s to 60s)

At this stage, middle-aged individuals often begin to focus more seriously on their estate planning. These individuals, who are often business owners or in their peak earning years, comprise a major market for planned gifts. Like younger donors, individuals in their 40s to 60s can designate a nonprofit as a beneficiary of their retirement account. By naming a nonprofit as the beneficiary of their 401(k) or IRA, the donor can reduce the taxable value of the donor's estate and leave a substantial gift to a nonprofit without incurring estate taxes. These donors can also include bequests to charitable organizations in their estate plans to ensure that the donor's philanthropic goals continue beyond their lifetime and create a meaningful legacy. Beyond these strategies, these donors can begin to explore CGAs and CRTs that are tailored to fit their specific needs.

Deferred Charitable Gift Annuities

Deferred CGAs are an appealing option for donors in their 40s to 60s. A CGA provides a guaranteed income for life in exchange for a gift to the nonprofit. This type of giving is particularly attractive for those who wish to make a charitable gift but also need guaranteed income in their retirement years. However, with an immediate CGA, middle-aged donors will only receive a low payout rate, which may be eroded over time by inflation. Some charitable organizations also have minimum age requirements, which may bar donors under a certain age from participating. In addition, there is an extended period from when the CGA is established to when the nonprofit receives the remainder. Thus, a deferred CGA is a solution to minimize these disadvantages since the longer the deferral period, the higher the annuity payout rate.

To provide even more flexibility in this age range, a donor could also consider a flexible deferred CGA. In PLR 9743054, the IRS approved the concept of a flexible deferred CGA. While a private letter ruling cannot serve as legal precedent, it can provide insight into the IRS's likely position on a given issue. Flexible annuities are created with a future payout, like a regular deferred CGA. With a flexible annuity, the annuitant reserves the right to select when payments commence at a future date. If he or she decides to take the payment early, then there will be

lower payout amounts. If a later payout date is selected, the payments will be higher. It is worth noting that the deduction does not change from when the deferred annuity is established. Instead, the payout rate will change depending on when the annuitant decides to commence payments so that the payouts will match up to the claimed deduction.

Example 1 Samantha, 55, wants to receive supplemental income when she retires, but has not decided when she plans to retire. She contributes stock with a value of \$150,000 and a cost basis of \$40,000 for a deferred gift annuity and reserves the option to start quarterly payments on June 30 of any year from 2032 to 2042. The longer she waits to begin the payments, the larger the payments will be. She can only elect to start the payments once and the annuity payments will become fixed at that time. If she elects payouts to start in 2032, it will total \$10,433 per year. If she waits until 2042 to begin payments, she will receive \$21,750 per year. Whichever year she chooses to begin the payments, she will be entitled to a deduction of \$67,922 which is generated in the year of the CGA creation and reduces current income tax.

In a flexible deferred CGA, when an annuitant wishes to start the payments during the time range, they must elect to do so by written notice to the nonprofit. If the annuity is a two-life annuity, this election may be made by either annuitant. The annuity contract usually requires that an election be made one payment period prior to the desired annuity start date.

Term-of-Years Charitable Gift Annuities

Another variation of deferred CGAs that can be attractive to middle-aged donors is the term-of-years CGA, though not available to annuitants in all states. A term-of-years CGA must begin as a one or two life deferred CGA and follow specific requirements, including that the contract cannot guarantee a minimum or maximum number of payments. IRC Sec. 514(c)(5). However, the CGA contract can include an option to convert the annuity to a term-of-years payout after the CGA is created but before the first payment has been made.

For example, a person may desire payouts between age 65 and 69 and transfer assets to a nonprofit initially for a one-life deferred payment gift annuity. The annuitant and the nonprofit may mutually agree to convert the life interest to a term-of-years with equal value. The individual then receives payments for five years and starts receiving retirement income from other sources when the annuity ends. By commuting the payments from a lifetime to a term-of-years, the annuitant receives higher annuity payouts for a limited term. This could provide supplemental income as the donor transitions to relying on retirement income. One note of caution is that term-of-years payments prior to age 59½ would be subject to a 10% additional income tax penalty under IRC section 72(q). Thus, advisors should ensure that the payout date begins after age 59½.

Term-of-Years Unitrust

A CRT is also an excellent option for individuals in this age group. With a CRT, the donor transfers assets to the CRT and the CRT makes income payments to the donor or other beneficiaries for life, lives, a term of up to 20 years or for a combination of both. Reg. 1.664-

3(a)(5)(i). In most circumstances, the income is paid to the donor for life or to the donor and spouse for two lives.

There are two types of CRTs: the charitable remainder annuity trust (CRAT) and the charitable remainder unitrust (CRUT). A CRAT pays out a fixed percentage of the initial funding amount each year while the CRUT pays out a fixed percentage of the trust, with revaluations each year. The donor receives a charitable income tax deduction in the year the trust is funded, based on the present value of the charitable remainder. After all payments have been made, the remaining trust assets are transferred to one or more designated nonprofits. Contributing appreciated assets to a CRT offers several advantages including an income tax deduction, bypass of capital gain and a payment stream. When the CRT ends, the remaining assets are distributed to the chosen nonprofits. For middle-aged donors, a CRT can help reduce taxable gain from the sale of an appreciated asset, provide a stream of income during retirement and allow for a significant charitable gift in the future.

A unitrust payout percentage must comply with three basic rules. The trust must pay between 5% to 50% and it must produce a charitable deduction equal to 10% or greater of the funding value (also referred to as the 10% minimum deduction test). A CRT for the lives of younger beneficiaries may fail the 10% minimum deduction test because the present value of the remainder is too low with the projected payout period length. A solution to this can be the CRT for a term of years. It also has the benefit of producing a larger charitable deduction which can be attractive to high earners.

Example 2 Sophia, 55, recently inherited undeveloped parcels of land from her parents' estate worth \$750,000. As a senior vice president of engineering at a technology firm, Sophia makes a considerable salary. In her free time, Sophia serves on the board of a local nonprofit that teaches area youth about careers in science and engineering. Sophia is interested in learning about options to offset her income by making a gift of the property to the nonprofit.

Sophia's advisor discusses the benefits of a CRT with a 5% payout for a term of 10 years. The CRT provides Sophia with a charitable deduction of \$456,211, a much larger charitable deduction than the \$226,455 she would receive if she established the CRT for her lifetime. Although this is an appreciated property gift which will limit the offset of the deduction to 30% of AGI, Sophia expects to take the full deduction within the first two years of the gift. Because it is only a 10-year term, the nonprofit will receive the remainder within a relatively short period of time. In addition, Sophia can expect to receive approximately \$40,000 each year from the CRT.

Retirement Unitrust

Another unitrust option for middle-aged donors with larger estates is a retirement unitrust. Compared to the deferred CGA, a retirement unitrust may result in a lower charitable deduction up front but higher income upon retirement. A unitrust can also be suitable for a donor willing to take on more investment risk, with the goal of providing more protection from inflation.

A retirement unitrust is structured with a FLIP payout. With a FLIP, the trust starts with a net income plus makeup charitable remainder unitrust (NIMCRUT) payout that pays the lesser of

trust income or the unitrust percentage. After the initial establishment of the unitrust, the investment strategy can focus on principal growth during the years before the FLIP, which keeps the trust income negligible before the FLIP when income is not needed. After a “trigger event” occurs, the trust “flips” to a standard unitrust payout. The trigger event must be some event not within the control of the trustee such as the sale of a nonmarketable asset or a planned retirement date. This will “turn on” the income stream for donors once they reach their retirement years. If zero or minimal payments are desired before the FLIP, the investment strategy should be designed accordingly to generate little or no income.

Example 3 Kathryn, 52, and Marty, 50, bought development real estate on the outskirts of town ten years ago. Local area developers are interested in purchasing their property to build new housing. Kathryn and Marty plan to retire in about ten years. Since now is the best time to sell, they believe that they should sell the property but would like to sell it without paying hefty taxes. By creating a FLIP unitrust and transferring half of the property this year and half of the property next year, they benefit in several ways.

First, the appreciated property charitable deduction of approximately \$70,000 each year may be fully utilized since their income is \$250,000 and 30% of that limit would be \$75,000. Second, the property logically would be developed in two phases. By gifting half this year and half next year, they maximize their total return. Third, their trustee may then transfer the proceeds into growth stocks for ten years. At that time, they may have over \$1 million in the trust and the trustee may then begin making retirement income payments of over \$51,000 annually to Kathryn and Marty.

During their two lives, the total income paid out is expected to be over \$3.5 million. With their income tax savings and the bypass of capital gain, they are very pleased with the retirement unitrust plan. After their two lives, a gift of approximately \$2.8 million will be made to their favorite nonprofits based on the financial projections of the CRUT.

Unitrust with Insurance Replacement Trust

Business owners with large estates and high income are well positioned to use a unitrust with insurance replacement as a planned gift option. A charitable gift to a CRT paired with an irrevocable insurance trust can be an effective option for donors who would like to make a gift to a nonprofit but also want to provide financial security to loved ones. In these situations, the donor creates two separate trusts, a CRT and an irrevocable life insurance trust (ILIT).

An ILIT is an irrevocable trust designed to use insurance as the principal trust investment. In the case of an ILIT created to provide inheritance for family members, the ILIT will receive one or more gifts of cash from the donor and will use those gifts to pay the premiums on an insurance policy. The donor can fund these premium payment gifts to the ILIT with income from the CRT or the tax savings from the CRT deduction.

It is essential that an ILIT is irrevocable, since a key goal is to avoid inclusion of the life insurance proceeds in the estate of the grantor. To avoid inclusion, the proceeds must be payable to the ILIT and the grantor cannot retain any "incidents of ownership" to the policy. IRC Sec.

2042(2). Incidents of ownership include the right to designate beneficiaries under the policy, to borrow against the policy or to control the policy in any manner.

Example 4 John, 55, has a \$20 million estate and is looking for ways to reduce his potential estate tax while benefiting his two children, Mike and Sarah. While meeting with his advisor, the advisor suggests a charitable remainder unitrust and ILIT structure. The advisor explains that John could establish a CRT with appreciated technology stock he bought years ago that is now worth \$500,000. The CRT will pay income to John over his lifetime starting at \$25,000 in the first year. At the same time the CRT is established, John sets up a separate ILIT to benefit his children after he dies. The income payments from the CRT are used to pay premiums on an insurance policy acquired by the ILIT. The insurance policy will pay out over \$515,000 upon John's death. As a result of the CRT, John receives a charitable deduction, bypasses capital gain on the stock and receives income each year. When he passes away, the nonprofit expects to receive over \$675,000 from the CRT. At that time, the ILIT will payout the insurance policy benefits of \$515,000 to John's children. The ILIT's proceeds are not considered part of John's estate for estate tax purposes.

CONCLUSION

There are many charitable strategies that can be used for different age and income levels depending on each donor's circumstances and charitable goals. Using charitable gifts, individuals of any age and income can align their financial objectives with their philanthropic efforts while realizing tax savings or other benefits. By understanding the different gift models and the tax advantages offered by charitable gift strategies, professional advisors will be well-equipped to guide and support individuals through every stage of life.



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