Helping Parents and Charity

Thanks to longer life expectancies, more clients may find themselves in the position of acting as caregivers to their parents. Even when the adult children don’t have responsibility for the day-to-day care of parents, they may be helping financially. There are ways for children to provide financial assistance, while also qualifying for an income tax charitable deduction.

Charitable remainder unitrust

A son or daughter who normally provides a parent with $500 per month ($6,000 annually) could establish a charitable remainder trust that would pay the income to the parent for life. For example, a child could fund a 5% charitable remainder unitrust with a cash gift of $120,000, naming an 85-year-old parent as income beneficiary. The child’s income tax charitable deduction would be nearly $90,000 (assumes quarterly payments and a §7520 rate of 3.6%). The child could avoid any gift tax on the creation of the trust thanks to the gift tax credit that shelters up to $11.18 million.

A child might also choose to fund a two-life unitrust with a cash gift of $120,000 that would continue payments for his or her own life after the parent’s death. Assuming the child is age 62, the charitable deduction would drop to about $47,000.

Charitable gift annuities

Charitable gift annuities, as with charitable remainder annuity trusts, offer the assurance of a fixed payment. In addition, because gift annuity rates are higher for older annuitants, the child may not have to contribute as

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Helping Parents . . . (continued from page 1)

much to provide the same benefit for the parent. The rate for an
85-year-old annuitant is 8.3%. The
child could contribute $75,000 in
cash, which would provide annual
payments of $6,225 for the parent.

The child’s income tax deduction
would be more than $42,000. The
child can retain the right to revoke
the parent’s interest to make the gift
incomplete for gift tax purposes.
With either the charitable remainder
trust or the charitable gift annuity,
the child will no longer have to make
gifts with after-tax dollars to provide
the same support for the parent,
while also making a substantial gift
to a favorite charity.

From Like-Kind Exchange to a Unitrust

The like-kind exchange provisions
of Code §1031 allow taxpayers to
postpone capital gains tax on the
disposition of income-producing or
investment real estate by “trading”
or exchanging for another parcel of
similar use. But what happens to real
estate investors when they finally
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UC Berkeley Planning Pointer:

Flexible Deferred Gift Annuities Give Baby Boomers
Grown Up Choices

Have you heard from your
Boomer clients that charitable
gift annuities are just for “old
people”? You can tell them that
establishing a Flexible Deferred
Gift Annuity (FGA) just might
be the perfect retirement strategy
for their generation, offering
them both control and stability
with respect to their supplemental retirement income. Your
clients can establish an FGA at Cal in exchange for an irrevo-
cable gift of cash or securities
($20,000 minimum), choosing
a range of possible dates for
payments to begin. That way,
they have the flexibility to “wait
and see” when they want to turn
on the annuity payment spigot.
This strategy is especially
appealing to Boomers who are
often unsure of when they will
retire. The best part is that the
payout rate increases for each year
defered – as with Social Security,
there is an incentive to delay
payments as long as possible.
We’ve talked in previous issues
about the benefits of the new
increased CGA rates for your clients.
We’re now going to highlight the
benefits of FGAs which, in
combination with the increased
rates, can provide “customized”
supplemental fixed retirement
income giving your Boomer clients
the control they desire. For example,
your 65-year-old client who is not
planning to retire anytime soon
could establish an FGA with the
UC Berkeley Foundation funded
with $200,000 in cash, choosing a
date range of 2019 (first year possible
to start payments) to 2038 (last
year possible to start payments).

If your client then decides to start
payments at age 68 in 2021, the
annuity rate would be 5.9%
paying an annual annuity of
$11,800. If your client instead
waited until age 73 in 2026
to turn on the fixed income
stream, the annuity rate would
be 7.9% paying an annuity of
$15,800; and at age 76 in 2029
a rate of 9.6% paying $19,200
annually. In addition to getting
rewarded for waiting, your client
would also enjoy the benefits
of a charitable deduction of
$74,218 in the year of the gift
(very beneficial for those high
income earners), along with a
portion of his or her annuity
payments being tax-free. In
sum, FGAs offer enticing benefits
for your “forever young” Boomer
clients as well as your older clients.
The New Look to Year-End Planning

With higher standard deductions, a $10,000 limit on the deduction for state and local taxes (“SALT” deduction) and the elimination of many miscellaneous itemized deductions, year-end planning takes on a whole new meaning in 2018. The deduction for charitable gifts remains the primary way for clients to exceed the standard deduction threshold. Consider creative ways for philanthropic clients to make gifts while also saving income taxes:

Qualified charitable distributions (QCD) – Clients age 70½ or older can make tax-free gifts of up to $100,000 from IRAs directly to charity. While there

is no charitable deduction allowed, the QCD can take the place of required minimum distributions that are taxed at ordinary income rates. This may also allow donors to avoid higher Medicare premiums by reducing taxable income.

Charitable gift annuities – Donors can contribute cash or appreciated property to charity in exchange for a charitable gift annuity that will pay a fixed sum annually for life. Annuity payments can begin in the year of the gift or can be postponed until some later time.

Mary and Kurt, both age 72, have a standard deduction of $26,600 for 2018. They plan to transfer appreciated securities worth $100,000 to arrange a charitable gift annuity that will pay them $5,200 (5.2%) annually for their joint lives. A portion of each year’s payments will be taxed at favorable capital gains rates. In addition, the couple will be entitled to a charitable deduction of $35,518 (assuming quarterly payments and a 3.6% §7520 rate), which will enable them to itemize for 2018.

Charitable remainder trusts – Remainder trusts offer the opportunity to turn low-yield, highly appreciated assets into a lifetime stream of income. It may make sense to arrange a flip unitrust [Treas. Reg. §1.664-3(a)(1)(i)(c)]. The trust would begin as a net-income or a net-income with makeup unitrust and then convert to a standard unitrust in the year after the sale of the real estate, entitling the donor to a fixed percentage of the trust’s annual value.

From Like-Kind . . .
(continued from page 2)

decide to get out of the real estate business? The taxpayer may have made several like-kind exchanges over the years, leaving him or her with a low basis in property with an appreciated fair market value.

Philanthropic clients faced with this dilemma could find that a charitable remainder unitrust is the solution to their problems due to the advantages listed here:

· There is no capital gains tax when the real estate is placed in the trust or sold by the trustee.
· There is a charitable deduction based on the fair market value of the property, not on the much lower adjusted basis.
· The client receives the payments over his or her life, so the cash flow can mimic the rental income the donor previously received.

· Rather than receiving rent, which is ordinary income, a significant portion (with Berkeley unitrusts, up to 75%) of each year’s trust payout may consist of capital gain income, taxed at 15% or 20% (commercial real estate subject to depreciation recapture will have the recapture amount taxed as capital gain at a maximum rate of 25%).
· The client is able to satisfy charitable goals.
The New Look . . . (continued from page 3)

payments, with the added bonus of a generous charitable deduction for the value of the remainder that will pass to charity when the trust ends. Mary and Kurt could use the $100,000 in securities to fund a charitable remainder unitrust that could pay them even more than the gift annuity for their lives. The exact amount they receive each year would depend on the annual value of the trust’s assets. Their deduction would be approximately $44,555, assuming a 5% payout rate.

Capital gains savings – Even donors who aren’t able to itemize might nevertheless find it economical to make gifts using long-term appreciated assets. They avoid the capital gains tax that would otherwise be due if they sold the property.

Giving through family members – Clients may enjoy overall family tax savings by making gifts through adult children or parents. For example, a couple in their late 60s who can’t itemize plan to give $5,000 to a favorite charity. They could transfer cash or appreciated stock worth $5,000 to a son or daughter who is close to the $12,000 standard deduction for a single individual. The child then makes a gift to the parents’ charity in their names and is entitled to the charitable deduction. A child in the 22% income tax bracket would save about $1,100 in taxes by making the gift on behalf of the parents.

Final Substantiation Regs Issued

The IRS has released final regulations on substantiation of charitable gifts that closely match proposed regulations issued in 2008. Among the final rules contained in T.D. 9836:

Pledge cards – A blank pledge card provided as part of a workplace giving campaign does not constitute adequate substantiation because it does not show the information required under Code §170(f)(17).

Appraiser privacy – Qualified appraisers may use a taxpayer identification number, rather than a Social Security number, when signing appraisals.

Form 8283 – Although there is no specified form for contemporaneous written acknowledgments, Form 8283 does not qualify under Code §170(f)(8) since it lacks some of the information required under Code §170(f)(8)(B).

Carry over deductions – A qualified appraisal must be attached to the income tax return on which a deduction is taken for a noncash gift in excess of $500,000. If any portion of the deduction is carried over to later years, the appraisal must also be attached to those returns. The IRS said its need for the information outweighs any burden on the taxpayer.

Qualified appraisers – A qualified appraiser is an individual with “verifiable education and experience” valuing the type of property for which the appraisal is performed. The IRS declined to change the standard to “education or experience,” saying it would be contrary to language in Code §170(f)(11)(E)(ii)(I).

IRS actuarial tables – The tables used to value charitable remainder trusts cannot be used as a substitute for qualified appraisals to value property in other contexts. The tables don’t provide a fair market value, the IRS said.