

Power to Sell CRT Annuity Adds Flexibility

Charitable Remainder Trusts are powerful tools for estate, tax, and financial planning. The potential sale of the income interest in a CRT adds more power and flexibility to planning. The CRT is a split interest trust where the grantor retains an income interest and the remainder goes to one or more charities, which can be chosen by the grantor or by somebody else.

For example, let's consider a business owner considering selling her business. Instead of a traditional business sale, she might consider donating the business to the Trustee of a Charitable Remainder Trust and having the Trustee sell the business. The gift to the CRT can create an immediate income tax deduction of a portion of the value of the business. The capital gains taxes that she would have to pay on the traditional sale would be deferred and possibly avoided altogether. The transfer to the trust is a charitable gift, so there are no gift tax concerns and the business is removed from the grantor's taxable estate.

The application of this tool in specific situations is potentially powerful and complex, and this planning should be undertaken only by those who have mastered this area. One downside to this planning is that the grantor receives an annuity payment from the trust rather than a lump sum or discretionary distributions. There is little flexibility to the income stream. What if the grantor finds that she has an immediate need for the funds?

One possibility is the sale of the income interest. There are companies that will purchase these income interests. They will pay the grantor the present value of the income stream, giving the grantor immediate funds and the company some profits over time. The sale is taxed as a capital transaction, so there will probably be capital gains taxes on the sale. The capital gains tax rate will be at the current 15% bracket (or less), rather than whatever the future rates will be. Without the sale of the income stream, the taxpayer will pay taxes on all or some of the distributions, perhaps as capital gains, perhaps as other types of income. A spendthrift provision in the CRT could prevent the sale entirely, so an attorney should review the trust to ensure the sale doesn't violate any trust provisions.

Roger Silk of Sterling Foundation Management points out that

CRTs are tax-deferral vehicles; they defer to the future the tax a client must pay on the donated assets. If tax rates are stable or falling, this deferral works great because the client gets to pay the tax at a lower rate. But if tax rates rise, the deferral works against the client by forcing them to take their income in the future, when tax rates are higher.

If a client does nothing and tax rates rise, they'll almost certainly suffer a loss on the value of their CRT. They can avoid this loss entirely by selling their CRT interest today, for a lump-sum cash payment. The benefit, of course, is that the sale is considered a capital transaction, so the proceeds are taxed at capital gains rates.

The sale of a CRT income interest is not always the right thing to do, but sometimes it is. Financial advisors, attorneys and CPAs who have clients who have CRTs should take a look at whether the sale of the income interest makes sense. This review is best done as a team to consider the family, income tax, estate tax, and financial consequences of such a sale.

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Our firm has a holistic approach to estate planning and estate administration. Attorney Anna E. Byrne is a member of the National Network of Estate Planning Attorneys and is currently the chairperson of the Massachusetts Conference.

VACATION ANNOUNCEMENT: *Anna will be away on vacation from August 9th-August 30th. Jennifer will be available to answer any questions.*

For more information please call Anna Byrne, Esq. or Jennifer Green, Esq.: (617) 444-8425.

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