Jeffrey Frye - Fri, 5/15/2020 - 16:03

PG Calc's *Planned Giving Manager* and *PGM Anywhere* include a question that sometimes causes confusion for the gift planning professional. When running the calculations for a charitable remainder unitrust, the following question appears in the Gift Options section: "Whole Months from Annual Valuation Date to First Payment Date." We have received a number of calls over the years about that question, and we thought this was a good chance to cover it.

For basic review:

A charitable remainder unitrust (CRUT) makes payments to the named beneficiary (or beneficiaries) one or more times each calendar year. The total of the payment amounts is computed by multiplying the official payout percentage of the trust by the fair market value of the trust assets on a specific date. The date is named in the governing trust document and is consistent from one year to the next. It is usually at or near the beginning of the year, but technically, it may be anytime during the year.

We are always delighted to receive calls from our clients, but the Help section in the software is also there to provide guidance. Here is the excerpt that explains the question:

Enter the number of whole months that transpire each year between the annual valuation date of the unitrust and the first income payment made after each annual valuation. The gift date is a special date of valuation and should be ignored for purposes of answering this question.

For example, a unitrust that is funded on December 1, is valued the first business day each year, and makes payments every June 30 and December 31, has a delay from valuation to first payment of 6 months, not 1 month.

Note: If the trust instrument does not specify the dates on which payments are to be made each year (e.g., June 30th and December 31st), enter 0.

The part that eludes many users of the software is that the *question does not apply to the first partial year – the initial short year that renders a proration of the total payment amount for the year. The question only applies to whole years of the CRUT*. In the calculation of the charitable income tax deduction, the IRS wants to know how long the beneficiary waits to receive the first payment after the official annual valuation date in a normal full calendar year.

Why does the IRS care about this seemingly minor detail? It is all about the corpus of the trust and the time value of the money. Remember, the charitable tax deduction for any life income gift arrangement reflects the estimated future remainder value going to the charity, discounted to present value. If the payments are made quarterly (most typical), the corpus of the trust is reduced every three months to make the beneficiary payment.

That is significantly different over the long run than when the payments are only made once a year at the very end of the year (e.g. annual payments on December 31). In that case, with the annual valuation date on January 1 and the payments annually on December 31, the assets of the trust are preserved for 12 full months before the beneficiary distribution is made. Even if the payout rate is only 5% (the lowest possible for a CRUT), the reinvestment of income, and the estimated growth on the value of the assets, produce a markedly larger residuum for the charity as compared to having quarterly payments. Keep in mind that the estimated duration of these trusts when executed is typically 10 or 15 years, or even more; it is the cumulative long-term effect of annual payments that really makes the difference.

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