TRUSTS AND ESTATES

CALIFORNIA LAWYERS ASSOCIATION

TRUSTS & ESTATES QUARTERLY

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THE BROAD ARRAY OF CHARITABLE GIVING VEHICLES DEMYSTIFIED

Written by Margot Edwards* and Aaron Hegji**

We, the authors, intend this article to review various vehicles that donors use to engage in philanthropy and to highlight the practical implications of each option. We recognize that a variety of charitable vehicles are routinely recommended by practitioners to assist donors in fulfilling their unique charitable intentions. No single method is a universally perfect solution and donors may wish to utilize more than one structure. We hope this article provides a roadmap for advisors to help clients match their individual goals to the best structure for them.

In this article you will find, first, a framework for discussing a donor's philanthropic intentions; second, a description of the various charitable vehicles used; and third, charts comparing the various vehicles to identify when each option might best be utilized.

I. THE FRAMEWORK

Prior to considering establishing specific charitable vehicles, the donor should consider and prioritize his or her goals and motives related to philanthropy. These may include supporting one or more specific causes or benefitting particular individual charities. Alternatively, the donor may also have a generalized intention to engage in charitable giving but not yet have had the opportunity to define their specific plans.

The donor may also wish to instill philanthropy in future generations as part of their giving and should consider how much engagement by others he or she wishes to require or encourage. They may also be interested in the tax benefits of charitable giving. Those tax goals may be focused on income tax planning, or wealth transfer planning may also be a priority.

Next, it is important to consider how the donor wishes to engage in philanthropic activity. This may be through direct charitable activities, or it could be through making grants to established individual charities that are well positioned to further the donor's mission.

Finally, the donor should also consider how much complexity they are willing to tolerate as part of achieving their philanthropic goals. Important factors include what degree of maintenance of the charitable vehicle is reasonable for the donor and what level of scrutiny the donor is comfortable enduring.

After taking stock of these considerations, the donor is ready to explore the philanthropic landscape.

II. TIMING AND VALUATION

It is important to note that the timing of a gift of appreciated assets to any charitable vehicle is key. The donor cannot be obligated to sell the asset at the time of its transfer, or they may be deemed to have recognized gain upon the charity's sale of the asset.[01]

The donor will need to obtain an appraisal to support a fair market value deduction for any gift of a non-marketable asset (even if an arms-length transaction takes place relatively close in time to the charitable gift).[02] Finally, the specific charitable recipient must be able to accept the asset. When gifting a non-marketable asset, this may mean working with a more sophisticated charity (such as a sophisticated Donor Advised Fund) and may also require some due diligence before the gift is made.

III. DIRECT GIVING

A. What Is It?

The simplest option for charitable giving is to give directly to individual public charities. This can be accomplished through writing a check, using a credit card, or gifting other assets such as marketable securities.

B. What Are Its Pros/Cons?

One of the primary benefits of direct giving is simplicity. There is no expense involved and there are no ongoing structures to maintain with this approach. In addition, a donor can generally deduct a larger portion of his or her adjusted gross income ("AGI") by gifting directly to public charities rather than certain other charitable recipients.[03] Finally, a direct gift to a public charity of appreciated securities held longer than a year, rather than giving cash, allows the donor to avoid recognition of gain on those securities, as well as to take a fair market value income tax deduction.[04]

This approach lacks customization and doesn't allow for the creation of an interactive philanthropic plan for the donor and their family. Direct giving does not provide the donor the ability to separate the timing of the deduction from the timing of the transfer to individual charities. Furthermore, when making a direct gift, the donor must already know the specific charity and have a desire to benefit that charity immediately. By contrast, the donor may utilize other charitable options to achieve the deduction in a high-income year but take the time later to make decisions about individual charities they wish to benefit. Finally, many charities cannot accept gifts of complex assets, such as closely held stock, which may limit the donor's options for maximizing their gifts and the related tax benefits.

C. When Would I Use It?

Many donors utilize direct gifts for smaller or individualized gifts that are not part of their overall philanthropic plan. The simplicity can be very appealing when the giving to this specific charity is likely to be limited or transactional in nature.

IV. DONOR ADVISED FUND

A. What Is It?

A Donor Advised Fund (sometimes called a "DAF") is an account held by a recognized charitable organization.[05] The account lists advisors (usually the donor(s) or family members selected by the donor) who can recommend investments and charitable grants over time.

B. What Are Its Pros/Cons?

A DAF is a relatively simple and inexpensive approach to charitable giving. Setting up a DAF does not require establishing a separate legal entity, such as a trust or nonprofit corporation, which means that contributing to a DAF is as easy as setting up an account. Many financial institutions have donor advised funds through a related charity or charitable partner. Additionally, community foundations often have DAFs and, in many cases, provide assistance with exploring philanthropic goals and the individual charities whose work furthers those goals.

When a donor makes a gift to a DAF, they receive an immediate tax deduction. Over time, the donor makes recommendations regarding grants to specific charities. Technically, the donor only recommends, and does not direct, those grants. From a practical perspective, so long as the recommended grant recipient is a recognized charity, the DAF typically follows the recommendations of the donor.

A DAF permits the donor to separate the timing of the charitable deduction from the actual grant to an individual charity. This means that the donor can make the gift to the DAF when it provides the greatest tax benefit to the donor but decide later which individual charities should receive funds from the DAF (and, potentially, involve family in the decision-making).

Some other frequently cited benefits of a DAF are:

- A DAF does not require a minimum distribution amount to charities each year.
- The AGI (adjusted gross income) limits that apply to charitable gifts are higher with a DAF than with some charitable vehicles (see chart below comparing DAFs and private foundations). Specifically, a donor gifting appreciated assets to a DAF may deduct up to 30% of his/her AGI.[06]
- The deduction available for a gift of non-marketable assets (such as interests in a closely held business) held longer than a year is equal to the asset's fair market value and not limited to basis.
- There are minimal set up and ongoing administrative costs in connection with a DAF.
- DAFs provide enhanced privacy because investments, expenses, individual grants, and donor names are not publicly available.
- The application of the complex "private foundation rules" to DAFs is limited.

When a donor gifts appreciated assets to a public charity, including a DAF, they may effectively realize two tax

benefits: (a) avoiding the recognition of gain on the asset once it is sold, and (b) a charitable deduction. For assets held longer than one year, the deduction is generally equal to the fair market value of the asset gifted. When the asset is held less than one year, the deduction is equal to the amount of the donor's basis.[07] In addition, if the asset is gifted to a private foundation, it must be readily marketable in order to qualify for the fair market value deduction.[08] For a gift of an interest in a closely held business, this means that the deduction available when gifting to a private foundation will typically be limited to basis, while a gift to a DAF will provide a full fair market value deduction.

Like direct giving, the DAF does not easily lend itself to succession planning for the family's philanthropic legacy over time. As noted above, while some sponsoring organizations of DAFs provide support in researching individual charities and engaging in philanthropy as a family, without this, the DAF structure doesn't provide a robust opportunity for a family to be collectively involved in their philanthropy the way a private foundation structure does. As a result, a DAF may not be the ideal structure for a family looking to create a multi-generational philanthropic legacy.

C. When Would I Use It?

Donors often use a DAF when they wish to have more flexibility related to timing gifts, and more structure around their charitable giving overall, but do not want the complexity of a private foundation. In particular, if a donor's philanthropic plans are straightforward and primarily designed for the donor's own lifetime, a DAF can be a great option.

V. PRIVATE FOUNDATION

A. What Is It?

A private foundation is a privately funded charity and a separate legal entity, such as a nonprofit corporation or trust. It is often funded by a single or series of gifts from an individual (person or company) possessing a predetermined charitable philosophy. Typically, the donor controls every level of its formation, implementation, organization, and activities, until such time as the donor terminates their involvement. Foundations may be terminated when the donor ends his or her involvement, or new participants may (and often are) identified to further the donor's original intent.

The key difference between a public charity and a private foundation is the source of funding. A private foundation is privately funded, typically by a group of related individuals, such as a specific family. A direct consequence of this is that the charitable causes it supports are more idiosyncratic to the original donor(s) and less generalized as with a public charity that solicits the general public for support.

A natural consequence to the above is that competitive forces are absent from a private foundation, while public charities are refined by competitive forces–i.e., because they compete for donations, they are motivated to efficiently use those donations and provide services appealing to society at large (e.g., The American Heart Association). Private foundations, on the other hand, are not refined by these same forces yet enjoy the same tax-exempt treatment. Accordingly, to ensure that private foundation endowments are used for charitable purposes and the operators maintain objectives that warrant tax-exempt treatment, a private foundation is subject to stricter limitations and compliance than a public charity.[09]

These "private foundation rules" are unforgiving and not always intuitive. They significantly limit the foundation's ability to engage in transactions with disqualified persons (typically donors of the foundation or related parties such as family members and trusts),[10] regardless of whether the transaction is beneficial to the foundation.[11] They also impact the types of investments a private foundation can hold[12] and the types of grants that it may make.[13] A donor looking to establish a private foundation should have ongoing guidance to avoid violating these rules, as the consequences are often severe.

Most private foundations do not conduct charitable activities (*e.g.*, operate a homeless shelter) but, instead, make contributions (or grants) to the actual charitable provider. A private *operating* foundation, however, does directly engage in charitable activities. It is a hybrid, or attempt at such, between a private foundation and a public charity. It is structured and funded like a private foundation but operated like a public charity and receives more favorable income tax charitable deduction treatment like a public charity (though not the same treatment as a public charity). Specifically, a private operating foundation must be actively engaged in the charitable activities[14] and satisfy at least one of three tests. These tests are the asset test[15], the endowment test[16], and the support test.[17] One of these tests must be satisfied to receive a favorable ruling from the IRS before the private foundation is deemed a private operating foundation and at least one of the tests must be satisfied each year of the private operating foundation's existence. Failure to satisfy at least one of the tests will result in loss of status.

B. What Are Its Pros/Cons?

Regardless of type (operating vs. not), all private foundations are onerous to operate. In large part, this is

the consequence of two factors: (i) the burden of operation is borne, at least initially, by a single benefactor, and (ii) because of the potential for abuse, regulatory oversight increases the level of scrutiny and compliance imposed on private foundations.

As noted above, a private foundation is a separate legal entity, typically a non-profit corporation or a trust, which involves significant cost to establish and maintain. The donor must establish this entity with appropriate legal documents and submit an application for tax-exempt status. The entity must be maintained and will require annual tax filings.

A private foundation's tax filings are publicly available, which significantly limits the privacy available to the donor and their family related to their charitable giving. A private foundation (that is not an operating foundation) is also required to distribute approximately five percent of its assets to individual public charities each year.[18] This requirement may be inconsistent with the donor's specific philanthropic goals.

A private foundation allows the donor to create a much more robust and customized structure for their charitable giving. The structure can be designed to involve various family members and to exist for multiple generations.

C. When Would I Use It?

Private foundations are a popular choice for families with (i) a distinct philanthropic objective, (ii) the desire, the funds, and the time to be involved in those causes, and (iii) a multi-generational approach to philanthropy. Absent this combination, given the intense scrutiny and heightened compliance to which private foundations are subject, families should seriously consider one of the other more efficient charitable vehicles.

VI. CHARITABLE REMAINDER TRUST ("CRT")

A. What Is It?

A CRT is an irrevocable trust with two distinct interests. The first is a stream of income, which is usually retained by the donor (and sometimes other family members) either for a set term or for their lifetime. The second is the remainder interest, which passes to charity at the end of the term.[19]

The CRT is tax-exempt[20] in that tax is not imposed on the CRT. This allows it to sell appreciated assets without immediate payment of income or capital gains tax. The unimposed tax liability is recorded and carried out when distributions are made to the holder of the income interest. Contributing to a CRT is a charitable gift entitling the donor to a charitable deduction.[21] Unlike other charitable bequests, this deduction is not equal to the fair market value of the asset gifted but, rather, is a reduced amount, specifically a present value calculation derived from (a) the fair market value of the asset transferred, (b) the length of the non-charitable term (often the donor's life expectancy), and (c) the section 7520 interest rate published by the IRS each month.[22]

The Internal Revenue Code ("IRC") grants the donor significant optionality in establishing the terms that comprise the trust's income interest. These variables generate a variety of typical types of CRTs. The donor may utilize a charitable remainder annuity trust ("CRAT") to retain an annuity interest (a fixed amount) or establish a charitable remainder unitrust ("CRUT") and retain a unitrust interest (a fixed percentage of the trust's asset value each year) to be distributed annually to the donor for their lifetime, or for a period of years not to exceed twenty.[23] It is also possible to create a joint interest, for example for the donor and their spouse. This permits the annual distribution to continue to be made to the donor's spouse for their lifetime after the death of the donor. This structure can be used to create significant financial security, with the income stream derived from the entire value of the asset(s) gifted to the CRT, undiminished by income or capital gains tax liability.

B. Types of CRUTs

There are several different types of CRUTs, which may be used depending on the donor's individual circumstances and the assets available to gift. A standard CRUT distributes a specific percentage of the fair market value of the trust assets each year during the term of the trust. This percentage must be between five (5) and fifty (50) percent. The fair market value of the assets must be determined each year, which may be cumbersome if the trust will hold difficult-to-value assets. Additionally, this determination must be made by a third party, either through a readily available market, an independent appraisal, or an independent trustee.

A Net Income CRUT (or NICRUT) distributes annually the lesser of the unitrust amount (*i.e.*, the fixed percentage of the fair market value of the assets) and the actual income of the trust. A Net Income with Make-up CRUT (or NIMCRUT) is a variation of the NICRUT. When the actual trust income is less than the unitrust amount in a given year this deficiency (the "make-up") is recorded and accumulates from year-to-year. In later years, if the actual income surpasses the unitrust amount, the excess, up to the amount of the accumulated make-up, is distributed to the donor to satisfy the accumulated deficiencies.[24] These

types of CRUTs may be used when the income from the trust assets is expected to initially be low, but to increase over time.

Finally, a Flip-CRUT is a trust that begins as a NICRUT or NIMCRUT but converts to a standard CRUT following the occurrence of an event, such as the sale of an asset or the lapse of time.[25] This approach is appealing when the sale of an asset is expected and will make it possible to administer a standard CRUT from that point forward. For example, the donor may desire a non-income producing hard asset to remain in trust until liquidation. A standard CRUT would create annual in-kind distributions, complicating the asset(s) titling. A Flip-CRUT keeps the asset in trust until it is sold at which time a standard CRUT distributes liquid assets.

There are many details and requirements for each variety of trust to qualify as a CRT. These rules are beyond the scope of this article, but anyone establishing a CRT should review them carefully.

C. What Are Its Pros/Cons?

Although a CRT must be irrevocable, the donor can retain the right to change the charity designated to receive the remaining assets when the term expires. The donor may also act as trustee, which allows them to retain control over the investments. Generally, the donor should not take compensation for serving as trustee.

As with all of the charitable vehicles, the CRT has some tradeoffs. Many donors find CRTs to be appealing because of the retained interest, so it is important for potential donors to recognize that they cannot access the principal in the trust—only the annual distributions. Furthermore, because of this retained interest, the charitable deduction is often much lower than that generated by a direct gift. Last of all, the private foundation rules apply to all charitable trusts (CRTs and CLTs, which are discussed below), which makes administration more cumbersome.

D. When Would I Use It?

A CRT is typically used for income tax planning by a donor who has strong charitable intent and has either appreciated assets or bunched income. The donor may utilize a CRT to accelerate a charitable deduction into a high-income year, and/or utilize the CRT to sell an appreciated asset or diversify a concentrated position pre-tax. Finally, it is a common choice for donors wishing to create financial security by retaining a stream of income.

VII. CHARITABLE LEAD TRUST

A. What Is It?

A Charitable Lead Trust (CLT) is another trust that creates two distinct interests (sometimes called a "split interest" trust). It creates the exact same interests as the CRT—an income interest and a remainder interest. With a CLT, however, the charity receives the income interest (*i.e.*, the leading interest) and the designated beneficiary (often the donor or the donor's heirs) receives the remainder interest. Like the CRT, the Internal Revenue Code grants the donor some optionality in the trust's construction, allowing them to choose, amongst other variables, the tax treatment, the term (years or lifetime(s)), and the income payout amount.

The tax consequences of a CLT vary dramatically based on the trust's composition. Contributions to grantor trust CLTs using a guaranteed annuity or unitrust interest are eligible for an income tax charitable deduction upon formation.[26] The deduction is equal to the present value of the charity's income interest, which, unsurprisingly, is determined by the value of the contribution, the trust term and payout, and the section 7520 rates published by the IRS.[27] While an immediate income tax charitable deduction is available *at formation* for a grantor trust CLT, there is no deduction available as income is actually paid to the charity(ies) and, because it is a grantor trust, the grantor is taxed on the trust's income.

On the other hand, contributions to a non-grantor CLT are not eligible for an income tax charitable deduction. Of course, the grantor is not subject to the ongoing income tax burden of the trust. Furthermore, pursuant to IRC section 642(c), the nongrantor trust may take an income tax charitable deduction for every dollar of income distributed to the charity(ies) in the year of the distribution.

These trusts[28] provide a unique intersection between income tax planning, charitable planning, and transfer tax planning. In general, section 2702 deems the value of a retained interest equal to zero, which prevents the donor of a split interest trust from reducing the gift tax liability of a completed gift by the value of his or her retained interest. There are many exceptions to this rule, however, including CRTs[29] and CLTs.

As it applies to CLTs, if the remainder interest is retained by the donor there is no taxable gift and, upon the donor's death, the trust assets are included in the donor's estate. However, if the donor names another remainder beneficiary, such as his or her children, a taxable gift results and the trust estate is not included in the donor's estate for estate tax purposes. In the case of a "zeroed out" CLT, the taxable gift will be zero, making this an attractive transfer

tax strategy similar to Grantor Retained Annuity Trusts ("GRATs").

A typical strategy uses a testamentary "zeroed out" CLT created by the donor's Last Will and Testament. After all basic estate tax exclusion is spent, the remaining assets fund the testamentary CLT, which is entitled to an estate tax charitable deduction in full, and thus does not create estate tax. The appreciation (net of income tax paid, as this type of CLT is not eligible for the section 642(c) income tax charitable deduction) passes to the heirs estate tax free.

This exact same concept—and it is the same used with GRATs—applies during life. If the donor identifies assets with appreciation potential in excess of the section 7520 rates, a "zeroed out" CLT will transfer appreciation to heirs estate tax free and, in the case of a grantor CLT, generate an accelerated charitable income tax deduction to offset bunched income.

Should the donor desire to make the gift exempt from generation skipping transfer tax, the donor will need to engage in more complex planning, as unfavorable rules make it difficult to leverage GST exemption in this context.

Last of all, care should be paid to selecting the term length for grantor trusts. If the donor predeceases the CLT term, the trust suffers an income tax recapture of the difference between the charitable deduction taken by the grantor upon formation and the actual distributions to charity made before the grantor's death.

B. What Are Its Pros/Cons?

A CLT presents the client with opportunity to alter their tax landscape through charitable giving and transfer tax planning. Carefully planning around asset selection and investment choices enhances these results. Unfortunately, considerable forecasting is required to put the client in precisely the position they plan to reach. CLTs (and CRTs) are sophisticated solutions and deliver tailored results for clients willing to work through all the options and potential, but uncertain, outcomes. They are much too complex for most philanthropic actors.

C. When Would I Use It?

Generally, donors with motives superior to the charitable motive, such as income tax planning or transfer tax planning, are better candidates for CLTs. A grantor trust CLT is an efficient tool for clients with bunched income because it provides an increased deduction in the year of the bunched income and recognition of the trust income in later years when the client's tax bracket is lower. A non-grantor trust CLT can shift to charity income that would otherwise go to pay transfer taxes.

VIII. SUPPORTING ORGANIZATION

A. What Is It?

The aptly named Supporting Organization is a corporation that receives tax exemption[30] because its sole purpose is the support of public charities other than Private Foundations and other Supporting Organizations. The public charities it supports are termed "Supported Organizations." Its stated purpose and actual activities are to provide contributions to Supported Organizations. It provides no other service and conducts no other kind of activity.

In this way it is very much like a Donor Advised Fund. In practice, a Supporting Organization is a holding pen for charitable contributions before they are employed in charitable activities. Accordingly, like a Donor Advised Fund, a Supporting Organization does not carry on charitable activities but, rather, donates to specified public charities. These charities may be specified by name or class.

B. What Are Its Pros/Cons?

Like a public charity, a Supporting Organization must clear a series of hurdles to receive tax-exempt status. Unlike a traditional public charity, the Supporting Organization is examined for its connection to the Supported Organizations.[31] In a way, a Supporting Organization's activities consist of contributions to the Supported Organizations. It does not carry on charitable activities. In a way, a Supporting Organization borrows tax-exempt status from the charities it supports, which carry on the charitable activities.

Rather than illustrate a Supporting Organization by drawing on its contrasts to other charitable vehicles, it is more informative to highlight that it is an amalgamation of the best attributes of several other vehicles. This does not mean it is the perfect solution. Far from it, as discussed in the next subheading.

A Supporting Organization combines the independence[32] of a private foundation, the high deductibility limits of a public charity, and the time-delay[33] of a DAF. Often the donor retains near-complete control over the investment policies, asset allocations, and types of investments. Furthermore, because the Supported Organizations possess transparency and, to some extent, participation in the management of the Supporting Organization, the donors to Supporting Organizations benefit from the same deductibility standards as the Supported Organizations.

C. When Would I Use It?

Because a Supporting Organization is best viewed as an amalgamation, it is best suited for donors whose preferences are also an amalgamation. These statements describe the type of donor that should seriously consider a Supporting Organization and identify the narrow circumstances in which its utility will be preferred to that of a DAF:

- I am willing to create and maintain this entity and apply for its tax-exempt status.
- I desire to contribute today while benefiting the charity at a later date, but I want *more* control over the organization than an advisory relationship, such as a DAF, provides.
- I am willing to surrender some control to gain higher deductibility limits, but my grant criteria differ from DAFs I know.

Additionally, Supporting Organizations provide utility in a few specific legal situations:

- The donor desires to make a large grant, which does not help the donee satisfy its public support test[34] in the long term. A Supporting Organization formed by the Supported Organization allows it to receive the large grant over time and, therefore, continue to satisfy the public support test.
- The donee may not accept the type of asset contributed. The donor can contribute it to a Supporting Organization and convert it into an asset class the donee will accept without suffering the tax consequences before contribution.
- Low basis, closely held stock contributed to a private foundation provides little deduction to the donor. This problem is eliminated by donation to a Supporting Organization.
- Adverse consequences arise when a public charity controls 80% or more of the stock of a for-profit corporation. Dividing stock ownership with the Supporting Organization eliminates these consequences while still benefiting the Supported Organization.

IX. CHARITABLE GIFT ANNUITY

A. What Is It?

A charitable gift annuity is a contract with a single charity. This option is relatively straightforward because it does not require the donor to create and administer a trust or entity. The donor makes a gift to the charity and, in return, receives an annuity for his or her lifetime (and potentially his or her spouse's lifetime). The donor will receive an income tax deduction based on the present value of the amount the charity will receive in the future.[35]

B. What Are Its Pros/Cons?

This option is somewhat like a CRT but much simpler in nature. However, with a Charitable Gift Annuity, the donor does not retain the flexibility to change the designated charity at a later date. It is also very important for the donor to carefully review the annuity payment projections and the assumptions underlying those projections to ensure that the annuity payments will be sufficient to support the donor's financial security, if that is important to the donor. Furthermore, because the charity will have control over the investments, the donor should also be very comfortable with the financial strength and sophistication of the charity. Finally, many charities will not have the ability to receive a complex asset, such as an interest in a closely held business.

C. When Would I Use It?

A charitable gift annuity makes sense for a donor who wishes to make one large gift to one charity and is very confident those wishes will not change over the donor's lifetime. Like the CRT, this approach can be used to time a charitable deduction and retain an income stream for financial security.

X. CHARITABLE LLC

A. What Is It?

A charitable LLC is simply an LLC where a family chooses to hold assets that are designated for charitable giving but have not been gifted yet.

B. What Are Its Pros/Cons?

A charitable LLC is the most flexible structure for charitable giving. The owner of the LLC has complete control over the investment of the assets and the timing and amount of any transfers to charity. There are no minimum distributions and no application of the private foundation rules related to self-dealing, excess business holdings, jeopardizing investments, or taxable expenditures. A charitable LLC is also completely private. This structure can be used to set aside assets that an individual wishes to utilize to further his or her charitable goals in the future while retaining complete flexibility in how those assets are managed in the meantime. If an immediate deduction is not necessary, this approach can allow for the development of a framework around charitable giving, and potentially a long-term philanthropic mission, without the complex and sometimes unforgiving rules that apply to some other charitable giving structures.

A charitable LLC, however, is not a tax-exempt entity. The tax consequences of any income generated inside the LLC are generally passed out to the owner of the entity.[36] In addition, there is no income tax deduction available upon the initial funding of the LLC. Any tax deductions will only be available when the LLC transfers assets to an individual charity. In this way, a charitable LLC isn't truly a charitable entity, at least for tax purposes.

Unfortunately, these vehicles have gained some notoriety for potential abuses. Detailing the types of transactions that approach the line between permissive and abusive is beyond the scope of this article, but we suggest a review of IRS Notice 2004-30 and *U.S. v. Meyer*[37] for additional information.

C. When Would I Use It?

Charitable LLCs are a great option for families that wish to plan for future charitable giving but have no need for a current deduction. The LLC governing documents can be used to express a family's values and begin to create a structure and succession plan for their philanthropy.

XI. CONCLUDING THOUGHTS & CHARTS

Philanthropy is inherently intimate and idiosyncratic and, therefore, warrants a tailored and thoughtful approach. We caution practitioners from developing familiarity with only one or two vehicles as they may fall victim to the adage: "To a man with a hammer, everything looks like a nail." With this article we believe the reader is armed with a variety of tools and, through detailed consultation, will marry their client's wishes with the legal and practical limitations encumbering the variety of structures.

To that end, we conclude with various charts to provide visual and ease-of-reference utility. Three visual charts track the progression of the various vehicles through three different important categories, namely Family Involvement, Control, and Simplicity vs. Complexity. Because DAFs, Private Foundations, and Private Operating Foundations are often discussed in the same breath, we provide a separate chart comparing those structures. Similarly, because CLTs and CRTs are seemingly related, a chart identifying their differences is included. Finally, a quick reference guide describes the timing and technical items of each vehicle.

** Margot Edwards is a Wealth Advisor with JP Morgan Private Bank in Denver, Colorado.*

***Aaron Hegji is a Chief Fiduciary Officer with Wealthgate Trust Company in Las Vegas, Nevada.*

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	Donor Advised Funds	Private Foundations	Operating Foundations
Governance and Succession	Donors may name advisors to recommend grants and investments. Donors may also name successor advisors to the account to ensure a continuing legacy.	Board of directors or trustees set general purpose and are responsible for operations based on bylaws or trust instrument. Board defines parameters for succession and perpetuity, including ongoing donor family participation and control.	Same as Private Foundation
Startup Costs and Timing	Typically none and can be established immediately	Startup is generally managed by an attorney or accountant to adhere to IRS and state filing requirements. Generally, takes several weeks or a few months to be formally approved by the IRS, but can operate immediately based on a good-faith effort to adhere to federal tax law.	Same as Private Foundation
Privacy	Sponsoring organization files informational tax returns with the IRS. Donor names may be disclosed to the IRS but are not made available to the public.	Files federal tax returns that are available for public review. Returns include information on donors, grants, investment fees, director or trustee fees, staff salaries, etc.	Same as Private Foundation

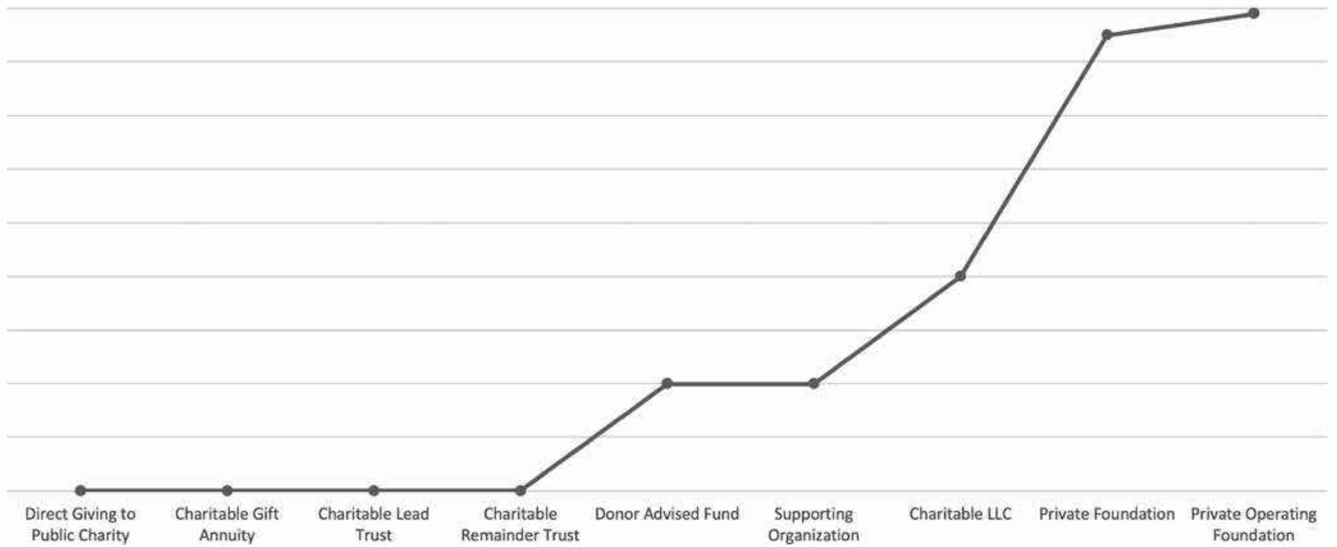
Control of Grants and Assets	Donors may recommend, but not direct, grants and investment allocations to a sponsoring organization, which reviews and makes all final decisions.	Board has complete control of all grantmaking and investment decisions, subject to self-dealing and prudent investment rules.	Same as Private Foundation
Ongoing Administrative Management	Varies according to the sponsoring organization and level of services.	Staffing generally based on scope and scale of grant making; must file annual federal tax returns and adhere to state requirements for nonprofit corporations or charitable trusts.	Staffing generally based on scope and scale of the foundation's operations; must file annual federal tax returns and adhere to state requirements for nonprofit corporations or charitable trusts.
Excise Tax (on Investment Income)	None	1.39% of net investment income annually[38]	Same as Private Foundation
Tax Deduction Limits for Gifts of Cash[39]	Up to 60% of adjusted gross income	Up to 30% of adjusted gross income	Up to 60% of adjusted gross income
Tax Deduction Limits for Gifts of Appreciated Property[40]	Up to 30% of adjusted gross income	Up to 20% of adjusted gross income	Up to 30% of adjusted gross income
Valuation of Gifts for Purposes of Tax Deduction (subject to holding period considerations)	Fair market value	Generally, fair market value for gifts of cash and publicly traded stock, and cost basis for gifts of closely held stock or real property.	Fair market value
Distribution Requirements	None	Generally, 5% annual minimum distribution is required, based on investment returns adjusted by income and investment tax payments, charitable expenses and distribution over five years.	Must spend at least 85% of its adjusted net income or its minimum investment return, whichever is less, directly for the active conduct of its exempt activities (the income test). In addition, the foundation must meet one of the following tests: assets test endowment test support test

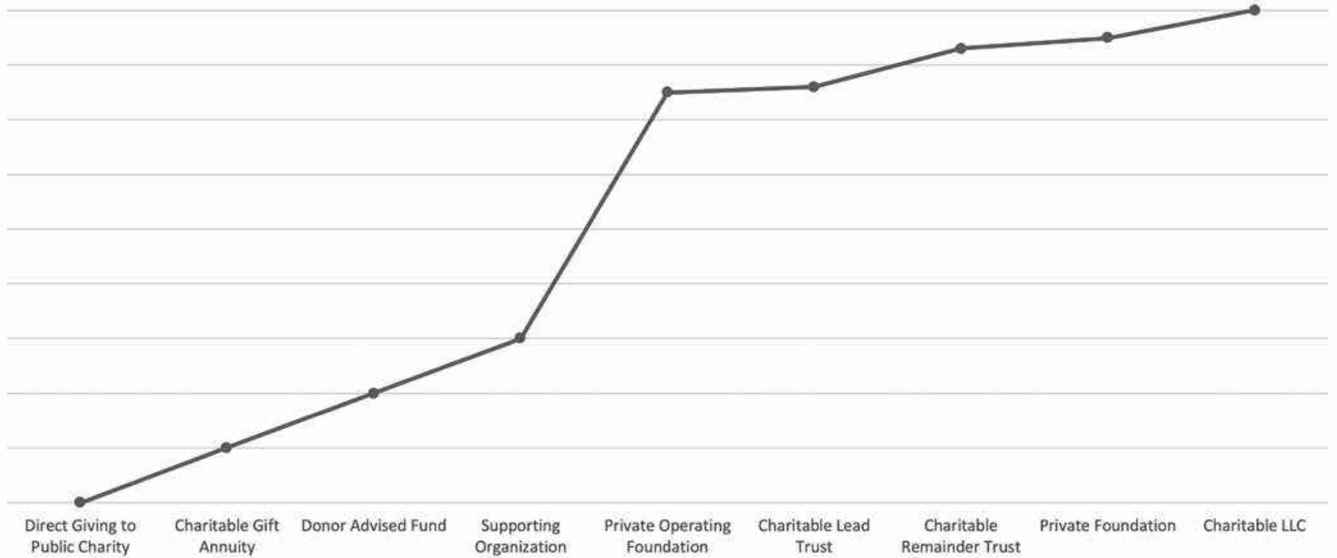
	Charitable Remainder Trust	Charitable Lead Trust
Income Interest	Donor's discretion	Charity
Remainder Interest	Charity	Donor's discretion
Best AFR	High	Low
Term	Life or term not to exceed 20yrs	Usually term, sometimes life
Taxation	Tax deferred	Taxable
Investment Performance	High appreciation accrues to charity	High appreciation accrues to donor/heirs
Common Usage	Tax deferral for sale of appreciated asset; secure income stream; also accelerated tax deduction to offset bunched income	Transfer tax planning; accelerated income tax deduction to offset bunched income for grantor trust

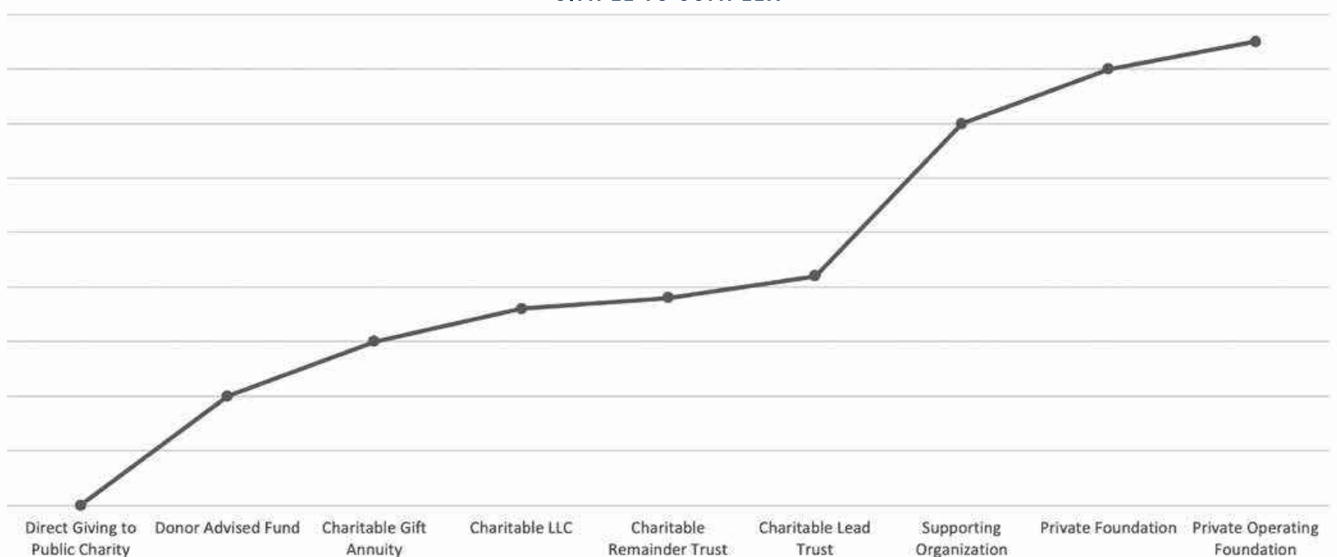
	Direct Giving to Public Charity	Donor Advised Fund	Private Foundation	Private Operating Foundation	Charitable Remainder Trust	Charitable Lead Trust	Supporting Organization	Charitable Gift Annuity	Charitable LLC
Timing of Deduction	Immediate	Immediate	Immediate	Immediate	Immediate	Immediate for grantor trust; N/A for nongrantor trust	Immediate	Immediate	Not until contribution made
Timing of Charity's Access	Immediate	At donor's discretion	Minimum annual grant requirement	Minimum annual grant requirement	Expiration of term	Annual payment requirement	At Supporting Org's discretion		Not until contribution made

	Direct Giving to Public Charity	Donor Advised Fund	Private Foundation	Private Operating Foundation	Charitable Remainder Trust	Charitable Lead Trust	Supporting Organization	Charitable Gift Annuity	Charitable LLC
Tax Deduction Limitations	60% of AGI for cash; 50% of AGI for noncash, noncapital assets; 30% of AGI for capital assets	Same as Direct Giving	30% of AGI for cash; 20% for all noncash	Same as Direct Giving	Correlates directly with the type of exempt organization eligible as remainderman	Correlates directly with the type of exempt organization eligible for income interest	Same as Direct Giving	Correlates directly with the type of exempt organization eligible as remainderman	N/A
Valuation Limitations	None	None	Cost basis for closely-held stock and real property	None	Correlates directly with the type of exempt organization eligible as remainderman	Correlates directly with the type of exempt organization eligible for income interest	None	Correlates directly with the type of exempt organization eligible as remainderman	N/A
Taxes*	Tax exempt	Tax exempt	Excise tax of 1.39% on net investment income	Excise tax of 1.39% on net investment income	Tax deferred	Grantor trust taxed to donor; nongrantor trust taxed to trust	Tax exempt	Taxed the same way as the charity recipient	Taxable entity

*Unrelated business taxable income applies to all vehicles except the Charitable LLC


LEAST TO MOST FAMILY INVOLVEMENT
Direct Giving to Public Charity
Charitable Gift Annuity
Charitable Lead Trust
Charitable Remainder Trust
Donor Advised Fund
Supporting Organization
Charitable LLC
Private Foundation
Private Operating Foundation


LEAST TO MOST CONTROL
Direct Giving to Public Charity
Charitable Gift Annuity
Donor Advised Fund
Supporting Organization
Private Operating Foundation
Charitable Lead Trust
Charitable Remainder Trust
Private Foundation
Charitable LLC


SIMPLE TO COMPLEX
Direct Giving to Public Charity
Donor Advised Fund
Charitable Gift Annuity
Charitable LLC
Charitable Remainder Trust
Charitable Lead Trust
Supporting Organization
Private Foundation
Private Operating Foundation

01 Rev. Rul. 78-197, 1978-1 C.B. 83.

02 IRC, section 170(f)(11)(C).

03 IRC, section 170(b).

04 IRC, section 170(e).

05 IRC, section 4966(d)(2).

06 IRC, section 170(e).

07 Treas. Reg. section 1.170A-4.

08 IRC, section 170(e)(1)(B).

09 For example, IRC section 4949 imposes an excise tax on net investment income, and IRC section 4942 imposes a minimum distribution requirement. Self-dealing is prohibited and insider compensation is scrutinized.

10 IRC, section 4946.

11 IRC, section 4941(d).

12 IRC, sections 4943 and 4944.

13 IRC, section 4945.

14 Substantially all (*i.e.*, at least 85% of its adjusted net income) is used in the charitable activities.

15 65% of the foundation's assets are directly used in the active conduct of the foundation's purpose.

16 The foundation makes qualifying distributions each year in an amount equal to 3.3% of its investment assets for the active conduct of its purposes.

17 At least 85% of the foundation's support comes from (1) five or more exempt organizations that are not related to either the private operating foundation or to each other and (2) the general public. No more than 25% of the foundation's support can come from any one of the exempt organizations. Finally, no more than half of the organization's support can come from gross investment income.

18 IRC, section 4942.

19 IRC, section 664(d).

20 IRC, section 664(c)(1).

21 IRC, section 170(f)(2).

22 Treas. Regs. 1.664-2 & 1.664-4.

23 Treas. Reg. 1.664-3(a)(5)(i).

24 Treas. Reg. 1.664-3(a)(1)(i)(b).

25 Treas. Reg. 1.664-3(a)(1)(i)(c).

26 For comparison purposes, higher section 7520 rates increase the deduction size of CRTs but lower the deduction size of CLTs. Higher section 7520 rates reduce the size of the present value of the income interest. A charitable deduction for a CLT is based on the income interest, which is reduced by higher section 7520 rates. Alternatively, the deduction for a CRT is based on the remainder interest, which is increased by higher section 7520 rates.

27 Rev. Proc. 2007-45, 2007-29 I.R.B. 89.

28 Both CLTs and certain types of CRTs. See Treas. Reg. 25.2702-1(c).

29 The exception does not apply to certain NIMCRUTs.

30 Tax exemption is provided by IRC, section 509(a)(3).

31 These hurdles are found in IRC, section 509(a)(3) and given the nomenclatures "Organizational Test," "Operational Test," "Control Test," and "Relationship Test." The Organizational Test requires the Supporting Organization's governing documents to limit the organization's purpose to supporting the Supported Organizations. The Operational Test requires the Supporting Organization's activities to actually support the Supported Organizations. The Control Test prevents disqualified persons from managing the Supporting Organization. Finally, the Relationship Test classifies Supporting Organizations into one of three types, according to the relationship between the Supported Organizations and the Supporting Organization.

32 Donors can control its formation, implementation, and administration, subject to statutory limitations. See IRC, section 509(a)(3).

33 That is, the tax consequences that flow from contributions received before the contributions are actually put to use by the charity.

34 The Public Support Test applies to public charities and, in simple terms, requires the public charity to receive at least one-third of its donations from donors that give less than two percent (2%) of the charity's total receipts. In short, it prevents a public charity from receiving a super-majority of donations from a limited set of donors.

35 IRC, section 501(m)(5).

36 Charitable LLCs are typically disregarded, or could be taxed as partnerships, but are unlikely to be taxed as C corporations.

37 See *U.S. v. Meyer* (11th Cir. 2022) 50 F.4th 23 (and related trial court filings).

38 For tax years beginning after December 20, 2019.

39 Any unused deductions may be carried forward up to five (5) additional years. Note: A gift to a DAF generates the same tax deduction as an outright gift to charity. This table assumes that all property has been held by the donor for more than one year. Federal tax law limits the deductible amount of charitable gifts depending on the asset given, the donor's adjusted gross income, and the status of the charity receiving the gift.

40 See note 39, *ante*.