

CHARITABLE PLANNED GIVING

BACKGROUND OF NONPROFIT ENTITY STRUCTURE AND TAXATION

America's strong tradition of philanthropy harkens back to the constitutional doctrine of separation of church and state, creating a society in which communities of faith have long led in traditional charitable endeavors such as medical services, care for the very young and very old, and education. The development of the federal income tax and estate tax laws in the early 20th century led to the introduction of the charitable contribution deduction and the exempt charitable organization. And so the inextricable intertwining of tax law and charitable giving was born!

As an initial matter, it is useful to understand the difference between "non-profit" or "not-for-profit" (in Arizona, a state corporation law concept) and "tax-exempt," referring to entities that are exempt under federal or state tax law from paying income tax. Tax-exempt entities can include not only many charitable organizations (such as churches, many educational institutions, certain hospitals) but also many fraternal organizations, governmental entities, chambers of commerce, labor unions, and the like.

Knowing a few Internal Revenue Code (IRC) section references is useful. Section 170 sets forth the federal income tax deductions and deduction limitations. The limitations on deductions depend on the category of recipient (whether the deductions were made to a public charity or a private foundation) as well as the assets contributed (ordinary income assets, capital gains assets, or tangible personal property).

Section 501 sets forth the categories of entities that can obtain exemption from federal income tax. Section 501(c)(3): Charitable Organizations. Section 501(c)(4): Social Welfare Organizations. Section 501(c)(5): Labor, Agricultural, and Horticultural Organizations. Section 501(c)(6): Business Leagues. Section 501(c)(7): Social Clubs. Section 501 status does not govern whether taxpayers' contributions to an organization are deductible. See Section 170 above.

Section 2055 creates the estate tax charitable contribution deduction. A charitable bequest generates an estate tax charitable contribution deduction if the organization is listed or described in Section 2055(a). The rules are similar to income tax code criteria, but there are differences, such as certain cemetery companies.

Section 2522 creates the gift tax charitable contribution deduction. A charitable gift during lifetime generates an estate tax charitable contribution deduction if the organization is listed or described in Section 2522(a). IRS Publication 78 lists exempt organizations.

FORMS OF CHARITABLE GIFTS AND BEQUESTS

Appealingly simple are the outright bequests and bequests to charitable organizations at death. Outright bequests can appear in a will. Revocable trust agreements can specify outright distributions to charitable distributions at death.

More complicated dispositive schemes can be set forth in various types of trust agreements. Two types, namely, charitable remainder trusts and charitable lead trusts, must meet highly particular requirements in order to qualify for favored federal income, gift, and estate tax treatment. The tax law refers to charitable remainder trusts and charitable lead trusts as “split-interest trusts,” describing the fact that these trusts invariably feature a lead interest and a remainder interest. In a charitable remainder trust, the lead interest goes to noncharitable beneficiaries, while the remainder will benefit charity. Conversely, in a charitable lead trust, the lead interest benefits charity, while the remainder will revert to the grantor or will benefit some other noncharitable beneficiaries.

Charitable lead trusts and charitable remainder trusts are designed to take advantage of favored federal income, gift, and estate tax treatment. However, if favored tax treatment is not a goal, more flexible trusts can be created that do not comply with the rules applicable to charitable lead trusts or charitable remainder trusts.

Gift annuities are an appealingly simple alternative to charitable remainder trusts. Gift annuities are private annuities between a donor and a charity. The donor’s contribution generates income and gift tax deductions while providing a stream of income back to the donor. The donor does bear the risk that the charity will be unable to meet the annuity payment obligation. The American Council on Gift Annuities provides benchmark rates.

Donors can create tax-exempt private foundations to carry out their charitable grantmaking on an ongoing basis. Private foundations must apply for tax-exempt status from the IRS. Donors appreciate the ability to control their own private foundation. Many donors will happily tolerate the additional administrative complexities and tax costs.

Sources of bequests and distributions other than the donor’s will or trust are increasingly important. Two largely untapped sources of charitable gifts at death are insurance proceeds and retirement plan benefits (such as IRAs or 401(k) plans accounts). Also, payable-on-death bank accounts or brokerage accounts could be set up to benefit charitable organizations upon the account holder’s death.

LEGAL AND DRAFTING ISSUES

Care must be taken even in drafting simple outright charitable bequests and distributions in wills and trusts. The most important task may be to correctly identify the charitable organization to receive the bequest or distribution. Many charitable organizations have confusingly similar names. For nationwide charities, it’s also important to be clear about whether a bequest or distribution is intended to benefit a local chapter or a national office, project, or effort. For fields of interest in which the existing organizations are precariously unstable, are prone to sudden changes in mission, or are otherwise not expected to be good stewards of a charitable gift, it may be wise to consider making the bequest or distribution to a community foundation or other umbrella organization.

Language commonly found in will or trust dispositive provisions may include:

1. Specific: I give, devise and bequeath to the (insert organization name here) (insert here the sum or description of property) to be used for general purposes as the governing body of the organization may direct.
2. Residuary: I give, devise and bequeath to (insert organization name here) all (or a portion, such as 50%) of the rest, residue, and remainder of my estate, to be used for general purposes as the governing body of the organization may direct.
3. Restricted: I give, devise and bequeath to (insert organization name here) (insert here the sum or description of property), to be used for (describe the primary purpose).

Sample IRS forms are available for charitable remainder trusts and charitable lead trusts. The sample forms do not include every provision that would be necessary to meet any donor's needs. However, the sample forms do provide the language that is necessary to qualify under the rigorous rules for charitable remainder trusts and charitable lead trusts to provide the desired tax results. It is advisable to make use of the sample form language, but not without other provisions.

Avoiding litigation is an important goal in planning charitable bequests and distributions. Adjustments to typical will and trust boilerplate (such as tax apportionment clauses and powers of appointment) may be necessary in order to avoid unanticipated consequences. Carefully defining the charitable beneficiaries can avoid vexatious litigation among competing charitable organizations. Imprecise identification ("the Humane Society for the Prevention of Cruelty to Animals") can lead to unintended and wasteful results.

Including appropriate contingent beneficiaries is wise. The donor's favorite charitable organization may no longer exist at the time the donor's estate or trust is administered. The will or trust should make clear what to do if a charitable legatee or distributee is no longer in existence. Appropriate contingency planning can avoid court involvement.

Drafters should anticipate that the donor's family or other noncharitable beneficiaries may be disgruntled by the donor's designation of a charity to receive "their inheritance." The will or trust can include provisions designed to disincentivize the family members or other noncharitable beneficiaries from filing will contest lawsuits or otherwise interfering with the administration of the charitable bequest or distribution.

A growing area of professional liability for drafting attorneys is mishandling of tax apportionment issues in estate planning. Many charitable gifts at death, notably including charitable remainder trusts created at death, can be traps for the unwary. The basic question is: Who should pay any income or estate tax due? Proper drafting often involves dovetailing tax apportionment provisions in various documents.

Special care must be taken with charitable gifts made through beneficiary designations of retirement accounts and IRAs. These accounts are especially attractive for charitable gifts at death, because the charities, as tax-exempt organizations, do not have the income tax liabilities that noncharitable beneficiaries would have upon inheriting an IRA or qualified plan account. The particular rules governing beneficiary designations of retirement accounts and IRAs are complex, and they have changed repeatedly in the past few years.

PRACTICAL ISSUES AND RESOURCES

One practical cornerstone of planning charitable gifts using charitable remainder trusts, gift annuities, and charitable lead trusts is the use of the various software programs available to calculate the income tax, estate tax, and gift tax charitable contribution deductions that may be generated by those gifts. Development officers at many charitable organizations will happily prepare illustrations for prospective donors or their advisors. Software Options to explore include Crescendo Interactive, PG Calc, Philanthrotec, Leimberg, and others.

Many resources in print exist for drafting tips for the professional adviser as well. Internal Revenue Service Publication 557 (“Tax-Exempt Status for your Organization”) assists charitable organizations with the daunting IRS application to obtain tax-exempt status. The Arizona Community Foundation provides its exhaustive Charitable Giving Guide for Professional Advisors upon request. Other charities, banks, and trust companies provide drafting guides as well.

Expert guidance is often available upon request. The American Council on Gift Annuities, which was formed to standardize interest rates offered under gift annuity contracts, now serves as a virtual clearinghouse for information on gift annuities. The National Committee on Planned Giving (NCPG) is an active trade association that counts many gift planners, development officers, attorneys, accountants, financial advisers, and other allied professionals among its members. Local chapters of NCPG in Arizona, including the Planned Giving Round Tables of Arizona (Phoenix) and Southern Arizona (Tucson), offer regular educational programming, peer networking opportunities, and government relations synergies.

Community resources include multiple community foundations, notably, the Arizona Community Foundation and its affiliates throughout the state, the Southern Arizona Community Foundation, the Jewish Community Foundations, and many umbrella foundations (religious affiliation, educational institutions, health care institutions, humanitarian organizations, and the like). Other charities in Arizona (Arthritis Foundation, American Cancer Society, Salvation Army) are now sponsoring periodic e-mail updates for professional advisers, annual CLE seminars, and occasional videoconferences, all regarding the latest developments in charitable planned giving.

Turning to the Internet, there are many useful resources on charitable planned giving.

NCPG: National Committee on Planned Giving

www.ncpg.org

Planned Giving Today (publication)

www.pgtoday.com

Arizona Community Foundation

www.azfoundation.org

DotChe (Donor and Community Exchange) and the Planned Giving Design Center

www.pgdc.net

Crescendo Interactive

www.crescendointeractive.com/home.asp

PG Calc

www.pgcalc.com

Cornell University Planned Gifts Gift Law

www.alumni.cornell.edu/giving/HOW/PlannedGifts/giftlaw.default.html

GuideStar: Nonprofit resources, Links, Fundraising

www.guidestar.org

Catalogue for Philanthropy

www.catalogueforphilanthropy.org/cfp/about/resources.php

American College of Trust and Estate Counsel

www.actec.org

Internal Revenue Service

www.irs.gov/charities/index.html

American Council on Gift Annuities

www.acga-web.org

Planned Giving Services

www.plannedgivingservices.com

R&R Newkirk

www.rnewkirk.com

ETHICAL ISSUES

It's wise for a lawyer to disclose potential conflicts of interest in writing to clients when they are including in their estate plans a distribution to a charitable organization. For example, if the lawyer serves on the board of directors of a charity to whom the clients are leaving a charitable bequest in their wills, written disclosure can alleviate future concerns that the lawyer unduly influenced the decision to make the charitable bequest.

Lawyers often keep complete notes and other records of client deliberations about their charitable estate planning. These records can later prove helpful in the event of claims by unhappy noncharitable beneficiaries that the charitable estate planning resulted from undue influence or was otherwise inappropriate.

Spouses and other couples do not always share charitable interests. As in all areas of potential conflict between spouses or between other couples in the estate planning process, the lawyer would do well to establish at the outset the parameters of the legal representation of the couple. Each of them should understand the extent to which the lawyer is able to advocate on his or her behalf in the charitable estate planning process.

Many charities advocate for donors and their professional advisers to disclose to the charities the nature of any planned charitable gifts. Of course, lawyers cannot disclose such confidential client information without client consent. Lawyer may discuss with clients the likely effects of such disclosure and allow the clients to make their own decision regarding disclosure of planned gifts to the anticipated charitable recipients.

When is it appropriate for lawyers to ask clients to consider charitable planned giving. Some lawyers ask all estate planning clients about charitable giving intentions as part of the estate planning process. Other lawyers do not mention charitable estate planning unless the client initiates discussion of the topic. To what extent should a lawyer conduct due diligence into a charitable organization that a client intends to benefit?

CHARITABLE REMAINDER TRUSTS

A donor may make a gift of cash or other valuable property to the Arizona Foundation for Legal Services and Education but retain the right to receive income from the donated asset for life. This special arrangement is available through the use of a Charitable Remainder Trust.

Tax Savings Benefits

- < Provides an income tax deduction for the value of the charitable gift in the year the gift is made.
- < Allows continued enjoyment of the income from the asset for life.
- < Eliminates the recognition of capital gain on the sale of the asset.

- < Removes the asset from the donor's estate for estate tax purposes.

At the donor's death, the remaining trust asset passes directly to the Arizona Foundation for Legal Services and Education.

Donors to the Arizona Foundation for Legal Services and Education have the opportunity to utilize two types of charitable life income trusts: annuity trusts and unitrusts. The difference between the two lies in the manner in which the trust benefits the donor, or such other person as the donor may designate, before the asset passes to the Arizona Foundation for Legal Services and Education. Under either of the two trusts, the donor, or the donor's designated beneficiary, is subject to income tax on the amount paid to them. The designation of a beneficiary other than the donor or donor's spouse could give rise to gift tax or generation-skipping transfer tax implications.

Charitable Remainder Annuity Trust ("CRAT")

A charitable remainder annuity trust guarantees that the income beneficiary will receive an annual fixed income from the trust, regardless of the amount of income actually earned by the trust. The annual payment to annuity income beneficiary must be a minimum of 5% of the value of the assets determined at the time the trust is created. The actuarially calculated remainder passing to the charity upon the annuity beneficiary's death must be at least 10% of the value of the assets as determined at the time the trust is created

Once established and funded, a charitable remainder annuity trust is not permitted to receive additional contributions. If a donor wishes to make additions, a separate charitable remainder annuity trust must be established for each new donation.

The donor in Illustration A contributes \$150,000 to the Arizona Foundation for Legal Services and Education, establishes a charitable remainder annuity trust, and designates herself as income beneficiary. The trust is obligated to pay a specified income to the donor for life, regardless of the income earned, even if the trust's principal must be used to fulfill the obligation to the donor. If the trust has excess income, then the excess is added to the principal of the trust.

Illustration A

A donor, age 65, without spouse or dependents and in the 36% tax bracket, contributes \$150,000 to the Arizona Foundation for Legal Services and Education and funds a life income annuity trust with her gift. The donor requires a fixed annual income of \$9,000 for her life. IRS-prescribed tables determine the assumed value of the trust that ultimately will pass to the Arizona Foundation for Legal Services and Education. The donor is recognized to have made a charitable donation of approximately \$65,000.

In the year of the gift, the donor receives \$23,400 in federal income tax savings attributable to the gift. She will continue to receive yearly a \$9,000 income from the

trust for the rest of her life. This \$150,000 is also removed from the donor's estate. If the donor's estate is \$1,250,000 at her demise, the charitable gift in trust will reduce the federal estate tax by \$64,500.

Charitable Remainder Unitrust ("CRUT")

Under a charitable remainder unitrust, the income beneficiary is entitled to a fixed percentage of the value of the trust principal determined annually. The minimum percentage allowable is five percent (5.00%). Accordingly, as the CRUT's principal grows, the payment to the income beneficiary grows. Conversely, to the extent that the trust principal diminishes, the payment to the beneficiary likewise diminishes.

If the donor in Illustration A were to establish a life income unitrust calling for an annual payout equal to 6.00% of the trust's value, and the trust's assets were to grow at an annual rate of 7.50%, her income payment in the first year would be \$9,000 and in subsequent years would grow to \$9,135 in year 2, \$9,272 in year 3, etc. (see Schedule A). The growth in the annual payout also means that a smaller residue will ultimately pass to the Arizona Foundation for Legal Services and Education at the termination of the trust (assuming the same total return overall).

The donor is permitted to make additional gifts to the CRUT in future years. Unlike the regulations for an annuity trust, the principal of a life income unitrust may be increased as often as a donor wishes. The donor is eligible to receive an income tax deduction for the assumed value of the trust residue that ultimately will pass to the Arizona Foundation for Legal Services and Education in the same manner as the donation to the annuity trust in Illustration A. The donor to the unitrust is recognized to have made a gift of approximately \$62,500.

In the year of the gift, the donor receives \$22,500 in federal income tax savings attributable to the gift. Assuming that the donor's estate amounts to \$1,250,000 at her demise, the federal estate tax savings will be \$64,500.

The benefits payable to the donor will be greater with a life income unitrust than an annuity trust so long as the trust grows in size over time. As Schedule A reveals, the donor would receive \$150,141 from the 6.0% unitrust but only \$135,000 (15 x \$9,000) from the annuity trust. On the other hand, the annuity trust usually will provide a larger charitable deduction than the unitrust, so long as the guaranteed payout rate is less than the IRS-assumed rate. The annuity trust arrangement described in Illustration A would result in a distribution to the Arizona Foundation for Legal Services and Education of \$282,124, assuming a 7.5% annual rate of growth of assets. With a unitrust, the value of the Arizona Foundation for Legal Services and Education's remainder interest is \$187,535.

Schedule A

Schedule of Increase in Trust Value Over 15 Years — assuming an annual growth of assets of 7.5% and an annual payout rate of 6%.

YEAR	VALUE OF TRUST	PAYMENT TO DONOR
1	\$ 150,000	\$ 9,000
2	152,250	9,135
3	154,534	9,272
4	156,852	9,411
5	159,205	9,552
6	161,593	9,696
7	164,016	9,841
8	166,477	9,989
9	168,974	10,138
10	171,508	10,291
11	174,081	10,445
12	176,692	10,602
13	179,343	10,761
14	182,033	10,922
15	184,763	11,086
16	187,535	
TOTAL PAYMENTS TO DONOR		\$ 150,141

CHARITABLE LEAD TRUSTS

A charitable lead trust is the "opposite" of a charitable remainder trust. It provides for payment of an income interest to the Arizona Foundation for Legal Services and Education for a specified period of time. At the termination of the trust, the principal is distributed to family members or other noncharitable beneficiaries designated by the donor. Only the remainder interest of the trust valued at the time of contribution may be subject to the unified gift and estate tax and to the generation-skipping transfer tax. Jacqueline Onassis' estate plan contemplated the use of charitable lead trusts that would have almost completely avoided estate taxes in her estate.

To qualify as a charitable lead trust, the trust must be created in the form of either an annuity trust or a unitrust. Table 1 illustrates the potential tax advantages of a charitable lead trust for transferring property to heirs. In this instance, the donor was able to avoid incurring much of the gift tax on the transfer of property to his heirs.

Special Note About the Lead Trust

Estate tax rates of up to 55% make the net cost (after tax) of the yearly income relinquished by the donor relatively small for taxpayers in high brackets.

If a donor's charitable contributions in a particular year exceed deductibility limitations, the lead trust may be used to make additional contributions that are not subject to the federal tax rules concerning personal percentage limitations. For a lead trust to work successfully, the assets used by the donor to fund the trust should be selected carefully.

It is also most advantageous for a donor to use property with potential for appreciation in value as the lead trust's assets.

Table 1

A donor contributes property worth \$100,000 to the Arizona Foundation for Legal Services and Education. It produces an income stream of 7.5% or \$7,500 per year. He establishes a charitable lead annuity trust, funding the trust with the property, and indicates his wishes that: (1) the trust shall exist for a period of 14 years; (2) the remainder is to be distributed to his children; and (3) the annual payout to the Arizona Foundation for Legal Services and Education shall be the income earned by the trust.

Calculating the assumed value of the children's interest in the principal at the end of the trust period using IRS tables, it is determined that the donor's gift tax liability on his donation will be substantially reduced because the gifts of income over 14 years to the Arizona Foundation for Legal Services and Education will offset much of the value of the property used to fund the trust. While the donor will incur gift tax liability, no actual tax will need to be paid to the extent that the donor has not fully utilized his unified credit.

In 14 years, the trust assets will be transferred to the heirs, at which time the assets maybe worth substantially more. In short, the value of the property was "frozen" for tax purposes, and the donor has avoided taxation on the income produced by the assets and has preserved more of his unified tax credit for use in other aspects of his estate plan.

LIFE INSURANCE

Life insurance can be a valuable asset for accomplishing an individual's philanthropic objectives at a relatively small net cost.

A donor may make an outright donation to the Arizona Foundation for Legal Services and Education of a new or existing policy by naming the Arizona Foundation for Legal Services and Education as both owner and beneficiary. The donor receives a charitable contribution deduction for the donation of the policy and all future premium payments made by the donor. The proceeds of the life insurance policy held by the charity will not trigger estate tax liability.

Donors may also use life insurance to provide substantial support for the continuity of specific programs and organizations in which they are especially interested. Arrangements can readily be made with the Arizona Foundation for Legal Services and Education to designate the charitable purpose of a donation and then fund the gift with a life insurance policy.

A donor may also utilize insurance to replace the value of assets that have been contributed to the Arizona Foundation for Legal Services and Education. Using the income tax savings resulting

from a donation to purchase a policy on the donor's life effectively assures that the donor's heirs inherit the full amount intended for them. Such usage also provides liquidity to help pay anticipated estate settlement expenses. Arrangements can be made to own the life insurance outside of the donor's estate resulting in no estate tax on the proceeds.

Illustration B describes circumstances that are typical to many families. The solution that was devised effectively incorporates life insurance to accomplish several interrelated objectives.

Illustration B

A couple, both age 66, are retired and have a net worth of \$2,000,000. They own a stock portfolio that has appreciated substantially since the investments were first acquired. However, it no longer produces a current income sufficient to meet the couple's needs. They want to increase their cash flow without either cutting into principal or selling off the investments and being faced with significant capital gains tax. The couple also wishes to pass as much of their estate as possible to friends and family.

In consultation with their professional advisor, they have developed a plan for achieving 4 objectives:

- < Meet cash flow requirements
- < Avoid diminishing the portfolio and incurring tax
- < Continue their commitment to the Jewish community after their deaths
- < Reduce taxes on the estate

The couple decided to establish a charitable remainder unitrust (CRUT). They also created a second, additional and irrevocable "wealth replacement" trust, which is funded with life insurance on their lives, to accomplish the rest of their plan.

Their CRUT was designed to provide the couple a guaranteed annual 6.00% income for the rest of their lives. This achieved their goal of an increase in current cash flow.

They also obtained a charitable contribution deduction for transferring their securities portfolio to the CRUT, reducing current year income taxes. When the trustee of their life income unitrust, sold the securities, it received the full fair market value for them without incurring capital gains tax because the unitrust is tax-exempt. The goals of preserving the value of the investments and avoiding taxes were satisfied

The Arizona Foundation for Legal Services and Education, as charitable beneficiary of the life income unitrust, will fulfill the couple's philanthropic commitment. At their deaths, the assets of the unitrust will pass to the Arizona Foundation for Legal Services and Education, helping to

assure the availability of resources for meeting long-term, emergency, and future financial needs of the community.

Although the couple's taxable estate has been reduced by transferring the portfolio assets to the Arizona Foundation for Legal Services and Education, their goal of providing for their heirs is accomplished by the "wealth replacement" trust. This trust is funded with second to die life insurance that pays a death benefit in an amount comparable in value to the investment assets used to fund the unitrust. Because the policy is owned by the wealth replacement trust and the trust is also the beneficiary of the insurance, the death benefits are not part of the couple's estates, and thus are free of any estate tax. Their friends and family are the beneficiaries of the wealth replacement trust.

GIFT OF A FUTURE INTEREST IN A HOME

A charitable donation can be made to the Arizona Foundation for Legal Services and Education of a future (or remainder) interest in an individual's home with the donor retaining a lifetime right to live on the property. (The term "home" is defined by the IRS as any property that is used as a personal residence, even though it may not be the donor's principal residence, and could encompass the donor's vacation home, a motor home, or even a boat.)

Opportunities for substantial tax savings are available from such a gift. The donor is eligible to receive a charitable income tax deduction in the year that the gift is made, and the value of the donor's estate is reduced by the Arizona Foundation for Legal Services and Education's interest in the property. The amount of the income tax deduction is determined from IRS-prescribed tables.

While the IRS generally does not allow a charitable income, gift, or estate tax deduction for the donation of a partial interest in property, an exception is permitted for a future interest in a home.

RETIREMENT PLANS

Retirement plans such as IRAs, Keoghs and other qualified plans are excellent tax and financial planning devices, but various taxes may cause shrinkage of 70% or more when the remaining portion is transferred to the participant's heirs upon death.

The following taxes may affect the distribution of the plan's balance:

Income Tax. Distributions will be subject to state and federal income tax upon the death of the participant. Today the effective federal income tax brackets range from 15% to 39.6%. Arizona income tax imposes an additional tax burden of up to 5.6%. Income tax may be deferred if the distribution is to the participant's spouse or to certain designated beneficiaries.

Estate Tax. Distributions will also be subject to estate tax at effective rates ranging from 37% to 55%. Distributions to a spouse will defer the estate tax liability until the spouse's death.

Generation-skipping Transfer Tax. A 55% tax is imposed upon the death of a participant who designates a beneficiary who is two or more generations younger than the participant.

Excise Tax. A 15% excise tax is imposed if the participant withdraws too much from a retirement plan on an annual basis. A 50% excise tax is imposed if the participant withdraws too little from a retirement plan for a particular year.

Because of the significant tax burden imposed on retirement plans, these assets can be an excellent gift at death to the Arizona Foundation for Legal Services and Education. Several approaches are possible:

By designating the Arizona Foundation for Legal Services and Education as the beneficiary of the plan, the distribution will avoid both estate and income taxes. One important caution: The amount distributed may be the entire amount or a fractional portion -- but not a fixed amount. To distribute a fixed amount, the estate must recognize in full the ordinary income for the amount specified and the income tax will not be avoided.

Plan assets can be transferred to a CRUT that is created on the death of the participant, which will then distribute income to heirs for a specified term, with the remainder to be transferred to the Arizona Foundation for Legal Services and Education. There will be a partial estate tax deduction based on the payout percentage and the term of the CRUT. The total amount of plan assets can be distributed to the CRUT and can be reinvested without current taxation on the distribution to or income earned by the CRUT. Income distributed to the heirs will be taxable to them upon receipt. Upon termination, the balance of the CRUT, comprised of the untaxed ordinary income originally contributed to the plan plus untaxed growth, passes to the Arizona Foundation for Legal Services and Education without any income or estate tax liability.

A final strategy to consider is the possibility of withdrawing plan funds, paying applicable federal and state income taxes, and then contributing the proceeds to a CRUT. The income tax deduction on the contribution to the CRUT will in part offset the ordinary income on the withdrawal. It is possible to preserve 60% to 70% of the withdrawn amount for contribution into the CRUT. This technique will not produce the same tax savings as the prior two approaches.

GIFTS AT DEATH

A gift of cash, or other valuable property, to the Arizona Foundation for Legal Services and Education may be provided in the donor's will or in the donor's "living" revocable trust, as described in Illustrations D and E.

Illustration D

I give the sum of One Hundred Thousand Dollars (\$100,000) to the Arizona Foundation for Legal Services and Education, an Arizona corporation, for its general purposes.

Illustration E

I give an undivided Ten Percent (10%) interest in my estate to the Arizona Foundation for Legal Services and Education of Phoenix, Arizona, an Arizona Corporation, for its general purposes.

Tax Savings Benefits

The taxable portion of the donor's estate is reduced by the entire fair market value of the bequest. No limitations are imposed by federal tax rules on the amount that may be deducted, and no distinction is made between ordinary income property and capital gain property.

The net cost of the gift to the donor's estate is reduced by the estate tax savings, which can be as high as 60% of the value of the gift.

OPPORTUNITIES FOR GIFTS BY BEQUEST

Contingent Gift in Will

A donor who provides in his will that his family or friends are the primary beneficiaries of his estate can also specify that the Arizona Foundation for Legal Services and Education should be a beneficiary of his estate in the event that the family or friends do not survive him. In the event that the Arizona Foundation for Legal Services and Education receives the gift, the donor's estate will receive a charitable estate tax deduction for the full fair market value of the property. This provision is known as a contingent gift to charity and is described in Illustrations F and G.

Illustration F

I give the sum of Ten Thousand Dollars (\$10,000) to James Martin, if he survives me for 30 days, and if he does not, then I give such sum to the Arizona Foundation for Legal Services and Education, an Arizona corporation, for its general purposes.

Illustration G

I give the residue of my estate as follows:

- a) If Mary Smith, survives me for 30 days, I give the residue of my estate to her.
- b) If Mary Smith does not survive me for 30 days, I give the residue of my estate to my brother, if he survives me for that period.
- c) If neither Mary Smith nor my brother survives me for 30 days, I give the residue of my estate to the Arizona Foundation for Legal Services and Education, an Arizona corporation, for its general purposes.