



The Tax Advantages of Charitable Gift Annuities

Would you like to donate to the causes you care about, while also generating a steady retirement income and saving on your taxes? If doing good, while continuing to work toward achieving your financial and estate planning goals sounds appealing, you may want to consider purchasing a charitable gift annuity.

Many charities have programs that assist donors in purchasing gift annuities, which are designed to provide long-term financial support to both the donor and the nonprofit organization. Essentially, a charitable gift annuity is a contract between the donor and the nonprofit organization that calls for the charity to make fixed lifetime payments to the donor and, in some cases, to his or her spouse. In exchange, the charity receives the remainder of the gift to further its work when the donor, or the donor's spouse, dies.

Recognized by the IRS as a form of philanthropic giving, a charitable gift annuity offers a number of potential tax advantages. The portion of the annuity purchase that is considered a gift can be included as a charitable contribution on your itemized deductions. In addition, a portion of the payments from a charitable gift annuity are tax-free until you reach your life expectancy, while another part is taxed at ordinary income rates. If you donate appreciated securities, you will owe some capital gains taxes for the sale portion of the transaction, but the taxes are payable over your expected lifetime, rather than being due immediately.

In addition, purchasing a charitable gift annuity can reduce the size of your taxable estate. You may, for example, wish to donate appreciated property that currently generates little or no income, but which would be taxable if it were sold or passed on to the next generation.

A charitable gift annuity can also be a great option if you want to donate to your favorite charity, but cannot afford to make a large gift outright. If you are thinking about purchasing a charitable gift annuity, you should, however, be aware that these annuities are not identical to commercial products, which generally offer higher rates of interest. But the tax savings associated with gift annuities can help to offset the smaller payments. The interest rates paid by all types of annuities are also usually superior to those paid on savings accounts and certificates of deposit.

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Dodd Consulting, LLC
One Landmark Square, 8th Floor
Stamford, CT 06901-2603
Phone: (203) 504-3633
Fax: (203) 504-3639
E-mail: info@doddconsulting.net
Website: www.doddconsulting.net

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Your Financial Affairs: What Your Children Should Know

Many parents may find it uncomfortable, or even believe it is unnecessary, to inform their children about personal finance matters. Yet, communicating openly with your family members can help to reassure them about your financial and health care wishes. This may also ease the decision-making process for your family in many important areas.

As time goes by, informing your children of financial, estate, and medical arrangements that could affect the entire family helps everyone prepare and plan for the future. This does not need to include detailed facts and figures; however, you may want to consider sharing the following information with your adult children:

- **Life Insurance.** Life insurance is typically purchased to provide a death benefit to help cover final expenses, estate taxes, outstanding mortgages, other liabilities, and lost income. Knowledge of the existence and location of life insurance policies can be of the utmost importance to children when settling their parents' finances in a timely manner.

- **Other Insurance.** Be sure to inform children of other insurance policies that you may have, including health, disability income, and long-term care insurance. If you're age 65 or older, make sure your children have a basic understanding of **Medicare** coverage and are aware of any health insurance policies that exceed Medicare coverage. Older adults can greatly benefit when their children understand and follow appropriate procedures, as well as submit any necessary forms on deadline.

- **Wills.** Preparing a will allows you to avoid leaving the disposition of your estate up to your particular state and its probate laws. To help ensure that your assets are distributed according to your wishes, both you and your spouse should prepare wills, review them regularly, and make necessary updates as circumstances change.

Although specific contents can be kept private, it is important to disclose the existence and location

of wills to several family members or a trusted legal advisor. Keep in mind that bank safe-deposit boxes may be temporarily sealed at death, so you may want to choose an alternate location for this key document. For example, the original will may be left with your legal advisor for safekeeping.

- **Trusts.** Trusts can help protect your estate from unnecessary taxation or mismanagement. Make sure to discuss pertinent terms with those who will be involved. As children reach adulthood, it is common for parents to select a responsible son or daughter to act as *trustee* in the event of the parents' death.
- **Living Will.** This document specifies your preferences regarding the administering or withholding of life-sustaining medical treatment. Under many state statutes, a patient must be considered "terminal," "permanently unconscious," or in a "persistent vegetative state" before life support can be withdrawn. Be sure to provide copies of living wills to anyone who may be involved with the health care of you or your spouse, and keep the originals in a safe, readily accessible place.
- **Health Care Proxy.** This legal document allows you to appoint a person to act as an agent on your behalf to make medical decisions, should you become incapacitated. It is important to file a copy of the health care proxy with your primary doctor and your hospital, if possible. In addition, be sure that the individual appointed as your agent retains a copy.



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Purchasing an annuity can be especially attractive at more advanced ages, as the payments will be higher. If you are younger and do not yet need the income, you can select an annuity that allows you to defer payments until reaching a specific age. If you are interested in buying a charitable gift annuity but do not yet know when you might wish to start collecting payments, you can opt for a flexible annuity, which does not require you to choose the payment starting date at the time of purchase.

To set up a charitable gift annuity, the donor typically makes a donation of cash, stock, or other assets for a set amount—usually no less than \$5,000. Under a “single life” agreement, the charity commits to making payments to one person for the course of his or her lifetime, while under a “two lives in succession” agreement, the charity makes payments first to one person, and then to a designated survivor. If you are

married, you may prefer to enter into a “joint and survivor” agreement, in which the organization splits the payments between spouses during their lifetimes, and makes the full payment to a surviving spouse.

Remember, however, that annuities are irrevocable, and you will not be able to extract your funds or property once the donation has been made. Keep in mind, too, that charitable gift annuity payments are not inflation-protected, and your income from this type of annuity will not go up even if the cost of living rises. On the other hand, the annuity payments become a general obligation of the charity, and the annuity is backed by the organization’s entire assets, not just by the property donated. The charity is therefore committed to continuing payments throughout the lifetime of the donor, regardless of whether the funds used to purchase the annuity have been exhausted.

Even if you are already familiar with the charity from which you are purchasing the annuity, it is nonetheless advisable to investigate the financial stability of the organization to ensure that it will be able to make payments well into the future. If the charity becomes insolvent, the funds will be lost and annuity payments will stop. Charitable gift annuities are not insured, but some states regulate this type of annuity, generally requiring charities to maintain sufficient reserves to meet its obligations to annuitants.

It is usually best to choose a charity that has an established charitable gift annuity program, as they will be able to guide you through the process of purchasing an annuity, and will be able to help you resolve any issues that might arise. ■

your financial affairs: what your children should know

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- **Durable Power of Attorney** With a durable power of attorney, an individual or financial institution may act as an agent to oversee your legal and financial affairs, even if you become incapacitated. Grown children need to be informed of the steps that have been taken to ensure the competent direction of your finances, should the need arise. However, their actual *involvement* in your financial matters may be limited, according to your wishes. A power of attorney automatically terminates upon the death of the principal.
 - **Assets and Debts.** It can be beneficial for your children to know that you have compiled a list of your assets and debts, even if you choose not to show them the list. An asset list updated regularly may include information on your bank accounts, real estate holdings, pension payments, annuities, business agreements, brokerage accounts, boats, cars, artwork, collectibles, jewelry, or other valuables, and insurance policies. A debt list may include information on your current mortgages, consumer indebtedness, personal loans, and business obligations. For both lists, be sure to identify where the paperwork and associated files for each item can be found.
- Initially, preparing these lists and the associated documentation may seem like an overwhelming task. However, once completed, both you and your adult children may experience a sense of relief in the knowledge that thoughtful planning was discussed and implemented according to your wishes. ■

Disability Income Insurance: Some Features Say it All

Prospective insurance buyers may often get confused about **disability income insurance** because the features and benefits can vary widely from one policy to another. Essentially, there are a few key elements that could make a difference when you choose a policy. If you are in the market for disability income insurance, here are some points you may want to consider:

Definition of “Total Disability.”

Does the policy define total disability as a condition during which you cannot perform the duties of your *own* occupation or *any* occupation? A policy that refers to your own occupation generally pays benefits if a sickness or injury prevents you from working in your occupation, even if you could work in a different job. A policy that refers to any occupation typically pays benefits only if you are unable to perform *any* job: your own job, a lower-paying job, or a job in a new occupation.

Duration of Benefits. Even if you have to choose a smaller benefit amount to keep the premiums affordable, look for coverage that protects you until age 65. Note that there are policies available that offer benefits only for a limited period (such as a maximum of two or five years), and the nature of your occupation may affect the duration of coverage.

Amount of Coverage. Policies usually set a limit on the percentage of income you can insure—usually 50% to 70% of your total gross earnings. If you have an employer-provided plan that offers only limited group coverage, you may want to supplement this coverage with individual disability income insurance.



Elimination Period. The waiting or “elimination” period is the amount of time you must be disabled before disability benefits begin to be paid. While a shorter waiting period requires a higher premium, a longer waiting period may mean you will have to rely on your savings until benefits begin. Keep in mind that the waiting period is determined when a policy is *issued*, not when you sustain the disability.

Taxation of Benefits. Benefits may be tax free if you pay the premiums using *after-tax* dollars. If you receive benefits under an employer-provided plan, they may be taxable if the premiums are paid with pre-tax dollars. Consult your tax professional for specific guidance on this matter.

Partial or “Residual” Coverage. After a serious disability, many people are able to return to work only on a part-time basis. Partial or “residual” benefits allow you to receive partial disability benefits, as well as your part-time income, until you fully recover. Without this feature, your benefits may stop as soon as you return to work, even if only part time.

Portable Coverage. Policies that allow you to carry your coverage from one job to another have an obvious advantage. Examples include coverage from a professional association providing portable coverage that is not tied to your place of employment, as well as any individual disability income policy that you might purchase independently.

It is important to determine the amount of coverage needed that best suits your situation before shopping for a policy. Review your insurance coverage and needs on a regular basis with a qualified professional to make sure that you are adequately protected. ■

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