



## Life Income Trust Payout Rates

**Q:** If I establish a life income trust, will a relatively high payout rate be better for me than a relatively low payout rate?

**A:** Not necessarily.

How you decide upon what payout rate to choose when establishing a charitable remainder trust will depend upon a number of factors, including the current and future cash flow needs of the income beneficiaries, the size of the gift that you wish to provide for the charity(ies) named as remainder beneficiary(ies), and tax and inflation rates. Another important factor is the expected duration of the trust, which is often a function of the ages of the income beneficiaries. As you are making this decision, you also will want to consider what you anticipate the projected investment return for the assets of the trust will be and the impact on the income beneficiaries' payments if the trust does not achieve these returns. This is especially true if the charitable remainder trust will be a unitrust.

When you establish a charitable remainder trust, you are entitled to an income tax deduction, but only based on an actuarial calculation of the "present value" of the expected amount the charity will receive when the trust terminates. The calculation of this value is set forth in the Internal Revenue Code ("the Code") and regulations thereunder. If you choose a lower rate of payout for the income beneficiaries, the present value of the charitable remainder will be higher and, therefore, the income tax charitable deduction will be higher. In other words, choosing a lower payout rate may result in a potentially greater reduction in income taxes as a result of a higher income tax deduction. The Code stipulates that the payout rate must be at least 5 percent and that the upper limit is the rate at which the present value of the charitable remainder is less than 10 percent of the market value of the assets contributed.

For charitable remainder unitrusts, another important factor to consider is that a lower payout rate may result in a substantially larger trust principal over time, which would provide (i) unitrust beneficiaries with a payout that is more likely to increase over time and (ii) a larger remainder for the charity(ies) named as the remainder beneficiary(ies). For an illustration, see the basic Projected Cash Flow Comparison chart (on reverse), which shows the payments a life income beneficiary might expect to receive from a 5 percent unitrust versus a 7 percent unitrust established with a gift of \$200,000. This chart is based on an assumed annual total investment return of 8 percent over the life of the trust. Actual results will differ and will depend on the trust's investment returns, which will vary from year to year.

With a charitable remainder annuity trust, the payout rate also should be considered carefully because the amount that will be received by the beneficiaries during the term of the trust will remain constant and will not change over time. A higher payout rate may be appealing, however, if the trust performance

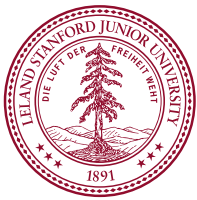
## ASSUMPTIONS

- Projection begins in 2010 and runs for 33 years.
- Beneficiary's age is 50.
- Original principal is \$200,000.
- Total investment return on trust assets is 8 percent annually.

## PROJECTED CASH FLOW COMPARISON

Year	Year-End Principal (CRUT 5%)	Before-Tax Beneficiary Income	Year-End Principal (CRUT 7%)	Before-Tax Beneficiary Income
2010	\$200,000	–	\$200,000	–
2011	206,000	\$10,000	202,000	\$14,000
2012	212,180	10,300	204,020	14,140
2013	218,545	10,609	206,060	14,281
2014	225,102	10,927	208,121	14,424
2015	231,855	11,255	210,202	14,568
2016	238,810	11,593	212,304	14,714
2017	245,975	11,941	214,427	14,861
2018	253,354	12,299	216,571	15,010
2019	260,955	12,668	218,737	15,160
2020	268,783	13,048	220,924	15,312
2021	276,847	13,439	223,134	15,465
2022	285,152	13,842	225,365	15,619
2023	293,707	14,258	227,619	15,776
2024	302,518	14,685	229,895	15,933
2025	311,593	15,126	232,194	16,093
2026	320,941	15,580	234,516	16,254
2027	330,570	16,047	236,861	16,416
2028	340,487	16,528	239,229	16,580
*2029	350,701	17,024	241,622	16,746
2030	361,222	17,535	244,038	16,914
2031	372,059	18,061	246,478	17,083
2032	383,221	18,603	248,943	17,253
2033	394,717	19,161	251,433	17,426
2034	406,559	19,736	253,947	17,600

\*Due to appreciation of principal, future income from a 5 percent unitrust may exceed income from a 7 percent unitrust.



## CONTACT US

For more information, please contact:

Office of Planned Giving  
 Frances C. Arrillaga Alumni Center  
 326 Galvez Street  
 Stanford, CA 94305-6105

bequests.trusts@stanford.edu

650.725.4358 (T)  
 650.723.6570 (F)

plannedgiving.stanford.edu  
 thestanfordchallenge.stanford.edu

is weak for a period of time, the trust assets could be exhausted due to the high annual distributions. A higher payout rate may be desired if the beneficiaries who are receiving the annuity have high current cash flow needs, short life expectancies, and/or trust interests that will expire at the end of a fixed term rather than at death. In addition to the “10 percent remainder” test described above, annuity trust rates are also limited by an additional calculation at the time the trust is established to determine whether the chosen rate will result in a probability of trust exhaustion that is greater than 5 percent. If the probability of exhaustion exceeds 5 percent, the annuity trust will not qualify as a charitable remainder trust.

The main financial benefit of a charitable remainder trust to the donor is typically long-term cash flow for the income beneficiaries, so it may be appropriate to think of a charitable remainder trust as a long-term investment planning vehicle. The payout rate should be chosen only after consideration of all relevant factors and only after evaluating cash flow modeling based on realistic investment return assumptions.