Vol. 34 No. 5
May 2002

Give & Take

News and Ideas for Development Executives of Nonprofit Organizations

Helping Donors Make the Most of Their Gifts in 2002

by Robert F. Sharpe, Jr.

Gifts of appreciated securities and other assets have been a mainstay of many development programs. During the boom times of the 1990s, significant gifts were often made from the portfolios of those who had benefited from markets that could only seem to go up. The message to donors was simple—give appreciated assets. Why? To make gifts while avoiding capital gains tax, the bane of every investor's existence, and in so doing to give away so-called "paper profits." This message had a certain appeal to many who had experienced large gains in hot investment markets, and many charities thus benefited from the "wealth effect" that also helped fuel growth in other sectors of the economy.

Join us for the Major Gift Planning I seminar in Washington, D.C., May 30-31. See page 7 for details.

Back to basics

Now, however, given the different environment we live and work in, we may need to consider adjusting our thinking, as well as the information we provide our donors about gifts of appreciated assets. As donors are increasingly taking a hard look at what they can afford to give, we must show them how to make gifts in the most economical ways. All too often we focus on tax avoidance and the desire to reduce tax bills alone when perhaps we should be emphasizing how tax savings actually help reduce the cost of gifts donors would like to make.

For example, if a donor is in the 38.6% tax bracket for federal tax purposes and gives $1,000 in cash, the "after-tax" cost of the gift is $614, yielding tax savings of $386. On the other hand, suppose the same donor owns securities worth $1,000 that cost only $250 six years ago. If the securities are given, the donor will save $386 in federal taxes, the same amount saved with the cash gift. But the donor also avoids payment of capital gains tax on the $750 increase in value, thereby saving as much as $150 in the 20% capital gains tax bracket. The total tax savings would then be up to $536, reducing the net cost by nearly 25%, to $464.

While the above math may be obvious to experienced development officers, how many donors really understand this? I once met a wealthy entrepreneur who had sold stock in his company to generate cash to make significant gifts for many years before a representative of one of his charitable interests finally asked him why he was giving cash instead of securities. The donor was understandably annoyed about the huge sums he had paid in unnecessary capital gains taxes over the years. The moral of the story is this: Don't assume that donors are experienced gift planners. They may need help in choosing the best asset to use to fulfill their gifts.

It is hard to imagine a case in which a donor would be better served by making a gift of $10,000 in cash instead of $10,000 in appreciated securities.

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- Exploring the possibilities of appreciated bonds p.2
- The two year-ends: anticipating the close of the fiscal year p.3

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"Bonding" with planned giving donors

Planning Matters

Over the years, many donors have enjoyed the satisfaction of establishing a gift annuity or charitable remainder trust with highly appreciated, low-yielding securities. More often than not, publicly traded stocks, real estate, and/or cash have been used to fund such gifts.

Today's economic environment can still be very attractive for life income gifts and may also favor another funding source—appreciated corporate and government bonds.

Taking bonds into account

In periods of stable interest rates, bond prices tend to be stable as well. However, as interest rates rise and fall, bond values can also be expected to fluctuate in a countercyclical fashion. As interest rates fall, the value of a bond goes up. Similarly, as rates increase, the value of a bond goes down, assuming other factors that bear on valuation remain the same.

Some trustees learned this lesson the hard way with net income variations of the charitable remainder unitrust that were, unfortunately, sometimes heavily invested in bonds in the late 1970s and 1980s. As interest rates rose to record levels, the market price of those bonds plummeted far below face value. Income beneficiaries then saw the amount of their unitrust payments decline, even though their trusts continued to receive the same level of bond income.

For example, if a 5% net income unitrust were invested in high quality bonds yielding 6%, the trust would appear to have no problem making the required 5% payment each year. In fact, the trust would potentially grow each year as a result of the excess interest being added to the trust corpus. If, on the other hand, interest rates rose to 12%, the market value of the bonds could be expected to fall by approximately 50%. If the trust were initially valued at $1 million, the annual payment would be $50,000 (5% of $1 million). If the market value of the bond portfolio fell to $500,000, the payments would fall to $25,000 (5% of $500,000) even though the bonds still generated $60,000 in interest that year. In this case, income would essentially be "trapped" inside the trust.

Conversely, another problem can occur if interest rates fall dramatically and the value of the bond portfolio *increases* in value. If the trust were a straight payment unitrust, the payee would be required to distribute not only the income but also a portion of the principal each year with potentially negative impact on future performance of the trust. In the example above, suppose the prevailing interest rates fell to 3% and the value of the bonds doubled to $2 million. The unitrust payment would then be $100,000 (5% of $2 million) while the interest income would still be $60,000, necessitating a $40,000 encroachment on the gain in the value of the trust principal.

Because of the havoc bond fluctuations can potentially wreak on unitrust payments, in recent years there has been a trend toward investing charitable remainder trust assets in portfolios more balanced between debt, equity, and cash designed to produce more stable total returns over time and "flattening" distributions accordingly.

During the 2001-2002 period we have seen interest rates of all types fall dramatically. The Federal Reserve Bank has cut interest rates charged to banks 11 times in an attempt to keep the economy from falling into an extended recession.

Many believe it is unlikely, however, that interest rates will fall much further. Indeed, history tells us it is more likely that interest

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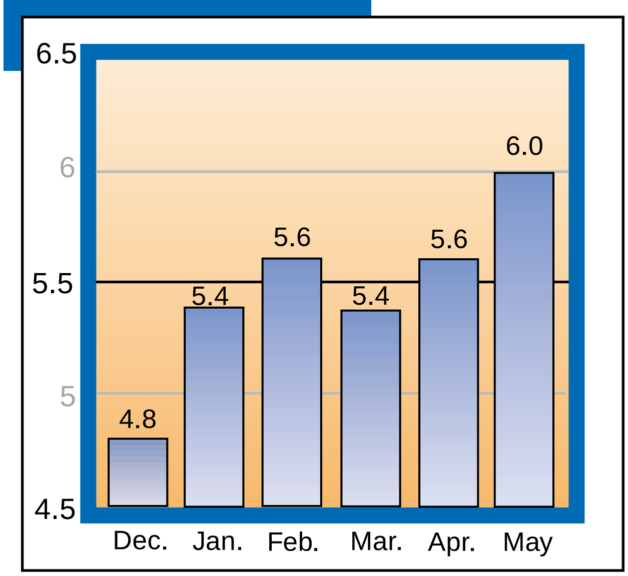
Discount Rates



Trend in applicable federal mid-term rates (AFMR's), which are used in calculating tax benefits of planned gifts.

Give & Take:

A client service publication published monthly since 1968 by Robert F. Sharpe and Company, 6410 Poplar Avenue, Suite 700, Memphis, TN 38119, (901) 680-5300. Fax (901) 761-4268.

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Year-End Comes but Twice a Year

by Barlow T. Mann

While most fundraisers are aware of the importance of the last few months of the calendar year to their fundraising efforts, they may not have considered how critical the fiscal year-end can be to their fundraising programs.

The success or failure of one's efforts is ultimately evaluated on the fiscal year-end rather than the calendar year-end.

While different charities have different fiscal years, the June 30/July 1 end and start dates are the most commonly used. This may mean that actions taken in May and June may be especially important to help assure a strong finish for fundraising programs that were negatively affected by the turmoil in the fall of 2001.

Preparing for fiscal year-end

This spring you may want to carefully review your fundraising appeals and segment solicitation letters based upon giving history. For the masses of donors, special attention should be given to people that have given in the past but have not made a contribution during the current fiscal year, especially those whose giving patterns may have been disrupted last fall. Remind them of their prior support and let them know that they still have until June 30 to be counted as part of this year's efforts. For larger prospects, consider personal calls or visits. Also make sure that pledge reminders are sent in time for people to respond in the current fiscal year. Acknowledgment inserts may attract additional gifts as well.

On the planned giving side, there are also steps that can be taken to improve your fiscal year-end results. Examine your open estate files and call or write the attorneys, executors, or trustees to close estates and expedite trust terminations. Carefully review all planned giving proposals that have been made over the previous year, and implement a reminder system for open proposals. Gift annuities, annuity trusts, lead trusts, and life estate agreements may all look more appealing today than they did a year ago.

Consider additional planned gifts from your expectancy list. In recent years there has been an increase in the number of donors that have multiple gift annuities. Remember that charitable remainder unitrusts can accept additional contributions. You may also want to seek referrals from individuals who are pleased with their planned giving arrangements. Finally, offer wills, gift, and estate planning seminars this spring, as milder weather and more daylight hours may boost attendance.

Do not forget to examine your budget and other plans and make any necessary adjustments for the coming July 1 fiscal year. Depending on the circumstances, you may find funds available that would otherwise be lost unless expended before the fiscal year ends.

Properly utilized, the fiscal year provides gift planners a second chance to finish the year on a positive note. G&T

What can you do to boost giving before the fiscal year-end?

ACGA Rates Remain Unchanged

At its April meeting, the American Council on Gift Annuities board voted to leave the recommended gift annuity payment rates unchanged except for the following instances: persons under the age of 39 for single-life annuities and persons under 57 for two-life agreements. All publications produced by Robert F. Sharpe and Company remain accurate for use. For more information, see www.acga-web.org.

Helping Donors...*Continued from page 1*

Donors are sometimes reluctant to make a gift of the stock, however, because they think it may further increase in value. Other donors are heavily invested in the stock of companies that employ them and are afraid that a gift of their stock may imply they have lost confidence in the future of the company and trigger sales by others. This is an especially important consideration today when many companies are urging employees to "keep the faith."

Don't assume that your donors are experienced gift planners.

There is a simple solution to the above concerns. In either case, donors should make their gifts in the form of stock and then use cash they might otherwise have given to repurchase shares of the same stock. That way, they realize additional savings from a gift of securities by avoiding capital gains tax, but when the dust settles they still own the security and enjoy a new, higher cost basis. If the security goes up in value from that point, the donors would have less gain to report if they sold it. If the value of the investment declines, they would realize a loss for tax purposes at sale, instead of perhaps just less gain if they had held the security and sold it after it had declined in value.

The strategy outlined above is not widely understood by donors for one important reason: Charities and/or their advisors too often fail to tell them about it. Now is the time to share this idea with your donors. There has not been a time in recent memory when more persons have held more appreciated investments but have also been so uncertain about the future direction of the market! Charitable organizations and institutions that take the initiative today by informing their donors may be surprised how much donors will appreciate the advice—and how much they may give.

The balanced sale

There is another little-understood technique for a donor who would like to make a gift while diversifying a *portion* of an investment position, all without incurring capital gains tax. Through a "balanced sale" a donor gives enough shares to generate the necessary tax savings to offset capital gains tax due on the sale of the remaining shares.

Example:

David Williams owns stock worth $20,000. He invested just $5,000 in the stock ten years ago. He believes his investment is unlikely to increase in value in future years and would like to sell it. He does not, however, want to pay capital gains tax of as much as $3,000, which would leave him with net sale proceeds of no more than $17,000.

He is also interested in making a charitable gift of approximately $6,000 while enjoying the greatest possible tax savings in his 35% tax bracket.

Through a balanced sale, Mr. Williams can accomplish both objectives by selling $14,000 worth of the security and donating the remainder, worth $6,000.

Note from the chart below that the $2,100 in tax savings he enjoys from his gift exactly offsets the $2,100 in capital gains tax due on the securities he sold.

Assuming 35% Ordinary Income and 20% Capital Gains Tax Rate	Step 1 Give $6,000 in Securities	Step 2 Sell $14,000 in Securities
Gift value	$6,000	-0-
Ordinary income tax savings	$2,100	-0-
Capital gains tax liability	-0-	$2,100
Net tax due	-0-	-0-

His tax liability on the portion of the securities sold is thus "balanced" by the tax benefit for the charitable gift portion.

Mr. Williams is able to enjoy cash proceeds of $14,000 along with the satisfaction of making a $6,000 gift—a total of $20,000 in value to him—while effectively bypassing the entire capital gains tax liability. Had he sold all of the securities, he would have netted just $17,000 after paying some $3,000 in taxes.

This case illustrates how it is possible to make a $6,000 gift at an after-tax "cost" of just $3,000 by utilizing incentives Congress has provided for those who choose to redirect a portion of their tax liability to fund charitable purposes.

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Helping Donors...*Continued from page 4*

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How to communicate

The best way for donors to learn how to make their gifts more effectively this year is for you to tell them. You may want to target the appropriate information to a select group of persons who have made cash gifts above a certain amount. You should also include persons who have made stock gifts in past years.

But how do you find stock donors if your record systems don't record the nature of property used to make gifts? If possible, search donor records for all gifts of odd amounts. For example, a gift of $3,567.34 was in all likelihood a gift of securities, as one would only write a check in this amount in very unusual circumstances.

You may also want to share information with your donors in person or via the telephone. If systems permit, consider holding all larger checks for an extra day while you call and personally thank the donors. While you are talking with them, ask them if they have considered making their gift in the form of securities. Most donors will still want you to cash the check, but some may actually give you a larger gift in the form of securities once they understand the benefit. Either way, you have made a very positive contact with your donors and shown that in challenging times you are going the extra mile to help them make their gifts in ways that are most beneficial to them.

This year can be an excellent year for charitable giving. The assets still exist, though their growth in value in many cases may be stalled. The economy may be in a "pause" mode, but don't let that affect your efforts. Go the extra mile for your donors and you may find they will do the same for you.

Editor's note: The Williams example featured in this article is reprinted from the new Sharpe publication, "A Guide To Year-End Giving 2002." Call 1-800-238-3253 for a copy or visit www.rfsco.com/yearendguide. G&T

Robert F. Sharpe, Jr., is president of the Sharpe company. He advises a number of the nation's leading nonprofits in the design and implementation of their gift planning initiatives.

Planning Matters...*Continued from page 2*

rates will gradually rise over time. Based upon these circumstances, persons that have invested heavily in bonds for income are facing a dilemma.

It may be difficult to reinvest the short-term bonds that are currently maturing to earn the same level of interest. Medium- and long-term bonds may have increased in value but pay no more income than they did originally. As a result, even though a donor's net worth may have increased, his or her spendable income may be flat or decreasing.

What to do?

One strategy to increase income, generate current tax deductions, achieve tax-free diversification, and make a charitable gift would be to select the most highly appreciated long- and mid-term bonds and use them to fund a charitable gift annuity, charitable remainder annuity trust, or unitrust.

With proper planning, it should be possible for donors with highly appreciated bond portfolios to "give out of the market" on a very advantageous basis. By using such investments to fund a gift annuity or charitable trust it is possible to lock in the appreciated value of these securities, avoid capital gains tax that would be due on the sale of the bonds, and receive very attractive rates of return based on the full value of the assets. As a bonus, a significant portion of the payments from the gift plans may be taxed at favorable capital gains rates, instead of higher ordinary income tax rates. A donor will also receive a significant income tax deduction for the charitable gift element, which may provide income tax savings in the year of the gift and for up to five additional years.

If interest rates have indeed bottomed out, now may be an ideal time to achieve the maximum benefits for donors by using bonds that are not normally thought of as "capital gain property" to fund life income gift plans. G&T

Footnotes

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News and ideas about Robert F. Sharpe and Company's services.

Looking for a way to encourage giving this year-end?

Let Robert F. Sharpe and Company's new booklet help you communicate the benefits of giving this year-end. Send your constituents "A Guide to Year-End Giving 2002." This booklet encourages your donors to give this fall by featuring a number of ideas to help them maximize their gifts while minimizing their tax burden.

"A Guide to Year-End Giving 2002" offers in-depth information and uses examples designed to help donors make the most of their gifts before the end of 2002. Since year-end is a time for outright gifts as well as more generalized estate planning, the benefits of a number of types of gifts are explored—immediate gifts of cash, appreciated and depreciated securities, and planned gifts through bequests, retirement accounts, life insurance, and living trusts.

This booklet can be an excellent addition to appeals directed to those who have made larger gifts in the past or are thought to be capable of such gifts. "A Guide to Year-End Giving 2002" can be used in a variety of ways to help your donors discover the benefits of some of the most popular giving plans as 2002 comes to a close.

Don't miss your chance to get a head start on encouraging your donors to make gifts this year-end. A copy of "A Guide to Year-End Giving 2002" is included with this month's issue of *Give & Take*. It may also be downloaded from www.rfsco.com/yearendguide.

To place your order, call 1-800-238-3253 or mail or fax the enclosed special order form to (901) 761-4268.

Look for information about our year-end brochure series designed for use with a broader range of donors in the June issue of *Give & Take*.

Flexible billing provides more choices

For many organizations and institutions, now is the time for closing out this fiscal year and beginning the process of planning for a new fiscal year. If you are facing this transition from one budget to the next, we would like to remind you about Robert F. Sharpe and Company's flexible billing options.

Sharpe flexible billing options allow you to:

- split your payments over two budget years
- make payments early while funds are still available in this fiscal year's budget
- delay billing for publications or other services you need now until funds become available in the new fiscal year

Don't let the fiscal year transitional period impede your gift planning efforts.

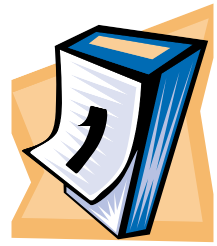
With flexible billing options, you can ensure that you will be able to secure professional products and services in a timely fashion. If you would like more information about flexible billing options, please call 1-800-238-3253 to talk with a Sharpe representative. G&T

Philanthropy in Uncertain Times

In this period of uncertain economic growth and aging donor bases, gift planners must be more innovative and informative with their donors than ever before. To continue the growth in giving many have experienced in recent years, development executives must help donors choose the vehicle that maximizes the impact of their gifts.

Robert F. Sharpe's article "Philanthropy in Uncertain Times," published in the March issue of *Trusts & Estates* magazine, explores this topic in depth. For a copy of the article, visit www.rfsco.com/current. G&T

Training Update



An Introduction to Planned Giving

For a comprehensive, in-depth training experience, consider attending Sharpe's 3-day seminar "An Introduction to Planned Giving."

Presenters Timothy Sharpe, Barlow Mann, and Phillip Adcock combine their experience to guide participants through the basics of charitable gift planning, from detailed explanations of gift planning techniques, to organizing and implementing an effective gift planning program, to communicating benefits of more effective charitable gift planning in the most efficient manner for your constituency.

Empower yourself with a wealth of gift planning knowledge that your donors will appreciate and that will help your organization or institution benefit from the unprecedented intergenerational wealth transfer that is now on the horizon. This seminar is especially helpful for those who are beginning their career in planned giving or have multiple responsibilities and are charged with incorporating gift planning capabilities into other development efforts.

Major Gift Planning I

In two concentrated, information-packed days, presenters Robert F. Sharpe, Jr., and Jonathan G. Tidd, Esq., address issues of vital importance to those charged with structuring major gifts to their organizations. By linking their knowledge and over 40 years of combined experience, Sharpe and Tidd lead participants who possess a basic understanding of gift planning tools through a comprehensive training experience designed to help them best utilize their skills in today's environment. Registration is limited to allow for more interaction among participants and instructors.

Major Gift Planning II

Designed with the more experienced gift planner in mind, "Major Gift Planning II" focuses on the skillful use of gift planning tools to help donors meet a variety of personal goals while making significant gifts. A working knowledge of various gift planning vehicles is assumed.

Instructors Robert F. Sharpe, Jr., and Jonathan G. Tidd, Esq., emphasize the impact of recent tax legislation and investment market conditions and ways to "salvage" gifts that might otherwise not be completed.

Managing Planned Giving Relationships

Someone has asked for information about a planned gift. What is the next step? How do you use the telephone, written correspondence, personal visits, and other communications in ways that are appropriate, tasteful, and effective?

These and other topics will be explored in a new seminar devoted to the process of developing and managing effective planned gift relationships. Beginning with how to handle initial requests for information, this seminar will also focus on what to do before, during, and after a personal visit.

Also included is an exploration of various ways to work most effectively with donors' advisors to help complete planned gifts.

Special attention will also be given to the process of building and maintaining relationships with the heirs of benefactors after a legacy has been received.

Presenters with decades of combined experience will share their insights regarding ways to build meaningful relationships, including helpful case studies and demonstrations of successful techniques.

Designed to complement "An Introduction to Planned Giving" and "Major Gift Planning I," this one and one-half day session follows those seminars in selected cities. Special tuition rates are available for concurrent or previous attendees of Sharpe seminars. G&T

Multiple registration discounts are available. For more information or to register, please contact the Sharpe company.
Phone 1-800-238-3253, ext. 5360
Fax 901-761-4268
Web site: www.rfsco.com
E-mail: seminars@rfsco.com

Seminar Training Dates

An Introduction to Planned Giving
Memphis
May 20-22
Washington, D.C.
June 17-19
New York
August 19-21
Chicago
September 9-11

Managing Planned Giving Relationships
Memphis
May 22-23
New York
August 21-22
Chicago
September 11-12

Major Gift Planning I
Washington, D.C.
May 30-31
Phoenix
September 5-6

Major Gift Planning II
Chicago
June 24-25