

**CHARITABLE PLANNING:
RETIREMENT ASSETS & IRAs**

BIG 12 CONFERENCE

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THE NEW ADMINISTRATION

| | <u>Democrats</u> | <u>Republicans</u> | <u>?</u> |
|-------------|------------------|--------------------|----------|
| White House | 1 | 0 | |
| House | 257 | 178 | |
| Senate | 56 | 41 | 3 ? |

FUTURE OF ESTATE TAX ?

| <u>Year</u> | <u>Threshold</u> |
|-------------|-------------------|
| 2001 | \$ 675,000 |
| 2002-2003 | \$ 1,000,000 |
| 2004-2005 | \$ 1,500,000 |
| 2006-2008 | \$ 2,000,000 |
| 2009 | \$ 3,500,000 |
| 2010 | REPEALED ! |
| 2011 | \$ 1,000,000 |

Obama Proposed Estate Tax

- Freeze estate tax threshold at \$3.5 million in the year 2010
- Top federal estate tax rate to stay at 45%
- Portability ?

Federal Estate Tax Returns Filed

| | | |
|------------|---------|------------|
| 2010 (est) | 14,300 | 25% charit |
| 2007 | 38,000 | 20% |
| 2004 | 62,700 | 18% |
| 2001 | 108,000 | 17% |
| 1998 | 97,900 | 17% |
| 1995 | 69,780 | 19% |
| 1992 | 59,200 | 19% |

THE YEAR 2010: The “Perfect Storm” for Taxes

Maximum Tax Rates 2008-2010 2011

| | | |
|------------------------|--------------|-------------|
| ■ Ordinary Income | 35% | 39.6% |
| ■ LT Capital Gains | 15% | 20% |
| ■ Dividends | 15% | 39.6% |
| ■ Estate Tax – 2008-09 | \$2 to \$3.5 | \$1 million |

(Estate tax is repealed in 2010)

THE YEAR 2010: ROTH IRA CONVERSIONS

- In 2009, if income is under \$100,000, a person can convert a regular IRA into a Roth IRA
- In 2010, there is no income limit

THE YEAR 2010: ROTH IRA CONVERSIONS

ADVANTAGES OF ROTH IRAs

- After 5 years, all withdrawals after age 59 ½ or after death are exempt from income tax
- Unlike regular IRAs, no mandatory lifetime distributions after age 70 ½
- Shrinking estate may reduce estate tax

ROTH IRA CONVERSION & MAJOR CHARITABLE GIFT

- A Roth IRA conversion is a taxable event; the amount converted is included in taxable income
- **PLANNING STRATEGY:** Make a very large charitable gift to produce an offsetting charitable income tax deduction, preferably with appreciated stock. Consider philanthropy: a private foundation or donor advised fund that can make many smaller grants in future, yet tax deduction in 2010 to offset Roth conversion

PLANNED GIVING 101

Lifetime Gifts -- Bequests

**USUALLY BEST SOURCE OF A
LIFETIME GIFT:**

**APPRECIATED STOCK or
APPRECIATED REAL ESTATE**

**USUALLY BEST SOURCE OF A
BEQUEST: RETIREMENT PLAN**

DONORS LIKE TO CONTRIBUTE APPRECIATED STOCK

DOUBLE-TAX ADVANTAGE

- Charitable Income Tax Deduction for the Full Appreciated Value of the Stock
- Never Pay Income Tax on the Growth of the Value of the Stock
- *Loss Property?* Sell for tax loss; give cash
- *Retirement Accounts While Alive?* Taxable income

Charitable IRA Rollover

-- Lifetime Gifts from IRAs --

- Pension Protection Act of 2006
- Eligible Donors:
 - Won't report charitable gifts from IRAs as taxable income
 - Not entitled to charitable income tax deduction

Charitable IRA Rollover

-- Lifetime Gifts from IRAs --

- IRA owner must be over age 70 1/2
- Maximum: \$100,000 per year
- Yes! Charitable gift satisfies required minimum distribution requirement from IRA!

2009: ONE YEAR WAIVER OF REQUIRED IRA DISTRIBUTION

- Worker, Retiree, & Employer Recovery Act of 2008
- **Impact on charitable giving from IRAs:** donors who were motivated to give to avoid taxable income from required IRA distributions have less *tax* incentive to donate in 2009
- **Donors who believe in the charitable mission of an organization will still donate**

WHO WINS, EVEN IN 2009 ?

- Donors who do not itemize tax deductions (“standard deduction”)
- Donors who live in states where state income tax laws have no charitable deduction

WHO WINS, EVEN IN 2009 ?

- Donors subject to annual charitable deduction limitation (50% of AGI)
- Wealthy individuals who want to reduce the proportion of retirement assets in their estates

WHO HAS LESS TAX INCENTIVE IN 2009 THAN 2008?

Donors who were motivated to donate required IRA distributions to charity to avoid increased taxable income:

- Donors who lose tax deductions as income increases (income $>$ \$160,000)
- Donors on threshold of A.M.T.

Will Law Be Extended to 2010?

Proposed: Public Good IRA Rollover Act of 2007

Expand law to include deferred gifts; DAFs; SOs

**Planning strategy for 2010 if,
like in 2008,**

law hasn't been extended until October:

>> Give RMD to charity; can't lose.

(Some IRAs balk)

Will Law Be Extended to 2010?

If law expires:

- Urge donors to prepay future pledge commitments if they will save taxes
- Consider use of “designated funds” (not donor advised funds) at community foundations to hold planned future distributions.

OTHER LIFETIME USE OF IRA: MAKE A LOAN TO CHARITY

- PLR 200741016
- -- Loan to charity from IRA at market rates not a “prohibited transaction”
- -- OK for charity to use loan proceeds to purchase life insurance on life of donor
- Financing tool for charitable purposes, too?
- Practical tip: Use “self-directed” IRA

BEQUESTS FROM QRPs

- Best type of bequest: taxable income !
- Easier than formality of a will: Name charity as beneficiary on form of plan
 - no need for attorney to draft
 - no need for witnesses, etc.

“You can’t make a charitable bequest unless you have a will”

Wrong. A retirement plan is a trust with its own beneficiary designations. Like other trusts, assets can pass outside probate.

Name a charity as a beneficiary

- the cheapest “charitable remainder trust”

TYPES OF QRRs

- 1. Sec. 401 – Company plans
- 2. Sec. 408 – IRAs
 - SEP & SIMPLE IRAs
- 3. Sec. 403(b) & 457–Charities
- 4. Roth IRAs & 401(k)/403(b)

WHAT CAN GO WRONG?

- Other beneficiaries cannot do stretch IRAs if charity is beneficiary?
- Solutions:
 - * cash out charity's share by Sept 30
 - or
 - * separate account for charity

REQUIRED MINIMUM DISTRIBUTIONS

LIFETIME DISTRIBUTIONS

| <u>Age of Account Owner</u> | <u>Required Payout</u> |
|-----------------------------|------------------------|
| 70 1/2 | 3.65% |
| 75 | 4.37% |
| 80 | 5.35% |
| 85 | 6.76% |
| 90 | 8.75% |
| 95 | 11.63% |
| 100 | 15.88% |

REQUIRED MINIMUM DISTRIBUTIONS

LIFE EXPECTANCY TABLE

| <u>Age of Beneficiary</u> | <u>Life Expectancy</u> |
|---------------------------|------------------------|
| 30 | 53.3 more years |
| 40 | 43.6 |
| 50 | 34.2 |
| 60 | 25.2 |
| 70 | 17.0 |
| 80 | 10.2 |
| 90 | 6.9 |

REQUIRED MINIMUM DISTRIBUTIONS

LIFE EXPECTANCY TABLE

| <u>Age of Beneficiary</u> | | <u>Life Expectancy</u> |
|---------------------------|--------------|------------------------|
| 30 | 1.9% | 53.3 more years |
| 40 | 2.3% | 43.6 |
| 50 | 2.9% | 34.2 |
| 60 | 4.0% | 25.2 |
| 70 | 5.9% | 17.0 |
| 80 | 10.0% | 10.2 |
| 90 | 14.5% | 6.9 |

REQUIRED MINIMUM DISTRIBUTIONS

** DEFINITIONS **

- **Required Beginning Date (“RBD”)**
April 1 in year after attain age 70 ½
- **Designated Beneficiary (“DB”)**
A human being. An estate or charity can be a beneficiary of an account, but not a DB.
- **Determination Date**
September 30 in year after death.

WHAT CAN GO WRONG ?

- Other beneficiaries cannot do stretch IRAs if charity is beneficiary?
- Solutions:
 - * cash out charity's share by Sept 30
 - or
 - * separate account for charity

WHAT CAN GO WRONG #2 ?

TWO WAYS TO MAKE A CHARITABLE BEQUEST FROM A RETIREMENT ACCOUNT

- #1 – NAME CHARITY AS BENEFICIARY OF THE ACCOUNT
- #2 – PAY ACCOUNT TO ESTATE OR TRUST THAT THEN MAKES A CHARITABLE BEQUEST

WHAT CAN GO WRONG #2 ?

Estate or trust has taxable income from receiving IRA distribution, but maybe there is no offsetting charitable income tax deduction when the IRA check is given to a charity.

WHAT CAN GO WRONG?

- IRS Chief Counsel Memorandum ILM 200848020
- Decedent left his IRA to a trust that benefited his six children and several charities
- Trust received cash from IRA; paid entire charitable share, leaving the six children as the only remaining beneficiaries of the trust.
- IRS: “Taxable income from IRA, but no charitable deduction.” Reason: trust had no instructions to pay income to charities

WHAT CAN GO WRONG?

- Solution #1 – Keep IRD off of estate’s/trust’s income tax return
 - a. Name charity as beneficiary of IRA
 - b. “Distribute” IRA to charity if document allows

Caution: IRS memo on danger of using retirement accounts to satisfy pecuniary bequests p.41

WHAT CAN GO WRONG?

SOLUTION #2 – draft document to get an offsetting charitable income tax deduction in case estate or trust has income

- *I instruct that all of my charitable gifts, bequests and devises shall be made, to the extent possible, from "income in respect of a decedent"*

2008 – PROPOSED REGULATION

-- Confusion over sanction --

Instructions to distribute specific types of income to a charity or to some other beneficiary will not be respected for federal tax purposes unless the instruction has an “economic effect independent of income tax consequences”

Reg. Sections 1.642(c)-2(b) contained in REG-101258-08, 2008-28 I.R.B. 111

WHAT IF NO “ECON EFFECT”?

- Sanction under Proposed Regulation: “estate's or trust's income will be allocated between charitable and non-charitable beneficiaries using the same proportionate ratio of all classes of income of the estate or trust”
- Proposed Regulation does not address whether a charitable income tax deduction will be allowed, denied or partially allowed/denied