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A grantor charitable lead annuity trust is a gift plan defined by federal tax law that allows an individual to retain ultimate possession of an asset while making a generous gift to charity.

The donor transfers assets, usually cash or securities, to a trustee of choice, such as a bank trust department. The donor receives an income tax deduction equal to the value of the income stream promised to the charity. Because the gift is deemed to be “for the use of” the charity, the deduction is subject to IRS 20%/30% limitations.

During the trust's term, the trustee invests the trust's assets and provides a fixed dollar amount each year to charity. These payments are used for the charitable purpose the donor designates.

Although the grantor trust's term may be for one or more lifetimes, a specific number of years (10-20 years is common) is almost always used. Payments are made out of trust income, or trust principal if the trust income is not adequate. They continue until the trust term ends or until the highly unlikely event that the trust distributes all of its assets.

When the grantor lead trust term ends, its charitable payments cease and the trust returns all of its accumulated assets back to the donor.

Because the donor retains ultimate possession of a grantor lead trust's assets, all taxable income earned by the trust during its term, including income distributed to charity, is taxable to the donor. For this reason, grantor lead trusts sometimes are invested to earn tax-free income.

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