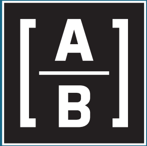


BERNSTEIN

THE SEEDS YOU PLANT

Growing Your Philanthropic Impact

WHY BERNSTEIN?

We're investment managers. Since our founding in 1967, Bernstein has focused only on investment research and management for clients, so our interests are aligned with our clients' interests, and we are accountable for their outcomes.

Bernstein provides a consistent, integrated approach to delivering investment outcomes:

- Individually tailored asset allocations and portfolios
- World-class research expertise across asset categories and geographies
- Integrated volatility and tax management (where applicable)
- Fully transparent fees
- Personalized service

We understand the challenges that philanthropic individuals and organizations face. For decades, our philanthropy team members have applied their expertise in financial modeling, planning, and regulatory issues to help clients achieve their philanthropic goals.

We integrate environmental, social, and governance (ESG) considerations into our research and investment processes.

Bernstein is part of AB, one of the world's largest investment firms, which manages nearly half a trillion dollars in assets for clients around the world. Bernstein clients benefit from the skill and experience of more than 3,000 employees in over 20 countries.

This publication is provided for informational purposes only and is not intended to be an offer, or the basis for any contract to purchase or sell any security or other instrument, or for AB to enter into or arrange any type of transaction as a consequence of any information contained herein. AB and its business units do not provide tax, legal, or accounting advice; you should consult your professional advisors with respect to such matters.

Table of Contents

The Seeds You Plant 2

Your Philanthropy, Empowered 3
Defining Your Philanthropic Mission 4
Making an Impact 6
Your Capacity to Give 7
Implementing Your Philanthropic Mission 8

Purely Philanthropic Strategies 10

Direct Gifts 11
Charitable IRA Rollovers 13
Donor-Advised Funds 15
Private Nonoperating Foundations 19
Private Operating Foundations 23
Charitable Pledges 27
Bequests 29

Partly Philanthropic Strategies 30

Charitable Lead Annuity Trusts 31
Charitable Remainder Trusts 35
Charitable Gift Annuities 39
Pooled Income Funds 41

Investments 42

Time Frame Matters 43
Assets to Give 45
Responsible Investing: What's Right for You? 46
For-Profit Charitable Strategies 47

Special Topics

What to Consider Before Joining a Board 5
If You Can't Part with a Favorite Stock 12
Total Philanthropic Value: A Measure of Financial Impact 14
Wealth Forecasting 18
Checklist for Establishing a Private Foundation 22
Perpetuity or Spend-Down? 24
Comparing Vehicles for Purely Philanthropic Giving 26
Compelling Combinations: Donor-Advised Funds and Private Foundations 28
Crafting Your Investment Policy Statement 48

Appendix 49

Glossary 49
Notes on Wealth Forecasting System 51

"Don't judge each day by the harvest you reap but by the seeds that you plant."

—Robert Louis Stevenson

Your Philanthropy, Empowered

"I've been writing checks to various causes for years, but this year I'll have much more to give. What does this mean for how I give?"

"I want to give back to society and have an impact. Can you help?"

"Over time, our family foundation has been a source of joy and fulfillment for my husband and me. But our children and grandchildren aren't interested in carrying it forward. What do you advise we do?"

We hear stories and questions like these day in and day out. Many of our clients are deeply committed to philanthropy. They take to heart a statement by Robert Louis Stevenson, "Don't judge each day by the harvest you reap but by the seeds that you plant."

Fortunately, there are many philanthropic strategies to consider. Selecting the right one for you and your family can be both daunting and exciting. Philanthropic giving is inherently personal because it is rooted in your values and in how you choose to fulfill your sense of responsibility to your family, the community, and the world. It inevitably raises questions like:

- What is my charitable goal?
- Is my commitment time-bound?
- What do I want my legacy to be?
- Do I want my family to be involved?
- What responsibilities and commitments am I willing to assume?
- How can I achieve the most impact with the gifts I make? and
- How much can I give?

This guide offers advice based on our experiences helping clients who were wrestling with these issues. In some cases, we can provide clear answers to client questions. More often, we help clients understand their choices by asking more questions—about their circumstances, preferences, and goals. Then we quantify the likely financial results of the decisions they make, and help them design and manage the strategy they choose.

This guide is organized around your choices and provides a framework for weighing trade-offs. It doesn't aim to provide all the details you need to design the plan that is right for you. Bernstein doesn't offer tax, legal, or accounting advice, so when you consider this material, you should discuss your individual circumstances with professionals in those areas before making any decisions.

Indeed, you may already be working with tax and philanthropic advisors to cultivate a giving strategy that is right for you. We have the tools and expertise to work with your advisors to empower you to grow your philanthropic impact.

DEFINING YOUR PHILANTHROPIC MISSION

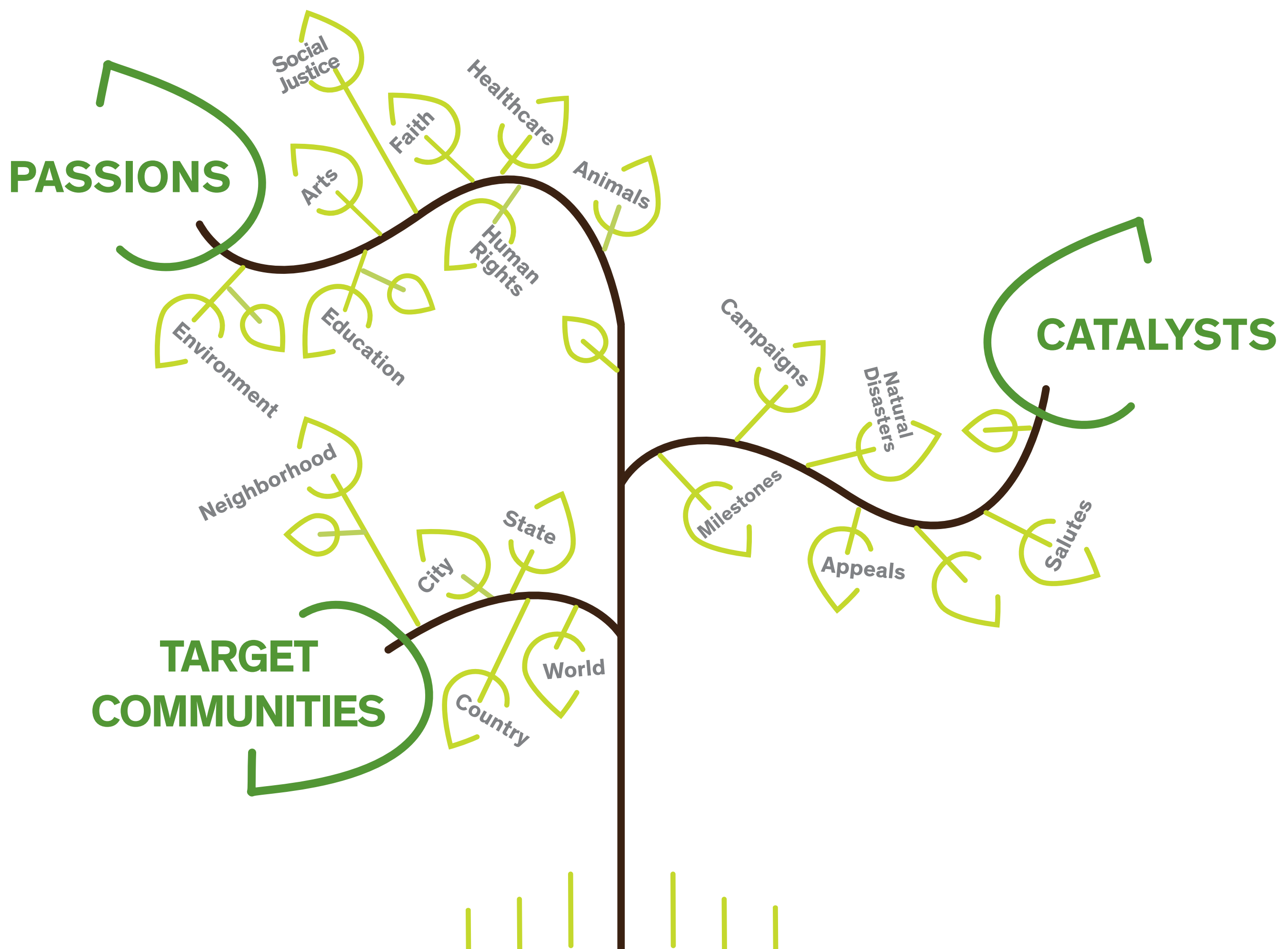
In deciding what and how much you want to give to philanthropic causes, it is useful to plot the elements of your philanthropic vision along various dimensions, as ***Display 1*** shows.

- **Your Passions:** What social, educational, faith-based, or health-related issues or organizations do you care about deeply?
- **Your Target Communities:** Do you want to help your local community, your own or another country, or the world?
- **Your Catalysts:** Do you react generously to other appeals, seek to form a unique relationship with an organization, or prefer to respond to crises?

Designing a philanthropic mission involves personal choices about your values, what you want to achieve, how you want to achieve it, and whether you prefer to give publicly or anonymously. You may find it easier to answer these questions if you reflect on how you have given in the past and how you felt about it. Did you have the impact you wanted?

Once you decide, be thoughtful about how you implement your choices. The size, frequency, and timing of your gifts, and the assets you donate, should make sense for you and for the causes or organizations you support. Some of the strategies in this guide will sync with your philanthropic mission; others won't.

DISPLAY 1: PLOTTING YOUR PHILANTHROPIC MISSION



Family Considerations

For some of our clients, philanthropy is a way both to make the world better and to instill their values in their children, or even to pass on a multigenerational legacy. If that's true for you, it's important to explain to your children what motivates you to be philanthropic and why you chose particular organizations or causes to fund.

How and when to expose your heirs to your philanthropy is up to you and your family. Some families involve their children in volunteer activities, starting at an early age. Others use private foundations, donor-advised funds, or annual charitable giving as ways to get their heirs involved in philanthropy and managing wealth now.

For example, one of our clients gave each of her two adult children responsibility for managing and distributing 15% of the family foundation's assets. In this way, she gave them a chance to understand her philanthropic goals, experience the joy of giving, and learn how a foundation works.

But before assuming your family members will want to be involved in your philanthropic plan or that they will share your passions, ask them. Think about their talents, too. Do you think they'd be better at grant-making, research, or investing? Would they be appropriate members of your foundation's board of directors?

As the steward of your philanthropic mission—and perhaps as a legal fiduciary of a trust or foundation—you need to ensure you recruit the right people for the task at hand. You may also need to enlist other nonfamily members or hire experts for certain roles.

Time Considerations

Think carefully, too, about how much time you and your family are likely to be willing to give. Writing checks is quick and easy; volunteering to paint a community center is a discrete task. Setting up a trust or a foundation, by contrast, can be time-consuming and expensive and commits you to certain obligations over time.

There are many options that fall between these extremes, such as coupling direct gifts with participation in a not-for-profit organization's board or committees. (See "What to Consider Before Joining a Board," below.)

How much time you're willing to give and to whom you give are your decisions to make. Be wary, though, of taking on a commitment that you may not be willing to fulfill in a few years.

What to Consider Before Joining a Board

- Does the organization's mission interest me?
- Do I have sufficient time to devote to board service?
- What is the overall time commitment, and what are my responsibilities? How much fund-raising will I have to do?
- How does the board deal with potential conflicts of interest, and are there conflict-of-interest rules I should know about?
- What is my liability as a board member, and does the organization provide directors' and officers' liability insurance?
- Is the organization financially stable?
- How does the organization decide what gifts to accept, and how does the organization ensure that donor intent is honored?

MAKING AN IMPACT

If you care about the cause you're giving to, you'll want to ensure that it has an impact. Selecting not-for-profit organizations that run effective programs and don't spend too much money on overhead costs is a crucial first step. Fortunately, you can get help in this regard. A few organizations seek to provide transparency on charities' effectiveness and use of funds. *GuideStar*, for example, provides online information on millions of public charities.

How you make your gifts can also affect the nature and scope of their impact. A matching grant that prompts other donors to give to a particular organization may have greater impact than a direct gift of the same amount—or more. A pledge of ongoing, annual support may have more impact than a series of one-time gifts, because it relieves the not-for-profit of having to raise the money each year and signals a long-term commitment.

Sometimes, establishing a public or private foundation with a long-term giving horizon—decades or more—can be transformational. Not only are resources available for the long haul, but the foundation structure can provide additional leverage by giving its creator a bully pulpit.

But perpetuity is not always the right formula. For some causes, establishing a foundation, trust, or program that spends down its wealth over 10 or 20 years may have more impact, because each dollar given today will have social and economic benefits that multiply over time. And a shorter time horizon makes more resources available.

For example, in 2002, Chuck Feeney, a longtime advocate for giving during your lifetime, announced that The Atlantic Philanthropies would have a fixed term: They would complete grant-making in 2016 and close by 2020. By then, they will have distributed more than $8 billion.

Whether your gift is perpetual or time-bound, you can assess its potential impact when making choices about its design. By quantifying the trade-offs, Bernstein can help you to determine how much to spend, and how much to invest for future giving. (See "Wealth Forecasting" on page 18.)

Once your philanthropic program is under way, assess its nonfinancial impact periodically. You can ask the not-for-profits you fund to provide you with an annual accounting of what your gift allowed them to do: How many students went to college with the help of your scholarship fund? How many children received TB vaccinations in Peru? How many solar panels were installed in remote villages off the electric grid?

Consider, too, the impact on your family. Have your children become engaged in giving through your program? Has it brought your family closer together?

YOUR CAPACITY TO GIVE

If you're reading this guide, you're willing to give. But how much can you give, without undermining your long-term spending needs or your goals to transfer wealth to your loved ones?

However and whenever you choose to give, it's important to analyze the likely impact on your financial plan and the associated trade-offs. Philanthropy is noble, but irrevocable gifts can have financial consequences that you should understand and plan for.

Our Core/Surplus Framework

To help clients understand their capacity to give, we developed a core/surplus framework for investment planning. First, we seek to ensure that you secure and sustain what we call your "core capital": the amount of money you need today to secure your living expenses for the rest of your life.

We use our Wealth Forecasting System℠, described on page 18, to conservatively estimate your core capital, assuming that you may live beyond what the mortality tables would suggest, that high inflation might drive up your spending needs, and that deep bear markets may depress your portfolio value at least temporarily. Your assets above your core capital are "surplus capital" that you could spend on big, optional purchases (such as a country home) or give to friends, family, or charity.

Less than You Think—or More?

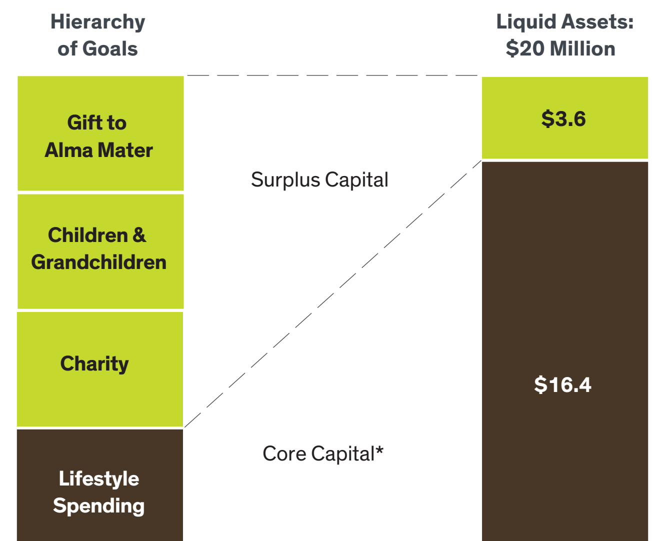
Let's say you're 65 years old, you're recently retired, and you have $20 million invested in a moderate allocation. You spend $500,000 per year, after taxes. You have been considering giving $1 million to your alma mater, which is building a new campus museum. Our analysis might show that you need $16.4 million to support your lifetime personal spending, so you have $3.6 million of surplus capital (***Display 2***). You certainly have the $1 million you'd like to give to your alma mater.

That's great. But before you make such a large, irrevocable gift, take the time to think through how much you'd like to give to other causes and to your family—and consider other ways to give. You could make smaller (but still substantial) annual gifts, which you could stop if, say, an unexpected medical expense arises—or if you become enamored with another cause.

You could also use one of the partly philanthropic vehicles discussed in this guide to provide your alma mater with gifts for many years, but leave the remainder to your family—or to provide your children with income for many years, and leave the remainder to the school.

Or, after careful reflection, you could go ahead with your original plan, or give your alma mater even more. Our core/surplus framework is meant to help you feel confident in your ability to give, and to help you understand how much you can give, considering all your other goals. In some cases—like this one—you may be pleasantly surprised to learn you can give more than you thought.

DISPLAY 2: DETERMINING CORE AND SURPLUS CAPITAL



Core capital is defined as the amount needed today to support annual spending of $500,000 after taxes and inflation with a 90% level of confidence. Portfolio is modeled as 60% global stocks and 40% bonds. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as intermediate-term municipal bonds. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016.* ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*

See Notes on Wealth Forecasting System on page 51.

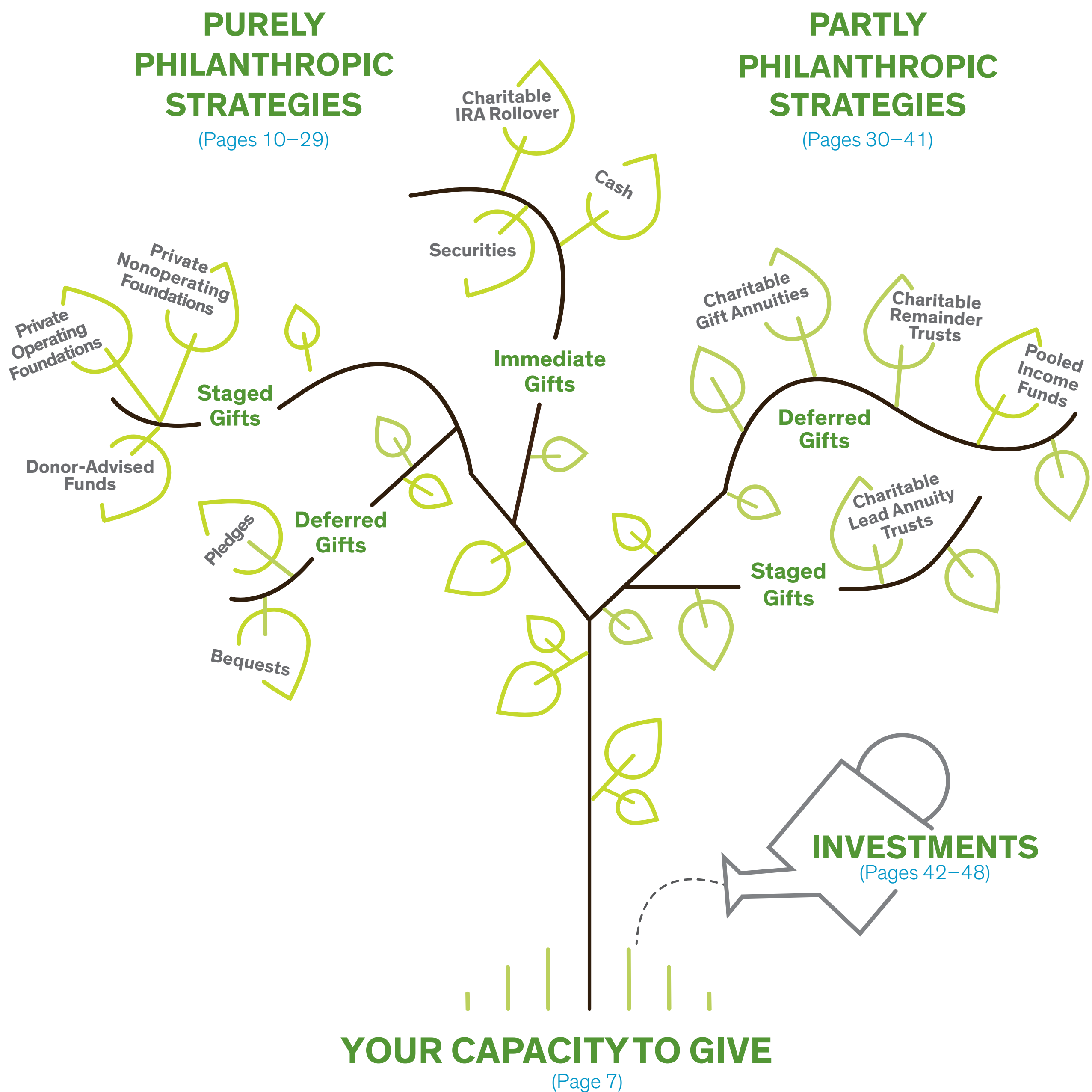
Source: Bernstein

IMPLEMENTING YOUR PHILANTHROPIC MISSION

Let's say you've established that you've secured your core capital and can afford to make substantial gifts. What philanthropic strategy should you use? Our decision tree can help you decide (***Display 3***).

We urge all clients to work with their legal and tax advisors on estate planning. In addition, in seeking to meet your philanthropic objectives, you have a choice between purely philanthropic gifts and gifts that provide some financial benefit to you or your family. Both purely philanthropic and partly philanthropic strategies give you the flexibility to make immediate, staged, or deferred gifts. The pages that follow provide more detail to help you identify strategies that could meet your goals.

DISPLAY 3: OUR DECISION TREE CAN HELP YOU NARROW DOWN YOUR CHOICES



LET YOUR JOURNEY BEGIN...

PURELY PHILANTHROPIC STRATEGIES

"No act of kindness, no matter how small, is ever wasted."

—Aesop

Direct Gifts

Best for:	Donors seeking a simple and flexible way to make a gift of cash or securities directly to charity
When Charity Receives Gift:	**Now** · **Staged over Time** · **Later**
Tax Impact:	Receive charitable income-tax deduction in year of gift, subject to AGI limitations
Distributions to Donor:	No
Limitations/ Drawbacks:	Gifts of cash can be less efficient than other strategies, from an income-tax perspective

The simplest way to give to a qualified charity is to make a direct gift of cash. Writing a check or using your credit card is easy, scalable, and flexible: You can give more or less from one year to the next, or stop giving altogether, if your situation changes financially or a new cause grabs your heart. You will receive a personal income-tax deduction for however much you give.

But too often, even financially sophisticated people miss another simple way to boost the tax benefit of their charitable donations: giving appreciated securities, rather than cash.

How It Works

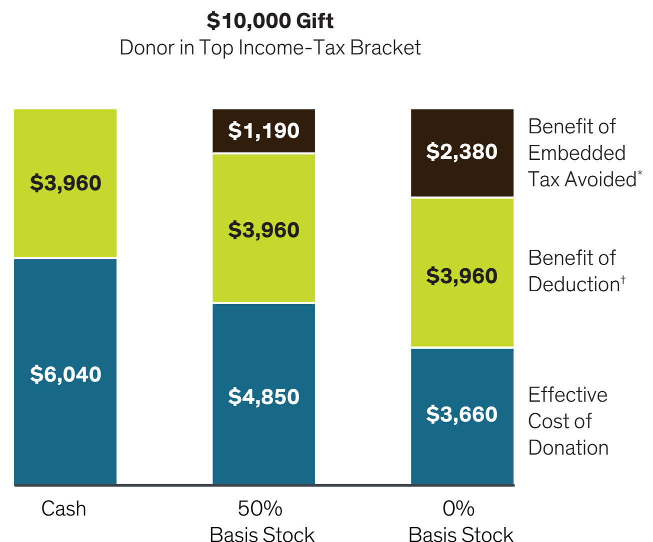
For someone in the top (39.6%) tax bracket, deducting the value of a $10,000 cash gift to a qualified charity reduces the federal income tax owed by $3,960 and thereby cuts the effective cost of the gift (the value of the gift minus the tax benefit) to $6,040, as the left-hand bar in ***Display 4*** shows. For clients who pay state and local income tax, the effective cost may be even lower.

By contrast, gifts of appreciated publicly traded stock or other assets can also reduce or eliminate tax on capital gains, as well as reduce tax on ordinary income.

If the same taxpayer donated $10,000 in publicly traded stock bought for $5,000, he could also avoid paying the 23.8% tax on the stock's $5,000 gain. The extra tax savings would cut the effective cost of the donation to $4,850, as the middle bar shows.

If he donated $10,000 in publicly traded stock that he received at no cost—perhaps when he founded his firm—he could avoid paying the 23.8% tax on the stock's $10,000 gain, as the right-hand bar shows. The extra tax savings would cut the effective cost of his $10,000 gift to $3,660.

DISPLAY 4: NOT ALL CHARITABLE GIFTS OFFER THE SAME TAX SAVINGS



*Applicable rate for stock gain is assumed to be 23.8%.

†Deduction limited to 50% of AGI in year of gift for cash or 30% of AGI in year of gift of appreciated publicly traded stock. Benefit of deduction assumes full use of deduction against income otherwise taxed at 39.6% tax rate. Gift is to a public charity.

Source: Bernstein

To receive a deduction for its fair market value, a capital asset must be held for more than one year, among other requirements. The Internal Revenue Code permits charitable deductions of up to 50% of adjusted gross income (AGI) in the year of the cash gift, and up to 30% in the year of the gift of appreciated publicly traded stock.[1] However, the deduction can be carried forward for five years.

Deferring a deduction is valuable if a taxpayer wants to give more than he or she can deduct in one year—perhaps to help a charity get a matching grant. The limitations on the charitable income-tax deduction vary with the donor's income, the type of property being donated, and the nature of the recipient charity (for example, a public charity versus a private foundation). See "Assets to Give" on page 45, and consult your tax advisor.

IF YOU CAN'T PART WITH A FAVORITE STOCK

One couple we worked with asked if there was a better way to help their local hospital than writing a large check, as they had done in years past. Their advisor suggested giving low-basis stock. They had a large position in a pharmaceutical stock that had appreciated since they bought it six years earlier for $15,000: It was now worth $100,000.

The couple really liked the stock, and struggled with the idea of giving away anything that had performed so well, and which they felt complemented the rest of their holdings. Fortunately, the advisor was able to suggest an alternative that would give them the best of both worlds.

The couple's large portfolio included over $100,000 in cash that they had accumulated in anticipation of the gift to the hospital. If they gave the cash to the hospital and retained the pharmaceutical stock, they would fulfill their charitable goal, receive a $100,000 charitable income-tax deduction, and hold the stock with its $15,000 tax basis.

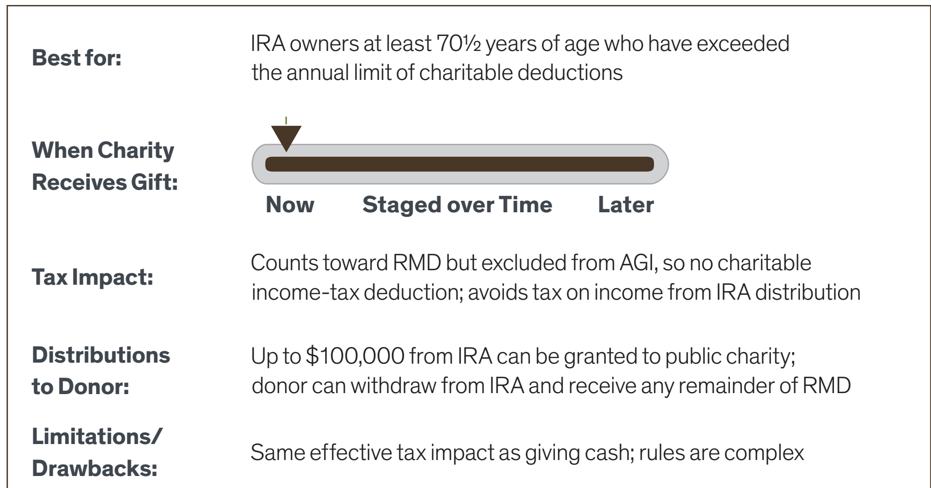
But if they gave the stock to the hospital, they could use the cash they'd accumulated to buy a new position in the same stock. They would still fulfill their charitable goal and receive a $100,000 charitable income-tax deduction—and they would reset the cost basis of their position in the stock to $100,000.

That's what they ultimately decided to do. If at some point in the future they decide to sell the stock, they would avoid $85,000 in embedded capital gains—and $26,000 in capital-gains taxes.[2]

[1] These are the deduction limitations for gifts to public charities, including donor-advised funds.

[2] Assumes the gain would otherwise be taxed at a blended long-term capital-gains rate of 30.2%, based on a federal rate of 20% with 3.8% Medicare surtax, including a combined state and local tax rate for New York City of 12.7%.

Charitable IRA Rollovers



If you are more than 70½ years old, don't need the required minimum distribution (RMD) from your individual retirement account (IRA) to fund your living expenses, and want to avoid paying income tax on the RMD, a charitable IRA rollover, technically called the qualified charitable distribution, may be a valuable strategy to consider. Donors who have exceeded the annual income limitations on charitable income-tax deductions or who do not itemize deductions generally benefit most.

How It Works

Giving opportunities are limited with regard to IRA accounts (see "Assets to Give" on page 45), but there's an exception for people who must take required distributions. The Protecting Americans from Tax Hikes (PATH) Act of 2015 allows IRA owners who are at least 70½ years old to donate up to $100,000 each year directly from their IRA to a qualified public charity, but not to donor-advised funds, supporting organizations, or private foundations.[3]

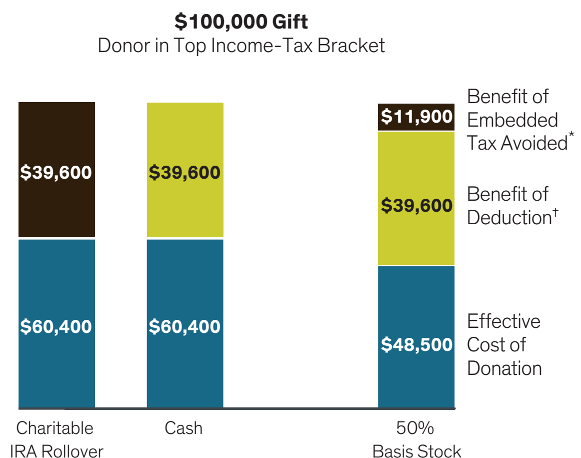
For donors who may not be able to fully use their charitable income-tax deductions, a charitable IRA rollover can be an efficient way to give. However, for donors who can use their charitable income-tax deductions, the effective tax impact is the same as for giving cash. Charitable IRA rollovers may require extensive documentation.

Assessing the Opportunity

For a donor in the top federal income-tax bracket, a $100,000 gift from an IRA to a charity will avoid $39,600 in embedded federal income tax (***Display 5***). That is, it would reduce the effective cost of the gift to just $60,400.

Note that a cash gift would result in the same economic benefit—if the donor could take full advantage of the charitable income-tax deduction in the current year. For donors who face deduction limits, the qualified charitable distribution may be a better strategy. However, if the donor gives highly appreciated stock, the combined benefit of avoiding the capital-gains tax and creating a charitable income-tax deduction may be greater than a charitable IRA rollover.

DISPLAY 5: IRA AND CASH GIFTS CAN HAVE SAME TAX IMPACT; APPRECIATED STOCK STILL ATTRACTIVE



**Applicable rate for IRA distribution is assumed to be 39.6% (no after-tax IRA contributions, and Medicare surtax does not apply). Applicable rate for stock gain is assumed to be 23.8%.*

†Deduction limited to 50% of AGI in year of gift for cash or 30% of AGI in year of gift of appreciated publicly traded stock. Benefit of deduction assumes full use of deduction against income otherwise taxed at 39.6% tax rate. Gift is to a public charity.

Source: Bernstein

[3] At the time of this writing, the *Grow Philanthropy Act of 2016, HR 4907*, would amend the Internal Revenue Code to allow donations from an IRA to donor-advised funds.

TOTAL PHILANTHROPIC VALUE: A MEASURE OF FINANCIAL IMPACT

Measuring the financial impact of direct gifts to charities can be complex, especially if some of those gifts will be made over time or at a future date. Bernstein created its total philanthropic value (TPV) metric to help you assess the projected financial impact of various giving strategies or spending policies. TPV is the sum of distributions over time and any remaining assets that will support future giving, in current dollar terms.

If you write checks directly to not-for-profit organizations, your TPV is the total you plan to give over time in today's dollars. The more you give and the earlier you give it, the greater the TPV.

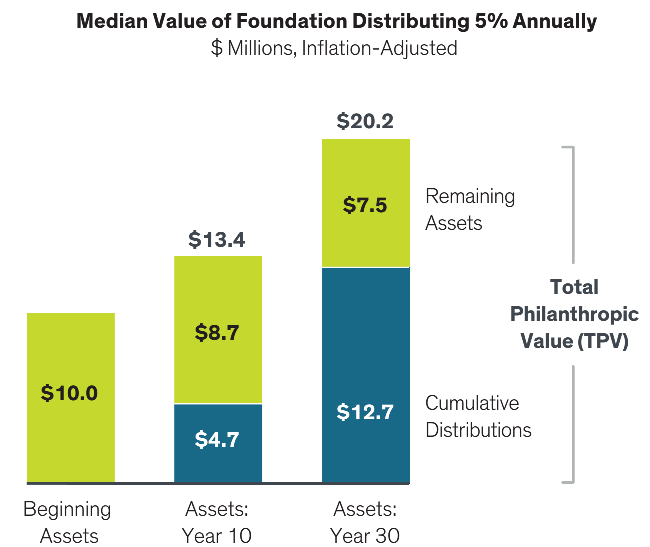
If you give now to a donor-advised fund (DAF), private foundation, or trust that will distribute money over time, your TPV is the sum of the expected annual grants and the expected amount remaining after, say, 20 years. The size of the annual grants, the time horizon for making the grants, the asset allocation of the charitable entity's investments, and the expected capital-market returns determine the TPV.

For example, if you establish a $10 million foundation, adopt a growth-oriented asset allocation, and distribute 5% of assets annually, we estimate that the TPV will grow to $13.4 million in 10 years and $20.2 million in 30 years, in the median case (***Display 6***). While in 30 years the real value of the foundation's remaining assets would decline to $7.5 million, the cumulative distributions would boost the TPV to more than double the initial gift.

TPV can also dimension the percentage you've already distributed versus the philanthropic reserve remaining, which can help you decide the size of future grants. But nonfinancial considerations should also play a role. If your philanthropic mission is focused on a near-term goal, such as halting an epidemic disease, you might decide to spend down your philanthropic assets. If your philanthropic mission has a longer horizon, such as sustaining an arts institution, you may want to keep a greater share of your philanthropic assets in reserve.

No matter what your mission, TPV can help you quantify the financial impact to charitable organizations.

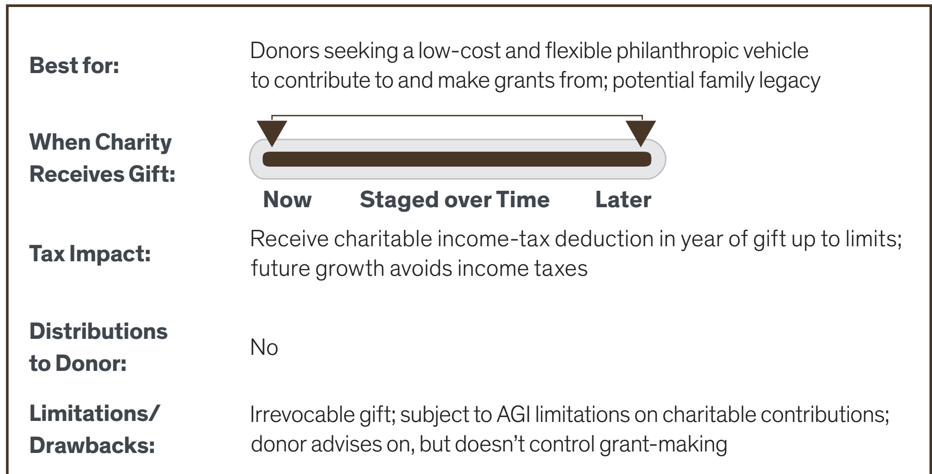
DISPLAY 6: TPV = TOTAL GIFTS + REMAINDER



TPV is the sum of cumulative distributions and the portfolio remainder value after inflation. Allocation is 80% stocks and 20% bonds. Global stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as 50% intermediate-term taxable bonds and 50% global intermediate-term taxable bonds, hedged. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*

Source: Bernstein

Donor-Advised Funds



Best for:	Donors seeking a low-cost and flexible philanthropic vehicle to contribute to and make grants from; potential family legacy
When Charity Receives Gift:	Now / Staged over Time / Later
Tax Impact:	Receive charitable income-tax deduction in year of gift up to limits; future growth avoids income taxes
Distributions to Donor:	No
Limitations/ Drawbacks:	Irrevocable gift; subject to AGI limitations on charitable contributions; donor advises on, but doesn't control grant-making

Low-cost and highly flexible, donor-advised funds (DAFs) have become philanthropy's fastest growing vehicle in recent years.

Here's why: Low operating costs reduce the minimum endowment generally required; you can contribute to a DAF as frequently as you like; there's no minimum annual grant; you don't have to administer the fund; and you can preserve your anonymity. The principal drawback is that you don't have complete control over grant-making and investments.

How a DAF Works

A DAF is an account or fund that you create at a sponsoring organization that is itself a qualified public charity—perhaps a community foundation, faith-based organization, or specialized provider. You make irrevocable gifts of cash or other assets to the fund, and you receive an immediate charitable income-tax deduction. The DAF is not part of your estate for gift and estate tax purposes.

The DAF can sell the assets you contribute, including highly appreciated stock, without triggering capital-gains tax. It can then reinvest the untaxed proceeds in a diversified portfolio, and benefit from its tax-free growth and income.

Most DAFs are not subject to annual giving requirements: You can grant as little as 0% or as much as 100% of the assets in any year.

As the name implies, in a DAF you play an advisory role with respect to investments and grants. The sponsoring entity (or administrator) handles check writing, record keeping, and other administrative tasks, and it disburses grants.

Setting the Payout Rate and Asset Allocation

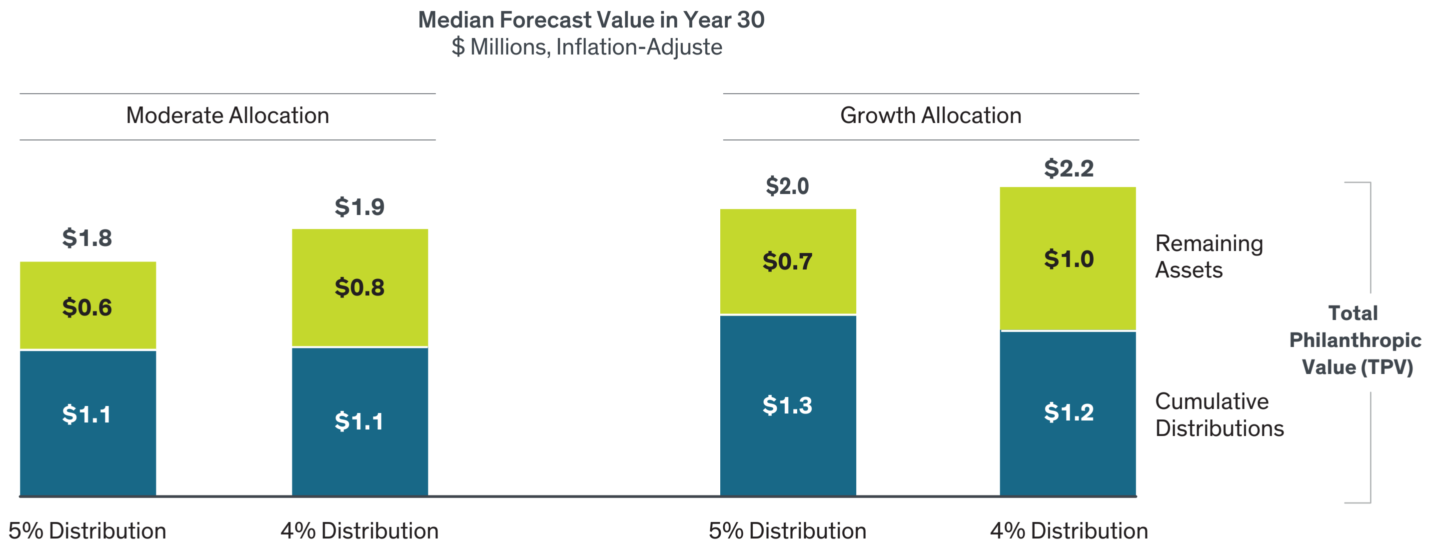
The flexibility of DAFs has a downside: Clients often have difficulty deciding how much to recommend that the fund distribute annually and what its asset allocation should be. To help frame the trade-offs, we use our total philanthropic value (TPV) metric to quantify the likely financial impact of a DAF's giving and investment choices. TPV measures the inflation-adjusted sum of total distributions and remaining assets after a stated period of time. (See "Total Philanthropic Value: A Measure of Financial Impact" on page 14.)

For example, one of our clients wanted to make a $1 million contribution to a DAF to fund his charitable giving over 30 years. While he thought giving 4% to 5% a year seemed reasonable, he wanted to know whether the higher giving rate or a growth allocation would increase its financial impact over time.

Display 7, next page, shows that with either asset allocation, the TPV would be higher over 30 years with a lower giving rate of 4%, in the median case. That's because the lower distribution rate would leave more assets in the fund to benefit from the compounding of investment returns. Of course, distributions of 4% would initially be smaller than distributions of 5% off the same asset base. But because the asset base grows more in the fund with a 4% distribution, the dollar value of its distributions would grow more, narrowing the gap.

The TPV would also be higher with a growth allocation than with a moderate allocation, in the median case: There would be more assets remaining after 30 years and more cumulative distributions.

DISPLAY 7: HOW YOUR CHOICES AFFECT THE TPV OF A $1 MILLION GIFT



Numbers may not sum due to rounding. TPV is the sum of real cumulative distributions and the real portfolio remainder value in a given year. Moderate allocation is 60% global stocks and 40% bonds. Growth allocation is 80% global stocks and 20% bonds. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as 50% US intermediate-term taxable bonds and 50% global intermediate-term taxable bonds, hedged. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*
Source: Bernstein

However, the growth allocation would also likely have more-volatile investment returns, which could lead to more volatility in distributions, if the donor remained wedded to the 4% giving rate.

Because there are no annual distribution requirements, DAFs have the flexibility to hold grants steady during bull markets so that the fund value can grow, and increase grants in challenging times. Some DAFs adopt a smoothing rule that applies the distribution rate to the average asset base for the last three or five years, in order to smooth out annual distributions. Some simply say that annual distributions will never decline more than, say, 5% from the previous year. This flexibility can be helpful to clients and to not-for-profits, which often receive fewer donations during market and economic downturns, when the need for their programs may rise.

Key Considerations

The various advantages and disadvantages of DAFs are laid out in the table on page 26. Here, we explore a few key issues in greater depth.

Control. When you donate assets to a DAF, you relinquish legal control. You don't make grants yourself; you submit recommendations for grants to a DAF administrator, which conducts due diligence to ensure the not-for-profit you recommended is a qualified public charity that meets the sponsoring charitable organization's own guidelines and mission. Most of the time, the administrator will follow your recommendations, but there's no guarantee.

DAF sponsors/administrators have the legal right to introduce restrictions on investments or grantees at any time, and can refuse a particular grant request, perhaps because the philanthropic cause, the geographic region, or the grantee lies outside the administrator's area of interest. For example, some DAFs will not make grants to non-US charities.

You can create an advisory board to help you with your grant suggestions, conduct official meetings, and make formal decisions on recommended grants and investments that you convey to the fund administrator. You cannot compensate the advisory board from the DAF's assets.

Time Horizon. Many DAFs are established for a defined term, such as two or three decades. Whether succeeding generations can participate in a DAF program depends on the sponsoring organization's rules. If you want your children or more distant descendants to continue your

philanthropic mission, you should find a DAF that permits successor advisors, or consider creating a private foundation instead.

Rules also differ regarding any assets remaining in the account when the DAF ends. In most cases, the donor can designate one or more charities or purposes for the remainder, but some programs require that remainders flow into the sponsoring charity's unrestricted fund. It's important to inquire about this in advance.

Anonymity. Most DAF programs will make grants in a way that does not disclose your identity, if you wish. If you want complete anonymity, you can give your DAF a name unrelated to your own. But DAFs can also make your gift public, if you want to attract attention to a cause, or be associated with the gift and the cause.

Taxes. The charitable deductions available for contributions to DAFs are generally based on the assets' fair market value, no matter if you give cash, marketable securities, business interests, real estate, or other privately owned assets. (See "Assets to Give" on page 45 for some exceptions.) If you give cash, the maximum deduction you can use in any year is equal to 50% of your adjusted gross income (AGI). If you donate assets, the maximum deduction you can use in any year is equal to 30% of your AGI. Charitable income-tax deductions can be carried forward for as many as five tax years. The DAF administrator has to file taxes annually for its entire portfolio of funds; that has no impact on the individual donor.

Self-Dealing. A DAF cannot make grants for which the donor would receive a tangible benefit. For example, it cannot buy a table at a charity event that would provide you and your friends or family with a nice meal and entertainment, as well as a tax deduction. In addition, DAF grants cannot be used to satisfy your existing charitable pledges.

Funding. Some DAF administrators won't accept gifts other than cash and readily marketable securities. But being part of the sponsoring organization makes DAFs eligible to invest in some alternative investment funds open only to qualified investors with a minimum of $25 million.

Legislative Risks. Some lawmakers have attempted to reduce the value of the charitable income-tax deduction and require that assets contributed to DAFs be distributed within five years of making the contribution.

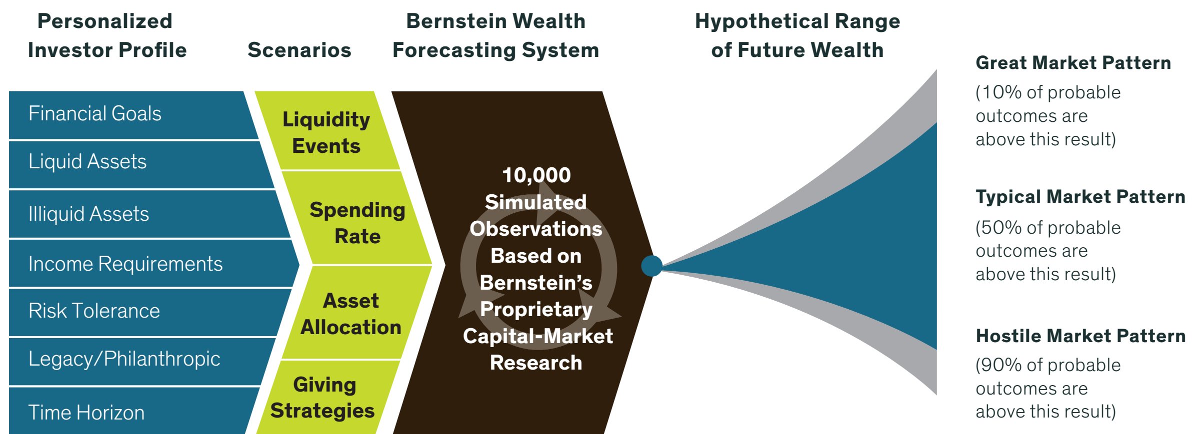
WEALTH FORECASTING

Investment-planning decisions can have ramifications over decades. Retirement plans may involve 40 or more years of saving—and another 30 to 40 years of spending. Charitable trusts may make grants over several decades. Foundations are often established with perpetuity in mind.

To make prudent decisions about the distant future, investors need a way to estimate the long-term results of potential strategies. Bernstein uses its Wealth Forecasting System℠ to make such estimates (***Display 8***). We start each analysis with your profile and time frame for achieving your goals. For lifetime spending goals, we use mortality tables[4] to determine roughly how long the funds will be needed to support spending. When allocating assets for a charitable trust, we consider its term and distributions. Then, we build scenarios around the decisions that you're weighing.

We use our Capital Markets Engine (CME) to project the range of likely outcomes. Our CME is a quantitative model that simulates 10,000 plausible paths of return, starting from today's conditions, for a wide range of investment assets and inflation. It takes account of the linkages within and among the capital markets, and their unpredictability. Our return forecasts derive from historical patterns in financial metrics, asset-specific factors, and the potential impact of inflation and taxes. While no one can predict future market returns with precision, our forecasts of the range of outcomes enable investors to make well-informed decisions about various strategies and the trade-offs they entail.

DISPLAY 8: THE CORE OF YOUR RELATIONSHIP—TAILORED WEALTH PLANNING

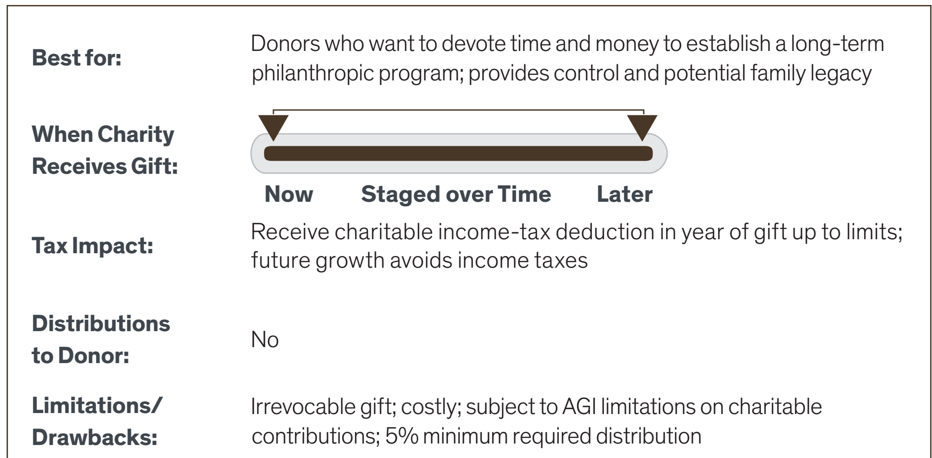


The Bernstein Wealth Forecasting System is based upon our proprietary analysis of historical capital-market data over many decades. We look at variables such as past returns, volatility, valuations, and correlations to forecast a vast range of possible outcomes relating to asset classes, not Bernstein portfolios. There is no assurance that any specific outcome suggested by the model will actually come to pass. *See Notes on Wealth Forecasting System on page 51.*

Source: Bernstein

[4]We add three years to most clients' expected life spans, because wealthy people tend to live longer than the general population. We can also adjust for a known risk factor, such as an inherited disease.

Private Nonoperating Foundations



Private nonoperating foundations provide flexibility and control to donors willing to devote substantial time and money to establishing a long-term philanthropic program. These vehicles are often intended to be perpetual (to last well beyond your lifetime), and thus can allow you to establish a legacy, engage your family in your giving program, and pass on your philanthropic values to younger generations.

They also offer some tax advantages that are particularly valuable if you want to reduce a larger-than-usual tax bite in a given year.

You or your designated representative is responsible for writing checks, corresponding with grantees, keeping records, applying to the IRS for tax-exempt status, and complying with regulations.

How a Private Foundation Works

Legally, a private nonoperating foundation is a freestanding entity that you and perhaps a few other donors (often family members or business partners) establish and control in order to make philanthropic grants. The limited number of donors makes it private. Private operating foundations, by contrast, run programs, such as a school or museum (see page 23).

The donor makes an irrevocable gift to the foundation and receives a charitable income-tax deduction in the year he or she makes the gift, although the money may only pass to charity over time. The foundation's assets grow tax-free.

To preserve the foundation's tax-exempt status, you must distribute at least 5% of its assets to qualified not-for-profit organizations each year.[5] If the foundation spends more than 5% in one year, it can apply the excess to reduce grants over the subsequent five years.

The foundation may make grants to any qualified not-for-profit organization in the US whose goals are consistent with the foundation's mission or purpose. Grants to charities outside the US are also acceptable, but extensive due diligence to ensure eligibility is necessary.

Within limits, a private foundation may also make mission-related investments. For example, a private foundation seeking to combat climate change might invest in an early-stage technology company that is developing advanced batteries for storing solar power. Since the mission-related investment is likely to be illiquid and difficult to value, it could complicate the process of determining the required 5% spending rate each year thereafter.

The Opportunity Today

Today's low expected returns for stocks and bonds pose significant challenges for foundations aiming for perpetuity. Foundations must distribute 5% a year to maintain their tax-exempt status, which increases their return hurdle. If perpetuity is a goal, they must earn at least a 5% return to avoid spending down their capital—and even more, to maintain their distributions on an inflation-adjusted basis.

[5] Program-related investments count toward the 5%.

Based on our forecasts, even the most aggressive asset allocations are unlikely to achieve 5% returns, after inflation. ***Display 9*** shows our median projected returns for various mixes of global stocks and taxable bonds for the next 30 years.

The conservative portfolio, with a 30% allocation to global stocks, would return 5.3% a year on average, in our median forecast. That's enough to cover the 5% required distribution, but it would only support sustainable spending of 2.3%, assuming future inflation averages 3%. To maintain its spending power, the foundation would have to spend from principal.

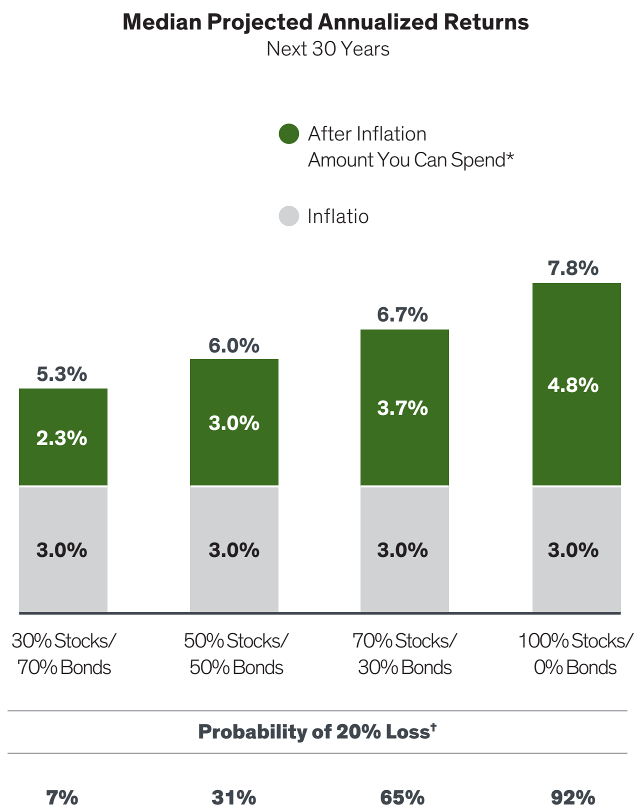
The more growth-oriented asset allocations would likely have higher returns, but even the all-stock portfolio wouldn't be able to spend 5%, on an inflation-adjusted basis.

While growth-oriented allocations generate higher returns, they also create more investment risk, defined as short-term drops in portfolio value. We estimate that there's a 92% chance that the all-stock portfolio would lose 20% from peak to trough at some point in the next 30 years, but only a 7% chance that the conservative portfolio would lose that much.

There are several ways to address the challenge of perpetuity:

- The foundation can take more investment risk, perhaps shifting from a moderate to a growth allocation, with a higher weight in stocks, if its board is comfortable with the investment risk this creates.
- The donor or other parties can make additional contributions to offset any decline in assets due to lower investment returns.
- The foundation can accept a decline in the purchasing power of its distributions.
- The foundation can decide that perpetuity is no longer paramount, and that spending down the foundation to maximize its impact over a decade or more is a more relevant strategy for it today. (See "Perpetuity or Spend-Down?" on page 24.)

DISPLAY 9: REAL RETURNS OF 5% ARE HARD TO ACHIEVE



**Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as 50% intermediate-term taxable bonds and 50% global intermediate-term taxable bonds, hedged.*

†Data indicate the probability of a peak-to-trough decline in pretax, pre-cash-flow cumulative returns of 20% over the next 30 years. Because the Wealth Forecasting System uses annual capital-market returns, the probability of peak-to-trough losses measured on a more frequent basis (such as daily or monthly) may be understated. The probabilities depicted above include an upward adjustment intended to account for the incidence of peak-to-trough losses that do not last an exact number of years. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*

Source: Bernstein

Key Considerations

The various advantages and disadvantages of private foundations are laid out in the table on page 26. Here, we explore a few key issues.

Time Horizon. Private foundations are often described as perpetual philanthropic vehicles—ones that last forever. As directors or trustees retire or pass away, successor trustees—often family members—take their place. A foundation could go on for hundreds of years, giving the family ongoing control over its assets and philanthropic program.

If you intend to pass on your private foundation to your children and grandchildren, it's critical to engage them in your giving program early—and to assess periodically whether they want to take on the responsibility when you're gone. Clients whose children are not interested in running their parents' or grandparents' foundations often shift their private foundations into spend-down mode or convert them into donor-advised funds (DAFs) that can spend down their assets within 20 years or so. (See "Perpetuity or Spend-Down?" on page 24.)

Operating Costs. Private foundations are generally more expensive to establish and run than other philanthropic vehicles, such as DAFs. Applying for tax-exempt status for a private foundation entails legal fees, and you will probably need accounting and bookkeeping services to prepare the foundation's annual tax returns.

Taxes. The tax advantage of a private foundation comes from decoupling the timing of asset donation and grant-making. For example, you can donate highly appreciated assets when you and your advisors deem appropriate, often because you face a particularly large tax bill. The foundation can sell these assets without incurring taxable gains, reinvest the proceeds, and make grants over years or decades to come.

If you fund a private foundation with cash, the maximum amount of the deduction you can use in any year is equal to 30% of your adjusted gross income (AGI); if you donate securities, the maximum deduction in one year is 20% of AGI. The deduction for gifts of private or illiquid assets may be limited to their cost basis, which in some cases could be zero. Charitable income-tax deductions above the stated limits can be carried forward for as many as five additional tax years.

Private foundations are subject to an excise tax on the income and realized capital gains they generate each year. If the foundation is managed effectively, the excise tax will be 1% of income, but if certain tests are not met, it could be 2%. Private foundations also face burdensome annual tax-filing requirements: Form 990-PF can be a long document, and its details are public, available for anyone to review.

Investment Policy. A long-term investment policy is critical to a foundation's success. To keep pace with inflation after spending 5%, a foundation typically invests the majority of its portfolio in return-seeking assets, such as stocks and high-yield bonds, with the balance in risk-mitigating assets, such as high-quality bonds and cash. Understanding the risk and return trade-offs in your foundation's asset allocation is especially important if you want your foundation to be able to step up grant-making when the economy is weak. A sound investment policy statement will give succeeding generations a road map for managing your foundation's assets. It also informs your board and investment manager on roles and responsibilities. (See "Crafting Your Investment Policy Statement" on page 48.)

Funding. Private foundations can be funded with a wide range of assets. If you are on the verge of selling a small family business, you may want to give an interest in the business to your foundation. If your company is closely held, the deduction will be limited to your cost basis. If you donate more than a minimal share to a private foundation, the IRS will consider it an "excess business holding" that you will have to remove from the foundation's balance sheet within five years. If the prospective sale of the business falls through and the holding is not removed, a stiff penalty becomes due.

Compensation of Board Members. Some private foundations provide "reasonable" salaries and benefits to board members, as defined by state law, and reimburse board members for expenses related to foundation work. Your children or other family members can be officers or directors, but paying yourself or family members requires strict adherence to detailed IRS rules (and, in some cases, state rules) to avoid legal complications and penalties for self-dealing.

Legislative Risks. Some lawmakers have attempted to reduce the value of the charitable income-tax deduction, reduce the tax advantage for growth in the foundation's portfolio, and increase the required minimum spending rate. While no significant legislation has passed since the rules for private foundations were revised in the Tax Reform Act of 1969, legislative action remains a risk.

Checklist for Establishing a Private Foundation

- ☐ Create entity documents, such as articles of incorporation
- ☐ Establish a board of directors
- ☐ Determine the foundation's charitable objectives and develop a mission statement
- ☐ Prepare and adopt bylaws and board policies, such as an investment policy statement, a spending policy, and a conflict of interest policy
- ☐ Obtain an employer identification number
- ☐ Establish a bank account
- ☐ Apply for federal tax exemption and state tax exemption, if applicable
- ☐ Register foundation with state agencies, if applicable
- ☐ Secure insurance
- ☐ Find suitable office space, if applicable
- ☐ Hire staff and develop employee manuals, if applicable
- ☐ Develop a fund-raising plan, if applicable

PRIVATE OPERATING FOUNDATIONS

Private operating foundations are sometimes referred to as "hybrids" of private nonoperating foundations and public charities. They are often established by a single family and operate charitable programs. A private operating foundation, like a private nonoperating foundation, is typically managed by a board of directors comprising the donor and members of the donor's family.

Private operating foundations use the majority of their income to operate charitable programs. They are not subject to the 5% payout requirement imposed upon private nonoperating foundations. However, the prohibitions against "self-dealing" and the Form 990-PF IRS reporting requirements applicable to private nonoperating foundations are also applicable to private operating foundations.

Gifts to private operating foundations enjoy more favorable charitable income-tax deductions than gifts to private nonoperating foundations. Charitable income-tax deductions for gifts to a private operating foundation of real estate or art not created by the donor are based on the fair market value of the real estate or art.

On the other hand, charitable income-tax deductions for gifts to a private nonoperating foundation of real estate or art not created by the donor are limited to the donor's cost basis.

At times, a family with a private nonoperating foundation may decide that the goals for the foundation would be better accomplished with a private operating foundation. Tax reasons may also make the private operating foundation attractive: Private operating foundations are not subject to the 1%–2% excise tax, as private nonoperating foundations are. Also, as discussed above, donors may receive more preferential income-tax deductions for contributions of certain assets to an operating foundation.

In any case, the family may be able to make the transition to a private operating foundation. However, the IRS requires that the foundation meet certain tests, and submit its governing documents for review. The rules surrounding a transition can be complex; please consult your tax and legal advisors.

PERPETUITY OR SPEND-DOWN?

A private foundation or donor-advised fund (DAF) is a way to establish your philanthropic intent today that allows for staged giving over time. But what does "over time" mean to you? You can spend down the assets over a given period, say, 20 years, or you can create a fund that will distribute grants in perpetuity.

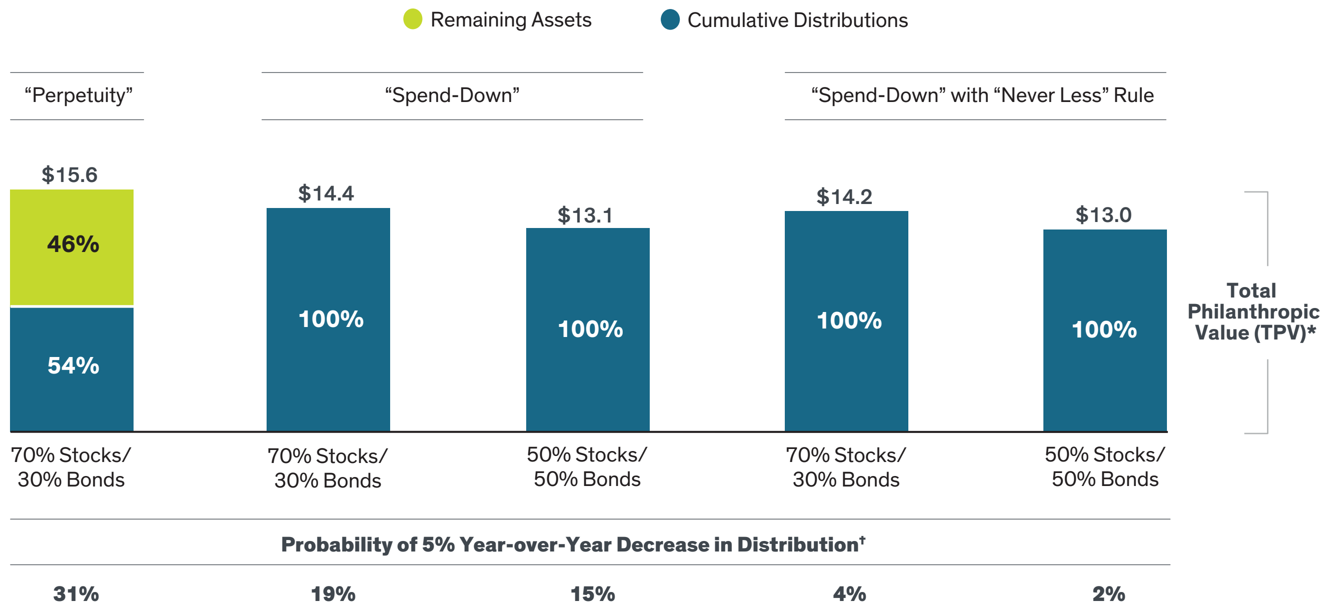
The spending policy should align with your philanthropic mission. To achieve some goals—such as earthquake reconstruction—you may want to spend down your foundation's or DAF's assets rapidly. For other goals, you might prefer to maximize how long the distributions last—or maximize the stability of distributions. Unfortunately, the investment policies that lead to longevity and stability tend to be at odds. Typically, you have to trade off between these goals.

Foundations aiming for perpetuity require a high allocation to return-seeking assets such as stocks (typically 70% or more) to generate the growth needed to sustain 5% annual distributions and stay ahead of inflation. This will likely result in greater volatility in both annual returns and distributions.

But foundations and DAFs that plan to spend down their assets have flexibility about their investment policies and can take steps to stabilize distributions, if that would serve their charitable goals.

Display 10 shows that we estimate a $10 million perpetual foundation with a 5% spending policy and a 70% stock allocation would have significantly more total philanthropic value (TPV) after 20 years than a foundation with the same asset allocation that is

DISPLAY 10: SPEND-DOWN POLICIES REDUCE TPV AND VOLATILITY OF DISTRIBUTIONS
MEDIAN FORECAST RESULTS FOR YEAR 20 ($ MILLIONS, INFLATION-ADJUSTED)



Probability of 5% Year-over-Year Decrease in Distribution†

31%	19%	15%	4%	2%

**TPV is the sum of real cumulative distributions and the real portfolio remainder value in a given year.*

†Data represent the likelihood of experiencing such a decline over the course of any one year. Distribution is defined as charitable distribution only, excluding expenses.

Initial assets of $10 million. "Perpetuity" refers to a 5% annual distribution for 20 years, and "Spend-Down" refers to linear spending from the foundation over 20 years. "Never Less" refers to the annual distributions never being less than the prior year's distribution. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as 50% intermediate-term taxable bonds and 50% global intermediate-term taxable bonds, hedged. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*

Source: Bernstein

spending down its assets. However, the foundation spending down its assets faces less risk of distributions falling 5% from one year to the next.

The foundation spending down its assets could stabilize distributions even further, if it's willing to give up some TPV. Reducing the stock allocation to 50% would lower the odds of a 5% year-over-year drop in distributions from 19% to 15%, but also reduce TPV from $14.4 million to $13.1 million. That option generally isn't available to a perpetual foundation, which needs the growth that a higher stock allocation can generate over time.

The foundation spending down its assets could also adopt a rule that it will never spend less from one year to the next, with minimal impact on its TPV, whether it allocated 70% or 50% of its assets to stocks. (The slight odds of a 5% decline in annual distributions shown capture the final year, when only a little capital may be left.)

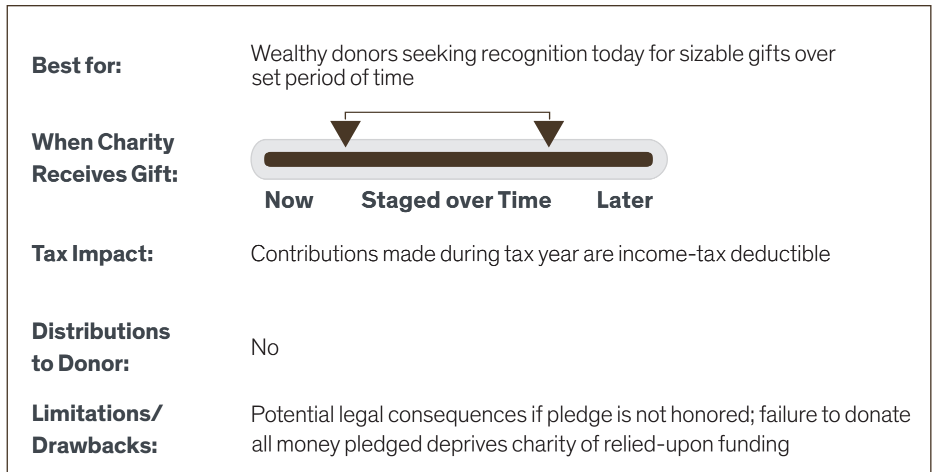
The choice is yours. If you think a drop in annual funding would be highly disruptive to the programs you support, you can reduce that risk—but it may mean granting less money over time.

DISPLAY 11: COMPARING VEHICLES FOR PURELY PHILANTHROPIC GIVING

	Donor-Advised Fund (Public Charities)	**Private Foundation** (Nonoperating)
Overview	Good fit for donors who desire fl xibility with grant-making; very little administrative burden on donor; generally cost-effective for small gifts; Bernstein provides advisory and management services and partners with sponsors	Good fit for donors who desire maximum control over gifts and assets and may wish to involve family deeply; donors must deal with administrative complexity and legal/regulatory scrutiny; Bernstein provides advisory and management services
When Charity Receives Gift	Beginning now, over time	Beginning now, over time
Income-Tax-Free Environment	Yes, assuming no unrelated business taxable income (UBTI)	Yes,* assuming no unrelated business taxable income (UBTI)
Operating Costs	Generally low, but varies among administrators	High, but declines (on percentage basis) as assets rise; includes legal fees, start-up costs; ongoing costs vary but can be significa t
Income-Tax Deductions for Contributions	Generally based on fair market value of gift; can be carried over fi e years	Generally based on fair market value of gift; can be carried over fi e years
	Deductions limited to:	Deductions limited to:
Cash	50% of adjusted gross income (AGI)	30% of adjusted gross income (AGI)
Marketable Securities	30% of AGI	20% of AGI
Private Securities	Fair market value, at 30% of AGI	Cost basis, at 20% of AGI
Excise Tax	None	1% or 2% of income
Control	Contingent on sponsor	Absolute
Funding	Fewer legal restrictions on types of noncash gifts they can receive; excess business holdings can be a challenge	Excess business holdings can be a challenge
Annual Grants	Flexible—no minimum or maximum	Required 5% distribution
Anonymity	Achievable if desired	No
Perpetuity	Contingent on sponsor	Yes
Compensation of Board Members	No	Yes
Administrative/ Compliance Burden	Minor; handled by sponsor	Can be significa t; subject to strict rules
Legislative Risks	Yes	Yes
Other Tax Issues	Can be subject to UBTI at corporate rate of 35% depending on some types of investments	Can be subject to UBTI at corporate rate of 35% depending on some types of investments
Beneficiary of IRA	Yes	Yes
Lead Beneficiary of CLAT	Yes	Yes, but requires careful documentation
Remainder Beneficiary of CRT	Yes	Yes

**There is an excise tax of 1%–2% on net investment income.*
Source: IRS and Bernstein

Charitable Pledges



Structuring a charitable gift as a pledge is a way to make a significant gift to your favorite not-for-profit organization in installments. Charities accept pledges because they realize that some donors are more comfortable making sizable gifts over time.

A pledge is an agreement between you and a charity that you will make a gift to the charity over a set period of time. Only contributions made during the tax year are deductible. Thus, if you pledged this year to donate $100,000 to your favorite charity but paid the charity only $25,000 by December 31, you can deduct only $25,000 this year.

Before you commit to a charitable pledge, be sure you are comfortable with locking in your obligation. If you know that you want to make a sizable charitable gift but are not comfortable picking just one charity, a gift to a donor-advised fund (DAF) or a series of gifts may make more sense for you.

Failure to donate all the money pledged may deprive the charity of funds upon which it relied for programs or capital expenditures. If the pledge is structured as a legally enforceable contract, under certain circumstances the charity can sue you or your estate to recover the unpaid portion of the pledge.

While charitable pledges can provide valuable benefits to you and your favorite charity, they can be complex. Consult with competent tax and legal counsel before you promise to pay a charitable pledge to make sure your interests are protected. Note that a DAF cannot benefit the donor by satisfying the donor's obligation to fulfill the pledge.

COMPELLING COMBINATIONS: DONOR-ADVISED FUNDS AND PRIVATE FOUNDATIONS

Some donors think they have to choose between creating a private foundation and a donor-advised fund (DAF). But to achieve some goals, it may make sense to create both.

For example, let's say your required distribution from your private nonoperating foundation is higher this year due to strong market performance. You don't have an additional grant lined up, and you need a little more time to decide where to send the money. Creating a "sister" DAF can make this possible.

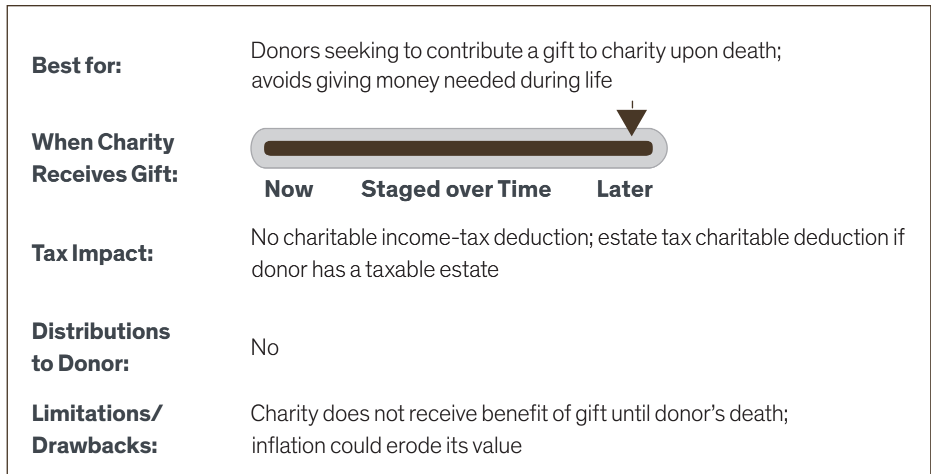
If the foundation has $10 million in assets and a minimum required distribution of $500,000, you could grant $400,000 to the qualified not-for-profit organizations that you've already identified and $100,000 to your sister DAF. Then, you could take your time in deciding how to advise the DAF administrator to distribute the $100,000.

While the private foundation and DAF are legally separate entities, you might view your combined balance sheets as a single pool of philanthropic capital that you can manage with this kind of transfer. Keep in mind, though, that grants between private foundations and DAFs are a one-way street running from foundations to DAFs, not vice versa.

The combination of a private foundation and a DAF would also allow you to make an anonymous grant from time to time. While the foundation itself cannot conceal its identity, you can grant part of the foundation's 5% annual distribution to your sister DAF, which can make an anonymous grant.

You can make additional contributions to either entity over time. If you have both, you can generate higher charitable income-tax deductions by donating certain assets, such as real estate and privately held securities, to the DAF. You can deduct only the cost basis of these assets if you donate them to a private foundation; you can deduct their fair market value if you donate them to a DAF.

Bequests



Best for:	Donors seeking to contribute a gift to charity upon death; avoids giving money needed during life
When Charity Receives Gift:	Now / Staged over Time / **Later**
Tax Impact:	No charitable income-tax deduction; estate tax charitable deduction if donor has a taxable estate
Distributions to Donor:	No
Limitations/ Drawbacks:	Charity does not receive benefit of gift until donor's death; inflation could erode its value

When you make your charitable gift is often as important as how much you give. It may make sense to hold off giving a large chunk of assets now to your favorite cause and instead write it into your estate plan, to ensure you can cover your expenses for as long as you live. But, from the not-for-profit's perspective, a gift in hand is worth two in the bush. Many promised gifts never arrive, and inflation often reduces the spending power of gifts that arrive after many years of waiting.

It's important to analyze your estate's charitable-giving capacity, just as it's important to analyze your capacity to make lifetime gifts. We can help you determine how much of your estate to earmark for philanthropy, given your other goals, such as providing for your family.

Here are three key ways to provide for charity in your estate plan:

Wills/Living Trusts. If you make a not-for-profit organization a beneficiary of your will or revocable trust, the gift passing to charity at your death qualifies for the unlimited estate tax charitable deduction.[6] Thus, the gift can reduce, and in some cases eliminate, tax on your estate. The gift can be general or directed to a specific program or cause. You can also establish a charitable remainder trust (CRT) or charitable lead trust (CLT) as part of your estate plan. Note, however, that the success of both strategies is uncertain, because it will be driven by the prevailing interest rate when the trusts are funded from your estate. (See "Charitable Lead Annuity Trusts," page 31, and "Charitable Remainder Trusts," page 35, for more details.)

Individual Retirement Accounts (IRAs). If you wish to leave some assets in your estate plan to family and some to a not-for-profit, it often makes sense to make the not-for-profit the IRA beneficiary, since it will not have to pay income tax on the IRA distributions. By contrast, IRA distributions to you during your lifetime and to your taxable beneficiaries after your death are taxable at ordinary income-tax rates. (You can also give to charity from your IRA late in life; see page 13.) It's less desirable to donate a Roth IRA to charity; because you contributed to the Roth IRA on an after-tax basis, the distributions are tax-free.

Insurance Proceeds. Naming your favorite charity as a beneficiary of your life insurance can provide the charity with liquid funds fairly soon after your death. This makes sense if your family does not need the proceeds to pay estate taxes or other expenses.

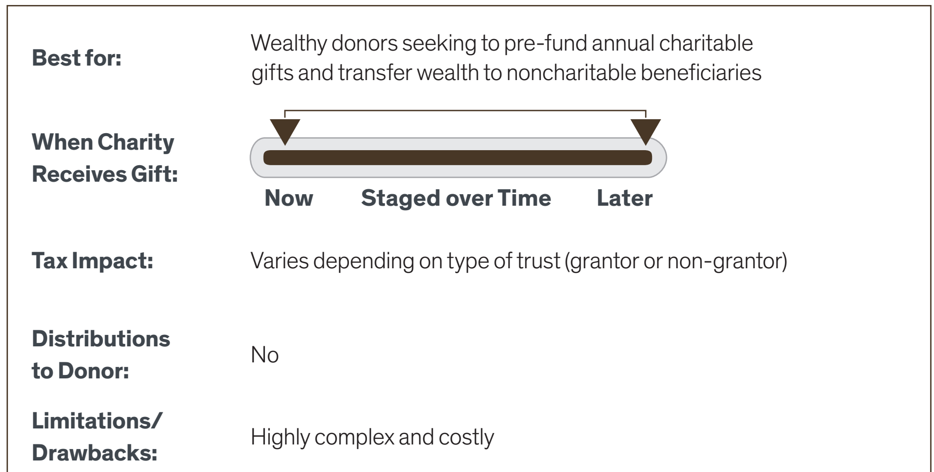
[6] Code Section 2055(a)(2)

PARTLY PHILANTHROPIC STRATEGIES

“As I give, I get.”

—Mary McLeod Bethune

Charitable Lead Annuity Trusts



Best for:	Wealthy donors seeking to pre-fund annual charitable gifts and transfer wealth to noncharitable beneficiaries
When Charity Receives Gift:	Now / Staged over Time / Later
Tax Impact:	Varies depending on type of trust (grantor or non-grantor)
Distributions to Donor:	No
Limitations/ Drawbacks:	Highly complex and costly

A charitable lead annuity trust (CLAT) allows you to pre-fund annual gifts to charitable organizations and may also transfer wealth to your children or other noncharitable beneficiaries, free of transfer tax. Some structures can also reduce income taxes. Setting up a CLAT can be costly, and as a result, CLATs are typically most economical for sizable contributions.

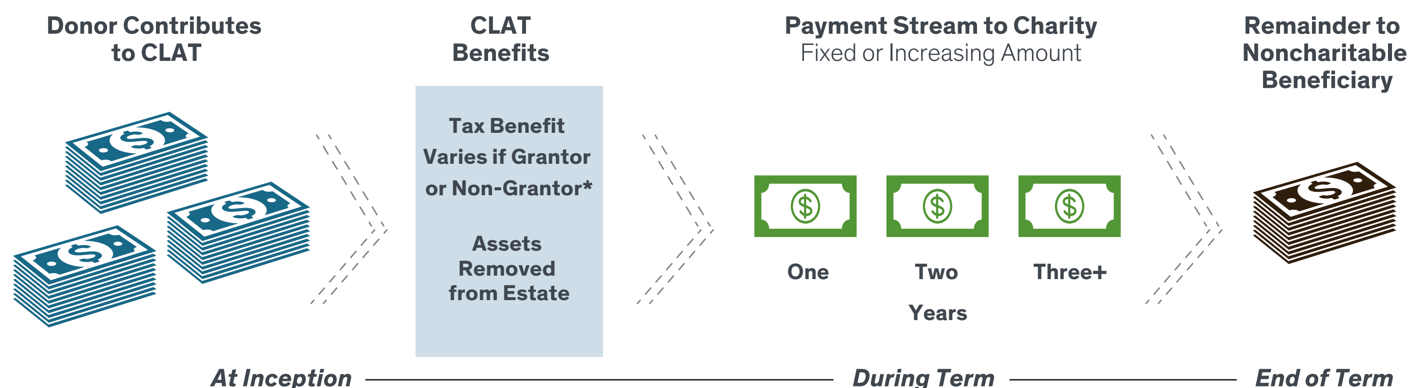
How the Strategy Works

You establish a CLAT by making a large gift to a trust, which will typically distribute all of its principal plus interest over time to one or more qualified charities of your choice (***Display 12***). The gift is usually irrevocable. (In some CLATs, the remainder reverts to the grantor at the end of the trust term.) The benefit of making an irrevocable gift is that the assets are permanently removed from your estate for estate tax purposes.

A CLAT is designed to make charitable distributions for many years, so in effect it's a way to pre-fund charitable donations. For example, someone who typically gives $50,000 a year to charity can pre-fund a 20-year CLAT today with $833,573.[7] That's less than $1 million (20 annual gifts of $50,000) because the IRS assumes a modest investment return.

When the trust expires, any remaining assets pass to taxable beneficiaries, typically children or a trust for their benefit, free of gift and estate tax.

DISPLAY 12: HOW A CHARITABLE LEAD ANNUITY TRUST WORKS

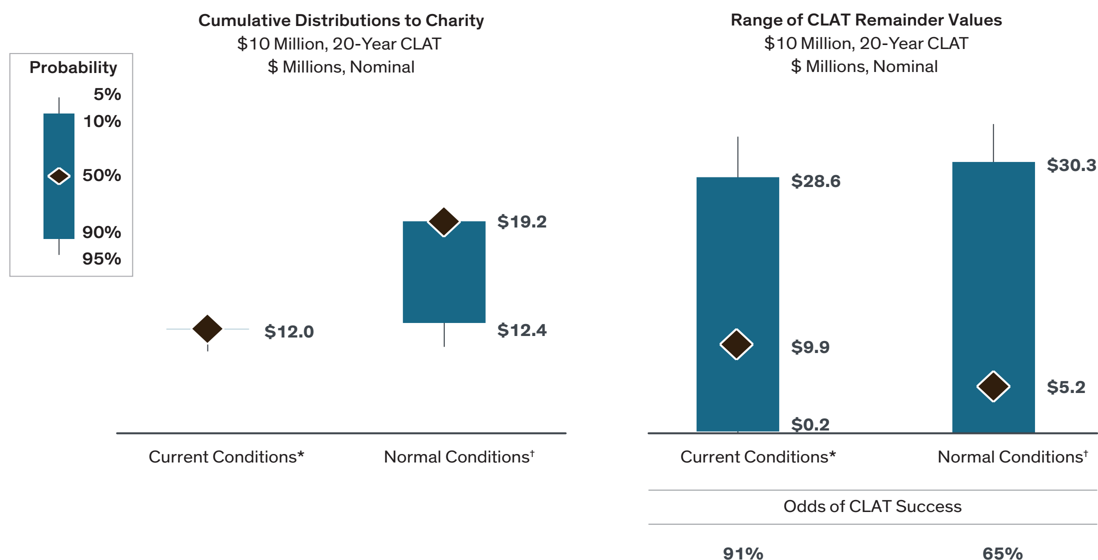


**A non-grantor CLAT is not exempt from income taxes but is entitled to an annual charitable deduction equal to the lesser of the annuity distribution to charity or the trust's income. There is no charitable income-tax deduction for the donor. A grantor CLAT is a grantor trust, and the grantor is responsible for any income tax generated by the assets in the trust. In the year he or she makes a contribution to the CLAT, the grantor receives a charitable income-tax deduction based on the size of the contribution; the deduction can be carried forward for five years.*

Source: IRS and Bernstein

[7]Assumes a zeroed-out CLAT, with level annuity payments and a 1.8% 7520 rate.

DISPLAY 13: TODAY'S LOW INTEREST RATES BOOST ODDS OF SUCCESS FOR CLATS



*Reflects Bernstein's estimates and the capital-market conditions as of March 31, 2016. CLAT is zeroed-out, assuming a 1.8% Section 7520 rate.

†Bernstein's estimates of capital-market equilibrium, which assumes all assets are fairly priced. CLAT is zeroed-out, assuming a 7.2% Section 7520 rate, which represents our projected median 7520 rate in 20 years.

Assumes a non-grantor CLAT with level annuity payments each year for 20 years and includes the impact of the income-tax deductions non-grantor CLATs receive for every dollar distributed to charity each year. "Odds of CLAT Success" is defined as remainder interest >$1. CLAT is allocated 80% to global stocks and 20% to bonds. Global stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as 50% intermediate-term taxable bonds and 50% global intermediate-term taxable bonds, hedged. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*

Source: IRS and Bernstein

The Opportunity Today

Today's extremely low interest rates reduce the annual charitable donations required and increase the odds of transferring assets to your children tax-free with a CLAT. The Section 7520 rate is the "hurdle rate" that applies to newly established CLATs and is applied to annuity payments paid each year to charity. Any remaining assets after making all annuity payments pass to the noncharitable beneficiaries. This rate was just 1.8% in June 2016, compared to its 5.5% average since the IRS established it in 1989.

Display 13 shows how attractive CLATs are now as a wealth transfer vehicle, compared to under normal initial conditions. In this example, a donor funded a $10 million non-grantor, zeroed-out CLAT for a 20-year term (see the definitions on the next page). He invested 80% of the trust's assets in global stocks and 20% in taxable bonds. Under current conditions, we project that there's more than a 90% chance that the CLAT will make its distributions to charity and pass wealth to the donor's kids.

There's no range of distributions, since the payments are fixed, based on today's 7520 rate: The CLAT will distribute $12 million to charity over 20 years. There is a range of potential remainder values, however, which will depend on capital-market conditions. In the median case, indicated by the diamond in the left-hand blue bar, the CLAT will have $9.9 million remaining for the children at the end of 20 years.

Under normal conditions, interest rates are much higher, and there's only a 65% chance that the CLAT will make its distributions to charity and pass wealth to the kids. A wide range of distributions is possible, based on our projections of normal 7520 rates; in the median case, the CLAT's cumulative distributions to charity would be higher ($19.2 million over 20 years). The median remainder value would be lower than under current conditions, with $5.2 million of wealth remaining for the kids.

Key Decisions

CLATs are complex, vary widely in structure, and are relatively expensive to set up and maintain. ***Display 14, next page,*** lists some key decisions you must make, and the impact of these decisions on the charity and the donor or taxable trust beneficiary. Here, we provide a bit more detail on a few strategies.

A ***non-grantor*** CLAT is a separate tax-paying entity subject to the income-tax rules associated with trusts. As the donor, you do not get a personal income-tax deduction after the initial donation, but the trust itself can deduct its annual payments to the charity against its income or gains, usually eliminating any tax due.

Most commonly, non-grantor CLATs are created upon the donor's death as part of an estate plan. The CLAT may be "zeroed-out" so that the value of the assets contributed to the trust is exactly equal to the present value of annuity payments made to the charity, which eliminates potential estate tax.

A ***grantor*** CLAT passes all trust income and expenses through to you for income-tax purposes. Hence, when you establish the CLAT, you can take an immediate income-tax deduction for the present value of the payments to be made by the trust to the charity. Minimizing income taxes (in addition to future transfer taxes) is especially valuable if you create the trust in a year when your tax bill would otherwise be unusually high, perhaps as a result of selling your business. Grantor CLATs may also be "zeroed-out" for transfer-tax purposes.

Note: If you receive the immediate income-tax deduction, you will not receive an annual charitable income-tax deduction when the trust makes payments to the charity. Furthermore, if you do not survive the trust term, the IRS may recapture part of the up-front income-tax deduction, and the CLAT will be taxed as a non-grantor trust.

Back-Loading

Unlike other partly philanthropic trusts, CLATs are not subject to minimum or maximum payout requirements. The annuity payment to the charity can be "back-loaded," starting low and increasing by a stated amount. Back-loading keeps more assets within the trust to grow, which benefits the noncharitable beneficiaries but delays distribution of assets to the charity. Analysis is required to see if back-loading aligns with your charitable goals or is likely to have a negative tax impact, or both.

Asset Allocation

The asset allocation challenge with CLATs is to balance the promise to deliver all the payments to the charity with the desire to generate additional growth that can be passed on to your family. If the CLAT takes too much risk and the market falls, the trust may "fail." That is, it may not deliver the intended amount to the charity, and the beneficiaries will get nothing. If it takes too little risk, the charity may have a better chance of receiving the payment intended, but the beneficiaries are more unlikely to get anything.

If the CLAT has 10 or more years remaining, a growth-oriented allocation with a sizable allocation to global stocks is generally appropriate. Diversifying investments, such as hedge funds, may enhance the overall risk/return trade-off of the portfolio.

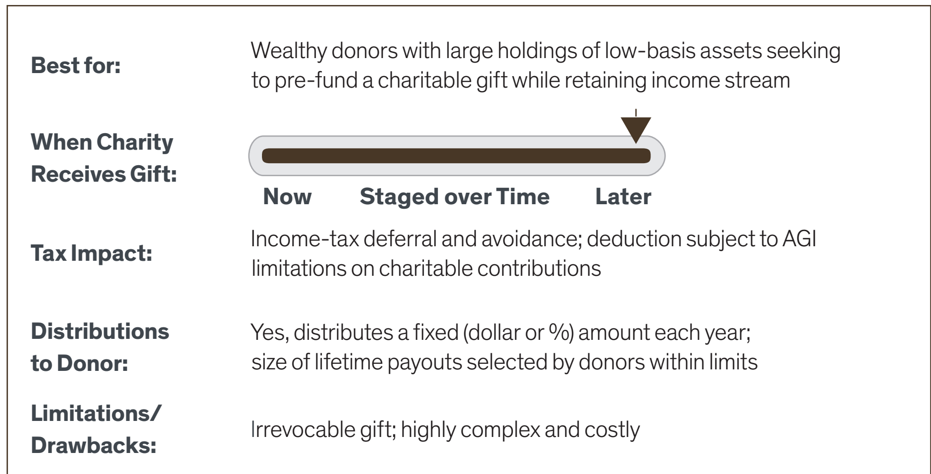
The trustee may make allocation changes during the trust term to help secure a "win" for the noncharitable beneficiaries and ensure that the charity receives its payments. Careful analysis is needed.

DISPLAY 14: THE IMPACT OF KEY CHARITABLE LEAD ANNUITY TRUST (CLAT) DECISIONS

	Impact to Donor/Beneficiary	Impact to Charity
TYPE OF CLAT		
Non-Grantor	No charitable income-tax deduction for donor; the trust gets a deduction each year	Potential for tax inefficienc and less wealth transferred
Grantor	Charitable income-tax deduction in year of contribution; grantor pays annual income taxes	Because the grantor pays income taxes, the odds are greater that the charity will receive all the payments promised
TRUST TIMING		
Funded at Death	Significa t estate-tax savings	Non-grantor CLAT; potential for tax inefficienc /less wealth to charity
Funded During Life	Donor can observe the impact of charitable gifts; possible income-tax deduction	Charity receives benefit soone
TRUST TERM		
Shorter	More immediate benefit to beneficiar , but wealth transfer may be smaller	Charity receives value of gift sooner
Longer	Delayed benefit to beneficiar , but potential for more wealth	Greater probability of receiving full benefit f gift
PAYOUT STRUCTURE		
Fixed Annuity	Lower wealth transfer to beneficiarie	Charity receives benefit soone
Back-Loaded Payments	Allows assets to work longer, allowing for possible increase in wealth transfer	Charity receives majority of benefit la er
ASSET ALLOCATION		
Best Type of Assets	High-basis assets	High-basis assets

Source: Bernstein

Charitable Remainder Trusts



Charitable remainder trusts (CRTs) can be viewed as a way to pre-fund a charitable gift while retaining income for yourself or another beneficiary for life or a term of up to 20 years. They are also an effective way to sell an appreciated asset while deferring and potentially reducing taxation on the resulting capital gains. For many donors, CRTs offer the opportunity to make a sizable contribution to charity at little, if any, cost to personal wealth.

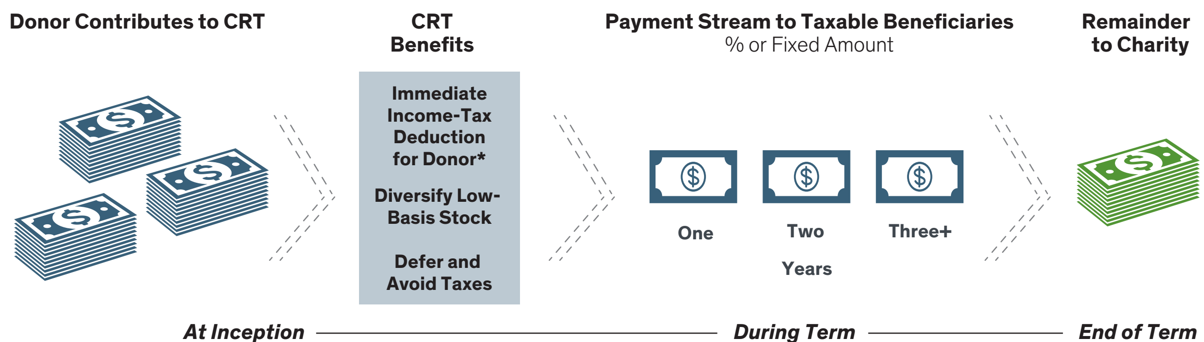
While the tax savings can be large, setting up a CRT can be costly, and there are ongoing legal and accounting fees. As a result, CRTs are typically most economical for sizable contributions. Some charities offer to serve as co-trustees of CRTs, which can lower costs to the donor.

How the Strategy Works

The donor makes an irrevocable gift to a trust that subsequently makes taxable payouts to the donor or another designated beneficiary (***Display 15***). The donor receives a charitable income-tax deduction for a percentage of the initial gift, equal to the portion of the trust's initial assets that the IRS assumes will go to charity. This amount is based on a calculation that incorporates current interest rates and the beneficiary's life expectancy or the trust's term. When the term ends, any remaining assets pass to charity.

The strategy works best when you contribute assets with a low tax basis, such as highly appreciated stock, that the trust subsequently sells to reinvest in a diversified portfolio. If you have a concentrated position in the stock, this can reduce your concentration risk and potentially reduce and defer capital-gains tax due. The appreciated assets are removed from your estate, so no estate tax is due on the assets at your death.

DISPLAY 15: HOW A CHARITABLE REMAINDER TRUST WORKS



**The income-tax deduction is not the total amount contributed, but rather the present value of what is expected to pass to charity. The calculation of the present value takes into account the value of the contributed assets, the discount rate (based on the Section 7520 rate), and the term of the trust (for lifetime trusts, a life expectancy table is used). See Sections 7520 and 664 of the Internal Revenue Code of 1986, as amended, and the Treasury regulations thereunder.*

Source: IRS and Bernstein

Typically, the trust immediately sells the appreciated position. Since the trust is a charitable entity, it does not pay tax on the capital gain. Instead, the income beneficiary pays taxes on the payouts, based on how the income was earned in the trust—as interest, dividends, or short- or long-term capital gains. Generally, the IRS requires that the most highly taxed type of income comes out first.

Careful portfolio management can avoid generating highly taxed income so that only qualified dividends and long-term capital gains, which are taxed at the lowest rates, are distributed from the trust each year.

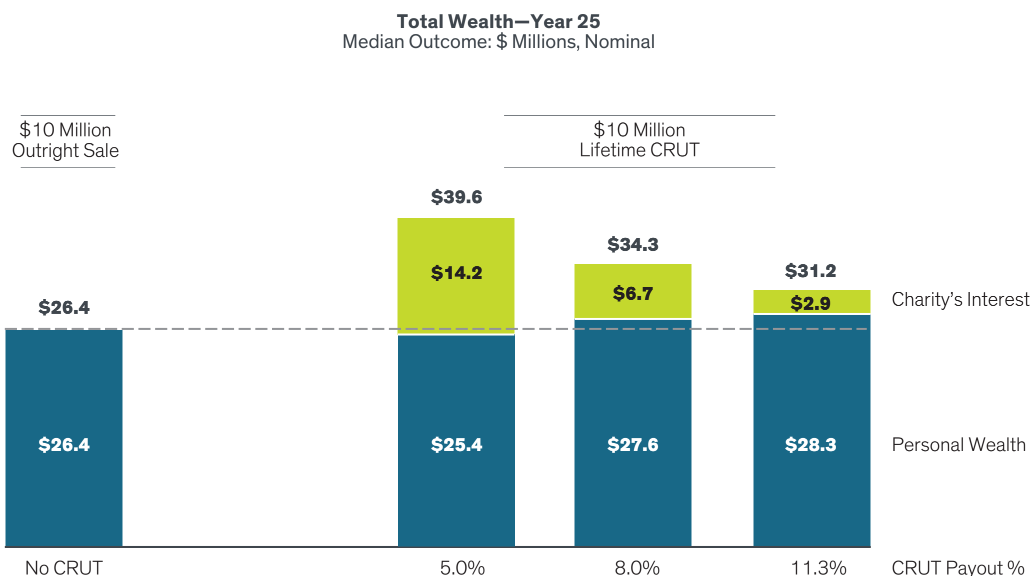
The Opportunity Today

Higher tax rates increase the benefit of the up-front income-tax deduction and of deferring recognition of capital gains. Thus, the tax benefit of a CRT increased in 2013, when top federal tax rates on ordinary income and long-term capital gains (including the net investment income tax) rose to 43.4% and 23.8%, respectively. State rates can lift taxes higher.

The benefit can be very large for the charity and both the donor or other income beneficiary; how large depends on the payout rate, the trust term, and the tax basis of the stock, as well as capital-market returns. To quantify the potential benefit, we sum the values of the charitable income-tax deduction, after-tax payouts, and wealth generated by reinvesting both, and compare it to the after-tax proceeds of selling the stock and reinvesting the proceeds in a taxable environment.

Display 16 illustrates this for a charitable remainder unitrust (CRUT), which pays out a percentage of principal each year to a 65-year-old couple. The couple funded the CRUT with $10 million of zero-basis stock that they still held from founding their company. The display shows the projected median value of the portfolio in year 25, with and without a CRUT. The blue bar labeled "No CRUT" shows that the couple's portfolio would be worth $26.4 million if they sold the stock, paid tax, and reinvested without a CRUT. The stacked bars at right show the value of the portfolio with a CRUT, divided between the couple's personal wealth from receiving annual CRUT payments and the charity's interest, for three different payout rates.

DISPLAY 16: CRUT HELPS CHARITY AT LITTLE OR NO COST TO DONOR'S PERSONAL WEALTH



The CRUT is based on a 65-year-old couple contributing $10 million in zero-basis assets to a lifetime CRUT with annual payouts. Assumes investor is subject to top federal tax rates and state income taxes of 6.5%. All calculations of permissible payouts and associated tax deductions are according to Sections 7520 and 664 of the Internal Revenue Code of 1986, as amended, and the Treasury regulations thereunder. The CRUT and personal portfolios are allocated 70% to global stocks and 30% to bonds. Global stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as intermediate-term municipal bonds. The above figures assume charitable deductions of $3,391,800 for the 5% CRUT, $1,849,900 for the 8% CRUT, and $1,000,200 for the 11.3% CRUT. In all scenarios, the deduction is used to offset ordinary income and is assumed to be used in the first six years of the analysis. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*

Source: Bernstein

If the trust terminates in the early years, the charity is likely to receive the lion's share of the benefit, whether the annual CRUT payout is 5%, 8%, or the maximum distribution of 11.3% a year for a joint lifetime CRUT for people their age. But as the donors reap the benefit of the tax deferral, their personal wealth approaches—and eventually eclipses—the amount they would have had without a CRUT. We call this the "crossover" point.

Whether or not the CRUT reaches "crossover," it typically creates more total wealth when you factor in the remainder benefit to charity. In this example, the portfolio with a 5% CRUT payout would have a median total worth of about $39.6 million, including the charity's interest, even though the CRUT hasn't reached the crossover point.

The charity will always receive a larger remainder if the CRUT pays a lower percentage rate to the donor than if it pays a higher rate. But after about 25 years, the payout rate makes little difference to the donor's personal wealth; the donor may even benefit slightly more from a lower payout.

Key Decisions

Timing. The charity is unlikely to receive any financial benefit for many years, particularly from a lifetime CRT. Does the charity that you want to support need the money now, or can it wait? If the cause needs the money sooner, another strategy might be better.

Payout Rate. CRUTs must pay out at least 5% of principal a year, recomputed annually, and no more than 50% of the initial fair market value of the trust's assets. At least 10% of the initial asset value on the date of contribution must be left to charity. The higher the payout, the lower the donor's charitable income-tax deduction, and vice versa. Our research has shown that for lifetime CRUTs, lower unitrust percentages provide a more balanced expected benefit for the donor and charity; over very long periods of time, they also tend to create more personal wealth for the donor than a higher payout percentage.

Type of CRT. Charitable remainder unitrusts (CRUTs) pay out a percentage of principal, revalued annually; the charity and donor/income beneficiary share the benefit of up markets and bear the losses in down markets. Charitable remainder annuity trusts (CRATs) pay a fixed dollar amount each year, and the charity gets the benefit of up markets and bears the losses of down markets.

CRUTs are more common. With today's low interest rates, it is difficult for lifetime CRATs to meet the IRS requirement that at least 10% of the initial asset value go to charity. They are now available only to donors/beneficiaries over age 71 if single, or age 74 if a joint-lifetime CRAT.[8]

Cost Basis. Low-basis assets are generally excellent candidates for funding a CRT. The lower the cost basis, the more powerful the benefit of tax deferral, and the earlier the expected date for crossover. The benefits diminish as the tax basis of the stock rises. For example, if you donate a stock with a 50% basis, it may take many years to reach crossover. If you donate a stock with a higher basis, you may never reach crossover. If crossover isn't a concern because you are not focused on maximizing your personal wealth, cost basis is less important.

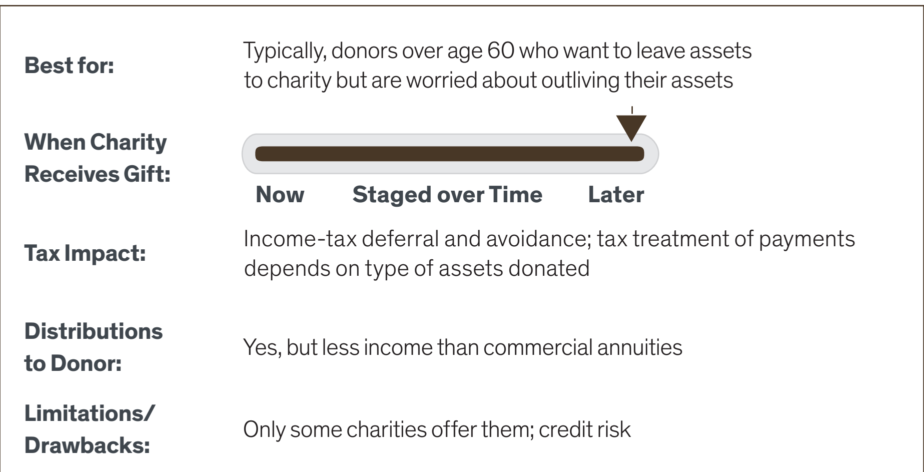
Asset Allocation. In most cases, CRT assets should be invested with an overweight to stocks to take maximum advantage of the tax-deferral benefit. Some bond exposure is advisable to preserve principal in down markets and lower the volatility of payouts. If the trust is deferring long-term capital gains, you may want to avoid investing in taxable bonds or real estate investment trusts (REITs), which are taxed at higher, ordinary income rates.

Assets to Give. A CRT can also help you to defer gains on the sale of other low-basis assets, such as artwork or real estate, but some charities will not accept artwork or real estate, and the charitable deduction for such gifts may be limited to their cost basis. There are many other complexities to consider.

Designated Charity. CRTs often do not distribute the remainder to a not-for-profit for decades; the not-for-profit that you may designate might not exist when the distribution occurs. Thus, some CRTs authorize the trustee to designate another not-for-profit to receive the remainder if the one originally designated no longer exists or is no longer qualified. In some CRTs, the grantor can designate another charity in his or her lifetime.

[8]On August 8, 2016, the IRS offered an alternative provision to the existing 10% calculation: If a CRAT annuity payment would cause the trust corpus to fall to less than 10% of the initial contribution to the trust, the trust would terminate prior to the annuity payment, and any remainder would be paid to the charitable beneficiary. This provision could allow younger noncharitable beneficiaries to contribute to a "lifetime" CRAT, with the understanding that the trust may terminate at some point before the end of that lifetime.

Charitable Gift Annuities



Best for:	Typically, donors over age 60 who want to leave assets to charity but are worried about outliving their assets
When Charity Receives Gift:	Now — Staged over Time — Later (indicator at Later)
Tax Impact:	Income-tax deferral and avoidance; tax treatment of payments depends on type of assets donated
Distributions to Donor:	Yes, but less income than commercial annuities
Limitations/ Drawbacks:	Only some charities offer them; credit risk

Charitable gift annuities (CGAs) are useful vehicles for donors who want to leave assets to charity but worry that they'll need the assets if they live much longer than expected.

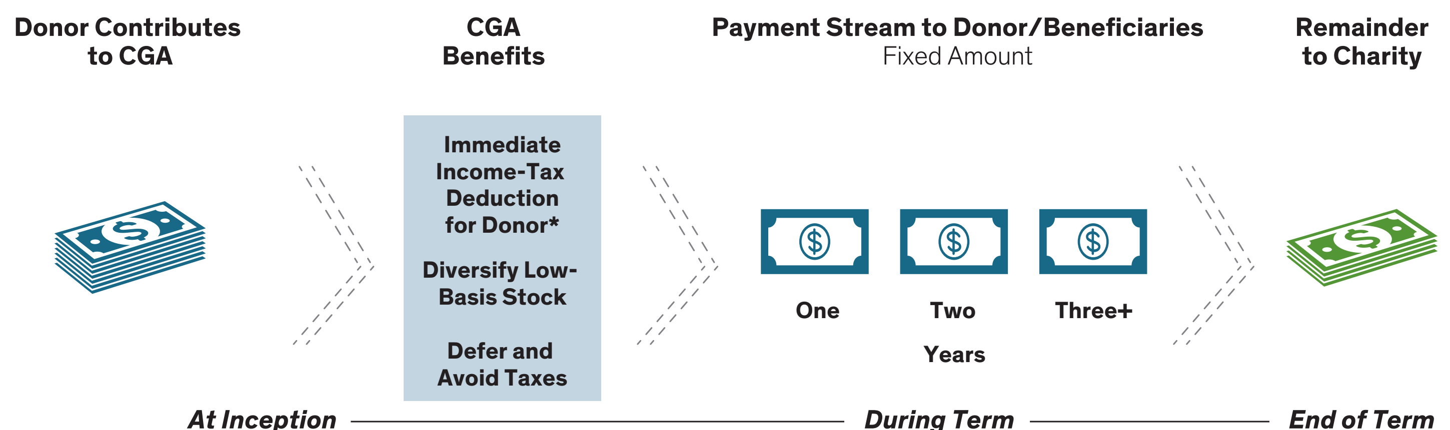
Like the commercial annuities sold by insurance companies, CGAs are a kind of longevity insurance: They protect you (or another designated beneficiary) against the risk of outliving your assets by promising a stream of annual payments for as long as you live. But unlike commercial annuities, which assume that no principal will be left at your death, CGAs are designed to leave some principal for charity. For this reason, charities that offer CGAs distribute less income to annuitants than commercial annuities; the yield give-up creates the charitable contribution.

How the Strategy Works

Not-for-profit organizations establish CGAs to provide a low-cost way for people to donate relatively small amounts (say, less than $100,000). The donor receives fixed payments for as long as he or she lives, and can take a charitable income-tax deduction in the year of purchase for the amount contributed minus the present value of the future annuity payments, based on his or her life expectancy. After the donor's death, any remaining assets pass to the not-for-profit (***Display 17***).

The annuity rate that the not-for-profit sets[9] and the donor's subsequent life span determine how the annuity's value is distributed between the donor and the charity. For most CGAs, the income beneficiary must be at least 60 years old.

DISPLAY 17: HOW A CHARITABLE GIFT ANNUITY WORKS



*The income-tax deduction is calculated pursuant to Sections 7520 and 170 of the Internal Revenue Code of 1986, as amended, and the Treasury regulations thereunder.
Source: IRS and Bernstein

[9] Most charities use the rates recommended by the American Council on Gift Annuities.

For example, a 70-year-old donor who buys a CGA with a 5.1% fixed payout would be entitled to a charitable deduction equal to 36% of the annuity's value. If the donor dies at 75, younger than the actuarial tables predict, he will receive less than one-third of the annuity's value in distributions, and the charity will receive more than two-thirds. But if the donor dies at 95, older than the actuarial tables predict, he'll get more than two-thirds of the value of the annuity, and the charity will get less than one-third.

If the donor lives long enough, the charity might receive nothing at all. That's the risk the charity takes, which it seeks to diversify by selling annuities to many different people.

The Opportunity Today

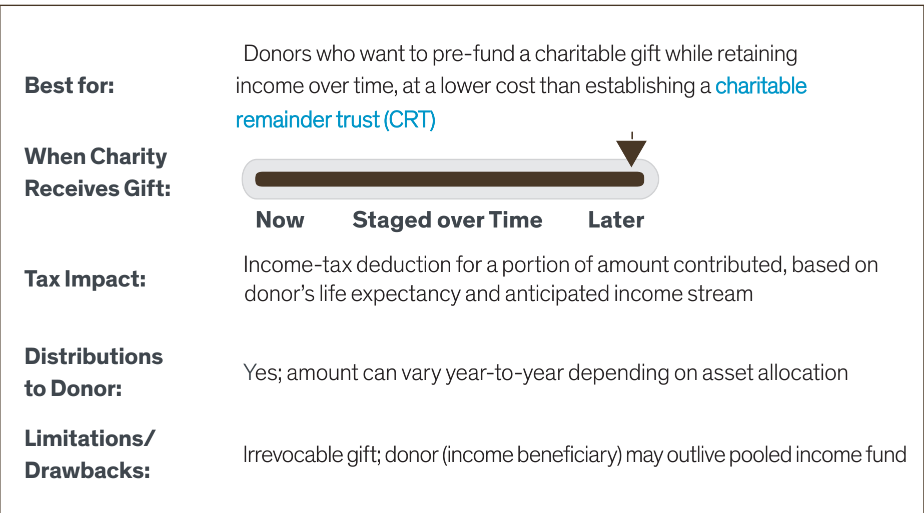
For the donor, today's low interest rates mean that CGAs currently offer historically modest income streams. While current annuity rates of 5% to 6% may seem attractive compared to high-quality bond yields, if you buy a bond, you retain the principal. With a CGA, you give up access to the principal: You're giving it to the not-for-profit. The CGA is attractive if the 5% to 6% payout meets your needs, you can use the tax benefit, and you want to support the not-for-profit.

Key Decisions

Assets to Give. For donors of low-basis assets, a CGA can provide additional tax benefits because the donor will not recognize a capital gain immediately. Instead, a portion of the annual payments will be considered capital gains, and a portion will be considered ordinary income. If you contribute cash, a portion of the annuity payments will be treated as tax-free return of principal, and a portion as ordinary income.

CGA Sponsor. Like any insurance product, CGAs also pose credit risk. If many donors live longer than the not-for-profit sponsor expected when it priced the annuities, the sponsor may be unable to keep making the payments promised. Donors who want to buy a CGA should select a not-for-profit in good financial health. Public charities must provide financial information on IRS Form 990, which can be accessed online via sites such as *GuideStar* and *Charity Navigator*.

Pooled Income Funds



Pooled income funds (PIFs) require the least time and effort from donors but are far less widely used than other partly philanthropic strategies. As their name suggests, they are collective vehicles. A public charity establishes a charitable trust to invest irrevocable contributions from many donors.

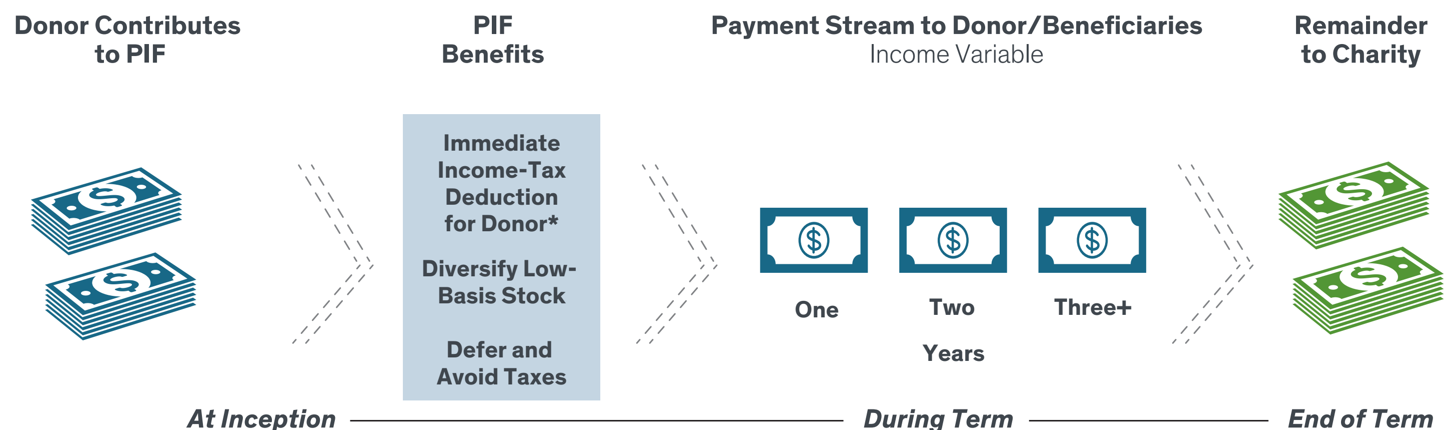
How the Strategy Works

Donors receive income-tax deductions in the year they make the contributions, equal to a portion of the amount contributed, based on their life expectancy and the anticipated income stream. If the donation is an appreciated asset, such as low-basis stock, the donor avoids capital-gains tax and receives an income-tax deduction.

The charity distributes the dividends, interest, and, in many cases, short-term capital gains from the fund to donors in proportion to the size of their contributions. Long-term capital gains are generally added to the fund's principal, which eventually passes to the charity. The income distributions are likely to vary from year to year.

Depending on the asset allocation and market conditions, the income can be substantial. Income distributions are typically taxed as ordinary income. After each donor's death, an amount equal to his or her contribution to the pooled income fund passes to the charity (***Display 18***).

DISPLAY 18: HOW A POOLED INCOME FUND WORKS



**The income-tax deduction is calculated pursuant to Sections 7520 and 642 of the Internal Revenue Code of 1986, as amended, and the Treasury regulations thereunder.*
Source: IRS and Bernstein

INVESTMENTS

"Growth is never by mere chance; it is the result of forces working together."

—James Cash Penney

Time Frame Matters

Whether you are the trustee of a charitable vehicle or the fiduciary of a qualified charity, you may be responsible for making prudent investment decisions. Here, we briefly review the key attributes of stocks, bonds, and cash, and how they can work together to support your philanthropic mission. As ***Display 19*** shows, time frame is generally a critical issue when making investment decisions.

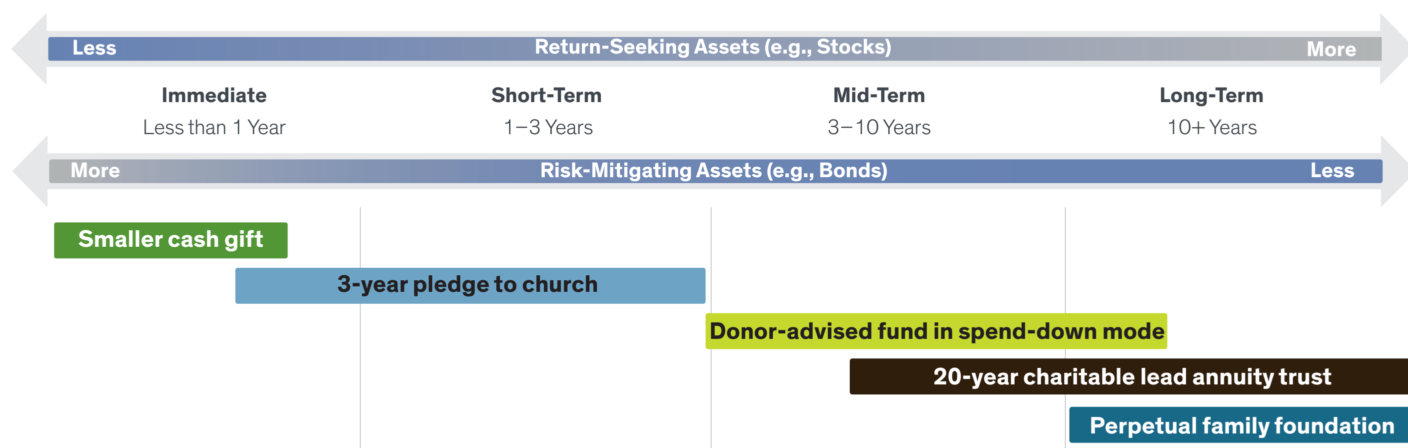
Stocks tend to perform best over the long term, but over shorter time periods, stock returns can vary widely. High-quality bond returns are far more predictable year-to-year but are generally lower than stock returns over long periods. Since you can't know for sure what will happen, the right asset allocation for your philanthropic plan will depend on the time frame for your giving strategies, as well as your appetite for return and risk.

If you plan to use the money to fulfill near-term grants or to make small but numerous gifts throughout the year, it generally makes sense to allocate the money to cash instruments or fairly short-term bonds. Over longer horizons, holding cash can have a cost, especially if you consider the potential impact of inflation.

Asset Allocation for the Long Term

For many philanthropic strategies, the money will be invested for longer time horizons. You may have a donor-advised fund (DAF) that you expect to spend down over 10 years—and a 20-year investment horizon for your charitable lead annuity trust (CLAT). If you want to endow a foundation for perpetuity, your horizon may be longer still, perhaps for multiple generations.

DISPLAY 19: IDENTIFYING THE TIME HORIZON—AND ASSET MIX—FOR YOUR GIFTS



Source: Bernstein

If you establish a private nonoperating foundation for perpetuity, you need to aim for investment returns that will cover the foundation's required 5% spending, plus inflation. To accomplish this goal, you are likely to need a substantial allocation to return-seeking assets (such as stocks), as well as a modest allocation to real assets or inflation-protected bonds.

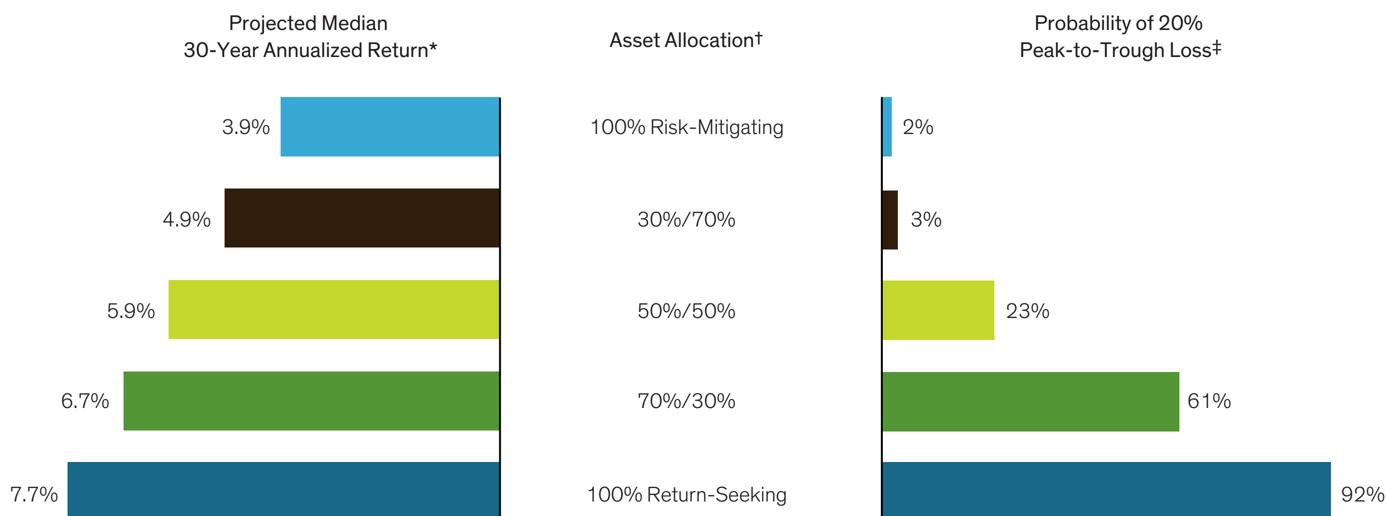
To help clients choose an asset allocation that is right for their philanthropic program, we project the range of outcomes for various asset allocations, based on our proprietary Wealth Forecasting System (see page 18). Because plans can succeed only if you stick with them in difficult times, we highlight the likelihood of experiencing a large peak-to-trough loss—such as 20%—at some point along the way.

The left side of ***Display 20*** shows our projected median annualized return over the next 30 years for various simplified asset allocations. The projected annualized return rises fairly steadily as the allocation to return-seeking assets rises. The portfolio invested only in return-seeking assets is expected to return far more, in the median case: 7.7% per year, almost twice the 3.9% return of the portfolio with none.

But it won't be smooth sailing. We project that there's a 92% chance that a portfolio invested 100% in return-seeking assets will lose 20% of its value from peak to trough at some point over the next 30 years. By contrast, the odds of such a large drop are tiny for the portfolio invested 100% in risk-mitigating assets (primarily bonds), and for an asset allocation with 70% in risk-mitigating assets.

For most long-term investors, neither all return-seeking nor all risk-mitigating assets would provide an acceptable trade-off between long-term growth and the risk of large losses. Careful consideration of your goals and time horizon can help you identify the investment mix that's right for your philanthropic mission.

DISPLAY 20: EXPECTED RETURN AND RISK GROW WITH SIZE OF EQUITY ALLOCATION



**Represents projected median compound annual growth rates over the next 30 years.*

†100% risk-mitigating allocation is all bonds; 30%/70% allocation is 30% stocks/70% bonds; 50%/50% allocation is 50% stocks/50% bonds; 70%/30% allocation is 70% stocks/30% bonds; and 100% return-seeking allocation is all stocks. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging-market. Bonds are modeled as 50% intermediate-term taxable bonds and 50% global intermediate-term taxable bonds, hedged.

‡Probability of a 20% peak-to-trough decline in pretax, pre-cash-flow cumulative returns within the next 30 years. Because the Wealth Forecasting System uses annual capital-market returns, the probability of peak-to-trough losses measured on a more frequent basis (such as daily or monthly) may be understated. The probabilities depicted above include an upward adjustment intended to account for the incidence of peak-to-trough losses that do not last an exact number of years.

Based on Bernstein's estimates of the range of returns for the applicable capital markets as of March 31, 2016. ***Data do not represent past performance and are not a promise of actual future results or a range of future results.*** *See Notes on Wealth Forecasting System on page 51.*

Source: Bernstein

ASSETS TO GIVE

You can give a wide variety of assets to philanthropic organizations, but some assets are much simpler for the donor to give—and for the not-for-profit to receive. Assets held for less than a year are generally subject to limited charitable income-tax deductions, and any unused deductions can typically be carried forward for five years. In addition, the tax benefit varies widely by type of asset and type of charitable recipient, creating difficult planning issues for donors.

For example, giving certain illiquid assets, such as private securities, art, and real estate, may be attractive from a tax perspective but typically requires time-consuming and expensive appraisals. Gifts of debt-encumbered real estate may impose on the not-for-profit the financial and reporting burden of unrelated business taxable income (UBTI). Some not-for-profits simply do not accept certain kinds of assets. ***Display 21*** provides a summary, with the simplest asset to give (cash) at left, and the most complex assets (art and retirement plans) at right.

DISPLAY 21: SOME ASSETS ARE MORE DIFFICULT TO GIVE AND TO RECEIVE

	Cash	Appreciated Publicly Traded Securities	Private Securities	Real Estate	Art and Tangible Property	Qualified Retirement Plans
	Simplest					**Most Complex**
Overview	Simplest for donor to give and for not-for-profit to receive	Simple; can avoid embedded capital gain by giving to not-for-profi	A little more complex; require qualified appraisals; may not be suitable for some strategies*	Can be very complex; requires qualified appraisals; may not be suitable for some strategies; debt can be problematic	Complex; subject to a higher top marginal capital-gains rate (28%); typically limited to cost basis for income-tax deduction unless related use†	Complex; typically a bequest, as giving options are limited while IRA owner is alive
Deductions	Yes	Generally based on fair market value of gift, if held for one year	Generally based on fair market value of gift, if held for one year	Generally based on fair market value of gift, if held for one year	Related use: fair market value; unrelated use: lesser of fair market value of gift or cost basis	At death, both income and estate tax can be avoided on contribution to not-for-profi
Public Charity	50% of adjusted gross income (AGI)	30% of AGI	30% of AGI	30% of AGI	Related use: 30% of AGI	Unlimited estate tax charitable deduction for gift at death
Private Operating Foundation	50% of AGI	30% of AGI	30% of AGI	30% of AGI	Related use: 30% of AGI	Unlimited estate tax charitable deduction for gift at death
Private Nonoperating Foundation	30% of AGI	20% of AGI	20% of AGI; lesser of fair market value or cost basis	20% of AGI; lesser of fair market value or cost basis	No related use exception, and deduction is lesser of fair market value or cost basis	Unlimited estate tax charitable deduction for gift at death
Valuation Required?	No	Generally no	Yes, if deduction above $5,000	Generally yes	Yes, if deduction above $5,000	Generally no
Exceptions	N/A	Will not realize a capital loss if you give securities with an embedded loss	Private business: may be subject to bargain-sale rules depending on capital structure; deductions for S-corp stock and LP and LLC interests are complex	If the property has a mortgage, the gift will be considered part sale, part gift, and the charity may incur unrelated business taxable income (UBTI) liability	Deductions for gifts of art by a dealer or the creator are limited to cost basis, not including time; if the donor retains copyright interest, there is no deduction	During life, donors over age 70½ can give up to $100,000 each year to a public charity (excluding DAFs) from a charitable IRA rollover; there is no income-tax deduction for the gift

**Contributing S-corporation stock to a charitable remainder trust (CRT) will cause a corporation to lose its S-corporation tax status.*

†Considered related use if an organization will use the property in a manner that is related to the philanthropic mission of the organization—for instance, contemporary art donated to a contemporary art museum for public viewing.

Source: Bernstein

RESPONSIBLE INVESTING: WHAT'S RIGHT FOR YOU?

Many philanthropists derive satisfaction from funding worthy causes and want their personal and charitable investments to align with their values and mission. Increasingly, philanthropists also want to be confident that their investments will further positive change—or, at least, not inflict harm.

Fortunately, a growing body of evidence suggests that firms with high environmental, social, and governance (ESG) scores tend to be better long-term investments.[10] Supporting strong ESG standards can reward businesses and their shareholders, while an ESG failure can do serious damage to a company's finances and market performance.

There are several approaches to applying values-based considerations to investment portfolios. These approaches differ in their breadth (***Display 22***) and their risk and return potential. It's important to evaluate the risk and return trade-offs; to the extent that a strategy focuses primarily on social impact rather than financial return, these strategies should probably be funded from the surplus capital portion of your portfolio.

DISPLAY 22: RESPONSIBLE INVESTMENT CHOICES

Source: Bernstein

ESG Integration: Investors consider ESG factors when doing research and integrate the expected economic impact into their investment analysis. An analyst might weigh the negative impact of toxic waste spills on a firm's reputation and the odds of steep fines or lawsuits that could hurt its earnings.

Pro: Considers ESG risks and opportunities without narrowing the opportunity set.

Con: May invest in companies with ESG risks.

ESG Screening: Narrows the opportunity set to include or exclude companies with certain traits.

Pro: Allows investors to make values-based investments customized to their own ideals.

Con: Narrows the investment opportunity set. Also, negative screens may not exclude firms that outsource to vendors that don't meet standards.

Sustainable Thematic: These strategies invest in companies that provide solutions or products to solve social and/or environmental needs. May have a single theme or multiple themes, such as renewable energy, and invest to support climate-related or other environmental projects.

Pro: Investors can allocate capital to public companies addressing one or more ESG issues. Adding themes can diversify the portfolio.

Con: May be a narrow opportunity set.

Impact Investing: Targets a specific social or environmental goal. Often includes private equity or private debt financing for specific projects in underserved areas, such as schools or hospitals in emerging countries. Increasingly, however, the term "impact" is also being applied to public investments that achieve a similar objective.

Pro: Funds are allocated directly to projects.

Con: Results may be difficult to measure.

Venture Philanthropy: The mission tends to be improving systems and sectors, rather than helping particular not-for-profit organizations or projects. Typically, foundations or private equity firms make three- to seven-year investments, and work closely with the grantees. Venture philanthropy is now being eclipsed by the rapid growth in impact investing.

Pro: May address "unpopular" social causes.

Con: Financial return is typically a secondary consideration.

[10] Gordon L. Clark, Andreas Feiner, and Michael Viehs, "*From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance*," University of Oxford, September 2014; Mozaffar Khan, George Serafeim, and Aaron Yoon, "*Corporate Sustainability: First Evidence on Materiality*," Harvard Business School, Working Paper 15-073, 2015

For-Profit Charitable Strategies

Most charitable gifts go to public charities, private foundations, donor-advised funds (DAFs), and charitable trusts. But in recent years, an increasing number of donors have decided to fulfill their philanthropic goals by investing in, or donating to, for-profit entities, in order to avoid the rules related to charitable giving or to profit while helping a favorite cause, or both. Here are a few of them:

Benefit Corporations. A benefit corporation is formed to create a "general public benefit." Its directors must consider the environment and community, employee, and customer interests, as well as the corporation and its shareholders. "General public benefit" must be measured against a third-party standard; an annual report is required. If a benefit corporation neglects its duty to serve the general public benefit, shareholders and other interested parties may institute an enforcement proceeding. Patagonia, Warby Parker, and Etsy are a few examples.

Social Purpose Corporations/Flexible Purpose Corporations. These vehicles are similar to benefit corporations, except that they permit but do not require consideration of social and/or environmental goals. A social purpose corporation may consider the interests of the corporation, its shareholders, and any specific purposes set forth in its Articles of Incorporation, as it deems appropriate. In some cases, the annual reporting is less stringent than for benefit corporations.

Low-Profit Limited Liability Companies (L3Cs). An L3C's primary mission is charitable; its profit is a secondary concern. Unlike a charity, an L3C is permitted to earn profits and distribute them to its members. In general, L3Cs are required to significantly further charitable or educational purposes, as defined by the IRS. Their purpose is not to produce significant income or appreciation of property, or to accomplish political, legislative, or lobbying activities.

Limited Liability Companies (LLCs). In some cases, donors decide to create traditional LLCs to accomplish their philanthropic missions, although it means forgoing an immediate charitable income-tax deduction and almost tax-free growth. Most famously, Facebook CEO Mark Zuckerberg and his wife, Priscilla Chan, announced in December 2015 that they will give 99% of their Facebook shares (currently worth about $45 billion) during their lives to the Chan Zuckerberg Initiative LLC (CZI).[11] Possible reasons include:

- They will be able to use CZI funds to lobby for and contribute to political causes;
- CZI will not be subject to private foundation rules;
- CZI will not be subject to unrelated business taxable income restrictions, and any income generated will be taxed at individual, and not corporate, income-tax rates;
- Annual tax returns will not be subject to public scrutiny; and
- If CZI makes charitable gifts in the future, the charitable income-tax deductions will flow through to Zuckerberg and Chan.

[11] The purpose of CZI is to "join people across the world to advance human potential and promote equality for all children in the next generation": *https://www.facebook.com/notes/mark-zuckerberg/a-letter-to-our-daughter/10153375081581634*

Crafting Your Investment Policy Statement

Writing an investment policy statement (IPS) is an important way that the board of directors of a not-for-profit organization can plan to meet its fiduciary duty to protect the organization's assets. The board must also adhere to the IPS and update it as needed. Here are some elements to include:

- ☐ Anticipated Fund Duration: How long should the organization's funds last? The anticipated time horizon is crucial to determining proper fund investments.

- ☐ Investment Goals: What purpose will these funds serve for the organization? If the goal is to preserve a perpetual endowment and generate a reasonable cash flow, the IPS should state that, so the responsible parties can manage the assets to meet that goal. If the goal is to support construction of a new campus, the IPS should say so clearly, so the board will adopt the (quite different) investments appropriate to that short-term goal.

- ☐ Roles and Responsibilities for Officers, Directors, and Committees: The IPS can be useful in defining roles and responsibilities in managing the organization's assets. If oversight of finances is delegated to an investment committee or finance committee of the board of directors, say so in the IPS. If the organization engages a professional investment manager, delineate the manager's authority.

- ☐ Target Asset Allocation: Define how the assets will be allocated among asset classes.

- ☐ Constraints: List any restrictions on investments, spending, and liquidity.

- ☐ Performance and Risk Guidelines: Specify benchmarks for assessing performance and risk.

APPENDIX

Glossary

Adjusted gross income (AGI): Gross income minus specific deductions, including alimony payments, contributions to qualified retirement accounts, qualified educational and medical expenses, and, for self-employed people, half of the self-employment taxes you pay.

Charitable income-tax deduction: When you make a contribution to a qualified charity or certain charitable strategies, you can deduct the value of the contribution from your taxable income, and thus reduce your tax bill.

Core capital: A Bernstein term for the amount of capital needed to support a desired level of retirement spending, even if capital-market returns are poor, inflation is high, and you live a long time.

Disqualified person: If you are a substantial contributor to a foundation, or act as a director, officer, or trustee of one, you are considered a “disqualified person” who cannot engage in certain acts of self-dealing, including selling items to the foundation, borrowing money from it, or leasing space to or from it.

Excess business holding: A private foundation can hold up to 20% of the voting stock of a corporation, partnership, or trust, including stock owned by disqualified persons; the IRS will consider any amount above 20% an “excess business holding” that will have to be removed from the foundation’s balance sheet within five years. If you donate shares in your business to a private foundation in anticipation of selling the business and the sale falls through, you must remove the excess holding from the foundation or a stiff penalty will become due.

Excise tax on investment income: Private nonoperating foundations are subject to an excise tax on net investment income, usually 1% to 2%. To be taxed at 1%, a foundation must make distributions equal to or greater than the average distribution ratio for the past five years, multiplied by the current portfolio value and increased by 1% of the year’s net investment income.

Form 990-PF: Private foundations are required to file a Form 990-PF each year. The form includes information on the foundation’s assets, grants made, financial activities, and the names of trustees and officers.

Investment policy statement (IPS): A formal, written document that outlines the strategy for investing the assets of a private foundation or not-for-profit, as well as defines roles and responsibilities of board members, staff, and investment managers. Spending policy guidelines may be included in the IPS or as a separate document.

Mission-related investment: An investment that supports a qualified not-for-profit’s, foundation’s, or donor-advised fund’s mission by generating positive environmental or social impact, while generating competitive rates of return. It may not count toward the 5% required annual spending for private nonoperating foundations.

Program-related investment (PRI): An investment made by a private foundation to support charitable activities, including a loan, a guarantee, and, potentially, an equity investment in another charity or commercial venture with charitable purposes. PRIs count toward the 5% required annual spending for private nonoperating foundations.

Qualified charities: "Qualified" charities or not-for-profit organizations as defined under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended ("Code").

Required minimum distribution (RMD): The minimum amount that you, as a participant in an individual retirement account (IRA), a SIMPLE IRA, a SEP IRA, or a defined-contribution retirement plan (but not a Roth IRA), must take, in a given year, from the retirement account when you reach age 70½ (can be delayed to retirement for defined-contribution plan).

Section 7520 rate: The IRS sets the Section 7520 interest rate each month for use in discounting present values, annuities, or future interests. For example, in a charitable lead annuity trust (CLAT), it is the "hurdle rate" established at funding that is applied to annuity payments paid to charity; any remainder after making all annuity payments passes to noncharitable beneficiaries. The 7520 rate is based off of intermediate-term US Treasury rates.

Self-dealing: If you are a substantial contributor to a foundation, or act as a director, officer, or trustee of one, you must act for the benefit of the foundation or charity, not your own benefit. You may not sell to it, borrow money from it, or lease space to or from it; such actions would be viewed as self-dealing.

Smoothing rule: A rule intended to increase the stability of distributions. For example, some private foundations and donor-advised funds base spending on a multiyear average of assets. Private nonoperating foundations have a built-in floor of 5%, since they are required to distribute 5% of assets each year.

Surplus capital: A Bernstein term for financial capital in excess of required core capital that may be available to fund other spending, charitable gifts, or wealth transfers.

Total philanthropic value (TPV): A Bernstein term for the total value of the distributions over time and the remaining principal of a private foundation, donor-advised fund, or other giving strategy, in current dollar terms.

Unrelated business taxable income (UBTI): A foundation or qualified charity can become subject to taxation at the corporate rate (35%) for any UBTI it receives. UBTI can arise through some types of investments in private equity funds, real estate investment trusts (REITs), and other partnership or limited liability company (LLC) structures that use debt to acquire property.

Notes on Wealth Forecasting System

1. Purpose and Description of Wealth Forecasting SystemSM

Bernstein's Wealth Forecasting SystemSM is designed to assist investors in making their long-term investment decisions as to their allocation of investments among categories of financial assets. Our planning tool consists of a four-step process: (1) Client-Profile Input: the client's asset allocation, income, expenses, cash withdrawals, tax rate, risk-tolerance level, goals, and other factors; (2) Client Scenarios: in effect, questions the client would like our guidance on, which may touch on issues such as when to retire, what his/her cash-flow stream is likely to be, whether his/her portfolio can beat inflation long-term, and how different asset allocations might impact his/her long-term security; (3) The Capital Markets Engine: our proprietary model that uses our research and historical data to create a vast range of hypothetical market returns, which takes into account the linkages within and among the capital markets, as well as their unpredictability; and finally (4) A Probability Distribution of Outcomes: based on the assets invested pursuant to the stated asset allocation, 90% of the estimated ranges of probable returns and asset values the client could experience are represented within the range established by the 5th and 95th percentiles on "box-and-whiskers" graphs. However, outcomes outside this range are expected to occur 10% of the time; thus, the range does not guarantee results or establish the boundaries for all outcomes. Estimated market returns on bonds are derived taking into account yield and other criteria. An important assumption is that stocks will, over time, outperform long bonds by a reasonable amount, although this is in no way a certainty. Moreover, actual future results may not meet Bernstein's estimates of the range of market returns, as these results are subject to a variety of economic, market, and other variables. Accordingly, the analysis should not be construed as a promise of actual future results, the actual range of future results, or the actual probability that these results will be realized. Of course, no investment strategy or allocation can eliminate risk or guarantee returns.

2. Retirement Vehicles

Each retirement plan is modeled as one of the following vehicles: traditional IRA, 401(k), 403(b), Keogh, or Roth IRA/401(k). One of the significant differences among these vehicle types is the date at which mandatory distributions commence. For traditional IRA vehicles, mandatory distributions are assumed to commence during the year in which the investor reaches the age of 70½. For 401(k), 403(b), and Keogh vehicles, mandatory distributions are assumed to commence at the later of (i) the year in which the investor reaches the age of 70½ or (ii) the year in which the investor retires. In the case of a married couple, these dates are based on the date of birth of the older spouse. The minimum mandatory withdrawal is estimated using the Minimum Distribution Incidental Benefit tables, as published on www.irs.gov. For Roth IRA/401(k) vehicles, there are no mandatory distributions. Distributions from a Roth IRA/401(k) that exceed principal will be taxed and/or penalized if the distributed assets are less than five years old and the contributor is less than 59½ years old. All Roth 401(k) plans will be rolled into a Roth IRA plan when the investor turns 59½ years old to avoid minimum distribution requirements.

3. Rebalancing

Another important planning assumption is how the asset allocation varies over time. We attempt to model how the portfolio would actually be managed. Cash flows and cash generated from portfolio turnover are used to maintain the selected asset allocation between cash, bonds, stocks, REITs, and hedge funds over the period of the analysis. Where this is not sufficient, an optimization program is run to trade off the mismatch between the actual allocation and targets against the cost of trading to rebalance. In general, the portfolio is expected to be maintained reasonably close to the target allocation. In addition, in later years, there may be contention between the total relationship's allocation and those of the separate portfolios. For example, suppose an investor (in the top marginal federal tax bracket) begins with an asset mix consisting entirely of municipal bonds in his/her personal portfolio and entirely of stocks in his/her retirement portfolio. If personal assets are spent, the mix between stocks and bonds will diverge from targets. We put primary weight on maintaining the overall allocation near target, which may result in an allocation to taxable bonds in the retirement portfolio as the personal assets decrease in value relative to the retirement portfolio's value.

4. Expenses and Spending Plans (Withdrawals)

All results are generally shown after applicable taxes and after anticipated withdrawals and/or additions, unless otherwise noted. Liquidations may result in realized gains or losses, which will have capital gains tax implications.

5. Modeled Asset Classes

The following assets or indexes were used in this analysis to represent the various model classes:

Asset Class	Modeled as...	Annual Turnover Rate
Cash Equivalents	3-month Treasury bills	100%
Intermediate-Term Diversified unicipals	AA-rated diversified municipal bonds f 7-year maturity	30
Intermediate-Term Taxables	Taxable bonds of 7-year maturity	30
Global Intermediate-Term Taxable Bonds—Hedged	7-year 50% sovereign and 50% investment-grade corporate debt of developed countries	30
US Diversified tocks	S&P 500 Index	15
US Value Stocks	S&P/Barra Value Index	15
US Growth Stocks	S&P/Barra Growth Index	15
US Small-/Mid-Cap Stocks	Russell 2500 Index	15
Developed International Stocks	MSCI EAFE Unhedged Index	15
Emerging-Market Stocks	MSCI Emerging Markets Index	20

6. Volatility

Volatility is a measure of dispersion of expected returns around the average. The greater the volatility, the more likely it is that returns in any one period will be substantially above or below the expected result. The volatility for each asset class used in this analysis is listed in the Capital-Market Projections section at the end of these Notes. In general, two-thirds of the returns will be within one standard deviation. For example, assuming that stocks are expected to return 8.0% on a compounded basis and the volatility of returns on stocks is 17.0%, in any one year it is likely that two-thirds of the projected returns will be between (8.9)% and 28.8%. With intermediate government bonds, if the expected compound return is assumed to be 5.0% and the volatility is assumed to be 6.0%, two-thirds of the outcomes will typically be between (1.1)% and 11.5%. Bernstein's forecast of volatility is based on historical data and incorporates Bernstein's judgment that the volatility of fixed income assets is different for different time periods.

7. Technical Assumptions

Bernstein's Wealth Forecasting System is based on a number of technical assumptions regarding the future behavior of financial markets. Bernstein's Capital Markets Engine is the module responsible for creating simulations of returns in the capital markets. These simulations are based on inputs that summarize the current condition of the capital markets as of March 31, 2016. Therefore, the first 12-month period of simulated returns represents the period from March 31, 2016, through March 31, 2017, and not necessarily the calendar year of 2016. A description of these technical assumptions is available on request.

8. Tax Implications

Before making any asset allocation decisions, an investor should review with his/her tax advisor the tax liabilities incurred by the different investment alternatives presented herein, including any capital gains that would be incurred as a result of liquidating all or part of his/her portfolio, retirement-plan distributions, investments in municipal or taxable bonds, etc. Bernstein does not provide tax, legal, or accounting advice. In considering this material, you should discuss your individual circumstances with professionals in those areas before making any decisions.

9. Tax Rates

Bernstein's Wealth Forecasting System has used various assumptions for the income-tax rates of investors in the examples included in this guide. See the assumptions in each example (including footnotes) for details. The federal income-tax rate is Bernstein's estimate of either the top marginal tax bracket or an "average" rate calculated based upon the marginal rate schedule. For 2014 and beyond, the maximum federal tax rate on investment income is 43.4% and the maximum federal long-term capital-gains tax rate is 23.8%. Federal tax rates are blended with applicable state tax rates by including, among other things, federal deductions for state income and capital-gains taxes. The state tax rate generally represents Bernstein's estimate of the top marginal rate, if applicable.

10. Core Capital Analysis

The term "core capital" means the amount of money necessary to cover anticipated lifetime net spending. All non-core-capital assets are termed "surplus capital." Bernstein estimates core capital by inputting information supplied by the client, including expected future income and spending, into our Wealth Forecasting System, which simulates a vast range of potential market returns over the client's anticipated life span. From these simulations we develop an estimate of the core capital the client will require to maintain his/her spending level over time. Variations in actual income, spending, applicable tax rates, life span, and market returns may substantially impact the likelihood that a core capital estimate will be sufficient to provide for future expenses. Accordingly, the estimate should not be construed as a promise of actual future results, the actual range of future results, or the actual probability that the results will be realized.

11. Mortality

In our mortality-adjusted analyses, the life span of an individual varies in each of our 10,000 trials in accordance with mortality tables. To reflect that high-net-worth individuals live longer than average, we subtract three years from each individual's age (e.g., a 65-year-old would be modeled as a 62-year-old). Mortality simulations are based on the Society of Actuaries Retirement Plan Experience Committee Mortality Tables RP-2000.

12. Endowment

The endowment is modeled as a nontaxable permanent fund bestowed upon an institution to be used to support a specific purpose in perpetuity. The endowment may receive an initial donation and periodic funding from either the personal portfolio modeled in the system or an external source. Annual distributions from the endowment may be structured in a number of different ways, including: (1) an annuity or fixed dollar amount, which may be increased annually by inflation or by a fixed percentage; (2) a unitrust, or annual payout of a percentage of endowment assets, based on a single year or the average over several years; (3) a linear distribution of endowment assets, determined each year by dividing the endowment assets by the remaining number of years; or (4) the greater of the previous year's distribution or any of the above methods. These distribution policies can be varied in any given year.

13. Private Foundation

The private foundation is modeled as a charitable trust or not-for-profit corporation, which can be either a private operating foundation or a private nonoperating foundation. The foundation may receive an initial donation and periodic funding from either the personal portfolio modeled in the system or an external source. Annual distributions from the foundation may be structured in a number of different ways, so long as the foundation distributes the minimum amount required under federal regulations, including: (1) only the minimum amount; (2) an annuity or fixed dollar amount, which may be increased annually by inflation or by a fixed percentage; (3) a unitrust, or annual payout of a percentage of foundation assets, based on a single year or the average over multiple years; (4) a linear distribution of foundation assets, determined each year by dividing the foundation assets by the remaining number of years; or (5) the greater of the previous year's distribution or any of the above methods. These distribution policies can be varied in any given year. For nonoperating foundations, the system calculates the excise tax on net investment income.

14. Charitable Remainder Trust

The charitable remainder trust (CRT) is modeled as a tax-planning or an estate-planning vehicle, which makes an annual payout to the recipient(s) specified by the grantor, and at the end of its term (which may be the recipient's lifetime), transfers any remaining assets, as a tax-free gift, to a charitable organization. Depending on the payout's structure, the CRT can be modeled as either a charitable remainder unitrust (CRUT) or a charitable remainder annuity trust (CRAT). The CRUT's payout is equal to a fixed percentage of the portfolio's beginning-year value, whereas the CRAT's payout consists of a fixed dollar amount. In the inception year of the CRT, its grantor receives an income-tax deduction typically equal to the present value of the charitable donation, subject to the applicable adjusted gross income (AGI) limits on charitable deductions and phaseout of itemized deductions, as well as the rules regarding reduction to basis of gifts to private foundations. Unused charitable deductions are carried forward up to five years. Although the CRT does not pay taxes on its income or capital gains, its payouts are included in the recipient's AGI using the following four accounting tiers: Tier 1—Ordinary Income (Taxable Interest/Dividends); Tier 2—Realized Long-Term Capital Gains; Tier 3—Other Income (Tax-Exempt Interest); and Tier 4—Principal. CRTs are required to pay out all current and previously retained Tier 1 income first, all current and previously retained Tier 2 income second, all current and previously retained Tier 3 income third, and Tier 4 income last.

15. Charitable Lead Trust

The charitable lead trust (CLT) is modeled as a portfolio that receives its initial funding from the grantor and transfers payments to one or more charitable recipients each year for a specified number of years or for the life or lives of certain individuals. The annual payments may be a fixed dollar amount (charitable lead annuity trust or CLAT) or a percentage of the trust's assets as valued every year (charitable lead unitrust or CLUT). In the case of a CLAT, annuities may be fixed (the same amount each year), or increasing. The annual payment is generally made first from available cash and then from other trust assets in kind. In a non-grantor CLT, the trust itself is subject to income taxation, and generally pays income tax with respect to retained income and receives a charitable income-tax deduction with respect to certain income paid to the charitable recipient(s). Realized capital gains may be taxable to the trust or treated as a distribution to charitable recipient(s) (and therefore eligible for a charitable income-tax deduction), depending upon the provisions of the trust instrument and other factors. In a grantor CLT, the trust is a "grantor" trust for income-tax purposes, such that the grantor is personally taxed on all items of trust income. The grantor is entitled to a charitable income-tax deduction upon funding for the portion of the CLT then calculated to be payable to the charitable recipient(s) over its term (often the entire funding amount). This charitable income-tax deduction is subject to recapture rules if the grantor dies during the term of the CLT. For both the non-grantor and grantor CLT, when the CLT term ends, the remainder, if any, may be transferred as directed by the trust agreement, including to a non-modeled recipient, a taxable trust, or a beneficiary's portfolio. The assets transferred from the CLT will have carryover cost basis.

16. Capital-Market Projections

	Median 30-Year Growth Rate	Mean Annual Return	Mean Annual Income	One-Year Volatility	30-Year Annual Equivalent Volatility
Cash Equivalents	3.10%	3.50%	3.50%	0.30%	10.10%
Intermediate-Term Diversified Municipals	3.20	3.40	3.40	3.70	7.80
Intermediate-Term Taxables	4.20	4.50	5.80	4.70	8.50
Global Intermediate-Term Taxable Bonds—Hedged	3.50	3.80	5.00	4.00	9.00
US Diversified tocks	7.20	8.80	2.90	16.30	19.90
US Value Stocks	7.50	9.10	3.50	16.00	19.50
US Growth Stocks	6.90	8.90	2.40	18.10	21.30
US Small-/Mid-Cap Stocks	7.40	9.50	2.60	18.70	22.20
Developed International Stocks	8.10	10.20	3.50	18.10	20.90
Emerging-Market Stocks	6.20	10.20	4.10	26.10	28.50
Inflatio	3.00	3.40	n/a	1.10	11.60

Based on 10,000 simulated trials, each consisting of 30-year periods. Based on Bernstein's estimates and the capital-market conditions as of March 31, 2016. Does not represent any past performance and is not a guarantee of any future specific risk levels or returns, or any specific range of risk levels or returns.

Note to All Readers

The information contained herein reflects the views of AllianceBernstein L.P. or its affiliates and sources it believes are reliable as of the date of this publication. AllianceBernstein L.P. makes no representations or warranties concerning the accuracy of any data. There is no guarantee that any projection, forecast, or opinion in this material will be realized. **Past performance does not guarantee future results.** The views expressed herein may change at any time after the date of this publication. This document is for informational purposes only and does not constitute investment advice. It does not take an investor's personal investment objectives or financial situation into account; investors should discuss their individual circumstances with appropriate professionals before making any decisions. This information should not be construed as sales or marketing material or an offer or solicitation for the purchase or sale of any financial instrument, product, or service sponsored by AllianceBernstein or its affiliates.

Information About Morgan Stanley Capital International (MSCI)

MSCI makes no express or implied warranties or representations, and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indexes or any securities or financial products. This document is not approved, reviewed, or produced by MSCI.

Bernstein does not provide tax, legal, or accounting advice. In considering this material, you should discuss your individual circumstances with professionals in those areas before making any decisions.

WHAT'S NEXT?

We hope this guide helped you understand the choices you face in defining and implementing your philanthropic mission, and some of the key strategies you may want to consider.

But that's only the beginning. Your plan should reflect your personal philanthropic goals, wealth, tax position, and time horizon.

Please be sure to consult your tax, estate, and financial advisors.

For more information:

- **Contact your Bernstein Advisor**
- **E-mail philanthropy@bernstein.com**
- **Visit *bernstein.com***

BERNSTEIN

bernstein.com
1.212.486.5800