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The Charitable Remainder Trust-Part 1

In this newsletter, I will describe the basics of the Charitable Remainder Trust. In part 2, I will follow up with answers to the most asked questions regarding the benefits and regulations of this type of Trust.

If you own a highly appreciated asset (such as stocks, real estate or a business) -- and if you'd like to sell the asset, I recommend that you consider a Charitable Remainder Trust (CRT). With a CRT, you can receive lifetime income, reduce taxes, help charity and pass your entire estate to your heirs

A CRT allows you to donate your property to charity -- lower your income and estate taxes -- and help a charity that is important to you. Plus, with the money you save, you can buy a life insurance policy that replaces the asset you transferred from your estate so your children don't lose any of their inheritance.

A CRT is simply an Irrevocable Trust into which you transfer your highly appreciated asset. The trustee (Trust manager) sells the asset at full market value and pays no capital gains tax on the sale. Then the Trustee invests the proceeds in other assets. The CRT pays you and your spouse an income for the rest of your lives. After you and your spouse die, the remaining Trust assets go to the charity you selected. When you set up the Trust, you can name one or several charities to receive your assets, as long as they are charities that qualify with the IRS. You can also retain the right to change the charitable beneficiaries, as long as they are also qualified charities.

Since you are donating the asset to charity, you reduce your income taxes now. And since you transferred the asset out of your estate, when you die, your heirs pay no estate taxes on that asset.

What types of assets are best suited to a Charitable Remainder Trust? You benefit the most when you donate assets that have greatly increased in value while you have owned them. These include real estate, stocks, other securities, and businesses. In most cases, you cannot donate real estate that has a mortgage against it. However, you may benefit enough from this arrangement to justify paying off the loan in full.

The selection of the proper Trustee for the Trust is very important in a CRT. You must make sure the Trust is managed correctly. Otherwise, you could lose the tax benefits and suffer penalties. The best Trustee is a person or corporation experienced with investments and accounting. You can serve as Trustee or you can select a corporate Trustee, such as a Trust Company or Bank. Or you can name the charity to manage the Trust, if they agree to provide this service. You should interview several potential Trustees and look at their experience managing investments before you decide. Since you are relying on the Trustee to make sure you have income the rest of your life, this decision is important.

Can you just sell the asset and invest the money yourself? Yes, but you'll have to pay a significant tax bill, so you'll receive less income. Here's an example:

John and Mary Smith (ages 65 and 62) are planning to retire next year. Fifteen years ago they bought 20 acres of real estate for $200,000. Today, a city has grown to within one-half mile of the property, which is now worth $2,000,000. The Smith's would like to sell the land so they can retire and use the money during their senior years.

If they sell the acreage, they would have a gain of $1,800,000 (its current value less what they paid for it). They would have to pay $360,000 in federal capital gains tax (20% of $1,800,000), which would leave them with $1,440,000.

If they invest the money and earn a 5% return, they would have a yearly income of $72,000. If their joint life expectancy is 22 years, they would receive a total lifetime income of $1,584,000 before taxes. Of course, they receive no tax deduction if they sell the real estate.

CRT's are very rewarding estate planning tools, but can be complicated to set up. However, the benefit outweighs the burden. If you have these types of assets, I suggest you set up a consultation with a qualified estate planning attorney and your financial advisor to discuss how this type of Trust may benefit you and your family.

Anthony J. Medico, Esq., *has practiced law for over 27 years. To ask a question regarding this article, send an e-mail to info@medicoandassociates.com or call us at (203) 661-8151. To read more highly informative Estate Planning articles, visit our website at www.medicoandassociates.com, where you can also download our free Estate Planning Survival Guide. Enjoy.*

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