More Income/Less Tax

If there were a way to provide more income for you during your retirement and to create less tax, you might be interested to learn more. If you were told that the federal government supports this offer, you'd say that there must be some mistake! Make no mistake about it; charitable planned gifts can make this happen. The IRS approves these plans that may benefit you and your loved ones with more retirement income and less tax.

Charitable planned giving is only one component of estate planning. Anyone with a taxable estate has the opportunity to distribute his or her taxable wealth in the way he or she wishes. But without making estate plans, you leave the decisions for distribution of your estate to the government.

Personal capital is the portion of your estate that you control and pass on to your heirs. *Social capital* consists of the assets that you cannot pass on to heirs, capital which will be paid in taxes unless you direct it to charities of your choice. Either you choose to distribute this social capital yourself, or the state and federal government will do it for you via estate taxation, which can run as high as 50 percent!

When individuals set up planned gifts, they are controlling the distribution of the social capital that they are unable to keep. And when this is done properly, the rewards may be more retirement income and less tax. A proper estate plan is a means to preserve and to control the wealth you have worked for and accumulated during your lifetime so that you may protect yourself and your loved ones, either at your incapacity or death. Planned giving redirects assets to charitable projects at no net cost to you or even at a net gain. You and your heirs may have even more money to use than would be the case if you had left nothing to charity.

Charitable planned giving instruments provide an individual with numerous benefits including:

- Avoid paying estate tax through redirection of your *social capital* to charity,
- Provide for a spouse, family members or other loved ones,
- Avoid capital gains taxation on highly appreciated assets, such as stock,
- Convert low income producing, highly appreciated assets into a healthy income stream,
- Relinquish management of assets and assure either a fixed or variable income for life,
- Establish a charitable legacy and receive recognition while living.

To help you understand how some of the common charitable planned giving instruments operate, the following information is provided for your review. Personalized illustrations of these charitable instruments are available from the ADA Foundation. The illustrations highlight the tax savings, expected income and operation. Simply call or write to request a personalized illustration. There is no charge or obligation for this service.

Charitable Remainder Trusts

The following description of a charitable remainder trust is provided from IRS income tax regulations:

Generally, a charitable reminder trust is a trust which provides for a specified distribution, at least annually, to one or more beneficiaries, at least one of which is not a charity, for life or for a term of year, with an irrevocable remainder interest to be held for the benefit of, or paid over to charity.

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There are different varieties of charitable remainder trusts (CRT). Each is designed to meet unique financial and charitable objectives. CRTs have their own set of rules and benefits.

- *Charitable Remainder Annuity Trust (CRAT)* - For individuals who are concerned that their income steam remain fixed and does not fluctuate up and down, a CRAT is an appropriate estate planning instrument to consider. A CRAT annually pays a fixed percentage, not less than 5%, of the initial net fair market value of the property placed in it. Cash, stock and other property may fund the trust. However, additions may not be contributed to a CRAT once it has been established.

  An initial income tax deduction is available based on the actuarial calculation of the remaining interest to the charity. Appreciated property contributed to the trust avoids capital gains taxation. Additional tax savings are also realized through the removal of taxable assets from the donor's taxable estate. The combined tax savings could be significant. Moreover, by freeing up the potential contained in non-income or low income producing assets, such as land or stock, the donor can realize a significant increase in cash flow. Payment of the annuity may be made annually, quarterly, or more frequently. Upon the death of the last named income beneficiary, remaining trust assets are used by the charity for its tax-exempt activities.

- *Charitable Remainder Unitrust (CRUT)* - For individuals who are concerned about the effects of inflation on their income stream, a CRUT is often used, since income distribution is based on a percentage of the trust, valued annually. And from this recalculation of its net fair market value, a fixed percentage must be paid, which is not less than 5% nor more than 50%, to one or more beneficiaries. Unlike a CRAT, additional gifts may be made to a CRUT at any time. At the time of each additional gift to the CRUT, a charitable income tax deduction may be taken, capital gains tax avoided, and the property permanently removed from inclusion in the donor's estate for state or federal taxation. Payment may be made annually, quarterly, or more frequently. Upon the death of the last named income beneficiary, the remaining trust assets are used by the charity for its tax-exempt activities.

- *Net Income Makeup Charitable Remainder Trust (NIMCRUT)* - Trust makers who wish to defer income find that a NIMCRUT is a good charitable estate planning instrument to use. A NIMCRUT, especially when invested in a well-designed variable annuity, allows trust makers to defer income until they need it. A NIMCRUT can also maximize the amount of the ultimate charitable distribution, because it allows tax-deferred accumulation of value.

Charitable Lead Trusts

Charitable lead trusts distribute income interests in the reverse order to the way charitable remainder trusts make distributions. These trusts provide income to the charity first, for a period of years. At the end of the defined period of time, the remaining proceeds are distributed to the donor's designated beneficiaries. The benefit of a charitable lead trust is that a donor can make gifts to heirs that for tax purposes are a fraction of the actual amount of the gift. This allows for leveraging of the donor's unified tax credit. Typically, individuals who do not need the contributed assets to provide an income stream use a CLT. Oftentimes, individuals who may wish to delay the transfer of assets to an heir use CLTs.

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Pooled Income Fund

A pooled income fund is a trust that acts much like a mutual fund. Property transferred to a pooled income fund is commingled with contributions from other donors. Unlike charitable reminder trusts, the minimum gift required to establish an interest in a pooled income fund may be as little as $10,000. The donor cannot serve as trustee of a pooled income fund, because the law requires that a charitable organization manage the funds. However, a donor may reserve the right to name more than one charitable beneficiary and to change any charitable beneficiary designation throughout his or her life. The amount of income received by an income beneficiary in any tax year of a pooled income fund must be determined by the rate of return earned by the fund for such year. Pooled income funds are not able to receive or invest in tax-free securities and are only able to distribute earnings, never principal.

Wills and Trusts

A properly executed estate plan requires professional advice from an attorney. In addition, a tax advisor and/or accountant may be consulted. Through the execution of a will, the expenses of estate administration may be greatly reduced. Additional savings and increased privacy may also be realized through the creation of one or more trusts. For information about wills and trusts, please see a copy of Advantages of Wills and Trusts.

The net result of effective estate planning that includes planned giving can be more retirement income, less tax, and control of the distribution of social capital. The ADA Foundation is prepared to provide you with personalized examples of the benefits that charitable planned gifts may provide to you.

For more information about estate planning and leaving a legacy, please contact the ADA Foundation at the address below.