



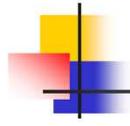
## **Charitable Gift Annuity Reinsurance Benefits, Options and Strategy**

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The goal of this presentation is to present a general overview of the benefits of using reinsurance options for the investment and administration of charitable gift annuity agreements. There are basically two commercial options for reducing and /or eliminating the investment and longevity risks associated with annuity agreements. They are a single premium immediate annuity (SPIA) and a variable annuity agreement (VA).

This presentation will address the options and strategy considerations of both the SPIA and the VA when they are considered for charitable gift annuity reinsurance.



## Demographic realities

- A 65 year old today has a 25% chance of living to age 92
- In 2010.....
  - men reaching age 65 had an average additional life expectancy of 17.2 years or 82.2
  - women reaching 65 could expect to live an additional 19.9 years or to age 84
- Today a husband and wife both aged 65 have approximately a 47% chance that at least one of them will live to age 90
- Life expectancy is a 50/50 chance of living beyond
- The average newborn today will live to be 78.7 yrs old  
The older someone is the longer they will live

To understand gift annuity reinsurance one must understand the powerful demographic forces currently effecting America.

In the senior generation both men and women are living longer. There is a self selected population of individuals who establish gift annuity agreements. They tend to be more educated, have a higher net worth than the median of the U.S. population, and contemporary folklore says they live longer than projected.

The above statistics are taken from both life insurance annuity tables and the U.S. Census bureau.



## The Case of Sally Smith

- Sally, age 75, walks into your office and hands you a check for \$100,000 single life 5.80% gift annuity!
- What do you do with the check?
  - Self manage the payments, and assume the investment and longevity risks
  - Send the check to your bank administrator for a 5 year CD
  - Put the funds into your endowment and hope you can figure out the remainder when Sally dies to deposit into her restricted fund
  - Reinsure with a Single Premium Immediate Annuity (SPIA)
  - Reinsure with a Variable Annuity (VA)

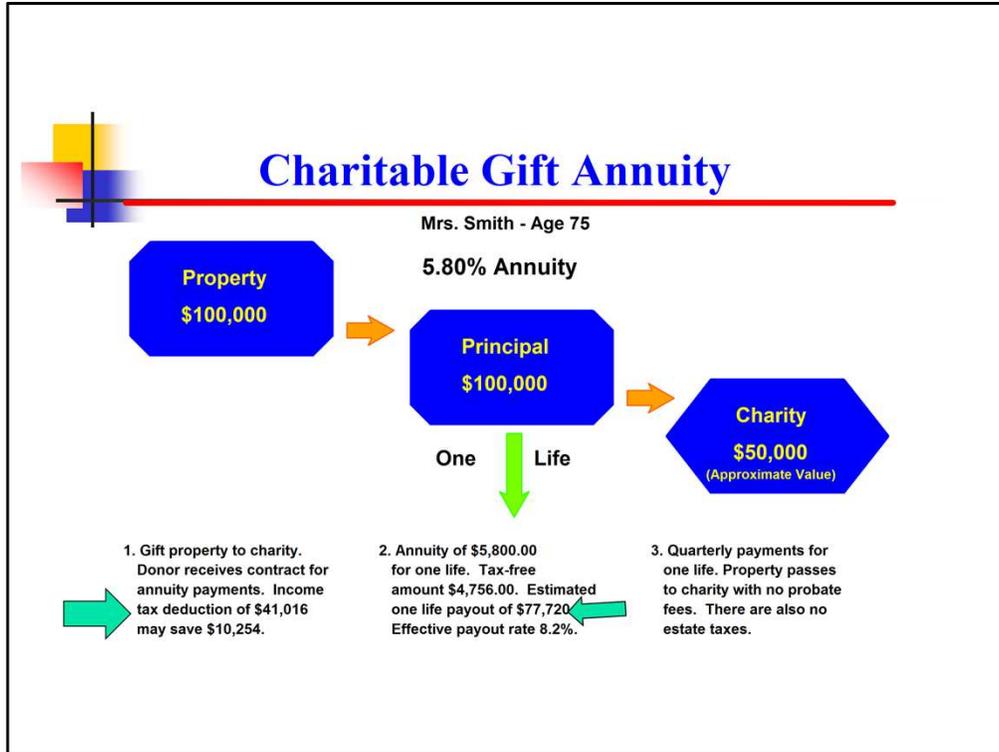
To illustrate the options let's begin with the case of Sally. Sally age 75 to her nearest birthdate wishes to establish a \$100,000 single life gift annuity agreement.

The approved ACGA rate is 5.80% based on her birth date.

The agreement is written and you have the check for deposit and administration.

Your options for the check are.....

1. Self-manage the investments, payments, tax reporting and assume the longevity risks.
2. Send the check to your established gift annuity administrator. Hopefully you are monitoring closely the residuum from terminated agreements and comparing the results to the expected 50% residuum.
3. Purchase a single premium immediate payment commercial annuity (SPIA) to match the payments required to be sent to the annuitant.
4. Establish a variable annuity account with a life annuity company, set the investment asset allocation, and have the account send payments to the annuitants.



The above is a typical Crescendo software printout of Sally's proposal indicating the rate of distribution (5.80%), the allowable income tax charitable deduction (\$41,016) and the projected lifetime payments (\$77,720) Sally will receive if she lives exactly to her projected 13.4 year life expectancy.

It also shows the 50% of gift amount that is projected to be the residuum from the charitable gift annuity agreement.

The effective payout amount of 8.2% is the combination of the financial benefit of the immediate income tax deduction driving down the cost of the gift and the advantage that a high percentage (82%) of Sally's payment will be received income tax-free over her projected life expectancy until she recovers her investment in the contract.

| CHARITABLE GIFT ANNUITY - INCOME TAXATION |          |              |  |              |              |             |
|---|----------|--------------|--|--------------|--------------|-------------|
| Mrs. Smith                                |          |              |  |              |              |             |
| TOTAL AMOUNT                              |          | \$100,000.00 |  | Annuity      |              | \$5,800.00  |
| ORDINARY                                  |          | CAPITAL      |  | Char. Gift   |              | \$41,016.32 |
| INCOME                                    |          | GAIN PAYOUT  |  | Capital Gain |              | \$0.00      |
|   |          |              |  | Basis        |              | \$58,983.68 |
| Years                                     |          |              |  | TAX FREE     | CUMULATIVE   | CUMULATIVE  |
|   |          |              |  | RETURN       | CAPITAL GAIN | TAX FREE    |
| 2013                                      | \$559.16 | \$0.00       |  | \$2,547.27   | \$0.00       | \$2,547.27  |
| 2014                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 7,303.27    |
| 2015                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 12,059.27   |
| 2016                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 16,815.27   |
| 2017                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 21,571.27   |
| 2018                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 26,327.27   |
| 2019                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 31,083.27   |
| 2020                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 35,839.27   |
| 2021                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 40,595.27   |
| 2022                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 45,351.27   |
| 2023                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 50,107.27   |
| 2024                                      | 1,044.00 | 0.00         |  | 4,756.00     | 0.00         | 54,863.27   |
| 2025                                      | 1,679.59 | 0.00         |  | 4,120.41     | 0.00         | 58,983.68   |
| 2026                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2027                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2028                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2029                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2030                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2031                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2032                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2033                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2034                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2035                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2036                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2037                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2038                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2039                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2040                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2041                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2042                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2043                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2044                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2045                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2046                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2047                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2048                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2049                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2050                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2051                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |
| 2052                                      | 5,800.00 | 0.00         |  | 0.00         | 0.00         | 58,983.68   |

Note: Tax-Free return of basis not recovered by date of death may be deducted on last income tax return. See IRC Sec. 72(b).  
Life Expectancy Based Upon Treasury Tables is 13.4 years.

Gift annuities are structured as a bargain sale. There is an investment in the contract and a gift portion. The gift portion generates a charitable deduction. The investment in the contract (donor's own capital) is paid back to the donor as non-taxable return of principal.

The investment in the contract i.e. tax-free portion runs out when the donor reaches their life expectancy.

In the example above an annuitant age 75 (male or female) has a gift annuity life expectancy of 13.4 years. The tax-free portion runs out in 13.4 year or in 2025 on the contract above. Note there is a short payment for 2013.

If the donor should die exactly at the gift annuity life expectancy date and the contract exactly performs according to the ACGA investment and expense assumptions the charity should have an available residuum of 50% of the initial gift amount or \$50,000 in this case.

If the donor dies early and all the assumptions are met then the charity should have an increased residuum amount. If the donor outlives their life expectancy the contract can go to zero assets and the charity would still be obligated to make distributions from their own capital.



## ACGA assumptions

- Every donor is female and 1 year younger than their actual age. Extended longevity assumption.
- 4.25% net *constant* investment return
- 1.00% administrative cost
- Average 50% remainder to charity
- Net 20% present value of gift amount

The ACGA has some simple assumptions posted on their web site: [www.acga-web.org](http://www.acga-web.org)  
The current rate structure and assumptions were approved effective January 2012.

**First**, all life expectancy calculations are based on female life expectancy set back one year. This is to control for longevity risks. Male annuitants are considered female for life expectancy ACGA calculations, and therefore receive a longer life expectancy than normally is the case for a commercial annuity company since commercial rates vary by the sex of the annuitant.

**Second**, the investment assumption rate of return is 4.25% net constant investment return. The ACGA investment return is based on an asset allocation target of 55% Bonds, 40% Equities and 10% Cash.

**Third**, there is an assumed 1% administrative fee for administration and investment.

**Fourth**, the expected residuum if the annuitant lives exactly their life expectancy and the principal of the annuity gift is invested to produce 4.25% and there is a 1.0% expense for the portfolio and administration will be 50% of the initial gift amount.

**Fifth**, the expected residuum return should have a present value of no less than 20% of the initial gift amount. This means on a \$100,000 gift amount today where the charity is expected to receive \$50,000 in the future, it will be the same as if you accepted \$20,000 today.

In our 75 year old female annuitant example with a life expectancy of 13.4 year and an interest rate assumption of 4.25% the present value of the 50% residuum is actually \$28,630, exceeding the ACGA assumption. Present value is an important concept when reinsurance is examined.



## Charitable Gift Annuity

- 1. Charity has to wait for money  
(time value of money risk)
- 2. Charity must invest the money  
(market risk)
- 3. Charity must administer payments  
(administrative risk)
- 4. Charity at risk if donor lives to long  
(longevity risk)
- 5. Donor gives up asset  
(size tends to be small)
- 6. Donor must rely on paying ability of charity  
(legal obligation)

This slide lists the basic characteristics of a charitable gift annuity and its risk effects on a charity. There are several risks involved with gift annuity agreements.

It is important to note even with gift annuity reinsurance the issuing charity is still responsible for donor distributions and tax reports.



## CGA/Reinsurance

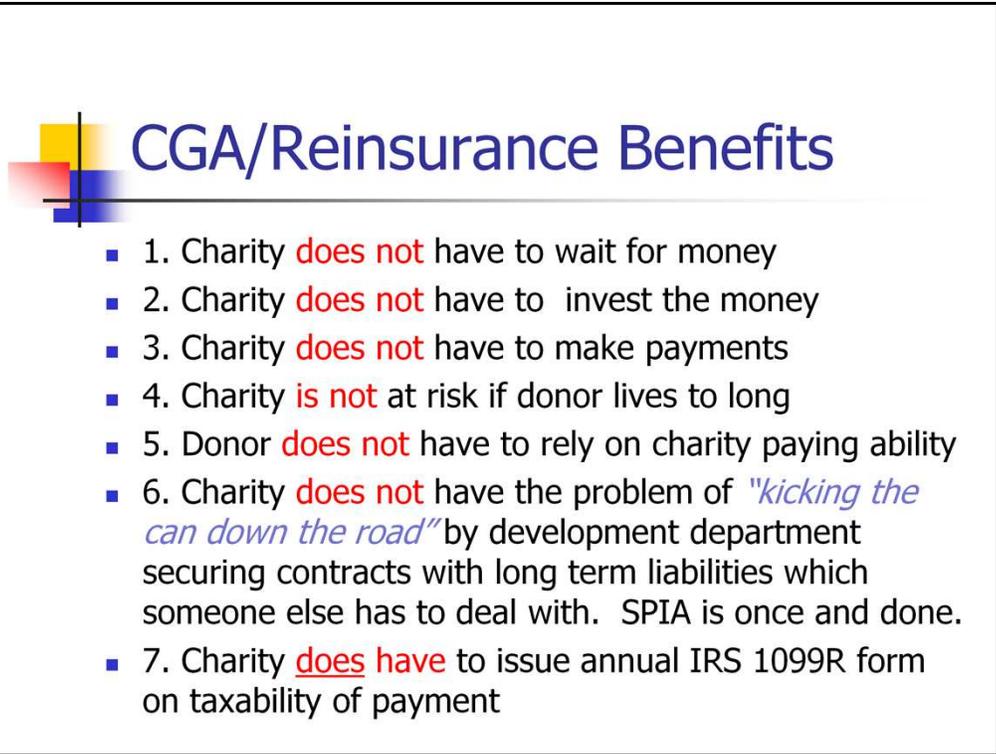
- Financing technique whereby a charity chooses to purchase a commercial single premium immediate annuity (SPIA) as an asset to back its contractual life-income liability owed to the donor.
- Fully “reinsure” or “partially reinsure”
- Contractual obligation remains with the charity
- Default risk nearly non-existent, use A or A+ rated companies only

Gift annuity reinsurance is a financing technique whereby a charity chooses a commercially available life insurance company sponsored product to cover the contractual life income payments to the annuitants.

A charity may reinsure all or part of the payment obligations.

While the contractual obligation remains with the charity a default risk of an insurance company product is practically non-existent. All insurance companies are required to register in the states they market their products and abide by the state’s regulations. One of the regulations require payments to the state guarantee insurance fund. This fund is available to policyholders should an insurance company get into financial trouble and not be able to make annuity payments or life insurance policy death payments. The insurance fund should give increased confidence to potential donors.

It is recommended a charity get a quote from at multiple companies if it is considering reinsurance. For reinsurance quotes from [Connell & Associates](#) we routinely survey at least 30 of the top A and A+ life and annuity companies to provide a broad overview of reinsurance options. Normally the quotes are valid for only two weeks prior to application for the agreement.

A graphic with a black border containing a decorative element of overlapping yellow, red, and blue squares on the left, followed by the title "CGA/Reinsurance Benefits" in blue. Below the title is a list of seven bullet points.

## CGA/Reinsurance Benefits

- 1. Charity **does not** have to wait for money
- 2. Charity **does not** have to invest the money
- 3. Charity **does not** have to make payments
- 4. Charity **is not** at risk if donor lives to long
- 5. Donor **does not** have to rely on charity paying ability
- 6. Charity **does not** have the problem of *"kicking the can down the road"* by development department securing contracts with long term liabilities which someone else has to deal with. SPIA is once and done.
- 7. Charity **does have** to issue annual IRS 1099R form on taxability of payment

Gift annuity reinsurance has many advantages for the charity.

1. There are funds available immediately to support programs or priority projects.
2. Charity is freed from any investment responsibilities.
3. Insurance company makes payments to annuitants so charity is not responsible.
4. The longevity risk is removed if the donor lives too long as the large insurance company pool of annuitants is used to fulfill the payment responsibilities.
5. Donor is secure that their payments are backed by a financially secure state regulated insurance company and a portion of their funds are put to work immediately for the charity.
6. An often hidden advantage of reinsurance is from long term payment liabilities of agreements entered into by previous employees.
7. The only responsibility of the charity is to issue IRS 1099R form at the end of the year representing the taxability of the payment from the previous year. This simple form information is taken directly from the income tax deduction letter issued by **Connell & Associates** for any reinsured gift annuity agreements.

# Life Expectancy & Present value

| Life Expectancy |        |       | Present Value of \$1.00 |        |        |
|-----------------|--------|-------|-------------------------|--------|--------|
| Age             | Single | Joint | Age                     | Single | Joint  |
| 50              | 34     | 40    | 50                      | \$0.10 | \$0.07 |
| 55              | 30     | 36    | 55                      | 0.13   | 0.09   |
| 60              | 25     | 31    | 60                      | 0.18   | 0.12   |
| 65              | 21     | 26    | 65                      | 0.24   | 0.17   |
| 70              | 17     | 22    | 70                      | 0.35   | 0.23   |
| 75              | 13     | 18    | 75                      | 0.42   | 0.30   |
| 80              | 10     | 14    | 80                      | 0.51   | 0.39   |
| 85              | 8      | 11    | 85                      | 0.58   | 0.48   |
| 90              | 6      | 8     | 90                      | 0.67   | 0.59   |
| 95              | 4      | 6     | 95                      | 0.76   | 0.67   |
| 100             | 3      | 4     | 100                     | 0.92   | 0.76   |

Annuity 2003 mortality table      Return assumption 7%

Gift annuities are subject to a cost benefit analysis.

**Are you better to accept a \$1.00 today or wait until the death of the donor at some future date.**

To understand this formula we must know the projected life expectancy of each annuitant. All gift annuity calculation software uses Section 72, Uniform Table of Expectancy . This is not the table more life insurance companies use as they continue to update their life expectancy tables.

Life insurance companies have the additional advantage of a large number of sex determined annuitants to spread their life expectancy risk. Whereas most charities deal with a small annuitant population.

Present Value examines the time value of money. Are you better to accept \$0.42 from a 75 year old annuitant or wait to receive \$1.00 after 13 years? The answer is take the \$0.42 today and invest it at 7% and you will have \$1.00 in the future. So taking \$0.42 today is the same as getting \$1.00 13 years later providing your investment return is 7%. If it is greater than 7% you will have more than \$1.00 and vice versa if the return is less then you will have less.

The above calculation assumes you are receiving a return of the full initial investment in the gift annuity contract and not the projected 50% residuum return.

Gift annuity reinsurance provides cash today to invest until the unpredictable date of death of the donor.

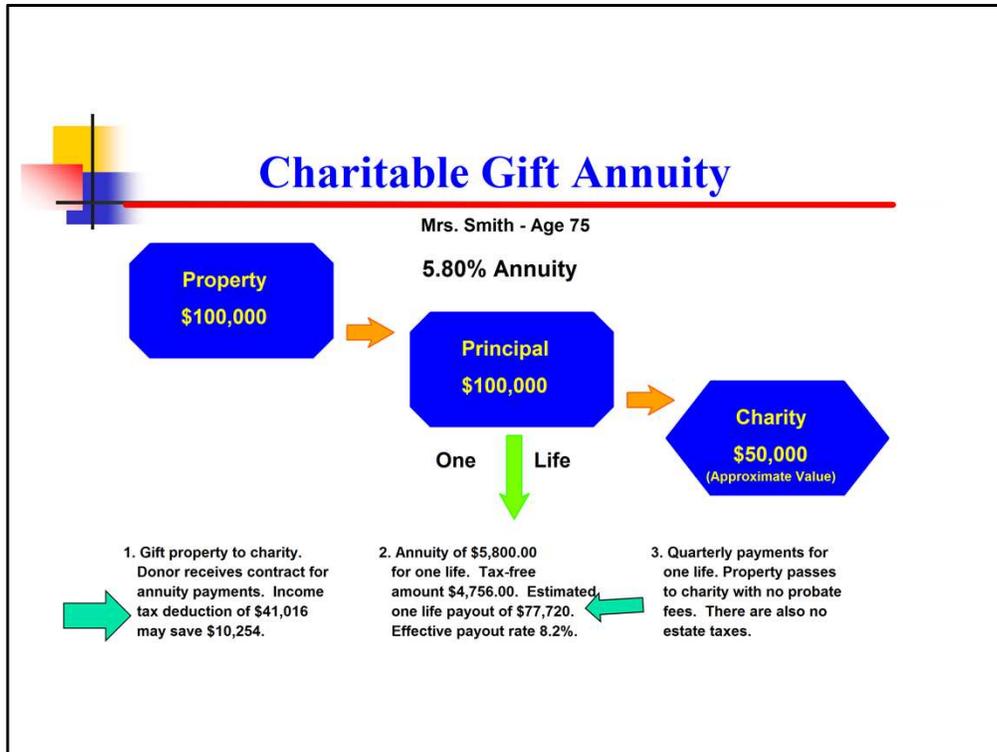


## CGA/Reinsurance

- Does reinsurance cost too much?
  - ACGA assumptions
    - Every donor is female and 1 year younger than their actual age
    - 4.25% net constant investment return
    - 1.00% administrative cost
    - Average 50% remainder to charity
    - Net 20% present value of gift amount

There is a natural question about reinsurance costs that comes up in any discussion of reinsurance. While there is an initial cost for the annuity premium which will normally have a range between 60 to 80% of the gift amount that is not a fair measure of the true cost .

To examine the true cost we need to go back to the ACGA investment and expense assumptions listed above. The target residuum, the true measure of cost, is a net 50% of the initial gift amount.



Here again is the example of Sally our age 75 \$100,000 gift annuity donor who has an expected life expectancy of 13.4 years.

If she is going to receive \$77,720 over her life expectancy and the charity is to receive a net \$50,000 then the investments must grow significantly or the donor must die early if the annuity investments do not perform well.

There are several possibilities but who can predict the future?



## Does reinsurance cost too much?

- It is not the amount needed to fund the reinsurance premium!!!
- The **cost** is the difference between the expected residuum if self-insured and the residuum if reinsured.
  - For female age 75 the residuum is 62% greater than self-insuring
  - For a male age 75 the residuum is 29% greater than self-insuring Source: Rock & Schultz 2012 Crescendo presentation, "Why you should be expecting CGA residual greater than 50%"
- Cost depends on where you put the difference!!!
  - Spend it or Invest it?

Therefore, the true cost of the gift annuity is to compare what you would have at Sally's death from a reinsured gift annuity to when your self-managed or administrative manager provides.

It all depends on what you do with the financial difference between the cost of the premium and the gift amount.

Bob Rock a former New York Life agent and Charles Schultz of Crescendo have done some work in this area and in a recent speech cited the statistic for a 75 year old male or female annuitants. A charity would be 29% or 62% better off using reinsurance than self-investing if the annuity gift differential was invested in the S&P 500 index fund.

Because a charity has virtually no payment risk it could easily choose to spend the net funds immediately on a priority projects.



## Why CGAs might fail!

- Donors lives too long
- Investments do not perform as anticipated
- Investments lose significant value in the first few years and never recover
- Fixed and/or increasing administrative fees decrease asset performance
- Charities think they are smarter than insurance companies
- Claims paying ability of charity examined by due diligence of donor and/or advisors

There are several reasons gift annuities might fail to provide a 50% residuum to a charity. The reasons both relate to the longevity and investment risks.

1. The donor may live too long, far beyond the projected life expectancy and the principal of the annuitants account is rapidly depleted.
2. Investments in the annuity pool may not earn a net return of 4.25%, the ACGA projection.
3. Investment performance is greatly effected by the performance in the early years of the gift annuity investment pool. If the initial few years of investment performance is negative it is almost impossible for the pool to recover and produce a 50% annuity residuum.
4. Investment performance is greatly effected by expenses of running the portfolio. If expenses are high it eats into the potential investment performance.

| Gift Annuity Reinsurance Principal Evaluation |           |           |         |                      |                     |                       |                     |           |           |
|---|-----------|-----------|---------|----------------------|---------------------|-----------------------|---------------------|-----------|-----------|
| Female age 75                                 |           |           |         |                      |                     |                       |                     |           |           |
| Year  | Value     | Quarterly |         | Earnings<br>at 4.25% | Constant            |                       | Reducing            |           | Net Value |
|   |           | Payments  | Payout  |                      | Expenses<br>at 1.0% | Dec 31st<br>Net Value | Expenses<br>at 1.0% | Net Value |           |
| 1   | \$100,000 | \$97,870  | \$5,800 | \$4,159              | \$1,000             | \$95,229              | \$1,000             | \$95,229  |           |
| 2   | \$95,229  | \$91,777  | \$5,800 | \$4,047              | \$1,000             | \$89,025              | \$952               | \$89,072  |           |
| 3   | \$89,025  | \$85,798  | \$5,800 | \$3,784              | \$1,000             | \$82,781              | \$890               | \$82,891  |           |
| 4   | \$82,781  | \$79,780  | \$5,800 | \$3,518              | \$1,000             | \$76,498              | \$828               | \$76,671  |           |
| 5   | \$76,498  | \$73,725  | \$5,800 | \$3,251              | \$1,000             | \$70,177              | \$765               | \$70,412  |           |
| 6   | \$70,177  | \$67,633  | \$5,800 | \$2,983              | \$1,000             | \$63,815              | \$702               | \$64,113  |           |
| 7   | \$63,815  | \$61,502  | \$5,800 | \$2,712              | \$1,000             | \$57,414              | \$638               | \$57,776  |           |
| 8   | \$57,414  | \$55,333  | \$5,800 | \$2,440              | \$1,000             | \$50,973              | \$574               | \$51,399  |           |
| 9   | \$50,973  | \$49,125  | \$5,800 | \$2,166              | \$1,000             | \$44,491              | \$510               | \$44,982  |           |
| 10  | \$44,491  | \$42,879  | \$5,800 | \$1,891              | \$1,000             | \$37,969              | \$445               | \$38,525  |           |
| 11  | \$37,969  | \$36,593  | \$5,800 | \$1,614              | \$1,000             | \$31,407              | \$380               | \$32,027  |           |
| 12  | \$31,407  | \$30,268  | \$5,800 | \$1,335              | \$1,000             | \$24,803              | \$314               | \$25,489  |           |
| 13  | \$24,803  | \$23,904  | \$5,800 | \$1,054              | \$1,000             | \$18,158              | \$248               | \$18,910  |           |
| 14  | \$18,158  | \$17,500  | \$5,800 | \$772                | \$1,000             | \$11,472              | \$182               | \$12,290  |           |
| 15  | \$11,472  | \$11,056  | \$5,800 | \$488                | \$1,000             | \$4,743               | \$115               | \$5,629   |           |
| 16  | \$4,743   | \$4,571   | \$5,800 | \$202                | \$1,000             | -\$2,027              | \$47                | -\$1,074  |           |
| 17  | -\$2,027  | -\$1,954  | \$5,800 | \$0                  | \$1,000             | -\$8,754              | -\$20               | -\$7,733  |           |
| 18  | -\$8,754  | -\$8,436  | \$5,800 | \$0                  | \$1,000             | -\$15,236             | -\$88               | -\$14,149 |           |
| 19  | -\$15,236 | -\$14,684 | \$5,800 | \$0                  | \$1,000             | -\$21,484             | -\$152              | -\$20,332 |           |
| 20  | -\$21,484 | -\$20,705 | \$5,800 | \$0                  | \$1,000             | -\$27,505             | -\$215              | -\$26,290 |           |

Life expectancy of 75 year old ACGA tables is 13.4 years

Back to our example of a \$100,000 gift annuity from Sally age 75. The above Excel spreadsheet is a simplistic example of Sally investment account.

Let's assume \$100,000 is deposited on January 1<sup>st</sup> and the charity commits to a 5.80% distribution paid quarterly in \$1,450 payments.

In column 3 the average yearly account value deducting for quarterly is computed. This is the average value on hand which is invested at 4.25%.

From the initial value of \$100,000 the distribution of \$5,800 (column 4) is subtracted but the average quarterly balance was invested at 4.25% so earning have to be added back into the account. In year 1 the earning are \$4,159.

Now expenses ( Column 6) need to be considered and subtracted from the investment balance. The are two assumptions for expenses: Frist, assumes a constant expense cost of \$1,000 or 1%. Second, the expenses are computed as a constant percentage of the end of year net asset value.

The final account value for each of the projected 20 years is computed in Column 7 or Column 9.

As the projections show the account value turns negative in year 16. The projected residuum at life expectancy of 13.4 years is \$18,158 to \$18,910.

| Gift Annuity Reinsurance Principal Evaluation |           |           |         |                      |                     |                       |                     |           |
|---|-----------|-----------|---------|----------------------|---------------------|-----------------------|---------------------|-----------|
| Female age 75                                 |           |           |         |                      |                     |                       |                     |           |
| Year  | Value     | Quarterly |         | Earnings<br>at 4.25% | Constant            |                       | Reducing            |           |
|   |           | Payments  | Payout  |                      | Expenses<br>at 2.0% | Dec 31st<br>Net Value | Expenses<br>at 2.0% | Net Value |
| 1   | \$100,000 | \$97,870  | \$5,800 | \$4,159              | \$2,000             | \$94,229              | \$2,000             | \$94,229  |
| 2   | \$94,229  | \$92,222  | \$5,800 | \$4,005              | \$2,000             | \$88,427              | \$1,885             | \$88,543  |
| 3   | \$88,427  | \$86,544  | \$5,800 | \$3,758              | \$2,000             | \$82,502              | \$1,769             | \$82,733  |
| 4   | \$82,502  | \$80,745  | \$5,800 | \$3,506              | \$2,000             | \$76,451              | \$1,650             | \$76,801  |
| 5   | \$76,451  | \$74,822  | \$5,800 | \$3,249              | \$2,000             | \$70,272              | \$1,529             | \$70,743  |
| 6   | \$70,272  | \$68,775  | \$5,800 | \$2,987              | \$2,000             | \$63,961              | \$1,405             | \$64,556  |
| 7   | \$63,961  | \$62,599  | \$5,800 | \$2,718              | \$2,000             | \$57,517              | \$1,279             | \$58,238  |
| 8   | \$57,517  | \$56,292  | \$5,800 | \$2,444              | \$2,000             | \$50,937              | \$1,150             | \$51,786  |
| 9   | \$50,937  | \$49,852  | \$5,800 | \$2,165              | \$2,000             | \$44,217              | \$1,019             | \$45,198  |
| 10  | \$44,217  | \$43,275  | \$5,800 | \$1,879              | \$2,000             | \$37,354              | \$884               | \$38,470  |
| 11  | \$37,354  | \$36,558  | \$5,800 | \$1,588              | \$2,000             | \$30,346              | \$747               | \$31,599  |
| 12  | \$30,346  | \$29,699  | \$5,800 | \$1,290              | \$2,000             | \$23,189              | \$607               | \$24,582  |
| 13  | \$23,189  | \$22,695  | \$5,800 | \$986                | \$2,000             | \$15,881              | \$464               | \$17,417  |
| 14  | \$15,881  | \$15,543  | \$5,800 | \$675                | \$2,000             | \$8,417               | \$318               | \$10,100  |
| 15  | \$8,417   | \$8,238   | \$5,800 | \$358                | \$2,000             | \$796                 | \$168               | \$2,628   |
| 16  | \$796     | \$779     | \$5,800 | \$34                 | \$2,000             | -\$6,987              | \$16                | -\$5,003  |
| 17  | -\$6,987  | -\$6,838  | \$5,800 | \$0                  | \$2,000             | -\$14,638             | -\$140              | -\$12,499 |
| 18  | -\$14,638 | -\$14,327 | \$5,800 | \$0                  | \$2,000             | -\$22,127             | -\$293              | -\$19,834 |
| 19  | -\$22,127 | -\$21,655 | \$5,800 | \$0                  | \$2,000             | -\$29,455             | -\$443              | -\$27,013 |
| 20  | -\$29,455 | -\$28,828 | \$5,800 | \$0                  | \$2,000             | -\$36,628             | -\$589              | -\$34,039 |

Life expectancy of 75 year old ACGA tables is 13.4 years

Back to our example of a \$100,000 gift annuity from Sally age 75. The above Excel spreadsheet is a simplistic example of Sally investment account.

This slide has all of the same assumptions included on the previous slide except the expenses have been increased for 1% to 2%

Now expenses ( Column 6) need to be considered and subtracted from the investment balance. The are two assumptions for expenses: Frist, assumes a constant expense cost of \$2,000 or 2%. Second, the expenses are computed as a constant percentage of the end of year net asset value.

The final account value for each of the projected 20 years is computed in Column 7 or Column 9.

As the projections show the account value turns negative again in year 16.

The projected residuum at life expectancy of 13.4 years is \$15,881 to \$17,417.

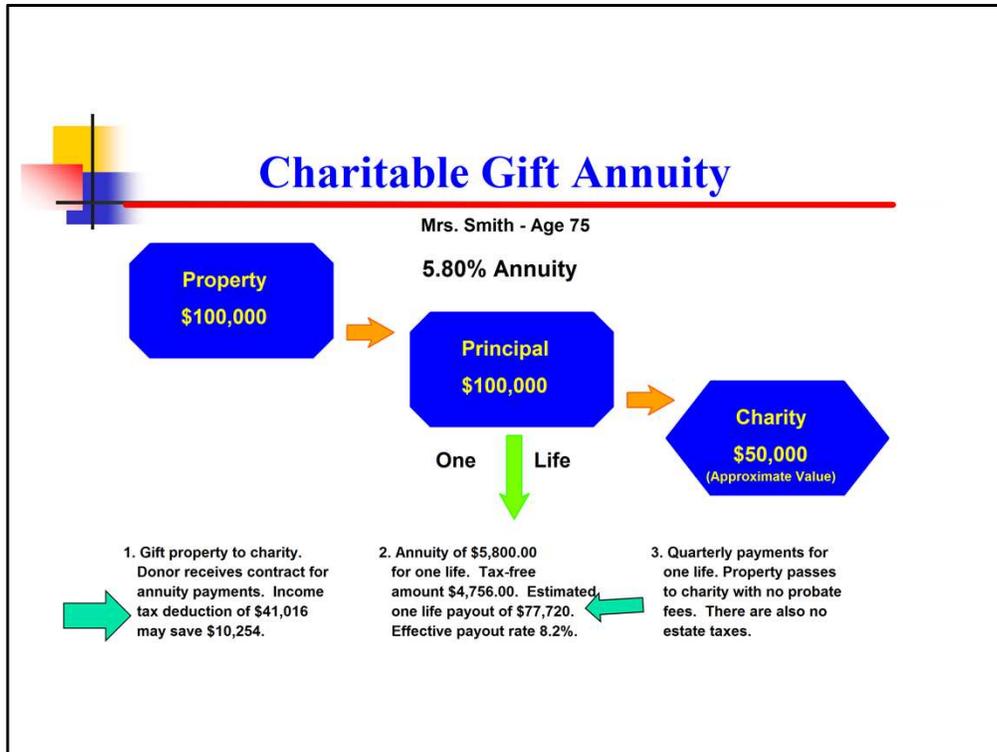
| Gift Annuity Reinsurance Principal Evaluation |           |                    |         |                   |                  |           |
|---|-----------|--------------------|---------|-------------------|------------------|-----------|
| Female age 75                                 |           |                    |         |                   |                  |           |
| Year  | Value     | Quarterly Payments | Payout  | Earnings at 4.25% | Expenses at 2.0% | Net Value |
| 1   | \$100,000 | \$96,375           | \$5,800 | \$4,096           | \$2,000          | \$83,404  |
| 2   | \$83,404  | \$80,380           | \$5,800 | \$3,545           | \$2,000          | \$76,125  |
| 3   | \$76,125  | \$73,366           | \$5,800 | \$3,235           | \$2,000          | \$68,801  |
| 4   | \$68,801  | \$66,307           | \$5,800 | \$2,924           | \$2,000          | \$61,431  |
| 5   | \$61,431  | \$59,204           | \$5,800 | \$2,611           | \$2,000          | \$54,015  |
| 6   | \$54,015  | \$52,057           | \$5,800 | \$2,296           | \$2,000          | \$46,552  |
| 7   | \$46,552  | \$44,865           | \$5,800 | \$1,978           | \$2,000          | \$39,043  |
| 8   | \$39,043  | \$37,628           | \$5,800 | \$1,659           | \$2,000          | \$31,487  |
| 9   | \$31,487  | \$30,346           | \$5,800 | \$1,338           | \$2,000          | \$23,884  |
| 10  | \$23,884  | \$23,018           | \$5,800 | \$1,015           | \$2,000          | \$16,233  |
| 11  | \$16,233  | \$15,645           | \$5,800 | \$690             | \$2,000          | \$8,535   |
| 12  | \$8,535   | \$8,226            | \$5,800 | \$363             | \$2,000          | \$788     |
| 13  | \$788     | \$760              | \$5,800 | \$34              | \$2,000          | -\$7,007  |
| 14  | -\$7,007  | -\$6,753           | \$5,800 | -\$298            | \$2,000          | -\$14,851 |
| 15  | -\$14,851 | -\$14,312          | \$5,800 | -\$631            | \$2,000          | -\$22,743 |
| 16  | -\$22,743 | -\$21,919          | \$5,800 | -\$967            | \$2,000          | -\$30,686 |
| 17  | -\$30,686 | -\$29,573          | \$5,800 | -\$1,304          | \$2,000          | -\$38,677 |
| 18  | -\$38,677 | -\$37,275          | \$5,800 | -\$1,644          | \$2,000          | -\$46,719 |
| 19  | -\$46,719 | -\$45,025          | \$5,800 | -\$1,986          | \$2,000          | -\$54,811 |
| 20  | -\$54,811 | -\$52,824          | \$5,800 | -\$2,329          | \$2,000          | -\$62,954 |

Life expectancy of 75 year old ACGA tables is 13.4 years

This chart shows the effect of a 10% decrease in principal value the first year of the investment.

A first year decrease in principal value accelerates principal reduction. Once the principal is reduced it is difficult to recover.

With a 13.4 year life expectancy there will be little or no residuum for the charity if the donor lives exactly their projected life expectancy.



Again we refer back to the original example of Sally who if she lives her life expectancy will receive total payments of \$77,720 or \$5,800 per year for 13.4 years.



## Donor Example Sally Age 75

- Female age 75, LE 13.4 yrs
- \$100,000, 5.8%, \$5,800 payment
- Gross expected lifetime payments \$77,720
- Deduction \$41,016
- Present value \$58,984
- **SPIA premium \$61,100**
- **Charity benefit \$38,900**
- Return after 11 yrs @ 5% = \$67,346
- Return after 12 yrs @ 6% = \$79,774
- Return after 14 yrs @ 5% = \$78,221

Let's look at reinsuring Sally's payment using a single premium immediate payment gift annuity and investing the difference until life expectancy or beyond.

Sally still receives a charitable deduction and the present value of the future payments (\$77,720) made over time totals \$58,984.

The cost of a SPIA purchased in July 2013 from an A+ rated company is \$61,100.

The immediate cash benefit to charity is \$38,900.

Now let's assume the immediate cash is invested at 5% for 11 years the net account value is \$67,346 more than the ACGA projected residuum of \$50,000.

In 12 years compounded at 6% the residuum would equal \$79,774.

If Sally should live 14 years and the net immediately to charity is invested at 5% the net result is a riskless return of \$78,221.



## Donor Example #1

- Joyce S., Florida, age 89, LE 5.3 yrs
- \$10,000 cash gift, 8.7% rate, first annuity
- \$870.00 annually, \$217.50 quarterly
- Deduction \$6,075
- Present value \$3,925
- SPIA premium \$5,720
- Charity benefit \$4,280
- Return after 5 yrs @ 5% = \$5,773
- Return after 6 yrs @ 6% = \$6,129

This is an actual case of an 89 year old Florida annuitant. Her gift annuity was the first one this Foundation wrote and it provided a distribution of 8.70% for life.

The net cost to charity for an SPIA was \$5,720 leaving \$4,280 available for charity.

If the charity takes the net difference and invests it over the donor's projected life expectancy it will have a net greater return than the ACGA projected residuum of \$5,000.



## Donor Example #2

- Cecelia H., Arizona, Age 77, LE 11.2 yrs
- New Jersey charity, second annuity, first 2 life
- \$10,000 cash, 6.20% rate
- \$620.00 annually, \$155.00 quarterly
- Deduction \$4,446.23
- Present value \$5,553.77
- SPIA premium \$7,699.44
- Charity benefit \$2,300.56
- Return after 10 yrs @ 5% = \$3,788
- Return after 12 yrs @ 6% = \$4,716

This actual example of a New Jersey charity with an Arizona donor. This is the second CGA from this individual but the first one was a two life with her still living husband. This CGA was for her life only as it provided more income .

The SPIA cost was \$7,699 leaving the charity an immediate benefit of \$2,300 (23%) to invest and/or spend.

Also the NJ charity did not have to report as a liability the present value of the future payments to this donor on their financial statement since it was a completely reinsured agreement.

The charity also has no administrative cost for administering the agreement as the insurance company is making all payments which are directly deposited into the donor's bank account.

The projected return after investing the difference over 10 to 12 years at various interest rates almost equaled the ACGA projection of a 50% residuum.



## Donor Example #3

- Charles & Suzanne F., 66 & 65, LE 24.6 yrs
- South Carolina, first annuity
- \$10,000, 5.0% rate
- \$500 annually, \$125 quarterly
- Deduction \$2,397.94
- Present value \$7,771.25
- **SPIA premium \$8,066.68**
- **Charity benefit \$1,933.32**
- Return after 23 yrs @ 5% = \$6,090
- Return after 25 yrs @ 6% = \$8,129

This actual example of a South Carolina charity was their first gift annuity agreement.

The couple had a joint and survivor life expectancy of 24+ years and the charity did not want to administer the agreement for all that time.

Shortly after the agreement was written the director of development left and they have not written another agreement.

The investment projections indicate if the balance after the cost of the SPIA was invested the charity would have more than bettered the ACGA projection of 50% residuum.



## Donor Example #4

- Zebedee and Evelyn M., 80 & 78, LE 13.4 yrs
- North Carolina, joint and survivor
- \$10,000, 6.0% rate
- \$600 annually, \$150 quarterly
- Deduction \$4,200.94
- Present value \$5,799.06
- SPIA premium \$7,558.70
- Charity benefit \$2,441.30
- Return after 13 yrs @ 5% = \$4,670
- Return after 14 yrs @ 6% = \$5,643

This actual example of a North Carolina charity was their seventh gift annuity agreement.

The couple had a joint and survivor life expectancy of 13.4 yrs and the charity did not want to administer the agreement for all that time. It is interesting to note the joint life expectancy is the same as a single payment agreement for a 75 year old.

The charity received an immediate 24% benefit from the gift with no continuing administrative or payment requirements except the end of year 1099R statement.

The investment projections indicate if the balance after the cost of the SPIA was invested the charity would have close to or would beat ACGA projection of a 50% residuum.



## Gift annuity reinsurance potential

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- Ten (10) \$100,000 gift annuity agreements reinsured with a 30% immediate present value gift to charity equals \$300,000 in unrestricted support
  - No longevity or investment risk



## Variable Annuity Option

- Contract issued by highly rated insurance company
- Portfolio: Combination of mutual funds (active/passive management or ETFs)
  - Wide range of investment choices – fixed income or securities for diversification
- Guaranteed internal rate of return
- Provides
  - Systematic withdrawals matched to annuity payments
    - Monthly, quarterly, semiannually, annually
  - Death benefits
    - Highest of current account value
    - Stepped-up-death benefit of the highest anniversary value minus subsequent withdrawals
    - **Return of initial premium amount**



## Donor Example #5 Single Life Variable Annuity

- Christine L., 74, LE 13.2 yrs, December 24, 2008 gift
- Texas resident, single life, first annuity
- \$25,000, 6.60% rate
- \$1,650 annually, \$412.50 quarterly
- Deduction \$10,512
- Present value \$14,487
- **VA premium \$25,000**
- Charity benefit \$0
- Donor died August, 2010
- **Final market value \$34,402**



## Donor Example #6 Two-Life Variable Annuity

- Clyde S. and Sandra S, Georgia charity
- DOB August 1939 (72) & January 1944 (68)
- Gift date October, 2011
- \$1,000,000 with \$500,000 to VA
- Younger life the measuring life for payments and death benefit
- Payment 5% or \$7,500 quarterly or \$25,000 annually from VA
- **FMV July 2013 after payments \$595,764**

## Donor Example #7

### Variable Annuity for Flexible CGA

- James C. age 68, Oct, 2011 agreement
- NC resident, single life, fourth Flex CGA
- \$10,000, target date & rate, 12-31-14 & 6.50%
- Deduction \$2,986.30
- Present value \$7,013.70
- **VA premium \$10,000**
- Charity benefit \$0
- **July 2013 fair market value \$11,113.97**



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