

[admin](#) - Fri, 11/15/2013 - 12:44

One of the reasons gift annuities are so popular is that they offer donors payments that are fixed and are backed by the general resources of the issuing institution. The resulting predictability and security of annuity payments has strong appeal for a broad range of planned gift donors. The age of the donors has a lot to do with this appeal.

According to the most recent gift annuity survey conducted by the American Council on Gift Annuities (ACGA), the average gift annuity **donor** is 78 years old. For a donor of this vintage, predictability of payment amounts typically is paramount. The donor's horizon for receiving payments is fairly short, perhaps 10 -15 years, so she is not too worried about how inflation may erode the value of her payments.

### **Gift Plans that Appeal to Younger Donors**

What about younger donors? Gift planners often suggest the deferred gift annuity as a way for a donor in her 50s or 60s to supplement retirement income. Make the gift now, they say, but defer the start of payments until retirement. The ACGA adjusts the annuity rate upward by 3.25% annually for each year of deferral, so a 10 or 15 year deferral can result in substantial payments relative to the initial funding amount. For example, the ACGA suggests a 6.4% annuity rate for a 55 year-old donor who defers payments 10 years.

While a 6.4% annuity rate looks very attractive when compared to a CD or money market fund yielding about half that, a savvy 55 year-old donor will recognize that the 6.4% is a fixed amount and that inflation is likely to reduce the value of the donor's payments substantially over her 30-40 remaining years of life. What other options are there?

### **Charitable Remainder Trust**

One solution is to suggest a plan defined by federal tax law that allows a donor to provide income to herself and/or others while making a generous gift to charity. The income may continue for the lifetimes of the beneficiaries, a fixed term of not more than 20 years, or a combination of the two.

The donor irrevocably transfers assets, usually cash, securities, or real estate, to a trustee of her choice, such as a bank trust department. The donor receives an income tax deduction equal to the trust's remainder value to the charity, subject to IRS 30%/50% limitations. The remainder value to charity must be at least 10% of the funding amount.

During the unitrust's term, the trustee invests the unitrust's assets. Each year, the trustee distributes a fixed percentage of the unitrust's current value, as revalued annually, to the income beneficiaries. If the unitrust's value goes up from one year to the next, its payout increases proportionately. Likewise, if the unitrust's value goes down, the amount it distributes also goes down. For this reason, it may be advantageous to choose a relatively low payout percentage so that the unitrust assets can grow, which in turn will allow the unitrust's yearly payments to grow.

Payments must be between 5% and 50% of the trust's annual value and are made out of trust income, or trust principal if income is not adequate. Payments may be made annually, semiannually, quarterly, or monthly.

When the unitrust term ends, the unitrust's principal passes to charity, to be used for the purpose designated by the donor. The donor may add funds to her unitrust whenever she likes.

You can analyze the benefits of a remainder unitrust in our Planned Giving Manager software in Basic Gift Illustrations, First Year Analysis, or Life Income Projections.

A charitable remainder unitrust is typically set up with a payout of 5%. Setting a low payout rate will give the trust the maximum potential for growth, and as the trust value grows, so will its payments. You might even suggest a flip unitrust, where the flip triggering event is the donor's expected date of retirement.

But what if the donor doesn't want to commit the \$100,000 or more needed to fund a unitrust (some charities have a minimum for charitable remainder trusts of \$250,000)? Or what if the donor is uncomfortable that unitrust payment amounts will be affected by fluctuations in financial markets?

There is another solution.

### **The Laddered Deferred Gift Annuity**

A donor can use the deferred gift annuity to achieve predictable and secure payments that also provide inflation protection. Here's how it works.

Rather than give a single deferred gift annuity that starts payments when the donor anticipates retiring, the donor gives a deferred gift annuity each year up to her year of retirement. Each annuity is set up with the same number of years of deferral, so once payments start they increase each year as each subsequent annuity commences payments.

Mr. and Mrs. Donofrio, currently 52 and 55, respectively, want to provide a supplemental retirement income once they retire, but they are concerned about inflation protection.

Each year they contribute the maximum permissible amount to their workplace retirement savings plans. Beginning this year, they also start contributing \$20,000 cash each year to fund a series of deferred gift annuities and continue to do so for another 12 years, until the year before Mr. Donofrio turns 65. The first annuity begins making payments in 13 years, the year Mr. Donofrio will retire at 65.

As a result of their gifts, Mr. and Mrs. Donofrio will receive a charitable income tax deduction each year in which they establish a new deferred annuity. The chart below shows the total annuity to which Mrs. and Mrs. Donofrio will be entitled each year as each annuity contract begins making payments. Notice that the total annuity increases every year until the all of the deferred annuity contracts have begun making payments.

Assuming a 2.4% IRS discount rate and current ACGA rates for all 13 gifts, Mr. and Mrs. Donofrio will receive a total charitable income tax deduction of \$72,336 over the 13 years. If they are in the 39.6% income tax bracket during all those years, they will enjoy income tax savings of \$28,645.

In addition, they will start receiving payments when Mr. Donofrio retires, totaling \$11,616 per year for the remainder of their lives.

### **Laddering Offers Flexibility**

Laddering deferred gift annuities allows the donors enormous flexibility. The funding amount and annuity starting date of each gift can be set to best meet their needs, whatever they might be.

For example, if the Donofrios prefer that their payments continue to increase through their 80s, they can always create additional deferred annuities that commence payments during those years. For instance, rather than create one \$20,000 annuity during each of the first ten years of their giving program, they could create each year one \$15,000 annuity that is deferred thirteen years and a second \$5,000 annuity that is deferred 26 years. As a result, new annuity amounts would continue to kick in until they are 87 and 90, respectively.

Another approach would allow the Donofrios to set up all of their deferred gift annuities at once. They could create thirteen separate deferred gift annuities at the same time, each funded with \$20,000. Each would have a different length of deferral period, ranging from 13 years to 26 years, so that each year from when Mr. Donofrio turns 65 to when he turns 78, their total annuity payment would increase.

## **Conclusion**

The laddered deferred gift annuity can be an effective giving program for meeting the goals of younger donors. When you meet a prospect who is looking to supplement retirement income, or simply to augment income later in life while minimizing risk, think of the laddered deferred gift annuity. It may be just the solution they're looking for.

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