PACIFIC WEALTH MANAGEMENT®

*A **Charitable Remainder Trust (CRT)** is an estate planning tool that can generate a long-term income stream for you, or other beneficiaries, while allowing the remaining assets to be donated to your favorite charity.*

A CRT is an advantageous donation vehicle that allows you to make contributions to a trust and be eligible for a partial tax deduction. This deduction is based on the CRT's remainder amount that will pass to charitable beneficiaries after you receive income for a term that you define upon its creation. You, or another beneficiary, can receive income for either a term of 20 years or less, or for life, and then name one or more charities to receive the remainder of the donated assets after the term is completed.

CRT's can be an efficient tax planning tool for highly appreciated assets like the stock in the company you work for or a position you've owned for a long time.

General Advantages of CRT's

Income

Receive a distribution from the CRT, at least annually. That distribution may be as large as 50% but not less than 5% of the initial net fair market value of all property placed in trust. This property can be anything from cash, stock, to real estate and other assets (certain exceptions apply, i.e., S Corp stock).

Tax Advantages on Income Received

The CRT itself does not pay tax on its income. Funds in the CRT compound tax-free, in the same manner as a qualified pension fund or an IRA. Like an IRA, you pay taxes when you take your money out. But unlike an IRA, you do not necessarily pay regular income taxes when you take your money out of the CRT. Instead, your taxes are calculated based on how the CRT earned the income; regular income and capital gains are taxed at their respective rates and distributions of trust principal are tax-free.

Income Tax Deduction

Once the CRT has been established and funded with assets you are allowed to take an income tax deduction, usually limited to 30% of adjusted gross income, but can vary from 20% to 50%, depending on how the IRS defines the charity and the type of asset. If the amount of the charitable donation exceeds your 30% AGI cap in the first year, you can carry forward the remainder of the charitable deduction amount for up to five years.

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Advantages of CRT's for Concentrated Stock Divestiture

Avoid Capital Gains Tax on Highly Appreciated Assets

CRTs are exempt from investment income taxation. Low-basis assets (e.g. stock which has appreciated significantly) are transferred to the trust so that when sold, there is no income or capital gains tax consequence for you. You are only taxed on income received from the trust.

Mitigate Risk Through Divestiture and Reinvestment

The trustee can liquidate the stock holding and because the trust is exempt from capital gains tax, the full amount of the proceeds from the sale is available to re-invest in a diversified portfolio thus avoiding capital gains tax on the stock's appreciation while simultaneously mitigating the market risk associated with a concentrated position.

Illustration

Bill, age 65, owns company stock with a cost basis of $100,000. It is now worth $500,000. His federal marginal tax rate is 35% and his capital gains tax rate is 15% and his life expectancy is 26 years. If he were to sell his company stock and generate a 5% return on the reinvestment of the proceeds of the sale, why would he be better off with a CRT than simply selling the stock on his own? The following chart illustrates the financial advantage of the CRT.

Comparison of Income After Sale		
	Without CRT	With CRT
Current Value of Stock	$500,000	$500,000
Federal Capital Gains Tax	-60,000	0
Balance To Re-Invest	$440,000	$500,000
5% Annual Income	$22,000	$25,000
Total Lifetime Income	$572,000	$650,000

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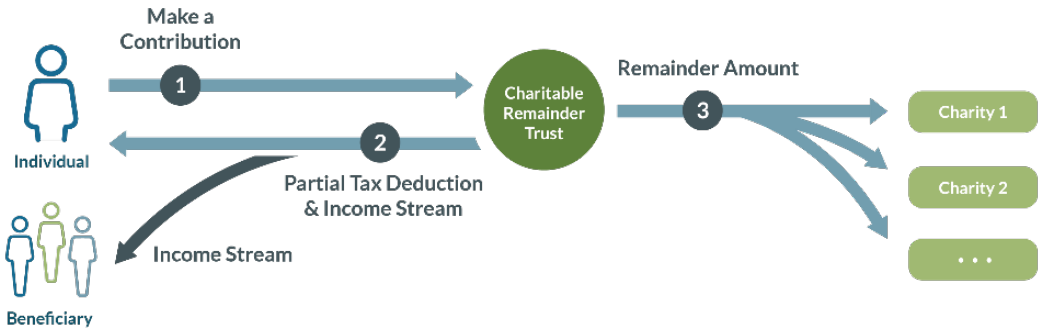
Process Overview and FAQs



Source: fidelitycharitable.org

Are there restrictions?

Yes. There must be a "reasonable likelihood" that at least 10% of the original amount that you contributed to the CRT (10% of the fair market value at the time of creation) will go to charity at the end of the trust term. If it's determined that there's a greater than 5% chance that the trust will exhaust its assets before the end of the trust term the CRT will not be viable. The term of the income stream must be either a fixed term of 20 years or less or a lifetime. If you are married, it can be paid for as long as *either* of you lives. The income can also be paid to your children for their lifetimes or to any other person or entity you wish, providing the trust meets certain requirements.

How is the Income Tax Deduction Determined?

The deduction is based on the amount of income received, the type and value of the asset, the ages of the people receiving the income, and the Section 7520 rate, which fluctuates. Generally, the higher the payout rate the less the remainder amount for the charity, and the lower the tax deduction for the donor.

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How is the Income Received?

Two options:

- *Charitable remainder annuity trusts* (CRATs) distribute a fixed annuity amount each year, and additional contributions are not allowed. This option is usually a good choice at older ages but doesn't provide protection against inflation.

- *Charitable remainder unitrusts* (CRUTs) distribute a fixed percentage based on the balance of the trust assets (revalued annually), and additional contributions can be made. This option is usually a good choice for those with longer life expectancies because it provides protection against inflation.

Is it a good fit for me?

It is important to consider your financial plan when evaluating whether a CRT is a good fit for your goals. If an immediate deduction and consistent income complement other strategies within your financial plan, a Charitable Remainder Trust may be the right path. Pacific Wealth Management can help you organize your goals and utilize the best vehicle to address your needs so you can have full confidence in your financial future.

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Sound Management for *your* Secure Future

Pacific Wealth Management is a fee-based, fiduciary firm offering comprehensive Retirement Planning expertise.

Our disciplined retirement planning process includes:

- Goals Based Needs Analysis
- Social Security Planning
- Long term Projections
- Monte Carlo Analysis
- 401(k), 403(b), 457 retirement plan analysis
- Retirement Distribution Strategies

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