



## BENEFITS OF A CHARITABLE LEAD TRUST

When it comes to charitable trusts, charitable remainder trusts (CRT) seem to get all the attention. But the cousin of the CRT, the charitable lead trust, also can provide significant charitable and tax benefits, particularly if you have a large estate-tax liability.

Before considering establishing any charitable trust or other form of charitable giving, it's usually best if you have a strong charitable intent. Creating charitable strategies merely to save taxes is generally not the best basis for charitable giving, say many charitable giving experts. This is particularly true for the charitable lead trust (CLT), which requires the donor to give up current income from the donated assets, and in some cases even pay taxes on that income.

With a charitable lead trust, sometimes called a charitable income trust, the donor transfers cash or income-producing assets to the trust and the trust pays out income earned by the assets to a designated charity or charities. The payout may be an annual fixed dollar amount set at the time of the transfer—called an annuity trust—or an amount based on a percentage of the assets in the trust at the time of each annual payout—called a unitrust.

At the end of a specified number of years, the remaining assets in the trust are distributed to the noncharitable beneficiary, usually someone other than the donor or the donor's spouse. This timing is unlike that of a charitable remainder trust, in which the donor receives current income from the trust assets and the assets go to the charity at the end of the designated time.

Charitable lead trusts can be either a nongrantor CLT or a grantor CLT. The most common by far is the nongrantor CLT, in which the beneficiary is someone other than donor. The biggest benefit of a nongrantor CLT is the reduction of gift or estate taxes. That's because any future appreciation of the donated assets is removed from the donor's estate and not subject to future estate or gift taxes. The only concern the donor might have is possible exposure to the generation-skipping transfer tax if the heirs are grandchildren or other heirs two generations removed.

A gift or estate tax may be due at the time the assets are transferred to the trust, because noncharitable beneficiaries ultimately receive the assets. However, the gift is discounted because

the beneficiaries won't receive the gift for some time. In addition, because a charity is receiving the income from the assets in the meantime, the donor receives a gift-tax deduction based on the amount transferred into the trust and the amount of time the assets are to remain in the trust (the longer they are left in, the larger the deduction). Furthermore, the gift won't be taxed at all if its discounted value is less than the donor's remaining gift and estate tax exemption (\$650,000 in 1999, rising to \$1 million in 2006).

A nongrantor CLT is beneficial for someone who puts in assets that are expected to appreciate in the future. A CLT created at the donor's death also can be a good way to delay the transfer of assets to an heir, perhaps at a time when the heir is more capable of handling the assets.

With a grantor CLT, the donor also can receive an income-tax deduction in the year the trust is created. The downside of this benefit is that the donor must pay income taxes on the income paid out to the charity. With a nongrantor CLT, the donor does not pay income taxes on the distributions to the charity throughout the term of the trust, but doesn't receive the income-tax deduction, either. A grantor CLT is probably most appropriate for someone who is in a high income-tax bracket at the time of the gift and expects to be in a much lower tax bracket in the subsequent years, and who eventually wants the assets back in their estate.

June 1999—This column is produced by the Institute of Certified Financial Planners, a national association representing the top financial planners in the country, and is provided by Joseph H. Hoffman, a local member in good standing of the Institute.