

CHARITABLE REMAINDER TRUSTS

1. Introduction

A Charitable Remainder Trust (“CRT”) is a split-interest trust under which one or more non-charitable beneficiaries receive annual payments for a designated term, and one or more charities receive the remainder of the trust property at the end of the designated term. The term can be a set number of years (not to exceed 20) or for the life or lives of the non-charitable beneficiaries. The annual payments to the non-charitable beneficiary or beneficiaries can either be defined as a fixed annuity amount (an “Annuity Trust”) or as a fixed percentage of an annually reappraised value of the trust (a “Unitrust”). A second type of Unitrust pays an annual amount equal to the lesser of the net income of the trust or the fixed percentage times the market value. If the net income is less than the amount determined by the fixed percentage in one year, it may be recouped in a later year when the income exceeds the amount determined by the fixed percentage.

2. Tax Benefits

There are two significant tax benefits associated with gifts to a CRT. The first tax benefit is the availability of a charitable income tax deduction upon the establishment of the trust. The deduction equals the difference between the value of the assets contributed and the present value of the annuity or unitrust interest, determined under the IRS actuarial tables. In general, the present value of the annuity or unitrust interest is dependent upon the payout rate, the term of the trust and the applicable federal rate at the time of the contribution.

The second tax benefit is that the trust is tax-exempt, except as to unrelated business income. This enables the trust to sell highly appreciated property without paying capital gains taxes. Further, if the trust realizes ordinary income in excess of what is paid out, the excess is not subject to tax. Even though the trust is tax-exempt, the non-charitable beneficiary is taxed on payments received based on a tier system. Distributions are first treated as made from ordinary income (including undistributed ordinary income from prior years), next from capital gains (including undistributed capital gains from prior years), next from tax-exempt income, and finally from principal.