

***Please note:** This email conversation between Holly Hall and John Havens and took place prior to the publication of the April 6, 2006 Chronicle of Philanthropy article, “Much-Anticipated Transfer of Wealth Has Yet to Materialize, Nonprofit Experts Say.”*

*The notes that Holly Hall refers to in her February 14, 2006 email are available in PDF form at <http://www.bc.edu/research/swri/features/wealthtransfer/>*

*They can be accessed by clicking on the link, “Notes on the Wealth Transfer Estimate Originally Presented in ‘Millionaires and the Millennium.’”*

## **Tuesday, February 14, 2006**

Holly Hall wrote:

Hi John and Paul:

Thank you for sending the notes yesterday from John. I have now read them closely and have the following six questions:

1. Your notes state that inter vivos giving could be lumped in with what you have estimated for bequest giving. But you specifically accounted for inter vivos giving in your 2003 reassertion (see page 12) that the 1998 wealth-transfer estimates were still valid...Are you now saying that you underestimated inter vivos giving back in 2003 ?

2. In the new “simple” model in your notes, you did not use the most recently adjusted bequest figures for Giving USA. Can you please recalculate your model with the recently adjusted figures?

The figures are as follows:

1998: \$12.98-billion

1999: \$17.37-billion.

2000: \$19.88-billion

2001: \$19.80-billion

2002: \$20.90-billion

2003: \$18.13-billion

2004: \$18.56-billion

3. You mention the lack of growth in household wealth (“it declined for three successive years [from 2000 to 2002] and only regained its 1999 level in 2004”). But didn’t you know this in 2003 when you re-affirmed all your projections?

4. You also say in 7b of the notes that some wealth holders would give to children and other heirs during their life rather than waiting until death. But there has been no elimination of the gift tax. The gift tax makes it more attractive for the wealthy to pass along assets at death, particularly if there is no estate tax.

5. You say in the notes: “No model is going to predict behavior 55 years into the future (or 20 years into the future) with close accuracy.” If that is the case, why put out these estimates in the first place?

6. Some years ago, you published a study on the number of charitable remainder trusts that was later pulled off the Planned Giving Design Center's web site, because it was found that the methodology greatly overestimated the number of such trusts. Why was your methodology for charitable trusts flawed? Could a similar "over-projection" be occurring with the wealth transfer?

**Wednesday, February 15, 2006**

John Havens wrote:

Hello Holly,

I am responding to your questions below. Paul emailed me that he will not have time in the next few days to respond himself and suggested I not wait to integrate our replies. He may add additional comments as he sees fit.

I also think I figured out the text to which you were referring in question 1. In the interest of moving ahead, I am moving ahead.

*Holly Hall wrote:*

*Hi John and Paul:*

*Thank you for sending the notes yesterday from John. I have now read them closely and have the following six questions:*

***1. Your notes state that inter vivos giving could be lumped in with what you have estimated for bequest giving. But you specifically accounted for inter vivos giving in your 2003 reassertion (see page 12) that the 1998 wealth-transfer estimates were still valid...Are you now saying that you underestimated inter vivos giving back in 2003 ?***

The answer is a little bit complicated. Let me try to explain. With respect to inter vivos giving, the model assumes the households will continue to give to nonprofit organizations (including family foundations if they have them) in the same way and in the same proportion as they did in 1998. If there is an increase in giving to such organizations above and beyond the baseline levels and proportions, not just by a few people but at the macro level, the shift will result in more inter vivos giving. It is not completely clear how this increase in inter vivos giving will affect charitable bequests. One possibility is that the increase in inter vivos contributions represents a shift from charitable bequests to inter vivos giving. It is the case, however, as indicated in the 2003 article, that increases in inter vivos giving will come at the expense of either reduced consumption expenditures and/or from the financial resources (new income and current

wealth) of the household. Since the majority of wealth transfer and the majority of charitable bequests comes from the estates of wealth holders, the important issues focus on the extent that wealth holders are or are not shifting their donations from charitable bequests to inter vivos giving.

I don't think anyone has looked at this issue in a comprehensive manner. We very much plan to do so as part of a larger study of wealth holders, subject to obtaining the funding support necessary. We are actively pursuing funding sources at the current time. The implication of what we said in 2003, is that projections of inter vivos giving could be underestimates and projections of charitable bequests could be overestimates but the sum of the two would remain our overall but conservative estimate.

***2. In the new "simple" model in your notes, you did not use the most recently adjusted bequest figures for Giving USA. Can you please recalculate your model with the recently adjusted figures?***

*The figures are as follows:*

*1998: \$12.98-billion*

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*2004: \$18.56-billion*

The numbers you cite above are "current dollars". Our analyses are done in inflation-adjusted ("constant" or "real") dollars. If you look at Giving USA 2005, the inflation-adjusted estimates are on page 195. These values should correspond to the simple model and thus I think the note is correct as it stands.

The simple model is only meant to demonstrate the points I made about it in my notes. One point it demonstrates is that it would take an annual increase averaging 17% per year in charitable bequests in the next 14 years (assuming that GUSA estimates are valid) in order to achieve the 20-year wealth transfer estimates. In order for this to occur there would have to be the kind of growth in the value of portfolios of wealth holders comparable to the 1992-1998 period starting within the next few years. It is very likely that we will see a period of such growth in the next 55 years but problematic that it will occur in the next few years.

***3. You mention the lack of growth in household wealth ("it declined for three successive years [from 2000 to 2002] and only regained its 1999 level in 2004"). But didn't you know this in 2003 when you re-affirmed all your projections?***

I don't think we stated that we re-affirmed all our projections in 2003, specifically not the 20-year projections. Repeatedly we talk about the \$41 trillion estimate. We looked in great detail at the 2%, 55-year scenario and re-affirmed the \$41 trillion wealth transfer estimates. We were aware that there was at least a 2-year downturn in household wealth when we did this analysis in the fall of 2002 (note that the piece was released on Jan 6, 2003). The wealth data for all of 2003 was not

yet released and even that for the second quarter was only in a first release when we finalized the report in November of 2002. Regardless the point is that even a reduction in household wealth of two or even three year duration will have relatively small impact on the \$41 trillion 55-year estimate mainly because markets and the economy will rebound over 55 years. It always has since 1950 and there is every reason to believe that such dynamics are still in play. There is even a chance that it could rebound even in the next 14 years, but it is much less certain and would require a period of high rates of growth in household wealth (and consequently in value of final estates) as indicated in my notes.

***4. You also say in 7b of the notes that some wealth holders would give to children and other heirs during their life rather than waiting until death. But there has been no elimination of the gift tax. The gift tax makes it more attractive for the wealthy to pass along assets at death, particularly if there is no estate tax.***

Most of the "action" in wealth transfer occurs among wealth holders. From our case studies as well as anecdotal evidence, we find that they are often motivated by values and personal objectives at least as much as tax considerations. If they want their children to have some of their "inheritance" while the wealth holder is still alive to see them enjoy it and/or because they need it to start or maintain a business among other reasons, the transfer to their children becomes the wealth holder's personal objective. Given this objective, wealth holders may seek to transfer funds to their children in such a way as to minimize the tax burden. But the taxes are not the sole nor often the determining factor. The wealth transfer model is not based on minimization of taxes but on data that reflects patterns of behavior. Your point about gift taxes is valid but not necessarily determinative among households of high wealth.

A second point, a donor and spouse (if any) can each transfer some amount of funds to any individual (children, grand children, spouse of children, friend, etc.) each year without being subject to the gift tax. If this is done each year, the amount transferred to children without gift tax over a 15 to 20 year period can sum to millions for some households, depending on the number of children, the presence of a spouse, and any grandchildren and/or other recipients of the transfer. I don't have the current annual caps on such transfers at my fingertips but you can readily find them on the IRS web pages.

***5. You say in the notes: "No model is going to predict behavior 55 years into the future (or 20 years into the future) with close accuracy." If that is the case, why put out these estimates in the first place?***

Many large institutions (many nonprofits and financial institutions) undertake long range planning and base some of this planning on long range estimates. With respect to wealth transfer, in 1998 such institutions were using the \$10.4 trillion (circa 1990 dollars) as their ballpark estimate of wealth transfer for the period from about 1990 to 2045. This estimate was developed by Avery and Rendell initially in conjunction with work they were doing on savings behavior of wealthy heirs. Our 2003 piece indicates that their estimates did not cover the entire amount of wealth transfer even in 1990. We developed our model to provide a more comprehensive ballpark estimate that explicitly took account of the growth in household wealth via our three growth scenarios. If our estimate had come out to be \$8 trillion or \$12 trillion, it would have been in the

Avery and Rendell ballpark. It came out to be \$41 trillion which indicated a significantly larger and different ballpark. If there is no major long term disruption in the economy (such as another Great Depression or a nuclear attack) the \$41 trillion ballpark figure is still our best estimate for 55 years. When the 2004 Survey of Consumer Finances is released by the Federal Reserve, we will develop a new analysis of wealth and new wealth transfer estimates based on all the data available at that time. We think we can have these estimates available in late spring if the Fed releases the data by the end of March, as they have stated. When we first talked on the phone I mentioned these plans to you. I wish we had this analysis in hand now because it would address several of the questions you have raised.

***6. Some years ago, you published a study on the number of charitable remainder trusts that was later pulled off the Planned Giving Design Center's web site, because it was found that the methodology greatly overestimated the number of such trusts. Why was your methodology for charitable trusts flawed? Could a similar "over-projection" be occurring with the wealth transfer?***

The wealth transfer analysis and estimates are based on government data, a series of assumptions, and a microsimulation computer model that combines the data using the assumptions to produce the estimates. We have tested the computer model rather thoroughly while developing it. We found and fixed about a half dozen bugs. We think the computer model is accurately combining the data and assumptions as it was designed to do. If the estimates are not fulfilled, we look to the assumptions and/or an unlikely anomaly in the government data as the source of discrepancy or perhaps there could be a problem with the estimates against which the wealth transfer estimates are being compared. I will not replicate the information in my notes any further here, but the short version is that since 1999 we have not been experiencing the growth in household wealth that the model assumes and it is problematic that the amount of wealth can rebound sufficiently over the next 14 years to meet the 20-year estimates. There is an outside chance of a data anomaly and a possibility that the GUSA estimates are a bit low.

Now to the withdrawn study -- the "2003 Survey of Planned Giving Vehicles" was a survey of 1,010 participants representative of the population regarding their use and interest in nine vehicles of planned giving. We released the report in June, 2003. Before we released the report we checked the surveys' prevalence of wills and charitable bequests against the National Council on Planned Giving 2000 Report on Planned Giving. Their survey focused on charitable bequests in the general population and CRTs among high income households. We found our survey results concurred with theirs with respect to prevalence of wills and charitable bequests in the general population. We also checked the sociodemographics against the CPS to make sure that the sample was representative of the population. We then performed an analysis of the prevalence of use of planned giving vehicles and released the report. There was no model involved, just an analysis of the data from 1,010 participants using survey weights developed by the survey company, hired by a third party that cosponsored the study. In August a practitioner brought to our attention that our estimates appeared high. We immediately spent a week translating all the percentages into numbers of households and compared these estimates with partial data from a variety of sources. When looked at in terms of numbers it was clear that only the charitable bequest estimates in our survey were valid. Now the important point: we immediately published a letter withdrawing the study and explaining its shortcomings. We sent this letter to everyone on our mailing list; we

posted the letter on our web site; we sent the letter to both the Chronicle of Philanthropy and the NonProfit Times; we sent the letter to our research colleagues. We tried to identify all references to the study, and sent the letter to all of them. It is not just that this study was withdrawn, it is that we withdrew it, just as we will publish any new wealth transfer estimates that we develop this spring, however they turn out. As I recall the Chronicle published a story or at least a blurb based on our letter -- you should find it in your archives.

To amplify, the problem with the study was that the survey data was just wrong when it came to vehicles of planned giving other than wills and bequests. My guess now is that a general population has no idea what a charitable remainder trust is and some think it is the same as a charitable bequest. We expected to get a relatively high number of "Don't Knows" on these questions and we did get a relatively high number. In hindsight we also got a small, but biased toward the high end number of "Yes" I have used a charitable remainder trust as part of my planned charitable giving. As was mentioned above, there was no model or complex assembly of data in this study -- just a reporting of survey results and "bad" survey data.

I hope this information helps. Paul may want to expand on some of it.

Sincerely,  
- John

#### **Thursday, February 16, 2006**

Holly Hall wrote:

Hi John: I have two final questions, I really do think these are the last ones. (FYI: I hope to start writing tomorrow or Monday at latest, and I may be in touch after that to make sure I am representing your perspective accurately.) Thanks again for your prompt responses.

7. In the original wealth-transfer study released in 1999, you assumed that for estates of \$5-million to \$10-million, 15 percent will go to charity; for estates of \$10-million to \$20-million, 16 percent will go to charity; and for estates of \$20-million and more, 41 percent will go to charity. Aren't those percentages too high? For all estates that file estate tax returns (the wealthiest estates), the percentage is 7-8 percent, according to Giving USA researchers who have analyzed the IRS estate tax returns to come up with that figure.

8. As you noted in response to my fifth question, Avery and Rendell released their study, using 1990 dollars, before the wealth buildup of the roaring 1990s. You started when wealth was at historic highs in the late 1990s and compounded from there, assuming growth would continue. Even at the modest 2 percent rate of annual growth you assume, is it credible to start with an historically high number and just keep building on it for 55 years?...it would seem that this approach would lead to overstating the transfer.

#### **Friday, February 17, 2006**

John Havens wrote:

Hello Holly,

I am replying to your two final questions below: I am being somewhat more succinct because I have already spent quite a bit of time assembling and in some instances doing some new calculations in order to respond, and I am falling behind on the work I am paid to do. So here are the responses in somewhat abbreviated form.

*Holly Hall wrote:*

*Hi John: I have two final questions, I really do think these are the last ones. (FYI: I hope to start writing tomorrow or Monday at latest, and I may be in touch after that to make sure I am representing your perspective accurately.) Thanks again for your prompt responses.*

***7. In the original wealth-transfer study released in 1999, you assumed that for estates of \$5-million to \$10-million, 15 percent will go to charity; for estates of \$10-million to \$20-million, 16 percent will go to charity; and for estates of \$20-million and more, 41 percent will go to charity. Aren't those percentages too high? For all estates that file estate tax returns (the wealthiest estates), the percentage is 7-8 percent, according to Giving USA researchers who have analyzed the IRS estate tax returns to come up with that figure.***

Four points:

1. The estate tax data are not used in our analysis to estimate the value of wealth transfer but how it is distributed to heirs, taxes, nonprofits, and estate fees. The estimates of wealth transfer are independent of these of the distribution estimates. The estimates of charitable bequests, of course, depend on these estimates.
2. GUSA's estimate of 7-8 percent is based on all estate tax forms filed in any given year. The are three salient points:
  - a. the GUSA estimate includes estates where there is a surviving spouse (from memory, about 55-65% of the estates filed), and most estates with a surviving spouse have small, if any, charitable bequests -- our analysis assumed there was no charitable bequests from such estates but that the entire estate of a decedent spouse was left to the surviving spouse;
  - b. the GUSA estimate includes all asset levels and does not break out the data by asset class as our analyses have done; the bulk of estates in 1998 were in asset categories below \$5 million and there were a large number below \$1 million. Estates at these asset levels bequeath relatively small proportions to charity and the GUSA estimates include all the asset categories together.
  - c. the GUSA uses its estate data differently in its estimation process than we use it in our projection analysis and each of our sets of estimates are appropriate to our use.
3. The 1998 analysis was based on the estate tax data available at that time (a comprehensive series was not yet available on line as it is now nor in the SOI Bulletin). We use the same tax data that our colleagues in Indiana use but for each asset class reported by the IRS, we estimate the amount of funds available to final estates (no surviving spouse) by subtracting off debt and the

amount going to surviving spouse from this total. In each asset category we estimate aggregate charitable bequests as a percentage of the aggregate value of the estates net of debts and distributions to surviving spouse. These percentages rise non-linearly as the value of assets increase. At the \$20 M or more asset category these percentages have consistently been multiples of the percentages in lower categories. In 1997-1998 we had data for three years. From memory, the high end estimates were something like 38%, 41%, and 44%. We took the middle figures (which happened to be approximately the average as well). The estimates we used were based on a careful analysis of the estate tax data available at that time. If you could get us access to the micro-level estate tax data at the IRS or if you could get the IRS to tabulate the data for final estates separately, you would be doing a great favor for research on charitable bequests.

4. The percentages above bounce around from year to year, influenced by the economy but influenced even more by which particular wealthy people die in any given year and how much that small group of people bequeathed to charity. As I mentioned earlier, the estate tax filings also are delayed from the death of the wealth holder by a year or two for some wealth holders and less than a year for others. This makes it difficult to identify changes in trend based on two or three years of data.

***8. As you noted in response to my fifth question, Avery and Rendell released their study, using 1990 dollars, before the wealth buildup of the roaring 1990s. You started when wealth was at historic highs in the late 1990s and compounded from there, assuming growth would continue. Even at the modest 2 percent rate of annual growth you assume, is it credible to start with an historically high number and just keep building on it for 55 years?...it would seem that this approach would lead to overstating the transfer.***

Four points:

1. A quibble: the Avery and Rendell work was based on data from the Survey of Consumer Finances for 1998 [sic 1989] and (from memory) was adjusted for inflation to then current [sic 1990] dollars when it was released on or about 1990 [sic 1993].

2. In 1950 aggregate household wealth was \$915 billion (measured in 1950 dollars). If we adjust for all the inflation from 1950 to 2004, the \$915 billion in 1950 dollars becomes \$7.172 trillion in 2004 dollars. The 1950 figure was neither a low nor a high value for household wealth at that time. For demonstration purposes, let's bump it up by 20% as if it were much higher due to a run up in value back then. So we will use \$8.606 trillion as our 1950 baseline (knowing it is 20% higher than the amount that actually occurred). Now suppose we let this amount grow at 2% in real terms every year to 2002 (the recent low point in household wealth), the 2% growth in household wealth would result in household wealth of \$23.6 trillion in 2002 (expressed in 2004 dollars). The federal reserve data indicate that there was \$37.7 trillion of wealth in 2002 (also expressed in 2004 dollars) -- nearly 60% more than the 2% growth estimate. "Is it credible to start with an historically high number and just keep building on it for 55 years?" Well if we look at the history of household wealth and start with an artificially high number, let it grow at 2% compounded each year for 52 years we come up with a projection that is too low by about 60% from the low point in the recent trough in household wealth, I would conclude the answer is "yes, it is credible" -- maybe rather conservative.

3. I cannot foretell the details, but rest assured that there will be additional runups and downturns in the next 55 years that will, in aggregate, outweigh the fact that we based our 1998 projections on household wealth near the end of a period of rapid growth in household wealth.

4. I note that household wealth seems to be recovering from its recent slump, is on the increase once again, and has returned to about its 1999 level. I note that at the bottom of the trough, it had not fallen to its 1992 level, its 1993 level, its 1994 level, its 1995 level, or any other of the levels from 1992 through 1997, each of which was a new high for household wealth when it occurred. My point is that these "run-up" levels of wealth were not just "bubble" highs but represented real growth in wealth combined with a "bubble" effect that turned out to be maybe 15%-20% inflated due to an overheated and overvalued market. Even as household wealth increases at 2% or more in the next year or two, it will be a year or two after that before its full effect will be felt in the IRS data on charitable bequests.

Once again, I hope this helps. Since I have been spending a good deal of time helping you, I am wondering if you would agree to let me use your name if we decide to post my note, your questions, and my replies on our web page?

Thanks,  
- John

P.S. I apologize for typos and fragmented sentences.