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THE WESTERN ILLINOIS UNIVERSITY PLANNER

Ideas on Financial, Gift, and Estate Planning

So, Who Benefits from the New IRA Legislation?

It took nearly a decade, but Congress has finally enacted legislation as part of the Pension Protection Act of 2006 (PPA 2006), which offers charitably minded individuals a golden opportunity to make gifts from their IRAs and exclude the amount of their gifts from gross income. To qualify:

- **The donor must be 70½ years of age or older;**
- **The transfers must go directly from the IRA to qualified charities;**
- **Gifts cannot exceed \$100,000 per taxpayer per year; and**
- **Gifts must be outright.***

** Transfers to donor advised funds, supporting organizations, and charitable remainder trusts and for charitable gift annuities do not qualify.*

This opportunity is available only for 2006 and 2007, and no charitable income-tax deduction is allowed.

Until now, individuals withdrawing \$100,000 from their IRAs and contributing it to charity would have had to include the \$100,000 in their income and would have been allowed a federal charitable income-tax deduction of up to \$100,000 (subject to limits of deductibility) to offset the inclusion. Ostensibly, the net result was zero tax implication—a “wash” for all practical purposes. But for those taxpayers unable to use some or all of the charitable deduction, the new law presents a significant opportunity.

Please call Brad Bainter at (309) 298-1861 to learn how this legislation might benefit you.

Planning a Charitable Bequest? A Lifetime Gift Annuity May Provide Surprising Benefits

Among the most popular ways to make a significant gift to a favorite charity are provisions in wills and trusts. Since such gifts—known as *testamentary provisions*—take effect at the death of the donor, they are particularly attractive to those who feel they need the income generated by all their assets during their lifetimes.

Many philanthropic people are discovering, however, that there may be some very attractive reasons to accelerate these kinds of testamentary provisions and make gifts during their lifetimes in the form of charitable gift annuities. “What are the advantages of a lifetime charitable gift

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Key Questions and Answers About Charitable Gift Annuities

annuity?” you may be asking. In this issue of *The Western Illinois Planner*, we will provide answers to many of the key questions about this powerful and versatile gift-planning strategy.

Realize Immediate Benefits by Making Your Gift Now

What exactly is a charitable gift annuity?

Simply stated, a charitable gift annuity is a contractual agreement between a donor and a charitable organization under which the charity agrees to pay a fixed annual amount to one or two designated beneficiaries for life.

I rely on the income my assets generate. Can I make a charitable gift annuity contribution and still maintain my standard of living?

Not only can a charitable gift annuity allow you to maintain your standard of living, but it may increase your annual cash flow. It does this in multiple ways.

First, the gift annuity provides you with a guaranteed, fixed stream of income for as long as you live. The specific rate you receive depends on your age, with older beneficiaries receiving a greater percentage than younger beneficiaries. The WIU Foundation issues gift annuities in any amount of \$10,000 or more, and the chart below shows

to exceed the interest you are getting on these traditional investments.

In addition, a gift annuity contribution will enable you to claim a sizable income-tax deduction. The deductions for a \$100,000 charitable gift annuity contribution are also shown in the chart.

Increase your cash flow with a charitable gift annuity.

the rates we currently offer at various representative ages.

Given current low interest rates on popular income-producing investments like CDs, money market funds, and bank savings accounts, the payment from your gift annuity is likely

If you itemize deductions on your federal tax return, this deduction will produce tax savings for you proportional to your marginal tax bracket.

***Example:** Joe T, 70, contributes \$100,000 to the WIU Foundation in exchange for a charitable gift annuity that will pay him \$6,500 each year for life. He can deduct \$44,273 as a result of the gift, which in his 33% tax bracket saves him \$14,610.*

Even if you typically take the standard deduction because you do not have enough deductions to itemize, the deduction from your charitable gift annuity may be large enough to allow you to enjoy the benefits of itemizing in the year of the gift.

Are there any other tax advantages of charitable gift annuities?

Definitely. Your gift annuity contribution is treated for tax purposes as two transactions: a gift to charity of a portion of the contribution and an investment in an annuity with the balance. Just as with a commercial annuity, part of each payment you receive from

Sample Benefits for a \$100,000 Gift Annuity

AGE(S)	ALLOWABLE PAYOUT RATE	ANNUAL PAYOUT	TAX-FREE PORTION	CHARITABLE DEDUCTION	TAX SAVINGS IN 33% TAX BRACKET
One annuitant					
60	5.7%	\$ 5,700	\$2,576	\$37,974	\$12,531
65	6.0%	\$ 6,000	\$2,952	\$41,310	\$13,632
70	6.5%	\$ 6,500	\$3,504	\$44,273	\$14,610
75	7.1%	\$ 7,100	\$4,189	\$48,082	\$15,867
80	8.0%	\$ 8,000	\$5,112	\$51,929	\$17,137
85	9.5%	\$ 9,500	\$6,659	\$54,744	\$18,066
90	11.3%	\$11,300	\$8,396	\$58,846	\$19,419
Two annuitants					
60-60	5.4%	\$ 5,400	\$2,327	\$31,173	\$10,287
65-65	5.6%	\$ 5,600	\$2,643	\$34,185	\$11,281
70-70	5.9%	\$ 5,900	\$3,044	\$37,535	\$12,387
75-75	6.3%	\$ 6,300	\$3,566	\$41,544	\$13,710
80-80	6.9%	\$ 6,900	\$4,264	\$45,853	\$15,131
85-85	7.9%	\$ 7,900	\$5,317	\$49,484	\$16,330
90-90	9.3%	\$ 9,300	\$6,668	\$53,302	\$17,590

Calculations are based on 6.2% representative discount rate.

a gift annuity over your life expectancy is deemed to be a return of your investment and is income-tax free.

This means the real return from a gift annuity is even higher than the stated rate of a traditional investment, such as the fully taxable yield from a CD, a money market fund, or a bank savings account.

Example: *Margaret W, 80, made a cash contribution of \$250,000 to the WIU Foundation for a charitable gift annuity that pays her \$20,000 per year. Each year for the rest of Margaret's life expectancy, \$12,780 of the annual payment will be considered a tax-free return of a portion of her investment in the annuity and the remaining \$7,220 will be taxable.*

Thus after paying federal income tax in her 33% bracket, Margaret will have spendable cash of \$17,617.

A fully taxable alternative (e.g., certificate of deposit) would have to generate a return of 10.5% to give her the same amount of spendable cash.

In addition, Margaret's gift annuity will generate an income-tax deduction of \$129,823 which means an actual tax savings of \$42,842. The tax savings reduces the cost of her gift to \$207,158 and boosts her effective return from the gift annuity to 9.65% (\$20,000 divided by \$207,158).

Note: You can use appreciated publicly traded stock to fund a gift annuity. If you do, you will avoid long-term capital-gain tax on some of your paper gain and the gain you do have to recognize will be spread over the balance of your life expectancy. In such cases, the long-term capital gain reduces what would otherwise be a tax-free return of your investment.

Use appreciated stock to fund your gift annuity and avoid recognizing some of the capital gain.

Will a gift annuity cause more of my Social Security income to be taxable?

On the contrary, it is possible that a gift annuity can actually result in less of your Social Security income being subject to tax.

Why? All income—even *tax-exempt income*—can work against you for purposes of determining how much of your Social Security income is taxable. Here is the good news: The tax-free portion of your gift annuity payout is not “income” but a return of your investment. You may actually be able to increase your cash flow and yet lower the amount that is treated as income.

If I wait and direct a gift to the WIU Foundation at my death, won't my estate get tax benefits from that?

The definitive answer is “Maybe!”

What your estate will *not* get is a federal income-tax deduction for a testamentary gift. A testamentary gift might generate federal estate-tax savings, depending on the size of your estate.

If your gross estate is less than the amount exempt from federal estate tax—currently \$2,000,000—your estate will owe no tax and the gift will produce no tax savings. As the exempt amount has risen, fewer and fewer people are subject to federal estate tax.



June's Gift Comparison

	By Will	Current Gift Annuity
Charitable contribution	\$100,000	\$100,000
Income-tax deduction	0	\$ 48,082
Income-tax savings	0	\$ 15,867
Value of savings—15 years at 6%	0	\$ 38,026
Additional annual net income	0	\$ 3,392
Value of additional income in 15 years at 6%	0	\$ 78,952
Total additional value in 15 years	0	\$116,978

Frankly, one of the reasons many people have chosen to accelerate their testamentary gifts and make current gift annuity contributions is to benefit from the income-tax savings available during their lifetimes. These savings could generate a meaningful amount of additional resources at your death.

For instance, let's compare the results of two different courses of action for June—a 75-year-old donor in the 33% tax bracket. In the first scenario, June has \$100,000 invested in a CD that pays 4.1%—or \$4,100—and she plans to give \$100,000 to the WIU Foundation under her will.

In the second scenario, June decides to make a \$100,000 contribution for a gift annuity with the WIU Foundation right now that will pay her 7.1%—or

\$7,100—each year. The gift will generate a deduction of \$48,082 and save her \$15,867 in federal income tax.

If she lives 15 years and is able to earn a 6% annual return by investing her tax savings and the additional net annual income from the gift annuity, June essentially adds almost \$117,000 to the amount available for other purposes at the time of her death. See the table above for a comparison of the two gift plans.

I am concerned that my spouse will also need income from all of my assets. Can a gift annuity make payments to both of us as long as either of us is alive?

Yes. As shown in the first chart, a gift annuity can be payable for one or two lives. The addition of a second beneficiary

does cause a small reduction in the annuity rate and will change the amount that is deductible.

Need More Answers?

Chances are you still have some questions about gift annuities and how one might benefit you. We welcome the opportunity to address your questions, and we encourage you to contact our office to discuss your concerns or to schedule a time when we can meet with you.

We would also like you to have a copy of our latest booklet, *12 Ways a Charitable Gift Annuity May Benefit You*. Request a complimentary copy by returning the enclosed card or calling our office.

You should consult your attorney about the applicability to your own situation of the legal principles contained herein.

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