His, Hers, or Theirs – You Need To Find Out!

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There is one important – and often overlooked – question to ask spouses who are funding a charitable gift annuity (CGA) with appreciated securities: "Who owns the securities?" Not knowing the answer to this question can result in a triggering of capital gains taxes never anticipated by the donors - and a donor relations nightmare for the gift officer.

Because of the unlimited federal marital deduction for both lifetime gifts and estate assets passing between spouses, gift officers tend to ignore the tax implications when spouses are funding a charitable gift annuity with appreciated assets.

General Rule - Funding a CGA with Appreciated Securities

Let's assume the funding assets in question are appreciated securities qualifying for long-term capital gains tax treatment (i.e. owned for at least one year). The *general rule* for a charitable gift annuity funded with appreciated securities is that the gain allocated to the charitable portion of the gift is completely forgiven. The gain allocated to the annuity payments is subject to capital gains tax, which is reported through the annuity payments and spread ratably over the life expectancy of the annuitant(s). Fortunately, PG Calc's *Planned Giving Manager (PGM)* and *PGM Anywhere* easily generate these calculations.

Exception to the General Rule – Donor is not the Annuitant

There is an important exception to the *general rule* if the donor is funding the gift annuity for *another* annuitant. In that case, the capital gains allocated to the annuity payments are immediately recognized and capital gains taxes are due from the donor in the year of the gift. In other words, there is no spreading out of the capital gains in the annuity payments and the donor must pay the capital gains tax up front. Ouch!

Spouses Funding a CGA

The rules that apply to non-spouses funding CGAs also apply to spouses. Where appreciated securities are being used to fund the gift annuity, the gift officer must ask the donor-spouses

who has title to the securities, lest an unexpected capital gain tax becomes due from the donor in the year of the gift. A few examples may be helpful.

Spouses jointly own the securities – both spouses are joint and survivor annuitants

When spouses fund a charitable gift annuity with appreciated securities, and the spouses are joint owners *and* joint and survivor annuitants, the realization of capital gains tax is not an issue. The taxable capital gain allocated to the annuity portion of the gift will be taxed through the annuity payments over the joint life expectancy of the spouse-annuitants. No capital gain tax trap here.

Spouses jointly own the securities – only one spouse is the annuitant

Gift officers may have donors where both spouses own the securities jointly, but only one spouse will be named as the annuitant. Sometimes this is done to increase the annuity rate with the hope that the younger annuitant-spouse will survive the older spouse. If spouses ages 80 and 75 fund a gift annuity and are joint annuitants, the annuity rate will be 5.3%. If the 75 year old spouse is the sole annuitant, the rate will be 5.8%. In this situation, one-half of the gain attributed to the annuitant-spouse can be reported ratably over the annuitant-spouse's life expectancy. However, the other one-half of the gain must be reported in the year of the gift by the spouse who is not the annuitant and capital gain taxes will be due. *Solution*: The spouse who will not be the annuitant should transfer their one-half interest in the securities to the annuitant-spouse *prior to the funding of the gift annuity*.

One spouse owns the securities - other spouse is the sole annuitant

Gift officers beware, because the tax ramifications for this gift scenario are most significant. Where one spouse owns the securities, but names the other spouse as the sole annuitant, the donor-spouse will immediately recognize gain in the year the gift is made and taxes will be due. None of the gain recognized can be reported ratably over the annuitant-spouse's life expectancy. *Solution*: Have the donor-spouse transfer the stock into the annuitant-spouse's name *prior to making the gift*. There is an unlimited federal gift tax exemption for lifetime gifts/transfers between spouses, so no gift taxes will be due.

One spouse owns the securities - both spouses are joint and survivor annuitants

Where one spouse owns the securities but will be naming both spouses as joint and survivor annuitants, the taxable capital gain will be reported as follows: (1) the donor-spouse will report one-half of the capital gain in the year of the gift; and (2) the remaining capital gain will be reported through the annuity payments over the life expectancy of the donor-spouse. *Solution*: Have the owning-spouse transfer the securities into joint ownership with the non-owning spouse *prior to making the gift*.

Caveats

Always have the donor in these situations consult their tax advisor *before making the gift*. Donors often do not want to be bothered with transferring stock when they are about to give it away. Should unanticipated taxes be assessed on the donor resulting from the gift, the gift

officer will be relieved to have a letter in her file informing the donor of a potential tax liability and having recommended that the donor consult their advisor.