

*If your estate- and tax-planning objectives include making a charitable gift, receiving an income for life, reducing income taxes and possibly increasing income, you may want to consider a gift to one of the pooled income funds available through the University of California. Your gift will provide the continuing support that allows the University to maintain its tradition of excellence.*

#### **WHAT IS A POOLED INCOME FUND?**

A pooled income fund is a type of trust that enables donors to make tax-deductible gifts to a charity and provide income to one or more individuals for life. After the lifetime of the last income beneficiary, the donor's interest in the pooled fund is transferred to the charity.

Pooled income funds are similar to mutual funds in that the contributions of many donors are commingled (or "pooled") for investment purposes. Each donor to the pooled fund is allocated a certain number of units in the fund, and every three months the designated beneficiary receives a proportionate share of the funds income.

Unlike a mutual fund, however, pooled income fund gifts involve an irrevocable transfer of cash or securities, part of which constitutes a tax-deductible gift.

Pooled income funds also differ from mutual funds in that any long-term capital gains realized by the fund are retained by the fund itself. Such gains cannot be distributed to the beneficiary, but instead become part of the ultimate charitable gift. The donor, therefore, avoids capital gain taxation when contributing highly appreciated assets to the fund and when receiving earnings from the fund.

#### **BENEFITS OF A GIFT TO A POOLED INCOME FUND**

Pooled income fund gifts allow donors to accomplish several tax- and estate-planning objectives. Donors may receive some or all of the following benefits:

- Increased annual income
- Lifetime variable income for the donor and/or others, paid quarterly
- An immediate income tax charitable deduction
- Avoidance of capital gain taxes on the original donation if it is made with appreciated securities
- Reduced estate taxes and probate costs
- Professional investment management
- The satisfaction of making a gift to the University of California

#### **TAXES ADVANTAGES**

In addition to maintaining or increasing current investment income, a contribution to a pooled income fund may reduce the donor's income tax liability. Donors may claim a charitable deduction on federal and state income tax returns for the year in which the gift is made.

For gifts of cash and non-appreciated securities, a donor may use the deduction up to 50 percent of adjusted gross income; for gifts of long-term appreciated property, the donor may use the deduction up to 30 percent of adjusted gross income. Any contributions in excess of the 50 percent or 30 percent limitations may be carried over for deduction in the five succeeding tax years, again subject to the same overall limitations.

#### **TWO FUNDS**

Donors to UC may select from two funds offered by the Regents of the University of California. In addition, donors are able to designate a specific campus or program, purpose and/or type of fund that they would ultimately like to support with their gift.

The following is a brief description of the Regents' pooled income funds. A more detailed description of the funds – including their current yields and fund size – is available on request.

#### **UC LONG-TERM INCOME FUND**

The investment objective of this fund is to produce a relatively high and stable income that will grow moderately over time while preserving principal. This fund is invested in the Regents' High Income Pool (HIP), which is a balanced portfolio invested in high-yielding common stocks and long-term bonds. However, on receipt of the assets by the Regents, the gift funds are invested on a temporary basis in the Short Term Investment Pool (STIP), pending the next monthly opportunity to be added to the High Income Pool.

#### **UC BALANCED GROWTH FUND**

This fund's objective is to generate a reasonable level of current income and to invest in such a way that income will grow consistently over time. It is invested in the University of California General Endowment Pool (GEP). However, on receipt of the assets by the Regents, the gift funds are invested on a temporary basis in the Short Term Investment Pool (STIP), pending the next monthly opportunity to be added to the General Endowment Pool.

While the two pooled income funds have different investment objectives, there are several similarities in the way in which they are managed.

First, distributions of income from the underlying investment funds are made monthly to the pooled income funds. Each fund issues payments to beneficiaries on a quarterly basis at the end of the month following the close of the quarter. Payments are made by direct deposit to a donor's bank account.

Second, beneficiaries are provided with annual reports, which review the performance of the pool in the previous three years, the fund's assets, number of participants, income earned and distributed, income per unit, and the yield based on market value according to the Internal Revenue Service-prescribed formula. A detailed list of assets in the underlying investment funds (STIP, HIP and GEP) is also available.

Third, the Regents' policy permits the assessment of a one-time fee on the distribution of the charitable remainder of individual pooled income fund agreements. The fee is equal to one-half percent of the market value calculated annually; this fee covers a portion of the accounting and tax preparation costs over the life of the individual pooled income fund agreement.

#### **MAKING A GIFT**

To make a pooled income fund gift, the donor signs a pooled income fund gift agreement and arranges for the transfer of \$20,000 or more in cash or marketable securities to one of the Regents' funds. Additional contributions of \$5,000 or more may be made to either fund at any time.

Real estate is not an appropriate gift to a pooled income fund, but may be used to fund other life income plans. Federal regulations prohibit pooled income funds from accepting or investing in tax-exempt securities.

Pooled income fund gifts are generally made during a donor's lifetime, but they may also be made by will. Donors who want to make testamentary gifts should consult their attorneys and confer with the staff of the Office of Planned Giving about fund requirements.

When making a pooled income fund gift, the donor designates one or more persons (which may include the donor) as the life-income beneficiaries and stipulates the ultimate use of the gift. After the death of the last life-income beneficiary, the beneficiary's units are withdrawn from the pooled income fund and the proceeds are used by the University for the purpose(s) specified by the donor.

Each year, the life-income beneficiary receives a written statement from the fund manager indicating the number of units held, the market value per unit and the account received by the beneficiary for that year. Income from a pooled income fund is fully taxable as ordinary income.

Unit value is established by dividing the value of the fund's total assets on the valuation day by the number of outstanding units. The number of units assigned to a gift does not change, but the market value of the pooled income fund's total assets fluctuates.

#### **GIFT OF LONG-TERM APPRECIATED SECURITIES**

Donors realize no taxable capital gain as a result of making a gift of appreciated securities to a pooled income fund, which permits a donor to increase income from donated assets without loss due to capital gain taxation. For example, an individual owning low-basis securities with a relatively low rate of return would have to sell them, pay a tax on the realized gain and then reinvest the net proceeds in order to get a higher yield. By making a gift to either of the University's pooled income funds, the assets can be sold and reinvested, while avoiding the tax on the appreciation. The donor may also claim a charitable deduction based on the full value of his or her gift.<sup>1</sup>

#### **THE CHARITABLE DEDUCTION**

The amount of the deduction the donor may claim is the "present value" of the dollar amount the University is expected to receive, based on IRS tables. The exact amount of the charitable deduction depends on the age of the beneficiaries, the individual pooled income fund's rate of return in the last three years and the current federal discount rate.

The charitable deduction is smaller for a gift with two beneficiaries because the time before the gift is available to the University is actuarially longer. In addition, the rate of return affects the amount of the charitable deduction. The lower the fund's historical rate of return, the higher the deduction.

<sup>1</sup>The effect of California's Alternative Minimum Tax may reduce the state tax benefits of charitable gifts of appreciated property.

#### **LEGAL CONSEQUENCES**

Pooled income funds are part of a "family" of gifts sometimes called "life-income gifts" or "planned gifts." This terminology is used because these gifts require a certain amount of planning before a transaction is completed. We strongly encourage every potential donor to seek tax and legal counsel before making a planned gift to the University.

As part of this process, we suggest that donors consider other life income arrangements (charitable remainder trusts and charitable gift annuities) as well as a pooled income fund. The brochure entitled "Life Income Gift Options" provides additional information on these different plans.

While pooled income funds share certain characteristics with other life income gifts, there are certain distinctions that merit some attention. A pooled income fund is a trust which pays out all of its income to its beneficiaries on an annual basis. As a result, income will inevitably fluctuate from year to year.

A declaration of trust is the legal document which governs the operation of a pooled income fund. Prior to making a gift, each donor shall receive a copy of the declaration of trust for the fund to which he or she is intending to contribute.

In addition, each donor enters into a gift agreement, which sets forth the specific terms and conditions of the gift, including the ultimate designation of the remainder interest.

The Regents of the University of California received from the Internal Revenue Service a ruling October 22, 1986, which states that the declaration of trust and the gift agreements for the pooled income funds meet the requirements of a pooled income fund as defined under IRC Section 642(c)(5).

As noted previously, the funds received in consideration of a pooled income fund are invested in underlying investment funds managed by the treasurer of the University of California.

Detailed current information regarding the pooled income funds and the underlying investment funds is available from the Office of Planned Giving. This information should be reviewed prior to entering into a pooled income fund gift.

The pooled income funds and the underlying investment funds are exempt from securities registration under the Philanthropy Protection Act of 1995.

#### **A FINAL NOTE**

If you would like us to send you a sample calculation showing the deduction you could claim for a pooled income fund gift to the University of California, or information about any of our other life-income plans, please contact us.

# Pooled Income Funds



UNIVERSITY OF  
CALIFORNIA

Berkeley  
Davis  
Irvine  
Los Angeles  
Merced  
Riverside  
San Diego  
San Francisco  
Santa Barbara  
Santa Cruz

Hastings College of the Law