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Private Foundations—An Alternative to Charitable Giving

For many individuals with accumulated wealth, occasional gifts to a favorite charity may satisfy their charitable inclinations. The added incentive of an often-substantial tax deduction, coupled with various estate planning benefits, can be the driving force behind such charitable gifts. However, for some individuals, philanthropy is a far more serious endeavor, often involving a *succession* of substantial gifts of at least $5 to $10 million, which may necessitate an amount of control and general oversight. In these situations, a **private foundation** can be an ideal venue for managing a large, ongoing charitable giving program.

The Basics

In its simplest form, a private foundation is a charitable, grant-making organization that is privately funded and controlled. When properly arranged and operated, a private foundation can be an entity that is exempt from income taxes and which thereby permits tax deductions for those who donate to the foundation.

Contributions to a private foundation are deductible for gift and estate tax purposes. However, the income tax deduction for gifts to a private foundation is a bit more complex.

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Traditional IRAs—Forgotten, But Not Gone

With the number of financial products available in today's retirement savings marketplace, the traditional **Individual Retirement Account (IRA)** can get easily overlooked, despite the potential for tax deferral and income tax deduction for individuals under the age of 70½. Here are some categories of savers who may benefit from a traditional IRA retirement savings account:

Individuals without a retirement plan. Single taxpayers who are not part of an employer-sponsored retirement plan (e.g., **401(k) plan**) may benefit the most from using a traditional IRA. The same holds true for married taxpayers whereby neither spouse is a participant in an employer-sponsored retirement plan. Each individual can then contribute up to $5,500 in 2018 ($6,500 for individuals who are age 50 and older) annually to an IRA without meeting any income eligibility requirements, and may deduct their entire contribution for income tax purposes.

Some individuals covered under an employer-sponsored plan. Any individual who is a participant in an employer-sponsored retirement plan may contribute up to $5,500 in 2018 ($6,500 if age 50 and older) to an IRA, but whether or not that contribution can be *deducted* for income tax purposes depends on the taxpayer's **adjusted gross income (AGI)**. Deductions in 2018 phase out for single filers with **modified AGIs (MAGIs)** between $63,000 and $73,000, and for married couple joint filers with MAGIs between $101,000 and $121,000.

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Private Foundations—An Alternative to Charitable Giving

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Generally, the deduction is based on the fair market value of the gift (at the time it was given), and it is limited by the donor's **adjusted gross income (AGI)**. The charitable deduction is also limited (to 20%, 30%, or 60% of AGI) by the type of charitable organization that is ultimately receiving the gift from the private foundation *and* the type of gift being made. Gifts that are not cash or publicly traded securities, and that are valued at more than $5,000, need to adhere to specific rules to ensure that they are tax deductible.

In addition to offering the advantages of a tax deduction (which is usually not exclusive to private foundations), private foundations may also offer an array of other benefits. Because a private foundation is typically established to manage a long-term charitable gifting program, it may highlight the philanthropic presence and identity of the donor within the community or associate the donor with a particular charitable cause. It can also serve to create a family charitable legacy while at the same time protecting individual family members from the pressures of other charitable appeals. Finally, a private foundation can serve as an appropriate mechanism for controlling distributions to charities, and it can determine which charities it will benefit.

The Technicalities

When a private foundation is established, two important questions need to be asked. First, what type of private foundation should the donor establish? And second, how should the private foundation be structured? There are generally three types of private foundations: **nonoperating**, **operating**, and **company-sponsored**. Each type of foundation has specific characteristics that make it appropriate for a particular situation. Also, each type of foundation must adhere to a set of strict requirements and guidelines.

The most common type of foundation is the *nonoperating*. Essentially, a donor or group of donors make contributions to the foundation, which in turn makes grants to a charity. In this case, the donor does not participate directly in any charitable work. There are several variations on this type of foundation.

An *operating* foundation may have direct involvement in charitable causes (e.g., an inner-city youth center) while retaining the tax benefits of a "private" foundation (in some respects, operating as a "public" charity does). To qualify as an operating foundation, several requirements need to be met.

A *company-sponsored* foundation is useful when the majority of contributions are from a for-profit corporate donor. Typically, the operation of this type of foundation is similar to that of a nonoperating foundation. It is usually managed by corporate officers, and it has the added benefit of allowing some contributions to accumulate over time. This can help the foundation make continual grants when corporate profits are low.

After careful thought is given to the type of foundation to be established, a decision about structure must be made. A foundation can be structured three ways; it can be a **nonprofit corporation**, a **trust**, or an **unincorporated association**.

A number of factors need to be considered to determine which structure is best. Generally, if the donor intends to keep the foundation in existence permanently, a nonprofit corporation or a trust may be the better choice. But it is important to consider a number of factors, including state and local laws governing private foundations, the type of foundation, the type of donor, the need or desire to make future changes or delegate responsibilities, and personal liability issues.

The Cost

Creating and maintaining a private foundation is much more involved than using more traditional charitable-giving vehicles (e.g., a charitable remainder trust). Therefore, legal and accounting professionals who have experience with private foundations must play a significant role in such an endeavor. And it is important to know that expenses are likely to be substantial because of the complexity of foundations, the need for highly specialized legal and tax expertise, and the costs associated with design, set-up, management, and grant administration. Typically, a private foundation is only viable for individuals who intend to make periodic gifts in excess of $5 million.

Certainly, the private foundation allows today's philanthropist the opportunity to manage substantial charitable gifts and to actually become involved in charitable work if he or she so chooses. It also affords the donor the opportunity to be recognized for charitable giving, while solidifying his or her philanthropic legacy. As with all advanced estate and tax planning, consult with your team of qualified legal, estate, and tax professionals to help ensure that you meet the goals and objectives of all involved parties. $

The Role of Estate Executor

When you write a will, you have the opportunity to appoint an **executor** for your estate. An executor is entrusted first with the responsibility to protect the deceased's property until all debts and taxes have been paid, and then to ensure that the remaining assets are transferred according to the will. This responsibility is both an honor and a burden. While the law does not require that an executor be a legal or financial expert, the job may require honesty, impartiality, and diligence. Executors have a number of duties, the complexity of which depends upon the deceased's financial and personal circumstances.

Specific duties of the executor include the following:

- Determining what the individual owns
- Paying any bills and claims against the estate, including funeral costs
- Paying all estate and inheritance taxes
- Collecting any money due to the estate
- Handling other estate assets, such as insurance or trusts
- Overseeing the investment of assets in the estate
- Distributing assets and property according to the will
- Settling the estate with the probate court, if required

Determining Estate Assets

As a part of his or her duties, the executor first needs to determine what assets are in the estate, such as property, pensions, savings, benefits from employers, and insurance proceeds. To help facilitate this process, a letter of instruction and/or a list of assets may be included with the will. In the absence of such instructions, it is the executor's job to explore all available channels to locate all distributable assets.

Some assets, such as art collections, real estate, and furniture or household goods, may then need to be valued. The executor may hire appraisers to assess the value of such items. Once valued, the executor is responsible for distributing property to the heirs. Property can pass directly or it may be sold, and the proceeds divided among the heirs.

A Few Finer Points

Is it valid? It is the executor's duty to notify all creditors, anyone named in the will, and anyone else who stands to inherit part of the estate. All potential beneficiaries then have a chance to protest if they believe the will is invalid. In most states, a surviving spouse is allowed to challenge a will if he or she is awarded less than a certain percentage of the estate. If there are no protestations, the probate court then issues "letters testamentary," documents that empower the executor to carry out the required duties.

What are the formalities? The executor transfers the decedent's bank accounts into estate accounts, and other assets can be transferred from the decedent's name to the executor's name. A "will construction proceeding" may be required if all parties agree that a will is valid, but disagree upon its meaning.

What about insurance? Insurance benefits are generally paid promptly once an insurance claim form with the original policy and a copy of the death certificate is submitted to the insurer.

What about bills? It is important that all bills are paid before the distribution of any assets begins. The executor needs to keep accurate records of joint property, even if it escapes probate by passing directly to the other owner, because all property, regardless of ownership, affects estate tax bills.

What about liability? The executor generally works with the lawyer for the estate until the estate is settled. Until that time, however, the executor is responsible for keeping the estate in order, protecting assets, and investing the estate's funds prudently. If these responsibilities are not upheld, he or she may be liable to the beneficiaries.

Alternate or Successor Executor

For complicated estates, the probate process may take years. Therefore, you may wish to appoint an alternate or "successor" executor in case the original executor is unable or unwilling to serve. In a family with children from more than one marriage, an individual may choose to designate co-executors. Should administration of the estate become deadlocked among co-executors, it may be necessary to enlist the assistance of a third party advisor, such as a professional accountant.

Make an Informed Choice

Now that you are aware of an executor's duties, you can make an informed choice about an executor for your estate. Choose an individual whom you trust to help ensure that your final wishes are fulfilled and your family benefits from your years of hard work. Once your decision has been made, be sure to work closely with your designated executor, so that he or she can fully understand and appreciate your wishes. $

Understanding Interest Rates and Your Financial Situation

When discussing bank accounts, investments, loans, and mortgages, it is important to understand the concept of interest rates. Interest is the price you pay for the temporary use of someone else's funds; an interest rate is the percentage of a borrowed amount that is attributable to interest. Whether you are a lender, a borrower, or both, carefully consider how interest rates may affect your financial decisions.

The Purpose of Interest

Although borrowing money can help you accomplish a variety of financial goals, the cost of borrowing is interest. When you take out a loan, you receive a lump sum of money up front and are obligated to pay it back over time, generally with interest. Due to the interest charges, you end up owing more than you actually borrowed. The trade-off, however, is that you receive the funds you need to achieve your goal, such as buying a house, obtaining a college education, or starting a business. Given the extra cost of interest, which can add up significantly over time, be sure that any debt you assume is affordable and worth the expense over the long term.

To a lender, interest represents compensation for the service and risk of lending money. In addition to giving up the opportunity to spend the money right away, a lender assumes certain risks. One obvious risk is that the borrower will not pay back the loan in a timely manner, if ever. Inflation creates another risk. Typically, prices tend to rise over time; therefore, goods and services will likely cost more by the time a lender is paid back. In effect, the future spending power of the money borrowed is reduced by inflation because more dollars are needed to purchase the same amount of goods and services. Interest paid on a loan helps to cushion the effects of inflation for the lender.

Supply and Demand

Interest rates often fluctuate, according to the supply and demand of credit, which is the money available to be loaned and borrowed. In general, one person's financial habits, such as carrying a loan or saving money in fixed-interest accounts, will not affect the amount of credit available to borrowers enough to change interest rates. However, an overall trend in consumer banking, investing, and debt can have an effect on interest rates. Businesses, governments, and foreign entities also impact the supply and demand of credit according to their lending and borrowing patterns. An increase in the supply of credit, often associated with a decrease in demand for credit, tends to lower interest rates. Conversely, a decrease in supply of credit, often coupled with an increase in demand for it, tends to raise interest rates.

The Role of the Fed

As a part of the U.S. government's monetary policy, the Federal Reserve Board (the Fed) manipulates interest rates in an effort to control money and credit conditions in the economy. Consequently, lenders and borrowers can look to the Fed for an indication of how interest rates may change in the future.

In order to influence the economy, the Fed buys or sells previously issued government securities, which affects the Federal funds rate. This is the interest rate that institutions charge each other for very short-term loans, as well as the interest rate banks use for commercial lending. For example, when the Fed sells securities, money from banks is used for these transactions; this lowers the amount available for lending, which raises interest rates. By contrast, when the Fed buys government securities, banks are left with more money than is needed for lending; this increase in the supply of credit, in turn, lowers interest rates.

Lower interest rates tend to make it easier for individuals to borrow. Since less money is spent on interest, more funds may be available to spend on other goods and services. Higher interest rates are often an incentive for individuals to save and invest, in order to take advantage of the greater amount of interest to be earned. As a lender or borrower, it is important to understand how changing interest rates may affect your saving or borrowing habits. This knowledge can help with your decision-making as you pursue your financial objectives. $

Tips for Sealing the Deal When Lending Funds to Your Child

Have you ever considered lending money to help your child with a down payment on a new home, to bankroll a business venture, or for some other major expense? Many adult children seek financial assistance from their parents if they encounter difficulty securing a bank loan because they lack a credit history or collateral. Often, parents want to help their children succeed in life and are willing to give them a financial boost. In general, parent-to-child business loans tend to go smoothly. However, if a loan is not paid back as agreed upon by both parties, it could affect family relations. So, here are four points to consider before lending funds to your child:

1) **Document the loan.** If you expect the money to be repaid, consider treating the loan as seriously as a bank would by requiring the proper documentation. You must be able to demonstrate to the Internal Revenue Service (IRS) that you made a *bona fide* loan in order to deduct it as a bad debt. For tax purposes, request the following:
   - A note and *written* loan agreement
   - Collateral or other form of security
   - A repayment schedule and repayment records
   - A plan indicating that the loan will be repaid as scheduled
   - Proof that a business was solvent when the loan was made, if applicable

   Proper documentation may also help you avoid other complications. For instance, if your child were to divorce, a written loan agreement identifying who is responsible for repayment, and on what terms, could prevent a former spouse from refusing responsibility for the debt or claiming that the money was a gift. It could also keep an ex-spouse from obtaining—through the division of marital assets a controlling interest in a company you funded.

2) **Know the rules.** The IRS allows you to deduct bad debts only *after* you have tried to collect them by legal means, if necessary. So if you want to write off the loan, you must be prepared to take legal action to collect it.

   If legal action is appropriate in your situation and you are still unable to collect the loan, you may write it off as a **short-term capital loss** by subtracting the outstanding loan balance from your total short- and long-term capital gain for the year. If the loss exceeds your total capital gain, you may deduct it in $3,000 increments each year until it is entirely written off.

3) **Treat the bad debt as a gift.** Instead of a lawsuit, you may have the option of treating the bad debt as a gift. In 2018, the IRS allows each taxpayer to give up to $15,000 per person per year free of gift and estate taxes. Thus, both parents together could offset an uncollectable debt with a combined gift of up to $30,000 per year with no tax consequences. (Any amount exceeding this limit may be subject to gift and estate taxes.)

4) **Use common sense.** Lending money to a child may have certain tax consequences for you, so it is important to consider the odds of a successful follow-through on your child's part. Think twice before lending money for a risky venture unless you are willing to part with it as a gift with possible tax consequences, if needed.

Helping a child to succeed in life can be an exciting and rewarding experience for a parent. But, be aware of potential tax traps and legal pitfalls *before* opening your checkbook, and remember to seek professional advice beforehand. $

Traditional IRAs—Forgotten, But Not Gone

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Working children. One commonly overlooked savings opportunity is for a working child to start making contributions to his or her own IRA. Many high school- and college-aged students work part-time during the summer, school vacations, and even the school year. In addition to instilling excellent saving habits, contributing to an IRA at an early age can give a child a significant head start in saving for retirement.

Individuals who are retiring or changing jobs. An IRA can allow an individual who is retiring to postpone taxation of his or her retirement plan proceeds. Likewise, an IRA can achieve similar tax benefits for individuals who are changing employers. A special type of traditional IRA—the **rollover IRA**—is used to accept the plan proceeds upon termination of employment. When properly executed, a rollover IRA avoids current income taxation, any unnecessary withholding of taxes by the former employer, and the 10% Federal income tax penalty for early withdrawals. It also allows the IRA owner to actively manage his or her IRA assets.

In addition to rolling over your 401 (k) to an IRA there are other options. Here is a brief look at all your options. For additional information on what is suitable for your particular situation, please consult us.

- Leave money in your former employer's plan, if permitted. The pros: You may like the investments offered in the plan; there may not be a fee for leaving money in the plan; and it is not a taxable event.
- Roll over the assets to your new employer's plan, if one is available and it is permitted. The pros: Keeping all your money together as a larger sum working for you. It is also not a taxable event. The con: Not all employer plans accept rollovers.
- Cash out the account. The cons: This is a taxable event and there is loss of investing potential. It is also costly for young individuals under 59½ and there is a penalty of 10% in addition to income taxes.

Non-spousal beneficiaries of an existing IRA. Since 2010, non-spousal beneficiaries are permitted to directly roll over funds inherited from employer-sponsored retirement plans into inherited IRAs. According to the IRS, retirement plan distributions to a non-spouse beneficiary are subject to many of the same rules that apply to other eligible rollover distributions. Retirement plan sponsors must offer a non-spouse beneficiary the option of making a direct rollover, or a trustee-to-trustee transfer, of eligible rollover distributions to an inherited IRA. This means the transfer is made from the retirement plan to the IRA, and not to the beneficiary. The non-spouse beneficiary may also have the option to leave the money in the qualified plan. Both qualified retirement plans and IRAs typically involve fees, expenses, and services that should be compared when considering a qualified plan rollover.

What about the Roth IRA?

While income taxes are due when IRA distributions are taken, Roth IRA contributions are made with after-tax dollars and earnings accumulate tax free. In contrast to the traditional IRA, Roth IRAs have neither an age limit for contributions nor minimum distribution requirements. However, both traditional and Roth IRAs have a minimum age for distributions: 59½.

Does the Roth IRA eliminate the need for a traditional IRA? Well, that depends on the situation. It is possible for some taxpayers to be eligible for and contribute to both a Roth IRA and a traditional IRA. It is important to note, however, that the IRA contribution limit ($5,500 in 2018 or $6,500 for those age 50 and older) applies to the total of all IRAs that a person may hold in a given tax year.

Is the Traditional IRA an Option for You?

When determining if an IRA is appropriate for *your* situation, you need to evaluate the following: 1) whether you are eligible to make a deductible contribution; 2) if comparable savings opportunities exist elsewhere (e.g., your employer-sponsored 401(k) plan); and 3) the current and long-term tax benefits.

Traditional IRAs may have been overlooked as viable retirement savings vehicles in recent years, but may still serve a valuable purpose for your unique financial situation. Be sure to consult a qualified financial professional to help you determine your retirement savings opportunities, and formulate your savings strategy for the future. $

Getting More Miles from a Tank of Gas

With an unpredictable economy and concerns about global warming, conserving gas has become a national priority. While trading in your car or truck for a more fuel-efficient compact or hybrid may not be an immediate option, there are strategies that can help you minimize gas consumption while continuing to drive your current vehicle.

A number of factors can affect fuel economy, including driver behavior, driving conditions, vehicle maintenance, fuel characteristics, and weather. While some of these are out of your control, the following steps may help you get more miles to the gallon:

Monitor tire pressure. Under-inflated tires create rolling resistance and lower fuel efficiency. By keeping tires inflated at the recommended pressure, you can improve your gas mileage. Proper inflation also lessens wear on tires and reduces the risk of accidents due to tire failures or blowouts.

Get regular tune-ups. Because malfunctions cause the engine to work harder, cars that aren't regularly maintained tend to burn more gas. Problems such as clogged air and fuel filters, faulty oxygen sensors, or worn and dirty spark plugs can lead to a dramatic drop in fuel efficiency. Getting a tune-up at intervals recommended by the manufacturer can save on gas and protect the engine from damage.

Monitor brakes and wheel alignment. Improper wheel alignment and the drag of poorly adjusted brakes can lower gas mileage. A simple inspection can reveal whether an adjustment or realignment is needed.

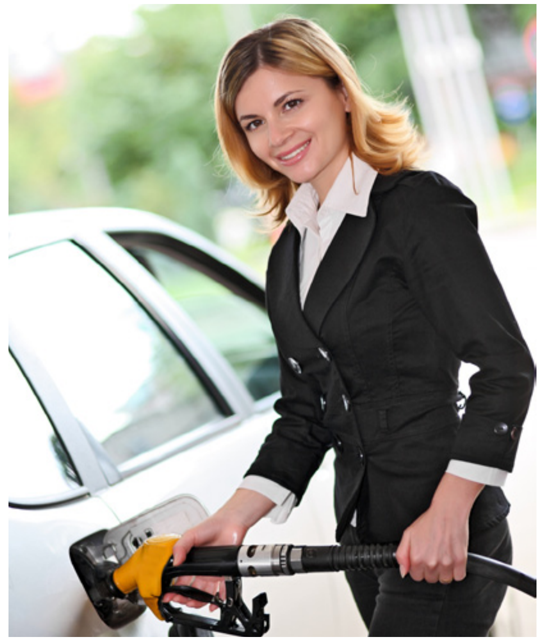
Park in the shade. Because gas evaporates in the heat, parking your car in the shade during the summer can conserve fuel.

Avoid idling for more than a minute. Turn off your car if you plan to stop for more than a minute, as idling for longer periods uses more fuel than turning off and restarting the engine. Avoid warming up your car, as it is unnecessary with today's engines.

Eliminate excess weight. Take the junk out of your trunk. It's easy to store extra items in the car, but excess weight has a negative effect on fuel efficiency.

Slow down. In most cars, fuel efficiency falls sharply when driven at speeds above 60 mph. Be sure to observe the posted speed limit and drive safely.

Curb aggressive driving. Acceleration, rather than sustained cruising, accounts for the greater amount of fuel burned in city driving. Accelerating smoothly from a standstill consumes much less gas than a sudden start.



Use of cruise control on the highway can also improve mileage.

Find ways to drive less. To avoid long waits in traffic, telecommute for at least part of the week or schedule your commute for off-peak hours, if possible. Look for opportunities to carpool with neighbors and co-workers, or check out rideshare programs in your community. Take advantage of public transit, if it is available in your area. Avoid making frequent trips to the mall by shopping online, or try walking or cycling to nearby destinations.

Combine trips. Making several trips from a cold start generally uses more gas than making a longer trip during which the engine remains warm. By planning your route in advance and finding ways to combine errands, you may also be able to reduce the amount of time you spend driving.

Monitor your gas consumption. Track your car's gas mileage by maintaining a log of the odometer reading and the number of gallons pumped each time you fill up. Besides alerting you to possible engine trouble when mileage changes drastically, a fuel economy log can help make you more aware of your gas consumption.

With proper vehicle maintenance and good driving habits, you can get better fuel economy and spend less at the pump. For more tips and further information, visit the website of the U.S. Department of Energy's Office of Energy Efficiency and Renewable Energy at www.fueleconomy.gov. $

Planning Your Estate Before Remarriage

Despite the best intentions, marriages may not last forever. If you are divorced or widowed, and planning to remarry, you may want to take the opportunity to review and revise your estate conservation strategies. This is especially important if you and your future spouse have children from previous marriages.

Consider the following points:

1) Regardless of the details of your situation, it is important to be aware of the potentially sensitive aspects of estate planning. When multiple families are involved, objective professional counsel may help you achieve your desired results.

2) Familiarize yourself with the advantages and disadvantages of different types of asset ownership. If you would like your assets to pass entirely to your children, you may want to put them in your own name. It is important to know that new assets acquired in **joint tenancy** with your spouse will automatically be passed on to the surviving spouse.

3) Consider a pre-marital agreement to legally detail your property arrangements. While you may feel ambivalent about broaching this subject, a formalized agreement can help facilitate your wishes.

4) Review your **will** and update the beneficiary arrangements of your **life insurance policy** to ensure that your property is distributed according to your wishes upon your death.

As you prepare for and experience a major life change, such as remarriage, be sure to consult with an estate planning team comprised of qualified tax, legal, and financial professionals to help ensure that you meet your overall objectives. $