



Charitable Remainder **Trusts**

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Knowing that you have a plan to achieve a particular financial goal is gratifying. It is even more gratifying when the plan not only accomplishes your goal, but also provides additional benefits.

Perhaps your goal is to make a significant donation to a favorite charitable organization. A charitable remainder trust (CRT) allows you to do that. Unlike making an outright contribution, however, using a CRT to make your gift lets you provide a noncharitable beneficiary (yourself or someone else) with an income stream from the donated assets. As an added benefit, a CRT offers tax advantages.

How a Charitable Remainder Trust Works

Trusts are a useful financial tool that can accomplish a variety of tax- and estate-planning goals. Under a trust arrangement, you transfer cash, securities, or other property to a trustee. The trustee then manages the trust assets for the benefit of the trust beneficiary/ies according to your instructions.

A charitable remainder trust has a dual purpose. The trust is established for a charity. However, the charity doesn't receive the trust assets immediately. Instead, the trust initially provides periodic payments to the trust's non-charitable income beneficiary/ies (yourself, yourself and your spouse, or your children, for example) for a specified term. When that term ends, the property remaining in the trust (the remainder) is given to the charity.

A Flexible Trust with Many Choices

A CRT is an irrevocable trust that you establish during your lifetime or create in your will. In addition to choosing a charity to receive the assets at the end of the trust term, you also choose one or more individuals to receive

payments from the trust (the *income beneficiary/ies*) during the trust term. And you decide how long the trust will last. The trust term can be for a set number of years (no more than 20) or for the life or lives of the noncharitable beneficiary/ies.

Your trust can take the form of a charitable remainder *annuity trust* or a charitable remainder *unitrust*.

Charitable remainder annuity trust. With this type of trust, the income beneficiary receives distributions of either a fixed dollar amount or a certain percentage (within the limits of the tax law) of the initial fair market value of the property placed in the trust.

Here's an example: Let's say you fund a charitable remainder annuity trust with \$250,000 in securities and direct the trust to pay a 5% annuity to the income beneficiary each year for ten years. Under these conditions, the income beneficiary receives \$12,500 a year for the term of the trust (\$125,000 total).

If the trust assets generate earnings that exceed the 5% payout amount, the amount the charity eventually receives will be greater than the amount you originally transferred to the trust. Conversely, if the trust assets earn less than the payout amount, the charity will receive less than the amount you put into the trust.

Charitable remainder unitrust. With this type of trust, the annual payout is a fixed percentage of the value of the trust property determined annually. So payments vary from year to year.

Let's say you set up a charitable remainder unitrust, fund it with \$500,000, and direct the trust to pay the income beneficiary 5% of the fair market value of the trust assets, valued annually. The first year, the beneficiary would receive \$25,000. But, if the value of the trust assets drops

to \$480,000 at the beginning of the second year, the beneficiary would receive only \$24,000 from the trust for the year. Conversely, if the value of the trust assets is \$520,000 at the beginning of the second year, the trust payment would be \$26,000 for the year.

Greater investment returns not only produce larger payments to the income beneficiary, they can also increase the value of the assets that eventually pass to the charity.

Add in Tax Advantages

There are several potential tax benefits associated with both types of CRT.

Income tax. Even though the charity you've chosen won't receive your gift until sometime in the future, you are eligible for a federal income-tax deduction (subject to limits) in the year the trust is established for the present value of the charitable remainder interest — the assets the charity will ultimately receive. Higher payments to the trust's income beneficiary/ies will reduce your deduction amount, while lower payments will increase it.

Capital gains tax. You may transfer appreciated stock or other assets to a CRT without incurring a capital gains tax liability. And, since a CRT is tax exempt, there will be no immediate capital gains tax liability if the trustee sells the assets. This leaves more money for reinvestment.

Gift tax. Creating a CRT during your lifetime will not have gift-tax consequences if you are the trust's only noncharitable beneficiary. However, if your trust will make payments to a noncharitable beneficiary such as your child, there will be gift-tax implications when you create the trust. The good news is that the value of your taxable gift will be reduced by the value of the charity's interest in the trust.

Estate tax. A CRT can help reduce estate taxes since amounts passing to a qualified charity are deductible for federal estate-tax purposes.

Charitable remainder trusts are a sophisticated planning option. And they can accomplish a variety of goals. Your professional advisors can help you decide if a CRT would be appropriate for you.

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