INTERVIVOS CHARITABLE REMAINDER UNITRUST
(SINGLE PERSON IS INCOME BENEFICIARY)
(CHARITY IS REMAINDER BENEFICIARY)

HIGHLIGHTS OF THE PLAN

OVERVIEW

A Charitable Remainder Trust (CRT) provides a Donor with a current income tax charitable deduction and a stream of income. It also gives one or more charities designated by the Donor what's left in the Trust when the Trust ends.

It works like this. The Donor works with an attorney who drafts a CRT document in which a Trustee is named to invest and manage the property transferred to the Trust. One or more charities is named to receive the property when the Trust terminates. The Donor can generally be the Trustee of the Trust. The Donor transfers cash or other property to the Trust and receives a charitable deduction equal to the present value of the remainder interest that will ultimately go to charity. This present value is determined through the use of government tables and a specified formula. A CRT may last for a term of years up to 20 years or for the lifetime or joint lifetimes of the income beneficiaries.

Amounts received by an income beneficiary are subject to income tax in accordance with the character of the income in the CRT. Distributions from the CRT are deemed to be received in the following order: (1) ordinary income, (2) capital gain, (3) tax-free income, and (4) return of basis. So, to the extent a CRT has ordinary income, such income will be distributed first, then capital gain, etc.

TYPES OF CRTS

There are essentially two main types of Charitable Remainder Trusts: Charitable Remainder Annuity Trusts (CRATs) and Charitable Remainder Unitrusts (CRUTs). A Charitable Remainder Annuity Trust pays the Donor a fixed percentage of the initial amount of property transferred to the Trust. For example, a contribution of $100,000 to an annuity Trust would provide a payout of $5,000 in the first year and each year thereafter. The payout percentage has to be at least 5% percent but no more than 50%.

A Charitable Remainder Unitrust pays a fixed percentage of the value of the Trust property as valued each year. For example, a contribution of $100,000 to a Unitrust would provide a payout of $5,000 in the first year. If the Unitrust property had an investment return of 8%, the second year payout would be 5% of $108,000, or $5,400., and so forth. Again, the payout percentage has to be at least 5% but not more than 50% percent.

There is a special type of CRUT called a Net Income with Make-up Charitable Remainder Unitrust, also known as a NIMCRUT. This Trust permits a payout based on the lesser of a stated percentage or actual Trust income. A NIMCRUT enables a Trustee to fund the Trust with property that does not produce an income. The property (often an annuity) simply sits in the Trust and increases in value until income from the Trust is desired, such as at retirement.

If an annuity is used to fund the NIMCRUT, at an appropriate time the Trustee will take taxable withdrawals from the annuity equal to the maximum Unitrust amount (including the make-up amount) and pass the withdrawals through to the Donor. The growth of values in an annuity are generally tax-deferred until withdrawals are made from the annuity. However, no case or ruling has addressed the issue of whether the "non-natural person" rules of IRC Sec. 72(u) apply to an annuity owned by a NIMCRUT. Sec. 72(u) provides generally that annuities owned by a "non-natural person," such as a corporation or a trust, will be subject to tax each year as interest in the annuity accrues instead of when withdrawals are made or annuitization occurs. However, the IRS has interpreted the "non-natural person" rules very narrowly by holding that a Trust that owns property for the benefit of a natural person is not subject to the "non-natural person" rules of Sec. 72(u). Since a NIMCRUT does not pay accounting income (interest and dividends) as defined by state law until withdrawals are actually made, and no income taxable amounts are actually realized by the Trustee, it is likely that no income need be recognized by the Trust until amounts are actually withdrawn.

If assets other than an annuity, such as growth stocks, are used to fund the NIMCRUT, the Trustee will sell the stock at retirement or other time when income is desired and invest in income producing investments. It is better that someone other than the Donor be the Trustee of a NIMCRUT.

INTERVIVOS OR TESTAMENTARY

A Charitable Remainder Trust may be created during the Donor’s lifetime (Intervivos Trust) or at death in the Donor’s will (Testamentary Trust). For obvious reasons, the income interest in a Testamentary CRT will be payable to the Donor’s spouse or other beneficiary and not to the Donor’s estate. When someone other than the Donor or the Donor’s spouse is the income beneficiary of a CRT, the income beneficiary’s interest is considered for estate and gift tax purposes to be a taxable transfer from the Donor to the beneficiary.

As a general rule, the Donor who establishes a CRT will also establish what has come to be known as a Wealth Replacement Trust (WRT) to replace the assets transferred to the CRT for the benefit of the Donor’s family. The WRT is simply an Irrevocable Life Insurance Trust (ILIT) that owns a life insurance policy on the life of the Donor with a face amount equal to the value of the property transferred to the CRT. The net effect of using a Wealth Replacement Trust is to keep the Donor’s estate from shrinking and give property to charity as a donation instead of to the government in transfer taxes.

ADVANTAGES TO THE DONOR

1. The Donor receives a current income tax deduction equal to the present value of the remainder interest that will ultimately go to charity.
2. The Donor and/or designated income beneficiary receives an income stream from the CRT.
3. The Donor avoids capital gains tax on appreciated property transferred to and later sold by the CRT.
4. Interest and other income grow tax-free within the CRT.
5. The Donor's future estate taxes are reduced.

ADVANTAGES TO THE CHARITY

1. The charity receives a gift that it might not receive in the absence of a CRT.
2. The charity receives a larger gift than the Donor could normally give.
3. Deferred gifts using a CRT do not generally interfere with the Donor's current gifting.

DISADVANTAGES TO THE DONOR

1. The assets in the CRT are inaccessible.
2. The CRT is irrevocable, which means that the property given to charity is gone forever.
3. Because of the complexity in setting up and operating a CRT, the document must be drafted by an attorney and administered by a professional administrator.

DISADVANTAGES TO THE CHARITY

1. The charity must wait to get the property transferred to the CRT.
2. The charitable beneficiary may be named as a class and one or more charities may be dropped from the list of charitable beneficiaries or never be added to the list.
3. The charity may be unaware that a gift will be coming when the CRT ends.