Aging Out: Is Your Donor Too Old to Make a Planned Gift?

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Because age is a relative concept, in certain cases it can be no problem for a very elderly donor to establish or modify a planned gift. Likewise, there can be all sorts of reasons a much younger person should not make a planned gift. Still, a handful of issues become increasingly worthy of close attention the older someone considering a planned gift is.

Legal Capacity to Make the Gift

Once a person reaches adulthood, he or she is generally presumed to have sufficient ability to make legally binding decisions and take legally binding actions. As people reach their later years, however, conditions such as dementia can diminish their legal capacity. In any given donor's case, although especially if the donor is well on in years, someone who might object to a donor making a charitable gift due to lack of capacity will ultimately be required to demonstrate a couple of things to the satisfaction of an appropriate court.

First, the challenger must establish that he or she has "standing," which largely equates to a monetary stake in the action the donor is contemplating. A child of the donor typically would have standing, whereas a concerned neighbor or friend probably would not.

The challenger must also prove that the donor does not have sufficient legal ability to do what the donor wants to do. What is sufficient can vary a bit depending on the type of gift in question. Thus, there may be one standard for a testamentary gift such as a bequest, another for conveying a piece of real estate, and yet another for a gift annuity, which is a type of contract.

Basically, a donor with adequate legal capacity understands the nature and extent of his or her assets (along with, perhaps, other details of his or her overall financial situation), as well as who would be what are often referred to as "the natural objects of the donor's bounty." With this understanding, the donor needs to know also what the consequences of the gift will be.

The applicable legal requirements will be a matter of state law. Interestingly, they need to be met only at the time the gift is made (which, in the case of a bequest, would be when the will is signed), meaning that a lack of capacity at some other time is technically irrelevant – although perhaps nevertheless significant for a gift planner.

Indeed, a gift planner who has concerns about a donor's capacity should take steps to ensure that the donor has independent legal counsel who can act to prevent the donor from completing a gift he or she is not legally able to make. Of course, if legal counsel determines the donor does have sufficient legal capacity, the gift planner can take a good measure of comfort that the gift will not be challenged.

Power of Attorney to the Rescue?

Even though the word "attorney" is often a synonym for "lawyer," its fundamental meaning is "agent." When a donor gives an individual or an entity power of attorney, the donor is making the recipient his or her agent for legal purposes. Within the scope of authority granted by the donor, the agent must act in the best interests of the donor.

Sometimes when a gift might be made by a donor whose legal capacity is doubtful, a party to whom the donor has given power of attorney may be able to complete the gift on behalf of the donor. That being said, a couple of hurdles can present themselves.

A threshold question will be whether the donor's granting of power of attorney is valid in the first place. If the power of attorney document was signed recently, yet concerns about the donor's capacity have existed for a longer period of time, the document may not be of much help. Ideally, the donor will have sought the assistance of legal counsel in drawing up and executing the document, and the drafting lawyer will have determined that the donor truly did have sufficient capacity to grant power of attorney.

Assuming the document is sound, it may not give the agent the power to make the gift in question. In practice, it is relatively unusual for an individual to give someone else legally binding authority to make any sort of gift, whether charitable or not. What one sometimes sees is a power to make gifts that reflect the continuation of a pattern of giving the donor has established in the past, but what if the gift at issue is much larger than past gifts or is to be made to a charity the donor has never supported before?

In short, counting on a power of attorney arrangement to save the day may not prove to be worthwhile. Furthermore, whenever a power of attorney document is to be relied upon, legal counsel for the recipient of the gift (whether a charity or a trustee) should confirm that the agent has the requisite donative power. Oh, and it's typically impossible for one person to give another the authority to make or revise a will.

Beware of Large Income Tax Deductions

The following four types of planned gifts produce an income tax charitable deduction for the donor:

- Charitable gift annuity (CGA)
- Charitable remainder trust (CRT), which can be either a charitable remainder annuity trust (CRAT) or a charitable remainder unitrust (CRUT)
- Pooled income fund (PIF)
- Retained life estate (RLE)

Except in the case of a CRT or a RLE established for a term of years or for the life of someone other than the donor, the older the donor is, the larger the deduction will be. (Note: In rare instances, a fifth type of planned gift – a charitable lead trust – can be structured to produce an income tax charitable deduction, but if the term of the trust is measured by the donor's life, then the older the donor is, the *smaller* the deduction will be.) In fact, depending on the type of gift and many other variables, someone age 90 can receive a deduction of from 60 percent to nearly 90 percent of the value of the assets contributed.

So long as a donor can claim all of the deduction resulting from a planned gift in the year the gift is made, the full benefit of the deduction is secured. Of course, many donors, regardless of their age, receive deductions that are quite large in comparison with their adjusted gross income (AGI). This phenomenon is largely attributable to the fact that planned gifts are commonly made from a donor's assets, rather than from his or her income.

Whenever a donor who itemizes his or her deductions is not able to benefit from the deduction completely in the year of gift because the donor's total charitable deductions are too large in relation to the applicable percentage-of-AGI limitation (50 percent for gifts of cash and ordinary income and 30 percent for gifts of long-term appreciated capital assets for gifts to public charities), the donor must carry the unused deduction forward. This can be done a maximum of five times. Deductions carried forward can be taken subject to the usual percentage-of-AGI limitations in each carry-over year and given the charitable deductions received that year and other unused deductions carried over from prior years.

While it may seem obvious, an unused deduction can be carried over only into a year in which the donor remains alive. Because older donors have shorter life expectancies, they have a somewhat smaller chance of benefiting fully from any deduction that cannot be used fully in the year of the gift.

In addition, the full amount of any carry-over is personal to the donor. Thus, if a planned gift was funded with a married donor's separate property, the last year in which to use the carry-over is the year the donor dies. This is true even if the donor and spouse file a joint income tax return. Similarly, if a married couple receives a deduction in connection with contributing jointly-owned or community property, one-half of the deduction is effectively assigned to each of them. If one of them dies before all of the deduction has been claimed, then the amount to be carried over into the year following the death of the first of the spouses to die is reduced by 50 percent on account of that death.

This consideration should not necessarily preclude an older donor from making a planned gift resulting in a deduction that is large in proportion to the applicable percentage-of-AGI limit. Nevertheless, a gift planner should draw the donor's attention to the rules and urge the donor to discuss the matter with an independent tax advisor.

A final issue that can be somewhat more relevant in the case of a gift arrangement measured by the life of an older person is that Treasury Regulations may require the deduction to be calculated using a "special factor" if the person "is known to have an incurable illness or other deteriorating physical condition" and "if there is at least a 50 percent probability the individual will die within 1 year." If such a factor must be used, it will increase the size of the deduction in the case of all relevant planned gifts except a charitable lead trust, which will feature a lower deduction. Of course, if a donor is that close to death, whether he or she should be arranging any such gift is highly questionable.

Skinning the Capital Gains Tax Cat

There's often a lot to be said for funding any of the three so-called "life-income" gifts – CGAs, CRTs, and PIFs – with long-term appreciated, publicly-traded securities (and sometimes with other long-term capital gain assets). This is not only because the deduction is based on the full value of the asset, but also because either all or a portion of the capital gain can be avoided or at least taxed over the course of many years. If a charitable individual has determined that, for whatever reason, the time has come to dispose of a long-term capital gain asset, then using that asset to fund a life-income can make a lot of sense.

As always, however, the totality of a donor's situation should be examined. If an older donor's objectives include providing for a surviving family member, the tax benefits normally associated with using long-term appreciated assets to fund a life income gift need to be viewed in perspective. True, sometimes all the donor will need to do is make the family member a co-beneficiary (or even the sole life income beneficiary) of the gift arrangement, although this can present a whole host of issues.

It might be preferable for an older donor to forego making any gift during life, for if the donor owns the assets in question upon death – and if they have held their value over time – their cost basis will be "stepped up" to whatever their fair market value is on the date of the donor's death. (Note: In the case of a married donor who dies as the co-owner of a community property asset, the entire asset, not just the donor's half, receives the step-up.) When those assets are distributed to family members or others for whom the donor wishes to provide, all of the capital gain as of the date of death will have been erased.

This leaves any such beneficiary of the donor's estate free to sell the inherited assets promptly upon receiving them while paying little or no capital gains tax. Separately, the donor could provide for charity through a bequest of other assets or even establish a testamentary life-income gift to benefit one or more survivors first before benefitting charity.

The following two examples illustrate why an older donor might not choose to use long-term capital gain assets to establish an *inter vivos* life-income gift as readily as a younger donor might.

Example one: *Oscar is age 90 and his wife Alice is age 78. The differences between them in terms of age and sex make it quite likely she will outlive him, perhaps by many years. On the one hand, he could use a piece of long-term appreciated real estate he owns as separate property to establish a CRUT that would make payments to Alice and to him so long as either of them is living. On the other hand, he might instead simply leave the real estate to her upon death or instruct his personal representative to sell it and*

use the proceeds in some manner that partly benefits her and partly benefits charity. By contrast, if both he and Alice were age 78, the lifetime CRUT option would probably hold more appeal.

Example two: *Louise is age 89 and wants to make a significant charitable gift during her lifetime but also leave substantially all of her estate to her two children, who are in their early sixties. Despite the attractive tax and cash-flow benefits that she would receive if she used long-term capital gain stock to fund a CGA making payments to her for life and that could be drawn upon to finance the purchase of a so-called "wealth replacement" life insurance policy for the ultimate benefit of her children upon her death, at her age she might no longer be insurable. Accordingly, she might hesitate to make a charitable gift that would strike her as more affordable if she were, say, 20 years younger.*

Additional examples could be constructed. Even though the donors in these or other conceivable examples might nevertheless opt for a life income arrangement, they would likely be weighing different considerations than would younger donors owning the same long-term capital gain assets.

A Quick Word about CGAs

Because most charities that issue CGAs offer the rates suggested by the American Council on Gift Annuities, and because those rates are "capped" for older annuitants, such an annuitant who is also the donor could be more inclined to secure lifetime payments through a commercial annuity. This is especially so in the case of a male donor annuitant, as insurance companies pay larger annuities to men of a given age than to women of the same age. Assuming the donor still desired to make a charitable gift, what would have been a CGA could end up being "unbundled," with the donor using some of what would have been contributed for a CGA to purchase a commercial annuity and the balance given to the charity during life or through a bequest or other testamentary arrangement.

Of course, as with a life insurance policy, securing an annuity contract could be a tall order for an older person, as many insurance companies have maximum ages for annuitants of new annuities. This also has implications for a charity issuing a CGA to an older donor if the charity would prefer to "reinsure" a CGA obligation it has undertaken by acquiring a commercial annuity that will serve as the source of the payments to be made.

Conclusion

In numerous respects, age matters. Just as gift planners may need to work with a smaller universe of options in the case of younger donors (e.g., those in their thirties and forties), a shrinking universe is also a reality at the other end of the age spectrum. In general, older individuals remain the best planned giving prospects – so long as they aren't *too* old. As noted at the outset, how old is too old is relative and will depend on the circumstances.