



The Charitable Remainder Trust: Giving, Getting, and Growing

Key Takeaways:

- **CRTs combine giving and financial benefits.** They offer a way to support charities while also creating income and tax advantages for the donor.
- **IRS rules and taxes require expert guidance.** Navigating the complexities of CRTs demands professional advice to ensure compliance and maximize tax savings.
- **CRTs can be tailored to fit individual financial and philanthropic goals.** Whether seeking stable income, tax reductions, or a lasting charitable legacy, a CRT can be structured to meet specific needs and objectives.
- **Diversify income and manage appreciated assets.** A CRT can help you avoid immediate capital gains taxes and create a diversified income stream.

Charitable giving is a powerful way to support causes you care about, but it can also be a strategic financial move. One sophisticated tool that combines philanthropy with potential financial benefits is the Charitable Remainder Trust (CRT).

WHAT IS A CHARITABLE REMAINDER TRUST (CRT)?

A CRT is an irrevocable trust that allows you to donate assets to a charity while retaining an income stream for yourself or designated beneficiaries for a specified period. When the trust term concludes, the remaining assets transfer to the chosen charity.

HOW IT WORKS

The process involves these key steps:

- **Establishment:** You create a CRT and transfer assets (e.g., stocks, real estate) into it. This initial step sets the foundation for the trust's operation.
- **Income Distribution:** The trust generates income, distributed to beneficiaries according to the trust's terms. This can be:
 1. A fixed annual amount (Charitable Remainder Annuity Trust - CRAT). This means you receive the same dollar amount each year, regardless of the trust's investment performance.
 2. A percentage of the trust's assets, revalued annually (Charitable



Remainder Unitrust - CRUT). This means your income varies based on the trust's annual asset value, providing potential for growth.

- **Charitable Remainder:** At the end of the trust term (a specific number of years or the lifetime of the income beneficiaries), the remaining assets are transferred to the designated charity, fulfilling the philanthropic purpose.

INCOME PRODUCTION AND DISTRIBUTION

The trust's income is derived from the assets held within it. For example:

- **Stocks generate dividends and capital gains.** This allows the trust to benefit from market appreciation and regular income.
- **Bonds produce interest payments.** Providing a more stable, predictable income stream.
- **Real estate may yield rental income.** Offering a potentially significant and consistent income source.

In a CRAT, a fixed dollar amount is paid annually, irrespective of the trust's performance. Conversely, a CRUT pays a fixed percentage of the trust's assets, revalued annually. The trust's trustee manages investments and distributes income according to the trust's terms.

TAXATION OF INCOME DISTRIBUTIONS

Income distributions from a CRT are taxable to the beneficiaries. The character of the income is retained when distributed, and taxed according to a "tier" system:

- **First, from ordinary income (e.g., dividends, interest).** This is typically taxed at the beneficiary's ordinary income tax rates.

- **Next, from capital gains.** These are taxed at the applicable capital gains tax rates.
- **Then, from tax-exempt income.** This income may be tax-free, depending on its source.
- **Finally, as a return of principal.** This portion is generally not taxed as income.

TAX BENEFITS

The CRT provides several significant tax advantages:

- **Immediate Income Tax Deduction:** For the present value of the charitable remainder interest, calculated using IRS tables. This reduces your taxable income in the year of the donation.
- **Capital Gains Tax Avoidance:** On the appreciation of donated assets at the time of transfer. This avoids immediate taxation of gains.
- **Estate Tax Reduction:** By removing the assets from your taxable estate.

EXAMPLE OF TAX SAVINGS

Imagine donating appreciated stock worth \$1,000,000 (cost basis \$200,000) to a CRUT.

Without the trust, selling triggers \$800,000 in capital gains. With a CRT, you avoid these gains. The IRS calculates your charitable deduction at, say, \$400,000. However, deductions are limited by your Adjusted Gross Income (AGI):

- For appreciated long-term capital gain property, the limit is typically 30% of your AGI (public charities). This means you can only deduct up to 30% of your AGI in the year of the donation.

If your AGI is \$500,000, you deduct \$150,000 this year and carry forward \$250,000 for up to five years, subject to AGI limits. Strategic timing and professional advice are crucial.



IRS REGULATIONS

The IRS has stringent regulations for CRTs:

- **Trust must be irrevocable.** This means you cannot change the trust's terms once it is established.
- **Remainder beneficiary must be a qualified charitable organization.** This ensures the charitable intent of the trust.
- **Specific payout requirements.** These dictate the minimum percentage or amount that must be distributed annually.
- **Actuarial calculations for deductions.** These are used to determine the present value of the charitable remainder interest.
- **Detailed trust document requirements.** These ensure the trust complies with all IRS rules.
- **10% remainder rule.** This stipulates that the present value of the charitable remainder must be at least 10% of the initial contribution.

CONCERNS AND CONSIDERATIONS

Important considerations include:

- **Irrevocability of the trust.** This limits your ability to access or alter the trust's assets.

- **Impact of payout rate on income and deductions.** Higher payout rates mean more income but a smaller charitable deduction.
- **Complexity and costs.** Setting up and administering a CRT involves legal and administrative expenses.
- **Investment risk affecting income.** The trust's income is tied to the performance of its investments.
- **Choice between CRAT and CRUT.** This depends on your financial goals and risk tolerance.
- **Need for professional advice.** Expert guidance is essential to ensure compliance and maximize benefits.
- **Charity selection due diligence.** Careful research is needed to choose a reputable and suitable charitable beneficiary.

CONCLUSION:

A Charitable Remainder Trust can be a valuable tool for combining charitable giving with financial benefits. Understanding tax advantages, IRS regulations, income generation, and potential concerns is key. Careful planning and professional guidance are essential.

Disclaimer: This article is intended for informational purposes only and should not be construed as legal or financial advice. It is imperative to consult with qualified professionals to address your specific needs and circumstances.