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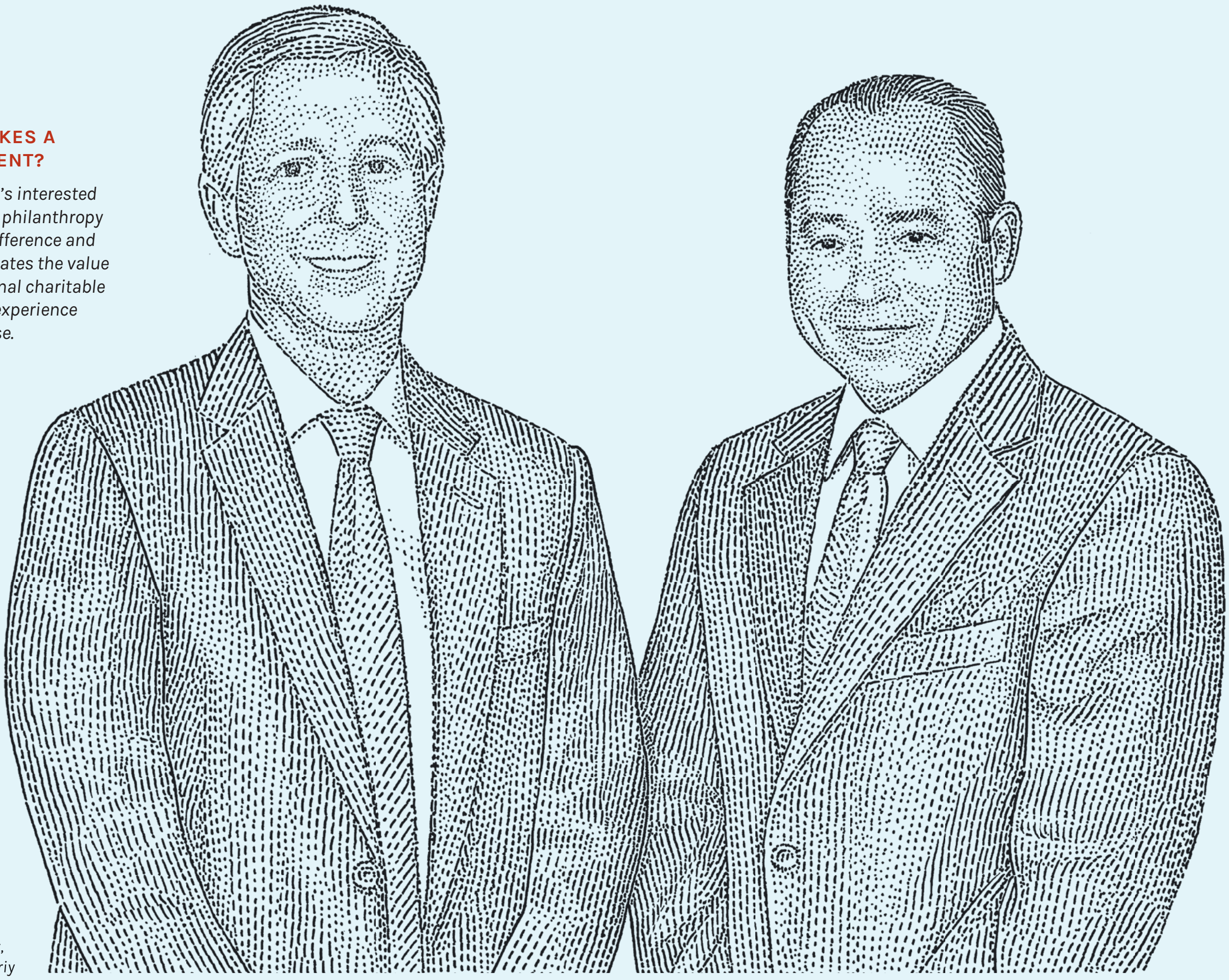
Does a CRT rollover make sense for your client?

BY JAMES W. LINTOTT

WHAT MAKES A GOOD CLIENT?

A donor who's interested in his or her philanthropy making a difference and who appreciates the value of professional charitable consulting experience and expertise.



Left to right:
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ILLUSTRATION BY KEVIN SPROULS

Charitable remainder trusts (CRTs) enable clients to convert appreciated assets into lifetime income streams, defer capital gains taxes, reduce estate taxes, protect assets from creditors and distribute funds to charities they're favorable to.

However, because CRTs are irrevocable, many clients get frustrated when a trust they established in the past becomes misaligned with their current needs and goals. In a previous article, we discussed how clients with CRTs can sell their interest to third-party buyers; this article focuses on an alternative secondary planning strategy: the CRT rollover.

FIXING MISALIGNMENTS WITH A CRT ROLLOVER

Consider a scenario in which joint beneficiaries of a CRT established years ago want to use their trust to benefit their children, who are now old enough to be added as lifetime beneficiaries. Or maybe an individual who remarried late in life wants to add the new spouse to his or her CRT.

At some point, joint beneficiaries of a standard charitable remainder unitrust (CRUT) might benefit from shutting off (and growing, tax-deferred) an income stream they don't need and don't like paying taxes on. What about a client with an underperforming net income with makeup charitable remainder unitrust (NIMCRUT), who would prefer a higher, more consistent payout rate?

The rollover is a technique for clients with CRTs to fix these (and other) misalignments. As this strategy gains widespread acceptance among the estate-planning community, more advisors are informing their clients with CRTs that they can use rollovers to (in effect) make changes to their trusts.

> “Most clients with CRTs don't understand the full range of available secondary planning options.”

NO, IT'S NOT DECANTING

While clients with CRTs pursue rollovers for different reasons, the underlying process and technique are always the same: Income beneficiaries use the interest in their CRT to form a new CRT that's more aligned to their current circumstances.

Because the initial CRT is unchanged, the rollover process is not decanting, which of course isn't possible with CRTs. Instead, the net result of a rollover is two CRTs, each with its own set of income and charitable beneficiaries. However, because the income beneficiaries are effectively removed from the original trust, clients don't have to deal with the hassles of an additional tax return or the administrative costs of managing a second CRT.

CASE STUDY: SCRUT TO NIMCRUT: ADDING DAUGHTERS AS BENEFICIARIES

Problem: A 76-year-old client we knew was the sole beneficiary of a $5.3 million standard charitable remainder unitrust with a 5 percent payout. This woman had plenty of wealth and income sources and did not like how the CRT was forcing taxable income upon her (so much so that in some years, her tax rate on the distributions approached 45 percent).

In addition, she had two daughters, ages 56 and 54. Neither was listed as a beneficiary of her CRT, so everything in the trust was set to be distributed to charity when the client passed away.

Solution: The client's advisors rolled her standard CRUT income interest into a NIMCRUT. The advisors also added her two daughters as contingent beneficiaries.

The NIMCRUT structure enabled the client to defer her income distributions in full year after year, growing the trust assets tax-free over the remainder of her life expectancy (11 more years, according to IRS life expectancy tables).

At her death, her daughters will split the future distributions (an estimated total of $5 million) from the trust for their joint lifetimes.

IN CASE YOU MISSED IT

A previous article in volume 25, edition 5 of *Worth* magazine explained how clients who sell their income interest to third-party buyers typically get more than they would by keeping their interest or terminating their CRT. Common sale drivers include cash needed for an investment opportunity, simplification of financial affairs, divorce, tax arbitrage, a lack of cash for charitable needs, desire for increased flexibility and value maximization.

Advisors should inform clients with CRTs of the sale and rollover options so that they're informed to make changes, should the need arise in the future. ●

ABOUT US

STERLING FOUNDATION MANAGEMENT, LLC IS THE OLDEST NATIONAL FOUNDATION-MANAGEMENT FIRM IN THE COUNTRY AND THE NATION'S LEADING FACILITATOR OF SALES OF INCOME INTERESTS IN CHARITABLE REMAINDER TRUSTS. Sterling works with a broad range of clients and high net worth individuals to develop solutions that help them achieve their philanthropic, family and financial goals through the effective use of private foundations and other charitable-planning vehicles and financial services. ●

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