

Why Wait? The Financial and Emotional Rewards of Philanthropic Giving

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Enterprise-owning families work for generations to build their wealth but most do not invest the time to plan for transferring it effectively. Preparing for transfer of assets can be a very daunting — and emotionally challenging — responsibility that often leads to inaction. Estate planning tends to be a reactive one or two time event. A successful wealth transfer plan should be a living and breathing one that is regularly reviewed and updated to meet the goals of the family.

The Great Recession of 2008 allowed many families to utilize their lifetime gift exemptions to transfer considerable amounts of their privately-held businesses at a deeply discounted rate. Since then, we have seen a significant increase in the value of these businesses, which has caused taxable estates to grow to levels that have exposure to estate taxes. So, reviewing plans and evaluating strategies for tax-efficient asset transfer should be on the priority list for many families.

Legacy Planning

One strategy that doesn't always get the appropriate attention is charitable giving, also referred to as legacy planning. While this often includes charitable bequests at death, we are now seeing more families choose to make an impact on the community while living. This is where legacy planning takes on a new life by providing families with the opportunity to see the how their hard-earned assets can make a difference to the causes that matter to them.

The estates that have surged in growth since 2008 have an opportunity that is right under their nose: the repurposing of monies towards philanthropy that otherwise are lost to estate taxes upon death. The idea

is to use these dollars to start building a legacy. Families can proactively take control of their planning by thinking entrepreneurially about their balance sheet in the same way they do about growing their businesses. Every dollar that is set aside for charitable planning is one that is not estate taxed. Simply stated, legacy planning is low-hanging fruit in the estate plan that provides the family with a balance sheet that affords a much greater impact.

Impact Giving

The following is a case of a family that has shifted much of their wealth to heirs but still has a \$52 million taxable estate. Their lifetime gift exemptions have already been used, so every dollar at death is exposed to estate taxes. The bottom line is that nearly \$21 million is going to be lost to taxes (applying the 40% maximum federal estate tax rate), leaving the heirs with approximately \$31 million.

The table (next page) shows an option of putting in place an additional wealth transfer strategy that allows the same \$31 million to go to heirs but reduces estate tax liability and allows for substantial philanthropic gifts. A series of actions achieved these outcomes. For starters, they designated \$34 million for charitable giving that is exempt from taxes. Their plan is to allocate this money to charitable gifts over a number of years.

In tandem, they loaned an \$18 million, high-growth asset to a trust for nine years for the funding of a \$20 million life insurance policy. Growth in the \$18 million is used to fund the premiums on the life insurance policy. The loaned \$18 million returns to the estate after year nine when the note is paid off and will remain in the

Methods of Efficient Asset Transfer

Current Estate Value \$52,000,000

Plan	Net to Heirs	Estate Taxes	For Charity/ Family Foundation	Effective Tax Rate	Total to Heirs & Charity	Net Gain Compared to Current Plan	Repositioned Assets to Accomplish	Per \$1 - Enhanced Legacy Benefit
Current	\$31,232,000	(\$20,768,000)	\$0	40%	\$31,232,000	\$0	\$0	\$0
Private Financing	\$31,232,000	(\$6,922,667)	\$34,613,333	13%	\$65,845,333	\$34,613,333	(\$6,000,000)	\$6

*Courtesy of Jeff Craig's Legacy Analysis System

estate. The \$18 million, now returned to the estate, will net approximately \$11 million for their heirs after estate taxes. The \$20 million life insurance policy makes up the rest to deliver the same \$31 million amount to heirs as was originally intended.

This plan allows the family to leave the same \$31 million to the heirs, while also making charitable bequests of \$34 million and reducing the estate tax liability substantially. When combined, the family's impact to heirs and charity is \$65 million as opposed to leaving the heirs \$31 million and none to charity. This is just one example of a combination of estate planning and charitable vehicles that can accomplish a similar result.

Making a Difference Proactively

The appealing part of this type of planning is the impact it can have beyond the financial benefits. For instance, the elder generation can witness the fruits of their hard work when deployed against a worthy cause. Rather than having a foundation created in their memory, they can share their philanthropic interests with the next generations and hopefully inspire them to give back as well.

For many entrepreneurs who have built successful enterprises, the estate-planning process can be discouraging and frustrating. Rather than a proactive, creative process, it is often viewed as reactive because it's focused on reducing wealth erosion rather than wealth creation. By deploying proactive strategies to leverage philanthropy, entrepreneurs can participate actively in their estate planning execution, and in a way, create a new family business focused around giving

back. Ultimately, the business that is created can be open to future generations of the family to pursue.

While grandchildren may not be interested in working for the family business, they may be responsive to participating in family service projects, visiting communities where money is given and developing charitable interests of their own. Philanthropy can become a rich part of your family's story — defining its legacy and values into future generations.

Many wealth holders fear the impact that family wealth will have on future generations. They would rather avoid talking to younger family members about their wealth than risk the potential fall-out of entitlement. Engaging the family in a conversation about the value of money and what good it can do in the world is a way to couch the wealth discussion in a more productive manner. It is also a way to proactively demonstrate a family's priorities and values.

That said, many clients we have worked with become disheartened with the time and effort involved to orchestrate philanthropic giving. Some struggle with joint family giving because they are challenged to find common interests across the family. To maximize the positive impact of family giving, consider making your philanthropic vehicle one through which all family members can pursue their personal giving interests, rather than execute on a family mandate defined by historical areas of giving.

One solution is to provide each family member with access to a pot of money for charitable donations that does not need to be specifically carved out. The

family could simply reach an understanding that each member above a certain age has discretion over a set giving amount each year. In addition, a process could be established where individuals share their philanthropic giving idea to the broader family in the hopes of getting family membership to co-invest with them. In this scenario, family members learn about others' interests and individuals have the opportunity to expand the impact of giving to their favorite cause.

Another challenge of establishing a giving mechanism is the time required to evaluate grant requests, research potential grant recipients, hold formal board meetings, file tax returns and oversee investment allocation and performance. In addition to making giving flexible, another lesson from philanthropic families is to make your structure and process as simple as possible. A private family foundation imposes minimum giving requirements every year which requires a formal board of trustees to provide oversight to the grant process and investment portfolio.

Alternatively, a donor-advised fund structure can be much less onerous. With this structure, the givers focus on grant requests which limits the time spent and expense of filing tax returns, holding formal board meetings, administering grants, etc. Donor-advised funds do not require a minimum grant distribution

each year (5% of assets for private foundations) and have other financial benefits as well (e.g., higher tax deductibility for gifts of stock, cash and other assets). Other giving structures to consider include supporting organizations (used if you are giving to one specific cause) or charitable remainder trusts.

If you haven't already established a giving vehicle, investigating options and developing your giving process together can be a rewarding project for multiple generations of a family. Through these efforts, the family can participate in building a new business together. Research shows that involvement in decision making increases engagement. So, family members who get to participate from the start are more likely to remain involved over time.

Even if you already have a sophisticated estate plan, you may want to reconsider how your assets are allocated given the opportunity that philanthropic giving provides as a shelter to taxable assets. A visit with your advisory team with these ideas in hand may suggest some revisions to your current plan.

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