CUMMINGS & LOCKWOOD LLC

WHY WOULD A CLAT BE OF INTEREST TO ME?

A charitable lead trust can be used to make a future gift to individuals while satisfying the donor's charitable goals.

When the donor funds a lead trust, he or she makes one gift to charity that is deductible for gift or estate tax purposes and a second, taxable, gift to the individuals who will receive the trust property when the charitable term ends. The value of the charitable gift is the present value of the stream of payments to be made to charity over the charitable term, determined by using the lowest applicable federal discount rate in effect at the time the trust is funded. The value of the taxable gift to the individual beneficiaries of the lead trust is the difference between the value of the property used to fund the trust and the value of the charitable gift.

The applicable federal discount rate used to value the donor's taxable gift to the lead trust is the government's assumption as to the expected rate of return for the trust's investments at the time of funding. The potential for the trust's actual investment performance to exceed the government's assumption presents an opportunity for the donor to make a tax-advantaged gift to individuals by using a charitable lead trust to make the donor's charitable gifts. If the annual rate of return on a charitable lead annuity trust's investments exceeds the federal discount rate used to value the charitable gift to the trust, all of the excess investment return will accrue for the benefit of the individual beneficiaries at no further gift or estate tax cost. With a charitable lead unitrust, the charity and the individual beneficiaries share the benefit of the excess investment return based on their relative interests in the trust.

The benefits of using an annuity trust to transfer property to individuals must be weighed against the generation-skipping transfer tax advantages of using a unitrust when grandchildren or more remote descendants are the beneficiaries.

A charitable lead annuity trust can be structured to "zero out" the taxable gift so that no portion of the donor's lifetime exemption from gift tax is used and no gift or estate tax liability is incurred in connection with the lead trust. To zero out the taxable gift, the donor selects a charitable term and payment amount that, using the applicable federal discount rate, creates a charitable gift that is equal in value to the value of the entire property used to fund the lead trust. If the trust's investments earn an annual rate of return that exceeds the federal discount rate, assets will be distributed to the individual beneficiaries at the end of the charitable term at no gift or estate tax cost. A charitable lead unitrust can also be structured to reduce, but not to "zero out," the taxable gift.