

*Giving Through*

# CHARITABLE REMAINDER TRUSTS



*Masonic Charities of the*  
**Grand Lodge of Pennsylvania**



## Understanding Charitable Remainder Trusts

- Are you looking for a way to leave a substantial gift to charity and minimize your estate taxes?
- Do you have a portfolio that is filled with highly appreciated assets that aren't generating sufficient income?
- Is the threat of capital gains tax keeping you from selling or reinvesting assets?

If so, a Charitable Remainder Trust (CRT) may make sense for you. It can be an effective way to transfer assets, provide an additional income stream and defer capital gains tax.

This brochure provides an overview of how CRTs work and some of the benefits they provide. For additional information, and to find out more about how the Masonic Charities of the Grand Lodge of Pennsylvania can assist you in achieving your charitable and financial goals, contact a gift planning specialist at the Office of Gift Planning at 1-800-595-6454, or complete the informational request card at the end of this booklet and return it to the Office of Gift Planning, Masonic Charities, One Masonic Drive, Elizabethtown, PA 17022.

### What investments may be used to generate income from a CRT?

**T**here is a wide range available. Keep in mind however, that the investment choice should be appropriate for your income needs and goals, as well as the goals of the charity.

## What is a Charitable Remainder Trust?

A Charitable Remainder Trust (CRT) is a tax-saving alternative for people who want to make a substantial gift to a charitable organization. It can be a powerful tool for many individuals, especially those who have highly appreciated assets such as stock or real estate.

A CRT is an irrevocable trust. This means that once it is set up and a charitable gift is made, it cannot be undone. In order to realize its full potential, a CRT requires special legal, accounting and tax administration. Your investment professional, attorney and tax adviser should all be included in discussions about whether this option is right for you.

Gifts to a CRT can be made in cash but, more often, consist of highly appreciated stock, real estate or a closely-held business interest. In exchange for a charitable gift, the CRT pays income to the trust income beneficiary (usually you and your spouse as donors) for a fixed period or for life. At the end of the trust (which is usually your lifetime), the remaining assets pass to one or more of the charities you have chosen.

### How a CRT Works

Donor	Trust	Charity
Makes a gift to a CRT	Sells assets (without paying capital gain tax)	Receives remaining trust balance when donor dies
Receives income tax deduction	Reinvests the proceeds into an income-producing portfolio	
Receives income	Pays income to the donor	

*Income distributed from a CRT is fully taxable in accordance to the way it existed in the trust, i.e. ordinary income, capital gain income, tax-free income or tax-free return of principal.*

## Here are Some of the Benefits a CRT Offers:

- **Provides a current income tax deduction.** A gift to a CRT creates an income tax deduction for the donor for the present value of the charitable gift. This current income tax deduction may help offset the donor's annual taxable income.
- **Defers capital gains taxes.** Because a CRT is tax-exempt, your capital gains tax is deferred when the appreciated assets are sold by the CRT. This allows the CRT to convert the full value of the asset into an investment that can provide a lifetime income for you and your spouse.
- **Reduces or eliminates estate taxes.** Since the donated assets generate a charitable estate tax deduction at the death of the income beneficiary, estate taxes may be decreased or eliminated.
- **Provides an income stream, often for life.** When assets are donated to a CRT and sold, the money generated from the sale may be placed in an income-producing investment. The income is then distributed according to the trust provisions. For some types of CRTs, principal may also be distributed. Because there have been no capital gains taxes paid, the amount invested may be greater than if the assets had been sold outside of a CRT and had been subject to capital gains or estate taxes. Depending upon the projected term of the trust, payout amounts may be 5 to 8% of the value of the trust when funded or based on the value of the trust, as determined each year.

## More Benefits of the CRT:

- **Benefits the charity of your choice.** When the trust ends, the assets remaining in the trust pass to the Masonic Charity of your choice. You may also reserve the right to change charities during your lifetime and/or select multiple charities to receive the remaining trust assets.
- **Flexibility in choosing a trustee.** For many donors, a CRT is attractive because the donor may serve as trustee of his or her own CRT within certain limitations. Also, the Masonic Charities will serve as Trustee at no fee, provided one of the Masonic Charities is an irrevocable beneficiary of at least one-half of the assets remaining in the trust when it ends.
- **Investment Opportunities.** The Masonic Charities provides several investment styles and managers when it serves as trustee. Assets can be invested in one of three styles: (1) growth portfolio; (2) income portfolio; or (3) balanced portfolio. In addition, the Masonic Charities permits the choice of either an institutional advisor (Bank) or individual investment manager to assist the Masonic Charities in achieving the trust investment goals.
- **Minimum investment flexibility.** Unlike many charitable organizations, the Masonic Charities will work with you in funding your CRT. A minimum investment of \$50,000 in cash and/or appreciated assets can be transferred to initially fund the trust with a goal of fully funding the trust over a period mutually agreeable between the donor and the Masonic Charities.

There are five types of Charitable Remainder Trusts, which can be customized to meet your personal goals. They are the following:

- 1 Standard Charitable Remainder Annuity Trust** - pays a fixed annuity payout
- 2 Standard Charitable Remainder Unitrust** - pays an annuity payment based on the value of trust assets, determined annually
- 3 Net Income Charitable Remainder Unitrust** - pays lower amount of trust income or a stated percentage of value of trust assets, determined annually
- 4 Net Income with make up Charitable Remainder Unitrust** - pays lesser of trust income or stated percentage of value of trust assets, determined annually, but deficiencies between stated percentage amount and income paid for year can be made up in later years
- 5 Flip Unitrust** - initially pays income from trust assets until a triggering event, such as the sale of certain property occurs, and then pays stated percentage of value of trust assets, determined annually

## Who's Involved in a CRT?

In order to understand how a CRT works, it is important to understand who's involved. Every CRT involves a donor, income beneficiary, charity, trustee and administrator.

### **Donors (also known as grantors)**

The donors are the individuals who make the initial contribution to the trust. They work with their attorney to set up the original trust document, make the gift and receive the income tax deduction. If one of the Masonic Charities is a remainder beneficiary of the CRT, we will assist your advisor in preparation and funding of your CRT.

### **Beneficiaries**

The income beneficiaries receive income under the terms of the trust. They are usually the same as the donors. If anyone other than the donor and spouse is named as income beneficiary, there may be tax consequences. For example, if a child is named, a gift or estate tax may result.

### **Charity (often called Remainder Beneficiary)**

The charity receives a benefit from the trust when the income beneficiaries' interest ends (this is usually at death). At that time, the charity will receive the assets left in the trust. The donor chooses the charity and may name more than one. If the trust is drafted accordingly, the donor may change or add charities at any time.

### **Trustee**

The trustee is selected by the donor and carries out the terms of the trust, invests the assets and protects the interests of the income beneficiaries and charity. A special independent trustee may be recommended for certain assets or investments.



## Administrator

The trust administrator helps the trustee prepare and file annual tax returns and other recordkeeping for the CRT. The administrator is not normally named in the trust document.

## A Comparison

**W**hen you sell and reinvest highly appreciated assets outside of a CRT, it can result in greater tax liabilities and less income. This chart looks at the possible income benefits when stock purchased for \$100,000 and now worth \$500,000 is sold outside of a CRT, compared to when it is donated and sold within a CRT. As you can see, when the stock is sold outside of a CRT, the capital gains tax reduces the amount available for reinvestment. The result: less income.

	Sell	Gift to a CRT
Current Value of Stock	\$500,000	\$500,000
Capital Gains Tax (15%)	\$(60,000)	\$0
Balance to Reinvest	\$440,000	\$500,000
7% annual income	\$30,800	\$35,000
Total lifetime income (gross)	\$862,400	\$980,000
Tax deduction benefit	\$0	\$123,495

Assumption: Annual 15% capital gains tax (stock with \$100,000 basis); investment returning net 7%; assumes 28 years of life expectancy; charitable income tax deduction generated from the CRT gift is based on IRS formula using federal rate of 5.6% when illustration was created.

## A Testimonial

In February 2006, Bro. Joseph Dougherty established a CRT to benefit the Masonic Children's Home at the Masonic Village at Elizabethtown. With the assistance of a gift planning specialist, Bro. Al, at the Masonic Charities, Bro. Dougherty initially funded his CRT with \$50,000, naming himself as trustee. The trust paid him at 8% of the value of the trust determined annually for the remainder of his life and will continue to make payments to his family for a period of 12 years after his death. At the end of the 12-year period, the remaining assets will be distributed to the Masonic Villages.

Bro. Dougherty then consulted with one of the investment advisors used by the Masonic Charities to develop an investment portfolio to meet his financial goals. Subsequently, he transferred an additional \$200,000 in appreciated assets to the CRT to increase the payment amount for his needs.

What Bro. Dougherty was most impressed with in setting up his CRT was the ability of the Masonic Charities to work with him and his advisors in providing numerous illustrations and sample documents of how the CRT would be structured to meet his personal goals.

Bro. Dougherty said, "Until I met with Bro. Al, I never realized the choices available to meet my financial goals while, ultimately, benefiting my favorite charity. I look forward to making additional contributions to my CRT in future years to take full advantage of the CRT benefits. I would highly recommend that a person holding significant appreciated assets contact a gift planning specialist at the Masonic Charities to discuss a personalized plan using a CRT to meet his or her financial goals."

## Commonly asked Questions

### ***Can a CRT be undone?***

No, a CRT is irrevocable. That means the gift cannot be taken back by the donor. Therefore, it is extremely important to carefully design a trust to fit a donor's long-term requirements.

### ***Can any changes be made to the CRT?***

There are some things that can be changed, if the trust allows it. These include the trustee, administrator, charity and the investments. All other changes would require the trustee to petition and receive court permission.

### ***Is there anything that a donor cannot change about the CRT?***

The following provisions of the trust cannot be changed except to comply with current law: the income payout rate, payment frequency and type of charity (for example, a private foundation versus a public charity).

### ***Can the income beneficiaries be changed?***

An income beneficiary may not be added. However, when the trust is drafted, it may allow for a contingent beneficiary through a special provision. The contingent beneficiary may be removed only by the donor's will and may not be replaced.

### ***How much income can the income beneficiaries receive?***

The minimum payout rate is 5%, and the maximum is 50%. The payout rate may be further limited by a 10% remainder interest requirement, which applies only to Charitable Remainder Unitrusts. The present value of the remainder interest passing to charity must equal at least 10% of the value of the gift on the date of contribution.

### ***Are there any income restrictions that apply to Charitable Remainder Annuity Trusts?***

Yes, Charitable Remainder Annuity Trusts (CRAT) must pass a 5% probability test in order to qualify as a valid charitable trust. A CRAT will not be valid if there is a 5% or greater probability that trust assets will be gone before the charity receives the assets. The 5% test only applies to CRATs that are set up to continue for your life expectancy.

### ***Can the donor's children be income beneficiaries of a CRT?***

Yes, the donor's children can be named as income beneficiaries of your CRT if the trust meets the 10% remainder interest requirement. However, on the date the gift becomes final, there may be a gift or estate tax due. Please consult your legal and tax advisers on tax consequences.

### ***Must donors purchase life insurance for their heirs?***

The donor is not required to purchase life insurance. However, they may purchase it if they wish to replace the asset gifted into the CRT. It may make sense to have the life insurance in force prior to making the gift. This helps to ensure replacement of the asset for heirs.

### ***Must the charity be told about a gift?***

A donor is not required to tell the charity about the ultimate gift; however, many opt to do so.

### ***Is it important to consider the charity's interest when making investment choices?***

Yes, the trustee has a legal responsibility to act prudently for the interests of all parties, including the beneficiary(s) and the charity.

### ***Can the donor act as trustee?***

Usually, the donor may act as the trustee for selecting the investments. It is important to remember that the trustee has a fiduciary duty to both the income beneficiary and to the charity. However, in certain situations, an independent trustee other than the donor must be available.

### ***What is an independent trustee?***

An independent trustee is an independent party that manages a number of responsibilities for the donor in order to maintain the integrity of the CRT. The independent trustee should be someone who is not within the close influence of the donor. This means that someone other than the donor's children, parents, other relative, business partner or long-term professional adviser should be chosen.

### ***Are there other situations in which an independent trustee is a good choice?***

In many cases, an independent trustee would be used to determine the value and to negotiate the sale of assets, such as real estate or a closely-held business that cannot be readily converted into cash.

### ***What section of the Internal Revenue Code governs whether a trust qualifies as a CRT?***

Internal Revenue Code Section 664 lists the requirements a trust must meet in order to qualify as a Charitable Remainder Trust.

## Masonic Charities' Office of Gift Planning

**F**or more information about the Masonic Charities, contact the Office of Gift Planning nearest you:

### **Central Pennsylvania Region**

(717) 367-1121, ext. 33460

Toll-free: (800) 599-6454

### **Western Pennsylvania Region**

(412) 741-1400, ext. 3011

Toll-free: (866) 872-0664

### **Eastern Pennsylvania Region**

(610) 825-6100, ext. 1348

### **From Outside of Pennsylvania**

Toll-free: (800) 599-6454

The purpose of this publication is to provide general gift, estate and financial planning information. It is not intended as legal, accounting or other professional advice. For assistance in planning charitable gifts with tax and other financial implications, the services of appropriate advisors should be obtained. Consult an attorney for advice if your plans require revisions of a will or another legal document. Tax deductions vary based on applicable federal discount rates, which can change on a monthly basis. Some opportunities may not be available in all states.

## For More Information

Please send the following information:

- Trust sample illustration based on the following information:

Age(s): \_\_\_\_\_ Amount: \$ \_\_\_\_\_

- Franklin Legacy Society materials  
*Recognizes those who have provided  
for one or more of the Masonic Charities  
of the Grand Lodge of Pennsylvania  
through their real estate plans*

- Please contact me for an appointment to discuss a possible Charitable Remainder Trust with the Masonic Charities

Name \_\_\_\_\_

Address \_\_\_\_\_

City \_\_\_\_\_

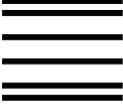
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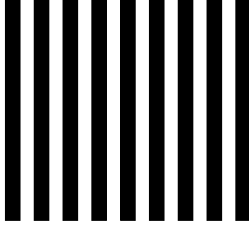
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