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Delaware Tax Institute

Charitable Planning After Tax Reform and In a New Interest Rate Environment

December 7, 2018

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Preliminary Note on Scope of Presentation

Charitable gift planning can be astonishingly complex. The purpose of this presentation is not to answer all of these complexities, but to consider how best to present complex structures to donors in light of their philanthropic goals, their assets, their family needs, and their tax concerns, particularly as impacted by the 2017 Tax Cuts and Jobs Act and by a changing interest rate environment.

Numerous technical rules apply to virtually every gift strategy, and failure to comply precisely can often lead to loss of the tax deduction for the gift or of tax-exemption for the structure created. An important part of charitable gift planning is meeting the complex regulatory requirements for valuation, including obtaining “qualified appraisals,” and acknowledgements of charitable contributions. A detailed discussion of these rules is beyond the scope of this presentation, but it is important for donors to ensure compliance, as the charitable deduction for the gift can be denied due to non-compliance.

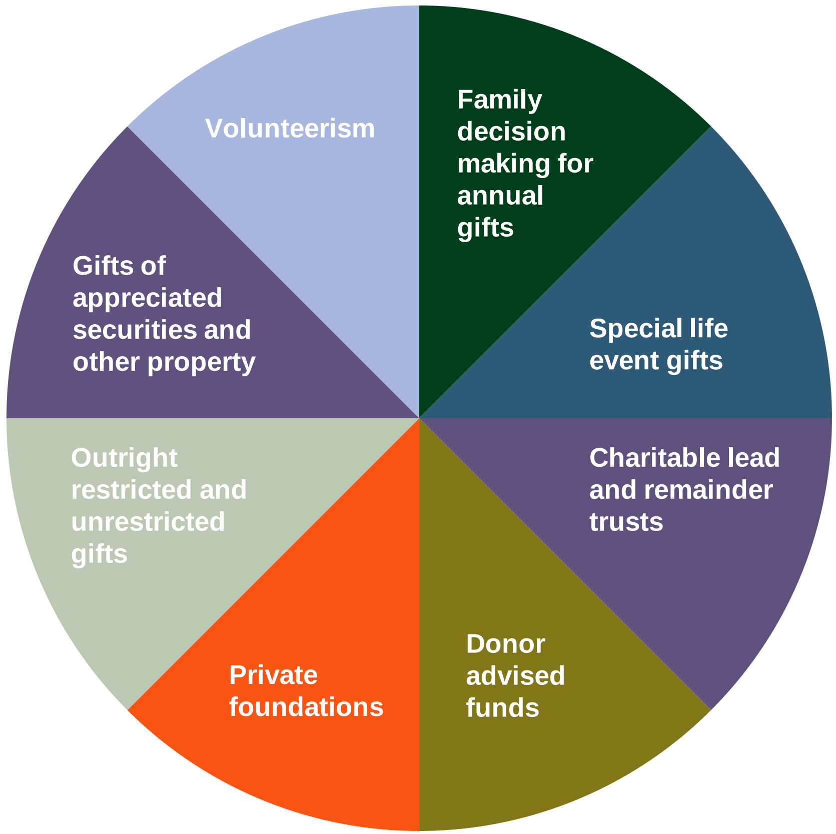
Joining the Philanthropic Conversation

Through philanthropy donors can:

- Give back
- Create a legacy
- Support causes they believe in
- Promote family values and social responsibility
- Leverage tax-deductible nature of charitable gifts

Discussing these goals with donors allows advisors to have a more complete picture for planning purposes and can deepen a relationship.

Advisors Can be Key in Helping Donors Organize a Philanthropic Portfolio



"Giving should be entered into in just the same careful way as investing. Giving is investing."

—John D. Rockefeller

THE NEW INCOME AND ESTATE TAX ENVIRONMENT

2018 Tax Landscape for Philanthropic Taxpayers

Income tax rates lowered	Top rate of 37% applies to taxable income over: $600,000 (married) $500,000 (single); rate returns to 2017 law after 2025
Capital gains (long term) and dividends highest rate unchanged	Top rate of 20% applies to taxable income over: $479,000 (married) $425,800 (single)
Surtax on Net Investment Income unchanged	3.8% tax applies to Adjusted Gross Income (AGI) over: $250,000 (married) $200,000 (single)
Standard deduction nearly doubled	$12,000 (single and all other taxpayers); $18,000 (head of household); $24,000 (married); indexed for inflation after 2018, returns to 2017 law after 2025
Charitable deduction slightly enhanced	Charitable contributions of cash gifts to public charities are deductible up to 60% of AGI; returns to 50% AGI limit after 2025
Charitable deduction eliminated for college athletic seating rights	Eliminate charitable deduction for 80% of payment to colleges and universities for right to purchase tickets for athletic events
Itemized deductions reduced	Limits combined deduction for state and local income, sales, and property tax to $10,000 through 2025 Limits home mortgage interest deduction for new mortgages from 2018-2025 to $750,000 of indebtedness; repeals deduction for home equity interest
Phase-out of Itemized deductions	Eliminates the phase-out of itemized deductions through 2025
Estate, gift, and GST tax exemption increased **Highest tax rate unchanged**	$11,180,000, as indexed for inflation In 2026, returns to $5,000,000 as indexed for inflation 40% Charitable deduction retained

Selected Changes Under the 2017 Tax Cuts and Jobs Act for Charitable Entities

	Law in 2017	Tax Cuts and Jobs Act*
Private Foundations – excise tax on net investment income	2% excise tax on net investment income, which is reduced to 1% for years in which foundation distributions exceed historic level. IRC Section 4940.	No change.
Private Foundations – excess business holding rules on business ownership	Private foundations are subject to an excise tax on ownership of more than 20% (35% if no control) of the voting stock, profits interest, or beneficial interest of a business enterprise. IRC Section 4943.	Unchanged by Act; but changed on February 9th, 2018 by the Bipartisan Budget Act of 2018 to provide an exception for business enterprise 1) held 100% by private foundation, none of which was purchased; 2) which distributes all income annually to the private foundation; and 3) meets an independent operation test. New IRC Section 4943(g).
Charitable deduction for electing small business trusts	Section 642(c) deduction applies.	Section 170 deduction applies.
Taxation of college and university endowments	Traditional endowment income such as interest, dividends, capital gains, rents, royalties, and annuities, exempt from tax under Section 512(b).	1.4% excise tax on net investment income of private colleges and universities meeting an assets and student tuition test. New IRC Section 4968.
Unrelated business taxable income	Income and losses from unrelated business activities aggregated.	Income and losses from separate unrelated business activities must be calculated separately, prohibiting deduction for losses from one activity against income from a different activity. New IRC Section 512(a)(7).
Excise tax on excessive compensation	None	21% excise tax on compensation greater than $1,000,000 paid to covered employees and on excess parachute payments. New IRC Section 4960.

New Exception to Private Foundation Excess Business Holding Rules Under IRC Section 4943(g)

- Section 4943 limits a private foundation's holding of a business enterprise, making it very difficult to craft an estate plan in which a closely held company can be owned long-term by a private foundation
- Section 4943 permits a private foundation to hold an interest in a business enterprise as follows:
  - 20% of the voting stock, profits interest, or beneficial interest
  - Ownership can be increased to 35% if it can be demonstrated that the 35% ownership interest is not controlling
  - In testing the ownership percentage, the foundation's ownership must be aggregated with the ownership of all disqualified persons with respect to the foundation
  - A de minimus limit permits ownership up to 2% without aggregation with disqualified persons
- A business enterprise includes any business, unless it is functionally related to the foundation's charitable purposes, or the business derives at least 95% of its gross income from passive sources
- New section 4943(g), often called the Newman's Own exception, sets forth a very limited exception, which fit the circumstances of the Newman's Own Foundation's sole ownership of the Newman's Own business. Because of its requirements, it may be difficult for many foundations to take advantage of the provision.

New Exception to Private Foundation Excess Business Holding Rules Under IRC Section 4943(g) (continued)

- New Section 4943(g) permits a foundation to own 100% of a business enterprise if the following requirements are met:
- Ownership requirement:
  - foundation must hold 100% ownership of the voting stock
  - all stock, voting and nonvoting, must be acquired other than by purchase
- Income requirement:
  - the net operating income of the business enterprise must be distributed to the foundation annually, within 120 days after the close of the taxable year
- Independence Requirement:
  - Independence of business enterprise: no substantial contributor to the foundation or a family member may serve as an officer, director, trustee, manager, employee, or contractor of the business
  - Independence of the foundation: a majority of the foundation's board must not be managers of the business, or family members of a substantial contributor to the foundation
  - No loans from business enterprise: the business enterprise may not make any loans to a substantial contributor or a family member
- Note that Section 4943(g)'s income distribution requirement is separate from the Section 4942 5% distribution requirement, which must also be met.

New Charitable Deduction Rule for Electing Small Business Trust (ESBT)

- Under prior law Section 642(c) provided a charitable contribution deduction for trusts, including ESBTs
  - To the extent of trust gross income
  - Pursuant to a governing instrument
- Section 681 limits the 642(c) deduction to the extent the trust has income, which if the trust were charitable, would be treated as unrelated business income under Section 511
- S Corporation income is treated as unrelated business taxable income, resulting in a reduced 642(c) deduction

New Rule

- When an electing small business trust (ESBT) is allocated a charitable deduction as an S Corp shareholder, it is now subject to the same limits that apply to an individual under Section 170. Note that the S Corp itself must make the charitable contribution.
- Consequence:
  - the individual AGI limits ranging from 20 to 60% apply
  - The trust document requirement is eliminated
  - The contribution need not be made from gross income
  - The carry forward rules of section 170 apply
- Note that for trusts which hold both S Corp stock and other assets, the trust will be subject to two different charitable deduction rules

Permitted Deductible Charitable Contributions for Federal Income Tax Purposes—IRC Section 170(b)(1)

Charitable Gift Categories	Adjusted Gross Income [(1)(3)(4)]
Gifts of Cash to Public Charities and Certain Foundations • Colleges, universities, museums, hospitals, United Way-type organizations • Donor Advised Funds • Supporting Organizations • Conduit Foundations • Operating Foundations	60% [5]
Gifts of Long-Term Capital Gain Property (including appreciated stock) to Public Charities and Certain Foundations	30%
Gifts of Cash to Private Foundations	30%
Gifts of Long-Term Capital Gain Property to Private Foundations Additional limitations: Full fair market value deduction permitted only for gifts of qualified appreciated stock, which is stock traded on an established securities market. [(2)]	20%

Notes

(1) Adjusted gross income does not include income exempt from federal income tax.

(2) Qualified appreciated stock is limited to 10 percent of the outstanding stock of a corporation, including all prior gifts made by donor and family members to any private foundations.

(3) Does not address phase-out of deductions for higher income taxpayers (Eliminated for tax years 2018 until 2025).

(4) Does not address alternative minimum tax.

(5) Reverts to 50% after 2025

Charitable Planning Under the New Tax Law

The 2017 Tax Cuts and Jobs Act (the Act) is voluminous and complex, and attorneys, accountants, financial advisors, donors and charities will be grappling with its impact for many years. But a number of themes and opportunities have emerged to consider in 2018 and beyond.

Changes impacting the charitable deduction

Although the Act eliminated or dramatically reduced most itemized deductions, it retained the charitable contribution deduction. The deduction for cash contributions to public charities was even enhanced, permitting cash contributions up to 60% of adjusted gross income, rather than 50% under prior law. However, for many donors the tax advantages of charitable giving will be impacted by rate reductions and other changes. As a consequence of the increased standard deduction and the elimination of many itemized deductions, many donors will no longer be able to itemize deductions, losing many (but not all) of the tax incentives for charitable giving. But for those donors who can still itemize, itemized deductions are no longer subject to the itemized deduction phase-out. And for very high-net-worth donors who are still subject to the federal or state estate tax, the charitable deductions from estate, gift, and generation-skipping transfer tax still apply.

Charitable planning for donors who still itemize

- Lifetime charitable gifts made outright to public charities, private foundations, and donor advised funds can provide both income and estate tax advantages.
- Gifts can also be structured to benefit both family and charity through charitable remainder and lead trusts, and for smaller gifts, charitable gift annuities.
- Gifts can be made even more tax efficient by donating appreciated property such as publicly traded stock, and in some cases, closely held businesses and collectibles.
- See general charitable planning rules on page 11.

Charitable planning for donors who can no longer itemize

- A donor over age 70½ can take advantage of the special rule permitting up to $100,000 of IRA distributions directly to a qualified charity. This has the same impact as a charitable deduction, because the amount of the IRA distribution to charity is not included in income.
- While not generating a deduction for non-itemizers, gifts of appreciated property still save the capital gains taxes that would have been due if the asset were sold. For low basis assets, that can still provide significant tax savings.
- Some donors will be able to bunch their deductions, making larger deductible gifts every few years, possibly into a donor advised fund.

General Income and Estate Tax Considerations in Charitable Giving

- Gifts to charity during life or at death are not subject to estate or gift tax
- With increased federal estate tax exemption, many donors will not need a charitable estate tax deduction
- Gifts during the donor's lifetime may provide an income tax deduction, and careful planning can take advantage of high adjusted gross income ("AGI") years
- Lifetime gifts also eliminate future taxable income to the donor from the gifted assets
- The value of the charitable contribution deduction, when available, depends on the applicable tax rate. Charitable contributions made when higher rates apply will generally produce more savings:
  - In 2018, the highest rate on capital gains and dividends is 20%, and the highest ordinary income rate is 37%
  - In addition, a surcharge of 3.8% applies to the net investment income of high income taxpayers
- The overall limitation on itemized deductions is eliminated for tax years 2018 until 20125
- In planning for a long-term series of gifts, note that the maximum deduction limits change annually based on adjusted gross income:
  - The carry-forward for unused deductions (above the applicable percentage limits) is only 5 years, so deductions can be lost permanently
- Cash gifts and gifts to public charities are subject to higher deduction limits, but cash gifts don't offer as many tax planning opportunities

Mitigating the Loss of the Charitable Income Tax Deduction

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Charitable Giving With IRAs—IRC Section 408(d)(8)

For a non-itemizer, charitable distributions from an IRA can be as tax-effective as the lost deduction

- IRAs are attractive assets for charitable gifts as they eliminate the income tax that non-charitable beneficiaries would otherwise pay on receipt of the assets and can also reduce estate tax
- The IRA charitable rollover provision for lifetime gifts of IRA assets, first enacted for 2006 and 2007, was made permanent by the Protecting Americans from Tax Hikes (PATH) Act of 2015
  - An individual who has reached age 70½ can transfer up to $100,000 from an IRA to a “qualified charity”
  - The transfer can count toward the required minimum distribution
  - The transfer is not deductible for income tax purposes as a charitable gift and is not subject to federal income tax
  - Transfers can not be made to most private foundations, or to donor advised funds or supporting organizations

Charitable Giving With IRAs (continued)

- The IRA charitable rollover is helpful for taxpayers
  - Who do not itemize deductions
  - Seeking to minimize their AGI so as to stay below the threshold for the 3.8% surtax on net investment income
  - Who have already maximized their permitted charitable contribution deductions
  - Who live in a state that does not provide for charitable contribution deductions from state income tax, or
  - Who can otherwise benefit from a lower amount of AGI
- Planning Opportunity with IRA Conversions:
  - IRA to Roth IRA conversions first became available to higher income individuals in 2010
  - A charitable gift may be an efficient offset to the tax on conversion
- IRA assets may be gifted at death without any limitations on age, amount, or type of charity, and will not be subject to estate tax
  - Naming a charity as beneficiary of an IRA can be very attractive as individual heirs will pay income tax on the entire IRA distribution

Bunching Deductions

- Some donors can avoid losing their ability to itemize deductions every year by “bunching” their contributions every 2 to 3 years and itemizing in those years
- Increased gifts to specific charities
- Growth in donor advised funds
- Donors need to communicate these plans to the receiving charities to avoid expectations of increased gifts annually and to allow the charities to plan appropriate budgets

Gifts of Appreciated Property—IRC Section 170(e)

Gifts can be tax-efficient, even if they are not always deductible

- A charitable gift can be made with stock, real estate, or tangible property, such as artwork
- If the donor has held the property for more than a year, a full fair market value deduction may be available for the gift — and the donor is not taxed on the appreciation
- If the donor no longer itemizes deductions, the capital gains tax savings is nevertheless a substantial tax benefit
- Detailed tax rules govern gifts of property
- The transfer will require paperwork, such as a deed of gift, or recording of a real estate deed

The related use requirements for gifts of tangible personal property – IRC Section 170(e)(1)(B) and (7)

- To obtain — and retain — the full fair market value deduction, a gift of tangible personal property must be used for a related purpose of the charitable donee
- In light of abuses in this area, Congress has imposed strict obligations on both the donor and donee
- Sales within 3 years of the gift trigger a number of consequences:
  - The donee must file IRS form 8282
  - If the sale is after the year of the donation, the donor must recapture the amount of the contribution that exceeded cost basis, plus interest, unless there is a donee certification on related use
  - If the property is sold by the charity in the year of donation, the donor's deduction will be limited to his or her cost basis, unless there is a donee certification on related use
  - The sale for substantially less than the amount claimed by the donor as the charitable contribution deduction may raise questions as to the validity of the initial appraised value

The New Interest Rate Environment

Applicable Federal Rate and Section 7520 Rate

Applicable Federal Rate (AFR)

- To avoid treatment of a family loan as a gift or an employee loan as compensation, loans must be made at the applicable AFR
- The AFR is set monthly by the Internal Revenue Service and tends to follow market interest rates. AFRs are set for short-term loans (up to 3 years), mid-term loans (3 to 9 years), and long-term loans (more than 9 years)

Section 7520 Valuation Rate

- The Section 7520 rate is used to value the annuity interest of a grantor retained annuity trust (GRAT) or a charitable lead annuity trust (CLAT), as well as the remainder interest of a charitable remainder trust
- The Section 7520 rate follows the AFR, as it is set at 120% of the mid-term AFR
- The Section 7520 rate is the "hurdle" that an investment in a GRAT or CLAT must out-perform in order to transfer appreciation tax-free

Both of these rates remain at relatively low historic levels, but have increased substantially from their 2013 low. The chart on the next page shows the Annual AFRs and Section 7520 rates for each January since 2001, as well as the monthly rates for 2018

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Applicable Federal Rates and Section 7520 Rates for 2018 and January 2001-2017 (Based on annual compounding)

Date	Short-term AFR (0-3 Years)	Mid-term AFR (3-9 Years)	Long-term AFR (Over 9 years)	Section 7520 Rate
Dec. 2018	2.76	3.07	3.31	3.6
Nov. 2018	2.70	3.04	3.22	3.6
Oct. 2018	2.55	2.83	2.99	3.4
Sept. 2018	2.51	2.86	3.02	3.4
Aug. 2018	2.42	2.80	2.95	3.4
July 2018	2.38	2.87	3.06	3.4
June 2018	2.34	2.86	3.05	3.4
May 2018	2.18	2.69	2.94	3.2
April 2018	2.12	2.72	3.04	3.2
March 2018	1.96	2.57	2.88	3.0
Feb. 2018	1.81	2.31	2.66	2.8
Jan. 2018	1.68	2.18	2.59	2.6
Jan. 2017	0.96	1.97	2.75	2.4
Jan. 2016	0.75	1.81	2.65	2.2
Jan. 2015	0.41	1.75	2.67	2.2
Jan. 2014	0.25	1.75	3.49	2.2
Jan. 2013	0.21	0.87	2.31	1.0
Jan. 2012	0.19	1.17	2.63	1.4
Jan. 2011	0.43	1.95	3.88	2.4
Jan. 2010	0.57	2.45	4.11	3.0
Jan. 2009	0.81	2.06	3.57	2.4
Jan. 2008	3.18	3.58	4.46	4.4
Jan. 2007	4.88	4.58	4.73	5.6
Jan. 2006	4.38	4.48	4.73	5.4
Jan. 2005	2.78	3.76	4.76	4.6
Jan. 2004	1.71	3.52	5.01	4.2
Jan. 2003	1.81	3.43	4.90	4.2
Jan. 2002	2.73	4.49	5.46	5.4
Jan. 2001	5.90	5.61	5.78	6.8

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Charitable Gifts with Split Interests

Vehicles	Description	Benefits
Charitable Remainder Trusts (CRTs)	• Grantor conveys an asset to the trust • Beneficiary receives a guaranteed income stream for life or a set term • Identified charity receives remaining value of the trust at the end of the term	• Tax-efficient for highly appreciated assets
Charitable Lead Trusts (CLTs)	• Charity receives the income from the donated assets for life or a set term • The assets pass to the beneficiaries at the end of the term	• Assets are gifted to the CLT at a reduced value • At the termination of the trust, assets pass to family without estate or gift tax
Charitable Gift Annuities (CGAs)	• Grantor gives assets to charity in exchange for an annuity • Beneficiary has a guaranteed income stream for life	• Since no trust is required, more appropriate for smaller gifts

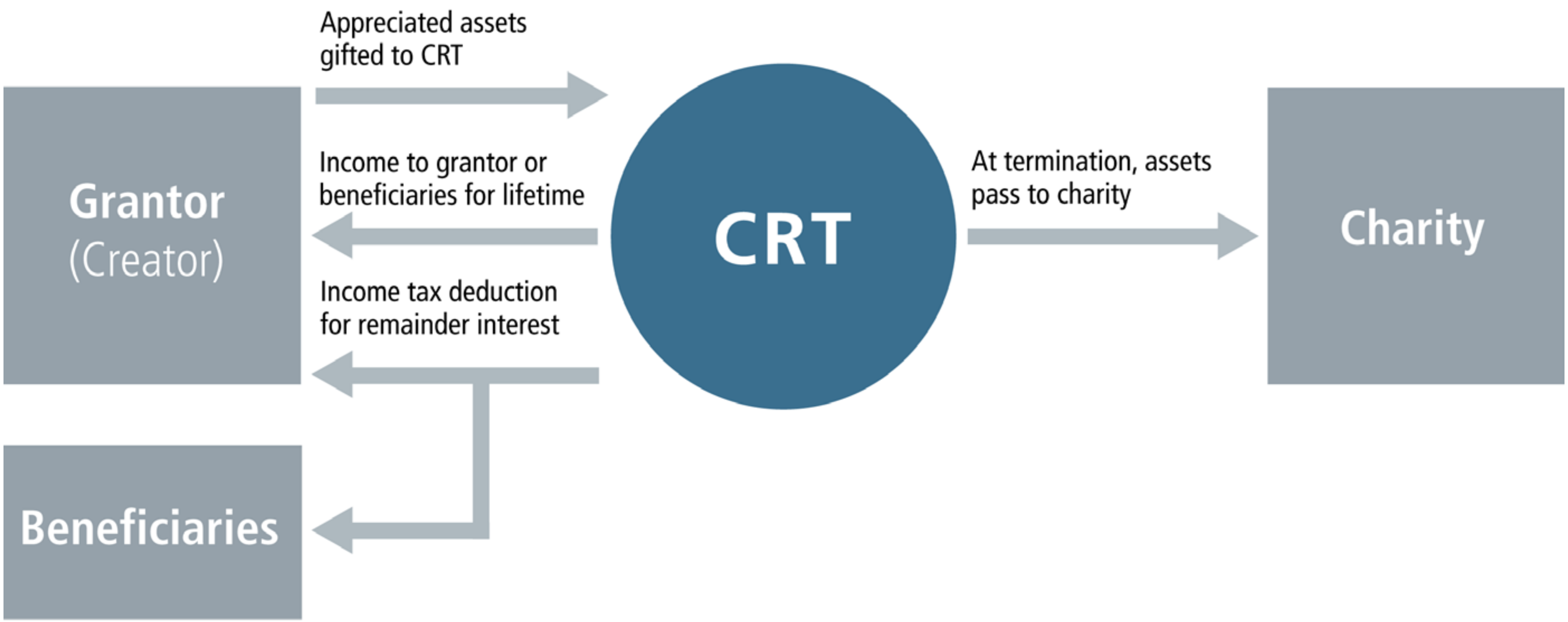
Charitable Remainder Trust (CRT)

- A CRT makes annual payments to one or more individual beneficiaries for a term of up to 20 years, or for the lives of the beneficiaries
- Form of CRT:
  - Charitable remainder annuity trust (CRAT)
  - Charitable remainder unitrust (CRUT)
  - Income only, or with makeup unitrust (NICRUT or NIMCRUT)
- Payout must be minimum of 5%, maximum of 50% of initial value (CRAT) or annual fair market value (CRUT)
- At the end of the term, the remaining assets are distributed to one or more charities, which may include a family foundation
- 10% remainder requirement
  - In a low interest rate environment it can be difficult for younger grantors of a CRAT to meet the 10% requirement
- A CRT may be created by a will or during lifetime
- Increasing AFR rates can make CRTs relatively more attractive

Charitable Remainder Trust (CRT)—IRC Section 664 (continued)

- The value of the remainder interest is not subject to estate or gift tax
- If the CRT is established during the client's lifetime, an income tax deduction is also available for the value of the remainder interest
- A CRT is particularly useful if the client's goal is to derive an income stream from highly appreciated assets for the client or other beneficiaries
- When a CRT sells appreciated assets, the capital gains tax is deferred until treated as paid to an income beneficiary
- Income from the CRT is taxed to the income beneficiaries under a tier system that taxes the distribution first as ordinary income, second as capital gains, third as other income, and last as corpus

Charitable Remainder Trust (CRT) (continued)

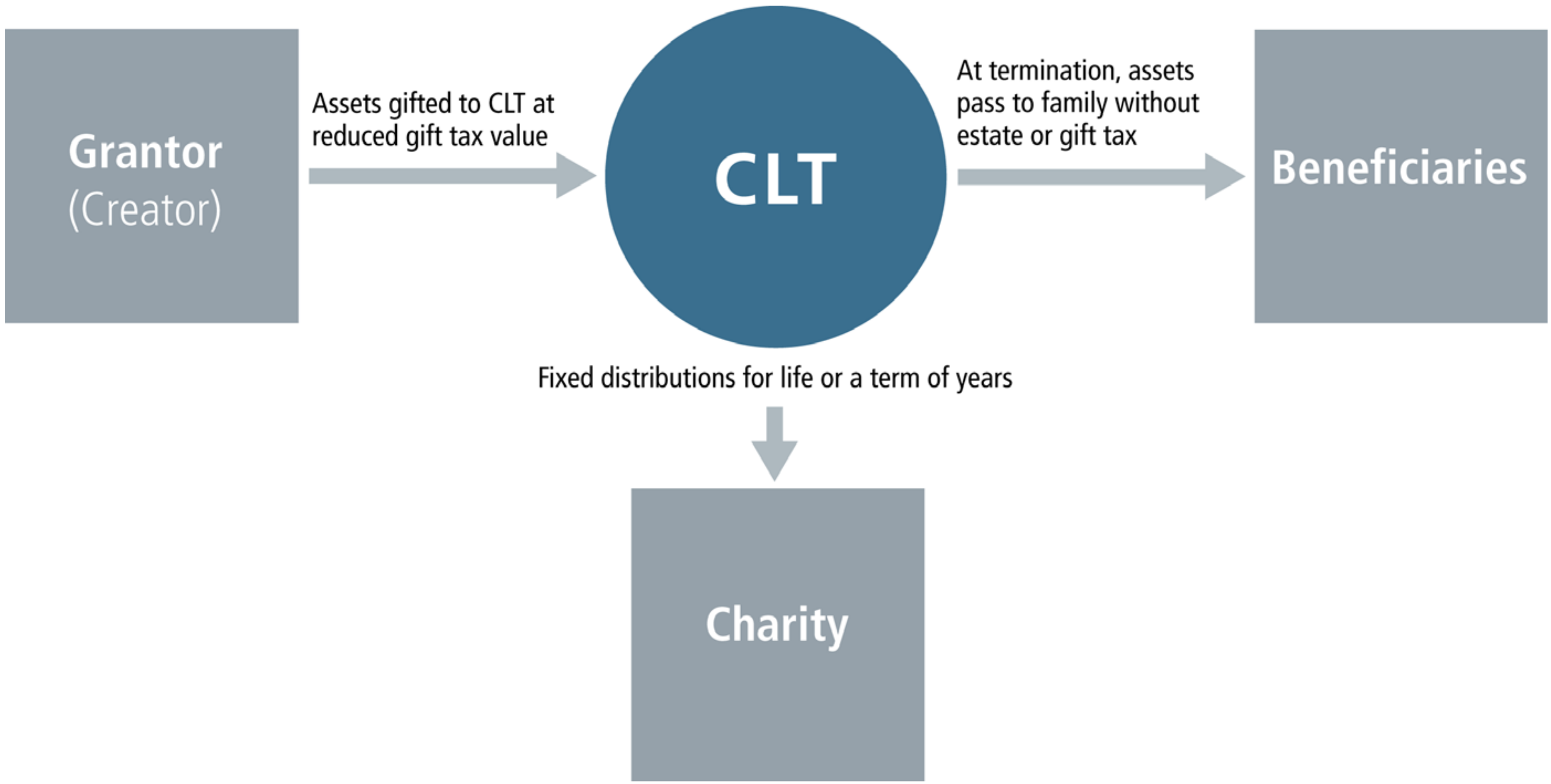


Appreciated assets may be sold by trustee and capital gains tax is deferred. Proceeds are invested in a diversified portfolio.

Charitable Lead Trust (CLT) —IRC Section 170(f)(2), 2055(e)(2)(B); 2522 (c)(2)(B)

- A CLT is the inverse of a CRT, providing an annual payment to one or more charitable beneficiaries for a period of time, with the remainder interest going to family members
- Like CRTs, a CLT may be structured with either an annuity or unitrust payout, but unlike CRTs, there is no minimum or maximum payout requirement
- A CLT structured as a unitrust can be used to leverage the Generation-Skipping Transfer Tax exemption
- A CLT may be structured as a grantor or non-grantor trust for income tax purposes
  - A grantor CLT permits the donor to take an income tax deduction for the actuarial value of the charitable lead interest, but the donor will be taxed on the income for the term of the CLT. Recapture rules also apply if the CLT ceases to be a grantor trust under IRC Section 170 (f)(2)(B)
  - A non-grantor CLT is taxed as a complex trust; the charitable distribution is deductible annually under IRC Section 642(c)
- A CLT permits the transfer of appreciation in excess of the IRS benchmark rate to a family, free of estate and generation-skipping transfer tax
- CLATs are particularly attractive in a low interest rate environment
- As the Section 7520 rate increases, CLUTs may become more attractive

Charitable Lead Trust (CLT) (continued)



Charitable Gift Annuity (CGA)—IRC Sections 501(m), 514(c)(5), 1011(b)

- A CGA is a form of bargain sale in which the donor transfers assets in exchange for an annuity that provides a fixed payment for the life of the donor and up to one additional individual.
- The net amount remaining at the annuitant's death passes to the charity.
- A charitable gift annuity operates much like a CRAT, except that the donor's gift is not preserved in a separate trust.
- A current charitable income tax deduction is available for the actuarial value of the remainder interest that will pass to charity.
- An annuity funded with appreciated property will receive favorable tax treatment of the gain under IRC Section 72, provided the annuity is not assignable, and the donor is the sole annuitant or one of two annuitants.
- Changing AFR rates can impact CGA planning: as the section Section 7520 rate increases, the charitable contribution deduction increases, but the excludible portion of the annuity under Section 72 decreases
- Charitable annuity rates generally follow the rates set by the American Council on Gift Annuities and often are higher than the return on other kinds of investments.
- Most organizations have a minimum size for a charitable gift annuity and many limit the minimum age of the individual donor.

Creating a Perpetual Family Vehicle

Donors can create a separate gift structure that will benefit and support existing charities for the long-term. Common approaches include:

Private Foundations	• Can be a charitable trust or nonprofit organization • Can support specific charities or provide for general giving • Can be a permanent endowment • Provides full family control
Donor-Advised Funds	• A fund created at an existing grant-making charitable organization • Family can advise but does not have control of charitable grants
Supporting Organizations	• Set up to support one or more existing public charities • Family may not control • Complex tax rules require careful planning

Private Foundations—IRC Sections 501(c)(3) and 509; Chapter 42

A private foundation is a nonprofit corporation or charitable trust that qualifies for tax exemption under IRC Section 501(c)(3) but does not meet a "public support test."

Private foundations, can provide a way to foster a family's values and provide a focus for charitable giving through a family-controlled entity, but the family must be motivated enough to accept the complexity of the structure.

Key benefits of family foundations include:

- Maintaining control of the charitable entity
- Encouraging intergenerational involvement
- Establishing a legacy
- Creating an endowment to fund future giving
- Providing exemption from federal income tax
- Delivering income, estate, and gift tax deductions for contributions

Disadvantages:

- Time and cost of maintaining separate entity
- Fair market value deduction for gifts of appreciated property limited to "qualified appreciated stock"
- Reduced AGI limits for deductibility
- Chapter 42 excise taxes

Private Foundations: Gift Planning and Operations

Form of entity	Independent entity, which may be nonprofit corporation or trust
Governance	Controlled by Board of Directors or Trustee
Investments, grant making, and operations	Controlled by Directors or Trustees
Contribution deduction gift limits: Cash IRC Section 170(b)	30% of AGI
Contribution deduction limits: Long-term Capital Gain Property IRC Section 170(b)	20% of AGI
Carry forward of deduction IRC Section 170(b)	Unused deductions carry forward for 5 years
Fair market value deduction for gifts of appreciated property IRC Section 170(e)(i)(B)(ii) and (5)	Qualified appreciated stock donation deductible at full FMV, subject to 20% AGI limits, provided total stock gifted by all family members not more than 10% of outstanding stock All other long-term capital gain gifts, including closely held stock and real estate, limited to lower of cost basis or fair market value

Private Foundations: Gift Planning and Operations

(continued)

Minimum payout requirement **IRC Section 4942**	5% of fair market value annually
Permitted grantees **IRC Section 4942(a)**	Public Charities. Certain grants require expenditure responsibility, ex. grants to other private foundations, but do not count toward 5% payout
Prohibited transactions **IRC Section 4941**	Disqualified persons may not engage in “self-dealing”
Disqualified person defined **IRC Section 4946(a)**	Includes: • Substantial contributors • Officers, directors, and trustees • Owner of more than 20% of a business that is a substantial contributor • Family members • Business entities more than 35% owned by any of the above
Compensation, loans, grants **IRC Section 4941(d)(1) and (2)**	Reasonable compensation permitted for disqualified persons. Loans and grants prohibited for disqualified persons

Private Foundations: Gift Planning and Operations

(continued)

Sales of property **IRC Section 4941(d)(1)(A)**	No sales, even at fair market value, between private foundation and disqualified person, including bargain sales
Excess business holding rules **IRC Section 4943**	Private foundation may not own more than 20% of the voting stock, profits interest, or beneficial interest in a business enterprise, together with all disqualified persons (increased to 35% if aggregated interest is not controlling) Exceptions: • Private foundation may own up to 2% of business (voting stock, partnership, joint venture, trust) regardless of disqualified person ownership • Limited exception for wholly owned business acquired by gift or bequest, which distributes all income annually to foundation, and meets an independent operation test
Tax on investment income **IRC Section 4940**	1% or 2%
Excise tax on jeopardizing investments **IRC Section 4944**	Investments that “jeopardize” the endowment are prohibited
Excise tax on taxable expenditures **IRC Section 4945**	Non-charitable expenditures, including lobbying, prohibited

Donor Advised Funds (DAFs)—IRC Sections 4966, 4967

- Some benefits of a private foundation can be achieved by establishing a donor advised fund (DAF) through a sponsoring charity that offers DAFs, such as a community foundation
- By law, donors may only recommend uses for the donated funds, but in most cases sponsoring organizations follow those recommendations
- A DAF is maintained by a public charity, so the deduction limitations and operational restrictions that apply to private foundations do not apply to them
- Donors may contribute appreciated property, such as closely held stock, to a DAF and still receive a full fair market value deduction.
    - Note, however, that DAFs are now subject to the excess business holding rules applicable to private foundations

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Donor-Advised Funds (DAFs)—IRC Sections 4966, 4967

Continued

- Under the Pension Protection Act of 2006, DAFs are subject to a number of restrictions, including rules prohibiting more than "incidental donor benefits" and "excess benefit transactions"
- Many DAFs have restrictions about the types of grants they will approve and DAF durations
- Because DAFs are simpler and less expensive to establish than private foundations, they are a good option for smaller donations
- Some DAFs allow donors to use their own investment advisors to invest the funds

Guiding a Donor to Find the Right Philanthropic Strategy

- Identify the donor’s philanthropic goals
- Identify the donor’s financial goals
- Identify the assets to be donated
- Encourage the donor to include family members in the decision-making process

Carol G. Kroch

Administrative Vice President, National Director of Philanthropic Planning

Carol is responsible for philanthropic planning for Wealth Advisory Services. She has extensive experience working with individuals and nonprofit organizations in estate, trust, and charitable gift planning and in advising nonprofit corporations and trusts, including private foundations and public charities.

Carol was named by Private Asset Management Magazine in June 2016 and May 2015 as one of the 50 most influential women in private wealth. Prior to joining Wilmington Trust in 2005, Carol was senior counsel at The Robert Wood Johnson Foundation, the largest foundation in the United States devoted to health and healthcare. She was responsible for legal matters related to the Foundation's investment portfolio, including the negotiation of alternative investment vehicles. In addition, she had responsibility for tax, business, corporate governance, and grant-making matters. Previously, Carol was in private practice at Drinker Biddle & Reath, LLP in Philadelphia and Cahill Gordon & Reindel, LLP in New York.

Carol holds a J.D. from Boston College Law School, where she was a member of the Law Review and the Order of the Coif, and a bachelor's degree from Wellesley College. She is a Fellow of the American College of Trusts and Estates Counsel and is a member of the National Conference of Lawyers and Corporate Fiduciaries. Carol is a past co-chair of the Art and Collectibles Committee of the Section of Real Property Trust and Estate Law (RPTE) of the American Bar Association ("ABA"). She is a past RPTE Council member and served as the Supervisory Council Member for the Charitable Planning and Organizations Group. She is also a member of the Exempt Organizations Committee of the ABA Tax Section and Co-Chair of the Subcommittee on Model State Regulatory Statutes. Carol was the ABA Advisor to the Drafting Committee of the Uniform Prudent Management of Institutional Funds Act and was an ABA Advisor for the Model Entity Transactions Act Drafting Committee. She is a member and past Chair of the Nemours A.I. duPont Hospital for Children Planned Giving Committee and is a member of the Children's Hospital of Philadelphia Legacy Advisors Group and the Barnes Foundation Professional Advisors Council.

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- Charitable gift planning
- Private foundation operations and governance
- Charitable trust administration
- Nonprofit investment restrictions
- Wealth preservation and protection strategies

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