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The Power of Gift Annuities

Charitable gift annuities create opportunities for your senior clients.

The seldom used "coupling" of a charitable gift annuity with a single premium immediate annuity can provide clients with an easy and tax efficient means of garnering guaranteed payouts that are excluded from the estate with no market risk. Leaving out trust documents and legal fees, this strategy will simultaneously provide tremendous benefits to charitable organizations and increase the visibility of your practice.

The charitable gift annuity is a contractual arrangement between a donor and a charity. The donor makes an irrevocable gift in exchange for guaranteed payments for life. The charity issues the gift annuity agreement, then sells (if necessary) the assets gifted, and places the funds into a separate account on behalf of the named annuitant. The charity can then either self-insure or reinsure its payout obligation while making the stipulated payments to the annuitant for life.

Although the term "reinsurance" is misused in this context, the charitable community does refer to such an arrangement as "reinsurance." It involves the purchase of a single premium immediate annuity contract by a charity from an insurance company. The insurance company guarantees the lifetime payments the charity is obligated to pay through a gift annuity agreement. The insurance company makes payments directly to the charity on the same periodic basis as the payout obligation that the charity has made to the named annuitant. The remainder (the amount donated less the reinsurance premium) is available to the charity immediately.

Government regulations require charities that self-insure gift annuities to reserve 100 percent of the risk, effectively restricting the use of amounts contributed until the annuitant's death. However, in most states, should 100 percent of the gift annuity risk be "reinsured" by an authorized insurance company, no reserves are required.

The following examples demonstrate how charitable "reinsurance" can be used for a variety of client planning goals:

Deferred Retirement Payments

John, a married 50-year-old father of two, wishes to supplement his retirement income by contributing $100,000 to a gift annuity and defer the lifetime payments to age 65. John can receive a substantial income tax deduction in the year of contribution and begin receiving an annual lifetime payout of over $10,500[1] at age 65.

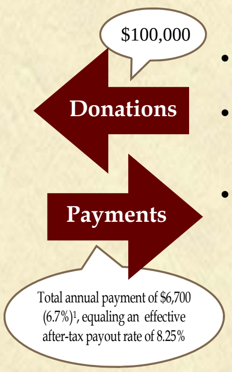
BREAKDOWN	
Donor/Annuitant	**John, age 50**
Gift Amount	$100,000
Payout Date	age 65
Annuity Payout Rate[1]	10.5%
Tax Free Payments[5]	$2,814
Total Annual Payments	$10,500
Tax Deduction[7]	$44,002
Income Tax Savings[2]	$9,334

HOW IT WORKS: Supplemental Retirement Payout

Donor/Annuitant: 75-year-old male with a $100,000 contribution

Charitable Organization

The charity sells the assets (if applicable) and makes a single premium annuity payment of $65,000[6] to an insurance company. The remaining $35,000[6] is available to the charity immediately. The charity receives payments from the insurance company on the same periodic basis that it has obligated itself to, and then uses those funds to make the obligated payments to the annuitant(s) for life.



Donor/Annuitant

- Donates cash (or other assets) to the charity.
- Receives an annual payout of $6,700; of which 70.76% is tax free.[1,5]
- Receives an income tax deduction of $41,214[7], which can be used to offset other income over a five-year period.

The Insurance Company

Upon receipt of the $65,000[6] (the reinsurance premium), the insurance company issues a single premium annuity contract to the charity and then makes the stipulated payments directly to the charity on the same periodic basis that the charity has obligated itself to for the life of the annuitant(s).

High Payout			
Tax Advantaged			
Age	Payout Rate[1]	Tax-Free Portion[2]	Effective Payout Rate[2]
65	5.70%	57.98%	6.28%
70	6.10%	62.62%	6.89%
75	6.70%	67.55%	7.78%
80	7.60%	72.54%	9.07%

Immediate Payments

Beth, age 75, is frustrated by the renewal rates of her bank certificates of deposit. Beth can use $100,000 of her maturing certificates of deposit to establish an immediate gift annuity. In doing so, she can generate an annual lifetime payout of $6,700 as well as a substantial income tax deduction.

BREAKDOWN	
Donor/Annuitant	**Beth, age 75**
Gift Amount	$100,000
Annuity Payout Rate[1]	6.7%
Tax Free Payments[5]	$4,741
Effective Payout Rate	8.25%
Total Annual Payments	$6,700
Tax Deduction[7]	$41,214
Income Tax Savings[2]	$11,540

Educational Funding

Proper design can allow Ann, age 70, to contribute $100,000 toward an *educational funding* gift annuity. Ann can designate her four-year old grandson, Joseph, as annuitant and stipulate his eighteenth birthday as the payout date. Prior to that date, Joseph or his guardian can elect a fixed, four-year payout that will generate annual payments of more than $36,000, partially funding Joseph's college tuition needs.

BREAKDOWN	
Donor	**Ann, age 70**
Annuitant	**Joseph, age 4**
Amount Contributed	$100,000
Deferred Payout Date	age 18
Annual Payout to Grandson (4-yr. period)[3,4]	$36,000
Tax-Free Portion of Payout to Grandson[5]	$18,151
Tax Deduction to Grandmother[7]	$27,395
Income Tax Savings for Grandmother[2]	$7,670

Contributing Appreciated Assets

Joe, age 75, purchased $20,000 of publicly traded stock in 1989. The stock value has increased to $100,000 but generates less than 3% per year in dividends. Joe needs more income but feels trapped by the $12,000 in capital gains tax he would owe if he sold the stock. However, Joe can contribute his stock toward a gift annuity. Doing so can reduce Joe's capital gains tax liability to $6,912, spreading that tax liability over the next 12 years; $576 per year. He can also generate a substantial tax deduction and an annual lifetime payout of $6,700.

BREAKDOWN	
Donor/Annuitant	**Joe, age 75**
Gift Amount	$100,000
Cost Basis	$20,000
Lifetime Payout Rate[1]	6.7%
Total Annual Payments[5]	$6,700
Tax-Free Payments	$1,120
Payments Taxable as Ordinary Income	$1,959
Payments Taxable as LT Capital Gains[2]	$3,621
Tax Deduction[7]	$41,214
Capital Gains Tax Savings[2,5]	$5,088

In summary, the dynamics of a reinsured gift annuity can help satisfy the needs, concerns and objectives of your clients while elevating your level of value in their eyes as a true financial solutions provider, earning more or their business.

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CGA Benefits Abound

The "reinsurance" of charitable gift annuities allows you and your clients to create new cash flow, providing the ability to:

- Satisfy other financial needs by using increased cash flow generated from tax savings and partially tax-free payments.
- Fund investments as well as long-term care and life insurance premiums.
- Satisfy the No.1 concern of retirees:"Will I outlive my money?"
- Convert low-yielding assets into a series of high tax-advantaged lifetime payments.
- Benefit from tax deductions while others receive annuity payments.
- Avoid estate tax on contributed assets, as well as capital gains taxes on appreciated assets.
- Convert investment risk assets into high, guaranteed lifetime payments.
- Offset taxable income from other sources.
- Provide future educational funds for others and get a tax deduction now.
- Increase future lifetime payout amounts by deferring the payout start date.

Benefits for charitable organizations

- Develop relationships with charitable organizations by providing:
- New cash flow for immediate use.
- Perpetual, cost-free planned giving power of financial services professionals.
- Use of the remainder for building campaigns and other fund raising activities while fulfilling the charity's key initiatives.
- The "reinsurance" of existing portfolios of self-insured gift annuities, releasing a portion of existing reserves immediately.
- 'The reduction of administrative costs and other requirements of self-insured gift annuity programs.

A CD ALTERNATIVE?

Here is a comparison of CGAs and CDs, assuming a 75-year-old male donor/annuitant who is contributing $100,000.

Charitable Gift Annuity	Certificate of Deposit
Substantial income tax deduction of $41,214[7]	No income tax deduction is generated.
A portion of the annual payment is tax free (70.76%)[5]	All interest is 100% taxable as ordinary income.
The payout rate is attractive, 6.7% ($6,700)[1]	The interest rate is relatively low.
Sale of a donated capital asset by a charity can partially avoid the capital gains tax obligation of donor.[5]	Sale of a capital asset to Purchase a CD generates capital gains taxation.[7]
Charitable intent is satisfied.	No charitable intent is satisfied.
Not FDIC insured.	FDIC insured.
Access to gifted assets is no longer possible.	Principal may be available for use, net of taxation.
At death, heirs do not receive the principal,	At death, heirs may receive the principal.

[1]Based on a one life chartable gift annuity and ACGA rates effective 6/1/2008. [2]Assumes a 28% tax bracket. Annuity exclusion ratio. [3]Assumes a 4 yr. accelerated payout is exercised by annuitant. [4]Payout maybe subject to gift tax, but may qualify for the annual gift tax exclusion for gifts of present interest. Annuity payments are part return of principal (non-taxable), part capital gain (if any) and part ordinary income. Once principal is recovered and/or capital gains are paid, remaining annuity payments then become fully taxable as ordinary income. If certain requirements are met, the donor may recognize any capital gain ratably over the time period the annuity is expected to be received. Assumes a 15% capital gains tax rate. [6]The amount varies by age, sex and current interest rates. Subject to change. [7]This deduction may have to be spread over more than one year if it exceeds a certain percentage of income limitations. Assumes a 4.2% Federal Mid-Term Rate (subject to change monthly) and annual payments.