

Two Charitable Trusts that Provide Dual Benefits

Two popular charitable giving vehicles are charitable remainder trusts (“CRTs”) and charitable lead trusts (“CLTs”). They are what's known as "split-interest" trusts. Why? Because of their dual beneficial interests: They can benefit a favorite qualified charity as well as non-charitable beneficiaries, such as your loved ones or even yourself.

Let's take a closer look at CRTs and CLTs.

CRTs Benefit Charity *Last*

A CRT provides non-charitable beneficiaries with exclusive rights to all distributions until their interests have terminated. At that time, charitable beneficiaries receive the *remainder* — the assets left over in the trust.

A CRT can be a particularly useful tool if you'd like to divest yourself of a highly appreciated asset to diversify your portfolio but are concerned about the capital gains tax. You create a CRT, name yourself the non-charitable beneficiary and transfer the appreciated asset to the trust. Then, the CRT can sell the asset (tax-free to the trust because the CRT is tax-exempt) and use the proceeds to purchase diverse, income-producing assets.

You can receive annual payments from the trust for a specified period of up to 20 years or for your lifetime, increasing your cash flow. A portion of each payment may be taxable to you based on the income earned or capital gains recognized by the trust. You might, for instance, have capital gains income attributable to the sale of the highly appreciated shares you transferred to the trust. But the gain you report will be spread out and taxed to you only as you receive payments.

In addition, you'll enjoy an immediate income tax charitable deduction on creation of the trust, calculated as the present value of the charity's remainder interest. You also can enjoy recognition within the charitable organization(s) and community as a result of the contribution, unless you prefer to donate anonymously.

If you're concerned that, should you die early in the CRT's existence (before you've received many payments from it), there won't be enough assets in your estate for your heirs to receive the inheritances you intended, there are two potential solutions:

- 1. Set the CRT term for a specific number of years** (rather than your lifetime) and name your heirs as contingent beneficiaries. Then, regardless of whether you live for one day or the entire term, you know that your loved ones will be provided for. In other words, either you or your heirs will receive the annual distributions for the whole term.
- 2. Purchase a life insurance policy** to make up for the shortfall your heirs might experience.

Finally, keep in mind that, you can name someone other than yourself as a non-charitable beneficiary and even fund the trust at your death, but the tax consequences will be different.

CLTs Benefit Charity *First*

A CLT reverses the timing of when the charitable and non-charitable beneficiaries receive distributions: The charitable beneficiaries receive the initial distributions and the non-charitable beneficiaries receive the remainder.

When can it be useful? A CLT can be helpful when an asset generates substantial income every year, you don't need the income and you wish to eventually pass the asset to your heirs. The CLT generates an income stream for the charity during the trust term, and at your death (or the end of the CLT term, if you've set it for a specific number of years) the asset passes to your family.

If structured as a grantor trust, the trust is essentially disregarded for income tax purposes, and a CLT then works similarly to a CRT in that you receive an immediate income tax deduction on the transfer of assets into the trust. But in subsequent years, the income generated by the CLT will be taxable to you. If you don't structure it as a grantor trust, the CLT income won't be taxable to you, but you also won't get an income tax deduction when you fund the trust.

Unlike a CRT with you as the non-charitable beneficiary, a CLT has a gift tax component, which is calculated as the present value of the non-charitable beneficiary's remainder interest. As with CRTs, CLTs can also be funded at your death, but the tax consequences will be different.

Examine Your Options

If philanthropy is important to you, consult with your estate planning advisor about whether a CRT or CLT can benefit your long-term plans. These split-interest trusts can benefit not only the qualified charities you support, but also you and your family.

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