

Horizons

AN EXCLUSIVE PUBLICATION FOR LOYAL SUPPORTERS OF THE PI KAPPA ALPHA EDUCATIONAL FOUNDATION

Charitable Remainder Trusts

CRTs can result in enhanced cash flow, income tax deductions and estate tax savings.



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Holding on to an under-productive asset in order to avoid paying the capital gains tax on such property can be very frustrating, not to say damaging to one's investment objectives. How many times have you overheard, "I wish that I could unload this poor performer, but I cannot afford the capital gains hit that would result," or worse yet, initiated this statement. There is no need to feel that your appreciated assets have you trapped without alternatives to increase the income realized by your portfolio, or otherwise fine-tune your portfolio to meet your financial plan. While there have been many recent changes to the Internal Revenue Code, the Charitable Remainder Trust has endured as one of the tremendous planning vehicles available to taxpayers.

A **Charitable Remainder Trust (CRT)** is a trust established to pay income to a non-charitable beneficiary, typically oneself, one's spouse or a family member, with the remainder to go to a specified charitable beneficiary, such as the Pi Kappa Alpha Educational Foundation. The income interest to be received may be arranged to continue for a fixed number of years not to exceed 20, or for the life of a designated beneficiary. The amount of income to be paid out is derived from the terms of the trust agreement, which may generally be set up in two ways: 1) a **Charitable Remainder Annuity Trust**, which pays out a fixed percentage of the initial value of the trust principal for the duration of the period specified in the trust instrument; or 2) a **Charitable Remainder Unitrust**, which pays out a fixed percentage of the annual value of the entire trust principal.

Potential Key Benefits. Whichever form is selected, the following advantages may be obtained by creating a Charitable Remainder Trust:

- ♦ deferral of capital gains tax which would otherwise be payable on the sale of appreciated long-term capital gain property;
 - ♦ ability to diversify or update your investment portfolio by converting appreciated long-term capital gain property into a portfolio that is more consistent with your current investment objectives without realizing current capital gains;
 - ♦ retained income rights for your life or the life of your wife and/or other beneficiaries;
 - ♦ the possibility of increased spendable income with certain arrangements;
 - ♦ elimination of federal estate tax on the value of the interest in property passing to the charity and the appreciation on such property;
 - ♦ reduced estate settlement costs during the administration of your estate;
 - ♦ the ability at death to provide your beneficiaries with an amount of cash equal to or greater than the value of the property contributed;
 - ♦ providing a source of liquid funds at your death which can be used to pay estate taxes and settlement costs;
 - ♦ the ability to avoid the "double tax" associated with qualified (pension plan) assets which may be included in one's estate;
 - ♦ avoidance of federal estate tax on such cash;
- ♦ income tax savings generated by a current deduction for charitable contributions based on the value of the future gift;

There is no need to feel that your appreciated assets have you trapped without alternatives to increase the income realized by your portfolio, or otherwise fine-tune your portfolio to meet your financial plan.

*Celebrating the
Educational
Foundation's
50th Anniversary!*

WINTER 1998

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PI KAPPA ALPHA EDUCATIONAL FOUNDATION SCORECARD

1948-1997-1998

New Alumnus Donors	172
Continuing/Renewing Alumnus Donors	4,885
ΦΦΚΑ Club Undergraduate Donors	693
Total Donors	5,750

Charitable Remainder Trusts

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- ◆ the possibility of savings on state and local income tax, inheritance tax, estate tax and gift tax; and,
- ◆ the ability to control or direct the disposition of your "social capital."

The Internal Revenue Service allows a current income tax deduction for the donor of the property contributed to a **Charitable Remainder Trust** equal to the present value of the remainder interest which will ultimately go to charity. To calculate the remainder interest, the IRS subtracts the present value of the income stream to be paid to the non-charitable beneficiary (spouse, self and/or others) from the current fair market value of the asset. In the case of a Unitrust, or an Annuity Trust for life, the IRS provides tables for calculating the approximate present value of the remainder. This is the amount that the donor may deduct from his or her income taxes in the year that the Charitable Remainder Trust is created, with certain limitations to be discussed.

1998 Law Changes. For those familiar with Charitable Remainder Trusts, you may be interested in some new regulations which have been recently enacted. New for 1998, the Internal Revenue Service has placed a limitation on the minimum allowable interest to go to charity, equal to 10% of the value of the property placed in trust. Viewed conversely, this limitation places a ceiling on the present value of the income stream to be received by non-charitable beneficiaries at 90%.

This has a minor effect as most donors tend to establish their Charitable Trust with a remainder interest to go to charity exceeding 10% to take advantage of the current income tax deduction allowed, one of the major benefits of a Charitable Remainder Trust. In addition, CRTs with short-term, 50% or greater payouts are prohibited.

Income Tax Deduction Limitations. Another limitation that deserves mention, although not derived from particularly recent legislation, is a limitation imposed on the current income tax deduction in the year that the trust is established. The IRS has implemented percentage limitations in calculating the maximum deduction allowable against the donor's Adjusted Gross Income (AGI). For cash contributions to a public charity, the maximum deduction allowed is 50% of the donor's AGI. For the donation of appreciated property (appreciated stock, real estate, etc.) to a public charity, the deduction is limited to 30% of the donor's AGI. For similar contributions to a private foundation, the maximum allowable deductions are 30% of AGI for cash contributions, and 20% of AGI for contributions of appreciated property. This provision has a bark worse than its bite because deductible amounts disallowed in the current year are allowed to be taken over the next five years, simply requiring more extended planning.

Major Advantages. As previously mentioned, a CRT allows the taxpayer to donate appreciated assets to the trust, and thereafter convert this property to another investment in order to better achieve the grantor's investment objectives, with the benefit of continued deferral of the capital gains tax which would otherwise have been due on such property. This permits

WANT MORE INFORMATION?

The Pi Kappa Alpha Educational Foundation offers numerous opportunities for you to enhance the lives of our undergraduate brothers, and Pi Kappa Alpha in general, while positively affecting your personal tax situation.

Our newest publication, "*Ways To Give*", provides a comprehensive summary of the numerous opportunities for charitable support of the Pi Kappa Alpha Educational Foundation.

Topics addressed include:

- ◆ the **PIKE Fund**
- ◆ Gifts of Appreciated Securities
- ◆ Gifts of Real Estate
- ◆ Planned Gifts using Wills, Charitable Trusts, and Life Insurance
- ◆ the Foundation's new **Pooled Income Fund**

Call, write or E-Mail us today and we'll gladly send you a complimentary copy of this informative brochure.

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diversification or conversion from a low or non-income producing asset to a high-income producer, as required by many financial plans. Therefore, with a CRT, the taxpayer no longer needs to retain appreciated property in order to obtain deferral of capital gain taxes.

Another tremendous advantage of the CRT which parallels this benefit is that the grantor may provide a stream of income payments to a non-charitable beneficiary of his or her choice, similar to an annuity. This stream of payments is consistent with many planning objectives, such as retirement planning, or providing school funding to family members. Furthermore, it permits deriving a benefit from an asset which has been removed from your estate and for which an income tax deduction has already been received. Again, the enhanced current income stream has been obtained from an appreciated asset while avoiding the disincentive of realized capital gains.

A third advantage is derived from the current income tax deduction allowed for a charitable contribution, equal to the present value of the remainder interest donated to charity. While the deduction has been limited by the aforementioned percentage of Adjusted Gross Income restrictions, the excess disallowed in the year the trust is created may be spread over the next five years. **This is a tremendous benefit for those seeking immediate relief on April 15th.**

Estate Planning Considerations. In addition to a reduction of income taxes payable, the CRT is also an effective vehicle to achieve a reduction of the donor's estate and reduce corresponding estate taxes. By placing the property in trust, the donor receives a reduction in his or her estate equal to, and often greater than the current value of the property, when compared with transferring the property at death. Use of the value of the property on the date transferred into trust is likely to be an underestimation of the actual effect on the estate, because the actual reduction of the taxable estate is equal to the fair market value of the asset at the date of the donor's death. To achieve a greater estate reduction, one must simply anticipate continued appreciation in the value of the property during the lifetime of the property owner. The consequences of the donor's retention of such assets until death will be inclusion in his or her estate at its appreciated value on the date of death, subject to a maximum estate tax rate of 55% in addition to other taxes and expenses.

Social Capital. A significant benefit not to be forgotten is that this vehicle allows the donor to select and control the distribution of his or her "social capital." The term "social capital" refers to those funds that are likely to be seized by means of taxes. When the property is placed into trust, the donor is able to designate, in the donor's discretion, the charitable beneficiary to which he or she would like to direct the charitable donation. This is an opportunity to achieve one's particular philanthropic objectives by making a difference in the social causes determined most worthy, rather than simply paying taxes and allowing the government to allocate such dollars in its wisdom.

Wealth Replacement Trusts. For those who remain tentative about reducing the estate that will pass to their heirs, by coupling the CRT with a life insurance trust, one can easily replace the wealth that is being removed from the estate. See, *More Cash In Your Pocket*, Horizons Letter, Winter (1992). The income payments may be applied to pay the premiums on a life

Donor Recognition Programs Enhanced

As an added thank you to the members of the Foundation's *Cumulative Giving Societies* for their loyalty and consistent generosity, the Educational Foundation has developed specialized donor lapel pins and certificates to signify membership in these select groups. Foundation donors will now receive these items as they enter each new society.

Also added this year to recognize the growing generosity of Foundation donors on an annual basis to the Foundation's **PIKE FUND** are four **new annual donor clubs**. The **1868 Club** will recognize new donors and those continuing alumnus donors who increase their annual support of the Foundation to at least \$18.68, to commemorate the Fraternity's founding. The **Anniversary Club** will recognize donors who make gifts of \$50 or more this fiscal year, to honor the Foundation in this its 50th Anniversary year. The **Ambassador's Club** (\$2,500 - \$4,999) and the **21st Century Club** (\$5,000+) also join the list of clubs recognizing our loyal alumni for their *annual* support.

Thank You Brothers!



insurance policy on the life of the donee, or any other insured, to provide a payment upon the death of the insured generally in an amount up to or exceeding the value of the property being transferred to charity. The life insurance payment passes outside of the estate and helps achieve an estate tax reduction while restoring to the family estate the value of the property going to charity without being subject to the 55% tax. This is a Win-Win!

Funding CRTs. The effect of the recent legislation has been to separate donors into two categories for choosing the optimal type of asset to be placed in trust. For high income earners seeking a significant income tax deduction over the next few years, it would be best to donate cash or securities that have not already accumulated a large unrealized capital gain. For others who are seeking to diversify their portfolio or convert some under-productive assets into income-producing assets without realizing the capital gains tax, gifts of appreciated property remain an ideal alternative. Either type of property placed in trust achieves the ultimate objectives of a reduction in the donor's estate and income tax deductions.

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ROBERT A. SMYTHE
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The LOYALTY BRICK CAMPAIGN

**TOM W. WADE, JR.,
TENNESSEE
ZETA '53**

at the

PI KAPPA ALPHA MEMORIAL HEADQUARTERS ANNIVERSARY COURTYARD

Etch your name permanently into Pi Kappa Alpha History!

It's simple, just make a gift of \$100 or more to the Foundation's 1998-1999 PIKE FUND.

To commemorate the Pi Kappa Alpha Educational Foundation's **50th** year of supporting scholastic achievement, leadership training, and personal development, an Anniversary Courtyard is being constructed at the Memorial Headquarters in Memphis, Tennessee.

The new brick Anniversary Courtyard will be filled with names of alumnus brothers from Pi Kappa Alpha's more than 250 chapters. The Educational Foundation invites you to join in this unique recognition opportunity simply by making your annual, *tax-deductible* gift of **\$100 or more** to the Foundation's **1998-1999 PIKE FUND**. In recognition of your generosity, a brick will be produced based on your order form, and permanently placed in the Anniversary Courtyard for all our alumnus brothers, undergraduate members, family and friends to see.

Bricks may be placed in your own name, as well as "In Honor" or "In Memory" of others who have played a part in your Pi Kappa Alpha Fraternity lifelong experience. To assure a permanent remembrance in the Anniversary Courtyard for yourself, brothers, friends or family members, please contact us at **800-456-7452**.

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Conclusion. The recently IRS enacted limitations emphasize the need for longer-range financial and estate planning by reducing the opportunity for an income tax deduction in the current taxable year. As a result, it has become even more critical for taxpayers to act promptly in an effort to limit the effect of spreading the income tax deduction over the next five years. This is consistent with other actions taken by the IRS in an effort to restrict large deductions, and to require that taxpayers spread large deductions over a period of years. Any movement in this direction will require more planning for the future and action by the taxpayer at earlier stages.

Charitable Remainder Trusts are well-established financial and estate planning vehicles which can achieve some rather unique results. If

you are interested in considering a gift of appreciated securities or unencumbered real estate through a CRT to the Pi Kappa Alpha Educational Foundation, please contact Executive Director Patrick F. Haynes at 800-456-7452.

About the author: Thomas J. Handler (Illinois, Beta Eta '74) was elected International President of the Pi Kappa Alpha Fraternity in 1998. He is the senior partner of Handler, Thayer & Duggan, a Chicago based business, taxation, and estate planning law firm. Handler is a published author and lecturer on tax, financial, and estate planning topics. He previously served the Fraternity as Supreme Council vice president, national rush director and as an undergraduate vice president. He is a member of the Educational Foundation's Oak Trust, as well as the Sabre & Key Society and a Charter Life Member of the International Alumni Association. Handler serves on the board of directors for several corporations and two educational foundations. He and his wife, Kim, have three children, Ross, Lauren and Kent.

Fast Facts Enclosed

As one of the Educational Foundation's loyal supporters, you have shown through your financial support that you believe in the Foundation's mission and the numerous scholarship and leadership programs it sponsors. It is the hope of the Foundation's staff and trustees that you will also encourage the fellow brothers you

keep in contact with to *join you* in your support of the Educational Foundation. **In short, we hope you say good things about Pi Kappa Alpha!** The enclosed fast facts is designed to keep you better informed and allow you to be well educated about Pi Kappa Alpha as you spread the news of our good work. *Enjoy!*

