McDermott Will & Emery

CUTTING THROUGH THE CHAOS: OFF THE BEATEN PATH – 6 NOT SO OBVIOUS PLANNING IDEAS

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QUESTION SUBMISSIONS

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- The presenters will answer questions at the end of the presentation as time permits
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NON-CHARITABLE PURPOSE TRUSTS

NON-CHARITABLE PURPOSE TRUSTS

- Generally, three elements are necessary to create a trust:
  - A trustee,
  - Trust principal, and
  - One or more individual beneficiaries.
- Under common law, the absence of a beneficiary prevented the establishment of a valid non-charitable trust.
  - The reasoning was that there would be no beneficiaries to enforce the trust (i.e., to hold the trustee responsible for administering the trust properly, or to take action in the event of a breach of fiduciary duty).
- A trust established for a purpose without identifiable beneficiaries was only permissible if the purpose was charitable in nature.
  - Charitable trusts are purpose trusts, and are valid even though they are not held for any particular beneficiaries.
  - The Attorney General of the relevant state is the “enforcer.”

NON-CHARITABLE PURPOSE TRUSTS

- Over the past few decades, many states have adopted statutes permitting the creation of trusts to accomplish one or more non-charitable purposes without identifiable beneficiaries.
- General features of a purpose trust:
  - No “beneficiaries” in traditional sense,
  - Protector or enforcer is appointed to enforce terms of the trust, and
  - The trust provides for one or more valid purposes (cannot be contrary to public policy).
- A purpose trust does not directly benefit any particular beneficiary, but the administration of the purpose trust often indirectly benefits certain individuals.
  - E.g., A purpose trust holding a family compound may provide for use of the compound by family members (at the trustee’s discretion), but the trustee would not have duties to those family members with respect to the management and control of the compound.

NON-CHARITABLE PURPOSE TRUSTS

- As guidance for state legislators, the Uniform Probate Code as amended in 1993 (UPC) and the Uniform Trust Code of 2000 (UTC) promulgated new sections to validate trusts specifically for the care of animals and trusts for other non-charitable purposes.
- Approximately 40 states have adopted statutes providing for some form of a purpose trust (with Illinois joining the ranks in 2020 by enacting relevant provisions of the UTC).
- Many states vary the language of their purpose statutes by:
  - Modifying the common law rule against perpetuities limitation,
  - Allowing for greater flexibility in who can enforce the trust (i.e., a trust protector),
  - Expanding or narrowing the scope of the permissible non-charitable purposes, and
  - Varying the degree of judicial oversight.

NON-CHARITABLE PURPOSE TRUSTS

- Duration may be an important feature, depending on the purpose the trust is intended to serve.
  - Most enacting states limit the duration of a purpose trust to 21 years (or the life of a pet).
  - Those provisions may be acceptable if a long-term purpose trust is not necessary (e.g., to manage and oversee the winding down of a private foundation).
- Other states provide for near perpetual duration (Nevada - 365 years) or have significantly extended the UTC's recommended 21 year duration rule (Tennessee – 90 years).
- Some states (expressly or by omitting a duration limitation) permit perpetual purpose trusts, such as:
  - Delaware,
  - New Hampshire,
  - South Dakota, and
  - Wyoming.

NON-CHARITABLE PURPOSE TRUSTS

- A non-charitable purpose trust can be created for any valid purpose.
  - Typical examples may include:
    - Ownership and management of particular assets, such as wine, artwork, collections, family residential compounds, or other assets with special meaning to the donor and the donor's family.
    - Pet trusts, providing for the care for animals after death of owner.
  - Less typical examples may include:
    - Voting owner (or full owner) of an operating business.
    - Purpose trust to provide a social statement.
    - Owner of interests in private trust company (PTC).
    - Permanent voting "member" of private foundation (formed as not-for-profit corporation).

NON-CHARITABLE PURPOSE TRUSTS

- Purpose Trust as Owner of Operating Business:
  - Example: *Organically Grown Company* (Oregon).
    - Transitioned ownership from ESOP to “Sustainable Food and Agriculture Perpetual Purpose Trust.”
  - Can also consider holding voting interests in purpose trust, with nonvoting interests owned by family members or trusts of which family members are beneficiaries.
- Purpose Trust as Social Statement:
  - “*Disgorgement,*” by Cameron Rowland.
  - *Reparations Purpose Trust* (Delaware perpetual purpose trust).
    - Created in 2016, holds 90 shares of Aetna stock.
    - Provides for termination upon action by U.S. government to make reparations for slavery.

NON-CHARITABLE PURPOSE TRUSTS

- Ownership of Private Trust Company (PTC):
  - To avoid potentially negative tax consequences, many PTCs are owned by a traditional irrevocable trust (with beneficiaries, trust principal and a trustee) formed solely to own equity interests in and control the PTC.
  - By the terms of the trust, the trustee is prohibited from voting to alter certain tax sensitive provisions in the PTC's governing documents.
  - Alternatively, a purpose trust could be created in a perpetual trust jurisdiction to own the equity interests in the PTC and control the PTC.
  - Unlike a common law irrevocable trust, the purpose trust can be administered for the purpose of owning and controlling the PTC ownership interests without the need to account to beneficiaries/family members.
- Same reasoning could apply to other family entities that are not intended to provide economic benefits, but rather serve an important ongoing governance purpose.
  - E.g., Domestic employee entity.

NON-CHARITABLE PURPOSE TRUSTS

- Private Foundation – Protection Against “Mission Drift”:
  - Many donors may be concerned about successor foundation managers (related or unrelated) failing to uphold their intentions with respect to the use of the foundation’s assets following the death of the donors.
  - Can consider gift or pledge instruments to the foundation, or gift agreements with the foundation (for prospective giving).
  - But what if the foundation is fully funded? Consider the Surdna Foundation, created by John Emory Andrus.
  - Example: Grantor has created a significant private foundation to support specific charitable purposes.
    - If formed as a membership nonprofit corporation, the grantor could create a purpose trust to serve as the sole member when the grantor is no longer acting as the member.
    - The bylaws can provide that the foundation’s purpose and governance provisions can only be changed with the approval of the trustee of the purpose trust.
    - The purpose trust instrument can contain provisions requiring the trustee to adhere to the charitable purposes and governance, perhaps with exceptions in specifically listed circumstances.
    - The purpose trust also may include (or enforce) a timeline for distributions.

PLANNING INTO IRC §6163 – EXTENDING THE TIME TO PAY ESTATE TAX ON REMAINDERS & REVERSIONS

IRC §6163 – EXTENSION OF TIME FOR PAYMENT OF ESTATE TAX ON REVERSIONARY OR REMAINDER INTEREST

- Section 6163 provides for:
  - Deferral of the payment of the estate tax,
  - Deferral of the payment of the interest on the estate tax,
  - Incurred on a remainder or reversionary interest, and
  - Until the termination of the preceding interests.

WHAT IS A REMAINDER OR REVERSION?

- A remainder interest is the future interest in a property that follows all life or term interests.
  - For example, Wife funds trust to pay income to Child for 30 years, remainder to Husband.
- A reversion is the name used for a remainder that “reverts” to the donor.
  - For example, Husband funds trust to pay an annuity to Child for 30 years, reversion to Husband.

IRC §6163 – REQUIREMENTS

- In order to qualify for the deferral, the remainder or reversion must be included in gross estate, but cannot be created by testamentary transfer of the decedent – lifetime transfer by the decedent okay.
- The portion of estate tax that may be deferred is that portion equal to:

  Total Estate Tax x Value of Reversionary Interest/Value of Gross Estate.
- Executor must elect to defer.
- May need to post bond.

§6163 RESULTS IN A LOW INTEREST LOAN FROM THE U.S. GOVERNMENT

- Interest on deferred estate tax is deductible from the gross estate as of the original due date of the tax as an administration expense, resulting in “retroactive” reduction in the estate tax and significant time value of money benefit.
- Pay nothing until the preceding trust interests terminate.
- Total of ever diminishing estate tax and ever increasing interest never exceeds the original estate tax value of the remainder or reversion.
- Growth on the government’s money in the meantime inures to the benefit of the trust, thereby effectively diminishing the estate tax rate.

§6163 MATH

- The rate of interest is set by IRC §6621 and fluctuates – 3% plus federal short-term rate.
- Because the interest is deductible as of the date of death, thereby reducing the estate tax on which interest is due, even high interest rates produce low effective compound costs of funds.
- Consider a remainder worth $10 million at death, the estate tax and interest on which will not be due for 30 years. The estate tax otherwise due is $4 million:
  - Under 6163, if the applicable interest rate is today's 3%, then in 30 years that $4 million estate tax and interest bill will have grown to only $6.18 million reflecting an internal compound rate over that time of only 1.46%.
  - Even if the applicable interest rate were 10% over that entire period, the amount due (tax and interest) would be $9.21 million reflecting only a 2.82% internal compound rate.
  - Normal investment returns should far outstrip these low interest costs, especially over long periods.

§6163 MATH

- $10 million reversion/remainder; 40% estate tax rate; $4 million estate tax due without §6163.
- With §6163, tax and interest deferred 30 years:

IRS Borrow Rate	10%	7%	5%	3%
Tax	527,721	1,097,423	1,717,640	2,546,303
Interest	8,680,697	7,256,442	5,705,900	3,634,243
Total Pay	9,208,418	8,353,865	7,423,540	6,180,546
Implied Interest Rate	2.82%	2.49%	2.08%	1.46%

PLANNING INTO 6163

- Consider “planning into” 6163 in order to delay paying any estate tax or interest on remainder or reversion interests for decades.
- May be particularly attractive for hard to value assets as the Internal Revenue Service (IRS) may be reluctant to fight the valuation battle where the estate tax is deferred for decades . . .

CONSTRUCTS FOR PLANNING INTO 6163

- Example #1
  - Shortly before her death, W creates a 30-year NCLAT (Non-Charitable Lead Annuity Trust) for her children, retaining the reversion.
  - W pays gift tax (and her estate, estate tax on the gift tax) incurred to create the small, upfront annuity interest.
  - The trust reversion is included in W's estate.
  - W's executor elects §6163 and the estate tax and interest is deferred for 30 years.
  - Results on a PV basis:

IRS Borrow Rate	10%	5%	10%	5%
After-tax Growth	5%	5%	10%	10%
Effective Est Tax Rate	31.87%	28.48%	18.73%	17.89%

CONSTRUCTS FOR PLANNING INTO 6163

- Example #2
  - Shortly W's death, H creates a trust providing that all income be paid to H&W's children for 30 years, remainder to W.
  - Gift tax imposed on the income interest; remainder qualifies for the gift tax marital deduction.
  - The trust reversion is included in W's estate, and
  - W's executor elects §6163 and the estate tax and interest is deferred for 30 years.
  - Results on a PV basis:

IRS Borrow Rate	10%	5%	10%	5%
After-tax Growth	5%	5%	10%	10%
Effective Est Tax Rate	26.72%	23.22%	13.12%	12.25%
Effective Est Tax Rate if set up at .4% and spouse dies at 2%	19.89%	17.71%	11.43%	10.89%

ADVANTAGES & DISADVANTAGES OF 2020 GIFTS

EFFECT OF CURRENT POLITICAL & ECONOMIC ENVIRONMENT ON ESTATE PLANNING

- Tax increases are likely needed to meet budget deficits and to meet current social, economic, and environmental needs.
- A possible regime change in the Federal Government could cause a portion of the tax increases to come from the Federal transfer tax system.
- Possible changes include decreases in the current transfer tax exclusion amount of $11.58 million and increases in the current top transfer tax rate of 40%, and tax recognition on gifts of appreciated property.
- Because these changes, if they occur, could be effective as early as January 1, 2020, clients who want to preserve their current $11.8 exclusion should consider using it before the end of the year.
- Clients who want to take advantage of the 40% transfer tax rate, should consider making gifts that are subject to gift tax before the end of the year.

ADVANTAGES OF 2020 GIFTS

- Gifts should be protected from gift tax up to the total amount of the donor’s remaining $11.58 million exclusion.
- Gifts of appreciated property can be made without tax recognition.
- Gifts of partial interests in property may be eligible for valuation discounts.
- Gifts to irrevocable grantor trusts can result in a lifelong obligation on the donor to pay income tax on trust income.
- Gifts will remove post-gift income and appreciation from donor’s transfer tax base.
- Gifts subject to gift tax will be subject to an effective gift tax rate of only 28.57% if the grantor lives three years after the gift.

POTENTIAL DISADVANTAGES OF CURRENT GIFTS

- Gifts can result in negative tax results if:
  - The gifted property declines in value.
  - The gifted property is appreciated and fails to produce a post-gift investment return sufficient to offset the adverse tax consequences of the loss of basis step-up at death.
  - The donor is a New York domiciliary and dies within three (3) years of making the gift.
- Donors may be reluctant to lose access to or control over any significant portion of their assets.

NEGATIVE POTENTIAL EXPLAINED

- Gifts that decline in value.
  - Gifts that decline in value remain in the donor’s estate tax base at their value on the date of the gift.
  - Unless the gifts were protected from gift tax by an amount of the current exclusion that is no longer available at death, the gift will cause the donor’s estate to pay a higher gift tax than would have been paid if the gift had not been made. The higher tax will be equal to 40% of the decline (or possibly more if estate tax rates are increased).

NEGATIVE POTENTIAL EXPLAINED

- Gifts of appreciated property that fail to produce an investment return sufficient to offset the tax cost of the loss of basis step-up at death.
  - A gift of an asset worth $1 million with a basis of $500,000 that produces a post gift return of $100,000 will save estate taxes of $40,000 (40% of $100,000).
  - The loss of basis step up will cost the donee at least $142,800 when the donee sells the asset (23.8% of $600,000).
  - Total tax cost of the gift is $102,800.
  - For this gift to achieve a “break-even” tax result, it would have to produce a post-gift investment return of about 73%.

NEGATIVE POTENTIAL EXPLAINED

- Special problem for New York domiciliaries – they pay New York estate tax on gifts they make within three (3) years of death.
  - State estate taxes are normally deductible in computing federal estate tax. As a result, the combined federal estate and New York estate tax of a New York domiciliary is generally no more than 49.6%.
  - The New York estate tax paid on gifts made within three (3) years of the date of death is not imposed on assets included in the federal gross estate.
  - As a result, it is likely not deductible; the total estate tax on the three-year gift can be as high as 56%.

GUARDING AGAINST THE POSSIBLE NEGATIVE CONSEQUENCES OF GIFTS

- The possible negative consequences of gifts are potentially avoidable by using techniques that will permit the inclusion of the gifted property in the gross estate of the donor if inclusion would produce a better tax result than exclusion. Inclusion would result in exclusion of the gifted property from the donor's adjusted taxable gifts at its date of gift value, inclusion of the gifted property in the donor's gross estate at its date of death value, and a basis adjustment to date of death value.
- Available Methods:
  - Disclaimers.
  - Gifts to trusts eligible for the marital deduction if an election is made.
  - Use of power to grant testamentary power of appointment to grantor.

DISCLAIMER

- Donor makes the gift to a trust.
- The terms of the trust provide that if a beneficiary disclaims his or her interest in the trust, the gifted property will be returned to the donor.
- If the beneficiary disclaims the property within 9 months of the gift, without having received any benefit from it, the gift will be treated for gift tax purposes as if it had never been made.

GIFTS TO QTIP

- Donor makes a gift to a trust the terms of which satisfy the requirements for qualified terminable interest property.
- If, before the due date for the donor’s gift tax return (generally October 15 of the year after the gift is made), the donor determines that a taxable gift would have negative tax consequences, the donor would elect to treat the trust as eligible for the marital deduction.

POWER TO GRANT A TESTAMENTARY POWER OF APPOINTMENT

- Donor makes a gift to a trust the terms of which give an independent person the power to give the donor a testamentary power of appointment over the trust principal but not its post death income if he or she reasonably concludes that inclusion would produce a better tax result.
- The donor’s power could be limited to the power to affect the time of enjoyment.
- The existence of the power to grant a testamentary power should not cause the gift to be incomplete or the gifted property to be included in the donor’s gross estate unless the power is granted and held by the donor on the date of the donor’s death.

POWER TO GRANT A TESTAMENTARY POWER OF APPOINTMENT

- If before the date of the donor's death, the power holder determined that a better tax result would be achieved if the trust principal were included in the donor's gross estate, the power holder would give the donor a testamentary power of appointment.
- If the donor dies holding the power of appointment, the gift would be removed from his or her adjusted taxable gifts and would be included in the donor's gross estate at its date of death value. Under current regulations, if the gift had been protected by the exclusion and the exclusion had been reduced before the date of death, the higher exclusion would still be available to the donor's estate. If the donor had paid gift taxes at rates lower than the rates in effect at the donor's death, the benefit of the lower rates would be preserved.

WAYS TO PRESERVE DONOR'S ACCESS TO GIFTED PROPERTY

- There are a number of ways that might be used to preserve a donor's access to gifted property. They include:
  1. Gifts to trusts of which donor's spouse is a beneficiary.
  2. Gifts to Domestic Asset Protection Trusts, trusts of which the donor is a beneficiary if established in a state that does not permit the donor's creditors to reach the assets.
  3. Gifts of promises to make gifts.
  4. Creation of an intentionally defective preferred interest in an entity.

CREATING AN INTENTIONALLY DEFECTIVE PREFERRED INTEREST

- An intentionally defective preferred interest is a senior interest in an entity such as a limited liability company that intentionally fails to comply with the requirements established by section 2701 of the Internal Revenue Code. Because it does not comply, the interest is deemed to have a zero (0) value for gift tax purposes.
- If the holder of the preferred interest transfers junior interests in the entity to family members or trusts for their benefit or if an individual acquires a preferred interest at the same time as his or her family members or trusts for their benefit acquire the junior interest, the preferred interest holder will be treated as having made a taxable gift equal to the value of his or her retained, preferred interest.

EXAMPLE OF INTENTIONALLY DEFECTIVE PREFERRED INTEREST TECHNIQUE

- D creates an irrevocable trust for her children and transfers property worth $1.1 million to the trustees.
- D and the trustees form a limited liability company (L) with two classes of membership interests, A and B.
- The holders of the A interests are entitled to a 1% noncumulative return on their investment plus 1% of any additional profits. They have the right to withdraw their investment at any time.
- The holders of the B interests are entitled to all additional profits.
- D contributes $9.9 million of appreciated assets to L; the trustees contribute $1.1 million.

EXPECTED RESULTS

- D should be treated as having made a taxable gift of $9.9 million at the time of the contribution.
- D's gift, if the contribution occurs in 2020, will be protected by D's remaining exclusion amount up to $11.58 million.
- D's contribution, to the extent it exceeds her exclusion amount will be subject to gift tax at the 40% rate. If she survives for three (3) years after the contribution, her effective tax rate on the deemed gift will be only 28.57%
- The $9.9 million contributed by D will be available to her during her life if needed.
- If D retains the preferred interest until death, her interest will receive a basis equal to its value on the date of death, presumably about $9.9 million.

EXPECTED RESULTS

- Because D was treated as having made a gift of assets she actually retained, the regulations under section 2701 will permit her estate to reduce the amount subject to estate tax at her death by the amount of her contribution to L that was treated as a gift because of the application of section 2701. The reduction amount should be $9.9 million.
- Under current regulations, D’s estate will be able to use the full amount of the exclusion used to protect the 2020 contribution to L for estate tax purposes regardless of the level of exclusion in effect at her death.

UPSTREAM EXEMPTION PLANNING

UPSTREAM EXEMPTION PLANNING

- Fact pattern:
  - Client and client's husband have children and grandchildren, and they have done significant irrevocable trust planning.
  - They still have sufficient wealth consisting primarily of appreciated assets.
  - Client and husband are inclined to use their remaining gift tax and GST tax exemptions in 2020 or 2021 (to avoid a risk of losing those exemptions).
  - Client's mother is in her late 90s and lives in California.
  - Mother has not made any significant lifetime taxable gifts, and she has nearly all of her transfer tax exemptions remaining.
  - Mother does not have sufficient assets to make taxable gifts (to use her exemptions), and the value of Mother's estate does not exceed her remaining exemptions.

UPSTREAM EXEMPTION PLANNING

- The Dilemma:
  - Transferring appreciated assets to use their exemptions is beneficial to guard against the loss/reduction of those exemptions.
  - However, transferring appreciated assets to an irrevocable trust may result in a loss of a stepped-up basis for those assets.
- The (general) Plan:
  - Client transfers assets to an irrevocable grantor trust.
  - Client's gift is split with client's husband, using both spouses' remaining gift and GST exemptions.
  - Initial beneficiaries of trust are client's descendants and Mother.
  - Mother is given a contingent general power of appointment over the trust, exercisable at her death.

UPSTREAM EXEMPTION PLANNING

- The Trust Terms:
  - Trustee is authorized to make distributions to client's descendants and Mother under HEMS standard, and an independent trustee is authorized to make distributions under a broader standard.
  - At Mother's death, she is permitted to appoint assets to her estate and/or creditors.
  - Mother's testamentary GPA would be made contingent so that:
    - The GPA would not result in Federal estate tax or state death taxes in Mother's estate; and
    - The GPA assets would not exceed Mother's remaining GST exemption.
  - Any unappointed assets would be allocated to separate long-term trusts for client's children and their descendants.

UPSTREAM EXEMPTION PLANNING

- Estate Tax and GST Tax Results:
  - To the extent Mother's GPA is applicable:
    - Those assets are included in Mother's estate for estate tax purposes, but there will be no estate tax consequences as a result of Mother's remaining exemption.
    - For GST purposes, Mother becomes the "transferor" with respect to the assets included in her estate for estate tax purposes.
    - Accordingly, Mother's remaining GST exemption can be applied to the portion of the trust subject to the GPA.

UPSTREAM EXEMPTION PLANNING

- Income Tax Results:

  To the extent Mother's GPA is applicable:

  - Assuming the assets included in Mother's estate are appreciated assets, those assets will receive a stepped-up basis for income tax purposes.
  - The trustee could then sell those assets without gain recognition.
  - The substitution power causes the trust to be treated as a grantor trust as to client.
  - If Mother does not exercise the GPA, the client should remain the "grantor" of the trust for income tax purposes, even though Mother becomes the "transferor" for transfer tax purposes.

UPSTREAM EXEMPTION PLANNING

- Why use clients' GST exemption?
- Couldn't clients just use their gift tax exemption to create the new trust, preserve their GST exemption, and rely on Mother's GPA to create a GST exempt trust at Mother's death?
- What about GRAT planning to set aside the initial trust?
- Uncertain timing as to the level of exemptions going forward may lead clients to use their gift and GST exemptions for this planning.
  - If not, the uncertain timeline with respect to changes in the exemptions could mean that Mother's exemptions will have been reduced prior to her death.
  - If that were to happen, the basis step-up ultimately may not be achieved as intended, but the trust still would be GST exempt.

GIFT TO CHARITY OF A REMAINDER INTEREST IN A RESIDENCE OR FARM

GIFT TO CHARITY OF A REMAINDER INTEREST IN A PERSONAL RESIDENCE OR FARM

- Statutorily sanctioned transaction whereby a donor transfers a remainder interest in a personal residence, farm or ranch to charity – not in trust, but directly to the charity.
- Donor retains the right to reside in the residence for life or a term of years, after which the charity becomes the full owner of the property.
- During that term, the donor continues to pay all the expenses the donor previously paid, just as if the transfer never took place.
- Under specific statutory exceptions to nondeductibility of partial interests, the donor obtains gift tax and income tax deductions for the value of the charitable remainder interest:
  - Income Tax – IRC §170(f)(3)(B)(i), and
  - Gift Tax – IRC §2522(c)(2).

GIFT OF REMAINDER INTEREST TO CHARITY – WHY NOW?

- Although the personal residence remainder gift has been available forever, it has not been used much, so why now?
- The answer is the current, historically low 7520 rate that is used to calculate the value of the charitable remainder.
- Low 7520 rates mean the value of a retained life estate is worth less and the value of the deductible remainder interest is worth more now than ever.

CALCULATING THE CHARITABLE DEDUCTION

- The donor’s federal income tax deduction for the remainder gift is equal to the charity’s actuarial interest in the property.
- The actuarial interest is dependent on several factors:
  - Value of the land on which the residence sits.
  - Value of the residence.
  - Useful life of the residence.
  - Salvage value of the residence at the end of its useful life.
  - Donor’s age at the time of the gift.
  - IRS 7520 rate at the time of the gift.

WHO IS THIS FOR?

- Who is this for?
- Clients who have committed to charity in their testamentary estate plans.
- Those clients can consider this a prepayment on that commitment, with the big benefit of obtaining a current income tax deduction that is not available for the charitable gift at death.
- Older clients – both because the charitable deduction is larger and because they are more likely to be able to envision and be comfortable with how the arrangement will play out over the balance of their lives – not planning to sell . . .

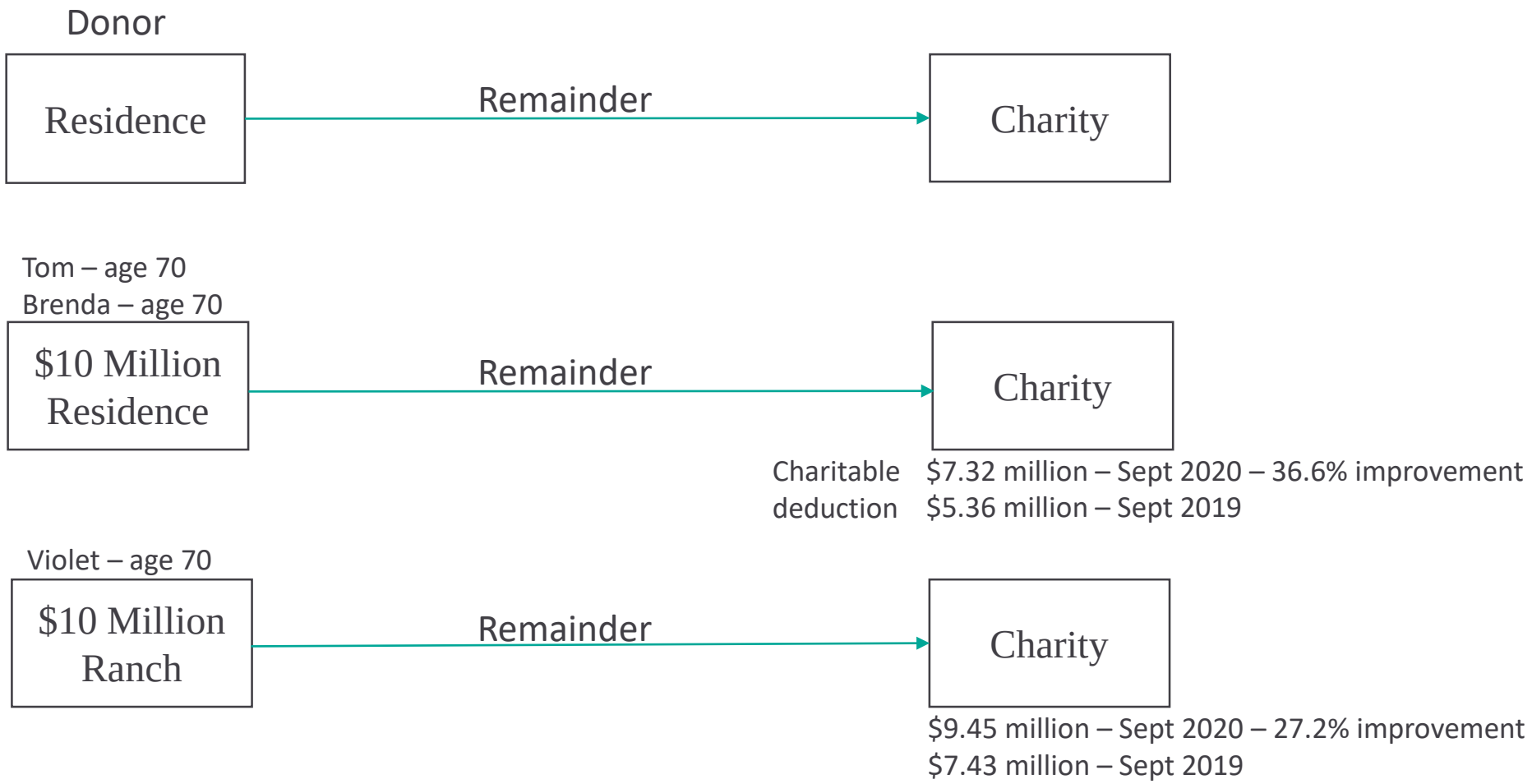
EXAMPLE – TOM & BRENDA – AGE 70

- Tom and Brenda – both age 70.
- Home appraised at $10 million – half structure and half land.
- Appraiser says the house has a useful life of 35 years after which it will have a residual value of 20% or $1 million.
- Tom and Brenda transfer the remainder interest to their alma mater, retaining the right to live in the residence rent-free until the second of them dies, subject to their continuing obligation to pay real estate taxes and all other expenses.
- Based on these facts and today's 0.4% 7520 rate, the charitable deduction is $7.32 million (73.2% X current value).
- If the 7520 rate from a year ago – 2.2% – applied today, the deduction would have been only $5.36 million – meaning the deduction today has increased about 36.6% since last year.
- If Tom and Brenda were both 80 today instead of 70, the deduction would jump from $7.32 million to $8.30 million.

EXAMPLE – VIOLET – AGE 70

- Violet, age 70, owns a cattle ranch worth $10 million (exclusive of the minimal improvements and the cattle).
- Violet transfers the ranch to her alma mater, retaining the right to possession of the ranch during her lifetime.
- Based on these facts and today's 0.4% 7520 rate, the charitable deduction is $9.45 million (94.5% X current value).
- Where only land is involved, there is no depreciation in value that reduces the charitable deduction.
- If this gift had been made with last year's 2.2%, the charitable deduction would have been $7.43 million – transacting now results in about a 27.2% improvement from last year.
- If Violet were 80 rather than 70 today, the charitable deduction would be 96.7%!

GIFT OF REMAINDER IN PERSONAL RESIDENCE TO CHARITY



OTHER “FUN FACTS” ABOUT GIFT OF REMAINDER

- Gift of long-term capital gain property deductible up to 30% of contribution base; 5 year carryover of excess.
- Any “residence” means any property used as a residence by the taxpayer as a personal residence even if not the principal residence – so a vacation residence qualifies.
- In applying the 7520 rate, there is an optional 2 month look back – use the current month or either of the two (2) preceding months – select the lowest 7520 rate.
- Capital expenses – contribute cash or other assets to charitable remainder beneficiary.
- Love no out-of-pocket cost for income tax charitable deduction – “nothing changes” except the tax benefit jingle in the donor’s pocket.

BONUS SLIDE

- Create a long-term CLAT today!
- Capitalize on the huge difference between how the charitable lead interest is valued at today's 0.4% and how it's valued based on expected investment return over many years

Charitable Lead Annuity Trust

7520 Rate for transaction	0.4%					
Term	30					
After income tax growth rate		3%	5%	7%	10%	12%
Principal		10,000,000	10,000,000	10,000,000	10,000,000	10,000,000
Zero out Annuity		354,399	354,399	354,399	354,399	354,399
Value annuity @ growth rate		6,946,377	5,447,978	4,397,749	3,340,887	2,854,748
Gift tax free gift to noncharitable remaindermen		**3,053,623**	**4,552,022**	**5,602,251**	**6,659,113**	**7,145,252**
Future value gift tax free to noncharitable remaindermen		**7,411,945**	**19,673,576**	**42,645,761**	**116,197,539**	**214,071,208**

THANK YOU

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