The Power of Charitable Remainder Trusts

Do well by doing good

A growing number of individuals and families want to use some of their wealth to support the causes and organizations they care about most. From helping those less fortunate to facilitating scientific breakthroughs, from providing safe habitats for wildlife to sharing the arts, philanthropy is a core value for many.

Of course, it's important to engage in smart philanthropy by using certain tools and strategies that can help you have a much bigger charitable impact than you otherwise could—while simultaneously enhancing your own financial flexibility.

In short, philanthropic planning can help you—as the old saying goes—"do well by doing good."

With that in mind, here's a closer look at one philanthropic tool that many charitably minded people and families use: **charitable remainder trusts.** CRTs can be extremely useful and powerful wealth planning tools that allow you to have a major impact on a charity you value while also providing benefits like lower taxes and a regular income stream.

The ABCs of a CRT

Let's start with some CRT basics and benefits.

- **Income stream.** You place money or appreciated assets in a CRT, which then provides an annual income stream. You can designate yourself or other people to receive that income. The income stream can last for your life or the lives of the people you designated. You can also have the income stream last for a term of years (within limits).
- **Tax-deferred growth.** The assets in the CRT grow tax-deferred. You are taxed only on the income you receive from the CRT.
- **Charitable impact.** Once the term of years is up or the last beneficiary dies, the income stream stops and the assets that remain in the trust go to one or more charities you selected.
- **Tax deduction.** When you create and fund the CRT, you get an income tax deduction—the size of which is based on the actuarial value of the remainder that the charity should receive.
- **Capital gains tax avoidance.** You can gift appreciated assets to a CRT without paying capital gains taxes. For example, say you have $1 million worth of stock that you bought 20 years ago for $200,000. You could sell that stock—and pay $160,000 in capital gains taxes (assuming a 20 percent rate)—leaving you with $840,000 to use for your philanthropy. Or you could gift the shares to the CRT and pay no capital gains taxes at all—funding the trust with the full $1 million.

TYPES OF CRTs

- ☑ **Charitable remainder annuity trusts.** With a CRAT, you or your designated recipient receive a fixed dollar amount from the trust every year. However, once you set the amount, it cannot be changed. Say, for example, you set the annual amount at $15,000. That is all you can receive every year, even if the assets in the CRAT are growing at a tremendous rate. Additionally, you cannot add assets to a CRAT once it's set up and funded.
- ☑ **Charitable remainder unitrusts.** With a CRUT, you (or the person you designate) receive a percentage of the current value of the assets in the CRUT. Example: You specify that you want to receive six percent of the assets in the trust annually. Every year, the assets are reappraised and you get six percent of that amount. Another difference: You can add more assets to a CRUT.

CRAT vs. CRUT

Type	Income distributions	Additional contributions
Charitable remainder annuity trust (CRAT)	A fixed amount each year	Not allowed
Charitable remainder unitrust (CRUT)	A fixed percentage based on the assets in the trust, revalued annually	Allowed, if governing trust instrument permits and unitrust amount takes into account the additional contribution

You can use a wide variety of assets to fund a CRT. Some examples include:

- Cash
- Stocks and bonds
- Some types of closely held stock (such as limited liability corporations, but not S corporations)
- Real estate
- Artwork and collectibles

Case study

Let's start with some CRT basics and benefits.

To see the potential power of a CRT, consider this example of funding a CRT with appreciated stock:

An investor in her 40s purchased $600,000 of stock in a new company. After a few years, those shares were worth $1.8 million. If she cashed out, she would have to pay capital gains taxes of 23.8 percent on the $1.2 million of appreciation—leaving her with a tax bill just shy of $300,000.

Instead, she and her advisors set up a CRUT, which enables her to add more assets in the future. The CRUT will last the shorter of 20 years or her lifetime. She will receive 12 percent of the assets each year—or just over $200,000 the first year. Over the course of 20 years, using assumptions of a return of 8 percent annually, she will receive approximately $2.9 million. She will receive a $180,000 charitable deduction. And at the end of the 20-year term, the charitable organization she chose will receive approximately $700,000.

Two caveats

The right intention is crucial. If you use a CRT, you must have a genuine charitable intent. The reason: A CRT is an irrevocable trust—once you put assets in a CRT, you cannot get them back.

It's not a personal piggy bank. At least 10 percent of the actuarial value of the CRT must go to charity. A CRT that does not meet the 10 percent remainder requirement is not a qualified charitable remainder trust and will lose its tax benefits.

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