THE • DAYTON FOUNDATION
We're here for good.

Futures

Spring 2009

A no-nonsense newsletter for estate planners and financial advisors from The Dayton Foundation

How Working with The Dayton Foundation Can Benefit Clients Who Are Small Business Owners

By Gary L. Hunt, JD, CPA, Partner, Battelle & Battelle LLP

Tax and estate planning can be a very satisfying and rewarding career, especially when your efforts benefit not only your clients but also the local community. The opportunity to do charitable gift planning presents these dual rewards, and working with the professionals at The Dayton Foundation makes the charitable planning component a much easier challenge.

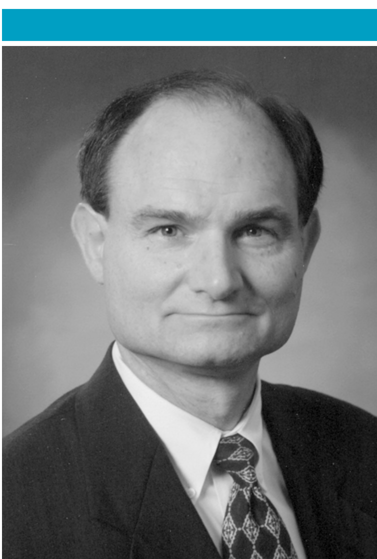
"...working with the professionals at The Dayton Foundation makes the charitable planning component a much easier challenge."

– Gary L. Hunt, JD, CPA

Case Example

In my 30 years of tax and estate planning, I have had many opportunities to work with clients in evaluating their charitable giving goals. Such a case arose when I was approached by a client (we'll call him Ted) who was interested in selling his business after a long and successful career.

Ted's business was still very profitable and had a bright future, but there was no viable succession plan other than a sale. He was 68 years old and his wife (we'll call her Tina) was 65. They had two children, Susan, age 36 and a stay-at-home mom, and Bill, age 38 and a middle manager in a large corporation. Ted and Tina (the Turners) were very interested in evaluating their charitable giving options.



GARY L. HUNT, JD, CPA

The Turners did not have an allegiance to any single charity, so using The Dayton Foundation and benefiting the local community through the Foundation appealed to them. We contacted the professionals of The Dayton Foundation to help us sort through the various options available to the Turners.

Our discussions focused on three primary vehicles: charitable remainder trusts (CRTs), a charitable lead annuity trust (CLAT) and The Dayton Foundation's Family Foundation *Plus*-℠Advised, which is a private foundation alternative.

Weighing Options

With respect to CRTs, we explained to the Turners that they could establish either a Charitable Remainder Annuity Trust (CRAT) or a Charitable Remainder Unitrust (CRUT).

A CRAT would provide Ted and Tina with a fixed-dollar payment for their joint lives. With a gift of $1 million into the CRAT and a $50,000 (5%) annual annuity, the Turners would receive an immediate tax deduction of slightly over $264,000.

A CRUT, on the other hand, would allow the 5% annuity payment to the Turners to fluctuate with the value of the assets in the CRUT. If the asset value increased, the annuity would increase by 5% of the increased value, and if the value decreased, the annuity would decrease by 5% of the decrease in value. This option provides for more risk, since there is a potential for the annuity to decrease. The same $1 million contribution to the CRUT would result in an immediate tax deduction of slightly over $253,000.

Benefits of CLATs

We then moved on to discuss the merits of a CLAT. Under the CLAT option, the Turners would get no annual annuity payable to them, but the annual annuity would be payable to a vehicle that they would establish at The Dayton Foundation. If they funded a CLAT with $1 million, a 5% payout and a 2% Section 7520 rate, which is the February 2009 rate, for 15 years, The Dayton Foundation would receive $50,000 per year for 15 years, for a total of $750,000. The Turners would have the CLAT assets pass to their children at the termination of the CLAT.

If the assets of the CLAT would grow at a 6% rate, the children would receive over $1.2 million at the end of the 15-year term. At an 8% growth rate, they would receive over $1.7 million. One cost of this option is that the Turners would be making a gift to their children at the inception of the CLAT of approximately $353,000.

If the same CLAT were established with a 20-year term, The Dayton Foundation would receive $1 million over the 20-year payout period, and the gift to the children would be approximately $176,000 at the inception of the CLAT. With a 6% growth rate, the CLAT would leave the children over $1.3 million, and with an 8% growth rate, they would receive over $2.3 million.

CLATs can be either grantor or nongrantor trusts. If the 15-year CLAT were a grantor trust, the Turners would receive a charitable deduction of approximately $647,000. For the 20-year CLAT, it would be almost $824,000. The disadvantage of a grantor CLAT is that the Turners would have to pay tax on the future income of the CLAT without receiving any cash

Continued...

> "The Dayton Foundation's Family Foundation Plus℠-Advised service provides essentially all of the advantages of a private foundation without the disadvantages."
>
> – *Gary Hunt, JD, CPA*

Futures is made possible by four

I Believe!

Dayton Foundation donors and families who have stepped forward to become the 2008-2009 "I Believe!" Partners of The Dayton Foundation. Their commitment underwrites a full year of Dayton Foundation publications, thereby freeing resources for the Foundation's other community work.

"I Believe!" Partners:
Dr. Soma S. & Veni Avva,
Karen S. & Kevin M. Crotty,
Susan & Shaun P. Nicholson,
Jane & Fred C. Setzer, Jr.

How Working with The Dayton Foundation Can Benefit Clients Who Are Small Business Owners

Continued from page 1

from the CLAT. In effect, they would be recapturing part or all of the tax saved from the initial charitable contribution deduction. For a nongrantor CLAT, there would be no charitable deduction at inception, and no requirement for the Turners to pay tax on the annual income of the CLAT.

Private Foundations and The Dayton Foundation Alternative

The Turners always had been intrigued with the idea of having their own private foundation. This option would have required them to hire an attorney to draft the foundation documents. They then would have to apply for exempt status with the IRS, file annual Forms 990-PF, be exposed to an annual 1% to 2% excise tax and be subjected to an annual payout requirement of 5% of net investment assets, not to mention several other administrative issues.

The Dayton Foundation's Family Foundation *Plus*-Advised (FF+A) service provides essentially all of the advantages of a private foundation without the disadvantages listed above. (The Foundation does suggest, however, that donors consult their own independent legal and financial counsel prior to opening such a fund.) The FF+A option appealed to the Turners.

Since the Turners did not need the security of a CRT, they decided to pass on that option. However, they did establish a FF+A fund, and prior to the sale of the company, they donated $1 million of their company stock to The Dayton Foundation for their FF+A fund. They received an immediate tax deduction for the $1 million donation and ultimately saved $280,000 in taxes. The stock donation required a valuation that cost approximately $10,000, but this was a small price to pay for the tax that was saved by the charitable donation and for the added benefit of pegging an approximate fair market value for the sale of their company.

When the company was sold, The Dayton Foundation sold the donated company stock to the buyer – and the Turners avoided $210,000 of federal and state taxes on its sale. In addition, they established a 15-year nongrantor CLAT with their FF+A fund as the charitable beneficiary and their children as the recipients of the assets at the end of the CLAT term. They contributed $1 million to the CLAT and provided for a 5% payout at a time when the Section 7520 rate was 2%. During the term of the CLAT, their FF+A fund would receive $750,000, and at the end of the term the children would receive between $1.2 million and $1.7 million, assuming a rate of return between 6% and 8% on the CLAT's investments. The CLAT also resulted in an immediate gift to the children of approximately $353,000.

When Ted retired from the company, he rolled his 401(K) into an IRA. We made Tina the IRA beneficiary with their FF+A fund the contingent beneficiary. If Ted predeceased Tina, she would have several options, including using the IRA money for herself, disclaiming it to their FF+A fund, making their FF+A fund her beneficiary or making the children her beneficiaries.

The charitable planning in the Turners' case satisfied a desire to save taxes, as well as providing a benefit to the local community for many years to come. ❧

Note: Solutions will differ from case to case. The above does not constitute professional financial or tax advice.

Gary Hunt is an attorney and CPA and has been a Partner of Battelle & Battelle LLP since 1981. His areas of expertise include tax, estate and financial planning; mergers and acquisitions; business consulting; and litigation support. He is admitted to practice before U.S. Tax Court.

Another Charitable Option for Business Owners

The Dayton Foundation's Charitable Checking Account℠ offers another option that small business owners may utilize to both their and the community's benefit. Small business owners have established Charitable Checking Accounts (CCAs) with The Dayton Foundation as a means of maintaining a charitable presence in the region. Here's how they use it.

When business is good, they contribute to their CCAs, loading them before the end of the tax year. They take the charitable deduction for that tax year, then make charitable grants in their company's name the following year or any future year they wish and to the charities they want to support.

When times are not so good economically, they can maintain their charitable presence in their community, continuing to give grants but not adding to their CCAs. Then when sales and profits improve, they load again, take the tax breaks and build up their charitable funds for future use. It's one more option available to business owners to help them and help them to help others.

***Futures:** Five-time national award-winning publication, Wilmer Shields Rich Awards, Council on Foundations*

President: Michael M. Parks. **Governing Board:** Charles A. Jones, *chair*, Gary L. LeRoy, *vice chair*, Thomas G. Breitenbach, Craig J. Brown, Franz J. Hoge, Ellen S. Ireland, Helen Jones-Kelley, Jamie King, Vicki D. Pegg, Colleen M. Ryan, Douglas C. Scholz, Richard W. Schwartz, Fred C. Setzer, Jr., Jerome F. Tatar, Fred E. Weber. **Financial Managers:** A.G. Edwards & Sons, Inc.; A.T. Whitehead, Ameriprise Financial Services, Inc.; Robert W. Baird & Co., Inc.; Behnken and Associates, Inc.; Buckingham Financial Group; C.H. Dean and Associates; Dover Partners; Eaton National Bank; Eubel, Brady & Suttman Asset Management; Fiduciary Trust Company International; Fifth Third Bank; First Alliance Asset Management Access Financial Group; The Huntington; JP Morgan; James Investment Research, Inc.; Key Bank, NA; Liberty Savings Bank, FSB; Linsco/Private Ledger Financial Services, Mead, Adam & Co., Inc.; Merrill Lynch and Company; Michael J. Monaghan & Associates; Morgan Stanley; National City Bank; Northwestern Mutual Fund Services; Oxford Financial Advisors Corp.; PNC Bank, Ohio, NA; Parker Carlson & Johnson; Principled Wealth Advisors; Prudential Preferred Financial Services; Smith Barney; Spears, Grisanti & Brown, LLC; Transamerica Investment Management, LLC; Truepoint Capital, LLC; UBS Financial Services, Inc.; US Bank; Wachovia Securities. **Investment Consultant:** Fund Evaluation Group, Inc.

We help you help others.℠

Meeting All Standards for U.S. Community Foundations.

The Regional Community Foundation