Making Charitable Donations with Unique and Hard to Liquidate Assets

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Preliminary Statement

Before we begin you should know that my organization, Charitable Solutions, LLC operates a public non-profit donor advised fund, Dechomai Asset Trust, that acts as an intermediary between donors and charities. I am a trustee of that Fund. If or when all of the difficulties that charities face in accepting unique and hard to liquidate assets and all the techniques professionals like you may use to overcome those difficulties fail we facilitate the gift. Last year we processed the gifting of $150MM in unique assets and made $90MM in grants

Why Charities Refuse Gifts of Unique and Hard to Liquidate Assets

- The charity as a matter of policy only accepts gifts of cash or marketable securities.

1. Aversion to any risk taking.
2. Bad experiences when deviating from the general policy.
3. Difficulties encountered when forced to accept an asset outside of the policy because of death or the offer of such gift by a significant donor.

Why Charities Refuse Gifts of Unique and Hard to Liquidate Assets

- The charity lacks the expertise to accept or reject the asset

1. The personnel lack appropriate training or knowledge.
2. The organization is new and/or there is insufficient funding in the development budget to perform the necessary due diligence.
3. The charity relies upon outside professionals to do the due diligence on a pro bono basis and/or hasn’t the necessary funds to hire professionals.

Why Charities Refuse Gifts of Unique and Hard to Liquidate Assets

- The charity has sufficient expertise but insufficient staff to accept or reject these types of gifts

1. Many charities are top heavy in development personnel asking for gifts of liquid assets but have few, if any, people in planned giving where such gifts are often processed.
2. On the other hand, one of our clients has a large staff of people working on the acceptance of unique and hard to liquidate assets but still calls upon us to handle a portion of its volume.

Why Charities Refuse Gifts of Unique and Hard to Liquidate Assets

- The charity has a complex decision making tree or a complex methodology for accepting these types of gifts that ultimately discourages donors and often results in the withdrawal of the gift offer.

1. Charities often form boards to make the ultimate decision to accept or reject a unique or hard to liquidate asset. By the time the due diligence has been performed, the diligence analyzed by either the Office of General Counsel and/or outside consultants and the gift is considered for acceptance by the board, the donor has either changed his/her mind, sold the asset or given it to another charity
2. Even when the time lag from offer to acceptance is short the methodology for accepting the gift may be so complicated that the donor gives up his/her desire to make the gift.

Creating Advantageous Conditions for Acceptance of an Outright Gift

- Your client wants to give his second home in the Florida Keys to his/her favorite charity or non- profit (“ the Charity”). You know from your conversations with the development people that its policy is not to accept real estate but they have been hard after your client to make a significant donation. The home has no debt and is worth $750,000. How can you overcome the reluctance of the Charity to take the real estate as a gift?

Real Estate Example

1. Get an up to date title insurance binder from the title company who insured the title originally.
2. Approach 2 or 3 highly regarded real estate brokers in the area and ask them to write letters expressing their opinion of value of the property.
3. Get an appraisal of the property from a well known appraiser in the area.
4. Have the property inspected and obtain a written report on its condition.
5. If there are any environmental problems that can be either easily solved or insured against, solve them or obtain appropriate insurance.
6. Make sure that the property and liability insurance can be transferred and if it cannot be transferred have the donor offer to reimburse the Charity for the premium as an additional donation while it is owned by the Charity and is being marketed.
7. Have the donor agree with the Charity that he/she will reimburse the Charity for all the expenses of maintaining the property, including but not limited to real estate taxes, condo fees etc. after it is owned and being marketed by the Charity.

Real Estate Example

- You might ask why my client would agree to undertake these tasks and pay these expenses in order to make a charitable contribution?
- The answer is that your client would probably undertake these tasks and incur most of these same expenses if he/she were merely selling the property. By paying for them he/she is able to treat the payments either as additional charitable contributions or as expenses of preparing the property for sale while at the same time saving capital gains taxes and getting a $750,000 plus income tax charitable deduction that can be spread over the year of transfer and the next 5 years, if necessary.

C-Corp Example

- Your client wants to give some stock in his company to his/her Charity. But its policy doesn't allow it to accept gifts of privately owned company stock. How can you overcome the reluctance of the Charity to accept your clients gift?

C-Corp Example

1. Give the Charity a brief written history of the corporation's activities, who are the other stockholders, if any, the number shares owned by each of them and their relationship to the donor.
2. Obtain an appraisal of the value of the stock that the donor desires to gift and share it with the Charity.
3. Give the Charity the right to redeem the stock for a fair and reasonable price based on the appraisal.
4. Gather all of the relevant documents: Articles/Management or Operating Agreements/Current By-Laws

   Recent Tax Returns and/or Financial Statements,

   Shareholder Agreements and share them with the

   Charity.

S-Corp and LLC Examples

1. Same as the C-Corp example except supply three years of tax returns and K-1s.
2. In addition to giving the Charity a right to redeem at some fair and reasonable price, provide it with a plan to provide sufficient cash flow to enable the Charity to pay the taxes on the Unrelated Business Taxable Income ("UBTI") generated by the entity during the holding period prior to redemption. **"The Put Agreement"**

Limited Partnerships

1. Same as the S-Corp and LLC examples with the additional protection in the “Put Agreement” that the donor will provide the amount of any calls or additional capital contributions.
2. Limited partnership agreements often enable the limited partners to transfer all or part of their interests in case of death or to make charitable contributions. Since the assignees of these interests may have little or no understanding of the partnership’s activities an agreement can create a class of partners, sometimes called “assigns”, who receive the benefits of the partnership but are not subject to the obligations that would make the Charity reluctant to take and/or continue to hold the interest. Amending the partnership agreement may allow the Charity to consider accepting the gift.

Creating Advantageous Conditions for Acceptance of a Planned Gift

- Your client is a similar donor to the one we encountered in Slide # 7 except the he/she wants to donate his/her **home** to the Charity and he/she prefers to do so though a planned gift so that he/she will have income for life and/or he/she can use his/her home for life before it is sold.

Retained Life Estates (“RLE”)

1. The donor conveys the home to the Charity retaining a life estate.
2. The deed or separate agreement places all the responsibilities for every aspect of owning the home on the donor for the balance of the donor’s life
3. Even though this document greatly reduces the Charity’s risk it does not eliminate its policy against owning the real estate.

Retained Life Estates ("RLE")

1. In addition to performing many of the tasks suggested in slide #8, the donor could form a single member LLC, transfer his/her interest in the home subject to the RLE to the LLC and then transfer his/her membership interest to the Charity.
2. The Charity may still have some misgivings about accepting a unique asset like a membership interest in an LLC, but it will not have to accept title to the real estate which in most cases is the main objection to accepting gifts of real estate.

Charitable Remainder Trusts (“CRT”)

Our hypothetical donor in slide #7 wants to use the property to fund a 5% charitable remainder unitrust so that he/she will receive income for life before the Charity has access to the funds. The Charity not only doesn’t accept real estate gifts, it will not act as a trustee of a trust holding an illiquid asset.

1. Have the donor act as the initial trustee or find an independent third party to do so.
2. After the sale of the property the donor or third party can resign his/her trusteeship in favor of the Charity who can then invest the funds from the sale.
3. The donor’s income increases or decreases based on the success of the Charity’s investment strategy.

Charitable Remainder Trusts (“CRT”)

1. Unlike the RLE the donor must move out of the property upon transfer to the trust and cannot use it for any purpose.
2. By acting as his/her own trustee he/she controls the sale process and can wait indefinitely for the right buyer and/or the best price.
3. However, during the marketing period he/she will have to make additional charitable contributions to the trust to cover operating expenses.
4. The donor should have no objection to initially self trusteeing the trust since it gives the donor maximum flexibility and the expenses of operation are the same as if he/she put the house up for sale without forming the trust.

Charitable Gift Annuities (“CGA”)

- Our hypothetical donor in slide #7 wants to use the property to fund a planned gift that will pay he/she a fixed amount each quarter for life no matter how the Charity’s investment strategy fares. Although the Charity does have charitable gift annuity program it doesn’t accept real estate gifts and wouldn’t consider paying a fixed sum each year while holding such an asset.

Charitable Gift Annuities (“CGA”)

1. If the Charity did accept real estate to fund an annuity it would probably want one or more concessions from the donor to reduce its risk
2. Either reduce the percentage payout and/or defer the payments a year or more until the property could be sold.
3. Neither concession may be acceptable to the donor.

Charitable Gift Annuities (“CGA”)

1. Consider writing a CGA that protects the Charity from almost all the risks of advance payment and combine it with the first 6 points of slide # 8 protecting the Charity from most of the risks of holding the property.
2. In this form of CGA the Charity begins paying the donor based on the appraised value of the property.
3. When the property is sold the principal amount of the annuity is reduced to the net selling price from the appraised value but the % payout (which based on the age of the donor) remains the same.

Charitable Gift Annuities ("CGA")

1. The Charity can recapture any overpayments made prior to the sale by withholding them from amounts due in the next quarterly distribution(s).
2. The adjustment period can be for any amount of time agreed to by the Charity and the donor. Therefore, if the house does not sell for three (3) years the adjustment from the appraised value to the net selling price can be made at that time and the recapture can be withheld from future distributions.

Charitable Gift Annuities (“CGA”)

1. The Charities only downside is the opportunity loss it suffers from the inability to invest the incremental amounts it paid to the donor prior to the sale of the property.
2. During the holding period all of the costs of maintaining the property are deducted from the sales proceeds to derive the net sales proceeds.

Summary

- Outright gifts of unique and hard to liquidate assets are challenging and gifts of these same types of assets to implement planned gifts are even more challenging. However, since real estate, private company stocks, private partnerships, collectibles and oil and gas interests etc. make up the bulk of the wealth in the country, ignoring the use of these assets to make gifts is a major mistake on both the part of donors and charities.