



NOVEMBER 2019, ISSUE 9

## A Generational Shift in Giving

As a multi-generational company, Houston Trust Company stands witness to the transfer of wealth from one generation to the next, with the biggest generational wealth transfer poised to take place within the next 25 years. It is estimated that 45 million U.S. households will transfer \$68 trillion in assets as Baby Boomers begin to retire,<sup>1</sup> and while there is an in-between generation, it is the vast generation of the Millennials who will inherit this wealth and shape the future. In this issue of Viewpoints, we will take an in-depth look at how this generational shift will affect one area in particular: philanthropy. Houston Trust Company and its clients have a long history of charitable giving and our shareholders have founded and supported philanthropic institutions from the earliest days of Houston and Texas. Our clients as a whole average 597 donations annually and gift an average of \$28 million each year. With such a strong philanthropic base, it is imperative that we stay informed of how emerging trends in philanthropy impact donors.

### Generational Influences On Giving

#### Attitudes, Values, and Behaviors

Baby Boomers (Boomers) currently are the largest resource for giving, and as they move into retirement, it is expected that they will donate more than

\$6.6 trillion over the next 25 years.<sup>2</sup> Boomers are more likely to have a local focus, concentrating their giving to organizations such as schools, arts organizations, churches, or community centers that are close to home.

<sup>1</sup> Fidelity Charitable. The Future of Philanthropy: Where Individual Giving is Going. FMR LLC, 2016. <http://fidelitycharitable.org>.

<sup>2</sup> Merrill Lynch, and New Age. "Giving in Retirement: America's Longevity Bonus." Giving in Retirement: America's Longevity Bonus, 2015.

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 over the next 25 years.

Millennials take a wider world view and are making social change an integral part of their personal and professional lives, perhaps attributable to growing up in a world interconnected through technology and travel. As such, Millennials tend to give to organizations with a global focus or those addressing larger societal or environmental problems such as human trafficking, immigration, and climate change. Fidelity's "The Future of Philanthropy" study notes that "almost half [of Millennials] say changes in technology have affected their giving, compared with only about a quarter of Baby Boomers. Likewise, almost a third of Millennials cite alternative forms of giving – such as impact investing and social involvement in giving – as having influence."<sup>3</sup> While Millennials do not yet have the capital of the Boomers, they are pushing the boundaries of "traditional philanthropy" in how they give, where they give, and what they expect from nonprofit organizations in return.

Nonprofits are evolving to meet these expectations. With requests for donations coming from all directions and devices (e.g. social media, email blasts, Kickstarter campaigns, and television spots), Millennials are putting more emphasis on being courted. Thus far, the trend is pointing to smaller donations being made sporadically with larger, concentrated gifts going to a few charities of choice where the donor is deeply involved as a Board member or volunteer. Nonprofits, in turn, are concentrating on donor retention. As a rule, retaining existing donors costs less than acquiring new ones, and current donors represent a curated universe that has already

demonstrated a belief in the organization's mission. As such, most nonprofit organizations are pursuing strategies to reduce donor losses.

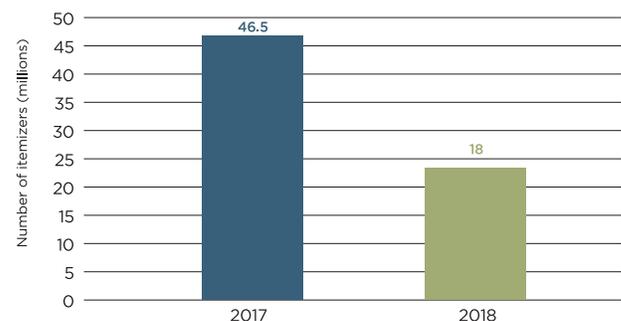
Houston Trust Company is privileged to work on both sides of the equation with public nonprofits, private foundations, and individual donors. In doing so, we have opportunities to explore new technologies to facilitate giving. We also can partner with different investment management firms if Environmental, Social, and Governance (ESG) and/or customized Socially Responsible Investing (SRI) strategies are desired. At the same time, we are educating our next generation of clients how to best navigate the rules and regulations of charitable giving and how to withstand periods of instability in the market.

### Responses to Policy Changes & Market Volatility

Each year, a variety of factors influence trends in philanthropy, most notably new tax legislation, economic growth (or the lack thereof), and market volatility. While reactions to these factors may not split across generational lines, they do affect the lens through which a generation reacts to the present and prepares for the future.

The most recent change to tax laws occurred on December 22, 2017, when President Trump signed the Tax Cuts and Jobs Act. While it may take several years to understand the full impact of this tax reform on

### The Tax Cuts and Jobs Act Reduced the Value of Complicated Itemized Deductions



Source: The Joint Committee on Taxation, "Tables Related to the Federal Tax System as in Effect 2017 Through 2026"

<sup>3</sup> Fidelity Charitable. The Future of Philanthropy: Where Individual Giving is Going. FMR LLC, 2016. <http://fidelitycharitable.org>.

charitable giving, previous research has shown that donors adjust how much they donate based in part on what they can deduct.<sup>4</sup> A side effect of this tax legislation occurred when nonprofits encouraged donors to increase their giving towards the end of 2017 in reaction to the rumors of what the tax reform would entail. This effort created a “bump effect” in charitable donations for 2017 and a decrease for 2018.

Another influence on giving patterns is the strength of the economy and market volatility. Market volatility in particular has increased in reaction to trade talks, mass shootings, natural disasters, and interest rate policies. As noted in *The Philanthropy Outlook 2018 & 2019*, “the S&P 500 has significant influence on corporate, individual/household, and foundation giving.”<sup>5</sup> Donors tend to overreact to market volatility, holding back donations or reducing them until they feel the future is less uncertain.

When advising clients on charitable giving, Houston Trust Company recognizes the experiences of different generations and how they shape reactions to current events. Millennial individuals, born between 1981 and 1996, came of age during the financial crisis and were faced with a feeble job market that took years to recover. As a result, they have a more pessimistic view of the future and are more cautious in uncertain times.



*Baby Boomers were born between 1946 and 1964. The first Boomers reached standard retirement age of 65 in 2011.*

On the other hand, Boomers experienced a relatively long period of economic stability and are the wealthiest generation to date. This is not to say that

they are immune to external forces, but that they are likely to maintain the status quo and not change pledges in the face of turbulent times. At Houston Trust Company, we have experience with both generations of charitable donors and strive to make sure we meet these needs for all our clients through in-person meetings, technology, or a combination of both.

## Vehicles For Giving The Tried and True

One obvious area of change in philanthropy is where funds come from, be it a personal checking account, a family foundation, or a charitable trust. While millennials are more likely to donate individually through social media or a crowdsourcing application, Boomers are creating increasingly sophisticated vehicles or entities through which they can make charitable donations, while at the same time saving on taxes or augmenting an estate plan. There are many advantages to using a planned giving vehicle, such as current-year tax deductions for gifts to be made in the future, favorable tax treatment of assets within the vehicle, and the ability to preserve the value of highly appreciated assets. While there are many varieties of charitable planning vehicles, this section will explore four of the most common and where and how Boomers and Millennials are using and shaping these strategies.

**Private Family Foundations:** Private Foundations are standalone entities that remain under family control and can exist in perpetuity, creating an enduring family legacy and a stream of support for



*Millennials are more likely to donate through social media or crowd sourcing.*

<sup>4</sup> Marts & Lundy. “The Philanthropy Outlook 2018 & 2019.” Reading, Indiana University Lilly Family School of Philanthropy, February 2018.

<sup>5</sup> Ibid, pg. 33.

grant recipients. Private foundations can be funded with any type of asset, including private equity, tangible assets, real estate and intangible personal property, although liquidity is important to foundations given their 5% distribution requirement. Another unique benefit is that they can engage in a wide array of philanthropic activities such as program related investments, grants to individuals, scholarship programs and directed charitable activities. One of the greatest benefits of a private foundation is the donor's ability to control both the grant making and the investment decisions. While there are many benefits to a private foundation, the most prohibitive attributes are ongoing administrative and investment costs (e.g. accounting and attorney fees, administrative support, etc.). As noted, private foundations also are required to pay out 5% of assets annually<sup>6</sup> and must adhere to governance procedures or by-laws. At Houston Trust Company, we find a private foundation should have a minimum initial market value of at least \$3 million to be economical and sustainable. By and large, private family foundations currently are being founded by the Baby Boomers since Millennials are still creating wealth.

**Qualified Charitable Distributions:** A qualified charitable distribution or "QCD", is an otherwise taxable distribution from an IRA to a qualified charity. QCDs can count towards one's required minimum distribution (RMD) for the year, if certain terms are met. First, you must be 70½ or older to make a QCD and the maximum allowable amount is \$100,000 per year and must be a contribution that would have otherwise been eligible for a full deduction. QCD's must be given to a 501(c)(3) organization that is eligible to receive tax-deductible contributions and cannot be made to a private foundation or donor-advised fund. In addition to the benefit of giving to a charity, QCDs have an added tax

advantage of being excluded from an individual's taxable income.

While on the subject of IRAs, another option to consider is designating a charity as the IRA's beneficiary. There can be significant tax advantages to donating retirement assets directly to a charity. When done properly, it can minimize the income taxes imposed on your heirs and estate. With Boomers starting to enter this stage of their lives, Houston

Trust Company is helping more of them turn to their IRAs as an alternative pool of assets for charitable purposes.

**Charitable Trusts:** Charitable Trusts come in a variety of flavors - CRUTs, CLATs, CRATs, PIFs - with the most common being variants of a Charitable Lead Trust ("CLT") or a Charitable Remainder Trust ("CRT"). A CLT invests capital and makes periodic payments to a charitable organization for the lifetime of the trust. When

the CLT terminates, any remaining assets pass to the grantor's family. The reverse is true of a CRT: in the year of funding, the grantor may take a current-year personal income tax deduction and begins receiving payments on a periodic basis. Upon the trust's termination, remaining assets are distributed to one or more charities predetermined by the grantor. Charitable trusts often are created as a part of an overall estate plan and do involve a complex web of tax rules and regulations; therefore, experienced legal and tax counsel is recommended for anyone setting up a charitable trust. Similar to family foundations, charitable trusts are being utilized by Baby Boomers as they near retirement and firm up their estate plans.

**Donor-Advised Funds:** Perhaps the most popular vehicle for giving today is the donor-advised fund or "DAF." DAFs are giving accounts and are the fastest-growing charitable vehicle in the United States.<sup>7</sup>

## TRIED AND TRUE VEHICLES FOR GIVING

*Private Family Foundations*

*Qualified Charitable  
Distributions*

*Charitable Trusts*

*Donor Advised Funds*

<sup>6</sup> IRC, § 4942

<sup>7</sup> "2015 Donor-Advised Fund Report." 2015 Donor-Advised Fund Report. National Philanthropic Trust, 2015.

Under current tax laws, contributions to a DAF are treated as if a donation was made to a charity. Donors receive a current-year charitable income tax deduction but are not required to pay out the funds within the same year. Instead, donations can be made whenever they choose. A DAF is extremely cost effective and its activity can be kept confidential. Sponsoring organizations, large financial institutions like Vanguard, Fidelity or community funds, may place certain restrictions on grant activity, such as minimum dollar amounts or number of grants per year. While DAFs are simple to administer, once the contribution is made, the donor has ceded all legal right to those funds. “For grant and investment choices, a DAF offers less control because technically, the donor’s wishes are ‘recommendations’.

Although these recommendations are almost always honored, final decision-making authority rests with the sponsor.”<sup>8</sup> While the convenience of a DAF can be appealing, it is not a “silver bullet”. The lack of ability to be directly involved in the grant making process sometimes frustrates donors. There may also be limited investment options. In addition, there is a growing problem of dormant DAFs. According to the National Philanthropic Trust’s 2018 DAF Report, “the publicly financed tax deduction that accrues to the donor may not be ‘recouped’ by the public for years.”<sup>9</sup> In our experience, the \$5 million mark is the tipping point where a private foundation is more advantageous than a DAF.

### Emerging Trends

**Social Media:** As already mentioned, donors of all generations are confronted with requests from all directions and devices. Support can be given through websites, text messages, PayPal accounts, and a myriad of other digital platforms. The 2018 Global Trends in Giving Report found that “generational differences are lessening when it comes to technological advances. Millennials, Gen Xers, and Baby Boomers all prefer to give online and digital communications significantly influence their giving.

Baby Boomers are the generation most likely to give as a result of direct mail/post (18%), but overall, generations are becoming more homogenous and tech-based in their giving habits.”<sup>10</sup> When you think about the core principles behind social media, collaboration, openness, sharing experiences, and creating community all come to mind. These characteristics also describe the purpose of foundations, charitable trusts, DAFs, nonprofit organizations, and donors who recognize this overlap are leading the transformation of traditional methods of grantmaking.

Since oftentimes donations made via social media are from individuals rather than charitable entities,



it is important for individual donors to bear in mind the limitation on charitable deductions for individuals. Charitable deductions cannot exceed 50% of an individual’s adjusted gross income (AGI) in a given year, although they can be carried forward. To complicate matters even further, only donations to certain organizations are allowed at that level, such as churches, hospitals and educational institutions. A lower limit of no more than 30% of an individual’s AGI applies to other types of charities, including but not limited to veterans’ groups, cemeteries, and volunteer organizations.

**Impact Investing:** As we noted in our fourth issue of Viewpoints, “socially responsible and impact investing have emerged as important areas of the investment landscape in recent years.”<sup>11</sup> Impact investing is a growing trend in which investments are made for the

<sup>8</sup> “Private Foundations and Donor-Advised Funds; Critical Differences That May Matter to Your Clients.” Private Foundations and Donor-Advised Funds; Critical Differences That May Matter to Your Clients. Fairfield, CT: Foundation Source Philanthropic Services Inc., 2018.

<sup>9</sup> “2015 Donor-Advised Fund Report.” 2015 Donor-Advised Fund Report. National Philanthropic Trust, 2015.

<sup>10</sup> Nonprofit Tech for Good. “2018 Global Trends in Giving Report,” 2018 Global Trends in Giving Report, 2018.

<sup>11</sup> Houston Trust Company, “Socially Responsible Investing,” Socially Responsible Investing, Viewpoints, No. 4, March 2017.

purpose of creating a social or environmental impact while earning a financial return. Donors are drawn to the flexibility of impact investing, which can either exclude companies that do not align themselves with a donor's values or only include companies that do. At Houston Trust Company, we have seen an increasing number of private foundations work to align their investments with their missions and are finally able to do so without sacrificing a return.

As an example, we recently performed an analysis of the Vanguard Social Index ("VFTAX") relative to the Vanguard S&P 500 Index ("VFIAX") and found that historical performance between the two funds is comparable. However, because of different sector weightings within the indices, the VFTAX outperformed the VFIAX primarily due to the large overweight in the tech sector over the analysis period.

#### Vanguard Social Index vs. S&P 500 Comparative Analysis

	VFTAX	VFIAX
	NAV	NAV
2018	-3.45%	-4.43%
2017	24.11%	21.79%
2016	10.24%	11.93%
2015	1.17%	1.36%
2014	15.75%	13.64%
2013	36.84%	32.33%
2012	17.84%	15.96%
2011	-0.78%	2.08%
2010	14.43%	15.05%
2009	35.12%	26.62%

Looking at the benefits of impact investing from the philanthropic side of the equation, there are strategies that allow charitable entities to make direct investments in for-profit companies that further an investor's values or favored causes. Other impact investing strategies allow for partnerships between donors and charitable organizations, which is highly appealing to Millennials who want to see the "impact" of their dollars. It invites a level of commitment to measure and report the performance of the investment and to encourage transparency and accountability.<sup>12</sup>

**Program Related Investments ("PRIs"):** PRIs are loans, loan guarantees, or even equity investments that are made to organizations, either for-profit or non-profit, that further a Foundation's mission. PRI funds can be recovered in part or in whole and might even earn a return, depending on the conditions. Houston Trust Company clients often turn to PRIs when they identify an organization that they are deeply passionate about and want to be more personally or financially involved with than as just a grant maker.

**Microlending:** Similar to PRIs, microloans can be made to both for-profits and non-profits and have become a socially-conscious way to provide funds to those in need at very low, affordable interest rates. Loans such as these are usually made to entrepreneurs or small businesses. In this sense, microloans are not much different than small business loans; however, it is the motivation behind these loans and the people involved that make them unique. Traditional lenders focus solely on earning a profit through interest rates and fees. Microlenders are more interested in making a difference in the lives of those who either do not have access to traditional loans or who might not qualify. Microlending was pioneered by an economics professor who was frustrated by the cycle of poverty in Bangladesh. In 1976, Professor Mohammed Yunus founded the Grameen Bank Project and made a loan of \$27 to a local woman who wove bamboo stools.<sup>13</sup> Using this capital, this woman purchased her own supplies, repaid the loan and was able to succeed as a small businesswoman. Since then, microlending has flourished both in developing countries and here in the United States. The Small Business Administration considers anything under \$50,000 to be a microloan, with the average being about \$13,000.<sup>14</sup> For most microlenders, the primary motivator is the opportunity to help people who work hard and need access to affordable business capital.

It is clear that technology has played an important role in philanthropy's emerging trends. Now more than ever, donors have direct access to information about philanthropic opportunities close to home and all over the world. In addition, donors are able to do their

<sup>12</sup> Greene, Sean. "A Short Guide to Impact Investing." A Short Guide to Impact Investing. Case Foundation, 2015.

<sup>13</sup> Peter Renton, A Brief History of Microlending (Lending Academy: Wordpress, 2008).

<sup>14</sup> www.sba.gov

own research, as evidenced by the growing popularity of sites such as Guide Star, Foundation Source, and Charity Navigator, and can hold those charities accountable. Gone are the days when most donors would write a check and assume their funds were being put to good use. Millennials want proof that their dollars are making a difference and now the information is at their fingertips.

## Conclusion

### The Future is Bright

Philanthropy is evolving at a rapid pace. External factors such as tax laws, the state of the economy and market conditions create a framework within which Boomers and Millennials are finding creative albeit different ways to donate. Boomers are taking advantage of increasingly sophisticated vehicles, such as CLTs and CRTs, to augment their estate plans and decrease their taxes. Meanwhile, millennials are blurring the lines between the for-profit and non-profit sectors, making philanthropy an integrated part of their daily lives.

At Houston Trust Company, we fully support the philanthropic endeavors of our clients and have spent the last few years focusing on the next generation. We see how millennials increasingly value brands, organizations, and even investment opportunities that share aligned values. To support them, we offer a variety of services ranging from performing due diligence on nonprofit organizations to sharing technological resources. We also work hard to educate our next generation of clients on how to be good stewards of their families' (and their own) legacies by investing both their money and their time in the causes they promote.

In conclusion, the future of philanthropy is bright. Definitions are broadening and there are more and more ways to make an impact on both charitable causes and in estate plans than by just writing a check. All the changes we are seeing only strengthen and benefit our world, locally and globally, and we at Houston Trust Company are excited to be a part of it.

## ABOUT THE AUTHOR



### **Katherine M. Lummis**

*Senior Vice President*

Kate Lummis joined Houston Trust Company in 2012. As Senior Vice President, Ms. Lummis is responsible for the company's Endowment, Foundation, and Charitable Trust practice. In addition, she oversees employee education and training and is a primary member of the marketing and business development team. Ms. Lummis holds a BA, magna cum laude, and an MA from the Morrissey College of Arts and Sciences at Boston College. She also is a graduate of the Texas Bankers Association Graduate Trust School and the Certified Financial Planner (CFP®) Program at Rice University.