The Blitz

October 2019

Information on Tax and Estate Planning from the Masonic Charities of the Grand Lodge of Pennsylvania

Is an Annuity Right for You?

The Single Premium Immediate Annuity (SPIA) vs. Charitable Gift Annuity (CGA)

I have been traveling the country for almost 20 years for the Masonic Villages and have seen how people deal with the so-called “golden years” of their lives. As we age, “change” becomes a difficult word to swallow. However, resisting change usually results in a bad outcome. I have worked with many of our fellow brethren and their spouses, or widows, who due to failure to prepare for life’s latter years, are forced into unfortunate circumstances for themselves and their loved ones. I thought I would take a moment to reflect on some steps you can take to address this matter before it is too late.

As we enter the fall season with the stock market moving all over the place like a chipmunk on the back porch, I am reminded about how we need to save our assets for the future like the chipmunk collecting his acorns for the long winter. During my travels, many of the brethren and their ladies or Masonic Village residents have asked me about charitable gift annuities (CGAs) as an investment. Most respond to the ad we place in all our publications about “Guaranteed Income for Life” and inquire about whether the attractive rates are right for them. I send them an illustration, and 90% of the time nothing happens. That is fine, but I reflect whether many people who inquire really understand how the product works. In this issue of The Blitz, I will address the important points of the CGA and compare it to the Single Premium Immediate Annuity (SPIA). Both products pay income for life, but the difference is that when you die, the CGA charity gets to keep any unused money.

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Why an SPIA?

I have never been a big fan of annuities due to the many hidden charges the issuers impose on annuity buyers, but there are some advantages to using them as part of your overall investment portfolio. The basic SPIA pays income for life, and the annuity company gets to keep the unused money, if any. This is the highest rate annuity. But there are up to 15 variations of the SPIA, and many give the unused portion, if any, to listed beneficiaries. However, the issued payout rate will be lower under such circumstances since the annuity company is assuming greater risk. The main advantage of purchasing a fixed annuity is that if you outlive your assets, you are assured income for life, and with many of us living longer these days, that is a distinct possibility.

What about the Charitable Gift Annuity (CGA)?

CGAs can be issued by a charity for immediate pay or at a later date. For this article, I will focus on the immediate pay CGA as a comparison to the SPIA. The main benefit of the CGA is that the projected unused portion of the CGA, based on your life expectancy, is available as an immediate tax deduction to the purchaser. This tax deduction could result in a significant savings of taxes in the year of the purchase. Additionally, if the donor uses appreciated securities or mutual funds to purchase the annuity, an additional savings from capital gains tax can be realized, making the transaction even more beneficial to the donor. I have worked with numerous donors over the years who avoided significant capital gains taxes which would have been incurred due to a buyout by a company by transferring the stock to Masonic Charities.

It should also be noted that rates for CGAs are set by the American Council of Gift Annuities (ACGA) so that rates issued by all charities are the same. The major limitation of a CGA is that the donor is an unsecured creditor of the charity issuer, so one must be careful to purchase annuities from organizations with sufficient assets available to back the payments over the life of the annuity.

A Comparison between the SPIA and CGA

John, an 80-year-old resident at Masonic Village, met with me recently to go over a comparison between purchasing a SPIA and CGA for $10,000. Here are the main illustrative points of our comparison.

We looked at purchasing his SPIA from discount broker Charles Schwab. Schwab quoted him a rate of 10% for life on his annuity if it kept the unused portion on his passing. If John wants to leave the unused portion to his heirs, the rate was 8.3%. John's life expectancy is 11.5 years, so he would receive $11,592 in payments over this time at 10% or $9,522 at 8.3%. As you can see, annuities aren't real winners until you outlive your life expectancy. Consequently, annuities are a modest return on investment unless you outlive your assets.

We then ran a CGA illustration for John for $10,000. The ACGA rate was 7.3%, significantly lower than the SPIA rate. This is because the CGA is calculated to try to preserve 50% of the contribution amount by the donor for the charity should the donor meet his or her life expectancy. Besides receiving income from the annuity, the donor has to intend for the charity to receive a gift from the transaction or it would not be a "charitable" annuity. Other factors can, however, make the CGA competitive with the rate of the SPIA. In this case, John receives a charitable tax deduction of $4,585 for his $10,000 CGA which he can immediately use to reduce his income taxes. If John is in the 24% tax bracket, he would realize an immediate savings of $1,100 from the transaction, which raises his effective rate for the CGA to 8.2%, which is close to the 8.3% rate for the SPIA contract that provides for heirs. If John decided to fund his CGA with appreciated securities worth $10,000 for which he paid $5,000, he would realize an additional savings of $406 in avoided and deffered capital gains tax, which raises the effective rate to 9.21%. Also, unlike the SPIA, he realizes the tax deduction and capital gains savings immediately rather than over the life of the annuity (provided that some of the capital gains is taxed when paid out over John's life expectancy).

Wow. That is a lot to absorb. The bottom line is this:

1. Income annuities are usually for healthy people who outlive their assets, unless you include a death benefit rider, which will cost you.

2. The rates are better on commercial annuities than CGAs, but the savings can be minimized if the donor can take advantage of the tax savings available to him or her.

3. If you have charitable intent, using a CGA as part of your investment strategy may be beneficial, especially if you intended to leave the charity in your estate plan. You can essentially make your gift now, get income for life, and your gift is released to the charity at your passing.

4. I was once told that people who purchase a CGA live longer because they are happier people and need to outlive their life expectancy to get their money back. (I doubt this is true, but it sounds good.)

I learned a lot about annuities in preparing this article, and I hope you did, too. If you would like to learn more about what a CGA can do to put income in your pocket and possibly more years onto your life, feel free to call our Gift Planning Office at 1-800-599-6454 to speak to a Gift Planner and get your own personalized CGA illustration.

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Issued amount ($10,000 annuity for 80-year-old male)	***SPIA Rate of Return**	**CGA Rate of Return**	**Paid over Life Expectancy (11.5 years)**
Income only rate	10.8%	Not applicable (NA)	$11,592
Payout available for heirs	8.3%	NA	$9,522
ACGA payout rate		7.3%	$8,395
With charitable deduction (24% tax bracket)		8.2% effective rate ($1,100 tax savings)	$9,495
With capital gain savings (securities with cost basis of $5,000)		**9.21% effective rate ($406 tax savings)	$9,881

**Based on a Charles Schwab offered SPIA*

***Subject to partial taxation for amounts paid out over life expectancy of annuitant*

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August 2019

As Chief Gift Planning Officer for the Masonic Villages in Pennsylvania, Alvin H. Blitz, Esq., serves the Masonic Charities of the R.W.Grand Lodge of Pennsylvania, which consists of the Masonic Villages, the Masonic Children's Home, the Pennsylvania Masonic Youth Foundation, the Masonic Library and Museum of Pennsylvania and the Masonic Charities Fund. Attorney Blitz holds a Bachelor of Science degree from the University of Scranton, a Master of Arts degree from Fairleigh Dickinson University, and a Juris Doctorate from Dickinson School of Law. He has given estate planning seminars throughout the country and is a member of Carlisle Lodge No. 260, Carlisle, Pa.

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Ask Alvin In Person!

Catch up with Alvin in person to learn updates on the Masonic Charities of the Grand Lodge of Pennsylvania and more about tax and estate planning.

Nov. 6 – 9:	Tampa, FL
Dec. 2 – 6:	West Palm Beach, FL
Jan. 12 – 16:	Phoenix, AZ
Jan. 27 – 31:	Ft. Myers, FL
Feb. 16 – 20:	Tampa, FL
March 1 – 5:	San Diego, CA