# "Giving" Advice

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TCF "GIVING" ADVICE NEWSLETTER

ABOUT YOUR FOUNDATION

Since 1973, the **Toledo Community Foundation** has provided individuals, families and businesses interested in the well-being of our community with an *efficient, effective, low-cost, professionally managed* mechanism to achieve their charitable goals.

For philanthropists wishing to maximize the impact and life of their charitable gifts, the Foundation provides *resources for thoughtful giving*. Using its expertise and personalized services, **Toledo Community Foundation** helps donors

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## CRUTS and CRATS

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**By Kevin McKinley**

April's column discussed charitable lead trusts, and why the vehicles might be an optimal solution for wealthy clients who wish to give more money to charity in the near term and family in the long term, and less to Uncle Sam forever.

But CLTs aren't for everyone. Specifically, they may not be the best idea for older clients who would like a nice income in return for their donations.

For those individuals, it may be better to consider a close sibling of CLTs: charitable remainder trusts. CRTs might be best for those who want tax deductions and income now, with an eventual benefit going to the charity of their choice.

### A Primer

As you no doubt remember from last month, CLTs usually provide the donor with near-term tax advantages, and an income stream to one or more chosen charities for a specified period. Then any remaining amount goes to heirs, usually family members, ideally free from estate taxes.

Like CLTs, charitable remainder trusts also offer tax inducements. But the money flows the opposite way: The income stream typically goes to the donor, and whatever's left over goes to charity.

### How It Works

In most instances, the donor places highly appreciated assets in the

transform their philanthropic impulse to measurable community impact. Beyond the gifting of assets, the Foundation helps donors identify issues of importance to them and *inspires engagement* with community organizations addressing these issues, thereby maximizing the impact of charitable gifts and creating a greater sense of fulfillment.

charitable remainder trust. The trust then sells the assets, and since there is a charitable beneficiary, no capital-gains taxes are owed. The trustee then reinvests the sales proceeds into a portfolio that is more suited to the donor's current goals—perhaps more diversified, or focused on generating income.

The current income generated by the new investments usually goes to the donor and/or his spouse, for a period based on their life expectancies, or a fixed term (not to exceed 20 years).

The income from the CRT can either come in the form of an annuity ("charitable remainder annuity trust," or CRAT), or a percentage of assets in the trust ("charitable remainder unitrust," or CRUT).

The CRAT requires a minimum of at least 5 percent of the initial value of the asset in the trust to be paid out each year. Once established, the figure does not change, regardless of the performance of the assets in the trust.

The CRUT requires that at least 5 percent of the annual value of the trust be paid out, with several other sub-variations available to the donor. The CRUT, unlike the CRAT, allows for future deposits from the donors.

Under certain circumstances, donors may be able to delay the income payments until a more optimal time, such as when the beneficiaries retire and are in need of more income, as well as in a lower income-tax bracket.

Once the term (or the donors) expire, any money left over in the trust goes to the designated charities. Although the initial gift to the trust is irrevocable, the trustee, income recipients, and final charity recipients can all be changed.

**Tax Savings**

There are several ways that a CRT can reduce a client's current and future tax bills. First, the client gets an immediate income-tax deduction based on the estimated present value of the money that will eventually go to charity.

The factors that determine this deduction include the size of the gift, the expected length of the income stream (i.e., beneficiaries' life expectancies, or a pre-established term) and the current "applicable federal rate"—available in Publication 7520 at www.irs.gov.

Since the assets donated will be sold within the CRT, there will be no capital-gains taxes either. Finally, the gifted asset is removed from the client's estate, avoiding potential "death taxes."

**For Example**

Jim and Ann are a 60-year-old married couple. They are retiring at the end of this year from their high-paying jobs. They have a stock position worth $500,000, with a $50,000 cost basis that they would like to donate to a qualified charity.

They create a charitable remainder trust, and donate the stock to the trust. The shares are sold with no capital-gains tax due. Jim and Ann decide on a 5 percent annual annuity rate for the income from the trust assets to last for the next 10 years.

According to the tools at www.pgcalc.com, they get a current income-tax deduction of almost $290,000. They will also get $25,000 per year for the next 10 years. Then whatever is left over will go to the charity (or charities) of their choice.

**But What About the Children?**

Although the benefits of CRTs to both donors and charities are clear, some interested parties may not be so enamored with the strategy: Specifically, the donors' descendants—who may end up eating from a smaller pie when the donors pass away.

Clients who are concerned about what's left for future generations may prefer to establish a wealth replacement trust at the same time the CRT income kicks in.

Let's say Jim and Ann want to provide for their children, but only after the couple have passed away. They choose to establish a second, irrevocable trust that will hold a second-to-die life insurance policy, with the policy premiums paid for by some, or all, of the income generated by the CRT.

Assuming the trust and life insurance policy have been funded and structured properly, when Jim and Ann have both died, the beneficiaries of the trust (i.e., the family members) would receive the policy death benefit—free from estate taxes.

**Don't DIY**

As compelling as this strategy seems to be, don't take it much beyond the "suggestion" stage without bringing in the experts to do the proverbial heavy lifting.

The client's preferred charity may have a planned-giving expert on staff who can guide you and your client through the initial steps. The client's CPA or tax adviser should be kept in the loop too.

In a shocking development, most charities prefer the charitable lead trust discussed last month, because the CLT gives them their due much sooner than the CRT normally would. But wise organizations will gladly accept donations later rather than never.

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