UTILIZING CHARITABLE REMAINDER TRUSTS TO MEET INCOME & PHILANTHROPIC

BY SO SUM LEE, CPA

Philanthropy is generosity in all forms and is often defined as the act of giving to better the lives of others.

Monetary donations go a long way to fund projects that provide resources to those in need. According to Giving USA, Americans donated more than $1 billion a day to various charities in 2022, resulting in close to $500 billion in contributions. This impressive amount comes from philanthropic individuals who want to support good causes.

Aside from the traditional mailing of a check, many charities now take donations electronically through their websites. Donor-advised funds can be set up, or for the more sophisticated philanthropists, a private foundation can be considered. Regardless of what method is used, once the donation is made, the money becomes out of reach. So what happens if you want to make a donation, but are not ready to completely give up your assets? What can you consider?

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A **charitable remainder trust** can be a useful tool to help you plan donations to charities that you support after you pass away. The charitable remainder trust will provide you with a predictable income stream for life or over a specific period of time. When the trust terminates, the charities of your choosing will receive the remaining balance in the trust. You get a charitable deduction at the time the money is funded into the trust based on your age, the term of the trust, and the amount of the annual distribution to you.

TYPES OF CHARITABLE REMAINDER TRUSTS

There are two types of charitable remainder trusts — charitable remainder annuity trust and charitable remainder unitrust.

A **charitable remainder annuity trust (CRAT)** pays a specific dollar amount each year to noncharitable beneficiaries, typically yourself. The payments must be at least 5% but no more than 50% of the value of the assets initially funded into the trust. The value of the remainder interest passing to charity must be at least 10% of the initial net fair market value of all property placed within a CRAT.

A **charitable remainder unitrust (CRUT)** pays a percentage of the value of the trust assets each year to noncharitable beneficiaries, typically yourself. The payments must be at least 5% but no more than 50% of the fair market value of the assets valued annually. The value of the remainder interest must be at least 10% of the contributed property value. A CRUT allows subsequent contributions into the trust. The 10% remainder requirement must be met for each contribution.

CHARITABLE DEDUCTIONS

When you set up a charitable remainder trust during your lifetime, you will receive a charitable deduction equal to the present value of the remainder interest that the charities are expected to receive. You can fund the trust with cash, securities, or other real or personal properties. If you do fund the trust with appreciated assets, you are not required to recognize the gain on the contribution of appreciated assets to the trust and the trust pays no tax on the sale of those assets.

TAXABILITY OF PAYMENTS RECEIVED BY NONCHARITABLE BENEFICIARIES

A charitable remainder trust is not subject to tax. However, payments from a charitable remainder trust to noncharitable beneficiaries are taxable to the beneficiaries up to the trust's income, either generated in the current year or from the prior year's cumulative undistributed income. Payments that are more than income are considered as corpus or "principal" of the trust and are not subject to tax.

> ***KROST Insight:*** *Since only payments, up to income, are subject to tax, when the trust sells assets with a large gain, tax is deferred for the portion that is retained by the trust and thereby will increase future payments to beneficiaries under a CRUT.*
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> ***KROST Insight:*** *A charitable remainder trust may be beneficial for high-income donors or noncharitable beneficiaries who are subject to net investment income tax. By transferring assets to the charitable remainder trust, the donor may be able to stretch the investment income over a longer period of time, thereby allowing the donor/noncharitable beneficiary to stay under the modified adjusted gross income threshold.*

ESTATE & GIFT TAX CONSIDERATION

For a charitable remainder trust that is set up during the donor's lifetime, if the noncharitable beneficiary is someone other than the donor, the trust's remainder generally is not included in the grantor's estate. If the donor is the noncharitable beneficiary, the rules become more complicated.

A charitable remainder trust is a very complex arrangement, but it is also an invaluable planning tool in the right circumstances. If you would like to learn more about charitable remainder trusts, please contact our team of Estate & Gift, Trust and Probate specialists.

Note: Any changes to your estate plan must be drafted by your attorney.

About KROST's Estate & Gift, Trust and Probate Services

Our estate planning team assists with the transition of family wealth and estate succession. Our team of experts has over 90 years of combined experience working with family-owned and privately held companies, as well as high-net-worth individuals. Our primary goal is to assist individuals and their attorneys to effectively transfer wealth while minimizing unnecessary estate, gift, and generation-skipping taxes. In addition, we can coordinate all of your Estate & Gift, Trust and Probate needs to ensure a smooth transition while minimizing emotional, tax, and administrative burdens. Contact us today.

We are offering a free preview of the planner for download. Schedule a call to assess your situation for access to the full book.

There is no better time to start, and it is never too early.

Would you like assistance with your Estate Plan? [Douglas Venturelli] and [Richard Umanoff] are available to review your current estate plan, provide recommendations, and consult with your estate attorney.

About the Experts

So Sum Lee, CPA, Principal
Tax, Real Estate, Hospitality, Estate & Gift, Trust and Probate
So Sum Lee is a Tax Principal at KROST. So Sum has over 25 years of experience in public accounting and has a wide range of experience in Taxation, as well as servicing high-net-worth clients. So Sum's area of expertise includes industries such as wholesale, real estate investments, and restaurants. » Full Bio

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Douglas A. Venturelli is a Principal at KROST. He has over 45 years of experience in tax, estate, and business services. His main focus is federal estate and gift taxes. Doug consults with clients in the entertainment, legal, real estate, and medical industries. » Full Bio

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Richard Umanoff is a Principal at KROST. Richard's career spans over 45 years, with a concentration in taxation. His primary emphasis is estate and trust tax compliance, planning, estate administration, and probate court accounting. Richard currently serves in the role of trustee for numerous clients. » Full Bio