

*DEMOGRAPHICS AND
PLANNED GIVING*

Presented at

THE CHICAGO COUNCIL ON PLANNED GIVING

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By

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I. Introduction.

A. Planned giving is to a large extent driven by demographics.

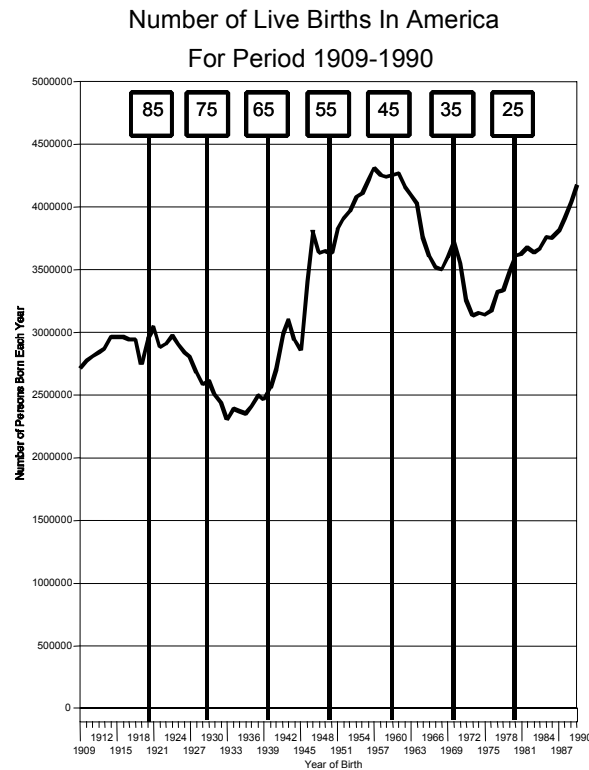
1. Age is an important factor when considering certain types of gifts.
2. Wealth is more important for other gifts.
3. In some cases both are a factor.

B. Issues related to demographic shifts will be an important determinant of growth in planned gifts in coming years and beyond.

1. The graying of America will affect fund raising along with many other aspects of our economy.
2. Those who work for nonprofits and advisors who counsel donors will need to be cognizant of the impact of demographics.

II. The age distribution of Americans is now beginning to reflect birth trends in the last century.

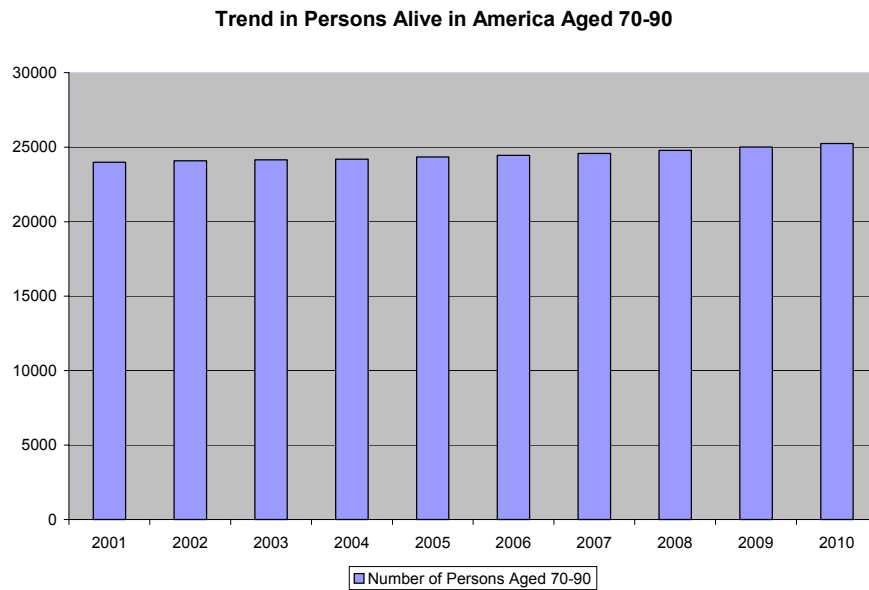
A. Note the distribution of births in America from 1909 to 1990.



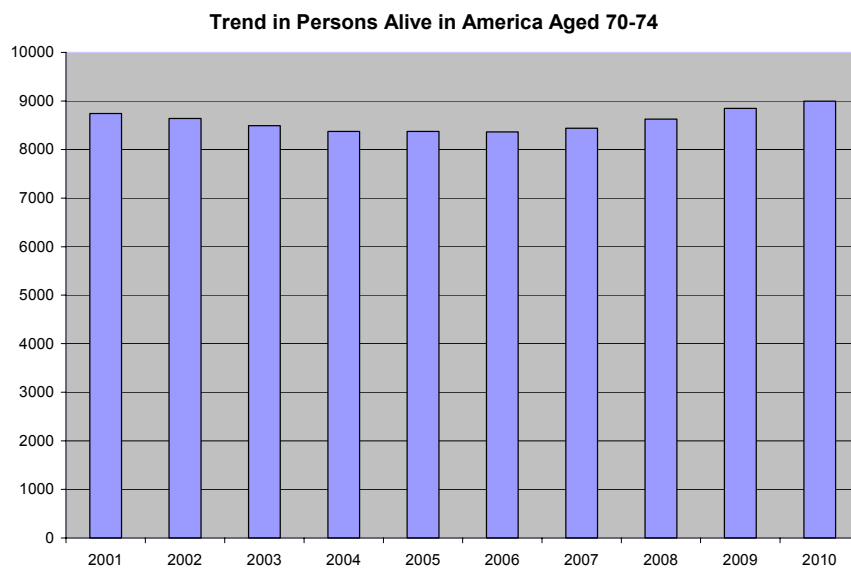
1. The “G.I.” Generation is passing away.
2. Being replaced by the “Silent Generation” and the “Baby Boomers.”

B. As a result, the number of older Americans will grow little in coming years. All data is from U. S. Census Bureau.

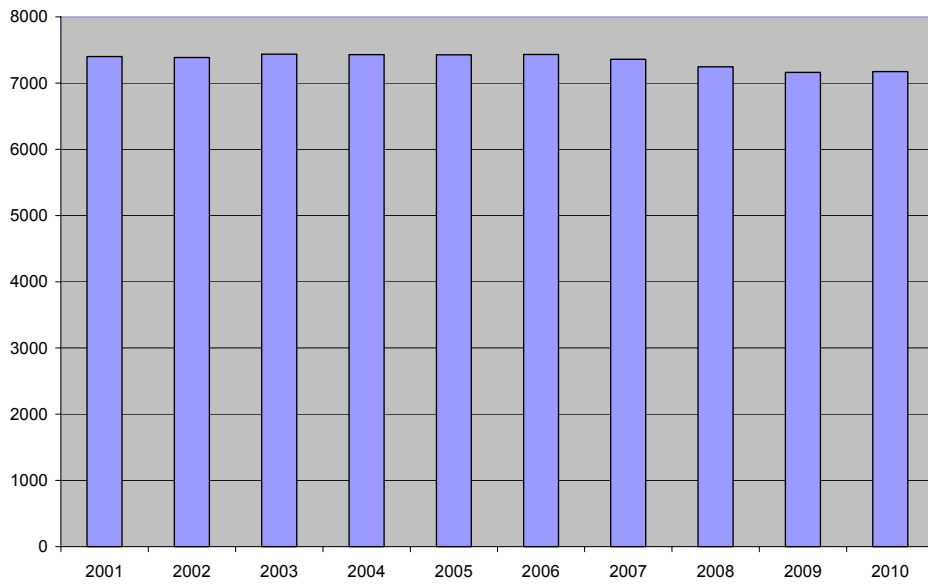
1. Trend in number of people age 70 to 90.



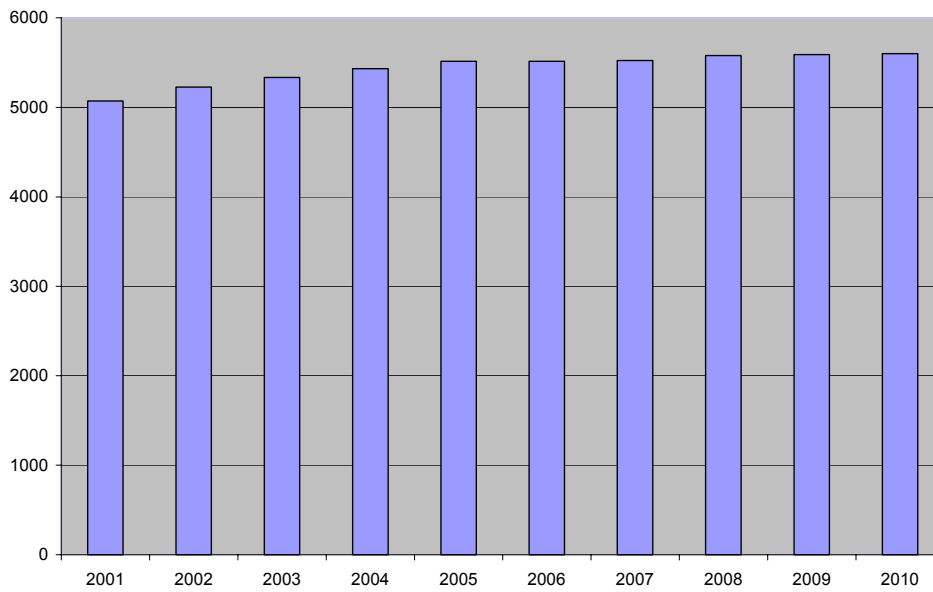
2. This can be broken down into subgroups:

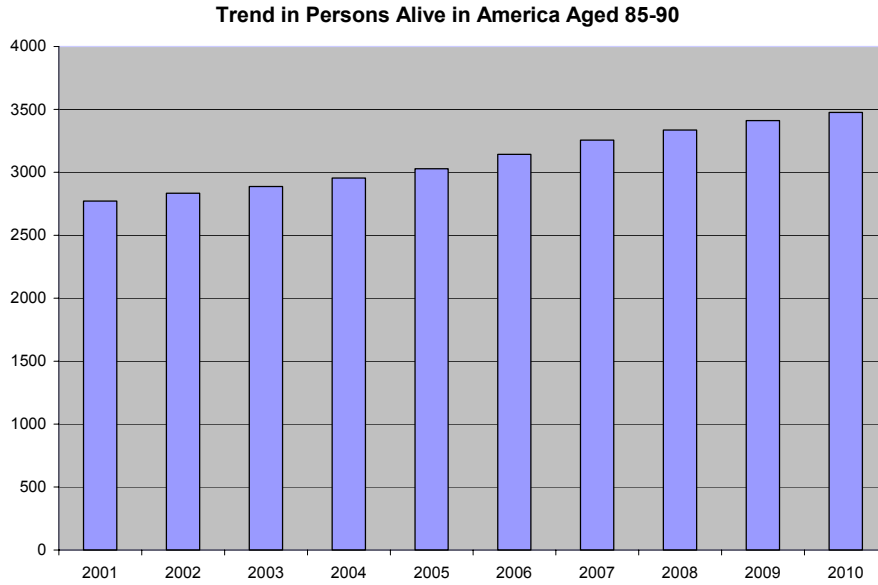


Trend in Persons Alive in America Aged 75-79



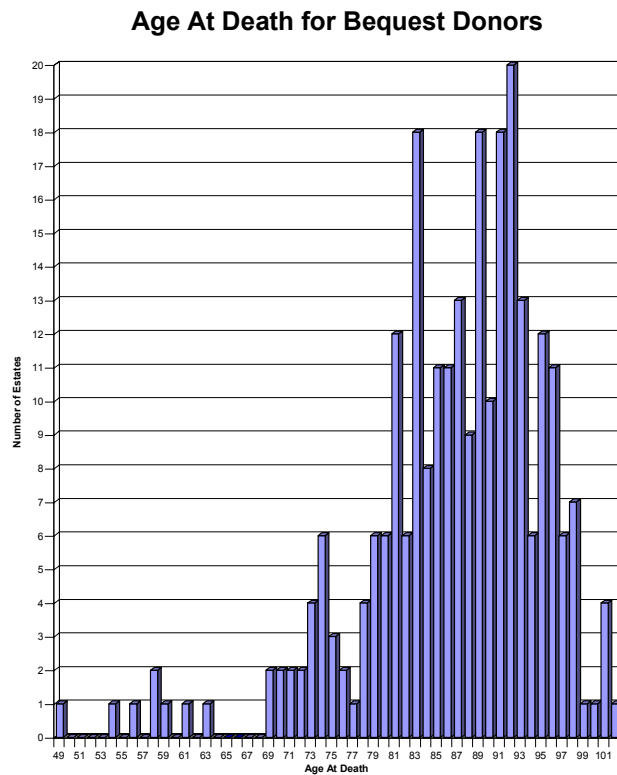
Trend in Persons Alive in America Aged 80-84



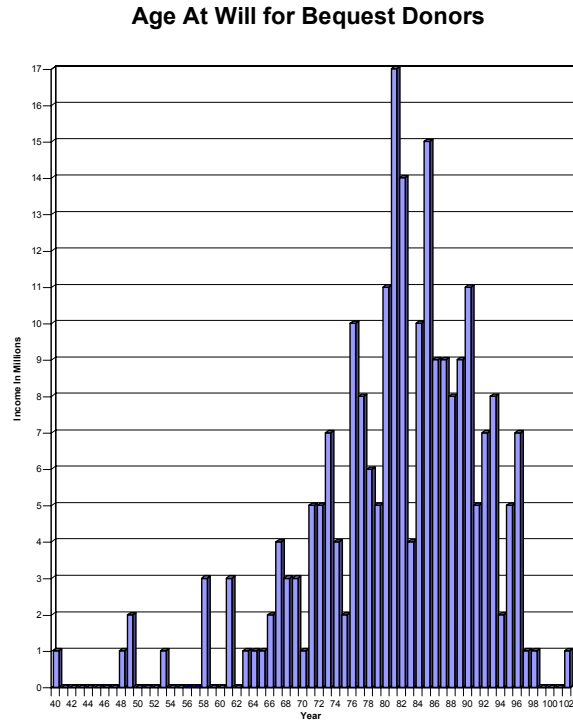


C. Impact of demographic trends on the future of bequest income.

1. Note the typical age distribution of donors who leave bequests to charity.



2. Age at time of will typically a few years younger.



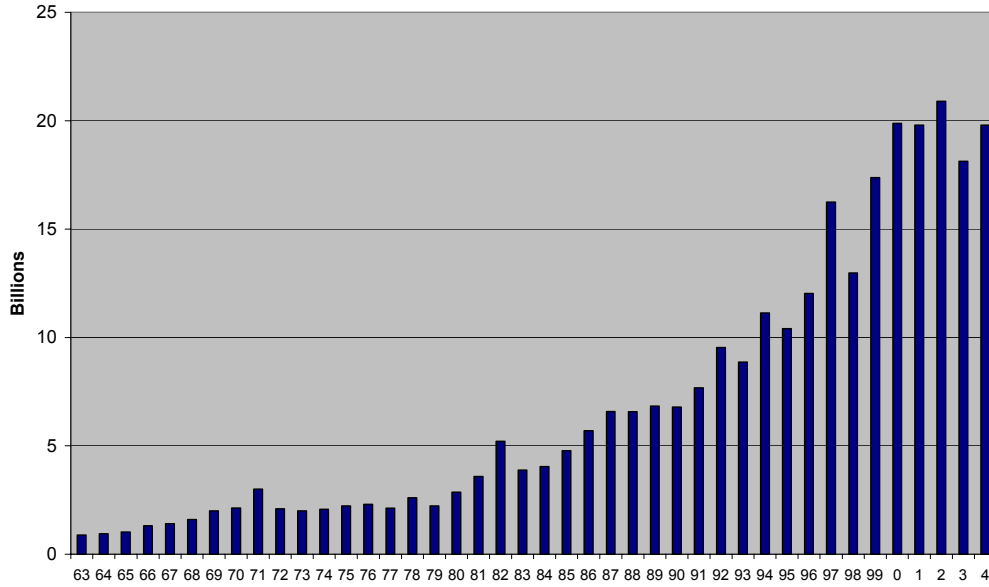
3. This doesn't normally vary more than a few years regardless of the type of organization. Note the results from the study of over 100 estates for each of 12 charities.

	Type of Organization	Age At Will	Age At Last Gift	Age At Death
1	Educational	77	81	83
2	Educational	77		86
3	Educational	77	80	83
4	Educational	79	80	83
5	Environmental	79	77	81
6	Health/Advocacy	78	81	83
7	Health	80	82	86
8	Health	79	81	85
9	Health	79	82	85
10	Health	81	83	86
11	Political Action	77	79	82
12	Religious/Relief	81	86	86
Average		78	81	84

4. Demographics may be leading to downward pressure on bequest income in recent years.

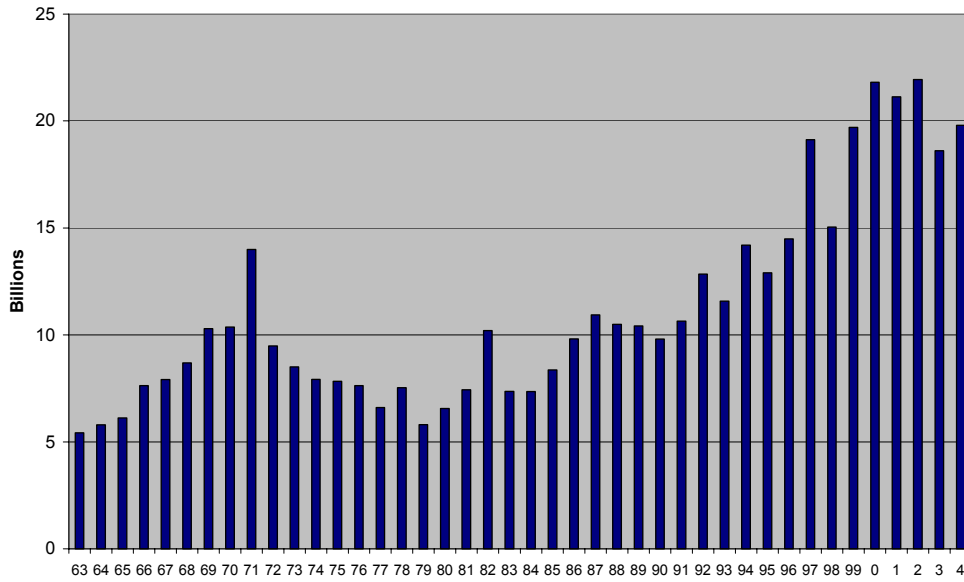
a. Note bequest income reported by Giving U.S.A. over past 40 years:

**Bequest Income Reported by GIVING USA
in Nominal Dollars**

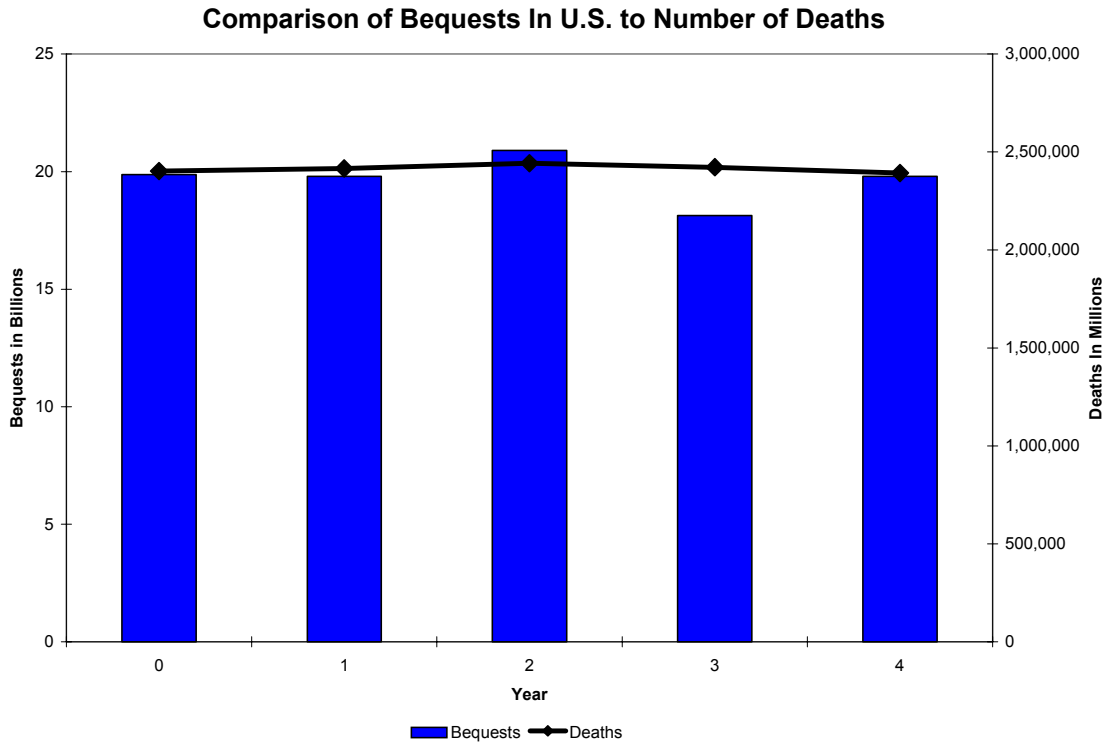


b. Trends are more evident when bequest dollars are adjusted for inflation.

**Bequest Income Reported by GIVING USA
Inflation Adjusted**



5. Number of deaths has been dropping in recent years.



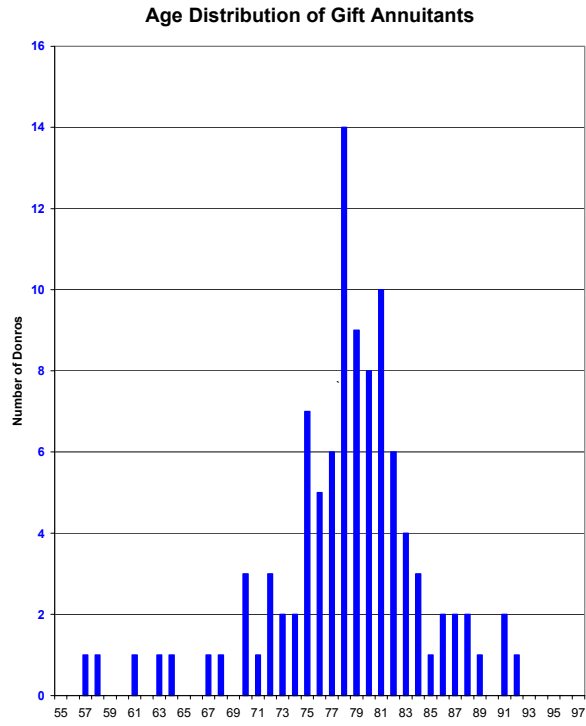
6. Other factors may also be in play.

- a. Investment market fluctuations.
- b. Estate tax repeal.
- c. Competition.

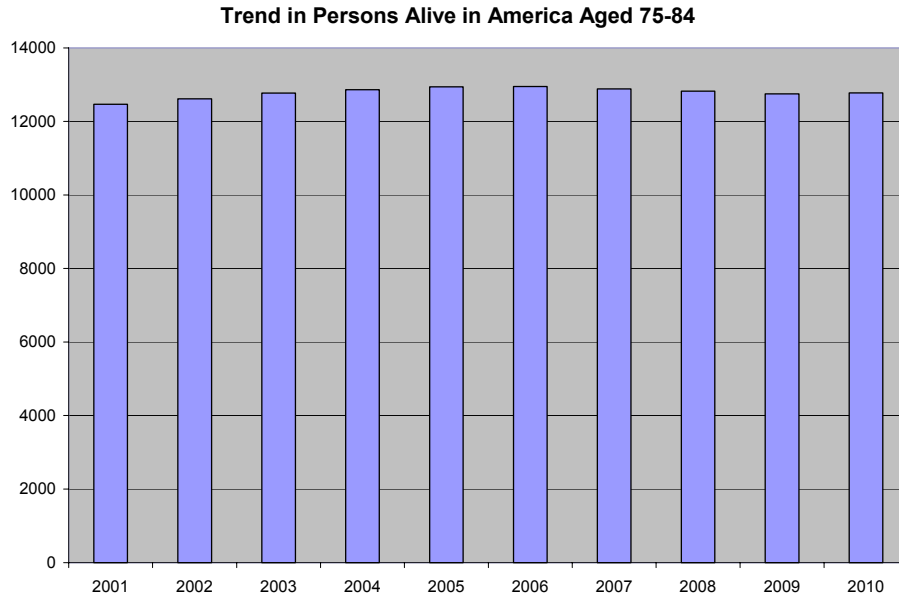
D. Impact of trends on various types of planned gifts other than bequests.

1. The ACGA has reported a large increase in the number of organizations and institutions issuing charitable gift annuities.
 - a. 1994 – 2,000 issuers of gift annuities.
 - b. 1999 - 3,000 issuers of gift annuities.
 - c. 2004 - 4,000 issuers of gift annuities.
2. According to the most recent ACGA survey, the average age of persons entering into gift annuities is 78.5.

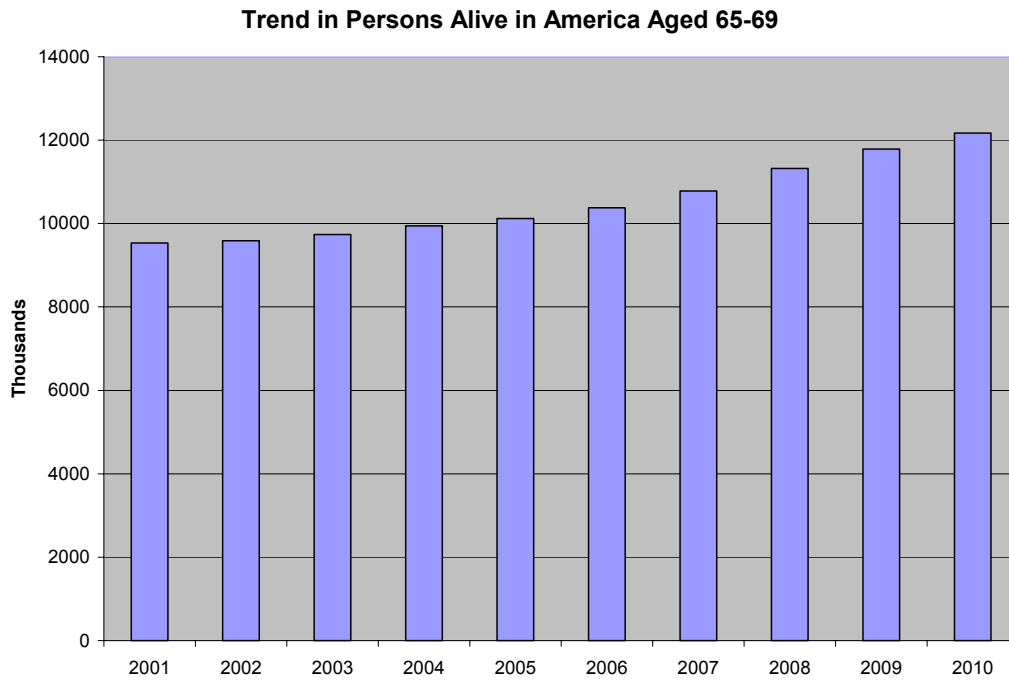
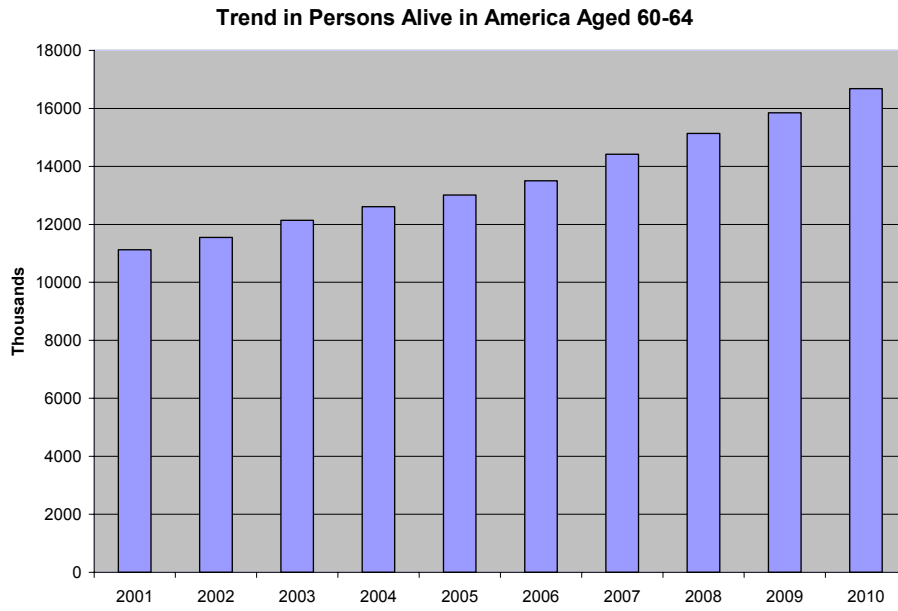
3. Note the age distribution of gift annuitants for a typical program.



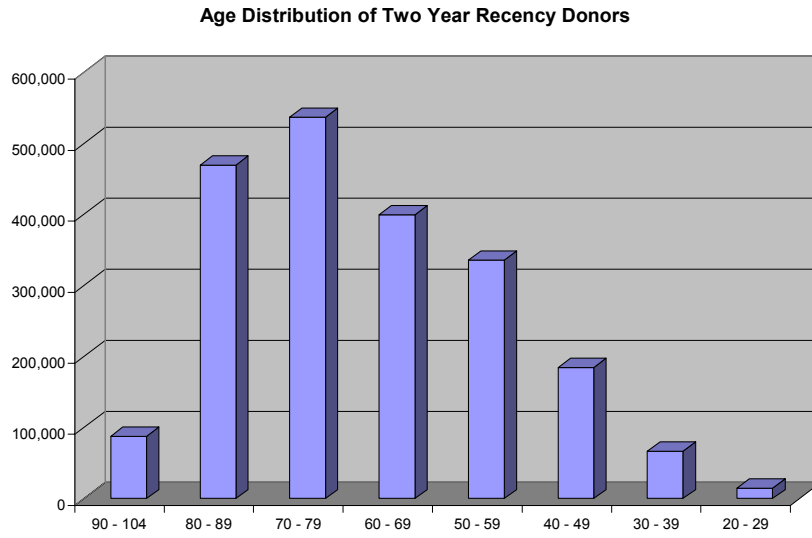
4. Most gift annuitants are in the 75 to 84 age range while the number of persons in that age range is declining.



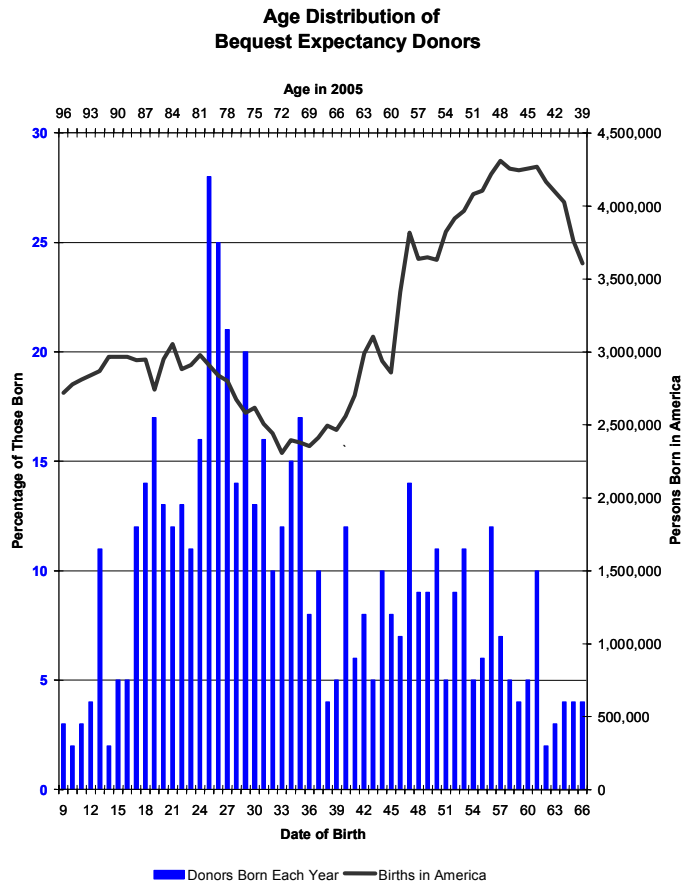
5. Population growth is in the younger 60 to 70 age range.



6. Note age distribution of donors for one large donor base.



7. Distribution of bequest expectancies reveals a “hole” in the 60 to 70 age range.



- E. Alternatives to traditional planned gifts for those in the 60-70 age range.
1. Gift annuity rates may not be that attractive to this age group.

Age	Rate	Age	Rate
55	5.5%	73	6.8%
56	5.6%	74	6.9%
57	5.6%	75	7.1%
58	5.7%	76	7.2%
59	5.7%	77	7.4%
60	5.7%	78	7.6%
61	5.8%	79	7.8%
62	5.9%	80	8.0%
63	5.9%	81	8.3%
64	6.0%	82	8.5%
65	6.0%	83	8.8%
66	6.1%	84	9.2%
67	6.2%	85	9.5%
68	6.3%	86	9.9%
69	6.4%	87	10.2%
70	6.5%	88	10.6%
71	6.6%	89	11.0%
72	6.7%	90+	11.3%

2. Alternatives to traditional gift annuities for relatively younger donors.
 - a. Deferred gift annuities may be an option.

Example:

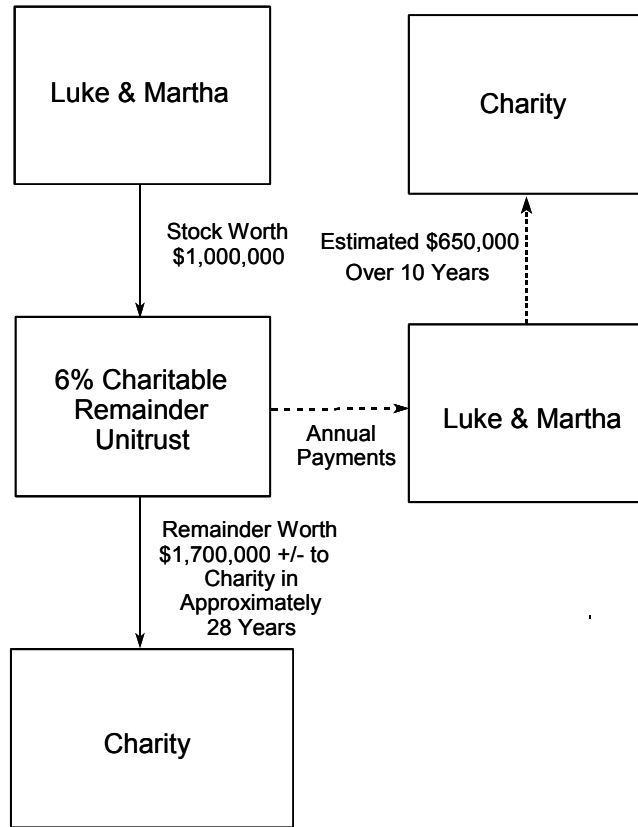
Luke and Martha, both age 60, have indicated their desire to make a lead gift to a capital gift development effort. They have been asked to make a gift of \$1 million, payable over a five-year period. They are worth \$15 million and the organization is counting on them to complete this gift.

After reading a planned giving newsletter from the organization announcing that planned gifts were being counted in the campaign and inviting them to visit the gift planning website, they did so. They were intrigued by the idea of funding a deferred gift annuity with \$1 million worth of appreciated stock that paid no dividends. They call the planned giving office and express interest in a deferred gift annuity that would begin making payments of 9.5% per year to them for life beginning in ten years at age 70. Their charitable deduction would be \$356,000.

The campaign leadership is not pleased with the prospect of this gift because it is not expected to terminate for 28 years (under today's life expectancies). They do not want to accept that gift at all and are adamantly opposed to giving credit for \$1 million toward the campaign goal even though their policies require this. The donor's advisors are also not pleased because they will no longer be able to manage the \$1 million used to fund the deferred gift annuity.

The planned giving officer is asked to come up with a better solution that the donor might see as a compromise. After careful consideration, the planned giving officer suggested that the donors create a 6% charitable remainder unitrust. The donors' advisors believe they can earn over time 8% on the trust assets, the same as the institution is projecting for the return on its endowment.

Their plan can be depicted as follows:



The donors agree that they will make a pledge of the first ten years of income from the trust. This should result in an income flow to the organization of some \$656,000. The donors will report this income each year and it will wash out as a charitable deduction. They have already indicated by their desire for a deferred gift annuity that they don't need the income from the assets for ten years in any event. No capital gains tax will be due at the time of the gift on the increased value of the assets used to fund the trust and they will be entitled to a charitable deduction of some \$228,000 as a result of making the gift in this way.

Note that the payments that Luke and Martha will transfer to the charity will grow gradually over the years, along with the assets in the unitrust.

Principal	\$ 1,000,000				
Earnings	8%				
Payout %	6%				
Year	Principal	Earn	Growth	Pay	Payment
0	\$ 1,000,000	8.00%	\$ 80,000	6.00%	\$ 60,000
1	\$ 1,020,000	8.00%	\$ 81,600	6.00%	\$ 61,200
2	\$ 1,040,400	8.00%	\$ 83,232	6.00%	\$ 62,424
3	\$ 1,061,208	8.00%	\$ 84,897	6.00%	\$ 63,672
4	\$ 1,082,432	8.00%	\$ 86,595	6.00%	\$ 64,946
5	\$ 1,104,081	8.00%	\$ 88,326	6.00%	\$ 66,245
6	\$ 1,126,162	8.00%	\$ 90,093	6.00%	\$ 67,570
7	\$ 1,148,686	8.00%	\$ 91,895	6.00%	\$ 68,921
8	\$ 1,171,659	8.00%	\$ 93,733	6.00%	\$ 70,300
9	\$ 1,195,093	8.00%	\$ 95,607	6.00%	\$ 71,706
10	\$ 1,218,994	8.00%	\$ 97,520	6.00%	\$ 73,140

If the trust performs as anticipated, the donors will enjoy an income stream of some \$1,670,000 over their remaining 18-year joint life expectancy when they begin to keep the payments at age 70.

11	\$ 1,243,374	8.00%	\$ 99,470	6.00%	\$ 74,602
12	\$ 1,268,242	8.00%	\$ 101,459	6.00%	\$ 76,095
13	\$ 1,293,607	8.00%	\$ 103,489	6.00%	\$ 77,616
14	\$ 1,319,479	8.00%	\$ 105,558	6.00%	\$ 79,169
15	\$ 1,345,868	8.00%	\$ 107,669	6.00%	\$ 80,752
16	\$ 1,372,786	8.00%	\$ 109,823	6.00%	\$ 82,367
17	\$ 1,400,241	8.00%	\$ 112,019	6.00%	\$ 84,014
18	\$ 1,428,246	8.00%	\$ 114,260	6.00%	\$ 85,695
19	\$ 1,456,811	8.00%	\$ 116,545	6.00%	\$ 87,409
20	\$ 1,485,947	8.00%	\$ 118,876	6.00%	\$ 89,157
21	\$ 1,515,666	8.00%	\$ 121,253	6.00%	\$ 90,940
22	\$ 1,545,980	8.00%	\$ 123,678	6.00%	\$ 92,759
23	\$ 1,576,899	8.00%	\$ 126,152	6.00%	\$ 94,614
24	\$ 1,608,437	8.00%	\$ 128,675	6.00%	\$ 96,506
25	\$ 1,640,606	8.00%	\$ 131,248	6.00%	\$ 98,436
26	\$ 1,673,418	8.00%	\$ 133,873	6.00%	\$ 100,405
27	\$ 1,706,886	8.00%	\$ 136,551	6.00%	\$ 102,413
28	\$ 1,741,024	8.00%	\$ 139,282	6.00%	\$ 104,461

At the death of the donors, the charity should receive \$1,741,024. The campaign committee agrees to a value of this amount of \$340,000, based on NCPG Valuation Standards with a negotiated discount rate of 6%. They agree to give full campaign credit for the \$656,000 in cash payments over the first ten-year period. The donors are thus credited with a \$1 million gift to the campaign.

At the end of the ten year period, the donors can decide to keep the income for the remainder of their lives or, as is likely to be the case, if they continue to not need the income, they could renew the pledge for some period of time, or they may decide to terminate the trust and let the charity have the funds earlier than anticipated.

In any event, the charitable remainder trust operates in much the same way as a lead trust for the first ten years, while the donors keep the option of enjoying the income for a period of time before an endowment is eventually funded.

b. Gift annuities for parents.

Example:

Mary and Bert, age 59 and 57, have recently sold their home for \$650,000. They paid \$250,000 for the home twenty years ago. After expenses they netted \$350,000. This was at least \$100,000 more than they ever expected to realize from the sale of their home. They are also pleased that in the wake of 1997 tax law changes they will owe no federal capital gains tax on the sale proceeds. The funds are now invested in relatively short-term, fixed income investments yielding 3%.

Bert's mother, age 87, has now exhausted her savings. Bert has been giving her on average about \$800 a month from his after-tax income. He has been asked to make a gift of \$50,000 to a charitable interest that is conducting an endowment campaign. He doesn't see how he can do both.

After consulting with representatives of the charity and his advisors, he decides to use a portion of the cash from the home sale to fund a \$100,000 gift annuity that will pay his mother 10.2%, or \$10,200. This amounts to \$850 per month in spendable income for his mother.

The gift will result in a charitable income tax deduction of \$54,000, saving him income taxes of about \$18,000. The remaining \$46,000 represents a taxable gift to his mother. He has not used any of his \$1 million gift tax exemption amount so he will owe no gift tax.

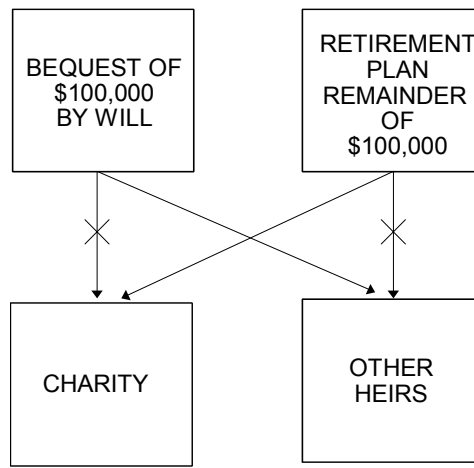
If the charity earns 6% on the gift annuity funds for the six years his mother is expected to live, there will be approximately \$65,000 remaining at the end of her life. The value of this amount discounted at 4% is \$53,000. Under the gift crediting guidelines of the charity, Bert is offered and he accepts recognition for a gift of \$50,000.

F. Designation of remainder from retirement plan can be preferable to a gift through a will for a number of reasons.

1. As a non-probate asset, a retirement plan remainder gift will be received sooner and with possibly less "shrinkage."
2. Can be better option from a tax planning standpoint.
 - a. Family will receive more if retirement assets left to charity than assets left to the family through the will.
 - (1) Retirement plan assets are part of the taxable estate along with other types of property.
 - (2) Retirement plan assets are "income in respect to a decedent" (IRD) and income tax must be paid on the amount an heir receives net of estate tax.
 - (3) Note the impact of this "double taxation" on an IRA balance of \$1 million, assuming an estate tax rate of 47% and effective income tax rate of 35%.

Amount Included in Estate	\$1,000,000
Estate Tax	\$470,000
Amount to Heirs	\$530,000
Income Tax Owed	\$185,500
Net to Heirs	\$344,500
Percent Paid in Taxes	65%
Net Percent to Heirs	35%

- (4) Both the estate and income taxes can be completely avoided if retirement plan assets are used to fund charitable gifts, resulting in these funds never being subject to tax.
- (5) This will be especially attractive for those who will no longer owe estate tax because the income tax benefit will remain regardless of estate tax laws.
- (6) Can be valuable insight to communicate to donors.



Note that consent by spouse may be necessary to leave all or a portion of retirement plan assets to charitable beneficiary.

- G. Outright gifts through a retirement plan withdrawal can also be a practical "pocket" from which to give.
 - 1. Donor should generally be older than 59 1/2 to avoid penalty for early withdrawal.
 - 2. Funds are reported as income and then "wash" out of tax return as a charitable deduction.
 - 3. Important not to exceed 50% of adjusted gross income after withdrawal.

Example:

John and Martha are a recently retired couple, both of whom are over the age of 59 1/2, with an adjusted gross income of \$125,000. They would like to make a pledge to a campaign of \$100,000 payable at the rate of \$25,000 per year for four years. They have an

IRA worth over \$1 million. Under today's law, they can withdraw \$25,000 from their IRA and use those funds to make the gift, which is fully deductible up to 50% of their adjusted gross income. Note that the IRA withdrawal serves to increase their AGI to \$125,000, so it is not a problem for them to fully deduct their gift each year resulting in a "wash" for tax purposes.

4. For some high income donors their charitable deductions must be reduced by 3% of the amount by which adjusted gross income for joint filers exceeds \$142,700. For instance, if a donor's income were \$100,000 over the threshold, his or her itemized deductions would be reduced by 3% of that amount, or \$3,000. The \$25,000 gift described above would be unaffected. Where the reduction comes into play the impact is normally minimal.

Example:

Tom and Judith are high income taxpayers with income over the threshold at which they have to reduce their deductions by 3%. If they decided to make a gift from IRA assets, the gift would still result in a virtual wash for tax purposes. In this situation, a \$100,000 IRA withdrawal followed by a charitable gift in the same amount increases adjusted gross income by \$100,000, which would entail a reduction of Tom and Judith's itemized deduction for the gift of the \$100,000 by 3%, or \$3,000. The result is a \$97,000 deduction, a 97% wash for tax purposes, with just \$3,000 of the withdrawal amount subject to tax. In a 35% tax bracket, some \$1,050 in tax would be due on the \$100,000 withdrawal.

5. The latest version of the CARE Act would allow persons over 70 ½ to make gifts directly to charity without having to consider the 50% of AGI limitation or the 3% reduction rule
 - a. CARE Act only applies to gifts from Individual Retirement Accounts.
 - b. Would not change rules for 401(k) accounts or other tax-favored retirement accounts.
6. With minimal planning, a donor over the age of 59 ½ can make tax efficient gifts using amounts withdrawn from IRAs without incurring significant tax penalties whether or not the CARE act is passed. Even if it becomes law, in its current form it would not allow tax-free outright gifts until age 70 1/2 and the tax consequences for donors between the age of 59 ½ and 70 ½ would remain the same as current law.

D. Tax-free "rollover" from qualified retirement plans to gift annuities, charitable remainder trusts and other split-interest charitable gift plans are not allowed under current law.

1. Tax must be paid on funds withdrawn even if placed in a charitable remainder trust or other qualified life income gift plan. This is generally not an attractive option.

Example:

Suppose a donor, age 70 would like to withdraw \$20,000 from a retirement account to fund a gift annuity. In a 25% tax bracket, the donor would have to pay income tax of \$5,000 on the withdrawal. If he or she then decided to fund a gift annuity with the \$15,000 in cash remaining, they would be entitled to an income deduction of \$5,893, saving taxes of \$1,495. This is not the most efficient way to make the gift. The optimal amount to fund the gift annuity is \$16,650. This results in a charitable deduction of \$6,643, resulting in tax of \$3,339, which absorbs the remainder of withdrawn cash.

Through this transaction the donor is able to reduce the tax on the withdrawal and has a greater amount to yield payments for the remainder of life. This can be summarized as follows:

Withdrawal	\$20,000
Gift Annuity	\$16,650
Tax Deduction from Annuity	\$6,643
Taxable Amount	\$13,357
Tax Paid	\$3,349
Net Cash	\$11

Note that without the gift annuity, the tax on the withdrawal would have been \$5,000. The tax on the withdrawal is reduced by some 33% by funding the gift annuity in this way. Because the annuity is funded with cash, the donor will receive 58% of the annuity payments free of tax for the first 16 years of payments.

2. The CARE Act would allow direct funding of deferred gifts such as gift annuities without the donor having to report the withdrawal. The full amount of the withdrawal could go directly into the split interest gift.
 - a. No charitable deduction allowed.
 - b. All income fully taxable from the outset. No amount is considered return of investment in a gift annuity.
 - c. Only applies to withdrawals from IRAs.
 - d. Payout rates from gift annuities and other plans are typically higher than mandatory withdrawal amounts.
 - e. There is a slight advantage to funding gift annuities with IRA assets if CARE Act is passed. In this example, after 16 years the payment from the gift annuity funded with other property would be fully taxable and the IRA funding option would be preferable from that point forward.

GIFT ANNUITY FUNDED WITH IRA FUNDS

Age	70
Payment Rate	6.50%
Tax Rate	25%
Deduction %	39.9%
Amount Excluded	58.0%

	Withdraw	Tax Paid On Withdrawal	Amount to Gift Annuity	Income	Excluded	Tax	Tax Amount	Net Received	Net %
Current Law	\$20,000	\$3,339	\$16,650	\$1,082	58%	25%	\$ 114	\$968	4.84%
CARE Act	\$20,000	0	\$20,000	\$1,300	\$0	25%	\$ 325	\$975	4.88%

- f. A donor would be better advised under current law or the proposed provisions of the CARE Act to fund a gift annuity with cash or appreciated property if they have those assets, rather than using funds from an IRA.

GIFT ANNUITY FUNDED WITH CASH FROM OTHER SOURCE

	Gift Amount	Charitable Deduction	Tax Savings	Net Cost of Gift Annuity	Payment Amount	Amount Excluded	Net Taxable	Tax Paid	Net Received	Net %
Current Law	\$20,000	\$7,978	\$1,995	\$18,006	\$ 1,300	58%	\$ 546	\$137	\$ 1,164	6.46%
CARE Act	\$20,000	\$7,978	\$1,995	\$18,006	\$ 1,300	58%	\$ 546	\$137	\$ 1,164	6.46%

- g. Similar analysis applies to charitable remainder trusts and other split interest gifts. All income from a charitable remainder trust funded with IRA funds is fully taxable as the tier structure of income reporting does not apply.
 - h. Remember that the principal of the gift is not available to the donor as would be the case if funds were left in IRA. For this reason and the economic advantages outlined above, even after the CARE Act many donors will use other assets that are vulnerable to claims of creditors to fund gift annuities.
3. It can be good planning in some cases to leave assets at death to a charitable remainder trust for the benefit of heirs. In that case a calculation must be made to minimize the amount of estate tax that would be due. This can be a way to give heirs an income from a portion of the retirement plan assets for life.

III. Conclusion.

About the Presenter

Robert F. Sharpe, Jr. is president of The Sharpe Group. A graduate of Vanderbilt University and Cornell University School of Law, he has in past years practiced law with a major law firm specializing in income, estate, and gift taxation and corporate planning.

Prior to his legal experience, he served as a development officer for a liberal arts college. He has authored many articles and other publications covering numerous gift planning topics. His remarks on this subject have been featured in the *Wall Street Journal*, *The New York Times*, *Newsweek*, *Forbes*, *Smart Money*, *CBS Market Watch*, *The Chronicle of Higher Education*, *Trusts & Estates*, *Kiplinger's* and other national publications.

The Sharpe Group consults nationwide with a number of leading health, education, social service, and religious organizations and institutions in implementing their major and planned gift development efforts. With offices in Memphis and Washington DC, The Sharpe firm has worked with over 10,000 U. S. nonprofits and many organizations and institutions worldwide during its 40 year history.

Mr. Sharpe is a frequent speaker for gatherings including Planned Giving Groups in New York, Los Angeles and other cities, the National Committee on Planned Giving National Conference, the American Bankers Association Trust Asset Management Conference, the Association of Fundraising Professionals National Conference, the Association for Healthcare Philanthropy Advanced Planned Giving Institute, Council for Advancement and Support of Education (CASE) National Conference, CASE Advanced Planned Giving Conference, the O.M.I. Non-Profit Tax Conference, and others.

Mr. Sharpe is an active volunteer and has served as a trustee of a number of arts, educational, and civic organizations.