What is a Charitable Trust

By Kevin McGrath, Vice President

A charitable remainder trust, often referred to as a CRT, is an irrevocable trust that creates a steady stream of income for a donor or other beneficiaries. The donor or beneficiaries receive an income stream from the trust for either a set term of years or for the life of the last remaining beneficiary. At the end of the term, the remainder of the assets in the trust go to the designated charity(ies). Donors can combine their charitable remainder trust with a donor-advised fund (DAF) by transferring the remainder of the asset funds to a public charity that sponsors a donor-advised fund. This strategy offers donors more control and flexibility to adjust and recommend grants with the donor-advised fund.

Two types of charitable remainder trusts

There are two types of charitable remainder trusts. The main difference is how the trust agreement defines the income interest. To receive the benefits of a qualified charitable remainder trust, the Internal Revenue Code (IRC) require that one of these types be used:

Charitable remainder annuity trusts (CRATs) – Income interest is paid as a fixed amount. The amount is determined by multiplying the payout rate by the value of the trust the day the trust is funded.

Charitable remainder unitrusts (CRUTs) – Income is paid as a fixed percentage of the trust's assets. The percentage is determined by multiplying the payout rate by the value of the assets (which are revalued annually).

Regardless of the payout structure, the payments may be taxable to the income beneficiary and made in monthly, quarterly, semi-annual, or annual installments.

What are the benefits of a charitable remainder trust?

Tax exempt. Charitable remainder trusts are not subject to tax on its investment income or capital gains. As a tax-exempt trust, a charitable remainder trust is an ideal method for selling an appreciated asset and avoiding the resulting tax liability while retaining an income stream for life.

Highly appreciated assets maintain value. A key benefit of a charitable remainder trust is that it can be funded with appreciated property and avoid an immediate income tax liability to the donor. This allows the donor to maintain the full market value of the assets, which can lead to additional income to the beneficiaries and larger benefit to the named charities.

Income tax deduction. Donors may be able to claim a partial income tax charitable deduction. Because the donor/income beneficiary retains a right to income, and the charity must wait to receive the assets after the term of the trust ends, the deduction amount is less than the fair-market-value of the gift. Some of the factors that impact the income tax deduction amount are age of the beneficiaries, payout rate of the trust, term of the trust, and the charitable midterm federal rate.

What assets can be donated to a charitable remainder trust?

- Cash
- Publicly traded securities
- Some closely held stock (not S-Corp stock)
- Real estate
- Cryptocurrency
- Other complex assets

Is a charitable remainder trust the right giving solution?

Charitable remainder trusts are a powerful tool that can address many personal financial goals and provide a significant gift to a charity of choice. Donors commonly create charitable remainder trusts to:

- Sell an asset that will generate a significant tax liability
- Convert a non-income producing asset to an income stream
- Achieve charitable goals and interests

These factors are not mutually exclusive and to the extent each describes a donor, the more likely a charitable remainder trust will be a satisfying solution. Because a charitable remainder trust can be funded with appreciated assets, a properly drafted, implemented, and administered charitable remainder trust enables donors to realize charitable goals that seem beyond their reach.

For example, making a current gift of cash to endow a chair in the donors' name at their alma mater may be infeasible, but by contributing real estate (for example) to a charitable remainder trust, the donors could:

- Achieve their charitable goal
- Obtain an immediate income tax deduction
- Sell an appreciated asset in a tax-exempt environment
- Create a lifetime income stream

All while supporting their alma mater by naming them as the beneficiary to endow a chair in the donor's name.

Learn more about charitable remainder trusts or contact us to speak with someone from our team.