

Gifts of IRAs Letter

Dear

Thank you for your inquiry regarding naming our organization as a beneficiary of your retirement plan. This letter presents a few key points you should discuss with your financial adviser and estate-planning attorney.

Traditional individual retirement accounts (IRAs) and other forms of deferred compensation are very efficient wealth accumulation devices. They are usually funded with tax-deferred income and grow tax-free. But they can be wealth transference disasters. (The Roth IRA is an exception to this rule, but only a small percentage of IRAs are Roths.) In other words, your hard-earned retirement nest egg may not make it to your heirs unscrambled; and estates subject to estate tax have the most to lose.

Take the case of a 74-year-old widower with an estate vulnerable to estate tax. Let's say he has \$150,000 remaining in his retirement account at death. How much of that \$150,000 will his heirs receive? About \$45,000, or 30 cents on the dollar.

It's just a matter of doing the math. An individual who dies with no spouse and an estate subject to estate tax will have the funds remaining in his retirement account taxed at about 45%. But it's not over yet. The surviving beneficiaries of the account will then pay income tax on the entire amount when distributed, less a credit. The result: a double tax of about 70%. This is one reason that some attorneys encourage clients who wish to leave gifts to charities in their estate plan to pass the IRA to charity and give less tax-vulnerable assets to their heirs. IRA gifts generally cost heirs less.

If you want to include our organization and other good causes as beneficiaries of your retirement plan, talk to the plan's manager or seek qualified counsel to make sure your retirement plan distributions take place the way you want them to.

Some pension plans are set up in such a way that nothing is left in the estate when the beneficiaries, usually husband and wife, die. But some individuals will have a high percentage of their retirement plan assets in their estate at death with little protection from taxes. And you don't have to have an estate subject to estate tax to see retirement fund principal diminished by taxes. A man wanted to leave half of his estate to charity and half to his heirs. The estate was worth about \$600,000, most of the value divided equally between his home and his IRA. He left the \$300,000 IRA to his heirs and the \$300,000 home to charity, the exact opposite of what he should have done.

The heirs had to pay almost \$80,000 in tax on the IRA distribution. If the man had left the \$300,000 home to his heirs, and the IRA to charity, the heirs would have had no tax to pay, nor would the charity.

There's one estate planning strategy that can allow you to benefit both your heirs and charity: the transfer of retirement funds to a testamentary charitable remainder trust. Instead of passing directly to heirs at death, the IRA assets pass to a charitable remainder trust with the

heirs named as income beneficiaries, either for life or a term of years. The benefits of using the testamentary charitable trust to capture and preserve IRA principal are:

1. The heirs may avoid a large income tax bill that might otherwise be immediately due
2. Trust principal, preserved from initial heavy tax, then pays income to heirs either for life or for a term of years
3. The contribution to the trust generates an estate tax deduction, with the size of the deduction determined by the ages of the income beneficiaries or the term of years chosen
4. Payments from the charitable trust to beneficiaries may last many years longer than payments from the IRA since IRA payments are determined by the life expectancy of the *oldest* beneficiary

For example, if a husband wanted to benefit his wife and then his children through his IRA, he could name the wife as the first beneficiary and his children as the successor beneficiaries. In that case, however, the IRA may be depleted when the wife dies, leaving nothing for the children. The IRA must be distributed according to the life expectancy of the oldest beneficiary, in this case, the wife. If she lives beyond her life expectancy, there will be no further payments to *her*, much less to the children. Charitable trusts avoid these problems while providing a future gift to charity.

Determining whether the use of a testamentary charitable trust fits your situation is a matter for careful study. We will provide you with tax and income calculations tailored to your particular situation. This will give you and your advisors the information needed to make an informed decision as to whether a charitable trust meets your financial and philanthropic objectives. All information is provided confidentially and without cost or obligation. Please do not hesitate to call.

Thank you for considering our organization in your estate plan. Your support is appreciated.

Sincerely