# Charitable Giving

When developing your estate plan, you can do well by doing good. Leaving money to charity rewards you in many ways. It gives you a sense of personal satisfaction, and it can save you money in estate taxes.

## A few words about estate taxes

The Economic Growth and Tax Relief Reconciliation Act of 2001 (the 2001 Tax Act) gradually eliminates federal estate taxes by increasing the amount that is exempt from these taxes over several years (from $1 million in 2002 and 2003 to $3.5 million in 2009); reducing the top rate over several years (50 percent in 2002, 49 percent in 2003, 48 percent in 2004, 47 percent in 2005, 46 percent in 2006, and 45 percent in 2007 through 2009); and finally repealing estate taxes for persons who die after 2009. However, under a provision in the law, pre-2001 Tax Act rules will return after 2010.

Whether you are subject to federal estate taxes depends on the size of your estate and the year you die. Tax law changes only increase the need for careful planning, and charitable giving can play an important role in many estate plans. By leaving money to charity when you die, the full amount of your charitable gift may be deducted from the value of your taxable estate.

## Make an outright bequest in your will

The easiest and most direct way to make a charitable gift is by an outright bequest of cash in your will. Making an outright bequest requires only a short paragraph in your will that names the charitable beneficiary and states the amount of your gift. The outright bequest is especially appropriate when the amount of your gift is relatively small, or when you want the funds to go to the charity without strings attached.

## Make a charity the beneficiary of an IRA or retirement plan

If you have funds in an IRA or employer-sponsored retirement plan, you can name your favorite charity as a beneficiary. Naming a charity as beneficiary can provide double tax savings. First, the charitable gift will be deductible for estate tax purposes. Second, the charity will not have to pay any income tax on the funds it receives. This double benefit can save combined taxes that otherwise could eat up a substantial portion of your retirement account.

## Use a charitable trust

Another way for you to make charitable gifts is to create a charitable trust. There are many types of charitable trusts, the most common of which include the charitable lead trust and the charitable remainder trust.

A charitable lead trust pays income to your chosen charity for a certain period of years after your death. Once that period is up, the trust principal passes to your family members or other heirs. The trust is known as a charitable lead trust because the charity gets the first, or lead, interest.

A charitable remainder trust is the mirror image of the charitable lead trust. Trust income is payable to your family members or other heirs for a period of years after your death or for the lifetime of one or more beneficiaries. Then, the principal goes to your favorite charity. The trust is known as a charitable remainder trust because the charity gets the remainder interest. Depending on which type of trust you use, the dollar value of the lead (income) interest or the remainder interest produces the estate tax charitable deduction.

## Why use a charitable lead trust?

The charitable lead trust is an excellent estate planning vehicle if you are optimistic about the future performance



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of the investments in the trust. If created properly, a charitable lead trust allows you to keep an asset in the family while being an effective tax-minimization device.

For example, you create a $1 million charitable lead trust. The trust provides for fixed annual payments of $80,000 (or 8 percent of the initial $1 million value of the trust) to ABC Charity for 25 years. At the end of the 25-year period, the entire trust principal goes outright to your beneficiaries. To figure the amount of the charitable deduction, you have to value the 25-year income interest going to ABC Charity. To do this, you use IRS tables. Based on these tables, the value of the income interest can be high--for example, $900,000. This means that your estate gets a $900,000 charitable deduction when you die, and only $100,000 of the $1 million gift is subject to estate tax.

## Why use a charitable remainder trust?

A charitable remainder trust takes advantage of the fact that lifetime charitable giving generally results in tax savings when compared to testamentary charitable giving. A donation to a charitable remainder trust has the same estate tax effect as a bequest because, at your death, the donated asset has been removed from your estate. Be aware, however, that a portion of the donation is brought back into your estate through the charitable income tax deduction.

Also, a charitable remainder trust can be beneficial because it provides your family members with a stream of current income--a desirable feature if your family members won't have enough income from other sources.

For example, you create a $1 million charitable remainder trust. The trust provides that a fixed annual payment be paid to your beneficiaries for a period not to exceed 20 years. At the end of that period, the entire trust principal goes outright to ABC Charity. To figure the amount of the charitable deduction, you have to value the remainder interest going to ABC Charity, using IRS tables. This is a complicated numbers game. Trial computations are needed to see what combination of the annual payment amount and the duration of annual payments will produce the desired charitable deduction and income stream to the family.

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