

## Charitable Lead Trusts (CLTs): A Powerful Tool for Philanthropy and Wealth Transfer

A Charitable Lead Trust (CLT) enables donors to provide charitable gifts while simultaneously transferring assets to heirs at a discounted value for tax purposes. In a CLT, a charitable organization receives an income stream from the trust, while non-charitable beneficiaries receive the remaining assets at the end of the trust's term. This structure allows for both charitable contributions and potential estate or gift tax savings.

### Types of Charitable Lead Trusts

#### ➤ Reversionary vs. Non-Reversionary Interest:

- **Reversionary CLT:** The grantor (or their spouse) receives the remaining trust assets after the income period. This type of CLT typically is most beneficial for individuals seeking income tax deductions, though estate tax deductions are not applicable due to the reversionary interest. The age of the income recipient (older recipients receive larger deductions)
- **Non-Reversionary CLT:** The remainder of the trust assets is distributed to someone other than the grantor or spouse (typically children or grandchildren). This structure allows the value of the assets to be removed from the grantor's estate, reducing the taxable estate and potentially allowing for significant estate tax savings, especially if the assets are expected to appreciate.

#### ➤ Grantor vs. Non-Grantor Tax Status

- **Grantor CLT:** The grantor is considered the owner of the trust's income for tax purposes. All income generated by the trust, including amounts distributed to charity, is taxable to the grantor. However, the grantor receives an immediate income tax deduction based on the present value of the charitable income interest. Reversionary CLTs are typically structured as grantor trusts.
- **Non-Grantor CLT:** The trust income is not taxable to the grantor, but there is no income tax deduction for the grantor when the trust is created. Non-reversionary CLTs are often structured as non-grantor trusts, though they may also be structured as grantor trusts.





### Charitable Lead Trust Requirements

To qualify for the associated tax benefits, a CLT must be irrevocable and meet specific requirements:

- **Income Payments:** Payments must be made at least annually to one or more charitable organizations.
  - **Charitable Lead Annuity Trust (CLAT):** The payment to charity is a fixed sum or a fixed percentage of the initial fair market value of the trust assets. If the trust's income is insufficient to meet the payment requirement, the trustee must dip into the principal.
  - **Charitable Lead Unitrust (CLUT):** Payments to the charity are based on a fixed percentage of the fair market value of the trust assets, which are revalued annually. Unlike a CRT, a CLUT must pay the full unitrust amount, even if net income is lower, ensuring that the charity receives consistent payments.
- **Trust Term:** Payments must continue for either a set term of years or for the lifetime of one or more individuals alive when the trust is created. CLTs do not have a maximum duration under federal tax law, though state rules regarding perpetuities may apply.

### Additional Contributions

- **CLAT:** While additional contributions are permitted, they do not provide further income, gift, or estate tax deductions since the annuity amount is fixed when the trust is created. However, these contributions will not invalidate the deductions from the initial contribution.
- **CLUT:** Additional contributions to a CLUT may qualify for additional income, gift, or estate tax deductions because the annual unitrust payment is based on the trust's fair market value, which is recalculated annually.

### Tax Implications of Charitable Lead Trusts

The taxation of CLTs varies depending on whether they are structured as grantor or non-grantor trusts. For grantor trusts, the income is taxable to the grantor, who may receive a charitable income tax deduction in the year the trust is established. Non-grantor trusts, on the other hand, do not generate income tax liability for the grantor, but they also do not allow for an immediate charitable income tax deduction.





## Conclusion

Charitable Lead Trusts can be an excellent strategy for individuals looking to support charitable organizations while simultaneously reducing estate or gift taxes. By providing a stream of charitable donations during the trust's term and transferring appreciated assets to heirs at a reduced tax cost, CLTs offer a versatile and tax-efficient solution for philanthropic individuals and families.

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