Charitable Giving — A Structured Approach

By Claire Costello, David Ratcliffe, and Ramsay Slugg

Individuals who are committed to philanthropy are motivated by a desire to have a positive impact on the organizations and causes they support. Structuring their giving — by using a donor-advised fund, private foundation or charitable trust — can help them enhance that impact. Moreover, compared with direct giving, the use of one or more giving vehicles correlates with greater personal satisfaction and results in higher giving levels.[1]

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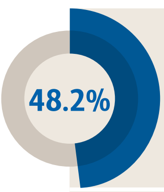
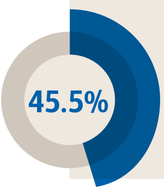
Donors give strategically

Today's dedicated donors are using charitable giving vehicles as part of a more deliberate and intentional charitable strategy that better allows them to integrate their giving with their broader wealth management strategy. The 2016 U.S. Trust® Study of High Net Worth Philanthropy found that approximately one in four wealthy donors have, or plan to have in the next three years, at least one giving vehicle. In addition, a significant percentage of wealthy donors have a specific strategy and annual budget in place to guide their charitable giving.



Percentage of high-net-worth donors that have a strategy for their giving.



Percentage of high-net-worth donors that have a budget for their giving.

Structured charitable giving benefits both donors and recipients

Giving in a structured way allows donors to make charitable decisions proactively, rather than reacting to individual appeals. Structured giving may target specific organizations, focus on specific needs, or both. The use of charitable giving vehicles may also allow donors to better monitor the impact of their giving over time while seeking to maximize tax and financial benefits.

Moreover, charitable giving vehicles offer the opportunity to involve children and grandchildren in the charitable gifting or granting process. By structuring giving, families can help build and enhance a family legacy of philanthropy, allowing donors to pass along values along with their assets to younger generations.

Structured giving offers a landscape of solutions

Donors may structure their charitable giving with as much or as little complexity and control as they choose. While direct charitable giving may have the advantage of simplicity as compared to the use of charitable giving vehicles, structured giving may also provide distinct advantages. Many donors find that a combination of approaches is needed to help meet their philanthropic and financial goals.

Selecting the giving vehicle that is appropriate for a particular individual or family depends on many factors, including family culture and traditions, tax structure, income needs, whether they monitor their giving and assess their impact, and the type of assets being donated.

Three broad categories of charitable giving vehicles:

1 Indirect Charitable Giving Vehicle
With indirect charitable giving, the donor gives assets to a charitable entity, such as a private foundation or donor-advised fund, which in turn makes charitable grants to operating charities.

2 Split-interest Charitable Trust
Assets donated to a trust are used to benefit both the donor and the charity.

3 Institutional Giving
Many nonprofits offer their own charitable giving vehicles that may provide income to donors or their beneficiaries, as well as benefit the charity.

1 Indirect Charitable Giving

Donor-Advised Fund[2]

Individuals and families who are looking for a simple giving vehicle may find a donor-advised fund (DAF) appropriate for their giving needs. A DAF is a nonprofit organization established with community foundations, certain financial services providers or other charitable organizations. The donor gifts cash, securities or other assets to the DAF and then receives an income tax charitable deduction for the current year.[3]

With the gift, the donor establishes an account in the DAF that can be named as the donor wishes. This offers the opportunity to include family members in charitable giving. The account is managed by an investment professional who seeks to grow the assets. Returns on the investment can further enhance the value of the gift to charity.

The DAF makes grants to charities based on the donor's recommendations. All grants must be approved by the sponsoring organization of the DAF. Grants can be made at any time, and there are no annual distribution requirements, as there are with private foundations.

In addition, granting can be done anonymously to protect the donor's privacy, a benefit not fully afforded in other giving vehicles.

DAFs may be established with community foundations, certain financial services providers, or other charitable organizations that sponsor them.

Private Foundation[2]

Those who intend to donate significant amounts while creating a charitable giving program for future generations may wish to consider a private foundation. Foundations are nonprofit legal entities that make charitable grants. The donor retains full decision-making authority over granting.

Private foundations involve costs to establish, and their grant-making activity is a matter of public record. Generally, 5% of a foundation's assets must be granted each year. In addition, foundations are required to file tax returns and pay an excise tax of up to 2% of net investment income.

The donor receives an income tax charitable deduction for assets that are contributed to the foundation.[3] The assets are typically invested to generate additional funds for future grants. The donor has the flexibility to choose how the investments are managed.

Key questions to consider when choosing an indirect charitable giving vehicle:

Are you interested in formalizing your legacy?

Would you like to create a forum for engaging family members?

Would you like to establish or continue family traditions?

How much control do you want to have over investments and grant-making?

How costly — both in terms of time and money — is it to establish and maintain the vehicle?

Are there required annual distributions?

Can you give anonymously?

2 Structured Giving Through a Split-interest Charitable Trust

Charitable Remainder Trust

Donors who wish to generate income from an asset while ultimately gifting it to charity can establish a charitable remainder trust (CRT). This type of structured giving vehicle is particularly advantageous for highly appreciated assets.

The donor contributes the asset to an irrevocable trust — one in which the terms of the trust cannot be amended or revised until the terms or purposes of the trust have been completed — and names the charity or charities that will ultimately benefit. The donor can claim an immediate income tax charitable deduction for the value that will ultimately pass to charity, and can defer the payment of capital gains taxes on the appreciation.[3]

The donor or other beneficiary receives specified distributions from the trust, either for a specific number of years or for their lifetime. At the end of that term or the beneficiary's life, the remaining assets pass to the charity that the donor has named.

Charitable Lead Trust

Donors who wish to provide income to charity while ultimately transferring assets to younger generations can establish a charitable lead trust (CLT). Depending on how the trust is structured, the donor may be able to remove income and future appreciation on an asset from his or her estate without permanently relinquishing management of the asset.

A donor contributes assets to an irrevocable trust and, depending on the structure of the trust, may be entitled to an income tax charitable deduction.[3] For a set term of years, or the duration of the donor or other beneficiary's life, the trust pays an annual amount to one or more charities named by the donor. At the end of the payment term, the remaining assets will pass to the donor's beneficiaries, typically their children or grandchildren.

Key questions to consider when choosing a split-interest charitable trust:

Who do you want to receive the income during the term of the trust?

Who do you want to receive the asset at the termination of the trust or the donor's death?

Are contributions tax deductible?

3 Structured Giving Through an Institution

Endowment

A donor giving to an institutional endowment may or may not restrict its use. This is an outright gift to a charitable organization for which the donor receives an income tax charitable deduction.[3] The donor retains control by placing restrictions on when and for what purposes the funds may be used.

Charitable Gift Annuity

Some charitable organizations offer a source of income for donors through a charitable gift annuity. This is a contractual agreement between the donor and the institution in which the donor contributes assets and the charity promises to pay a lifetime annuity to the donor or another individual of the donor's choosing.

The amount paid through a charitable gift annuity is typically less than what can be expected from a commercial annuity, because a portion of the amount contributed ultimately goes to charity. However, by making a gift, the donor receives both an income and estate tax charitable deduction.[3] The charitable annuity also allows the donor to reduce the size of his or her taxable estate.

Pooled Income Fund

Another way for donors to access income is through a pooled income fund. These are funds, run by nonprofit organizations, in which donors' contributions are pooled and invested together.

Income from the fund is distributed to each participant according to his or her share of the fund. Upon the death of the income participant, the remaining assets are retained by the designated nonprofit organization.

Key questions to consider when giving through a charitable organization:

How much control do you want to have over how your gift is used?

How much income do you want your gift to generate?

Are you sure of your long-term commitment to the particular organization?

Direct giving: advantages and considerations

Most people give directly, without the use of a giving vehicle, to the organizations and causes they wish to support. This approach is straightforward and uncomplicated. Donors receive an immediate income tax charitable deduction, they are not committed to make repeat gifts, and they can give as quickly as they can write a check or transfer stock.

Often, however, direct giving is reactive rather than proactive. And if the direct giving is solely based on solicitation, donors may not feel as connected to the recipients of their gifts as more consistent supporters do.

As donors become more focused in their philanthropy, they may wish to make a longer-term impact on a particular issue. And as the complexity of a donor's financial situation evolves, it may make sense to consider more structured ways to give.

Choose the right team and the right approach

By moving from direct giving to structured giving, you can provide more consistent and meaningful support to the organizations you care about. Structured giving can offer greater personal satisfaction by deepening your connection to the causes you value. Taking a strategic approach allows you to integrate giving into your overall wealth management and estate strategy.

Other potential benefits of structured giving include:

- Involving your family in your philanthropic efforts can create a legacy of charitable giving.
- Donating appreciated securities may help you minimize capital gains taxes and help reduce the risk of holding a concentrated stock position.
- Philanthropic planning may reduce the size of your estate and the resulting estate tax liability.

Various giving vehicles might be appropriate, from the simple to the complex, with various levels of control. Your advisor, working with the trust and philanthropic specialists at U.S. Trust, will help you determine the right solutions for your situation.

With more than 200 years of specialized philanthropic management experience, U.S. Trust is well positioned to provide you with the guidance, support and resources you need.

Case study[4]: A combination of giving vehicles may be the right approach

Jeanne, a prominent entrepreneur, was committed to philanthropy. She and her husband Tim had long used a donor-advised fund for their charitable giving. When Jeanne decided to sell her company, she realized it was time for a more strategic approach.

Jeanne and Tim had several goals:

- Defer capital gains from the sale of the business
- Leave a financial legacy to future generations
- Involve their children in philanthropy
- Retain the freedom to give outside of the public eye

Jeanne's advisor, working with a philanthropic specialist, recommended a strategy that involved several charitable giving vehicles. Prior to the sale of the business, Jeanne transferred part of the ownership to a charitable remainder trust to defer capital gains taxes. After Jeanne and Tim draw income for their lifetime, the remaining value in the trust will be payable to their donor-advised fund.

After she sold her business, Jeanne and her family used a portion of the proceeds to establish a private foundation dedicated to environmental and educational concerns. Because all grants by the foundation are a matter of public record, Jeanne and Tim maintained their donor-advised fund as a vehicle for making anonymous grants.

As part of her estate plan, Jeanne established a charitable lead trust using some of the income from the sale of her company. The terms of the trust create a flow of income to Jeanne's private foundation for 30 years. When the trust terminates, the assets will be transferred to Jeanne's children and grandchildren.

Making the shift from direct to structured giving

High-net-worth individuals and families have counted on us to help them achieve their personal visions and create a tradition of giving. Now it's your turn.

Talk to your advisor about making the shift from direct giving to structured giving.

We can help turn your values into an actionable and effective strategy.

ml.com/legacy

1 Source: The 2016 U.S. Trust® Study of High Net Worth Philanthropy. The purpose of the 2016 U.S. Trust® Study of High Net Worth Philanthropy is to provide comprehensive information on the charitable giving and volunteering activities of high-net-worth households. The sixth in this series of biennial studies, once again written and researched in partnership with the Indiana University Lilly Family School of Philanthropy, is based on a nationally representative random sample of wealthy donors, including, for the first time, deeper analysis based on age, gender, sexual orientation and race. This expanded methodology enables further exploration of the philanthropic trends, strategies, and behaviors among the high-net-worth population. The study is based on a survey of more than 1,500 United States households with a net worth of $1 million or more (excluding the value of their primary home) and/or an annual household income of $200,000 or more.

2 Donor-advised fund and private foundation management are provided by U.S. Trust.

3 All charitable gifts are subject to several limitations.

4 The case studies presented are hypothetical and do not reflect specific strategies we may have developed for actual clients. They are for illustrative purposes only and intended to demonstrate the capabilities of U.S. Trust, Bank of America Corporation and/or Bank of America. They are not intended to serve as investment advice since the availability and effectiveness of any strategy is dependent upon your individual facts and circumstances. Results will vary, and no suggestion is made about how any specific solution or strategy performed in reality.

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