The Tax Discount on Educational Gifts Booklet, n.d.

3.16

the xtra

TAX DISCOUNT

on

Educational Gifts

14 tax-saving methods of giving

WILKES COLLEGE

Wilkes-Barre, Pennsylvania

the

TAX DISCOUNT

on

Educational

Gifts

© 1959 Kennedy Sinclaire, Inc.

CONTENTS

page

EDUCATIONAL GIFTS REDUCE YOUR TAXES 5

JUST WHAT DOES THE TAX LAW SAY?

Federal income tax 7
Federal estate tax 9
Federal gift tax 9

14 WAYS TO GIVE TO A COLLEGE OR UNIVERSITY:

—Gifts by Will—

1. Outright bequest (by unmarried person) 10
2. A "delayed" bequest (by unmarried person) 11
3. Husband's estate in trust for wife and college 13
4. Family business preserved by educational bequest . . 15

—Gifts During Life—

5. Outright gift of cash 17
6. Gift of securities 18
7. Gift of life insurance 20
8. Trust for self and university 21
9. Trust for self, wife, and educational institution 23
10. Life income acquired from educational institution . . 24
11. Estate "poured into" trust for family and college . . . 25
12. Trust for 5 years for education, then for wife 26
13. Business owner gives preferred stock to a college . . . 27
14. Art objects deeded to university but kept for life . . . 29

WHERE TO GET INFORMATION AND ASSISTANCE ON EDUCATIONAL GIFTS 30

Tables:

"The Estate Tax Discount on Bequests for Education" . . . 16
"Values of Life Estates and Remainders" 22

Educational Gifts Reduce Your Taxes

People who make gifts for education are generously rewarded by our tax laws. The rewards are in the form of special tax deductions and exemptions . . . which, of course, lower the taxes that otherwise would have to be paid by these people or their estates.

Certainly the tax rewards, alone, cannot move anyone to give to a college or university. They are not the starting point of a gift. One does not, first, decide he must do something to lower his taxes and then, upon looking around, hit upon a gift for education as a way to obtain the relief.

The aim to help an educational institution, or to help young people further their education, comes first. It is only when this aim exists that the favorable tax treatment becomes interesting. "Perhaps I can do more for the college than I thought," reflects the person who is considering a gift. "Taxes will make my gift all the larger."

Make the gift larger? Yes, in a way that is so. It's much as though Uncle Sam* matches, to some extent, every gift by an individual. If, for example, you give $1,000 to a college and your top rate of income tax is about 40%, you will get back about $400 as a reduction in your income tax. The college receives $1,000. *But only $600 of this really comes from you. The other $400 comes from the Government.*

So, it may seem to you, there is not a "reward" but a "discount." You may find you can "buy" $1,000 of benefits for an educational institution at a cost of only $700, $600, $500, or even less.

The "discount rate" to which you are entitled is the highest rate at

*Only *Federal* taxes are discussed in this booklet. State income and inheritance taxes usually increase the "reward" or "discount."

which you pay income taxes; or it may be, if you are considering an educational bequest in your will, the highest rate at which your estate will pay estate tax. In some cases it's quite possible for a gift to result in income tax AND estate tax advantages, so that a college or university can be benefited at surprisingly little cost indeed.

Whether you look on the tax effect as a reward or as a discount, you will wish to give some thought to the best *way* to make a gift. This booklet, briefly outlining the tax treatment of various methods of giving to a college or university, will be helpful to you in making a choice.

Just What Does the Tax Law Say?

First, Let's Consider the

FEDERAL INCOME TAX

"There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year."

This opening sentence of section 170 of the Internal Revenue Code is the main authority for the deduction you can take on your U. S. income tax return for contributions for education.

"It speaks of *charitable* contributions," it may be objected. "What about *educational* contributions?"

There is nothing to worry about. In that mysterious subsection (c) that's referred to you will find that a "charitable contribution" is defined to include a gift to (or for the use of)—

"A corporation, trust, or community trust, fund, or foundation—

(A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State or Territory, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, *or educational* purposes . . . ;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation."

Also considered a charitable contribution is a gift to or for the use of a State or city "for exclusively public purposes."

But it is dangerous to read tax laws quickly and incompletely. Although that opening sentence of section 170 says you can deduct "any" contribution of the type spelled out, there is an ominous caption a little further along reading "LIMITATIONS."* Under that caption you find that an individual generally can deduct, as "charitable" contributions in any year, no more than—

20% of his adjusted gross income,
plus another
10% of his adjusted gross income in some cases.

The extra 10% is a special allowance for contributions *to* (not merely for the use of) educational organizations, hospitals, and churches. This is a bit complicated, but for most practical purposes it simply means that gifts to colleges and universities can be deducted in full up to 30% of adjusted gross income.

Some examples: **Assume a man's adjusted gross income is $10,000.**

If he contributes $3,000 to a college and nothing to any other "charity" he can deduct the full $3,000.

If he contributes $3,000 to a university and $1,000 to another "charity" he can deduct only $3,000 in all.

If he contributes $1,000 to a college and $3,000 to another "charity" (not a school, hospital, or church), he can deduct $3,000 in all.

But if he contributes $500 to a university and $3,000 to another "charity" (not a school, hospital, or church), he can deduct only $2,500 in all.

What is "adjusted gross income"? It is gross income—all your taxable income—less business and certain employment-connected expenses, and less also any deduction for a net capital loss up to $1,000. For many persons, adjusted gross income is very close to gross income.

Warning: You can't take a deduction for contributions of any kind if you use the "standard" deduction. The "standard" deduction is supposed to take the place of deductions for contributions, medical expenses, interest and taxes paid, and so forth.

*There's no limitation on your deduction if your contributions plus income tax payments amount to over 90% of taxable income, and if this has gone on for a number of years. Understandably, very few people qualify for the unlimited-deductions privilege.

Now for the

FEDERAL ESTATE TAX

When a person dies his estate must pay a Federal estate tax if the total value of his assets and certain other property subject to tax exceeds the allowable exemptions and deductions.

One of the deductions is "the amount of all bequests, legacies, devises, or transfers . . . —

"to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, *or educational* purposes, including the encouragement of art . . . no part of the net earnings of which inures to the benefit of any private stockholder or individual . . .

"to a trustee or trustees . . . but only if such contributions or gifts are to be used by such trustee or trustees . . . exclusively for religious, charitable, scientific, literary, *or educational* purposes . . ."

This is from section 2055 of the Internal Revenue Code. As under the income tax provision, a deduction is allowed also for gifts to States or cities "for exclusively public purposes."

But the estate tax provision is shorter and simpler than the income tax provision. *It does not impose any limitations on the amount of the deduction.*

A person could leave his entire estate to a college or university (if State law permits him to do this) and thereby completely eliminate the Federal tax.

The FEDERAL GIFT TAX

The Federal gift tax does not, as a practical matter, apply to gifts to colleges and universities. Such gifts are to be reported by the donor, if they exceed certain amounts. But they are fully deductible in arriving at net, or "taxable," gifts, so they do not result in tax. Section 2522 of the Internal Revenue Code allows the deduction.

14 Ways to Give to a College or University

Anyone who is concerned with taxation today is likely to divide educational gifts into these two classes:

(1) Gifts by will (2) Gifts during life

Class No. 1 gifts—those made by will—save estate tax.

Class No. 2 gifts—made during life—save income tax, *and usually save estate tax too.*

Thus it is apparent that, from a tax standpoint, a gift during life is likely to be more advantageous than a gift by will. The gift during life leaves the donor and his family with larger tax savings; or—another way of looking at it—the gift during life permits the educational benefit to be "purchased" at a greater "discount," so that perhaps a larger benefit can be provided with the same amount of money.

Even so, the tax treatment of an educational gift by will is quite favorable. Many such gifts occur, and four of them are analyzed below. Names, of course, are fictitious.

GIFTS BY WILL

PLAN 1:	OUTRIGHT BEQUEST (BY UNMARRIED PERSON)

Example: **In his will Mr. Bell, a widower, leaves $20,000 to a college. The rest of his estate goes to his children.**

The Tax Results: Assume that Mr. Bell's total estate is $200,000. The $20,000 gift, therefore, is one-tenth of the total. Would you suppose that the gift to the college reduces the tax on his estate by one-tenth?

The fact is that tax is reduced by almost *one-fifth.* Without the deduction for the educational gift, the Federal tax on his estate would be $32,700. With the $20,000 deduction, it is $26,700.

The $20,000 gift saves $6,000 tax, so the real "cost" of the gift is only $14,000.

The tax we are speaking of is the Federal estate tax before reduction by the credit for State inheritance or estate taxes.

And note this, in connection with Mr. Bell's $200,000 estate:

If the gift had been—	The tax saved would have been—	Leaving, as the "cost" of the gift,—
$40,000	$12,000	$28,000
60,000	17,600	42,400
80,000	23,200	56,800

The above figures are for a $200,000 estate of an unmarried person. On larger estates the tax rates—therefore the tax savings—are higher.

"But why," it may be asked, "is the tax saving disproportionate to the gift? When one-tenth of the estate goes for education, why isn't the tax reduced by one-tenth, instead of by almost one-fifth?"

The reason is that the gift, like any other deduction, comes "off the top" of the estate, where the rates are highest. The Federal estate tax rates (and the income tax rates too) are "progressive"; they rise as the size of the estate increases. If, by means of an educational gift, you can reduce your taxable estate by 10% or any other percentage, you are likely to reduce the tax by a much greater percentage, for you are removing from your estate *the highest taxed property.*

PLAN 2:	A "DELAYED" BEQUEST (BY UNMARRIED PERSON)

Example: **Mrs. Dell, a widow, leaves her entire estate in trust, with income payable to her invalid brother for life. When he dies the trust is to end and the principal is to go to a university.**

The Tax Results: Again let's assume the estate is $200,000. The brother, at the time Mrs. Dell dies, is 75 years old.

Every dollar that goes into this trust is considered, for estate tax purposes, to be partly a gift or bequest to the brother and partly a gift to the university. The brother is entitled to the income from that dollar for the rest of his life; the university is entitled to the dollar itself—but only in the future, when the brother dies.

The "present value" of each of these two rights—the brother's and the university's—is easily found from a table that is part of the Federal estate tax Regulations. It is shown, in part, in this booklet at page 22.

You will see from the table that the university's right to receive $1 at the death of the brother, now aged 75, is about 78¢. Inasmuch as 200,000 dollars go into the trust, the value—at the time Mrs. Dell dies—of the bequest to the university is 200,000 x 78¢, or $156,000.

$156,000, then, is the estate tax deduction her executors can claim for the educational gift. That brings her $200,000 estate down to $44,000. The $44,000 is less than the $60,000 exemption that the estate of every U. S. resident or citizen is entitled to, *so there's no Federal tax whatever to be paid by Mrs. Dell's estate.*

Suppose Mrs. Dell, in her will, authorized the trustee to pay some of the principal, in addition to the income, to the brother in certain circumstances. That *might* jeopardize the tax deduction; it might make the value of the gift to the university "unascertainable," as the courts say. It's a matter to be discussed with one's lawyer, for the rules in the situation are complex.

Another complication—more bothersome than costly—can arise if the educational gift is not enough to wipe out the tax entirely. Suppose Mrs. Dell's brother were only 50 when she died. In that case you might think the gift to the university would be 200,000 x 48¢, or $96,000. (The table shows a remainder interest in $1 after the death of a person now aged 50 to be about 48¢.) But that isn't quite right, for the university

would not receive the full $200,000 when the brother died. Mrs. Dell's estate would pay *some* tax, and that tax would reduce the $200,000 principal of the trust. So the executor of the estate has an arithmetic problem: "X" is the tax, and the deduction is $.48(200{,}000 - X)$. An equation can then be written down and worked out to find out exactly what "X," the tax, is.

But at the initial planning stage most persons are not interested in knowing the exact figures. The tax deduction and the tax can be approximated.

PLAN 3: HUSBAND'S ESTATE IN TRUST FOR WIFE AND COLLEGE

Example: **Mr. Fell leaves his entire estate in trust for Mrs. Fell. But he does so by means of two trusts, each for about one-half his estate. When Mrs. Fell dies the principal of one of the trusts will go as directed in her will. The principal of the other will go to a college.**

The Tax Results: This arrangement would be practical for small, as well as large, estates; but to emphasize the favorable tax treatment let's assume that Mr. Fell's property is worth $400,000 when he dies. Mrs. Fell has relatively little property in her own name.

As for the tax results, they can be quickly stated: there will be no Federal tax whatever on Mr. Fell's estate.

Moreover, there probably will be none on Mrs. Fell's estate either, when she dies.

How is it possible for a $400,000 estate to escape tax completely . . . not once, but twice?

The explanation: One half of Mr. Fell's estate qualifies for the estate tax "marital deduction." This half is the property that goes into the



trust over which Mrs. Fell has a general "power of appointment"—the right to say who shall receive the principal when she dies.

The other one-half of Mr. Fell's estate doesn't qualify for the marital deduction but much of it (about three-quarters, if Mrs. Fell is 72 years of age when her husband dies) qualifies for a charitable or educational deduction.

Thus, his estate's deductions are:

Marital deduction	$200,000
Charitable deduction	150,000
	$350,000

These, deducted from the $400,000 estate, leave $50,000. That is less than the $60,000 exemption, so there is no Federal tax on Mr. Fell's estate.

When Mrs. Fell dies later she has a gross estate, for Federal tax purposes, of $200,000 (the assets of the trust over which she has the power of appointment). But she decides to exercise this power by having the $200,000 go to the same college (and into the same memorial fund, we'll say) which receives the principal of the other trust under her husband's will. So her estate has a $200,000 deduction on this account, leaving no Federal tax to be paid.

Mr. Fell, when this plan was explained to him, said: "I'm amazed that we can do so much for the college—*and at the same time make even MORE funds available to my wife.*"

Without the educational gift in his will, he would have left for Mrs. Fell $400,000 less the tax on his estate. But with the tax eliminated there was a full $400,000 of capital available to her. (For simplicity, estate-settlement costs other than taxes are ignored.)

Moreover, the whole $400,000 of capital was NOT "tied up," though it was held in trust. Mrs. Fell had the right to withdraw principal from one of the two trusts, the "marital deduction" trust. She would never lack funds, whatever the financial emergency.

PLAN 4: FAMILY BUSINESS PRESERVED BY EDUCATIONAL BEQUEST

Example: Mr. Kell owned all the stock—common and preferred—of a small but prosperous company. He leaves some of this stock (the preferred) in trust, with income payable to Mrs. Kell for life. When she dies the trust is to continue, as the Kell Foundation, in perpetuity for the benefit of a university. The rest of his estate (including the common stock of his company) he leaves to his wife; she, in turn, plans to leave her estate to the children.

The Tax Results: Assume that Mr. Kell's estate, in all, is $1,000,000. Mrs. Kell is 65 when her husband dies.

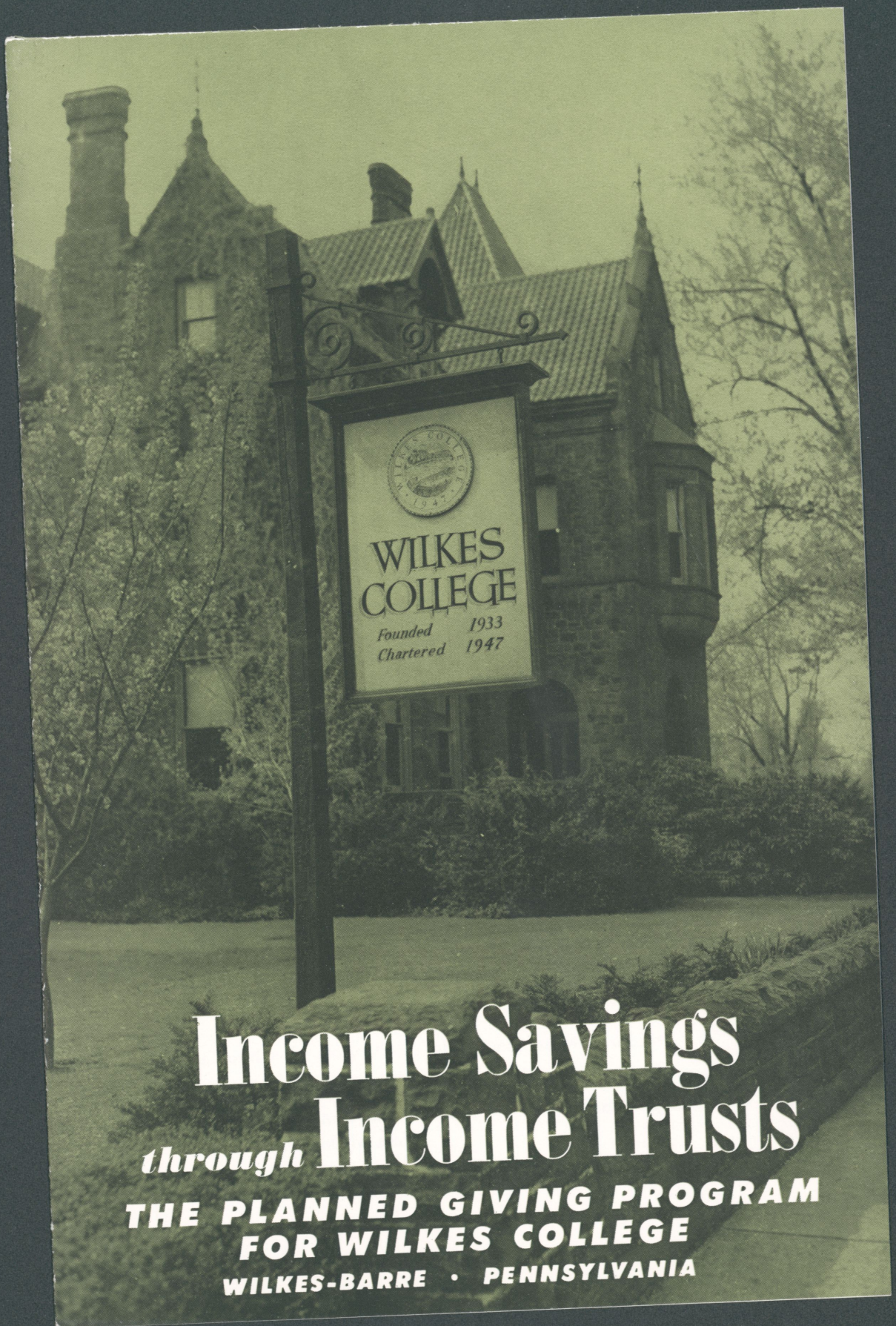
Thanks to a *charitable* deduction (amounting to about two-thirds of the value of the property left in trust for Mrs. Kell and the university) and to the *marital* deduction (amounting to the value, up to half the estate, of the property passing to Mrs. Kell), Mr. Kell's estate pays relatively little Federal estate tax. It probably will be less than $25,000.

This—the drastic reduction of the estate tax—was one of the key objectives of Mr. Kell's plan. The bulk of his estate was represented by the family company. If the estate should have to pay a huge estate tax, along with State taxes and estate-settlement costs, where would the executors obtain the cash?

Perhaps cash could be obtained from the company itself. But this is not always a practical solution to the problem. The *company* may have little cash to spare. If it comes to the aid of the estate—by redeeming some of the estate's stock, for example—there may remain inadequate cash to carry on business. The impairment of current assets, coinciding with the loss of the business owner's skills, contacts, and services, might be disastrous.

Perhaps the executor could pay the Federal tax, insofar as it was attributable to the business interest, in ten annual installments. A relief provision added to the estate tax law in 1958 permits this, under certain conditions. Yet the tax must eventually be paid (plus interest on the extended payments), so the estate-liquidity problem is not necessarily solved; it is merely put off.

One of the best solutions to the liquidity problem in a business owner's estate is, simply, the reduction of the probable *need* for cash. Mr. Kell accomplished such a reduction by his bequest to the university . . . and he fulfilled, at the same time, a desire to set in motion an everlasting benefit for education.



Income Savings through Income Trusts

THE PLANNED GIVING PROGRAM FOR WILKES COLLEGE

WILKES-BARRE • PENNSYLVANIA

© 1960 KENNEDY SINCLAIRE, INC.
(3)

A "Gift" to Self, Wife, and Education

. . . how it saved $23,000 tax

Long ago Max R_____, a young immigrant, entered a college in New York City. He had very little money. So he dropped out after a brief period, got into the business of manufacturing neckties, and eventually made a fortune. When he died a few years ago he left more than a million dollars to be divided among a number of educational institutions.

We *read* about spectacular gifts like this.

But what of the thousands and thousands of ordinary, "close-to-home" situations in which needed support is given to schools, colleges, and universities?

"Give us a case involving an average person of moderate means," someone may say. "How can he gain the satisfaction of making a substantial gift for education? To what extent would his gift reduce his taxes?"

Gift by Will Would Reduce Tax by $10,000

Consider the story of Mr. John Donor, as we'll call him.

Is he "average"? That is a question that would be hard to answer, but certainly in an economic sense Mr. Donor is neither at the top nor the bottom of the scale.

He is 60 years of age. He has a wife and two children. His total "estate"—including his life insurance and the property that he and his wife owned together—might total $300,000.

Some months ago Mr. Donor spoke to his lawyer about his will.

He already had a will, leaving all his estate in trust for his wife and children. It was a good, up-to-date will taking full advantage of the Federal estate tax "marital deduction" and other relief provisions of the tax law.

But Mr. Donor wished to make a change. He wanted $50,000 to go to a certain educational institution when his wife died (or when he died, if he survived her).

"It will be a memorial to my wife," he said to his lawyer, "– and with taxes considered, it's an attractive idea. You see, I've figured that the $50,000 gift for education will reduce the Federal tax on my estate by approximately $10,000. That brings the 'cost' of the gift down to $40,000.

"It's like buying for $40,000 something that's worth $50,000."

Would you like to go into the arithmetic of Mr. Donor's $10,000 saving?

First, find the Federal tax on Mr. Donor's estate if he does NOT leave the $50,000 for education . . .	$17,900
Then find the tax on the same estate but with an additional deduction – for the "present value" of $50,000 to be paid to an educational institution at the wife's death. Assume she is 70 when the husband dies. In that case the tax deduction allowed for the $50,000 gift will be $36,315, and the Federal tax on the husband's estate will be	$ 7,921
Tax saved	$ 9,979

How to Save $13,000 MORE Tax

But Mr. Donor's lawyer suggested an even better plan.

It was a plan that would save $13,000 MORE tax. The "cost" of the $50,000 gift would be reduced to ABOUT $27,000!

"Beginning now," said the lawyer, "put $10,000 a year of your own property in a trust for yourself and your wife.

"Do this for five years, until you have put $50,000 into the trust.

"The *income* from this trust *will be paid to you while you live, then will go to your wife as long as she lives.*

"When the survivor dies, the trust ends and the principal goes to the educational institution.

"You and your wife are both 60 at the present time. Here are the Federal *income* tax results:

Year	*Deposited in the trust*	*Tax deduction for the "contribution" for education*	*Tax saved*
1st	$10,000	$5,038	$2,519
2nd	10,000	5,171	2,586
3rd	10,000	5,306	2,653
4th	10,000	5,441	2,721
5th	10,000	5,579	2,790
Total Federal income tax saved			$13,269

"That's assuming you pay tax at 50% on your top-bracket income," the lawyer continued. "Actually, you're paying somewhat more, and probably will continue to do so for the next five years."

Technical matters: If you put money or property in an irrevocable trust, you're generally considered to make gifts—

(1) to the persons who will receive the income, and

(2) to the "remainderman"—the person or organization that will receive the principal when the trust ends.

The "remainderman" of Mr. Donor's trust, of course, is the educational institution. For Federal income tax purposes, then, it's much as though Mr. Donor makes a gift, or "contribution," for education whenever he puts money or property in the trust.

The *amount* of the contribution is not the full amount deposited in the trust. It's only the portion considered to be the gift to the "remainderman." This portion—it depends on the ages of the income beneficiaries—can be readily computed from tables issued by the Internal Revenue Service.

A Closer Look at a Tax-Saving Gift for Education

Mr. Donor was interested in the trust arrangement. He had these questions:

Will the trust save estate tax too?

"Yes," the lawyer said, "it will save the full $10,000, just as if you made the $50,000 gift by will. This is so, at least, if you spend the $13,000 income tax that you save; if you save the saving, the estate tax results get a little complicated."

Must I agree to put in $10,000 every year?

"Oh, no. You may add to the trust when and if you wish. I've assumed the $10,000 addition each year for five years just to make a comparison of tax results. You're not bound to make *any* deposits."

May I deposit securities worth $10,000, instead of $10,000 cash?

"Yes, indeed. And that brings up an interesting point. Suppose you have some shares of stock that are now worth $10,000 but which cost you only $2,000. If you were to sell that stock now you would have to pay a tax on the gain, of course. But if you put the stock in the trust, and the *trustee* sells it, then neither you nor the trust is taxed for the gain. The gain, you see, is 'permanently set aside', as the tax law says, for education, so it isn't taxed."

Must the trust be irrevocable?

"Yes. The favorable tax results we have been discussing depend on that. Once you put money or property in, you can't get it back. All you and Mrs. Donor can have is the income. For that reason it probably would be advisable for you to proceed with this plan gradually, depositing only $10,000 or so a year, and to give careful thought to the whole arrangement at the very start."

But I've heard about a Federal gift tax on irrevocable trusts.

"In your particular situation," said the lawyer, "don't be concerned about the gift tax. It's true that you would be making gifts to your wife, and you would have to file gift tax returns.

But you would have no tax to pay. If you deposited $10,000 a year for five years the gifts to her would be only a little over $1,000 for each of the five years. Your $30,000 lifetime exemption, which is still intact, more than covers this."

Other Advantages of the Trust

Mr. Donor learned also that the income from the trust, if the trustee should invest the fund in tax-exempt securities, would be free of income tax to him and Mrs. Donor. "It's a rule that has long applied to all trusts—whether they are for educational purposes or not," said the lawyer. "The character of the income doesn't change when the trust pays it to you; if it's tax-exempt when collected by the trust, it's tax-exempt when paid to the beneficiary."

Moreover, the trust offered a measure of lifelong protection to Mrs. Donor. She would be assured of a small but steady income for as long as she lived. And this income would become payable to her without delay when her husband died; it would not be held up until his estate was settled.

"With all these favorable aspects," said the lawyer, "you have the wonderful tax savings. Your $50,000 gift will save about—

$10,000 in estate tax, and

$13,000 in income tax.

You give $50,000 for education . . . but it costs only $27,000 to do it."

In our booklet, "The Tax Discount on Educational Gifts," there are more illustrations of how people have increased the usefulness of their property to themselves and their families—and, at the same time, have given great assistance to educational institutions.

If you would like to have a copy of this interesting and up-to-date booklet—"The Tax Discount on Educational Gifts"—just fill in and send back to us the enclosed postpaid card. You will be under no obligation whatever.

Inherent in the material progress of our century are the paradoxical promises of greater well-being and the threat of extermination. To survive man must resolve this paradox, and it is only in the mind and heart that the answers can be found.

The highest intelligence is required if we are to realize the possibilities of a finer life and are to maintain stability and equilibrium in the midst of change. Only by a trained and disciplined intelligence can we hope to resolve the innumerable economic, social, and political problems arising from the advance of science and technology and from the growing expectations of all people.

To reduce the great cultural gap of this century and to assure the growth of freedom, a bridge of understanding must be built, and this bridge must be based upon respect for the individual.

From the Annual Report of
the President of Wilkes College

THE ESTATE TAX DISCOUNT ON BEQUESTS FOR EDUCATION

If your "taxable estate," before deducting educational bequests and the $60,000 exemption, is—	And if you bequeath for education—	THE ACTUAL "COST" of your bequest (with Federal estate tax* taken into consideration) is—
$ 100,000	$ 10,000	$ 8,200
120,000	12,000	9,060
140,000	14,000	10,080
160,000	16,000	11,520
180,000	18,000	12,600
200,000	20,000	14,000
240,000	24,000	16,800
300,000	30,000	21,000
400,000	40,000	27,200
500,000	50,000	34,000
600,000	60,000	39,600
700,000	70,000	45,500
800,000	80,000	52,000
900,000	90,000	56,700
1,000,000	100,000	63,000
1,500,000	150,000	87,000
2,000,000	200,000	110,000
2,500,000	250,000	127,500
5,000,000	500,000	185,000
10,000,000	1,000,000	240,000

*The Federal estate tax before reduction by the credit for State inheritance or estate taxes.

GIFTS DURING LIFE

Writes a lawyer in a treatise on estate planning:

"A newspaper item concerning a huge bequest to charity almost always causes the blanching of a tax lawyer's hair, because of the enormous waste of lifetime tax dollars."

There indeed can be, as pointed out earlier, a waste of tax dollars when an educational gift is made by will. The donor does not obtain his full "reward" for making the gift.

The waste can usually be averted by making the gift during life, instead of by will. The lifetime gift may result in an *income tax* deduction as well as an estate tax advantage. Here are examples:

PLAN 5: **OUTRIGHT GIFT OF CASH**

Example: **Mr. Ball sends a check for $1,000 to a college. It is an outright gift, to be merged with the general funds of the college.**

The Tax Results: Mr. Ball can deduct the $1,000 on his Federal income tax return as a contribution, provided his total contributions are within the usual percentage-of-income limits (see page 8). The gift may reduce his tax for the year by several hundreds of dollars, the exact amount depending on the highest rate at which his income is taxed.

In addition, Mr. Ball reduces his estate subject to estate tax. The true amount of the reduction is the $1,000 gift minus the income tax benefit he obtains. For example, if his top rate of income tax is 53% and his income tax is reduced by $530, then his "estate" is reduced by $470.

A few questions that might arise over a simple gift like this:

What if Mr. Ball merely pledged the $1,000?

The gift would not be deductible until the year of actual payment. Mere pledges are not considered to be completed gifts.

Suppose Mr. Ball mailed the check on the last day of the year.

Probably it would be deductible in the year mailed, if mailed directly to the college. The income tax Regulations say: "In the case of a check, the unconditional delivery (or mailing) of a check which subsequently clears in due course will constitute an effective contribution on the date of delivery (or mailing)." But why wait until the last minute and raise a question?

Is it all right for Mr. Ball to give the money through an alumni association?

The income tax Regulations say: "A gift to an educational institution through an alumni association or a class organization, which acts simply as a fund-raising or collection agency through which gifts may be made currently to the institution, is a gift to the educational organization if the entire gift inures to its benefit, but not if any part of it inures to the general or operating fund of the agency.

PLAN 6: GIFT OF SECURITIES

***Example:* Mr. Call owns shares of stock that are now worth $10,000 but which cost him, many years ago, only $2,000. He gives the stock to a college or university.**

The Tax Results: Mr. Call's contribution is $10,000. He can deduct this on his Federal income tax return for the year in which he makes the gift (within the percentage-of-income limits).

He does NOT report any gain upon making the gift.

As for the Federal estate tax, Mr. Call reduces his estate by $10,000 minus the income tax he saves by means of the deduction.

He pays no Federal gift tax.

Here is one of the most advantageous ways to give for education. If Mr. Call had *sold* the stock, instead of giving it to the college, he would have had a gain of $8,000 and his capital gains tax could have been as much as $2,000. But he has no such tax to pay if he gives the stock to the college.

"What about the college?" it may be asked. "Doesn't it have to pay a big tax if it ever sells the stock?"

No, the college is exempt from paying Federal income tax. It is not interested in what the "cost basis" is of any property it receives.

Carefully notice that Mr. Call gave stock that had gone *up* in value since he acquired it.

If he held stock that had gone *down,* it would be better for him to sell the stock, take the loss (which he could deduct on his income tax return), and give the college the proceeds of sale.

PLAN 7: GIFT OF LIFE INSURANCE

Example: Mr. Dall—when his children were grown and after he and his wife had accumulated a good deal of property—decided he was carrying more life insurance than he now needed. He was about to surrender one of his policies for cancellation. Instead, he gave the policy to a college and continued paying the premiums.

The Tax Results: Mr. Dall can, within the usual percentage-of-income limits, deduct on his Federal income tax return the value of the policy. This would be the cash surrender value, with possibly a small adjustment on account of the advance premium last paid.

Mr. Dall will also be entitled to deduct all premiums as he pays them in the future.

The proceeds of the policy, when Mr. Dall dies, will not be part of his estate for Federal estate tax purposes.

When Mr. Dall gave the policy to the college he irrevocably assigned it, keeping no rights in it whatever. As for future premium payments, Mr. Dall intended to pay them; but he was not legally obligated to do so, and could stop at any time.

A possible variation of Mr. Dall's plan would be an irrevocable designation of the college as beneficiary of the policy, instead of an absolute assignment. It has been suggested that such an arrangement might offer certain estate tax advantages, especially if the insured is a married person. It's a matter to be discussed with one's tax adviser.

If Mr. Dall had a large amount of insurance and wished to establish a long-lasting fund or foundation for a particular educational use at the college, he might have been inclined to assign the policies to an irrevocable insurance trust, with a bank or trust company as trustee. In the insurance trust agreement he could have specified the exact purposes and uses of the income and principal of the trust. The tax results, if the trust was wholly for educational purposes, would be the same as in the case of an outright gift of the insurance.

PLAN 8: TRUST FOR SELF AND UNIVERSITY

Example: Miss Fall wished to make a substantial gift to a university but did not wish to reduce her income from investments. So she put some of her investments into an irrevocable living trust, with all income payable to herself for life. At her death the principal will go to the university.

The Tax Results: Assume Miss Fall is 60 when she creates the trust. At the start she deposits $30,000 of her investments in the trust.

The educational gift considered to occur this first year is 30,000 x 60¢, approximately, or $18,000. (60¢ is the present value of $1 at the death of a person now aged 60; see the table at page 22.)

The $18,000 is deductible on Miss Fall's income tax return, but only within the applicable percentage-of-income limits.

The next year and each year thereafter Miss Fall intends to deposit $10,000 more of her investments in the trust. Each year she will become entitled to a contributions deduction for doing so. For example, the second year her contribution will be 10,000 x 61½¢, approximately (61½¢ being the present value of $1 after death of a person now aged 61), or $6,150.

VALUES OF LIFE ESTATES AND REMAINDERS

Table showing the present worth of a life interest and of a remainder interest in $1. You need these figures to compute the exact amount of educational gifts in Plans Nos. 2, 3, 4, 8, 11, and 14.

Age of Life Tenant	Life Estate	Remainder	Age of Life Tenant	Life Estate	Remainder
1	$.87162	$.12838	46	$.56559	$.43441
2	.87122	.12877	47	.55436	.44564
3	.86886	.13114	48	.54297	.45703
4	.86582	.13418	49	.53141	.46859
5	.86237	.13763	50	.51970	.48030
6	.85864	.14136	51	.50785	.49215
7	.85466	.14534	52	.49587	.50413
8	.85044	.14956	53	.48377	.51623
9	.84600	.15400	54	.47157	.52843
10	.84135	.15865	55	.45926	.54074
11	.83653	.16347	56	.44688	.55312
12	.83160	.16840	57	.43442	.56558
13	.82656	.17344	58	.42191	.57809
14	.82143	.17857	59	.40936	.59064
15	.81618	.18382	60	.39679	.60321
16	.81083	.18917	61	.38422	.61578
17	.80536	.19464	62	.37165	.62835
18	.79979	.20021	63	.35911	.64089
19	.79404	.20596	64	.34663	.65337
20	.78813	.21187	65	.33420	.66580
21	.78203	.21797	66	.32186	.67814
22	.77576	.22424	67	.30962	.69038
23	.76930	.23070	68	.29750	.70250
24	.76266	.23734	69	.28552	.71448
25	.75582	.24418	70	.27370	.72630
26	.74880	.25120	71	.26205	.73795
27	.74157	.25843	72	.25059	.74941
28	.73416	.26584	73	.23934	.76066
29	.72653	.27347	74	.22831	.77169
30	.71871	.28129	75	.21752	.78248
31	.71068	.28932	76	.20698	.79302
32	.70245	.29755	77	.19670	.80330
33	.69401	.30599	78	.18671	.81329
34	.68536	.31464	79	.17700	.82300
35	.67650	.32350	80	.16759	.83241
36	.66743	.33257	81	.15849	.84151
37	.65815	.34185	82	.14970	.85030
38	.64867	.35133	83	.14123	.85877
39	.63898	.36102	84	.13308	.86692
40	.62908	.37092	85	.12526	.87474
41	.61899	.38101	86	.11777	.88223
42	.60869	.39131	87	.11060	.88940
43	.59820	.40180	88	.10377	.89623
44	.58751	.41249	89	.09726	.90274
45	.57664	.42336	90	.09107	.90893

The above table, single life, 3½%, is from section 20.2031-7 of the Federal estate tax Regulations.

Thus, her income is not reduced; *but her income tax is.* In addition, of course, she reduces her estate for Federal estate tax purposes.

Miss Fall was warned by her lawyer, when she created the trust, that the trust would be absolutely irrevocable, and she could never have any of the principal paid back to her in any circumstances. This was one of the reasons she "went slowly," depositing only a small fraction of her assets at the start and making relatively small additions each year afterwards. As it happened, though, she obtained the largest possible income tax deductions, for the percentage-of-income limitations put a "ceiling" on her contributions deductions in any event.

PLAN 9: TRUST FOR SELF, WIFE, AND EDUCATIONAL INSTITUTION

Example: **Mr. Hall owned "growth" securities acquired many years ago at prices far below current values. He realized his spendable income could be much higher now if he held tax-free State and municipal bonds instead. But selling his present holdings would result in huge gains.**

He created an irrevocable living trust and deposited his low-cost securities in it. The trustee, aware of his need for income, sold these securities and reinvested in State and municipal bonds.

Mr. Hall receives all the income of the trust for life, then Mrs. Hall receives the income for her life. When the survivor dies the trust ends and principal goes to a university.

The Tax Results: Mr. Hall is entitled to claim an income tax deduction for a contribution in the year he deposits securities in the trust. As in Plan No. 8, the amount of the deduction can be computed from tables issued by the Government—although, since *two* lives are involved here, a special table must be used. (It's included in the booklet, "Actuarial Values for Estate and Gift Tax Purposes," obtainable at a small price from the Government.)

The outstanding tax feature of Mr. Hall's plan, however, is the freedom from income tax on sale of the low-cost "growth" securities. It is the trustee—not Mr. Hall—who sells these. And since gains on sales made by the trustee are part of the principal, and thus are held for the eventual benefit of the university, the trustee pays no tax on these gains.

As for estate tax, the trust would be wholly or largely free of tax at Mr. Hall's death; and there would be no tax at Mrs. Hall's death.

Mr. Hall, in creating the trust, makes a gift in some amount to Mrs. Hall: he gives her the right to receive income if she survives him. The value of the right, however, might well be less than Mr. Hall's "lifetime" exemption from the Federal gift tax, so it is quite possible that he pays no Federal gift tax whatever.

PLAN 10: LIFE INCOME ACQUIRED FROM EDUCATIONAL INSTITUTION

Example: **Mr. and Mrs. Mall pay $10,000 direct to a college. In return they receive a monthly or quarterly income that will continue until the survivor dies.**

The Tax Results, in this case, depend partly on the precise type of plan that is entered into.

In some cases the plan is really an annuity contract. The individual donor or donors buy the annuity, the college sells it. A portion of the purchase price is considered for income tax purposes to be a gift to the college, and this portion is deductible, up to 30% of adjusted gross income, on the purchaser's Federal income tax return. Then a relatively small portion of each monthly or quarterly payment of income is taxable; the rest is exempt. (The taxable portion depends on the ages of the annuitants when the plan is entered into.)

In other cases there may be a "transfer with reservation of a life estate," as the lawyers say, or perhaps the creation of a trust. In these cases the tax results are just about the same as in Plans Nos. 8 and 9, where typical trusts are shown.

PLAN 11: ESTATE "POURED INTO" TRUST FOR FAMILY AND COLLEGE

Example: **Mr. Nall, an executive of a large company, carries much life insurance and has a large sum standing to his credit in his company's profit-sharing plan; but he has a relatively small estate passing by will.**

He makes his life insurance policies and profit-sharing money payable to a bank as trustee of a "revocable trust." Then in his will he directs that the rest of his assets be "poured into" this same trust when he dies.

Mrs. Nall is to receive the income from this trust during widowhood. (Technically, there may be two trusts for her, one qualifying for the Federal estate tax "marital deduction" and one not qualifying.) When she dies 9/10ths of the principal is to go to the children and 1/10th to a college.

The Tax Results: Mr. Nall's financial situation is typical of modern times. Like so many other high-salaried men, he has little ready cash but nevertheless will leave substantial sums for his family.

He would like to give to the college in a way that would entitle him to income tax deductions now, for his tax rate is high. But none of the usual plans seems feasible. He can't spare the cash. (Perhaps he's already in debt.) He can't irrevocably assign any of his life insurance to the college, he feels, for at all costs his arrangements must be flexible, adaptable to new developments. His children are still young, and he is aware that there will be heavy college "contributions" of a very direct (but non-deductible) nature just a few years ahead.

After talking with his lawyer* and the trust officer of his bank, he adopted the "revocable trust with pour-over" arrangement. He can change it whenever he wishes, though he thinks it unlikely that he ever will. And there is no drain on his limited cash resources.

He does not save income tax. But, by means of the "tithe" for the college, he removes the topmost part of his estate from the impact of the Federal estate tax.

And he has the satisfaction of doing something—perhaps it will be a a good deal, if he continues to prosper—for the college.

*A "pour-over" arrangement may not be possible in every State. Your lawyer can advise you on this.

PLAN 12: TRUST FOR 5 YEARS FOR EDUCATION, THEN FOR WIFE

Example: **Mr. Wall is 60 years of age. He has a good income from his profession and expects it to continue for the next five years. He pays very high income taxes. After age 65, perhaps, his income and taxes will be much lower.**

Unlike Mr. Nall in Plan No. 11, Mr. Wall has a fund of investments. He creates an irrevocable trust with a bank as trustee. All income for the first five years is to be paid to a university. Then the income (and some of the principal too, if needed) will be paid to Mrs. Wall during the rest of her life. When she dies she can direct in her will how the principal is to be distributed. (In legal language, she has a "*limited* power of appointment.")

The Tax Results: The income of the trust during the first five years will not be taxed to Mr. Wall. It completely escapes tax even though it may be more than 20% or 30% of his income.

He could give to charities and deduct on his tax return *another* 20% or 30% of his income. The trust income isn't counted as his at all.

Being a heavy contributor to various causes while his income is high, Mr. Wall thus finds the trust to be a valuable arrangement during these first five years. In effect, it permits him to take unlimited deductions for contributions.

After the five years have ended the trust offers no particular income tax advantage. The income will be taxed to Mrs. Wall, and thus it will find its way back onto the joint returns that Mr. and Mrs. Wall file while both are living. The trust does, however, give Mrs. Wall financial protection for as long as she lives. And it assures her of an uninterrupted income if, after she begins to receive the income, her husband should die; there would be no delay in income payments while his estate was being settled, for the trust would not be a part of his estate.

As for the Federal estate tax, the property in the trust would normally escape tax *at Mr. Wall's death and also at Mrs. Wall's death.* This would

be so even though Mrs. Wall should exercise her "limited power of appointment" in such a way that the principal goes to children or other relatives.

Mr. Wall may have a Federal gift tax to pay, but the amount would be much less than the estate tax saving.

There is still another favorable tax provision applicable to such a trust, but it is one that Congress has threatened to remove. It is the income tax "contributions" deduction allowed the grantor *when he creates the trust.* When, for example, Mr. Wall deposited $50,000, we'll say, in the trust at the start, he really gave the income for the next five years on that money to the university. The entire gift is considered to have occurred then, when the money or securities were put in the trust, even though actual payment of the income to the university will be strung out over the following five years. The university's right to receive this income can be valued (it's a little less than $8,000, if $50,000 was put in the trust), and that value is the measure of a contribution, deductible within the percentage-of-income limits.

Ask your lawyer about the deduction in this particular situation.

PLAN 13: BUSINESS OWNER GIVES PREFERRED STOCK TO A COLLEGE

Example: **Mr. Black and his wife own all the stock of a company. The stock is all of one class.**

They have the company issue a dividend payable in preferred stock. Then they give this newly issued preferred stock to a college, to establish a memorial fund.

The Tax Results: It's usually difficult for an owner of a company to "get money out of the company" without having the money taxed to him as a dividend.

But it is now clearly possible (since 1954) for a tax-free dividend to be paid in preferred stock.

What can the owner do with the preferred stock after he gets it? Usually he dares not sell it, for the sale might result in the taxing to him of a huge sum as ordinary income. The 1954 provision, freeing the *receipt* of the stock from tax, imposed this special tax liability on a subsequent *sale or redemption.*

Neither, ordinarily, is it always safe to give the stock away—to a member of the family, for instance—for the donee might have the special tax to pay if *he or she* should sell the stock or have it redeemed.

A 1957 ruling (Rev. Rul. 57-328) opens a door. It suggests the use of this preferred stock as a gift to a charity (which, of course, includes an educational institution).

Could the stockholder making such a gift take a contributions deduction on his income tax return, subject to the usual percentage-of-income limitations? *Yes, says the ruling.*

Would the stockholder be considered to realize income upon giving the preferred stock to the charity? *No, he would not.*

Finally, would the stockholder be considered to realize income if the charity should later sell the preferred stock or have it redeemed? *The ruling holds that he would not.*

The ruling deals with a specific situation in which there had been no pre-arrangement for the sale of the stock by the charity or for redemption of the stock by the company.

Even so, the ruling is good news to many who own controlling interests in family or closely held corporations. It points the way to tax-economical gifts for education—*gifts that consist of business interests yet which do not (if the company can issue non-voting stock) disturb voting rights.*

PLAN 14: **ART OBJECTS DEEDED TO UNIVERSITY BUT KEPT FOR LIFE**

Example: **Mr. White is an art collector. By written deeds he gives some of his pictures to a university; and he also gives fractional interests in other pictures. But, in accordance with the terms of the deeds, he keeps all the pictures right on his own walls as long as he lives. The university gets them only after he dies.**

The Tax Results: Mr. White is considered to contribute to the university the "remainder interests" in his pictures. He can deduct on his income tax returns, for the years he gives the deeds, the "present values" of these interests. The deductions, of course, must be within the usual percentage-of-income limits. Two rulings—Rev. Rul. 57-293 and Rev. Rul. 58-455—deal specifically with the situation.

Presumably the remainder interests would be valued by reference to the same tables of the Regulations that are applicable to income-producing property. See page 22 of this booklet.

The rulings refer to "art objects" and paintings. Nothing is said about libraries, although it may be that the same principle would apply to a valuable collection of books. This is a matter to be taken up with one's lawyer.

Where to Get Information and Assistance on Educational Gifts

If you would like to have direct and personalized assistance in the making of a gift for educational purposes, here are some of the people you can call upon:

1. ***A Representative of the College or University.*** The need for support is so urgent in educational institutions today that any college or university can be counted on to give every possible assistance to persons who are considering gifts. For our part, we will say this: If you are nearby, drop in at our administration offices at any time. You are always welcome. Or, you can write or telephone, stating that you wish information and assistance. A qualified representative will gladly discuss with you our financial situation and will tell you just what could be accomplished by your gift. This discussion would put you under no obligation whatever.

2. ***Your Lawyer.*** It is your own lawyer who should be consulted on all legal matters involved in the making of a gift for education. He should draft any legal instrument—such as a will or trust agreement —that is required to put the gift into effect. Your lawyer, too, might well be asked to consider the effect of your gift on your estate plans in general. "Estate planning" today is a comprehensive subject; it surely includes a study of any substantial gifts, whether to educational institutions or to members of the family, and your lawyer's assistance in this planning is vitally important.

3. ***A Trust Officer of a Bank or Trust Company.*** Many of the methods of making gifts for educational purposes call for the services of a bank or trust company as trustee. You will find that a trust officer

will gladly explain these services to you in detail, and will also offer his assistance in the investment and financial aspects of your planning, without charge or obligation.

4. ***Your Life Insurance Agent.*** If you are considering an educational gift that involves your life insurance in any way it is advisable that your life insurance agent be brought into the discussions. He is qualified to inform you regarding the values of your policies and also regarding the various procedures of assignment and change of beneficiary.

5. ***Your Accountant.*** Some educational gifts are related to the donor's business, or may consist of shares of his business. His accountant may be the one best qualified to advise him on the value of the shares, the possible effect of a gift on the continued profitable operation of the concern, and other such matters.