



Secondary Planning for CRTs

Spokane Estate Planning Council

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Sterling Foundation Management

- Oldest national foundation administrator in the U.S.
- Non-competitive
 - ✓ *Don't manage or custody assets*
 - ✓ *Support financial, insurance, legal and tax advisors*
 - ✓ *Don't provide tax, legal, financial or insurance advice*
- Charitable consulting
- Secondary planning for CRTs

House Analogy

- When a client buys a house, they probably don't expect to keep it forever
 - ✓ *Kids grow up and move out*
 - ✓ *Health changes and a different house serves better*
 - ✓ *Cold winters grow old and a warmer state beckons*
 - ✓ *Etc.*
- But that doesn't mean it was a mistake to buy the house in the first place

House Analogy

- Same logic applies to clients' CRTs
- Circumstances change over time
 - ✓ *The CRT was a great solution and worked well for years*
 - ✓ *But is it the best possible use of those assets today?*
- Advisors are making their clients aware of their options with respect to their CRTs

Charitable Remainder Trusts – the Pros

- Powerful tax-planning vehicles
 - ✓ *Defers capital gain*
 - ✓ *Generates an up-front income tax deduction*
 - ✓ *Diversifies a concentrated position*
 - ✓ *Creates an income stream*

Charitable Remainder Trusts – the Cons

- Irrevocable
- Usually span decades of clients' lives
- Combination can lead to a misalignment between client's situation and the CRT

The Importance of CRT Reviews

- CRT income interests are capital assets
 - ✓ *Rev. Rul. 72-243, 1972-1 C.B. 233*
 - ✓ *PLRs (e.g., PLR 2007390041)*
- Yet they are rarely reviewed like other capital assets
 - ✓ *Clients left in the dark (“my CRT is a lifetime lockup”)*
- Goal of review
 - ✓ *Ensure client is aware of available options*
 - ✓ *Assess client’s fit with CRT*

Options Available

- Gift income interest
 - ✓ *Gives the entire trust to charity today*
- Terminate CRT
 - ✓ *Less common because of sale option*
- Sell income interest
 - ✓ *Maximizes present value of income stream to client*
- CRT Rollover
 - ✓ *Enables client to make strategic changes regarding CRT*

Sale of Income Interest

- Key Benefits
 - ✓ *Client receives more money than keeping CRT*
 - ✓ *Client receives more money than if they terminated*
 - ✓ *Sale typically takes 2-4 weeks to complete*
- 15 years, hundreds of transactions
- Drivers
 - ✓ *Need or desire for liquidity*
 - ✓ *Simplification*
 - ✓ *Divorce*

Composite Example

| | <i>No Action</i> ¹ | <i>Terminate</i> ² | <i>Sell Interest</i> ³ |
|--------------------|-------------------------------|-------------------------------|-----------------------------------|
| After-Tax Proceeds | \$ 804,183 | \$ 696,850 | \$ 920,000 |

- Financial benefit of sale
 - ✓ vs. No Action: \$115,817 or 14%
 - ✓ vs. Terminate: \$223,150 or 32%

¹ Does not include trustee, administration or similar fees. Prepared using advisor/client assumptions.

² Does not include fees associated with termination. Calculated via charitableplanning.com.

³ Includes all associated fees.

CRT Rollover

- Aligns CRT with client's current situation
 - ✓ *Named Beneficiaries*
 - ✓ *New Spouse, Children*
 - ✓ *Type of CRT*
 - SCRUT to NIMCRUT
 - ✓ *Income deferral*
 - ✓ *Build wealth tax-free for children/younger spouses*
 - NIMCRUT to SCRUT
 - ✓ *Frustration with NIMCRUT*
 - ✓ *Larger and more reliable income stream*

CRT Rollover

- How is it done?
 - ✓ *New CRT created*
 - ✓ *Client uses income interest to fund new CRT*
 - ✓ *New trust reflects client's desired changes*
- Client garners immediate tax deduction
- Decanting not possible

CRT Rollover

- Key Fact Pattern
 1. *Have children*
 2. *Don't need income from their CRT*
- These clients are ideal Rollover candidates
 - ✓ *Create an income stream for their children*
 - ✓ *Reduce their own taxable income*
 - ✓ *Garner an immediate income tax deduction*

Case Study – Situation

- Client profile
 - ✓ *77-year-old*
 - ✓ *Husband deceased*
 - ✓ *Two daughters; 56- and 54-years old*
- CRT
 - ✓ *5.43M*
 - ✓ *5% Standard CRUT*
 - ✓ *Expected to distribute \$3M to client over remaining lifetime*

Case Study – Execution of Rollover

- Rollover
 - ✓ *Client's attorney formed new CRT (a Flip CRUT) with client and daughters as income beneficiaries*
 - ✓ *Client gifted income interest in 5% CRUT to new CRT*
 - ✓ *New CRT eventually sold income interest*
 - ✓ *After a deferral period (mom's lifetime), daughters receive income from CRT*

Case Study – Result

- Income
 - ✓ *In effect, client converted \$3M of income into \$5.4M of income for her daughters*
- Taxes
 - ✓ *Client avoids paying tax on \$3M of income*
 - ✓ *Client receives income tax deduction of \$600,000*
 - ✓ *Total tax savings could easily exceed \$1M*

No Action

The Standard CRUT structure forces taxable income to the client each year, regardless of whether the income is needed. The client cannot defer the taxable income. What's in the trust at the client's death goes to charity. The client's children do not benefit directly from the trust.

| | |
|-------------------|-------------|
| Tax Deduction | None |
| \$ to Client Only | \$2,986,500 |

| Yr. | Beginning CRT Value | Growth (5%) | Payout (5%) | Ending CRT Value |
|-----|---------------------|-------------|-------------|------------------|
| 1 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 2 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 3 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 4 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 5 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 6 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 7 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 8 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 9 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 10 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |
| 11 | 5,430,000 | 271,500 | 271,500 | 5,430,000 |

Roll SCRUT to NIMCRUT & Add Children

Rolling to a NIMCRUT provides flexibility to defer the taxable income. The deferred income grows tax-free in the NIMCRUT and is available to the client at any time. The client can add her children as contingent income beneficiaries, creating an income stream that begins at the end of the client's lifetime and lasts for the remainder of her children's lifetimes. What's in the trust when the last of the children passes goes to charity. The client receives a tax deduction in connection with the Rollover.

| | |
|-------------------------|-------------|
| Tax Deduction | \$600,000 |
| \$ to Client's Children | \$5,377,565 |

| Yr. | Beginning CRT Value | Growth (5%) | Payout | Ending CRT Value | Cumulative Deferred Income (accessible any time) |
|-----|---------------------|-------------|--------------|------------------|--|
| 1 | 2,500,000 | 125,000 | Deferred | 2,625,000 | 125,000 |
| 2 | 2,625,000 | 131,250 | income grows | 2,756,250 | 256,250 |
| 3 | 2,756,250 | 137,813 | tax-free in | 2,894,063 | 394,063 |
| 4 | 2,894,063 | 144,703 | trust | 3,038,766 | 538,766 |
| 5 | 3,038,766 | 151,938 | | 3,190,704 | 690,704 |
| 6 | 3,190,704 | 159,535 | | 3,350,239 | 850,239 |
| 7 | 3,350,239 | 167,512 | | 3,517,751 | 1,017,751 |
| 8 | 3,517,751 | 175,888 | | 3,693,639 | 1,193,639 |
| 9 | 3,693,639 | 184,682 | | 3,878,321 | 1,378,321 |
| 10 | 3,878,321 | 193,916 | | 4,072,237 | 1,572,237 |
| 11 | 4,072,237 | 203,612 | | 4,275,848 | 1,775,848 |
| 12 | 4,275,848 | 213,792 | 298,357 | 4,191,284 | 1,691,284 |
| 13 | 4,191,284 | 209,564 | 294,128 | 4,106,720 | 1,606,720 |
| 14 | 4,106,720 | 205,336 | 289,900 | 4,022,156 | 1,522,156 |
| 15 | 4,022,156 | 201,108 | 285,672 | 3,937,592 | 1,437,592 |
| 16 | 3,937,592 | 196,880 | 281,444 | 3,853,027 | 1,353,027 |
| 17 | 3,853,027 | 192,651 | 277,216 | 3,768,463 | 1,268,463 |
| 18 | 3,768,463 | 188,423 | 272,987 | 3,683,899 | 1,183,899 |
| 19 | 3,683,899 | 184,195 | 268,759 | 3,599,335 | 1,099,335 |
| 20 | 3,599,335 | 179,967 | 264,531 | 3,514,771 | 1,014,771 |

Client defers income over her remaining lifetime (years 1-11)

Client's children receive income over their remaining lifetimes (years 12-20)

Case Study: SCRUT to SCRUT/Add Children

- Situation

- ✓ *Husband and wife; 72- and 71-year-old*
- ✓ *Joint income beneficiaries of Standard CRUT*
- ✓ *Looking to benefit two sons during clients' lifetimes*

- Solution

- ✓ *Roll to new Standard CRUT*
 - *Two sons are immediate income beneficiaries*
 - *20-year term*
 - *Max payout (~11%)*

Case Study: SCRUT to SCRUT/Add Children

Keep 5% SCRUT

| | |
|-------------------|-------------|
| Tax Deduction | None |
| Expected Duration | 18 Years |
| \$ to Parents | \$3,757,500 |

| Yr. | Beg. CRT Val | Growth (5%) | Dist. (5%) | End CRT Val. |
|-----|--------------|-------------|------------|--------------|
| 1 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 2 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 3 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 4 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 5 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 6 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 7 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 8 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 9 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 10 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 11 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 12 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 13 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 14 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 15 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 16 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 17 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |
| 18 | 4,175,000 | 208,750 | 208,750 | 4,175,000 |

Roll to 11% SCRUT & Add Children

| | |
|-------------------|-------------|
| Tax Deduction | \$223,059 |
| Expected Duration | 20 Years |
| \$ to Children | \$3,774,288 |

| Yr. | Beg. CRT Val. | Growth (5%) | Dist. (11%) | End CRT Val. |
|-----|---------------|-------------|-------------|--------------|
| 1 | 2,900,000 | 145,000 | 319,000 | 2,726,000 |
| 2 | 2,726,000 | 136,300 | 299,880 | 2,562,440 |
| 3 | 2,562,440 | 128,122 | 281,888 | 2,408,694 |
| 4 | 2,408,694 | 120,435 | 264,956 | 2,264,172 |
| 5 | 2,264,172 | 113,209 | 249,059 | 2,128,322 |
| 6 | 2,128,322 | 106,416 | 234,115 | 2,000,622 |
| 7 | 2,000,622 | 100,031 | 220,068 | 1,880,585 |
| 8 | 1,880,585 | 94,029 | 206,884 | 1,767,750 |
| 9 | 1,767,750 | 88,387 | 194,452 | 1,661,685 |
| 10 | 1,661,685 | 83,084 | 182,785 | 1,561,984 |
| 11 | 1,561,984 | 78,099 | 171,818 | 1,468,265 |
| 12 | 1,468,265 | 73,413 | 161,509 | 1,380,169 |
| 13 | 1,380,169 | 69,008 | 151,819 | 1,297,359 |
| 14 | 1,297,359 | 64,868 | 142,709 | 1,219,517 |
| 15 | 1,219,517 | 60,976 | 134,147 | 1,146,346 |
| 16 | 1,146,346 | 57,317 | 126,098 | 1,077,565 |
| 17 | 1,077,565 | 53,878 | 118,532 | 1,012,912 |
| 18 | 1,012,912 | 50,646 | 111,420 | 952,137 |
| 19 | 952,137 | 47,807 | 104,735 | 895,009 |
| 20 | 895,009 | 44,750 | 98,451 | 841,308 |

Case Study: NIMCRUT to SCRUT/Add Spouse

- Situation

- ✓ *73-year-old male*
- ✓ *Sole surviving income beneficiary of 7% NIMCRUT*
- ✓ *Remarried, younger spouse*

- Solution

- ✓ *Roll to SCRUT*
 - Creates reliable income stream
- ✓ *Add wife as contingent income beneficiary*
 - Creates income stream for younger spouse

Case Study: NIMCRUT to SCRUT/Add Spouse

Keep NIMCRUT

7% NIMCRUT paying half of anticipated income. Due to limitations on accounting income, all income to client is taxable as ordinary income. Client's younger wife receives no benefit from the NIMCRUT as it is distributed to charity upon client's death.

| | |
|-------------------|-------------|
| Tax Deduction | None |
| Expected Duration | 12 Years |
| Total Income Paid | \$2,520,000 |

| | Beg. of Year CRT Value | Growth (3.5%) | Payout (3.5%) | End of Year CRT Value |
|----|------------------------|---------------|---------------|-----------------------|
| 1 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 2 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 3 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 4 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 5 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 6 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 7 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 8 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 9 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 10 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 11 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |
| 12 | 6,000,000 | 210,000 | 210,000 | 6,000,000 |

(1) Growth is net of any fees.

Roll NIMCRUT to SCRUT & Add Wife

Rollover to Standard CRUT creates an income stream that is larger, more reliable and more tax favorable. Rollover also enables client to add his younger wife as a contingent income beneficiary of the CRUT, which provides her with an additional source of income after his death. Client receives an immediate income tax deduction of \$870,751.

| | | | |
|-------------------|-------------|----------------------|----------------|
| Tax Deduction | \$870,751 | ← Impact of Rollover | |
| Expected Duration | 20 Years | | ← 67% increase |
| Total Income Paid | \$4,076,838 | | ← 62% increase |

| | Beg. of Year CRT Value | Growth (3.5%) | Payout (7%) | End of Year CRT Value |
|----|------------------------|---------------|-------------|-----------------------|
| 1 | 4,000,000 | 140,000 | 280,000 | 3,860,000 |
| 2 | 3,860,000 | 135,100 | 270,200 | 3,724,900 |
| 3 | 3,724,900 | 130,372 | 260,743 | 3,594,529 |
| 4 | 3,594,529 | 125,808 | 251,617 | 3,468,720 |
| 5 | 3,468,720 | 121,405 | 242,810 | 3,347,315 |
| 6 | 3,347,315 | 117,158 | 234,312 | 3,230,159 |
| 7 | 3,230,159 | 113,058 | 226,111 | 3,117,103 |
| 8 | 3,117,103 | 109,099 | 218,197 | 3,008,005 |
| 9 | 3,008,005 | 105,280 | 210,560 | 2,902,724 |
| 10 | 2,902,724 | 101,595 | 203,191 | 2,801,129 |
| 11 | 2,801,129 | 98,040 | 196,079 | 2,703,090 |
| 12 | 2,703,090 | 94,608 | 189,218 | 2,608,481 |
| 13 | 2,608,481 | 91,297 | 182,594 | 2,517,185 |
| 14 | 2,517,185 | 88,101 | 176,203 | 2,429,083 |
| 15 | 2,429,083 | 85,018 | 170,036 | 2,344,065 |
| 16 | 2,344,065 | 82,042 | 164,085 | 2,262,023 |
| 17 | 2,262,023 | 79,171 | 158,342 | 2,182,852 |
| 18 | 2,182,852 | 76,400 | 152,800 | 2,106,452 |
| 19 | 2,106,452 | 73,728 | 147,452 | 2,032,728 |
| 20 | 2,032,728 | 71,145 | 142,291 | 1,961,581 |

Many Possibilities

SCRUT

NEW CRT

NIMCRUT

Adjust payout
Manage payout
Income tax deduction

ust payout
Manage payout
Income tax deduction

Questions

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