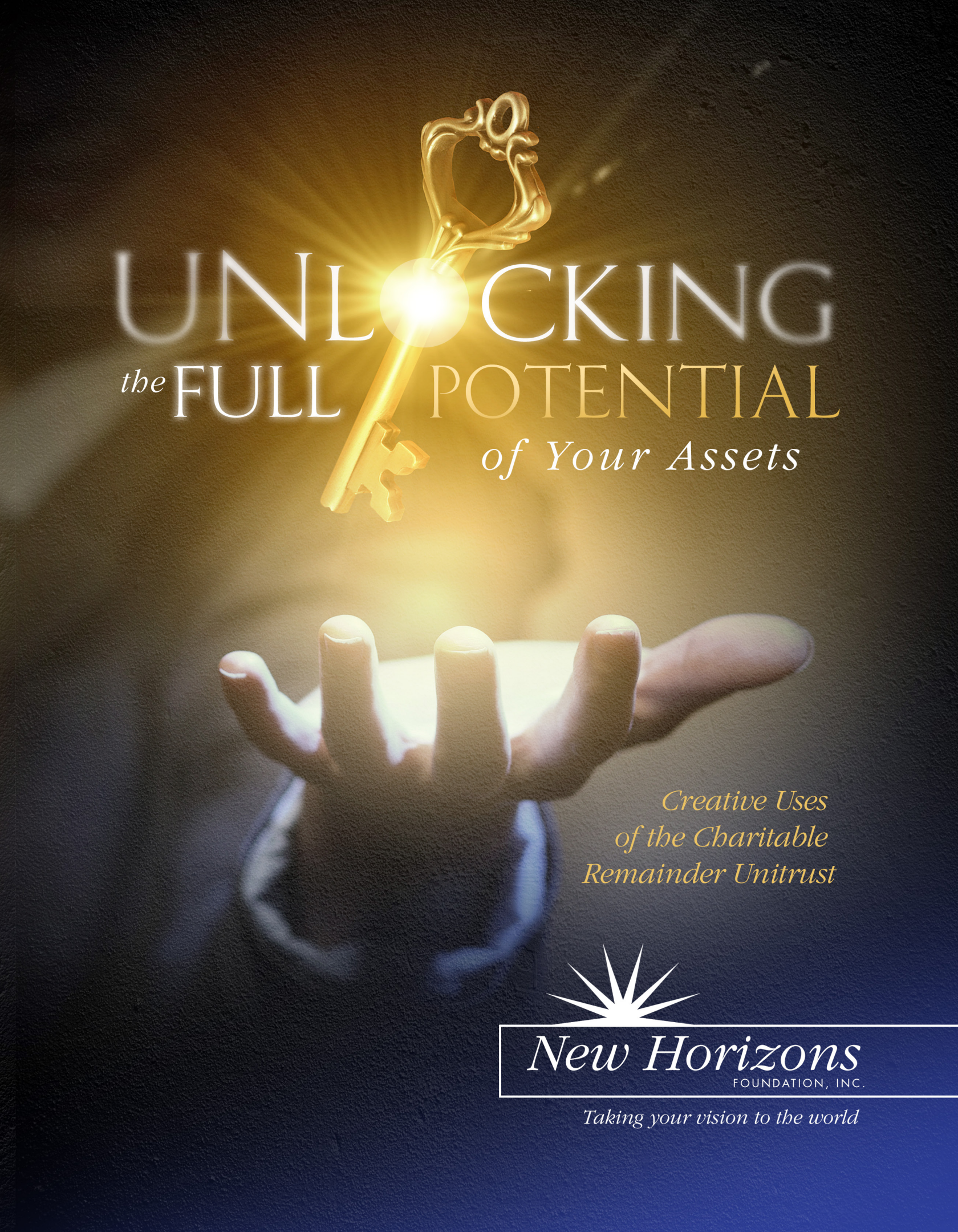
UNLOCKING the FULL POTENTIAL of Your Assets



Creative Uses of the Charitable Remainder Unitrust

New Horizons
FOUNDATION, INC.

Taking your vision to the world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Setting up a charitable remainder unitrust is a lot like buying a new car. You can buy one off of the lot that has been outfitted with standard features that most people commonly need or you can have a car customized for you at the factory with not only everything on it that you need, but also everything that you want. In most cases, you will be driving this "car" for a long time. Wouldn't it be better to get a car with all the extras that you might need or want in the future, rather than settling for a basic model, especially if there is no difference in the price?

When a family buys a new car, they are also buying it for one or more particular purposes. If they buy an SUV, they want an all weather, all terrain solid vehicle. If they buy a Prius they want good fuel economy. If they buy a van, they want a vehicle that can carry more people and hold more cargo. Bigger cars for long driving and smaller cars for commuting. Different types of cars have different purposes.

In the same way, when a family gets a charitable trust they are setting it up for one or more particular purposes. **This booklet organizes the discussion about charitable trusts around the primary purposes that a family might choose for setting up a charitable trust.** As with a new car, a family is usually establishing a charitable trust to meet multiple purposes and it will usually last a long time. The problem is that if a car dealer only sells a few types of cars or only one brand, they usually have just the basic package available for customers. They don't really know about other types of cars or what extras can be available. Instead of ordering a customized car from the factory, they settle for what the factory gives them. The same is true for charitable trusts. Many charities or financial advisors utilize the basic package for a charitable trust because it is all they have ever seen or all they have access to get through their attorneys.

Most attorneys, even those who do a fair amount of estate planning, will only draft a handful of charitable trusts in their career. Because of the degree of regulations with charitable trusts, they tend to stick with a basic trust form. They have not had a reason or the chance to research all that can be done with the charitable trust. As an Attorney that specialize in charitable planning I have taken the time to understand and research all of the options available for charitable trusts and I have drafted hundreds of charitable trusts not just a handful. The New Horizons Foundation has access to all the options and can customize the trust specifically for each family's needs around their primary purposes for setting up the trust.

This booklet will help you understand what purposes are available for a charitable trust and what options can be included in your trust so that it can be customized for your family.

Bill Moritz, JD
Executive Director
The New Horizons Foundation


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UNLOCKING THE FULL POTENTIAL OF YOUR ASSETS:
Creative Uses of the Charitable Remainder Unitrust

TABLE OF CONTENTS

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Taking your vision to the world

BASIC TRUST DECISIONS

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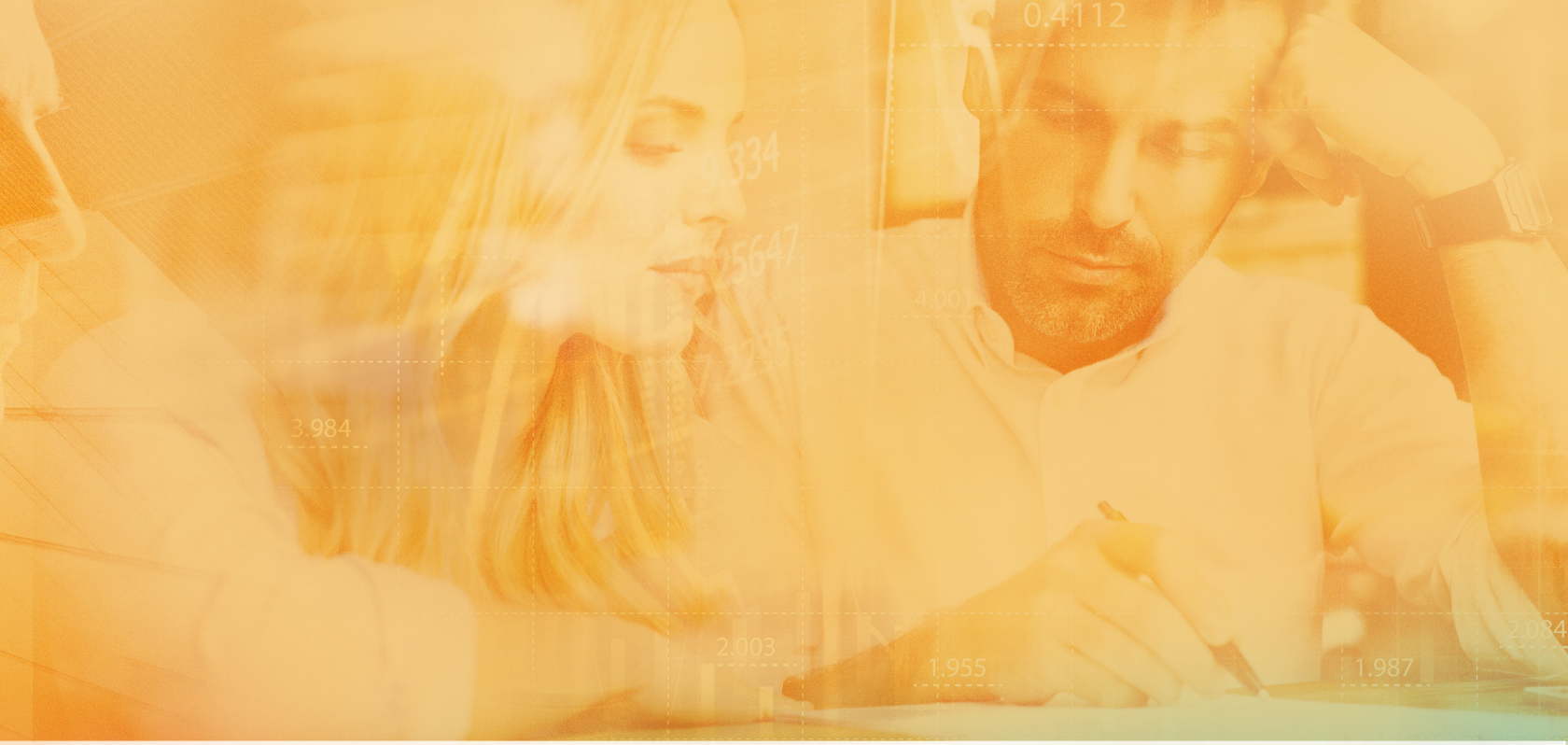
Charitable techniques have been given special treatment under the Internal Revenue Code because of their benefit to society through the support of charities and charitable projects. Charitable planning can utilize many different types of planning techniques, but this booklet will focus on the charitable remainder unitrust because this type of trust is the most versatile charitable planning instruments that a family can utilize.

Charitable remainder unitrusts (CRUTs) make up the largest share of the split interest trusts (85%) and there are over 100,000 CRUTs in operation today. The examples in this booklet have been given to illustrate different primary purposes the trusts can serve, but the trusts can have a high degree of customization with multiple benefits to produce exactly the results that a family wants and needs. I have used all of the examples given in the booklet and many hybrids and combinations. This booklet has not been written to be a comprehensive technical treatise on charitable remainder unitrusts, but rather a starting point for discussions to see if a charitable remainder unitrust could be an important part of your family's estate and financial plan. As I often ask clients who are facing different tax consequences that could be helped by charitable planning, "would you allow a charity to compete for the government's share of the transaction."

Though there are many significant and beneficial advantages to the charitable remainder trust and its ability to solve tax, financial and estate planning issues, if benefiting charity is not a substantial interest for setting up the trust, then you will likely never be completely satisfied with the trust. If you are delighted at the idea that a substantial gift to charity will occur at the end of the trust, then it is likely that your satisfaction will grows during the term of the trust.

There are three primary parties that benefit from a charitable remainder unitrust; the family that creates the trust, the charity who will receive the principal after the trust terminates and the investment advisor who will invest the funds during the term of the



trust. Though all will benefit, there is a possibility for those interests to compete. It is important for the attorney who is drafting the document to know who their primary client is in the transaction. The family may want to maintain the most flexibility during the term of the trust and maximize the income coming out of the trust, which reduces the future principal to the charity and cause less to be available for investment during the trust term. The charity would like to be guaranteed that they will stay the charitable beneficiary and that the principal will grow over time. The investment advisor is interested in seeing the principal grow (more to invest) and the trust be in existence for as long as possible. There is also one other interested party to the transaction who wants to be satisfied and that is the IRS which is why they have provided sample documents for charitable remainder unitrusts that most people end up following without fully exploring their options.

While it seems obvious that the grantor should be the primary client, if the trust is initiated by the charity or the investment advisor, the attorney may not consider all of the options available to the grantor and his or her family or if the attorney in not very familiar with charitable trusts he or she may choose to utilize a simple basic trust or the IRS sample documents. Considering and choosing the options available can greatly increase the satisfaction with the trust and its operation. My experience as an attorney having drafted over 200 of these trusts is simple, "if momma ain't happy, ain't nobody happy!" So I work hard to make sure the grantor's family feels like the trust has been customized for them and meets as many of their needs as possible.

There are seven primary considerations that should be addressed in order to properly draft the trust:

1. What asset(s) will be used to fund the trust?
2. Who will be the income beneficiaries and what are their needs?
3. What will be the term or length of the trust?
4. What should be the payout rate for the trust?
5. Which charities will benefit from the trust and when?
6. Who should be the Trustee of the trust?
7. What are the tax consequences for the trust?

DRAFTING YOUR TRUST

The following questions illustrate some of the important decisions that need to be considered when drafting the trust document.

1. WHAT TYPE OF CHARITABLE TRUST WOULD BE BEST?

There are three primary types of charitable trusts allowed under IRC 4947, the charitable remainder trust, the charitable lead trust and the straight charitable nonexempt trust.

A. Charitable Remainder Trusts are irrevocable tax exempt split interest trusts where the income is paid to non-charitable beneficiaries and then at the end of the trust term the principal goes to charity. A charitable tax deduction is received for the present value of the future interest that will be going to charity.

B. Charitable Lead Trusts are irrevocable non-exempt split interest trusts where charitable beneficiaries receive the income for the trust term and then the principal either is returned to the grantor or goes to the grantor's family. A charitable tax deduction is received for the present value of the income interest that will paid to charity over the term of the trust.

C. 4947(a)(1) Charitable Trusts are irrevocable non-exempt trusts where both the income and principal are dedicated to charity. This trust is a bit of a hybrid under the tax code because it is treated like a public charity for charitable deduction purposes but then is not exempt from taxation during the term of the trust.

2. WHAT FORM OF CHARITABLE REMAINDER TRUST SHOULD BE USED?

There two primary forms of Charitable Remainder Trusts.

A. The Charitable Remainder Annuity Trust (CRAT) is a charitable remainder trust in which the income payments to the non-charitable beneficiaries are fixed throughout the life of the trust. The Trustee calculates the amount by multiplying the initial fair market value of the principal by the trust payout percentage and then the trust will pay that amount each year for the remainder of the trust.

B. The Charitable Remainder Unitrust (CRUT) is a charitable remainder trust in which the income payments to the non-charitable beneficiaries fluctuate based on the fair market value of the principal each year. The Trustee calculates the annual payout each year by multiplying the percentage payout of the trust times the fair market value. Eighty-five percent of the charitable remainder trusts in existence are CRUTs because of the extra advantages that they hold, so the information in the booklet will focus on these types of trusts.

3. WHAT PAYOUT METHOD SHOULD BE USED FOR THE CRUT?

There are four methods of payout for the charitable remainder unitrust.

A. The Straight Payout Method pays out the payout percentage listed in the trust times the fair market value of the trust principal regardless of what is earned by the trust.

B. The Net Income Payout Method pays out the lesser of the net income earned by the trust or the percentage listed in the trust times the fair market value of the trust principal for the year.

C. The Net Income With Makeup Payout Method pays out the lesser of the net income earned by the trust or the percentage listed in the trust times the fair market value of the trust principal for the year however, any deficiencies from previous years must be paid out of excess income that is earned above the trust percentage amount. Deficiencies that result from income not paid in previous years because of the lack of trust income, accrue and can be made up in future years when the net income is greater than the unitrust amount.

D. The FLIP Payout Method pays out the lesser of the net income earned by the trust or the percentage listed in the trust times the fair market value of the trust principal for the year however, any deficiencies from previous years must be paid out of excess income that is earned above the trust percentage amount. A Trust with the FLIP provision allows for a triggering event that will cause the trust to "Flip" from a

Net Income With Makeup Trust to a Straight Payout Trust for the remainder of the trust term. This can be useful to provide a guaranteed income in later years.

4. HOW IS THE PAYOUT PERCENTAGE FOR THE TRUST DETERMINED?

The payout percentage of the Trust must be at least 5% but can then be adjusted based on the term of the trust. The CRUT must have a charitable value (the present value of the future gift to charity) of at least 10% of the value of the trust principal.

This is what determines the value of the charitable deduction that is available to the grantors. The higher the percentage and the longer the length of the term, the lower the charitable percentage. This decision is very important because it effects the amount of income that will be paid out, the length of the trust and the amount of the initial income tax deduction.

5. HOW LONG SHOULD THE TRUST LAST?

There are four ways to determine how long a charitable remainder unitrust can last the term must be included in the trust document.

A. The Term can be based on a set number of years. The term of the trust may be from 1-20 years.

B. The Term may be based on individuals' lifetimes. The trust term may stipulate that the trust is to exist for one or more named beneficiaries lifetimes.

C. The Term may be for a term of years or lives in being whichever is longer. This ensures that if a couple set up a trust for their lifetimes, but then die within the first couple of years that their children will be paid the remainder of the trust term.

D. The Term may be for lives in being plus a term of years. This can be useful with older income beneficiaries who want to extend the length of the trust after their deaths as an inheritance to their children.

6. WHO CAN BE THE CHARITABLE BENEFICIARY?

The charitable remainder unitrust must list a public charity or private foundation that is in existence when the trust is formed to be the charitable beneficiary. The deduction limitations for public charities and private foundations are different so this will need to be discussed before naming a private foundation. The grantor may retain the right to change the charitable beneficiary during the term of the trust or give the Trustee the right to do so. A private foundation can be changed to a public charity, but because of the differences in the deduction amounts a grantor cannot change a public charity to a private foundation.

7. WHO CAN BE THE TRUSTEE?

The Trustee of the trust can be the grantor, a charity, trusted friends, family members, advisors or a professional trustee. If you want to have the ability for the Trustee to "spray" income to a variety of beneficiaries, then the trustee cannot be the grantor or a member of the grantor's family. A spraying provision allows the Trustee each year, in its sole discretion, to pay to a variety of income beneficiaries or classes of income beneficiaries who are named in the trust the income for the trust that year. Distributions do not have to be equal or the same from year to year.

8. WHO CAN BE THE INCOME BENEFICIARIES?

The income beneficiaries are most often the grantors and/or the grantor's family members but they really can be anyone or any entity. Charities may be income beneficiaries though there must be at least one non-charitable beneficiary for the trust in order to qualify as charitable remainder trust. The trust document can even list classes of people, such as grandchildren, so long as the term of the trust is ascertainable at the outset of the trust.

9. WHAT ASSETS ARE YOU USING TO FUND THE TRUST?

Often the best assets to use in funding the charitable remainder unitrust are appreciated assets or assets that have been depreciated because of the avoidance of capital gain at the sale of the asset in the trust. There are however many other assets that can be used with a variety of advantages but there are also assets that should not be used to fund the trust. Assets with debt, that produce debt

financed income or business interests that produce business income should generally be avoided. This is an important discussion to have with your legal advisor.

10. WHAT INCOME TAX DEDUCTION METHOD SHOULD BE USED?

The income tax deduction is usually a choice between a deduction based on the grantor's basis in the asset or by the fair market value of the asset as determined by a qualified appraisal. The choice often depends on the charitable value of the trust, the cost of the appraisal, when a sale of the asset is contemplated, if there is to be a bargain sale of the asset, the type of asset being given or several other important issues. This is a decision to make in consultation with an accountant and/or legal advisor.

11. HOW SHOULD THE TRUST ASSETS BE INVESTED?

This is a discussion that will be based on how much income is to be paid out, when income will be paid and the grantor's tax preference for the income. There are several types of investments that are toxic for the trust and generally should be avoided such as debt financed income and business income. It is important to note that similar to Obamacare, "if you like your broker, you can keep your broker!" or you can choose a Trustee like The New Horizons Foundation that will have professional money management available for charitable trusts.

12. CAN THE TRUST BE TERMINATED EARLY?

In special circumstances the trust can be terminated early. Depending on the state where the trust resides, the district court or the state attorney general's office may need to be involved in the process. As a general rule, if the trust is terminated and divided between the charity and the income beneficiaries, the income beneficiaries will be receiving their income interest as an appreciated asset with a basis of zero that has been sold and the proceeds distributed to them and thus a capital gain tax will be due. If the income interest is donated to charity then the grantor will receive a charitable deduction for the fair market value of the income interest. The later can be usually accomplished without court or state intervention.

13. HOW IS INCOME THAT IS PAID OUT TAXED TO THE INCOME BENEFICIARIES?

There is a four tier system for determining the taxability of income that is received by the income beneficiaries from a charitable trust. The tiers of income are booked in the trust and must be paid out in order as trust income is paid out depending on how the income was earned or on the accrued amount in tiers from previous years.

A. Tier One is Ordinary Income. If the trust earns any ordinary income it must be paid out first to the income beneficiaries. Any ordinary income that is not paid out will accrue in the trust and be paid out first in future distributions.

B. Tier Two is Capital Gain Income. If the Trust earns long term capital gain income or if the asset that was originally sold and a capital gain resulted but was not paid out, then the second tier of income from the trust is long term capital gain.

C. Tier Three is Tax Exempt Income. If the Trust earns tax exempt income and it has paid out all of the accrued income from tiers one and two then the income will be reported to the beneficiaries as tax exempt income.

D. Tier Four is Return of Principal. If the Trust is required to make a distribution and it has not earned or accrued any ordinary income, capital gain income or tax exempt income and there is none of these types of income that have accrued from previous years in the trust, then the distribution will be a return of principal and thus not taxable.

14. WHICH TAXES SHOULD BE AVOIDED OR REDUCED?

Because the charitable remainder unitrust is a tax exempt entity, it can help a family avoid or reduce several different kinds of taxes at

1) the establishment of the trust,

2) during the trust term and 3) when the trust terminates.

Taxes that can be affected include capital gains tax, income tax, estate tax and gift tax. Taxes that the grantors are trying to avoid or mitigate now or in the future are an important consideration in drafting the trust document.

HOW THE CHARITABLE REMAINDER UNITRUST WORKS

A charitable remainder unitrust is a tax advantaged way to benefit yourself, loved ones and your favorite charity or charities. In exchange for your charitable gift to the unitrust, you and/or your loved ones can receive an income for a lifetime or a term of years, then the trust principal is distributed to charity. The charitable remainder unitrust maximizes tax and financial benefits while allowing families to make a significant gift to charity after they have used the funds. The federal government provides tax benefits to encourage families to utilize the charitable trust to support charity. The CRT allows families to have an income for life, avoid capital gains tax at the sale of an asset, get an income tax deduction for the gift, avoid probate and estate tax on the principal, choose who they want to benefit, place the trust assets outside of the reach of creditors and provide a significant benefit to their favorite charity or charities.

A charitable remainder trust is an irrevocable trust that is funded with a gift of cash or property which provides income payments to named beneficiaries for a term which can be their lifetimes or a term of years with the principal going to charity at the end of the term. The property in the trust is managed as a separate entity and is not comingled with other funds. The payout percentage rate from the trust is established when the trust is drafted and is based on the principal amount in the trust as valued annually. The payout percentage must be at least 5% and the maximum is based on the number of years the trust will potentially be in existence and the IRS's Applicable Federal Rate. The present value of the future gift to charity must also be at least 10% of the trust value at funding. Once established, the percentage payout rate will be the same each year but the amount may go up or down based on the amount of the principal at the beginning of the year. Because the funding of the trust is an irrevocable future gift to charity, the grantor gets a charitable tax deduction based on the present value of the future gift to charity. IRS tables will determine what percentage of the trust principal is apportioned to the income interest that the beneficiaries will be receiving and what percentage is apportioned to the charity which will receive its funds at the termination of the trust. The chart illustrates the basic elements of the charitable remainder unitrust.

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids Capital Gains Tax
- Current income tax deduction
- Possible future tax deductions
- Avoids probate
- Avoids estate tax
- Liability Protection
- A hedge against inflation
- Asset Management
- Flexible Income Payments
- Benefiting other family members
- Favorable tax treatment
- A Significant Gift to Charity

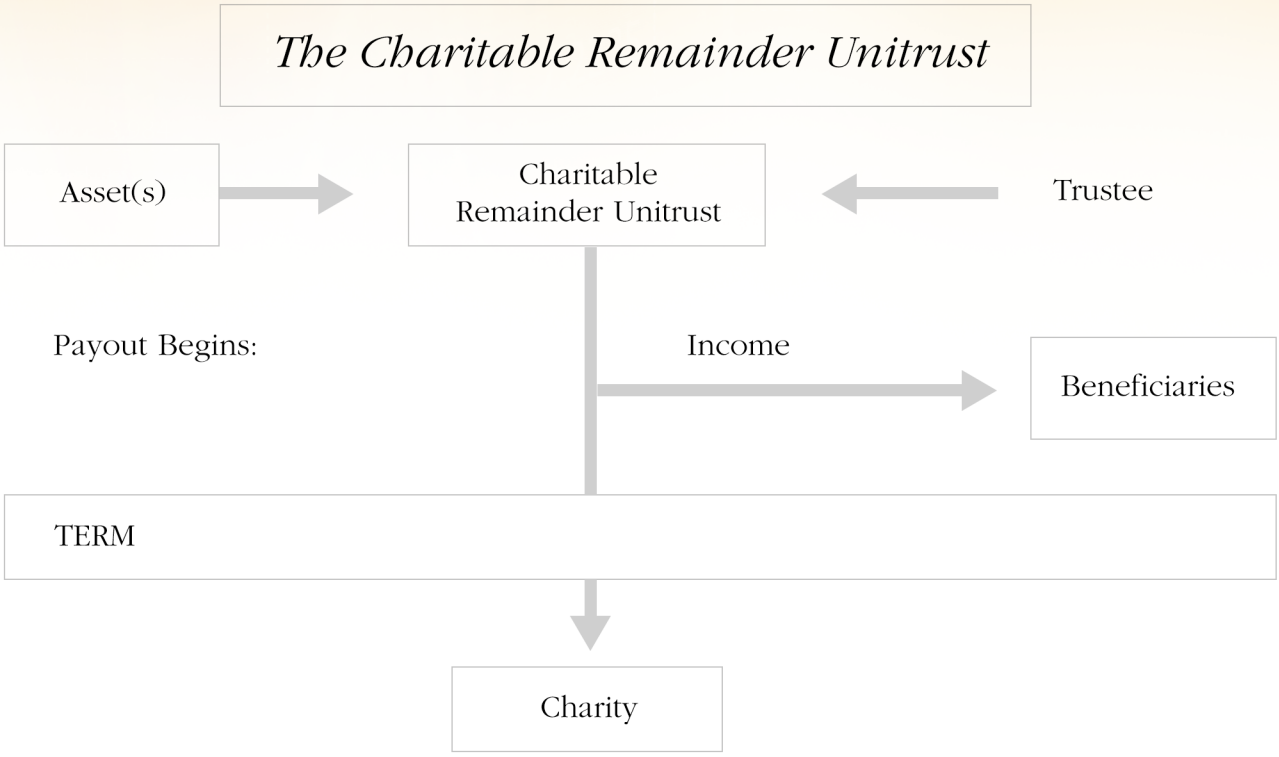
THE UNITRUST BENEFITS:

Avoid Capital Gains Tax

Funding the unitrust with appreciated property is the best way to realize the full advantages of the unitrust. Currently, if your appreciated property is sold in most states, approximately one fourth of the value of the appreciation is lost to capital gains tax. If you have a low basis in the property either because you have owned it a long time or it has been depreciated, it could result in a significant tax. Because the unitrust is tax exempt there will be no capital gain tax on a transfer of appreciated property to the trust and there will be no tax payable by the trust if the property is sold later.

Current Income Tax Deduction

A grantor who itemizes can get a sizable charitable income tax deduction in the year that the unitrust is funded. The



deduction can either be the fair market value of the asset or the grantor's basis in the property. The deduction is for the future gift to charity and so is a percentage of the value of the gift. The choice as to which method of calculating the charitable deduction should be used will be based on how much can be used by the grantor and when. The income tax deduction can be carried forward five additional years. Charitable deductions for gifts of appreciated property can be used against 30% of a grantor's adjusted gross income. Charitable deductions for gifts of property using the basis are used against 50% of a grantor's adjusted gross income. The amount of the tax deduction is based on the Treasury tables.

Future Income Tax Deductions

Income tax deductions may also be taken during the term of the trust by releasing principal from the trust early to charity. When principal is released, the income beneficiary gets the value of the income interest in the property that he is giving up as a current charitable deduction. For example, if a there was a 10% charitable value at the funding of the trust, then the income interest would be worth 90% of the value. If a portion of the principal were released in the second year of the trust the income beneficiary would get a charitable tax deduction for approximately 90% of what was released. This can be a great way to do charitable giving because the grantor gets the charitable deduction without receiving any taxable income. The deduction can then be used against other earned income.

Estate Tax Deduction

When an individual or husband and wife are the only beneficiaries of the unitrust, the trust assets are not taxed in either of their estates at death, there is a 100% charitable estate tax deduction. With the increase of the value of the estate tax deduction this has become less of an issue and more people are adding a term of years or a guaranteed term to the unitrust to pay out to children after their death. In this case the value of the income interest going to children will be included in the estate.

Avoids Probate

The unitrust is a separate legal entity outside of the estate, so it is not subject to the administrative fees and other probate costs of assets includable in the estate.

A Hedge Against Inflation

The annual amount that is received from the unitrust reflects

any increase or decrease in the trust's value. If the unitrust earns more than the stated percentage, that additional amount is added to the principal and the next year's annual income is based on the higher principal value. In the same way if the trust principal decreases in value then the payout amount may be less than the previous year.

Asset Management

You can relieve management or investment worries for yourself or your loved ones because the assets transferred to your trust can be managed by experienced and competent advisors.
If you wish to be involved in the investment decisions or management of the trust, that can also be arranged. The Trustee of the trust has the legal responsibility for management of the assets.

Liability Protection

Because the unitrust assets are removed from your estate and the trust is irrevocable, the assets can be set up so that they are beyond the reach of creditors, providing you and your loved ones with some security during these troubled times. The trust can also be written so that it is not considered marital property and will not negate disability or other government benefits.

Favorable Tax Treatment of Income

Depending on how the trust assets are invested you may be able to receive part or all of your income as capital gain, or as tax-free income if the assets are invested in tax-exempt securities. There may also be a way to convert current ordinary income to capital gain income in the future.

Flexible Income Payments

The Trustee of your trust can cause the income to be accumulated in the tax-free environment of the trust or maximize the income payment to the beneficiaries depending on your needs. Decisions regarding who receives income and how much is received can often be made on a year to year basis if the trust is written to include that option.

Benefiting Family Members

There are many ways that the trust can benefit family members other than the grantors. The trust can be written to allow the Trustee to pay the trust income to different family members during the term of the trust, allowing the trustee to pay for children's or grandchildren's education. The trust can also be written for a guaranteed term of years in case the grantors die prematurely or a term of years can be added on to the trust after the grantors' deaths.

A significant Gift to Charity

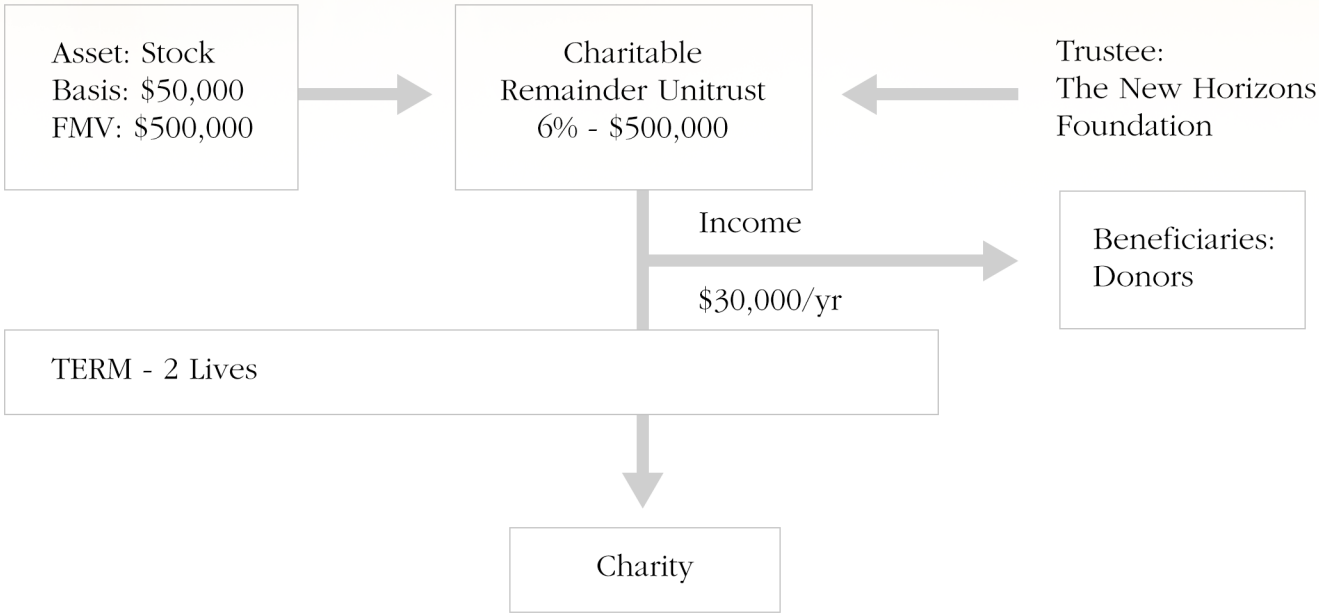
Perhaps the biggest benefit is the "measure of immortality" you receive from knowing that your significant gift to charity at the end of the trust term will support the ideals and programs of your favorite charities long after your own life.

INCREASED INCOME TRUST

Many people are currently in a "Catch 22" situation. They are receiving a low income return from appreciated real estate or securities, but if they sell the property or stock they face a significant capital gains tax on the appreciation which diminishes the value of the asset. Many people are using CDs which may be paying as little as 1% a year which does not even keep up with inflation.

The charitable remainder untrust can be a great way to solve this problem and increase the income you will receive from an asset either currently or at your retirement. Since the unitrust can be used to avoid tax on capital gains at the sale, the trust will have that much more to reinvest. This means greater income because the amount of the tax that would have been paid if the assets were sold, will be invested by the trust, not paid over to the Internal Revenue Service.
In addition to the capital gain tax savings, you also will receive a current income tax deduction for the future value of the gift to charity in the year the trust is funded, further increasing the initial benefits of the trust. After the trust is funded, the Trustee can find investments that have a better annual return.

The Increased Income Trust



Example:
A couple is earning 1% on dividends that they are receiving from stock they have owned for many years. The value of the stock is $500,000 so they are only earning $5,000 a year. Because of the length of time they have owned the stock, their basis is only $50,000. If they sold the stock and paid the capital gains tax they would have $387,500 left to invest for income. By transferring the stock to a CRT and then selling the stock, the trust will have the full $500,000 to invest for income. If the Trustee were able to earn 6% per year, the annual income would be $30,000 instead of $23,250 if the tax were paid, both are better than the $5,000 they are currently receiving. If the Trustee were able to earn 8% per year then the trust income would actually grow by 2% each year helping with inflation. In addition to avoiding the capital gains tax, they would also have a current income tax deduction of at least $50,000 which could be used against other ordinary income. The couple chose The New Horizons Foundation as Trustee of the trust so that they would not have to worry about the administration and tax reporting. They would also have the other benefits of a charitable remainder unitrust including a significant gift to the charity of their choice after their deaths.

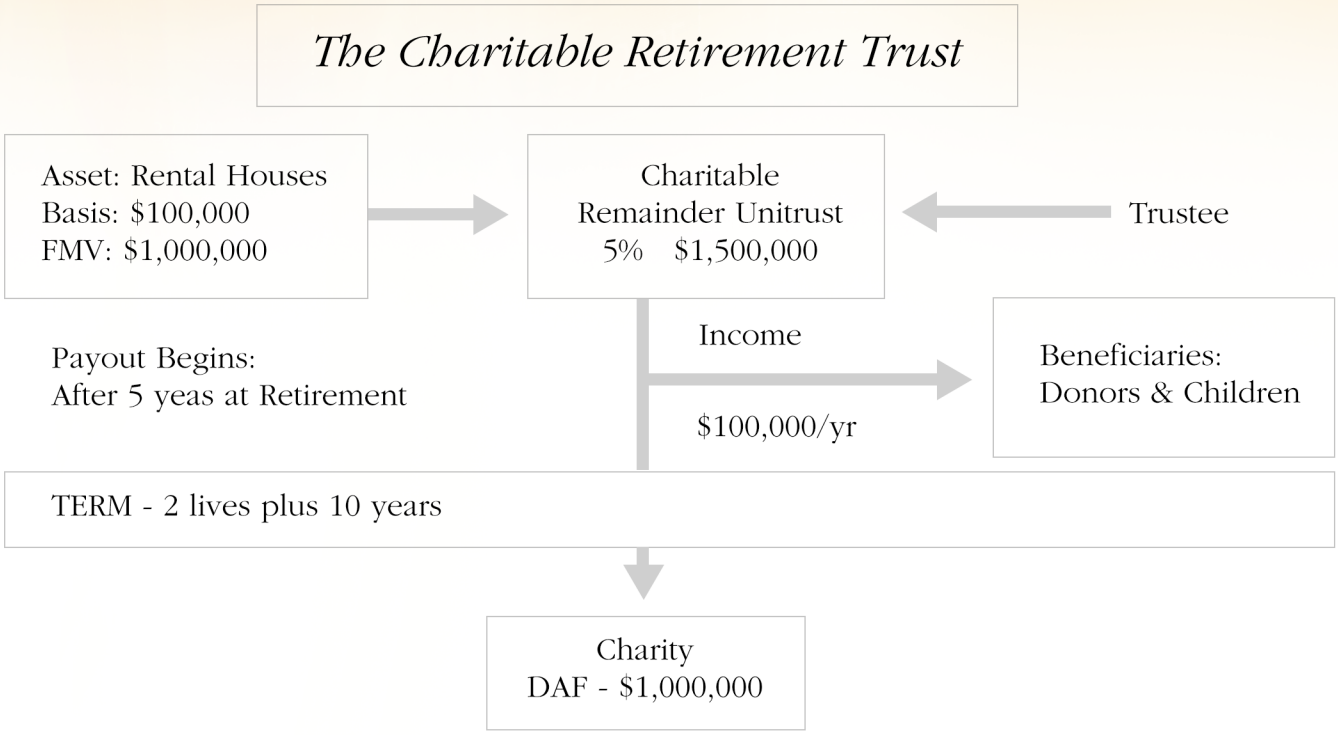
TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids Capital Gain of $450,000 at sale
- Current income tax deduction of at least $50,000
- Possible future tax deductions
- Avoids probate
- Avoids estate tax
- Liability Protection – not subject to creditors also can be Medicaid exempt
- A hedge against inflation, income could grow by 2% per year
- Asset Management – the charitable foundation they have chosen will manage the trust
- Flexible Income Payments – they can choose to take reduced income now and increased income later
- Benefiting other family members – they can add a term of years on to the end of the trust
- Favorable tax treatment
- A Significant Gift to Charity

THE CHARITABLE RETIREMENT TRUST

One of the biggest challenges of estate and financial planning today deals with assisting individuals and families prepare for retirement. Although people look forward to the years when their time is not devoted to a job or business, they still want to enjoy their current lifestyle and standard of living which usually means maintaining an appropriate level of annual income. Qualified Retirement Plans have been a popular means of saving money for the retirement years. The deductibility of contributions, the tax-free environment in which the funds can accumulate, the liability protection and the extended time of withdrawal at retirement make the qualified retirement plan an excellent planning vehicle for retirement. However, legislation has taken about several of the benefits of the plan. Limitations on the kind of assets that can be contributed to a plan, the escalating costs associated with maintaining the plan, the inability to discriminate between employees, all income coming out is ordinary income and the inclusion of the plan in the owner's estate have caused the qualified retirement plan to lose a little of its luster.

The Charitable Retirement Trust is similar to an IRA or qualified retirement plan in that it is a trust, which is exempt from income tax, and it is possible to obtain tax-free growth on the investment of assets within the trust. In addition, the Charitable Remainder Trust may be easier and less expensive to maintain. Many charities will manage these trusts with a small fee if the charity is named as a beneficiary. The CRT can be discriminatory and there is no limit on the minimum or maximum amount of contribution each year. You can begin taking income before age 59 ½ without penalty and you are not required to take mandatory minimum distributions after you turn 70 ½ . You can contribute property other than cash and the proceeds from the trust can be out of your estate at death for probate purposes and only the value of any income interest that is going to children in the future will be included in your estate for figuring estate tax. The chart illustrates the operation of the Charitable Retirement Trust.



EXAMPLE:

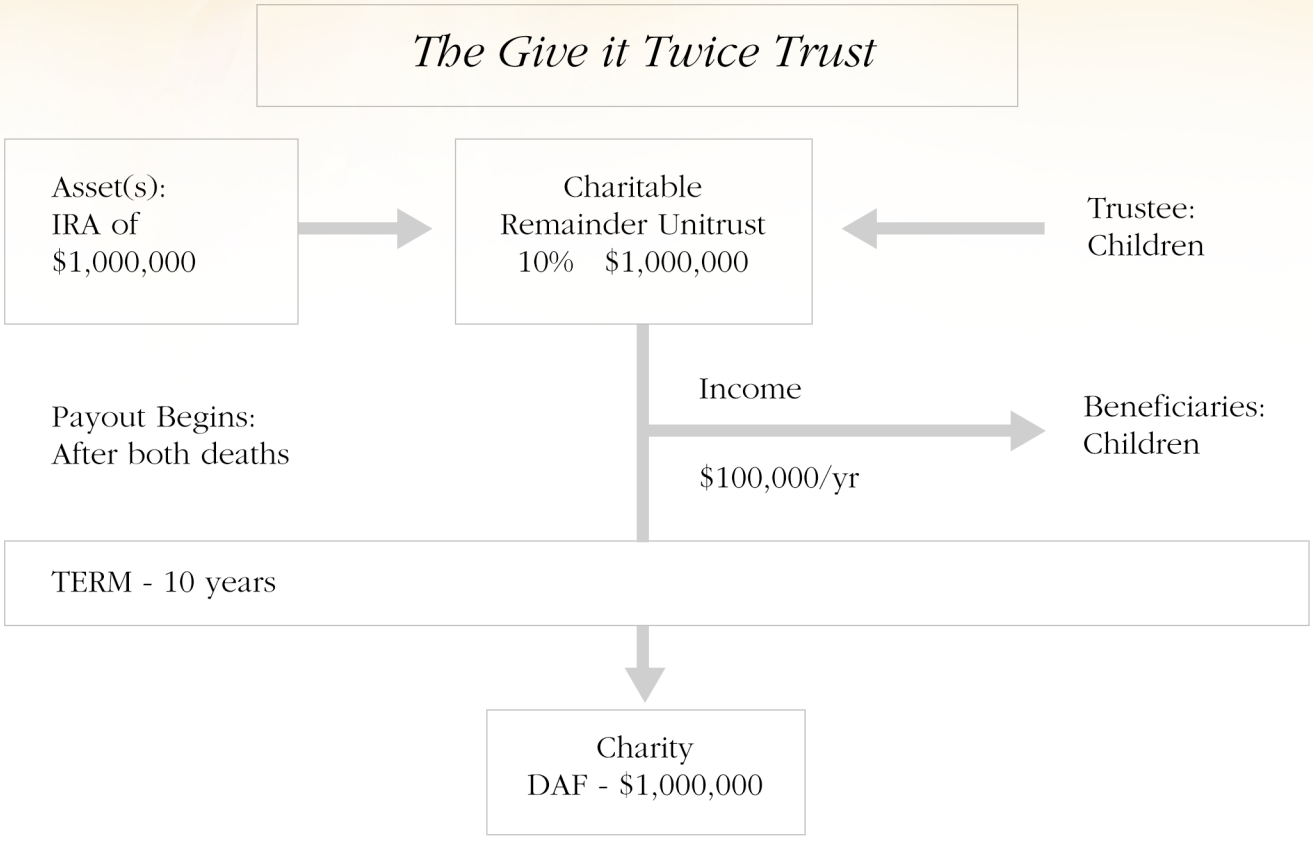
An individual has decided to purchase rental real estate instead of maximizing his qualified retirement plan each year. The rental real estate not only gives him a current income but also accelerated current tax deductions. In later years, as the properties mature and lose their tax deductions he will contribute the properties to a CRT and then sell them. If he owned 4 properties, each worth $250,000 he would have $1,000,000 to initially fund his charitable remainder unitrust. If he waited an extra five years until age 70 before taking any income out of the trust the trust principle might grow to as much as $1,500,000 before beginning to pay out, increasing his annual income by 50%. In addition, he could also make annual cash contributions to the charitable retirement trust also increasing his future annual income payments. Since he is delaying payment, he has added an additional 10 years onto the trust term to pay to his children after both his and his wife's deaths. Since he will be delaying payment for 5 years after funding, he will be able to make up for past income during the payout period of the trust allowing him to take out $100,000 in income even though the trust is only set to payout 5%. Assuming that the trust can actually earn 8% the $100,000 payout should last for the full term of the trust. The principal in the trust should be about $2,000,000 when it goes to charity making a truly significant gift to their favorite charities.

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids Capital Gain of $900,000 at sale of properties
- Current income tax deduction of at least $100,000
- Possible future tax deductions if principal is released to charity
- Avoids probate
- The income payment of $100,000 a year for 10 years is in his estate but the value will be less than $800,000 in the estate.
- Liability Protection – not subject to creditors also not marital property for children or even reportable on a FAFSA form for college
- A hedge against inflation
- Asset Management for grantors and children
- Flexible Income Payments – they can choose to not take income for five years and have an increased income later that will increase the size of the payout going to heirs
- Benefiting other family members – they have added a term of 10 years on to the end of the trust
- Favorable tax treatment – unlike a qualified plan the income will be taxed at capital gain rates if invested properly
- A Significant Gift to Charity

THE GIVE IT TWICE TRUST

The Give it Twice Trust is a great way to give an IRA or Retirement plan first to your children and then to your favorite charity. The Give it Twice Trust can be included in your revocable living trust and will come into being after both of your deaths and is a great choice for your IRA or qualified plan because the ordinary income tax that would have been due when the retirement assets are paid to another beneficiary are deferred. After both of your deaths the trust will be funded directly from your IRA or qualified retirement plan, since the CRUT is an exempt trust, the full value of the retirement plan will be in the trust to generate income. The Trust will then pay 10% a year to your children for 10 years and then the trust principal will go to charity so the trust principal has actually been given twice, once to your children and later to charity.



EXAMPLE:

An individual has an IRA with a value of $1,000,000. If, at his death, the IRA goes to his wife there will be no income tax due, but if at his wife's death the IRA goes to their two children there will be a tax due and since it will be on top of their annual income, the tax will be at the top tax rate. Depending on the state where the children live the tax could be as high as 40-45%. If the IRA goes to a Give it Twice CRUT and pays out 10% for 10 years then the children will get $100,000 a year for ten years or a $1,000,000 and then the principal will be given to charity. The distributions to the children will be taxed as ordinary income, but a lump sum payout with significant tax consequences has been converted to an installment payout which lessens the tax burden. This individual chose a Grantor Advised Fund at The New Horizons Foundation as the charitable beneficiary and named his children as the project managers for the fund. After the trust ends, his children will be able to give the $1,000,000 to the charities of their choice or even spend their retirement in charitable service.

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids income tax at initial funding, saves up to 40%
- Avoids probate on plan
- Allows for payout over a period of years instead of all at once
- Children can be the Trustee since there will be a simple 10% payout each year or the Charity could be the Trustee
- The trust benefits the children, because they will receive the full value of the IRA over a period of years instead of 60% if it went outright
- The children will get to either give the money away over time to the charities of their choice or spend their retirement doing good in charitable service with the DAF to fund their charitable activities

SPOUSAL CHARITABLE IRA TRUST

THE SPOUSAL CHARITABLE IRA TRUST

There are probably no more highly regulated entities under the IRS code than the qualified retirement plans. Retirement plans can be structured as corporate plans, IRAs, KEOGHs, 403(b) plans or 401(k) arrangements. Plan assets are potentially subject to four types of taxes:

1. The 10% penalty tax for distributions before age 59 ½ under IRC 72(t).
2. The income taxes during life (IRC 61(a)) or at death (IRC 691(a)), which are due when assets are taken out of the plan.
3. Estate tax under IRC 691(a) which could be up to 55%, depending on the size of the estate.
4. Even Generation Skipping tax can occur when retirement assets go directly to grandchildren or great-grandchildren. (IRC 2601).

The 10% penalty tax is easily avoided by waiting until age 59 ½ to withdraw money. Estate tax and generation skipping tax are often handled with normal estate planning, but the income tax consequences will affect almost everyone.

Income In Respect Of A Decedent

The proceeds of IRAs and qualified retirement plan accounts after death are taxable for income tax purposes to the direct recipient of the plan assets in the year received. This additional income is called Income in Respect of a Decedent (IRD). This income is normally taxed at the top tax rates because the total is added to your heirs' income in the year received -- usually driving them into the top tax bracket for some or all of the proceeds. This income is subject to both federal and state income taxes, leaving the recipient often with less than two-thirds of the value of the assets. For example, if an individual had a retirement plan of just $300,000 at death, over $100,000 could be due in income taxes. Given such erosion in value, it's no wonder that increased attention has been paid to combining charitable gift planning with retirement plan distributions.

Because of the tax-free accumulation and growth that occurs in retirement plans, the government has gone to great lengths to build a complicated tax structure to reclaim any lost tax revenue. Fortunately, the tax code has continued to protect charitable planning, which is one of the few ways left to ease the tax burden from retirement plans at death.

Contribution To A Charitable Remainder Trust

Perhaps the most useful technique to minimize the adverse tax effects of IRD and maximize the benefits available to children and other heirs is to distribute the plan assets to a charitable remainder trust. The goals of this type of planning are to eliminate IRD tax, enable the children to enjoy the economic benefits of the retirement plan proceeds over time, and provide a substantial gift to charity. The CRT is a tax-exempt entity and is not subject to the IRD tax. It also provides a charitable estate tax deduction for a portion of the amount placed in trust.

The Spousal Charitable IRA Trust

The Spousal Charitable IRA Trust (SCIT) is a specially designed charitable remainder unitrust that has been developed to benefit a surviving spouse who is due to receive a large retirement plan inheritance at the death of their mate. Since retirement income has not been taxed, it is taxed at the highest possible tax rate as ordinary income, compounded by required Mandatory Minimum Distributions. A surviving spouse may be paying a large amount of income tax, as high as 40% in some states, on money that he or she really doesn't need for living expenses. With the SCIT, this money could accumulate in a tax-free environment during the spouse's lifetime and be used for the income he or she needs and then for charity, children or both. Here's how it works:

1. The Spousal Charitable IRA Trust is a part of your revocable living trust with the surviving spouse as the primary beneficiary and can have children as the secondary beneficiaries. At the death of the first spouse, if he or she is the owner of the retirement plan, the funds in the plan are distributed directly to the SCIT. There will be no tax on this distribution since the trust is tax-exempt. One planning option might be to name the spouse as the primary beneficiary of the retirement plan and the SCIT as the successor. That way the surviving spouse will have a choice as to whether to roll over the full retirement plan or part of the retirement plan into an IRA or have it paid into the SCIT by disclaiming her interest.

2. The SCIT is a net income with make-up charitable trust which invests its assets so that income is only paid out when the surviving spouse wants to receive it. There are no Mandatory Minimum Distributions with a charitable trust. Income they don't want to receive can either accumulate for their future use, be saved for the children or be given away to charity. One advantage that comes with giving money to charity from the SCIT is that the surviving spouse gets a current income tax deduction in the year of the gift without having to declare any income. The IRA Charitable Rollover that has been used the last couple of years was a benefit because money went to the charity without having to be received personally, making it a wash. This is even better, because the spouse gets a tax deduction without having to declare the income so he or she can use the deduction against their other ordinary income.

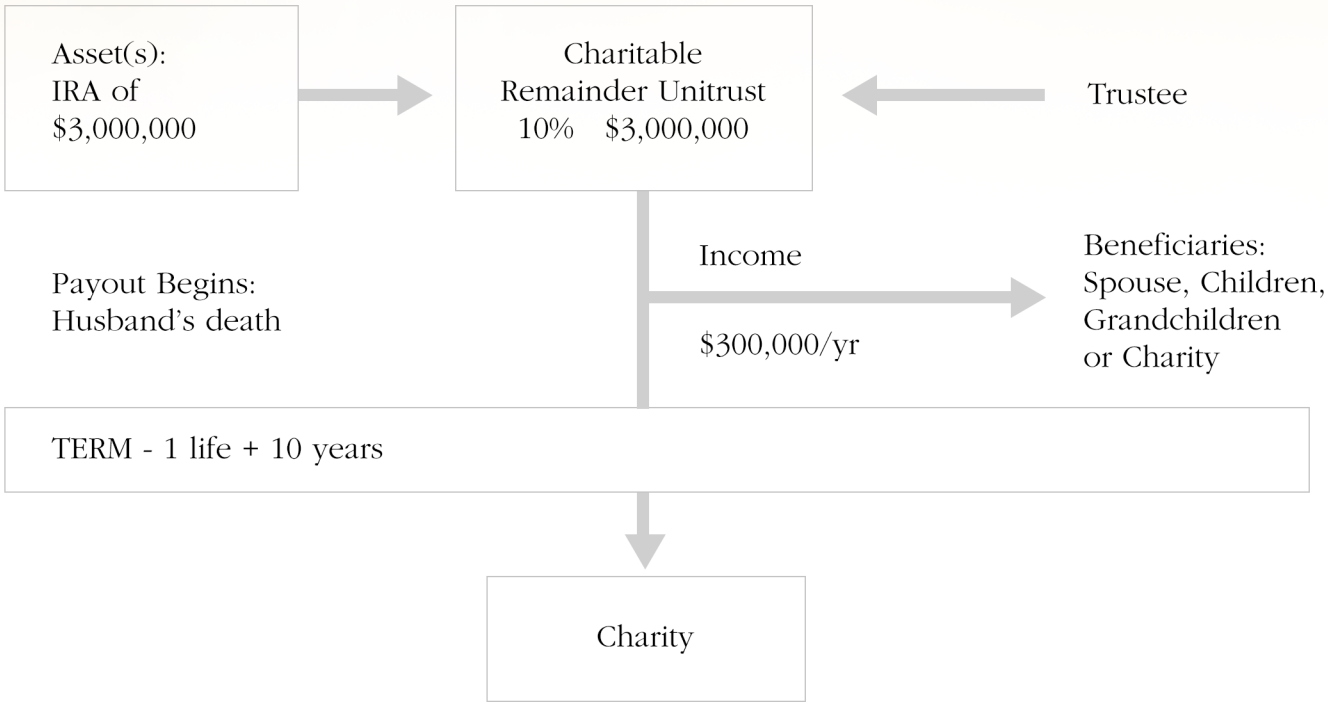
3. The SCIT is written so that it can pay a large income to the spouse, for example 10% a year, and then pay that income to the children for a period of years, up to 20, after the surviving spouse's death. Because one of the advantages of the trust is the ability to receive a current charitable tax deduction for gifts to charity, the SCIT is written so that it has the least charitable value allowed by law, which is 10% of the value of the trust, and the greatest amount attributable to the income interest for the spouse and the children, which is 90%. This will produce the highest amount of current tax deduction when gifts are given to charity during the term of the trust.

4. The SCIT is also outside of the estate of the surviving spouse and the children so it cannot be reached by creditors, it is not marital property and does not disqualify beneficiaries from receiving government benefits like social security disability.

5. The SCIT does not have to be funded with all of the retirement plan. The spouse can roll over half of the IRA to their own IRA and disclaim half so it will go into the SCIT. In so doing, charitable deductions from the SCIT can be used against Mandatory Minimum Distributions from the personal IRA.

The Spousal Charitable IRA Trust is a great way to enable charitably minded couples to plan to make significant charitable gifts, while saving taxes, after a spouse passes away. Because the trust is not funded until after the retirement plan owner's death, it can be changed up to that time or the surviving spouse can choose not to fund it or only partially fund it. But if the SCIT is not in the revocable living trust and named as a successor to the plan, you will not be able to take advantage of the benefits. If the spouse that does not own the plan dies first, then the SCIT operates for the benefit of the children at the owner's death. The payout to children will be 10% of the value for 10 years or more and then the assets in the SCIT will go to the charities of your choice. This enables you to give the assets in your retirement plan away twice, once to your children for a term of years and then to charity. Unfortunately, unless congress changes the law, the SCIT cannot be funded during the retirement plan owner's lifetime, which would make the benefits even greater.

The Spousal Charitable IRA Trust



EXAMPLE:

A doctor has been able to accumulate a $3,000,000 qualified retirement plan in addition to $3,000,000 that is the balance of his estate. At his death the retirement plan will go to his wife. The wife has income from other sources and so does not need or want the income from the retirement plan which she is forced to take because of Mandatory Minimum Distributions. Even if she would like to give the money away to their children, it will first be taxed to her and then be a gift subject to gift tax. If a Spousal Charitable Income Trust was included in their revocable living trust, then at his death, the trust would be funded without tax. Each year the surviving spouse could receive the income from the trust, have it paid to her children or grandchildren taxed to them in their tax bracket or give the income away to charity and receive a charitable income tax deduction that she can use against other ordinary income that she receives or any combination of the above. The trust can continue for 10 years after her death, paying out to the children and then the principal will go to charity.

TAX CONSEQUENCES AND OTHER BENEFITS:

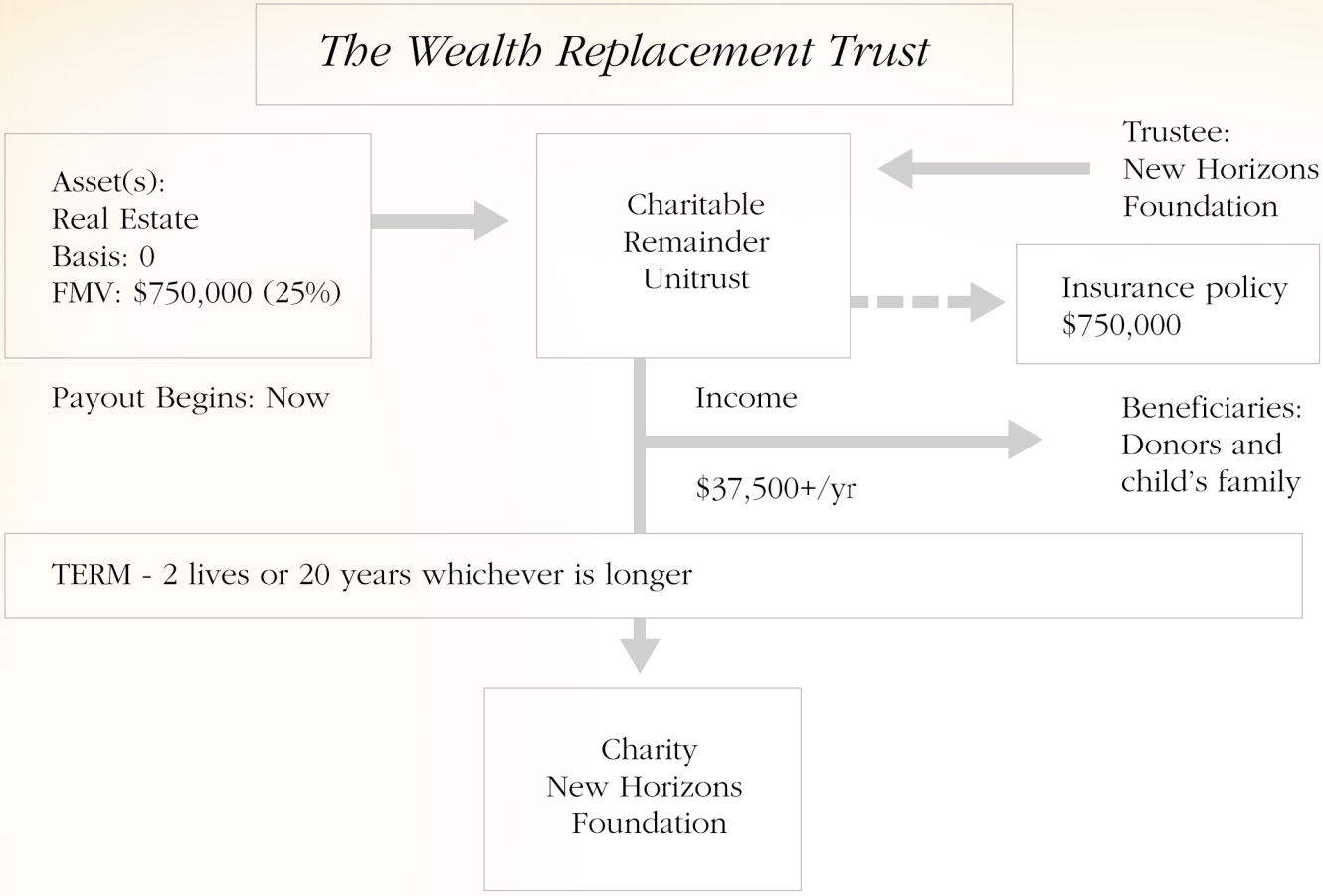
- Avoids current income tax due when plan goes to children
- Avoids Mandatory Minimum Distribution requirements
- Allows for decision making each year as to who will receive the income
- Reduced value in estate for estate tax purposes
- Can make tax advantaged gifts to children and grandchildren
- Liability protection for spouse and children, not marital property so will not go to a future spouse
- Flexible income payments
- Allows for income tax planning for spouse
- Great benefit to children and grandchildren
- A significant gift to charity at the end of the term

WEALTH REPLACEMENT

THE WEALTH REPLACEMENT TRUST

Perhaps the most significant drawback for most people when considering the various forms of the charitable remainder unitrust is the fact that the principal must ultimately go to charity instead of their children. This disadvantage can be reduced or eliminated through the use of a Wealth Replacement Trust. Each transfer of property or cash to a charitable remainder unitrust will produce a current income tax deduction for the grantor. If the tax savings were transferred to an irrevocable insurance trust which has the children as beneficiaries, then the value of the principal could be replaced by the insurance proceeds. Some of the income payments from the CRUT could also go to the insurance trust to help fund the premium. After both spouses deaths the CRUT principal would go to charity and the irrevocable insurance trust would be funded for the children's benefit replacing the asset going to charity in the estate. In this way a grantor is able to make a significant gift to charity without depriving his children. The insurance proceeds go tax-free to the children and are not part of the estate so there are no estate tax or probate costs.

The transfer to the insurance trust can be accomplished without gift tax problems through the use of a "Crummey power" in the trust. The Crummey power states that each beneficiary has the right for a period of time to withdraw his or her portion of any transfer to the trust. This makes the gift a current interest and allows it to be covered by the annual gift tax exclusion. As long as the beneficiaries do not withdraw the amount within the specified time, the trustee will have the funds available to purchase the life insurance. The Wealth Replacement Trust can be combined with any type of charitable remainder unitrust where the grantors wish to replace the value of the asset given away. Care should be taken to make sure that the grantor(s) are insurable before setting up either trust if the replacement trust is a significant factor in setting up the unitrust. The insurance trust could also purchase individual policies on the lives of the children. The accumulated cash value in the policy can grow and provide tax free income to the children in retirement and a death benefit to grandchildren.



EXAMPLE:

A couple has a piece of commercial real estate which they purchased for $50,000 thirty years ago and which is now worth, $1,000,000. The real estate has now been fully depreciated so it has lost its tax advantages and to sell it would mean a $1,000,000 capital gain. The real estate represents about 70% of their estate so they are very reluctant to give it all away. The couple are both 66 and would like to take their social security and go on the mission field with their son and his family who are in Africa. The couple decided to put an undivided 75% interest in the real estate into a charitable trust and keep 25% or $250,000 out of the trust. The couple chose a 5% payout for the trust so that the income will start at $37,500 a year and if the trust can year 10% the income will grow by 5% each year. The couple will also get a charitable income tax deduction for the transfer to the trust. They have decided to fund an insurance policy for their son for $750,000 with their tax deduction and part of the money they kept out of the trust to replace the value of the CRUT in their estate. The insurance policy will not only provide a nice retirement plan for their son, since he will be able to take out income tax-free in retirement but it will also provide for his family if anything happened to him.

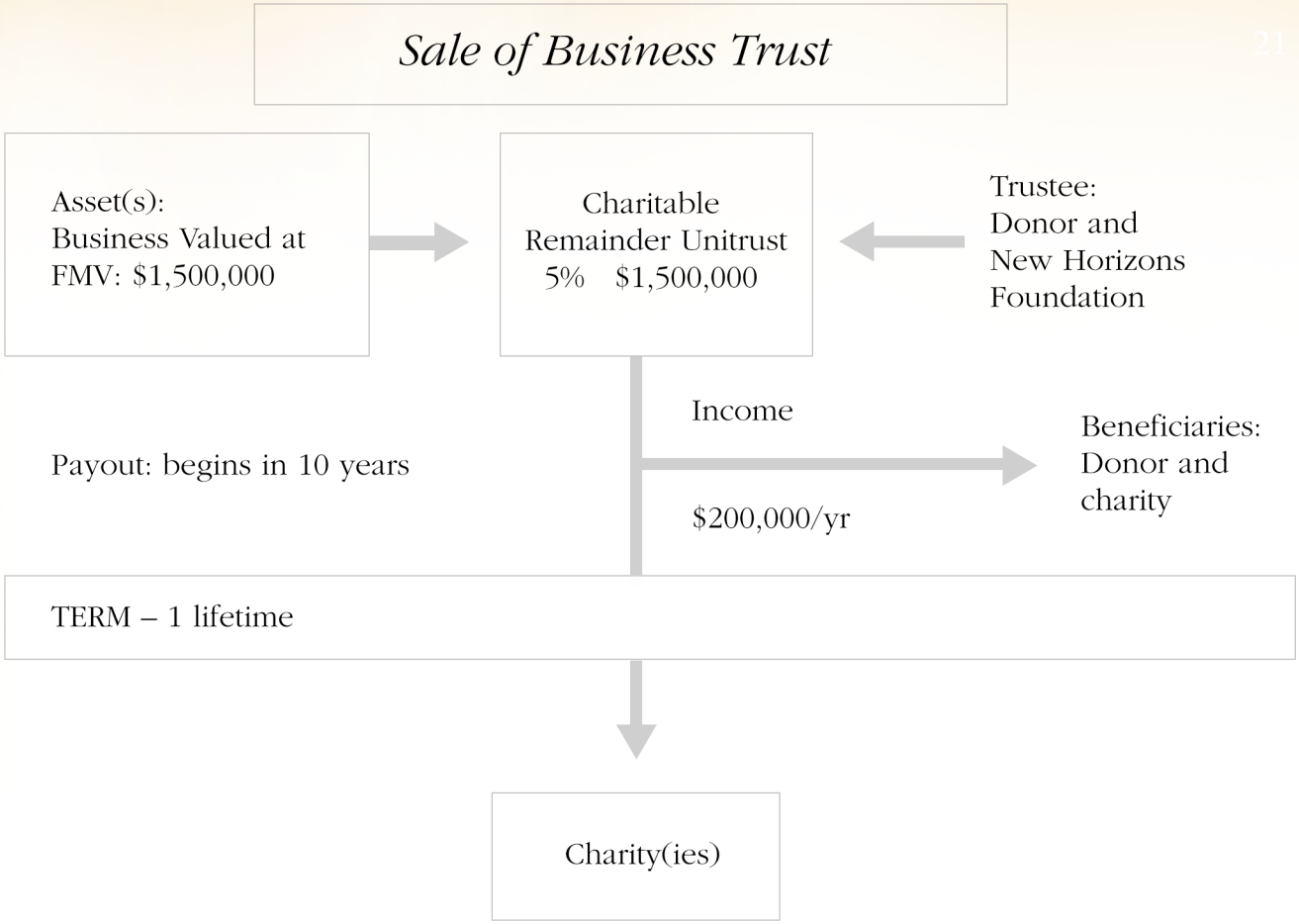
TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids capital gains tax
- Current income tax deduction used to fund insurance policy
- Can convert the income to tax-free income with foreign income credit
- Avoids probate
- Liability protection for assets in trust
- Flexible income payments
- Child's family benefits from insurance policy
- Charitable funds can eventually go to support the son's charitable activity
- They have also chosen a 20 year guaranteed term in case they would die prematurely

SALE OF BUSINESS TRANSFER

THE SALE OF BUSINESS TRUST

Selling a business has never been easy but with the current tax laws it can also be expensive. If the business is a C corporation, there can also be a double tax on the sale at the corporate level and then at the shareholder level. The tax laws and our society encourage free enterprise and many individuals have been able to start with nothing or very little and turn it into a thriving business. The problem then becomes how to sell an asset (the business) that is 99% appreciation. Another issue that affects the price of a business is the value that is placed on the assets of the business verses the goodwill. They buyer will want to attribute the highest possible figure to the business assets because he will have more tax deduction for depreciation. The business owner however may want a lower price attributed to business assets because of the depreciation recapture. If the thought of all that hard equity in your business going for taxes has you staying up late at night, you should consider the Sale of Business Trust. By transferring the stock or assets of your business to the trust and then having the trust sell your business you can avoid the capital gain on the sale of your business if it is a stock sale or reduce the tax on the sale of the business if it is an asset sale. If the employees might be the potential buyers of the business then the owner should consider a Charitable Employee Stock Ownership Plan or CHESOP.



EXAMPLE:

An individual started a business ten years ago from scratch out of her garage and built it up so that now it has a fair market value of $1,500,000. She has received a very lucrative job offer from another company and knows that she could easily sell her business, but the thought of paying one third or the sales price in taxes has left her in indecision. She does not need current income with the new job but would like to put the business profits into a "retirement" program so that she can retire early and she would have the income she needs to maintain her lifestyle.

TAX CONSEQUENCES AND OTHER BENEFITS:

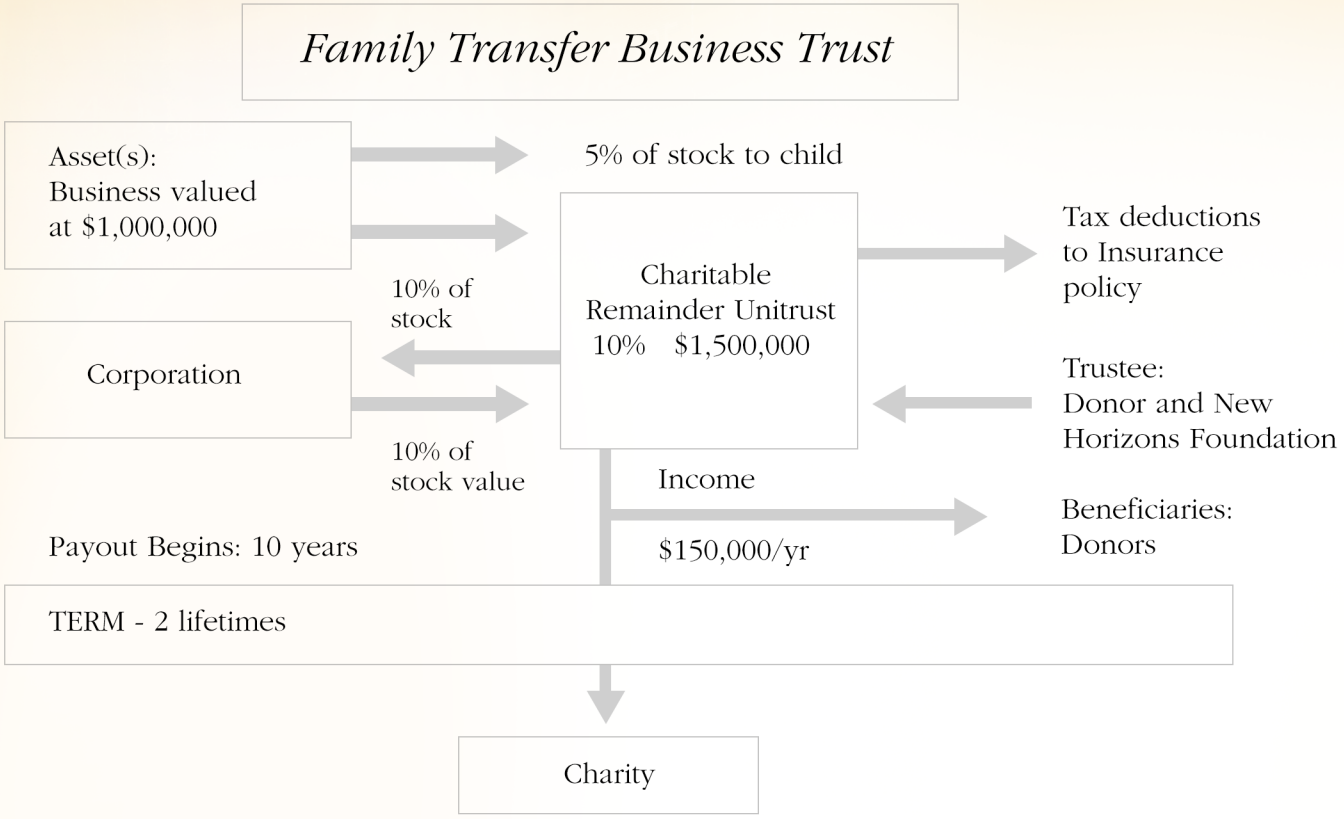
- Avoids capital gain on business sale
- Income tax deduction for funding $150,000+
- Possible future income tax deductions with releases of principal to charity
- Avoids probate
- Provides liability protection for funds which cannot be reached by creditors and is not marital property
- Flexible income payments each year based on her needs
- Provides a hedge against future inflation
- Asset management and trust administration if she is not able to do it
- Provides a significant gift to her favorite charity at her death

Family Transfer Business

THE FAMILY TRANSFER OF BUSINESS TRUST

The Family Transfer of Business Trust differs from the Sale of Business Trust in that it addresses the problem of how to transfer a business to other family members in the most economical way. If you are a small or large business owner and you are nearing retirement, one of your biggest concerns is how to sell or transfer your business so that you can get the income or value you need for retirement in a way that will not cripple the business or make it unprofitable for your children to operate. For many people the question is how to keep the business in the family while maximizing the benefits to the parents and not short-changing children who are not involved in the business. If the business is simply given to the children, then how do the parents get value out of it to provide for their retirement? If the business is sold to the children the parents will have to realize capital gain on the sale and where do the children get the money to pay for the business? The ability of the children to pay for the business may depend on how well they can operate the business and when you sell the business you will no longer have management control and the sale proceeds may not be so secure.

The Family Transfer of Business Trust may be your answer. A small amount of stock can be given or sold to the children who are involved in the business. Each year the parents can contribute stock to a charitable remainder unitrust and then have the corporation redeem the stock from profits or retained earnings and retire the stock. Not only is a retirement trust being funded, but each year the parents will get a current tax deduction based on the fair market value of the stock contributed.
As time goes by the children are owning more and more of the company as the value of their stock rises with the retirement of the remainder of the parent's stock. Eventually, the children will own the company without any sale debt, and the parents will have a charitable remainder trust paying them an income for the rest of their lives. The yearly tax savings could be used to purchase a cash value life insurance policy on the parents for the children not involved in the business. All this plus a significant gift to the family's favorite charity.



EXAMPLE:

The family business has been appraised for $1,000,000. The owners are approaching retirement and would like to work in the business 10 more years. One child works in the business and one child does not. They could gift 5% of the value of the stock to one child and make a $50,000 cash gift to the other child. Then each year they can give 10% of the stock in the corporation to a Family Transfer of Business Trust and the trust can sell the stock to the corporation. Cash goes to the charitable trust and the stock is retired by the corporation. Each year, the owners will also receive a charitable tax deduction for the gift of the stock. They can use this deduction to pay for a $500,000 life insurance policy on their lives that will be payable to the child not in the business. After 10 years the child involved with the business will own the business and the parents will have over $1,000,000 in the charitable trust, because they have not taken any income during the 10 years since they were still being paid by the corporation. The funding of the CRUT will have come from the corporation and will not be a debt on the child in the business.

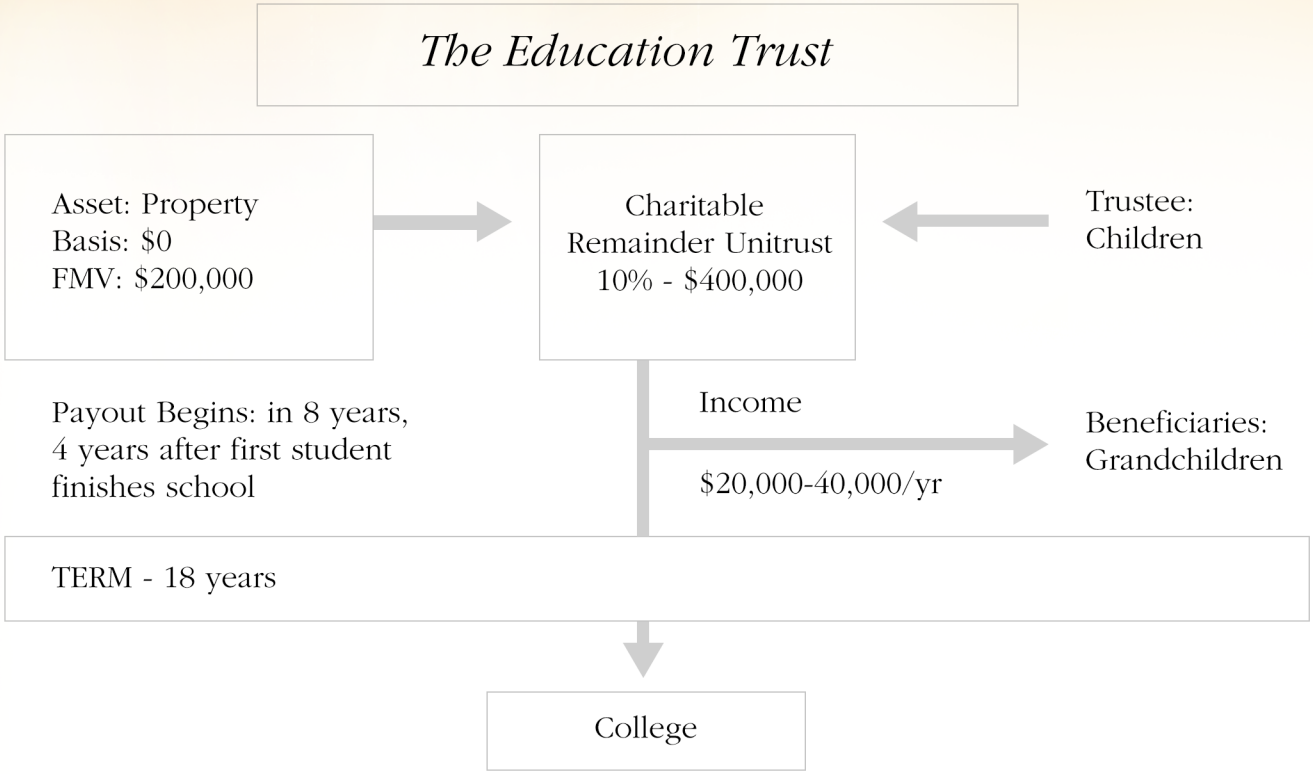
TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids capital gain on business sale
- Income tax deductions for funding used for insurance policy
- Business is transferred to child without debt and in most economical way
- Child learns the business from father and father can make sure that business value stays strong
- Both children are provided for with assets that are best for them
- Possible future income tax deductions with releases of principal to charity
- Avoids probate and any estate tax
- Provides liability protection for funds which cannot be reached by creditors
- Flexible income payments each year based on the family needs
- Provides a hedge against future inflation
- Asset management and trust administration if they are not able to do it
- Provides a significant gift to their favorite charity after their deaths

EDUCATION

THE EDUCATION TRUST

The costs of a college education have risen faster than inflation over the past ten years, yet the need for a college education to achieve the career that many want for their children has never been greater. Money placed in a savings account for college costs is taxed each year unless a 529 plan is used, but then the funds are not available in case of an emergency. If a family plans to pay for college costs with money that is earned each year, they will do so with after-taxed dollars and there is only a limited tax deduction for college expenses. The Education Trust may be the solution to the problem, particularly if there is a grandparent that would like to help. The Education Trust is a charitable remainder unitrust that is set up for a term of years with the express purpose of funding children's education expenses. Because the unitrust only lasts for a short length of time, the donor receives a larger current income tax deduction and the income received by the child will be taxed to them in their tax bracket. At the termination of the trust, the principal can go to the college as a scholarship fund in the family's name or be used to support a favorite charity. Appreciated property such as stock or real estate can be contributed with the advantage that the family will not have to pay for college expenses out of current income each year. It may be possible to talk to the school about freezing the tuition rate if the school is the charitable beneficiary.



EXAMPLE:

A couple has 4 grandchildren ages 8, 10, 11 and 14. The couple would like to be able to help their children with the grandchildren's college educations. They have an office building that has been depreciated and is now worth $200,000 with a basis of almost zero. If the couple contributes the property to an Education Trust and then sells it, they will have the full value of the property in the trust. Since it will be 4 years before the oldest child goes to college, the trust can accumulate in value during that time. They have estimated that each child will need $20,000 a year for college expenses for four years. That will mean $320,000 for college expenses that their children would have to pay with after tax dollars. If the grandchildren are able to take out deferred loans for their education until the graduate then the trust could accumulate for 8 years before making payments. If the trust could earn 9% then the funds in the trust could double in value to $400,000 by the time the funds were first needed. The Education Trust would need to last for 18 years until the youngest child gets through school and four years of loan repayment. The Trust could begin paying $20,000 in years 8-10, $40,000 in year 11, $20,000 in year 12, $40,000 in years 13-16 and then $20,000 in years 17-18 for a total of $320,000. If the Trust were able to earn 8% there would still be a significant gift going to charity at the end of the trust term.

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids Capital Gain of $200,000 at sale
- Current income tax deduction of $20,000
- Avoids probate
- Avoids estate tax
- Liability Protection – not subject to creditors also not reportable on a FAFSA form
- A hedge against inflation, income could grow during trust
- Asset Management – the parents could manage the trust
- Powerful investment using a $200,000 asset to pay for $320,000 of college expenses
- Flexible Income Payments – Income can pay out to each grandchild as it is needed
- Benefiting other family members – children know their children's college education is covered
- Favorable tax treatment
- A Significant Gift to Charity

PRIVATE FOUNDATION TRUST

THE PRIVATE FOUNDATION TRUST

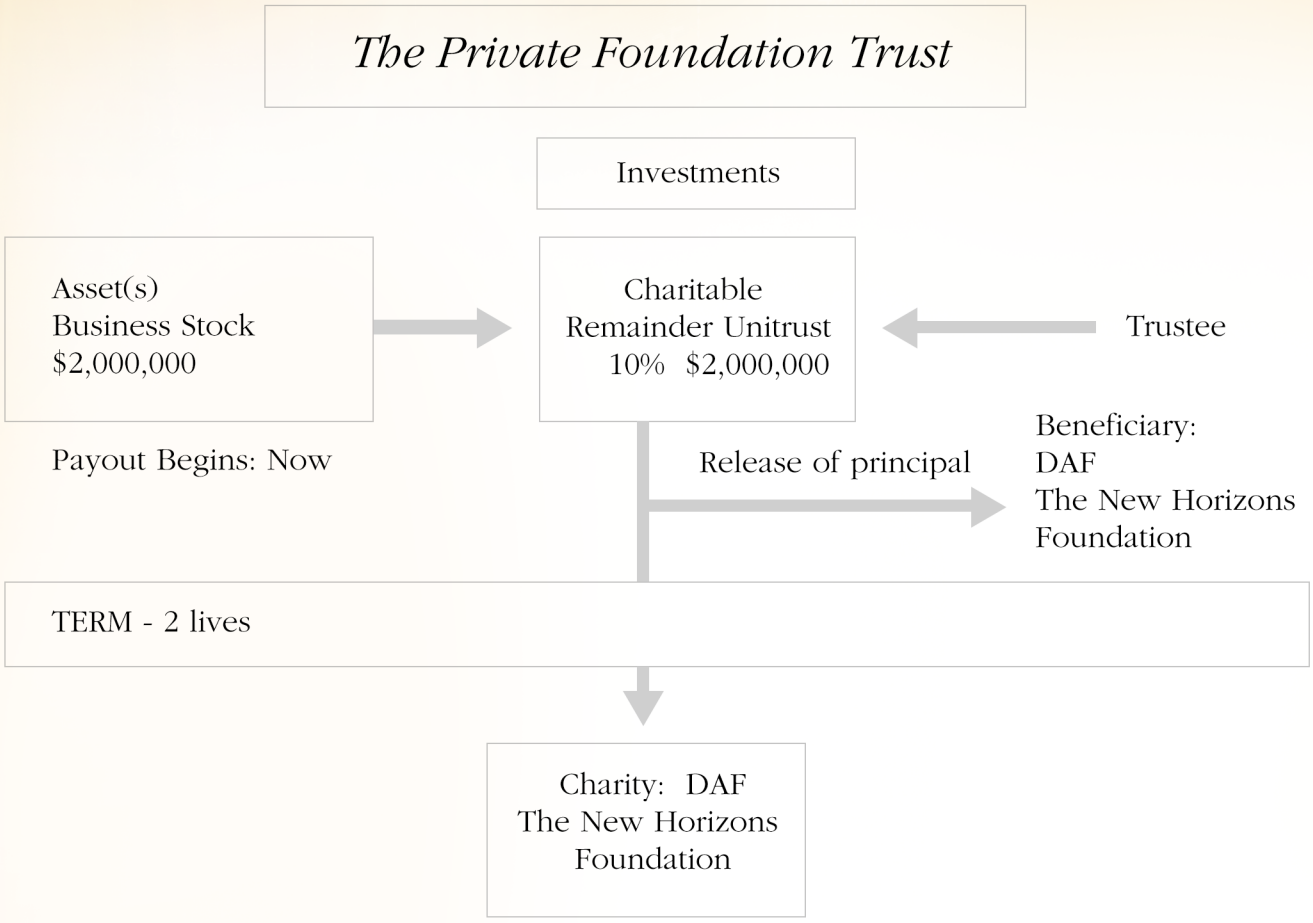
Private philanthropy plays a special and vital role in our society. Beyond providing for areas into which government cannot or should not advance, private philanthropic organization can be uniquely qualified to initiate thoughts and actions, experiment with new and untried ventures, dissent from prevailing attitudes and act quickly and flexibly. Private foundations have an important part in this work. They enable individuals and families to establish new charitable endeavors and to express their own bents, concerns and experiences. Because their funds are frequently free of commitment to specific operating programs, they can shift the focus of their interest and their financial support from one charitable area to another. They can hence, constitute a powerful instrument for accountability, growth and improvement in the shape and direction of charity.

The Private Foundation Trust may be structured to provide the benefits of a private foundation without the high administrative costs and extensive IRS restrictions and regulations. In addition, unlike a private foundation, the Private Foundation Trust the grantor may elect even on an annual basis to give funds away to charity or receive income from the trust.

The Private Foundation Trust works in the following manner. A grantor establishes a unitrust with a sum of money, appreciated property or even an income producing asset such as oil and gas royalties. The grantor is designated as the income beneficiary but a single member LLC owned by the charitable trust is used to invest the assets. Because the Private Foundation Trust is a net income with make-up trust, income is only paid out to the income beneficiary when the income is released from the LLC to the CRUT. The grantor may direct the Trustee to release a portion of principal early directly from the Trust to the charitable beneficiary. The donor can request just the income earned in that year or income and principal whatever is needed to accomplish the desired charitable gift. The donor will receive a charitable income tax deduction in the year of the release for the value of the income interest. The trust can be written so that this deduction will equal 80-90% of the value of what is released. The release can go into a Donor Advised Fund at a community foundation and then be given away to any charity or any charitable purpose the donors have in mind. Even if the donors never intend to get any income from the trust, it may be a valuable tool to create ongoing charitable tax deductions, especially if the gift to charity that a donor would like to make would generate more charitable tax deduction than could be used by the donor before it expires or if the donor would like to use the charitable deduction against ordinary income in the future and not capital gain in the present.

EXAMPLE:

An individual is selling a business for ten million dollars and he would like to give two million dollars of that to establish a private foundation. The charitable trust can be set up and approved in one day, the private foundation often takes several months before approval is issued by the IRS. The gift to the charitable trust should occur before the business is sold so that the grantor will not only get the charitable deduction for the fair market value of what is given, but he will avoid capital gain on the $2,000,000 value of stock that has been given to the trust. Since the stock has appreciated in value, the charitable deduction can only be used against 30% of the grantor's adjusted gross



income for the first year and then carried forward for 5 additional years. The grantor would use the charitable tax deduction mostly against the capital gain on the portion of the stock that he sold individually. While this is an advantage, it would be better to spread the tax deduction over several years and be able to use it against ordinary income each year which is taxed at a higher tax rate. The grantor has chosen The New Horizons Foundation to be the charitable beneficiary of the Trust because every year he plans to release to his Donor Advised Fund what has been earned and then give it away during the year based on the needs of his favorite charities. If there is a need greater than the income that he would like to benefit, he can also release principal and give it away.

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids capital gains tax on stock given to the trust
- Receives a current income tax deduction of a portion of the value of the stock
- Receives ongoing tax deductions from the release of principal that can go against ordinary income in the future
- Extends the value of their charitable gift, because they can give away 2-3 times as much to charity over the donor's lifetimes as opposed to giving it all at once
- Donors can be more strategic with their gifts because gifts to the DAF allow them to get their tax deduction when they want it and give the funds away when they are needed
- Provides liability protection for the assets and allows the opportunity to receive income from the trust in later years if there is ever a need
- Flexible income payments based on the annual desires of the donors
- Not one significant gift to charity but many years of significant gifts, because the funds in the trust will be invested and can then be given away over time the grantors can give away 2-3 times the value of a single gift

ASSET MANAGEMENT

THE ASSET MANAGEMENT TRUST

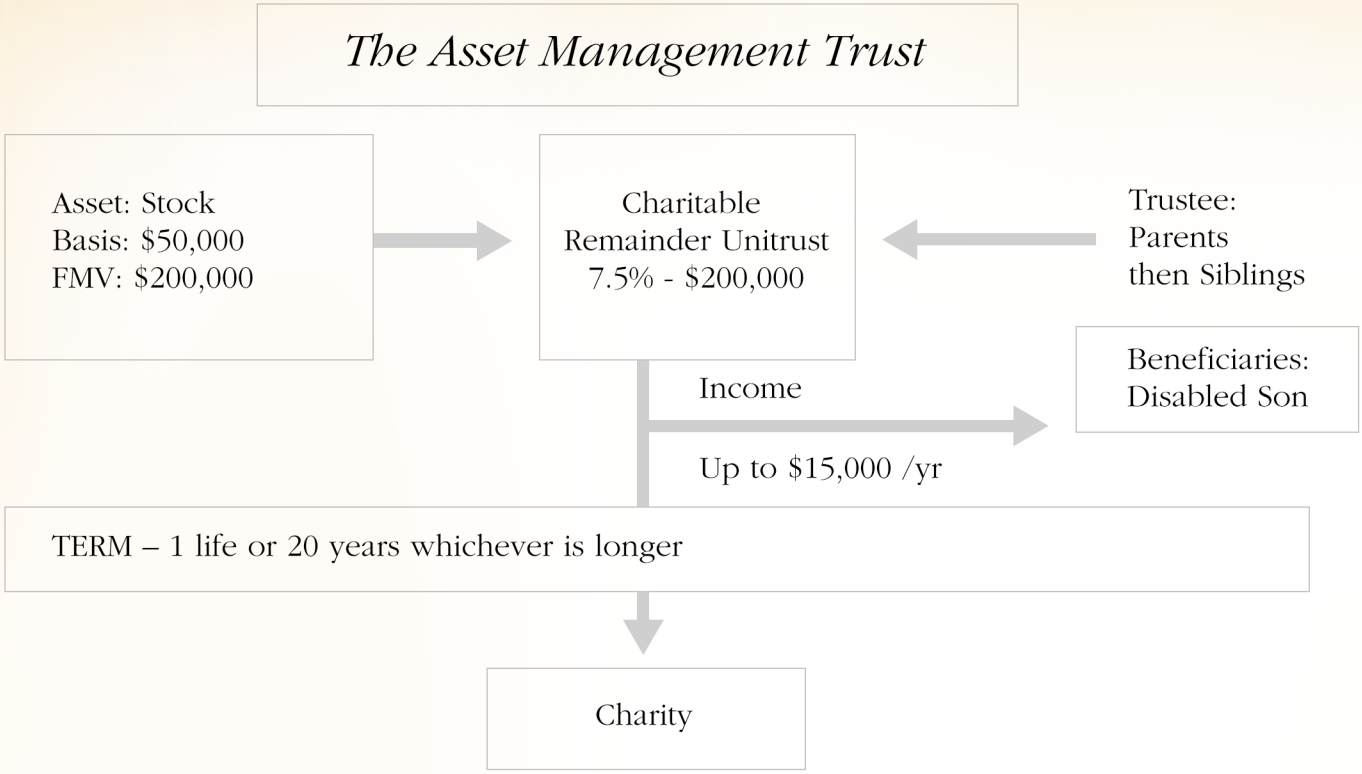
There are a variety of reasons that make asset management an important benefit of the charitable remainder unitrust, but perhaps the four most important are mentioned below. The basic reasons individuals choose an asset management trust are:

1. To insure an individual or group of individuals will be provided for as long as they need it.
2. To insure the principal will not be lost or squandered by the income beneficiaries.
3. To preserve the value of the trust so it cannot be reached by creditors
4. To insure that state or federal benefits that accrue to a person because of disability or incompetency are not voided because the value of the trust in their estate.

The three situations where an Asset Management Trust makes the most sense are:

1. Where a person without much experience managing money, such as a widow, and the person setting up the trust believes that others may take advantage of them.
2. Where a person has been known as a spendthrift and the grantor setting up the trust wants to make sure that the money is not squandered away.
3. Where an individual is disabled and/or legally incompetent and is qualified to receive funds or services from state or federal programs.

This last situation requires specialized language which does not disqualify a person from their state or federal benefits. Funds from the trust cannot be used to support the person but only to provide non-support items. This type of trust is commonly known as a Special Needs Trust. The Asset Management Trust can be an excellent vehicle to provide for the needs of a disabled family member or friend who qualifies for state or federal benefits or programs. The trust can make payments to or for the benefit of the disabled person, in the discretion of the Trustee, without jeopardizing funding from the government programs. This income can be used to provide for what courts have described as "the dignities of life" non-support items such as magazines, books, computers, haircare, trips home etc., which would not be available to a person who must survive solely on the government programs. The Trust principal at the disabled person's death, goes on to charity.



EXAMPLE:

A couple has a disabled child who qualifies for social security disability. If the child receives an inheritance, he will lose the benefits until the inheritance is gone. His parents considered giving all of their money to the other two children with the charge that they would take care of their brother, but that is a big responsibility and their son will need care the rest of his life. They decide to set up a special needs Asset Management Trust for their son now and see how it works for him. They put some appreciated stock with a low basis and a fair market value of $200,000 into the trust. The trust is set up to last for their son's lifetime or twenty years whichever is less. With the social security disability their son does not need a lot of money, but just access to funds for the necessities of life. The Trust is set up to pay out up to $15,000 a year for his benefit. If he doesn't need that much in any year it will accumulate for his future benefit. With this Trust there will always be funds available to assist him. If he dies before the 20 year term is up, the income can go to his brother and sister. After the Trust terminates it will go the Downs Syndrome Association to help other children with similar needs.

TAX CONSEQUENCES AND OTHER BENEFITS:

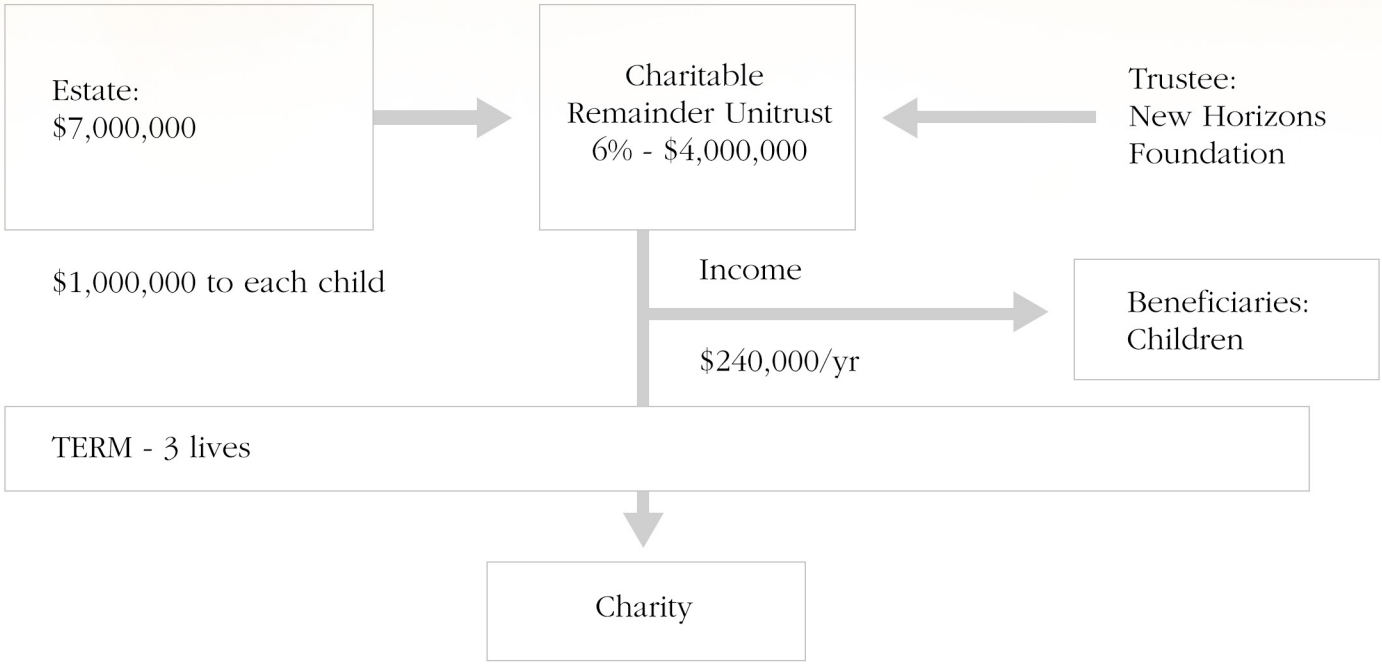
- Avoids Capital Gain of $150,000 at sale
- Current income tax deduction of at least $20,000
- Avoids probate
- Sets up a managed way to provide for their son with a disability for the remainder of his life
- Liability Protection – not subject to creditors also can be Medicaid and SSD exempt
- A hedge against inflation, income could grow by 2% per year
- Asset Management – the parents and then siblings will manage the trust for his benefit
- Flexible Income Payments – they can choose how much to use each year and accumulate the rest for later needs
- Benefiting other family members – provides a way for siblings to cover their brother's expenses in a way that does not produce a financial hardship on them
- Favorable tax treatment – income taxed to disabled child so no tax
- A gift to a Charity that will help other families with similar situations

Estate Tax Avoidance

THE ESTATE TAX AVOIDANCE TRUST

The Estate Tax Avoidance Trust is a charitable remainder unitrust that is a part of a will or revocable living trust and which is inactive until death. With the increased value of the estate tax exemption this Trust is not as necessary as it was earlier but still can provide some advantages. At death the trust is usually funded with the least amount that will eliminate the greatest amount or all of the estate tax due at that death. This Trust is especially valuable for those people who do not want to give anything away prematurely, allowing them to make decisions about their estate right up until the second spouse's death. This Trust also allows a person to make sure that not too much is given to charity at the expense of the family members, while still insuring that all estate tax is avoided in favor of charity if the estate is large enough to have an estate tax due. The Estate Tax Avoidance Trust can be especially valuable if there is a large retirement plan in the estate because it will also avoid the income tax at funding. People often plan to give children an outright gift from the estate at their death and then a stream of income for 20 years or even their lifetimes coming from the Estate Tax Avoidance Trust to ensure that the distribution of the funds will be over a period of years and provide a certain amount of security as well as a retirement income for children.

The Estate Tax Avoidance Trust



EXAMPLE:

A widow has three children that she would like to benefit. She has an estate of $7,000,000 so if she were to die now there would be some estate tax due on her estate. She also would like for the assets from her estate to be utilized in the best way possible for her children. All three have their own businesses but have not been able to put away any money for retirement. By making an outright gift of $1,000,000 to each of her children at her death and having the balance of the estate go into an Estate Tax Avoidance Trust, she will avoid any estate tax while preserving an income stream for her children that will last through their retirement for the remainder of their lives. If her IRA goes to the Estate Tax Avoidance Trust then she will also avoid a current income tax on those funds. If her estate grows even larger, she has designated that if there would be a taxable estate even with the Estate Tax Avoidance Trust then that additional amount would go directly to charity, thus avoiding any estate tax no matter how large her estate grows to be.

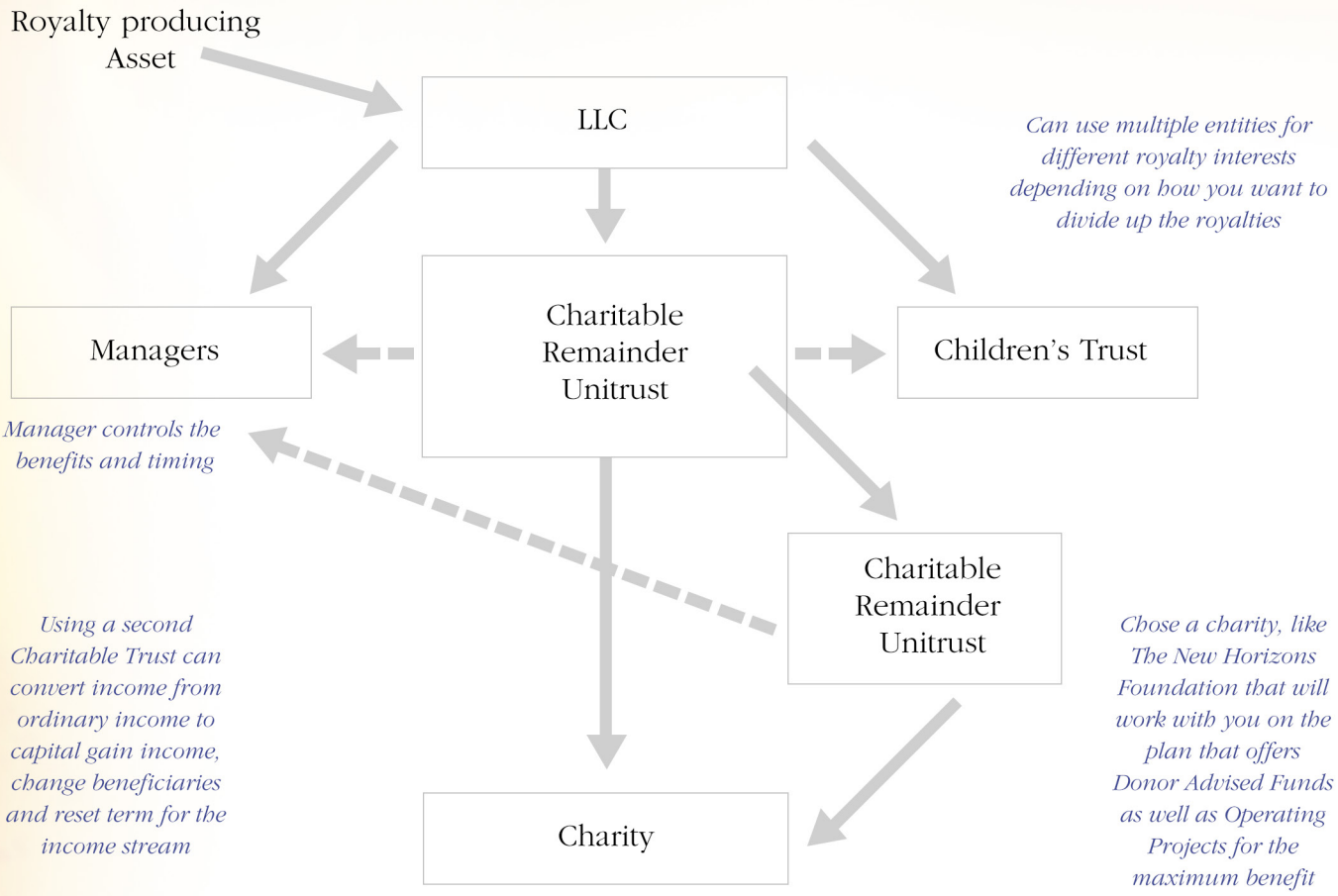
TAX CONSEQUENCES AND OTHER BENEFITS:

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids estate tax
- Avoids probate
- Provides a steady stream of income to each child for retirement or other needs
- Liability Protection – not subject to creditors also it is not marital property
- A hedge against inflation, income could grow each year
- Asset Management – the charitable foundation she has chosen will manage the trust
- Flexible Income Payments – they can choose to take reduced income now and increased income later
- Benefiting other family members – The Trust has been set up for the children's benefit, giving them a "retirement plan" that can provide for them in later years
- Favorable tax treatment
- A Significant Gift to Charity after it has served its purpose

Income Tax Avoidance Trust

The Income Tax Avoidance Trust



THE INCOME TAX AVOIDANCE TRUST

Royalty income from mineral, oil and gas rights, water rights, literary rights and other intellectual property rights are generally classified as ordinary income and taxed at the highest tax rate for most taxpayers, which in many states is approaching 50% and in states like California or Oregon can be as high as 53%! For most taxpayers, an asset that produces royalty income can be an expensive asset to own because of the ordinary income challenges, but it is the asset of preference for a charitable remainder trust. This produces a problem similar to the one in the Bible that Joseph faced in Egypt based on Pharaoh's dream, "how can a person store up in a tax exempt barn during the times of plenty, resources that can be available to him and his family during the times that might not be so plentiful?" If properly structured, there are some significant benefits for charitably minded families and the ordinary income they receive may even be able to be restructured into capital gain income in special situations. Philanthropic families utilizing an Income Tax Avoidance Trust take advantage of a tax-exempt environment to grow assets, secure a long-term stream of income for retirement and get a more tax efficient way to make charitable gifts.

3 KEYS TO SUCCESS WITH ROYALTY INCOME:

1. Use a Charitable Trust friendly LLC as your entity to hold the income producing asset
2. Utilize the Income Tax Avoidance Trust to provide benefits and tax savings
3. Choose The New Horizons Foundation as your charitable partner for maximum flexibility

CHARITABLE TRUST

THE CHARITABLE TRUST FRIENDLY LLC:

A charitable trust friendly LLC is used as the owner of income producing assets to give the greatest amount of flexibility for control and benefit. The LLC operating agreement can be written so that it allows the tax benefits to go to members that are not the charitable trust and keeps unrelated business income away from the charitable trust which can cause it to lose its charitable tax exemption. The Grantor can choose what percentage he or she would like to have owned by the charitable trust or many Grantors start owning a larger percentage in the beginning and then make gifts of membership interest at a later date to the charitable trust to allow the asset base to grow for retirement or future use or to a Children's Trust set up for the Grantor's children and grandchildren as a part of their estate plan. This allows the Grantor to receive a reduced proportion of the initial income for personal use and then defer a greater percentage of future income in the tax-free environment of the charitable trust. The individual can always make gifts of membership interest to the charitable trust, but the charitable trust cannot make gifts of membership interest to the individual. If the charitable trust owns 50% of the membership interest, then 50% of the income received by the LLC will be exempt from tax because the charitable trust is a tax exempt entity and the tax nature of the income flows through to the members. This allows the Grantor to invest 50% of what is received by the LLC in a tax- free environment for future benefit. The manager or managing member of the LLC determines when assets are distributed to members from the LLC, so the Grantor as manager, can maintain control over how much and when income is received by members.

With this structure you will want to use an experienced Trustee that know what can and cannot be done with the trust and its assets so that you are not making new law with a creative use for the Trust. The Ultimate Charitable Trust can pay income to the Grantors, their children or their grandchildren. This is known as "spraying" and allows the income to be taxed to whoever receives it. This makes it a great technique for paying for children's or grandchildren's college expenses. In order for this ability to be available, the Trustee of the trust must be someone other than the Grantor or his immediate family. If the family is working with The New Horizons Foundation, the foundation is an experienced Trustee that is very responsive the Grantor's desires. The Grantor can

FRIENDLY LLC

also release money from the Trust to charity early producing a current tax deduction for the Grantor. The managing member of the LLC determines when and how much income will be available to the Trustee to distribute, maintaining the control with the Grantor as manager of the LLC. The Trust can last for lifetimes, for a term of years or for a lifetime and/or a term of years. The goal is to create a trust with only a 10% current charitable value and a 90% income value which is the lowest charitable value the IRS will allow. If needs change or if the Grantor would like to convert the ordinary income that is paid out to beneficiaries to capital gain income, this Trust can be rolled into a new Trust with a new term, additional beneficiaries and which will produce capital gain income instead of ordinary income. There is a specific tier system in the IRS code that requires any ordinary income to be paid out before capital gain income so this can be very beneficial. Assets held in the trust are outside of the Grantor's estate, are not subject to creditors and are not considered marital property if income is going to children providing a level of asset protection for the family.

EXAMPLE:

A farmer and his wife have oil and gas royalties from their land of approximately $500,000 a year. They are only spending $100,000 of that to meet their current needs because of their other farm income. By placing the oil and gas royalties into a limited liability company, they have decided to give a 75% interest in the LLC to an Income Tax Avoidance Trust. With the Trust, 75% of the income received each year by the LLC will not be taxed and can be invested in the tax exempt trust for future use. The couple will receive 25% of the income or $125,000 a year which will meet their family needs. The couple plans to wait for at least 6 years before taking any income from the charitable trust. This will allow the principal to grow to approximately $3,000,000. They can also use the income from the Income Tax Avoidance Trust to make gifts to their children.

Tax Deduction Maximizer Trust

THE TAX DEDUCTION MAXIMIZER TRUST

The use of a Charitable Remainder Unitrust (CRUT) with the sale of a piece of property or a business is fairly well known. The CRUT allows the grantor to avoid the capital gains tax when the property is contributed to the trust and then sold, it produces a current income tax deduction for a portion of the value of the property or business interest depending on the payout schedule of the trust and the trust provides a stream of income to the grantors or other named beneficiaries for their lifetime or for a term of years depending on which they prefer. The CRUT is a separate legal entity that is tax-exempt and operates for the benefit of the income recipients during the term of the trust and then distributes the assets to charity after the trust terminates. Though the primary focuses of the CRUT are usually the charitable gift, capital gains tax avoidance and the stream of income to the beneficiaries, the CRUT can also provide some significant advantages for people who would like to make current gifts to charity, as opposed to waiting until the end of the trust term when the CRUT normally distributes its assets to charity.

Even if the grantor is planning to contribute all of the value of the property or business to charity and does not need or want the income stream, the CRUT can provide some special advantages listed below which can make the trust a valuable tool to save taxes in the future as well as help accomplish charitable goals and objectives. If the charitable remainderman for the CRUT is a Donor Advised Account in a community foundation, there are even more advantages. The CRUT should be a Net Income Trust, so that no income needs to be paid out to the Donors, if the steps in number 5 below are followed.

THE TAX DEDUCTION

1. DONOR CONTROL BEFORE THE SALE. The Donors can be the Trustees of the Trust and maintain control over the Trust and the property until the sale of the property or business. In order to avoid the capital gain on the sale of the property or business, the property or business interest must be contributed to charity before any sales documents are signed. If the anticipated sale does not go through or the property or business is not sold the grantors need to understand that the CRUT now owns all or part of the business or property. The CRUT does however, allow the grantors to keep control as Trustees of the Trust even though the gift has been made to the Trust.

2. REDUCES THE DUE DILIGENCE TIME AND EXPENSE FOR CHARITY. Normally if a piece of real estate or a business interest is contributed to a charity, the charity must do an environmental study on the property and a due diligence review to determine if there are any potential liabilities to the charity from the property or business interest. Though usually an environmental study is not needed for the gift of a business interest, the charity does need to make a thorough due diligence review of the business for liability issues as well before the business interest can be accepted. This process can be expensive and time consuming. If there is a potential buyer who is waiting to make an offer or if the Donors want to make the gift before the end of the year for tax purposes, it can be a problem. Establishing the CRUT to receive the property or business interest can reduce or eliminate these concerns. The Trust then as owner of the property or business interest can sell the asset. Because the charity is the remainder beneficiary, it does not need to make a decision on acceptance of the assets until the termination of the trust and then all that will be left in the Trust should be cash. Particularly if the grantor acts as Trustee of the Trust, the charity does not even need to be involved in the process until later. When the charity only receives cash from the trust there are no due diligence issues.

3. BETTER UTILIZATION OF THE CHARITABLE TAX DEDUCTION. When a piece of property or a business interest is contributed to charity, the Donors receive a current tax deduction for the full fair market value of the property gifted. If the property or business interest is appreciated property, then the tax deduction can be used against 30% of the Donors' adjusted gross income in any year. The tax deduction can be carried forward for five additional tax years. If the value of the gift is significant, this can sometimes produce a tax deduction that cannot be utilized in the time period allotted. Also the tax deduction occurs in the year of the gift, so if the property or business is not sold in that tax year, the donation year will not match the sales year. This is especially important if only a portion of the business or property is being contributed to charity. If the property or business is hard to value, the Qualified Appraisal which must be done for each gift of appreciated property, may not match the potential sales price if the sale does not occur in that year. This can

be tricky because the Appraiser will have to potentially justify his appraisal to the IRS and there are penalties for over stated appraisals. When a CRUT is used, the Donors will receive a tax deduction in the year of the gift for only a portion of the value of the property. Typically, with this type of arrangement, the tax deduction is about 10% of the value of the property. If the property or business sells in that tax year, the Donors can make an additional contribution of the sales proceeds from the trust to charity in that year and get the other 90% of the deduction that they did not receive from initial funding of the trust. If they cannot utilize all of the tax deduction, even with the five year carry forward provision, they can keep the CRUT and make annual contributions out of the trust to their community foundation account and receive a current tax deduction in the year of the contribution. Using this technique, the tax deductions can be pushed forward and utilized over a long period of time based on when the grantors need them the most. It may be more valuable to defer the tax deductions into later years so that they can be used only against ordinary income as opposed to capital gain.

4. DISTRIBUTION TO CHARITY OVER TIME. Many times Donors will want to make distributions to charity over a period of time or make the distributions to a variety of charities. The Donor Advised Fund in a community foundation enables Donors to achieve these two objectives. If the Donors would like to maintain control over the investment of the assets over this time, the CRUT can allow them to do this as well. The Donors can continue as Trustees of the CRUT and invest the assets of the Trust. Each year the Donors can determine how much they want to give away and then make a gift to their community foundation account by releasing principal from the Trust. They can then make the charitable distributions all at one time or over the course of the year from their Donor Advised Fund.

5. INSURING THAT NO INCOME IS RECEIVED BY DONORS. If a CRUT earns income, then the income or the payout percentage of the trust, whichever is less, must be paid out to the Donors in the year earned. This problem can be eliminated if the CRUT uses a single member LLC to hold the assets of the Trust. If the CRUT exchanges all of its assets for 100% of the membership units of an LLC and the CRUT is written appropriately, then only the income that comes out of the LLC to the CRUT would have to be paid to the Donors. This would be controlled by the Trustee of the Trust who would also be the Managing Member of the LLC. Because the LLC is 100% owned by the CRUT, the LLC does not file an annual tax return and everything is reported on the CRUT tax return. Since the CRUT is a tax-exempt entity, no tax should be due for income that is kept in the LLC and not distributed.

Using a CRUT for the sale of a piece of property or a business interest can often save time, taxes and frustration. In many situations it still makes a lot of sense even when it is the Donors' intent to give the whole amount to charity.

GRANDPARENTS

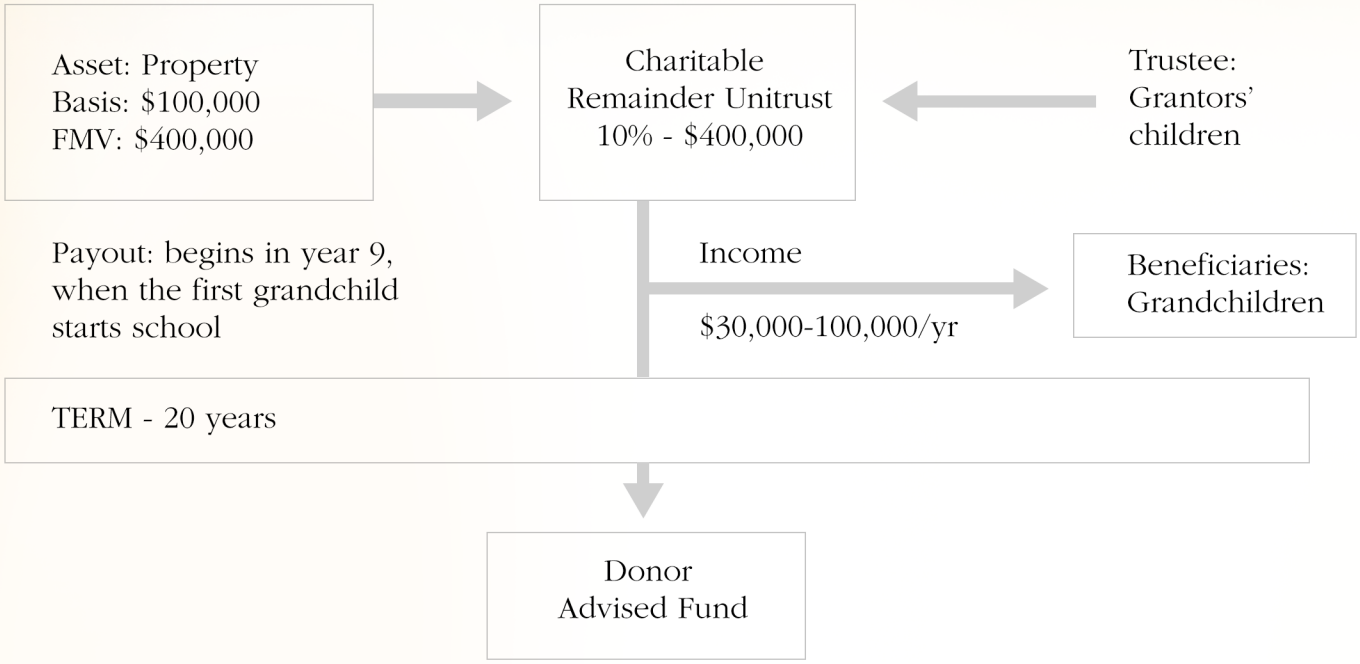
THE SHARE THE WEALTH/GRANDPARENTS' TRUST

A charity friendly LLC and a charitable remainder unitrust (CRUT) are created with the Grantors as the beneficiaries along with any grandchildren that they may have during the term of the trust. The trust is created for a term of years up to twenty that would cover the college years for all the grandchildren. The trust would be written so that the Trustee would have complete discretion as to who received distributions from the trust each year. The Trustee could not be one of the Grantors, but could be a trusted friend, advisor or The New Horizons Foundation. The LLC would hold the assets and allow them to accumulate and grow in a tax-free environment until the grandchildren reached college age. Then depending on the criteria that the grandparents use to determine how much income a grandchild should receive for their education, income can be paid out each year to the grandchildren in college and taxed to them in their tax bracket by releasing that money from the LLC to the CRUT. Because the trust is not part of the estate of the parents or grandchildren, it will not be considered on the financial aid form which could disqualify them from other forms of scholarships or grants. If the grandchildren do not need all the funds or do not use some that is available to them, then the income can be paid out to the grandchildren for other needs like weddings or starting a business or to the Grantors but what is left will ultimately wind up in a Donor Advised Fund at The New Horizons Foundation for the Grantors to give away.

Example:

The Grantors have 4 grandchildren ages 9, 7, 5 and 3. They put a piece of property to be sold or an income producing asset worth $400,000 into the LLC for the benefit of a 20 year CRT that will be worth approximately $800,000 in 9 years when the first grandchild goes off to college. The CRT would be a net income with make-up provisions so that the accumulated income could be used for the college educations. If the trust had earned 8% per year in the first year of payout there would be up to $64,000 of income without touching any principal. It is expected that each child will receive $30,000 a year for 4 years of college for a total of $480,000 for the 4 grandchildren. In order to make sure that there will be enough money to pay out to the grandchildren, the trust could convert to a straight payout of 10% if the trust principal ever fell to $300,000 or less. The payout schedule would be as follows:

The Share the Wealth/Grandparents' Trust



YEARS:

9	$30,000	15	$60,000
10	$30,000	16	$60,000
11	$60,000	17	$30,000
12	$60,000	18	$30,000
13	$60,000	19	$100,000
14	$60,000	20	$100,000

In years 19 and 20 the trust income can either be paid to the Grantors, used to finish up with students who took longer than 4 years or used for weddings or graduation gifts. The balance of the appreciation in the trust could be paid out in these last two years leaving the original $400,000 principal or whatever principal is left in the Trust to go to the Grantors Donor Advised Fund. If an income producing asset was put into the trust, then the Grantors would have the advantage of not being taxed on the income as it is received. If an appreciated asset were used to fund the trust, the Grantors would not have to pay the capital gains tax on the sale of the asset. All taxes would be paid by the students in their low tax brackets. If a student dropped out of school, didn't go to school or graduated early, the Trustee could choose not to pay anything out to that student since all distributions are in the Trustees discretion.

TAX CONSEQUENCES AND OTHER BENEFITS:

- Avoids Capital Gain of $300,000 at sale
- Current income tax deduction of $40,000
- Avoids probate
- Avoids estate tax
- Liability Protection – not subject to creditors also not reportable on a FAFSA form
- A hedge against inflation, income could grow during trust
- Asset Management – the parents could manage the trust
- Powerful investment using a $400,000 asset to pay for $480,000 of college expenses
- Flexible Income Payments – Income can pay out to each grandchild as it is needed
- Benefiting other family members – children know their children's college education is covered
- Favorable tax treatment
- A Significant Gift to Charity

Ultimate Family Charitable Trust

THE ULTIMATE FAMILY CHARITABLE TRUST

The Ultimate Family Charitable Trust (UFCT) provides an excellent way for a family to protect against the six financial hazards of life which are death, disability, emergency, taxes, liability and retirement. By combining all of the most advantageous uses of charitable trusts into one trust, a family can get a dynamic asset management tool which accomplishes a variety of objectives. Below are listed some of the ways the UFCT can help your family with the financial hazards of life.

DEATH

AVOIDS PROBATE - The ultimate family charitable trust is not subject to administration fees or other probate expenses because it completely bypasses the probate process and simplifies your estate.

AVOIDS OR REDUCES ESTATE TAXES - When an individual or husband and wife are the only income beneficiaries of a charitable trust the trust assets are not taxed in either of their estates. When third parties like children or grandchildren are added to the trust, only the income interest they receive after the Grantors= death is part of the estate for tax purposes and this can be adjusted in the will to reduce or avoid estate taxes.

TRUST CAN FUND AN INSURANCE TRUST OR FAMILY LEGACY TRUST – Many times a "Wealth Replacement Trust" is funded with the savings from the tax deduction that the donors receive when funding a charitable trust. However, the income from the UFCT can also be used to fund an irrevocable insurance trust or a Family Legacy Trust which is outside the grantors= estates for estate tax purposes and which can pass a substantial inheritance on to children or grandchildren estate tax free.

PROVIDES FOR MANAGEMENT OF ASSETS - The assets in the UFCT are managed by the Trustee for the benefit of the income beneficiaries. This provides management of assets for the surviving spouse and/or the children.

AN INHERITANCE FOR CHILDREN - Children or grandchildren can either receive a life income interest from the UFCT, an income stream for a period of years or a lump sum payout from an irrevocable insurance trust funded by the trust. Planning can provide exactly what you want for your heirs with reduced or eliminated estate taxes.

SIMPLIFIES THE ESTATE - Because everything is set up in advance and management of assets is already occurring, the death of one or both of the grantors does not directly effect the trust operation or its ability to provide for the family.

A SIGNIFICANT GIFT FOR MINISTRY - You can have the confidence that after the income beneficiaries interest expires your assets will provide a significant gift to your favorite church and/or ministries.

DISABILITY

TRUST CAN BE MEDICAID EXEMPT - Because the Trustee is given discretionary powers for the distribution of income, the trust can be written so that it does not negate SSI payments and can allow an income beneficiary to qualify for medicaid while still receiving some benefit from the trust.

INCOME DURING DISABILITY - The UFCT can provide an income to a trust beneficiary during times of disability or it can purchase disability insurance to supplement that income if the need is greater.

ULTIMATE FAMILY

MANAGEMENT DURING DISABILITY - Because the UFCT functions apart from the Grantors, it continues to operate smoothly even when one or both of the grantors are disabled. This includes any time the grantors are outside of the county which is a legal incapacity.

EMERGENCY

CASH WHEN NEEDED - The UFCT can accumulate cash for emergencies and then pay it out when the grantors need it. The cash accumulates in a tax-free environment and the grantors are taxed only on what is received without a penalty which makes it better than a qualified retirement plan or IRA withdrawal.

CHILDREN'S EDUCATION - The UFCT can be set up to pay an income to children or grandchildren during college years so that the income received is taxed to the children in their tax bracket and not to the grantors in their tax bracket. Income payments can pay only during college and end when college ends.

TAXES

AVOIDS CAPITAL GAINS TAX - Funding the UFCT with appreciated property is the best way to realize the full advantages of the trust. Currently, if your appreciated property is sold, up to one-third of the value of the appreciation is lost as a capital gain which is currently taxed at both the federal and state level. Because the UFCT is tax exempt, there will be no capital gain on a transfer of appreciated property to the trust. There is also a way to defer the capital gain until a later time when capital gains will possibly have a more tax favored position.

TAX FREE GROWTH - Because the UFCT is a tax exempt trust assets grow in the trust tax free until they are withdrawn.

CAN DEFER INCOME - Appreciated assets can be contributed to the trust, sold and income can be paid out in future years. This can make every sale an installment sale for tax purposes even when you have a complete cash transaction.

PROVIDES CURRENT OR DEFERRED TAX DEDUCTIONS - A grantor who itemizes can get an income tax charitable deduction in the year that assets are contributed to the trust. These deductions can be carried forward for 5 additional years. In most instances the deduction will be small because it is based on the present value of the future gift to charity and the trust works best if the value of that future gift is 10% and the income interest equals 90%. However, if assets from the trust are released to charity during the term of the trust, the grantors will receive a current tax deduction in the year of the release without having to take in any income. This can allow grantors to extend or defer charitable tax deductions if they are not able to use them currently.

SHIFT INCOME TO CHILDREN - If the grantors children are named as possible income beneficiaries of the trust, money can be paid to them and taxed to them in their tax bracket provided they are over age 14. This can be a tax benefited way to provide for college, a down payment on a house or money to start a new business.

CAN AVOID IRD TAX FROM RETIREMENT PLANS - When an individual who has a retirement plan dies without a spouse or subsequently the surviving spouse dies, there is a current income tax on the distribution of the retirement funds. This tax is known as Income with Respect to a Decedent or IRD. If the retirement plan pays into a UFCT, no IRD tax will be payable at the time of transfer to the trust.

Charitable Trust

POTENTIAL FAVORABLE TAX TREATMENT - Depending on how the trust assets are invested and what assets are used to fund the trust, you may receive all or part of your income as capital gain. This could be used to offset capital losses and the trust can generate capital gain instead of ordinary income. It may even be possible to receive tax-free income if the assets are invested in tax exempt securities. If the trust has been funded with an ordinary income asset, like royalties, then a second charitable trust can be established to convert the ordinary income to capital gain income.

LIABILITY

PROTECTION FROM CREDITORS - Because the UFCT is an irrevocable trust and is outside of the grantors estates, it is protected from creditors. Provided the trust is not established to avoid a current creditor, the assets should be out of reach providing a family with valuable security. The trust income cannot be anticipated or reserved for creditors and the grantors= expenses can be paid directly by the trust. The trust protects the assets for the benefit of your children and preserves the assets from their creditors as well.

ASSETS IN TRUST NOT MARITAL PROPERTY – If the Trust is written properly, the assets in the trust and the income interest will not be considered marital property and subject to distribution in a divorce action.

RETIREMENT

SECURITY FOR THE LIFETIME OF THE FAMILY - The UFCT provides a secure retirement plan for the grantors and ultimately for their children and/or grandchildren. Assets in the trust are beyond the reach of creditors and are not reduced by taxes during accumulation years.

ADJUSTABLE INCOME STREAM - The income stream from the trust can be adjusted based on the needs of the Grantors. It can produce a higher income in early years or a large one year income for unusual expenses. If the income is not needed it can be distributed to children and taxed to them or conserved for later use. There is no required distribution based on age or any excess accumulations tax.

OTHER BENEFITS

TRANSFERRING A BUSINESS TO FAMILY - The UFCT provides a tax-free way for small business owners to transfer the family business to their children and receive money back from the business.

CAPITALIZE BUSINESS VENTURES - If structured properly the UFCT can provide capital for business ventures in which the Grantors or their children wish to participate.

FAVORABLE STATE LAW - Some states are more favorable for the operation of trusts than others. The UFCT can live in any state you chose and be interpreted under that state's laws.

CURRENT CHARITABLE GIFTS - Through the release of trust principal, the Grantors can make significant gifts to charity and receive a current income tax deduction without having to report income for the money given. The gifts can also be given through a family foundation account with a community foundation so that the gift is given anonymously if desired.

FUNDING SOURCE FOR MINISTRY - The Grantors can establish a charitable project account with a community foundation and then release principal from their UFCT to the foundation to pay for ministry expenses and ministry trips.

Charitable Trust Friendly LLC

THE CHARITABLE TRUST FRIENDLY LLC:

Limited Liability Companies are a very versatile form of business entity and can also have some great advantages in the charitable world. A charitable trust friendly LLC can be used as the owner of income producing assets to give the greatest amount of flexibility for control and benefit. The LLC operating agreement can be written so that it allows certain benefits to go to members that are not charitable trusts and the operating agreement can keep unrelated business income away from the charitable trust which can cause the trust to lose its charitable tax exemption. The Grantor can choose what percentage he or she would like to have owned by the charitable trust or often the Grantors start owning a larger percentage in the beginning and then make gifts of membership interest in the LLC at a later date to the charitable trust to allow the asset base to grow for retirement, future use or to a Children's Trust set up for the Grantor's children and grandchildren as a part of their estate plan.. This allows the Grantor to receive a greater proportion of the initial income for personal use and then defer a greater percentage of future income in the tax-free environment of the charitable trust for use by his or her family. The individual can always make gifts of membership interest to the charitable trust, but the charitable trust cannot make gifts of membership interest to the individual. If the charitable trust owns 50% of the membership interest, then 50% of the income received by the LLC will be exempt from tax because the charitable trust is a tax exempt entity and the tax nature of the income flows through to the members. This allows the Grantor to invest 50% of what is received by the LLC in a tax-free environment for future benefit. The manager or managing member of the LLC determines when assets are distributed to members from the LLC, so the Grantor as manager, can maintain control over how much and when income is received by members. The Trustee can also charge a management fee for providing services to the LLC if that is desired.

Tax Flexibility:

The IRS does not consider an LLC to be a distinct separate entity for tax purposes. This means that, at least initially, the IRS will not tax the LLC directly. Instead, members of the LLC can determine how they want to be taxed. There are several options:

- Single member LLC: This structure is taxed like a sole proprietorship. Profits or losses from the business are not taxed directly but instead are taxed through the single member's personal federal tax return. A single member LLC does not have to file a tax return since everything flows through to the owner's return. Single member LLCs are often used with charitable remainder unitrusts to give the managing member a choice as to when the CRT receives income. Income is only paid out to an income beneficiary of the CRT when the income moves from the LLC to the CRT.
- Partners in an LLC: Members elect to be treated like a traditional partnership for tax purposes. The operating agreement can be used to allocate tax deductions to individuals who can use them and keep operating income away from charitable trusts.
- LLC filing as a Corporation: The members of the organization may also choose to file as if they were corporation.
- Generally, members of an LLC will create an Operating Agreement that outlines how the LLC will be treated for tax purposes.

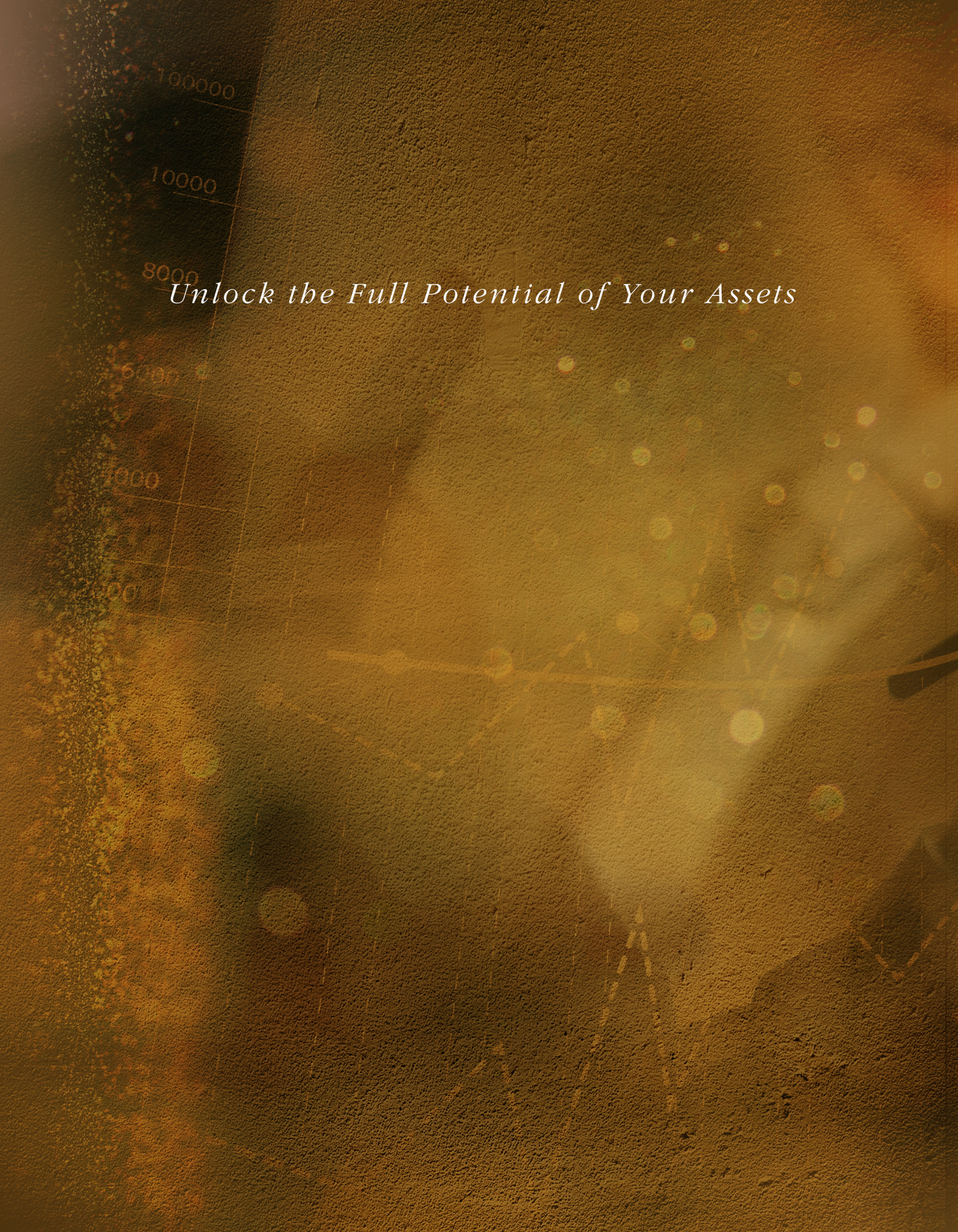
Less Paperwork:

Compared with C-Corps or S-Corps, LLCs are very flexible. Once again, you'll want to have an LLC Operating Agreement so you can create rules that govern your business. Otherwise, your company will be governed by the default rules in your state.

With less stringent requirements for compliance and less necessary paperwork, LLCs are easier to form and easier to keep in good legal standing.

Limited Liability:

Like corporations, LLCs provide their members protection from liability. This means that members are not personally liable for debts and often court judgments incurred by the LLC. Creditors are foreclosed from seeking the personal assets of the LLCs members. It is a meaningful shield not provided in a sole proprietorship or traditional partnership.



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