TAX MANAGEMENT
PORTFOLIOS™

ESTATES, GIFTS, AND TRUSTS

Charitable Remainder Trusts, Charitable Gift Annuities, and Pooled Income Funds (Sections 664 and 642(c)(5))

by

Laura H. Peebles
Retired Director
Deloitte Tax LLP

&

Lawrence Katzenstein
Partner
Thompson Coburn LLP

Laura H. Peebles, retired director (2014), Deloitte Tax LLP. B.S., Accounting, University of New Orleans (*summa cum laude*) (1987); Certified Public Accountant (Retired), (Elijah Watts Sells Award 1988). Senior Fellow, Bloomberg Tax. Frequent writer and speaker on estate planning and charitable planning topics.

Lawrence Katzenstein, B.A., Washington University in St. Louis (1969); J.D. Harvard University (1972); partner, Thompson Coburn LLP, St. Louis, Missouri; Member, American Bar Association Section of Taxation, National Association of College and University Attorneys; Fellow, American College of Trust and Estate Counsel; Director, American Council on Gift Annuities; creator of Tiger Tables actuarial software.

This portfolio revises and supersedes previous versions of 865-3rd T.M., *Charitable Remainder Trusts, Charitable Gift Annuities, and Pooled Income Funds (Sections 664 and 642(c)(5))*.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

BLOOMBERG TAX
makes available the following professional resources:

U.S. INCOME PORTFOLIO SERIES
MEMORANDUM
ESTATES, GIFTS AND TRUSTS PORTFOLIO SERIES
ESTATES, GIFTS AND TRUSTS JOURNAL
FOREIGN INCOME PORTFOLIO SERIES
INTERNATIONAL JOURNAL
COMPENSATION PLANNING JOURNAL
REAL ESTATE JOURNAL
TAX PRACTICE SERIES
FINANCIAL PLANNING JOURNAL
IRS PRACTICE ADVISER
ACCOUNTING POLICY & PRACTICE REPORT
ACCOUNTING PORTFOLIO SERIES
TRANSFER PRICING REPORT
STATE TAX PORTFOLIO SERIES
WEEKLY STATE TAX REPORT

For information, call 1-800-372-1033
Visit our website at: https://pro.bloombergtax.com

BOARD OF EDITORS
Josh Eastright, CEO;
Bobby Puglia, CHIEF PRODUCT OFFICER;
Alex Butler, HEAD OF CONTENT AND ANALYSIS;
Jayanti Singh, SENIOR DIRECTOR;
Lindsay Bartholomew, Esq., René Blocker, Esq., Tiwa Nwogu, Esq., LL.M., Claire Tarrant, LLB, CONTENT SENIOR TEAM LEADS;
Lauren Colandreo, Esq., LL.M, William Dunn, CPP, Dillon Fowler, J.D., John McManus, CPA, Maria Menezes, Morgan Oliver, Esq.,
Peter H. Rho, Esq., Sean Richardson, Farah Roy, Esq., Benjamin J. Rubelmann, Esq., Robb Trott, Morgan Vercillo, Esq.,
Jazlyn Williams, CONTENT TEAM LEADS;
Peter E. Burt, Esq., CONTENT ACQUISITIONS TEAM LEAD;
Jane Baniewicz, Esq., Anie Bista, J.D., Ian Campbell, Esq., Amanda Donati, J.D., Kate Driscoll, Mike Dazé, Esq., Emmanuel Elone,
Chelsey Emmanuel, Esq., LL.M, David Epstein, Esq., Brad Espinosa, J.D., Olivier Fute, Corey Gibbs, Esq., Chloe Gilchrist,
Dardi Gomez, Esq, Amber Gorski, Esq., Ryan Hartnett, LL.M., Nida Hasan, Esq., Rebecka Haynes, Esq., Hayden Harris, Esq., Laura Holt, Esq.,
Ernst Hunter, Esq., Al Kish, Esq., Ryan Kerbel, J.D., LL.M, Chase W. Lanfer, J.D., Nadia Masri, Esq., James Min, Esq., Ballinger Mills, Esq., LL.M.,
Maddie Moore, Esq., Joyce Musuku, J.D., LL.M., Joanna Norland, Alejandro Parada, J.D., LL.M., Christina Parello, Esq., Fatima Pervaiz, Esq.,
Lisa Pfenninger, Esq., James Rathjen, Craig Rose, Caleb Siebeneck, J.D., Alexis Sharp, Esq., Merve Stolzman, Esq., David Sweetland, Esq.,
Tome Tanevski, Esq., Christian Tennant, Esq., Kevin Thayer, Esq., LL.M, Jocelyn Tilan, Esq., Ariam Tsighe, Esq., Yasmin Dirks, J.D., LL.M.,
Robert Walker, Bob Wells, Esq., Nick Webb, Alexa Woods. J.D., LL.M., Michael Zeitler, Esq., Rosaline Zulaikhah, CONTENT ANALYSTS;
Larry Frank, EDITOR

TECHNICAL ADVISORS
BUCHANAN INGERSOLL & ROONEY PC
Lisa M. Starczewski, Esq., Technical Director

FOUNDER OF TAX MANAGEMENT PORTFOLIOS
Leonard L. Silverstein, Esq. (1922–2018)

Copyright Policy: Reproduction of this publication by any means, including facsimile transmission, without the express permission of Bloomberg Industry Group, Inc. is prohibited except as follows: 1) Individual pages that are ''Published by Tax Management Inc.'' may be reproduced without permission, but reproduction of entire chapters or tab sections is prohibited. 2) This publication may contain forms, notices, sample letters, or working papers. These may be copyrighted by Tax Management, but your permission fee includes permission to reproduce them for internal use or to serve individual clients or customers. 3) Subscribers who have registered with the Copyright Clearance Center and who pay $1.00 per page per copy fee may reproduce other portions of this publication but not the entire contents. The Copyright Clearance Center is located at 222 Rosewood Dr., Danvers, Mass. 01923. Tel. (508) 750-8400. 4) Permission to reproduce Tax Management material otherwise can be obtained by calling (703) 341-5937. Fax (703) 341-1624.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

TAX MANAGEMENT
PORTFOLIOS™

ESTATES, GIFTS, AND TRUSTS

Charitable Remainder Trusts, Charitable Gift Annuities, and Pooled Income Funds (Sections 664 and 642(c)(5))

PORTFOLIO DESCRIPTION

Tax Management Portfolio, *Charitable Remainder Trusts, Charitable Gift Annuities, and Pooled Income Funds (Sections 664 and 642(c)(5))*, No. 865-3rd, outlines the basic requirements for the creation and administration of qualified charitable remainder trusts (CRTs), charitable gift annuities, and pooled income funds.

The creation of a CRT, establishing a charitable gift annuity, or a contribution to a pooled income fund requires both donative intent and tax planning. With proper compliance, the transaction will result in various tax and financial benefits to the donor, the trusts, the beneficiaries, and the charity.

The Portfolio starts by discussing when and why a CRT might be appropriate, then continues with a discussion of what type of CRT fits different types of assets that might be used for funding the CRT. The technical analyses of CRT creation, operation, and termination follow. The analysis includes the relevant income, gift, estate, and generation-skipping transfer tax considerations, as well as the private foundation regulations that apply to qualified charitable remainder trusts.

The Portfolio then examines charitable gift annuities, including the requirements governing the creation of charitable gift annuities and the availability of income, gift, or estate tax charitable deductions for creation of gift annuities. Income tax treatment of annuity payments and factors to consider in deciding which month's interest rate to elect will also be analyzed.

This Portfolio also covers the rules applicable to pooled income funds, including the requirements governing the creation of a qualified pooled income fund and the availability of income, gift, or estate tax charitable deductions for gifts to such funds. Pooled income funds are similar to CRTs in that a donor retains an income interest in the property donated (or creates such an interest in another) and the donor is entitled to an immediate charitable deduction for the present value of the remainder interest passing to charity.

This Portfolio may be cited as Peebles, and Katzenstein, 865-3rd, *Charitable Remainder Trusts, Charitable Gift Annuities, and Pooled Income Funds (Sections 664 and 642(c)(5))*.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

This Bloomberg Tax Portfolio is not intended to provide legal, accounting, or tax advice for any purpose and does not apply to any particular person or factual situation. Neither the authors nor the publisher assume responsibility for the reader's reliance on information or opinions expressed in it, and the reader is encouraged to verify all items by reviewing the original sources.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

TABLE OF CONTENTS

PAGE

DETAILED ANALYSIS

I. Introduction and Definitions A-1

II. When Should a Donor Consider a Charitable Remainder Trust as Part of His or Her Tax Planning? A-3

- A. When the Donor Has Charitable Intent A-3
- B. When the Donor Has an Appreciated Asset that Can Be Sold A-3
- C. When the Donor Can Benefit from an Income Tax Deduction A-3
- D. When the Donor Would Benefit from an Additional Source of Retirement Income A-3
- E. When the Donor Would Benefit from a Regular Flow of Income A-3
- F. When Diversifying or Otherwise Managing a Publicly Traded Stock Portfolio A-3
- G. When Selling, or Retiring from, a Closely Held Business A-3
- H. When Planning a Sale of Real Estate A-3
- I. When Funding a Private Foundation that Needs Time to Set up Operations A-3
- J. When a Closely Held Entity Is Selling an Appreciated Asset A-4
- K. When the Donor Would like to Provide Income for Another Individual A-4
- L. When the Donor Has a Large IRA but Desires to Control Income Stream Payable After Death A-4

III. The Basic Structure of Charitable Remainder Trusts A-5

- A. Description A-5
- B. Tax Consequences A-6

IV. Establishing an Inter Vivos Charitable Remainder Trust A-7

- A. What Types of Assets Are (or Are Not) Suitable for Charitable Remainder Trusts? A-7
  1. Publicly Traded Securities and Cash A-7
  2. Real Estate and Real Estate Partnerships A-7
  3. Art, Collectibles, and Other Tangible Personal Property A-7
  4. Options A-7
  5. Property Subject to Debt A-7

PAGE

  6. Installment Notes A-8
  7. Assignment of Income Issues A-8
  8. Assets Used by Related Parties A-8
  9. Illiquid Assets A-8
  10. Assets Owned by Corporation A-9
- B. Choosing a Charitable Remainder Annuity Trust, a Charitable Remainder Unitrust, or a Charitable Gift Annuity A-9
  1. Factors in Favor of a CRAT A-9
  2. Factors in Favor of a CRUT A-9
  3. Factors in Favor of a Gift Annuity (in Lieu of a CRAT) A-10
- C. Opportunities with Illiquid Assets: NICRUTs, NIMCRUTs, and FLIP-CRUTs A-10
- D. Setting the Annuity or Unitrust Rate A-11
  1. Minimum and Maximum Payout Rates A-11
  2. The Minimum 10% Value of the Remainder Interest A-12
  3. The 5% Exhaustion Rule, Generally Applicable Only to CRATs for a Measuring Life A-12
- E. Choosing the Noncharitable Beneficiaries and the Term for the Trust A-15
  1. Life of One or More Individual Beneficiaries (Concurrent or Successive) A-15
  2. Term of Years A-16
  3. Combination of Life and Term A-16
  4. Option for Trustee to Sprinkle Payments Among Beneficiaries A-17
  5. Donor's Retained Power to Revoke Successor Interest(s) or Invade the Trust A-18
  6. Portion of Annuity or Unitrust Payment Payable to Charity A-18
  7. Including a Qualified Contingency in the Trust A-19
- F. Choosing the Remainder Charity or Charities A-20
  1. Qualified Charities for Income, Gift, and Estate Tax Deductions A-21
  2. Remainder Charities Could Include Private Foundations A-22
- G. Selecting a Trustee A-22
  1. The Donor as Trustee A-23
  2. Individuals Other than the Donor as Trustee A-23
  3. Financial Institution as Trustee A-23

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

PAGE

4. Charity as Trustee A-24
H. Calculating the Income and Gift Tax Charitable Deduction A-24
1. Valuation of an Annuity Interest A-24
2. Valuation of a Unitrust Interest A-25
a. Adjusted Payout Rate A-26
b. Valuation Factor A-26
c. Computing the Value of the Remainder Interest A-27
d. Special Cases A-27
3. Additional Contributions to a Unitrust A-27
4. Income Tax Charitable Deduction: Remainder to Public Charity A-27
a. Deductibility Floor — Post-2025 Tax Years A-27
b. Deductibility Ceilings and Reduction Rules A-28
c. Property Other than Long-Term Capital Gain Property to Public Charities A-28
d. Gifts to Public Charities of Appreciated Long-Term Capital Gain Property A-29
5. Election to Use the Prior Month's §7520 Rate A-29
6. Income Tax Deduction if the Remainder Could Pass to a Private Foundation A-29
7. Election to Apply 50% Deduction Ceiling A-30
8. Gift of Ordinary Income Property, Including Short-Term Capital Gain Property A-31
9. Gift of Tangible Personal Property A-31
10. Gift "to" or "for the Use of" A-32
11. Interaction of the Percentage Limitations and Five-Year Carryforward A-32
12. Gift of Certain Intellectual Property A-33
I. Gift Tax A-33
1. Donor Is the Only Noncharitable Beneficiary A-33
2. Donor or U.S. Citizen Spouse (or Both) Are the Only Noncharitable Beneficiaries A-33
3. Donor and Noncharitable Beneficiaries Other than a U.S. Citizen Spouse A-34
4. Donor and Non-Citizen Spouse A-35
5. Donor and Spouse Retain No Interest in the Trust A-35
6. Gift Tax Rules Applicable to the Charitable Remainder A-35
a. Incomplete Gifts A-36
b. Completed Gifts A-36

PAGE

c. Reformation if Document Is Defective A-36
d. The 5% Exhaustion Rule A-36
e. The 10% Minimum Charitable Remainder Value Requirement A-36
f. Identity of Charitable Remainder Beneficiaries A-36
g. Section 508 A-37
h. Amount of Charitable Deduction A-37
J. Generation-Skipping Transfer Tax A-37
K. Charitable Remainder Trust Documents Requirements A-39
1. Working with the IRS Sample Forms A-39
2. Governing Instrument Requirements A-39
a. Calendar Year Requirement A-39
b. Requirement that Trust Must Be Either an Annuity Trust or a Unitrust A-40
c. Trust Must Function Exclusively as Charitable Remainder Trust from Date of Creation A-40
d. Investment Restrictions A-40
e. Prohibition on Invasion and Reversion A-41
(1) Invasion Powers A-41
(2) Reversion Issues A-42
(3) Reformation of Inter Vivos Charitable Remainder Trusts A-43
(4) Effect of Spousal Elective Share Rights A-44
L. Initial Tax Reporting at the Creation of the Trust A-45
1. Income Tax Return for the Donor A-45
a. Income Tax Reporting and Return Attachments A-45
b. Income Tax Reporting if Property Subject to Debt Is Donated A-45
2. Gift Tax Reporting for the Donor A-45
3. Initial Income Tax Return for the Charitable Remainder Trust A-46
4. Section 2801 Transfer Tax A-46

V. Testamentary Charitable Remainder Trusts A-47

A. Document Provisions A-47
B. Impact of Private Foundation Rules A-48
C. Estate Tax Deduction Allowed for Value of Charitable Interest A-49
1. Calculation of the Estate Tax Charitable Deduction A-49
2. Death of Annuity or Unitrust Recipient Before Due Date of Estate Tax Return A-50

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

	PAGE
3. Taxes Payable out of Charitable Bequests	A-50
4. Surviving Spouse Elects Against the Will	A-51
5. Estate Tax Charitable Deduction for Settlement in Lieu of Funding a Charitable Remainder Trust	A-51
6. Electing to Use a Prior Month's §7520 Rate	A-51
D. Effect on Estate Income Taxation Between Date of Death and Date of Trust Funding	A-52
E. Reformation of Defective Trusts	A-53
F. Allocation of GST Exemption	A-55
G. Estate Tax Inclusion of Property Subject to a Power of Appointment	A-55
VI. Administering a Charitable Remainder Trust	A-57
A. Calculating the Required Payments to the Noncharitable Beneficiaries	A-57
1. Charitable Remainder Annuity Trust (CRAT)	A-57
2. Charitable Remainder Unitrust (CRUT or "Straight CRUT")	A-57
3. Charitable Remainder Trusts with "Net Income" Limitations (NICRUT, NIMCRUT, FLIP-CRUT)	A-57
4. Special Calculation for NIMCRUTs Established Under the Proposed Regulations	A-58
5. Correction of Over- or Under-Payment to the Noncharitable Beneficiary	A-59
6. Computation of Annuity or Unitrust Amount for Short Taxable Years Including Last Taxable Year of Payment Period	A-59
7. Requirement for Annual Valuation of Non-Marketable Assets	A-60
B. Making the Payments to the Beneficiary	A-60
1. In Cash	A-60
2. Payments in Kind	A-61
C. Taxation of Trust	A-61
1. Assigning Income to Categories and Classes	A-61
2. Allocating Expenses to Categories	A-63
a. General Cash Expenses	A-63
b. Depreciation	A-64
c. Deduction for Taxes Paid on Income in Respect of a Decedent	A-64
d. Credits	A-64
e. Taxes	A-65
3. Effect of Unrelated Business Taxable Income (UBTI)	A-65
4. Effect of Charitable Distributions Before Trust Termination	A-66
5. Taxation of Charitable Remainder Trust in States that Do Not Treat Them as Exempt	A-67
6. Section 2801 Transfer Tax	A-67
D. Recordkeeping	A-68
1. General Recordkeeping	A-68
2. Additional Recordkeeping for Trusts with a Net Income Limitation	A-68
E. Filing the Federal Tax Return for the Charitable Remainder Trust	A-68
1. Regular Filing Requirements	A-68
2. Additional Filing Requirements Triggered by Unrelated Business Taxable Income	A-69
F. Taxation of Beneficiary	A-69
1. Taxation of Distributions to Beneficiary	A-69
2. Multiple Beneficiaries	A-71
3. Effect of Timing of Payments on Beneficiary's Income	A-71
a. Regular Payments	A-71
b. Payments Due to Incorrect Valuation or Other Adjustments	A-72
c. Payments for the Year of Recipient's Death	A-72
4. Special Rules to Determine Beneficiary's §1411 Net Investment Income	A-73
a. General Rule	A-73
b. "Simplified Method" Election	A-74
c. Special Provisions for Charitable Remainder Trusts that Own CFCs or PFICs	A-74
G. Avoiding Penalties Under the Private Foundation Rules	A-75
1. Private Foundation Provisions Applicable to Charitable Remainder Trusts	A-75
a. Section 508(e) — Governing Language Requirement	A-76
b. Section 4941	A-76
c. Section 4945	A-78
2. Selected Exceptions to Self-Dealing	A-78
a. Interest-Free Loans to a Charitable Remainder Trust	A-79
b. Provision of Goods, Services, or Facilities	A-79
c. Corporate Restructuring Exception	A-79
d. Estate Administration Exception	A-79
3. Additional Rules if a Charity Receives a Portion of the Unitrust or Annuity Payment	A-79

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

PAGE

4. Exception to Private Foundation Rules for Segregated Amounts and Pre-1969 Trusts A-80
   a. Segregated Amounts A-80
   b. Pre-May 27, 1969, Transfers A-80

H. Additional Contributions to a Charitable Remainder Unitrust A-80
1. Calculation of Charitable Income and Gift Tax Deduction A-80
2. Calculation of the Noncharitable Payment for the Year of the Contribution A-81
3. If the Additional Contribution Fails the Minimum 10% Remainder Requirement A-81

VII. Dividing a Charitable Remainder Trust A-83

A. Dividing a Charitable Remainder Trust Due to Divorce or Similar Reason A-83
B. Dividing a Charitable Remainder Trust in Order to Donate a Portion to Charity A-84

VIII. Terminating a Charitable Remainder Trust A-87

A. Winding up at the End of the Trust Term A-87
1. Income Tax Reporting for the Final Year of the Trust A-87
2. Additional Issues if a Private Foundation Is the Remainder Interest Holder A-87
3. Split-Interest Trusts that Become Charitable Trusts A-87
4. Winding-Up Period Unduly Prolonged A-88

B. Termination by Donation of the Income Interest A-88
C. Termination by Partition of the Charitable Remainder Trust Between the Beneficiary and the Charity A-89
D. Termination by Simultaneous Sale of the Income Interest and Remainder Interest A-90
E. Termination by Exchange for a Charitable Gift Annuity A-91
F. Termination by Merger with Another Charitable Remainder Trust A-91

IX. Estate Tax Treatment of Inter Vivos Charitable Remainder Trusts A-93

A. Amount Included in the Taxable Estate A-93
1. Charitable Remainder Trust Established by the Noncharitable Beneficiary A-93
2. Charitable Remainder Trust Established by Someone Other than the Noncharitable Beneficiary A-93

B. Charitable and Marital Estate Tax Estate Tax Deductions Allowed A-94

PAGE

1. Donor Is the Only Noncharitable Beneficiary of the Charitable Remainder Trust A-94
2. Donor's U.S. Citizen Spouse Is the Only Noncharitable Successor Beneficiary A-94
3. Donor's U.S. Citizen Spouse Is a, but Not the Only, Noncharitable Successor Beneficiary A-94
4. Trust Has Successor Beneficiaries Not Including a U.S. Citizen Spouse A-94
5. Trust Has a Noncitizen Spouse as a Successor Income Beneficiary A-95
6. Income Beneficiary Dies Before the Estate Tax Return Is Filed A-95

C. Generation-Skipping Transfer (GST) Tax Issues A-95
D. Basis Adjustment for Trust Assets A-96

X. Advanced Planning Options A-97

A. Deferral Mechanisms in a NIMCRUT A-97
B. Real Estate in a Charitable Remainder Trust to Generate Passive Income A-98
C. Charitable Remainder Trust with a Charitable Purpose A-98

XI. Charitable Remainder Trust History A-99

A. Legislative History A-99
1. Charitable Remainder Trust Provisions Added to Code, Effective Date, and Grandfathering A-99
2. Valuation Rules and Minimum Remainder Requirements A-100
3. Pre-1986 Fiscal Year Rules A-100
4. Non-Application of Throwback Rules and Former §644 A-100
5. Alternative Minimum Tax Provisions Before 1993 A-100
6. Pre-2007 Unrelated Business Income Tax and Reporting Rules A-100
7. Former and Transition Rules Applicable to Changes in the Capital Gains Rates (1997–2005) A-101

B. Prior Calculation Rules A-102
1. Treatment of Contingencies Before the Tax Reform Act of 1984 A-102
2. Deduction Calculations for Valuation Dates Before May 1, 1989 A-102
3. Deduction Calculations Before the Issuance of the Regulations Under §7520 A-102
4. Prior Marital Deduction Provisions A-103
5. Estate Tax Deduction for Successor Annuity or Unitrust Interests Before Boeshore A-103

XII. Charitable Gift Annuities: Introduction A-105

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

PAGE

A. Basic Concept A-105
B. Legislative Background A-105

XIII. Structuring the Gift Annuity A-107

A. Bargain Sale Treatment A-107
B. Setting the Annuity Rate A-107
C. One Life Annuities A-107
1. Calculating the Deduction A-107
2. Taxation of Annuity Payments A-108
3. Annuity Purchased with Appreciated Property A-109
4. Electing the Section 7520 Rate in Valuing the Annuity A-109

XIV. Deferred Gift Annuities A-111

A. Calculating the Deduction A-111
B. Taxation of Annuity A-111

XV. Gift Tax Rules A-113

A. One Life Immediate Gift Annuity A-113
B. Two Life Immediate Gift Annuity for Donor and a Second Person A-113
C. Deferred Gift Annuity A-113
D. Marital Deduction Gift Tax Issues A-113

XVI. Estate Tax Rules A-115

A. General Estate Tax Rules A-115
B. Marital Deduction Estate Tax Issues A-115

XVII. Taxation of Charitable Organization Issues A-117

XVIII. Generation-Skipping Transfer Tax Considerations A-119

XIX. Sophisticated Charitable Gift Annuity Structures A-121

XX. Early Termination A-123

XXI. Planning Options A-125

XXII. Introduction and Summary of Requirements A-127

XXIII. Specific Requirements for Qualification A-129

A. Contribution of Remainder Interests A-129
1. Qualified Organizations A-129
2. Only One Remainder Beneficiary A-130
3. Alternative Remainder Beneficiary A-130
B. Retention of Income Interest A-130
1. Duration of Income Interest A-130
2. Concurrent or Successive Life Beneficiaries A-130
3. Revocation of Income Interests A-130

PAGE

4. Charitable Remainder Beneficiary as Income Beneficiary A-131
C. Commingling of Property A-131
D. Investment Prohibitions A-131
1. Tax-Exempt Securities A-131
2. Depreciable and Depletable Assets A-131
E. Maintenance of the Fund A-132
F. Who May Serve as Trustee A-132
G. Income Realized by the Income Beneficiary A-133
1. Amount of Income — Unit Plan A-133
2. Calendar Year Requirement A-134
3. Partial Years A-134
4. Transfers Between Determination Dates A-134
5. Testamentary Transfers A-134
6. Partial Allocation of Income to Charity A-135
H. Termination of Life Income Interest A-135
I. Death Taxes A-135

XXIV. Type of Property Contributed to or Held by a Pooled Income Fund A-137

A. Property Subject to an Indebtedness A-137
B. Tangible Personal Property A-137
C. Depreciable Property A-137

XXV. Valuation of Income and Remainder Interest A-139

A. Computation of the Present Value of the Life Income Interest A-139
B. Computation of Present Value of Remainder Interest A-141

XXVI. Amending the Governing Instrument A-143

A. Fund Created After May 6, 1971 A-143
B. Funds Created Before May 7, 1971 A-143

XXVII. Tax Considerations A-145

A. Taxation of the Fund A-145
B. Income Tax Charitable Deduction A-146
C. Estate Tax Charitable Deduction A-147
D. Gift Tax Charitable Deduction A-148
E. Generation-Skipping Transfer (GST) Tax A-148
F. Taxation of the Beneficiary A-148
G. Tax on Capital Gains A-148
H. Private Foundation Rules A-149

XXVIII. Securities Law A-151

A. Philanthropy Protection Act of 1995 A-151
B. Disclosure Statement A-152
C. State Blue Sky Considerations A-152

XXIX. Planning Considerations A-153

A. Advantages A-153

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

		PAGE
	B. Disadvantages	A-153
	C. Practical Considerations	A-153
XXX.	Drafting Considerations	A-155
XXXI.	Filing Requirements	A-157
	TABLE OF WORKSHEETS	B-1

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

DETAILED ANALYSIS

Part 1: Charitable Remainder Trusts

I. Introduction and Definitions

Properly implemented, a charitable remainder trust (CRT) is one of the most powerful tax planning mechanisms in the Code. There are other statutory tax deferral mechanisms, such as §1031[1] exchanges for real estate, but no other code section offers so many options for both deferral of income and a charitable deduction. While CRTs can be complex, the gain deferral and deduction on the way to fulfilling the donor's charitable goals represent a worthwhile trade-off. The IRS has thoughtfully provided annotated sample documents that cover most of the possible permutations of the CRT, easing the drafting process and highlighting the optional provisions and their tax consequences.

This Portfolio outlines the basic requirements for the creation and administration of a qualified CRT and summarizes the relevant income, gift, estate, and generation-skipping transfer tax considerations, as well as the private foundation prohibitions that relate to qualified CRTs. The Portfolio also includes practical ideas for use of CRTs to meet donors' charitable, tax, and financial goals. CRTs were added to the Code in 1969 to better synchronize the amounts to be received by charity with the deduction allowed to the donor.[2] For those interested, or to assist in the interpretation of older documents, historical aspects of CRTs are covered at the end of the section. More detailed discussions of related tax issues are found in the Tax Management Portfolios covering income, estate, gift, and trust taxation. Throughout this Portfolio reference will be made to such Portfolios where appropriate.

A few basic terms are defined initially:

- A charitable remainder annuity trust (CRAT) pays the noncharitable beneficiary a fixed percent or amount for a term of years or the lifetime of one or more beneficiaries.
- A charitable remainder unitrust (CRUT) pays the noncharitable beneficiary a percent of value of the trust recalculated annually. In addition, a unitrust may permit the following variations on the standard percentage calculation of the amount distributable.
- A unitrust may provide for the payment of the lesser of the fixed percentage or the trust accounting income (a "net income only" unitrust or NICRUT).
- A net income unitrust may provide that any amount by which the trust's accounting income falls short of the fixed percentage is to be distributed in future years to the extent the trust's accounting income exceeds the fixed percentage in the later years (a "net income with make-up" charitable remainder unitrust or NIMCRUT).
- Also permitted are "flip" unitrusts. Such unitrusts start out as a NICRUT or NIMCRUT, and then "flip" into a regular unitrust payment upon the occurrence of a triggering event (FLIP-CRUT).[3]

---

[1] Section references are to the Internal Revenue Code of 1986, as amended, and the regulations thereunder, unless otherwise indicated.

[2] Before the Tax Reform Act of 1969, Pub. L. No. 91-172, a donor might establish a trust, retain the income rights, and then invest the trust principal in risky high-yield bonds. The amount received by the donor might substantially exceed the hypothetical value of the retained interest using the standard rates for valuation. When GRATs and GRUTs were added to the Code (§2702) by the Small Business Job Protection Act of 1996 (SBJPA), they were modeled on CRATs and CRUTs. Pub. L. No. 104-188.

[3] "Flip" unitrusts are authorized by Reg. §1.664-3(a)(1)(i)*(c)*.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

II. When Should a Donor Consider a Charitable Remainder Trust as Part of His or Her Tax Planning?

Given the variety of financial and personal situations, there are no hard-and-fast rules for the right time and place for a CRT. The two minimum essential ingredients for a successful CRT are charitable intent and willingness of the donor to abide by the applicable operating rules. The following are some situations where a CRT may be appropriate.

A. When the Donor Has Charitable Intent

The need for this cannot be overstated. Although some taxpayers may be initially intrigued by the tax deferral available through a CRT, if they lack charitable intent eventually the trade-off between deferral and compliance will begin to irritate them, especially as the initial tax benefits fade in the rear-view mirror. For those donors who have reached that point, see the section on terminating charitable remainder trusts at VIII., below.

B. When the Donor Has an Appreciated Asset that Can Be Sold

In the current tax system, excluding gain from current income is more valuable to individuals than a deduction of the same amount, given the various deduction limitations. A properly implemented CRT will provide both the gain exclusion and an income tax deduction. Although C corporations are not subject to the same deduction limitations, closely held corporations selling an appreciated asset may find a CRT appropriate.[4]

C. When the Donor Can Benefit from an Income Tax Deduction

A current income tax deduction is available for the present value of the remainder interest, even if the donor retains the right to change which charity receives the remainder interest.[5] Donors who are planning a testamentary charitable bequest should consider a CRT instead. The property will still pass to the charity at the death of the donor, but the donor receives an income tax deduction as well as an estate tax deduction, while retaining a life income stream.[6]

D. When the Donor Would Benefit from an Additional Source of Retirement Income

A NIMCRUT or FLIP-CRUT can defer income to the donor-beneficiary until the date the donor expects to retire, thus allowing tax-free accumulation without qualified-plan or IRA-contribution limits.[7] Also, unlike qualified plans and IRAs, a NIMCRUT or FLIP-CRUT allows the accumulated income to retain its character as qualified dividends and capital gains upon eventual distribution.[8]

E. When the Donor Would Benefit from a Regular Flow of Income

CRTs can be a dependable source of income for life or a term of years. A CRT can provide income to a donor for his or her lifetime, or to one or more individuals for their lives or a term of years (i.e. during a child's or grandchild's college years).[9]

F. When Diversifying or Otherwise Managing a Publicly Traded Stock Portfolio

A donor can transfer appreciated stock to a charitable remainder trust as part of a diversification or rebalancing plan, where the stock can be sold in a tax-exempt environment. It is not generally necessary to create a new trust each time: additional securities can be contributed to existing CRUTs.[10]

G. When Selling, or Retiring from, a Closely Held Business

If the business is to be sold, a donation to a CRT before the sale commitment can be beneficial for the seller without impairing the sale from the purchaser's perspective. A CRT can also be a mechanism for passing control to the next generation: the donor contributes stock, then the corporation redeems the stock from the CRT. The younger generation's ownership percentage increases without a taxable gift, and the departing owner has the income from the CRT for retirement.[11] If some or all of the business is sold to an ESOP, some or all of the qualified replacement property under §1042 can be contributed to a CRT (as long as the trustee is not obligated to sell the property).[12]

H. When Planning a Sale of Real Estate

CRTs can be funded with real estate or real estate partnerships, although debt on the property may preclude its eligibility for funding a CRT.[13]

I. When Funding a Private Foundation that Needs Time to Set up Operations

Establishing a short-term CRT instead of making an immediate large donation can allow the private foundation to be ready to operate by the time the funds arrive from the CRT. The CRT can always release funds early to the private foundation.[14]

---

[4] See IV.A.10., below, for more about corporate charitable remainder trusts.

[5] See IV.F., below, for more about choosing the remainder charity.

[6] See IV.H., below, for the calculation of the charitable deduction.

[7] See IV.C., below, for more about NIMCRUTs and FLIP-CRUTs.

[8] See VI.F., below, for taxation of beneficiaries of charitable remainder trusts.

[9] See IV.E., below, discussing the selection of a term and beneficiaries for the trust.

[10] See VI.H., below.

[11] See VI.G.2.c., below, for the details of this transaction.

[12] *See* PLR 9715040 (no gain recaptured under §1042 on contribution of qualified replacement property resulting from sale to ESOP where trustee of CRAT was not obligated to sell such property).

[13] See IV.A.2., below, for more about contributing debt-financed property.

[14] See VI.C.4., below, for more on early distributions to charity. See VIII.B., below, for a discussion of early termination of the trust by donation of the income interest.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

J. When a Closely Held Entity Is Selling an Appreciated Asset

The tax and philanthropic advantages of a CRT are not limited to individuals; any entity can fund a CRT.[15]

K. When the Donor Would like to Provide Income for Another Individual

Either a testamentary or inter vivos CRT may be considered if the donor desires lifetime or term income for one or more individuals in a trust form that is not subject to invasion by the beneficiary (e.g., surviving spouse, long-term employee).[16]

If the donor desires an invasion power for his or her surviving spouse but is concerned about successor beneficiaries' invasion of trust principal, a testamentary or inter vivos qualified terminable interest property (QTIP) trust can convert to a CRT on the death of the surviving spouse. The spouse will then have maximum invasion power (i.e. for medical expenses), but successor beneficiaries will be precluded from invading principal.[17]

L. When the Donor Has a Large IRA but Desires to Control Income Stream Payable After Death

If an individual has a large IRA and is concerned that the named beneficiary might withdraw all the funds immediately after the owner's death, the IRA-owner can designate a CRT as the beneficiary of the IRA. The IRA will have to be paid to the CRT within five years or ten years, as the case may be, of the owner's death, as a CRT cannot be a "designated beneficiary." However, the IRA distribution is tax-free when received by the CRT, and the beneficiary will only receive the CRT distributions as dictated by the document.[18]

A testamentary CRT may also be suitable in lieu of naming an older individual as the beneficiary of an IRA, especially if the beneficiary might outlive the standard life expectancy tables. The testamentary CRT does preclude a surviving spouse from treating the IRA as his or her own IRA, but that treatment may not be desirable anyway. The CRT can continue for the life of the beneficiary or beneficiaries in a tax-deferred environment, whereas the IRA would otherwise need to make ever-larger distributions as the beneficiary ages.[19]

The Consolidated Appropriations Act, 2023 provides taxpayer the opportunity to make a one-time qualified charitable distribution of up to $50,000 (adjusted for inflation) from taxpayer's IRA to a split-interest entity.[20] Split interest entity is defined by §408(d)(8)(F)(ii) as (i) a charitable remainder annuity trust if such trust is funded exclusively by qualified charitable distributions, (ii) a charitable remainder unitrust if such unitrust is funded exclusively by qualified charitable distributions, or (iii) a charitable gift annuity if such annuity is funded exclusively by qualified charitable distributions and commences fixed payments of 5% or greater not later than one year from the date of funding. This definition effectively prevents addition of the one-time $50,000 qualified charitable distribution to an existing split-interest entity with existing corpus or making additions to the split-interest entity after funding. Although the $50,000 limitation may seem like too little money for too much hassle and expense in setting up a CRAT or CRUT, spouses may each make a $50,000 election into the same CRAT or CRUT; however, no person other than the taxpayer and the taxpayer's spouse may hold an income interest in the split-interest entity, and the income interest may not be assignable.[21] A qualified charitable distribution to a charitable remainder trust is treated as ordinary income in the hands of the noncharitable beneficiary, and such distribution to a charitable gift annuity is not treated as an investment in the contract (and, therefore, tax-free) under §72(c).[22]

Editor's Note: Although the $50,000 ($55,000, effective Jan. 1, 2026) election is a taxpayer-friendly provision, time may prove it to be a fairly unused election because many clients may be reluctant to expend the time for and endure the expense of creating the CRAT or CRUT. Taxpayers may be more likely to utilize the election in conjunction with a charitable gift annuity, rather than a charitable remainder trust, due to the cost-savings in making the qualified charitable distribution to a charitable gift annuity. For discussion of other planning options with charitable gift annuities, see XXI., below.

---

[15] See IV.A.10., below, for a discussion of specific issues pertaining to corporations.

[16] See IV.E., below, discussing the selection of a term and beneficiaries for the trust.

[17] See 843 T.M., *Estate Tax Marital Deduction*, for further discussion of the marital deduction and marital trust structuring.

[18] See V., below. *See* PLR 9634019 (death benefit payable to CRT; benefit was income in respect of a decedent, but only taxable to beneficiaries when distributions made from the trust).

[19] See 367 T.M., *IRAs*, for further discussion of the IRA rules.

[20] §408(d)(8)(F), *added by* the Consolidated Appropriations Act, 2023, Pub. L. No. 117-328, §307 (effective for distributions made in taxable years beginning after December 29, 2022). *See also* §408(d)(8)(G) (adjusting $50,000 amount for inflation). Effective Jan. 1, 2026, the distribution amount is $55,000. Notice 2025-67.

[21] §408(d)(8)(F)(iv).

[22] §408(d)(8)(F)(v).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

III. The Basic Structure of Charitable Remainder Trusts

A. Description

A charitable remainder trust (CRT), as defined in §664, must provide for the distribution of a specified payment, at least annually, to one or more persons (at least one of which is a noncharitable beneficiary). The payment period must be for the life or lives of the individual beneficiaries (all of whom must be living at the time the trust is created) or for a term of years, not exceeding 20.[23] Upon the termination of the noncharitable interest or interests, the remainder must either be held in continuing trust for charitable purposes or be paid to or for the use of one or more organizations described in §170(c).[24] A qualified charitable remainder trust is exempt from income tax, and the grantor is entitled to an income, gift, and/or estate tax charitable deduction based on the present value of the remainder interest ultimately passing to charity.

There are two basic types of qualified CRTs: charitable remainder annuity trusts (CRATs) and charitable remainder unitrusts (CRUTs).

A substantial portion of the tax return of a CRT is publicly available.[25] Therefore, omitting identifying information in the name of the trust may be advisable.

A CRAT is required to pay a sum certain annually to one or more beneficiaries, at least one of which is not a charity. The payment must be equal to at least 5% but not more than 50% of the net fair market value of the assets on the date they are contributed to the trust.[26]

A CRUT is required to pay a fixed percentage of its net fair market value at least annually to one or more beneficiaries, at least one of which is not a charity. The fixed percentage must be equal to at least 5% but not more than 50% of the net fair market value of the trust assets as valued annually.[27] Thus, the amount paid by a unitrust fluctuates from year to year with the value of the trust assets, whereas the amount distributable from an annuity trust remains constant from year to year. In addition, a unitrust (but not an annuity trust) may permit variations on the standard percentage calculation of the amount distributable. For example, a unitrust may provide for the payment of the lesser of the fixed percentage or the trust accounting income (a "net income only" unitrust or NICRUT). A net income only unitrust trust may include a provision to distribute accounting income in excess of the stated percentage, to the extent of any prior accumulated shortfall when trust accounting income was less than the stated percentage (a "net income with make-up" unitrust or NIMCRUT). Also permitted are "flip" unitrusts (FLIP-CRUT). Such a unitrust starts out with a "net income only" requirement, and then "flip" into a regular unitrust payment upon the occurrence of a triggering event.[28]

[23] The trust can be designed to terminate earlier than its stated term if certain events occur. See the discussion of qualified contingencies at IV.E.7., below.

[24] §664(d)(1), §664(d)(2).

[25] §6104(b). Beneficiary information is not disclosed, so leaving the beneficiary's name out of the name of the trust can preserve donor privacy.

[26] §664(d)(1)(A).

[27] §664(d)(2)(A).

[28] Reg. §1.664-3(a)(1)(i)*(c)*.

To be a qualified charitable remainder trust, the trust instrument must satisfy all of the requirements set forth in §664 and the regulations thereunder.[29] The failure to incorporate one of the mandatory provisions will prevent the trust from qualifying under §664. In addition, failure to administer the trust as a charitable remainder trust will retroactively disqualify the trust.[30]

The IRS has published revenue procedures with sample instruments for inter vivos and testamentary charitable remainder annuity and unitrusts, including "net income only" unitrusts,[31] which incorporate the mandatory provisions and serve as a convenient starting point for drafting. The revenue procedures provide that the IRS will recognize a trust as satisfying the requirements of §664(d)(1), §664(d)(2), or §664(d)(3) if: (1) the trust operates in a manner consistent with the terms of the trust instrument; (2) the trust is a valid trust under applicable local law; and (3) the trust instrument is substantially similar to the sample in the appropriate revenue procedure (or properly integrates one or more alternate provisions from the revenue procedure into a document substantially similar to the sample in the revenue procedure).

The IRS has stated that it will no longer issue rulings on whether trusts that substantially comply with the requirements of the applicable revenue procedures qualify under §170, §664, and §2522.[32] The IRS will, however, continue to consider requests for rulings regarding trusts that do not substantially comply with the requirements of the revenue procedures.[33] In addition, a taxpayer may request a ruling to obtain an actuarial factor necessary to calculate the present value of the remainder

[29] Rev. Rul. 72-395, Rev. Rul. 80-123, Rev. Rul. 82-128, Rev. Rul. 88-81.

[30] Reg. §1.664-1(a)(4); *Estate of Atkinson v. Commissioner*, 115 T.C. 26 (2000); Notice 94-78. Note that the Tax Court in *Atkinson* did not explain the various tax consequences of retroactive disqualification. Therefore, it is not clear how taxable income in otherwise closed years should be treated and whether the trustee must amend all returns filed.

[31] See Worksheet 2 for a list of the Revenue Procedures, including the description of the type of trust in each sample document. The IRS provided updated sample annuity trust forms in Rev. Proc. 2003-53, Rev. Proc. 2003-54, Rev. Proc. 2003-55, Rev. Proc. 2003-56, Rev. Proc. 2003-57, Rev. Proc. 2003-58, Rev. Proc. 2003-59, and Rev. Proc. 2003-60. *See also* Rev. Proc. 2016-42 (alternative CRAT language to satisfy 5% probability of exhaustion test). The updated sample unitrust forms are in Rev. Proc. 2005-52, Rev. Proc. 2005-53, Rev. Proc. 2005-54, Rev. Proc. 2005-55, Rev. Proc. 2005-56, Rev. Proc. 2005-57, Rev. Proc. 2005-58, and Rev. Proc. 2005-59.

[32] This proscription is found in the third annual revenue procedure, which lists the "no ruling" areas, published in the first annual Internal Revenue Bulletin. Additional information is provided in the revenue procedures containing the sample charitable remainder trust forms.

[33] *See, e.g.*, Rev. Proc. 2003-53, §3. An example would be a trust with three life income beneficiaries, as in PLR 9117038. Because the rules governing charitable remainder trusts are extremely technical and gifts to such trusts are irrevocable, where possible a grantor may wish to request and obtain a favorable private ruling from the IRS regarding the qualification of the trust before funding. The first annual revenue procedure published in the first annual Internal Revenue Bulletin establishes the procedures to be followed in obtaining a ruling from the IRS. The IRS will not generally issue a ruling with respect to hypothetical situations or alternative plans. The IRS imposes a user fee for such rulings. In PLR 201935013, the IRS rejected an attempt by a charitable remainder trust to use Form 1023, *Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code*, to determine its qualification in lieu of a private letter ruling.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

interest for purposes of determining the applicable charitable deduction.[34]

The sample annuity trust and unitrust instruments issued by the IRS in 2003 and 2005 include a number of common alternative provisions. For example, Rev. Proc. 2003-55, Rev. Proc. 2003-56, Rev. Proc. 2005-54, and Rev. Proc. 2005-55 contain an alternative provision by which the donor of a two-life inter vivos trust retains the right to revoke the interest of the surviving noncharitable beneficiary. Also, all of the sample trust instruments issued in 2003 and 2005 apply only the private foundation provisions commonly applicable to charitable remainder trusts; the annotations explain when it is necessary to apply two other private foundation provisions.[35] Although the sample trust instruments continue to illustrate only quarterly payments, the annotations explain how the annuity and unitrust payments may be made in some manner other than quarterly. Rev. Proc. 2003-54, Rev. Proc. 2003-58, Rev. Proc. 2005-53, and Rev. Proc. 2005-57 provide sample term-of-years annuity trust and unitrust instruments.

For illustrations of the charitable remainder annuity trusts in Rev. Proc. 2003-54 and Rev. Proc. 2003-53, see *Charitable Remainder Annuity Trust — Term of Years* and *Charitable Remainder Annuity Trust — One Life*, respectively, in the Bloomberg Tax Transactional Diagrams Library.

B. Tax Consequences

The creation of a qualified CRT has significant tax consequences. The grantor of an inter vivos trust is entitled to an immediate income[36] and gift[37] tax charitable deduction for the present value of the remainder interest ultimately passing to charity. The creation of the income interest may, however, have gift tax consequences if the recipient is an individual other than the grantor. The creation of a testamentary charitable remainder trust entitles the testator's estate to an estate tax (but not an income tax) charitable deduction for the present value of the remainder interest.[38]

The funding of a CRT with appreciated property will not result in a capital gain to the grantor unless the grantor receives property in exchange (other than retention of an annuity or unitrust amount), property transferred to the trust has indebtedness in excess of its basis,[39] or the assignment of income doctrine applies because the sale of the contributed property to a specific buyer had been negotiated and was practically certain to occur.[40]

A qualified CRT is a tax-exempt entity, but that does not mean it will never have to pay a tax. Section 664(c)[41] provides that a CRT is not subject to income tax but is subject to a 100% excise tax on any unrelated business taxable income the trust has during a taxable year.[42] This amendment replaced the former §664(c) rule that took away the income tax exemption of a charitable remainder trust for any year in which the trust had unrelated business taxable income.[43]

The tax treatment of distributions from a charitable remainder trust is determined pursuant to §664(b) and the regulations thereunder.[44] The provisions of §664 and the regulations thereunder supersede all other provisions of Subchapter J (Estates, Trusts, Beneficiaries, and Decedents).[45]

[34] Reg. §1.664-4(b). See the discussion of the valuation of the remainder interest at IV.H., below.

[35] See the discussion of the applicability of the private foundation rules to charitable remainder trusts at VI.G., below.

[36] §170(f)(2)(A).

[37] §2522(c)(2)(A). A gift tax deduction is not needed if the gift is incomplete; if no taxable gift has been made, no deduction is needed. In many CRTs, the charitable gift is incomplete because the donor has retained the right to change the remainder charity.

[38] §2055(e)(2)(A).

[39] Rev. Rul. 55-275. *See also* Reg. §1.1011-2.

[40] *See, e.g., Estate of Hoensheid v. Commissioner*, T.C. Memo 2023-34; *Chrem v. Commissioner*, T.C. Memo 2018-164. For a detailed discussion of assignment of income issues, see IV.A.7., below.

[41] Effective for taxable years beginning after 2006, the Tax Relief and Health Care Act of 2006 (TRHCA), Pub. L. No. 109-432, §424.

[42] Section 664(c) is discussed in more detail in VI.C.3., below.

[43] Under the former rule, the trust was subject to tax as if it were a complex trust in any year in which the trust realized unrelated business taxable income. See discussion in XI.A.6., below.

[44] Taxation of recipients of distributions is discussed in more detail in VI.F., below.

[45] §664(a).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

IV. Establishing an Inter Vivos Charitable Remainder Trust

A. *What Types of Assets Are (or Are Not) Suitable for Charitable Remainder Trusts?*

1. *Publicly Traded Securities and Cash*

Publicly traded securities and cash are the easiest assets to use for charitable remainder trust (CRT) funding, as they are for other charitable transfers. There are no valuation issues, and the assets are easily transferred. Liquidity is immediately available to make the required payments to the beneficiaries. Gifts of appreciated marketable securities are even appealing to a donor who wants to retain the security in an individual portfolio. The appreciated securities can be sold immediately by the CRT without tax[46] and the donor can at the same time buy the same security on the stock market to replace the donated security but now with a new purchase price cost basis.[47] Non-publicly traded C corporation stock (restricted or closely held) may be a good donation, assuming there is a plan for eventual liquidity so that the payments can be made to the income beneficiary.[48]

2. *Real Estate and Real Estate Partnerships*

Real estate and real estate partnerships/LLCs that are not subject to debt can be donated and sold inside a CRT. If the real estate is not to be sold immediately, it may be advisable to use one of the alternative versions of the CRT discussed in IV.C., below.

If considering donating land with unharvested crops, only proceed after considering the assignment of income and associated self-employment issues.[49] Also consider that any business income earned by the trust would likely be unrelated business taxable income subject to the 100% excise tax, discussed below at VI.C.3.

Comment: The IRS issued proposed regulations that would define certain CRAT transactions, such as the type of transaction in *Furrer*, as listed transactions.[50] The IRS would define use of a charitable remainder annuity trust as a listed transaction if: (1) the grantor creates a CRAT and funds the trust with property having a fair market value in excess of its basis; (2) the trustee sells the contributed property and used some or all of the proceeds from the sale to purchase an annuity; and (3) on a federal income tax return, the beneficiary of the trust treats the annuity amount payable from the trust as if it were, in whole or in part, an annuity payment subject to §72, instead of carrying out to the beneficiary amounts in the ordinary income and capital gain tiers of the trust in accordance with §664(b).

3. *Art, Collectibles, and Other Tangible Personal Property*

Tangible personal property (e.g., art, collectibles) can be donated and sold in a CRT, but if a current tax deduction is desired the property must be sold before the end of the donation year.[51]

4. *Options*

Donations of options are challenging. Donations of compensatory options are likely to lead to unexpected, and unpleasant, tax outcomes.[52] A donation of options on real estate may be considered incomplete transfers and therefore ineffective as a donation, leading to disqualification of the trust.[53]

5. *Property Subject to Debt*

If property is subject to debt, it is generally not suitable for an inter vivos donation to a CRT.[54] The following issues may arise:

a. The bargain sale rules would trigger gain on donation.[55]

b. The income may be taxable as unrelated business income at a 100% tax rate. However, an exception may apply if the debt is sufficiently old.[56]

c. If the trust assumes or pays the debt, the trust will be a grantor trust, thus precluding treatment as a CRT.[57] Thus, encumbered property may not be transferred to a charitable remainder trust, unless: (1) the grantor is released from any personal liability for the debt before the property is transferred to the CRT; or (2) the encumbrance is otherwise removed from the property before the transfer. Depending on the flexibility of the lender, it may be possible

[46] The gain will go into the CRT capital gain tier.

[47] Both transactions can be done the same day: the wash sale rule of Code section 1091 applies only to losses, not gains.

[48] Payments may be made in kind, although making payments in kind triggers tax complications. See VI.B.2., below.

[49] *See* IRS AM 2020-006. *See also Furrer v. Commissioner*, T.C. Memo 2022-100 (where taxpayers engaged in transaction similar to that described in IRS AM 2020-006 by donating crops to CRATs and having CRATs purchase single premium immediate annuities (SPIAs), Tax Court held that annuity distributions to taxpayers were taxable as ordinary income; because taxpayers fully expensed crops on personal income tax returns, CRATs acquired from taxpayers had basis of zero in crops, CRATs realized ordinary income on sale of crops, and, therefore, CRATs' annuity payments to taxpayers could only be characterized as ordinary income, rather than return of principal). The court also ruled similarly to *Furrer* in a case involving the contribution of high-value, low-basis real property, followed by the trustee's sale of real property and purchase of SPIAs. *See Gerhardt v. Commissioner*, 160 T.C. 436 (2023) (court reiterated that "income earned [by CRATs] was relevant for determining the character of the distributions [the income beneficiaries] received" and that "nothing in [§]72 overrides their obligation to comply with the rules of [§]664(b) with respect to [the annuity income]"; court further reiterated that real property contributed to CRATs retained donors' basis, and did not book at fair market value of asset at date of contribution).

[50] Prop. Reg. §1.6011-15, REG-108761-22, 89 Fed. Reg. 20,569 (Mar. 25, 2024), would be effective on the date of publication of final regulations.

[51] PLR 9452026 (musical instrument gifted to CRAT was tangible personal property; no deduction available for remainder interest as long as taxpayer retained income interest in instrument, but income tax deduction would be allowed on sale of instrument). The self-dealing rules of §4941(d)(1)(E) would apply if the taxpayer continued to use the instrument after it was contributed to the trust. *See also* §170(a)(3).

[52] *See* PLR 9737014 (no income or gain on transfer of option, but on exercise of option optionee, if living, would recognize compensation income equal to excess of fair market value over exercise price).

[53] Rev. Rul. 82-197; PLR 9417005 (withdrawing PLR 9240017, which had approved the technique), PLR 9501004 (transfer to unitrust of option to purchase encumbered property would disqualify trust).

[54] *But see* PLR 199952071 (CRT funded with partnership units, followed by REIT conversion; debt allocation avoided by timing of donation).

[55] Reg. §1.1011-2.

[56] §514(c)(2)(B); Reg. §1.514(c)-1(b)(3).

[57] *See* PLR 9015049. This was a reversal of an earlier ruling policy that permitted the contribution of such property. *See* PLR 8931023, PLR 7807041.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

to partition the property and agree to limit the collateral to the non-donated portion.

d. Donating debt-financed property can trigger a self-dealing penalty, although an exception may apply if the transfer is the initial donation to the CRT.[58] Publicly traded partnerships and closely held partnerships with debt inside them are subject to the same rules and risks.[59]

6. Installment Notes

Transferring an installment note to a CRT is deemed a disposition by gift, and will trigger the gain inherent in the note.[60]

7. Assignment of Income Issues

A donation may be ineffective if the donor does not realize his or her charitable intent until a sale is too close to completion. If the CRT can be compelled to sell the donated asset (for example, because the donor has a binding agreement to sell the property), the donor will be taxed on the gain from the sale — although the donation is still a valid donation.[61] In *Hoensheid v. Commissioner*, the donor was taxed on gain attributed to shares in a closely-held corporation contributed to a donor-advised fund, even though only a non-binding letter of intent had been signed rather than a definitive purchase agreement.[62] The court reasoned that at the time of the gift, the sale was virtually certain to occur where there were no material unresolved sale contingencies. A grantor generally recognizes no gain on the transfer of appreciated property to an inter vivos charitable remainder trust.[63] However, in funding such a trust, a grantor may face the principles articulated in *Ferguson v. Commissioner*.[64] If *Ferguson* applies, then, pursuant to the assignment of income doctrine, if the right to receive the income inherent in the transferred property has ripened for tax purposes, the grantor who earned or created the right must recognize any income that results from that right, even if the grantor transfers the right to a charitable remainder trust before actually receiving the income. In a donation of closely held stock, it is permissible for the donated stock to be subject to a put right by the trustee or a right of first refusal by the issuer of the stock.[65] When considering such a donation, the donor (or the donor's advisors) should consider the redemption exception to the self-dealing rules discussed at VI.G.2.c., below.

Practice Note: As the Tax Court noted in *Rauenhorst v. Commissioner*,[66] there has been some contention over the anticipatory assignment of income doctrine in the context of charitable gifts of appreciated property. The IRS announced in Rev. Rul. 78-197 (acquiescing to *Palmer v. Commissioner*)[67] that it would treat the proceeds of a redemption of stock under facts similar to those in *Palmer* as income to the donor only if the donee is legally bound or can be compelled by the corporation to surrender the shares for redemption. In *Rauenhorst*, the Tax Court, although noting that the courts had not adopted the bright line test focusing on the donee's control over the donated property as devised by the IRS in Rev. Rul. 78-197, treated Rev. Rul. 78-197 as a concession by the IRS and applied the bright line test by deciding the case on the basis of whether the donees were legally obligated or could be compelled to sell stock warrants at the time of the assignments. Although the court in *Estate of Hoensheid* reiterated that it did not adopt a bright-line "legally-obligated" test, the court may have issued an opinion contrary to the holding in *Rauenhorst* and, therefore, may have broken away from the bright-line test and not treated Rev. Rul. 78-197 as a concession by the IRS. Given the result in *Hoensheid*, it is risky to proceed with a charitable transfer if a letter of intent is in place, even if denominated non-binding.

8. Assets Used by Related Parties

Because CRTs are subject to the same self-dealing rules as private foundations, assets that are being used by a disqualified person (generally, a related person) should not be transferred to a CRT until the use has terminated.[68] For example, personally owned real estate being used by the donor's closely held business should not be donated, as the use by the business would be an act of self-dealing subject to penalties (even if fair rent is being paid). However, property formerly used by the business may be an appropriate asset for a CRT. If a donor wants to sell a personal residence in a CRT, he or she must move out before the donation.

9. Illiquid Assets

Illiquid assets that are unlikely to be sold in the near future should not be donated to CRATs or to CRUTs that may be required to make payments to the beneficiaries before the assets are sold. A trust that must pay an annuity or unitrust amount to a beneficiary, and has no liquid assets, will have to make payments in kind of a fractional interest in the asset held by the trust. Valuation may be difficult if a fractional interest is involved, and gain will be triggered by the payment in kind.[69] If this type of asset is to be donated, consider one of the CRUT variations (i.e., a NICRUT, NIMCRUT, or FLIP-CRUT) discussed at IV.C., below. Alternatively, a combination of liquid and illiquid assets can be donated to avoid the problems triggered by payments in kind until the illiquid assets are sold.

[58] Reg. §53.4941(d)-1(a). See VI.G., below.

[59] *Goodman v. United States*, No. 98-8649, 1999 BL 3162 (S.D. Fla. 1999).

[60] Rev. Rul. 79-371, Rev. Rul. 76-530.

[61] Rev. Rul. 78-197.

[62] *Estate of Hoensheid v. Commissioner*, T.C. Memo 2023-34.

[63] Rev. Rul. 55-275.

[64] 174 F.3d 997 (9th Cir. 1999), *aff'g* 108 T.C. 244 (1997).

[65] In PLR 200321010, citing both *Palmer* and Rev. Rul. 78-197, the IRS ruled that the transfer by the donor of stock, subject to the issuer's right of first refusal, to a charitable remainder unitrust, followed by the redemption of the stock, did not result in income to the transferor. The IRS based its ruling on the fact that the issuer could not compel the charitable remainder unitrust to surrender the stock for redemption. The IRS also stated that the same rationale would apply if the charitable remainder unitrust sold the stock. See 863 T.M., *Charitable Contributions: Income Tax Aspects*, for more information.

[66] *Rauenhorst v. Commissioner*, 119 T.C. 157 (2002).

[67] *Palmer v. Commissioner*, 62 T.C. 684 (1974), *aff'd on other grounds*, 523 F.2d 1308 (8th Cir. 1975)).

[68] Reg. §53.4941(d)-1(a). See VI.G., below, for further discussion of the private foundation rules. But see PLR 200715015 for a permissible royalty structuring arrangement between a corporation and a private foundation.

[69] See discussion at VI.B.2., below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

10. Assets Owned by Corporation

Although CRTs can be established by any type of taxpayer,[70] special caution is indicated when a corporation (C or S) is considering funding a charitable remainder trust.

a. For C corporations, the charitable deduction is generally limited to 10% of taxable income.[71] For tax years beginning after 2025, any corporate charitable contribution must also exceed 1% of the corporation's taxable income for the year.[72] C corporations are allowed the same five-year carryforward as individual taxpayers are.[73]

b. Because corporations do not have a lifetime, the measuring term for a CRT funded by a corporation must be expressed in years.[74]

c. Either type of corporation must consider the effect of Reg. §1.337(d)-4 when planning a donation, including to a CRT. A corporation that transfers "substantially all" of its assets to a charitable entity, including a CRT, will trigger gain on the transfer.[75] The definition of "substantially all" is cross-referenced to the corporate reorganization provisions under §368(a)(1)(C). Partnerships are not subject to Reg. §1.337(d)-4, so no gain is triggered if a partnership donates "substantially all" of its property. If a partner has insufficient basis in his or her partnership interest, the partner's deduction for his or her share of the basis portion of donated property may be limited. The deduction for the appreciation portion is not so limited.[76]

d. A C corporation that converts to S status may not use any remaining charitable contribution carryforward against its Built-In Gains tax.[77] However, a recently converted S corporation may use a CRT to defer (or perhaps avoid) the Built-In Gains tax.[78]

S corporations pass any allowable deduction through to their shareholders, who include the passed through deduction with their own charitable deductions.[79] An S corporation shareholder's adjusted basis in the shareholder's stock is only reduced by the shareholder's pro rata share of the adjusted basis of the contributed property.[80] For 2017 and prior years, if the S shareholder was an electing small business trust (ESBT), the deduction was limited to the portion of the deduction that would be "out of income" if the trust had made the donation directly. The contribution is deemed to have been paid by the S portion of the ESBT pursuant to the terms of the trust's governing instrument, provided the other requirements of §642(c)(1) are met and the deduction is attributable to gross income of the S portion.[81] The "out of income" limitation precludes an ESBT from taking a charitable deduction for the unrealized appreciation in donated property on a pre-2018 tax return. The ESBT may or may not be entitled to a deduction for the basis portion of the donation, since the basis must be traceable to gross income.[82] Beginning in 2018, deductions passed through to an ESBT are deductible by the ESBT subject to the individual limitations and carryover provisions.[83]

B. Choosing a Charitable Remainder Annuity Trust, a Charitable Remainder Unitrust, or a Charitable Gift Annuity

Choosing between a charitable remainder annuity trust (CRAT) and a charitable remainder unitrust (CRUT) involves several factors, both technical and practical. Both types of trusts must value their assets every year. Both types require that the charitable remainder be at least 10% of the value of the property transferred as of the time that the trust is funded. Especially if a relatively small amount is involved, a donor desiring an annuity for one or two lives should consider a gift annuity.

1. Factors in Favor of a CRAT

a. Predictability. The income beneficiary knows exactly how much cash he or she will receive each year (unless the trust is depleted). CRUT payments will vary from year to year.

b. Simplicity for the trustee. The trustee does not have to recalculate the annual or quarterly distribution.

c. When compared to a charitable gift annuity, a CRAT allows a change of charitable beneficiary and is not subject to the creditor risk of the charity. Also, a gift annuity can only be for one or two lives, not a term of years or more than two lives.

d. The donor can retain the right to change the remainder charity; indeed, the tax law does not require the donor to inform the charity that the trust exists.

2. Factors in Favor of a CRUT

a. Payments will increase over time (assuming growth of the trust — which is obviously not guaranteed), potentially providing the donor with some inflation protection.

---

[70] *See* PLR 9205031 (corporation), PLR 9340043 (S corporation), PLR 9821029 (trust), PLR 199952071 (LLC).

[71] §170(b)(2)(A)(ii). Note that for cash contributions made during the 2020 and 2021 tax years, the 10% corporate limit is increased to 25%. Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. No. 116-136, §2205(a) (non-Code provision), as amended by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, Pub. L. No. 116-260, Div. EE, §213. A corporation may elect the application of the increased limitation, and a contribution is not required to be used in connection with the Coronavirus relief to be eligible for the increased percentage limitation. In the case of an S corporation, the corporate contributions are passed through to the shareholders and aggregated with the shareholder's own contributions. The CARES Act election for individuals increases the deduction limit for certain cash contributions to 100% of the individual's contribution base. That election must be made separately by each shareholder.

[72] §170(b)(2)(A)(i), added by the One Big Beautiful Bill Act (OBBBA), Pub. L. No. 119-21, §70426(a).

[73] §170(d)(2).

[74] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

[75] Reg. §1.337(d)-4(a)(1), §1.337(d)-4(c)(2)(ii).

[76] §704(d)(3)(B).

[77] §1374(b)(2). Because only net operating losses and capital losses are listed as allowable carryovers, all other potential carryovers (e.g., charitable, depletion) are unavailable.

[78] *See* PLR 200644013.

[79] Reg. §1.1366-1(a)(2)(iii).

[80] §1367(a)(2).

[81] Reg. §1.641(c)-1(d)(2)(ii).

[82] *See Van Buren v. Commissioner*, 89 T.C. 1101, 1109 (1987) ("Tracing is required since the statute specifically requires that the source of the contribution be gross income."); Rev. Rul. 2003-123.

[83] §641(c)(2)(E)(i).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

b. Certain variations on a CRUT are suitable for donations of illiquid assets that may not be sold before the first payment is due.[84] CRATs do not have the flexibility of waiting for the sale of the donated asset before beginning payments.

c. CRUTs and CRATs must both meet the minimum 10% charitable remainder value when funded. CRATs that use a measuring life for their term must also meet the "exhaustion test" discussed at IV.D.3., below. Due to the exhaustion test, in a low interest rate environment younger donors may not be able to establish a CRAT. CRUTs are not subject to this additional requirement.

d. CRUTs are less likely to run out of funds if there is an economic downturn. The payments may decrease, of course, but not to zero.

e. A significant difference between a unitrust and an annuity trust is that no additional contributions may be made to an annuity trust after the initial funding, whereas additional contributions can be made to a unitrust. If the donor might want to add assets later, a CRUT is probably a better alternative to creating additional CRATs (all other factors being equal).

f. As in the case of a CRAT, the donor can retain the right to change a CRUT's remainder charity.

3. *Factors in Favor of a Gift Annuity (in Lieu of a CRAT)*

a. Minimal cost is required to establish (no trust document required) and administer. Beneficiary receives a Form 1099-R each year rather than a trust Form K-1. For donors who like to file their tax returns promptly each year, this may be an important advantage because the Form 1099-R has a due date of January 31.

b. Assuming the charity is financially sound, there is no risk of a trust running out of principal should the donor substantially outlive his or her life expectancy.

c. No "5% exhaustion test" applies (unlike the CRAT situation).[85]

d. A gift annuity can be funded with S corporation stock, assuming the charity is willing to accept the stock. S corporation stock cannot be transferred to a CRT without terminating the S election.[86]

e. If the property transferred has significant basis, the CGA allows basis recovery over the beneficiary's expected lifetime, resulting in a portion of each payment being tax-free. In a CRT, basis is only recovered once all current and accumulated income (including capital gains) has been distributed.[87]

f. The self-dealing prohibition and other private foundation rules do not apply to CGAs.[88]

g. Although the donor cannot change the charity once the gift annuity is established, many donor-advised funds will issue gift annuities, effectively allowing the donor or a successor fund advisor to choose the charitable beneficiary.

C. *Opportunities with Illiquid Assets: NICRUTs, NIMCRUTs, and FLIP-CRUTs*

There are many situations where a donor would consider contributing an illiquid asset to a CRT. However, if the CRT were required to make payments to the beneficiary before the assets were to be sold, the payment would have to be made in kind and, thus, would trigger gain on the distribution.[89] Loss could be realized, but not recognized, as a trust and its beneficiary are related parties under §267(b)(6). The beneficiary would then have a fractional interest in an illiquid asset — and taxable income. This situation can be avoided by using one of three variations on CRUTs that are suitable for donations of illiquid assets. Which one is most appropriate will depend on the balance between the donor's charitable intent and his or her desire for income. The IRS sample documents include each of these variations:[90]

1. NICRUT (net income CRUT). This CRUT pays the recipient the lesser of the trust's net income or the stated percentage. This version would be chosen by a donor whose focus is on providing the maximum amount of remaining principal for the charity at the termination of the trust. It may also be suitable if the trust is funded with lower-yielding property that is expected to pass intact to the charity (e.g., real estate that will be used by the charity).

2. NIMCRUT (net income with make-up provision CRUT). The net income unitrust can include an optional "make-up" provision stating that if the income in any year exceeds the unitrust amount for the year, such excess is paid out to the extent necessary to make up for any shortfalls in prior years. This type of trust is often chosen if the donor expects that a significant amount of investment return will consist of post-contribution capital gains. Because post-contribution gains may be included in trust income, the "make-up" amount can be satisfied as investments are sold. This type of CRUT may also be chosen by a donor who does not currently need income but may want some in the future.[91]

3. FLIP-CRUT. The governing instrument may provide that the unitrust will use either the net income or net income with make-up provisions payout method for an initial period, and then "flip" to the fixed percentage method for the remaining portion of the term. The "flip" must be triggered "on a specific date or by a single event whose occurrence is not discretionary with, or within the control

[84] See IV.C., below.
[85] Rev. Rul. 77-374, discussed at IV.D.3., below.
[86] §1361(e)(1)(b)(iii).
[87] See VI.F.1., below, for taxation of beneficiaries.
[88] Private foundation rules are discussed at VI.G., below.
[89] Reg. 1.664-1(d)(5).
[90] See Rev. Proc. 2005-52, §6.07 for the NICRUT, §6.08 for the NIMCRUT, and §6.09 for the FLIP-CRUT. All sample CRUT Revenue Procedures include these variations.
[91] See X., below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

of, the trustees or any other persons."[92] Examples of such events (which must be specified in the governing instrument) include the sale of unmarketable assets, as well as marriage, divorce, death, or the birth of a child. The conversion date must be the beginning of the taxable year immediately following the year containing the date of the triggering event. Any remaining "make-up" amount is forfeited upon the conversion. This type of trust is often chosen when the CRUT is funded with an illiquid asset (e.g., land, closely held stock) but the donor would like a more consistent stream of income once the asset is sold.

Practice Point: The unmarketable asset to be sold does not have to represent any particular percentage of the trust corpus. A relatively small nonmarketable asset can be contributed and then sold when the "flip" is desired.

> *Example:* Donor establishes a FLIP-CRUT on January 1, 20X1, retaining a 6% unitrust interest for life, limited to trust accounting income until the January 1 following the "triggering event." The trust is funded with a tract of undeveloped land worth $500,000. The triggering event is defined as the sale of the land. No income is earned in 20X1 or 20X2, but the land is sold for $550,000 in January of 20X3. The trustee calculates the make-up amount as $60,000 ($500,000 × 6% × 2 years). The post-contribution gain is allocated to income by the trustee, allowing a make-up distribution of $50,000 to the donor. As of January 1, 20X4, the trust converts to a regular unitrust without an income limitation. To the extent that the remaining make-up amount of $10,000 cannot be paid during 20X3, it disappears.[93]

D. Setting the Annuity or Unitrust Rate

1. Minimum and Maximum Payout Rates

As long as the payout rate meets the criteria below, the donor is free to choose the payout rate. Although some donors retain the maximum payout, resulting in an exact 10% value for the remainder, other donors prefer to retain a smaller percentage, either to provide more for the remainder charity or to provide more investment cushion during challenging market conditions.

The annual annuity amount may not be less than 5% of the initial fair market value of the property placed in trust.[94] Similarly, the total fixed percentage payable by a unitrust to all beneficiaries may not be less than 5% of the fair market value of the trust property as revalued each year.[95] If the donor wants a smaller payout than 5% to the noncharitable beneficiaries, he or she can direct that a portion, but not all, of the annual payment be directed to a charity. This option is discussed below at IV.E.6.

The minimum amount rule will not be violated where the governing instrument of an annuity trust or a unitrust provides for a reduction of the stated amount or fixed percentage upon the death of a recipient or upon the expiration of a term of years, provided that: (1) a distribution of corpus is made to a §170(c) organization at the same time; (2) the total amount payable each year by the annuity trust after such distribution is not less than a stated dollar amount that bears the same ratio to 5% of the initial net fair market value of the trust assets as the net fair market value of the trust assets immediately after the distribution bears to the net fair market value of the trust assets immediately before the distribution; and (3) for a unitrust, the total percentage of trust assets payable is at least 5%.[96]

> *Example:* The initial net fair market value of the assets of CRAT T is $100,000. The annuity payment is $2,500 to each of J and B for life. Upon the death of the first to die, the trust is to distribute one-half of the then value of its assets to an organization described in §170(c) and continue to pay a $2,500 annuity to the survivor. J dies two years later, when the trust assets are still valued at $100,000. The minimum amount rule is not violated, because a distribution is made to a §170(c) organization upon the death of J, and at that time the amount payable to B ($2,500) will bear the same ratio (one-half) to 5% of the initial net fair market value of the trust assets ($5,000) as the net fair market value of the trust assets immediately after such distribution ($50,000) bears to the net fair market value of the trust assets immediately before such distribution ($100,000).[97]

The maximum annuity amount is 50% of the fair market value of the property placed in the annuity trust valued as of the date of transfer.[98] Similarly, the maximum payout percentage to noncharitable beneficiaries of a charitable remainder unitrust is 50% of the fair market value of the unitrust assets valued on the same date each year.[99]

It is possible that, as a result of an incorrect valuation of the trust property, a stated dollar annuity amount payable by an annuity trust may turn out to be less than 5% of the initial net

[92] Reg. §1.664-3(a)(1)(i)(c)(1). See also the sample CRUT Revenue Procedures.

[93] See VI.A.3., below, for further discussion of the calculation of the payment to the beneficiary.

[94] Reg. §1.664-2(a)(2)(i). The annuity amount may not vary. *See* IRS AM 2020-006 (addressing type of abusive transaction involving CRATs; where CRAT provided that income beneficiary would receive annuity equal to greater of "10% of the initial FMV of all property transferred to the trust or … the payments received by the trustee from one or more SPIAs purchased by the trustee," IRS ruled that CRAT would fail to qualify under §664(d)(1)(B) because income beneficiary would be entitled to payment in excess of amount determined at funding of CRAT and amount payable could change if CRAT purchased SPIA, thus violating sum certain requirement under Reg. §1.664-2(a)(1)). The IRS issued proposed regulations that would define certain CRAT transactions, such as the type of transaction in IRS AM 2020-006, as listed transactions. The IRS would define use of a charitable remainder annuity trust as a listed transaction if: (1) the grantor creates a CRAT and funds the trust with property having a fair market value in excess of its basis; (2) the trustee sells the contributed property and used some or all of the proceeds from the sale to purchase an annuity; and (3) on a federal income tax return, the beneficiary of the trust treats the annuity amount payable from the trust as if it were, in whole or in part, an annuity payment subject to §72, instead of carrying out to the beneficiary amounts in the ordinary income and capital gain tiers of the trust in accordance with §664(b). Prop. Reg. §1.6011-15, REG-108761-22, 89 Fed. Reg. 20,569 (Mar. 25, 2024), would be effective on the date of publication of final regulations.

[95] Reg. §1.664-3(a)(2)(i).

[96] Reg. §1.664-2(a)(2)(ii), §1.664-3(a)(2)(ii).

[97] Reg. §1.664-2(a)(5)(ii)*(e)* (indicating that total amount given to J and B must not be less than 5% of initial net fair market value of trust assets). For application of this rule to a unitrust, see Reg. §1.664-3(a)(5)(ii)*(e)*.

[98] §664(d)(1)(A).

[99] §664(d)(2)(A).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

fair market value of the property placed in trust. The regulations provide that the trust will be deemed to have satisfied the 5% requirement where the discrepancy is due to the good faith underestimation of the initial net fair market value of the property placed in trust by the grantor of an inter vivos trust. However, the IRS exacts a penalty from the grantor (who is permitted to correct the underpayment), requiring the grantor to consent, by agreement with the IRS, to accept an amount equal to 20 times the stated annuity as the fair market value of the property placed in trust for purposes of determining the appropriate charitable contribution deduction.[100]

Comment: The foregoing exception is specifically limited to inter vivos trusts. There is no compelling reason why a testamentary annuity trust should be denied the ability to correct the underpayment. A testamentary annuity trust, however, could attempt to remedy the situation by reformation under §2055(e)(3). Such reformations are discussed at V.E., below.

2. *The Minimum 10% Value of the Remainder Interest*

In addition, the present value of the remainder interest must be at least 10% of the initial net fair market value of the assets contributed.[101] Special rules apply where the sum certain is expressed as a fraction or percentage and the initial fair market value of the trust property is valued incorrectly.[102]

To ensure that the charitable remainder beneficiary receives a minimal portion of the property transferred to the trust, §664(d)(1)(D) and §664(d)(2)(D) require that, at the time the property is transferred to the trust, the value of the charitable remainder interest be at least 10% of the value of the property transferred to the trust.[103] The applicable §7520 rate is used to determine whether this minimum value requirement has been satisfied.[104]

The effect of the minimum 10% remainder interest is to limit the use of CRTs with very young beneficiaries or with several individual beneficiaries (unless they are all elderly).

> *Example:* A 5% unitrust for the life of a 23-year-old with quarterly payments (first payment to be three months after the valuation date), established when the §7520 rate is 3.2%, will have a remainder interest of only 8.2%, disqualifying the trust under §664(d)(2)(D).

In the case of trusts for two lives, the beneficiaries must be even older to satisfy the 10% remainder requirement.

> *Example:* A 5% unitrust, established under the terms described above for two lives, both of whom are age 36, will have a remainder value of only 8.4%, causing it to fail to qualify under §664.

The higher the payout rate, the older the beneficiary will have to be to satisfy the 10% requirement. Even if the donor retains the right to revoke potential successor beneficiaries' income rights, those rights are not disregarded in calculating the value of the remainder interest.[105]

An annuity trust must expressly prohibit additional contributions.[106] The governing instrument of a unitrust must either prohibit or permit additional contributions after the trust is funded.[107] If the governing instrument permits additional contributions, it must contain certain provisions for the calculation of the unitrust amount payable in the event additional contributions are made.[108] TRA '97 imposed a 10% minimum charitable benefit requirement on not only the original contribution to a unitrust but all subsequent contributions as well.[109] To avoid the possibility that an additional contribution to a unitrust created before July 28, 1997, will invalidate the entire trust, the IRS will treat any such contribution as being transferred to a separate trust.[110] The grantor will receive no charitable deduction for any such additional contribution that is treated as being contributed to the "separate trust."[111]

3. *The 5% Exhaustion Rule, Generally Applicable Only to CRATs for a Measuring Life*

The IRS takes the position that for income, estate, and gift tax purposes a deduction is not available for a gift of a remainder interest in trust where the probability that the charitable remainder beneficiaries will not receive any trust corpus exceeds 5% (the "probability of exhaustion test"). The basis for the IRS's position is found in both the estate and gift tax regulations, which provide that no deduction is allowable where a charitable transfer is subject to a condition "unless the possibility that the charitable transfer will not become effective is so remote as to be negligible."[112] The 5% benchmark appears to be derived from §2037 and §2042, both of which specify that 5% is the value at which a reversionary interest is sufficient to cause inclusion in the grantor's estate.[113] The IRS has also as-

[100] Reg. §1.664-2(a)(2)(iii).

[101] §664(d)(1)(D), added by the Taxpayer Relief Act of 1997 (TRA '97), Pub. L. No. 105-34, §1089(b). *See, e.g.*, PLR 201040021 (trust that did not satisfy §664(d)(1)(D) remainder interest requirement was never CRAT). According to the Conference Report on TRA '97, where a CRAT is created for the joint lives of two individuals, the trust will not fail to qualify as a CRT if the value of the remainder interest is less than 10% of the trust's assets at the death of the first of the noncharitable beneficiaries. The same result should obtain for a two-life CRAT where payments are made first to the donor and subsequently to a successor noncharitable beneficiary. H.R. Conf. Rep. No. 105-220, at 607 (1997).

[102] See the discussion at IV.D.1., above, regarding annuity trusts with stated dollar annuity amounts.

[103] This requirement, which was added by TRA '97, Pub. L. No. 105-34, §1089, is effective for transfers in trust made after July 28, 1997, subject to certain transition rules. Pub. L. No. 105-34, §1089(b)(6)(A). The requirement does not apply to wills executed on or before July 28, 1997, if the decedent died before January 1, 1999, without having republished or amended the will by codicil or otherwise. Pub. L. No. 105-34, §1089(b)(6)(B). The requirement also does not apply if the will was executed on or before July 28, 1997, and the decedent was, on July 28, 1997, under mental disability to change the disposition of his or her property and did not regain his or her competence before the date of his or her death. Pub. L. No. 105-34, §1089(b)(6)(B).

[104] §664(d)(1)(D), §664(d)(2)(D).

[105] *See Simmons v. United States*, 667 F.2d 832 (9th Cir. 1982), *aff'g* 80-1 USTC ¶9,287 (D. Ark. 1980).

[106] Reg. §1.664-2(b).

[107] As noted in IV.B.2., above.

[108] Reg. §1.664-3(b).

[109] *See* §664(d)(2)(D), added by Pub. L. No. 105-34, §1089(b)(1).

[110] §664(d)(4), added by Pub. L. No. 105-34, §1089(b)(4).

[111] §170, §664.

[112] Reg. §20.2055-2(b)(1), §25.2522(c)-3(b)(1).

[113] *See* Rev. Rul. 70-452.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

serted the 5% rule within the context of the income tax charitable deduction.[114]

In Rev. Rul. 77-374, a $400,000 testamentary annuity trust was to pay an annuity of $40,000 to a 61-year-old female for her lifetime. Upon the annuitant's death, the trust would terminate and the corpus be paid to a qualified charitable organization. The IRS disallowed any estate tax charitable deduction for the gift of the remainder interest, because the IRS determined that, using the 6% valuation tables and given the income beneficiary's age and the size of the annuity amount, there was more than a remote possibility that the trust would have no assets remaining upon termination. The ruling explains the calculations as follows:

> The mathematical formula used to determine the number of years it would take to completely exhaust a fund with an initial value of $400,000, invested at 6% per annum, that is subject to fixed annual payments of $40,000 out of both income and principal is: 1.06 × $400,000 (initial value of corpus) − $40,000 (fixed annual payment) = $384,000 (value of corpus at end of year after first invasion). By a series of similar successive computations (that is: 1.06 × $384,000 (value of corpus at end of first year) − $40,000 (fixed annual payment) = $367,040 (value of corpus after second invasion), it was determined that the original fund of $400,000 would be completely exhausted in less than sixteen years. Based on Table LN, which is found in section 20.2031-10(e) of the regulations, the probability that a female aged 61 … will survive to age 77 is greater than 63 percent. See example 12 contained in I.R.S. Publication 723A (12/70), "Actuarial Values II: Factors at 6 Percent Involving One and Two Lives." Thus, the entire estate tax charitable deduction was denied because the probability that the trust assets would be exhausted before the death of the annuitant was greater than 5%.

In a low interest rate environment, the income assumptions built into the valuation tables made it difficult to create a qualified CRAT except in the case of the oldest donors. The IRS responded to this issue in 2016 by providing an exception to the 5% probability of exhaustion test. In Rev. Proc. 2016-42,[115] the IRS provided language to be included in the governing instrument of a CRAT that could qualify as a qualified contingency under §664(f). If this language is included, the CRAT is exempt from the exhaustion test (although, of course, it must still meet the 10% remainder test). The language provided by the IRS causes an "early termination" contingency.[116] According to the contingency, if the value of the trust corpus minus the annual payment and multiplied by a specific discount factor falls below 10% of the initial trust corpus, the provision allows the trust to terminate early and immediately distribute the remainder to charity. The date of the contingent termination is the date immediately preceding the date of an annuity payment where such scenario would occur.

Rev. Proc. 2016-42 illustrates the necessary calculation with this example:

> On January 1, Year 1, Donor transfers property valued at $1,000,000 to Trust, an inter vivos trust providing for an annuity payment of $50,000 (5% of the value of the initial trust corpus) on December 31 of each year to S for S's life followed by the distribution of trust assets to Charity. Trust includes the precise language of the sample provision in Rev. Proc. 2016-42, §5, providing for an early termination contingency and specifies the §7520 rate in effect for January, Year 1, which is 3%. But for the early termination provision, Trust meets all of the requirements of §664(d)(1). In accordance with the revenue procedure, the IRS will treat the early termination contingency as a qualified contingency under §664(f). Therefore, the early termination provision does not cause Trust to fail to qualify as a CRAT under §664. In addition, Trust qualifies as a CRAT regardless of whether it passes the probability of exhaustion test on January 1, Year 1.
>
> Each year, prior to payment of the annuity to S, the trustee performs the calculations required to determine if Trust will terminate early in accordance with the terms of the qualified contingency. In each year from Year 1 through Year 17, the trustee determines that the value of the trust corpus, minus the $50,000 annual payment, and then multiplied by the specified discount factor, is greater than 10% of the initial trust corpus. The value of the trust corpus as of December 30 in Year 18 is $210,000. Only in Year 18 does the value of the trust corpus as of December 30, when reduced by the annuity payment and multiplied by the specified discount factor, fall below 10% of the value of the initial trust corpus. The calculations required to determine if Trust will terminate early in Year 18 are as follows:
>
> 1. $1,000,000 × 10% = $100,000
> 2. ($210,000 − 50,000) × $[1 / (1 + .03)]^{18}$
>
> $160,000 × $(1/1.03)^{18}$
>
> $160,000 × 0.970874^{18}
>
> $160,000 × 0.587397 = $93,984.
>
> Because the value of the trust corpus ($210,000), when reduced by the annuity payment ($50,000) and then multiplied by the specified discount factor (0.587397), is less than 10% of the value of the initial trust corpus ($100,000), Trust terminates on December 30, Year 18, and the principal and income remaining in Trust (including the annuity payment for

[114] Rev. Proc. 2016-42 ("If the probability that the life beneficiary or beneficiaries will survive exhaustion of the CRAT assets is greater than 5 percent, then the charitable remainder interest of the CRAT does not qualify for an income, gift, or estate tax charitable deduction and the CRAT is not exempt from income tax under §664(c).").

[115] The revenue procedure is effective August 8, 2016, and applies to trusts created after that date. The IRS provided language for both inter vivos and testamentary CRATs. The IRS explained in the revenue procedure that the 5% probability of exhaustion test is difficult to meet when interest rates are low and the trust is accruing less than it would in a high rate environment. As a result, the use of CRATs was limited as an effective charitable-giving vehicle.

[116] Qualified contingencies are discussed at IV.E.7., below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Year 18 that otherwise would have been payable to S) then must be distributed to Charity.

Practice Point: Although Rev. Proc. 2016-42 does allow a qualified CRAT to be created in a low interest environment, the same donors who want a steady payout from a CRAT may not be comfortable with the idea that the trust could terminate prematurely during a period of market turbulence. It is doubtful that anyone would wish to be the trustee in the example above who has to tell S that her expected $50,000 year-end payment will not be forthcoming? Such donors might consider instead a charitable gift annuity, where the annuity is payable from the general assets of a charity and, therefore, is neither subject to exhaustion nor the exhaustion test.

In 1982, the Tax Court[117] questioned the mathematical formula set forth in Rev. Rul. 77-374 and held that the "so remote as to be negligible" rule can be satisfied if the annual earnings of the trust exceed the required annual payout to the annuity or unitrust amount recipient. The Tax Court permitted a charitable estate tax deduction for the creation of two testamentary charitable remainder trusts because the trusts were invested in assets yielding more than the required payout, even though, using the then applicable 6% tables, the probability that the trust's assets would be depleted before termination exceeded 5%.

The 1997 enactment of §664(d)(1)(D) and §664(d)(2)(D), requiring that the actuarial value of the charitable remainder be at least 10%, must be considered in conjunction with the 5% exhaustion rule. Both rules have the same intent — to ensure that the charity will receive more than a de minimis amount at the termination of the trust. Although any trust failing the 10% remainder requirement may also fail the 5% exhaustion rule, the converse is not always true. Thus, if a trust satisfies the 10% remainder requirement, it is still necessary to determine whether the 5% exhaustion requirement has been satisfied. The commercial software calculators used by most advisors will highlight this issue when performing a CRAT calculation. At any time when the §7520 rate exceeds the annuity rate, the trust will pass the exhaustion test, as the calculations presume that the trust is earning more than it is paying out. The trust may even fail the 5% test when the §7520 rate equals the annuity rate if payments are made more frequently than annually.

Example 1: Grantor, age 60, created a charitable remainder annuity trust with $1,000,000 in which he retained a 5% annuity, payable annually on the last day of each year, for life. The transfer was made in a month when the best available §7520 rate was 2.4%. The value of the remainder interest is $156,955, which means that the trust passes the 10% remainder test. However, the probability that Grantor will survive 28 years, when the fund will be exhausted, is 34.63%. The trust fails the 5% exhaustion test, and no gift tax deduction is allowed. Unless the §7520 rate rises significantly, this donor will not be able to create a CRAT for the donor's lifetime, although a CRUT or a term CRAT are possible.

Example 2: Grantor, age 70, created the same trust. The value of the remainder interest is $386,180 per the IRS tables, well above the required 10% minimum. The probability of the grantor's surviving to the exhaustion of the trust is only 4.91%, so the 5% probability test is passed.

In 1995, the IRS issued regulations under §7520 that contain a different exhaustion rule applicable to charitable remainder annuity trusts, in which the annuity interest is measured by a life. The regulations are effective for transfers made after December 13, 1995.[118] Rather than replacing the 5% exhaustion rule, the regulations create a parallel rule that affects the valuation of the deductible charitable remainder interest if the measuring life outlives his or her life expectancy. This rule explicitly applies for income, gift, and estate tax purposes. The regulations provide that, in the case of an annuity interest for life, the annuity interest may not be valued under the regular §7520 method when the trust corpus will be exhausted if the measuring life lives to age 110.[119] The reasoning given in the regulations for this rule is that "the annuity is not considered payable for the entire defined period if, considering the applicable section 7520 interest rate on the valuation date of the transfer, the annuity is expected to exhaust the fund before the last possible annuity payment is made in full."[120]

To determine whether the fund will be exhausted by age 110, it is necessary to multiply the applicable term annuity factor for the difference between the annuitant's age and age 110 by the amount of the annuity. If this results in a value for the annuity that exceeds the value of the fund, the exhaustion rule applies and a special method must be used to value the annuity.[121] This method requires determining the number of payments that can be made before exhausting the fund, and then calculating the present value of those payments, taking into consideration the fact that they may end at the earlier death of the measuring life. This will result in a smaller value for the annuity (and a larger deduction for the remainder) than avails under the regular §7520 valuation method.

Example 3: Using the same facts as in Example 2, above, it is determined that the $50,000 annuity will exhaust the trust fund in 28 years, when Grantor is age 98. The present value of the payments received up to the date of exhaustion (also taking into consideration Grantor's possible earlier death) is $610,147. The value of the remainder is $389,853, which is $3,673 greater than the value of $386,180 determined under the usual method.

Comment: The IRS has not approved this method for valuing a charitable remainder interest, although the Example follows the calculation described in Reg. §25.7520-3(b)(2)(v)(E). The example in the regulations is concerned with the valuation of a charitable lead annuity interest, and the intent of the ex-

[117] *Estate of Moor v. Commissioner*, T.C. Memo 1982-299.

[118] Reg. §1.7520-3(c), §20.7520-3(c), §25.7520-3(c), *as amended by* T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023), applicable on or after June 1, 2023.

[119] Reg. §1.7520-3(b)(2)(i), §20.7520-3(b)(2)(i), §25.7520-3(b)(2)(i). The regulations use 110 as the limiting age because that is the oldest age considered in the life tables.

[120] Reg. §1.7520-3(b)(2)(i), §20.7520-3(b)(2)(i), §25.7520-3(b)(2)(i).

[121] Reg. §25.7520-3(b)(2)(v)(E), *as redesignated and amended by* T.D. 9974.

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ample is to demonstrate that the amount of the deductible charitable annuity interest must be reduced when the fund will be exhausted before the measuring life attains age 110. Given the mandatory nature of the regulation, it would be reasonable to apply the same valuation method to a charitable remainder interest, although the IRS has never officially approved it.[122]

E. Choosing the Noncharitable Beneficiaries and the Term for the Trust

The governing instrument must require payment of the annuity or unitrust amount for a period that begins with the first year of the charitable remainder trust (CRT) and continues: (i) for the life or lives of a named individual or individuals living at the creation of the trust; or (ii) for a term of years not to exceed 20.[123]

1. Life of One or More Individual Beneficiaries (Concurrent or Successive)

Only an individual or a §170(c) organization may receive the annuity or unitrust amounts for the life of an individual.[124] If an individual receives an amount "for life," it must be payable solely for the life of that individual. An interest based on the life of another (i.e., "*pur autre vie*") is not permissible.[125] Therefore, if the annuity or unitrust amount is paid to a class of individuals, it must be paid to each individual for life until the death of the last survivor.

The sum certain or fixed percentage (i.e., annuity or unitrust amount) must be paid to one or more named persons.[126] The beneficiaries may, but are not required to, include the donor. A portion of the amount may be paid to a charitable beneficiary so long as there is at least one noncharitable beneficiary.[127] The Code generally defines "person" to include, in addition to an individual, the following entities: trust, estate, partnership, association, company, or corporation.[128] Where the amount is to be paid to an individual or individuals for life, all of the recipients must be living when the trust is created. Payments may be made "for the use of" a named person, thus permitting distributions to the guardian of a minor or any other individual who is suffering from a legal incapacity.[129]

Payments may be made by a CRT measured by the life of an individual to a noncharitable trust under limited circumstances. In Rev. Rul. 2002-20,[130] the noncharitable beneficiary of a CRUT was a separate trust established for the benefit of an individual who was "financially disabled" within the meaning of §6511(h)(2)(A). The trustee of the recipient trust was directed either to pay the unitrust amounts each month to the disabled individual or to distribute income and principal of the recipient trust for the individual's benefit in a manner that supplemented, but did not supplant, any governmental benefits available to the individual. At the individual's death, assets of the recipient trust would be distributed to the individual's estate or, after reimbursement of the state for Medicaid benefits provided to the individual, distributed subject to the individual's exercise of a general power of appointment. The IRS approved the charitable remainder unitrust and stated that the payments to the recipient trust would be treated as made directly to the disabled individual.[131] The IRS noted that the same result would apply if the CRT were an annuity trust instead of a unitrust.

A pet animal is not a permissible income recipient and, therefore, a grantor is not entitled to a charitable deduction for the value of the gift of a remainder interest in a trust where a pet is the named income beneficiary. Rev. Rul. 78-105 addressed three instances in which a unitrust provided a life income for a pet with the remainder to charity. In each case, the IRS found that the trust did not qualify as a charitable remainder trust. The IRS allowed a charitable deduction only where, under applicable state law, the pet's interest in the trust was void. This terminated the trust and accelerated the charity's remainder interest to a present interest.

Comment: Rev. Rul. 78-105 was written before the qualified contingency provisions were added to the Code.[132] It may now be possible to effectively create a qualified CRT for the life of a pet by paying the annuity or unitrust interest to a person for a term of years, with the death of the pet as a qualified contingency that would accelerate the charitable remainder. The IRS has not ruled on this specific combination, but it seems to fall within both the letter and intent of the existing guidance.

It is common for a CRT to have both spouses as beneficiaries. The spouse who contributes the assets is often the initial beneficiary, while there is a contingent successor benefi-

---

[122] However, in *Shapiro v. Commissioner*, T.C. Memo 1993-483, the court stated that:

> Taking respondent's argument to its theoretical conclusion, *any trust* created with corpus funds equivalent to the present value of a lifetime annuity obligation as computed under [the then-applicable 10% table] would be deemed to be "underfunded" in that it would have insufficient funds to sustain the annual payments should the annuitant live beyond his or her average life expectancy. In this regard, respondent's argument contravenes the fundamental purposes and presumptions underlying the actuarial tables.

[123] §664(d)(1)(A), §664(d)(2)(A); Reg. §1.664-2(a)(5), §1.664-3(a)(5).

[124] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

[125] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i). But see the discussion of "qualified contingencies" below at IV.E.7.

[126] §664(d)(1)(A), §664(d)(2)(A).

[127] *See* PLR 200108035 (trust that paid its unitrust amount to both individual and charity simultaneously, and satisfied all other §664(d)(2) requirements, qualified as CRUT).

[128] §7701(a)(1).

[129] Reg. §1.664-2(a)(3)(i), §1.664-3(a)(3)(i). A bankruptcy court has held that a bankrupt unitrust recipient's payments from a charitable remainder unitrust can be turned over to the bankruptcy trustee without violating the requirement that payments be made for the use of a named individual. *Lindquist v. Mack (In re Mack)*, 269 B.R. 392 (Bankr. D. Minn. 2001).

[130] *Amplifying and superseding* Rev. Rul. 76-270. *See* PLR 200240012 (citing Rev. Rul. 2002-20, IRS approved payment of unitrust amount to separate noncharitable irrevocable trust for individual adjudicated as incapacitated).

[131] In PLR 9710008, PLR 9710009, and PLR 9710010, the IRS revoked three earlier letter rulings (PLR 9619042, PLR 9619043, and PLR 9619044) that had allowed a CRT to pay the unitrust amount to a trust for the benefit of the grantor's child for the child's life, stating that the earlier rulings were not in accord with current IRS views. The IRS indicated that it had determined that, under §664(d)(2), an otherwise qualifying CRUT making distributions for a named individual's life to another trust "whose only function is to receive and administer those distributions for the benefit of the named individual beneficiary" will not be a CRUT unless the named individual is incompetent. The IRS noted that Reg. §1.664-3(a)(5)(i) provides that "[o]nly an individual or an organization described in section 170(c) may receive an amount for the life of an individual." *Cf.* PLR 201947007 (citing Rev. Rul. 2002-20, IRS allowed reformation of CRUT to name Child's estate as remainder beneficiary of child's special needs trust).

[132] §664(f). See the discussion of qualified contingencies at IV.E.7., below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

cial interest in the other spouse. The donor spouse usually retains the testamentary right to revoke the successor spouse's interest. This revocation power, besides avoiding current gift tax consequences, is useful in case of divorce or other valid reason. However, there is no reason that the spouses cannot have concurrent interests as well as contingent successive interests.[133] Indeed, that arrangement is common when the CRT is funded with community or joint property.[134]

The phrase "named person or persons" is defined in the regulations to include members of a named class.[135] However, if the class includes any individuals, and the payment period is for life, all individuals in the class must be alive and ascertainable when the trust is created.[136] Thus, children adopted after the date of the creation of a trust for the grantor's children could not be included in the class of recipients, even if they were alive on the date the trust was created, because they would not be "ascertainable" as of that date.

> *Example:* An inter vivos CRT provides for annuity or unitrust payments in equal shares to all of the grantor's children for life, including children born after the creation of the trust. At the death of the last survivor, the corpus will be paid to a §170(c) organization. The trust does not qualify, because the trust provides for payment for life to a class that includes beneficiaries who are not alive at the time the trust is created.

A special rule applies where the annuity or unitrust amount is to be paid for a period of years. In that case, afterborn individuals may be included in the class of beneficiaries.[137]

> *Example:* An inter vivos charitable remainder trust provides for annuity or unitrust payments in equal shares to all of the grantor's children for a period of 20 years. Because the payment is made solely for a term of years, afterborn or after-adopted children of the grantor may be included in the class. If the annuity or unitrust amount were to be paid to the grantor's children for life, afterborn or after-adopted children could not be included in the class.

General trust principles presumably control in determining whether individuals are "living" at the time of the creation of the trust and, therefore, a child *en ventre sa mere* may be considered living at the date of the creation of the trust if allowed by local law. While it is unclear whether the applicable date is the date on which the trust is actually created or the date of deemed creation under §664,[138] the date of deemed creation would seem to be the appropriate controlling date.

> *Example:* G transfers property to a trust qualifying as a CRUT except that G retains the inter vivos power of revocation. The unitrust amount is payable to G's children. Several children are born to G after the initial creation of the trust and before her death, at which time the trust becomes irrevocable and is "deemed created." Such children should be considered part of the class of income recipients because they were living on the date of deemed creation.

Certain class closing difficulties can be avoided by having the governing instrument specifically refer to each recipient by name.[139] For example, in PLR 7918002, the grantor named himself as beneficiary of a unitrust amount and provided a successive income interest for his "wife" if she survived him. At the time the trust was executed, the grantor was married to B, but after B's death the grantor remarried. The IRS questioned whether the trust satisfied the requirement that a recipient who is an individual must be named and living at the time of the trust creation. In order to receive an estate tax charitable deduction, the grantor's personal representative was required to show that the donor intended his first wife to be the unitrust recipient. By reference to state law, the IRS determined that the grantor did intend B to be the recipient and, therefore, the estate tax deduction was permitted.

2. *Term of Years*

Where payment is made to a noncharitable entity, such as a partnership, corporation, or trust, the period of payment must be measured by a term of years not to exceed 20.[140]

Where payments are to be made for a term of years, it is permissible for payments to be made to the beneficiary's estate for the duration of the term. In Rev. Rul. 74-39 the governing instrument of a CRUT provided for payment of the unitrust amount to B for a term of 20 years. If B died before expiration of the 20-year term, payments were to be made to C for the balance of the period. If C also died, payments were to be made to C's heirs at law (excluding the grantor and his spouse) for the remainder of the 20-year period. The IRS ruled that the trust qualified because the trust term could not last longer than 20 years.

As discussed above, if the trust is for a term of years, afterborn individuals may be included in the class of beneficiaries.

3. *Combination of Life and Term*

A term will not qualify if it is possible that the payment period may extend beyond both: (i) the lives of the beneficiaries living at the creation of the trust; and (ii) 20 years. This would occur where a payment is to be made to B for life and then to C for a term of years. The regulations permit a trust to be measured by the shorter of either a term of years not to exceed 20 or an individual life.[141]

> *Example 1:* The governing instrument of an otherwise qualified CRT provides for the annuity amount to be paid to B for life or for 20 years, whichever is shorter. The trust

[133] *See* PLR 201321012.
[134] *See, e.g.*, PLR 201249002.
[135] Reg. §1.664-2(a)(3)(i), §1.664-3(a)(3)(i).
[136] Reg. §1.664-2(a)(3)(i), §1.664-3(a)(3)(i).
[137] Reg. §1.664-2(a)(3)(i), §1.664-3(a)(3)(i).
[138] *See* Reg. §1.664-1(a)(4).
[139] This is not possible in a testamentary CRT, where the testator must rely on the deemed date of creation rule. In such case, the instrument need not refer to the beneficiaries by name but should expressly limit the class by modifying the eligible recipients to include only those "who are living on the date of my death."
[140] Reg. §1.664-2(a)(5), §1.664-3(a)(5). *See* PLR 8749052 (payment to "educational trust" for benefit of three minor beneficiaries approved for 20-year term CRT).
[141] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

will qualify because the payment period cannot last longer than either B's life or a period of 20 years.[142]

It is permissible to tack a period measured by the life of an individual onto a period measured by a period of years, provided the individual is living on the date of the creation of the trust.

Example 2: The CRT provides for payments to partnership P for 10 years and then to B for his life. B is living at the creation of the trust. The trust qualifies.

Example 3: The charitable remainder trust provides for payment to B for his life and after B's death to C for her life or for 20 years, whichever is shorter. The trust is qualified if B and C are both living at the creation of the trust because it is not possible for the period to last longer than the lives of named individuals living at the creation of the trust. However, it would not be permissible to provide for C's payments to continue for B's life or 20 years, whichever is longer.[143]

It is not permissible to tack a period measured by a term of years onto a period measured by the life of an individual, because the durational limit must be either a term of years not to exceed 20 or the life of an individual beneficiary.

Example 4: A CRT provides for payment to B for life and upon B's death to C for 10 years. The trust does not qualify, because it is possible that the period of payment of the annuity or unitrust amount will not expire within either of the required time limits. If B were to die after 15 years and C were to die five years after B's death, with payments of C's income interest made to his estate or his heirs for the remaining five-year period, the income interest would extend for a period longer than 20 years and also longer than the measuring lives. Because B lived for 15 years, the aggregate trust term would be 25 years (i.e., longer than 20 years). Further, the trust term would continue beyond the lives of named beneficiaries B and C, because payments would be made to C's estate for the remainder of the 10-year term.[144] To qualify, the trust would need to terminate at the death of B or C.

Example 5: The charitable remainder trust provides for payments to X for life, or 20 years if longer. (If X dies before 20 years, the payments would be made to X's estate or heirs). This is permissible, because the trust could not last longer than a measuring life or 20 years.

4. *Option for Trustee to Sprinkle Payments Among Beneficiaries*

Although it is permissible to give the trustee of a term CRT the power to sprinkle the annuity or unitrust payments among a class of beneficiaries, this is infrequently done. The practical situation when this might be useful is if the trust is intended to provide support for a group of children, grandchildren, or nieces and nephews during their college years. If this sprinkling power is desired, neither the donor nor his or her spouse can be the trustee, as the retention of this power would trigger grantor trust status.[145]

A trust will not qualify as a CRT if any person has the power to alter the amount to be paid to any noncharitable beneficiary and such power would cause such person to be treated as the owner of the entire trust or a portion of the trust under the grantor trust rules of §671–§678.[146] Thus, where the grantor retains discretion over the payment of the annuity or unitrust amount (i.e., the only amount that can be paid to a noncharitable beneficiary), the power must be limited so as to avoid application of the grantor trust rules and the subsequent disqualification of the trust. The power to sprinkle income must be restricted to a disinterested trustee.[147] If the grantor acts as a co-trustee, the ability to "sprinkle" income causes the grantor to be treated as the owner unless the co-trustee has an adverse interest.[148] The grantor trust rules also impute to the grantor any powers held by his or her spouse.[149] Although trusts in which a grantor retains the right to receive income are treated as grantor trusts under §677, this specific grantor provision is negated for CRTs.[150]

Rev. Rul. 77-73 addressed the extent to which a trustee can have the power to "sprinkle" income. The grantor created an inter vivos CRT with an independent corporate fiduciary as sole trustee. The trustee was authorized by the governing instrument to make specified distributions to and among three named individuals in such amounts and proportions as the trustee determined, in its sole discretion, until the death of the survivor of them. The ruling concludes that the trustee could maintain (and exercise) the right to sprinkle without disqualifying the trust.

Any power exercisable by a trustee is imputed to the grantor if the grantor retains the power to remove, substitute, or add trustees.[151] Rev. Rul. 77-285 illustrates this point in conjunction with the "sprinkle" concern in its two fact patterns. In both situations, the governing instruments, which otherwise qualified under §664, permitted the grantor to remove the trustee for any reason and substitute any other person, including the grantor, as trustee. In the first situation, the specified distribution was payable to the grantor for life. In the second situation, the specified distribution was payable to two beneficiaries for their lives, one of whom was the grantor, and the

[142] Reg. §1.664-2(a)(5)(ii)*(b)*, §1.664-3(a)(5)(ii)*(b)*.

[143] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

[144] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

[145] For a full discussion of grantor powers, see 819 T.M., *Grantor Trusts (Sections 671–679)*.

[146] Reg. §1.664-2(a)(3)(ii), §1.664-3(a)(3)(ii).

[147] §674(c). *See* PLR 200813023, PLR 200813006 (CRTs were not grantor trusts where special trustee who held power to sprinkle unitrust amount could be removed and replaced by grantors but grantors and persons related or subordinate to grantors within meaning of §672(c) could not serve as special trustee).

[148] §674(a). In PLR 9223040, the IRS ruled that the grantors' ability to name themselves as successor trustees of a CRT would not cause the trust to become a grantor trust since they would have no discretion over the payment of income.

[149] Under §672(e), a grantor is treated as holding any power or interest held by his spouse at the time of the transfer. Section 672(e) applies generally to transfers in trust made after March 1, 1986.

[150] Reg. §1.664-1(a)(4).

[151] Reg. §1.674(d)-2(a).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

trustee was granted the sole discretion to allocate the amount of the distribution between the two beneficiaries.

The IRS ruled that only the first trust qualified. The IRS explained that under §674(a) a grantor will be treated as the owner of any portion of a trust over which the grantor or a nonadverse party has the power of disposition and that the regulations attribute any power held by the trustee to the grantor where the grantor is able to remove, substitute, or add trustees.[152]

In the first situation, the trustee did not hold any discretionary power that would cause the grantor to be treated as the owner of the trust under the grantor trust rules, even if the grantor had been the trustee. Thus, the power to remove the trustee and appoint another did not disqualify the trust. However, in the second situation, the discretionary power to allocate income, if attributed to the grantor, would cause the grantor to be treated as the owner of the entire trust under §674(a). Thus, the grantor's power to remove the trustee and appoint another disqualified the trust, because the removal power resulted in imputing a prohibited allocation power from the trustee to the grantor. Consequently, the trust failed to satisfy the requirement that a charitable remainder trust cannot permit any person to alter the amount to be paid to a non-§170(c) beneficiary if such power would cause the person to be treated as the owner of the trust under the grantor trust rules.[153]

Practice Point: Where the trustee does not have any power to determine the amounts payable to the annuity or unitrust beneficiary, the grantor may serve as trustee, or retain the right to serve as trustee, without causing the disqualification of the trust.[154]

5. *Donor's Retained Power to Revoke Successor Interest(s) or Invade the Trust*

In general, CRTs may not be subject to a power of invasion for the beneficial use of a person other than a §170(c) organization or to a power of revocation. However, an exception to this rule permits the grantor to retain the power, exercisable solely by will, to revoke or terminate the interest of any non-§170(c) beneficiary.[155] Retaining this right will not allow the potential successor income interest to be disregarded in valuing the charitable remainder interest.[156]

Practice Point: This power is frequently retained by the grantor in two-life CRTs to take into account the possibility of divorce after the trust is funded, or in case it becomes clear that the income will not be needed by the survivor and, thus, the charitable interest can be accelerated.

Practice Point: This power may only be exercised by will: there is no parallel provision allowing the power to be exercised through a revocable trust used as a testamentary substitute.[157]

Retention of the right of revocation will also prevent a completed gift at the funding of the trust. See the gift tax discussion at IV.I., below.

The use of the term "terminate" permits the grantor to cut off the interest of a person who has been receiving payment of the annuity or unitrust amount during the grantor's lifetime.[158]

6. *Portion of Annuity or Unitrust Payment Payable to Charity*

A CRT may pay a portion of the annuity or unitrust amount to a §170(c) organization. The amount of the payment may be mandated by the governing instrument, or the trustee may be given the discretion to sprinkle a portion of the annuity or unitrust amount between a §170(c) organization and the noncharitable beneficiary or beneficiaries. However, there must always be a non-§170(c) recipient of some portion of the annuity or unitrust amount because of the requirement that an annuity or unitrust amount be paid to a person other than a §170(c) organization.[159]

---

[152] Reg. §1.674(d)-2(a).

[153] Reg. §1.664-1(a)(4), §1.664-2(a)(3)(ii), §1.664-3(a)(3)(ii).

[154] *See* Rev. Rul. 77-285. Trustee selection is further discussed at IV.G., below.

[155] Reg. §1.664-2(a)(4), §1.664-3(a)(4); Rev. Rul. 74-149. The IRS sample documents each contain sample provisions for this power. See Worksheet 2 for the list of Revenue Procedures with sample documents.

[156] In *Simmons v. United States*, 667 F.2d 832 (9th Cir. 1982), *aff'g* 80-1 USTC ¶9,287 (D. Ariz. 1980), the grantor established a valid CRT that paid her an annuity, with a successive annuity to her son if he survived her. The grantor reserved the right to terminate her son's annuity interest. The IRS had denied an income tax charitable deduction because the present value of the two annuity interests, based upon the life expectancies of the beneficiaries, exceeded the value of the trust corpus. The grantor's conservator asserted that the son's interest should not be taken into account in determining the value of the remainder interest because his interest was subject to termination by the grantor at the time the trust was created. The court rejected this argument, stating that the taxpayer had failed to satisfy her burden of establishing with a considerable degree of certainty the value of the remainder because she had failed to show that the existence of the son's annuity could not place in doubt the value of the charitable remainder.

[157] *See also* §674(b)(3) (also requiring will provision).

[158] Without an exception, the grantor's testamentary right to terminate an income beneficiary's interest could disqualify the trust, as the income beneficiary's interest would be measured by another's life. *See* Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i). However, this power is specifically allowed under §664.

[159] Reg. §1.664-2(a)(3)(i), §1.664-3(a)(3)(i). The following PLRs may be helpful if similar provisions are desired. In PLR 200245058, the IRS ruled that a charitable remainder unitrust was not disqualified under §664 because of provisions (i) giving the noncharitable beneficiaries (the grantor and then possibly his wife) an inter vivos power to appoint the unitrust interest to organizations described in §170(c), §2055(a), and §2522(a), (ii) requiring that the adjusted basis of the property distributed pursuant to the power be fairly representative of the adjusted basis of the property available for distribution, and (iii) requiring, in a year when the power is exercised, that the unitrust amount be determined using a method similar to that required for years when additional contributions are made. In PLR 201117005, the IRS ruled that a testamentary CRUT would not be disqualified under §664(d)(2) by provisions (1) giving the independent trustees the power to allocate part of the unitrust amount between the decedent's surviving spouse and the charitable remainder beneficiary (provided the amount paid to the spouse was not de minimis) and to make unequal unitrust payments within a calendar year, (2) requiring alternative dispute resolution and binding arbitration of trust-related controversies, and (3) limiting the portion of the unitrust amount paid to the surviving spouse if she remarried (provided the amount paid to the spouse was not de minimis). The IRS reasoned that the remarriage provision was similar in concept to a §664(f) qualified contingency (see IV.E.7., below), except that the remarriage would not cause termination of the unitrust payments. Although the value of the spouse's unitrust interest was unclear, the IRS ruled that the §2056(b)(8) marital deduction would completely offset the value of the assets passing to the unitrust at the decedent's death, after deduction of the value of the remainder interest qualifying for a §2055(a) charitable deduction. *See also* PLR 201845014, PLR 200813023, PLR 200813006 (provision giving independent trustee power to allocate unitrust amount among charitable and noncharitable beneficiaries on annual basis was not inconsistent with §664 and regulations thereunder as long as governing instrument required that portion of unitrust amount had to be allocated and paid to noncharitable beneficiaries each year and amount so paid was not de minimis).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

In CCA 202233014, the IRS appeared to reverse its position that charitable and marital deductions are permissible for the value of the portion of a unitrust interest of a testamentary CRUT that may be distributed between charity and the decedent's spouse at the trustee's discretion. A testamentary CRUT provided for annual unitrust payments of 5% for the spouse's life, and the spouse was entitled to 25% of the unitrust amount, while the trustee had discretion to distribute the remaining 75% of the unitrust amount to the spouse or the charitable remainder beneficiary. The IRS affirmed the marital deduction for the 25% unitrust amount, but disallowed charitable and marital deductions for the 75% unitrust amount. With respect to the distributions to the charity from the 75% unitrust amount, the IRS reasoned that the distributions to charity was not in the form of a fixed unitrust amount because such amounts were not ascertainable or severable from the spouse's noncharitable interest. With respect to distributions to the spouse from the 75% unitrust amount, the IRS reasoned that the extent of the spouse's interest could not be established because it could not be ascertained whether and to what extent the spouse would receive any portion of the 75% interest. Because CCA 202233014 runs counter to analysis in prior PLRs, the IRS went further to explain that it has changed its position taken in PLR 201845014, PLR 201117005, PLR 200832017, and PLR 200813006.[160]

The regulations permit other amounts, such as the amount of income in excess of the annuity or unitrust amount, to be paid to a §170(c) organization.[161] Where the governing instrument contains an optional provision for payments to a §170(c) organization, the instrument must either prohibit such payments from being made in kind, or provide that the adjusted basis of property distributed in kind be "fairly representative of the adjusted basis of the property available for payment on the date of payment."[162] The statement concerning representative basis is a mandatory provision[163] if in kind payments are not prohibited, and failure to include such a provision will disqualify the trust. This provision prevents the trustee from distributing low basis assets to the §170(c) organization, which is exempt from income taxation, thereby benefiting the noncharitable annuity or unitrust beneficiary by the retention of high basis assets. The IRS sample documents include this provision.[164]

Comment: The regulations appear to permit the grant of complete discretion to the trustee as to what amount in excess of the annuity or unitrust amount, if any, will be paid to a §170(c) organization in a given year.[165]

A grantor is not permitted an additional income tax deduction for any portion of an annuity or unitrust amount that is payable to a §170(c) organization.[166] This is consistent with the treatment of charitable lead trusts, where no income tax deduction is allowed for the lead interest unless the trust is taxed as a grantor trust. In Rev. Rul. 76-225,[167] the IRS ruled that an estate tax charitable deduction was not allowable for the value of an annuity interest in a CRAT passing to a §170(c) organization upon the death of the individual recipients. Rev. Rul. 76-225 was revoked by T.D. 9068,[168] which conformed the estate, gift, and income tax regulations to the Tax Court's decision in *Estate of Boeshore v. Commissioner*.[169] The preamble states that the effect of the regulations is to allow an estate, gift, or income tax charitable deduction for charitable annuity or unitrust interests that are preceded by a noncharitable unitrust or annuity interest.[170] However, Reg. §1.664-2(d) and Reg. §1.664-3(d) still preclude an income tax deduction for the value of the charitable interests other than the remainder interest in the CRT. An exception applies if some or all of the income interest is donated separately at a later date; see VII.B., below.

7. Including a Qualified Contingency in the Trust

Especially in a testamentary CRT, the donor may want the noncharitable interest to terminate if a specified event occurs (typically remarriage of a surviving spouse).[171] For an inter vivos trust with a successor interest to a surviving spouse, the trust can terminate at the death of the initial beneficiary if the couple are no longer married at the time of the first spouse's death. This type of provision, a "qualified contingency," will not disqualify the CRT. A contingency is qualified provided it does not extend the duration of the otherwise allowable trust term. However, the existence of a qualified contingency is not taken into account for purposes of determining the value of any charitable contribution or the actuarial value of any interest. All of the IRS sample documents include an optional provision for a qualified contingency to trigger an early vesting of the charitable remainder.

Before the Tax Reform Act of 1984,[172] the IRS had ruled that a charitable remainder trust was not qualified if it termi-

[160] In PLR 201117005 involving a testamentary CRUT, the IRS ruled that where the taxpayer established a testamentary CRUT for one measuring life in which the surviving spouse was the only noncharitable beneficiary, the estate tax marital deduction would completely offset the value of the assets distributed to CRUT as of the taxpayer's date of death, after deducting the value of the remainder interest qualifying for a charitable deduction. Citing legislative history, the IRS found that both the charitable and marital deduction would be available where an individual created a qualified CRAT or CRUT and the only noncharitable beneficiaries were the donor and the donor's spouse, the logic likely being that both beneficiaries would be deduction-favored taxpayers.

[161] Reg. §1.664-2(a)(4), §1.664-3(a)(4). In PLR 8651030, the IRS allowed the amendment of a CRAT to pay income in excess of the annuity amount to the charitable remainder beneficiary. In PLR 9817010, the trustee used this provision to accelerate the payment of the charitable remainder interest. *See also* PLR 200950032 (excess principal paid to charitable remainder beneficiary), PLR 200950032, PLR 200617026, PLR 200010035 (excess income and principal paid to charitable beneficiary), PLR 200726005 (testamentary trust reformation to pay annuity to beneficiary and three charities for five years or until prior death of beneficiary), PLR 199929033 (trust reformation to allow principal payment to charitable remainder beneficiary).

[162] Reg. §1.664-2(a)(4), §1.664-3(a)(4).

[163] Rev. Rul. 72-395, §5.05, §7.05.

[164] See Worksheet 2 for the list of Revenue Procedures with sample documents.

[165] Sections 5.05 and 7.05 of Rev. Rul. 72-395 set forth the following sample language: "During the life of A, the trustee may pay to M charity any income of the trust in excess of the [annuity or unitrust] amount payable to A for the taxable year of the trust in which the income is used." The sample provision only addresses payments to be made out of the current year's income.

[166] Reg. §1.664-2(d), §1.664-3(d).

[167] *Revoked by* T.D. 9068, 68 Fed. Reg. 40,130 (July 7, 2003).

[168] 68 Fed. Reg. 40,130 (July 7, 2003).

[169] 78 T.C. 523 (1982), *acq.*, 1987-1 C.B. 1. *Boeshore* held invalid the regulation disallowing an estate tax charitable deduction for a charitable unitrust interest that was preceded by a noncharitable unitrust interest in a CRT.

[170] See PLR 8845012 for an example of an estate tax charitable deduction allowed for the value of the portion of the annuity payable to charity as well as the value of the remainder.

[171] PLR 201117005 and PLR 200430012 include this provision.

[172] Pub. L. No. 98-369.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

nated on a beneficiary's remarriage because the duration of the trust was not based on either a term not in excess of 20 years or a life (or lives) in being.[173] A trust could qualify if the annuity or unitrust amount payable to a spouse was reduced, but not discontinued, on the occurrence of a specified event (e.g., remarriage) and the amount of the reduction was thereafter paid to the charitable remainder beneficiary.[174] However, an estate tax charitable deduction was not allowed for the value of the contingent annuity or unitrust amount that would be payable to the charitable remainder beneficiary on the beneficiary's remarriage.[175]

The Tax Reform Act of 1984 added §664(f), which allows noncharitable annuity and unitrust payments to end upon the occurrence of a "qualified contingency," thereby accelerating the charitable remainder interest. In PLR 9322031, the IRS concluded that the early termination of a unitrust interest on the death of a nonbeneficiary was a qualified contingency.[176]

F. Choosing the Remainder Charity or Charities

When funding a charitable remainder trust (CRT), many donors already have specific plans for the remainder interest (perhaps intending for it to end up in their family foundation or a favorite public charity). Others have only a general idea, perhaps an area of interest. Either way, donors should consider reserving the right to change the remainder charity. The donor's charitable priorities may change, the activities of a charity may change, tax laws may change. Given that the income tax deduction is not precluded by this retained right, there is no downside to keeping the options open (although a charity will generally not serve as trustee unless it has an interest in the trust).[177] However, if the remainder could pass to a private foundation, the income tax deduction may be limited. If the donor prioritizes the maximum income tax deduction, or is sure that a private foundation is not an option, then the trust can be drafted for the maximum charitable income tax deduction.

For the trust to qualify as a CRT, the governing instrument must provide that upon the termination of the last income interest "the entire corpus of the trust is … to be irrevocably transferred, in whole or in part, to or for the use of one or more organizations described in section 170(c) or retained, in whole or in part, for such use."[178] Thus, the entire corpus must be transferred outright to or for the use of one or more §170(c) organizations, or retained in trust for the use of one or more of such organizations, or in part distributed outright to such organizations and in part retained in trust for the use of such organizations.[179]

A donor is not limited to a single named charity as a remainder charity. The remainder can be divided among a number of charities either initially or later on.[180] The donor can limit a portion of the remainder interest to public charities while allowing the remaining portion to pass to any eligible charity.[181] This type of provision will allow a balance between charitable flexibility and the income tax deduction.

The donor may retain the power to change the charity during his or her lifetime or by will.[182] Alternatively, the choice can be left to trustees or successor beneficiaries, either in the document itself or indirectly by naming a donor-advised fund as the remainder beneficiary. The donor-advised fund option will give the successor advisors the ability to choose the charitable beneficiaries (within the fund's rules).[183]

The governing instrument must provide for the selection of an alternative remainder beneficiary in the event that the designated remainder beneficiary does not qualify as an organization described in §170(c) at the expiration of the last noncharitable interest.[184] The reason for the alternative-remainder-beneficiary requirement is that upon creation of the trust a donor is entitled to an immediate income, gift, or estate tax deduction for the present value of the remainder interest reserved for a qualified charity. The alternative-remainder-beneficiary provisions insure that, upon expiration of the noncharitable interests, the remainder will actually be paid to or held in further trust for one or more organizations described in §170(c). The alternative organization or organizations may be selected in any manner provided by the terms of the governing instrument.[185]

Comment: The governing instrument should require that both the designated charitable remainder beneficiary and the alternative remainder beneficiary (or remainder beneficiaries) be organizations described in each of the Code sections under which a charitable deduction is desired. This is necessary because of the lack of congruence among §170(c), §2055(a), and §2522(a), as discussed immediately below.

In Rev. Rul. 76-307, the governing instrument appointed the designated charitable remainder beneficiary X as the trustee. X was an organization described in each of §170(c), §2055(a), and §2522(a) at the time the trust was created. The instrument contained an alternative remainder beneficiary clause providing that if X were not described in §170(c) at the time it was to receive its remainder interest, its interest would be transferred to another organization described in §170(c). The ruling found as a matter of fact that the probability that X would be an organization described in §170(c) but not in §2055(a) and §2522(a) upon termination of the trust was so remote as to be negligible.

---

[173] Rev. Rul. 76-291.

[174] Rev. Rul. 76-291.

[175] Rev. Rul. 76-291.

[176] *See also* PLR 200414011 (unitrust not disqualified under §664(d)(2)(A) when one-half of unitrust amount was payable to three individuals, or survivors, for life of fourth individual, because termination of payments upon death of fourth individual was §664(f) qualified contingency; however, value of remainder interest had to be calculated without regard to qualified contingency, and unitrust failed to satisfy §664(d)(2)(D) 10% remainder requirement).

[177] See discussion of choice of trustee, at IV.G., below.

[178] Reg. §1.664-2(a)(6)(i), §1.664-3(a)(6)(i).

[179] Permissible remainder beneficiaries include certain employee stock ownership plans (ESOPs) to which "qualified gratuitous transfers" of employer securities are made. §664(d)(1)(C), §664(d)(2)(C), §664(g), amended/added by the Taxpayer Relief Act of 1997 ('97 TRA), Pub. L. No. 105-34, §1530, only applicable to CRTs funded by decedents before January 1, 1999. *See also* PLR 200716031.

[180] Rev. Rul. 77-385.

[181] *See* PLR 200813023.

[182] Rev. Rul. 76-8.

[183] Rev. Rul. 76-7. *See also* PLR 9445010 (income beneficiaries/trustees could have power to designate by majority vote which departments within university would receive remainder; relying on Rev. Rul. 76-8), PLR 8919016 (trustee of charitable remainder unitrust could have power to name substitute charitable remainder beneficiary; relying on Rev. Rul. 76-7).

[184] Reg. §1.664-2(a)(6)(iv), §1.664-3(a)(6)(iv).

[185] Reg. §1.664-2(a)(6)(iv), §1.664-3(a)(6)(iv). Sample language is set forth in the IRS's sample charitable remainder trust forms. See Worksheet 2 for the Revenue Procedures with the sample documents.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

On this basis, the ruling allowed a gift tax deduction for the year the trust was created even though the alternative remainder beneficiary provision did not require that the alternative remainder beneficiary be described in §2522. Consistent with its then-current policy not to rule on the estate tax consequences for a living grantor, the IRS declined to rule on the availability of an estate tax deduction and noted that the validity of such a deduction would depend on the circumstances existing at the time of the grantor's death. For example, if X was then described in §170(c) but not §2055(a), an estate tax charitable deduction would not be allowed, because the trustee would be required to distribute the remainder to X. However, if X was then described in §2055(a) but not §170(c),[186] the interest would pass to another organization described in §170(c) but not necessarily §2055(a). As noted above, such problems can be avoided by careful drafting to provide that the alternative remainder beneficiaries must be described in each of the Code sections under which a deduction may be sought.

Practice Point: The IRS sample documents' default language is "§170(c)." This provision should be changed to §170(b)(1)(A) where the donor seeks to obtain an income tax charitable deduction based on the public charity limits. See the discussion at IV.F.2., below.

In Rev. Rul. 80-38, the remainder interest was payable to a university described in §170(b)(1)(A)(ii) (i.e., a "public charity"). The governing instrument provided that if the remainder beneficiary did not qualify at termination, the remainder was to be distributed to an organization, to be selected in the sole discretion of the trustee, described in §170(c) (but not necessarily in §170(b)(1)(A)). The ruling noted that the regulations[187] provide that a deduction is allowable even if an interest in property transferred to charity may be defeated by the subsequent performance of some act or by the happening of some event, where the possibility that the act or event will occur and defeat the charity's interest is so remote as to be negligible. The ruling concludes, based on the facts and circumstances, that the gift of the remainder interest to the university was eligible for the 50% limitation because there was "small likelihood" that the university would cease to exist as a public charity described in §170(b)(1)(A).

Practice Point: The facts and circumstances test of Rev. Rul. 80-38 would seem less favorable to organizations that avoid private foundation status by virtue of qualifying as "publicly supported" organizations described in §170(b)(1)(A)(vi) or §509(a)(2). This is because the public charity status of such an organization depends on the nature of the support it receives, which is measured by two mathematical tests the organization must satisfy each year. Thus, if a donor wishes to insure that the maximum percentage limitations will apply, the governing instrument should require that the designated charitable remainder beneficiary and any subsequently designated remainder beneficiary be described in §170(b)(1)(A) as well as §170(c) at the time the trust terminates.

Comment: A completed gift will not occur when the grantor retains the power to substitute charitable remainder beneficiaries and the grantor is the only noncharitable beneficiary. This result does not preclude the charitable income tax deduction when the trust is funded, but it does preclude the need for gift tax reporting. See the gift tax section at IV.I., below.

[186] *E.g.,* if X were then a foreign charitable organization.

[187] Reg. §1.170A-1(e).

Where interests in the corpus of a CRT are given to more than one organization described in §170(c), such interests may be enjoyed by the designated organizations either concurrently or successively.[188]

> *Example:* Trust A, which otherwise qualifies under §664, provides that upon termination the remainder is to be held in trust, with the income payable 50% to each of two §170(c) organizations. Trust B, which otherwise qualifies under §664, provides that upon termination the remainder is to be retained in trust, with all of the income payable for 20 years to a §170(c) organization and that thereafter the corpus is to be paid outright to another §170(c) organization. Both Trust A and Trust B qualify under §664.

1. *Qualified Charities for Income, Gift, and Estate Tax Deductions*

In planning for the donor's income tax deduction, qualification under §170(c) is the beginning of the discussion, not the end. Several other factors affect the deduction limitation, which is discussed in detail at IV.H., below.

First, the method of distribution of the remainder interest will affect the ceiling imposed on the grantor's income tax charitable deduction under §170 (but not the amount of the gift or estate tax deduction). If the trust corpus is retained in trust for the benefit of a designated charitable remainder beneficiary,[189] the deductibility for income tax purposes is limited to 30% of the grantor's "contribution base"[190] in the year of the gift with a five-year carryover.[191] If the remainder interest will pass outright to a charity, either a 30% or a 50% limitation applies, depending upon the nature of the property placed in trust. Second, a lower limitation applies where a private foundation (as opposed to a public charity) is named as the remainder beneficia-

[188] Reg. §1.664-2(a)(6)(iii), §1.664-3(a)(6)(iii).

[189] Such a trust would most likely be a §4947(a)(1) wholly charitable trust, which could apply for tax-exempt status under §501(c)(3) as either a supporting organization under §509(a)(3) or a private foundation.

[190] §170(b). "Contribution base" is defined as "adjusted gross income (computed without regard to any net operating loss carryback to the taxable year under section 172)." §170(b)(1)(H) (as redesignated by the Tax Cuts and Jobs Act, Pub. L. No. 115-97, §11023(a)). Note that for cash contributions made during the 2020 and 2021 tax years, individuals who itemize may elect to deduct up to 100% of his or her contribution base. Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. No. 116-136, §2205(a) (non-Code provision), applicable to tax years ending after December 31, 2019, as amended by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, Pub. L. No. 116-260, Div. EE. §213. *See also* IRS News Release IR-2021-190. Under this non-Code provision, qualified contributions must be to an organization described in §170(b)(1)(A). Contributions to charitable remainder trusts are generally deductible pursuant to §170(b)(1)(B). Therefore, contributions to a charitable remainder trust generally are not qualified contributions, unless the charitable remainder interest is paid in cash to an eligible charity during the applicable time period. Additionally, a qualified charitable contribution does not include an amount that is treated as a contribution in the taxable year by reason of being carried forward from a prior contribution year under §170(b)(1)(G) or §170(d)(1). *See* Staff of J. Comm. on Tax'n, 116th Cong., Description of the Tax Provisions of Public Law 116-136, the Coronavirus Aid, Relief, and Economic Security ("CARES") Act 22-23 (J. Comm. Print 2020).

[191] §170(d); Reg. §1.170A-10.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ry. The private foundation limitations are discussed in IV.F.2., below.

The designation of a qualifying remainder beneficiary can be complicated because the organizations described in §170(c) (income tax), §2055(a) (estate tax), and §2522(a) (gift tax) are not identical. The vast majority of charitable organizations fit in all three categories, but there are exceptions. For example, certain nonprofit cemetery companies are described in §170(c) but not in §2055(a) or §2522(a). Accordingly, a trust provision requiring the corpus be distributed to or for the use of, or retained for the use of, a §170(c) organization will qualify under §664 but may not qualify for an estate or gift tax charitable deduction.[192]

Deductible veterans' organizations have slightly different definitions for income and gift tax than for estate tax. The income and gift tax statutes allow deductions for transfers to posts or organizations of war veterans, or auxiliary units or societies of any such posts or organizations, if such posts, organizations, units, or societies are organized in the United States or any of its possessions, and if no part of their net earnings inures to the benefit of any private shareholder or individual.[193] The estate tax statute restricts the deduction to "any veterans' organization incorporated by Act of Congress."[194] Therefore, if the charitable remainder is intended for a veteran's charity and the estate tax will be relevant, the status of the charity should be checked.

Even for inter vivos trusts, it is necessary to consider the estate tax charitable deduction if the trust will be included in the donor's taxable estate. If the donor retains any interest in the trust that would cause estate inclusion under §2036 or §2038, the donor generally would want a charitable estate tax deduction to offset the amount included.[195]

Foreign charities are not eligible remainder beneficiaries, as they are not described in §170. If a donor desires to benefit a foreign charity through a CRT, this may be possible indirectly through a "Friends of the Foreign Charity" organization, or a cross-border focused donor-advised fund.[196]

2. *Remainder Charities Could Include Private Foundations*

If there is any possibility that a private foundation will receive the remainder interest, the lower deduction limits will apply, even if a public charity is initially named. In Rev. Rul. 79-368, a public charity was designated as the remainder beneficiary of an inter vivos charitable remainder trust. The governing instrument provided that the grantor and the income recipients had the power to change the identity of the remainder beneficiary to another charitable organization described in §170(c) (but not necessarily in §170(b)(1)(A)). The ruling noted that there was a possibility that the ultimate remainder beneficiary would not qualify as a public charity. Accordingly, for income tax purposes, the IRS ruled that the gift was subject to the lower percentage limitation applicable to gifts to private foundations.

The calculation for the income tax charitable deduction is discussed at IV.H., below.

Practice Point: If the deduction is subject to the private foundation limitations, this may or may not matter to the donor. If the deductible charitable remainder interest is the minimum 10% and the trust is funded with qualified appreciated (marketable) stock,[197] the donor's deduction may not be affected by this provision. On the other hand, if the remainder value is significant and the trust is funded with highly appreciated closely held securities, the private foundation limitations could significantly reduce the allowable income tax deduction.[198] If the income tax deduction is important, consider the use of a donor-advised fund as a remainder beneficiary in lieu of a private foundation.

G. Selecting a Trustee

Non-tax factors should be considered first when deciding on a trustee for a charitable remainder trust (CRT). Is the trustee willing and able to serve? Is the trustee sufficiently experienced (or willing to hire experienced professionals for advice)? What fees will the trustee charge? Would the residence of the trustee trigger unexpected state filing requirements?[199] Should a co-trustee arrangement be considered, perhaps including the donor and an independent trustee? (An independent trustee may be needed to annually value certain assets. See VI.A.7., below.) If a charity serves as trustee, would the trust then have access to certain investments or a reduced (or zero) trustee fee?

Trustee compensation must not reduce the unitrust amount or annuity amount, and the trust will be disqualified if the governing instrument authorizes such payment.[200] For fiduciary accounting purposes, the fee is apportioned between income and principal in accordance with local law or the provisions of the governing instrument. In the case of an annuity trust, the payment of the fee normally will have no effect on the amount of the annual annuity payment. For unitrusts, the compensation will reduce the net value of the trust assets, resulting in a smaller unitrust amount payout. In either case, a smaller corpus ultimately will be available for distribution to the remainder beneficiary.

States may require a trustee to post a bond but permit this requirement to be waived in the governing instrument.

The only situation in which a tax provision limits the choice of trustee is the rare CRT which includes a power to sprinkle the annuity or unitrust payment among beneficiaries. Such a power to sprinkle income must be restricted to a disinterested trustee.[201] If the grantor acts as a co-trustee, the ability to "sprinkle" income will cause the grantor to be treated as the owner unless the co-trustee has an adverse interest.[202] The

[192] Rev. Rul. 77-385, Rev. Rul. 76-307.

[193] §170(c)(3), §2522(a)(4).

[194] §2055(a)(4).

[195] §2055(a). See discussion at V.C., below.

[196] For further discussion of cross-border giving, see 6810 T.M., *U.S. International Tax Aspects of Charitable Giving and Charitable Operations.*

[197] §170(e)(5).

[198] §170(e)(1)(B)(ii).

[199] This issue is discussed in 869 T.M., *State Income Taxation of Trusts.*

[200] Rev. Rul. 74-19; PLR 200245058.

[201] §674(c).

[202] §674(a). In PLR 9223040, the IRS ruled that the grantors' ability to name themselves as successor trustees of a CRT would not cause the trust to become a grantor trust since they would have no discretion over the payment of income. *Cf.* PLR 200813023, PLR 200813006 (CRTs were not grantor trusts where special trustee who held power to sprinkle unitrust amount could be re-

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

grantor trust rules also impute to the grantor any powers held by his or her spouse.[203] For a more detailed discussion of the restrictions on the choice of trustee of a CRT which includes a sprinkle power, see the discussion at IV.E.4., above.

1. The Donor as Trustee

Other than in the case of a CRT that includes a sprinkling power, there is no tax impediment to the donor serving as trustee. The impediments are generally the practical ones: CRTs are complicated to administer, and are subject to various federal and state rules governing charitable trusts. The donor may feel that it is not time well spent to learn these rules, especially given the penalties for even unintended errors. If the donor insists on being trustee to avoid the cost of a trustee or co-trustee, he or she may end up paying more in legal, accounting, and appraisal fees than the trustee fees saved.

If a CRT holds unmarketable assets, in order to qualify as a CRT, any required valuations of the unmarketable assets must be valued by an independent trustee or in a qualified appraisal by a qualified appraiser.[204] If the trust will be investing only in cash, mutual funds, or publicly traded stock and bonds, this requirement is not an impediment to the donor (or other non-independent person) serving as trustee. However, if the CRT will be investing in partnerships, LLCs, financial products, insurance products, or other unmarketable assets, the cost and complexity of annual appraisals may become significant if the trustee is not an independent trustee.

Practice Point: While Reg. §1.664-1(a)(7) allows unmarketable assets to be valued by an independent trustee or in a qualified appraisal by a qualified appraiser, a qualified appraisal will generally be necessary for CRTs holding unmarketable assets for the initial contribution in order to satisfy the rules for claiming an income tax charitable deduction.

A grantor (or any other party) who serves as trustee is entitled to receive compensation for his or her services as trustee, provided the compensation does not exceed that which is allowable under applicable state law. Payment by the trust of such compensation to the grantor or a related party does not constitute self-dealing where the payments are reasonable, not excessive, and are based on the amount ordinarily paid to trustees under state law.[205]

In Rev. Rul. 80-83, the donor was a co-trustee of a CRUT and also a director of a publicly held corporation, the stock of which comprised the entire corpus of the trust. Any sale of the stock was subject to a right of first refusal by the corporation. In valuing the stock, the trustees consistently adopted the valuation established by the corporation in exercising its right of first refusal. The IRS ruled that because the donor was bound by fiduciary duty to exercise independent judgment on behalf of both the trust and the corporation in valuing the stock, the trust was qualified under §664 and the arrangement was permissible.

2. Individuals Other than the Donor as Trustee

The donor may know a related party who is willing and qualified to serve as trustee. As long as the trust does not provide for a sprinkling power, there is no tax impediment to a related individual serving as trustee. An appropriate succession mechanism must be established, of course, and the donor will probably want to retain a removal power; but those considerations apply no matter who is named trustee. The same requirements discussed above regarding appraisals of unmarketable assets which apply to donors also apply to non-independent individuals.

If the trust includes a sprinkling power, then the trustee must be a disinterested (not "related or subordinate")[206] trustee to avoid creation of a grantor trust.[207] If an individual trustee is desired, a qualified professional, a sufficiently remote family member, or someone in a family office may be independent, qualified, and willing to serve.

Rev. Rul. 95-58 allows a grantor to retain the right to appoint a successor trustee without triggering estate inclusion under §2036 or §2038, as long as the trustee is not related or subordinate to the grantor. If the donor has retained the income rights in the trust, the trust will be included in his or her taxable estate anyway under §2036. Thus, he retention of the right to appoint any successor trustee is not as relevant to estate inclusion. However, if the donor has not retained any economic rights, retaining the right to appoint a related or subordinate successor trustee, even in a trust without sprinkling powers, can trigger unexpected estate inclusion.

3. Financial Institution as Trustee

Especially if the donor already has a working relationship with a bank or trust company, an institutional trustee is a logical choice. Fees are always a consideration with an institutional trustee, but the cost may be worth the level of experience included. When interviewing potential trustees, to the donor should focus on their experience with CRTs and not just general trusts. An institutional trustee, such as a bank or trust company, may serve as trustee provided it is authorized to do so by the governing instrument and it is not otherwise prohibited by state law. An institutional trustee may invest the trust assets in its own common trust funds without jeopardizing the trust's exemption or the grantor's charitable deduction.[208]

Practice Point: When considering a financial institution as trustee, keep in mind that fees charged by trustees tend to vary be region. The client may desire to compare fee rates then prevailing across various metropolitan areas.

---

moved and replaced by grantors but grantors and persons related or subordinate to grantors within meaning of §672(c) could not serve as special trustee).

[203] Under §672(e), a grantor is treated as holding any power or interest held by the grantor's spouse at the time of the transfer. Section 672(e) applies generally to transfers in trust made after March 1, 1986.

[204] Reg. §1.664-1(a)(7). The qualified appraisal must be consistent with the requirements of Reg. §1.170A-13(c)(3) (for appraisals prepared for returns or submissions filed on or before August 17, 2006), Notice 2006-96 (for appraisals prepared for returns or submissions filed after August 17, 2006, if the donations are made before January 1, 2019), and Reg. §1.170A-17(a) (for appraisals prepared for returns or submissions for donations made on or after January 1, 2019). Pursuant to Reg. §1.664-1(f)(4), these valuation requirements are generally effective for trusts created on or after December 10, 1998.

[205] §4941(d)(2)(E); PLR 8035078, PLR 8033026.

[206] See Rev. Rul. 95-58.

[207] Reg §1.664-2(a)(3)(ii), §1.664-3(a)(3)(ii).

[208] Rev. Rul. 73-571.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

4. Charity as Trustee

Charities, especially the larger ones, are sometimes willing to serve as trustee. Generally, they will only do so if they hold a vested interest in the remainder (sometimes 100% of the remainder, sometimes less than 100%). In consideration of this option, the discussion should include the investment strategy for the CRT; some charities will have all their CRTs invested in a single investment pool. This may or may not be acceptable to the donor. It is unlikely that a charity serving as trustee would want to hold donated nonmarketable assets for any significant period of time. However, the charity may be willing to step in as soon as the nonmarketable assets are sold. Again, a full discussion of these issues should be held before any decisions are made. For the largest CRTs, it may be possible for the donor to make arrangements to have the CRT assets continue to be managed by the donor's money manager.

If the charitable remainder beneficiary does serve as trustee, it may invest the trust assets with its general endowment fund or with the assets of other CRTs.[209] The charity may use specialized structures to avoid allocating unrelated business taxable income to CRTs, although such structures may result in the trust receiving ordinary income instead of capital gain and, thus, affect the donor's taxable income.[210] However, as noted elsewhere,[211] the Philanthropy Protection Act of 1995[212] requires a charity acting as trustee to provide written disclosure to the donor concerning commingling of funds.[213] If a charity is acting as trustee of a CRT in which the remainder interest is irrevocably dedicated to any charitable organization, and if the assets of the charitable remainder trust are not segregated but instead are commingled with other charitable assets in a collective investment vehicle, the trustee must disclose enough information about the operation of the fund in which the gift may be pooled to permit the donor to make informed decisions as to whether or not to make a gift and whether or not to permit a gift to be invested in such fund. It is important to note that charitable funds are exempt from registration under the Investment Company Act of 1940,[214] and interests in such funds are exempt from registration under the Securities Act of 1933[215] and the Securities Exchange Act of 1934.[216] The Philanthropy Protection Act of 1995 exempts from registration under state securities registration statutes (blue sky laws) interests in charitable income funds and the offer and sale of such interests.[217] However, the Act does not provide any exemption from various anti-fraud provisions of federal and state securities laws. Those provisions continue to apply.[218]

H. Calculating the Income and Gift Tax Charitable Deduction

The first step in determining the allowable income and gift tax charitable deduction is to calculate the value of the charitable remainder interest. Commercial software is often used for that purpose, but in case a manual calculation is desired the following calculations should be reviewed. Once that value is determined, it may be used for the gift tax calculations, reporting, and disclosure. However, the income tax deduction may be lower if any limitations apply. See IV.H.4., below for the potential income tax adjustments.

The governing instrument may provide that the annuity or unitrust payment is to terminate with the regular payment preceding the termination of the payment period. This avoids the necessity of prorating the final payment to the income beneficiary or his or her estate. However, the fact that the beneficiary will not receive the final prorated payment does not affect the valuation of the remainder interest for purposes of computing the grantor's charitable contribution deduction.[219]

An income or gift tax charitable deduction is not available for a gift of a remainder interest in trust unless the trust qualifies as a charitable remainder trust (CRT) under §664.[220] The requirements for §664 qualification are discussed in detail at IV.K.2., below.

1. Valuation of an Annuity Interest

The present value of a remainder interest in an annuity trust is the net fair market value (as of the appropriate valuation date) of the property placed in trust less the present value of the annuity.[221] The appropriate valuation date for an inter vivos CRT is generally the date on which the property is transferred to the trust by the grantor.

Valuation dates for transfers after April 30, 1989, are governed by §7520. Section 7520 rejects the use of a fixed discount rate, such as the 10% and 6% rates used to value earlier transfers, in favor of a discount rate that fluctuates monthly.[222] In addition, §7520 prescribes the use of actuarial tables that reflect more recent mortality data and requires the data to be updated every 10 years. Section 7520 requires the use of a discount rate equal to 120% of the applicable federal mid-term rate under §1274(d), compounded annually and rounded to the nearest two-tenths of 1%. The monthly revenue ruling reporting the applicable federal rates also reports the §7520 rate.[223] In the case of a transfer to a charitable remainder trust for which an income, gift, or estate tax deduction is allowed, a taxpayer may elect to use the rate in effect for the month of the transfer or the

---

[209] Rev. Rul. 83-19; PLR 8220120 (other charitable remainder trusts), PLR 8212067 (endowment funds), PLR 8903019 (pooled income fund).

[210] PLR 201613015, PLR 201613014, PLR 201311036, PLR 201311032, PLR 200817038, PLR 200710013–PLR 200710016, PLR 200703037–PLR 200703038, PLR 200702040–PLR 200702041 (*modifying* PLR 200352017–PLR 200352018).

[211] See the discussion at IV.K.2.d., below.

[212] Pub. L. No. 104-62.

[213] *See* 15 U.S.C. §80a-7(e), added by Pub. L. No. 104-62, §2.

[214] Ch. 686, Title I, 54 Stat. 789 (1940). *See* 15 U.S.C. §80a-3(c)(10), amended by Pub. L. No. 104-62, §2.

[215] Ch. 38, Title I, 48 Stat. 74 (1933). *See* 15 U.S.C. §77c(a)(4), amended by Pub. L. No. 104-62, §3.

[216] Ch. 404, 48 Stat. 881 (1034). *See* 15 U.S.C. §78c(a)(12)(A), amended by Pub. L. No. 104-62, §4.

[217] Pub. L. No. 104-62, §6.

[218] *See* H.R. Rep. No. 104-333 (1995).

[219] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

[220] §170(f)(2)(A), §2522(c)(2)(A), §2055(e)(2)(A).

[221] Reg. §1.664-2(c), T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (effective June 1, 2023). *See Simmons v. United States.*, 667 F.2d 832 (9th Cir. 1982), *aff'g* 80-1 USTC ¶9,287 (D. Ariz. 1980).

[222] See XI.B.2., for the rules applicable before May 1, 1989.

[223] The Revenue Procedures giving the monthly rates are available at Tables, Charts & Lists and on the IRS website at https://www.irs.gov/applicable-federal-rates.

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

rate in effect for either of the two months preceding the transfer.[224] That election is discussed in IV.H.5., below.

Practice Point: The lower the §7520 rate, the smaller the income, gift or estate tax deduction will be. That is because as the §7520 rate rises, the annuity value is discounted more and is therefore worth less, making the value of the charitable remainder more. During the 2020 tax year, rates declined to historically low levels, due in large part to unprecedented government stimulus spending during the COVID-19 pandemic, and thus disincentivized the formation of CRATs at least as a tool to generate an income, gift or estate tax charitable deduction. In fact, at many age ranges CRATs could not be created at all because they failed the 10% remainder test of §664, the 5% exhaustion test of Rev. Rul. 77-374, or both. However, as rates rise, CRATs will be more likely to pass these actuarial qualification tests. Note that neither of these tests will deny charitable gift annuity donors a charitable deduction, although the separate 10% remainder test of §514(c)(5) may cause the charity to realize unrelated debt-financed income.

The valuation of the charitable remainder interest in an annuity trust is determined under Reg. §1.664-2(c), which states that the value of the remainder interest is equal to the fair market value of the property placed in trust less the present value of the annuity.[225] The regulation further provides that the tables in the estate tax regulations are used to value the annuity interest.[226] If the annuity is for a term of years, it is necessary to use Table B in Reg. §20.2031-7(d)(6), which contains the applicable remainder factors for §7520 rates ranging from 4.2% to 14.0%. To convert a remainder factor to an annuity factor, subtract the Table B remainder factor from 1.000000, and then divide the result by the applicable §7520 rate. This annuity factor is multiplied by the amount of the annual annuity payment to arrive at the present value of the annuity. This amount is then subtracted from the value of the property placed in trust to arrive at the value of the charitable remainder interest.

> *Example:* T creates and funds a CRAT on July 1, 20X1. The trust is funded with property with a fair market value of $100,000 and will pay T a $5,000 annuity on December 31 for 15 years. T uses the §7520 rate for July 20X1 (4.6%) because it is more favorable than the rate for June 20X1 (4.2%) or for May 20X1 (4.4%). The Table B annuity factor for 15 years at 4.6% is 10.6661.[227] This factor is multiplied by $5,000 to calculate a present value for the annuity of $53,331 and a charitable remainder value of $46,670.

[224] §7520(a) (flush language); Reg. §1.7520-2(a)(2), §20.7520-2(a)(2), §25.7520-2(a)(2). This exception facilitates planning for the amount of the deduction associated with the transfer. See Additional Resources, below, for a sample election to use the §7520 rate in effect for a prior month.

[225] Reg. §1.664-2(c), *as amended by*, T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023), applicable on or after June 1, 2023.

[226] Reg. §1.664-2(c) states that Reg. §20.2031-7(d) applies if the valuation date is on or after June 1, 2023, and that Reg. §20.2031-7A(a) through §20.2031-7A(g) applies if the valuation date is before June 1, 2023. Reg. §20.2031-7(d)(3) contains transitional rules related to valuation dates after April 30, 2019 and on or before June 1, 2023.

[227] *See* IRS Publication 1457, *Actuarial Valuations Version 4A* (providing examples of valuations using actuarial factors effective on June 1, 2023, and thereafter). Table B and the other actuarial tables can be found at https://www.irs.gov/retirement-plans/actuarial-tables.

Note that the use of Table B assumes that the annuity will be paid annually at the end of each period. If the annuity is instead to be paid at the beginning of the period (on January 1 in the Example), it is necessary to make an adjustment using Table J in Reg. §20.2031-7(d)(6), which also allows for the use of semiannual, quarterly, monthly, and weekly payments at the beginning of each interval. If the payment is made at the end of the interval, but is made more frequently than annually, adjustment factors are found in Table K of Reg. §20.2031-7(d)(6).

If the noncharitable interest in the trust uses a measuring life rather than a term of years, and the valuation date is on or after June 1, 2023, it is necessary to use the Table S factors referenced in Reg. §20.2031-7(d)(7) (and available at https://www.irs.gov/retirement-plans/actuarial-tables) to determine the value of the charitable remainder.[228] Once the proper Table S remainder factor has been determined, the value of the charitable remainder is calculated in the manner described in the Example above. If the payment is made more frequently than annually, it will be necessary to make adjustments to the value using Table K in Reg. §20.2031-7(d)(6). If the payment is made at the beginning of the period, use the Table J adjustments in the same regulation, or add the initial payment to the calculated value.

In Notice 2009-18, the IRS supplemented Tables B, J, and K, which are not based on mortality data, by providing factors for interest rates below 2.2%.[229] The applicability dates for the most recent updating of IRS tables works a little differently than in the past. Section 7520 requires the IRS to update the tables to reflect the most recent available mortality data at least every 10 years. That 10 years was up on May 1, 2019 but because the necessary mortality data was not yet available to the IRS, the final regulations (T.D. 9974) were not released until June 1, 2023. In response to comments from professional groups, the final regulations extended the transition period to provide that for valuation dates on or after May 1, 2019 and before June 2, 2023, taxpayers may elect to use either the new mortality assumptions or the mortality assumptions that were previously in effect. However, taxpayers "must be consistent in using the same mortality basis with respect to each income interest (income, remainder, partial, etc.)." As of June 1, 2023, all valuations must use the new mortality assumptions based on the 2010CM table.

2. *Valuation of a Unitrust Interest*

Calculating the value of the remainder interest in a charitable remainder unitrust (CRUT) is more complex than in an annuity interest. The present value of the remainder interest in a CRUT is determined by computing an "adjusted payout rate" and following the procedures outlined in Reg. §1.664-4(e)(3) or Reg. §1.664-4(e)(4), depending on whether the unitrust amount is to be paid for a term of years or for the life of an individual. The interest rate has little effect on the valuation of a unitrust interest.

[228] If the valuation date is after April 30, 1999, but before May 1, 2009, then Table S in Reg. §20.2031-7A(f) is used; likewise, Reg. §20.2031-7A(g) generally applies for valuation dates after April 30, 2009, but before June 1, 2023.

[229] Notice 2009-18 also supplemented the factors in the Table S, now found in Reg. §20.2031-7A(f)(4), for valuation dates after April 30, 1999, and before May 1, 2009.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

a. Adjusted Payout Rate

The adjusted payout rate for transfers made after April 30, 1989, is determined by multiplying the fixed unitrust percentage provided in the instrument by a "payout factor" contained in Table F under Reg. §1.664-4(e)(6).[230] The purpose of Table F is to adjust the basic fixed percentage for the fact that the payout sequence of the unitrust affects the amount of trust corpus that ultimately will go to the charitable remainder beneficiary. The more payouts of the unitrust amount to the noncharitable recipient or recipients (e.g., payments at the end of each month or quarter of the trust's taxable year, as opposed to one payment at the end of the year), the smaller the value of the charitable remainder interest. Table F contains subtables, each of which corresponds to a §7520 rate. It is necessary to use the subtable for the §7520 rate that applies to the valuation.

Comment: There is an inconsistency between the example contained in Reg. §1.664-4(e)(4) and Rev. Rul. 77-471.[231] In the regulations, the governing instrument provides that the trust assets are to be valued on the first day of the trust's taxable year and the unitrust amount is to be paid at the end of each calendar quarter. For purposes of selecting the payout from Table F in Reg. §1.664-4(e)(6), the example assumes that the number of months by which the valuation date (January 1) precedes the first payout date (March 31) is at least three months but less than four months. However, in Rev. Rul. 77-471, the valuation date is the first day of the trust's taxable year, and the unitrust amount is to be paid in four equal quarterly installments on the last day of each quarter. For purposes of selecting the appropriate payout factor from Table F, Rev. Rul. 77-471 states that the payout sequence is at least two months but less than three months. This longer payout sequence in the regulations would provide a slightly larger charitable deduction and would appear to be the correct and controlling result, especially since the regulations were issued after the ruling.

It is important that the unitrust instrument specifically state the date or dates on which the unitrust amount is to be paid. If the instrument does not so state, it will be assumed that the distribution of the unitrust amount or a portion thereof will be payable on the first day of the period for which the payment is made.[232] For example, if the instrument provides that the unitrust amount is to be paid in equal quarterly installments in each quarter of the trust's taxable year, but does not further provide a specific payment date, it will be assumed that the quarterly payment will be made on the first day of each quarter. As noted above, this assumption will reduce the amount of the deduction available for the gift of the charitable remainder interest.

b. Valuation Factor

Once the adjusted payout rate is determined from Table F, reference is made in Reg. §1.664-4(e)(6) to either Table D (in the event the unitrust amount is payable for a term of years) or, by cross-reference to Reg. §1.664-4(e)(5), to Table U(1) (in the event the unitrust amount is payable for the life of the individual).[233] A valuation factor is obtained from these tables by matching the adjusted payout rate with the appropriate term of years or the appropriate age of the measuring life. The appropriate age of the measuring life is the individual's age at his or her birthday nearest to the date of the transfer to the unitrust.[234] In many instances, the precise adjusted payout rate determined from Table F will not be found in either Table D or Table U(1). In such case, it is necessary either to interpolate the appropriate factor or compute the remainder exactly with software. For the first time, the final regulations permit calculation of the unitrust remainder factor using either the interpolated method, which has always been used before, or a more exact method which will require software to compute. Because the interpolated remainder factor will always be higher than the remainder factor computed using the exact method, the prior interpolated method will almost always be used to calculate the remainder in a charitable remainder unitrust. Regardless of which calculation method is selected, the taxpayer must be consistent in valuing all interests in the same transfer in the same way.[235]

> *Example:* T, who turned 60 years old on July 1, 20X1, transfers $100,000 to a charitable remainder unitrust on August 30, 20X1, when the §7520 rate is 5.0%. The trust has a taxable year ending December 31. The governing instrument requires that the trust pay to T on December 31 of each year 5% of the fair market value of the trust assets as determined on January 1 of each year for life. The adjusted payout rate is 4.762% (5% × .952381), with the payout factor taken from Table F.[236] The valuation factor is computed as follows:
>
> Factor at 4.6% at age 60 (Table U(1)) = 0.37755
>
> Factor at 4.8% at age 60 (Table U(1)) = 0.36342
>
> Difference = 0.01413
>
> (4.762% − 4.6%) ÷ 0.2% = X ÷ 0.01145
>
> Factor at 4.6% at age 60 = 0.37755
>
> Less: X = 0.36610
>
> Interpolated remainder factor 0.36610
>
> $100,000 × 0.36610 = Present value of remainder interest = $36,610.

---

[230] T.D. 9974 replaced the payout factors using updated mortality information.

[231] Note that these regulations apply only to transfers made after April 30, 1989. The regulations presumably are controlling because §7520(a)(1) states that valuations must be made "under tables prescribed by the Secretary."

[232] Reg. §1.664-4(a)(3).

[233] Reg. §1.664-4(e) applies if the valuation date is on or after June 1, 2023, although there is transitional relief that allows for the use of mortality table 2000CM for transfers made from May 1, 2019 through June 1, 2023. Table U(1) for valuation dates on or after June 1, 2023, is found at https://www.irs.gov/retirement-plans/actuarial-tables. *See also* Reg. §1.664-4(e)(7), *as amended by* T.D. 9974, applicable on or after June 1, 2023. If the transfer was made after April 30, 2009, and before May 31, 2023, and the unitrust amount is payable for the life of an individual, it is necessary to use Table U(1) in Reg. §1.664-4A(g).

[234] Reg. §1.664-4(e)(5), as amended by T.D. 9974 (for valuation dates on or after June 1, 2023), §1.664-4A(g), *as added by* T.D. 9974 (for valuation dates after April 30, 1999, and before May 1, 2009).

[235] The example uses the method shown in Reg. §1.664-4(e)(5)(iii), *as amended by* T.D. 9974.

[236] IRS Publication 1458, *Actuarial Valuations Version 4B*, is applicable for valuation dates on or after June 1, 2023.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

c. Computing the Value of the Remainder Interest

Once the appropriate valuation factor is obtained from either Table D or Table U(1), the present value of the remainder interest is determined simply by multiplying the factor by the net fair market value of the assets placed in trust.[237]

Comment: The present value of the remainder interest of the charitable trust must be at least 10% of the fair market value of the property transferred to the trust.[238] In calculating the value of the remainder, the rate stated in the trust must be used, even if the trust is a NIMCRUT that is unlikely to earn sufficient income to satisfy the stated rate. In *Estate of Schaefer*,[239] the Tax Court addressed the issue of how to value the charitable remainder interest in a net income with makeup charitable remainder unitrust (NIMCRUT). The two trusts in the case provided for distributions to the income beneficiaries during the unitrust period payable in quarterly installments. The payments equaled the lesser of: (a) the net trust accounting income for the taxable year; or (b) a percentage (11% for the first trust and 10% for the second trust) of the net fair market value of the trust assets, valued annually. The sole issue for consideration was whether the remainder interest left to a charitable organization should be valued using (a) the fixed percentage (11% and 10%, respectively), or (b) the expected net income according to the applicable §7520 rate so long as the rate was above 5%. Citing both the legislative history of the statute and the calculations contained in Rev. Proc. 2005-54, the Tax Court held that the charitable remainder interest had to be valued using a distribution amount equal to the fixed percentage.

d. Special Cases

In the case of a unitrust with two measuring lives, the valuation factor is determined using Table U(2) referenced in IRS Publication 1458, *Actuarial Valuations Version 3B*.[240] Tables are not available if there are more than two measuring lives. In addition, Table F cannot be used for a trust with a payout sequence not contained in Table F (which assumes monthly, quarterly, semiannual, or annual payouts) or for a trust that values its assets by taking average valuations on more than one date during the taxable year. Where the tables do not supply the appropriate factor, a taxpayer may request an IRS ruling as to the necessary valuation factor.[241]

Comment: If a taxpayer requests a ruling as to the appropriate valuation factor, the IRS will be free to examine the governing instrument to determine whether it qualifies under §664.

3. Additional Contributions to a Unitrust

The donor is entitled to a charitable income and gift tax deduction for the value of the property transferred to the trust, reduced by the value of the noncharitable unitrust interest. When the term of the trust is for one or two measuring lives, the calculation follows the methodology shown in IV.H.2., above. The deduction allowed may be a greater or lesser percentage of the value of the property transferred when compared to the percentage allowed for the original contribution. Although one might expect that the increased ages of the noncharitable beneficiaries would result in an increased deduction, changes in interest rates since the original funding also affect the calculation.

If the trust is for a term of years, then, unless the donor transfers property on (or close to) the anniversary date of the trust, a special calculation may be required to determine the correct charitable deduction.[242] If the software used for the deduction calculation does not accommodate a fractional year, see IRS Publication 1457 and IRS Publication 1458.

4. Income Tax Charitable Deduction: Remainder to Public Charity

Computing the fair market value of the remainder interest in a CRT is only the first step in determining the amount of the income tax charitable deduction available for the gift of that interest. The grantor also must consider the charitable deduction rules of §170, particularly the percentage limitation rules.[243] If the remainder interest has the potential to pass to a private foundation, additional limits may apply.

a. Deductibility Floor — Post-2025 Tax Years

The One Big Beautiful Bill Act (OBBBA) introduces a significant change to the charitable contributions deduction landscape by establishing a 0.5% floor for individual taxpayers.[244] Section 170(b)(1)(I) sets a threshold that must be met before charitable contributions can be deducted. Specifically, individual taxpayers can deduct charitable contributions only to the extent that their total contributions are more than 0.5% of their contribution base. In other words, the first 0.5% of contributions is not deductible.

The law also establishes a specific prioritization system for applying this floor. Once the 0.5% threshold is calculated, contributions are applied against this floor in a specified order: (1) contributions of capital gain property made for the use of charitable organizations;[245] (2) contributions of capital gain property made directly to public charities;[246] (3) other non-cash property contributions to certain organizations;[247] (4) qualified conservation contributions;[248] (5) contributions to certain public charities, private foundations, and governmental units;[249] and

[237] *See* Reg. §1.664-4(e)(4) (illustration of valuation for term of years for transfer made after April 30, 1989), §1.664-4(e)(5) (illustration of valuation for life of one individual for transfer made on or after June 1, 2023).

[238] §664(d)(2)(D).

[239] 145 T.C. 134 (2015).

[240] The regulations contain no tables for valuations using two measuring lives. IRS Publication 1458, *Actuarial Valuations Version 4B*, which is available on the IRS website, applies to valuation dates on or after June 1, 2023 and provides examples using actuarial factors from the 2010 census. The actuarial tables are available at https://www.irs.gov/retirement-plans/actuarial-tables.

[241] Reg. §1.664-4(b).

[242] Reg. §1.664-4(e)(4).

[243] For detailed discussion of the §170 rules, see 863 T.M., *Charitable Contributions: Income Tax Aspects*. Note that the requirement of §170(f)(8) that a donor obtain a written acknowledgment of the gift does not apply to gifts to charitable remainder trusts. Reg. §1.170A-13(f)(13). Supporting the continuing applicability of this exception is Reg. §1.170A-16(b), cross-referencing §170(f)(8) and Reg. §1.170A-13(f), which applies to donations made after July 30, 2018, but can be relied on for contributions made after June 3, 2004.

[244] *See* §170(b)(1)(I), as added by OBBBA, Pub. L. No. 119-21, §70425(a), effective for tax years beginning after December 31, 2025.

[245] *See* §170(b)(1)(I)(i), cross-referencing §170(b)(1)(D).

[246] *See* §170(b)(1)(I)(ii), cross-referencing §170(b)(1)(C).

[247] *See* §170(b)(1)(I)(iii), cross-referencing §170(b)(1)(B).

[248] *See* §170(b)(1)(I)(iv), cross-referencing §170(b)(1)(E).

[249] *See* §170(b)(1)(I)(v), cross-referencing §170(b)(1)(A).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

(6) cash contributions to public charities, private foundations, and governmental units subject to the 60% limit.[250]

This prioritization determines the order in which different types of charitable contributions are considered in reaching and exceeding the 0.5% threshold. Contributions are added in this order until the total exceeds the floor. Once the floor is exceeded, any additional contributions in the current category and remaining categories can be deducted, subject to other applicable limitations. Under this ordering rule, contributions higher in the priority list are taken into account first in applying the 0.5% floor, thereby increasing the likelihood that such contributions will be included in the nondeductible portion.

In tax years beginning after 2025, OBBBA imposes a new §68 itemized deduction limitation that significantly impacts charitable contributions. This limitation reduces itemized deduction by 2/37 of the lesser of the total itemized deductions or the amount of taxable income exceeding the 37% tax bracket threshold.[251] Charitable contributions, being part of itemized deductions, are subject to this limitation. The §68 limitation applies after other itemized deduction limitations and there is no provision exempting estates and trusts from its application.[252] This new rule could potentially reduce the tax benefit of charitable giving for high income taxpayers as it effectively decreases the value of itemized deductions, including charitable contributions for those taxable income surpasses the specified threshold. For more information, see 863 T.M., *Charitable Contributions: Income Tax Aspects.*

This change is set to take effect for taxable years beginning after December 31, 2025. It's important to note that this new floor and prioritization system doesn't change other existing limitations on charitable deductions; it simply adds an additional hurdle that must be cleared before any deductions can be taken.

b. Deductibility Ceilings and Reduction Rules

The deductibility ceilings impose a limitation on the deduction of charitable contributions based on a percentage of an individual's "contribution base" in the taxable year of the gift. A donor's contribution base for a given year is his or her adjusted gross income without regard to any net operating loss carrybacks.[253] The extent of the limitation depends on the type of charitable donee, the type of property contributed, and the terms of the gift. For individuals, the deductibility ceilings are as follows:

(1) 60% of the donor's contribution base for cash contributions to "50% charities;"

(2) 50% of the donor's contribution base for gifts (other than cash or qualified long-term capital gain property) to 50% charities;

(3) 30% for gifts (other than long-term capital gain property) to charities other than 50% charities or "for the use of" 50% charities or for gifts of qualified long-term capital gain property to 50% charities; and

(4) 20% for gifts of appreciated property to charities other than 50% charities.[254]

If a donor is unable to use the full amount of a charitable contribution in the year of the gift, he or she may carry over any unused portion for a period of five years.[255] In addition to the ceiling rules, certain charitable deduction reduction rules operate to reduce the amount of the contribution depending on the character of the donee and the type of property donated.[256]

c. Property Other than Long-Term Capital Gain Property to Public Charities

If a donor makes a gift of property other than qualified long-term capital gain property or ordinary income property[257] to a "50% charity," the donor is entitled to a deduction equal to the full fair market value of the property, subject to the 50% deductibility ceiling (60% for cash).[258] Types of property falling within this limitation are cash, long- or short-term capital loss property, and any property with basis in excess of fair market value. Because losses are not recognized upon donation, the donor should consider selling the loss asset and donating the cash proceeds (as a donation is not a sale or exchange that would trigger a loss).[259] However, sometimes that is not possible; there is nothing wrong with donating built-in loss property.

---

[250] *See* §170(b)(1)(I)(vi), cross-referencing §170(b)(1)(G).

[251] §68(a), as revised by OBBBA, Pub. L. No. 119-21, §70111(a).

[252] §68(b), as revised by OBBBA, Pub. L. No. 119-21, §70111(a).

[253] §170(b)(1)(H), as redesignated by the Tax Cuts and Jobs Act (TCJA), Pub. L. No. 115-97, §11023.

[254] §170(b)(1), §170(b)(1)(G), revised by OBBBA, Pub. L. No. 119-21, §70425(b), effective for contributions made after December 31, 2017 (increasing percentage limitation for cash contributions made after 2017). Note that for cash contributions made during the 2020 and 2021 tax years, individuals who itemize may elect to deduct up to 100% of his or her contribution base. Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. No. 116-136, §2205(a) (non-Code provision), applicable to tax years ending after December 31, 2019, as amended by the Taxpayer Certainty and Disaster Tax Relief Act of 2020, Pub. L. No. 116-260, Div. EE. §213. *See also* IRS News Release IR-2021-190. Under this non-Code provision, qualified contributions must be to an organization described in §170(b)(1)(A). Contributions to charitable remainder trusts are generally deductible pursuant to §170(b)(1)(B). Therefore, contributions to a charitable remainder trust generally are not qualified contributions, unless the charitable remainder interest is paid in cash to an eligible charity during the applicable time period. Additionally, a qualified charitable contribution does not include an amount that is treated as a contribution in the taxable year by reason of being carried forward from a prior contribution year under §170(b)(1)(G) or §170(d)(1). *See* Staff of J. Comm. on Tax'n, 116th Cong., Description of the Tax Provisions of Public Law 116-136, the Coronavirus Aid, Relief, and Economic Security ("CARES") Act 22-23 (J. Comm. Print 2020).

[255] §170(b)(1), §170(d).

[256] §170(e).

[257] For this purpose, "ordinary income property" includes short-term capital gain property §170(e)(1)(A).

[258] §170(b)(1)(G), revised by OBBBA, Pub. L. No. 119-21, §70425(b), effective for contributions made after December 31, 2017 (increasing percentage limitation for cash contributions made after 2017). As explained above, for cash contributions made during the 2020 tax year, individuals who itemize may elect to deduct up to 100% of his or her contribution base. CARES Act, Pub. L. No. 116-136, §2205(a) (non-Code provision), applicable to tax years ending after December 31, 2019. However, contributions to a charitable remainder trust generally are not qualified contributions, unless the charitable remainder interest is paid in cash to an eligible charity during the applicable time period. Additionally, a qualified charitable contribution does not include an amount that is treated as a contribution in the taxable year by reason of being carried forward from a prior contribution year under §170(b)(1)(G) or §170(d)(1). *See* Staff of J. Comm. on Tax'n, 116th Cong., Description of the Tax Provisions of Public Law 116-136, the Coronavirus Aid, Relief, and Economic Security ("CARES") Act 22-23 (J. Comm. Print 2020).

[259] A bargain sale is a sale or exchange; gain, but not loss, may be recognized on a bargain sale. Reg. §1.1001-1(e).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

As more fully discussed in IV.H.8., below, a gift of ordinary income property (including short-term capital gain property) is entitled to a deduction equal to the fair market value reduced by 100% of the ordinary income gain, but also subject to a 50% deductibility ceiling. Such property includes inventory and depreciated personal property used in a trade or business. These types of property are rarely used to fund charitable remainder trusts. However, this category also includes income that would be ordinary on disposition of a partnership interest, and such assets are occasionally used to fund CRTs.[260] Again, there is nothing wrong with funding a CRT with property that will not generate an income tax deduction, as long as the donor is not surprised by the limitations.

Included among "50% charities" are: (1) exempt organizations that are not private foundations by reason of being described in §509(a)(1), §509(a)(2), §509(a)(3), or §509(a)(4), such as schools, churches, hospitals, government units, and publicly supported organizations;[261] (2) private operating foundations as defined in §4942(j)(3); (3) conduit foundations as described in §170(b)(1)(F)(ii); and (4) private foundations whose assets are pooled in a donor directed fund as defined in §170(b)(1)(F)(iii).[262]

d. *Gifts to Public Charities of Appreciated Long-Term Capital Gain Property*

A donor generally will not recognize gain or loss as a result of a charitable gift.[263] A donor who contributes appreciated long-term capital gain property (i.e., property held for more than one year) to a 50% charity is entitled to a deduction equal to the full fair market value of the property, subject to a 30% deductibility ceiling.[264] A donor is entitled to a five-year carryforward for any unused portion of his or her charitable deduction.[265]

> *Example:* On March 1, 20X1, D, an individual, contributes to a church intangible property to which §1245 applies which has a fair market value of $60,000 and an adjusted basis of $10,000. At the time of the contribution D has used property in his business for more than 6 months. If the property had been sold by D at its fair market value at the time of its contribution, it is assumed that under §1245 $20,000 of the gain of $50,000 would have been treated as ordinary income and $30,000 would have been long-term capital gain. Under Reg. §1.170A-4(a)(1), D's contribution of $60,000 is reduced by $20,000.

5. *Election to Use the Prior Month's §7520 Rate*

In the case of a transfer to a charitable remainder trust for which an income, gift, or estate tax deduction is allowed, a taxpayer may elect to use the rate in effect for the month of the transfer or the rate in effect for either of the two months preceding the transfer.[266] The taxpayer must use the same rate for the valuation of all the interests involved in the transfer.

Practice Point: Generally, the taxpayer will select the highest available §7520 rate. This increases the discount factor applied to the retained interest and therefore increases the deductible value of the charitable remainder interest.

The regulations describe the procedure a taxpayer must follow to elect the §7520 rate for either of the two months preceding the transfer.[267] The taxpayer makes the election by attaching the following information to the first return on which the charitable deduction is claimed: (1) a statement that a §7520(a) election is being made; (2) a description of the interest being valued; (3) the applicable valuation date; (4) the names and identification numbers of the beneficiaries; (5) the names and birth dates of any measuring lives, a description of any relevant terminal illness of any measuring life and how such illness was taken into account in valuing the interest; and (6) a computation of the deduction showing the month and rate that have been used under the election. The election may be made for the first time on an amended return, provided that the amended return is filed within 24 months of the later of the due date of the original return or the date the original return was filed.[268] The taxpayer can revoke the election by filing an amended return within 24 months of the later of the due date of the original return or the date the original return was filed.

6. *Income Tax Deduction if the Remainder Could Pass to a Private Foundation*

In the case of a gift of long-term capital gain property to other than a "50% charity," the amount of the donor's charitable deduction is reduced by 100% of the appreciation attributable to the remainder interest.[269] In other words, the deduction is limited to basis.[270] This reduced amount is then subject to a 20% deductibility ceiling.[271]

> *Example:* The facts are the same as the example in IV.H.4. above, except that the property is contributed to a private foundation not described in §170(b)(1)(E). Under Reg. §1.170A-4(a)(1) and Reg. §1.170A-4(a)(2), D's contribu-

[260] §170(e)(1), §751.

[261] As described in §170(b)(1)(A)(vi) and Reg. §1.170A-9(f)(2), an organization is "publicly supported" if it normally receives a substantial part of its support from the general public or a governmental unit. Typically, such organizations include museums, libraries, organizations focused on specific diseases, and organizations supporting the performing arts.

[262] §170(b)(1)(A).

[263] Gain can be recognized if the property is subject to debt. See IV.L.1.b., below.

[264] §170(b)(1)(C)(i).

[265] §170(b)(1)(C)(ii).

[266] §7520(a) (flush language); Reg. §1.7520-2(a)(2), §20.7520-2(a)(2), §25.7520-2(a)(2). See also *Charitable Contribution (Individual): Prior Month Rate Election for Valuing Charitable Remainder or Lead Interests (§7520(a))* in Bloomberg Tax & Elections Compliance Statements. This exception facilitates planning for the amount of the deduction associated with the transfer. See Additional Resources, below, for a sample election to use the §7520 rate in effect for a prior month.

[267] Reg. §1.7520-2(a)(4), §1.7520-2(b), §20.7520-2(a)(4), §20.7520-2(b), §25.7520-2(a)(4), §25.7520-2(b). These regulations are generally effective for all transfers made after April 30, 1989. Reg. §1.7520-2(c), §20.7520-2(c), §25.7520-2(c). For elections made on or before June 10, 1994, Reg. §301.9100-8(a)(4)(ii) provided that the election could be revoked only with the consent of the IRS.

[268] *See, e.g.*, PLR 201518007 (extension of time granted to make election under §7520 to value charitable lead trust interest using prior month interest rate).

[269] §170(e)(1)(B)(ii).

[270] An important exception, generally not relevant to CRTs, applies to a corporation's donation of its own stock. *See* Rev. Rul. 75-348.

[271] §170(b)(1)(D).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

tion is reduced by $35,000 (100 percent of the ordinary income of $20,000 and 50 percent of the long-term capital gain of $30,000).

There is a limited exception for gifts of certain marketable stock.[272] In the case of such gifts, it is unnecessary to reduce the amount of the deduction by the amount of long-term gain, but the deduction is still subject to the 20% ceiling. The exception applies to stock held as long-term capital gain property for which market quotations are readily available on an established securities market as of the date of the contribution.[273] However, it does not apply to any stock contributed by a donor to the extent that the amount of the stock so contributed, increased by the aggregate amount of all prior contributions of such stock by the donor and certain related persons, exceeds 10% in value of all of the outstanding stock of the corporation.[274]

Caution: This exception applies to publicly traded stock, not publicly traded securities. Other types of publicly traded securities, such as bonds and partnership interests, are not included in this exception.

If a donor contributes long-term capital gain property subject to the reduction rules of §170(e) to a charitable remainder trust with a private foundation as a potential remainder beneficiary, an allocation of basis must be made between the charitable and noncharitable interests.[275] The basis allocated to the charitable interest is that portion of the basis of the entire property contributed in trust that bears the same ratio to the total adjusted basis of the property as the fair market value of the interest contributed to the charity bears to the fair market value of the entire property contributed in trust.[276]

Example: On May 1, 20X1, T transfers appreciated property (other than marketable securities) that T has held for more than one year to a CRAT. At the time of the transfer to the trust, the property has a fair market value of $250,000 and an adjusted basis in T's hands of $50,000. The §7520 interest rate for May 20X1 is 4.4%. However, T elects to use the more favorable rate of 5.0% from April 20X1. The remainder interest is payable, or could be payable, to a private foundation.[277] An annuity of $12,500 is payable to T at the end of each year for 20 years. Under Reg. §1.664-2(c), the fair market value of the remainder interest is $94,223 ($250,000 less [$12,500 × 12.4622]). Under the basis allocation rule, the adjusted basis of the property allocated to the charitable remainder interest is $18,845 ($50,000 × [$94,223 ÷ $250,000]). In accordance with §170(e)(1)(B)(ii), the amount of the deduction is limited to basis and, as a result, the donor's deduction is reduced by $75,378. The reduced amount of the gift ($18,845) would be subject to the overall 20% of contribution base limitation.[278]

Comment: Where the remainder interest in a CRT is given to a private foundation, funding the trust with appreciated property (other than qualified stock) is especially undesirable in terms of maximizing the charitable income tax deduction under §170 because of the concurrent operation of the reduction rules of §170(e) and the overall percentage of contribution base ceiling of §170(b)(1)(D).

Comment: When drafting a charitable remainder trust from the IRS sample documents,[279] to avoid this reduction it is important to describe the remainder charities as "described in §170(b)(1)(A)." Conversely, if the donor wants the remainder to pass to a private foundation, or wants to leave his or her options open, the remainder should pass to charities "described in §170(c)." The sample documents highlight these options.

7. Election to Apply 50% Deduction Ceiling

A donor may elect to have the 50% ceiling apply to gifts of appreciated property to a public charity that would otherwise be subject to the 30% limit.[280] However, there is no equivalent election for donations to private foundations. If the donor makes the election, the amount of the contribution is reduced in accordance with §170(e)(1)(B) (i.e., by 100% of the long-term capital gain attributable to the gift of the remainder interest). However, a charitable deduction is available for the reduced amount for up to 50% (rather than 30%) of the taxpayer's contribution base.

Once made, the election applies to all gifts of appreciated property during the year. In addition, the election applies to any carryovers from and to the year in which the election is made. Thus, all carryovers from previous years must be computed under the reduction rules.[281] The election generally is advisable in three situations. First, it may be advantageous to make the election where the donated property has appreciated only slightly but where the amount of the contribution is large enough that application of the "normal" 30%-of-contribution-base limitation would result in unused deductions. Second, it may be advantageous where the donor plans to make contributions of appreciated property every year in excess of the 30% limit but does not fully utilize the 50% limit. Third, the election may be advantageous where there is a high likelihood that the donor will die shortly after the gift and the donor's gifts exceed (or would exceed) the 30% limit but not the 50% limit, since the donor's death eliminates any excess deduction carryovers.

Where the election is made over a gift of a remainder interest in trust, the basis allocation rules discussed at IV.H.4., above, must be applied.[282]

---

[272] §170(e)(5). Until made permanent by the IRS Restructuring and Reform Act of 1998, Pub. L. No. 105-206, this provision was subject to several temporary extensions, not all of which were coterminous. The exception did not apply to gifts made after December 31, 1994, and before July 1, 1996.

[273] §170(e)(5)(B).

[274] §170(e)(5)(C).

[275] §170(e)(2); Reg. §1.170A-4(c)(1).

[276] Reg. §1.170A-4(c)(1)(ii).

[277] *See* Rev. Rul. 79-368.

[278] *See* Reg. §1.170A-4(d) (examples of application of rules before Tax Reform Act of 1984, Pub. L. No. 98-369).

[279] See Worksheet 2.

[280] §170(b)(1)(C)(iii).

[281] Reg. §1.170A-8(d)(2)(i)*(b)*.

[282] §170(e)(2); Reg. §1.170A-4(c)(1).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

8. Gift of Ordinary Income Property, Including Short-Term Capital Gain Property

The maximum amount of the deduction available for a contribution of any "ordinary income" property is the fair market value of the property reduced by the amount of gain that would not have been long-term capital gain if the property had been sold by the donor at the time of the contribution to charity.[283] In other words, the deduction is limited to basis or value, whichever is less.[284]

Example: If a donor purchases stock on January 1, 20X1, for $10 and contributes that stock to a charitable organization on December 31, 20X1, at which time the stock has a fair market value of $100, the amount of the deduction is $10 (i.e., the donor's basis in the property). Because the stock was not held by the donor for more than one year, all of the gain would have been short-term had the donor instead sold the stock on December 31, 20X1.

Other examples of ordinary income property are inventory and works of art created by the donor.[285] The ordinary income property reduction rule applies regardless of the character of the charitable donee.

If ordinary income property is used to fund a CRT, the donor must allocate his or her basis to the remainder interest. The computations can be somewhat complex where the property also has unrealized long-term appreciation.

Example: Assume that in the Example in IV.H.6., above, the property contributed to the trust was intangible property described in §1245 and that $100,000 of the $200,000 gain would have been ordinary income had the donor sold the property instead of contributing it to the trust. Also, assume that the charitable remainder beneficiary is not a 50% charity. The fair market value of the remainder interest is $56,964, and the basis allocable to the remainder interest is $11,393. Presumably, of the total gain of $45,571 ($56,964 − $11,393) attributable to the charitable gift, $22,785.50 ($45,571 × [$100,000 ÷ $200,000]) would be treated as the §1245 ordinary gain attributable to that gift. The charitable gift of $56,964 would be reduced by the sum of this ordinary income for a deduction of $34,178.50. Since the charitable remainder beneficiary is not a 50% charity, the gift is further reduced by 100% of the long-term gain attributable to the remainder interest. In such case, the amount of the deduction would be limited to the $11,393 basis ($34,178.50 − $22,785.50 [long-term gain]).

9. Gift of Tangible Personal Property

Care should be taken before funding an inter vivos charitable remainder trust with tangible personal property, because the donor may not be entitled to an immediate charitable income tax deduction.[286] Section 170(a)(3) provides that a charitable contribution of a future interest in tangible personal property is complete only when all intervening interests in, and rights to the actual possession or enjoyment of, the property have expired or are held by persons other than the donor or those standing in a relationship to the donor described in §267(b) or §707(b).

For example, §170(a)(3) applies where an individual conveys a painting to a museum but retains the right to the use, possession, and enjoyment of the painting during his or her lifetime. Under these circumstances, no deduction is available under §170 for the gift of the future interest to the museum at the time the transfer is made.

The regulations under §664 suggest that in certain circumstances §170(a)(3) will apply to gifts made to a CRT, stating in part: "For rules for postponing the time for deduction of a charitable contribution of a future interest in tangible personal property, see section 170(a)(3) and the regulations thereunder."[287]

An example in the regulations[288] considers a gift of a painting to a pooled income fund maintained by a university. The donor retained a life interest in the painting. The example concludes that no charitable contribution is considered to have been made in the year the painting was transferred to the pooled income fund because the contribution consisted of a future interest in personal property. However, if the intervening income interest had been given to an unrelated individual, an immediate charitable deduction would have been allowed.[289] It is also possible that the donor's deduction, once deferred by §170(a)(3), may nevertheless be allowed in a later taxable year if the transferee (i.e., the trustee of a pooled income fund or charitable remainder trust) disposes of the tangible personal property. At that time, the donor's interest in the transferred property would no longer relate to tangible personal property.

In PLR 9452026, the IRS considered the income and gift tax consequences of a gift of a musical instrument to a CRAT. The taxpayer's representations were that the musical instrument was used by the taxpayer in his profession, that the taxpayer was not a dealer in this type of musical instrument, and that the taxpayer had never depreciated the musical instrument. The IRS ruled that because the musical instrument was tangible personal property, §170(a)(3) prevented any deduction for the remainder interest so long as the taxpayer retained an income interest in the musical instrument. However, an income tax deduction would be allowed when the trustee sold the musical instrument. At that time, the taxpayer would possess only

[283] §170(e)(1)(A). Property that, if sold at fair market value, would generate in whole or in part gain other than long-term capital gain is referred to herein as "ordinary income" property. *See* Reg. §1.170A-4(b)(1).

[284] An important exception, generally not relevant to charitable remainder trusts, applies to a corporation's donation of its own stock. Rev. Rul. 75-348.

[285] *See* §1221, §1231. In general, "property used in a trade or business" as defined in §1231(b) is treated as a capital asset (i.e., not ordinary income property) for purposes of the rules of §170(e), except to the extent §617(d)(1), §1245(a), §1250(a), or §1252(a) applies to any gain involved. Reg. §1.170A-4(b)(4).

[286] §170(a)(3), §267(b), §707(b); Reg. §1.664-2(d); Rev. Rul. 73-610, Rev. Rul. 69-63. In addition, the value of appreciated tangible personal property, whether contributed to a public charity or a private foundation, must be reduced by 100% of the long-term capital gain if the property is not related to the organization's exempt purpose or function. §170(e)(1)(B)(i); Reg. §1.170A-4(a)(3).

[287] Reg. §1.664-2(d), §1.664-3(d).

[288] Reg. §1.170A-5(b) *Ex.* 6.

[289] Related persons include, for example, the taxpayer's brothers, sisters, spouse, ancestors, and lineal descendants. §267(b)(1), §267(c)(4).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

an income interest in the sale proceeds. Because the gift of the musical instrument would be for an unrelated use, the taxpayer's deduction would be reduced to that portion of his basis allocable to the remainder interest in the musical instrument under §170(e)(1)(B)(i).[290]

Comment: Once the personal property is sold, thus completing the gift, perhaps it is then considered a donation of cash rather than personal property. No official guidance is available on this point.

Practice Point: If funding a charitable remainder trust with tangible personal property, establish the trust early enough in the donor's tax year to allow time to sell the property so that the deduction will be allowed in the year the trust is funded. Although the income tax deduction may be relatively small, the ability to exclude taxable gain from the donor's income may make the donation worthwhile, especially given the income tax rates applicable to collectibles.[291] Note also that continued use of the instrument by the donor after the contribution would be subject to the self-dealing excise taxes imposed by §4941(d)(1)(E).

10. Gift "to" or "for the Use of"

Deductions for gifts "for the use of" charities are limited to 30% of the donor's contribution base.[292] A gift is considered to be "for the use of" where it is held in trust for the continuing benefit of the charity. A gift of a remainder interest in a charitable remainder trust or a pooled income fund is considered a gift of the remainder interest "to" the charity and, assuming a gift of cash or other qualifying property, is subject to the 50% limitation (60% for cash),[293] provided the remainder interest is to be distributed outright to the charity upon the termination of the intervening noncharitable interests. In such case, the donor is entitled to deduct the fair market value of the remainder interest to the extent of 50% (or 60%) of the donor's contribution base, assuming the trust is not funded with long-term appreciated property and the remainder beneficiary is a public charity. However, if the trust corpus is to be held in further trust for the benefit of the charitable remainder beneficiary, the gift of the remainder interest is considered to be "for the use of" rather than "to" the charitable remainder beneficiary, and the gift is limited to 30% of the donor's contribution base where the remainder beneficiary is a public charity.[294]

Example: The donor transfers cash to an annuity trust that is required to pay to B for life an annuity equal to 5% of the initial fair market value of the property transferred in trust. The trust provides that after B's death, the remainder is to be distributed to a charity, C. The contribution of the remainder interest is considered as made "to" C. However, if the trust instrument directs that after B's death the remainder interest is to be held in further trust for the benefit of C, the contribution is considered as made "for the use of" C.

11. Interaction of the Percentage Limitations and Five-Year Carryforward

The 50%, 30%, and 20% limitation ceilings are inclusive. Thus, the 30% limit and the 20% limit are not in addition to the 50% ceiling but are separate limitations within the overall 50% ceiling.[295] Unless the donor makes a cash contribution in excess of 50% of his or her AGI, the overall limitation will be 50%.

Where amounts are carried over into succeeding years, gifts made in the succeeding years are taken into account first when applying the limitations. For contributions made after 2017, when the 60% limitation for cash contributions is applicable, the following priority is used where amounts are carried over into succeeding years:

(1) current gifts of cash to 50% charities (60% limitation);

(2) carryover gifts of cash to 50% charities (60% limitation);

(3) current gifts of 50% property;

(4) carryover gifts of 50% property (oldest first);

(5) current gifts of 30% property;

(6) carryover gifts of 30% property (oldest first);

(7) current gifts of 20% property; and

(8) carryover gifts of 20% property (oldest first).[296]

Example: In 2024, T gives $40 in cash to a public charity (60% ceiling), $10 of long-term capital gain property to the same public charity (30% ceiling), and $20 of qualifying stock to a private foundation (20% ceiling). T's contribution base is $100. T must first use all $40 of the 60% property and then all $10 of the 30% property. The $20 of 20% property is carried over, retaining its character. If T could have chosen the contributions to be applied toward the ceilings, T would have used $20 of the 20% property, $10 of the 30% property, and $20 of 50% property. T would then have carried over $30 in 50% property.

For taxable years beginning after December 31, 2025, when the 0.5% floor on individual charitable contributions applies, additional complex carryforward rules may apply.[297]

[290] This private letter ruling contains a misleading analysis of the percentage limitation of the taxpayer's contribution base applicable to a gift of the musical instrument.

[291] §1(h)(4).

[292] §170(b)(1)(B).

[293] §170(b)(1)(G), revised by the OBBBA, Pub. L. No. 119-21, §70425(b), effective for contributions made after December 31, 2017 (increasing percentage limitation for cash contributions made after 2017). The OBBBA also establishes a 0.5% floor on charitable contribution deductions for individuals, allowing deductions only for an aggregate amount that exceeds 0.5% of the individual taxpayer's contribution base, with specific prioritization for different types of contributions. *See* §170(b)(1)(I), as added by OBBBA, Pub. L. No. 119-21, §70425(a), effective for tax years beginning after December 31, 2025. *See also* IV.H.4.a., above.

[294] Reg. §1.170A-8(a)(2).

[295] §170(b)(1).

[296] *See* §170(b)(1)(C)(ii), §170(b)(1)(D)(ii), §170(d)(1).

[297] *See* §170(d)(1)(C), as added by OBBBA, Pub. L. No. 119-21, §70425(a). *See also* §170(b)(1)(I); IV.H.4.a., above.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

12. Gift of Certain Intellectual Property

A donor's initial income tax charitable deduction for a contribution of a patent, copyright (other than a §1221(a)(3) or §1231(b)(1)(C) patent or copyright), trademark, trade name, trade secret, know-how, software (other than §197(e)(3)(A)(i) software), or similar property, or applications or registrations of such property, is limited to the donor's basis in the property or, if less, the property's fair market value.[298] However, the donor may be entitled to an income tax charitable deduction for certain additional amounts in the year of contribution or in subsequent taxable years based on a specified percentage of the "qualified donee income" received or accrued by the donee on such property.[299] The additional deduction is not available for income received or accrued by the donee after the expiration of the property's legal life or after the 10th anniversary of the contribution date.[300]

Thus, the income tax charitable deduction of a donor funding a CRT with one of the specified types of intellectual property is generally limited to the basis of the property. To obtain a deduction for any additional amounts, the charitable remainder beneficiary cannot be a private foundation (other than a §170(b)(1)(F) private foundation)[301] and, if the trust terminates while the additional deduction is available, the charitable remainder beneficiary must generate qualified donee income on the property. Also, since one of the requirements for the additional deductions is that the donee must be notified at the time of the contribution, the donor must notify the remainder charity at the time the trust is funded.[302]

It seems unlikely that income earned while the property is held in the trust would qualify, because some or all of it would be payable to the CRT beneficiary, not to the donee.[303]

For more information on §170(e)(1)(B)(iii) and §170(m), see 863 T.M., *Charitable Contributions: Income Tax Aspects*.

I. Gift Tax

Only the creation of an inter vivos charitable remainder trust (CRT) will give rise to gift tax consequences, because the gift tax has no application to testamentary charitable remainder trusts. A CRT is composed of two distinct interests: a noncharitable annuity or unitrust interest and a charitable remainder interest. Each interest involves different gift tax considerations.

The gift tax consequences also vary based on the initial and contingent successor beneficiaries, and whether the donor has retained the right to change or revoke the beneficiaries' interests. Additional favorable rules apply if the donor's U.S. citizen spouse is the only other beneficiary of the trust. Each possible situation is addressed separately below. For gift tax return filing requirements, see IV.L.2., below.

Whether a gift is complete or incomplete for gift tax purposes does not affect the charitable income tax deduction.[304]

The present value of the annuity or unitrust interest created by the grantor in another individual generally is a taxable gift as of the date on which the irrevocable charitable remainder trust is created and funded. If there is a taxable gift, the value of the gift of the annuity or unitrust interest is the present value as computed in accordance with the rules discussed at IV.H., above. When additional contributions are made to a unitrust, the gift is valued in the same manner as the initial contribution to the unitrust. Detailed discussions concerning the creation and taxation of gifts are found in 845 T.M., *Gifts*.

1. Donor Is the Only Noncharitable Beneficiary

The creation of an inter vivos charitable remainder trust will have gift tax consequences only if an individual other than the grantor is designated as the recipient of the annuity or unitrust amount. The donor/grantor does not make a taxable gift where he or she retains the annuity or unitrust interest for life or for a period of years and is the only noncharitable beneficiary.

If the donor has retained the right to change the remainder charity, the gift is incomplete for gift tax purposes.[305] Therefore, although it is not wrong to report the gift as an incomplete gift on a gift tax return, there is no advantage to doing so.[306]

If the donor has irrevocably named the remainder charity, there is still no gift tax filing requirement[307] (although there is no harm in filing a gift tax return).

2. Donor or U.S. Citizen Spouse (or Both) Are the Only Noncharitable Beneficiaries

Section 2523(g) provides that a gift tax marital deduction is automatically available for the gift to the donor's spouse, as the sole noncharitable beneficiary other than the donor, of an annuity or unitrust interest in a CRT.[308] Transfers to a CRT in which the transferor's spouse receives the annuity or unitrust interest will not be eligible for a QTIP election, because the spouse will not receive a qualifying income interest in the property.[309]

The marital deduction provision does not apply to the creation of an annuity or unitrust interest in a spouse if a similar interest is created in another individual other than the donor. For example, a donor was denied a marital deduction where the donor created a unitrust interest in his brother and a secondary unitrust interest in his wife.[310]

[298] §170(e)(1)(B)(iii), effective for contributions made after June 3, 2004. A donor who contributes property described in §170(e)(1)(B)(iii) and claims a charitable income tax deduction of over $500 must comply with the notice and substantiation requirements of §170(f)(11)(B) (but not §170(f)(11)(C) or 170(f)(11)(D)). *See* §170(f)(11)(A)(ii)(I).

[299] §170(m).

[300] §170(m)(5), §170(m)(6).

[301] §170(m)(9) (cross-referencing §170(e)(1)(B)(ii)).

[302] §170(m)(8)(B).

[303] §170(m)(3).

[304] *See, e.g.*, PLR 9326049.

[305] Reg. §25.2511-2(c).

[306] Reg. §301.6501(c)-1(f)(5).

[307] §6019(3)(A)(ii).

[308] *See, e.g.*, PLR 200813006. Note that the IRS has *removed* the following from its no-rule list beginning in 2023: (1) "[w]hether an estate is entitled to an estate tax marital deduction for any portion of the annuity or unitrust interest of a charitable remainder trust (as described in §664) that may be distributed between the decedent's spouse and an organization described in §170(c) at the discretion of a trustee"; and (2) "[w]hether a donor is entitled to a gift tax marital deduction for any portion of the annuity or unitrust interest of a charitable remainder trust (as described in §664) that may be distributed between the donor's spouse and an organization described in §170(c) at the discretion of a trustee."

[309] *See* §2523(f)(2)(B), §2056(b)(7)(B)(ii).

[310] TAM 8730004.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

The most common structure for a CRT that includes a spouse as a beneficiary is for the donor to name the spouse as a contingent successor beneficiary, but to retain the testamentary right to revoke the spouse's successor interest. (If the trust is funded with community property, the retained interest is typically joint and survivor.) The contingency is that the spouse must survive the donor to receive the successor interest. This allows the donor the maximum flexibility: should the couple divorce, the testamentary documents can be amended to revoke the ex-spouse's interest. If the couple has sufficient other resources, the successor interest can be revoked to accelerate the charitable transfer. Also, by making the spouse's interest an incomplete gift, gift tax reporting is avoided. The estate tax consequences are not altered by the retention of the revocation right: a charitable remainder trust with a retained interest by the donor will be included in his or her taxable estate under §2036 (transfer with a retained life estate), so the retention of additional rights will not change the estate tax outcome.[311]

The trust may be drafted to include a qualified contingency (e.g., divorce) that would accelerate the charitable remainder without impairing the marital deduction.[312] Such a trust is a clear advantage over a lifetime QTIP trust, which cannot qualify for the marital deduction if it includes such a contingency.

If the donor spouse does not want to retain the right to revoke the spouse's contingent successor interest, then the gift should be reported on the donor's Form 709. Although the marital portion of the transfer is excluded from gift tax reporting under §6019(2), the split interest portion is no longer excluded under §6019(3)(A)(ii). Thus, no gift tax reporting is required. The marital deduction for any interest passing to a spouse is automatic under §2523(g). No QTIP election under §2523(f) is required or possible.[313] The same tax and reporting rules apply if the donor gives the annuity or unitrust interest to his or her spouse outright rather than giving him or her a successor interest.

Note: Section 2523(g) does not apply to spousal interests in pooled income funds. See the discussion at XV.D., below.

3. Donor and Noncharitable Beneficiaries Other than a U.S. Citizen Spouse

A donor may want to give a contingent successor interest to his or her children or other non-spouse beneficiaries. The interest may take effect either after the donor's death or after the death of the donor and his or her spouse.

Practice Point: If the donor wants to give his or her spouse an invasion power (e.g., for medical expenses) but preclude invasion by successor beneficiaries, consider an inter vivos or testamentary QTIP trust that will become a charitable remainder trust after the death of the spouse. The gift or estate tax marital deduction is allowable for the interest passing to the spouse if appropriately elected.[314] A charitable deduction will be allowed to the spouse's estate for the value of the remainder interest.

The regulations provide that the grantor may retain the testamentary right to revoke the annuity or unitrust interest of a noncharitable recipient.[315] If the grantor retains the testamentary power to revoke or terminate the annuity or unitrust interest of any recipient, the creation of such interest is not a completed gift for gift tax purposes.[316]

Practice Point: Where a donor wishes to create a successor unitrust or annuity trust interest in an individual that does not qualify for the marital deduction, the donor should retain the testamentary right to revoke the successor interest. This will avoid the creation of a completed taxable gift at the time of the creation of the trust.[317] The transfer will be completed only on the donor's death or his or her earlier renunciation of the testamentary power. If the power is relinquished, a taxable gift occurs at that time. If the power is retained until the donor's death, the full value of the trust will be included in the donor's estate under §2036.[318]

If the donor does not retain the right to revoke the interests of the successor beneficiaries, there are immediate gift tax consequences. If the donor retains an annuity interest, or a "straight" unitrust interest (i.e., with no net income limitations), the special valuation rules of Chapter 14 will not apply to the gift. The taxable gift will be the value of the property transferred to the trust less the donor's retained interest and the value of the charitable remainder.[319] The annual gift tax exclusion is not available for the gift of an annuity or unitrust interest that commences on the occurrence or nonoccurrence of a future event, because it is a gift of a future interest.[320] Future interests include the amount payable to a secondary life beneficiary vesting upon the termination of a period of years or after termination of a preceding life estate.

> *Example:* C transfers certain insurance policies on his own life to a trust created for the benefit of D. Upon C's death the proceeds of the policies are to be invested and the net income therefrom paid to D during his lifetime. Since the income payments to D will not begin until after C's death the transfer in trust represents a gift of a future interest in property against which no exclusion is allowable.

If the donor does not retain the right to revoke a nonspousal successor interest in an "income exception CRT" (a NICRUT, NIMCRUT or FLIP-CRUT, as discussed at IV.C., above), the gift tax consequences are more severe.

Under §2702(a), an interest retained by the transferor or any applicable family member in a trust for the benefit of a family member is valued at zero, unless the retained interest is a qualified interest. Section 2702(a) does not apply to charitable remainder annuity trusts or to unitrusts that do not use the income exception.[321] Under Reg. §25.2702-1(c)(3), for transfers made on or after May 19, 1997, the unitrust interests of the

---

[311] *See* PLR 9326049. See Reg. §20.2036-1(b)(2) for guidance calculating the portion of a CRT with a retained life estate that must be included in a decedent's estate.

[312] *See* PLR 9511029.

[313] Reg. §25.2523(g)-1. *See* PLR 9707027.

[314] See 843 T.M., *Estate Tax Marital Deduction*, and 845 T.M., *Gifts*, for further discussion of the marital deductions.

[315] Reg. §1.664-2(a)(4), §1.664-3(a)(4).

[316] Rev. Rul. 79-243. *See, e.g.*, PLR 9326049.

[317] *See* PLR 201714002. *See also* Reg. §25.2511-2(c).

[318] Reg. §20.2036-1(a)(3)(ii).

[319] Reg. §25.2702-1(c)(3), §25.2522(c)-3(d).

[320] Reg. §25.2503-3(c) *Ex.* 2.

[321] Reg. §25.2702-1(c)(3).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

donor or any applicable family member in a charitable remainder unitrust using an income exception method will be valued at zero under §2702 when someone other than the donor, the donor's U.S. citizen spouse, or both the donor and the donor's spouse (who is a U.S. citizen) are noncharitable beneficiaries of the trust, unless such person holds the first of two consecutive noncharitable interests and the donor holds the second. If the Chapter 14 valuation rules apply, any interest retained by the donor (and his or her spouse) are valued at zero, thus substantially increasing the taxable gift. For further discussion of the Chapter 14 valuation rules, see 836 T.M., *Partial Interests — GRATs, GRUTs, and QPRTs (Section 2702).*

Comment: The reason for the 1997 change in the regulations was that the IRS realized it would be possible to manipulate trust accounting income and therefore defer the receipt of the trust accounting income until after the interest retained by the donor had expired. The taxable gift of a successor income interest might be relatively small compared to the amount of actual income that could be received through a "make-up" distribution. Such manipulation would not affect the amount received by the donor from an annuity trust or "straight" unitrust, so the exception to the Chapter 14 rules was allowed to continue for those trusts.[322]

4. Donor and Non-Citizen Spouse

If the donor's spouse is not a U.S. citizen, it is still possible to give the surviving spouse a successor interest in a CRT.[323] See 842 T.M., *Transfers to Noncitizen Spouses*, for further discussion of the applicable gift and estate tax issues.

5. Donor and Spouse Retain No Interest in the Trust

The donor may give the unitrust or annuity interest to a child or other person. (If a grandchild or other skip person is involved, see the discussion of the generation-skipping transfer tax in IV.J., below.) This is a completed taxable gift when the trust is funded, unless the donor retains the right to revoke the noncharitable beneficiary's interest.[324] The special valuation rules of Chapter 14 do not apply, even if the CRT is an "income exception" trust (as discussed in IV.C., above), because the donor and his or her spouse do not retain any interest in the trust. Therefore, the taxable gift is the amount of the transfer to the trust, reduced by the value of the charitable remainder interest as calculated in IV.H., above. If the gift is complete, a gift tax return to show the taxable gift, and possibly to elect gift splitting, must be filed. If the gift is incomplete, then a gift tax return is due annually as the distributions are made.[325] An outright gift of an income interest, or the annual distribution if the initial gift was incomplete, qualifies for the annual gift tax exclusion.[326]

The gift tax annual exclusion is available only in the case of a gift of a present interest.[327] The gift of an annuity or unitrust interest will qualify as a present interest where the trustee is required to make annual distributions.[328]

Courts have held that the annual exclusion is not available for the gift of an income interest where non-income-producing property is transferred to a trust that was not a charitable remainder trust.[329] However, this analysis should not apply to a charitable remainder annuity trust or unitrust, provided the governing instrument requires payment of a specified amount or percentage. In such case, the trustee is required to make the annual payments even if the amounts exceed income. The only exception would be a net income unitrust that provides for payment of the lesser of a specified percentage or annual income.

For gift tax purposes, the beneficiaries of the trust are considered the donees of a gift made in trust. If the trust has more than one vested beneficiary, the gift is deemed to have been made to each beneficiary in proportion to his or her respective interest in the trust, and a separate annual exclusion is available for each beneficiary. An annual exclusion is not available for a gift to a "sprinkle trust" where the trustee has the sole discretion to distribute income among a class of beneficiaries in such amounts and proportions as the trustee sees fit. In such case, the gift is not subject to valuation on the date of the initial transfer, because the amount actually distributed is within the sole discretion of the trustee.[330] It is the right of a beneficiary to receive the distributions that determines the availability of the exclusion and not the actual distributions. For example, a unitrust that provides for payment of the lesser of a specified percentage or actual trust income (but not funded with non-income-producing property) should qualify for the annual exclusion, even though it is possible that the beneficiary may not receive any distribution in a particular year when the trust has no income.[331]

Practice Point: If a sprinkling trust is desired, the donor should not be the trustee; that arrangement would create a grantor trust. See IV.G.1., above.

Practice Point: If the donor retains the testamentary right to revoke individual beneficiaries' interests, the initial gift will be incomplete, distributions from the trust will be completed gifts subject to the gift tax annual exclusion, and the trust will be included in the donor's taxable estate under §2038. If the beneficiaries in such a trust are grandchildren of the donor (or other "skip persons") the generation-skipping transfer (GST) tax consequences can be unexpected. See the discussion of GST at IV.J., below.

6. Gift Tax Rules Applicable to the Charitable Remainder

Assuming all qualifications for a charitable remainder trust are met, a charitable gift tax deduction will be available

[322] T.D. 8791, 63 Fed. Reg. 68,188 (Dec. 10, 1998).

[323] *See* PLR 9244013.

[324] *See* PLR 8949061 (donor retained right to revoke each of seven beneficiaries' interests; gift was only complete as distributions were made each year from trust, allowing annual distributions to qualify for gift tax annual exclusion).

[325] *See* PLR 8949061.

[326] *See* PLR 8949061.

[327] §2503(b). The amount of the exclusion, originally $10,000, is indexed for inflation in $1,000 increments beginning in 1999, using 1997 as the base year. §2503(b)(2). In PLR 8637084, the IRS ruled that a unitrust interest payable for a term of years qualified for the annual exclusion.

[328] Reg. §25.2503-3(b). *See, e.g., Commissioner v. Sharp*, 153 F.2d 163 (9th Cir. 1946); *Commissioner v. Lowden*, 131 F.2d 127 (7th Cir. 1942).

[329] *See Maryland Nat'l Bank v. United States*, 609 F.2d 1078 (4th Cir. 1979); *Berzon v. Commissioner*, 534 F.2d 528 (2d Cir. 1976); Rev. Rul. 76-360.

[330] Reg. §25.2503-3(c) *Ex.* 3; Rev. Rul. 55-303.

[331] Reg. §25.2503-3(b).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

for the value of the remainder interest as calculated at IV.H., above. The following are issues that should be addressed to be sure the gift tax deduction is available if needed. Also, if the donor has retained an interest in the trust, and the estate tax will be relevant to the donor, the estate tax deduction criteria should be reviewed. If the donor retains an interest in the trust, the trust will be included in his or her taxable estate (giving the trust assets new basis under §1014). Thus, the estate tax charitable deduction, not just the gift tax charitable deduction, will be relevant. This applies whether the gift was originally complete or incomplete.[332]

a. Incomplete Gifts

Section 2522(a) provides a gift tax deduction for transfers to be used exclusively for public, charitable, and religious purposes. Unlike the income tax charitable deduction, the gift tax charitable deduction is subject to no percentage limitations. In many cases, the charitable remainder interest will be an incomplete gift because the donor has retained the right to change the charity. As discussed above, a gift is incomplete where the donor reserves the power to alter the beneficial enjoyment of the beneficiaries. In PLR 9707027, the grantor of a CRUT retained the power to name new charitable remainder beneficiaries and/or to alter the interests of the remainder beneficiaries. The transfer of property to the trust was an incomplete gift of the remainder interest and was not subject to gift tax.[333]

If a charitable remainder trust includes a provision allowing an independent trustee to sprinkle the annual payment between the donor/beneficiary and charities chosen by the donor, the gift to the lead charities is incomplete until the designation is made. This is important because otherwise the portion of the annual payment that could go to the lead charities may be a taxable gift not qualifying for the gift tax charitable deduction because it is unascertainable.[334]

b. Completed Gifts

If the donor does not retain the right to change the charity, or relinquishes the right to change the charity during his or her lifetime, the gift of the remainder interest will be complete. Assuming all qualifications are met, a charitable gift tax deduction will be available for the value of the remainder interest as calculated at IV.H., above. A gift tax charitable deduction is permitted for a charitable gift of a remainder interest made after July 31, 1969, only if it is in the form of a charitable remainder annuity trust, a charitable remainder unitrust, or a contribution to a pooled income fund.[335]

The regulations impose certain conditions on transfers that are not exclusively for charitable purposes. A gift tax charitable deduction may be taken for a remainder interest only where the interest is presently ascertainable and severable from the noncharitable interest.[336] In Rev. Rul. 80-83, the donor was a cotrustee of a CRUT and also a director of a publicly held corporation, the stock of which comprised the entire corpus of the trust. Any sale of the stock was subject to a right of first refusal by the corporation. In valuing the stock, the trustees consistently adopted the valuation established by the corporation in exercising its right of first refusal. The IRS ruled that because the donor was bound by fiduciary duty to exercise independent judgment on behalf of both the trust and the corporation in valuing the stock, the value of the charitable remainder was ascertainable within the meaning of the regulations.

Comment: This ruling leaves several questions unanswered. First, it is not clear to what extent the regulations relating to "ascertainability and severability" are applicable to charitable remainder trusts in view of the strict §664 rules that seek to insure a charity's interest in the remainder, and the separate reference to charitable trusts in the same regulation.[337] Second, although the holding is limited to the initial deduction, the ruling appears to sanction the trust's continuing tax-exempt status as well. Lastly, the unusual nature of the corporate arrangement set forth in the ruling in effect limits the precedential value of the ruling to situations where the corpus consists of stock of a closely held corporation. It is rare for a publicly held corporation to hold a right of first refusal in the shareholder's stock.

c. Reformation if Document Is Defective

See V.E., below, for a discussion of the authorities concerning reformation under §2055(e)(3). Although this is an estate tax provision, the gift tax provision is cross-referenced to it.[338]

d. The 5% Exhaustion Rule

The "5% rule" discussed at IV.D.3., above, may cause disallowance of the gift tax charitable deduction for a CRAT if the test is failed.[339]

e. The 10% Minimum Charitable Remainder Value Requirement

Failure to satisfy the minimum charitable benefit rule (i.e., the requirement that the present value of the charitable remainder interest be at least 10% of the fair market value of the property contributed), discussed at IV.D.2., above, will cause disallowance of any gift tax charitable deduction.[340]

f. Identity of Charitable Remainder Beneficiaries

The charitable remainder beneficiary must satisfy the requirements of both §2522(a) and §170(c) for the gift to qualify for the charitable deduction.[341] The category of organizations qualifying for an income tax charitable deduction is not identical to the class qualifying for a gift tax charitable deduction. To ensure that a gift tax charitable deduction is allowed, the governing instrument should expressly limit the ultimate distribution of the transferred property to one or more organizations described in both §170(c)[342] and §2522(a). This is also discussed at IV.F.1., above. In Rev. Rul. 76-371, a gift tax deduction was allowed where the trustee had the power, exercisable during the

[332] §2036, §2038.
[333] *Citing* Reg. §25.2511-2(c).
[334] Reg. §25.2511-2(c); PLR 201845014.
[335] §2522(c)(2)(A).
[336] Reg. §25.2522(c)-3(a).
[337] Reg. §25.2522(c)-3(c)(2)(v).
[338] §2522(c)(4).
[339] Rev. Rul. 77-374.
[340] §2522(c)(2)(A), §664(d)(1)(D), §664(d)(2)(D).
[341] Reg. §25.2522(c)-3(c)(2)(v).
[342] If the income tax deduction allowable for gifts to public charities is desired, the document should refer to §170(b)(1)(A) rather than §170(c).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

grantor's life, to add and/or substitute additional organizations described in §170(b)(1)(A) as remainder beneficiaries, because any such organization would also be described in §2522(a).

> *Example:* If the remainder beneficiary of an otherwise qualified CRT is a cemetery organization, an income tax charitable deduction will be allowed but a gift tax charitable deduction will not. This is because — although the remainder beneficiary is described in §170(c)(5) and, thus, satisfies the §664 requirements — it does not qualify under §2522(a)(2).

In Rev. Rul. 76-307, the governing instrument of a unitrust provided that the remainder interest would be paid to a foundation that qualified as an organization described in §170(c) and §2522(a) and §2522(b) at the time of the transfer. The governing instrument further provided that if, upon termination of the trust, the foundation was not an organization described in §170(c), distribution of the remainder would be made to one or more organizations that qualified under §170(c) as selected by the trustee.

The governing instrument in the ruling did not require that any alternative remainder beneficiary also qualify as a §2522(a) organization at termination of the trust. Reg. §25.2522(c)-3(b)(1) provides that a gift tax charitable deduction will be allowed if the interest is vested in a charity on the date of the transfer even if the interest is subject to divestment upon the performance of some act or the occurrence of a future happening, provided that the likelihood that the event will take place is so remote as to be negligible. Rev. Rul. 76-307 concluded that a gift tax charitable deduction was permitted, because the foundation qualified under §170(c) and §2522(a) at the time of the transfer in trust and the possibility that the foundation would not continue to be an organization described in both sections was so remote as to be negligible.

Although Rev. Rul. 76-307 does not state the basis on which the IRS made this determination, Rev. Rul. 80-38 provides some clarification. Rev. Rul. 80-38 discusses the applicable income tax charitable deduction percentage limitation in the case of a CRT providing that if the designated charitable remainder beneficiary, a §170(c) organization also a public charity described in §170(b)(1)(A), is not described in §170(c) at trust termination, the trustee must select another §170(c) organization. The ruling concludes that "[b]ecause the designated organization in the present case is a public university, there is a small likelihood that it will cease to exist as an organization described in sections 170(c) and 170(b)(1)(A)." The governing instrument also failed to limit the alternative remainder beneficiary to an organization described in §2522(a) in addition to §170(c). Rev. Rul. 80-38 suggests that a gift tax charitable deduction would have been permitted where the designated remainder beneficiary was a public university even though there was a possibility that another organization not qualifying under §2522(a) could be named. It remains unclear whether the IRS would extend this presumption to other organizations and, if so, what types of organizations would qualify for the presumption. Thus, the governing instrument should contain the appropriate limiting language to ensure that a gift tax charitable deduction is allowed. The IRS sample documents include appropriate language and highlight this issue.

g. Section 508

As discussed at VI.G.1.a., below, §508(d)(2) requires trusts described in §4947 (which generally include CRTs) to include certain provisions in their governing instruments. Failure to include these provisions will cause the disallowance of a gift tax charitable deduction. Charitable remainder trust documents do not need to include all of the private foundation provisions, only those that apply to CRTs.[343] However, if the trust will continue as a private foundation after the noncharitable interests expire, all private foundation provisions should be included. The IRS sample documents highlight this issue and provide alternative clauses. Many documents include the full set of private foundation provisions specifically or by reference; there is nothing wrong with including them.

h. Amount of Charitable Deduction

The amount of the deduction for the remainder interest is discussed at IV.H., above.

If a designated charitable remainder beneficiary also receives a portion of the annuity or unitrust amount, a charitable gift tax deduction is available for the creation of an annuity or unitrust interest in the charitable remainder beneficiary.[344] However, an income tax deduction is not available for the value of an annuity or unitrust interest given to charity, except in the case of a later donation of the interest, as discussed in VII.B., and VIII.B., below.[345]

In Rev. Rul. 76-225,[346] the IRS had ruled that an estate tax charitable deduction was not allowed for the value of an annuity interest in a CRAT passing to a §170(c) organization upon the death of each of the designated individual recipients because the payment did not constitute a guaranteed annuity for estate tax purposes. The same result presumably would have been reached for gift tax purposes. Rev. Rul. 76-225 was revoked by T.D. 9068,[347] which modified the estate, gift, and income tax regulations to eliminate the provisions disallowing a charitable deduction for charitable annuity or unitrust interests that are preceded by noncharitable unitrust or annuity interests.

J. Generation-Skipping Transfer Tax

The generation-skipping transfer (GST) tax applies to inter vivos transfers after September 25, 1985.[348] The GST tax is imposed at a flat rate equal to the top federal estate tax rate[349] on direct transfers in which assets pass to individuals more than one generation below that of the transferor (e.g., grandparent to

---

[343] §508(d)(2)(A); Reg. §1.508-3(e)(2).

[344] Reg. §25.2522(c)-3(c)(2)(vi)(*f*), §25.2522(c)-3(c)(2)(vii)(*e*).

[345] Reg. §1.664-2(d), §1.664-3(d).

[346] *Revoked by*, T.D. 9068, 68 Fed. Reg. 40,130 (July 7, 2003).

[347] 68 Fed. Reg. 40,130 (July 7, 2003).

[348] There is a limited exception for a transfer under a will executed before October 22, 1986, if the testator died before January 1, 1987. The Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, §1014(h), extended the transitional rule to revocable trusts.

[349] §2641(a)(1). The exception is generation-skipping transfers made in 2010, which were subject to a 0% tax rate, in a year when the maximum estate tax rate was 35%. *See* Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (2010 TRA), Pub. L. No. 111-312, §302(c), a non-Code provision.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

grandchild)[350] and on certain "taxable terminations"[351] or "taxable distributions."[352] Each individual has a GST exemption that the individual can allocate to transfers in any way he or she sees fit.[353] The GST exemption amount for a calendar year equals the §2010(c) basic exclusion amount for that year.[354] Of course, the GST exemption will not eliminate any estate or gift tax that would have been due on the transfer.

The creation of a charitable remainder trust (CRT) will have GST tax implications only if one of the noncharitable beneficiaries is two or more generations below that of the donor (a "skip person"). For non-family members, this includes any individual born more than 37½ years after the date of birth of the grantor.[355] The charitable remainder beneficiary is considered to be in the grantor's generation.[356]

The transfer to the trust itself is not a generation-skipping transfer because of the charitable remainder beneficiary's interest in the trust.[357] Thus, the only taxable event would be the distribution of the annuity or unitrust amount to the younger-generation beneficiary. There would not be a taxable termination, because the remainder interest is distributable to the designated charity.[358]

The recipient of a taxable distribution is responsible for paying the GST tax.[359] A trustee is responsible for the payment of GST tax only in the case of a direct transfer from a trust on a taxable termination.[360] In any event, the GST tax should never be paid by the trust, because that would violate the requirement that no amount other than the annuity or unitrust amount may be paid to a noncharitable beneficiary.[361]

There are three possible structures to which the GST tax may apply. This is not a full discussion of the GST tax rules; these are only intended to highlight the situations where the GST might apply. If it appears that it might apply, refer to 850 T.M., *Generation-Skipping Transfer Tax (Chapter 13),* for further analysis.

First, the trust could be designed for a skip person to receive an immediate interest. For example, a trust could be established for a term to pay to a grandchild attending college. In this case, the person funding the trust would probably want to allocate enough of his or her GST exemption so that the trust (and therefore the distributions) would be exempt from GST tax. That allocation is made on the gift tax return for the year in which the trust is funded. The trust will not receive an automatic allocation of exemption,[362] so it is important to file the return and make the timely allocation. See 850 T.M., *Generation-Skipping Transfer Tax (Chapter 13).*

Practice Point: For trusts with immediate skip-person beneficiaries, the donor should not retain the right to revoke the noncharitable beneficiaries' interests. If that power is retained, the gift is incomplete, so any GST exemption allocation will be ineffective to fully exempt the trust.[363]

The second situation where GST considerations might apply is if the donor is the initial noncharitable beneficiary and a skip person is a contingent beneficiary after the donor (or after the donor and spouse). Because such a trust will be included in the donor's taxable estate, allocating GST exemption at the time the trust is funded would not be effective.[364] The GST analysis and possible allocation of GST exemption should occur at the death of the donor spouse as part of the estate tax return preparation process.[365]

The third situation where GST considerations might apply is if the skip person is expected to receive a secondary interest after a non-skip person and the donor does not retain an interest in the trust. This situation usually would be a completed gift and not result in inclusion in the donor's estate, so the GST analysis should take place when the trust is initially funded. An example would be a 20-year term CRT in which the donor's child is the initial noncharitable beneficiary and a grandchild is to receive the interest if the child dies within the trust term. In this case, it may or may not be a good use of the donor's GST

[350] §2613(a).

[351] §2612(a)(1).

[352] §2612(b).

[353] §2631(a). If a trust is potentially subject to GST tax, the transferor's GST exemption must be allocated on the gift tax return reporting the gift. Relief may be available if the allocation is missed. In PLR 200303053, donors entered into five separate pooled income fund agreements naming their five grandchildren as income beneficiaries and a university as the remainder beneficiary. For the first four of the five years in which donors made contributions, the donors' accountant failed to allocate any of their GST exemptions on the gift tax returns. The donors requested an extension of time for the allocation. Citing now obsolete Notice 2001-50, the IRS granted the donors a 60-day extension to allocate their exemptions to the transfers. The IRS found that the donors had satisfied the requirements for granting relief by showing that they had reasonably relied on a qualified tax professional to properly make the allocations. *See also* PLR 202233002 (extension of time granted under Reg. §301.9100-3 where three CRATs had GST potential and taxpayer's estate did not intend equal allocation of GST between CRATs, but estate, relying on attorney, did not affirmatively allocate any GST exemption on Form 706), PLR 202133006 (IRS granted extension to allocate GST exemption to transfers to CRUTs where accounting firm reported value of transfer to CRUT on gift tax return, but did not allocate any part of donor or donor's spouse's GST exemption to transfer to CRUT). In 2024, the IRS issued final regulations under §2642(g)(1) that govern requests for extensions of time to allocate GST exemptions, to make an election not to have GST exemption automatically allocated under §2632(b)(1) to a direct skip or under §2632(c)(1) to an indirect skip or to any transfers made to a trust, and to make an election to treat any trust as a GST trust (in lieu of requests under Reg. §301.9100-3). *See* Reg. §26.2642-7, *as added by* T.D. 9996, 89 Fed. Reg. 37,116 (May 6, 2024), applicable to requests for relief to which §2642(g)(1) applies that are filed on or after May 6, 2024.

[354] §2631(c). For generation-skipping transfers made after 2025, the GST exemption amount is $15 million, as adjusted for inflation. *See* §2010(c) (as amended by the One Big Beautiful Bill Act (OBBBA), Pub. L. No. 119-21, §70106, effective for transfers made after December 31, 2025). For generation-skipping transfers made after 2017 and before 2026, the GST exemption amount is $10 million, as adjusted for inflation. *See* former §2010(c) (as amended by Tax Cuts and Jobs Act, Pub. L. No. 115-97, §11061, effective for transfers made after December 31, 2017, and before January 1, 2026). For the inflation-adjusted GST exemption amounts (and a detailed discussion of the GST tax generally), see 850 T.M., *Generation-Skipping Transfer Tax (Chapter 13).*

[355] §2651(d)(2).

[356] §2651(f)(3).

[357] §2652(c)(1)(C).

[358] §2612(a)(1)(A).

[359] §2603(a)(1). The tax is payable with Form 706-GS(D), *Generation-Skipping Transfer Tax Return for Distributions.*

[360] §2603(a)(2).

[361] §664(d)(1)(B), §664(d)(2)(B).

[362] GST exemption is automatically allocated to indirect skips in trust. §2632(c)(1). However, CRTs are excluded from the definition of indirect skips by §2632(c)(3)(B)(v).

[363] Reg. §26.2632-1(c)(5) *Ex.* 2.

[364] Reg. §26.2632-1(c).

[365] *See* 822 T.M., *Estate, Gift, and Generation-Skipping Tax Returns and Audits*, and 850 T.M., *Generation-Skipping Transfer Tax (Chapter 13).*

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

exemption; the beneficiary sequence would need to be analyzed on a case-by-case basis.

K. Charitable Remainder Trust Documents Requirements

To qualify as a charitable remainder trust (CRT), the trust instrument must be irrevocable,[366] and it must create a valid trust under applicable local law.[367] Thus, the trust instrument must incorporate any applicable requirements of local law relating to charitable trusts and comply with §664 and the regulations thereunder. The IRS has ruled that the trust instrument must create a valid trust, not only under applicable local law, but also for income tax purposes under the entity classification regulations.[368] In PLR 200203034, the arrangement was deemed to create a business trust and, therefore, not a qualified charitable remainder trust.[369]

The IRS has published a series of revenue procedures containing annotated sample charitable remainder trust instruments that can be used in drafting the governing instrument. These sample instruments include annuity trusts and unitrusts, inter vivos and testamentary trusts, and trusts for one and two lives and terms of years.[370]

1. Working with the IRS Sample Forms

The IRS sample trust forms should be the starting point for any CRT instrument. Use the list at Worksheet 2 to select the applicable form for the type of trust desired. For example, Rev. Proc. 2005-54 is the inter vivos unitrust with consecutive interests for two lives. The sample document includes alternative paragraphs that incorporate almost all of the variations that a drafter could want, including the "net income" variations (NICRUT, NIMCRUT, and FLIP-CRUT discussed above at IV.C., above), the right to change the remainder charity, qualified contingencies that would accelerate the charitable remainder, continuation of the trust as a wholly charitable trust, and the right to revoke the successor income interest.

Each paragraph in the sample forms includes annotations explaining the consequences of the use (or non-use) of a particular provision. The drafter should consider each alternative and document the donor's intentions regarding each alternative.

There will be times when the sample documents do not include the terms desired by the donor. For example, the donor may want more than two concurrent or consecutive beneficiaries. Although the IRS will not rule on CRTs that entirely follow the sample documents,[371] it will rule on provisions not included in the samples.[372] The donor and advisor will have to decide whether the variation from the sample documents is sufficiently important to warrant the expense and delay of a ruling. If a custom actuarial factor is required, then a ruling may be necessary. The donor, alternatively, may retain an actuary without obtaining a ruling.[373]

For convenience in administering the trust, the trust may be drafted to terminate the income interest with the payment immediately preceding the death of the beneficiary. This avoids having to make a final prorated payment to the estate of the beneficiary. If the trust is a two-life trust, the successor beneficiary receives a full payment for the period that includes the date of death of the initial beneficiary. This adjustment does not affect the valuation of the annuity or unitrust interest.[374]

For a testamentary trust, it is advisable to include a provision adjusting the payout rate or term of the trust in case the trust as originally drafted does not meet the minimum 10% remainder value as of the date of death. If the trust is self-adjusting, a reformation proceeding under §2055(e)(3)(J)(ii) would not be needed.

2. Governing Instrument Requirements

The sample documents include all the required elements for a valid charitable remainder trust (other than specific local requirements for a valid trust, which also must be included). The following are specific requirements for a governing instrument.

a. Calendar Year Requirement

The Tax Reform Act of 1986 (1986 Act)[375] required all trusts, both existing and newly created, to adopt a calendar year for taxable years beginning after December 31, 1986.[376]

---

[366] *See* Reg. §1.664-1(a)(1)(i).

[367] *See, e.g.*, Rev. Proc. 2003-53 (annuity trust), Rev. Proc. 2005-52 (unitrust).

[368] Reg. §301.7701-4(b).

[369] The IRS ruled, specifically, that a proposed charitable remainder unitrust to be created by an S corporation and its shareholder would not be classified as a trust for income tax purposes and, thus, would fail to qualify under §664. The result was similar in PLR 9547004, where the IRS ruled that a proposed CRUT with multiple grantors and beneficiaries was classified as an association, rather than a trust, and did not satisfy the §664(d) definition of a charitable remainder trust. The trust was established by a husband and wife and their six grandchildren, who planned to fund it with appreciated securities. The trust provided that the husband and wife would receive the unitrust payment for their joint lives and for the life of the survivor of them. On the death of the survivor, the grandchildren would have the right to the unitrust payment until the death of the survivor of them, at which time the remainder would pass to a charity. The IRS explained that under the regulations, if an entity has both associates and a business purpose, it is classified as an association rather than a trust.

[370] See Worksheet 2 for a list of the specific trust forms.

[371] This proscription (first stated in superseded Rev. Proc. 89-19 and Rev. Proc. 90-33) is found in the third annual revenue procedure, which lists the "no ruling" areas, published in the first annual Internal Revenue Bulletin. Additional information is provided in the revenue procedures containing the sample CRT forms. The IRS has also stated that it will not issue rulings on CRUTs that use the §664(d)(3) income exception if the grantor, a trustee, a beneficiary, or a person related or subordinate to such person can control the timing of the trust's receipt of income from a partnership or deferred annuity contract. This proscription (first stated in superseded Rev. Proc. 97-23) is found in the third annual revenue procedure published in the first annual Internal Revenue Bulletin. *See* Rev. Proc. 2026-3, §4.01(39). In Rev. Proc. 97-23, the IRS stated that it is studying the issue of whether, because of the potential for manipulation of trust income for the benefit of the unitrust beneficiary, such trusts qualify as CRTs.

[372] *See, e.g.*, PLR 201845014 (sprinkling power between individual beneficiary and charity vested in independent trustee), PLR 201126007 (ability of trustee of CRAT to invest in annuity), PLR 200813023, PLR 200813006 (special trustees who held power to sprinkle unitrust amount), PLR 9712031 (retention of powers to designate charitable beneficiary by will, to instruct trustee to distribute assets to charity during trust term, to negotiate trustee compensation, and to remove trustee or investment manager and appoint successor), PLR 9504012 (reservation of powers to change remainder beneficiary and appoint successor trustee), PLR 9419021 (partnership as noncharitable beneficiary), PLR 9117038 (three life income beneficiaries).

[373] Reg. §1.664-4(b).

[374] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).

[375] Pub. L. No. 99-514, §1403(a).

[376] §644.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

b. Requirement that Trust Must Be Either an Annuity Trust or a Unitrust

A trust qualifies as a charitable remainder trust only if it is either a charitable remainder annuity trust or a charitable remainder unitrust.[377] The different payment requirements for the two types of trusts may not be combined; in fact, such combination will cause disqualification of the trust.

> *Example:* A trust that provides for an annual payment to a noncharitable beneficiary of the greater of a sum certain or fixed percentage of the annually determined value of the trust assets does not qualify as a CRT. The trust is not a CRAT because the payment for a particular year may be of a fixed percentage of the annually determined value of the trust assets, which is not a "sum certain" as required for qualification as a CRAT. The trust is not a CRUT because the payment for a particular year may be of a sum certain, which is not a "fixed percentage" (or lesser of "fixed percentage or trust income") of the annually determined value of the trust assets as required for CRUTs.[378]

An annuity trust will not qualify unless its governing instrument expressly prohibits additional contributions.[379] The governing instrument of a unitrust must either prohibit additional contributions or provide special rules for the valuation of unitrust payments in the case of additional contributions.[380]

c. Trust Must Function Exclusively as Charitable Remainder Trust from Date of Creation

To qualify as a CRT, the trust must satisfy the definition of a CRT and function exclusively as a CRT from the date of its creation.[381] An inter vivos trust is never deemed created before the date on which property is transferred to the trust.[382] For the purposes of §664, the trust is deemed created as soon as no person (including the grantor) is considered the owner of the entire trust corpus pursuant to the grantor trust rules of §671–§678.[383]

> *Example 1.* On January 1, G transfers property in trust and retains the power to revoke the trust during his lifetime. The trust otherwise would constitute a qualified CRT if it were irrevocable. For purposes of §664, the trust is not deemed created on January 1, because on that date G is treated as the owner of the entire trust under §676(a) of the grantor trust rules.[384] Three years after the creation of the trust, G dies, at which time the trust becomes irrevocable. For purposes of §664, the trust is deemed created on the date of G's death, because that is the earliest date on which G (or any other person) is not treated as the owner of the entire trust under the grantor trust rules. The trust qualifies as a CRT because it will thereafter function exclusively as a CRT.[385]

> *Example 2.* The facts are the same as in Example 1, except that G retains the inter vivos power to revoke only one-half of the trust. Pursuant to §676(a), G is treated as the owner of one-half of the trust. For purposes of §664, the trust is deemed created on January 1, because on that date G is not treated as the owner of the entire trust under the grantor trust rules. Consequently, a charitable deduction is not allowable either at the creation of the trust or at G's death because the trust does not satisfy the definition of a CRT from the date of its creation.[386]

Comment: Under Example 2, the regulations could have treated the trust as severable. One trust composed of one-half of the trust assets would have been completely irrevocable from the date of creation and, thus, a qualified charitable remainder trust. The other trust would have been completely revocable by the grantor and, thus, a grantor trust that was a qualified charitable remainder trust only on the death of the grantor. Since the regulations do not adopt this interpretation, separate trusts should be created whenever a grantor desires to retain a power over a portion of the trust assets. This situation could arise if a trust was funded with community property. Spouses with community property may decide to transmute their property to separate property before funding to avoid this issue.

d. Investment Restrictions

A trust does not qualify as a CRT if its governing instrument "restricts the trustee from investing the trust assets in a manner which could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets."[387] A provision that restricts the trustee to a certain type of investment (e.g., tax-exempt bonds) will disqualify the trust. The regulations do not expressly require a specific provision in the governing instrument to the effect that the trustee is not restricted in his or her investments, but the sample instruments published in the revenue procedures[388] all contain such a provision. An area that has received considerable attention is the investment of trust assets in tax-exempt securities. The IRS ruled in Rev. Rul. 60-370 that if a trustee is under any obligation, whether express or implied, to sell or exchange the property transferred to the trust and to reinvest the proceeds in tax-exempt securities, any gain realized on the sale is taxed to the

[377] Reg. §1.664-1(a)(2).

[378] Reg. §1.664-1(a)(2). The net income only unitrust, the net income with make-up unitrust, and flip unitrust options discussed at IV.C., above, involve variations of the unitrust payment requirements and are not exceptions to the rule that a charitable remainder trust must function either as an annuity trust or a unitrust.

[379] See Worksheet 2.

[380] See Worksheet 2. For example, such special rules applicable in the case of additional contributions include provisions to enable the trust to meet the 10% test under §664(d)(4) when an additional contribution is made to the trust at a time when the federal midterm rate is lower such that the present value of the remainder interest is no longer 10% of the initial net fair market value of all property placed in the trust. See VI.H.3., below, for further discussion.

[381] Reg. §1.664-1(a)(4).

[382] Reg. §1.664-1(a)(4). See the discussion at V., below, concerning the date of creation of a testamentary trust.

[383] Reg. §1.664-1(a)(4).

[384] Section 676(a) provides that the grantor is treated as the owner of any portion of the trust with respect to which the grantor reserves the power to regain title to the trust assets.

[385] Reg. §1.664-1(a)(6) *Ex.* (1).

[386] Reg. §1.664-1(a)(6) *Ex.* (2).

[387] Reg. §1.664-1(a)(3).

[388] See Worksheet 2 for a list of the Revenue Procedures for the sample forms.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

grantor. This ruling is referenced in most private letter rulings issued regarding inter vivos transfers.

Practice Point: If tax-exempt bonds are contributed to, and retained by, the trust, distributions from the trust generally are nontaxable to the recipient (although fiduciary considerations may preclude this technique). If appreciated assets are contributed to the trust, sold by the trustee, and then reinvested in tax-exempt securities, the beneficiary will be taxed on capital gain and ordinary income, not tax-exempt income, due to the operation of the "class and category system" discussed at VI.C., below.

In Rev. Rul. 73-610 the IRS disqualified a trust where the grantor's spouse retained a life interest in a portion of the trust assets (an antique collection). As a result of the spouse's intervening life estate, the trustee was unable to invest all of the trust assets to produce income or sell or dispose of all the assets. The IRS ruled that this violated the requirement that the trustee must be free to invest the assets in a manner that will permit the assets to realize a reasonable rate of return.

In Rev. Rul. 73-571, the IRS ruled that a bank serving as trustee of a CRUT could invest the trust assets in the trustee's common trust funds used primarily by revocable inter vivos noncharitable trusts.

A university serving as trustee of a CRT is permitted to invest the trust's assets in its general endowment fund without jeopardizing the trust's exempt status or the donor's charitable deduction.[389] In addition, a charity serving as trustee of several CRTs was permitted to invest the assets of the trusts jointly.[390] However, the Philanthropy Protection Act of 1995[391] requires written disclosure to the donor by a trustee concerning commingling of funds. If a charity is acting as trustee of a CRT in which the remainder interest is irrevocably dedicated to any charitable organization and if the assets of the CRT are not segregated, but instead are commingled with other charitable assets in a collective investment vehicle, the trustee must disclose enough information about the operation of the charitable income fund in which the gift may be pooled to permit the donor to make informed decisions about whether or not to make a gift and whether or not to permit a gift to be pooled in such fund.

The IRS has ruled that a provision in a CRAT giving the trustee discretion to allocate a portion of the trust assets to purchase an annuity contract to fund the annual annuity payments (to the trust's grantor) would not prevent the trust from qualifying under §664(d)(1).[392] Before actually purchasing such a policy, the trustee should also consider fiduciary responsibilities to the remainder charity.

A CRT may not hold S corporation stock, because the ownership of such stock would terminate the corporation's election under subchapter S.[393] In Rev. Rul. 92-48, the IRS ruled that a CRT cannot be the subject of a qualified subchapter S trust election under §1361(d)(2). Likewise, a CRT may not hold S corporation stock by qualifying as an electing small business trust.[394]

The grantor's income tax deduction may be affected where the grantor or a "related party" retains the annuity or unitrust interest in a trust funded with tangible personal property; however, this issue arises only in the case of an inter vivos trust.[395]

e. Prohibition on Invasion and Reversion

(1) Invasion Powers

The sample documents all include a standard provision negating any state law trustee powers that would conflict with the trust's qualifying as a CRT.[396] This provision is needed because CRTs are governed by applicable state laws as well as §664. In Rev. Rul. 77-58, the IRS ruled that a trust did not qualify because of its failure to negate certain provisions of applicable state trust laws. The trust law of the state in question provided that, unless otherwise provided in the trust instrument, a trustee had the power in certain circumstances to invade the trust for the benefit of the grantor and the income beneficiary. The IRS ruled that, in the absence of a contrary provision in the governing instrument, the trustee possessed the powers granted by state law. As a result, the trust did not qualify under §664 because it violated the requirement that no person may have a power to invade the trust for the use of a non-§170(c) organization.

A trust will not be a qualified CRT if it is subject to a power to invade, alter, amend, or revoke for the benefit of a person other than an organization qualifying under §170(c). The exception to this rule is that the grantor may retain a testamentary power to revoke or terminate the life interest of a noncharitable beneficiary and retain the power to substitute one charitable beneficiary for another.[397] Of course, the testamentary power to revoke or terminate a noncharitable interest can only benefit the charitable remainder interest, by accelerating the vesting of the charitable interest.

[389] Rev. Rul. 83-19, *amplifying* Rev. Rul. 73-571. The IRS has issued a number of favorable private letter rulings on contractual arrangements under which a CRUT that could not directly invest in a college or university endowment fund, because a direct investment would generate unrelated business taxable income (UBTI) that would cause a charitable remainder trust to lose its tax-exempt status for that tax year, instead received units under which the college or university was contractually obligated to make payments based on the performance of the endowment fund. In these rulings, the IRS ruled that UBTI was not generated by (i) the issuance of units, (ii) the receipt of payments on the units, or (iii) the redemption of units. *See* PLR 201613015, PLR 201613014, PLR 201408034, PLR 201311036, PLR 201311032, PLR 201218015, PLR 200817038, PLR 200711037, PLR 200711034, PLR 200711025, PLR 200710013–PLR 200710016, PLR 200704036, PLR 200703037–PLR 200703038, PLR 200352017–PLR 200352018 (*modified by* PLR 200702040–PLR 200702041). In PLR 200826026 and PLR 200735019, the IRS ruled that a CRUT's units in a university's endowment fund were §1221 capital assets and that a redemption of the units would generate short- or long-term capital gain under §1234A, depending on the holding period.

[390] PLR 8903019.

[391] Pub. L. No. 104-62, §21.

[392] PLR 201126007. The PLR indicated that the CRAT would possess all incidents of ownership in the annuity contract, be entitled to all payments from the annuity, and receive such payments each year for the trust's duration in an amount equal to or greater than the trust's annual annuity payout.

[393] §1361(b)(1)(B), §1361(c)(2), §1361(e)(1)(B)(iii).

[394] §1361(e)(1)(B)(iii). When the provision for electing small business trusts was added by the Small Business Job Protection Act of 1996, Pub. L. No. 104-188, it was unclear whether CRTs would qualify. TRA '97, Pub. L. No. 105-34, §1601, added §1361(e)(1)(B)(iii) as a technical correction to make it clear that CRTs do not qualify under §1361(e).

[395] See the discussion at IV.A.3., above.

[396] *See, e.g.,* Rev. Proc. 2005-52 (unitrust), Rev. Proc. 2003-53 (annuity trust).

[397] Reg. §1.664-2(a)(4), §1.664-3(a)(4).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

(2) Reversion Issues

Overly cautious drafters have sometimes included provisions requiring the return of trust assets if the grantor does not receive the desired tax results. The IRS has not viewed such provisions in a favorable light and has ruled that such provisions disqualify a trust from being treated as a CRT, because they authorize the payment of an amount other than the annuity or unitrust amount and are not a completed charitable gift. The IRS ruled in Rev. Rul. 76-309 that a fully funded and otherwise qualifying annuity trust failed to qualify because the governing instrument provided that the trust would be deemed null and void and all the assets returned to the grantor if the IRS disallowed the grantor's income tax deduction for the value of the charitable remainder interest. The IRS ruled that this condition made it possible for an amount other than the annuity payment to be paid to a noncharitable beneficiary and disallowed the income tax charitable deduction because the remainder interest had not been transferred to or for the use of a charitable organization or retained by the trust for such charitable use.

In Rev. Rul. 76-309, the IRS distinguished Rev. Rul. 60-276.[398] There, a newly established pension trust had not been disqualified where the employer's contributions were to be returned to the employer if the IRS refused to rule that the trust was initially qualified. The distinguishing factor was that, in Rev. Rul. 60-276, the trust assets could not be returned to the employer after the IRS ruled the trust qualified, whereas the return of assets in Rev. Rul. 76-309 would occur upon disallowance of the grantor's tax deduction even if the trust was otherwise qualified. Although Rev. Rul. 60-276 is now obsolete, it suggested, when read together with Rev. Rul. 76-309, that the IRS might permit a conditional return provision in a CRT where the return of the assets is contingent on the receipt of a favorable private letter ruling and not the approval of the grantor's income tax deduction.

Although a provision to return the assets to the grantor upon receipt of an unfavorable ruling may not itself disqualify the trust, the charitable deduction will not be allowed if the IRS finds the trust is not otherwise qualified. If the grantor has already funded the trust, the disallowance of the deduction may have harsh results, particularly for gift tax purposes.

To a large extent, the need to include a return provision in the governing instrument can be eliminated by authorizing the trustee to amend the trust for the purpose of ensuring that the trust qualifies as a CRT. The sample governing instruments published by the IRS grant the trustee a limited power to amend the trust in any manner required for the sole purpose of ensuring that the trust qualifies and continues to qualify as a CRT under §664.[399]

Comment: Even with the limited power of amendment, Rev. Rul. 76-309 illustrates the importance of careful drafting and thorough planning before a donor funds a CRT. A donor may wish to consider the advisability of obtaining a private letter ruling before funding the trust if the trust provisions vary significantly from the sample provisions.

Another situation in which contributed assets may return to a grantor is when, in accordance with state law, the trust instrument contains a provision that, while not explicitly requiring the return of assets, nevertheless results in such a return. In PLR 200052026, the IRS ruled that the grantors, as trustees, could return to themselves the proceeds from a second contribution that they made to a CRUT without disqualifying the trust. Under state law, a trustee was allowed to accept a second contribution to a trust unless the trust instrument contained a prohibition to the contrary. Here, the trust instrument contained such a provision. As a result, the IRS determined that the trustees/grantors acted without legal authority in accepting the second contribution, viewed their acceptance as a legal nullity, and treated the second contribution as though it had never been made. The IRS ignored the second contribution for federal tax purposes, except that the grantors had to recognize any capital gains or dividend income contained in the proceeds returned to them as grantors.

Contributed assets may also be returned to the grantor if a local court validly rescinds a CRT because of substantial mistakes surrounding the execution of the trust. In PLR 200219012, the grantors created a §664(d)(2) standard CRUT from which they were to receive each year a fixed percentage of the net fair market value of the trust assets, valued annually, from income or, if income was insufficient, from principal. The grantors were incorrectly advised that no distributions had to be made to them until the trust sold the closely held stock they contributed to it and that neither the funding of the trust nor the distribution of the stock to them in satisfaction of the unitrust payment would cause them to recognize capital gains. The trust was unable to sell the stock and received no dividends or other income, so no distributions were made to the grantors. After concluding that the court order rescinding the trust was consistent with state law, the IRS ruled that the rescission of the trust was recognized for federal tax purposes as of the date of the trust's creation. Because the statute of limitations had expired for the year of the trust's creation, the tax benefit rule applied to cause the grantors to recognize income in the year the trust assets were returned to them equal to the income tax charitable deduction they took for the trust in the year of creation. The statute of limitations had not expired for the year following the year of the trust's creation, so the grantors were able to file an amended return eliminating the portion of the income tax charitable deduction they had carried over to that year. The IRS observed that all parties were in the same position they would have been in if the trust had never been created because the grantors' income tax charitable deductions for the trust were negated and the trust had no income.

In another instance, the IRS ruled that funds transferred to a CRUT in error could be restored to the grantor pursuant to a court order without disqualifying the unitrust under §664 or resulting in self-dealing under §4941.[400] The grantor in the ruling had not taken a charitable deduction for the transfer of the funds, but the trustee had included the value of the funds in calculating the unitrust distributions to the income benefi-

[398] *Obsoleted by* Rev. Rul. 91-4 (reversions of employer contributions to qualified pension, profit-sharing, or stock bonus plan permissible under conditions described in §403(c)(2) of Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, as amended).

[399] *See, e.g.,* Rev. Proc. 2005-52 (unitrust), Rev. Proc. 2003-53 (annuity trust).

[400] PLR 200601003. Self-dealing is discussed in VI.G., below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ciaries (the grantor and her husband). The court order specified that the trustee was to restore the funds to the grantor because the grantor did not make a valid donation of the funds. The trustee was to restore the amount of the funds reduced by any unitrust distributions attributable to the funds and increased by any earnings attributable to the funds. The income beneficiaries and the unitrust were to amend their tax returns for the affected years and the income beneficiaries were to report any income generated by the investment of the funds (as adjusted for any income already reported as part of the unitrust distributions). The IRS stated that the restored funds would be deemed never to have been part of the unitrust's principal for federal tax purposes.

However, not every court order terminating a charitable remainder trust has had so favorable an outcome. In PLR 201714002 and PLR 201714003, the IRS addressed the consequences of a conditional court order stating that the trusts would be deemed void *ab initio* if the IRS ruled that the termination did not have adverse tax consequences to the noncharitable beneficiaries. Due to bad legal and tax advice, the trusts had not been operated in accordance with their documents. The IRS ruled unfavorably, holding that the trusts were subject to the Chapter 42 private foundation rules because the original donor had taken charitable income tax deductions. Therefore, any attempt to distribute assets to the beneficiaries to terminate the trusts would expose the trusts to various penalties under Chapter 42.[401]

If a situation arises where it appears appropriate to declare a trust (or a specific contribution) void, a private letter ruling is highly recommended. The author generally follows this sequence: (1) making an informal "no-name" call to IRS Chief Counsel's office to see if they would consider a ruling, given the facts, (2) obtaining a conditional court order that would be self-executing if a favorable ruling is received, and (3) submitting a ruling package to IRS. State charitable regulatory authorities, and potentially any named charitable remainder beneficiaries, will probably need to be noticed.

(3) Reformation of Inter Vivos Charitable Remainder Trusts

A provision in the sample documents gives the trustee the power to amend the document to conform it to the requirements for a CRT. If a minor omission is discovered, the trustee can exercise that power without the need to obtain a ruling. If, however, a significant error is discovered (e.g., a CRAT has been created instead of a CRUT), a court-ordered reformation will be required, along with a private letter ruling. Typically, informal conversations with the relevant state regulators and the IRS Chief Counsel's office are the first steps in the process. Assuming both of those are at least potentially favorable, the process of obtaining the conditional court order and then the ruling can proceed. If a charity was given a vested remainder interest, it may also need to agree to the reformation. The court order is typically self-executing once a favorable private letter ruling is received.

The IRC provisions for reformation requirements for inter vivos CRTs are cross referenced to the estate tax charitable deduction provisions in §2055(e)(3). Those requirements, including the deadlines for instituting reformation proceedings, are discussed in detail in V.E., below.

Many inter vivos reformation private letter rulings involve correction of scrivener's errors. A number of them are discussed below, as they may be helpful in drafting a ruling request if similar corrections are needed. Any ruling request should address both the continued qualification of the trust under §664, and the potential issue of self-dealing (discussed at VI.G., below).

Judicial reformation may be available as a remedy if the CRT contains a scrivener's error. In PLR 200251010, the grantor intended to create a CRUT. However, because of an error in the attorney's computer software, the grantor created a charitable remainder annuity trust instead. As soon as the error was discovered, the trust was reformed by a state court to make it a CRUT, *ab initio.* The IRS ruled that under these circumstances, the judicial reformation of the trust would not adversely affect the trust's qualification as a CRUT. Similarly, in PLR 200338006 the IRS ruled that the judicial reformation, *ab initio*, of a trust incorrectly drafted as a NIMCRUT to make it a standard CRUT, as intended, would not affect the trust's qualification under §664.[402] In PLR 200441019, the IRS approved the retroactive reduction, by court order, of a CRT's unitrust amount from 7% to 5% to correct a scrivener's error. In PLR 200850046, the IRS issued a favorable ruling on a retroactive judicial reformation that potentially extended the noncharitable interest in a CRUT to correct a scrivener's error. In PLR 200932020, the IRS approved the judicial reformation, *ab initio*, of a CRUT to remove the requirement that the remainder beneficiary be an organization described in §170(b)(1)(A), thus allowing the donors' private foundation to be the remainder beneficiary as the donors intended.

In PLR 200932003, the IRS ruled that the judicial reformation, *ab initio*, of a NIMCRUT to include a provision converting it into a standard CRUT upon the sale of the contributed assets, as the donor intended, did not constitute self-dealing. Although noting that the reformation could increase the annual amount payable to the donor, the IRS observed that the donor's advisors had made a scrivener's error and that, under §4947(a)(2),[403] the self-dealing rules do not apply to amounts payable to the income beneficiaries under the terms of a CRT as long as no charitable deductions were allowed for such income interests. In PLR 201042012, the IRS cited this §4947(a)(2) provision in concluding that a judicial reformation retroactively converting a single-life CRUT into a two-life CRUT to correct a scrivener's error was not an act of self-dealing.

In PLR 201332011 and PLR 201332012, the IRS ruled that the judicial reformation of NIMCRUT (entered into prior to the 1998 addition of Reg. §1.664-3(a)(1)(i)(b)(3), as discussed at IV.C., above, which removed a make-up liability provision, did not constitute an act of self-dealing under §4941. Although the elimination of the make-up liability provision increased the net fair market value of assets and, in turn, increased the amount that could be paid or transferred to the unitrust beneficiary/grantor (a disqualified person), the self-deal-

[401] The Chapter 42 private foundation rules are discussed at VI.G., below.

[402] *See also* PLR 200818002.

[403] See VI.G., below, for the private foundation rules.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ing rules of §4941 did not apply because the grantor neither took nor was allowed a deduction under §170(f)(2)(B), §2055(e)(2)(B), or §2522(c)(2)(B) for the grantor's unitrust interests). Further, the IRS ruled that the grantor, as a substantial contributor, was not subject to the self-dealing rules of §4941, because the reformation was necessary to achieve the grantor's intent and enable the trust to continue to qualify under §664.

In PLR 9107010, the CRAT instrument failed to include, due to a drafting error, a provision stating that no part of federal or state estate or inheritance tax arising from the donor's death may be paid from the CRAT and that the donor should provide by will or otherwise for the payment of such taxes from other sources. The trustee of CRAT proposed to amend the trust to include the omitted provision, retroactive to the date of CRAT's creation. Because the CRAT would pay an annuity to the donor until his death followed by an annuity to donor's spouse until her death and it would be possible for the secondary life interest to give rise to estate taxes in the donor's estate if the donor's spouse survived the donor, the CRAT was disqualified as a charitable remainder annuity trust under §664(d)(1) on the grounds that an invasion of trust assets to pay death taxes would violate §664(d)(1)(B). Finding that the fact pattern was practically identical to that in Rev. Rul. 82-128, the IRS ruled that the proposed amendment would be a qualified reformation, which would allow the CRAT to qualify as a charitable remainder annuity trust under §664(d)(1).[404]

Under some circumstances, it may be possible to reform a CRT that already satisfies the requirements of §664. For example, in PLR 9517020, the IRS approved the reformation of a CRUT. The trust had two successive noncharitable beneficiaries, and the trust language was unclear as to the timing of those interests, as well as to the ability of the beneficiaries to designate the charitable remainder beneficiaries. The IRS ruled that a court-approved reformation to correct these ambiguities in the trust instrument did not affect the qualification of the trust.

In PLR 200617026, the IRS approved a modification of a CRAT to allow the trustee to distribute a limited amount of principal to itself, as the charitable remainder beneficiary, each year. The annuity recipient had consented to the distributions, which would not jeopardize his annuity. In accordance with Reg. §1.664-2(a)(4), the adjusted basis of the distributed assets had to be fairly representative of the adjusted basis of the assets available for distribution on the distribution date. In PLR 200950032, the IRS approved a second modification of the same CRAT providing that the charitable remainder beneficiary, as trustee, could distribute trust principal to itself if the value of the trust assets exceeded a specified amount on the valuation date.

If, however, a reformation materially changes the beneficial interests in the trust, it will cause the trust to lose its qualification under §664. In PLR 9516040, the grantor of a CRUT sought to reform the trust to delete an "income only" provision, increasing the value of the noncharitable interest. The IRS ruled that the reformation would disqualify the trust, causing it to lose its tax-exempt status. The IRS also noted that the disqualification could have an effect on the charitable deduction taken by the grantor at the funding of the trust. Similarly, in PLR 9506015, the IRS ruled that a proposed reformation of a CRUT to eliminate a "net income with make-up" provision would cause the trust to be disqualified. (Under current law, this trust could have been drafted as a FLIP-CRUT, but that option was not available when this trust was created.)[405]

In PLR 200827011 through PLR 200827013, the IRS ruled that the reformation of NIMCRUTs to conform them to regulations promulgated after the unitrusts' establishment did not disqualify the unitrusts under §664.[406]

(4) Effect of Spousal Elective Share Rights

Rev. Proc. 2005-24 allows a grantor's spouse to waive his or her state law elective share right if such right could be satisfied from the assets of a CRT and, thus, disqualify the trust under §664(d).[407] Rev. Proc. 2005-24 also provided a safe harbor (i.e., no waiver necessary) for trusts created before June 28, 2005. In Notice 2006-15, the IRS extended this safe harbor indefinitely, so that the existence of any such right of election, even without a waiver, will be disregarded provided that the surviving spouse does not exercise his or her right of election.

---

[404] *See also Midgett v. Hardcastle*, No. 2:17-cv-663, 2021 BL 356568 (E.D. Va. Aug. 10, 2021) (where CRAT failed to include requisite federal tax payment clause, trustee of decedent's revocable trust paid estate tax on decedent's estate and sought reimbursement from CRAT, trustee of CRAT retroactively amended CRAT to include federal tax payment clause, and beneficiary of both CRAT and revocable trust refused to agree to CRAT amendment, court held that CRAT amendment was necessary to be qualified charitable remainder annuity trust and, therefore, was valid exercise of CRAT trustee's authority). Note that the CRAT trustee in *Midgett* provided the CRAT income beneficiaries with 10-days notice to either agree to the CRAT amendment or forfeit any interest in the CRAT and reimburse the CRAT for all annuity payments received by CRAT, which the court held was an unreasonable period of time. Although the trustee of CRAT did not breach a fiduciary duty in providing such a brief notice period, the court's holding reinforces the notion that practitioners should research and understand the scope and length of notice expected pursuant to relevant state law.

[405] *See also* PLR 200649027 (reformation of NIMCRUT to make it standard unitrust would disqualify trust because reformation would not correct scrivener's error; taxpayers had proposed to reform trust because (1) attorney had not advised them of availability and advantages of standard unitrust, and (2) changes in investment climate were frustrating taxpayers' desire to receive suitable income stream from unitrust).

[406] *See also* PLR 201332011–PLR 201332012, PLR 200829015–PLR 200829016.

[407] As discussed in V.C.4., below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

L. Initial Tax Reporting at the Creation of the Trust

1. Income Tax Return for the Donor

a. Income Tax Reporting and Return Attachments

Unless the charitable remainder trust (CRT) is funded solely with cash, the donor will be required to file Form 8283, *Noncash Charitable Contributions*, with the income tax return for the year of the donation to the trust. In order to claim a charitable deduction for a gift of a remainder interest in trust, the taxpayer must attach a statement to the appropriate return that sets forth the computation of the present value of the remainder interest.[408] The statement must also include the information normally required to support a deduction under §170, §2055, or §2522, whichever is applicable.[409] See Worksheet 3 for a sample contribution attachment. Unless the trust is funded solely with cash and marketable securities, the deduction must also be supported by a qualified appraisal.[410] If the deduction (not the contribution to the trust) exceeds $500,000, the appraisal must be attached to the return.[411] Form 8453, *U.S. Individual Income Tax Transmittal for an IRS e-file Return*, must be filed to transmit the required attachments and appraisal if the return is electronically filed.

Reg. §1.170A-13(f)(13) states that the contemporaneous written acknowledgement requirements of §170(f)(8) for contributions of $250 or more does not apply to a transfer to a charitable remainder trust.[412] This exception reflects the fact that often the charitable beneficiary of a split-interest trust has not been identified at the time the trust is funded, and the trust document itself reflects the amount contributed and the value the donor received in return.

The amount of the income tax deduction calculation is discussed at IV.H., above.

b. Income Tax Reporting if Property Subject to Debt Is Donated

In general, the grantor does not realize gain or loss when he or she transfers property, including appreciated property, to an inter vivos CRT. However, the grantor may be required to recognize gain if the property transferred is subject to an indebtedness that exceeds the grantor's basis in the property,[413] or if the grantor receives property from the trust in exchange for the transfer to the trust.[414] The bargain sale rules of §1011(b) will apply if the transferred property is subject to an indebtedness, regardless of whether the trust assumes the indebtedness.[415] This provision may apply when a donor transfers a partnership to the trust if the partnership has allocated debt to the donor.[416]

Practice Point: A donation of property subject to debt should be approached with extreme caution. The donation should proceed only if the following issues have been considered:

- Potential gain on donation under the bargain sale rules.
- Potential self-dealing issues under the private foundation rules, discussed at VI.G., below.
- Potential unrelated business taxable income from debt-financed property, discussed at VI.C.3., below.
- Potential disqualification of the trust. A donor will be deemed to be the grantor where the income is applied in discharge of the grantor's legal obligation. This may result in disqualification of the trust where a grantor transfers mortgaged property to the trust and remains liable on the mortgage but the trust makes the payments.[417]

If the issues have been addressed, and the donation triggers a bargain sale, the gain should be reported with the donor's other capital gains.[418] If the return is filed electronically, there is no specific provision for attaching a calculation; the calculation should be retained with other supporting documentation. If filing of Form 8453, *U.S. Individual Income Tax Transmittal for an IRS e-file Return*, is otherwise required, the calculation could be included with the other attachments if desired.

2. Gift Tax Reporting for the Donor

In many cases, gift tax reporting on Form 709, *United States Gift (and Generation-Skipping Transfer) Tax Return*, for the donor will not apply. See the following chart (noting that "spouse" means U.S. citizen spouse):

---

[408] Reg. §1.664-2(d), §1.664-4(c).

[409] Reg. §1.170A-16, §20.2055-1(c), §25.2522(a)-1(c). For donations made prior to July 31, 2018, see Reg. §1.170A-13.

[410] Reg. §1.170A-17(a), added by T.D. 9836, 83 Fed. Reg. 36,417 (July 30, 2018), applicable to charitable contributions made on or after January 1, 2019. However, the rules may be applied to appraisals prepared for returns or submissions filed after August 17, 2006. See also Reg. §1.170A-13(c)(3) for returns or submissions applicable to donations made before January 1, 2019.

[411] §170(f)(11)(D); Reg. §1.170A-16(e)(1)(iv). For more information on §170(f)(11), see 863 T.M., *Charitable Contributions: Income Tax Aspects*. *See also WT Art Partnership LP v. Commissioner*, T.C. Memo 2025-30 (discussing Reg. §1.170A-13(c)(3) requirement that "qualified appraisal" be done by "qualified appraiser," and applying the §170(f)(11)(A)(ii)(II) reasonable cause exception to qualified appraisal requirement).

[412] See also Reg. §1.170A-16(b), cross-referencing §170(f)(8) and Reg. §1.170A-13(f), which applies to donations made after July 30, 2018, but can be relied on for contributions made after June 3, 2004.

[413] *See, e.g.*, Reg. §1.1001-2.

[414] See the basic rules under §1001 and Reg. §1.1001-2 for more guidance on the income tax consequences of discharged liabilities.

[415] Reg. §1.1011-2(a)(3).

[416] Rev. Rul. 75-194; *Goodman v. United States*, 2000-1 USTC ¶50,162 (S.D. Fla. 1999).

[417] §677; Reg. §1.677(a)-1(d). *See* PLR 9015038.

[418] See 863 T.M., *Charitable Contributions: Income Tax Aspects*, for the details of the calculations.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Terms of CRT:	Gift Tax Return Required?	Possible Taxable Gift?
Donor is the only noncharitable beneficiary, whether or not he or she retains the right to change the remainder charity.	No.	No.
Donor is the initial noncharitable beneficiary, and retains the testamentary right to revoke the interests of any other noncharitable beneficiaries (spouse or non-spouse). Donor also retains the right to change the charitable remainder beneficiary.	No.	No.
Donor is the initial noncharitable beneficiary, and retains the testamentary right to revoke the interests of any other noncharitable beneficiaries (spouse or non-spouse). Donor did not retain the right to change the charitable remainder beneficiary.	Yes.	No.
Donor is the initial noncharitable beneficiary, donor's spouse is the only contingent successor beneficiary, but the donor did not retain the testamentary right to revoke the spouse's interest. Donor may or may not have retained the right to change the charitable remainder beneficiary.	Yes.	No.
Donor (and/or donor's spouse) is the initial noncharitable beneficiary, there are other successor beneficiaries, and the donor did not retain the right to revoke the interests of the successor beneficiaries.	Yes.	Yes. See caution below.
Donor does not retain an interest in the trust, but the donor's spouse is the only noncharitable beneficiary. The donor may or may not have retained the right to change the remainder charity.	Yes.	No.
Donor does not retain an interest in the trust, and the donor's spouse is not the only noncharitable beneficiary. Donor may or may not have retained the right to change the remainder charity.	Yes.	Yes. See caution below.

Caution (applicable only to the two situations noted): If the donor's or the donor's spouse's retained right is neither an annuity interest nor a "straight" unitrust interest (e.g., it is a NIMCRUT or other "net income" trust), the taxable gift may be unexpectedly large. See the discussion of the Chapter 14 issues at IV.I.3., above.

3. *Initial Income Tax Return for the Charitable Remainder Trust*

The annual tax reporting for a CRT is discussed at VI.E.1., below. For the trust's first taxable year, a copy of the governing instrument, certified by the fiduciary under penalties of perjury to be true and complete, must be attached to Form 5227, *Split-Interest Trust Information Return*.[419]

4. *Section 2801 Transfer Tax*

For individuals expatriating after June 16, 2008, Congress created a new transfer tax in §2801.[420] If, during any calendar year, any U.S. citizen or resident receives any covered gift or bequest, there is a tax equal to the product of the highest rate of tax specified in the table contained in §2001(c) as in effect on the date of such receipt, and the value of such covered gift or bequest.

On January 24, 2025, the IRS issued final regulations generally adopting the September 9, 2015, proposed regulations.[421] However, the final regulations did not adopt the proposed rules on CRTs, contained at Prop. Reg. §28.2801-4(a)(2)(iii). In general, the proposed regulations would make CRTs liable for the payment of the §2801 tax attributable to the value of the noncharitable U.S. person's interest in the trust.[422]

[419] Reg. §1.6012-3(a)(6); instructions to Form 5227.

[420] Added by the Heroes Earnings Assistance and Relief Tax Act of 2008 (HEART Act), Pub. L. No. 110-245, §301(b), §301(g)(2).

[421] *See* Reg. §28.2801-1 through §28.2801-7, T.D. 10027, 90 Fed. Reg. 3376 (Jan. 14, 2025); REG-112997-10, 80 Fed. Reg. 54,447 (Sept. 10, 2015).

[422] *See* Prop. Reg. §28.2801-4(a)(2)(iii).

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

V. Testamentary Charitable Remainder Trusts

A. Document Provisions

Section 2055(a) provides for a deduction from the value of the gross estate of bequests for public, charitable, and religious purposes.[423] Unlike the income tax charitable deduction, there are no percentage limitations with respect to the amount of the estate tax charitable deduction. An estate tax deduction is permitted only for transfers to organizations that fall within the categories set forth in §2055(a). It is important to note, however, that the charitable organizations and purposes set forth under §2055(a) are not identical to those described in §170(c) and §2522(a). This is discussed in more detail at IV.F.1., above. To qualify for the estate tax charitable deduction, the document must include all of the requirements discussed at IV.K.2.,[424] above, including a minimum 10% charitable remainder interest. If the initial calculations indicate that the charitable remainder is less than 10%, see V.E., below, to see if the trust can be reformed to save the charitable deduction.

Practice Point: For clients with substantial retirement benefits, consideration should be given to the benefits of designating a testamentary CRT as the beneficiary thereof in order to still preserve the plan assets for the benefit of family and then charity, while also avoiding the income in respect of a decedent doctrine.

Practice Point: A testamentary trust can be drafted to be self-adjusting, either by lowering the payout rate or by shortening the term, so that a qualified reformation is not needed.

For purposes of the estate tax charitable deduction under §2055, a testamentary charitable remainder trust (CRT) is deemed created at the decedent's death even though the actual funding of the trust may be deferred. The regulations provide that the funding of a CRT can be delayed until the end of a reasonable period of administration.[425] Rev. Rul. 80-123 requires that the governing instrument of a testamentary CRT grant the trustee the authority to defer the payment of the annuity or unitrust amount until the end of the taxable year of the trust in which the trust is completely funded. The obligation to pay the annuity or unitrust amount, however, begins at the decedent's death.[426] The sample documents for testamentary CRTs include appropriate provisions to meet this requirement.[427]

> *Example:* G transfers property to a trust over which she retains an inter vivos power of revocation. Upon G's death, the trust is required to pay the debts and administration expenses of G's estate. When the expenses are paid, the trust terminates and distributes all of its remaining assets to a separate trust T, which satisfies the definition of a CRT. T will qualify as a charitable trust from the date of G's death because it will function exclusively as a CRT from its creation. For purposes of §2055, T will be deemed to be created at G's death, provided the governing instrument requires that the obligation to pay the annuity or unitrust amount begins on the date of G's death, even though the same instrument provides that payment will be deferred until the end of the taxable year in which T is funded.[428]

For purposes of these rules, all property passing by reason of the death of the grantor is considered one contribution even though complete funding of the trust may require several transfers during the administration of the grantor's estate.[429] This rule facilitates the creation of testamentary annuity trusts.

If payment is deferred, a correcting adjustment must be made within a reasonable period after the close of the trust's taxable year in which it is completely funded.[430] In the event of an underpayment, the trust must pay the excess to the annuity or unitrust recipient; in the case of an overpayment, the recipient must repay the difference to the trust.[431] All payments must include interest. The applicable rate of interest depends on when the instrument was executed and whether it has been subsequently amended.[432] The rate is the §7520 rate for transfers made after April 30, 1989.[433]

A testamentary CRT must set forth provisions for the retroactive determination of the annuity or unitrust payments to which the beneficiary was entitled during the period from the testator's death until the complete funding of the trust.[434] The provisions must require that within a reasonable period after the trust is funded, the trustee must pay (in the case of an underpayment) or must receive from the recipient (in the case of an overpayment) the difference between: (i) any amounts actually paid, plus interest computed at the §7520 rate, compounded annually; and (ii) the annuity or unitrust amounts payable, plus interest computed at the §7520 rate, compounded annually.[435] The deferred amounts payable to the recipient are determined

---

[423] For further discussion of §2055(a), see 839 T.M., *Estate and Gift Tax Charitable Deductions*.

[424] See Worksheet 2 for the sample documents.

[425] Reg. §1.664-1(a)(5)(i).

[426] Reg. §1.664-1(a)(5)(i).

[427] See Worksheet 2 for the list of Revenue Procedures with the sample documents.

[428] Reg. §1.664-1(a)(6) *Ex.* (4).

[429] Reg. §1.664-2(b), §1.664-3(b).

[430] Reg. §1.664-1(a)(5)(i).

[431] Reg. §1.664-1(a)(5)(i).

[432] The rates were 10% for instruments executed or amended on or after August 9, 1984, and before May 1, 1989, and not subsequently amended; 6% or 10% for instruments executed or amended after October 24, 1983, and before August 9, 1984; and 6% for instruments executed before October 25, 1983, and not subsequently amended.

[433] Reg. §1.664-1(a)(5)(iv). The §7520 rate corresponds to the rates used in Reg. §20.2031-7(d)(6) (for transfers made after April 30, 1989), §20.2031-7(d)(7), *as amended by* T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023), applicable on or after June 1, 2023 (to reflect updated mortality data for transfers made on or after June 1, 2023), §20.2031-7A(g) (for transfers made after April 30, 2009 and before June 1, 2023), §20.2031-7A(f)(4) (for transfers made after April 30, 1999 and before May 1, 2009), and §20.2031-7A(e) (for transfers made after April 30, 1989 and before May 1, 1999). The rates for pre-May 1, 1989, instruments are found in Reg. §20.2031-7A(a)–§20.2031-7A(d). Note that Reg. §20.2031-7(d)(3) provides transitional relief allowing for use of 2000CM or 2010CM for valuations after April 30, 2019 and before June 1, 2023. The actuarial tables are available online at https://www.irs.gov/retirement-plans/actuarial-tables.

[434] Rev. Rul. 88-81, *modified by* Rev. Rul. 92-57 (applying to CRUTs). These required provisions, but not the calculation details, are incorporated into the 2003 and 2005 sample documents. See Worksheet 2, below, for a list of the sample documents.

[435] Reg. §1.664-1(a)(5)(i), §1.664-1(a)(5)(iv)(a). The use of Table D was unaffected by the enactment of §7520. Notice 89-60. Table D is available at https://www.irs.gov/retirement-plans/actuarial-tables. *See also* Reg. §1.664-4(e)(6), *as amended by* T.D. 9974, applicable on or after June 1, 2023.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

retroactively by using the valuation method and valuation dates that are ultimately adopted by the CRT.

In the case of a unitrust, the amount payable for the deferral period is determined by multiplying:[436]

• the sum of (a) the value of the property passing to the trust as valued on the earlier of the date of death of the last income recipient or the last day of the taxable year in which occurs the complete funding of the trust, (b) any distributions in respect of unitrust amounts paid by the trust or estate before such date, and (c) interest on such distributions computed at the §7520 rate for the transfer, compounded annually from the date of distribution to such date, by

• a factor equal to 1.000000 less the factor under the appropriate adjusted payout rate in Table D opposite the number of years in column 1 between the date of the decedent's death and the date of the earlier of (a) the death of the last recipient, or (b) the last day of such taxable year.

The appropriate adjusted payout rate is determined using Table F (available at https://www.irs.gov/retirement-plans/actuarial-tables) under the §7520 rate for the valuation date.[437]

In Rev. Rul. 80-123,[438] the IRS ruled that a testamentary trust must contain a formula for retroactively determining the payments to the beneficiary before the complete funding of the trust. Sample calculation language was provided in Rev. Rul. 82-165.[439] The 2003 and 2005 sample documents do not include the detailed calculation language.[440] Instead, they offer two alternative clauses. The first incorporates the language of Reg. §1.664-1(a)(5)(i), the second incorporates the alternative calculation of Reg. §1.664-1(a)(5)(ii). Rev. Rul. 92-57 contains sample language that should be used if the alternative calculation is desired.

Practice Point: Use of the 2003 or 2005 sample document default language, which incorporates the calculation rules by reference to the regulations under §664, may be preferable. Given the number of years that may pass between the date the document is executed and the death of the testator, omitting unnecessary calculation details may avoid the need for a postmortem reformation if the calculation requirements are changed in the interim.

As noted above, all deferred payments must bear interest at the §7520 rate, compounded annually. The regulations requiring the use of the §7520 rates were effective May 1, 1989.[441] Rev. Rul. 88-81 provided sample provisions that simply refer to "the rate of interest that federal income tax regulations under §664 of the Internal Revenue Code prescribe," rather than the specific rate of interest. This language was preferable to specifying a rate, not only because it was the IRS-suggested language, but also because it allowed for a change in the prescribed interest rate. In Rev. Rul. 92-57, the IRS ruled that the sample trust language in Rev. Rul. 88-81 and Rev. Rul. 82-165 incorrectly computed the interest to be paid on the deferred unitrust amount. The 1992 ruling noted that the sample language required that interest be added to the amount specified in Reg. §1.664-1(a)(5)(ii), which already included a calculation for the addition of interest.

B. Impact of Private Foundation Rules

Section 4947(a)(2), which brings charitable remainder trusts (CRTs) under certain of the private foundation rules,[442] applies to a trust if the trust holds amounts for which a charitable deduction was allowed. The regulations provide that a trust will be treated as having amounts in trust "from the date of its creation, even if a deduction was allowed for such amounts only at a later date."[443] For this purpose, the date of creation of a CRT is determined by applying the rules contained in Reg. §1.664-1(a)(4).[444] The regulations under §4947 state that a split-interest trust created by will is generally considered a split-interest trust under §4947(a)(2) as of the decedent's date of death.[445] However, the regulations under §664 provide that "[s]olely for purposes of section 664 and the regulations thereunder" a CRT is not deemed created until it is first funded.[446] Therefore, although income tax treatment as a CRT begins only when the trust is funded (as discussed at V.D., below), the trust is potentially subject to the private foundation rules as of the date of death, subject to the exception for a reasonable period of settlement. However, the self-dealing provisions of §4941 may apply immediately, even during the period of settlement.[447]

An estate[448] (or revocable trust that becomes irrevocable upon the death of the grantor)[449] that must hold some or all of its net assets in trust thereafter for both charitable and noncharitable beneficiaries is not considered a split-interest trust under §4947(a)(2) until the expiration of a "reasonable period of settlement."[450]

"Reasonable period of settlement" means the period reasonably required (or actually required, if shorter) by the trustee to perform the ordinary duties of administration necessary to settle the trust, including such duties as collecting assets, paying debts, taxes, and distributions, and determining the rights of subsequent beneficiaries.[451]

---

[436] Reg. §1.664-1(a)(5)(ii). This formula applies to valuation dates after April 30, 1989. The regulation also describes the computation of the deferral period payment for transfers made after November 30, 1983, and before May 1, 1989. Reg. §1.664-1(a)(5)(ii).

[437] Reg. §1.664-1(a)(5)(ii), §1.664-4(e)(6).

[438] Before this ruling, the IRS had taken the position in Rev. Rul. 72-395 that such language was optional. The requirement did not apply to: (1) a decedent who dies after May 5, 1980, but before May 5, 1981, without having amended any dispositive provision of his or her will after May 5, 1980; or (2) a decedent who dies after May 5, 1981, and was under a mental disability (as defined in Reg. §1.642(c)-2(b)(3)(ii)) on May 5, 1981, and at all times thereafter. Rev. Rul. 80-123.

[439] *Modified by* Rev. Rul. 88-81 and Rev. Rul. 92-57.

[440] See Worksheet 2 for the list of sample documents.

[441] *See* Reg. §1.664-1(a)(5)(iv)*(a)*. Trusts created before October 25, 1983, are subject to a 6% rate provided the trust is not amended after that date. Reg. §1.664-1(a)(5)(iv)*(d)*. In addition, trusts created or amended after October 24, 1983, and before August 9, 1984, may use a 10% rate. Reg. §1.664-1(a)(5)(iv)*(c)*. The 10% rate applies to any trust executed or amended after August 8, 1984, and before May 1, 1989. Reg. §1.664-1(a)(5)(iv)*(b)*.

[442] See VI.G., below, for the private foundation rules.

[443] Reg. §53.4947-1(c)(1)(iii).

[444] Reg. §53.4947-1(c)(1)(iii).

[445] Reg. §53.4947-1(c)(6)(i).

[446] Reg. §1.664-1(a)(4).

[447] Reg. §53.4947-1(c)(6)(iii).

[448] Reg. §53.4947-1(c)(6)(ii).

[449] Reg. §53.4947-1(c)(6)(iii).

[450] Reg. §53.4947-1(c)(6)(iii).

[451] Reg. §53.4947-1(c)(6)(iii).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

If the administration of an estate is unreasonably prolonged, the estate will be considered terminated for federal income tax purposes after the expiration of a reasonable period for the performance by the executor of all of the duties of administration.[452] Accordingly, the estate will be subject to all applicable private foundation provisions after the date the estate is considered terminated. For example, a loan of estate assets to any disqualified person would be an act of self-dealing under §4941.[453]

During the administration of the estate (or formerly revocable trust), the executor or successor trustee may determine that certain assets should not be used to fund a CRT (e.g., Subchapter S stock). The only logical purchasers for such closely held assets may be individuals who could not normally buy or sell assets from the estate or trust due to the self-dealing rules of §4941 (as discussed in VI.G., below). However, as long as the regulatory requirements are followed, assets may be sold to "disqualified persons" during the estate administration period.[454] The sale may be for a note that can then be used to fund the CRT without being subject to penalties.[455]

C. Estate Tax Deduction Allowed for Value of Charitable Interest

As mentioned above, §2055(a) provides for a deduction from the value of the gross estate of bequests for public, charitable, and religious purposes.[456] An estate tax deduction is permitted only for transfers to organizations that fall within the categories set forth in §2055(a). It is important to note that the charitable organizations and purposes set forth under §2055(a) are not identical to those described in §170(c) and §2522(a). This is discussed in more detail at IV.F.1., above.

If the annuity or unitrust recipient of a testamentary remainder trust makes a qualified disclaimer,[457] the annuity or unitrust interest is considered never to have existed and the bequest is viewed as though it were an outright bequest to charity.[458] In such case, the charitable deduction is not reduced by the value of the annuity or unitrust interest.[459]

The 5% exhaustion rule discussed at IV.D.3., above, disallows a charitable deduction where the likelihood that the charitable interest will vest is less than 5%. Rev. Rul. 78-255 applied the 5% cut off where a decedent's will provided that if his wife died within 30 days of his death, a specific bequest was to go to a relative. If the wife survived, this amount was to become part of the residue that would be transferred to an otherwise qualified charitable remainder trust (CRT). The IRS ruled that the contingent pre-residuary bequest qualified for the deduction because the actuarial probability, at the decedent's death, that the wife would die within 30 days was less than 1%, meaning that the possibility that the contingent bequest would defeat the charitable bequest did not exceed 5%.

Although an estate tax charitable deduction is allowed for property passing outright to non-United States charities,[460] it is not possible to create a qualified CRT that will pass to a foreign charity at termination. Section 2055(e)(2)(A), which allows the charitable estate tax deduction, cross-references the description of a permissible trust to §664. Section 664 limits remainder interests to charities described in §170(c), which includes only domestic charities.

Similar rules exist in the case of a nonresident non-citizen decedent where a bequest is to be used for public, charitable, or religious purposes.[461] The limitation on deductions set forth in §2055(e)(2)(A) where a noncharitable income interest and a charitable remainder interest exist in the same property also applies to the estate of a nonresident non-citizen decedent.[462] Special rules disallow an estate tax (or gift tax) marital deduction for an annuity trust or unitrust interest payable to a non-citizen spouse.[463] The estate, however, will be allowed a marital deduction for the annuity or unitrust interest if the CRT is established as a qualified domestic trust (QDOT) under §2056A.[464] For further discussion of QDOTs, see 842 T.M., *Transfers to Non-Citizen Spouses.*

1. Calculation of the Estate Tax Charitable Deduction

The amount of the charitable estate tax deduction under §2055(a) is generally the value of the property included in the estate and transferred to a charitable organization. There are no percentage limitations comparable to those restricting the availability of an income tax charitable deduction, nor is there a difference between public charities and private foundations. The regulations provide that where property is transferred for both a charitable and noncharitable purpose, a deduction may be taken for the value of the charitable beneficial interest only to the extent the interest is presently ascertainable and severable from the noncharitable interest.[465] For example, the charitable deduction for a charitable remainder unitrust (CRUT) would be limited where the CRUT provides a unitrust amount for the life of a noncharitable beneficiary and the trustee must distribute 25% of the unitrust amount to the noncharitable beneficiary at least annually, but has discretion to distribute the remaining 75% of the unitrust amount to either the named charitable beneficiary or the noncharitable beneficiary. Because the remaining 75% portion is within the complete discretion of the trustee, such amount is not ascertainable or severable from the noncharitable interest and, therefore, not eligible for a charitable deduction.[466]

---

[452] Reg. §53.4947-1(c)(6)(ii).

[453] Reg. §53.4947-1(c)(6)(ii)*(B) Ex.*

[454] *See* Reg. §53.4941(d)-1(b)(3), §53.4947-1(c)(6)(ii). *See* PLR 201850012 as an example. Although the ruling includes a private foundation rather than a CRT, the rules and the exception are the same.

[455] Reg. §53.4941(d)-2(c)(1).

[456] The Tax Reform Act of 1969 (1969 Act) amended §2055(e)(2) to provide that a deduction under §2055(a) is allowed for a bequest of a remainder interest in trust to a charitable organization, provided the interest is in the form of a charitable remainder annuity trust, a charitable remainder unitrust, or a contribution to a pooled income fund. These rules are effective for estates of decedents dying after December 31, 1969. For the history and transition rules, see XI., below. For further discussion of §2055(a), see 839 T.M., *Estate and Gift Tax Charitable Deductions.*

[457] *See* §2518.

[458] Reg. §20.2055-2(c)(1).

[459] *See* TAM 8031018.

[460] Reg. §20.2055-1(a).

[461] §2106(a)(2).

[462] §2106(a)(2)(E).

[463] §2056(d), §2523(i).

[464] *See* PLR 9244013.

[465] Reg. §20.2055-2(a). For a discussion of the method for computing the value of the remainder interest, see IV.H., above.

[466] CCA 202233014.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Practice Point: A testamentary CRT provides more flexibility/ongoing control by the Donor's family over which charities shall benefit because the estate tax rules do not recognize a difference between public charities and private foundations.

If under applicable state law there is equitable reimbursement to principal as a result of the executor's election to deduct administration fees on the estate's income tax return rather than on the estate tax return, the reimbursement is included in principal for determining the amount of the charitable deduction.[467]

The document must prohibit a testamentary trust from bearing the cost of any administration expenses and debts. The appropriate methodology is to have the estate or formerly revocable trust pay the expenses and debts, and then fund the CRT from the residual estate or trust.[468]

In Rev. Rul. 78-283, the testator created a testamentary annuity trust to be funded with the estate residue, less administration expenses. The annuity amount was stated as a dollar amount, rather than a specified percentage and, therefore, it was not possible to determine whether the stated annuity would satisfy the requirement that it comprise at least 5% of the initial fair market value of the trust assets before computing the death taxes. The ruling states that if it is possible to compute an amount for the charitable deduction that will result in the trust being funded with an amount that satisfies the 5% minimum annuity test, a deduction will be allowed for that amount. Thus, a deduction would be allowed for the amount that would cause the residue to be sufficient for the stated annuity amount to satisfy the 5% test.

2. *Death of Annuity or Unitrust Recipient Before Due Date of Estate Tax Return*

Several rulings have considered the effect of the annuity or unitrust recipient's death before the due date for filing the estate tax return where the governing instrument fails to qualify. In the case of a defective governing instrument, §2055(e)(3)(F) provides that if, by the due date for the filing of an estate tax return (including extensions), an interest in property passes directly for a charitable use described in §2055(a), a deduction will be allowed as if the governing instrument satisfied the requirements of §2055(e)(2) on the date of decedent's death. This amount is computed by reference to the beneficiary's actuarial life expectancy.[469]

Before the enactment of §2055(e)(3)(F), the IRS ruled in Rev. Rul. 76-546 that the death of the annuity recipient of a CRT before the due date of the decedent's estate tax return was not equivalent to a disclaimer of that interest or termination of a power to consume or invade the property as provided in the flush language of §2055(a). The deduction was computed by reducing the value of the trust by the income beneficiary's interest.[470]

A related issue concerns the requirement in the regulations that the value of the annuity be determined on the basis of the recipient's actuarial life expectancy on the date of the decedent's death notwithstanding the beneficiary's death shortly thereafter. Taxpayers have argued that it is unreasonable for a charitable remainder interest to be valued on the basis of the beneficiary's actuarial life expectancy instead of the actual life expectancy in the situation where actual expectancy is known on the date the return is filed. Although this argument has been rejected by some courts,[471] one revenue ruling did use the actual life expectancy where the beneficiary had an incurable disease at the date of decedent's death.[472]

The IRS altered its position on the use of the mortality tables when it issued final regulations under §7520, effective for transactions after December 13, 1995. The regulations, which govern valuations of life, term, and remainder interests under §7520 for income, estate, and gift tax purposes, provide that the mortality tables may not be used to value a life interest if the person who is the measuring interest is terminally ill at the time of the transaction.[473] The regulations define a terminal illness as "an incurable illness or other deteriorating physical condition … if there is at least a 50 percent probability that the individual will die within 1 year." The regulations further provide that, if the individual who is presumed to be terminally ill should survive for 18 months after the transaction, that individual will not be presumed to have been terminally ill unless the contrary is established by clear and convincing evidence.

Therefore, unless the income beneficiary meets the regulatory definition of "terminally ill," the standard actuarial tables must be used even if the beneficiary dies before the estate tax return is filed.

3. *Taxes Payable out of Charitable Bequests*

In certain instances, the federal, state, and/or local death taxes may be payable in whole or in part out of property transferred to the charitable remainder trust before funding. This may be pursuant to the terms of the governing instrument or local law and commonly would take place where the trust is to be funded with the residue of an estate.[474] Where this occurs, the deduction permitted for estate tax purposes is the amount of the transferred property reduced by the amount of the tax.[475] In such case, federal estate tax is payable out of the property to be transferred to charity, which reduces the amount of the charitable transfer. The decrease in the amount passing to charity fur-

[467] *Estate of Britenstool v. Commissioner*, 46 T.C. 711 (1966); Rev. Rul. 78-445. *See also* TAM 8016003.

[468] Reg. §1.664-1(a)(6) *Exs.* (3), (4), (5).

[469] Before the enactment of §2055(e)(3)(F), former temporary estate tax regulation 24 C.F.R. §24.1 (1975) provided that the amount was determined as if the transfer were to a CRAT providing an annuity of 6% of the initial fair market value of the property. Taxpayers challenged the validity of this regulation, arguing that it conflicted with §664(e), which states that in valuing a charitable contribution the remainder interest is computed on the basis that an amount equal to 5% of the net fair market value of the CRT assets (or a larger amount if the trust instrument so provides) is to be distributed each year. However, the courts held that the regulation was not unreasonable nor in contravention of the statutory objective. *See Shriners Hospitals for Crippled Children v. United States*, 602 F.2d 302 (Ct. Cl. 1979); *Merchants Nat'l Bank v. United States*, 583 F.2d 19 (1st Cir. 1978); Rev. Rul. 76-545, *clarified by* Rev. Rul. 82-97.

[470] *See also Simmons v. United States*, 80-1 USTC ¶9,287 (D. Ariz. 1980), *aff'd*, 667 F.2d 832 (9th Cir. 1982); PLR 8026022.

[471] *Shriners Hospitals for Crippled Children v. United States*, 602 F.2d 302 (Ct. Cl. 1979); *Merchants Nat'l Bank v. United States*, 583 F.2d 19 (1st Cir. 1978).

[472] Rev. Rul. 80-80, *obsoleted by*, Rev. Rul. 96-3. In *Bank of California v. United States*, 672 F.2d 758 (9th Cir. 1982), the Ninth Circuit specifically adopted the position of Rev. Rul. 80-80. *See also* PLR 8621049, PLR 8630012.

[473] Reg. §1.7520-3(b)(3), §20.7520-3(b)(3), §25.7520-3(b)(3).

[474] *See* PLR 200539022.

[475] §2055(c); Reg. §20.2055-3(a)(1).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ther reduces the allowable deduction, leading to an interrelated calculation.[476] Where this occurs, the methods of calculating the amount passing to charity and the estate tax are described in IRS Pub. 904, *Estate and Gift Tax Interrelated Computations*.[477]

Comment: Most practitioners now use commercial software to make these often complex interrelated computations although spreadsheets can also be useful in computing interrelated computations or in confirming the commercial software calculations.

The trust instrument should specify how any tax burden is to be allocated within the trust. Absent a direction in the instrument, state apportionment statutes may require that the tax be allocated to principal, which could have the effect of allocating the entire tax to the charitable remainder, reducing the amount of the deduction. In the absence of a specific direction, the IRS indicated in TAM 9419006 that estate and inheritance taxes should be allocated to the entire trust property, even if the apportionment statute would apportion the tax to trust principal. The National Office, citing *Estate of Jack v. Commissioner*,[478] advised that if federal estate tax is apportioned to a CRT, the charitable remainder is valued after deducting the taxes from the value of all the property transferred to the trust. This will produce a larger §2055 deduction than if the taxes were deducted only from the charitable remainder interest, as it will have the effect of making the noncharitable beneficiary bear a portion of the tax. An even larger deduction can be obtained if the instrument specifies that the entire tax is to be apportioned to the noncharitable portion.

4. *Surviving Spouse Elects Against the Will*

If a surviving spouse elects to take against the will, and his or her rights could be satisfied from the CRT, the trust will be disqualified unless the spouse waives his or her rights with respect to the trust.[479] Rev. Proc. 2005-24 allows a grantor's spouse to waive his or her state law elective share right if such right could be satisfied from the assets of the CRT and, thus, disqualify the trust under §664(d). Rev. Proc. 2005-24 also provided a safe harbor (i.e., no waiver necessary) for trusts created before June 28, 2005. In Notice 2006-15, the IRS extended this safe harbor indefinitely, so that the existence of any such right of election, even without a waiver, will be disregarded provided that the surviving spouse does not exercise his or her right of election.

5. *Estate Tax Charitable Deduction for Settlement in Lieu of Funding a Charitable Remainder Trust*

The IRS has issued rulings involving the deductibility of a charitable remainder interest that was accelerated, due to the settlement of a will contest or as a result of the surviving spouse's election to take against the will. For some time, the IRS took the position that a deduction was permitted only in the latter case because of a distinction for federal estate tax purposes between a spouse's election and a settlement agreement. In Rev. Rul. 89-31,[480] acknowledging that several court decisions had been adverse to its position, the IRS ruled that an estate was entitled to an estate tax charitable deduction where a charitable remainder interest in a nonqualified trust was accelerated as the result of a settlement of a bona fide will contest. The IRS warned that it would continue to scrutinize all will contest settlements in order to avoid collusive attempts by the parties to circumvent §2055(e)(2).

In *Estate of Strock v. United States*,[481] the district court allowed a deduction under §2055(a) for a lump sum charitable distribution where it was paid in settlement of a will contest in lieu of a remainder interest in a split-interest trust. Citing *Flanagan v. United States*,[482] the court held that §2055(e) was inapplicable because the charitable interest passed directly to the charity and, as a result, the transfer involved none of the abuses that §2055(e) was enacted to eliminate.

Comment: The courts have gone considerably further than the IRS in allowing a deduction for accelerated charitable remainder interests. In *Oetting v. United States*[483] and *Estate of Thomas v. Commissioner*,[484] the courts held that an estate could receive a §2055(a) deduction for an accelerated remainder interest in a nonqualifying trust as long as there was a valid nontax reason for the severance.

A deduction is permitted where a charitable remainder interest in a nonqualified trust is accelerated as a result of a spouse's election to take against the will.[485] In Rev. Rul. 78-152,[486] the decedent's will provided for income to be paid to decedent's spouse for life with remainder to a qualified charity. The spouse elected pursuant to state law to take against the will, and, as a result of the election, the estate was distributed as though the spouse had predeceased the decedent. Rev. Rul. 78-152 concluded that a deduction was permitted in that instance, but not in the situation presented in Rev. Rul. 77-491 (since revoked),[487] because of the legal distinction for federal estate tax purposes between a spouse's election and a settlement agreement.

6. *Electing to Use a Prior Month's §7520 Rate*

The executor may use the §7520 rate for the month of the date of death of the decedent, or elect to use one of the two prior months' rates. This election is discussed at IV.H.5., above. The taxpayer must use the same rate for the valuation of all the interests involved in the transfer.

Practice Point: The executor will select the highest available §7520 rate. This increases the discount factor applied to

[476] Reg. §20.2055-3(a)(2).

[477] *See also* 844 T.M., *Estate Tax Credits and Computations*, and 834 T.M., *Transfer Tax Payment and Apportionment.*

[478] 8 T.C. 272 (1947).

[479] Rev. Proc. 2005-24 provides that the grantor's spouse need not make a waiver if applicable state law does not give him or her a right of election against the grantor's estate or if the state law elective share could not include charitable remainder trust assets (other than an annuity or unitrust amount payable to the spouse as the named recipient).

[480] *Revoking* Rev. Rul. 77-491, and *modifying* Rev. Rul. 78-152.

[481] 655 F. Supp. 1334 (W.D. Pa. 1987).

[482] 810 F.2d 930 (10th Cir. 1987).

[483] 712 F.2d 358 (8th Cir. 1983).

[484] T.C.M. 1988-295.

[485] Reg. §20.2055-2(e)(1) provides that the principles of §2056 and the regulations thereunder apply in determining whether an interest in property passes or has passed from the decedent. Reg. §20.2056(c)-2(c) provides, in part, that if the surviving spouse elects to take against the will, the property that the spouse does not acquire is not considered as having passed from the decedent to the surviving spouse.

[486] *Modified by* Rev. Rul. 89-31.

[487] *Revoked by* Rev. Rul. 89-31.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

the retained interest in a charitable remainder annuity trust and, therefore, increases the deductible value of the charitable remainder interest. In the case of a charitable remainder unitrust, selection of a higher §7520 rate will slightly increase the value of the remainder because it will reduce the Table F adjustment factor in cases in which the payments are required to be paid more frequently than annually or there is any gap between the valuation date and the payment date. That reduction of the Table F adjustment factor will in turn reduce the adjusted payout rate, which will in turn increase the value of the remainder. No Table F adjustment is necessary if payments are made annually and there is no gap between the valuation date and the payment date in the first full taxable year of the trust.

D. Effect on Estate Income Taxation Between Date of Death and Date of Trust Funding

The obligation to pay the unitrust or annuity trust amount arises as of the date of the decedent's death, but the actual payment of such amount may be deferred until the end of the year in which occurs a complete funding of the trust.[488] The regulations permit either the estate or the partially funded trust to pay the annuity or unitrust amount during the period of administration.[489] During the period of estate administration, the trustee of a charitable remainder trust (CRT) is granted the discretion to determine the amount of any distributions to be made to the annuity or unitrust recipient and may defer payments until the year in which occurs a complete funding of the trust.[490] The timing of these interim distributions will obviously determine when the recipient must report the income. For example, the decision by the trustee to defer payments until the year of full funding will create a bunching of several years' income at the beneficiary level.

The taxation of distributions to an income recipient made by an estate is governed by the normal rules of Subchapter J, Chapter 1, subtitle A of the Code other than §664.[491] Distributions to an estate beneficiary carry out distributable net income (DNI) from the estate that is then taxable to the beneficiary. However, distributions made by a partially or fully funded CRT are governed by §664. This means that distributions from a partially funded trust, but not an estate, are governed by the class and category rules discussed at VI.F., below. The taxable nature of income earned pending funding should be considered.

A testamentary CRT funded with estate assets is considered a beneficiary of the estate.[492] For purposes of its fiduciary income tax, the estate can deduct its funding distributions to the trust or distributions to the recipients on account of the annuity or unitrust amount to the extent the distribution carries out DNI.[493] A CRT is exempt from tax as soon as it is partially funded and, therefore, the DNI carried out from the estate to the trust is not taxed to the trust.[494] Tax is due on the distribution to the trust only to the extent it is ultimately redistributed to a noncharitable beneficiary.[495]

The tax consequences to the estate are different where the bequest to a CRT is considered a pecuniary legacy within the meaning of §663(a)(1). In such case, the estate is not entitled to a deduction for the funding distributions, and the estate could recognize gain or loss on the distribution if it funds the trust with distributions in kind.[496]

Section 642(c) grants an estate an unlimited charitable deduction for the amount of its gross income that is required to be paid for a purpose specified in §170(c) or set aside for such a purpose. A distribution to a CRT that possesses both noncharitable and charitable beneficiaries does not satisfy this requirement.[497]

For a distribution to qualify for the deduction, the likelihood that the amounts set aside for charity may be used for a noncharitable purpose must be so remote as to be negligible.[498] The National Office has advised that the possibility of invasion is negligible where a partially funded trust pays the annuity or unitrust amount currently or the estate sets aside such amount for future payment, including a sum for the satisfaction of any interest due at the applicable rate.[499] In GCM 39249 (June 27, 1984), commenting on a proposed revenue ruling, the IRS equivocated as to whether either option would guarantee the allowance of a set-aside deduction. Even if the executor were setting aside funds for payment of the annuity or unitrust amount, the remaining corpus could be invaded in future years if the trust income were insufficient to make the annuity or unitrust payments. Therefore, an estate does not seem to be entitled to a §642(c) deduction for the amounts set aside because of the possibility that the amounts could be paid to a noncharitable beneficiary, with an arguable exception in the case of a net income unitrust.

Funding distributions to a CRT carry out current DNI, and the estate is entitled to a distribution deduction to the extent of such DNI. The distribution deduction is not available where the estate defers funding the trust and instead sets aside current income for future distribution.

Accordingly, partial funding distributions may be advisable in the case of a testamentary CRT, because items of income received by the estate before the funding of the trust will be subject to tax at the estate level, whereas these same items would not be subject to tax if realized by the trust.

---

[488] Reg. §1.664-1(a)(5)(i).

[489] Reg. §1.664-1(a)(5)(iii).

[490] The IRS sample documents, listed below on Worksheet 2, include provisions to this effect. For the authorities, see Rev. Rul. 80-123, *clarified by* Rev. Rul. 82-165, and *modified by* Rev. Rul. 88-81 (requiring that trustee be given option to defer payments of unitrust amount until year of full funding). *See also* Rev. Rul. 92-57, *modifying* Rev. Rul. 82-165 *and* Rev. Rul. 88-81.

[491] Reg. §1.664-1(a)(5)(iii).

[492] Reg. §1.643(c)-1.

[493] *See* TAM 8810006; GCM 39707 (Dec. 11, 1987). The TAM and GCM, which deal with the same estate, also conclude that any distribution made by the estate to the trust beneficiary is treated as if made to the trust because the trust beneficiary is not a beneficiary of the estate. This conclusion seems to contradict Reg. §1.664-1(a)(5)(iii).

[494] Reg. §1.664-1(a)(6) *Ex.* 5. A testamentary trust is treated as a CRT as soon as it is partially funded and is exempt from tax immediately. Reg. §1.664-1(a)(6) *Ex.* 5.

[495] Even though DNI passed out from the estate to the trust may be composed of ratable portions of the various types of income, to the extent the DNI includes ordinary income that income will be deemed to be distributed first when the estate beneficiary receives distributions. Generally, capital gains are not included in DNI and, therefore, are taxed at the estate level rather than carried out to the trust or trust beneficiary. See 852 T.M., *Income Taxation of Trusts and Estates*, for further discussion of DNI.

[496] Reg. §1.661(a)-2(f). *See also* §267(b)(13).

[497] Reg. §1.642(c)-2(a), §1.642(c)-2(d).

[498] Reg. §1.642(c)-2(d).

[499] TAM 8341001.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Once the trust is fully funded, the trustee must determine the unitrust or annuity trust amount payable to the recipient. The determination must be made within a reasonable time following the end of the taxable year in which the trust is fully funded.[500] Those distributions by the trust are taxed to the beneficiary under the "category and class" system discussed at VI.C. and VI.F., below.[501]

In computing the amount payable, the trust is credited with any direct distributions made by the estate to the annuity or unitrust recipient during the period of administration. The distributions made directly by the estate are governed by the general rules of subchapter J[502] and, as a result, should not impact on the trust's class and category system. This notwithstanding, GCM 39707 (Dec. 11, 1987) concluded that an estate discharged the legal obligation of a CRT where the estate paid a recipient directly. The GCM further reasoned that the trust was the deemed recipient of the payment and that the recipient was deemed to receive the payments from the trust, governed by the class and category rules applicable to distributions from CRTs. Accordingly, the trust received credit for any payments made by the estate and had to take such payments into account for purposes of the computation of the trust's class and category system of tracking income. This GCM (i) would be difficult to apply in a year before the funding of the trust. as the system would not yet be operative, and (ii) appears to render Reg. §1.664-1(c)(5)(iii) a nullity.

E. Reformation of Defective Trusts

If a split interest trust is defective, a qualified reformation may save the estate tax charitable deduction.[503] For a reformation to be qualified, the following five criteria must be met (each element discussed further below):[504]

1. the charitable interest prior to reformation must be eligible for a deduction under §2055(a) but for the provisions of §2055(e)(2);

2. the reformation must be effective as of the decedent's date of death;

3. the nonremainder interest must terminate at the same time before and after reformation;

4. the actuarial value of the charitable remainder as reformed must not differ by more than 5% from the actuarial value of the charitable remainder prior to reformation; and

5. if, prior to reformation, the noncharitable interest is not expressed in terms of a specified dollar amount, or a fixed percentage of the property, the reformation must be commenced within the time limit prescribed by §2055(e)(3)(C)(iii).

Qualified reformations may include the reformation of a trust that fails to satisfy the minimum charitable benefit rules.[505] To qualify for reformation, the otherwise nonqualifying interest must be a "reformable interest."[506] Section 2055(e)(3)(C)(i) defines "reformable interest" as an interest for which an estate tax charitable deduction would have been allowed at the time of the decedent's death but for the qualifying rules imposed on split-interest trusts by the 1969 Act. This threshold requirement can sometimes raise serious problems.

Although a defective CRT may qualify as a reformable interest for purposes of §2055(e)(3), the existence of a power to invade corpus will prevent a trust from qualifying as a CRT under §664. Accordingly, the reformation must delete the power to invade, which in turn requires the noncharitable beneficiary to disclaim irrevocably his or her right to receive any discretionary distributions. Typically, the beneficiary also is the recipient of the unitrust or annuity trust amount. In such case, the recipient must execute an irrevocable partial disclaimer.[507]

Practice Point: State law should also be consulted to determine the requirements for such a disclaimer.[508]

An interesting issue arises where the defective CRT grants the trustee a wholly discretionary right to invade corpus. Because the right to invade is not limited by an ascertainable standard, the interest would not have qualified under the pre-1969 Act rules and, therefore, does not qualify as a "reformable interest." Arguably, a disclaimer also should work in this case to create a reformable interest.

The time restrictions imposed on the reformation vary, as do the means by which the reformation may be made, depending on the extent to which the governing instrument fails to comply with these qualifying rules. For example, there is no time limitation on the commencement of the reformation proceedings where the interest of the noncharitable beneficiary or beneficiaries is fixed either as a specified dollar amount or as a fixed percentage of the fair market value of the property involved.[509] In addition, such trusts may be reformed by nonjudi-

---

[500] Reg. §1.664-1(a)(5).

[501] Reg. §1.664-1(a)(5)(iii).

[502] Reg. §1.664-1(a)(5)(iii).

[503] The Tax Reform Act of 1984 (Pub. L. No. 98-369) amended §2055(e)(3) to provide permanent rules governing the reformation of charitable split-interest trusts that do not satisfy the technical requirements imposed by the Tax Reform Act of 1969 (Pub. L. No. 91-172). Before 1984, there had been a series of temporary reformation provisions, the first of which was enacted in 1974. The last temporary reformation provisions covered trusts created or wills executed before December 31, 1978, and required any amendment to be completed (or judicial proceedings begun) by December 31, 1981. See former §2055(e)(3), before amendment by the 1984 Act.

[504] §2055(e)(3)(C).

[505] §2055(e)(3)(J), added by TRA '97, Pub. L. No. 105-34, §1089(b)(3). See XI., below, for the effective date of these rules.

[506] §2055(e)(3)(C). *See* PLR 200927013 (judicial reformation of trusts into §664(d) CRATs was §2055(e)(3) qualified reformation because reformation satisfied §2055(e)(3) requirement that pre-reformation charitable interests be reformable interests), PLR 200330028 (judicial reformation of charitable trusts into §664(d)(2) unitrusts was §2055(e)(3) qualified reformation because reformation satisfied §2055(e)(3) requirement that pre-reformation charitable interests be reformable interests, and partial disclaimer was effective).

[507] *See* PLR 9004011 (approving reformation where beneficiaries made qualified disclaimer under §2518). *See also* PLR 9349010 (permitting reformation when unitrust beneficiary disclaimed her right to receive discretionary distributions of principal for her health). *Cf.* PLR 201333006 (judicial reformation of trust to establish portion as §664(d) CRUT and eliminate trustee's authority to pay noncharitable beneficiaries' funeral and last illness expenses from such portion — along with clarification of funding amount, which was based on §2010(c) unified credit where decedent/grantor died in early 2010, and correction of unitrust payment amount and certain administrative provisions — was §2055(e)(3) qualified reformation). See also 848 T.M., *Disclaimers — Federal Estate, Gift and Generation-Skipping Tax Considerations*.

[508] See 848 T.M., *Disclaimers — Federal Estate, Gift and Generation-Skipping Tax and State Law Considerations*.

[509] §2055(e)(3)(C)(ii). A time constraint is imposed to the extent that the estate wishes to take a §2055 deduction for the split interest on the estate tax return, as the reformation must be completed before filing the Form 706. If the

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

cial means. This liberal reformation rule was designed as a relief provision for trusts that do not qualify due to minor technical shortcomings.[510]

A trust that fails to qualify under the above rules must be reformed by judicial proceedings within a specified time period. In such case, the judicial reformation proceedings must be commenced on or before the 90th day following the due date, including extensions, of the decedent's estate tax return or, if no estate tax return is required, the due date, including extensions, of the fiduciary income tax return for the first taxable year for which the trust must file such a return.[511] For example, the Tax Court in *Estate of Tamulis v. Commissioner* held that a trust could not be reformed because the noncharitable beneficiaries' interests were not fixed as required by §2055(e)(3)(C)(ii) and the estate did not commence the reformation within 90 days after estate tax return was due pursuant to §2055(e)(3)(C)(iii)(I). In affirming the Tax Court's decision, the Seventh Circuit rejected the executor/trustee's argument that the executor/trustee had substantially complied with the reformation requirements by administering the trust as a §664 CRUT and including a statement on the decedent's estate tax return that the trust would be administered as such. The Seventh Circuit held that the doctrine of substantial compliance does not apply to a CRT reformation that fails to satisfy §2055(e)(3)(C)(iii).[512]

Practice Point: If the reformation of a defective split-interest trust is contemplated, it should be instituted as soon as possible regardless of the applicable time limitations, because the IRS will seek payment of interest on any pre-reformation tax liability. The interest will run from the due date of the return until the date on which the IRS receives notice of the reformation and possibly for 180 days thereafter.[513]

The governing instrument must be reformed by amendment, construction, or otherwise in such a way as to qualify as a CRT under §664. The difference between the date of death actuarial value of the remainder interest before reformation and the date of death value of the remainder interest after reformation cannot vary by more than 5% of the actuarial value of the pre-reformation interest.[514]

In certain circumstances, it may not be possible to reform the trust in such a way as to comply with the literal terms of these rules. In a particularly liberal private letter ruling, the IRS permitted the reformation of a defective CRT that resulted in the recipient of the annuity amount receiving an annuity that was less than the required 5%.[515] The trust did not qualify under §2055(e)(2) because the stated annuity amount was less than 5% of the fair market value of the assets. Under the reformation, the trust in the ruling was to pay the amount specified in the trust to the annuity recipient and was to pay the difference between that amount and the required 5% annuity currently to the charitable remainder beneficiary.[516] The IRS allowed the estate a charitable deduction for the actuarially determined present value of the charitable remainder interest and the charitable lead annuity interest. The IRS did not address whether the reformation violated the 5% variance rule requiring that the difference between the pre-reformation charitable remainder interest and the post-reformation charitable remainder interest not exceed 5% of the pre-reformation value.

The reformation must be effective as of the date of the decedent's death[517] and cannot alter the timing for the termination of the noncharitable interest.[518] This latter requirement is satisfied if a CRT with a term that exceeds 20 years is reformed to have a 20-year term.[519]

For estate tax purposes, a CRT that would qualify but for satisfying the minimum 10% charitable benefit requirement may either be: (i) declared null and void *ab initio*; or (ii) changed or reformed by reducing the payout rate or duration, or

estate is unable to reform the trust by that date, the estate could file the return without taking the deduction and then claim a refund when the reformation is complete. In such cases, the reformation (and the refund claim) must be completed within three years of the filing of the return or two years of payment of the tax, whichever is later. §6511(a).

[510] Examples of such minor technical shortcomings are incorrect or missing valuation or interest provisions for short taxable years, additional contributions, and years in which the noncharitable interest terminates. H.R. Rep. No. 98-432 (1984), *reprinted in* 1984 U.S.C.C.A.N. 697.

[511] §2055(e)(3)(C)(iii). If an estate tax return is not to be filed, the estate should choose a year end that will allow it the greatest period of time to commence reformation proceedings.

[512] *Estate of Tamulis v. Commissioner*, T.C. Memo 2006-183, *aff'd*, 509 F.3d 343 (7th Cir. 2007). *See also Estate of Hall v. Commissioner*, 93 T.C. 745 (1989) (no qualified reformation of trust that required net income payments to income beneficiary because judicial proceeding was not timely commenced); *Estate of Block v. Commissioner*, T.C. Memo 2023-30 (where CRAT established upon decedent's death provided that income beneficiary receive greater of all net income or $50,000 at least annually and trustees did not amend CRAT to remedy CRAT's failure to provide fixed dollar amount until nearly two years following decedent's death, Tax Court held that (i) CRAT did not qualify for default qualified reformation under §2055(e)(3)(B), and (ii) CRAT trustees remedied CRAT defect without judicial process far beyond "90-day following estate tax return" due date; Tax Court rejected substantial compliance argument because "Congress made clear that the rules for qualified reformations are to be construed strictly, in order to prevent abuse of the charitable deduction," even though court acknowledged that abuse in this instance was unlikely because income payment would likely never vary from fixed amount ($50,000) due to size of CRAT and trustees had always paid such fixed amount); PLR 200548019 (IRS ruled that decedent's estate did not qualify for Reg. §301.9100-3 extension of §2055(e)(3)(C)(iii) 90-day deadline because Reg. §301.9100-3 allows discretionary relief for regulatory, but not statutory, elections (or deadlines)).

[513] *See Shriners Hospitals for Crippled Children v. United States*, 14 Cl. Ct. 51 (1987), *rev'd*, 862 F.2d 1561 (Fed. Cir. 1988).

[514] §2055(e)(3)(B)(i). *See* PLR 201947007 (reformation approved where difference between actuarial value of qualified interest and actuarial value of reformable interest did not exceed 5% of actuarial value of reformable interest), PLR 200122045 (amendment of trust that initially failed to qualify as CRUT did not cause trust to qualify because difference in value between qualified interest and reformable interest was greater than 5% of value of reformable interest). See PLR 9349010 for a successful reformation where the difference was less than 5%.

[515] PLR 8845012.

[516] *See also* PLR 201947007 (judicial reformation approved by IRS where unitrust amount increased from 3.5% to required 5% minimum), PLR 200622005 (approving reformation of testamentary CRT to increase unitrust amount from 4% to required 5% minimum and make portion of unitrust amount payable to charity), PLR 200306008–PLR 200306009 (reformation of testamentary CRAT to increase annual annuity to required 5% minimum, with increase to be paid to charity, was §2055(e)(3) qualified reformation, provided reformation was effective under local law and requirements of §664(d)(1)(D) were satisfied).

[517] §2055(e)(3)(B)(iii).

[518] §2055(e)(3)(B)(ii)(I). *See* PLR 200122045 (amendment of trust that initially failed to qualify as CRUT did not cause trust to qualify because pre-reformation nonremainder interest and post-reformation nonremainder interest did not terminate at same time).

[519] §2055(e)(3)(B). *See* PLR 201947007 (judicial reformation approved by IRS where unitrust payments to grandchild who was not living at the time of the creation of the trust would cease on earlier of grandchild's death or 20 years from commencement of unitrust payments).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

both, to reduce the noncharitable beneficiaries' interest to satisfy the requirement.[520] In the case of a testamentary transfer, the reformation must be commenced judicially within 90 days of the due date of the federal estate tax return (including extensions) or, if no estate tax return is due, by the last day for filing the income tax return for the first taxable year in which such a return is required to be filed by the trust.[521] Unlike a reformation commenced under §2055(e)(3)(B), a reformation solely to meet the 10% remainder requirement does not need to meet the 5% variance test of §2055(e)(3)(B)(i)(II).[522]

Practice Point: Because it is not possible to know the §7520 rate for the date of death, it may be appropriate to draft the testamentary CRT with the provisions desired by the testator while including a self-correcting mechanism if the rate at the date of death would cause the trust to be disqualified. For example, the payout amount could be determined by formula or the executor could be directed to lower the payout rate to the percentage that would allow the trust to qualify.

Practice Point: If the remainder is close to 10%, run calculations to determine if the election to use one of the prior months' §7520 rate would allow the trust to qualify. See IV.H.5., above, for this election.

In the case of a trust that is declared void, no estate tax charitable deduction will be allowed for any transfer to that trust.[523]

The amount of the post-reformation charitable deduction cannot exceed the actual amount that would have been allowed for the remainder interest if the trust had qualified.[524] The IRS is not entitled to any interest on the estate tax that would have been payable on the defective trust for the period before the reformation, since the reformation is considered effective as of the testator's death.[525]

Practice Point: When filing a Form 706 showing a charitable deduction for a reformed CRT, attach all relevant documents, including the calculations showing that the interest was reformable within the meaning of §2055(e)(3).

In Rev. Rul. 74-283, the IRS ruled that it was bound by the decision of state trial courts approving reformations of nonqualified CRTs under the transition rules and was not free to question the reformations.

The IRS's response to a state court's decision is also illustrated by Rev. Rul. 76-17. A decedent's will established a nonqualified CRT, and the executors attempted, in a timely manner, to reform the will to obtain a charitable deduction. The local probate court refused to approve a reformation creating a qualified CRT and directed that a life annuity be purchased for the income beneficiary and the remaining funds be delivered to the named charity upon the completion of the administration of the estate. The IRS ruled that because the court's order to the executors did not result in a qualifying charitable remainder trust, no charitable deduction was allowable under §2055.

F. Allocation of GST Exemption

If a testamentary charitable remainder trust (CRT) could have a skip person (i.e., grandchild) as a beneficiary, even a remote beneficiary, the generation-skipping transfer (GST) tax issues must be considered. The automatic allocation rules at death[526] are different from the automatic allocation rules that apply to lifetime transfers, so unintended allocations could occur. The following is not a full analysis of the GST tax consequences; it is only intended to highlight situations that must be analyzed further. See 850 T.M., *Generation-Skipping Transfer Tax (Chapter 13)*, for the detailed analysis.

If a testamentary CRT is drafted to have a grandchild or other skip person as the initial noncharitable beneficiary, typically the estate plan would contemplate that the executor should allocate GST exemption to the trust. If it were not allocated, the distributions to the noncharitable beneficiary would be subject to the GST tax.

If the trust were instead drafted as a term trust, with a non-skip person (i.e., child) as the initial beneficiary and the grandchild only receiving distributions if his or her parent dies within the 20-year term, then an allocation of GST exemption might or might not be appropriate. Considerations would include the age and health of the child and possible other alternative uses of the decedent's exemption. This is the type of trust that could receive an unintended allocation under Reg. §26.2632-1(d)(2) because it has the potential for distributions to a skip person.

Practice Point: Even if the executor's decision regarding allocating the GST exemption is to allow the automatic allocation rules to apply, the effect of that decision should be clearly shown on the estate tax return. This will assist future generations and their professionals in determining the GST profile of the affected trusts, as well as make it clear that the executor considered the issue. See 822 T.M., *Estate, Gift, and Generation-Skipping Tax Returns and Audits.*

G. Estate Tax Inclusion of Property Subject to a Power of Appointment

Section 2041(a)(2) provides that property over which a decedent at death holds a general power of appointment created after October 21, 1942, is included in the decedent's estate. If property is includible under this provision, and the property passes to a charitable organization described in §2055(a), a corresponding charitable deduction is allowed. For purposes of §2055, the property is considered a bequest to charity from the holder of the power in whose estate the property is included.[527] Therefore, the same rules apply as discussed above if an estate tax charitable deduction is to be allowed.

In Rev. Rul. 76-504, a decedent's spouse, who died in 1968, created a testamentary trust under which the decedent

---

[520] §2055(e)(3)(J), added by TRA '97, Pub. L. No. 105-34, §1089(b)(3). The monthly applicable federal rate, the age of each beneficiary, and the adjusted payout rate will all affect the value of the charitable remainder.

[521] §2055(e)(3)(J), referring to §2055(e)(3)(C)(iii). *See* PLR 200414011 (decedent's inter vivos unitrust that failed to satisfy §664(d)(2)(D) 10% remainder requirement from its inception was not eligible for qualified reformation because reformation not commenced within §2055(e)(3)(J) and §2055(e)(3)(C)(iii) period).

[522] H.R. Rep. No. 105-220, Conference Report to Accompany H.R. 2014, Taxpayer Relief Act of 1997 (Pub. L. No. 105-34).

[523] §2055(e)(3)(J).

[524] §2055(e)(3)(E).

[525] *Oxford Orphanage, Inc. v. United States*, 775 F.2d 570 (4th Cir. 1985). *Cf. Shriners Hospitals for Crippled Children v. United States*, 862 F.2d 1561 (Fed. Cir. 1988) (estate entitled to interest on deficiency paid before reformation of trust under transitional rule in 1984 Act).

[526] Reg. §26.2632-1(d)(2).

[527] §2055(b).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

was given a life income interest and a testamentary power of appointment over trust corpus. If the decedent failed to exercise her power of appointment, the trust income was payable upon her death to another person for life with the remainder to a charity. The decedent died testate in 1975 and did not exercise the power of appointment. The trust property was includible in the decedent's estate due to her power of appointment.

The IRS disallowed an estate tax charitable deduction in Rev. Rul. 76-504 because the trust created under the spouse's will was not in the form of a CRT or a contribution to a pooled income fund. Pursuant to the predecessor of §2055(b), the remainder interest in the trust was deemed to result from a transfer made by the decedent after the effective date of §2055(e)(2)(A).[528] Thus, the trust was subject to the rules of §2055(e)(2)(A), which require a deductible remainder interest in trust to be in the form of either a CRT or a contribution to a pooled income fund.

Comment: To obtain the charitable deduction while retaining the spouse's dispositive pattern, the decedent should have exercised her power of appointment to create a qualified CRT.

[528] Effective for decedents dying after December 31, 1969, under a will executed after October 9, 1969. Pub. L. No. 91-172, §201(d).

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

VI. Administering a Charitable Remainder Trust

A. *Calculating the Required Payments to the Noncharitable Beneficiaries*

1. *Charitable Remainder Annuity Trust (CRAT)*

An annuity trust must pay a sum certain to one or more permissible recipients.[529] The payments must be made at least annually for the life of the recipient (or the lives of the recipients, as the case may be) or for a term not to exceed 20 years.[530] The sum certain may be stated in the trust document as an absolute dollar amount or as a fraction or percentage of the initial net fair market value of the property placed in trust.[531] Therefore, the payment will not vary from year to year, except in the initial and final year of the trust. If the payments are made more frequently than annually, the annual amount is divided by the number of payments (typically, four for quarterly payments, but occasionally twelve for monthly payments).

2. *Charitable Remainder Unitrust (CRUT or "Straight CRUT")*

A unitrust must pay a fixed percentage of its net fair market value, as revalued each year, to permissible recipients at least annually.[532] The payments must be for the life of the recipient (or the lives of the recipients, as the case may be) or for a term not to exceed 20 years.[533]

There are three types of unitrusts. The standard unitrust pays the recipient a fixed percentage of the net fair market value of the trust assets as revalued annually. To calculate an annual payment, the trustee multiplies the value of the trust assets on the valuation date in the document by the stated percent.

Practice Point: When calculating the value of the trust, do not overlook any liabilities, including unpaid professional or investment management fees. Liabilities may also include the payment to the noncharitable beneficiary that will be made after the valuation date. The final quarterly or the annual payment for the prior year may be made in January, after the valuation date for the following year. Not reducing the value of the unitrust for the outstanding payment will overstate the value of the trust.

Many charitable remainder trusts (CRTs) are invested in marketable securities. The regulations under §664 do not give any specific guidance if the valuation date (i.e., "first day of the year") is not a business day, and the sample documents use the phrase "first day of each taxable year." There are at least two other areas in the regulations where valuation of traded securities is required: the estate tax valuation rules under §2031 and the private foundation distribution rules under §4942. The estate tax valuation rules require averaging of the securities' values before and after the non-business day valuation date.[534] The private foundation rules permit the choice of a business day for valuation, as long as the practice is followed consistently.[535] If the CRT document is silent as to the valuation date, the trustee is allowed to select the valuation date by indicating it on the initial return.[536]

Practice Point: In the author's experience, institutional trustees have read the word "business" into the phrase "first day of the year," and calculated the values accordingly. If the payments are to be made quarterly, the calculated number is then divided by four. This "first day of year" issue can be avoided by describing the valuation date as the "first business day of the taxable year" when drafting the trust.

3. *Charitable Remainder Trusts with "Net Income" Limitations (NICRUT, NIMCRUT, FLIP-CRUT)*

The net income unitrust (NICRUT) pays the recipient the lesser of the trust's net income or the stated percentage.[537] "Net income" refers to trust accounting income as calculated under the relevant state law and any document provisions; it is not taxable income. There are times when taxable income and trust accounting income are the same (e.g., when the trust receives only taxable dividends, but that is only a coincidence). The net income unitrust can include an optional "make-up" provision that provides that if the income in any year exceeds the unitrust amount for the year, such excess is paid out to the extent necessary to make up for any shortfalls in prior years.[538] Such trusts are referred to a NIMCRUTs, with the added "M" for "make-up."

Charitable remainder trusts with strict "net income" limitations and no make-up provisions are relatively uncommon. They are occasionally used by donors who prioritize the charity's remainder interest. For an example of when one of these might be appropriate, see the discussion of CRTs with a charitable purpose at X.C., below.

The following is an example of a trust utilizing the make-up provision.

> *Example:* The governing instrument provides that the recipient is to receive the lesser of trust income or 5% of the net fair market value of the trust assets, valued on the first business day of the taxable year (i.e., the trust is a NICRUT). On January 1, 20X1, and January 1, 20X2, the net fair market value of the trust assets is $100,000. In 20X1 and 20X2, the trust has net income (within the meaning of §643(b)) of $4,000 and $6,500, respectively. Accordingly, the beneficiary would receive $4,000 (the net income) in 20X1 and $5,000 (the fixed percentage amount) in 20X2. If the governing instrument included a make-up provision, the beneficiary would, instead, receive $6,000 in 20X2, $1,000 of which would represent the shortfall for 20X1.

The sample unitrust forms provided by the IRS contain language for use in drafting "income only" unitrusts, both NICRUTs and NIMCRUTs.[539]

---

[529] §664(d)(1)(A); Reg. §1.664-2(a)(1)(i).
[530] §664(d)(1)(A); Reg. §1.664-2(a)(5).
[531] Reg. §1.664-2(a)(1)(ii), §1.664-2(a)(1)(iii).
[532] §664(d)(2)(A); Reg. §1.664-3(a)(1)(i).
[533] §664(d)(2)(A); Reg. §1.664-3(a)(5).
[534] Reg. §20.2031-2.
[535] Reg. §53.4942(a)-2(c)(4).
[536] Reg. §1.664-3(a)(1)(iv).
[537] §664(d)(3)(A); Reg. §1.664-3(a)(1)(i)(b)(1).
[538] §664(d)(3)(B); Reg. §1.664-3(a)(1)(i)(b)(2).
[539] See Worksheet 2 for the list of Revenue Procedures with sample unitrusts.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

For years, the IRS took the position that a unitrust could not use more than one of the three permissible types of payments during its term; that is, the unitrust could not "flip" from one method to another.[540] This type of unitrust came to be known as a flip unitrust (or FLIP-CRUT). For example, if a grantor contributes an appreciated non-income-producing asset (such as undeveloped land) to a unitrust, it would be desirable to include an income only feature in the trust until the land is sold because of the difficulties in paying the unitrust amount. Once the asset has been sold, however, the grantor would prefer that the income only feature be removed so that he or she receives a unitrust payment regardless of how the funds are invested.

The IRS reversed its former private letter ruling position by issuing regulations, effective for trusts created on or after December 10, 1998.[541] Under certain circumstances, the governing instrument may provide that the unitrust will use either the net income or net income with make-up provisions payout method for an initial period, and then "flip" to the fixed percentage method for the remaining portion of the term beginning with the next tax year of the trust after the year of the flip event.[542] The "flip" must be triggered "on a specific date or by a single event whose occurrence is not discretionary with, or within the control of, the trustees or any other persons."[543] Examples of such events (which must be specified in the governing instrument) include the sale of unmarketable assets,[544] as well as marriage, divorce, death, or the birth of a child.[545] Any "make-up" amount is forfeited upon the conversion as of the first of the year following the year of the "flip" event.[546] A trust cannot convert from a NICRUT or NIMCRUT to a CRAT, only to a CRUT.[547]

Practice Point: The "unmarketable asset," the sale of which will trigger the change in the trust, is often the only significant asset contributed to the trust. However, there is no requirement that the "unmarketable asset" that would trigger the "flip" be any specific proportion of the contribution to the trust.

If a unitrust has a net income feature, the trust instrument may allow treatment of certain realized capital gains as income. Reg. §1.664-3(a)(1)(i)(b)(3) provides that trust income is to be determined under §643(b) and the applicable regulations. Section 643(b) indicates that capital gains may be treated as income if allowed by state law and the trust instrument so provides. In the case of a net income unitrust with a make-up provision, treatment of capital gains as income can be a useful tool if the trust assets are invested in appreciated property that has not produced sufficient income on an annual basis to satisfy the unitrust amount.

For sales or exchanges, pre-contribution gain may not be used in determining the trust's income.[548] Reg. §1.664-3(a)(1)(i)(b)(3) provides that proceeds from the sale or exchange of assets contributed to the trust must be allocated to principal, at least to the extent of the fair market value of the assets on the date of contribution. In addition, proceeds from the sale or exchange of assets purchased by the trust must be allocated to principal, at least to the extent of the purchase price paid by the trust.[549] Otherwise, Reg. §1.664-3(a)(1)(i)(b)(3) states that proceeds from the sale or exchange of trust assets may be allocated to income pursuant to the terms of the governing instrument if not prohibited by applicable state law.[550] For trusts created after January 2, 2004, the governing instrument may give the trustee discretion to make this allocation to the extent a state statute permits the trustee to make adjustments between income and principal so that the beneficiaries are treated impartially.

To conform to the 2004 modification of the definition of income in Reg. §1.643(b)-1, Reg. §1.664-3(a)(1)(i)(b)(3) provides that, for taxable years ending after January 2, 2004, trust income may not be determined by reference to a fixed percentage of the annual fair market value of the trust property, despite any contrary provision in applicable state law. The preamble to T.D. 9102 indicates that the IRS amended Reg. §1.643(b)-1 to reflect changes to the definition of fiduciary accounting income under state laws, which in some cases allowed "trust accounting income" to be defined as a unitrust amount.[551] Because some state laws allow trust accounting income to be defined as a unitrust amount of less than 5%, to allow such a state law to define "trust accounting income" would effectively permit a NIMCRUT with a less-than-5% unitrust amount.

4. *Special Calculation for NIMCRUTs Established Under the Proposed Regulations*

An additional adjustment may be required in the calculation of a unitrust amount for documents drafted before 1998. Before issuing the 1998 and 2004 regulations, the IRS had approved so-called "capital gain unitrusts" in rulings[552] involving net income unitrusts with make-up provisions that treated realized capital gains as trust income. In each case, this was permitted by state law. The IRS, however, required that to the extent that there was a deficiency in the unitrust payments for pri-

[540] *See, e.g.*, PLR 9522021, PLR 9516040, PLR 9506015.

[541] Reg. §1.664-3(a)(1)(i)(c), T.D. 8791, 63 Fed. Reg. 68,188 (Dec. 10, 1998). An existing net income unitrust could be reformed to add a flip provision if the trustee initiated proceedings to reform the trust by June 8, 1999 (subsequently extended to June 30, 2000), so long as the triggering event did not occur in a year before the year in which the court issued the order reforming the trust.

[542] Reg. §1.664-3(a)(1)(i)(c)(2). A mid-year flip is not possible, as §664(d)(2) and §664(d)(3) require that a trust be a CRUT or a NIMCRUT for "any year."

[543] Reg. §1.664-3(a)(1)(i)(c)(1).

[544] Reg. §1.664-1(a)(7)(ii) provides that the term "unmarketable assets" applies to "assets that are not cash, cash equivalents, or other assets that can be readily sold or exchanged for cash or cash equivalents." Examples include real property, closely held stock, and unregistered securities for which there is no available exemption permitting public sale.

[545] Reg. §1.664-3(a)(1)(i)(d).

[546] Reg. §1.664-3(a)(1)(i)(c)(3).

[547] Reg. §1.664-3(a)(1)(i)(c).

[548] Reg. §1.664-3(a)(1)(i)(b)(3), §1.664-3(a)(1)(i)(b)(4), T.D. 8791, 63 Fed. Reg. 68,188 (Dec. 10, 1998), effective for sales or exchanges occurring after April 18, 1997, and further *amended by* T.D. 9102, 69 Fed. Reg. 12 (Jan. 2, 2004) (finalizing REG-106513-00, 66 Fed. Reg. 10,396 (Feb. 15, 2001)), effective for taxable years ending after January 2, 2004.

[549] Reg. §1.664-3(a)(1)(i)(b)(3), §1.664-3(a)(1)(i)(b)(4).

[550] Under Reg. §1.664-3(a)(1)(i)(b)(4), this provision is effective for taxable years ending after January 2, 2004. The 1998 final regulations had implied that the IRS would permit post-contribution gains to be allocated to income because those regulations only prohibited the allocation of pre-contribution gains to income.

[551] See 852 T.M., *Income Taxation of Trusts and Estates*, for a further discussion of the 2004 amendments to Reg. §1.643(b)-1.

[552] *See, e.g.*, PLR 9633013–9633007, PLR 9609009, PLR 9511029, PLR 9511007, PLR 9442017.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

or years, the fair market value of the trust assets be reduced by the amount of that deficiency for purposes of determining the unitrust payment. The reduction, however, could not exceed the amount of unrealized gain in the trust assets as of the valuation date. It is likely that the IRS imposed this requirement as a condition of obtaining a favorable ruling. This adjustment to the value of the unitrust could result in a significant reduction in the amount of the payment due to the noncharitable beneficiary.

Although practitioners had expressed concern that the 1998 final regulations might require the maintenance of a liability account for net income with make-up unitrusts that allocate post-contribution gain to income, the preamble to the final regulations states that taxpayers "do not have to treat the make-up amount as a liability when valuing the assets of a NIMCRUT."[553] However, many NIMCRUTs drafted before 1998 did include that provision in their document. If the document was not amended to delete that provision, the adjustment would still be required.[554]

> *Example (pre-1998 NIMCRUT with the deficiency provision):* Grantor funded a CRUT on January 1, 1994, retaining an 8% unitrust interest for life, payable on December 31 (the valuation date). The trust has net income with make-up provisions and includes realized capital gains in the definition of trust income. Grantor funded the trust with assets with a value of $100,000 and basis of $50,000. In 1994 and 1995, when the trust assets had a value of $100,000, the trust had no income, and no unitrust payments were made. In 1996, the trust realized its only income for the year when the trust assets were sold for $100,000, resulting in a $50,000 capital gain. On December 31, 1996, the trust made a $23,360 unitrust payment to Grantor. This payment represents an $8,000 make-up payment for 1994 (when the trust assets were valued at $100,000), a $7,360 make-up payment for 1995 (when the value of the trust assets was reduced to $92,000 to reflect the $8,000 unitrust deficit), and an $8,000 payment for 1996 (when the post-sale assets were valued at $100,000).

5. Correction of Over- or Under-Payment to the Noncharitable Beneficiary

The governing instrument must contain a provision addressing the possibility of an incorrect valuation of the net fair market value of the trust assets.[555] If the trustee incorrectly determines the net fair market value of the trust assets and the payment amount is expressed as a fraction or a percentage of the net fair market value of the trust property, the error in valuation will affect the amount payable to the recipient. For a discussion of the rules applicable to trustees and the obtaining of qualified appraisals, see III.G.1., above. Where this occurs, the trustee must pay to the beneficiary (in the case of an undervaluation) or be repaid by the beneficiary (in the case of an overvaluation) an amount equal to the difference between the amount the trustee paid the beneficiary and the correct payment amount. The payments or repayments must be made within a reasonable period after the final determination of the value of the trust assets.[556] Any payments due to a recipient by reason of an incorrect valuation are includible in the recipient's income in his or her tax year in which or with which ends the taxable year of the trust in which the overpayment is paid, credited, or required to be paid.[557] Where a recipient is required to make payments to the trust, the recipient is entitled to a deduction from gross income in the year the repayment is made, but only to the extent the amounts originally paid were included in the recipient's gross income.[558] It is possible that the §1341 claim-of-right rules would apply where the amount of the deduction is substantial.[559]

Practice Point: The regulations only discuss an over- or under-payment in the context of an incorrect valuation of the assets. As a practical matter, over- or under-payments for any other reason should be handled in the same manner. If the adjustment is substantial, especially if the beneficiary has been overpaid, the trustee may decide that it is appropriate to disclose the reason for the adjustment in an attachment to the annual income tax return for the trust.

Practice Point: It is not unusual for an institutional trustee to make a payment, only to discover that the income beneficiary has died and the trustee has not been notified. If there is a successor noncharitable beneficiary, and the check was not cashed, a corrected check (or checks) can be issued. However, if the trust was to terminate on the death of the beneficiary, an adjustment, including repayment by the estate of the beneficiary (assuming the executor deposited the check), may be required. If an erroneous payment is refunded by the estate of the noncharitable beneficiary, the estate may benefit from the §1341 claim-of-right rules as a successor to the noncharitable beneficiary.[560]

6. Computation of Annuity or Unitrust Amount for Short Taxable Years Including Last Taxable Year of Payment Period

The governing instrument of an annuity trust or unitrust must provide that in the case of a short taxable year other than the final year, the annuity or unitrust amount otherwise payable will be prorated for the actual number of days in the short taxable year.[561]

> *Example:* The annuity payment of charitable annuity trust T is $5,000 per year to individual B for life. T is funded on July 1, and, as required, the trustee adopts a calendar year. The annuity amount payable to B for the initial year

[553] T.D. 8791, 63 Fed. Reg. 68,188 (Dec. 10, 1998).

[554] In PLR 200827013, PLR 200827012, and PLR 200827011, the IRS ruled that the reformation of net income with make-up unitrusts to conform them to Reg. §1.664-3(a)(1)(i)(b)(3) as promulgated after the unitrusts' establishment did not disqualify the unitrusts under §664. Otherwise, as reformed, all capital gain realized by the unitrusts was to be allocated to income. *See also* PLR 201332012, PLR 201332011 (similar reformation did not disqualify unitrusts under §664 or result in §4941 self-dealing), PLR 200829016, PLR 200829015.

[555] Reg. §1.664-2(a)(1)(iii), §1.664-3(a)(1)(iii).

[556] Reg. §1.664-2(a)(1)(iii), §1.664-3(a)(1)(iii).

[557] Reg. §1.664-1(d)(4)(ii).

[558] Reg. §1.664-1(d)(4)(ii).

[559] Reg. §1.664-1(d)(4)(ii).

[560] See 502 T.M., *Gross Income: Tax Benefit, Claim of Right and Assignment of Income*, for discussion of §1341.

[561] Reg. §1.664-2(a)(1)(iv)*(a)*, §1.664-3(a)(1)(v)*(a)*.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

of funding is $5,000 × 184 (the number of days in the short taxable year beginning July 1) ÷ 365 (the number of days in a full taxable year) = $2,520.55.

The final year of the trust often will be a short taxable year, and the final payment to the noncharitable beneficiary is prorated in the manner shown above, unless the document terminates the payments with the payment preceding the death of the beneficiary. In the case of a CRT measured by an individual's life, any required prorated payment for the year in which the trust ends is based on the number of days the beneficiary lived in the taxable year of his or her death and not on the number of days in the last taxable year.[562] The latter generally is greater, because the taxable year will run until the assets are distributed to the charitable remainder beneficiary. If the governing instrument of a unitrust provides for the payment of the lesser of net income or a specified percentage of trust corpus, the amount payable for the last taxable year is determined by comparing the actual income for the last year to the prorated fixed percentage amount for the period.[563] In the case of a unitrust, if the annual valuation date does not occur in the final short year, the trust assets are valued as of the last day of the short year.[564] If the beneficiary is entitled to a prorated amount for the beneficiary's year of death, with the result that payment is made after the death of the beneficiary, the payment amount is included in the income of the beneficiary's estate as income in respect of a decedent.[565]

The governing instrument may provide that the annuity or unitrust payments terminate with the payment preceding the death of the recipient.[566] If the document includes that provision, any accidental post-mortem payment must be returned or repaid in full. This is an optional provision and is not required. However, the IRS takes the position that a trust cannot qualify as a CRT where the governing instrument fails to specify how the amount of the final payment to the beneficiary is to be determined.[567]

7. Requirement for Annual Valuation of Non-Marketable Assets

A unitrust requires an annual valuation of the trust assets to determine the amount of the unitrust payment. Because of continuing fears that the valuation of unmarketable assets could be manipulated to the advantage of the noncharitable beneficiaries, the IRS in 1997 proposed a regulation that would require certain charitable remainder trusts to obtain a qualified appraisal of "unmarketable" trust assets for purposes of determining the annuity or unitrust amount.[568] The regulation was finalized in substantially the same form in 1998, and is effective for trusts created on or after December 19, 1998.[569]

The final regulation, Reg. §1.664-1(a)(7), applies to both annuity trusts and unitrusts and requires that any valuation of unmarketable trust assets either be made by an independent trustee or be determined by a current qualified appraisal.[570] For this purpose, an "independent trustee" is defined as a person who is not the grantor, a noncharitable beneficiary, or a person who is subordinate or related to the grantor, the grantor's spouse, or a noncharitable beneficiary.[571] "Unmarketable assets" are defined as those that are not cash, cash equivalents, or other assets that can be readily converted into cash. The regulation lists real estate, closely held stock, and unregistered securities as examples of unmarketable assets.[572]

In the case of an annuity trust, a valuation is generally required only at the time the assets are transferred to the trust. That initial valuation fixes the amount of the annuity, which does not thereafter change. Because the transfer of assets other than cash or publicly traded stock will require a qualified appraisal under Reg. §1.170A-17(a),[573] that same appraisal can be used to fulfill the appraisal requirements of Reg. §1.664-1(a)(7) if there is no independent trustee.

In the case of a unitrust, the valuation requirement will have to be satisfied each time the trustee makes its annual valuation of the trust assets, although the initial qualified appraisal to support the income tax deduction can be used for the first valuation date (assuming the first valuation date is the date the on which the trust is funded).

B. Making the Payments to the Beneficiary

No amount other than the annuity or unitrust amount can be paid to a person other than a §170(c) organization.[574] This restriction does not prohibit the trust from making a transfer to a person other than a §170(c) organization in exchange for full and adequate consideration, as long as it is permissible within the self-dealing rules discussed at VI.G., below.[575] Therefore, if the donor is the trustee, he or she may receive a trustee's fee as long as it is reasonable. See the discussion at IV.G.1., above.

1. In Cash

In virtually all cases, the required payments to the noncharitable beneficiary will be made in cash. This does not normally raise any complications. The taxation of the payment received is discussed in VI.F., below.

[562] Reg. §1.664-2(a)(1)(iv)*(b)*, §1.664-3(a)(1)(v)*(b)(1)(i)*.
[563] Reg. §1.664-3(a)(1)(v)*(b)(1)(ii)*.
[564] Reg. §1.664-3(a)(1)(v)*(b)(1)(iii)*.
[565] Reg. 1.664-1(d)(4)(iii).
[566] Reg. §1.664-2(a)(5)(i), §1.664-3(a)(5)(i).
[567] Rev. Rul. 79-428.
[568] REG-209823-96, 62 Fed. Reg. 19,072 (Apr. 18, 1997).
[569] T.D. 8791, 63 Fed. Reg. 68,188 (Dec. 10, 1998). If a trust in existence on December 10, 1998, requires that an independent trustee value unmarketable assets, the trust can be amended to provide that the valuation may be made either by an independent trustee or by a qualified appraisal. Reg. §1.664-1(f)(4).

[570] For this purpose, a qualified appraisal is defined in Reg. §1.170A-17(a), generally applicable for charitable contributions made on or after January 1, 2019. Reg. §1.664-1(a)(7)(i)(b). See also Reg. §1.170A-13(c)(3) and Notice 2006-96 for charitable contributions made prior to January 1, 2019.
[571] Reg. §1.664-1(a)(7)(iii). The determination of whether a person is subordinate or related is made under §672(c) and its regulations. Reg. §1.664-1(a)(7)(iii). In the preamble to the final regulation, the IRS stated that an independent trustee who is a co-trustee may value the unmarketable assets. T.D. 8791.
[572] Reg. §1.664-1(a)(7)(ii).
[573] Reg. §1.170A-17(a), *added by* T.D. 9836, 83 Fed. Reg. 36,417 (July 30, 2018), applicable to charitable contributions made on or after January 1, 2019. However, the rules may be applied to appraisals prepared for returns or submissions filed after August 17, 2006. See also Reg. §1.170A-13(c)(3) for returns or submissions applicable to donations made before January 1, 2019.
[574] §664(d)(1)(B), §664(d)(2)(B); Reg. §1.664-2(a)(4), §1.664-3(a)(4).
[575] Reg. §1.664-2(a)(4), §1.664-3(a)(4).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

2. Payments in Kind

The distribution of the annuity or unitrust amount may be made in property other than cash.[576] Perhaps the asset to be distributed is illiquid, or the trustee decides not to incur the sales costs if the beneficiary plans to hold the property. The tax consequences to the noncharitable beneficiary are the same as if the payment were received in cash.

From the trust's perspective, a distribution in kind is deemed to be a sale of the property by the trust. The recipient's basis in the property is its fair market value at the date the property is paid, credited, or required to be distributed by the trust.[577] The trust will realize gain or loss to the extent that the then fair market value of the property distributed differs from the trust's basis in the property. The trust cannot recognize any loss, as the deemed sale is a transaction with a beneficiary and, thus, subject to the loss limitations and deferral provisions of §267.[578]

> *Example:* On January 1, 20X1, X creates a qualifying CRAT, whose taxable year is the calendar year, under which X is to receive $5,000 per year. During 20X1, the trust receives $500 of ordinary income. On December 31, 20X1, the trust distributed cash of $500 and a capital asset of the trust having a fair market value of $4,500 and a basis of $2,200. The trust is deemed to have realized a capital gain of $2,300. X is required to recognize the distribution of $5,000 as being ordinary income of $500, capital gain of $2,300 and trust corpus of $2,200. The basis of the distributed property is $4,500 in the hands of X. See example under Reg. §1.664-1(d)(5).

Practice Point: If possible, distribution of loss property should be avoided due to the complexity of the loss deferral provisions.

The beneficiary's holding period begins the day after the property is received.[579] He or she is not entitled to add the trust's holding period because the trust's basis does not carry over to the beneficiary.[580]

> *Example:* On January 1, 20X1, G creates a qualifying CRAT. As required of all split-interest trusts, the annuity trust is on a calendar year. G is entitled to receive $5,000 per year. During 20X1, the trust receives $500 of ordinary income. On December 31, 20X1, the trust distributes cash of $500 and a capital asset having a fair market value of $4,500 and a basis of $2,200. As a result of this distribution in kind, the trust is deemed to have realized a capital gain of $2,300. G's $5,000 distribution is deemed to consist of $500 of ordinary income, $2,300 of capital gain, and $2,200 of nontaxable corpus. G's basis in the distributed property is $4,500.[581]

If an in-kind distribution is made in the year following the year for which the payment is made, see the discussion at VI.F.3., below. The gain on the distribution may be allocated to the year for which the payment is made rather than the year in which the payment is actually made.

C. Taxation of Trust

1. Assigning Income to Categories and Classes

The income tax character of distributions to the recipient is determined under a unique "category" and "class" system under the rules set forth in §664(b) and the regulations thereunder. This system supersedes all other provisions of the Code.[582] Many previous discussions refer to the "four tier system," which is perhaps a better descriptive term, but to avoid confusion this narrative will use the terms from the regulations. When the system was originally designed, the basic idea was that the highest-taxed income would be distributed first, then the lower-taxed income (i.e., capital gains), and then finally the non-taxable income (the "worst-in, first-out" or WIFO system). However, the creation of special tax rates for certain types of ordinary income (e.g., qualified dividends) and the addition of the net investment income tax mean that WIFO is no longer strictly followed.

The first step in determining the taxation of the beneficiary is to assign the income of the trust to the appropriate category and class. Once assigned, the income remains in that category and class permanently until it is distributed to the beneficiary or the trust terminates. Unlike other trusts, the income calculation does not start anew each year. The Form 5227, *Split-Interest Trust Information Return*, shows the categories' cumulative balances but does not detail the classes of income within each category. Therefore, the trustee must keep separate records to be able to accurately file the tax return and determine the correct income to allocate to the beneficiaries. The beneficiaries' tax consequences are discussed at VI.F., below.

The beneficiary is taxed based on his or her rates for the year in which the distributions are made to the beneficiary, not the year in which the income is received by the trust.[583]

Reg. §1.664-1(d)(1)(i)*(a)* assigns all CRT income to either the ordinary income category, the capital gains category, or the other income (e.g., tax-exempt) category in the year the trust must take the income into account. (The fourth category is "corpus," but no income can be allocated there.) Income includes non-cash items such as consent dividends, subpart F income, or Global Intangible Low-Taxed Income under §951A, even when these items of income are not treated as income under §643(b) for distribution purposes.[584]

Reg. §1.664-1(d)(1)(i)*(b)* specifies that all items within the ordinary income and capital gains categories are then assigned to different classes based on the federal income tax rate applicable to each type of income in that category in the year the trust must take the item into account. The ordinary income category could include a class of §1(h)(11) qualified dividend income, a class of income not subject to the net investment income tax

[576] Reg. §1.664-1(d)(5). *See* PLR 8846058.

[577] *Kenan v. Commissioner*, 114 F.2d 217 (2d Cir. 1940), *aff'g* 40 B.T.A. 824 (1939).

[578] §267(b)(6); Reg. §1.267(d)-1.

[579] *See* Rev. Rul. 70-598.

[580] §1223(1); Reg. §1.267(d)-1(a)(4) *Ex.* 1.

[581] Reg. §1.664-1(d)(5) *Ex.*

[582] §664(b); Reg. §1.664-1(d)(1).

[583] Reg. §1.664-1(d)(1)(ii)(*a*). See also the discussion of §1411 at VI.F.4., below.

[584] PLR 199952035.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

under §1411,[585] and a class of all other ordinary income.[586] The capital gains category could include separate classes for short-term capital gains, for §1(h)(4) 28% long-term capital gains, for §1(h)(6) unrecaptured §1250 long-term capital gains, for former §1(h)(9) (before its amendment by JGTRRA) qualified five-year long-term capital gains, and for all other long-term capital gains. If the tax rates change so that items in two classes would be taxed at the same rate if distributed in a particular year, and the change is permanent, then the undistributed items in those classes are combined into one class.[587] Typically the "other income" category would include only tax-exempt interest or dividends, but could also include life insurance proceeds.

Comment: The IRS issued proposed regulations that would define certain CRAT transactions, such as the type of transaction in *Furrer*, as listed transactions.[588] The IRS would define use of a charitable remainder annuity trust as a listed transaction if: (1) the grantor creates a CRAT and funds the trust with property having a fair market value in excess of its basis; (2) the trustee sells the contributed property and uses some or all of the proceeds from the sale to purchase an annuity; and (3) on a federal income tax return, the beneficiary of the trust treats the annuity amount payable from the trust as if it were, in whole or in part, an annuity payment subject to §72, instead of carrying out to the beneficiary amounts in the ordinary income and capital gain tiers of the trust in accordance with §664(b).[589] The preamble to the proposed regulations also walked through the serious deviations from the IRS's approved CRAT samples, which cause these certain types of CRATs from qualifying as CRATs, such as providing for a current payment to a charitable organization in lieu of payment of the remainder interest required under §664(d)(1)(C). Note that charitable remainder beneficiaries would not be treated as participating in a listed transaction or as a material advisor to a listed transaction solely by reason of being a recipient of a remainder interest; however, the charitable remainder beneficiary could be subject to penalties under Reg. §53.4965-4(a) depending upon its knowledge of the transaction.[590]

If the trust receives any non-UBTI income that could be subject to the deduction allowed under §199A, that income does not appear to be a separate class of income from other ordinary income (such as interest income). Although a deduction may be allowed to the beneficiary on his or her own return, §199A income is not subject to a different income tax rate. Therefore, §199A-eligible income would be included in the ordinary income category along with other income that might receive special treatment on the beneficiary's return, such as passive income or foreign-source (nonqualified) dividends.[591] As with all other income that could receive different treatment, the trustee should provide sufficient detail to the beneficiary. Direct guidance from the IRS would be helpful.

Under Reg. §1.664-1(d)(1)(iii)*(a)*, ordinary losses in the current year are used first to reduce undistributed ordinary income for prior years that is in the same class as the loss. Any excess is then used to reduce current and undistributed ordinary income from other classes, in turn, beginning with the class subject to the highest federal income tax rate and ending with the class subject to the lowest rate. If any further excess remains, it is carried forward indefinitely to reduce ordinary income in future years. As noted above, current and prior years' undistributed income for this purpose is calculated without regard to the §172 or §642(d) net operating loss deduction.

If there is a current-year loss in the other income category, Reg. §1.664-1(d)(1)(iii)*(b)* provides that it is used to reduce undistributed income in this category for prior years. Any excess is carried forward indefinitely to reduce other income in future years.

Reg. §1.664-1(d)(1)(iv) describes how capital gains and losses are netted. The capital gains are determined on a cumulative net basis under Reg. §1.664-1(d)(1) without regard to §1212.[592] Each year, current and undistributed gains and losses within each class are netted to determine the net gain or loss for that class. The classes of capital gains and losses are then netted against each other in the following order: (i) a net loss from the long-term capital gain and loss class (beginning with the class subject to the highest federal rate and ending with the class subject to the lowest rate) offsets net gain from each other class of long-term capital gain and loss, in turn, until exhaustion of the class, beginning with the class subject to the highest federal rate and ending with the class subject to the lowest rate; and (ii) either (a) a net loss from all the classes of long-term capital gain

[585] See VI.F.4., below, discussing the application of the §664(b) rules to the determination of whether items of income allocated to a noncharitable annuity or unitrust recipient constitute §1411 net investment income to him or her.

[586] Other ordinary income includes the ordinary income portion of payments from annuity policies. Although the amount of ordinary income and return of principal is calculated under §72, the annuity income portion is assigned to the "ordinary income subject to §1411" class once received by the CRT. *See* IRS AM 2020-006; *Furrer v. Commission*, T.C. Memo 2022-100 (when analyzing interplay of §72 and §664 regarding annuity payments from single premium immediate annuities (SPIAs) purchased by CRATs in abusive transactions similar to those discussed in IRS AM 2020-006, court stated that §72 does not call for treatment different than under §664; rather, "[§]72(b) allows an exclusion from income only to the extent the taxpayer has an 'investment in the contract,'" and neither taxpayers nor CRATs had any investment in SPIAs because SPIAs were purchased with proceeds from sale of agricultural crops that had basis of zero). *See also Gerhardt v. Commissioner*, No. 11127-20, 2023 BL 134075 (T.C. Apr. 20, 2023) (court reiterated that "nothing in [§]72 overrides [the income beneficiaries' obligation to comply with the rules of [§]664(b) with respect to [the annuity income]"; court rejected income beneficiaries' argument that "all taxable gains (on the sale of the asset[s contributed to the CRATs]) disappear and the full amount of the proceeds [from the sale of real property by the CRAT is] converted to principal to be invested by the CRAT … . The gain disappearing act the Gerhardts attribute to the CRAT is worthy of a Penn and Teller magic show").

[587] If the rate change is temporary (such as where a sunset applies), Reg. §1.664-1(d)(1)(i)(b) specifies that the classes are kept separate. The preamble to the final regulations on ordering rules for characterizing distributions from CRTs notes that no commentators indicated that this requirement would be unduly burdensome. T.D. 9190, 70 Fed. Reg. 12,793 (Mar. 16, 2005).

[588] Prop. Reg. §1.6011-15, REG-108761-22, 89 Fed. Reg. 20,569 (Mar. 25, 2024), would be effective on the date of publication of final regulations.

[589] Prop. Reg. §1.6011-15(b). *See also* Preamble, REG-108761-22 (in these transactions, beneficiaries report as income only small portion of the amount received from SPIA, treats balance of annuity amount as excluded portion representing return of investment, and beneficiary is taxed as if owner of SPIA, rather than SPIA being asset owned by CRAT, which trustee purchased to fund annuity amount payable from trust; furthermore, trustee takes position that transfer of appreciated property to purported CRAT gives assets step-up in basis to fair market value as if such assets were sold to trust, rather than proper treatment of having assets retain same basis as in hands of donor, increased by any gift tax paid on transfer).

[590] Prop. Reg. §1.6011-15(c), §1.6011-15(d). *See also* Reg. §1.6011-4(c)(3)(i)(A).

[591] See the discussion of PLR 9313018 at VI.C.2.d., below.

[592] Section 1212 is the capital loss carryover and carryback provision.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

and loss (beginning with the class subject to the highest federal rate and ending with the class subject to the lowest rate) offsets any net gain from the short-term capital gain and loss class or (b) a net loss from the short-term capital gain and loss class offsets net gain from each long-term capital gain and loss class, in turn, until exhaustion of the class, beginning with the class subject to the highest federal rate and ending with the class subject to the lowest rate.

If a CRT has a net loss or net gain at the end of the taxable year after the application of Reg. §1.664-1(d)(1)(iv) and the gain or loss is not treated as distributed from the capital gains category under the Reg. §1.664-1(d)(1)(ii)*(a)* allocation provisions, then Reg. §1.664-1(d)(1)(v) provides that such net gain or loss is carried forward to succeeding taxable years. It retains its character as gain or loss from its particular class in the succeeding years.

In addition to income actually received by the trust during the year, gain assigned to the capital gains category may include deemed gains from the following year. Under Reg. §1.643(a)-8,[593] the trust will be deemed to have sold a pro rata portion of the appreciated assets in any year that the trust must make a distribution and the distribution is not characterized in the hands of the recipient as income from the categories described in §664(b)(1), §664(b)(2), or §664(b)(3). As a result, the trust will have income, and the beneficiary must recognize the income upon receiving a distribution. Of course, the income is not recognized again in the following year.

> *Example:* In 20X1, H funds a CRAT using an appreciated non-dividend paying stock. The trustee sells some of the stock early in 20X2 to make the required payment to the beneficiary. If it were not for the Reg. §1.643(a)-8 special rule, the beneficiary would not be taxed on the distribution for 20X1 because the trust would not have accumulated any income in the year for which the distribution was made. The gain on the sale of the stock is allocated to the capital gain category in 20X1, not 20X2.

Reg. §1.664-1(d)(1)(vi) contains transitional rules that may affect the calculation of classes and categories for trusts established in 2003 or earlier.[594] Reg. §1.664-1(d)(1)(viii) includes detailed examples of how the Reg. §1.664-1(d)(1) rules apply.

2. *Allocating Expenses to Categories*

a. *General Cash Expenses*

The next step in determining the income allocable to the noncharitable beneficiary is to allocate any expenses among the categories. The trust is permitted certain deductions in calculating the annual amount of income and corpus in each category. However, the permissible deductions do not include several deductions ordinarily available to trusts. The nonallowable deductions include the following: (1) the personal exemption (§642(b)); (2) the charitable deduction (§642(c)); and (3) the distributions deduction (§661).[595]

Deductions that are directly attributable to one or more classes of items within a category are allocated to the items to which they are attributable (e.g., rental expenses are allocated to rental income).[596] All other deductions are allocated among the items in a given category in the proportion that the gross income of each class of items included in the category, reduced by the deductions attributed to that class under the first allocation, bears to all income in the category.[597] However, the allocation cannot create or increase a net loss within a class. Any deductions that are not allocable under either of the first two provisions can be allocated in any manner.[598]

Practice Point: The trustee must keep in mind that the allocation of tax preference items may result in alternative minimum tax liability for the recipient of the annuity or unitrust amount.

All taxes imposed on the trust as a result of its unrelated business taxable income in any year and any excise taxes imposed pursuant to §4940–§4945 (the excise taxes on private foundations) are allocated to corpus.[599] The regulations also provide that any expense not deductible in determining taxable income and not allocable to any class of items in the "other income" category is allocated to corpus.[600]

Although guidance can be found in the regulations concerning the allocation of deductions in the case of taxable trusts, and those rules contain a similar provision for the allocation of deductions directly attributable to a class of income items, application of such rules in the §664 context is not clearly provided.[601] For example, the regulations governing taxable trusts state that the trustee's commissions are considered not directly allocable to a specific class of income.[602] For the purposes of §664, however, it is unclear whether this expense is directly allocable to corpus.[603]

[593] Reg. §1.664-1(d)(1)(vii) provides for the application of Reg. §1.643(a)-8 (related to the application of the §643(a)(7) anti-abuse rule) to CRT distributions. The regulation applies to distributions made by a CRT after October 18, 1999.

[594] Reg. §1.664-1(d)(1)(iv) indicates that the class of "all other" long-term capital gain or loss includes long-term capital gain or loss that the trust properly takes into account: (i) before 1997; (ii) on or after January 1, 1997, and before May 7, 1997, if not treated as distributed in 1997; and (iii) on or after January 1, 2003, and before May 6, 2003, if not treated as distributed during 2003 (other than 28% rate gain as defined in §1(h)(4), unrecaptured §1250 gain as defined in §1(h)(6), and qualified five-year gain as defined in former §1(h)(9), before its amendment by JGTRRA). Reg. §1.664-1(d)(1)(vi) contains additional transitional rules, including a provision stating that qualified five-year gain that the trust properly takes into account after 2000 and before May 6, 2003, if not treated as distributed in 2003 or a prior year, is maintained in a separate class within the capital gains category.

[595] Reg. §1.664-1(d)(2).

[596] Reg. §1.664-1(d)(2).

[597] Reg. §1.664-1(d)(2).

[598] Reg. §1.664-1(d)(2).

[599] *See* Reg. §1.664-1(c)(1), §1.664-1(d)(2).

[600] Reg. §1.664-1(d)(2).

[601] *See* Reg. §1.652(b)-3.

[602] Reg. §1.652(b)-3(c).

[603] For CRTs under pre-Tax Reform Act of 1969 (1969 Act), Pub. L. No. 91-172, §201(e), which added §664, effective for transfers in trust made after July 31, 1969, income commissions generally were charged to income, while principal commissions were charged to principal. This type of allocation is now irrelevant for qualified remainder trusts, because the distinction between income and principal is eliminated for post-1969 Act trusts (except for unitrusts that provide for distribution of the lesser of the unitrust amount or the trust accounting income).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

b. Depreciation

As a matter of policy, the IRS requires CRTs (or at least NICRUTs) to establish a depreciation reserve if trustees invest in depreciable property, although the IRS has not formally ruled on the subject. Rev. Rul. 90-103 provides that the governing instrument of a pooled income fund must require the creation of a depreciation reserve pursuant to generally accepted accounting principles if the trustee has the authority to accept or invest in, or is not specifically prohibited from accepting or investing in, depreciable or depletable property. The IRS, in private letter rulings (discussed below), has applied similar principles to CRTs.

Generally, when a CRT invests in depreciable property, the depreciation deductions are allocable under Reg. §1.167(h)-1(b) among the trust and its beneficiaries in proportion to their respective shares of trust accounting income. It is the position of the IRS that, at least in the case of a net income unitrust, a depreciation reserve is important to insure that the principal ultimately passing to the charity reflects the amount the grantor was entitled to claim as a deduction at the time of funding the trust. The depreciation reserve must be based on generally accepted accounting principles, using actual economic depreciation rather than tax depreciation (which may be greater), and the trust must annually set aside and add to principal a portion of the trust income that reflects the depreciation in the value of the trust property.

Since 1986 the IRS has privately ruled that noncharitable beneficiaries of CRTs are entitled to depreciation deductions[604] where the trust invests in depreciable property.[605] In PLR 8931023, the IRS ruled that a unitrust that paid its beneficiaries a stated percentage, which was not limited to the net income, was not required to maintain a reserve. A possible explanation for this discrepancy is that the IRS perceives that the need for a reserve does not exist in the case of a regular unitrust because trust distributions have no relationship to trust income as defined by fiduciary accounting principles. On the other hand, as long as trust income exceeds the unitrust percentage, a net income unitrust may pay out the unitrust amount without regard to the net income limitation.

Comment: In the absence of a clear statement from the IRS, drafters should pay particular attention to Rev. Rul. 90-103 when considering the creation of a net income unitrust that may invest in depreciable property. Rev. Rul. 90-103 not only requires a depreciation reserve, but also one that must be maintained in accordance with generally accepted accounting principles. Again, the IRS has not expressly imposed this requirement on CRTs, but this ruling is a good indication of IRS views on the subject.

A special rule applies where the charitable remainder beneficiary is controlled by the annuity or unitrust recipient (including in conjunction with related parties) within the meaning of §267(b)(9). In such case, the trustee may not allocate any portion of the depreciation deduction to the recipient.[606] This provision would apply if the remainder beneficiary is a private foundation controlled by the annuity or unitrust recipient and his or her family.

c. Deduction for Taxes Paid on Income in Respect of a Decedent

In addition, the regulations do not specifically mention the §691(c)(1)(A) income in respect of a decedent (IRD) deduction. In PLR 199901023, the IRS illustrated the impact of §691(c) where a CRUT received IRD as the designated beneficiary of the decedent's qualified retirement plan. Upon receiving the proceeds from the qualified retirement plan, the IRS explained, §691(a)(1)(B) required the trust to include the IRD in gross income. Citing §691(a)(3), the IRS indicated that the ordinary income character of the IRD was retained and that these amounts constituted ordinary income for purposes of §664(b)(1). The IRS stated that the trust was entitled to a deduction for the estate tax attributable to the IRD. Thus, the IRD that constituted ordinary income described in §664(b)(1) was the amount of the IRD net of the deduction provided in §691(c)(1)(A). The IRS specified that the deduction was reported as an "other" deduction on Form 5227, *Split-Interest Trust Information Return*, and was not directly made available to the trust's income beneficiaries under §664(b). The deduction would be allocated to the ordinary income category, reducing the amount of accumulated income that could be distributed to the beneficiaries. However, unless the full amount of the category was distributed through the life of the trust, the deduction might prove of little benefit to the beneficiaries.

d. Credits

Although the §664 regulations discuss the effect of certain deductions, they are silent regarding the effect of credits, such as the foreign tax credit. Beneficiaries would want any available credit allocated entirely to the recipient of the annuity or unitrust amount, because the charitable remainder trust has no tax against which a credit can be used.[607] The questions remain whether the computation should be made initially at the trust level and whether the credit would be deemed to be "distributed" in the same year in which the income to which it relates is distributed.[608]

The only available guidance indicates that the foreign tax credit benefits the annuity or unitrust recipients currently, rather than just reducing the net income in the ordinary income category. In PLR 9313018, a U.S. couple established a CRUT designed to invest in stocks and bonds of foreign corporations that were not controlled foreign corporations. The IRS ruled that, for each taxable year of the CRUT in which the CRUT did not have any unrelated business taxable income, each spouse would be treated as having paid his or her proportionate share of foreign taxes paid or accrued by the CRUT on income that would be treated as distributed to that spouse. Each spouse could, therefore, claim a credit under §901(b)(5) for his or her

[604] *See, e.g.*, PLR 8610067.

[605] *See* PLR 9030042, PLR 9030041, PLR 8931020, PLR 8931019 (requiring trustees to maintain reserve for depreciation).

[606] §167(e), *added by* the Revenue Reconciliation Act of 1989, Pub. L. No. 101-239, §7645, effective for interests created on or acquired after July 27, 1989, in taxable years ending after that date.

[607] As discussed in VI.C.3., below, payment of an excise tax does not create a tax credit distributable to any beneficiary.

[608] *See* Reg. §1.48-6 (allocation of former investment tax credit in case of simple or complex trust), §1.642(a)(2)-1 (allocation of foreign tax credit to trust and its beneficiaries).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

proportionate share of foreign taxes. If a spouse did not elect to take a credit for the foreign taxes previously paid or accrued by the trust that are deemed paid by such spouse, that spouse could deduct such taxes from his or her share of the trust's current and accumulated income that was deemed to be distributed to such spouse during the taxable year.

Practice Point: When preparing the tax return for a CRT with a foreign tax credit, it may be necessary to override the software to show the gross-up of the foreign tax credit being received and then distributed to the beneficiary.

e. Taxes

The only taxes addressed in the §664 regulations are the private foundation taxes, including the taxes on unrelated business taxable income treated under §664(c)(2) as imposed by Chapter 42. As noted above, both categories are allocated to corpus.[609] The rules governing noncharitable trusts provide that state income and personal property taxes are not considered directly attributable to a specific class of income.[610] By analogy such taxes would appear to be allocable to an income category rather than to corpus. This could be relevant for those trusts subject to tax in states that do not treat CRTs as exempt. If a state assesses non-resident state taxes on rental or royalty income, it would seem reasonable to allocate that tax directly against that category and class of income.

3. Effect of Unrelated Business Taxable Income (UBTI)

After 2006, if a charitable remainder trust earns any unrelated business taxable income (UBTI),[611] the trust is subject to a 100% excise tax on that income. The legislative history to the Tax Relief and Health Care Act of 2006 (TRCHA)[612] indicates that the tax is treated as paid from corpus but the UBTI is considered as income of the trust in determining the character of trust distributions to the beneficiaries. (See VI.F.1., below.)[613] Before the TRHCA,[614] a CRT would lose its exemption for any year in which it had UBTI.

Practice Point: If a CRT engages an investment advisor, it is very important to inform the advisor of this penalty tax on an UBTI. The best investment return is worthless if the tax is 100%. Any publicly traded partnership's prospectus should be reviewed for this issue before investing.

Several types of investments can generate UBTI. It is unlikely that a CRT would directly operate a business, but UBTI can be generated in a number of other ways.

Debt-financed income (usually indirectly through a partnership) is the type of income most likely to expose the trust to the tax. If the trust desires leveraged investments, the UBTI exposure can be avoided by investing through offshore blocker corporations.[615]

Certain investments in real estate investment trusts (REITs) and real estate mortgage investment conduits (REMICs) could have triggered UBTI exposure. In Rev. Rul. 2006-58, the IRS ruled that a CRT does not have §860E(b) UBTI if the trust is a shareholder of a REIT or partner in a partnership that has §860E(c) excess inclusion income from holding a residual interest in a REMIC. Thus, the IRS concluded that the §860E(c) excess inclusion income allocated to the CRT did not affect the trust's exemption from tax under pre-TRHCA §664(c). The IRS also determined that a CRT that is a shareholder/partner of a §860E(e)(6)(B) pass-through entity is a §860E(e)(5) disqualified organization for purposes of the §860E(e)(6) tax on pass-through entities. Describing the operation of pre-TRHCA §664(c), the IRS explained that a CRT can never be an organization "subject to the tax imposed by section 511" as referenced in §860E(b) and §860E(e)(5). Although the IRS issued Rev. Rul. 2006-58 before Congress passed the TRHCA, presumably the result would be the same under post-TRHCA §664(c) because, if a tax is imposed on the trust's UBTI under that section, the tax is treated as imposed by chapter 42 (not by §511).[616]

The IRS has ruled privately that short sale obligations are not "debt" for purpose of the debt-financed income rules.[617]

---

[609] Reg. §1.664-1(d)(2), *amended by* T.D. 9403, 73 Fed. Reg. 35,583 (June 24, 2008).

[610] Reg. §1.652(b)-3(c).

[611] For this purpose, "unrelated business taxable income" is defined in §512. §664(c)(2)(A).

[612] Pub. L. No. 109-432, §424.

[613] The excise tax is treated as imposed by chapter 42 for purposes of the Code (other than §4961–§4963). §664(c)(2)(B). Staff of J. Comm. on Tax'n, 109th Cong., Technical Explanation of H.R. 6408, the "Tax Relief and Health Care Act of 2006" 115 (J. Comm. Print 2006). Section 664(c)(2)(C) provides that the references to §4940 in §6212(c)(1) (relating to Tax Court proceedings) are deemed to include references to §664(c).

[614] Pre-TRHCA law is discussed at XI.A.6., below.

[615] *See, e.g.*, PLR 201043041 (CRUT's dividends, subpart F income, and distributive share of income and gains from wholly owned foreign corporation that invested in hedge funds via debt financing was not UBTI because: (1) unitrust did not debt finance its ownership interest in corporation for §512(b)(4) and §514(b) purposes; (2) §512(b)(1) dividend exclusion applied; and (3) corporation's subpart F income was not attributable to insurance income for §512(b)(17) purposes), PLR 200623069 (§512(b)(1) dividend exclusion applied to CRT's share of dividends received from LLC that invested in foreign corporation that in turn invested in foreign partnership because: (1) income foreign corporation passed through to LLC and trust was not insurance related under §512(b)(17); and (2) although foreign partnership incurred debt to acquire investments, LLC and trust did not incur debt per §512(b)(4) to acquire their respective interests in foreign corporation and LLC), PLR 200252096 (CRUT did not realize UBTI from its wholly owned subsidiary's allocable share of partnership income because income constituted dividends under §512(b)(1) and was not debt-financed income under §514; any gain on trust's disposition of its wholly owned subsidiary's stock would be excluded from UBTI under §512(b)(5)), PLR 200251018, PLR 200251017, PLR 200251016 (CRUT that was limited partner did not realize UBTI from partnership because partnership's income from controlled foreign corporation constituted dividends under §512(b)(1) and was not debt-financed income under §514). Note that Global Intangible Low-Taxed Income (GILTI) must be included in a U.S. shareholder's income, including CRTs, but is generally treated in a manner similar to an inclusion of subpart F income resulting in GILTI generally excluded from the calculation of UBTI. *See* Reg. §1.512(b)-1(a)(1), *amended by* T.D. 9933, 85 Fed. Reg. 77,952 (Dec. 2, 2020), applicable to tax years beginning on or after December 2, 2020, but may be applied to tax years beginning after 2017. For more information on unrelated business taxable income, see 462 T.M., *Unrelated Business Income Tax (Sections 511, 512, and 513)*, and 465 T.M., *Debt-Financed Income (Section 514)*.

[616] §664(c)(2)(B).

[617] PLR 201434026, PLR 201434024. In those rulings, a CRT invested in partnerships that took short positions in certain stocks. The IRS ruled that where a CRT takes a short position in stock, the mechanical process by which the short position is taken (i.e., creation by the investor of an obligation by borrowing stock from the investor's broker) does not give rise to acquisition indebtedness pursuant to §514. Therefore, any resulting income from the short sales does not constitute UBTI to the trust. *See also* Rev. Rul. 95-8, *applying Deputy v. du Pont*, 308 U.S. 488 (1940). For more information on debt-financed income, see 465 T.M., *Debt-Financed Income (Section 514)*.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Other potential sources of UBTI are mortgaged property and investments in a partnership or limited liability company that reports any unrelated business taxable income.[618]

In addition, a CRT can be subject to excise tax in a year in which it fails to timely make the required payment to the noncharitable beneficiary,[619] or fails to make a timely payment of real property taxes or assessments, resulting in a lien on trust property.[620]

In 2008, the IRS issued final regulations that reflect the §664(c) amendments made by the TRHCA.[621] Consistent with the statutory language, Reg. §1.664-1(c)(1) provides that, for each taxable year beginning after 2006 in which a CRT has UBTI, the §664(c)(2) excise tax is imposed on the trust in an amount equal to such UBTI.[622] "Unrelated business taxable income" is defined under §512, determined as if §511 through §515 applied to the trust. In the examples provided in Reg. §1.664-1(c)(2), the IRS indicates that the §512(b) modifications, including the §512(b)(12) $1,000 deduction, apply in computing the trust's UBTI. The excise tax is treated as imposed by the chapter 42 private foundation excise tax provisions (other than the §4961 through §4963 abatement provisions). The tax is reported and payable as indicated on the appropriate forms and instructions. A trust reports and pays the excise tax on Form 4720, *Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code*.

Reg. §1.664-1(c)(1) and Reg. §1.664-1(d)(2) provide that the §664(c)(2) excise tax (and any other taxes imposed under chapter 42)[623] are allocated to corpus and, thus, not deductible in determining taxable income distributed to a beneficiary. Reg. §1.664-1(c)(1) specifies that the trust's UBTI constitutes trust income for purposes of determining the character of a distribution made to a beneficiary and that the trust income is allocated among the Reg. §1.664-1(d)(1) categories without regard to whether part of the income is UBTI.

The IRS included two examples of the calculation of the §664(c)(2) excise tax in Reg. §1.664-1(c)(2). Reg. §1.664-1(c)(2) *Ex.* 1 illustrates a CRAT with ordinary income that includes UBTI from a partnership. Reg. §1.664-1(c)(2) *Ex.* 2 illustrates a CRAT with capital gains (from the sale of real estate) that include §514 debt-financed income.

> *Example (prior rules):* In 2006, a CRT has $2,000 of ordinary income, of which $1,500 is UBTI. The trust is required to pay $700 to a noncharitable recipient. The trust is not exempt from tax because it has unrelated business taxable income for the year. Consequently, the trust is treated as a complex trust. Pursuant to §661(a), the trust is allowed a $700 distribution deduction and a $100 deduction for its personal exemption. The trust has no other deductions. Thus, the taxable income of the trust for the year is $1,200 ($2,000 of taxable income less the sum of the $700 distributions deduction and the $100 personal exemption).[624] By contrast, if these facts occurred in a taxable year beginning after 2006, post-TRHCA §664(c) would apply and the trust would not be subject to income tax but would instead pay a $500 excise tax under chapter 42.[625]

4. *Effect of Charitable Distributions Before Trust Termination*

If the trust makes a distribution to a §170(c) organization, other than a distribution of a portion of the annuity or unitrust amount, the distribution is considered as being made out of the categories discussed above, but the order of distribution is in the reverse of that prescribed for distributions to noncharitable beneficiaries.[626] Thus, any distribution other than of the annuity or unitrust amount to a §170(c) organization is attributed to corpus. If corpus is exhausted, the amount is considered paid out of "other income," capital gains, and ordinary income, in that order. The effect is that distributions to §170(c) organizations will not deplete the ordinary income category unless all other categories are exhausted. This rule, which only applies to distributions of amounts other than the annuity or unitrust amount, insures that the noncharitable beneficiary cannot benefit from such distributions. Where a §170(c) organization receives a portion of the annuity or unitrust amount, the class and category rules discussed at VI.C.1., above, are applicable.[627] See IV.E.6., above, for a discussion of the payment of the annuity or unitrust amount to charity. If the trust is divided to transfer a portion of the whole trust to charity, see the discussion of at VII.B., below.

Practice Point: If the income beneficiary wants to accelerate only a small portion of the charitable remainder, a cash or property distribution charged to trust corpus is probably the most efficient solution, although there is no immediate tax benefit to the income beneficiary/donor. If he or she desires to donate a larger portion of the trust, consider dividing the trust and donating the desired fraction, which will allow an income tax deduction (unless the charitable donee is a private foundation).

The character of the amounts distributed to a §170(c) organization is determined at the end of the taxable year of the trust in which the distribution is made, after the determination of the

---

[618] §514(c)(2)(A). There is an exception for a mortgage on property transferred to a trust where the mortgage was placed on the property more than five years before the inter vivos transfer to the trust and the donor owned the property more than five years before the transfer. §514(c)(2)(B). In such case, the trust will not be deemed to have "acquisition indebtedness" for the 10 years following the transfer. This exception only applies to inter vivos transfers. For more information on debt-financed income, see 465 T.M., *Debt-Financed Income (Section 514)*.

[619] Reg. §1.664-2(a)(1)(i)*(a)*, §1.664-3(a)(1)(i)*(a)*, §1.664-3(a)(1)(i)*(g)*, §1.664-3(a)(1)(i)*(h)*.

[620] §514(c)(2)(C). The lien is treated as debt, and the trust will have debt-financed income.

[621] T.D. 9403, 73 Fed. Reg. 35,583 (June 24, 2008). The regulations apply to taxable years beginning after 2006. Reg. §1.664-1(c)(3). The IRS declined to provide transitional relief in the final regulations, noting that, although the TRHCA amendments to §664(c) were designed to alleviate the severity of the loss of tax-exempt status when a CRT has UBTI, the amendments "did not reflect any change in the long-standing policy to sanction and thus to discourage such investment by charitable remainder trusts." T.D. 9403 (preamble).

[622] *See also* Reg. §1.664-1(a)(1)(i).

[623] The excise tax is treated as imposed by chapter 42 for purposes of the Code (other than §4961–§4963). §664(c)(2)(B). Staff of J. Comm. on Tax'n, 109th Cong., Technical Explanation of H.R. 6408, the "Tax Relief and Health Care Act of 2006" 115 (J. Comm. Print 2006). Section 664(c)(2)(C) provides that the references to §4940 in §6212(c)(1) (relating to Tax Court proceedings) are deemed to include references to §664(c).

[624] Former Reg. §1.664-1(c) *Ex.*

[625] $1,500 UBTI less the $1,000 deduction allowed under §512(b)(12) equals $500.

[626] Reg. §1.664-1(e)(1).

[627] Reg. §1.664-1(d)(1)(ii)*(a)*.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

character of the annuity or unitrust amount.[628] Where a §170(c) organization receives a distribution other than the annuity or unitrust amount, and the distribution is in property other than cash, the trust does not realize gain or loss as a result of the distribution unless the distribution is in satisfaction of a right to receive a specific dollar amount or specific properties other than that distributed.[629] Generally, the realization of income will only be significant for the category rules computation (and the eventual taxation of the beneficiary), because a charitable remainder trust is exempt from income taxation.[630]

The trustee should not attempt to prepay the charity's entire remainder interest or otherwise buy out the charity. Doing so would terminate the trust's status as a CRT under §664.[631]

It is not clear under what circumstances the governing instrument would provide for distribution of specific property to a §170(c) organization. If the trustee were directed to hold specific property to be distributed to a charitable organization on a designated date or upon the occurrence of a specific event, such provision likely would violate the rule that the trustee must be able to invest the trust assets in a manner that could result in a reasonable amount of income or gain from the sale or disposition of the trust assets.[632]

In Rev. Rul. 73-610, a CRT was disqualified because a portion of its assets was subject to a life estate vested in the income beneficiary. The IRS ruled that the inability of the trustee to dispose of the assets subject to the life estate impermissibly restricted the trustee's investment powers. The same reasoning should apply to a trustee who is prohibited from selling certain property because it is earmarked for distribution to a §170(c) organization before the termination of the trust. To avoid this issue, the governing instrument could provide for the distribution of certain property only if held by the trust at the relevant date. In such case, the distribution of property other than that specified in the governing instrument could be viewed as a sale or exchange of the property by the trust. The trust would in turn recognize gain or loss equal to the difference between the trust's basis and the fair market value of the property on the date of distribution.

The method of computing the gain or loss upon the deemed sale is problematic. If a trust instrument required that the trustee distribute 100 shares of X company stock on the death of the income beneficiary and in lieu thereof the trustee distributed Y company stock, the trustee would be obligated to distribute Y stock with the same fair market value as the X stock, valued as of date of distribution. In effect, the trust would be viewed as satisfying a right to receive a specific dollar amount (the value of the X stock) with appreciated or depreciated property, and the basis of the Y stock would be compared with the fair market value of the X stock in computing the gain.

Example: A CRT provides that upon the death of one of the two recipients of the annuity or unitrust amount, the trustee will distribute one-half of the trust assets to a §170(c) organization. Upon distribution of property to the §170(c) organization, the trust does not realize income or loss. However, if the governing instrument had directed that the §170(c) organization was to receive specified stock or designated assets, and in lieu thereof other property was distributed, there would be a deemed sale or exchange. Any gain or loss realized would enter into the class and category computations.

5. *Taxation of Charitable Remainder Trust in States that Do Not Treat Them as Exempt*

Although most states treat CRTs as tax-exempt, not all do. A handful of states treat them as complex trusts. Even if the trust is resident in a state that exempts the trust, the trust could have rental or royalty income sourced from a non-exempt state. The IRS has not issued any specific guidance on income tax paid by a CRT. See 869 T.M., *State Income Taxation of Trusts*, for further discussion of the state taxation issues. See VI.C.2.e., above, for allocation of any state taxes paid to the classes and categories of income.

6. *Section 2801 Transfer Tax*

For individuals expatriating after June 16, 2008, Congress created a new transfer tax in §2801.[633] In enacting §2801, Congress determined that it was appropriate, in the interest of tax equity, to impose a tax on U.S. citizens or residents who receive, from an expatriate, a transfer that would otherwise have escaped U.S. estate and/or gift taxes as a consequence of expatriation.[634] If, during any calendar year, any U.S. citizen or resident receives any covered gift or bequest, there is a tax equal to the product of the highest rate of tax specified in the table contained in §2001(c) as in effect on the date of such receipt and the value of such covered gift or bequest.[635]

Proposed regulations issued on September 9, 2015, apply on and after the date of final publication and can be relied on beginning June 17, 2008, until the date preceding publication of final regulations, which were issued on January 14, 2025.[636] The final regulations did not adopt the proposed rules on CRTs that are contained in Prop. Reg. §28.2801-4(a)(2)(iii), noting a need for further consideration due to the fundamental and complex nature of such rules.[637] The proposed regulations would

[628] Reg. §1.664-1(e)(1).

[629] Reg. §1.664-1(e)(2).

[630] See the discussion at VI.C.1., above, regarding the taxation of CRTs, and at VI.F., below, regarding the taxation of the beneficiaries.

[631] *See* IRS AM 2020-006 (where trustee of CRAT could, in lieu of distributing remainder interest to charitable beneficiary, pay charitable organization cash equal to 10% of initial FMV of trust property plus $100, IRS advised that such trust would be disqualified for failing to require payment of remainder to charitable beneficiary; IRS clarified that §664(d)(1)(D) provides for minimum value of remainder interest at creation of trust, but "neither states nor implies that a current payment of that amount to charity vitiates the requirement to also pay the remainder at the end of the term").

[632] Reg. §1.664-1(a)(3).

[633] Added by the Heroes Earnings Assistance and Relief Tax Act of 2008 (HEART Act), Pub. L. No. 110-245, §301(b), §301(g)(2).

[634] *See* the preamble to the proposed §2801 regulations, REG-112997-10, 80 Fed. Reg. 54,447 (Sept. 10, 2015). *See also* T.D. 10027, 90 Fed. Reg. 3,376 (Jan. 14, 2025).

[635] §2801(a).

[636] *See* Reg. §28.2801-1 through §28.2801-7, §28.6001-1, §28.6011-1, §28.6060-1, §28.6071-1, §28.6081-1, §28.6081-1, §28.6091-1, §28.6101-1, §28.6107-1, §28.6109-1, §28.6151-1, §28.6694-1 through §28.6694-4, §28.6695-1, §28.6696-1, §28.7701-1, T.D. 10027, 90 Fed. Reg. 3376 (Jan. 14, 2025); REG-112997-10, 80 Fed. Reg. 54,447 (Sept. 10, 2015).

[637] Preamble to T.D. 10027, 90 Fed. Reg. 3376 (Jan. 14, 2025).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

make a CRT liable for the payment of the §2801 tax attributable to the value of the noncharitable U.S. person's interest in the trust.[638] Further, the proposed regulations would clarify that a CRT's payment of the §2801 tax on the portion of each transfer to the trust that is a covered gift or covered bequest is not a distribution to or for the use of any person within the meaning of §664(d)(1)(B) and §664(d)(2)(B), and that the CRT's liability for such a payment will not cause the trust to be disqualified as a charitable remainder trust as defined in §664.[639] The proposed regulations would confirm that the charitable remainder interest's share of each transfer to the CRT is not a covered gift or bequest.[640] The proposed regulations would also provide the method for computing the net covered gifts and covered bequests that are taxable to the CRT under §2801.[641]

A full discussion of the §2801 tax is beyond the scope of this Portfolio. For a detailed discussion of the §2801 tax, see 837 T.M., *Non-Citizens — Estate, Gift and Generation-Skipping Transfer Taxation.*

D. Recordkeeping

1. General Recordkeeping

The trust must maintain detailed records listing all income items as adjusted for carryovers and carrybacks and all deductions and the allocations thereof. Such information is essential for computing the character of current and undistributed income for purposes of the class and category rules discussed at VI.C.1., above. In addition, the trustee must note and characterize all sales of property and certain deemed sales,[642] as well as maintain a record of items of tax preference for alternative minimum tax purposes (because such items must be allocated to the beneficiary in the year the income is distributed).[643]

As discussed above in VI.C.1., trust income is accumulated in "categories" and "classes" that affect the taxation of the beneficiary throughout the life of the trust. Some information is carried from year to year on the Form 5227, *Split-Interest Trust Information Return*, but not in sufficient detail to use the return as a substitute for complete workpapers. For example, although rents and interest income are both "ordinary income" and would be allocated to the same class and category of income under the system discussed above at VI.C.1., the type of income may matter to the beneficiary. If the rent income is passive income, the beneficiary might be able to use that income to deduct passive losses on his or her return.

Clear documentation regarding the basis and holding period of all trust assets also is important. In the case of an inter vivos gift to a CRT, the trust receives a carryover basis in the property transferred,[644] with a basis increase equal to any gift tax paid on the transfer, subject to certain adjustments.[645] In addition, the trust takes over the transferor's holding period.[646] A testamentary CRT receives a "stepped-up" basis in the transferred property (other than income in respect of a decedent items) equal to the date of death (or alternate valuation date) value of the property transferred.[647] The trustee of a testamentary trust is deemed to have held all property received from the decedent's estate for the long-term holding period for purposes of determining whether any gain or loss on the sale of the property is long term.[648]

It is also necessary to know the basis of the trust's assets if a corpus distribution is made to charity before the termination of the trust. Such distributions must be made using property that is "fairly representative" of the trust's adjusted basis in its property on the date of payment.[649]

In the final year of the trust, the tax return asks for the value of the property initially contributed to the trust. This amount should be kept in the permanent records of the trust, as it is often decades between the funding and the termination of the trust.

2. Additional Recordkeeping for Trusts with a Net Income Limitation

In addition to the general recordkeeping requirements, a trustee of a trust with a net income limitation (a NIMCRUT or FLIP-CRUT, as discussed at IV.C., above) must keep records of the net income, any make-up deficit, and any payments made toward that deficit.

Practice Point: Although these amounts are shown on the annual federal tax return for the trust, a separate, permanent, record should be kept. Especially in years where there is a change in the tax preparation software or the preparer, carryover amounts can be lost.

E. Filing the Federal Tax Return for the Charitable Remainder Trust

1. Regular Filing Requirements

The tax return requirements for CRTs are referenced in the §664 regulations.[650]

A CRT must electronically file (if certain requirements are met) an information return (Form 5227, *Split-Interest Trust Information Return*) on an annual basis, with an exception for a trust to which no transfers for which a deduction was allowed under any of the sections listed in §4947(a)(2) have been made since May 26, 1969.[651] For the trust's first taxable year, a copy

[638] *See* Prop. Reg. §28.2801-4(a)(2)(iii).

[639] *See* Prop. Reg. §28.2801-4(a)(2)(iii).

[640] *See* Prop. Reg. §28.2801-4(a)(2)(iii).

[641] *See* Prop. Reg. §28.2801-4(a)(2)(iii), referencing Prop. Reg. §28.2801-4(b).

[642] For example, certain distributions to a §170(c) organization are treated as sales. Reg. §1.664-1(e)(2).

[643] §59(c); Reg. §1.58-3(a)(3).

[644] §1015(a).

[645] §1015(d).

[646] §1223(2); Reg. §1.1223-1(b). PLR 200335017 illustrates the application of the holding period and basis rules to an inter vivos CRUT.

[647] §1014(a), §1014(c).

[648] §1223(9).

[649] Reg. §1.664-2(a)(4), §1.664-3(a)(4).

[650] Reg. §1.664-1(a)(1)(ii). See XI.A.6., below, for the filing requirements before 2007.

[651] §6034, *amended by* the Pension Protection Act of 2006, Pub. L. No. 109-280, §1201(b)(1) (effective for taxable years beginning after 2006), §4947(a)(2)(C); Reg. §1.6034-1(a). *See also* Reg. §301.6011-13(a), *added by* T.D. 9972, 88 Fed. Reg. 11,754 (Feb. 23, 2023) (applicable to split-interest trust returns required to be filed for taxable years ending on or after December 31, 2023). Section 6034(a) requires a CRT to furnish such information concerning its taxable year as may be required by the IRS. Effective for returns for taxable years beginning after 2006, the Pension Protection Act of 2006 also: (1) increased the penalties for failing to file a return required by §6034(a); and (2) exempted information regarding noncharitable beneficiaries of trusts re-

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

of the governing instrument, certified by the fiduciary under penalties of perjury to be true and complete, must be attached to Form 5227.[652]

2. *Additional Filing Requirements Triggered by Unrelated Business Taxable Income*

If a CRT is liable for private foundation excise taxes, the trust must electronically file an annual Form 4720, *Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code*, if certain requirements are met.[653] As discussed in VI.C.3., above, effective for taxable years beginning after 2006, §664(c) provides that a CRT is subject to a 100% excise tax on any unrelated business taxable income (UBTI) the trust has during a taxable year. Form 4720 and its instructions encompass the reporting of UBTI and the payment of the §664(c)(2) excise tax.[654]

The instructions to Form 5227, *Split-Interest Trust Information Return,* require CRTs to distribute Form 1041, Schedule K-1, to the recipient of the unitrust or annuity trust amount reporting the income and deductions reflected on the Form 5227.

Form 5227 and Form 4720, as applicable, must be filed annually on or before the 15th day of the fourth month following the close of the trust's taxable year.[655] Generally, this means that all returns must be filed on or before April 15 of the following year. For Form 5227 and Form 4720 due after June 11, 2003, a CRT may obtain a six-month filing extension by filing Form 8868, *Application for Extension of Time to File an Exempt Organization Return or Excise Taxes Related to Employee Benefit Plans*, with the appropriate IRS office on or before the due date of the return for which the extension is requested.[656]

quired to file returns under §6034(a) from certain publicity requirements. *See* §6652(c)(2)(C), §6104(b), *added/amended by* Pub. L. No. 109-280, §1201(b)(2), §1201(b)(3), §1201(c)(2). However, IRS Info. Letter 2010-0050 states that the exception regarding noncharitable beneficiaries does not protect the trust's name from the §6104(b) public inspection requirements, even if the name includes the name of a noncharitable beneficiary or contributor. For more information on §6652(c)(2)(C) and other penalty provisions and on §6104 publicity requirements, see 452 T.M., *Tax-Exempt Organizations — Reporting, Disclosure, and Other Procedural Aspects.*

[652] Reg. §1.6012-3(a)(6); Instructions to Form 5227.

[653] *See* Reg. §53.6011-1(b); Reg. §301.6011-12(a), *added by* T.D. 9972, 88 Fed. Reg. 11,754 (Feb. 23, 2023) (applicable to excise tax returns required to be filed for taxable years ending on or after December 31, 2023). *See also* Rev. Proc. 83-32, §3; Instructions to Form 4720.

[654] *See* Reg. §1.664-1(c)(1), *amended by* T.D. 9403, 73 Fed. Reg. 35,583 (June 24, 2008).

[655] Reg. §1.6034-1(c), Reg. §53.6071-1. Form 5227 and Form 4720 must be filed electronically if certain requirements are met. *See* Reg. §301.6011-12(a), §301.6011-13(a), *added by* T.D. 9972, 88 Fed. Reg. 11,754 (Feb. 23, 2023) (applicable to returns required to be filed for taxable years ending on or after December 31, 2023). *See also* Instructions to Form 5227; Instructions to Form 4720.

[656] Pursuant to the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015, Pub. L. No. 114-41, §2006(b)(5), §2006(b)(6), Reg. §1.6081-9 provides an automatic six-month extension for the filing of Form 4720 and Form 5227. Reg. §1.6081-9, T.D. 9892, 85 Fed. Reg. 5323 (Jan. 30, 2020) (former temporary regulations (T.D. 9821) provided identical extension for automatic extensions prior to January 30, 2020). Returns required to be filed prior to January 1, 2016, were able to obtain an automatic extension of three months, and a subsequent three-month extension upon explanation to allow the IRS to determine whether to grant the extension. Former Reg. §1.6081-9 (as finalized by T.D. 9163, 69 Fed. Reg. 70,547 (Dec. 7, 2004), and before amendment by T.D. 9892). *See also* Instructions for Form 1041-A; Instructions for Form 5227; Instructions for Form 4720; Instructions for Form 8868.

F. *Taxation of Beneficiary*

The tax character of distributions of the annuity or unitrust amount in the hands of the recipient is determined by the rules set forth in §664(b) and the regulations thereunder, which for this purpose supersede all other provisions of the Code.[657] Many discussions refer to this as the "four-tier" system, but since the regulations now use the terms "categories" and "classes" this discussion will use those terms to avoid confusion.

The IRS has allowed unitrust payments to be made to a trust for the benefit of an incompetent beneficiary, with the beneficiary taxable on the payments.[658]

1. *Taxation of Distributions to Beneficiary*

Before the taxation of the beneficiary can be determined, the income and expenses must be allocated into the categories and classes discussed at VI.C., above. The income distribution calculation is performed at year-end after the income and expenses have been allocated to the categories and classes.[659] The payment must be made by the trustee, not directly from a trust investment, to avoid implications that the trust has distributed the asset itself to the beneficiary.[660] New cumulative totals are determined for each category and class of income, including the undistributed income from prior years.[661] The character of a distribution in the recipient's hands is determined by treating the distribution as made from each category in the following order:

(i) from ordinary income to the extent of the trust's accumulated undistributed ordinary income;

(ii) from capital gain to the extent of the trust's capital gains as determined under Reg. §1.664-1(d)(1)(iv);

(iii) from other income to the extent of the trust's accumulated undistributed other income; and

(iv) from corpus.[662]

For purposes of item (iv), "corpus" is defined as the net fair market value of the trust's assets less the total undistributed income (but not loss) in the preceding categories.[663]

[657] §664(b); Reg. §1.664-1(d)(1). For tax years beginning after 2012, also see the discussion of the final regulations under §1411 (T.D. 9644, 78 Fed. Reg. 72,394 (Dec. 2, 2013)) in VI.F.4., below, which addresses application of the §664(b) rules to the determination of whether items of income allocated to a noncharitable annuity or unitrust recipient constitute net investment income to him or her. *See* Reg. §1.1411-3(d)(2); preamble to T.D. 9644. Additionally, the IRS reserved Reg. §1.1411-3(d)(3) for rules allowing charitable remainder trusts to elect between the simplified method in the 2012 proposed regulations and the §664(b) method in the final regulations. To address these new rules, the IRS issued new proposed regulations simultaneously with the final regulations. *See* REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[658] *See* Rev. Rul. 2002-20; PLR 9710010, PLR 9710009, PLR 9710008.

[659] Reg. §1.664-1(d)(1)(ii)(*a*). The income categories and classes are used to determine the character of a charitable remainder trust distribution in the hands of the recipient, regardless of whether the trust is exempt from tax under §664(c) in the year of the distribution. This rule was more relevant when charitable trusts lost their exemption for a year in which they had unrelated business taxable income.

[660] *See* IRS AM 2020-006.

[661] Reg. §1.664-1(d)(1)(ii)(*a*).

[662] §664(b).

[663] Reg. §1.664-1(d)(1)(ii)(*a*)(*4*).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Within each category, the income is deemed distributed from the highest tax rate class first.[664]

Reg. §1.664-1(d)(1)(i)(a) clarifies that the recipient is to calculate the tax on the distribution by using the tax rates applicable to the classes of income from which the distribution is derived in the year in which the trust is required to make the distribution rather than the rates applicable in the year the trust receives the income.[665]

> *Example 1:* A trust adds $20,000 to its long-term capital gain category and class in a year in which the tax rate on long-term gains is 15%. The trust distributes that $20,000 in a year in which the tax rate on long-term gains is 20%. The beneficiary includes the distributed long-term gain in his or her taxable income as a long-term gain at the 20% rate; he or she does not benefit from the prior 15% rate.[666]

If there are different classes of income in the ordinary income category, Reg. §1.664-1(d)(1)(ii)*(b)* indicates that the distribution from that category is treated as made from each class, in turn, until exhaustion of the class, beginning with the class subject to the highest federal income tax rate and ending with the class subject to the lowest rate. "Highest federal income tax rate" includes the tax under §1411, if applicable.[667] If there are different classes of net gain in the capital gains category, the distribution from that category is treated as made first from the short-term capital gain class and then from each class of long-term capital gain, in turn, until exhaustion of the class, beginning with the class subject to the highest federal income tax rate and ending with the class subject to the lowest rate. If two or more classes within a category are subject to the same current rate but at least one of the classes will be subject to a different rate in the future (e.g., if there is a sunset of the current rate), then the order of the distributions is based on the future rates applicable to the classes. If there is more than one type of income in a class, the distributions from that class are treated as consisting of the same proportion of each type of income as the total current and undistributed income of that type bears to the total current and undistributed income included in the class.

> *Example 2:* A trust has no accumulated ordinary income, but does have $4,000 of accumulated short-term capital gain, $10,000 of capital gain taxable at the 25% rate, and $50,000 of long-term capital gain. A distribution of $20,000 would carry out the $4,000 of short-term capital gain, the $10,000 of 25% capital gain, and $6,000 of long-term capital gain.

> *Example 3:* A trust established in 2016 has $20,000 of accumulated ordinary income, composed of $4,000 of rent income, $6,000 of interest income, and $10,000 of IRA income in its ordinary income category. A distribution of $15,000 would carry out the $4,000 of rent, the $6,000 of interest, and $5,000 of IRA income, since the IRA would not be subject to the tax under §1411. The character of the distributions may or may not matter to the beneficiary, depending on his or her exposure to the net investment income tax under §1411 and the possible existence of passive loss carryovers on his or her return.

> *Example 4:* The trust has the same accumulated income classes as in the previous example. A distribution of $5,000 would carry out $2,000 of rent income, $3,000 of interest income, and no IRA income. The highest tax rates applicable to rent and interest income are identical, although if the beneficiary has passive losses his or her effective rate on the classes of income may not be the same.

If a distribution in a particular year exhausts the cumulative undistributed ordinary income, the distribution is next deemed to be composed of capital gain income to the extent of the trust's cumulative undistributed capital gains.[668] As explained at VI.C.1., above, the various classes of undistributed capital gains are determined on a cumulative net basis pursuant to the rules set forth in the regulations.[669]

> *Example 5:* A charitable remainder trust (CRT) has accumulated $10,000 of ordinary income and $5,000 of qualified dividend income in the ordinary income category, and $3,000 of short-term capital gain and $20,000 of long-term capital gain in the capital gain category. If the required distribution to the beneficiary is $12,000, the beneficiary would be taxed on $10,000 of ordinary income and $2,000 of qualified dividend income.

> *Example 6:* Assuming the same accumulation as the previous example, a distribution of $20,000 would carry out $10,000 of ordinary income, $5,000 of qualified dividend income, $3,000 of short-term capital gain, and $2,000 of long-term capital gain. The remaining $18,000 of long-term capital gain would remain for potential future distribution.

Notice that the result of the "category and class" system generally results in the highest-taxed income being distributed first. However, since qualified dividends are considered in the ordinary income category, those are deemed distributed before short-term capital gains. Thus, the "worst-in, first-out" priority is not absolute.

After the income and capital gain categories are exhausted, distributions are deemed to come from "other income" to the extent of the trust's cumulative undistributed "other income."[670] "Other income" includes income that is excluded from gross income as provided in subtitle A, chapter 1, subchapter B, part III (i.e., §101 through §140).[671] These amounts include the proceeds of life insurance, gifts and inheritances,[672] and tax-ex-

[664] Reg. §1.664-1(d)(1)(ii)(*b*).

[665] *See also* T.D. 9190, 70 Fed. Reg. 12,793 (Mar. 16, 2005).

[666] An exception may apply to pre-2013 capital gains in the calculation of net investment income tax under §1411. See the discussion at VI.F.4., below.

[667] Reg. §1.1411-(3)(d)(2).

[668] §664(b)(2); Reg. §1.664-1(d)(1)(ii)*(a)(2)*.

[669] Reg. §1.664-1(d)(1)(iv).

[670] §664(b)(3); Reg. §1.664-1(d)(1)(ii)*(a)(3)*.

[671] Reg. §1.664-1(d)(1)(i)*(a)(3)*.

[672] Because a gift of a specific sum of money or specific property within §663(a)(1) is excluded from gross income under §102, when an estate makes a

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

empt bond income. A loss in this category for a current year reduces accumulated undistributed "other income" from prior years, and any excess is carried forward indefinitely to reduce the "other income" category in future years.

Example 7: A trust is funded with a long-term capital asset with a zero basis and a value of $400,000. The asset is sold, and the gain is allocated to the capital gain category, long-term gain class. The funds are invested in tax-exempt bonds, which produce income of $10,000 in the initial year, allocated to the "other income" category. The required distribution to the beneficiary in the initial short year is $12,000. Although the trust has earned ordinary income under the traditional definition of trust accounting income, the distribution is deemed to come from the capital gain category. The beneficiary is taxed on $12,000 of long-term capital gain. The balance in the long-term capital gain class is reduced to $388,000. The other income category now has a balance of $10,000.

Example 8: The same facts as above, except that the trust is a NIMCRUT. Assuming trust accounting income is the $10,000 of tax-exempt income, the trustee will distribute $10,000 to the beneficiary. The distribution of $10,000 is still deemed to come from the capital gain category. The undistributed income in the capital gain category is $390,000 and the other income category is $10,000.

When the cumulative undistributed income of the ordinary, capital gain, and other income categories is deemed to have been exhausted, remaining distributions are considered to have been made from trust corpus.[673] The term "corpus" means the net fair market value of the trust assets less the total undistributed income, but not losses, in each of the above three categories.[674]

These rules are applicable for every taxable year of the trust, even if the trust realized unrelated business taxable income (UBTI).[675] If the trust is required to pay excise tax because of its UBTI, the amount of tax is not taken into account in determining the character of distributions.[676] Thus, the beneficiary does not receive any credit for excise taxes paid by the trust, nor is any income category reduced by the tax paid. As discussed at VI.C.3., above, any excise tax is charged to corpus.[677]

For the former rules and transition rules regarding capital gains in CRTs, see XI.A.7., below.

2. Multiple Beneficiaries

As noted above, the determination of the character of amounts deemed distributed to the beneficiaries is made as of the end of the trust's taxable year.[678] If there is more than one annuity or unitrust recipient, each recipient is treated as receiving a pro rata share of each category of income and corpus.[679]

Example: X transfers $40,000 to a charitable remainder annuity trust (CRAT) that is to pay $3,000 per year to X and $2,000 per year to Y for a term of five years. During the first taxable year and after the allocation of all expenses, the trust has $3,000 of ordinary income, $500 of capital gain, and $500 of tax-exempt income. X is treated as receiving ordinary income of $1,800 ($3,000/$5,000 × $3,000), capital gain of $300 ($3,000/$5,000 × $500), tax-exempt income of $300 ($3,000/$5,000 × $500), and corpus of $600 ($3,000/$5,000 × [$5,000 − $4,000]). Y is treated as receiving ordinary income of $1,200 ($2,000/$5,000 × $3,000), capital gain of $200 ($2,000/$5,000 × $500), tax-exempt income of $200 ($2,000/$5,000 × $500), and corpus of $400 ($2,000/$5,000 × [$5,000 − $4,000]).[680]

3. Effect of Timing of Payments on Beneficiary's Income

a. Regular Payments

In certain circumstances, the regulations allow the payment of the annuity or unitrust amount to be made after the close of the taxable year.[681] A payment from a net income unitrust can be made after the close of the taxable year if the payment is made within a reasonable time after the close of the taxable year.[682] Effective for distributions made on or after January 5, 2001, if the payment is from an annuity trust or a fixed percentage unitrust, the regulations allow a distribution after the close of the year if: (i) the trust pays the annuity or fixed percentage unitrust amount within a reasonable time after the close of the taxable year; and (ii) the entire amount is characterized as income in the hands of the recipient or the amount is characterized as corpus because the trust pays the amount by (a) distributing property (other than cash) after the close of the taxable year and the trustee elects to treat any income generated by the distribution as occurring on the last day of the taxable year that the amount was due, (b) distributing cash contributed to the trust for which a deduction was allowable under §170, §2055, §2106, or §2522, or (c) distributing cash received as a return of basis in an asset contributed to the trust for which a deduction was allowable under §170, §2055, §2106, or §2522, and which

---

distribution of a specific sum to a CRT the distribution presumably is treated as "other income" rather than as "corpus."

[673] §664(b)(4); Reg. §1.664-1(d)(1)(ii)*(a)(4).*

[674] Reg. §1.664-1(d)(1)(ii)*(a)(4).*

[675] *See* Reg. §1.664-1(c), *amended by* T.D. 9403, 73 Fed. Reg. 35,583 (June 24, 2008). The 2008 final regulations are effective for taxable years beginning after 2006. Reg. §1.664-1(c)(3). As discussed in XI.A.6., below, effective for taxable years beginning after 2006, the Tax Relief and Health Care Act of 2006 (TRHCA), Pub. L. No. 109-432, §424, amended §664(c) to provide that a CRT is not subject to income tax but is subject to a 100% excise tax on any UBTI the trust has during a taxable year.

[676] Reg. §1.664-1(c)(1), §1.664-1(d)(2), *amended by* T.D. 9403. The regulations, as amended in 2008, are consistent with the legislative history to the TRHCA, Pub. L. No. 109-432. *See* Staff of J. Comm. on Tax'n, 109th Cong., Technical Explanation of H.R. 6408, the "Tax Relief and Health Care Act of 2006" 115 (J. Comm. Print 2006).

[677] §664(b).

[678] Reg. §1.664-1(d)(1)(ii)*(a).*

[679] Reg. §1.664-1(d)(3).

[680] Reg. §1.664-1(d)(3) *Ex.*

[681] Reg. §1.664-2(a)(1)(i)(a), §1.664-3(a)(1)(i)(g), §1.664-3(a)(1)(i)(h), §1.664-3(a)(1)(i)(j).

[682] Reg. §1.664-3(a)(1)(i)(j).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

the trust sold during the year for which the amount was due.[683] However, if the annuity trust or fixed percentage unitrust was created before December 10, 1998, less restrictive rules allow the trust to pay the annuity or unitrust amount within a reasonable time after the close of the taxable year if the percentage payout to the annuity or unitrust recipient is 15% or less.[684]

The recipient reports such income in the recipient's taxable year in which the trust's year ends. If the trust and the recipient have different taxable years, the income attributable to the payment of the annuity or unitrust amount must be included in gross income for the recipient's taxable year that includes the last day of the trust's taxable year in which the amount is required to be distributed.[685] This latter rule of inclusion is the same as in the case of simple or complex trusts.[686]

The effect of these rules is that the beneficiary will be taxed on his or her distribution in the year for which the payment was due, not necessarily in the year in which the payment was received.[687]

Comment: The post-2001 rules were added to preclude a strategy of contributing a highly appreciated asset in Year One, holding the asset, and then making the required distribution for Year One at the beginning of Year Two. Because there would be little or no income earned by the trust in Year One under the prior strategy, the beneficiary would receive the distribution tax-free.[688]

The trust will satisfy the reasonable time requirement if it makes the payment before the due date, including extensions, for Form 5227, *Split-Interest Trust Information Return*, for the year in which the payment is due.[689]

If a trust makes the annuity or unitrust payment after the close of the taxable year and does not satisfy the appropriate requirements noted above, the trust will be deemed to have: (1) failed to function exclusively as a CRT; (2) engaged in a prohibited act of self-dealing (within the meaning of §4941); (3) received unrelated debt-financed income, within the meaning of §514; and (4) received an additional contribution (which will disqualify an annuity trust).[690] [691]

b. Payments Due to Incorrect Valuation or Other Adjustments

There are three instances (in addition to the year of the beneficiary's death) in which the general rule of inclusion is not applicable and the annuity or unitrust amount is included in the gross income of the recipient for his or her taxable year within which falls the end of the taxable year of the trust in which the amount is "paid, credited or required to be distributed."[692] The three situations involve payments made: (1) from a testamentary trust, where the payments are delayed until the year of full funding of the trust;[693] (2) pursuant to an amendment to the governing instrument for certain grandfathered trusts;[694] or (3) as a result of an incorrect valuation of the trust's assets.[695]

Where the trust has made a payment to a recipient by reason of an incorrect valuation of the trust assets, the payment is considered to have been a payment required to be distributed at the time of the final determination of the correct valuation.[696] If a recipient is required to repay an amount to the trust, he or she is permitted a deduction in the year the amount is paid, credited, or required to be paid to the extent that the amount repaid was included in his or her gross income.[697] The deduction is computed by reference to §1341 and the regulations thereunder relating to the tax computation upon the restoration of a substantial amount held under a claim of right.[698]

Practice Point: The regulations do not contemplate any reason for an untimely payment other than the three listed. However, in the author's experience, calculation errors happen for any number of reasons beyond valuation errors. The trustee may have misinterpreted the document, miscalculated a make-up amount in a NIMCRUT, missed a trust asset (thereby undervaluing a CRUT), or simply multiplied incorrectly. An error may continue for years, resulting in a substantial payment to a beneficiary. The author's practice has been to follow the tax treatment for "payment due to incorrect valuation" and disclose the reason for the payment in the return for the year in which the payment is made.

c. Payments for the Year of Recipient's Death

A special rule of inclusion applies to the year of the recipient's death. If the recipient reports income on a cash basis, the final individual income tax return must include only amounts actually distributed before death.[699] Any amount required to be distributed that is distributed after death to the recipient's estate or beneficiary thereof is treated as income in respect of a decedent (IRD) pursuant to §691(a).[700] The payment retains its tax character and may enable the recipient to claim an income

[683] Reg. §1.664-2(a)(1)(i)(a), §1.664-3(a)(1)(i)(g), *as amended by* T.D. 8926, 66 Fed. Reg. 1034 (Jan. 5, 2001). If the distribution from such a trust was made before January 5, 2001, the two options in Reg. §1.664-2(a)(1)(i)(a)(2), §1.664-2(a)(1)(i)(a)(3), §1.664-3(a)(1)(i)(g)(2), and §1.664-3(a)(1)(i)(g)(3) for distributing cash when the distribution was treated as corpus to the unitrust beneficiary did not apply. *See* Reg. §1.664-2(a)(1)(i)(e), §1.664-3(a)(1)(i)(l).

[684] Reg. §1.664-2(a)(1)(i)(b), §1.664-3(a)(1)(i)(h).

[685] Reg. §1.664-1(d)(4)(i).

[686] *See* Reg. §1.652(c)-1, §1.662(c)-1.

[687] Reg. §1.664-1(d)(4)(i).

[688] Reg. §1.643(a)-8, added to preclude the result discussed in Notice 94-78.

[689] Reg. §1.664-2(a)(1)(i)(c), §1.664-3(a)(1)(i)(k). Form 5227 is filed on April 15 following the close of the taxable year. *See* §6011, §6071(a); Reg. §53.6011-1(c) (redesignated by T.D. 9972, 88 Fed. Reg. 11,754 (Feb. 23, 2023)), §53.6071-1(c). *See also* Reg. §1.6012-3(a)(6) (prescribing Form 1041-B, which has been replaced with Form 5227); Reg. §301.6011-13(a), *added by* T.D. 9972, 88 Fed. Reg. 11,754 (Feb. 23, 2023) (electronic filing applicable to split-interest trust returns required to be filed for taxable years ending on or after December 31, 2023, if certain requirements met). Reg. §1.6081-9 provides an automatic six-month extension for the filing of Form 5227. Reg. §1.6081-9, T.D. 9892, 85 Fed. Reg. 5323 (Jan. 30, 2020).

[690] Reg. §1.664-2(b).

[691] Reg. §1.664-2(a)(1)(i)(a), §1.664-2(a)(1)(i)(b), §1.664-3(a)(1)(i)(g), §1.664-3(a)(1)(h), §1.664-3(a)(1)(j).

[692] Reg. §1.664-1(d)(4)(ii). It is assumed that this phrase has the same meaning here as it does in §661(a)(2).

[693] Reg. §1.664-1(a)(5). See the discussion of testamentary charitable remainder trusts at V., above.

[694] Reg. §1.664-1(f)(3).

[695] Reg. §1.664-2(a)(1)(iii), §1.664-3(a)(1)(iii).

[696] Reg. §1.664-2(a)(1)(iii), §1.664-3(a)(1)(iii).

[697] Reg. §1.664-1(d)(4)(ii).

[698] Reg. §1.664-1(d)(4)(ii).

[699] Reg. §1.664-1(d)(4)(iii).

[700] Reg. §1.664-1(d)(4)(iii).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

tax deduction pursuant to §691(c) depending on the amount of estate tax paid by the estate.[701]

Comment: Where the governing instrument terminates the payment of the annuity or unitrust amount with the payment immediately preceding the death of the recipient of the annuity or unitrust amount, the recipient could still die before he or she receives the distribution. In that situation, the last payment would constitute IRD in the hands of the recipient's estate or the beneficiary thereof. The character of the amount to be included in the recipient's final income tax return if received by the recipient, or in the return of the recipient's estate or beneficiary thereof if the amount is IRD, is based on the "category and class" rules for the full taxable year of the trust in which the recipient's final taxable year ends. In the case of a decedent, his or her taxable year ends on the date of death.[702]

4. *Special Rules to Determine Beneficiary's §1411 Net Investment Income*

a. *General Rule*

Effective for tax years beginning after 2012, §1411 imposes a 3.8% tax (generally referred to as the "net investment income tax") on certain unearned income of individuals, trusts, and estates.[703] Under Reg. §1.1411-3(a)(1)(i), §1411 applies to all trusts that are subject to Part I of Subchapter J in Subtitle A, Chapter 1, of the Code, unless specifically exempted by Reg. §1.1411-3(b). Reg. §1.1411-3(b) exempts charitable remainder trusts (CRTs) described in §664. However, as discussed below, Reg. §1.1411-3(d)(1)(i) provides special rules regarding the treatment of annuity or unitrust distributions from CRTs to persons who are subject to tax under §1411.

As background, "net investment income" is defined as investment income reduced by deductions allocable to that income.[704] Investment income consists of three items: (1) gross income from interest, dividends, annuities, royalties, and rents to the extent not derived in the ordinary course of a trade or business (unless that trade or business is described in item (2)); (2) other gross income from a trade or business that is a §469 passive activity or that consists of trading in financial instruments or §475(e)(2) commodities; and (3) net gain that is taken into account in computing taxable income and attributable to the disposition of property not held in a trade or business (unless that trade or business is described in item (2)).[705] An individual CRT beneficiary is subject to the 3.8% net investment income tax (in addition to any other tax imposed by Subtitle A of the Code) each tax year on the lesser of: (1) his or her net investment income for the tax year; or (2) the excess (if any) of his or her modified adjusted gross income for the year over a threshold amount.[706] The threshold amount is $250,000 for married taxpayers filing jointly (or a surviving spouse), $125,000 for a married taxpayer filing separately, and $200,000 for all other individual taxpayers.[707]

Under the final regulations, items of net investment income allocated to a CRT's annuity or unitrust payments retain their character as net investment income in the hands of the recipient of that annuity or unitrust distribution, as determined under the §664(b) rules.[708] If the CRT has more than one annuity or unitrust beneficiary, the trustee must apportion the net investment income among such beneficiaries based on their respective shares of the total annuity or unitrust amount paid by the trust for that tax year.[709] A CRT's accumulated net investment income is the total amount of net investment income received by the trust for all tax years that begin after 2012, less the total amount of net investment income distributed for all prior tax years of the trust that begin after 2012.[710] In other words, the regulations "grandfather" pre-2013 amounts (amounts that would be net investment income, but for the fact that they were realized before 2013).[711]

---

[701] §691(a)(3).

[702] Reg. §1.443-1(a)(2).

[703] *See* §1411(a). The Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, §1402(a)(1), §1402(a)(4), enacted §1411 in a separate Chapter 2A of the Code, titled "Unearned Income Medicare Contribution." The IRS refers to the tax as the "net investment income tax" in the preamble to the final regulations providing guidance on the application of §1411. *See* T.D. 9644, 78 Fed. Reg. 72,394 (Dec. 2, 2013); Reg. §1.1411-0 through §1.1411-10, §1.469-11(b)(3)(iv). The regulations apply to tax years beginning after 2013, except that Reg. §1.1411-3(d) (special rule for §664 charitable remainder trusts) applies to tax years beginning after 2012. Reg. §1.1411-1(g), §1.1411-2(e), §1.1411-3(f), §1.1411-4(i), §1.1411-5(d), §1.1411-6(c), §1.1411-8(c), §1.1411-9(d), §1.1411-10(i), §1.469-11(b)(3)(iv)(D). According to the preamble of the proposed regulations, taxpayers were able to rely on the proposed regulations in complying with §1411 until the effective date of final regulations. REG-130507-11, 77 Fed. Reg. 72,612 (Dec. 5, 2012). The IRS website includes "Questions and Answers on the Net Investment Income Tax" (http://www.irs.gov/uac/Newsroom/Net-Investment-Income-Tax-FAQs), which answers some basic questions regarding §1411. For a more detailed discussion of §1411, see 511 T.M., *Section 1411 — Net Investment Income Tax*.

[704] §1411(c)(1). *See* Reg. §1.1411-3(e), §1.1411-4(a).

[705] §1411(c)(1)(A), §1411(c)(2). *See* Reg. §1.1411-4, §1.1411-5. For exceptions and special rules applicable in determining net investment income, see §1411(c)(4), (5). *See also* Reg. §1.1411-6 through §1.1411-10.

[706] §1411(a)(1). *See* Reg. §1.1411-2(b). For trusts subject to §1411, the 3.8% tax applies (in addition to all other taxes imposed by Subtitle A of the Code) each tax year to the lesser of: (1) the trust's undistributed net investment income for the tax year; or (2) the excess (if any) of the trust's §67(e) adjusted gross income for the tax year over the dollar amount at which the highest §1(e) tax bracket begins for the year. §1411(a)(2). *See* Reg. §1.1411-3(a). The calculation of undistributed net investment income is not explained in the Code, but is described under Reg. §1.1411-3(e).

[707] §1411(b). *See* Reg. §1.1411-2(d).

[708] Reg. §1.1411-3(d)(1)(i). Although the 2012 proposed regulations (REG-130507-11, 77 Fed. Reg. 72,612 (Dec. 5, 2012)) suggested special computational rules to calculate the §1411 tax ("simplified method"), the IRS adopted the recommendations of several commentators to apply the §664(b) rules instead. *See* Reg. §1.1411-3(d)(2); preamble to T.D. 9644; American Institute of Certified Public Accountants, "AICPA Comments on Proposed Rules (REG-130507-11) on Net Investment Income Tax" (May 8, 2013), reprinted in *Bloomberg BNA Tax Core* (May 14, 2013) ("The rule in the proposed section 1411 regulations overrides the statutory provision of section 664(b) because [net investment income] that is capital gain will be distributed prior to accumulated ordinary income earned before 2013. While this would be beneficial to taxpayers, we believe it is contrary to the requirements of section 664(b). We believe that the various types of [net investment income] should be treated as separate classes of income within each category, and the normal rules should apply to determine which category of income and which class of income within that category is being distributed to the annuity or unitrust recipient."). Additionally, the IRS reserved Reg. §1.1411-3(d)(3) for rules allowing CRTs to elect between the simplified method in the 2012 proposed regulations and the §664(b) method in the final regulations. To address these new rules, the IRS issued new proposed regulations simultaneously with the final regulations, discussed below. *See* REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[709] Reg. §1.1411-3(d)(1)(ii).

[710] Reg. §1.1411-3(d)(1)(iii).

[711] Reg. §1.1411-3(d)(1)(iii). Individuals, estates, and trusts must use Form 8960, *Net Investment Income Tax — Individuals, Estates, and Trusts*, attached to Form 1040, to compute their net investment income tax. Form 8960 provides a simple method for CRT annuity or unitrust recipients to reduce their net

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Applying the §664(b) rules to the net investment income items of a CRT, the final regulations provide that the net investment income item's applicable federal income tax rate for purposes of allocating that item to the appropriate class within a category of income as described in Reg. §1.664-1(d)(1)(i)(b) is the sum of the item's income tax rate and the §1411 tax rate.[712] The result is that the accumulated net investment income and excluded income in the same income category constitute separate classes of income within that category.[713] With the adoption of the §664(b) method in the final regulations, the IRS simultaneously issued new proposed regulations that would provide special rules and method elections relating to its application.[714]

b. "Simplified Method" Election

The proposed regulations would allow a CRT to elect between the "simplified method" (previously contained in the 2012 proposed regulations, with one modification) and the "§664(b) method" (contained in the final regulations), to be effective for tax years after 2012.[715] The proposed simplified method would provide that the net investment income of a CRT annuity or unitrust beneficiary includes an amount equal to the lesser of (1) the beneficiary's share of the total amount of the distributions for that year, or (2) the beneficiary's same share of the accumulated net investment income.[716] Notwithstanding the general excess deduction rule in Reg. §1.1411-4(f)(1)(ii), if in a tax year a CRT's properly allocable deductions under §1411(c)(1)(B) exceed the gross investment income and net gain under §1411(c)(1)(A), then such excess deductions must reduce the beneficiary's share of the accumulated net investment income for that year and for subsequent tax years, should any deductions remain.[717] Therefore, the proposed simplified method would retain the Chapter 1 principle that losses are carried forward and offset income in future years.

For a CRT established after December 31, 2012, the election would be required on its income tax return for the tax year it was established. For a CRT established before January 1, 2013, the election was required on its income tax return for its first taxable year beginning after 2012. A return could be amended to make the election as long as the period of limitations on the amended returns and affected returns thereafter for both the beneficiaries and the trust had not closed. Once the election was made it would be irrevocable.[718]

Editor's Note: For a sample statement electing the simplified method of calculating net investment income at the trust level, see *Trust: Simplified Net Investment Income Tax Election for Charitable Remainder Trusts (§1411)* in the Tax Elections & Compliance Statements Library.

c. Special Provisions for Charitable Remainder Trusts that Own CFCs or PFICs

The regulations include special rules for the application of the §664(b) rules to certain distributions made to CRTs that own interests in controlled foreign corporations (CFCs) and passive foreign investment companies (PFICs).[719] The rules would apply to income from CFCs and PFICs not making the Reg. §1.1411-10(g) election to synchronize the income tax and §1411 treatment of income inclusions from these investments. The election is intended to avoid additional recordkeeping for owners of CFCs or PFICs, but the tradeoff is potential acceleration of net investment income subject to §1411.[720] Not making the election could result in income recognition that is different for purposes of Chapter 1 than for §1411.[721]

While Reg. §1.1411-10 provides §1411 guidance applicable to CFCs and PFICs, Prop. Reg. §1.1411-3(d)(2)(ii) would coordinate it with the §664(b) rules.

First, the proposed regulations would provide that §951 and §1293 amounts that are included in gross income for Chapter 1 purposes and in one or more Reg. §1.664-1(d)(1) categories are excluded from net investment income.[722]

Second, when a CRT receives a distribution of previously taxed earnings and profits that is not treated as a dividend for Chapter 1 purposes under §953(d) and §1293(c), but is a dividend for §1411 purposes, the trust would be required to allocate such amounts among the §664(b) categories.[723] To the extent the trust has excluded income in the ordinary income category and capital gain category, the net investment income amount would be allocated to the trust's excluded income class in the ordinary income category, then to the excluded income class in the capital gain category, and until exhaustion of each such class, beginning with the class of excluded income with the highest income tax rate, with the remaining net investment income allocated to the other income category.[724] If the trust distributes other income category amounts, the distribution would cause the beneficiary to increase its modified adjusted gross income or adjusted gross income by the same amount.[725]

Third, the proposed regulations would address the differential in gain or loss associated with the tax basis disparities between Chapter 1 and §1411.[726] The allocation of such gain is similar to that in Prop. Reg. §1.1411-3(d)(2)(ii)(B), the difference being that the additional gain would be allocated within the capital gain category before any allocation to the ordinary income category.[727] The allocation of such loss is also similar to that in Prop. Reg. §1.1411-3(d)(2)(ii)(B), except that losses are accompanied by a reduction in modified adjusted gross income or adjusted gross income and allocated first to the other income category (so that the accumulated net investment in-

---

investment income by the grandfathered amounts (which will be taken from the Schedule K-1 received by the beneficiary) on line 7 of Form 8960. See Freda, "IRS Draft Form on Net Investment Income Addresses Grandfathered Amounts for CRTs," 32 Tax Mgmt. Wkly. Rpt. 1070 (Aug. 12, 2013).

[712] Reg. §1.1411-3(d)(2); preamble to T.D. 9644.

[713] Reg. §1.1411-3(d)(2); preamble to T.D. 9644; Reg. §1.664-1(d)(1)(i)(b). *See also* Reg. §1.1411-3(d)(2)(iii) *Ex.* 1.

[714] *See* REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[715] *See* Prop. Reg. §1.1411-3(d)(3), REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[716] Prop. Reg. §1.1411-3(d)(3)(i).

[717] Prop. Reg. §1.1411-3(d)(3)(ii).

[718] Prop. Reg. §1.1411-3(d)(3)(iii).

[719] *See* Prop. Reg. §1.1411-3(d)(2)(ii), REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[720] T.D. 9644, 78 Fed. Reg. 72,393 (Dec. 2, 2013), §II.11.D.

[721] T.D. 9644, 78 Fed. Reg. 72,393–72,449 (Dec. 2, 2013), §II.11.D.

[722] Prop. Reg. §1.1411-3(d)(2)(ii)(A), REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[723] Prop. Reg. §1.1411-3(d)(2)(ii)(B).

[724] Prop. Reg. §1.1411-3(d)(2)(ii)(B).

[725] Reg. §1.1411-10(c)(4), §1.1411-10(e)(1).

[726] *See* Prop. Reg. §1.1411-3(d)(2)(ii)(C).

[727] Prop. Reg. §1.1411-3(d)(2)(ii)(C)(1).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

come is eliminated first, and the beneficiary will not have to account for modified adjusted gross income or adjusted gross income).[728]

Practice Point: If the trust has relatively small investments in CFCs or PFICs, the Reg. §1.1411-10(g) election will reduce the required recordkeeping. The trustee will not need to track two sets of basis numbers for each CFC or PFIC or allocate a "NII inclusion amount" when a distribution is received from the CFC or PFIC.[729] On the other hand, if the CFC or PFIC investment is substantial, the effort resulting from not making the election may be worthwhile, especially in a trust with a net income limitation (such as a NIMCRUT). Although the (non-cash) income inclusions from the CFC or PFIC will accumulate in the categories and classes within the CRT, no net investment income is created by those inclusions.[730] Depending on the type of other income and the amount and source of distributions from the trust, not making the Reg. §1.1411-10(g) election may reduce the beneficiary's exposure to the net investment income tax.

This section of the proposed regulations would be effective for tax years beginning after 2013, but may be relied on for tax years beginning after 2012.[731] For more information on CFCs and PFICs, see 930 T.M., *CFCs — Sections 959–965 and 1248 (Foreign Income Series)*, and 6300 T.M., *PFICs (Foreign Income Series)*, respectively.

G. Avoiding Penalties Under the Private Foundation Rules

1. Private Foundation Provisions Applicable to Charitable Remainder Trusts

Charitable remainder trusts (CRTs) are subject to many of the private foundation provisions contained in §4940 through §4948 of the Code.[732] This means that anyone drafting the governing instrument of a CRT or administering such a trust should have some familiarity with these provisions.

Section 4947(a)(2) provides in part:

> In the case of a trust which is not exempt from tax under section 501(a), not all of the unexpired interests in which are devoted to one or more of the purposes described in section 170(c)(2)(B), and which has amounts in trust for which a deduction was allowed under section 170, 545(b)(2), 642(c), 2055, 2106(a)(2), or 2522, section 507 (relating to termination of private foundation status), section 508(e) (relating to governing instruments) to the extent applicable to a trust described in this paragraph, section 4941 (relating to taxes on self-dealing), section 4943 (relating to taxes on excess business holdings) except as provided in subsection (b)(3), section 4944 (relating to investments which jeopardize charitable purpose) except as provided in subsection (b)(3), and section 4945 (relating to taxes on taxable expenditures) shall apply as if such trust were a private foundation.

Charitable remainder trusts fall within this provision because: (1) they are not exempt from tax under §501(a); (2) not all of their unexpired interests (i.e., the noncharitable income interests) are devoted to charitable (§170(c)(2)(B)) purposes; and (3) they have amounts in trust for which a deduction was allowed under §170, §2055, or §2522.[733] Pursuant to Reg. §53.4947-1(a), "in the absence of proof to the contrary" a deduction is "allowed" if it would have been allowable under one of the cited sections. Thus, CRTs are subject (with certain exceptions explained herein) to the private foundation provisions set forth above.

Comment: A newly created trust is treated as having amounts in trust for which a deduction was allowed from the date of its creation, even if the deduction would be allowed for such amounts only at a later date.[734] Presumably, a trust intended to be a CRT, but which failed to satisfy one or more of the technical requirements for CRT status, would not be subject to §4947(a)(2) and the private foundation provisions because there would be no "amount in trust for which a deduction was allowed" under any of the listed provisions.

Any qualified CRT that does not have any income beneficiaries described in §170(c), §2055(a), or §2522(a) is excluded from the application of §4943 and §4944.[735] However, if any portion of the income interest in a CRT is payable to an organization described in §170(c), §2055(a), or §2522(a) and a charitable deduction was allowed for a gift of such income interest, the §4947(b)(3)(B) exclusion will not apply and §4943 and §4944 will apply.[736] The application of the private foundation rules to CRTs with charitable income beneficiaries is discussed at VI.G.3., below.

In the normal course, §507 should not apply to split-interest trusts. The regulations under §4947 provide that §507(a) does not apply to payments made by a §4947(a)(2) split-interest trust as directed by its document.[737]

---

[728] Prop. Reg. §1.1411-3(d)(2)(ii)(C)(2).

[729] *See* Prop. Reg. §1.1411-3(d)(2)(ii)(B).

[730] Prop. Reg. §1.1411-3(d)(2)(iii) *Ex.* 2(ii).

[731] Preamble to REG-130843-13, 78 Fed. Reg. 72,451 (Dec. 2, 2013).

[732] For detailed discussions of the applicable private foundation rules, see 470 T.M., *Private Foundations — Self-Dealing (Section 4941)*; 473 T.M., *Private Foundations — Excess Business Holdings (Section 4943)*; 458 T.M., *Private Foundations and Public Charities — Termination and Special Rules (Sections 507 and 508)*; 474 T.M., *Private Foundations — Taxable Expenditures (Section 4945)*; and 468 T.M., *Private Foundations — Investment Income Tax and Jeopardy Investments (Sections 4940 and 4944).*

[733] In PLR 201713003 and PLR 201713002, the IRS interpreted the "in the absence of proof to the contrary" language to rule that two CRUTs would not be §4947(a)(2) split-interest trusts, even though a deduction was allowable, because the taxpayer satisfactorily established that no deduction had, in fact, been taken. The IRS noted that the taxpayer would need to continue to maintain records sufficient to establish that no deduction is taken over the life of the CRUTs to avoid subsequent application of §4947(a)(2). In the IRS's annual no rulings list, the IRS continues to include the following as an area in which rulings or determination letters will not be issued: "Whether a split-interest trust is described in §4947(a)(2) because it has no amounts in trust for which a deduction was allowed under §170, 545(b)(2), 642(c), 2055, 2106(a)(2), or 2522." Rev. Proc. 2026-3, §4.01(66). *See also* PLR 201831009 (testamentary trust, for which QTIP election was made and that would distribute income and principal to surviving spouse during life and remainder to charitable foundation upon surviving spouse's death, would not be §4947(a)(1) or §4947(a)(2) trust subject to private foundation rules (i) during spouse's lifetime as long as no charitable deduction would be allowable prior to spouse's death, and (ii) for reasonable period of settlement following surviving spouse's death).

[734] Reg. §53.4947-1(c)(1)(iii).

[735] Reg. §53.4947-2(b)(1).

[736] Reg. §53.4947-2(b)(1)(ii).

[737] Reg. §53.4947-1(e)(1).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Therefore, the vast majority of CRTs are only subject to the following private foundation provisions: §508(e) (relating to governing instruments), §4941 (relating to taxes on self-dealing), and §4945 (relating to taxes on taxable expenditures).

a. Section 508(e) — Governing Language Requirement

The sample documents provided by the IRS include the language necessary for meeting all the requirements of §508(e) as applicable to charitable remainder trusts.[738]

Section 508(d)(2) disallows income, gift, and estate tax charitable deductions for gifts made to a trust described in §4947 that fails to satisfy the "governing instrument" language requirements of §508(e). Section 508(e) provides that the governing instrument of a private foundation must require the foundation to distribute income in such a way as to avoid the excise tax imposed on undistributed income under §4942. In addition, the governing instrument must prohibit the foundation from: (1) engaging in any act of self-dealing (as defined in §4941(d)); (2) retaining any excess business holdings (as defined in §4943(c)); (3) making investments in such a manner as to subject the foundation to tax under §4944; and (4) making any taxable expenditures (as defined in §4945(d)).

The governing instrument of a private foundation will satisfy the §508(e) language requirements, regardless of whether the appropriate language is used, if applicable state law either requires the foundation to operate in conformity with the mandatory language or deems that the language is contained in the terms of the governing instrument.[739]

Practice Tip: Drafters should include the required §508(e) language in the governing instrument of all CRTs, and the IRS has provided sample language to satisfy §508(e).[740]

b. Section 4941

The private foundation provision most likely to cause problems for donors and their professionals is §4941: the prohibition against self-dealing. This section is not a full analysis of §4941; rather, it focuses on the rules, and the exceptions to those rules, most applicable to CRTs.[741] For purposes of these rules, a CRT is treated as a private foundation.

The essence of §4941 is that certain transactions between "disqualified persons" and CRTs are subject to penalties[742] and must be undone. This penalty is not waivable, not even for reasonable cause.[743] The trustee of the trust who permits the transaction can also be subject to penalties,[744] although the trustee can avoid the trustee penalties for reasonable cause[745] or reliance on the advice of counsel.[746]

Practice Point: It is imperative that any trustee, especially the donor as trustee, understand and accept these rules. Because the penalty is not waivable for reasonable cause, the trustee must understand that even unintentional "foot-faults" are subject to these penalties.

Section 4947(a)(2)(A) states that the private foundation provisions enumerated in §4947(a)(2) do not apply to any amounts payable under the terms of a CRT to income beneficiaries unless a deduction was allowed for such amounts under §170(f)(2)(B), §2055(e)(2)(B), or §2522(c)(2)(B).[747] For example, payments by a qualified CRT to a noncharitable income beneficiary are not subject to the self-dealing provisions of §4941 or the taxable expenditure provisions of §4945 because no deduction was allowed for that payment.

Section 4941 imposes a two-tier excise tax on the amount involved in certain acts of self-dealing between the private foundation and "disqualified persons."[748] The initial tax is imposed at a rate equal to 10% of the amount involved and is payable by the disqualified person who participates in the act of self-dealing.[749] In some cases, an additional tax equal to 5% of the amount involved is imposed on participating "foundation managers" (e.g., trustees, in the case of a CRT).[750] If the act of self-dealing is not "corrected," the disqualified person is subject to a so-called second-tier excise tax imposed at a rate equal to 200% of the amount involved.[751] In such case, a foundation manager who refuses to correct the act of self-dealing is subject to a second-tier excise tax equal to 50% of the amount involved.[752]

Acts of self-dealing include: (1) the sale,[753] exchange, or lease of property between a private foundation and a disqualified person; (2) the lending of money or other extension of credit between a private foundation and a disqualified person; (3) the furnishing of goods, services, or facilities between a private foundation and a disqualified person; (4) the payment of compensation (or payment or reimbursement of expenses) by a private foundation to a disqualified person; (5) the transfer to, or for the benefit of, or use by, a disqualified person of the income or assets of a private foundation;[754] and (6) the agreement by a private foundation to make any payment of money or oth-

[738] See Worksheet 2 for the list of Revenue Procedures with sample documents.

[739] Reg. §1.508-3(d)(1).

[740] *See* Pub. 557, *Tax-Exempt Status for Your Organization. See also* Rev. Rul. 2024-10, *obsoleting* Rev. Rul. 75-38.

[741] See 470 T.M., *Private Foundations — Self-Dealing (Section 4941).*

[742] §4941(a)(1), §4941(b)(1).

[743] §4962(b).

[744] §4941(a)(2), §4941(b)(2).

[745] Reg. §53.4941(a)-1(b)(5).

[746] Reg. §53.4941(a)-1(b)(6).

[747] *See also* Reg. §53.4947-1(c)(2)(i).

[748] "Disqualified person" is defined in §4946.

[749] §4941(a)(1), *amended by* the Pension Protection Act of 2006, Pub. L. No. 109-280, §1212(a)(1), effective for taxable years beginning after August 17, 2006. For taxable years beginning on or before that date, former §4941(a)(1) imposed the tax at a rate of 5%.

[750] §4941(a)(2), *amended by* Pub. L. No. 109-280, §1212(a)(1), effective for taxable years beginning after August 17, 2006. For taxable years beginning on or before that date, former §4941(a)(2) imposed the tax at a rate of 2½%.

[751] §4941(b)(1).

[752] §4941(b)(2).

[753] In PLR 8846058, the IRS ruled that trust assets transferred to the noncharitable unitrust recipient in satisfaction of the unitrust amount came within the §4947(a)(2)(A) exception and, therefore, were not subject to the §4941 excise tax imposed on self-dealing.

[754] *See* Notice 94-78. The IRS stated that the sale of the assets of a CRT, even if not to a disqualified person, could be self-dealing if the purpose of the sale was to benefit a disqualified person. In the example in the Notice, the trustee deferred the sale of appreciated assets contributed to the trust so that the trust would have no income in its initial year. This had the effect of benefiting the grantor, who was also the unitrust beneficiary, by making the initial unitrust payment a tax-free return of corpus. The result in the Notice was overruled by Reg. §1.643(a)-8. *See* preamble to T.D. 8926, 66 Fed. Reg. 1034 (Jan. 5, 2001). See also PLR 9522021, where the IRS ruled (before the 1998 change to the regulations) that the "flip" of a CRUT would result in self-dealing.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

er property to a government official.[755] There are exceptions to these rules, which are discussed in VI.G.2., below.[756]

> *Example:* Private foundation P owns the controlling interest of the voting stock of corporation X, and as a result of such interest, elects a majority of the board of directors of X. Two of the foundation managers, A and B, who are also directors of corporation X, form corporation Y for the purpose of building and managing a country club. A and B receive a total of 40% of Y's stock, making Y a disqualified person with respect to P. In order to finance the construction and operating of the country club, Y requested and received a loan in the amount of $4 million from X. The making of the loan by X to Y shall constitute an indirect act of self-dealing between P and Y.

Disqualified persons include the donor, his or her spouse, certain family members, the trustee of the CRT, and entities in which these individuals have certain levels of ownership or control.[757] "Family members" does not include siblings, in-laws, nieces or nephews, cousins, or other more remote relatives.

Practice Point: The relatively narrow definition of "family member" may provide opportunities for transactions within an extended family group that would be precluded for the donor. Of course, all transactions must be at fair market value.

The self-dealing prohibition penalizes certain activities regardless of their fairness to the trust. For example, assume that a donor sells stock worth $100,000 to the donor's CRT for $10,000. Although the trust will have benefitted from the transaction, the $10,000 sale is subject to the self-dealing penalty,[758] and the transaction must be corrected.[759] Also, a donor cannot use funds from a CRT to satisfy a charitable pledge; again, that would be self-dealing.[760]

Self-dealing issues can arise in a number of situations, beginning with the initial contribution to the charitable remainder trust. If real estate subject to a mortgage, a partnership with allocated debt, or a life insurance policy subject to a loan, is contributed to the trust, those are bargain sales[761] and would be subject to a penalty unless an exception applies.[762] If the mortgaged property is the initial contribution to the trust, an exception (colloquially referred to as the "first bite" exception) may apply. A transaction is not self-dealing if the disqualified person only becomes disqualified as a result of the transaction;[763] this rule may protect initial transfers to CRTs. (Of course, the exposure to the 100% tax on unrelated business taxable income should also be considered before transferring property subject to debt. See the discussion at VI.C.3., above.)

The second situation in which self-dealing may arise is the sale of the trust's assets. If an interest in a closely held business has been contributed, the logical course to liquidity is to sell that interest — but all the likely purchasers may be disqualified persons. A thorough analysis of the disqualified person status of any potential purchasers should be performed. If there is a logical non-disqualified person purchaser (e.g., sister), then the sale can go forward. If there is no available non-disqualified person purchaser, then the corporate redemption exception discussed at VI.G.2.c., below, should be reviewed.

The third potential situation is investment activities with related parties. During the operation of the trust, any proposed economic transaction between the trust and the donor (or any other disqualified person) must be reviewed. Loans by the trust and lease arrangements between the trust and the donor are subject to the self-dealing penalties (although interest free loans to the trust and free use of office space by the trust are permitted).[764] This question sometimes arises if real estate is donated to a CRT and the donor wants to lease back all or a portion of the property.[765] That is not permissible, even at fair market value rent.

Especially in charitable remainder trusts managed by individuals or by family offices, the question of co-investment often arises. Can a CRT co-invest in the family investment partnership to obtain access to investment diversification? The IRS has issued a number of favorable rulings on this issue. For example, in PLR 200548026, the IRS found that a "co-investment" arrangement between a private foundation and disqualified persons was not a "sale or exchange," and that any benefits derived from the private foundation's participation were incidental and tenuous and, therefore, permissible under the self-dealing rules. The IRS explained that in co-investment situations there is no economic benefit to the other investors and that the ownership or holdings of the other investors does not change in any economic or other material respect.[766] If the

[755] §4941(d)(1).

[756] *See* §4941(d)(2).

[757] §4946(a).

[758] Reg. §53.4941(d)-2(a)(1).

[759] Reg. §53.4941(e)-1(c)(3)(i).

[760] Reg. §53.4941(d)-2(f)(1).

[761] Reg. §53.4941(d)-1(a); *Goodman v. United States*, No. 98-8649, 1999 BL 3162 (S.D. Fla. 1999).

[762] Section 4941(d)(2)(A) provides that the transfer of real or personal property by a disqualified person to a CRT is treated as a sale or exchange if the property is subject to a mortgage or similar lien that the trust assumes, or if such property is subject to a mortgage or similar lien that a disqualified person placed on the property within the 10-year period ending on the date of the transfer. *See also* Rev. Rul. 80-132; PLR 9241064.

[763] Reg. §53.4941(d)-1(a). *See, e.g.,* PLR 202016006–PLR 202016002 (where surviving spouse agreed via settlement agreement to receive present value of her lifetime income interests in multiple QTIP trusts with remainder being distributed to charitable trust, IRS ruled that such transaction would not result in self-dealing because spouse's transfer of remainder interests would cause charitable trust to be subject to §4947(a)(1) and spouse's disqualified person status (as substantial contributor and family member of charitable trust founder) would arise solely as result of settlement agreement).

[764] §4941(d)(2)(B), §4941(d)(2)(C).

[765] In GCM 39445 (July 11, 1985), the Chief Counsel's Office advised that a proposed lease of office space by an estate in the personal residence of the executor's spouse was an act of "indirect self-dealing" where the executor was also the trustee of a CRT funded by the estate. The GCM stated that the proposed lease was an attempt to use the estate as an intermediary to circumvent the self-dealing prohibitions of §4941.

[766] *See also* PLR 200043047 (CRUT's contribution to investment fund of LLC — a disqualified person created by the unitrust's grantors — in exchange for a membership interest constituted neither: (1) a sale or exchange between the unitrust and the LLC, pursuant to §4941(d)(1)(A); nor (2) a transfer to, or use by or for the benefit of, a disqualified person on the income or assets of a private foundation pursuant to §4941(d)(1)(E)). In PLR 201043041, the IRS ruled that a CRUT's formation and operation of a foreign corporation as an investment vehicle was not self-dealing because the corporation — the unitrust's wholly owned subsidiary — was not a disqualified person as to the unitrust. In PLR 9705013, the IRS ruled that participation by each of six CRUTs in an investment partnership was not self-dealing. The IRS did state that later capital contributions by a trust for a larger partnership interest could be acts of self-dealing. The IRS also ruled that participation in the investment partnership did

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

amount is material, the trustee of the trust may decide to seek his or her own ruling.

In various private letter rulings, the IRS has held that division of a CRT and reformation to correct scrivener's errors are not self-dealing. Those rulings are discussed in VII., below, and IV.K.2.e.(3), above, respectively.

c. Section 4945

Section 4945 imposes an excise tax on each "taxable expenditure" made by a private foundation. The term "taxable expenditure" includes amounts paid or incurred by a private foundation: (1) to influence legislation; (2) to influence the outcome of a public election or carry on voter registration drives; (3) as a grant to an individual for travel, study, or other similar purposes (unless the IRS gives advance approval of the foundation's grant-making procedures); (4) as a grant to an organization other than a "public charity" described in §509(a)(1) or §509(a)(2), a public charity described in §509(a)(3) (but not including a supporting organization described in §4942(g)(4)(A)(i) or §4942(g)(4)(A)(ii)), or an "exempt operating foundation" described in §4940(d)(2),[767] unless the foundation exercises "expenditure responsibility";[768] and (5) for any purpose other than one specified in §170(c)(2)(B).

If a CRT makes an inappropriate disbursement (e.g., pays personal expenses of the donor) the trust would be subject to a 20% penalty under §4945.[769] The trustee could also be subject to a 5% penalty, unless the trustee's action was not willful and was due to reasonable cause.[770]

not result in excess business holdings under §4943, was not a jeopardizing investment under §4944, and did not result in a taxable expenditure under §4945. *See also* PLR 200423029 (co-investment by 10 CRUTs).

[767] §4945(d)(4)(A), *amended by* the Pension Protection Act of 2006, Pub. L. No. 109-280, §1244(b), §1244(c), effective for expenditures made after August 17, 2006. The nonqualifying §509(a)(3) supporting organizations are: (i) a non-functionally integrated Type III supporting organization as defined in §4943(f)(5) (*added by* Pub. L. No. 109-280, §1243(a)); and (ii) any other supporting organization if a disqualified person of the grant-making private foundation directly or indirectly controls the supporting organization or one of its supported organizations as defined in §509(f)(3) (*added by* Pub. L. No. 109-280, §1241(b)) or if the IRS issues regulations indicating that a distribution (grant) to the supporting organization is inappropriate. *See* §4942(g)(4)(A)(i), §4942(g)(4)(A)(ii), *added by* Pub. L. No. 109-280, §1244(a). Under §4943(f)(5), a "Type III" supporting organization is an organization satisfying the §509(a)(3)(A) and §509(a)(3)(C) requirements and the §509(a)(3)(B)(iii) requirement of operating in connection with one or more §509(a)(1) or §509(a)(2) organizations. Section 4943(f)(5) provides that a Type III supporting organization is "functionally integrated" if it is not required to make payments to supported organizations because the supporting organization's activities are "related to performing the functions of, or carrying out the purposes of, such supported organizations." In 2012 and 2015, the IRS issued final regulations that provide guidance on functionally integrated and non-functionally integrated Type III supporting organizations. *See* T.D. 9605, 77 Fed. Reg. 76,382 (Dec. 28, 2012), effective December 28, 2012; T.D. 9746, 80 Fed. Reg. 79,684 (Dec. 23, 2015), effective December 21, 2015; Reg. §1.509(a)-4(i)(1), §1.509(a)-4(i)(4), §1.509(a)-4(i)(5), §1.509(a)-4(l). In October 2023, the IRS issued final regulations that provides rules on qualification as "functionally integrated" for both new and existing Type III supporting organizations that support governmental supported organizations. *See* Reg. §1.509(a)-4(i)(4)(iv), T.D. 9981, 88 Fed. Reg. 71,287 (Oct. 16, 2023), effective for taxable years beginning on or after October 16, 2023. For a detailed discussion of supporting organizations, see 459 T.M., *Supporting Organizations.*

[768] §4945(d)(4)(B).

[769] §4945(a)(1).

[770] §4945(a)(2).

Example: T gives the residue of his estate in trust for the benefit of D, his daughter, and Y, an organization described in §501(c)(3) and §170(c). A guaranteed annuity interest of $10,000 is to be paid to D for 20 years. In addition, a guaranteed annuity interest of $5,000, which satisfies the requirements for deduction set forth in Reg. §20.2055-2(e)(2)(vi)(a), is to be paid to Y for 20 years. Upon termination of the 20-year term, the corpus is to be distributed to Z, another organization described in §501(c)(3) and §170(c). The trust qualifies as a CRAT and a deduction is allowed under §2055(e)(2)(B) for the value of the annuity to Y and under §2055(e)(2)(A) for the value of the remainder to Z. The assets in the trust are not segregated. (See VI.G.4.a., below.) Because §4945 generally applies to this trust, if Y becomes a private foundation the trust will be required to exercise "expenditure responsibility" over the annuity it pays to Y. Under §4947(a)(2), the trust is treated as a private foundation. If Y is, or becomes, a private foundation, the exception to the grant-expenditure-responsibility requirements for grants from private foundations to public charities will not apply.[771] On the other hand the amounts paid to D are not subject to §4947(a)(2) or §4945 because no deduction is allowed for such amounts.[772]

As noted in VII.A., below, Rev. Rul. 2008-41 provides guidance, including guidance under §4945, on the pro rata division of a charitable remainder trust into separate charitable remainder trusts. The IRS concluded that the division of a CRT under the facts in Situations 1 and 2 of the ruling, as described in VII.A., below, does not constitute a taxable expenditure. The IRS explained that the transfer of the original trust's assets to the separate trusts will not be expenditures that require the original trust to exercise expenditure responsibility pursuant to Reg. §1.507-3(a)(9) if the original and separate trusts are controlled by the same person(s), or to Reg. §1.507-3(a)(7) if the original and separate trusts are not controlled by the same person(s). Because the original trust made no prior distributions requiring expenditure responsibility, the IRS noted, the separate trusts will assume no preexisting expenditure responsibility. The IRS indicated that a similar analysis applies to the subsequent consolidation of a separate trust in Situation 1 upon the death of an individual annuity or unitrust beneficiary.

2. Selected Exceptions to Self-Dealing

Section 4941(d)(2) carves out some very specific exceptions to self-dealing, a number of which may apply to charitable remainder trusts (CRTs). Although an in-kind payment of the annuity or unitrust amount would be treated as a sale, such a transaction is not subject to self-dealing.[773]

One exception the IRS has carved out relates to the division of a CRT. As discussed in VII.A., below, a CRT divided for divorce or similar reason is not subject to self-dealing penalties.[774]

[771] Reg. §53.4945-5(a)(1).

[772] Reg. §53.4947-1(c)(2)(ii) *Ex.* (2).

[773] §4947(a)(2)(A); PLR 8846058.

[774] Rev. Rul. 2008-41.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

a. Interest-Free Loans to a Charitable Remainder Trust

The lending of money or other extension of credit by a disqualified person to a private foundation is not an act of self-dealing if the loan or other extension of credit is without interest or other charge (determined without regard to foregone interest described in §7872) and if the proceeds of the loan are used exclusively for purposes specified in §501(c)(3).[775] It would be unusual for a CRT to need funds for "purposes specified in §501(c)(3)." However, the regulations[776] and several rulings[777] only require that the loan be without interest.

If the donor decides to loan funds to a CRT, the imputed interest rules of §7872 may apply. Although the IRS has addressed imputed interest privately,[778] it is not clear whether a charitable contribution would be allowed for any portion of the imputed interest.

b. Provision of Goods, Services, or Facilities

A disqualified person may provide goods, services, or facilities to a CRT without charge.[779] Also, a CRT may pay reasonable compensation for personal services (but not goods or facilities) to a disqualified person.[780] Personal services can include trustee fees and investment management fees.[781] If the donor or another disqualified person is to be paid investment advisory or trustee fees, documentation should be retained to support how the fees were determined to be reasonable and necessary.

c. Corporate Restructuring Exception

One additional exception, the corporate restructuring exception, may apply to CRTs that own closely held stock. Under §4941(d)(2)(F), any transaction between a CRT and a corporation that is a disqualified person will not be self-dealing if done pursuant to a liquidation, merger, redemption, recapitalization, or other corporate adjustment, organization, or reorganization, so long as all of the securities of the same class as held (prior to the transaction) by the trust are subject to the same terms and such terms provide for receipt by the foundation of no less than fair market value.[782] For this purpose, all securities are not subject to the same terms unless, pursuant to the transaction, the corporation makes a bona fide offer on a uniform basis to the foundation and every other person who holds these securities.[783] The IRS has applied §4941(d)(2)(F) even where it is clearly anticipated that only the trust will accept a corporation's redemption offer made to all shareholders on a uniform basis.[784] Such redemptions must be for cash, not a note, because a note would be an extension of credit and, thus, not covered by the exception.[785]

> *Example:* X owns 60 shares of the stock in a closely held company. Her children own the remaining 40 shares. As part of a succession plan, X transfers 40 of her shares to a CRT. Pursuant to the restructuring exception, the company offers to redeem any shares that the shareholders should desire to have redeemed. Only the trust accepts the offer. After the redemption, X owns 20 shares and her children own 40. X has reduced her ownership from a majority to a minority interest, the CRT can serve as a supplemental retirement fund, and X is entitled to a charitable income tax deduction.

Although the Code limits the restructuring exception to corporations, the IRS has occasionally extended the exception to partnerships.[786] Given the lack of clear statutory authority, a trust contemplating a partnership transaction may deem it prudent to obtain its own ruling.

d. Estate Administration Exception

This exception to self-dealing only applies to transactions during the period of estate administration (or the winding up of a formerly revocable trust). This exception is discussed at V.B., above, as it would only apply to testamentary CRTs.

3. Additional Rules if a Charity Receives a Portion of the Unitrust or Annuity Payment

The excess business holdings provisions of §4943 and the "jeopardy investment" provisions of §4944 do not apply to a split-interest trust if either: (1) all of the income interests of the trust are (and none of the remainder interests of the trust is) devoted solely to charitable purposes, and all amounts in trust for which a charitable deduction was allowed have an aggregate value of not more than 60% of the aggregate fair market value of all amounts in trust;[787] or (2) a charitable deduction was allowed for amounts payable under the terms of the trust to every remainder beneficiary but not to any income beneficiary,[788] as is the case with the majority of charitable remainder trusts. Exception (1) is only relevant to charitable lead trusts. If a charity is receiving a portion of the annuity or unitrust payment, then exception (2) will not apply because a charitable gift or estate tax deduction will have been allowed for the value of the charitable interest. As this is a relatively rare situation, only a brief summary of §4943 and §4944 are presented here.[789]

Section 4943 imposes an excise tax on the value of the "excess business holdings" of any private foundation. A private foundation created after May 26, 1969, has excess business holdings to the extent that it, together with all disqualified persons, own in the aggregate more than 20% of the voting stock of an incorporated business enterprise (or corresponding

[775] §4941(d)(2)(B).

[776] Reg. §53.4941(d)-2(c)(2).

[777] PLR 200116047 (travel costs), PLR 9210025 (investments).

[778] In PLR 200503004, the IRS addressed the income tax consequences of interest-free loans by a disqualified person to a private foundation. The IRS ruled that: (1) such loans cause the lender to recognize gross income from §7872 imputed interest; (2) the lender's imputed interest income is §163(d)(4)(B)(i) investment income; and (3) any interest paid by the lender on a line of credit used to fund the loans is §163(d)(3)(A) investment interest.

[779] §4941(d)(2)(C).

[780] §4941(d)(2)(E).

[781] Reg. §53.4941(d)-3(c).

[782] Reg. §53.4941(d)-3(d)(1).

[783] Reg. §53.4941(d)-3(d)(1).

[784] PLR 200720021, PLR 9338046.

[785] Reg. §53.4941(d)-3(d)(2) *Ex.* (2).

[786] PLR 200734023, PLR 9237032; FSA 200015007.

[787] §4947(b)(3)(A).

[788] §4947(b)(3)(B).

[789] For detailed discussions of the applicable private foundation rules, see 473 T.M., *Private Foundations — Excess Business Holdings (Section 4943)*, and 468 T.M., *Private Foundations — Investment Income Tax and Jeopardy Investments (Sections 4940 and 4944).*

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

interests in unincorporated business enterprises).[790] In general, where a private foundation acquires excess business holdings by gift or bequest, the foundation has five years from the date it acquires such holdings to dispose of them.[791] Section 4943 is generally not applicable to qualified CRTs. However, a CRT that is subject to the excess business holding rules may not take advantage of the exemption under §4943(g) for certain private foundations, because §4945(g)(5) specifically excludes charitable trusts and split-interest trusts.[792]

Section 4944 imposes an excise tax on a private foundation (and under some circumstances foundation managers) for investing any amount in such a manner as to jeopardize the carrying out of the foundation's exempt purposes.[793] The imposition of an excise tax on "jeopardy" investments is intended to assure that the foundation managers adopt a "prudent person" approach toward the investment of foundation assets.

4. *Exception to Private Foundation Rules for Segregated Amounts and Pre-1969 Trusts*

a. *Segregated Amounts*

Section 4947(a)(2)(B) provides that the private foundation provisions do not apply to "any amounts in trust other than amounts for which a deduction was allowed under section 170, 545(b)(2), 642(c), 2055, 2106(a)(2), or 2522, if such other amounts are segregated from amounts for which no deduction was allowable."[794] For purposes of this provision, §4947(a)(3) provides that a trust under which amounts are segregated must separately account for the various income, deduction, and other items properly attributable to each of the segregated amounts.[795] Thus, the segregated portion that is earmarked exclusively for noncharitable income and remainder interests is not subject to the private foundation provisions. The balance of trust assets will be treated either as a §4947(a)(1) charitable trust or as a §4947(a)(2) trust depending on whether it is devoted exclusively to charitable purposes or partially to noncharitable purposes and partially to charitable purposes.

This provision is unlikely to apply to any existing charitable remainder trust drafted after §664 was enacted.

b. *Pre-May 27, 1969, Transfers*

The private foundation rules do not apply to any amounts transferred in trust before May 27, 1969.[796] For this purpose, an amount is considered transferred in trust only if the transfer satisfied the requirements for the allowance of a deduction under §170, §545(b)(2), former §556(b)(2), §642(c), §2055, §2106(a)(2), or §2522 (or the corresponding provisions of prior law).[797] Moreover, income and capital gains derived from amounts transferred in trust before May 27, 1969, also are excluded from the application of the private foundation provisions.[798] The purpose of this rule is to correlate the applicability of §4947(a)(2) with the general effective date of the charitable remainder trust provisions of §664.

Where amounts are transferred to the same trust both before and after May 27, 1969, the amounts transferred before May 27, 1969, are excluded from application of the private foundation rules only if such amounts are accounted for separately. The separate accounting required for this purpose is the same as that discussed above under the §4947(a)(2)(B) "segregation" exception.[799]

For testamentary trusts, amounts are deemed transferred before May 27, 1969, if the transfers are made under the will of a decedent who died before May 27, 1969.[800] In addition, such amounts are deemed transferred in trust before May 27, 1969, if: (1) the trust was created by the will of a decedent who died after May 26, 1969; (2) the will was executed before May 27, 1969; (3) no dispositive provision of the will was amended (within the meaning of Reg. §20.2055-2(e)(4) and (5)) by the decedent after May 26, 1969; and (4) the decedent was, at all times after May 26, 1969, under a mental disability (as defined in Reg. §1.642(c)-2(b)(3)(ii)) and not competent to amend the will, by codicil or otherwise.[801]

H. *Additional Contributions to a Charitable Remainder Unitrust*

Rather than creating an additional unitrust, a donor may contribute additional assets to an existing unitrust if the document permits additional contributions to the unitrust. (No additional contributions may be made to an annuity trust.)[802] This raises three potential issues.

1. *Calculation of Charitable Income and Gift Tax Deduction*

The donor is entitled to a charitable income and gift tax deduction for the value of the property transferred to the trust, reduced by the value of the noncharitable unitrust interest. When the term of the trust is for one or two measuring lives, the calculation follows the methodology shown in IV.H., above. The deduction allowed may be a greater or lesser percent of the value of the property transferred when compared to the percentage allowed for the original contribution. Although one might expect that the increased ages of the noncharitable beneficiaries

---

[790] §4943(c).

[791] For an analysis of whether a pre-1969 CRT was a §4946 disqualified person as to a private foundation for purposes of determining whether the foundation had §4943 excess business holdings, see TAM 200827039, TAM 200827038, TAM 200827037.

[792] §4943(g), *added by* the Bipartisan Budget Act of 2018, Pub. L. No. 115-123, §41110, effective for tax years beginning after December 31, 2017. For a detailed discussion of §4943(g), see 473 T.M., *Private Foundations — Excess Business Holdings (Section 4943)* and 468 T.M., *Private Foundations — Investment Income Tax and Jeopardy Investments (Sections 4940 and 4944).*

[793] The regulations provide that no category of investment is per se a jeopardizing investment, but list the following examples of investments as warranting close scrutiny: "Trading in securities on margin, trading in commodity futures, investments in working interests in oil and gas wells, the purchase of 'puts,' 'calls,' and 'straddles,' the purchase of warrants, and selling short." Reg. §53.4944-1(a)(2).

[794] *See also* Reg. §53.4947-1(c)(3).

[795] *See also* Reg. §53.4947-1(c)(4).

[796] §4947(a)(2)(C).

[797] Reg. §53.4947-1(c)(5)(i).

[798] Reg. §53.4947-1(c)(5)(i).

[799] Not surprisingly, Reg. §1.508-3(e)(2) provides that the governing instrument of a trust that has amounts received both before and after May 27, 1969, may except from the application of the private foundation provisions only those segregated amounts excluded from the application of §4947(a)(2) by §4947(a)(2)(C).

[800] Reg. §53.4947-1(c)(5)(iii).

[801] Reg. §53.4947-1(c)(5)(iii).

[802] Reg. §1.664-2(b).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

would result in an increased deduction, changes in interest rates since the original funding also affect the calculation.

If the trust is for a term of years, a special calculation may be required to determine the correct charitable deduction unless the donor transfers property on (or close to) the anniversary date of the trust.[803] If the software used for the deduction calculation does not accommodate a fractional year, see IRS Publications 1457 and 1458.

2. *Calculation of the Noncharitable Payment for the Year of the Contribution*

As one would expect, a mid-year addition to a unitrust does not entitle the donor to a full year's worth of unitrust payments based on the additional contribution. Both the regulations and the IRS sample documents[804] describe the method that is to be used to calculate the unitrust payment in the year of the contribution.

A governing instrument permitting additional contributions must provide that where no valuation date occurs after the date of the contribution and during the taxable year in which the contribution is made, the additional property is valued as of the time of the contribution. Further, the governing instrument must provide that the unitrust amount is computed by multiplying the fixed percentage by the sum of: (i) the net fair market value of the trust assets (excluding the value of the additional property and any income earned therefrom and any appreciation on such property after its contribution); and (ii) that proportion of the value of the additional property (that was excluded under (i)) which the number of days from the date of the contribution to the earlier of the last day of the taxable year or the last day of the payout period bears to the number of days from the first day of the taxable year to the earlier of the last day of the taxable year or the last day of the payout period.[805]

Example 1: On March 2, 20X1, B makes an additional $5,000 contribution to a CRUT. The regular valuation date is January 1 of each year. The fixed percentage is 5%. Between March 2, 20X1, and December 31, 20X1, the additional property earns $250 in income. Because the regular valuation date for the year of contribution occurs before the date of the additional contribution, the additional contribution, without the income earned on it, is valued on the date of contribution (Mar. 2, 20X1). Thus, the required payout applicable to the additional contribution for the year of contribution is $209 (5% × $5,000) × (305 ÷ 365).[806]

Example 2: On July 1, 20X1, B makes an additional contribution of $10,000 to a CRUT. The taxable year of the trust is a calendar year, and the regular valuation date is December 31 of each year. The fixed percentage is 5%. Between July 1, 20X1 and December 31, 20X1, the additional property appreciates in value to $12,500 and earns $500 of income. Because the regular valuation date for the year of contribution occurs after the date of the additional contribution, the additional contribution, including income earned by it, is valued on the regular valuation date. Thus, the required payout applicable to the additional contribution is $327 (5% × ($12,500 + $500)) × (184 ÷ 366).[807]

3. *If the Additional Contribution Fails the Minimum 10% Remainder Requirement*

Although in a perfect world this would not happen, an additional contribution to a unitrust may fail the requirement that the charitable interest be at least 10% of the amount contributed. If the number is close, the election to use one of the two previous months' §7520 rate could increase the remainder value to 10%. Note, however, that this is unlikely to occur with a unitrust because interest rates have very little effect on the valuation of the remainder. This election is discussed at IV.H.5., above.

If an additional contribution to a unitrust fails the 10% requirement, then the additional contribution will be treated as a separate trust.[808] The effect of this splitting of the trust is that, while the new contribution would not qualify under §664 or §170, the existing trust would not lose its qualification. This situation could occur when an additional contribution is made to a unitrust that was established before the effective date of the 10% requirement.[809] A similar situation could occur when an additional contribution is made to a post-July 28, 1997, unitrust that satisfied the 10% requirement when established but no longer does because a change in the §7520 rate has caused the remainder interest to fall below 10% as a result of the additional contribution.

[803] Reg. §1.664-4(e), T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (effective June 1, 2023).

[804] See Worksheet 2 for the list of Revenue Procedures with the sample documents.

[805] Reg. §1.664-3(b)(1), §1.664-3(b)(2).

[806] Reg. §1.664-3(b)(2) *Ex.* (1).

[807] Reg. §1.664-3(b)(2) *Ex.* (2), adjusted for a leap year calculation.

[808] §664(d)(4).

[809] H.R. Conf. Rep. No. 105-220, at 608 (1997). In PLR 200245058, the IRS ruled that a CRUT was not disqualified under §664 by provisions: (i) permitting the downward adjustment of the unitrust amount for additional contributions to ensure that the value of the remainder interest for the addition was at least 10% of the value of the addition, as long as the total unitrust amount for the addition did not fall below 5%; and (ii) requiring that the trustee reject an additional contribution that would fail the 10% test after a downward adjustment of the unitrust amount. The IRS stated that these provisions complied with §664(d)(2)(D) and §664(d)(4) because they treated the addition as a separate trust. The ruling did not indicate when the unitrust was established. These provisions are not included in the sample IRS documents.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

VII. Dividing a Charitable Remainder Trust

A. *Dividing a Charitable Remainder Trust Due to Divorce or Similar Reason*

When a divorcing couple are beneficiaries of a charitable remainder trust (CRT), they will often want to divide the CRT as part of the divorce process. Perhaps they want different investment strategies or trustees, or perhaps they simply want to avoid dealing with each other. The former spouses, if they have taxable estates, will want to avoid a situation where the CRT is included in a decedent's taxable estate but no marital deduction is allowed for a successor income interest. Whatever the reason, the IRS has been accommodating by allowing the division of such trusts with a minimum of income, excise, and gift tax consequences. The division does not have to be related to a divorce, although that is often the trigger for the division.

In Rev. Rul. 2008-41, the IRS ruled that the division of a CRT under the facts in Situations 1 and 2 of the ruling, as described below: (1) does not cause the original trust or any of the separate trusts to fail to qualify as CRTs under §664(d); (2) is not a sale, exchange, or other disposition producing gain or loss, the basis under §1015 of each separate trust's share of each asset is the same share of the basis of that asset in the hands of the original trust immediately before the division, and each separate trust's §1223 holding period for an asset transferred from the original trust includes the original trust's holding period for that asset immediately before the division; (3) does not cause a §507(a)(1) termination of the §4947(a)(2) status of the original trust or result in the imposition of a §507(c) tax; (4) does not constitute an act of self-dealing under §4941; and (5) does not constitute a taxable expenditure under §4945.[810]

In Situation 1 of Rev. Rul. 2008-41, a CRT has two or more individual beneficiaries who each receive an equal portion of the unitrust or annuity amount annually for life. Upon an individual's death, each surviving individual will receive an equal share of the deceased individual's annuity or unitrust amount for life. Upon the last surviving individual's death, the remaining assets will be distributed to charity. The original trust has no liability for chapter 42 excise taxes and has made no distributions to charity. A state court approved a pro rata division of the original trust into separate and equal CRTs (of the same type as the original trust) for each individual beneficiary with the same charitable remainder beneficiaries as the original trust. Each asset of the original trust will be divided equally among the separate trusts.[811] Each separate trust will be deemed to have an equal share of the original trust's income in each §664(b) class and category. The individual beneficiaries will pay all costs of the division. When an individual dies, the assets of his or her separate trust will be divided pro rata among the surviving individual beneficiaries' trusts and, therefore, will increase the survivors' annuity or unitrust amounts. The separate trusts may have different trustees and will be administered independently (and, thus, annual unitrust payments from separate unitrusts could vary). Upon the last surviving individual beneficiary's death, his or her separate trust will terminate and the remaining assets will be distributed to charity. All beneficiaries will be entitled to the same amount before and after the division. Except as indicated, each separate trust will have the same governing provisions as the original trust.

The facts in Situation 2 of Rev. Rul. 2008-41 are the same as in Situation 1 except that the only individual beneficiaries of the original trust are a husband and wife (both U.S. citizens) in the process of getting a divorce, the separate trusts will terminate upon the death of the individual beneficiary of each trust, and the remaining assets of each trust will be distributed to charity at that time. Because the charities will receive half the original trust's assets at each spouse's death (rather than all at the surviving spouse's death), the value of the remainder interest after the division may be greater than it was before the division. However, no additional charitable deduction is permitted. Although each spouse will be entitled to receive the same share of the annuity or unitrust amount after the division as before, each spouse will relinquish all survivorship interests he or she had in the original trust.

In concluding that the division does not cause any of the CRTs to fail to qualify under §664(d), Rev. Rul. 2008-41 notes that the original trust's assets will be divided on a pro rata basis among the separate trusts, which will have the same governing provisions (except as noted) and, collectively, the same beneficiaries as the original trusts. In Situation 1, the IRS observed, the annuity or unitrust amount to be paid annually will remain the same and each beneficiary will have essentially the same beneficial interest after as before the division. The IRS stated that a transfer of assets from a deceased individual beneficiary's separate trust to the other trusts will not be treated as a transferred remainder interest that would violate §664(d)(1)(C) or §664(d)(2)(C) or a prohibited additional contribution to an annuity trust. In Situation 2, the IRS explained, the total annuity or unitrust amount payable will be the same after as before the division, except for the survivorship interest of the surviving spouse.

Rev. Rul. 2008-41 did not discuss another manner in which the trusts might have been divided. Rather than divide the trust between the spouses into two trusts of equal value, the trust might be divided into two one-life trusts, each with a value equal to the spouse's actuarial value in the trust before the division. In that case, the trust for the younger spouse will be larger than the trust for the older spouse. The calculation can be done with IRS published tables. The first step is calculation of the right to receive one half of the total payment until the first to die of the two beneficiaries. The second step is a calculation of the right of beneficiary X to the entire payment for such period as beneficiary X survives beneficiary Y. The third step is a calculation of the right of beneficiary Y to the entire payment for such period as beneficiary Y survives beneficiary X. One reason to consider a division in this manner is in a case when the division is not incident to a divorce under §1041 — for example where the division was not done before the six-year an-

[810] For a more complete discussion of the application of the private foundation rules to CRTs, see VI.G., above.

[811] Rev. Rul. 2008-1 involves the division of a CRT where the assets are divided equally on an asset by asset basis. In the more common case, CRT assets may be divided on a pro rata basis with each new trust receiving assets with an equal aggregate basis. Such a division should also be allowed with a minimum of income, excise, and gift tax consequences. *See* Rev. Rul. 81-292; Carlyn S. McCaffrey, Linda J. Ravdin, Scott L. Rubin, *Structuring the Tax Consequences of Marriage and Divorce After the 2017 Tax Act*, 53 U. Miami Heckerling Inst. on Est. Plan., Session I-B (2019).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

niversary of the divorce.[812] If the division is not done on actuarial basis the parties may have gain on the division.

Before Rev. Rul. 2008-41, taxpayers obtained a number of private letter rulings approving their division of their CRTs. It is no longer necessary (or even possible) to obtain a ruling if the desired facts and outcome match either Situation 1 or 2 in the revenue ruling. However, if the facts or desired outcome are different, obtaining one's own ruling may be advisable. Some rulings may be of interest:

- Change of income rights between the parties: In PLR 201029002 (community property),[813] the IRS approved a divorce-related division of a charitable remainder unitrust (CRUT) into separate unitrusts for each spouse. Funding would be based on the percentage of assets attributable to each spouse's contribution to the original unitrust and with same terms as original, except that the husband's interest would be significantly reduced because he received the entire unitrust amount for life under the original trust, and the wife's interest would be significantly increased because she received the unitrust amount under the original trust only if she survived her husband and he did not revoke her interest. The IRS also ruled that: (1) were it not for application of the §1041 exception for transfers incident to divorce, the spouses would have recognized gain or loss under §1001 because they had materially different rights and entitlements after the division; (2) the new unitrusts determined their bases in assets under §1015 by reference to the original unitrust's bases; (3) pursuant to §1223, the new unitrusts' holding periods for assets included periods for which the original unitrust held assets; (4) each spouse would be treated as transferor of his or her respective unitrust assets for §2036 purposes; (5) each spouse's unitrust would be included in his or her respective estate under §2036 if that spouse retained income and charitable beneficiary designation rights at death; (6) each estate would be entitled to a §2055 charitable deduction for the value of the remainder interest passing to charity; and (7) based on principles of *Harris v. Commissioner*,[814] and the divorce court's order effectuating division of the original unitrust, the division did not cause either spouse to make taxable gift.

- Make-up account in NIMCRUT: In PLR 200045038, the IRS approved a divorce-related division of a net income with make-up charitable remainder unitrust (NIMCRUT), which a court had authorized to convert into a standard unitrust, into two standard unitrusts funded with unequal amounts of assets from the original trust. In PLR 200035014, the IRS approved a divorce-related division of NIMCRUT into two separate NIMCRUTs funded with pro rata amounts of the original trust's assets and an accumulated deficiency make-up account.

- Payment of legal fees by the CRT: In PLR 200616008, the IRS ruled that the payment from trust assets of reasonable legal fees and other expenditures incurred by a CRT to effectuate the division of the trust into two separates trusts after the divorce of the taxpayers would not constitute an act of self-dealing under §4941 or a taxable expenditure under §4945. PLR 201029002 includes a similar ruling under §4945.

B. Dividing a Charitable Remainder Trust in Order to Donate a Portion to Charity

There are times when a charitably motivated income beneficiary of a charitable remainder trust (CRT) may be willing to relinquish a portion of his or her CRT in order for the charity to benefit immediately rather than waiting to the end of the CRT term. The motivation may be lifetime recognition by the charity, a willingness to share unexpected investment success within the trust, a financial crisis at the chosen charity, or other charitable motive. If the income beneficiary desires a charitable income tax deduction for relinquishing a portion of his or her income interest, this "divide and donate" process is necessary. If the beneficiary is indifferent to the income tax deduction, then a distribution of a portion of the trust corpus to the charity is much more straightforward. See VI.C.4., above, for that technique.

In PLR 200808018, the IRS ruled that the division of a net income with make-up charitable remainder unitrust (NIMCRUT) into two trusts, followed by the contribution of the income interest in one of the resulting trusts to the charitable remainder beneficiary (which caused a merger of interests and termination of that trust), did not disqualify the remaining trust under §664, did entitle the grantor/income beneficiary to income and gift tax charitable deductions, and did not cause the grantor/income beneficiary to recognize any income on prior capital gains realized by the unitrust, provided that the original unitrust assets were divided between the two new unitrusts in a manner fairly representative of the aggregate adjusted bases of the unitrust assets and on a pro rata basis as to each major class of investments held by the original unitrust on the division date (with the assets within each class divided in a manner fairly representative of the overall appreciation/depreciation of the assets in the class). PLR 200524014 and PLR 200140027 reached similar results.

Practice Point: If following the format of these rulings, review state law regarding merger of interests. As discussed in the rulings, a merger of interests is needed to avoid a split interest problem under Reg. §1.170A-6(a)(2).

The IRS ruled in PLR 200205008 that the recipient's gift of an undivided portion of her unitrust interest in a CRUT to one of the charitable remainder beneficiaries qualified for the income and gift tax deductions. However, because the trust in PLR 200205008 was a NIMCRUT, the deduction was limited, for both income and gift tax purposes, to the lesser of: (1) the present value of the recipient's right to receive the unitrust amount; and (2) the present value of the recipient's right to receive income for life. See PLR 9550026 for an earlier ruling in which the deduction for a donation of a NIMCRUT interest was not so limited. The 2015 amendment to §664(e) allows donors

[812] Reg. §1.1041-1T.

[813] *See* PLR 200502037 (similar). See also PLR 201648009, PLR 201648008, and PLR 201648007 for more recent rulings.

[814] 340 U.S. 106 (1950).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

to ignore the net income limitation in valuing donated interests in NIMCRUTs, giving donors the results in the 1995 ruling.[815]

A qualified appraisal may be required if the donor desires an income tax deduction even if the trust corpus consists of only cash and publicly traded securities, the item being donated is an interest in a trust and not the underlying assets of the trust. Therefore, the exception for donations of publicly traded securities[816] is arguably not met, and an appraisal is required under the letter of the law.[817]

Comment: There are good arguments that an appraisal should not be required if the trust only holds assets that would not require an appraisal on donation. However, based on the author's informal conversations with the IRS, the IRS does not share that point of view.

Practice Point: All of the rulings mentioned in this section involved transfers of interests to public charities described in §170(b)(1)(A). If the income interest is to be donated to a private foundation described in §170(c) but not §170(b)(1)(A), the income tax deduction may be limited under §170(e)(1)(B)(ii). Although the income interest is a capital asset, the basis of a term interest is zero under §1001(e)(1). Therefore, even though the charitable gift tax deduction is allowed for a donation of an income interest to a private foundation, no income tax deduction is allowed (unless the foundation qualifies as an operating foundation[818] or makes a conduit election).[819]

[815] Protecting Americans from Tax Hikes Act of 2015, Pub. L. No. 114-113, effective for trust terminations after December 18, 2015.

[816] Reg. §1.170A-16(d)(2)(i) (cross referencing Reg. §1.170A-13(c)(7)(xi)).

[817] Reg. §1.170A-17(a), applicable for charitable contributions made on or after January 1, 2019. See also Reg. §1.170A-13(c)(3) for charitable contributions made prior to January 1, 2019.

[818] §170(b)(1)(F)(i).

[819] §170(b)(1)(F)(ii).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

VIII. Terminating a Charitable Remainder Trust

A. *Winding up at the End of the Trust Term*

If the last noncharitable interest in a charitable remainder trust (CRT) has terminated, and the charitable beneficiaries have become entitled to distributions of corpus, the trust continues to be treated as a CRT until it is considered terminated under Reg. §1.641(b)-3(b).[820] From the time it is considered terminated, the trust is treated as a §4947(a)(1) charitable trust until final distribution of all net assets to or for the benefit of the charitable beneficiaries.[821] Treatment of the trust as one described in §4947(a)(1) should be avoided, if possible, because all the private foundation provisions apply to such a trust (unless it applies for, and receives, recognition of exemption as a public charity such as a "supporting organization" pursuant to §509(a)(3)).[822]

Once the noncharitable interest has terminated, the trustee will normally either liquidate the trust assets and transfer cash to the remainder beneficiary, or transfer assets in kind. Most of the time, this process takes only a few weeks, especially if the remainder charity has been serving as the trustee. The trust will be considered terminated even if the trustee reserved sufficient funds to cover final expenses (e.g., tax returns).[823] However, not all trusts are wound up so smoothly. Among the reasons that distribution may be delayed are the following:

- The trust owns illiquid assets that the remainder interest holder does not want to receive. For example, some investment funds only allow quarterly redemption, after the quarterly appraisals are complete. Or, the trust may be invested in a family investment partnership, so the family must develop an exit strategy that works within the self-dealing restrictions of §4941.

- There is a dispute or lack of clarity regarding the correct charity to receive the remainder interest. This can occur if the donor uses the name of a chapter of a charity, and that chapter no longer exists or uses a name that could include several legal entities. For example, does "Girl Scouts" mean the local troop or the national organization?

- Relatives of the donor are suing because they believe the trust should not have been established at all.

- The trust is included in a taxable estate, and the trustee is being cautious about potential exposure to transfer taxes and, therefore, wants to wait for the IRS closing letter before making final distributions.

- If the issue delaying the final distribution causes the trust to continue beyond the end of the year in which the noncharitable interest terminates, the trustee should be ready to explain the issue to the IRS in an attachment to the return for the subsequent year.

1. *Income Tax Reporting for the Final Year of the Trust*

Certain additional information is required on the final Form 5227, *Split-Interest Trust Information Return*. As mentioned above, if the final distribution of the asset has been delayed, an explanation should be attached. Final Form K-1's should be issued to the income beneficiary, and possibly to the beneficiary's estate (if distributions were made to his or her estate).[824] The form asks for the initial value of the assets contributed to the trust. That question was added to the form relatively recently, so there may be situations where the final trustee does not have that information (e.g., change of trustees or a bank merger, resulting in lost files). The trustee can make its best estimate (and disclose it as such) or attach a statement explaining why it is unavailable.

Practice Point: The author has been asked a number of times, "What should be done with any undistributed make-up amount in a net income with make-up charitable remainder unitrust (NIMCRUT)?" The answer is: "nothing." To the extent that it was not required to be distributed to the noncharitable beneficiary in the final year of the trust, it simply expires.

2. *Additional Issues if a Private Foundation Is the Remainder Interest Holder*

In addition to the usual reasons for winding up a CRT promptly, there are other reasons when the remainder interest holder is a private foundation. If the assets of the trust should be included in the various private foundation calculations but they are omitted, the foundation could be subject to penalties. Income subject to the 1.39% excise tax imposed by §4940 could be omitted; omitting the trust assets in the minimum distribution calculation could result in an under-distribution penalty under §4942; or the foundation could unknowingly exceed the excess business holdings threshold under §4943.

Any income earned during the final year of the trust, and any accumulated income in the categories and classes, is not subject to the private foundation excise tax imposed by §4940 when the income is distributed from the trust to the foundation. See Notice 2004-35 for the requirement that certain foundation include "Filed pursuant to Notice 2004-35" on the front page of their Form 990-PF, *Return of Private Foundation or Section 4947(a)(1) Trust Treated as a Private Foundation*. Although Notice 2004-35 indicates that the Treasury will update Reg. §53.4940-1(d)(2) to conform with the position stated in the Notice, this has not yet occurred. Foundations, therefore, should continue to follow the guidance in the notice for the foreseeable future.

3. *Split-Interest Trusts that Become Charitable Trusts*

The regulations under §4947 provide that if the last noncharitable interest in a CRT has expired and some or all of the charitable beneficiaries are not entitled to distributions of corpus in trust or free of trust (i.e., the trust is to continue to hold assets for the benefit of those charitable organizations), the trust continues to be treated as a CRT for a "reasonable period of settlement."[825] "Reasonable period of settlement" means

[820] Reg. §53.4947-1(b)(2)(iii).
[821] Reg. §1.664-2(a)(6)(ii), §1.664-3(a)(6)(ii).
[822] §508(a).
[823] Reg. §1.641(b)-3(a).

[824] See VI.F.3.c., above.
[825] Reg. §53.4947-1(b)(2)(iv).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

that period reasonably required (or if shorter, actually required) by the trustee to perform the ordinary duties of administration necessary for the settlement of the trust.[826] Thereafter, the trust is treated as a charitable trust described in §4947(a)(1).[827] Being subject to §4947(a)(1) brings the trust under the full complement of private foundation rules. In most situations, the trustees will proceed to apply for recognition of exempt status for the trust by filing Form 1023, *Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code.*

This rule is difficult to reconcile with the regulations under §664, which provide that if all of the trust corpus is to be retained for the use of one or more §170(c) organizations upon the termination of the last noncharitable income interest, the taxable year of the trust terminates at that time and the trust ceases to be treated as a CRT for all purposes.[828] Moreover, the continuing trust is stated to be subject to the provisions of §4947(a)(1). Thus, unlike the §4947 regulations, the §664 regulations do not appear to permit a CRT that becomes a charitable trust to enjoy a reasonable period of settlement before being subject to the more stringent rules of §4947(a)(1).

Practice Point: As a practical matter, once the last noncharitable interest has expired, the trustees should proceed as if the trust is subject to the provisions of Chapter 42. That includes filing Form 1023 timely. Although there is a significant grace period,[829] filing before the deadline will reduce the risk of confusion with the IRS if the trust were to start filing Form 990-PF before the IRS records are updated.

4. *Winding-Up Period Unduly Prolonged*

There will be times when a trustee, likely a successor trustee, faces a situation where it appears that the winding-up period of a CRT has been unduly prolonged. When facing this situation, the trustee first should determine what should have happened, and when it should have happened. Certainly, if there are assets to be distributed to a charitable remainder interest holder, the distributions should be made as soon as reasonably possible, subject to any fiduciary issues. The trustee may decide to hold some assets in reserve in case there is some penalty exposure, or a need to retain professionals to engage with the IRS or state authorities. If the assets are to be distributed to a private foundation, the foundation may need to amend its 990-PF to include certain trust income in the excise taxable income under §4940, or the trustee may determine that the trust should file its own Form 990-PF as a §4947(a)(1) trust. If the assets are to be distributed to a public charity, that charity will need to decide whether an amended return is required. Depending on the reason for the delay, the trustee may be able to convince the IRS to waive any penalties, based on reasonable cause.[830]

If the CRT is to become a wholly charitable trust, the trustee may need to file a late Form 990-PF (or Form 990, if the trust will be timely able to qualify as a public charity), and address any of the potential excise tax issues discussed above.

B. *Termination by Donation of the Income Interest*

At some point during the life of the beneficiary, he or she may decide to donate the income interest to a charity, thus terminating the charitable remainder trust (CRT). Perhaps the beneficiary has sufficient other income, perhaps a naming opportunity is available at a charity, or perhaps the trust has become too small to be effectively administered.

The first step is to be sure that the named charity has a vested interest in the remainder interest in the CRT. Often donors will name a charity as a remainder interest holder, but retain the right to substitute another charity either during lifetime or by will. If that power exists, the donor should relinquish that power.[831] It may also be necessary to remove any spendthrift provisions in the document if they would preclude an effective donation.

The donor will need to consult with counsel to determine the steps necessary under state law to vest all the rights to the CRT property in the chosen charity. A donation of the income interest to the charity is an obvious step, but the charity may also need to accept the trusteeship so that all property rights are vested in the charity. If the donor's spouse (or another party) has any contingent beneficiary rights, it may be necessary for that party to waive or relinquish those rights.[832] It is necessary for the donee charity to have all rights in the property so that the income tax deduction is not denied by the split interest rules of Reg. §1.170A-7.

In Rev. Rul. 86-60, the IRS ruled that transfers by a grantor/recipient and a successor recipient of their interests in a charitable remainder annuity trust (CRAT) to the charitable remainder beneficiary qualified for income tax and gift tax charitable deductions. The partial interest rule of §170(f)(3) did not disqualify the deduction because the grantor's interest in the trust property was not divided in order to avoid the partial interest rule. In PLR 9721014, the IRS ruled that a renunciation of a joint unitrust interest in a CRT was a gift to the charitable remainder beneficiary qualifying for the gift and income tax charitable deductions.

Comment: Note that although the gift of the annuity interest in a charitable remainder annuity trust will generate an income tax charitable deduction, that is not the case for a gift of an annuity interest in a charitable gift annuity. In that case, the deduction will be limited to the donor's unrecovered basis in the contract.

In PLR 202047005, the IRS ruled that a taxpayer and his spouse's assignment of their annuity interests in a trust, where a private foundation was the remainder beneficiary, would not result in a charitable income tax deduction, but would be considered a gift for income tax purposes. The IRS stated that similar to the situation in Rev. Rul. 86-60, §170(f)(3)(A) does not

---

[826] Reg. §53.4947-1(b)(2)(iv)(A).

[827] Reg. §53.4947-1(b)(2)(iv).

[828] *See* Reg. §1.664-2(a)(6)(ii), §1.664-3(a)(6)(ii).

[829] The due date of the Form 1023 is 27 months from the date of formation (or deemed formation when a CRT converts to a wholly charitable trust). *See* Reg. §1.664-2(a)(6)(ii); instructions for Form 1023.

[830] See 634 T.M., *Civil Tax Penalties.*

[831] *See* PLR 200631006 (unitrust recipient/grantor of net income unitrust with make-up provision was entitled to income and gift tax charitable deductions for value of her unitrust interest and gift tax charitable deduction for value of remainder interest that passed to charity after she renounced her unitrust interest and her right to name remainder beneficiaries (after irrevocably naming such beneficiaries)), PLR 201321012 (similar).

[832] See analysis in PLR 200808018 and PLR 9550026.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

apply to a donation of a taxpayer's entire interest. The IRS also ruled that the taxpayer and his spouse would be entitled to a gift tax charitable contribution deduction for the present value of the annuity interest. Because they had retained the right to change the remainder charity (so the initial funding was an incomplete gift), once the foundation was irrevocably designated as the charitable remainderman of the trust, the taxpayer and his spouse would also be entitled to a charitable gift tax deduction for the fair market value of the remainder interest. The IRS stated that following the assignment of the annuity interest, which would result in a merger of the income and remainder interests under state law, the taxpayer and his spouse would seek a termination of the trust. The IRS noted that the taxpayer and his spouse would not recognize any gain or loss because the transfer is an assignment rather than a disposition for money or property. The IRS differentiated the situation in the PLR from that in Rev. Rul. 72-243, where the annuity interest was sold to the remainder beneficiary. Finally, the IRS found no act of self-dealing and no applicable termination tax where the transfer was an assignment.

In PLR 8805024, however, the assignment of a successor unitrust amount did not qualify for an income or gift charitable tax deduction because the holder's interest was contingent on surviving the first recipient and the nonexercise of his testamentary power of revocation. Query whether the holding would have been different had the initial income recipient relinquished his revocation power.

A qualified appraisal may be required if the donor desires an income tax deduction because even though the trust corpus may consist of only cash and publicly traded securities, the item being donated is an interest in a trust and not the underlying assets of the trust. Therefore, the exception for donations of publicly traded securities[833] may not be met, and arguably an appraisal is required.[834]

In the valuation of the noncharitable interest in the trust for purposes of the charitable deduction, any net income limitation in the trust is disregarded.[835]

C. Termination by Partition of the Charitable Remainder Trust Between the Beneficiary and the Charity

Not every charitable remainder trust (CRT) beneficiary is interested in a donation of his or her income interest. Instead, he or she may want to convert the interest to cash, thereby accelerating the remainder interest to the charity. The income beneficiary may need cash, may be tired of the compliance burden, or may be motivated by desire to accelerate the charitable remainder. Charities are interested in this transaction as it accelerates their access to the value of the remainder, and avoids the risk that the donor will change his or her mind before the remainder vests. Larger charities are familiar with the process of this type of termination, and are generally eager to assist.

The IRS takes the position that the termination of the income interest by partition of the trust in accordance with actuarial values is treated as a sale of the income interest to the remainder beneficiary,[836] although the case cited for support does not specify whether the funds paid to the income beneficiary were from partition of the trust or from the remainder interest holder's other funds. If the transaction is treated a sale of the income interest to the remainder beneficiary, it would, where the remainder beneficiary is a private foundation, be self-dealing without regard to the reasonableness of the terms.[837] The IRS issued a few favorable PLRs permitting partitions of CRTs between the income beneficiaries and their private foundations[838] before changing its mind and revoking the third ruling.[839]

Additionally, some commentators have speculated on the opportunities for overvaluation of the income interest when terminating a "lesser of unitrust amount or net income" unitrust if little income is being produced, and the low interest rate climate would benefit the income beneficiary on termination.[840] Post-2006 letter rulings had required special valuation methodology for early terminations of net income with make-up charitable remainder unitrusts (NIMCRUTs) to avoid self-dealing, unless the unitrust payout rate does not exceed the §7520 rate for the month of termination.[841]

Practice Point: Although §664(e) allows the net income limitation to be disregarded in the early termination of a CRT, it does not address potential self-dealing issues if the noncharitable beneficiary is advantaged over the remainder charity when allocating the assets between the beneficiaries. Barring a change to §4941 comparable to the addition of the last sentence of §664(e), income beneficiaries and their advisors should proceed with caution when terminating CRTs with net income limitations. Fiduciary duties and any relevant provisions of state law should also be considered. If the trust has a "flip" provision, consider activating that provision before the termination so that the trust being terminated is a CRUT rather than a NIMCRUT at the time of termination. Rather surprisingly, the amendment to §664 says nothing at all about self-dealing — no amendment was made to §4941. Just because the income interest is "valued" without taking into account the income-only feature, it doesn't necessarily follow that a division which results in the income beneficiary getting substantially more on the division than would otherwise be paid out is not self-dealing. Further, how can the charity and the trustee ever consent to such a division without violating their respective fiduciary duties? If the trust can only be divided by court order, shouldn't the state attorney general object? It is difficult to see how a division of a net-income CRUT which results in the income beneficiary receiving far more than he or she could ever dream of

[833] Reg. §1.170A-16(d)(2)(i) (cross referencing Reg. §1.170A-13(c)(7)(xi)).

[834] Reg. §1.170A-17(a), generally applicable to charitable contributions made on or after January 1, 2019. See also Reg. §1.170A-13(c)(3) for returns or submissions pertaining to donations made before January 1, 2019.

[835] §664(e). For the IRS position before the changes to §664(e), see PLR 200808018, PLR 200524014 (net income limitation disregarded), PLR 200205008 (deduction limited to value based on current §7520 rate).

[836] *McAllister v. Commissioner*, 157 F.2d 235 (2d Cir. 1946).

[837] §4941(d)(1)(a); Reg. §53.4941(d)-2(a)(1).

[838] PLR 200525014, PLR 200304025, PLR 200252092.

[839] PLR 200614032 (revoking PLR 200525014).

[840] In PLR 200816033, PLR 200816032, PLR 200809044, PLR 200733014, and PLR 200725044 (each providing for payment of a unitrust amount equal to the lesser of trust income or a stated percentage of the fair market value of trust assets, and most of which included a make-up provision), the IRS approved the calculation of the actuarial values of the income and remainder interests using an assumed payout that was a fixed percentage equal to the lesser of the trust's stated percentage payout or the §7520 rate for the month of termination.

[841] PLR 200912036.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

receiving otherwise could not be self-dealing and the amendment to §664 just doesn't address this. This amendment to §664 is not good for charities and one hopes that trustees, charitable remainder beneficiaries, and state attorney generals will all do their duty when interest rates are low and resist divisions which so grossly overpay the income beneficiary absent some pretty unusual circumstances.

In PLR 200304025, the IRS concluded that the division of a CRUT resulted in the sale of the grantors' interests under §1001(a), and that the grantors would have zero bases in those interests under §1001(e) and the amount realized would be the value of the property distributed to the grantors. Presuming a long term holding period for the income interest, the transaction would result in long-term capital gain.

The IRS will no longer rule on issues pertaining to the tax consequences of the termination of a CRT before the end of the trust term as defined in the trust's governing instrument in a transaction in which the trust beneficiaries receive their actuarial shares of the value of the trust assets.[842] Previous favorable rulings on terminations may be useful as informal guidance.[843]

A CRT may be divided to settle litigation. In general, a private letter ruling is highly recommended.[844]

Comment: Because the IRS fictionalizes the transaction as sale of the income interest to the charitable remainder beneficiary, what if instead the income beneficiary actually buys the remainder interest from the charity? Obviously, that would not be possible with a private foundation as a remainder interest holder. The economic results would be similar: all parties would end up with amounts representing their actuarial interests in the trust. The unrealized income in the CRT tiers would have to be dealt with in some way but the proposed regulations issued in response to a transaction identified as a transaction of interest in Notice 2008-99 provides a method.[845] The proposed regulation dealt with the basis issue this way:

> Accordingly, these proposed regulations provide a special rule for determining the basis in certain CRT term interests in transactions to which section 1001(e)(3) applies. In these cases, the proposed regulations provide that the basis of a term interest of a taxable beneficiary is the portion of the adjusted uniform basis assignable to that interest reduced by the portion of the sum of the following amounts assignable to that interest: (1) the amount of undistributed net ordinary income described in section 664(b)(1); and (2) the amount of undistributed net capital gain described in section 664(b)(2). These proposed regulations do not affect the CRT's basis in its assets, but rather are for the purpose of determining a taxable beneficiary's gain arising from a transaction described in section 1001(e)(3).

If the trust is terminated by purchase of the charity's remainder interest, does the §507 termination tax apply? Section 507 (which §4947(a)(2) makes applicable to charitable remainder trusts) provides that on termination of private foundation status, a termination tax can be imposed in certain situations. The most typical way of avoiding the private foundation termination tax is by transferring all of the assets to a public charity which has been in existence for at least 60 calendar months. In this situation, all of the assets of the trust would be distributed to a private individual so the termination tax should not apply based on language in many private letter rulings in which the trust proceeds were divided actuarially between the income and remainder beneficiaries. In those cases, of course, not all of the assets were distributed to the public charity either. So how do the rulings manage to avoid the §507 termination tax? The language in PLR 201325021 is typical:

> Furthermore, because the effect of the transaction is to vest the income interests with the income beneficiaries and the remainder interests in the remainder beneficiary, the trust no longer will be a split-interest trust and §4947(a)(2) will no longer apply and §507 will not apply.

The same reasoning should apply here: the charity ends up with the value of its interest and the income beneficiary ends up with the value of its interest.

In addition, the logic of this ruling suggests that when the trust collapses because the income beneficiary now owns all the pieces, the trust should not be treated as carrying out income to the income beneficiary under the tiers — the trust is no longer a split interest trust at that point.

D. *Termination by Simultaneous Sale of the Income Interest and Remainder Interest*

For many years, due to an unintended gap between §664 and §1001(e)(3), it was possible to take the position that the income beneficiary could use the actuarial share of the trust's basis in its assets as his or her basis in the trust interest, as long as the income and remainder interests in the charitable remainder trust (CRT) were sold simultaneously to a third party. For years after §664 was added to the Code this was only a theoretical concern, because interests in CRTs were not sold. That changed in the early 2000's: transactions were designed to take advantage of the gap. Finally acknowledging that there was a potential for untaxed gain, the IRS first treated these transactions as reportable "transactions of interest." The IRS acknowledged the gap and requested comments on a permanent fix.[846]

Several years later, the IRS issued regulations providing special rules for determining a taxable beneficiary's basis in a term interest in a CRT upon a §1001(e)(3) sale or other disposition of all interests in the trust, to the extent the basis consists

[842] *See* Rev. Proc. 2026-3, §3.01(85).

[843] PLR 201325021–PLR 201325018 (early termination of CRUT by deemed sale of income interest to remainder beneficiary did not result in self-dealing between income beneficiaries and unitrust or between trustee and unitrust because: (1) income beneficiaries did not receive more than they would have received during full trust term; (2) state law permitted early termination; and (3) income beneficiaries did not have medical conditions expected to result in shorter-than-average life expectancies), PLR 200912036, PLR 200816033, PLR 200816032, PLR 200809044, PLR 200739004, PLR 200733014, PLR 200616035, PLR 200441024 (early termination of CRT by sale of income interest to remainder beneficiaries for amount equal to present value of interest was not act of self-dealing by trust's donor/trustee or independent trustee).

[844] *See* PLR 200802033, PLR 200802032.

[845] REG-154890-03, 79 Fed. Reg. 3142 (Jan. 17, 2014), finalized by T.D. 9729, 80 Fed. Reg. 48,249 (Aug. 12, 2015).

[846] Notice 2008-99.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

of a share of adjusted uniform basis.[847] The regulations provide that the basis is the portion of the adjusted uniform basis assignable to that interest, reduced by the portion of the sum of: (1) the trust's undistributed net ordinary income under §664(b)(1); and (2) the trust's undistributed net capital gains under §664(b)(2). Therefore, the income beneficiary/seller will incur a long-term capital gain, only benefitting from his or her actuarial share of the original contributed basis.

Because the regulations (which are applicable to simultaneous sales after January 16, 2014) preclude the possibility of untaxed gain, these transactions have been removed from the "transactions of interest" list.[848]

Depending on the basis of the original contributed assets, a simultaneous sale of the income and remainder interests to a third party may produce a better tax result than a partition or sale of the income interest alone. This tax result has to be weighed against the additional administrative and legal complexity of the simultaneous sale. Depending on the document and state law, it may also be necessary to address any spendthrift restrictions in the document.

E. Termination by Exchange for a Charitable Gift Annuity

In PLR 200152018, the IRS ruled that, where the grantor/recipient transferred his unitrust interest to the charitable remainder beneficiary in exchange for an annuity to be paid by the charity to the grantor for life, the grantor had long-term capital gain in the amount of the annuity's value but was entitled to charitable income and gift tax deductions in the amount by which the value of the unitrust interest exceeded the value of the annuity. The grantor's adjusted basis in the unitrust interest was determined by allocating the grantor's aggregate adjusted basis in the property transferred to the Trustee at the trust's formation between (i) grantor's unitrust interest and (ii) the remainder interest, in proportion to the respective values of those interests as those values were determined on the date of transfer to the Trustee.

This exchange of a CRT income interest for a charitable gift annuity (CGA) is a potential solution for the "too small" CRT (assuming the beneficiary is unwilling to donate the income interest to the charity). It may also be applicable if the beneficiary desires simplicity and/or a steady stream of income rather than the variability of a unitrust interest.

F. Termination by Merger with Another Charitable Remainder Trust

PLR 201420010 involved two virtually identical charitable remainder unitrusts (CRUTs) that the taxpayers wished to consolidate. The assets of one trust were transferred to the other trust in order to eliminate duplicative administrative time and expenses as well as the filing of duplicative state and federal tax returns. The IRS ruled that the consolidation of the two trusts would terminate the status of the trust transferring its assets but would not cause the trust which accepted the transfer to fail to qualify as a charitable remainder trust (CRT) under §664; however, the IRS did not rule on any other matters regarding the consolidation. Given the rarity of this transaction, taxpayers contemplating a CRT merger may desire their own rulings. The situation can be avoided by making additional contributions to existing unitrusts rather than funding an additional trust.

---

[847] Reg. §1.1014-5(c).

[848] T.D. 9729, 80 Fed. Reg. 48,249 (Aug. 12, 2015).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

IX. Estate Tax Treatment of Inter Vivos Charitable Remainder Trusts

A. Amount Included in the Taxable Estate

1. Charitable Remainder Trust Established by the Noncharitable Beneficiary

If the noncharitable beneficiary of the charitable remainder trust (CRT) was the person who established it, some or all of the value of the trust will be included in his or her taxable estate if the donor dies during the term of the trust.[849] If the creation of the trust resulted in a taxable gift, and the trust is also included in the donor's taxable estate, this does not result in double taxation. Taxable gifts that are included in the taxable estate are eliminated from "lifetime taxable gifts" when the taxable estate is calculated.[850]

The full value of the trust will be included in the donor's taxable estate if he or she retained the power to designate the charitable remainder beneficiary.[851]

If the grantor retained the testamentary power to revoke the interest of the successor annuity or unitrust recipient,[852] the entire trust will be included in the grantor's estate under §2038.[853]

If the decedent did not retain either of the above rights, then less than all of the CRT may be included in his or her taxable estate. Reg. §20.2036-1(c)(2)(i) provides that the portion of the CRT includible in the decedent's estate is the portion of the trust corpus necessary to generate enough income to satisfy the retained annuity or unitrust (without reducing or invading principal), using the §7520 interest rates and the Reg. §20.2031-7 (or Reg. §20.2031-7A) adjustment factors, if applicable.[854] The portion of the trust included in the decedent's estate cannot exceed the value of the trust corpus at the date of death.[855] Reg. §20.2039-1(e) provides that §2039 does not apply to such trusts (other than a trust constituting an employee benefit) if the retained interest or use is described in §2036.[856]

Section 2035(a) includes in the estate any interest in property transferred by the decedent within three years of death that, if retained by the decedent, would have been includible under §2036, §2037, §2038, or §2042.[857] The gift of the remainder interest would not be includible under any of these sections and, therefore, §2035 should not operate to bring any part of the trust into the donor's estate unless the donor retained and then relinquished an annuity or unitrust interest within three years of death.[858]

If the CRT was funded with community property, only the decedent's retained one-half interest in the trust would be includible in his or her taxable estate; however, both halves of the community property would receive a new basis as of the date of the first decedent's death.[859]

Practice Point: If the donor was the only noncharitable beneficiary, and the remainder passes to one or more public charities, the amount of the estate-includible portion of the trust has no tax impact. If the remainder passes to a private foundation, however, only the estate-includible portion of the trust will receive date-of-death adjusted basis.[860] This may affect the foundation's excise tax on investment income under §4940 if it sells assets that are distributed to it from the trust.

2. Charitable Remainder Trust Established by Someone Other than the Noncharitable Beneficiary

If the trust was established by another person (i.e., by a parent for the benefit of his or her child), and the beneficiary dies, nothing is included in the taxable estate of the beneficiary (other than any payments receivable). The beneficiary did not make a transfer that would require inclusion in his or her taxable estate under §2036.[861] Even if the beneficiary is given the choice of remainder charitable beneficiary, that power is not a general power of appointment that would trigger estate inclusion for the beneficiary.[862]

Practice Point: Although the value of a CRT not established by the beneficiary is not included in the decedent's taxable estate, it will need to be disclosed on Form 706, assuming filing of that form is required.[863]

---

[849] Reg. §20.2036-1(c)(2).

[850] §2001(b). For transfers before 1977, §2012 grants a credit against a decedent's estate tax where the same transfer is taxed under both the estate and gift tax. Rev. Rul. 74-363.

[851] Reg. §20.2036-1(b)(3).

[852] Reg. §1.664-2(a)(4), §1.664-3(a)(4).

[853] *See, e.g.*, PLR 8020098.

[854] *See* Reg. §20.2036-1(c)(2)(iv) *Ex.* 1 (illustrating charitable remainder annuity trust), *Ex.* 3 (illustrating charitable remainder unitrust). For illustrations of these examples, see *Reg. §20.2036-1(c)(2)(iv) Ex. 1: Valuation of Retained Interests in Charitable Remainder Annuity Trust at Grantor's Death* and *Reg. §20.2036-1(c)(2)(iv) Ex. 3: Valuation of Retained Interest in Charitable Remainder Unitrust at Grantor's Death*, in the Bloomberg Tax Transactional Diagrams Library.

[855] Reg. §20.2036-1(c)(2)(i).

[856] The preamble to the proposed regulations (REG-119097-05, 72 Fed. Reg. 31,487 (June 7, 2007)) stated that the IRS believes it is appropriate to provide a regulatory rule under which only one of §2036 and §2039 would apply if both are potentially applicable to these trusts, to ensure similar tax treatment for similarly situated taxpayers. The preamble also noted that the retained interests in these trusts are more similar to the interests addressed under §2036 and that it appears Congress intended §2039 to address annuities purchased by or on behalf of a decedent and annuities provided by the decedent's employer.

[857] Applicable to decedents dying after December 31, 1981.

[858] Preamble to T.D. 9414, 73 Fed. Reg. 40,173 (July 14, 2008); Reg. §20.2036-1(c)(2)(iv) *Ex.* 1 (illustrating application of §2035).

[859] §1014(b)(6). See 802 T.M., *Community Property: General Considerations*, for further discussion.

[860] §1014(b)(9).

[861] Reg. §20.2036-1.

[862] Reg. §20.2041-1(c)(1)(a).

[863] See 822 T.M., *Estate, Gift, and Generation-Skipping Tax Returns and Audits*, for the reporting requirements.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

B. Charitable and Marital Estate Tax Estate Tax Deductions Allowed

A charitable or marital estate tax deduction may be allowed to offset the value of the included property, as discussed below in each of the possible scenarios. Of course, the charitable remainder trust (CRT) must be a valid trust under state law and include all the provisions required by §508(d)(2)(A).[864] Those provisions are discussed above at IV.K., above.

The calculation of the charitable remainder interest deduction is the same as the calculation of the lifetime charitable gift tax deduction, discussed above at IV.H., above. The charitable remainder must be at least 10% for the estate to be eligible for a charitable deduction.[865] If it is not, a reformation may be timely undertaken to reduce the payout rate (or term) so that the trust will qualify for the charitable deduction. Based on the Conference Report on the Taxpayer Relief Act of 1997 (TRA '97),[866] even if the trust is not reformed, so that no charitable estate tax deduction is allowed, the trust continues to be a CRT.[867]

1. Donor Is the Only Noncharitable Beneficiary of the Charitable Remainder Trust

If the donor was the only noncharitable beneficiary of the charitable remainder trust (CRT), the grantor's estate will receive a corresponding charitable deduction for the amount of the property so included. This presumes that the charities receiving the remainder interests qualify for the estate tax charitable deduction.[868] See the discussion of qualifying charities at IV.F., above.

2. Donor's U.S. Citizen Spouse Is the Only Noncharitable Successor Beneficiary

A common CRT structure is for the donor to retain an interest for life, followed by a successor life interest in the donor's spouse. If the donor's spouse is a U.S. citizen, the full amount of the noncharitable interest will qualify for a marital deduction.[869] The sum of the charitable remainder and noncharitable beneficial interest will equal the value of the trust, so the inclusion of the trust should not result in any estate tax. This result applies whether the trust is for a term of years or a joint and survivor interest, and whether the trust is an annuity trust or a unitrust (including a unitrust with a net income limitation).

Practice Point: The estate tax marital deduction allowed is not a qualified terminable interest property (QTIP) deduction.[870] No QTIP election is required or available as the terminable interest rules do not apply.[871]

3. Donor's U.S. Citizen Spouse Is a, but Not the Only, Noncharitable Successor Beneficiary

This situation is most likely to occur if the trust has been established for a term of years, with the successor interests payable to the donor's spouse and then to other beneficiaries should the spouse die within the term. Such a trust does not qualify for the special estate tax marital deduction discussed above.[872] Also, since a CRT cannot be drafted to qualify for the QTIP marital deduction (because it cannot pay "all income" to the spouse as required by §2056(b)(7)(B)(i)(II)), no marital deduction is available. Therefore, the only deduction allowed will be for the charitable remainder.[873]

Practice Point: A successor annuity or unitrust recipient of an inter vivos CRT can make a qualified disclaimer of his or her interest within nine months of the preceding unitrust recipient's death if the transfer of the unitrust interest to the successor recipient is not complete until the preceding recipient's death.[874] A qualified disclaimer of his or her successor interest will allow the marital deduction.[875]

4. Trust Has Successor Beneficiaries Not Including a U.S. Citizen Spouse

A charitable deduction will be allowed for the value of the remainder interest, as calculated in IV.H., above. The noncharitable value of the trust will contribute towards the taxable estate. If there is federal or state estate tax due, some portion of the tax may be allocated, under state law and the testamentary documents, to the noncharitable interest.[876] This situation may occur if state law provides for the equitable apportionment of any federal estate or state death taxes imposed on the primary beneficiary's estate and for the payment of such taxes from the trust assets.

A charitable remainder trust created on or after October 4, 1982,[877] must provide that the vesting of the interest of the sec-

[864] In TAM 7918002, the grantor named himself beneficiary of a unitrust amount and provided a successive income interest for his "wife" if she survived him. At the time the trust was executed, the grantor was married to B, but after B's death the grantor remarried. The National Office questioned whether the trust satisfied the requirement that a recipient who was an individual be named and living at the time of the trust creation. In order to receive an estate tax charitable deduction, the grantor's personal representative was required to show that the donor intended his first wife to be the unitrust recipient. By reference to state law, the National Office determined that the grantor did intend B to be the recipient and, therefore, the estate tax deduction was permitted.

[865] *Estate of Schaefer v. Commissioner*, 145 T.C. 134 (2015).

[866] H.R. Conf. Rep. No. 105-220, at 607 (1997).

[867] §664(d)(1)(D), §2055(e)(3)(J), added by the TRA '97, Pub. L. No. 105-34, §1089(b). According to the Conference Report on TRA '97, where a charitable remainder annuity trust (CRAT) is created for the joint lives of two individuals, the trust will not fail to qualify as a CRT if the value of the remainder interest is less than 10% of the trust's assets at the death of the first of the noncharitable beneficiaries. The same result should obtain for a two-life CRAT where payments are made first to the donor and subsequently to a successor noncharitable beneficiary. H.R. Conf. Rep. No. 105-220, at 607 (1997).

[868] Rev. Rul. 77-385.

[869] §2056(b)(8). In the case of pre-1982 decedents where the trust corpus was includible in the gross estate pursuant to §2035, §2036, or §2038, and the decedent's will provided for a marital deduction based on 50% of the adjusted gross estate, the marital deduction was increased as a result of the inclusion, notwithstanding the offsetting charitable deduction. *Estate of Russell v. Commissioner,* 70 T.C. 40 (1978), *acq.*, 1979-1 C.B. 1; Rev. Rul. 72-552.

[870] *See* TAM 8730004.

[871] Reg. §20.2056(b)-8(a)(1).

[872] §2056(b)(8).

[873] Reg. §20.2056(b)-8(b); TAM 8730004.

[874] *See* PLR 200204022. For further discussion of qualified disclaimers, see 848 T.M., *Disclaimers — Federal Estate, Gift and Generation-Skipping Tax Considerations.*

[875] TAM 8730004.

[876] See 834 T.M., *Transfer Tax Payment and Apportionment*, for apportionment issues.

[877] Additional contributions to a pre-October 4, 1982, unitrust should not disqualify the unitrust, provided the governing instrument authorizes additions and contains the special rules for the revaluation of the unitrust amount in any year in which additional contributions are made. PLR 8313052 permitted income and gift tax charitable deductions for additional contributions to a pre-

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ondary beneficiary upon the death of the primary beneficiary is contingent upon the secondary beneficiary's payment of any death taxes attributable to his or her annuity or unitrust interest.[878] For the trust to qualify as a CRT, the document must include a requirement that the successor interest holder pay any taxes. The IRS sample documents include such a provision as follows:

> The lifetime annuity interest of the Successor Recipient will take effect upon the death of the Initial Recipient only if the Successor Recipient furnishes the funds for payment of any federal estate taxes and state death taxes for which the Trustee may be liable upon the death of the Initial Recipient. If the funds are not furnished by the Successor Recipient, the annuity period shall terminate on the death of the Initial Recipient, notwithstanding any other provision in this instrument to the contrary.[879]

If the decedent has provided for the taxes to be paid from other funds, then the amount "for which the Trustee may be liable" would be zero, and the successor's interest in the trust would vest. If no provision has been made, then the successor interest holder would need to pay those taxes before the interest holder could receive any payments. To do otherwise invites disqualification of the trust, and loss of the charitable deduction.[880] This provision is necessary even if the only successor beneficiary is the donor's spouse; taxes could be due if the spouses divorce or state inheritance taxes apply.

Practice Point: If the successor interest holder is unwilling or unable to pay the taxes, consider a qualified disclaimer by the interest holder so that a full estate charitable deduction will clearly be available on the estate tax return.[881]

Under certain circumstances, the payment of the annuity or unitrust amount may constitute a generation-skipping transfer.[882] Although it is unlikely that any generation-skipping transfer (GST) tax would be payable from the trust assets, the grantor should consider adding trust language obligating the secondary beneficiary to pay any GST tax for which the trust would otherwise be liable. See the discussion of allocation of GST exemption at V.F., above.

5. *Trust Has a Noncitizen Spouse as a Successor Income Beneficiary*

If the surviving spouse is not a U.S. citizen, the marital deduction discussed in IX.B.2., above is not available. It may be possible to qualify for the marital deduction by assigning the payments to a qualified domestic trust (QDOT) under the process described in Reg. §20.2056A-4(c)[883] or drafting the charitable remainder trust to qualify for the QDOT election.[884]

6. *Income Beneficiary Dies Before the Estate Tax Return Is Filed*

Unless the successor income beneficiary is terminally ill at the time of death of the initial income beneficiary, the normal life expectancy tables must be used to value the beneficiary's income interest. See the discussion at V.C.2., above.

C. Generation-Skipping Transfer (GST) Tax Issues

If a charitable remainder trust (CRT) is included in a decedent's taxable estate, and one or more successor beneficiaries are "skip persons" with respect to the decedent, the GST tax issues must be considered. See the discussion of GST tax issues at IV.J., above, and 850 T.M., *Generation-Skipping Transfer Tax (Chapter 13)*, for a full discussion of these issues. The following brief discussion is only intended to highlight the issues that should be considered.

If a skip person is the immediate successor beneficiary of a CRT, the executor may determine that an allocation of the decedent's GST exemption to the CRT would be appropriate. To fully exempt the trust from GST tax,[885] it is only necessary to allocate the amount of exemption equal to the noncharitable interest.[886] However, if a skip person is only a contingent successor beneficiary, the executor may decide that the exemption is best allocated elsewhere because such an allocation where the skip person's actuarial interest in the trust is relatively low could be an inefficient use of the executor's available exemption.

> *Example:* If a non-skip person (e.g., a child) has an actuarial interest in the trust of 70%, a skip person (e.g., a grandchild) has an 10% actuarial interest in the trust, with the charity's remainder interest valued at 20%, exempting the trust would require an allocation equal to 80% of the val-

October 4, 1982, unitrust notwithstanding the fact that it did not comply with Rev. Rul. 82-128.

[878] Rev. Rul. 82-128. In PLR 9225026, the IRS ruled that this requirement was not satisfied by a trust provision allowing the trust to recover the taxes from the beneficiary or the estate, because the estate and beneficiary could have insufficient funds with which to pay the tax.

[879] Rev. Proc. 2003-55, §4.3.

[880] *See Estate of Atkinson v. Commissioner*, 115 T.C. 26 (2000) (holding that CRT did not qualify when trust assets were used to pay estate tax following death of initial noncharitable beneficiary), *aff'd on other grounds*, 309 F.3d 1290 (11th Cir. 2002) (failing to reach issue of whether trust was also disqualified because of its exposure to estate tax liability because trust was disqualified for failing to make required annuity payments during settlor's lifetime), *cert. denied*, 540 U.S. 946 (2003).

[881] See 848 T.M., *Disclaimers — Federal Estate, Gift and Generation-Skipping Tax and State Law Considerations* for further information on planning with disclaimers. In PLR 200539022, the trustee of the decedent's trust was directed to pay estate taxes from the portion of the trust that was to be used to fund two testamentary charitable remainder unitrusts. The IRS ruled that, before the estate tax liability resulting from the grantor's death had been finally determined, the trustee of the decedent's trust could fund the unitrusts and could make distributions to the unitrust beneficiaries without causing the unitrusts to fail to qualify under §664 if the trust was modified to: (1) require the unitrust beneficiaries to pay any insufficiency in the event there were not enough assets remaining in the original trust to pay the taxes, (2) require the trustee to terminate a unitrust if the unitrust beneficiary did not pay his or her share of the insufficiency, and (3) prohibit the trustee from returning any assets transferred to the unitrusts or paying any of the taxes from those assets. The IRS also ruled that the estate tax charitable deduction should be determined as if the taxes were paid out of the share used to fund the unitrusts, even if the unitrust recipients paid those taxes personally, and should be based on the actuarial value of the remainder interests as of the date of the decedent's death, even if a unitrust were terminated because a unitrust beneficiary failed to pay his or her share of any insufficiency.

[882] §2601 *et seq.* See the discussion at IV.J., above.

[883] See 842 T.M., *Transfers to Noncitizen Spouses*, for further information on QDOTs and the assignment process.

[884] PLR 9244013.

[885] Technically, an inclusion ratio of zero under §2642.

[886] §2642(a)(2)(B)(ii)(II).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ue of the trust. The trust cannot be fully exempt from GST tax by an allocation equal to only the actuarial value of the skip person's interest.

D. Basis Adjustment for Trust Assets

Property included in the decedent's estate receives a basis stepped up to the date of death (or §2032 alternate valuation date) value in the hands of the person acquiring the property from the decedent.[887] Thus, for purposes of the rules discussed at VI.C.1., above (and, in particular, the capital gain category), if the value of the trust is included in the decedent's estate, the assets of the trust will take as their basis the value for estate tax purposes. As is always the case, items that constitute income in respect of a decedent as defined in §691(a) do not receive a stepped-up basis.[888] If the charitable remainder trust was funded with community property, both halves of the community property receive a stepped-up (or down) basis.[889]

Practice Point: The new basis for the trust property does not affect the existing accumulated income in the classes and categories. There is no guidance on how the adjustment to basis should be shown on the trust balance sheet on the Form 5227. Indeed, depending on when during the year the decedent died, and the assets held by the trust, the information may not be available by the time the Form 5227 is due. The author's suggestion is to adjust corpus on the balance sheet, and attach an explanatory statement.

---

[887] §1014(a).

[888] §1014(c). See 862 T.M., *Income in Respect of a Decedent (Section 691).*

[889] §1014(b)(6).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

X. Advanced Planning Options

A. Deferral Mechanisms in a NIMCRUT

Because a "net income with make-up" charitable remainder unitrust (NIMCRUT) pays the lesser of trust accounting income or the stated percentage of value, a substantial amount of "make-up" can accumulate if there is no trust accounting income for a period of years. This structure may appeal to donors who are currently working and therefore can use a current charitable deduction, but might want income when they retire. It may also be appropriate as a "safety net" for serial entrepreneurs: funding a charitable remainder trust (CRT) with some of the first IPO stock locks away some of the assets in case the next venture does not go as well.

There are plenty of assets that do not generate much, if any, trust accounting income. However, if the donor wants to be able to go to the trustee at some point and ask if any trust accounting income might be forthcoming, the investment needs to be such that trust accounting income could be produced — if not upon request, at least within a reasonably short period of time. Among the issues that the donor and his or her advisor will need to consider is constructive receipt during the deferral period: if the CRT trustee would be deemed to have received the income for income tax purposes, the IRS might raise the issue of whether that income should be deemed to be trust accounting income as well.

Any such assets will need annual appraisals by an independent trustee or qualified appraiser.[890]

Among the types of investments that may be suitable, assuming fiduciary responsibilities have been addressed, are the following:

- Annuities. A CRT might purchase a deferred annuity from an insurance company.[891] The investment return would not be trust accounting income until withdrawn. The disadvantages of this arrangement include the costs associated with purchasing the annuity, and the fact that all the income will be ordinary when withdrawn from the contract (with the result that the income distribution to the beneficiary will be taxed at his or her maximum tax rate).

- Flow-Through Entities. Although the IRS has occasionally become confused during examinations, it is generally settled that distributions from a partnership or LLC are trust accounting income,[892] unrelated to the taxable income or loss shown on a Form K-1. A CRT trustee holding a pass-through investment entity will report the income annually, filling up the categories with the various classes of ordinary income and capital gains from the Form K-1, whether or not any distributions are made from the entity. Once a distribution is received from the entity, the trustee can calculate the make-up amount and make a significant distribution to the beneficiary.[893] The beneficiary will receive the benefit of capital gain and qualified dividend income taxed at lower rates, assuming the entity investments have generated that type of income. Due to the constructive receipt issue, it is probably advisable to have a managing member of the LLC (or GP of the partnership) other than the CRT trustee or the donor/beneficiary. It is essential that the entity avoid any debt-financed or business investments due to the 100% tax on UBI.

- Zero Coupon Bonds. The noncharitable beneficiaries of a charitable remainder unitrust (CRUT) also may benefit if the assets of a net income only unitrust are invested in zero coupon bonds. Generally, zero coupon bonds are subject to the original issue discount (OID) rules as set forth in §1271 *et seq.*, and the regulations thereunder. As a result, the holder of a bond with OID would include a certain amount of the yearly increment in the value to the bond in his or her income each year for federal income tax purposes.

In PLR 8604027, the IRS ruled that a net income only unitrust was qualified where its governing instrument provided that the discount element of a bond issued with OID was considered income only in the year in which the bond was redeemed or matured. This would appear to eliminate the requirement that the noncharitable beneficiary include the increment in value to the bond in his or her income for federal income tax purposes and thereby provides a significant opportunity for income deferral.

However, the private ruling was based, at least in part, on an interpretation of the California Income and Principal Act. A second private letter ruling reached an identical conclusion under Tennessee law.[894] Section 643(b) provides that for purposes of certain subparts of Subchapter J of the Code, the term "income" means the amount of income of a trust for a given taxable year determined under the terms of the governing instrument and applicable local law. "Trust provisions that depart fundamentally from traditional principles of income and principal will generally not be recognized."[895] Before the 2004

[890] Reg. §1.664-1(a)(7).

[891] *See, e.g.*, PLR 201126007. This should not be confused with the abusive structure described in IRS AM 2020-006, wherein the promoter of a CRAT-based "structured transaction" attempted to use a single-premium annuity investment (SPIA) by a CRAT to create tax-free income. The structure ignored the accumulated income created by the sale of contributed assets and purported to use the annuity taxation rules under §72 instead of the category and class system of §664 when taxing the beneficiaries (among other defects). *See also Gerhardt v. Commissioner*, No. 11127-20, 2023 BL 134075 (T.C. Apr. 20, 2023) (where taxpayers contributed low-basis, high-value real property to CRAT, trustee sold real property and purchased SPIAs with proceeds, and income beneficiaries reported majority of annuity income as return of corpus, court held that annuity income to income beneficiaries should be reported as ordinary income; court reiterated that "nothing in [§]72 overrides their obligation to comply with the rules of [§]664(b) with respect to [annuity income]"); *Furrer v. Commissioner*, T.C. Memo 2022-100 (taxpayers attempted to engage in transaction similar to that described in IRS AM 2020-006, and court held that SPIA annuity amounts distributed by CRAT to taxpayers were "treated first as ordinary income, to the extent of the CRAT's ordinary income"). The IRS issued proposed regulations that would define certain CRAT transactions, such as the type of transaction in *Furrer*, as listed transactions. Prop. Reg. §1.6011-15, REG-108761-22, 89 Fed. Reg. 20,569 (Mar. 25, 2024), would be effective on the date of publication of final regulations. For more details on these proposed regulations, see IV.A.2. and VI.C.1., above.

[892] 1997 Uniform Principal and Income Act (UPIA) §401(b).

[893] This type of deferral structure is discussed in "Charitable Remainder Trusts: The Income Deferral Abuse and Other Issues" in the Additional Resources.

[894] PLR 9018015.

[895] Reg. §1.643(b)-1, as amended by T.D. 9102, 69 Fed. Reg. 12 (Jan. 2, 2004), effective for taxable years ending after January 2, 2004. Specifically,

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

amendments, former Reg. §1.643(b)-1 provided that allocations of items between income and principal that departed fundamentally from "concepts of local law" would not be recognized for this purpose.

In PLR 8604027, the IRS found that the provision was not contrary to California law and, therefore, was permissible under §643(b). The California Income and Principal Act provided, at the time, that the increment in value to a discounted bond was income and that such income was distributable to the beneficiary who was the income beneficiary at the time of the increment. The income obligation had to be satisfied from the first "principal cash available or, if none is available, when realized by sale, redemption, or other disposition." Thus, the California Income and Principal Act expressly recognized an instance where principal cash was not readily available to satisfy the income obligation. In the absence of such a provision, the question could arise as to whether the trustee is required to liquidate principal assets in order to satisfy the income obligation. Accordingly, the provisions of local law must be reviewed to determine whether such a provision is permissible.

Practice Point: An inter vivos CRT funded with zero coupon bonds will produce an immediate federal income tax charitable deduction for the grantor and a substantial deferral of income. This can be accomplished by a NIMCRUT or by a FLIP-CRUT. Such a strategy may be particularly attractive as a way to finance educational expenses or supplement retirement income at a known future point.

B. Real Estate in a Charitable Remainder Trust to Generate Passive Income

Although it is common for a donor to transfer appreciated real estate to a charitable remainder trust (CRT) and have the real estate sold and reinvested in securities, there is no reason that the process cannot be reversed. If a donor has portfolio securities and a passive loss carryover,[896] a CRT can invest in a passive income generator and therefore pay passive income to the beneficiary. A passive investment in a business would be inadvisable due to the unrelated business income tax, so unleveraged rental real estate is a plausible alternative. Either a direct investment by the trustee or an investment in an unleveraged real estate partnership could generate the desired passive income.[897] If a direct investment is chosen, the plan should include a reserve fund for unexpected expenses or an understanding that the donor may have to make additional, and perhaps substantial, contributions to the CRT.

C. Charitable Remainder Trust with a Charitable Purpose

Obviously, charitable remainder trusts (CRTs) have a charitable component: the remainder interest. But it is also possible to have a CRT with a charitable aspect before the remainder interest vests. (Or, the remainder can be transferred to the charity early. See VIII., above, for early terminations.)

First, the CRT can pay a portion of its required distribution to a charity. This may be attractive if the minimum 5% payment would be in excess of what the donor would like the beneficiary to receive. This form of payment is discussed at IV.E.6., above.[898]

Second, a CRT can make a partial principal distribution to charity before its term ends, as discussed at VI.C.4., above. Alternatively, the CRT can be divided and one portion donated to the charity while the remaining portion continues for the noncharitable beneficiary, as discussed at VII.B., above.

Third, a CRT can allow the remainder charitable beneficiary to use trust property for below-market or minimal rent. If the donor is concerned about the financial or managerial stability of the charity, this allows the donor to provide property for the charity to use, but also can allow the donor to change the remainder beneficiary should the original charity go out of existence or if the donor becomes dissatisfied with the charity. The author has seen this arrangement with organizations providing supportive housing for the mentally ill, group homes for people with developmental challenges, and student housing for educational organizations.

Reg. §1.643(b)-1 provides that the IRS will respect amounts allocated between income and principal pursuant to applicable local law if local law provides for a reasonable apportionment between the income and remainder beneficiaries of the trust's total return, including ordinary and tax-exempt income, capital gains, and appreciation, for the year. For further discussion of the 2004 amendments, see 852 T.M., *Income Taxation of Trusts and Estates.*

[896] *See* §469(b).

[897] §469(c)(2).

[898] *See* Rev. Proc. 2003-53; PLR 200832017. Note that the IRS appears to have reversed course on the ruling from PLR 200832017. The IRS advised in CCA 202233014 that a decedent's estate is not entitled to an estate tax or marital deduction for the value of the portion of the unitrust interest of a testamentary CRUT that may be distributed between the charity and the decedent's spouse at the trustee's discretion. Thus, even though it is well-established that the unitrust amount can be split between a charitable and noncharitable beneficiary, the IRS has put taxpayers on notice that the benefit of the charitable and marital deductions may not be available.

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XI. Charitable Remainder Trust History

A. *Legislative History*

1. *Charitable Remainder Trust Provisions Added to Code, Effective Date, and Grandfathering*

The Tax Reform Act of 1969 substantially changed the tax rules applicable to charitable remainder trusts (and pooled income funds). The rationale for these changes is well summarized in a 1980 Tax Court case[899] which upheld the constitutionality of §2055(e)(2) as follows:[900]

> Prior to the Tax Reform Act of 1969, Pub. L. 91-172, 83 Stat. 487, an estate tax deduction was allowed for transfers of property in trust with a remainder interest to charity if the value of the charitable interest was presently ascertainable, and if the possibility that the charitable transfer will become effective was not so remote as to be negligible.[901] Thus, if a decedent who died before January 1, 1970, transferred property to a trust to pay income to an individual for life and then to pay the principal to charity, the present value of the remainder interest qualified for an estate tax charitable deduction. However, Congress concluded that such rule resulted in certain abuses. For example, the assets of such a trust might be invested in a manner so as to maximize the income interest with the result that there would be little relationship between the interest assumptions used in calculating the present value of the charitable remainder and the present value of the amount actually received by the charity. H. Rept. 91-413 (1969), 1969-3 C.B. 200, 237. Also, a deduction was often allowed for a conditional bequest to charity even though it was not probable that the full amount of the bequest would ultimately be received by the charity. H. Rept. 91-413, *supra*, 1969-3 C.B. at 237–238. For example, a deduction was allowable for a charitable bequest even though the charity's interest was contingent upon the failure of issue or even though the trust's terms permitted invasion of the charitable share for the benefit of the income beneficiary. See, e.g., *Estate of DeFoucaucourt v. Commissioner*, 62 T.C. 485 (1974); *Estate of Jack v. Commissioner*, 6 T.C. 241 (1946).
>
> In order to correct these perceived abuses, and to insure closer correlation between the amount of the estate tax charitable deduction and the present value of the amount ultimately passing to charity, the Tax Reform Act of 1969 added section 2055(e)(2) to the Internal Revenue Code of 1954. Pub. L. 91-172, sec. 201(d)(1), 83 Stat. 560. Such section is effective, with certain exceptions not here relevant, with respect to decedents dying after December 31, 1969. It provides that an estate tax charitable deduction is not allowed for transfers of property to a trust which has both charitable and noncharitable interests unless, in the case of a remainder interest, the trust is in one of three qualifying forms: a charitable remainder annuity trust, a charitable remainder unitrust, or a pooled income fund.

Thus, Congress's action in 1969 was a response to the perceived lack of correlation between the income, gift, and estate tax charitable deductions claimed by taxpayers for gifts of remainder interests to charity and the value of the interests ultimately passing to charity. To correct this discrepancy, Congress amended §170, §2055, §2106, and §2522, and added §664 and §642(c)(3) through §642(c)(6) to set forth the highly technical requirements governing charitable deductions for gifts of remainder interests in trust. Congress also enacted the private foundation rules in 1969. In order to prevent taxpayers from using nonexempt charitable trusts and charitable remainder trusts (CRTs) to avoid the strict rules applicable to private foundations, Congress enacted §4947.[902]

The 1969 Act provided that §2055(e)(2)(A) (no deduction if not in form of a CRT or pooled income fund) would not apply in the case of property passing under a will executed on or before October 9, 1969, or involving property transferred in trust on or before that date, if the decedent died before October 9, 1972, without amending the will or trust instrument after October 9, 1969, or the decedent was prevented from amending the will or trust instrument or was under a mental disability after this date.[903] In *Ellis First National Bank of Bradenton v. United States*,[904] the Court of Claims disallowed a charitable deduction for a remainder interest passing to a nonqualified remainder trust because the decedent's will was executed after October 9, 1969. The estate had argued unsuccessfully that the provisions of an earlier (pre-October 9, 1969) will controlled and, therefore, the deduction should be permitted.

The rules relating to the effective date provisions are discussed in Rev. Rul. 76-198, where the will of a decedent's spouse, executed on September 3, 1969, established a nonqualified CRT. The spouse's estate was permitted an estate tax charitable deduction, because the spouse died before October 9, 1972, and the will was executed before October 9, 1969, without subsequent republication or amendment thereof. However, under the will of the decedent, who died on March 4, 1974, the residue of the decedent's estate was bequeathed to the trust established under the spouse's will. The IRS ruled that a charitable deduction was not available to the decedent's estate, because the decedent died after October 9, 1972. The deduction would have been available if the appropriate action had been taken to reform the trust before December 31, 1975 (the final date for reformations at the time the ruling was promulgated).

[899] *Estate of Gillespie v. Commissioner*, 75 T.C. 374 (1980).

[900] Although the *Gillespie* case involved only the estate tax charitable deduction, the discussion of the legislative history quoted here applies equally to the income and gift tax charitable deductions.

[901] Reg. §20.2055-2(a), §20.2055-2(b).

[902] *See* S. Rep. No. 91-552 (1969), reprinted in 1969 U.S.C.C.A.N. 2027.

[903] Pub. L. No. 91-172, §201(d)(1). *See* PLR 7802045 (estate was permitted deduction for trust that did not qualify under §2055(e)(2)(A); decedent had executed his will before October 9, 1972, had become mentally incompetent before October 9, 1972, and remained incompetent until his death). *See also Southeast Bank Trust Co., N.A. v. United States*, 79-1 USTC ¶13,297 (M.D. Fla. 1979).

[904] 550 F.2d 9 (Ct. Cl. 1977).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

2. Valuation Rules and Minimum Remainder Requirements

The next major statutory change affecting CRTs (and pooled income funds) was the Technical and Miscellaneous Revenue Act of 1988,[905] which added §7520. This provision requires that the value of any annuity, any interest for one or more lives or a term of years, and any remainder or reversionary interest be determined using tables (or formulae) prescribed by the Secretary of the Treasury.[906] Any charitable valuation under the tables is to be based upon an interest rate equal to 120% of the federal midterm rate under §1274(d)(1) in effect for the month in which the valuation date falls (or either of the two preceding months, as the taxpayer elects).[907] Section 7520 applies to all interests to be valued on or after May 1, 1989.

In 1997, this time responding to perceived abuses of CRT, Congress imposed two additional rules on CRTs.[908] First, the charitable remainder interest is required to have a minimum value of 10% of the property transferred to the trust. Second, a maximum 50% annual payout rate was imposed.

3. Pre-1986 Fiscal Year Rules

Before the Tax Reform Act of 1986 (1986 Act),[909] trusts could adopt any taxable year that satisfied the §441 requirements without obtaining prior IRS approval, provided the year was adopted on or before the time prescribed by law (not including extensions) for the filing of the return for the trust's first taxable year.[910] This rule permitted a recipient to receive a considerable benefit through the deferral of taxation where the taxable year of the trust differed from that of the recipient.

The 1986 Act required that an existing trust not already on a calendar year have a short taxable year beginning with the first day of its fiscal year beginning in 1987 and ending on December 31, 1987. As a result, a noncharitable beneficiary of a unitrust or annuity trust that was not on a calendar year experienced a "bunching" of income in 1987. The beneficiary was allowed to report the income attributable to the short year ratably over four years. Initially, section 1403(c)(2) of the 1986 Act required beneficiaries of simple or complex trusts (including pooled income funds) to report the income from the short year ratably over four years. The carryforward was mandatory and was not expressly available for annuity or unitrust recipients. The Technical and Miscellaneous Revenue Act of 1988 (1988 Act)[911] later confirmed that the carryforward provisions were optional and extended to the beneficiaries of CRTs. Notice 88-45 further provided that a beneficiary who died before the expiration of the four-year carryforward period had to include any remaining unreported income on the beneficiary's final return. In PLR 8825095, the IRS ruled that a change in the valuation date of a CRT required by a §644 change to a calendar year would not result in a loss of qualification.

4. Non-Application of Throwback Rules and Former §644

The throwback rules of §665 through §668 were never applicable to a qualified CRT.[912]

Also, even if a CRT was taxed as a complex trust under former §664(c), it was not subject to former §644, which taxed a trust at the transferor's tax rate if the trust sold appreciated property within two years of the date the transferor contributed the property to the trust.[913]

5. Alternative Minimum Tax Provisions Before 1993

Before 1993, the unrealized long-term capital gain component of the deductible portion of a gift was an item of tax preference for purposes of the alternative minimum tax (AMT) in the year or years the deduction was claimed.[914] This AMT treatment of contributions of appreciated property was repealed by the 1993 Act, effective for contributions made after December 31, 1992.[915] Before the repeal of this AMT provision, there were temporary statutory exceptions to AMT treatment for gifts of tangible personal property made in any taxable year beginning in 1991, as well as for such gifts made before July 1, 1992, in any taxable year beginning in 1992.[916] Thus, with respect to contributions of appreciated tangible personal property, AMT treatment does not apply to any gifts made in a taxable year beginning after December 31, 1990; for gifts of other property, the AMT provision does not apply for contributions made after December 31, 1992.

6. Pre-2007 Unrelated Business Income Tax and Reporting Rules

For taxable years beginning before 2007, pre-TRHCA[917] §664(c) provided that a CRT lost its income tax exemption in any year in which it had unrelated business taxable income. Under the pre-2007 taxable year rules, a trust that was nonexempt under pre-TRHCA §664(c) was treated as a complex trust and taxed pursuant to the rules of §641 through §644 and §661 through §664.[918] Accordingly, the trust was subject to all the

---

[905] Pub. L. No. 100-647, §5031(a).

[906] §7520(a)(1).

[907] §7520(a).

[908] Taxpayer Relief Act of 1997, Pub. L. No. 105-34, §1089, applicable to transfers in trust after June 18, 1997. These amendments do not apply to transfers in trust under the terms of a will (or other testamentary instrument) executed on or before July 28, 1997, if the decedent (i) died before January 1, 1999, without having republished the will (or amended such instrument) by codicil or otherwise, or (ii) was on July 28, 1997, under a mental disability to change the disposition of his or her property and did not regain competence to dispose of such property before the date of his or her death.

[909] Pub. L. No. 99-514.

[910] Former Reg. §1.441-1T(b)(2) (removed by T.D. 8996, 67 Fed. Reg. 35,009 (May 17, 2002), effective May 17, 2002).

[911] Pub. L. No. 100-647, §1014(c).

[912] See former Reg. §1.664-1(d)(1)(ii)(a) (before amendment by T.D. 9190, 70 Fed. Reg. 12,793 (Mar. 16, 2005), which deleted specific references to non-application of the throwback rules).

[913] Former §644(e)(3), repealed by the Taxpayer Relief Act of 1997, Pub. L. No. 105-34, §507.

[914] Former §57(a)(6), before its repeal by the Omnibus Budget Reconciliation Act of 1993 (1993 Act), Pub. L. No. 103-66, §13171. This discussion of the AMT is limited to noncorporate taxpayers.

[915] Pub. L. No. 103-66, §13171(a), §13171(d).

[916] Former §57(a)(6)(B).

[917] Tax Relief and Health Care Act of 2006 (TRHCA), Pub. L. No. 109-432, §424.

[918] *See* former Reg. §1.664-1(c) (before amendment by T.D. 9403, 73 Fed. Reg. 35,583 (June 24, 2008)). In *Leila G. Newhall Unitrust v. Commissioner*, 104 T.C. 236 (1995), *aff'd*, 105 F.3d 482 (9th Cir. 1997), the Tax Court upheld former Reg. §1.664-1(c), holding that the entire income of the trust was taxable in the year the trust was in receipt of unrelated business taxable income. Although the complex trust rules could apply to a CRT in a year it was nonexempt

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

taxes imposed on complex trusts, including, for example, the alternative minimum tax and depreciation recapture.

Before the Tax Reform Act of 1969 (1969 Act),[919] a split-interest trust was permitted a deduction for amounts of gross income set aside for charitable purposes. Section 642(c)(2), as amended by the 1969 Act, however, eliminated the charitable set-aside deduction for CRTs. Therefore, such a trust with unrelated business taxable income under the pre-TRHCA rules could not take a deduction for income items allocated to corpus.

Effective for taxable years beginning after December 31, 1986, nonexempt CRTs were required to make estimated tax payments in the same manner as individuals.[920] Although CRTs technically may still be subject to the estimated tax payment rules after the TRHCA amendments to §664(c), a qualified CRT will not have taxable income for taxable years beginning after 2006.

Before the TRHCA changes to §664,[921] Rev. Proc. 83-32 summarized the charitable remainder trust filing requirements, indicating that such returns could include Form 1041-A, *U.S. Information Return — Trust Accumulation of Charitable Amounts*, Form 5227, *Split-Interest Trust Information Return*, Form 4720, *Return of Certain Excise Taxes on Charities and Other Persons Under Chapters 41 and 42 of the Internal Revenue Code*, and Form 1041, *U.S. Income Tax Return for Estates and Trusts*.[922] For taxable years beginning before 2007, an exception to filing Form 5227 also applied for any year in which the trust was required to distribute all of the net income for the year currently to the beneficiaries.[923] The exception for distribution of all net income should have applied only in the case of a net income unitrust where the trust was required to distribute the lesser of a specified percentage or the trust accounting income and the trust accounting income was less than the specified percentage.[924]

7. *Former and Transition Rules Applicable to Changes in the Capital Gains Rates (1997–2005)*

Although the former and transition rules are unlikely to affect any current trust returns, the historical reference may be useful in interpreting existing trusts' carryovers or previous years' returns or workpapers.

In 2003, the IRS issued proposed regulations[925] to update the tier rules (now "category and class" rules) to take into account changes to the tax rates applicable to capital gains and certain dividends that were made by the Taxpayer Relief Act of 1997 (TRA '97),[926] the IRS Restructuring and Reform Act of 1998 (1998 Act),[927] and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA).[928]

under the pre-TRHCA rules, the regulations provided that the grantor trust rules of §671 through §678 were never applicable with respect to a CRT. Former Reg. §1.664-1(c).

[919] Pub. L. No. 91-172.

[920] §6654(l).

[921] Pub. L. No. 109-432, §424.

[922] See also 452 T.M., *Tax-Exempt Organizations — Reporting, Disclosure, and Other Procedural Aspects.*

[923] Former §6034(a), former §6034(b); Reg. §1.6034-1(a), §1.6034-1(b); Rev. Proc. 83-32, §3.

[924] §664(d)(3)(A).

[925] REG-110896-98, 68 Fed. Reg. 65,419 (Nov. 20, 2003). The IRS proposed that the regulations would apply to taxable years ending after November 20, 2003, with earlier effective dates for certain provisions.

[926] Pub. L. No. 105-34, §311. The TRA '97 introduced three categories of long-term capital gain property, taxable at rates of 20%, 25%, and 28%, under §1(h). The TRA '97 did not specify what impact the three-tier system would have upon the §664(b) income ordering rules. The IRS responded by providing initial guidance in Notice 98-20, pending the issuance of proposed regulations. *See also* Notice 97-59 (providing general netting rules for different classes of capital gains and losses). Notice 98-20 stated that the underlying policy of the §664(b) tier rules is to ensure that undistributed income taxed at the highest rate is distributed first to the beneficiary before distributions of lower-taxed income. In line with that policy, the Notice provided that distributions of long-term capital gain by a CRT would be deemed to be made first out of 28% gains, then out of 25% gains, and finally of 20% gains. In addition, the Notice stated that if a CRT had undistributed long-term capital gains that it realized before 1997, it could treat those as 20% gains when distributing them. If a long-term gain was realized by the trust from January 1, 1997, through May 6, 1997, the Notice required the gain to be treated as a 28% gain when distributed to the beneficiary. Notice 98-20 observed that §1(h) gave the IRS authority to issue regulations on the application of the long-term capital gains rates to pass-through entities, such as CRTs. The Notice stated that proposed regulations, when published, would be effective for taxable years beginning after 1997, but that the Notice could be relied upon for the 1997 taxable year.

[927] Pub. L. No. 105-206, §5001, §6005. The 1998 Act further amended §1(h) to reduce the holding period for long-term capital gains from 18 months to one year, effective for taxable years ending after December 31, 1997. The 1998 Act's amendment of §1(h) also clarified the order in which the different classes of capital gains (20%, 25%, and 28%) had to be taken into account at the entity level, but §1(h) still left to the IRS the task of determining the treatment of distributions from a CRT. Subsequently, the Tax and Trade Relief Extension Act of 1998, Pub. L. No. 105-277, §4002, added former §1(h)(13)(D), which provided a special rule for determining the §1(h)(4) 28% gain (from collectibles and §1202 gain) and the §1(h)(6) unrecaptured §1250 gain (taxed at 25%) with respect to a distribution from a CRT. Former §1(h)(13)(D) directed that, in computing the amount of such gains in a distribution from a CRT, the former 28% long-term gain for property held more than one year but less than 18 months was not taken into consideration. The IRS, in Notice 99-17, modified Notice 98-20 to take into account the enactment of former §1(h)(13)(D). Notice 99-17 concluded that the effect of former §1(h)(13)(D) was to change the treatment of distributions of gains that were realized by the trust in 1997. Under former §1(h)(13)(D), any 28% gain (other than collectibles gains) realized in 1997 was to be treated as 25% or 20% gain if distributed by the trust in taxable years ending after 1997. Because Notice 98-20 mandated that all pre-1997 gains be treated as 20% gains, the issuance of Notice 99-17 meant that, for distributions made in taxable years after 1997, the only long-term capital gains taxed at the 28% rate would be those attributable to the sale or exchange of collectibles. Former §1(h)(13) was struck as deadwood for tax years beginning after December 31, 2000. *See* Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), Pub. L. No. 107-16, §101(c), as extended by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (2010 TRA), Pub. L. No. 111-312, §101(a), and made permanent by the American Taxpayer Relief Act of 2012 (ATRA), Pub. L. No. 112-240, §101(a).

[928] Pub. L. No. 108-27, §301, §302. JGTRRA enacted §1(h)(11), which treats a noncorporate shareholder's "qualified dividend income" as net capital gains rather than ordinary income, effective for tax years beginning after December 31, 2002. Also, for tax years ending after May 5, 2003, JGTRRA amended §1(h) to generally provide for a 15% maximum tax rate on long-term capital gains. The Working Families Tax Relief Act of 2004, Pub. L. No. 108-311, §402, amended §302 of JGTRRA to provide that, in the case of passthrough entities, including trusts, the JGTRRA amendments relating to qualified dividend income are effective for tax years ending after December 31, 2002, except that dividends received by such an entity on or before that date would not be treated as qualified dividend income. For a discussion of the current §1(h) long-term capital gain rates (0% to 28%), including changes made by ATRA, Pub. L. No. 112-240, §102 (effective for tax years beginning after 2012), and the Tax Cuts and Jobs Act, Pub. L. No. 115-97, §11001 (effective for tax years beginning after December 31, 2017), see 507 T.M., *Income Tax Liability: Concepts and Calculation* (*U.S. Income Series*); specifically, a maximum 20% rate generally applies to long-term capital gains and qualified dividends for taxpayers in the highest (39.6%) §1 regular income tax bracket

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

In 2005, the IRS finalized the proposed regulations, with some modifications, generally effective for taxable years ending after November 20, 2003.[929] As explained in the preamble to the proposed regulations, the final regulations: (i) incorporate the guidance on the treatment of capital gains under §664(b)(2) provided in Notice 98-20, as modified by Notice 99-17; (ii) provide guidance for netting different classes of capital gains and losses based on Notice 97-59; and (iii) provide guidance on the treatment of qualified dividend income under §664(b)(1).

B. Prior Calculation Rules

1. Treatment of Contingencies Before the Tax Reform Act of 1984

Before the Tax Reform Act of 1984,[930] the IRS had ruled that a charitable remainder trust (CRT) was not qualified if it terminated on a beneficiary's remarriage, because the duration of the trust was not based on either a term not in excess of 20 years or a life (or lives) in being.[931] A trust could qualify if the annuity or unitrust amount payable to a spouse was reduced, but not discontinued, on the occurrence of a specified event (e.g., remarriage) and the amount of the reduction was thereafter paid to the charitable remainder beneficiary.[932] However, an estate tax charitable deduction was not allowed for the value of the contingent annuity or unitrust amount that would be payable to the charitable remainder beneficiary on the beneficiary's remarriage.[933]

The Tax Reform Act of 1984 added §664(f), which allows noncharitable annuity and unitrust payments to end upon the occurrence of a "qualified contingency" and, thereby, accelerates the charitable remainder interest. A contingency is qualified provided it does not extend the duration of the otherwise allowable trust term. The existence of a qualified contingency is not taken into account for purposes of determining the value of any charitable contribution or the actuarial value of any interest. Section 664(f) applies to transfers made after December 31, 1978.

2. Deduction Calculations for Valuation Dates Before May 1, 1989

If the appropriate valuation date for the charitable remainder interest was after November 30, 1983, and before May 1, 1989, the present value of the charitable remainder is determined under Reg. §20.2031-7A(d)(6), Tables A and B, which use an assumed 10% interest rate.[934]

> *Example:* On January 1, 1988, a grantor who is nearer age 60 transfers property with a net fair market value of $100,000 to an annuity trust and retains an annuity, payable annually on December 31, of $5,000 for life. The present value of the annuity equals the factor for age 60, taken from Table A of Reg. §20.2031-7A(d)(6), which is 7.4491, multiplied by the amount of the retained annuity ($5,000), or $37,246. The value of the charitable remainder interest equals $62,754 ($100,000 – $37,246).

Where the annuity is payable for a term certain, the grantor must use a factor from Table B of the regulations to compute the present value of the annuity.[935] In the alternative, if the annuity is measured by the life of the survivor of two or more individuals or a term certain concurrent with one or more lives, the grantor must use a special factor.[936] Finally, if an annuity is payable at the end of less than annual periods (e.g., quarterly or semiannually), or if the payment of an annuity is to be made at the beginning of the payment period, special adjustments must be made to the Table A or Table B factors.[937]

For unitrust transfers made after November 30, 1983, and before May 1, 1989, the adjusted payout rate is determined using Table F(1) in Reg. §1.664-4A(d)(6). If the transfer was made after April 30, 1989, and before May 1, 1999, and the unitrust amount is payable for the life of an individual, it is necessary to use Table U(1) in Reg. §1.664-4A(e)(6) to calculate the unitrust adjustment factor.

3. Deduction Calculations Before the Issuance of the Regulations Under §7520

Notice 89-24[938] contained guidelines for the valuation of interests in accordance with §7520 before the IRS published regulations. In particular, the Notice contained a formula that, together with the applicable monthly discount rate, could determine the value of an annuity interest for a term of years in a charitable remainder annuity trust (CRAT). Also, before the publication of tables in the regulations, Notice 89-60 provided some of the tables necessary to calculate the value of interests

---

(ATRA), and capital gains rates are affixed to thresholds under a "maximum zero rate amount" and a "maximum 15% rate amount" (2017 Act).

[929] T.D. 9190, 70 Fed. Reg. 12,793 (Mar, 16, 2005); Reg. §1.664-1(d)(1)(ix). The rules requiring long-term capital gains to be distributed in a specified order and the rules providing for the netting of capital gains and losses apply to taxable years ending on or after December 31, 1998. The rule in the second sentence of Reg. §1.664-1(d)(1)(vi) (including long-term capital gains or losses the trust properly took into account before 1997 in the all other long-term capital gains and losses category) applies to taxable years ending on or after 1998. The rule in the third sentence of Reg. §1.664-1(d)(1)(vi) (including long-term capital gains and losses the trust properly took into account on or after January 1, 1997, and before May 7, 1997, if not treated as distributed in 1997, in the all other long-term capital gains and losses category) also applies to distributions made in taxable years ending on or after 1998.

[930] Pub. L. No. 98-369.

[931] Rev. Rul. 76-291.

[932] Rev. Rul. 76-291.

[933] Rev. Rul. 76-291.

[934] Reg. §25.2512-5A(d)(6), the gift tax regulations for the valuation of pre-May 1, 1989, annuity interests, cross referencing the estate tax valuation tables in Reg. §20.2031-7A(d)(6). The tables in the regulations are based upon a 10% discount rate and are gender neutral. May 1, 1989, is the effective date of §7520. *See* Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, §5031. Reg. §20.2031-7A governs the valuation of annuities for which the valuation date is before May 1, 2009. Any transfer after December 31, 1970, and before December 1, 1983, is subject to the 6% gender-specific valuation tables that were set forth in former Reg. §20.2031-10 and §25.2512-9 before their amendment by T.D. 8540, 59 Fed. Reg. 30,100 (June 10, 1994). *See also* Reg. §20.2031-7A(c). Reg. §20.2031-7A(d)(1), §25.2512-5A(d)(1)(i)(B), and §25.2512-5A(d)(1)(i)(C) contain transitional rules under which an election can be made to have the 6% tables, rather than the 10% tables, apply to certain transfers made after November 30, 1983.

[935] Reg. §20.2031-7A(d)(6).

[936] Reg. §20.2031-7A(d)(5), §25.2512-5A(c). Some of these factors were published in former IRS Publication 723E, *Actuarial Values II: Factors at 10 Percent Involving One and Two Lives.*

[937] Reg. §20.2031-7A(d)(2), §25.2512-5A(d)(2).

[938] A transferor could rely on Notice 89-24 in lieu of the §7520 regulations if the transfer was made after April 30, 1989, and before June 10, 1994, the date the regulations were issued. Reg. §1.7520-4(a), §20.7520-4(a), §25.7520-4(a).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

in CRTs and pooled income funds. Factors for determining the value of a charitable remainder interest in a single life annuity trust were found in Table R(1) using the age of the income beneficiary and the applicable interest rate. Factors for determining the value of the charitable remainder interest where the noncharitable interest was for a term certain were found in Table B. Notice 89-24 and Notice 89-60 were both superseded by the publication of regulations.

4. Prior Marital Deduction Provisions

The Economic Recovery Tax Act of 1981 (ERTA)[939] enacted §2523(g), providing that a gift tax marital deduction is available for the gift of an annuity or unitrust interest in a CRT to the donor's spouse as the sole noncharitable beneficiary other than the donor. Before the enactment of §2523(g), the gift of an annuity or unitrust interest to a spouse was considered a nondeductible "terminable interest." ERTA also added §2523(f), which allows a donor to elect the §2523(a) marital deduction for a transfer in which his or her spouse receives a life income interest (the QTIP provisions). Transfers to a CRT in which the transferor's spouse receives the annuity or unitrust interest are not eligible for the QTIP election, since the spouse will not receive a qualifying income interest in the property. See the gift tax discussion at IV.I., above. However, for CRTs established before October 24, 1992, the marital QTIP deduction was available, if elected, for the value of the annuity or unitrust interest.

5. Estate Tax Deduction for Successor Annuity or Unitrust Interests Before Boeshore

In Rev. Rul. 76-225, the IRS ruled that an estate tax charitable deduction was not allowable for the value of an annuity interest in a CRAT passing to a §170(c) organization upon the death of the individual recipients. The ruling held that the payment did not constitute a "guaranteed annuity interest"[940] and, therefore, was not deductible. A gift tax charitable deduction presumably would not be allowed under similar circumstances, because the rules for obtaining a gift tax charitable deduction in the case of a guaranteed annuity are similar to those governing the estate tax deduction. In PLR 8845012, however, the IRS approved the reformation of a defective CRT and allowed an estate tax charitable deduction for a portion of the annuity amount payable to charity. PLR 8845012 does not refer to Rev. Rul. 76-225 and simply states that the portion of the annuity amount payable to charity constitutes a qualified annuity interest within the meaning of §2055(e)(2)(B). It may be possible to distinguish PLR 8845012 on the basis that, unlike Rev. Rul. 76-225, the annuity amount was payable immediately. Such a distinction, however, would not be persuasive for income tax purposes, given the clear language of the regulations.

Rev. Rul. 76-225 was revoked by T.D. 9068,[941] which conformed the estate, gift, and income tax regulations to the Tax Court's decision in *Estate of Boeshore v. Commissioner*.[942] The preamble states that the effect of the regulations is to allow an estate, gift, or income tax charitable deduction for charitable annuity or unitrust interests that are preceded by a noncharitable unitrust or annuity interest. However, Reg. §1.664-2(d) and §1.664-3(d) still preclude an income tax deduction for the value of the charitable interests other than the remainder interest in the CRT.

---

[939] Pub. L. No. 97-34.

[940] *See* Reg. §20.2055-2(e)(2)(v).

[941] 68 Fed. Reg. 40,130 (July 7, 2003).

[942] 78 T.C. 523 (1982), *acq.*, 1987-1 C.B. 1. *Boeshore* held invalid the regulation disallowing an estate tax deduction for a CRT with a private interest that preceded a charitable interest.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Part 2: Charitable Gift Annuities

XII. Charitable Gift Annuities: Introduction

No discussion of charitable remainder trusts (CRTs) can be complete without a discussion of charitable gift annuities. In many respects, charitable gift annuities are comparable to charitable remainder annuity trusts (CRATs); in each case an annuity is payable either to the donor or others and in each case the charitable income or estate tax deduction is computed in the same manner. There are also substantial differences, however, and in many cases the charitable gift annuity is preferable. Because the charity issuing the annuity is typically a public charity, the self-dealing rules and other private foundation restrictions that apply to transactions between charitable remainder trusts do not apply. In addition, the way gift annuities are taxed is often superior to taxation under the charitable remainder trust tier system. It may also be possible for individuals who cannot create a qualifying annuity trust because of the 5% exhaustion rule of Rev. Rul. 77-374 to create a gift annuity instead.

A. Basic Concept

A charitable gift annuity is one of the oldest planned giving vehicles. The first gift annuity was apparently issued by the American Bible Society in 1843.[943] The concept is simple: the donor transfers cash or other assets, typically marketable securities, to a charitable organization in exchange for the unfunded contractual promise of the charity to pay the donor, or the donor and another person, an annuity for life. Charitable gift annuities, unlike charitable remainder trusts, are not a creature of statute. The charitable gift annuity is, in effect, a bargain sale in which the donor purchases something from the charity — in this case an annuity — for more than its actual value with the excess deductible as a charitable contribution. Because the annuitant will be relying on an unsecured promise of the charity to pay the annuity, donors need to be satisfied that the issuing charity will be solvent and able to pay the annuity. Similarly, charities should not undertake a gift annuity program unless they have adequate resources to fund it. Most charities will find it prudent to segregate funds received for gift annuity purchases from other charitable assets and set those aside untouched for any particular annuitant until there are no more noncharitable interests in a particular annuity.

B. Legislative Background

Perhaps surprisingly, charitable gift annuities are not specifically authorized by the Code. In contrast, charitable remainder trusts are described in detail in §664 and the regulations under that section. The only references to charitable gift annuities in the Code are found in §514, dealing with unrelated business income and discussed hereafter; §170(f)(10)(D), dealing with personal benefits contracts; and §501(m)(5). Section 501(m) provides that certain organizations providing commercial-type insurance are not exempt from tax, and §501(m)(3) and §501(m)(5) exempt charitable gift annuities from the definition of commercial-type insurance.

---

[943] One of the first documented cases of a charitable gift annuity involved the celebrated painter John Trumbull (1756–1843), whose painting of the signing of the Declaration of Independence you may have seen hanging in the U.S. Capitol building in Washington. Destitute in his old age, Trumbull agreed to transfer over 100 of his paintings to Yale University in exchange for an annual annuity of $1,000. Another early gift annuity was apparently issued in 1843 by the American Bible Society, which still issues CGAs.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XIII. Structuring the Gift Annuity

A. *Bargain Sale Treatment*

Because the charitable gift annuity is treated for tax purposes as a bargain sale, some background about bargain sales is useful. A bargain sale is simply the transfer of cash or property by a donor to a charity in exchange for payment by the charity of less than the fair market value of the cash property transferred. The excess of the value of the property transferred over the payment received by the charity is deductible as a charitable contribution.

> *Example:* Donor transfers undeveloped land worth $1,000,000 to a charity in exchange for the charity's payment of $600,000. The difference between the $600,000 purchase price and the $1,000,000 fair market value of the property ($400,000) is deductible as a charitable contribution.

If the annuity is purchased with appreciated property, the donor's basis must be allocated between the gift portion and the sale portion, resulting in loss of the benefit of basis to the extent it is allocated to the charitable portion. This is discussed in more detail under Taxation of Annuity Payments at XIII.C.2., below. Although charitable gift annuities, like charitable remainder annuity trusts (CRATs), provide a fixed annuity, there are many differences. Not only are the payments taxed in a different manner, but, as discussed in more detail below, gift annuities issued by public charities are not subject to the private foundation rules made applicable to charitable remainder trusts by §4947. Creative planning techniques taking advantage of this difference are discussed below. In addition, gift annuities can be deferred. On the other hand, CRATs can be established for a term of years or for more than two lives (assuming they pass the 5% exhaustion and 10% remainder tests).

B. *Setting the Annuity Rate*

Most charities follow the recommended annuity rates issued by the American Council of Gift Annuities (ACGA), which has been making maximum suggested rates available for many years.[944] The recommended maximum rates are unisex and age-based, with the payout increasing with age, and are issued for both one life and for two lives on a joint and survivor basis. Because the gift annuity presumes a charitable element, the annuity rates are set so that for a large enough pool of annuitants, on average about 50% of original contributions should be left for the charity after the deaths of the annuitant or the annuitants. The suggested rates change from time to time as prevailing interest rates and market yields change. The suggested rates were most recently amended effective January 1, 2024. The maximum suggested rates are available from the American Council on Gift Annuities.[945]

C. *One Life Annuities*

1. *Calculating the Deduction*

Although the regulations under §170 provide that the charitable deduction is measured by the amount contributed over the cost of a comparable commercial annuity,[946] since 1984 it has been clear that the value of the annuity is calculated for charitable deduction purposes by reference to the IRS tables found in the regulations under §2031 and §2512.[947] As a result, the charitable deduction will be the same regardless of whether the annuity being valued is the annuity retained in a charitable remainder trust (CRT) or a charitable gift annuity.[948] The IRS actuarial tables can be found in IRS Publication 1457 as well as in the §2031 regulations, which provide as follows:[949]

> (A) If the interest to be valued is the right of a person to receive an annuity that is payable at the end of each year for a term of years or for the life of one individual, the present value of the interest is computed by multiplying the aggregate amount payable annually by the appropriate annuity actuarial factor (that corresponds to the applicable section 7520 interest rate and annuity period). Internal Revenue Publication 1457 includes actuarial factors for a remainder interest in Table B (after an annuity payable for a term of years) and in Table S (after an annuity payable for the life of one individual when the valuation date is on or after June 2, 2023).
>
> (B) If the annuity is payable at the end of semiannual, quarterly, monthly, or weekly periods, the product obtained by multiplying the annuity factor by the aggregate amount payable annually is then multiplied by the applicable adjustment factor as contained in Table K in paragraph (d)(6) of this section for payments made at the end of the specified periods.[950]

---

[944] Although annuity rate fixing might appear to be a violation of federal antitrust laws, the Charitable Gift Annuity Antitrust Relief Act of 1995, Pub, L. No. 104-63, exempts charities issuing gift annuities based on ACGA rates from antitrust laws. Since purchasers of gift annuities are primarily motivated by a desire to help charity, the Philanthropy Protection Act of 1995, Pub. L. No. 104-62, similarly exempts charities issuing charitable gift annuities from application of most aspects of federal securities laws so long as donors are provided with certain basic information. Charities issuing gift annuities should be aware, however, that state insurance regulators may require registration, specific annuity contract language, prior notification, reserve requirements, or other actions. The Philanthropy Protection Act is discussed at XXVIII.A., below.

[945] American Council on Gift Annuities, *Current Gift Annuity Rates* (available at https://www.acga-web.org/current-gift-annuity-rates).

[946] Reg. §1.170A-1(d)(1).

[947] The IRS ruled in Rev. Rul. 62-137 that for purposes of §72 of the Code, the aggregate amount of consideration paid (the investment in the contract) in the case of life annuity contracts issued by an organization "such as a corporation, trust, fund, or foundation" other than an insurance company would be measured by reference to the cost of a comparable contract issued by an insurance company. This was superseded by Rev. Rul. 84-162, which provided that the valuation tables in Reg. §25.2512-5 of the gift tax regulations and §20.2031-7 of the estate tax regulations are to be used in valuing annuity contracts issued after November 23, 1984, by such a corporation, trust, fund, or foundation other than an insurance company.

[948] There may be one difference: because the regulations under §7520 require that the probability of trust exhaustion be taken into account in valuing annuities issued by trusts, there is an argument that a slightly enhanced charitable deduction may be available to a donor to a CRT that has a probability of exhaustion greater than zero but less than 5%. In addition, charitable remainder annuity trusts must pass the 5% exhaustion test of Rev. Rul. 77-374 to qualify at all.

[949] Reg. §20.2031-7(d)(2)(iv), §25.2512-5(d)(2)(iv), T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (effective June 1, 2023).

[950] If the payments are made at the beginning rather than the end of each payment period, the applicable adjustment factor is found in Table J rather than

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

The following example illustrates calculation of a life annuity from the IRS tables:

Example: In April 20X1 Donor, age 69, purchases a charitable gift annuity from Charity X for $100,000, payable quarterly at the end of each quarter. The American Council on Gift Annuities maximum recommended annuity is 6.0%, or $6,200. The donor is therefore entitled to receive an annuity of $6,200 a year for life. The §7520 rate for April 20X1 is 5.4%. Under Table S (available at https://www.irs.gov/retirement-plans/actuarial-tables), the annuity factor at 5.4% for an individual aged 69 is 10.0657. Under Table K, the adjustment factor for payments made at the end of each quarter at the rate of 5.4% is 1.0200. The amount of $6,200 is multiplied by the factor 10.0657, and the product is multiplied by 1.0200. The present value of the annuity is, therefore, $62,407 and the charitable remainder is worth $100,000 − $62,407 = $37,593.

Note that the IRS tables to do not provide annuity factors for two lives. The two-life factor can be determined by subtracting the remainder factor from 1 and dividing it by the applicable §7520 rate.

Example: The IRS Tables provide that at the July 20X1 §7520 rate of 4.6%, the actuarial value of the remainder after two lives ages 70 and 75 is .46095. The number 1 minus .46095 = .53905, and .53905 ÷ the section 7520 rate of 4.6% equals the annuity factor of 11.7185.

Practice Point: Software is now available for calculation of these factors.

2. Taxation of Annuity Payments

Although a charitable gift annuity generates the same tax deduction as a CRAT, payments are taxed to the annuitant under the §72 rules for taxing commercial annuities. In the case of a commercial annuity, the annuitant's basis in the annuity (i.e., the "investment in the contract") is spread over the annuitant's life expectancy and recovered tax free. The remaining portion of each payment from a commercial annuity is taxed as ordinary income. Once the annuitant has completely recovered the basis in the contract, the payments received thereafter are fully taxable.[951] In the case of a charitable gift annuity with an annuitant who dies before life expectancy — and has, therefore, not fully recovered the investment in the contract — the remaining unrecovered basis is allowed as a charitable deduction on the annuitant's final income tax return. Calculation of the taxation of the annuity payments from a charitable gift annuity is more complicated because a charitable gift annuity is a bargain sale; the investment in the contract is not the amount contributed in exchange for the annuity but that portion of the purchase price that is attributable to the purchase of the annuity. The purchase price is easily determined by subtracting the amount contributed from the portion that is deductible as a charitable contribution. What remains is the purchase price of the annuity. The annuitant's (or annuitants') life expectancy(ies) is (are) not derived from the §7520 mortality assumptions used to calculate the charitable deduction, but from the §72 return multiples found in tables V and VI. The return multiples are simply years of life expectancy. The return multiple found in the table must then be adjusted up or down to reflect frequency of payment.

Example: A donor whose nearest age is 70 contributes $100,000 to Charity X in exchange for an immediate charitable gift annuity payable quarterly at the end of each quarter. The donor elects to use the §7520 rate in effect for the month of the gift. That rate is 3.4%. Charity X issues gift annuities at maximum American Council on Gift Annuities rates. The ACGA rate at age 70 is 5.6%, so the annual annuity is $5,600. Using the calculation method described above, the charitable deduction is $36,178.48. Therefore, the amount of the contribution allocable to the cost of the annuity (the "investment in the contract") is $100,000 minus $36,178.48, or $63,821.52. The donor's life expectancy (the section 72 Table V return multiple) is 16.0. If payments are made other than monthly the return multiple must be adjusted using the frequency of payment adjustment table found at Reg. §1.72-5:

Table K. Reg. §20.2031-7(d)(2)(iv)(C), §25.2512-5(d)(2)(iv)(C), *as amended by* T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023), applicable on or after June 1, 2023.

[951] Before the 1986 tax law changes, the annuity continued to be partly nontaxable even after the annuitant had recovered investment in the contract over life expectancy.

If the number of whole months from the annuity starting date to the first payment date is	0–1	2	3	4	5	6	7	8	9	10	11	12
And payments under the contract are to be made												
Annually	+5	+4	+3	+2	+1	0	0	−.1	−.2	−.3	−.4	−.5
Semiannually	+2	+1	0	0	−.1	−.2	…	…	…	…	…	…
Quarterly	+1	0	−.1	…	…	…	…	…	…	…	…	…

Because the annuity is payable at the end of each quarter, the return multiple of 16 is adjusted by subtracting 0.1. The resulting adjusted return multiple is 15.9 years. The expected return over the annuitant's lifetime is the annual annuity of $5,600 times 15.9 or $89,040. That expected return divided by the value of the annuity, i.e., $63,821.52, produces an exclusion ratio 71.7%. Thus, 71.7% of $5,600, or $4,015.20, of each year's $5,600 annuity pay-

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

ment is excluded from income and $1,584.80 of each year's annuity payment is taxable. After 15.9 years, the entire investment in the contract will have been recovered and all of the annuity will be taxable.[952] If the annuity is for two lives, the calculation is the same except that the return multiple would come from the two-life Table VI. In order that no basis go unrecovered, as with commercial annuities, a deduction is permitted by §72(b)(3) on the annuitant's final income tax return for any unrecovered investment in the contract; this is true whether or not the annuitant was the purchaser of the contract.

Practice Point: This deduction is still available despite the suspension through 2025 of miscellaneous itemized deductions defined in §67. That is because §67 defines "miscellaneous itemized deductions" as itemized deductions *other than*, among other things, "the deduction under section 72(b)(3) (relating to deduction where annuity payments cease before investment recovered)."[953]

3. Annuity Purchased with Appreciated Property

If the annuity is purchased with appreciated property, the calculation is more complicated. In that case, the basis and gain are allocated between the gift portion and the portion attributable to purchase of the annuity. If the annuitant is the purchaser of the annuity and the annuity is nonassignable, the portion of the gain allocated to the purchase of the annuity is spread over the annuitant's life expectancy and reduces (but not below zero) what otherwise would have been non-taxable return of basis.

Example: The facts are the same as in the example in XIII.C.2., above, except that the annuity is purchased with $100,000 of appreciated securities held for more than a year with a basis of $40,000. Because part of the basis must be allocated to the charitable portion, some of the value of that basis is lost. The annuity value of $63,821.52 is 63.82152% of the total amount contributed. Thus, 63.82152% of the $60,000 gain ($100,000 − $40,000), or $38,292.91, will be spread over the donor's life expectancy of 15.9 years. Therefore $2,408.36 ($38,292.91 ÷ 15.9) of each payment will be capital gain. That leaves only $1,606.84 as nontaxable income each year, and, as in the first example, $1,584.80 to be taxed as ordinary income.

If the purchaser is not the annuitant, the gain is recognizable immediately. In the two-life situation, if the donor is the sole owner of the appreciated property, the gain will be spread over that person's life only. A common strategy where annuitants are spouses and only one spouse owns the appreciated property used to purchase the annuity is to transfer the property to joint name so that both spouses can be the purchaser. In that case the gain can be spread over both life expectancies, resulting in less gain being recognized each year.[954]

Caution: If the annuity is granted in an employment context, §83 may cause the employee to be taxed immediately on the discounted value of the annuity.

4. Electing the Section 7520 Rate in Valuing the Annuity

Effective on January 1, 2018,[955] charities now have many more donors who do not itemize. They should, therefore, take special care in working with donors who purchase charitable gift annuities. Section 7520 provides that in valuing a gift any part of which is deductible as a charitable deduction, the donor can elect the §7520 rate for the month of the transfer or either of the two prior months.[956] In the case of charitable gift annuities, choice of a higher interest rate produces a higher charitable deduction. Choice of a lower interest rate produces a lower charitable deduction but results in more of each payment being excludible from income as part of the nontaxable return of basis in the contract. Because fewer people will be itemizing, perhaps the default for charities issuing gift annuities is to opt for the lower interest rate for reporting purposes. Even better, of course, is to inquire of each donor when the annuity is issued whether the donor itemizes and, if the donor does itemize, whether a higher income tax deduction or exclusion of more of each payment is preferred.

Example: In July 20X1, a donor, age 70, purchases a $100,000 charitable gift annuity with cash. The annuity will be paid quarterly at the American Council on Gift Annuities recommended annuity rate of 5.6%, or $5,600. If the donor defaults to the July 20X1 §7520 rate of 4.6%, the income tax deduction will be $41,910.64 and $3,651.20 of each year's $5,600 annuity will be excludable from income. However, if this non-itemizing donor had elected to use the May 20X1 §7520 rate of 4.2%, the amount of each payment excluded from income each year would have been $3,768.80 until the donor's basis in the contract was fully recovered over the next 15.9 years.

---

[952] A different scheme was in effect before 1987. Prior to amendment of §72(b), the exclusion ratio continued to be applied even after all of the basis was recovered.

[953] §67(b)(10).

[954] Taxation of non-charitable private annuities purchased with appreciated property is radically changed by proposed regulations, REG-141901-05, 71 Fed. Reg. 61,441, issued on October 18, 2006. Once those regulations are effective, in the case of a private annuity the purchase with appreciated property will result in immediate recognition of gain, i.e., gain cannot be spread out over the annuitant's expected life. The IRS had this to say about charitable gift annuities purchased with appreciated property: "This notice of proposed rulemaking does not propose to change the existing regulations in §1.1011-2. However, comments are requested as to whether a change should be made in the future to conform the tax treatment of exchanges governed by section 1.1011-2 to the tax treatment prescribed in these proposed regulations." Preamble to REG-141901-05. The IRS has taken no steps since to indicate its intentions with regard to charitable gift annuities purchased with appreciated property.

[955] Under the Tax Cuts and Jobs Act, Pub. L. No. 115-97.

[956] A link to a model election is in the Additional Resources section below.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XIV. Deferred Gift Annuities

A major difference between charitable gift annuities and charitable remainder trusts is that payments from charitable gift annuities can be deferred. This can be a useful tool for individuals who would like to generate an income tax deduction during their high-tax earning years while also providing a stream of income for retirement. As with current gift annuities, most charities follow American Council on Gift Annuities (ACGA) deferred gift annuity rates. The method for determining the rate, however, is somewhat more involved than simply looking at the ACGA rate table, and takes several steps:[957]

1. Determine the annuity starting date, which is:

   - One year before the first payment, if payments are made annually.
   - Six months before the first payment, if payments are made semi-annually.
   - Three months before the first payment, if payments are made quarterly.
   - One month before the first payment, if payments are made monthly.

2. Determine the number of whole and fractional years from the date of the contribution to the annuity starting date (the deferral period). Express the fractional year as a decimal of four numbers.

3. Use the following formula to determine the compound interest factor:[958]

   - $F = 1.0425^d$, where

     — F is the compound interest factor, and

     — d is the deferral period

   Example: If the period between the contribution date and the annuity starting date is 10.25 years, the compound interest factor would be $1.0425^{10.25} = 1.532074$.

4. Multiply the compound interest factor (F) by the immediate gift annuity rate for the nearest age or ages of a person or persons at the annuity starting date.

   Example: If the sole annuitant will be nearest age 65 on the annuity starting date and the compound interest factor is 1.532074, the deferred gift annuity rate would be 1.532074 times 5.4%, or 8.3% (rounded to the nearest tenth of a percent.)

A. Calculating the Deduction

Calculation of the value of a one life deferred gift annuity is more complicated for an immediate annuity; most practitioners will use software for this purpose. But the basic idea is simple: take the annuity factor for an immediate annuity beginning at the starting age and multiply it by both a discount factor for the period of deferral and the probability of survival from the annuitant's age with annuities issued until the annuity starting date. Calculation of the value of a two-life deferred gift annuity is an extremely complex, many-step process; practitioners will almost invariably require software for this purpose.

B. Taxation of Annuity

Once the values of the annuity and charitable portions have been determined, taxation of each annuity payment is calculated in the same manner as for an immediate annuity described above, whether or not appreciated property has been used.

---

[957] New York and New Jersey may require different interest factors for deferred gift annuities with longer deferral periods.

[958] The ACGA website should be consulted to determine if the discount factor is still current.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XV. Gift Tax Rules

A. One Life Immediate Gift Annuity

The purchaser of a one life annuity for the donor's life makes a gift of the remainder interest to charity that qualifies for the gift tax charitable deduction. The purchaser of a one life annuity for a life other than the donor makes a gift of the life income interest, but the gift qualifies for the §2503 gift tax present interest exclusion.[959] If the donor retains the right to revoke the income interest, no gift is made at the time the annuity is purchased; however, a gift is made with each annuity payment that qualifies for the gift tax annual exclusion. Retention of the right to revoke causes the remaining value of the annuity to be included in the donor's estate for estate tax purposes.

B. Two Life Immediate Gift Annuity for Donor and a Second Person

The purchaser of an annuity for the donor's life followed by a second life makes a gift of the successor income interest as well as a gift of the remainder (which qualifies for the gift tax charitable deduction). However, because the survivorship interest will not commence until the future, it does not qualify for the present interest annual exclusion under §2503.[960] The taxable gift of the successor income interest can be avoided by retaining the right to revoke the successor income interest, which will also cause estate tax inclusion at the donor's death of the value of the remaining life interest. The purchaser of a joint and survivor annuity makes a current gift of a portion of the annuity payments to the other joint annuitant, but, because that annuity interest commences immediately, it will qualify for the gift tax annual exclusion.

C. Deferred Gift Annuity

Because a deferred gift annuity will commence only in the future, is likely that the IRS would characterize the annuity as a future interest not qualifying for the present interest gift tax exclusion. That conclusion is reinforced by the fact that, as noted above, gift annuity contracts invariably prohibit assignment of the contract to prevent present taxation of the stream of payments. This feature seems to make gift annuities different from other assets, such as term life insurance policies, which provide for payment only in the future.

D. Marital Deduction Gift Tax Issues

The marital deduction issues involved in charitable gift annuities are surprisingly complex. If the donor's spouse is the only annuitant, the gift qualifies for the gift tax marital deduction because it is not a terminable interest; no interest passes to someone other than spouse at termination of interest. If the contract provides for payment of an annuity to the donor for life and then to the donor spouse for life, it is not clear whether the marital deduction is available for the spouse's survivorship interest. Section 2523(f)(6) provides for a marital deduction for the spouse's survivorship interest in a joint and survivor annuity only. In that case, the donee spouse's interest is treated as a qualifying income interest for life and the donor spouse is treated as having made a QTIP election unless the donor spouse elects out. What about an annuity for the donor followed by continuing life annuity for the donor's spouse? Because of uncertainty, the donor spouse should retain the right to revoke the survivorship interest. This retention can be an inter vivos or a testamentary right; there is no trust to cause inclusion under §2036, as there would be in the case of a charitable remainder trust. If the annuity may be funded with joint property, each spouse could retain the right to revoke the other spouse's survivorship interest.

---

[959] Under the Taxpayer Relief Act of 1997, Pub. L. No. 105-34, the $10,000 annual exclusion is indexed for inflation in $1,000 increments for calendar years after 1998. *See* §2503(b)(2). For 2018, the annual exclusion is $15,000. Rev. Proc. 2017-58, §3.37(1).

[960] If the taxable gift of the successor annuity is to a non-spouse, the donor and his or her spouse can elect to gift-split. This will equalize the spouses' use of their lifetime exemptions. Gift-splitting is often used to obtain additional annual gift tax exclusions, but those are not allowable for future interests.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XVI. Estate Tax Rules

A. *General Estate Tax Rules*

As with commercial annuities, the death of the annuitant-purchaser of a one life gift annuity ends all rights in the annuity. Because nothing passes to another person, nothing is includible in the decedent's estate. If the annuity continues for another person, the actuarial value of the survivorship interest will be included in the decedent's estate. A marital deduction will be available to the spouse as the successor beneficiary. Charitable gift annuities can be created at death by testamentary transfer so long as the value of the annuity and, therefore, the charitable estate tax deduction are ascertainable at death. This is typically accomplished by providing for payment of an annuity at the American Council on Gift Annuities maximum recommended annuity rate in effect at the decedent's death. The amount of the annuity will depend, of course, on the annuitant's age at the time of the decedent's death and the deferral period, if any. The difference between the amount of the bequest and the actuarial value of the annuity will be deductible as an estate tax charitable deduction.[961]

B. *Marital Deduction Estate Tax Issues*

A gift annuity created at the donor's death for a spouse qualifies for the estate tax marital deduction because it is not a terminable interest; nothing passes to someone else after the spouse's death.[962] If the annuity is created for the donor and then the spouse, a marital deduction is available because the annuity is treated as a QTIP. In that situation, the QTIP election is deemed made automatically unless the decedent's executor elects out of automatic QTIP treatment. A deferred gift annuity may not qualify as no interest passes to the spouse until after the deferral period; it would not qualify as QTIP property.

---

[961] *See* PLR 200230018 (involving purchase of a charitable gift annuity with IRA distributions at death). Because IRA benefits are income in respect of a decedent, it is not clear whether, as a result, the investment in the contract is zero or the face amount of the distribution.

[962] *See* Reg. §20.2056(b)-1(g) *Ex.* 3. Reg. §20.2056(b)-1(f) provides that no marital deduction is allowed if the decedent directs his executor to acquire a terminable interest for his surviving spouse. The donor's will or trust must itself create the interest by means of a bequest to charity in exchange for a gift annuity.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XVII. Taxation of Charitable Organization Issues

As noted previously, charitable gift annuities, unlike charitable remainder trusts, are not creatures of statute. Because charities issuing gift annuities could in a sense be considered competitors of commercial insurance companies, §514(c)(5) carves out a safe harbor for charities issuing gift annuities. If the gift annuity issued meets the requirements of the statute, the issuing charity will not generate unrelated business taxable income on issuance of the annuity. Those requirements are as follows:

(A) the value of the annuity must be less than 90% of the value of the property received in exchange for the annuity;

(B) the annuity must be payable over the life of one or two individuals in being at the time the annuity is issued;

(C) the annuity contract may not guarantee a minimum amount of payments or specify a maximum amount of payments; and

(D) the annuity contract may not provide for any adjustment of the amount of the annuity payments by reference to the income received from the transferred property or any other property.

The requirement that the value of the annuity be less than 90% of the contributed property ensures that charitable gift annuities will not be competitive with commercial annuities.

Practice Point: Annuities issued following American Council on Gift Annuities rate tables will not run afoul of the 10% remainder requirement except in extremely low interest rate environments. Charities should always double check their own software to make certain that the 10% charitable remainder requirement is met.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XVIII. Generation-Skipping Transfer Tax Considerations

Generation-skipping transfer (GST) tax considerations play a role as well. If a donor wishes to create a gift annuity for a grandchild whose parents are living, the grandchild is a skip person and GST exemption must be allocated in an amount sufficient to cover the actuarial value of the grandchild's annuity. This situation will not arise frequently, as most charities have minimum age limits, often 60 years old or older, so gift annuities will not usually be created for skip persons. Section 2652(b)(3) provides that the kind of arrangements that are subject to generation-skipping tax, even though not in the form of a trust, are "arrangements involving life estates and remainders, estates for years, and insurance and annuity contracts."

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XIX. Sophisticated Charitable Gift Annuity Structures

Although in their original form gift annuities were structured as an unvarying annuity amount, whether current or deferred, more sophisticated variations have been developed in more recent decades. One benefit of the lack of detailed statutory and regulatory requirements for gift annuities is that, unlike charitable remainder trusts, gift annuities can be structured as flexible arrangements. These include not only annuities that change in payment amount, but also annuities that are delayed but are subject to commencement at the annuitants' election. As long as the actuarial value of the annuity can be ascertained when the annuity is issued, there is no prohibition against fanciful and creative annuity structures. The key is structuring the annuity so that it can be valued at inception. Planned giving software has been developed by various providers. The annuities are typically structured so that the range of charitable deductions does not vary widely from one to another and so that the amount passing to charity by actuarial calculations would be roughly the same as with the more standard annuities issued in accordance with American Council on Gift Annuities (ACGA) rate tables. This is not dissimilar from the way that some charitable lead annuity trusts are structured, allowing increases of an unlimited amount or even balloon payments.

Deferred annuity variations have also been developed providing for an initial deferral period followed by a window of some years during which the annuitant can elect, or not elect, to have the annuity commence. The longer the annuity is deferred, the higher the annuity payout. In a private letter ruling obtained by the author,[963] the IRS ruled that the annuitant would not have constructive receipt until the annuitant actually began receiving payments, even though the annuitant had the right to request that payments commence at an earlier time in the window. As with increasing, or step, annuities, the annuities must be structured so that the actuarial value of the remainder does not vary depending on when the annuity is commenced. The annuity must be capable of valuation at the time the annuity is issued. Commercial planned giving software is available to make these calculations and projections.

Subject to state law restrictions, almost any kind property can be used to create a gift annuity. Although most charities would not be willing to issue a gift annuity for an illiquid asset, in some cases the charity may be willing to do so because the property contributed may be on the charity's wish list. For example, the donor may own a valuable painting which he or she would like to contribute to an art museum. At the same time, however, the donor may want some income from the gift. The donor could contribute the painting to a museum in exchange for a charitable gift annuity. In cases of contributions of illiquid property that is to be sold, the charity may require payment of an annuity lower than the usual ACGA rates. This is helpful because the charity may know only within a reasonable range what the property is likely to sell for. In such cases, the charity may also require that the annuity be deferred for a reasonable period to allow sale.

[963] PLR 200742010.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XX. Early Termination

If the gift annuitant no longer needs the annuity income, can the annuitant transfer the remaining life interest to the issuing charity? One might at first expect that the deduction would be equal to the actuarial value of the annuity, as would be the case where the donor contributes his or her remaining life income interest in a charitable remainder annuity trust to the charitable remainder beneficiary. Unfortunately, it appears that different treatment applies in case of the surrender of the remaining life interest in a charitable gift annuity. That is because, although the remaining life interest in a charitable remainder trust is a capital asset under §1001(e), a gift annuity, like a commercial annuity contract, is an ordinary income asset. As a result, it appears that only the donor's unrecovered investment in the contract is deductible and, in the case where the entire investment in the contract has been recovered (because the donor has lived longer than the donor's life expectancy when the annuity was issued), no deduction is available.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXI. Planning Options

Because charitable gift annuities are issued by public charities, transactions between the donor and the annuity issuer are not subject to the self-dealing rules that apply to transactions between charitable remainder trusts and disqualified persons. This opens the possibility for various kinds of transactions not possible with a charitable remainder trust. For example, a donor could contribute an office building to a charity in exchange for a gift annuity and lease all or part of the property back at fair market value rent. A donor also could contribute closely held stock to a charity in exchange for a charitable gift annuity, and a family member could later purchase the stock from the charity at its fair market value as determined by independent appraisal.

The absence of self-dealing rules can be helpful in cases where a donor wishes to contribute a residence to charity in exchange for an income interest but wishes to reside in the residence until it is sold. Because of the self-dealing rules, this arrangement is not possible with a charitable remainder trust even if fair market value rent is paid. A gift annuity will work in this situation.

Other sophisticated plans have been suggested as well. In GCM 39826, the IRS looked favorably upon a plan in which family members would purchase deferred charitable gift annuities designed to commence when the annuitant reached college age. At that point, in theory, the student-annuitant could exchange his or her remaining life interest in exchange for tuition. The GCM approved the form of the transaction, which was presumably otherwise in compliance with the §514(c)(5) requirements discussed in XVII., above.

Other transactions may be possible as well that would not be possible with a charitable remainder trust, such as issuance of charitable gift annuities in exchange for S corporation stock. A charitable remainder trust is not a permissible S corporation shareholder, but a public charity is. The downside to public charity ownership of S corporation stock is that all of the income generated will be taxable to the charity, as will any gain on the sale or redemption of the stock.[964] It is unlikely in many cases that a charity will be willing to issue a charitable gift annuity for S corporation stock.

Other strategies may take advantage of the fact that a gift in exchange for a gift annuity is a gift directly to charity rather than to a trust. If a donor contributes an appreciated musical instrument to a charitable remainder trust, for example, the tangible personal property related use rule of §170(e) will limit the charitable deduction to basis even if the charitable remainder beneficiary is a symphony orchestra that will purchase the instrument for its own use. However, a gift of the same instrument to a symphony orchestra in exchange for a gift annuity is not subject to this limitation, and the full actuarial value of the charitable remainder based on fair market value will be deductible.

The Consolidated Appropriations Act, 2023 provided taxpayers another opportunity to make a one-time qualified charitable distribution of up to $50,000 (adjusted for inflation) from taxpayer's IRA to split-interest entity, which is defined to include a charitable gift annuity if such annuity is funded exclusively by qualified charitable distributions and commences fixed payments of 5% or greater not later than one year from the date of funding.[965] This definition effectively prevents addition of the one-time $50,000 qualified charitable distribution to an existing split-interest entity with existing corpus or making additions to the split-interest entity after funding. Spouses may each make a $50,000 election to a charitable gift annuity. No person other than the taxpayer and the taxpayer's spouse, however, may hold an income interest in the split-interest entity, and the income interest may not be assignable.[966] A qualified charitable distribution to a charitable gift annuity is not treated as an investment in the contract under §72(c).[967] Although §408(d)(8)(F) allows for a $50,000 qualified charitable distribution to a CRAT or CRUT, the time and expense involved in creating a CRAT or CRUT significantly takes away from the benefit thereof; however, such distribution to a charitable gift annuity makes much more sense in terms of cost efficiency.

Although charitable remainder annuity trusts and charitable gift annuities are superficially similar (for example, the charitable deductions is the same for each) there are many important differences.

Here is a side by side comparison of differences between the annuity payable from a CRAT and the annuity payable by a CGA:

[964] §512(e).

[965] §408(d)(8)(F), *added by* the Consolidated Appropriations Act, 2023, Pub. L. No. 117-328, §307 (effective for distributions made in taxable years beginning after December 29, 2022). *See also* §408(d)(8)(F)(ii) (defining "split-interest entity"), §408(d)(8)(G) (adjusting $50,000 amount for inflation). Effective Jan. 1, 2026, the distribution amount is $55,000. Notice 2025-67.

[966] §408(d)(8)(F)(iv).

[967] §408(d)(8)(F)(v).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Comparison of CGA and CRAT	
CGA	**CRAT**
Can be deferred	Cannot be deferred
Annuity can increase each year	Annuity must be fixed
Charitable remainder beneficiary cannot be changed	Donor can retain right to change charitable remainder beneficiary
Donor cannot control investments	Donor can control investments
Part of income tax-free return of basis	Income is taxed under the tier system — may be entirely taxable
Not subject to 5% exhaustion rule	Subject to 5% exhaustion rule — may make CRAT impossible in times of low interest rates
Cannot run out of money so long as charity is solvent	Can run out of assets if trust exhausted
Must be for one or two lives only	Can be for term of years or more than two lives, or shorter of life or lives and term
Charitable deduction for gift of remaining income interest limited to unrecovered basis … may be zero	Charitable deduction for actuarial value of remaining income interest
Many charities accept CGA contributions for as little as $5,000 or $10,000–low administrative costs	Not economical unless trust will be $100,000 or possibly greater
Private foundation rules including self-dealing penalties do not apply	Most private foundations rules apply
Most charities issue annuities at ACGA recommended maximum rates	Donor sets annuity rate, subject to 5% and 10% limitations
Charity can hold S Corporation stock (although income will be taxable including on sale of stock)	CRAT is not a permissible S Corporation shareholder

©2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Part 3: Pooled Income Funds

XXII. Introduction and Summary of Requirements

The Tax Reform Act of 1969[968] permitted certain qualified charitable organizations to establish pooled income funds. A pooled income fund is similar in structure to a common trust fund. A donor makes an irrevocable transfer of assets to the fund, where the assets are invested together with the transfers from other donors. The donor either retains an income interest in the assets for life or creates an income interest in another for his or her life. An income interest may be enjoyed concurrently or successively. On the death of the income beneficiary, the corpus allocated to such income interest is severed from the fund and paid to the charitable remainder beneficiary. Pooled income funds can be an attractive option for donors wishing to make gifts too small to justify a separately invested charitable remainder trust. Many pooled income funds accept gifts as small as $10,000 if the donor has reached a specified minimum age, typically age 60, although because of the low interest rates and dividend yields of the last decade, many of those donors will opt instead for a charitable gift annuity.

A pooled income fund is created to receive and hold property transferred to the fund by two or more individual donors. Although a fund need not qualify as a trust under local law, it is taxed as a trust for federal income tax purposes, and the grantor trust rules do not apply. The general requirements for pooled income funds are set forth in §642(c)(5) and the regulations thereunder.

The donor must give an irrevocable remainder interest in all property transferred to the fund to an organization described in §170(b)(1)(A), other than a §170(b)(1)(A)(vii) or §170(b)(1)(A)(viii) organization. The donor must retain an income interest for his or her life or create a life income interest in one or more beneficiaries living at the date of the transfer. The property transferred to the fund must be commingled with property transferred by other individual donors to the fund. Generally, the donor will not recognize any gain or loss on the transfer of property to the fund.

A corporation can be a donor to (but not a beneficiary of) a pooled income fund. In Rev. Rul. 85-69, the IRS stated that nothing in the statute or regulations precludes a "person" other than an individual from being a donor to a pooled income fund.[969]

A pooled income fund may not invest in any securities the income from which is exempt from federal income taxation, and it only may hold assets acquired in transfers satisfying the requirements of §642(c)(5). Except for the limited exception of a supporting organization,[970] the fund must be "maintained" by the organization to which the remainder interest is contributed. Under certain circumstances a "supporting organization"[971] may act as trustee of a fund established for the benefit of a qualified charitable remainder beneficiary.[972] A donor or noncharitable income beneficiary may not act as a trustee of the fund. The amount of income received by the income beneficiary is determined by the annual rate of return realized by the fund.

[968] Pub. L. No. 91-172, §201, amending §642(c).

[969] *See* PLR 8720065 (charitable remainder beneficiary could not hold income interest in fund and retain right to revoke the interest at any time).

[970] Described in §170(b)(1)(A)(viii).

[971] A supporting organization is described in §170(b)(1)(A)(viii) and §509(a)(3) as an organization that: (i) is organized and operated exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in §170(b)(1)(A)(i) through §170(b)(1)(A)(vi) and §170(b)(1)(A)(ix); (ii) is operated, supervised, or controlled by or in connection with one or more organizations described in §170(b)(1)(A)(i) through §170(b)(1)(A)(vi) and §170(b)(1)(A)(ix); and (iii) is not controlled directly or indirectly by one or more disqualified persons (as defined in §4946) other than foundation managers and other than one or more organizations described in §170(b)(1)(A)(i) through §170(b)(1)(A)(vi) and §170(b)(1)(A)(ix).

[972] *See* Reg. §1.642(c)-5(b)(5).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXIII. Specific Requirements for Qualification

The regulations set forth specific requirements that all pooled income funds must satisfy. If a fund fails to satisfy any one of these requirements, it will not qualify as a pooled income fund. Such disqualification will result in the disallowance of certain income, estate, and gift tax charitable deductions with respect to property contributed to the fund.

In Rev. Proc. 88-53, the IRS published a sample declaration of trust and instruments of transfer for a pooled income fund and provided that transfers to trusts in substantial compliance with the sample form qualify for a charitable deduction without the necessity of requesting a ruling.

At the same time, the IRS issued now-superseded Rev. Proc. 88-54,[973] stating that ordinarily it will no longer issue rulings as to the qualification of a pooled income fund under §642(c)(5) or whether a transfer to a fund qualifies for a charitable deduction. This IRS ruling position on pooled income funds is now contained in the third annual revenue procedure published in the first annual Internal Revenue Bulletin.[974] The IRS apparently will continue to issue rulings on specific provisions in pooled income funds that substantially differ from the sample provisions but may refuse to rule on the entirety of such funds.[975]

In Rev. Proc. 88-50, the IRS reversed its long-standing policy of not issuing rulings on prospective estate tax matters. As a result, taxpayers are not barred from obtaining prospective rulings on testamentary transfers to pooled income funds, although the restrictions on rulings contained in the third annual revenue procedure still apply.

It is very important that a donor confirm that a pooled income fund qualifies under §642(c)(5) before making a transfer, because a transfer is irrevocable. With respect to funds created before the issuance of Rev. Proc. 88-54 or funds falling outside of the model pattern in Rev. Proc. 88-53, the donor should obtain a copy of the fund's IRS letter ruling. Where a fund has not obtained an IRS letter ruling, the donor should ask counsel experienced in this area to review the governing instrument before the donor makes a gift to a fund; such gifts are irrevocable and may affect the donor's estate plan and current income situation.

A. Contribution of Remainder Interests

When a donor transfers property to a pooled income fund, the donor must contribute an irrevocable remainder interest in the transferred property to or for the use of a public charity.[976] At the time of the transfer, the donor must either retain an income interest in the property for life or create an income interest for life in one or more individuals living at the date of the transfer.[977] A gift of a contingent remainder interest will not qualify as an irrevocable remainder interest.[978]

[973] *Superseded by* Rev. Proc. 89-3.

[974] *See* Rev. Proc. 2026-3, §4.01(16), §4.01(36), §4.01(52), §4.01(58).

[975] *See, e.g.*, PLR 8929070 (declining to rule on qualification of pooled income fund and directing taxpayer to follow model provisions in Rev. Proc. 88-53).

[976] Reg. §1.642(c)-5(b)(1).

[977] Reg. §1.642(c)-5(b)(2).

[978] Reg. §1.642(c)-5(b)(1).

1. Qualified Organizations

Unlike charitable remainders trusts, only organizations described in specific clauses of §170(b)(1)(A) are qualified to be remainder beneficiaries of pooled income funds.[979] Qualified organizations include the following:

- churches or conventions or associations of churches;
- educational organizations with a regular faculty and curriculum and a regular student body attending resident classes;
- hospitals;
- organizations directly engaged in continuous medical research in conjunction with hospitals;
- organizations operated exclusively to hold and administer property for state and municipal colleges and universities and governmental units;
- publicly supported organizations;[980] and
- organizations directly engaged in continuous agricultural research in conjunction with land-grant colleges or universities or non-land grant colleges of agriculture.[981]

Private operating foundations, private non-operating foundations, "broadly publicly supported organizations,"[982] and supporting organizations are not qualified to be remainder beneficiaries.

Although a "supporting organization"[983] may not have a remainder interest in the fund, a supporting organization may manage or maintain a pooled income fund, provided the supporting organization also acts as trustee and the remainder is vested in a qualified organization of the type outlined above.[984] In addition, the charitable remainder beneficiary's board of trustees must have the ability to remove the members of the board of trustees of the supporting organization and designate new trustees. These powers are deemed to give the public charity sufficient control of the fund.[985]

An organization that is not a private foundation because it is both a supporting organization described in §509(a)(3) and a public charity by virtue of being described in §170(b)(1)(A)(i)

[979] Specifically, a qualified charitable organization is one described in §170(b)(1)(A)(i), §170(b)(1)(A)(ii), §170(b)(1)(A)(iii), §170(b)(1)(A)(iv), §170(b)(1)(A)(v), §170(b)(1)(A)(vi), or §170(b)(1)(A)(ix). §642(c)(5)(A).

[980] As described in §170(b)(1)(A)(vi) and Reg. §1.170A-9(f)(2), an organization is "publicly supported" if it normally receives a substantial part of its support from the general public or a governmental unit. Typically, such organizations include museums, libraries, community centers, and organizations providing facilities for the support of the performing arts.

[981] §170(b)(1)(A)(ix), added by the Protecting Americans from Tax Hikes Act of 2015, Pub. L. No. 114-113, Div. Q, §331(a) (effective for contributions made after December 18, 2015). *See* Staff of J. Comm. on Tax'n, 114th Cong., Technical Explanation of the Protecting Americans from Tax Hikes Act of 2015, House Amendment #2 to the Senate Amendment to H.R. 2029 197–98 (J. Comm. Print 2015) (qualifying agricultural research organizations to receive special treatment consistent with treatment of medical research organizations under §170(b)(1)(A)(iii)).

[982] A "broadly publicly supported organization" described in §170(b)(1)(A)(viii) and §509(a)(2), and Reg. §1.509(a)-3 must satisfy a one-third support test and a one-third gross investment test.

[983] Described in §170(b)(1)(A)(viii), §509(a)(3), and Reg. §1.509(a)-4.

[984] Reg. §1.642(c)-5(b)(5).

[985] Reg. §1.642(c)-5(b)(5).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

through §170(b)(1)(A)(vi) and §170(b)(1)(A)(ix) is qualified to be the remainder beneficiary of a pooled income fund.[986]

2. *Only One Remainder Beneficiary*

A pooled income fund may not benefit more than one charitable remainder beneficiary.[987] Before 1981, it was commonplace for a pooled income fund governing instrument to provide that if the charitable remainder beneficiary ceased to qualify upon the termination of the intervening income interests, the remainder interest was to be paid to one or more alternative organizations.

In PLR 8130070, the IRS ruled that a pooled income fund with such a provision in its governing instrument did not qualify, because it did not satisfy the requirement that the remainder interest may be distributed only to one qualified charitable remainder beneficiary. If the trustees of pre-1981 pooled income funds have not already done so, they should consider an amendment to the fund's governing instrument to conform with PLR 8130070. The IRS approved an amendment in the cited ruling. See XXIII.A.3., below, for a discussion of permissible provisions for the designation of an alternate remainder beneficiary.

A national organization may maintain a pooled income fund for the benefit of its local chapters or auxiliaries. This is not entirely an exception to the requirement that the fund only benefit a single remainder beneficiary, because only one local organization would be designated as the remainder beneficiary of each gift and the national organization would not have a remainder interest in the fund.[988]

3. *Alternative Remainder Beneficiary*

The regulations require that the remainder interest be paid to a "public charity" upon the termination of the income interest.[989] Rev. Rul. 85-57 states that the governing instrument may provide for the selection of an alternative remainder beneficiary by the trustee if the designated charity ceases to qualify at the time of the termination of an income interest.

Rev. Proc. 88-53 sets forth the following sample language for the selection of an alternative remainder beneficiary for use in governing instruments:

> If at the time of the severance of the remainder interest Public Charity has ceased to exist or is not a public charity (an organization described in clauses (i) through (vi) of section 170(b)(1)(A) of the Code), the amount severed shall be paid to an organization selected by the Trustee that is a public charity.

B. Retention of Income Interest

1. *Duration of Income Interest*

The donor may retain, or create for one or more other beneficiaries, a life income interest in the transferred property. If the donor creates an income interest in one or more individual beneficiaries, all of the beneficiaries must be living at the time of the transfer to the fund.[990] The term of the income interest must be measured by the life of each individual beneficiary. In addition, an income interest *pur autre vie* is not permitted.[991] The income interest cannot be measured by the life of another even if the other individual also is a beneficiary of the income interest established by the same gift.[992] Unlike charitable remainder trusts, a pooled income fund may not have an income interest measured by a term of years.[993]

2. *Concurrent or Successive Life Beneficiaries*

If the donor creates a life interest in more than one beneficiary, the beneficiaries may enjoy their respective shares of income concurrently, consecutively, or both concurrently and consecutively.[994] Thus, the donor may retain the income for life and specify that on his or her death income should be paid to another beneficiary, such as the donor's spouse, for life. In the alternative, the donor may specify that two beneficiaries should share the income. The second life income interest may commence either at the date of transfer or upon the death of the first beneficiary. The donor must specify in the instrument of transfer the identity of the beneficiaries, their respective shares, and the timing for the distribution.[995] Rev. Proc. 88-53 sets forth sample instruments of transfer for one life, two lives with consecutive interests, and two lives with concurrent and consecutive interests.

3. *Revocation of Income Interests*

A gift to a pooled income fund must be irrevocable.[996] Once a gift has been made, its terms cannot be changed, except that the donor may reserve the testamentary right to terminate or revoke the income interest of any designated beneficiary other than that of the charitable remainder beneficiary.[997] As a practical matter, this allows a donor to measure an income interest created in another by the donor's life rather than by the life of the designated beneficiary. As a result, a donor may circumvent the requirement that the duration of an income interest must be measured by the life of each individual income beneficiary. In order to do so, a donor must: (1) expressly reserve the testamentary right to revoke the interest in the instrument of transfer; and (2) make the appropriate provision in his or her will exercising the power of revocation.

Comment: Where the donor retains the testamentary power to terminate or revoke a beneficiary's interest, the donor will not be considered to have made a completed gift to the income beneficiary for gift tax purposes unless the beneficiary is entitled to receive income during the donor's life. Otherwise, the gift is not complete unless and until the donor dies without exercising the power of revocation. The retention of such a right, however, will cause the interest to be included in the donor's

---

[986] Reg. §1.642(c)-5(a)(5)(iv).
[987] Reg. §1.642(c)-5(b)(1).
[988] *See* Reg. §1.642(c)-5(b)(5); PLR 200252066 (affiliates of pooled income sponsor could be named as charitable beneficiaries of fund).
[989] Reg. §1.642(c)-5(b)(1). A "public charity" is described in Reg. §1.642(c)-5(a)(5)(iv).
[990] Reg. §1.642(c)-5(b)(2).
[991] Rev. Rul. 79-61.
[992] Rev. Rul. 79-61.
[993] §642(c)(5)(A).
[994] Reg. §1.642(c)-5(b)(2).
[995] Reg. §1.642(c)-5(b)(2).
[996] Reg. §1.642(c)-5(b)(1).
[997] Reg. §1.642(c)-5(b)(2); PLR 200608002–PLR 200608003.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

estate for federal estate tax purposes. See the discussion at IX., above.

4. *Charitable Remainder Beneficiary as Income Beneficiary*

The donor also may designate the public charity to which the remainder interest is contributed as a recipient of an income interest, provided there is also at least one individual recipient. The charity must receive the income within the taxable year in which it is earned by the fund.[998] For this purpose, distributions made within 65 days after the close of a taxable year complying with the requirements of Reg. §1.642(c)-5(b)(7) are considered made on the last day of such taxable year.

Comment: PLR 8720065 concluded that a corporate public charity could not hold an income interest in a pooled income fund, because the public charity was a corporation. Although a pooled income fund can have a corporate donor, it cannot have a corporate income beneficiary. This conclusion is in direct contravention of the statement in the regulations that "[t]he public charity to or for the use of which the remainder interest is contributed may also be designated as one of the beneficiaries of an income interest."[999]

Caution: The donor is not permitted an additional charitable deduction for the value of the income interest created in the public charity or for the amount of any income actually paid to the organization.[1000]

C. Commingling of Property

The governing instrument of the pooled income fund must require the commingling of all property transferred to the fund from individual donors.[1001] The fund may not include property transferred with a retained life interest other than that permitted for a pooled income fund. The fund or any portion of its assets may be invested or reinvested jointly with property that is held by or for the use of the charitable organization that maintains the fund, such as the charity's general endowment funds, provided that the income attributable to the pooled income fund portion is easily identifiable.[1002] In PLR 8903019, the IRS permitted a public charity to commingle its pooled income fund assets with its charitable remainder trust assets.

The special investment and tax rules governing pooled income funds may serve to limit the desirability or practicality of a joint investment program. For example, a pooled income fund may not hold or invest in tax-exempt securities. This prohibition would also apply to any endowment fund with which the pooled income fund is invested.[1003] In addition, unlike the endowment fund of a public charity, a pooled income fund is subject to tax on short-term capital gains, because it is not a tax-exempt trust. The endowment fund of a public charity is not subject to tax on a short-term capital gain. Accordingly, joint investment of the assets may require the adoption of a different investment strategy in order to avoid otherwise nontaxable short-term gains.

A public charity may maintain more than one pooled income fund. Many of the large universities maintain more than one pooled income fund in order to implement different investment strategies for the different funds. For instance, a fund maintained for younger donors can offer long-term growth. The fund's relatively low rate of return increases the value of the donor's charitable deduction and defers taxable income until the donor needs it later in life. On the other hand, a public charity may market a high yield fund to older donors. If an organization sponsoring multiple funds later decides to merge the funds, it may do so without adverse tax consequences, as in PLR 9818048. In that ruling, the IRS stated that the rate of return for the post-merger surviving fund would be determined as if the funds had been combined for the three preceding years.

A financial institution that serves as the trustee of more than one pooled income fund may maintain a common trust fund described under §584 for the collective investment and reinvestment of the pooled income funds and assets unrelated to the funds.[1004] Such collective investment is permitted, provided separate accounting is maintained and the institution does not violate any of the investment restrictions discussed below.

D. Investment Prohibitions

1. *Tax-Exempt Securities*

The governing instrument of a pooled income fund must prohibit the trustee from acquiring or holding any securities the income from which is exempt from federal income tax.[1005] Accordingly, a pooled income fund may not accept a transfer of tax-exempt securities. In addition, where a pooled income fund's assets are jointly invested in a common trust fund or other joint investment vehicle, the investments held thereunder may not include any tax-exempt securities.[1006]

2. *Depreciable and Depletable Assets*

In Rev. Rul. 90-103, the IRS ruled that the governing instrument of all pooled income funds created after February 15, 1991, and all existing funds that accept additional contributions after that date, must require the creation of a depreciation reserve pursuant to generally accepted accounting principles. The requirement applies to any pooled income fund where the trustee has the authority to accept or invest in, or is not specifically prohibited from accepting or investing in, depreciable or depletable property. Failure to include the necessary provisions may disqualify the trust. Rev. Rul. 90-103 sets forth the following two alternate provisions for inclusion in governing instruments: (1) "If the trustee accepts or invests in depreciable or depletable property, it shall establish a depreciation or depletion reserve in accordance with Generally Accepted Accounting Principles (GAAP)." (2) "The trustee shall not accept or invest in any depreciable or depletable assets."

[998] Reg. §1.642(c)-5(b)(2).
[999] Reg. §1.642(c)-5(b)(2).
[1000] Reg. §1.642(c)-5(b)(2). However, see the discussion of a gift of an existing income interest at VIII.B., above.
[1001] Reg. §1.642(c)-5(b)(3).
[1002] Rev. Rul. 83-19 (exempt university, as trustee, may commingle assets of charitable remainder trusts in university endowment fund).
[1003] *See, e.g.*, Rev. Rul. 74-247 (institutional trustee could invest pooled income fund assets in its common trust funds only if funds held no tax-exempt securities and could not obtain any such securities).
[1004] Reg. §1.642(c)-5(b)(3).
[1005] Reg. §1.642(c)-5(b)(4).
[1006] *See* Rev. Rul. 74-247.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Rev. Rul. 90-103 required existing funds to amend their governing instruments on or before February 15, 1991, or refuse to accept additional contributions. The refusal to accept additional contributions may not always be in the discretion of the trustee or public charity maintaining the fund, as would be the case with a testamentary transfer to a fund.

Rev. Rul. 90-103 was modified by Rev. Rul. 92-81 to extend the time for compliance by existing pooled income funds. The IRS stated that pooled income funds that had not modified their governing instrument by February 15, 1991, could still comply with Rev. Rul. 90-103 if the fund: (1) disposed of all depreciable or depletable property before January 1, 1993; or (2) is reformed retroactively to include the earliest date of any contributions made after February 15, 1991. The ruling contains no deadline for making such reformations.

Rev. Rul. 90-103 was the IRS's long-awaited answer to the question of whether a trustee must maintain a substantial depreciation reserve for the benefit of the remainder beneficiary. In GCM 38866 (Dec. 10, 1981), GCM 39076 (Apr. 21, 1983), and TAM 8347010, the IRS approved pooled income funds with a pass-through of depreciation deductions and investment credits. The governing instruments of the funds in question authorized the trustee to establish a reserve, but did not require the maintenance of one except as necessary to maintain the actual value of the property contributed (i.e., in the event of economic depreciation). In the absence of a reserve, all depreciation deductions would be allocable under §167(d) to the income beneficiaries, because such deductions are allocable among the beneficiaries in the same proportion as the income.

In 1985, the IRS informally began to require that governing documents provide for a depreciation reserve where the trustee was not expressly prohibited from investing in depreciable property. However, a 1987 private letter ruling, PLR 8712046, which addressed the issue of a depreciation pass-through, did not require a reserve. In 1988, GCM 39709 (Mar. 4, 1988) concluded that the IRS had the authority to require that all funds maintain a depreciation reserve. The IRS did not formalize this position until the issuance of Rev. Rul. 90-103. For an example of a pooled income fund with a depreciation reserve satisfying the requirements of Rev. Rul. 90-103, see PLR 9334020.[1007]

The IRS has not introduced a similar requirement with respect to charitable remainder trusts. See the discussion at VI.C.2.b., above.

E. Maintenance of the Fund

The regulations require that the fund be maintained by the charitable remainder beneficiary.[1008] This requirement is satisfied if the public charity exercises direct control over the fund or has the ability to remove the trustee of the fund and designate a new trustee.[1009]

The regulations specifically allow a national organization that implements its purposes through local chapters or subsidiary organizations to maintain a pooled income fund for the general benefit of all the local subsidiary organizations, provided the local organizations are also qualified public charities.[1010] For example, a donor to such a fund would designate the local chapter or subsidiary as the recipient of the remainder interest of the property transferred to the fund. The ability of a national organization to establish a single fund on behalf of and for the ultimate benefit of its local chapters permits the organization to realize an economy of scale.[1011] The fact that local organizations or chapters are separately incorporated from the national organization is immaterial.[1012]

A supporting organization that is a hospital foundation can be the trustee of the hospital's pooled income fund provided the hospital's board of trustees has the power to remove members of the foundation's board of trustees and appoint the new members.[1013]

A bank may act as trustee of a fund created by a qualified charity provided the public charity retains the right to designate a new trustee.[1014]

In Rev. Rul. 96-38, the IRS ruled that a pooled income fund maintained by a community trust will satisfy the maintenance requirement, even if the donor may designate a component fund of the community trust to receive the charitable remainder. The IRS stated that as long as the community trust is the designated charitable remainder beneficiary, the remainder interest may be placed in a component fund that meets the requirements of former Reg. §1.170A-9(f)(11)(ii). Since the regulations treat the component fund as part of the community trust, the IRS reasoned, the community trust is the charitable beneficiary, even though the funds will eventually be used for the benefit of another charity.

F. Who May Serve as Trustee

The governing instrument must prohibit a donor or noncharitable income beneficiary from serving as a trustee of the fund.[1015] However, the regulations specifically permit the chari-

[1007] *See also* PLR 200608002–PLR 200608003.

[1008] Reg. §1.642(c)-5(b)(5).

[1009] Compare Rev. Rul. 75-116 (lack of power to remove trustee disqualified fund) with Rev. Rul. 74-247 (retention by charity of power to control trustee meant that fund was qualified). *See also* Rev. Rul. 74-132, (fund not disqualified where board of directors of supporting foundation that was acting as trustee of pooled income fund could be removed by board of directors of public charity).

[1010] Reg. §1.642(c)-5(b)(5). The IRS also requires that: (1) the national and local organizations share an identity of aims and purposes; (2) the local organizations expressly consent to be included in the fund; (3) the governing instrument provide that a designated local organization may not sever its connection to the fund before the death of the named income beneficiary; and (4) the governing instrument provide that if the designated local organization is no longer affiliated with the national organization when the remainder interest is to be transferred, the remainder will be transferred to the national organization or another affiliated local organization chosen by the national organization. Rev. Rul. 92-107. *See* PLR 9503018, PLR 9345007 (examples of pooled income funds that comply with requirements of Rev. Rul. 92-107). *See also* PLR 200252066 (addition of affiliates as charitable beneficiaries of trust funds satisfied requirements for a pooled income fund under Rev. Rul. 92-107 and satisfied maintenance requirement of §642(c)(5)(E) and Reg. §1.642(c)-5(b)(5); proposed amendments would not cause funds to fail to satisfy requirements for pooled income fund under §642(c)(5)).

[1011] *See* PLR 9703023.

[1012] PLR 9703023. Note that, as in PLR 9203010, the local organization may merge its separate fund into the pooled income fund of the parent organization without jeopardizing the status of the surviving fund.

[1013] Rev. Rul. 74-132.

[1014] Reg. §1.642(c)-5(b)(5).

[1015] Reg. §1.642(c)-5(b)(6).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

table remainder beneficiary to be designated as trustee.[1016] However, state law may restrict the ability of the charitable remainder beneficiary to serve as trustee. The fund may be maintained by an institutional or other trustee provided that the public charity maintains the power to remove the trustee and appoint a successor trustee.[1017]

Practice Point: State law should be reviewed to ensure that the trustee is a permitted party.

The prohibition against a donor or a noncharitable beneficiary serving as trustee applies to members of a charity's board of trustees who are beneficiaries of or donors to the charity's pooled income fund. A fund will not qualify where the donor or noncharitable beneficiary directly or indirectly has any responsibilities with respect to the fund that are ordinarily exercised by a trustee.[1018]

The mere fact that the donor or beneficiary is an officer, director, or other official of the public charity is not sufficient to disqualify the fund.[1019] Where the charitable remainder beneficiary serves as trustee, the governing instrument must prohibit board members and other officials who directly or indirectly participate in the fund's management from being donors to, or beneficiaries of the fund.[1020] Further, the governing instrument must exclude any trustee or other official who is a pooled income fund beneficiary or donor from participation in the maintenance of the fund. This requirement differs substantially from those for a charitable remainder trust, according to which a donor can serve as trustee in many circumstances.[1021]

Practice Point: To eliminate this issue, a public charity that intends to act as trustee of its own pooled income fund could enact a board resolution similar to the following:

> RESOLVED, that no trustee, officer, director, or other official of Public Charity X who is a donor to or beneficiary of Public Charity X Pooled Income Fund may directly or indirectly have general responsibilities with respect to the fund which are ordinarily exercised by a trustee.

A bank can invest pooled income fund assets in its common trust fund provided the common trust fund does not hold or invest in tax-exempt securities. However, note that certain Securities and Exchange Commission banking law considerations may have an impact on such collective investment even though authorized by the regulations. A bank is not qualified to be a trustee of a pooled income fund under which the donors have the power to name a charitable remainder beneficiary. In such case, the remainder beneficiary is not ascertainable and, therefore, it could not control the investment policies or have the power to remove the bank as trustee,[1022] thus violating the requirement that a public charity must maintain the fund through either direct or indirect control.

The provision in a governing instrument that the payment of a pooled income fund's administrative expenses are to (or may) be paid by the charitable remainder beneficiary will not jeopardize the fund's qualification or constitute self-dealing prohibited under §4941 or a taxable expenditure under §4945.[1023]

G. *Income Realized by the Income Beneficiary*

The income of each beneficiary must be based solely upon the rate of return realized by the fund.[1024] The governing instrument must provide for the distribution of the net income from the fund and must require that the net income be distributed to the beneficiaries during the taxable year in which it is received. If necessary, adjusting payments may be made on or before the 65th day following the close of the fund's taxable year to ensure that the beneficiaries receive their full share of the fund's net income for that year. Any adjusting payments made during the 65-day extension are includible in the income of the recipient as if paid on the last day of the prior taxable year.[1025]

> *Example:* After the close of the fund's year on December 31, 20X1, it is discovered that an adjusting payment must be made to income recipient X. The payment is made on February 15, 20X2. X must include the payment in his or her gross income for 20X1, even though X did not receive the payment until 20X2.

1. Amount of Income — Unit Plan

A fund's net income generally means those receipts that are classified as income in accordance with fiduciary accounting principles, less expenses of administration.[1026] The amount of income payable to the income beneficiary depends on the rate of return earned by the fund for the taxable year. The governing instrument may provide for any reasonable method of allocating income to participation units that reaches a result reasonably consistent with the units of the participation method outlined in the regulations.[1027]

For purposes of determining the respective interests in the fund attributable to each contribution, the fund is divided into units of participation.[1028] All units are of equal value, and each represents a proportionate undivided interest in the fund as a whole.[1029] The trustee revalues each unit as of the first day of the fund's taxable year and on the first day of each quarter. The unit value is determined as of each valuation date by dividing the net fair market value of the entire fund as of the valuation date by the total number of units (and fractions of a unit) outstanding on that date. Income that is accrued but undistributed as of any valuation date is not considered part of the fund for purposes of its valuation. Each new contribution of property to the fund is allocated a number of units. The allocation is determined by dividing the net fair market value of the property contributed by the value of the unit in the fund immediately before the contribution is received.[1030]

[1016] Reg. §1.642(c)-5(b)(6).
[1017] Reg. §1.642(c)-5(b)(5).
[1018] Reg. §1.642(c)-5(b)(6).
[1019] Reg. §1.642(c)-5(b)(6).
[1020] Reg. §1.642(c)-5(b)(6).
[1021] *See* Rev. Rul. 77-285 (grantor of charitable remainder trust may retain right to remove trustee and substitute another including himself).
[1022] Rev. Rul. 75-116.
[1023] PLR 8326064.
[1024] Reg. §1.642(c)-5(b)(7).
[1025] Reg. §1.642(c)-5(b)(7).
[1026] Reg. §1.642(c)-5(a)(5)(i). *See* §643(b).
[1027] Reg. §1.642(c)-5(c)(2)(ii).
[1028] Reg. §1.642(c)-5(c)(1).
[1029] Reg. §1.642(c)-5(c)(2).
[1030] Reg. §1.642(c)-5(c)(2)(i)(b).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

Example: X transfers property worth $100,000 to a pooled income fund on April 1, 20X1, a valuation date. X retains the income interest in the property transferred. On April 1, the fair market value of the property in the fund, exclusive of the new transfer, is $1,000,000 with 2,000 units of participation outstanding. Therefore, each unit has a value of $500 ($1,000,000 ÷ $2,000). X is allocated 200 units ($100,000 ÷ $500).

Once determined, the number of units assigned to an income interest (or share thereof) of a gift to the fund will not change, but the value of a unit will change as the value of the fund's assets increases or decreases. Of course, additional gifts by a donor with the same named beneficiaries will result in the issuance of an additional number of units determined in the same manner as described above. Every unit in the fund is of equal value at all times.[1031]

2. Calendar Year Requirement

The Tax Reform Act of 1986[1032] required all trusts, with the exception of wholly charitable trusts, to adopt a calendar year as the taxable year.[1033] This change required pooled income funds on a fiscal year to adopt a short year for the first fiscal year beginning after 1986, which year began on the first day of the fund's fiscal year beginning in 1987 and ended on December 31, 1987. The income beneficiaries of a pooled income fund were permitted to report the income earned during the short year ratably over four years. This was designed to minimize the impact of the "bunching" of income that otherwise would have occurred in 1987. See the discussion at XI.A.3., above.

3. Partial Years

Income from the fund is allocated to units only for the period during the taxable year that such units are outstanding, as would be the case with a transfer made on other than the first day of a fund's taxable year. For this purpose, either the actual income for the applicable portion of the taxable year or a prorated portion of annual income can be used. In either case, adjustments may be necessary to reflect fluctuations in the fair market value of the property of the fund that occur during the year.[1034]

4. Transfers Between Determination Dates

A "determination date" is the date the assets of a pooled income fund are valued. The regulations require the fund's assets to be valued on the first day of the fund's taxable year and on at least three other days during the taxable year. The period between two "determination dates" cannot be more than three months.[1035]

The usual practice is to designate the first day of each quarter as the determination date. If a contribution is made to the fund between determination dates, the number of units assigned to the contribution is determined by using a prorated unit value as of the contribution date. The prorated unit value is calculated by taking the difference between the values of a unit on the valuation dates immediately preceding and succeeding the date of the transfer and prorating any difference on a per diem basis according to the number of days between valuation dates to arrive at a unit value as of the contribution date. In determining the prorated unit value, the value of property contributed to the fund between the preceding and succeeding determination dates is excluded.[1036]

Example: The determination dates of a pooled income fund are the last day of each quarter. On March 31, 20X1, the fair market value of the assets of the fund is $100,000, and there are 1,000 units of participation outstanding. On May 31, 20X1, G transfers $10,000 to the fund. There are no other transfers to the fund, and on June 30, 20X1, the value of the fund is $120,000. The appreciation over the three-month determination period is $10,000, or $3,333 per month. Thus, on May 31, 20X1, the date of G's transfer, the fair market value of the fund assets is $106,667, and the value of a participation unit is $106.67. G receives 93.75 units ($10,000 ÷ 106.67) for G's $10,000 transfer.

Note: The example in the regulations[1037] is unclear with respect to whether appreciation in the transferred property is disregarded from the date of transfer through the next determination date. Under certain circumstances, property that retains its character after contribution may experience changes in market value different from the change in the remaining fund assets. In such cases, reducing the value of the corpus at the succeeding determination date by the fair market value of the contributed property at the time of the contribution does not accurately reflect the performance of the corpus during this interim period. The language of the regulations provides that such method is acceptable, but that other methods that yield "reasonable" results are permissible. A more "reasonable" method would appear to be one that takes into account the fluctuation in the market value of all of the assets of the fund during the time they are held by the fund.

5. Testamentary Transfers

Income accrues on principal earmarked for a pooled income fund during the period of administration of a grantor's estate. The fund is disqualified where such income is transferred to the fund and is payable to the income beneficiary but not included in determining the beneficiary's participation interest in the fund.[1038] Thus, both the principal and the income accrued on a testamentary transfer to a pooled income fund must be transferred to the fund. The estate may retain the income accrued from the date of death and pay it directly to the income beneficiary if permitted under state law and the decedent's will.[1039] Where this is the case, only the principal is transferred to the fund, and only the property transferred, is used in computing the participation interest.

[1031] Reg. §1.642(c)-5(c)(2)(i)(b).
[1032] Pub. L. No. 99-514, §1403.
[1033] §644.
[1034] Reg. §1.642(c)-2(c).
[1035] Reg. §1.642(c)-5(a)(5)(vi).
[1036] Reg. §1.642(c)-5(c)(2)(iii).
[1037] Reg. §1.642(c)-5(c)(2)(iii) *Ex.*
[1038] Rev. Rul. 76-445.
[1039] Rev. Rul. 76-445.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

6. Partial Allocation of Income to Charity

The governing instrument may provide that a portion of the income allocable to a given participation interest may be paid to the charitable remainder beneficiary of the fund rather than the noncharitable beneficiary. Such income must be paid to or for the use of the charity in the year in which the income is realized by the fund.[1040] However, consistent with the treatment of non-grantor charitable lead trusts, the donor is not entitled to an additional charitable deduction for the gift of the income interest to charity.[1041]

The regulations include an example in which the governing instrument of a qualified pooled income fund provides that the units of participation are issued based upon the relative fair market value of the property at the time of contribution.[1042] All income from the units is payable to private beneficiaries, except that the instrument further provides that the income allocable to appreciation in the fair market value of each unit is, to the extent in excess of its initial fair market value, to be distributed currently to a charitable organization.

H. Termination of Life Income Interest

The income interest of any designated beneficiary must either terminate with the last regular payment before the death of the income beneficiary or be prorated to the date of death.[1043] On the termination of an income interest, the trustee is required to remove from the fund an amount equal to the value of the remainder interest in the property originally transferred.[1044] A fraction or percentage of the corpus of the fund corresponding to the units of participation allocable to the terminated life interest must be severed from the fund and transferred to the charitable remainder beneficiary. The value of this remainder interest may be either its value on the next determination date after the date of termination or its value on the last regular payment date, if the income interest is in fact terminated on such payment date.[1045] Amounts of corpus severed from the fund must be paid to or retained for the use of the public charity.

Rev. Rul. 76-196 involved an income beneficiary who died on May 15. The governing instrument provided that the income interest of each beneficiary was to terminate with the income payment immediately preceding the beneficiary's death (March 15) but that the fund was to sever the assets as of the valuation date immediately following the date of death (July 1). Valuation dates for the fund were the first day of each quarter, but payment dates were made on the 15th day of the second month after the valuation date. The IRS ruled that the fund was disqualified, because the property to be severed was not valued as of the determination date next succeeding the termination of the income interest (April 1) or as of the date on which the last regular payment was made before the death of the beneficiary (March 15).

I. Death Taxes

Unlike charitable remainder trusts, pooled income funds are not subject to the requirement imposed by Rev. Rul. 82-128 that the survivor beneficiary's income interest cannot become effective unless the survivor agrees to be responsible for any taxes for which the fund may otherwise be liable upon the death of the first beneficiary. Rev. Rul. 82-128 established this rule, prohibiting the possibility of payment of taxes, based on the requirement that a charitable remainder trust may not pay any amount other than the "unitrust amount" or "annuity amount" to a noncharitable beneficiary. GCM 39012 (Mar. 18, 1993) states that the possibility that a pooled income fund could be liable for such taxes will not disqualify the fund, because the statutory requirements for pooled income funds do not prescribe a similar directive concerning amounts payable to the noncharitable beneficiaries.

[1040] Reg. §1.642(c)-5(c)(3).
[1041] Reg. §1.642(c)-5(b)(2).
[1042] Reg. §1.642(c)-5(c)(4) *Ex.* (3).
[1043] Reg. §1.642(c)-5(b)(7). *See, e.g.,* PLR 200608002–PLR 200608003 (illustrating proration).
[1044] Reg. §1.642(c)-5(b)(8).
[1045] Reg. §1.642(c)-5(b)(8).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXIV. Type of Property Contributed to or Held by a Pooled Income Fund

With the exception of the prohibition on the holding of tax-exempt securities, the Code and regulations do not impose any limitations on the type of property that may be contributed to or held by a pooled income fund. As a practical matter, many pooled income funds accept only gifts of cash and marketable securities.

A. *Property Subject to an Indebtedness*

A donor recognizes no gain or loss on the transfer of appreciated property to a pooled income fund, provided the transferred property is not subject to any outstanding indebtedness.[1046] The donor recognizes gain to the extent of any indebtedness as provided by the bargain sale rules.[1047] The IRS has ruled that a fund's investment in an office building does not disqualify the fund, even where the fund assumes a mortgage as part of the transaction.[1048] In PLR 8002034, the IRS sanctioned the transfer to a pooled income fund of a farm encumbered by a lease to a tenant farmer and by a mortgage on which the donor was obligated.

If the donor transfers property to the fund and receives property in return from the fund, the fair market value of the property received from the fund is deemed to be the amount realized and the transaction is subject to tax.[1049]

Comment: In the case of a transfer of property in exchange for any other property, the bargain sale rules of §1011(b) may apply such that if a charitable deduction is allowed by reason of a sale, then the adjusted basis for determining the gain from such sale shall be that portion of the adjusted basis which bears the same ratio to the adjusted basis as the amount realized bears to the fair market value of the property.[1050]

B. *Tangible Personal Property*

A contribution consisting of a transfer of a future interest in tangible personal property is deemed to be complete only when all intervening interests and rights to the actual possession or enjoyment of the property have either expired or are held by persons other than the taxpayer or persons who would be considered related to the taxpayer under §267(b) or §707(b).[1051] Accordingly, an income tax charitable deduction for a contribution of tangible personal property to a pooled income fund is not available in the year of the transfer unless the donor concurrently gives the income interest to an "unrelated" beneficiary not related to the donor under §267(b) or §707(b), including family members of the taxpayer, corporations and partnerships controlled by the taxpayer, and trusts of which the taxpayer is a fiduciary or beneficiary.[1052] If tangible personal property contributed is long-term appreciated capital gain property and is not related to the furtherance of the public charity's exempt purpose, the deduction is subject to a reduction equal to 100% of any appreciation attributable to the gift portion of the transfer.[1053] Because a pooled income fund (unlike the sponsoring charity) is never engaged in its own charitable activities, the income tax deduction for a gift of tangible personal property to charity arguably will be limited to basis.

C. *Depreciable Property*

Rev. Rul. 90-103 requires governing instruments of pooled income funds to either prohibit the trustee from accepting or investing in depletable or depreciable assets or to maintain a depreciation reserve in accordance with generally accepted accounting principles. See the discussion at XXIII.D.2., above.

[1046] Reg. §1.642(c)-5(a)(3).
[1047] §1011(b).
[1048] Rev. Rul. 79-387.
[1049] Reg. §1.642(c)-5(b)(3), §1.170A-5(b) *Exs.* 6, 7.
[1050] *See, e.g.*, PLR 8002034.

[1051] §170(a)(3).
[1052] §170(a)(3).
[1053] §170(e)(1)(B)(i); Reg. §1.170A-4(b)(3). As discussed in XI.A.3., above, §170(e)(1)(B)(iii), as added by the American Jobs Creation Act of 2004, Pub. L. No. 108-357, §882(a), limits a donor's initial income tax charitable deduction for a contribution of certain intellectual property to the donor's basis in such property or, if less, the property's fair market value, effective for contributions made after June 3, 2004. Under §170(m), as added by Pub. L. No. 107-357, §882(b), the donor may also be entitled to an income tax charitable deduction for certain additional amounts in the year of contribution or in subsequent taxable years based on a specified percentage of the "qualified donee income" received or accrued by the donee on such property.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXV. Valuation of Income and Remainder Interest

For income, estate, and gift tax purposes,[1054] the deductible value of the remainder interest in property transferred to a pooled income fund is the present value of the remainder interest at the time of the transfer of the property.[1055] The present value of the remainder interest is determined by subtracting the present value of the life income interest from the fair market value of the property on the date of transfer or, if elected for estate tax purposes, the §2032 alternate valuation date.[1056] As discussed below, the present value of the life income interest depends upon two factors, the actuarial life expectancy of the income beneficiary and the fund's deemed rate of return.

Comment: The fact that under the terms of the governing instrument the beneficiary of the income interest may not be entitled to the last income payment on termination of the income interest is not taken into account in determining the present value of the life income interest.[1057]

A. *Computation of the Present Value of the Life Income Interest*

In the case of an interest for one life, a donor may use Table S set forth in Reg. §1.642(c)-6(e)(6)[1058] to compute the value of remainder interests in pooled income fund transfers after April 30, 2009. (The calculation of the deemed rate of return of the fund is discussed below.) A donor should attach to his or her federal income tax return on which the deduction is first claimed a brief statement showing the calculation of the present value of the remainder interest.[1059] For further discussion of the valuation rules under §7520, effective for transfers made on or after May 1, 1989, see IV.H., above.

The actuarial factors for the computation of the value of an income interest payable for two lives may be found in Table R(2) on the IRS's website at https://www.irs.gov/retirement-plans/actuarial-tables.[1060] An income interest for more than two lives requires use of a factor that is not provided in the published actuarial tables. Although the regulations note that the Commissioner will provide the factor for an income interest with a survivor beneficiary upon request,[1061] the filing fees now required will usually make this an unattractive option. Several inexpensive commercial software programs are available to compute these factors for multiple lives, which was not the case when the regulations were issued. If a ruling is requested, the taxpayer's request must recite the fund's yearly rate of return for the three taxable years preceding the date of transfer and the date of birth of each income beneficiary and include copies of the relevant documents. If the Commissioner furnishes the factor, the donor should attach a copy of the letter supplying the factor to the tax return on which the deduction is claimed.

After determining the age of the beneficiary at his or her nearest birthday, one must determine the deemed rate of return of the fund, which is then used as a discount factor to arrive at the present value of the remainder interest. The deemed rate of return of a pooled income fund is the highest annual rate of the average yearly rate of return for the three taxable years immediately preceding the year in which the transfer of property to the fund is made.[1062] For this purpose, the first taxable year of the pooled income fund, even though less than 12 months, is considered a full taxable year. However, the rate of return earned by the fund for a period of less than 12 months must be annualized.[1063]

[1054] §170, §2055, §2106, §2522.

[1055] Reg. §1.642(c)-6(a)(1).

[1056] Reg. §1.642(c)-6(a)(2). Reg. §1.642(c)-6, which provides the actuarial tables for valuing interests in a pooled income fund, was extensively amended by T.D. 8540, 59 Fed. Reg. 30,100 (June 10, 1994), to reflect the enactment of §7520, effective for transfers made on or after May 1, 1989. The former provisions of Reg. §1.642(c)-6, governing valuation of transfers made before the May 1, 1989, effective date of §7520, were removed to Reg. §1.642(c)-6A(d). The regulations were amended again by T.D. 8819, 64 Fed. Reg. 23,187 (Apr. 30, 1999), which included temporary regulations that updated the actuarial tables, based on mortality data from the 1990 census. These regulations were finalized in T.D. 8886, 65 Fed. Reg. 36,907 (June 12, 2000). In 2009, the IRS issued final, temporary, and proposed regulations reflecting updated mortality data from the 2000 census. T.D. 9448, 74 Fed. Reg. 21,438 (May 7, 2009). In T.D. 9540, 76 Fed. Reg. 49,570 (Aug. 10, 2011), the IRS finalized the proposed regulations and removed the temporary regulations. In 2023, the IRS finalized regulations reflecting updated mortality data from the 2010 census. T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023). The amended regulations, which are effective for transfers to pooled income funds made on or after June 1, 2023, are found at Reg. §1.642(c)-6. T.D. 9448 transferred the regulations containing the tables that are effective for valuation dates after April 30, 1999, and before May 1, 2009, to Reg. §1.642(c)-6A(f). The tables that are effective for valuation dates after April 30, 2009, and before May 31, 2023, are located in Reg. §1.642(c)-6A(g). Reg. §1.642(c)-6(e)(2) contains transitional rules that allow the use of either the pre-June 1, 2023, or the post-May 31, 2023, tables for transfers made during the period beginning April 30, 2019, and ending on June 1, 2023.

[1057] Reg. §1.642(c)-6(a)(2).

[1058] Reg. §1.642(c)-6(e), *as amended by* T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (to reflect updated mortality data for valuation dates on or after June 1, 2023). The value of a remainder interest may also be calculated using the remainder factors in Table S available on the IRS website at https://www.irs.gov/retirement-plans/actuarial-tables. For transfers made after April 30, 2009, and before June 1, 2023, a donor must consult Table S under Reg. §1.642(c)-6A(g).

[1059] Reg. §1.642(c)-6(a)(3).

[1060] IRS Publication 1457, *Actuarial Valuations Version 3A* (for valuation dates after April 30, 2009), is available at no charge electronically on the IRS website and references tables with factors for one and two lives and terms of years at interest rates ranging from 0.2% to 20.0%. IRS Publication 1457, *Actuarial Values, Book Aleph* (for valuation dates after April 30, 1999 and before May 1, 2009), is also available on the IRS website and contains tables with factors for one and two lives and terms of years at interest rates ranging from 2.2% to 22.0%. *See also* Notice 2009-18 (supplementing certain pre-May 1, 2009 tables based on mortality and certain tables not based on mortality with factors for interest rates below 2.2%). For valuations of transfers with income interests for more than one life and made after April 30, 1989, and before May 1, 1999, a donor should consult former IRS Publication 1457, *Actuarial Values, Alpha Volume.*

[1061] Reg. §1.642(c)-6(b).

[1062] Reg. §1.642(c)-6(c). If it appears that the highest yearly rate of return for the three preceding years was purposely manipulated to be substantially less than the rate of return that would be reasonably anticipated (thus increasing the amount of the deductible remainder interest), the donor must determine the highest yearly rate of return as if the fund had been in existence for less than three years. Reg. §1.642(c)-6(e)(3), (valuation dates on or after June 1, 2023), §1.642(c)-6A(g) (valuation dates after April 30, 2009, and before June 1, 2023). This method is explained below. If a pooled income fund is merged into another pooled income fund, the rate of return for the surviving fund is determined by treating the assets of both funds as if they had been combined during the three years preceding the merger. PLR 9513012.

[1063] Reg. §1.642(c)-6(c)(2).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

In the case of funds in existence less than three years, a donor must use an assumed rate of return for purposes of calculating the value of the charitable remainder interest and hence the deduction. For funds created after April 30, 1989, the regulations provide the method for determining the assumed rate of return. The donor must: (1) compute the annual average of the monthly rates prescribed in §7520(a)(2) for each of the three preceding calendar years, rounded to the nearest 2/10 of 1%; (2) select the highest annual average rate; and (3) subtract 1% from that rate. The resulting rate is the deemed rate used in valuing the remainder interest in the property transferred to the fund.[1064]

Comment: If the fund's actual rate of return is less than the assumed rate, the value of the remainder interest and the donor's charitable deduction are less than what they would otherwise be. Conversely, a donor will benefit where the fund's actual rate of return is greater than the assumed rate.

In Rev. Rul. 85-20, the IRS ruled that, for purposes of determining the present value of a life interest in a pooled income fund under Reg. §1.642(c)-6, the first taxable year is that year in which the pooled income fund receives assets.

The yearly rate of return of a pooled income fund is the percentage obtained by dividing the amount of income earned by the fund during the year by the amount equal to (i) the average fair market value of the property in the fund during the taxable year, less (ii) the "corrective term adjustment."[1065] The average fair market value of the property in the fund is the fair market value of all property in the fund on each "determination date," not including any income earned by the fund, divided by the number of "determination dates" in the taxable year.[1066]

Comment: For purposes of computing the rate of return, the term "income" has the same meaning that it does in §643(b),[1067] which generally provides that income is defined by terms of the governing instrument rather than federal income tax law. Thus, one must consider the terms of the governing instrument when determining the rate of return.

To find the "corrective term adjustment," income payments made by the fund are weighted according to the actual quarter during the year in which they are made. Earlier payments receive the greatest weight under the formula in the regulations:[1068]

Payment Period	Percentage of Payment
Last week of 4th quarter	0
Balance of 4th quarter	25
Last week of 3d quarter	25
Balance of 3d quarter	50
Last week of 2d quarter	50
Balance of 2d quarter	75
Last week of 1st quarter	75
Balance of 1st quarter	100

Example 1: The pooled income fund maintained by W University is on a calendar year, and its determination dates are the first day of each calendar quarter. The pooled income fund earns $5,000 of income during 2018. The fair market value of its property (determined without including any income earned by the fund), and the income paid out, on the first day of each calendar quarter in 2018 are as follows:[1069]

Date	Fair Market Value of Property	Income Payment
Jan. 1	$100,000	$1,200
Apr. 1	105,000	1,200
July 1	95,000	1,200
Oct. 1	100,000	1,400
	$400,000	$5,000

The average fair market value of the property in the fund for 2018 is $100,000 ($400,000 ÷ by 4). The corrective term adjustment for 2018 is $3,050, determined by applying the percentages obtained above.

Multiplication	Product
100% × $1,200	$1,200
75% × $1,200	900
50% × $1,200	600
25% × $1,400	350
Sum of Products	$3,050

The pooled income fund's yearly rate of return for 2018 is 5.157%, determined as follows:

$5,000 ÷ ($100,000 − $3,050) = 0.05157

Example 2: The pooled income fund maintained by X University is on a calendar year, and its determination dates are the first day of each calendar quarter. The pooled income fund earns $5,000 of income during 2018 and pays out $3,000 on December 15, 2018, and $2,000 on January 15, 2019, the last amount being treated under Reg. §1.642(c)-5(b)(7) as paid on December 31, 2018. The fair

[1064] Reg. §1.642(c)-6(e)(4) (valuation dates after April 30, 2009), §1.642(c)-6A(f)(4) (valuation dates after April 30, 1999, and before May 1, 2009; cross-referencing Reg. §1.642(c)-6(e)(4)), §1.642(c)-6A(e)(3) (valuation dates after April 30, 1989 and before May 1, 1999). *See also* Prop. Reg. §1.642(c)-6(e), §1.642(c)-6A(g). This rate must be recomputed by the fund for each calendar year until the fund has been in existence for three tax years. Reg. §1.642(c)-6(e)(4) (valuation dates after April 30, 2009), §1.642(c)-6A(f)(4) (valuation dates after April 30, 1999 and before May 1, 2009; cross-referencing Reg. §1.642(c)-6(e)(4)), §1.642(c)-6A(e)(3) (valuation dates after April 30, 1989 and before May 1, 1999). If the fund was created before May 1, 1989, and after November 30, 1983, the regulations provide that, for funds in existence less than three tax years, the highest yearly rate of return is deemed to be 9%. Reg. §1.642(c)-6A(d)(2). The IRS publishes an annual revenue ruling providing the deemed rates of return for pooled income funds in existence for less than three years. The deemed rate of return for 2023 is 2.2%, and the deemed rate of return for 2022 is 1.6%. Rev. Rul. 2023-1.

[1065] Reg. §1.642(c)-6(c)(1).

[1066] Reg. §1.642(c)-6(c)(2).

[1067] Reg. §1.642(c)-5(a)(5)(i).

[1068] Reg. §1.642(c)-6(c)(3)(i).

[1069] Reg. §1.642(c)-6(c)(5) *Ex.* (1).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

market value of its property (determined without including any income earned by the fund), on the first day of each calendar quarter in 2018 is as follows:[1070]

Date	Fair Market Value of Property	Income Payment
Jan. 1	$125,000	$ —
Apr. 1	125,000	—
July 1	75,000	—
Oct. 1	75,000	—
Dec. 15	—	$3,000
Dec. 31	—	2,000
	$400,000	$5,000

The average fair market value of the property in the fund for 2018 is $100,000 ($400,000 ÷ by 4).

The corrective term adjustment for 2018 is $750, determined by applying the percentages obtained above.

Multiplication	Product
0% × $2,000	$ 0
25% × $3,000	750
Sum of Products	$750

The pooled income fund's yearly rate of return for 2018 is 5.038%, determined as follows:

$5,000 ÷ ($100,000 – $750) = 0.05038

A special calculation is required where the taxable year of the fund consists of less than 12 months. In such case, the corrective term adjustment is obtained by multiplying each income payment made by the pooled income fund within the taxable year by the percentage obtained by subtracting from the number 1 a fraction the numerator of which is the number of days from the first day of the taxable year to the date of such income payment and the denominator of which is 365.[1071]

B. Computation of Present Value of Remainder Interest

A donor can compute the value of the remainder interest once the donor has determined the life expectancy factor for the one or more income beneficiaries and the yearly rate of return of the fund. For transfers after April 30, 1989, with a single income beneficiary, Table S in the regulations is used to compute the value of the remainder interest.[1072] If the yearly rate of return is a percentage that is between the yearly rates of return for which factors are provided by Table S, an exact method of obtaining the applicable factors (such as through software using the actual rate of return and the actuarial formulas provided in Sec. 20.2031-7(d)(2)(ii)(B) of this chapter) or a linear interpolation must be used, provided whichever method used is applied consistently in valuing all interests in the same property. The applicable remainder factors derived by an exact method or by interpolation must be expressed to at least five decimal places. The present value of the remainder interest is determined by multiplying the fair market value of the property on the valuation date by the appropriate remainder factor.[1073]

Example: M, who is 60 years old, transfers $100,000 to a pooled income fund on July 1, 20X1, and retains a life income interest. The highest yearly rate of return earned by the fund for the three preceding taxable years is 2.2%. The factor in Table S for 60 years of age at 2.2% is 0.64039. This factor is multiplied by the amount of the transfer to compute the value of the remainder ($100,000 × 0.64039 = $64,039).

The following example illustrates the computation of a remainder interest when the yearly rate of return on the fund is a percentage falling between the factors provided, using the linear interpolation method of determining the remainder.[1074]

Example: After June 1, 20X1, N, who will be 54 years and 8 months old, transfers $100,000 to a pooled income fund and retains a life interest in the property. The highest yearly rate of return earned by the fund for its three preceding taxable years is 5.43%. In Table S, the factor for 55 years under 5.4% is 0.28442 and under 5.6% is 0.27363. The present value of the remainder interest is $28,280, computed as follows:

Factor at 5.4% for person aged 55	0.28442
Factor at 5.6% for person aged 55	(0.27363)
Difference	.01079
((5.43% – 5.40%) / (5.60% – 5.40%)) * .01079 =	z
z = 0.00162	
Factor at 5.4% for person aged 55	0.28442
Factor at 5.4% – .00162	0.28442 – 0.00162 = .28280
Present value of remainder interest ($100,000 × 0.28280)	$28,280

[1070] Reg. §1.642(c)-6(c)(5) *Ex.* (2).

[1071] Reg. §1.642(c)-6(c)(3)(ii).

[1072] Reg. §1.642(c)-6(e)(5), §1.642(c)-6(e)(6) (valuation dates on or after June 1, 2023), §1.642(c)-6A(g) (valuation dates after April 30, 2009, and before June 1, 2023). Table S is available at https://www.irs.gov/retirement-plans/actuarial-tables.

[1073] Reg. §1.642(c)-6(e)(5) (valuation dates on or after June 1, 2023), §1.642(c)-6A(g) (valuation dates after April 30, 2009 and before June 1, 2023), §1.642(c)-6A(f)(5) (valuation dates after April 30, 1999, and before May 1, 2009).

[1074] *See* Reg. §1.642(c)-6A(f) *Ex.* (valuation dates after April 30, 1999, and before May 1, 2009). Reg. §1.642(c)-6(e)(5)(ii) *Ex.* illustrates the computation for valuation dates after April 30, 2009. *See also* Prop. Reg. §1.642(c)-6(e)(5)(iii) for an illustration or the computation for valuations dates after the proposed regulations become final.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXVI. Amending the Governing Instrument

A. *Fund Created After May 6, 1971*

Unlike the provisions for charitable remainder annuity and unitrusts, there are no permanent reformation procedures for defective governing instruments of pooled income funds. However, when the reformation provisions relating to charitable remainder trusts were enacted in 1984, Congress directed Treasury to issue regulations governing the reformation of defective pooled income funds.[1075] Until such regulations are forthcoming, the procedures pertaining to the reformation of pooled income funds remain uncertain. In light of this uncertainty, it is recommended that the governing instrument authorize the trustee to amend the governing instrument to qualify as a pooled income fund, but that particular care should be taken in drafting to avoid the necessity of resorting to such a solution. Before the enactment of the §2055(e) permanent reformation rules in 1984, it was clear that a defective pooled income fund created after May 6, 1971, that had accepted nonqualifying transfers of property could not be amended for the purposes of qualifying under §642(c)(5). In any event, a donor contemplating a gift to a particular pooled income fund should consider having the fund's governing instrument reviewed by knowledgeable tax counsel to avoid making an irrevocable transfer that is not eligible for a charitable deduction and may constitute a taxable gift.

[1075] §2055(e)(3)(I)(ii).

Note: The fund's governing instrument may be amended to qualify prospectively if the fund has not accepted property under a defective instrument of transfer.[1076]

The IRS has approved the merger of two pooled income funds, with the funds of the merged fund being transferred into the surviving fund.[1077]

The IRS also approved the amendment of a pooled income fund's governing instrument to substitute a new parent charity for the charity originally named as the remainder beneficiary, ruling that the change would not affect the fund's §642(c)(5) qualification.[1078] In addition, Reg. §1.642(c)-2(e), as added in 2004, allows the amendment or reformation of a fund's governing instrument in limited circumstances relating to the definition of fiduciary accounting income, such as to eliminate the possibility of determining income by reference to a fixed percentage of, or the unrealized appreciation in, the value of the fund's assets, so that the fund may be considered permanently set aside for charitable purposes. See XXVII.A., below, for further discussion.

B. *Funds Created Before May 7, 1971*

Certain transitional rules apply to the amendment of otherwise nonqualifying funds created before May 7, 1971.[1079]

[1076] Rev. Rul. 79-61.
[1077] PLR 9513012.
[1078] PLR 200329035, PLR 200329031.
[1079] Reg. §1.642(c)-7.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXVII. Tax Considerations

The tax considerations for a pooled income fund are in many respects parallel to the tax considerations for a charitable remainder trust. However, one important difference is that a pooled income fund is not a tax-exempt trust.

A. *Taxation of the Fund*

Although a pooled income fund is taxed as a trust under Subchapter J, it is expressly exempt from the grantor trust rules.[1080] A pooled income fund theoretically could be taxed as a simple trust, because it is required to distribute all of its income currently. As a result of the charitable set-aside, however, a pooled income fund must be taxed as a complex trust.[1081]

In general, it is unlikely that a pooled income fund will pay any income tax, except to the extent of short-term capital gains or tax on any unrelated business taxable income. A pooled income fund is permitted a §661 distribution deduction for all income earned that is then distributed to a beneficiary based on the beneficiary's percentage interest in the fund. The distribution deduction and the deduction for administration expenses will offset all of the fund's income with the exception of capital gains. Although all capital gains are taxable to the trust, the trust receives a set-aside deduction for long-term capital gains earmarked for ultimate distribution to the charitable remainder beneficiary.[1082] However, no amount of net long-term capital gain will be considered permanently set aside for charity if the fund's governing instrument and local law give the trustee the power, whether exercised or not, to satisfy the income beneficiaries' right to income with either: (i) an amount equal to a fixed percentage of the fair market value of the fund's assets (i.e., a unitrust amount), whether determined each year or averaged over multiple years; or (ii) an amount that takes into account unrealized appreciation in the value of the fund's assets.[1083] Further, a charitable set-aside deduction for long-term capital gains is not allowed to the extent the trustee distributes proceeds from the sale or exchange of the fund's assets as income as described in Reg. §1.642(c)-5(a)(5)(i).[1084] A charitable set-aside deduction is not allowed for short-term capital gains (i.e., gains realized on sales or exchanges of capital assets for which the fund has a holding period of one year or less).[1085] For purposes of determining whether property held by a fund is short-term or long-term capital gain property, the fund assumes the donor's holding period and cost basis. Ordinary gains are included in income and distributed to income beneficiaries. Thus, a distribution deduction is available to offset ordinary gains.

Pooled income funds are also subject to the §1411 net investment income tax.[1086] Under Reg. §1.1411-3(a)(1)(i), §1411

[1080] Reg. §1.642(c)-5(a)(2).

[1081] *See* §651(a).

[1082] §642(c)(3).

[1083] Reg. §1.642(c)-2(c), amended by T.D. 9102, 69 Fed. Reg. 12 (Jan. 2, 2004) (finalizing REG-106513-00, 66 Fed. Reg. 10,396 (Feb. 15, 2001)), effective for taxable years beginning after January 2, 2004. If a governing state statute allows income to be determined by reference to a fixed percentage of, or the unrealized appreciation in, the value of the fund's assets, and the fund has not determined income in this manner, Reg. §1.642(c)-2(e), which contains the effective date rules for the 2004 amendment, provides that the fund's governing instrument may be amended or reformed to eliminate the possibility of determining income in such a manner. Such an amendment or reformation would allow the fund's net long-term capital gain to be considered permanently set aside for charity. Reg. §1.642(c)-2(e) indicates that a judicial reformation of the fund's governing instrument must be commenced, or a valid nonjudicial reformation must be completed, by nine months after the later of January 2, 2004, or the effective date of the state statute authorizing income to be determined in such manner.

[1084] Reg. §1.642(c)-2(c), amended by T.D. 9102. Effective for taxable years beginning after January 2, 2004, Reg. §1.642(c)-5(a)(5)(i) was amended by T.D. 9102 to provide that, while a fund's income generally may not include any long-term capital gains, a fund's income may, under governing state law, be defined as or satisfied by a unitrust amount or pursuant to the trustee's power to adjust between income and principal to fulfill the trustee's duty of impartiality. Such governing state law must provide for the fund's total return to be reasonably apportioned between the income and remainder beneficiaries and must satisfy the Reg. §1.643(b)-1 requirements. In exercising a power to adjust, the trustee must allocate to principal any proceeds from the sale or exchange of fund assets, at least to the extent of the fair market value of the assets when the donor contributed them or to the extent of the purchase price paid when the fund purchased them. As noted in the T.D. 9102 preamble, these amendments were made to conform with the 2004 modifications to the Reg. §1.643(b)-1 definition of income to take into account changes in the definition of fiduciary accounting income under state law. For further discussion of the 2004 amendments, see 852 T.M., *Income Taxation of Trusts and Estates.*

[1085] Reg. §1.642(c)-2(c).

[1086] The Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, §1402(a)(1), §1402(a)(4), enacted §1411, which imposes the unearned income Medicare contribution tax, generally referred to as the "net investment income tax," on the unearned income of a trust, potentially including a pooled income fund, effective for tax years beginning after 2012. *See* §1411(a)(2). The IRS refers to the tax as the "net investment income tax" in the preamble to final regulations that provide guidance on the application of §1411. *See* T.D. 9644, 78 Fed. Reg. 72,394 (Dec. 2, 2013); Reg. §1.1411-0 through Reg. §1.1411-10, §1.469-11(b)(3)(iv). The §1411 tax applicable to trusts is an additional tax equal to 3.8% of the lesser of: (1) the trust's "undistributed net investment income" for the tax year; or (2) the excess (if any) of the trust's §76(e) adjusted gross income for the tax year over the dollar amount at which the highest §1(e) tax bracket begins for the tax year. *See* §1411(a)(2); Reg. §1.1411-3(a)(1)(ii). "Undistributed net investment income" is defined as the trust's "net investment income" reduced by distributions of net investment income to beneficiaries and §642(c) deductions. Reg. §1.1411-3(e). "Net investment income" is defined as "investment income" reduced by deductions allocable to that income. §1411(c)(1); Reg. §1.1411-3(e)(1), §1.1411-4(a). "Investment income" consists of three items: (1) gross income from interest, dividends, annuities, royalties, and rents to the extent not derived in the ordinary course of a trade or business (unless that trade or business is described in item (2)); (2) other gross income from a trade or business that is a §469 passive activity or that consists of trading in financial instruments or §475(e)(2) commodities; and (3) net gain that is taken into account in computing taxable income and attributable to the disposition of property not held in a trade or business (unless that trade or business is described in item (2)). §1411(c)(1)(A), §1411(c)(2); Reg. §1.1411-4, §1.1411-5. The preamble to the final regulations notes that, for purposes of §1411, the rules generally mirror the treatment of pooled income funds under Chapter 1. Preamble to T.D. 9644. For general exceptions and special rules applicable in determining net investment income, see §1411(c)(3) through §1411(c)(6). *See also* Reg. §1.1411-6 through §1.1411-10. The regulations apply to tax years beginning after 2013, except that Reg. §1.1411-3(d) (special rule for §664 charitable remainder trusts) applies to tax years beginning after 2012. Reg. §1.1411-1(g), §1.1411-2(e), §1.1411-3(f), §1.1411-4(i), §1.1411-5(d), §1.1411-6(c), §1.1411-8(c), §1.1411-9(d), §1.1411-10(i), §1.469-11(b)(3)(iv)(D). According to the preamble of the proposed regulations, taxpayers were able to rely on the proposed regulations in complying with §1411 until the effective date of the final regulations. REG-130507-11, 77 Fed. Reg. 72,612 (Dec. 5, 2012). The "Questions and Answers on the Net Investment Income Tax" posted on the IRS website (http://www.irs.gov/uac/Newsroom/Net-Investment-Income-Tax-FAQs) to provide answers to some basic questions regarding §1411 state that trusts report and pay the §1411 tax on Form 1041. The website also indicates that individuals, estates, and trusts use Form 8960, *Net Investment Income Tax — Individuals, Estates, and Trusts* to compute the §1411 tax. Form 8960, according to the instructions, is to be attached to the trust's Form 1041. For a more detailed discussion of the §1411 regulations, see 852 T.M., *Income Taxation of Trusts*

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

applies to all trusts that are subject to Part I of Subchapter J in Subtitle A, Chapter 1, of the Code, unless specifically exempted by Reg. §1.1411-3(b). The regulations do not exempt pooled income funds and the preamble states that pooled income funds are subject to §1411. The §1411 tax applicable to trusts is an additional tax equal to 3.8% of the lesser of: (1) the trust's undistributed net investment income for the tax year; or (2) the excess (if any) of the trust's §67(e) adjusted gross income for the tax year over the dollar amount at which the highest §1(e) tax bracket begins for the tax year.[1087]

B. *Income Tax Charitable Deduction*

A donor who makes a lifetime gift to a pooled income fund is entitled to a federal income tax charitable deduction for the year in which the gift is made.[1088] Subject to the limitations mentioned below, the amount of the deduction is the present value of the charity's remainder interest in the donated property as of the date of the gift. The value of the remainder interest is based upon the number of income beneficiaries, the age of each income beneficiary, and the highest yearly rate of return of the fund for any one of the three taxable years immediately preceding the year of the gift. See the discussion at XXV.B., above, regarding calculation of the value of the remainder interest and the determination of the fund's highest yearly rate of return.

The age of the income beneficiary will have a significant effect on the value of the charitable contribution deduction. The following example, based on Table S in Reg. §1.642(c)-6A(f)(6), assumes that the donor made a gift in the amount of $100,000 on or after May 1, 2009, with income payable to one beneficiary for his or her life, and a highest yearly rate of return of 2.5%.[1089] The value of the remainder increases steadily with an increase in the age of the beneficiary:

Value of Remainder Interest	
Age	Deductible Portion of Gift
40	$ 40,261
50	49,767
60	60,478
70	71,551
80	81,951

The amount of the income tax deduction at each age level may be significantly smaller if the gift provides for a second beneficiary to succeed to the income upon the death of the first beneficiary.

If a gift is made in the form of appreciated property that has been held by the donor as capital gain property for more than one year, the donor is generally entitled to an income tax charitable deduction for the full fair market value of the charity's remainder interest.[1090] However, the amount deductible by the donor in the year of the gift is subject to a charitable deduction ceiling.[1091] A donor's yearly deductions for all such gifts to "public charities" cannot exceed 30% of the donor's "contribution base," which is the donor's adjusted gross income without regard to any net operating losses.[1092] On the other hand, if the gift is made in cash, the limitation on the amount of the deduction for the gift and for all other cash gifts to "public charities" made during the year is 60% of the donor's adjusted gross income.[1093] (The 60% limitation is inclusive of, and not in addition to, the 30% limitation.) The limitation for cash gifts in the 2017 legislation adds an additional level of complexity to deduction limitation calculations. Prior, and current, law provided for a 50% limitation for contributions of capital gain property which if sold would not produce long-term capital gain. As drafted, gifts of such property are not eligible for the increased percentage limitation.

A donor may elect to have the 50% limit apply to gifts of long-term appreciated property otherwise subject to the 30% limit.[1094] In such case, the amount of the deduction is limited to the property's basis. Such an election would be advisable if the amount of appreciation is relatively small in comparison to the taxpayer's basis.

If a donor gives appreciated securities held for one year or less, the donor must use his or her cost basis for the securities rather than the fair market value in computing the value of the remainder interest.[1095] As stated above, however, the 50% rather than the 30% limitation applies.

Caveat: The regulations provide that a current income tax charitable deduction will be disallowed in the case of a transfer of tangible personal property to a pooled income fund if the donor or related party under §267(b) retains the income interest.[1096] Such a transfer is deemed to be a transfer of a future interest. See the discussion at XXIV.B., above.

Any portion of the gift exceeding the 60%, 50%, and 30% limitations can be carried forward as a deduction for the succeeding five years, subject to the applicable limits in those

and Estates, and 511 T.M., *Section 1411 — Net Investment Income Tax (U.S. Income Series).*

[1087] *See* §1411(a)(2); Reg. §1.1411-3(a)(1)(ii).

[1088] §170(a), §170(f)(2)(A).

[1089] *See* Table S in Reg. §1.642(c)-6(e)(6). If the gift was made after April 30, 1999, and before May 1, 2009, see Reg. §1.642(c)-6A(f)(6). Reg. §1.642(c)-6A(f)(6) applies to valuation dates after April 30, 1999, and before May 1, 2009, to reflect updated mortality data. If the gift was made after April 30, 2009, see Table S in Reg. §1.642(c)-6(e)(6). If the gift was made before May 1, 1999, see Table S in Reg. §1.642(c)-6A(e)(5). Note that proposed regulations state that Table S will no longer be available in the regulations and will be available on the IRS website, https://www.irs.gov/retirement-plans/actuarial-tables.

[1090] *See* §170(e)(1). As discussed in IV.H.12., above, §170(e)(1)(B)(iii), as added by the American Jobs Creation Act of 2004, Pub. L. No. 108-357, §882(a), limits a donor's initial income tax charitable deduction for a contribution of certain intellectual property to the donor's basis in such property or, if less, the property's fair market value, effective for contributions made after June 3, 2004. Under §170(m), as added by Pub. L. No. 107-357, §882(b), the donor may also be entitled to an income tax charitable deduction for certain additional amounts in the year of contribution or in subsequent taxable years based on a specified percentage of the "qualified donee income" received or accrued by the donee on such property.

[1091] See the discussion of charitable deduction limitations at IV.H., above.

[1092] §170(b)(1)(C)(i).

[1093] §170(b)(1)(A). The limitation was 50% for gifts made before 2018.

[1094] §170(b)(1)(C)(iii).

[1095] §170(e)(1)(A).

[1096] Reg. §1.170A-5(b) *Ex.* 6.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

years.[1097] In such a carryover situation, a donor is deemed to deduct his or her basis first.[1098]

> *Example:* Donor X transfers to the P pooled income fund securities that she held as appreciated long-term capital gain property. X bought the securities years ago for $40,000, but they now have a fair market value of $90,000. Based on X's age and the yearly rate of return of P, X is entitled to an income tax charitable deduction of $50,000. However, X's charitable deduction ceiling (i.e., 30% of her adjusted gross income) is $30,000. Assuming that in subsequent years X makes no other charitable contributions and her adjusted gross income remains constant, the deduction consequences are as follows:
>
> Year 1. X is entitled to deduct $30,000.
>
> Year 2. Again, X is entitled to deduct $30,000, but this year $10,000 represents a deduction of basis (i.e., basis $40,000 less year 1 deduction of $30,000).
>
> Year 3. X deducts $30,000.

Although a donor is not entitled to an income tax charitable deduction for a gift of an income interest in a pooled income fund to the charitable remainder beneficiary, a donor is entitled to a charitable deduction for a subsequent gift of his or her income interest, provided this is not intended to defeat the partial interest rules under §170(f)(3). Thus, a donor who retains an income interest is entitled to an income tax charitable deduction where the donor gives his or her income interest to the charitable remainder beneficiary and the gift accelerates the remainder interest of the public charity. In PLR 8611023, the IRS ruled that such a gift did not violate the prohibition against gifts of "partial interests," that the income interest was held by the donor as long-term capital gain property, and, therefore, that the donor was entitled to deduct its full fair market value.

A donor who makes a gift of $250 or more to a pooled income fund is not entitled to an income tax deduction for the transfer unless he or she receives a written substantiation statement from the fund.[1099] The statement must include: (1) the amount of cash and a description of any property contributed to the fund; (2) an indication whether the donee charity provided any goods or services to the donor in consideration of the transfer; and (3) a good faith estimate of the value of such goods or services provided to the donor and, if such goods or services consisted solely of intangible religious benefits, a statement to that effect.[1100] The statement does not have to include an estimate of the value of the income interest received by the donor.[1101] There is some uncertainty whether deductibility of more than $5,000 requires a qualified appraisal of the income interest, even if all of the underlying fund assets are cash and marketable securities. See the discussion of this issue at VIII.B., above.

C. Estate Tax Charitable Deduction

A testamentary transfer to a qualified pooled income fund under §642(c)(5) qualifies for an estate tax charitable deduction, provided the charitable remainder beneficiary is described in §2055(a). The amount of the deduction is equal to the value of the remainder interest at the time of the transfer of the property to the fund, and there are no percentage limitations as in the case of an income tax charitable deduction. Generally, the estate tax considerations for transfers to pooled income funds are parallel to those discussed at V.C.1., above, with respect to charitable remainder trusts.

If the terms of a lifetime gift to a pooled income fund provide for the payment of income to the donor, or if the donor reserves the testamentary right to revoke the income interest of another beneficiary, the entire value of the units of the fund assigned to that gift, computed as of the date of death, is includible in the donor's gross estate for federal estate tax purposes.[1102] However, the value of the remainder interest, computed as of the date of death, is deductible as a charitable gift.[1103] Accordingly, the only amount, if any, that is subject to federal estate tax is the value at the donor's death of any income interest that continues after the donor's death. If that interest is held by the donor's spouse, the donor's personal representative may elect to qualify it for the unlimited marital deduction, which will offset any federal estate tax on that interest. In such case, the donor's personal representative would elect to qualify the entire interest (i.e., the spouse's life interest and the charitable remainder interest) as qualified terminable interest property (QTIP).[1104] The remainder interest would then be included for federal estate tax purposes in the spouse's estate,[1105] but the remainder interest would qualify for an offsetting estate tax charitable deduction. Conversely, any transfer of property to a CRT in which the transferor's spouse receives the annuity or unitrust interest will not be eligible for a QTIP election, because the spouse will not receive a qualifying income interest in the property. See IV.I.2., above, for further discussion.

Caveat: Provision should be made in the donor's testamentary arrangements for the payment of federal and state death taxes on the value of any continuing income interest that is subject to such taxes. Failure to make such a provision may entitle the fund to recover any taxes imposed on it from the donor's estate.

[1097] §170(b)(1)(C)(ii), §170(b)(1)(D)(ii).

[1098] Staff of J. Comm. on Tax'n, 99th Cong., General Explanation of the Tax Reform Act of 1986 (Pub. L. No. 99-514) 444–445 (J. Comm. Print 1987).

[1099] Reg. §1.170A-13(f)(13). *See also* Reg. §1.170A-16(d)(1)(i) (property), cross-referencing §170(f)(8) and Reg. §1.170A-13(f) and §1.170A-15(g) (cash). Reg. §1.170A-16(b) and §1.170A-15(g) are applicable to donations made after July 30, 2018.

[1100] §170(f)(8)(B). To qualify for a deduction, the donor must obtain the statement by the earlier of: (i) the date the donor files the return for the taxable year of the contribution; or (ii) the due date for the return, including extensions. §170(f)(8)(A), §170(f)(8)(C). *See also* §170(f)(17) (donor will not be allowed §170 deduction for cash, check, or other monetary contribution unless donor keeps as evidence: (1) bank record; or (2) written communication from donee showing donee's name and contribution's date and amount, effective for contributions made in taxable years beginning after August 17, 2006).

[1101] Reg. §1.170A-13(f)(13). *See also* Reg. §1.170A-16(b) (cross-referencing §170(f)(8) and Reg. §1.170A-13(f)).

[1102] §2036(a). *See also* Reg. §20.2036-1(c)(2)(iv)(E), T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (effective June 1, 2023).

[1103] §2055(e)(2)(A); Reg. §20.2055-2(e)(2)(v), §1.642(c)-6 (valuation dates on or after June 1, 2023), §1.642(c)-6A (valuation dates before May 31, 2023), T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (effective June 1, 2023).

[1104] §2056(b)(7).

[1105] §2044.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

D. Gift Tax Charitable Deduction

A gift tax charitable deduction is permitted for a transfer of property to a qualified pooled income fund, provided the charitable remainder beneficiary is described in §2522(a), including a corporation, trust, or community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.[1106] The gift tax consequences of transfers to pooled income funds are parallel to those described at IV.I., above, for charitable remainder trusts.

The gift of the remainder interest in a pooled income fund to a public charity is not subject to gift tax, although it must be reported by the donor on a gift tax return.[1107] The donor then is entitled to an offsetting gift tax charitable deduction. If an income beneficiary other than, or in addition to, the donor is designated, the actuarial value of the beneficiary's interest is subject to gift tax. The creation of an income interest in an individual other than the donor will qualify as a present interest for the annual exclusion.[1108] However, the creation of a secondary (i.e., successive) life interest will not qualify for the annual exclusion because it is a future interest.[1109]

If the donor's spouse is the only income beneficiary, the donor may elect to treat the interest of the spouse as a qualified terminable interest[1110] and, thus, qualify the interest for the unlimited marital deduction, in which case the interest is not subject to gift tax. The election is made on the donor's gift tax return on which the gift to the spouse is reported and must be filed in a timely manner in order to elect QTIP treatment. If a donor's spouse is the secondary beneficiary, it is not clear whether QTIP election can be made. To avoid a taxable gift, the donor spouse should retain the right to revoke the successor spouse's interest.[1111]

In most instances, a taxable gift can be avoided if the donor reserves the testamentary right to revoke the income interest of the secondary beneficiary.[1112] The retention of the right to revoke prevents the donor from making a completed, and therefore taxable, gift. The retention will result in the inclusion of the value of the secondary income interest in the donor's estate and should be used only where the donor is the first income beneficiary.[1113]

E. Generation-Skipping Transfer (GST) Tax

Generation-skipping transfer tax implications arise in instances where successive life income beneficiaries are assigned to a generation more than one below that of the donor. This would be the case where a donor assigned an income interest to his or her child for the child's life followed by an income interest to the donor's grandchild for the grandchild's life. See the discussion at IV.J., above, with respect to charitable remainder trusts.

F. Taxation of the Beneficiary

Generally, all of the income received by a noncharitable beneficiary of a pooled income fund will be taxable to the beneficiary as ordinary income. Conversely, before the taxation of the beneficiary of a CRT can be determined, the income and expenses must be allocated into the categories and classes discussed at VI.C., above. Distributions from a pooled income fund are not taxed under a tier system such as that applicable to charitable remainder trusts. Although income beneficiaries usually do not receive distributions of capital gains (because capital gains and losses are accumulated for the charitable remainder beneficiary), a fund's income may, under governing state law, be defined as or satisfied by a unitrust amount or pursuant to the trustee's power to adjust between income and principal to fulfill the trustee's duty of impartiality.[1114] The cost of doing this, however, is loss of the §642(c)(3) set aside deduction for long term capital gains. In addition, none of the income of a pooled income fund can ever be tax-exempt, because the fund is prohibited from investing in tax-exempt securities.

G. Tax on Capital Gains

Similar to property transferred by the donor to a CRT, as discussed in IV.L.1.b, above, the donor realizes no taxable capital gain (or loss) as a result of making a gift to a pooled income fund, provided the transferred property is not subject to any indebtedness.[1115]

Comment: This rule can provide an attractive planning consideration to a donor who owns low-cost but highly appreciated securities producing a relatively low rate of return and who wishes to convert them into securities yielding higher income. Ordinarily, such an individual would have to sell the low-cost securities, pay a tax on the gain realized, and then reinvest the net proceeds of the sale. However, by giving the securities to a pooled income fund, the donor will receive the benefit of a charitable deduction and also obtain the advantages of diversification and, at least potentially, a larger amount of income. This could be accomplished without paying any tax on the capital gain.

[1106] §2522(c)(2)(A); Reg. §25.2522(c)-3(c)(2)(v), §1.642(c)-6 (valuation dates on or after June 1, 2023), §1.642(c)-6A (valuation dates before June 1, 2023), T.D. 9974, 88 Fed. Reg. 37,424 (June 7, 2023) (effective June 1, 2023).

[1107] §6019.

[1108] §2503(b).

[1109] *See* Rev. Rul. 75-415.

[1110] *See* §2523(f).

[1111] Such a gift will fail to satisfy the requirement that a qualifying terminable interest must entitle the spouse for life to all of the income from the entire or a specified portion of the interest, payable annually or more frequently. §2523(f)(2), §2523(f)(3).

[1112] Reg. §1.642(c)-5(b)(2), §25.2511-2(c); PLR 7908026.

[1113] *See* §2036(a). *See also* Reg. §20.2036-1(c)(2)(iv) *Ex. 5.*

[1114] Reg. §1.642(c)-5(a)(5)(i), effective for taxable years beginning after January 2, 2004. *See* T.D. 9102, 69 Fed. Reg. 12 (Jan. 2, 2004). Such governing state law must provide for the fund's total return to be reasonably apportioned between the income and remainder beneficiaries and must satisfy the Reg. §1.643(b)-1 requirements. In exercising a power to adjust, the trustee must allocate to principal any proceeds from the sale or exchange of fund assets, at least to the extent of the fair market value of the assets when the donor contributed them or to the extent of the purchase price paid when the fund purchased them. Reg. §1.642(c)-5(a)(5)(i). As the preamble to T.D. 9102 observes, "The proper exercise of a power to adjust may provide the income beneficiaries with amounts in excess of the amount of traditional income." In conjunction with this amendment, Reg. §1.642(c)-2(c) was amended to provide that long-term capital gains from the sale or exchange of fund assets do not qualify for the §642(c)(3) charitable deduction to the extent distributed to the income beneficiaries.

[1115] Reg. §1.642(c)-5(a)(3). The transfer of property subject to an indebtedness will trigger the application of the bargain sale rules. §1011(b).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

A pooled income fund generally pays no tax on capital gains realized on its sales of securities with a holding period of more than one year.[1116] The fund takes over the donor's holding period and basis. The only time there can be capital gain is on the sale by the fund of securities with a holding period of one year or less[1117] or, for taxable years beginning after January 2, 2004, of securities with a holding period of more than one year if the long-term capital gain does not qualify for the §642(c)(3) set-aside deduction pursuant to Reg. §1.642(c)-2(c). In such case, tax on the gain is paid by the fund itself, and the fund uses the donor's cost basis for sales of donated securities.

[1116] This is by operation of the §642(c)(1) charitable set-aside deduction.

[1117] Reg. §1.642(c)-2(c), amended by T.D. 9102, 69 Fed. Reg. 12 (Jan. 2, 2004). See XXVII.A., above, for further discussion.

A donor will recognize gain if he or she receives property from the fund in exchange or transfers property subject to an indebtedness, whether or not assumed by the fund. In such instances, the bargain sale rules apply.[1118]

H. Private Foundation Rules

A pooled income fund is subject to the governing instrument requirements of §508(e). This requirement is discussed at VI.G.1.a., above. Section 4943 and §4944, however, will not apply to pooled income funds that satisfy the exception of §4947(b)(3)(B).

[1118] §1011(b); Reg. §1.642(c)-5(a)(3).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXVIII. Securities Law

A. *Philanthropy Protection Act of 1995*

The Philanthropy Protection Act of 1995 (1995 Philanthropy Act)[1119] was enacted to exempt charitable organizations that maintain pooled income funds from the registration requirements of the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. The legislation was prompted by uncertainty as to whether pooled income funds fell within the definition of "charitable organization" in the federal securities laws.

Even before its amendment by the 1995 Philanthropy Act, the Investment Company Act of 1940 excluded from its registration requirements any company organized and operated exclusively for religious, educational, benevolent, fraternal, charitable, or reformatory purposes, provided that no part of the company's net earnings inured to the benefit of any person or individual.[1120] Similarly, the Securities Act of 1933 and the Securities Exchange Act of 1934 excluded from their provisions (other than the anti-fraud provisions) any security issued by a person organized and operated exclusively for religious, educational, benevolent, fraternal, charitable, or reformatory purposes, and not for pecuniary profit, provided that no part of the company's net earnings or profits inured to the benefit of any person or individual.[1121] However, pooled income funds, arguably, fell outside the exemptions, because they provide a financial interest in the funds' net earnings, and, thus, the earnings inure to the benefit of persons and individuals.[1122]

The SEC received many requests from individual charities asking the SEC to confirm that it would take no action if a charity established a qualifying pooled income fund and failed to comply with the registration requirements. The first request for a so-called "no-action letter" was made by the American Council on Education in 1972.[1123] The American Council asserted that units in its pooled income fund were exempt from registration because: (1) units are securities issued by an exempt organization; and (2) a gift to a pooled income fund does not constitute a "sale" for "value" under the Securities Act of 1933 or the Investment Company Act of 1940. The SEC rejected the American Council's position, but stated that it would take no action provided that certain requirements were satisfied.

In 1980, the SEC issued a press release[1124] in which it expanded this no-action position and announced that pooled income funds did not need to comply with the registration requirements of the Securities Act of 1933 and the Investment Company Act of 1940.[1125]

The SEC's no-action position did not, however, protect pooled income funds from liability to litigants claiming that particular transactions violated the federal securities laws. Partly in response to a class action alleging that pooled income funds were investment companies required to register under the Investment Company Act of 1940,[1126] Congress enacted the 1995 Philanthropy Act.[1127] The 1995 Philanthropy Act codified and expanded the SEC's no-action position.

Specifically, the 1995 Philanthropy Act amended §3(c)(10) of the Investment Company Act of 1940 to exclude from the definition of "investment company" any fund maintained by a charitable organization exclusively for the collective investment and reinvestment of certain defined assets, including assets of a pooled income fund.[1128] Thus, such funds are not subject to registration. The 1995 Philanthropy Act also exempts the interests in such funds from the registration requirements of the Securities Act of 1933[1129] and from the registration provisions of the Securities Exchange Act of 1934.[1130]

In addition, the Securities Exchange Act of 1934, as amended, provides that a charitable organization and its trustees, directors, officers, employees, and volunteers, acting within the scope of their duties, will not be subject to the broker-dealer requirements of the Securities Exchange Act of 1934 solely because the organization or person trades in securities on behalf of a fund, including a pooled income fund, or the settlors or beneficiaries of such a fund.[1131] The exemption from the broker-dealer provisions of the Securities Exchange Act of 1934 is subject to the condition that any person soliciting donations on behalf of a charitable organization must be either a volunteer or employed in the overall fund-raising activities of a charitable organization, and must not receive special compensation based on the number or value of donations collected for the fund.[1132]

The 1995 Philanthropy Act — in addition to amending the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940 — added a new category of investment advisers exempt from registration under the Investment Advisers Act of 1940. A charitable organization and its trustees, directors, officers, employees, and volunteers, acting within the scope of their duties, are exempt from registration if they provide advice, analyses, or reports solely to a fund excluded from the definition of "investment company" in the Investment Company Act of 1940.[1133] Thus, investment advisers who provide advice to pooled income funds are exempt from registration under the Investment Advisers Act of 1940.

While exempting pooled income funds, interests in such funds, and their investment advisers from the registration and

---

[1119] Pub. L. No. 104-62.

[1120] 15 U.S.C. §80a-3(c)(10).

[1121] 15 U.S.C. §77c(a)(4), §78l(g)(2)(D).

[1122] H.R. Rep. No. 104-33, at 7 (1995).

[1123] American Council on Education, [1972–1973 Transfer Binder] *Fed. Sec. L. Rep.* §79,179.

[1124] Pooled Income Funds, Release No. 33-6175, 34-16478, IC-11016 (1980). See Additional Resources, below.

[1125] To qualify under the 1980 press release, a pooled income fund had to provide each prospective donor with a written disclosure statement that fully and fairly described the operation of the fund, and all solicitations for donations either had to be made by volunteers or by individuals who were employed by the charity in its general fund-raising activities and did not receive any commissions or bonuses based on the number of donations obtained. A public charity that intended to establish a pooled income fund did not have to submit a request to the SEC, unless the particular nature of the fund presented a new factual pattern.

[1126] *Richie v. Am. Council on Gift Annuities*, 943 F. Supp. 685 (N.D. Tex. 1996).

[1127] *See* H.R. Rep. No. 104-333, at 8 (1995).

[1128] Pub. L. No. 104-62, §2(a).

[1129] 15 U.S.C. §77c(a)(4), amended by Pub. L. No. 104-62, §3.

[1130] 15 U.S.C. §78c(a)(12)(A), amended by Pub. L. No. 104-62, §4(a).

[1131] 15 U.S.C. §78c(e)(1), added by Pub. L. No. 104-62, §4(b).

[1132] 15 U.S.C. §78c(e)(2), added by Pub. L. No. 104-62, §4(b).

[1133] 15 U.S.C. §80b-3(b)(4), added by Pub. L. No. 104-62, §5.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

broker-dealer requirements of the federal securities laws, the 1995 Philanthropy Act does not exempt them from application of the anti-fraud provisions of the securities laws.[1134]

B. Disclosure Statement

Each fund that is exempted from the registration requirements of the federal securities laws must provide a disclosure statement to each donor at the time of donation.[1135] The disclosure statement must contain "written information describing the material terms of the operation" of the fund.[1136]

In general, a disclosure statement should provide the following:

- a description of the charitable remainder beneficiary;
- a statement that the fund cannot guarantee a fixed rate of return and is not covered by SEC protection;
- a copy of the pooled income fund trust agreement and a sample instrument of transfer; and
- a brief summary of (a) the operation of the fund, including the calculation of units of participation and the distribution of income, (b) the fund's investment policies and the names and qualifications of the investment manager, and (c) the taxation of donors, beneficiaries, and the fund.

If the fund's investment policy is atypical (e.g., the fund invests in depreciable real estate), then the statement should disclose the specifics of the policy.

A public charity maintaining a pooled income fund should update the statement annually or more frequently if there is a material change in the nature of the public charity, the fund or its operation, or the federal tax law.

Each beneficiary of the fund should receive on request an annual report and certified financial statements, including a balance sheet showing the number and value of the units in the fund. The financial statements should give the total market value of the fund including separate schedules of all securities and any gains and losses thereon for the past three years.

Comment: The instrument of transfer should state that the donor has reviewed a copy of the disclosure statement.

A sample disclosure statement is included in the Worksheets, below.

[1134] H.R. Rep. No. 104-333, at 7 (1995).

[1135] 15 U.S.C. §80a-7(e), added by the 1995 Philanthropy Act, Pub. L. No. 104-62, §2(b).

[1136] 15 U.S.C. §80a-7(e), added by the 1995 Philanthropy Act, Pub. L. No. 104-62, §2(b).

C. State Blue Sky Considerations

The 1995 Philanthropy Act[1137] preempted, for at least three years, state securities laws. State securities laws (known as "blue sky laws") require registration of securities and impose regulatory requirements on dealers, brokers, agents, and investment advisers. Before the 1995 Philanthropy Act, the extent to which state securities laws applied to pooled income funds was uncertain.[1138]

The 1995 Philanthropy Act amended the Investment Company Act of 1940 to provide, in general, that interests in pooled income funds excluded from the definition of "investment company" are exempt from any state law that requires the registration or qualification of securities.[1139] The Investment Company Act of 1940, as amended, also provides that no charitable organization or trustee, director, officer, employee, or volunteer of a charitable organization acting within the scope of his or her duties is subject to regulation as a dealer, broker, agent, or investment adviser under any state securities law because the organization or person trades in securities on behalf of a charitable organization, a pooled income fund, or the settlors, potential settlors, or beneficiaries of a pooled income fund.[1140]

However, the 1995 Philanthropy Act also contained an opt-out provision. During the three-year period beginning on the date of the legislation's enactment, any state could enact a statute that referred to §6 of the 1995 Philanthropy Act and provided prospectively that §6 would not preempt the laws of that state.[1141] Several states took advantage of the opt-out provision and enacted legislation stating that §6 of the 1995 Philanthropy Act does not preempt state laws after the effective date of the state legislation.[1142]

States continue to apply their securities laws to pooled income funds in different ways. An organization that intends to establish a pooled income fund should seek the advice of counsel to determine the applicability of local securities laws.

[1137] Pub. L. No. 104-62.

[1138] *See Richie v. Am. Council on Gift Annuities*, 943 F. Supp. 685 (N.D. Tex. 1996). Before the 1995 Philanthropy Act, many jurisdictions had adopted some form of the Uniform Securities Act, which provides that the units in a pooled income fund are exempt from registration if they are issued by a qualifying non-profit organization. However, even in jurisdictions enacting versions of the Uniform Securities Act, it was not clear if broker-dealer registration was required.

[1139] 15 U.S.C. §80a-3a(a), added by Pub. L. No. 104-62, §6.

[1140] 15 U.S.C. §80a-3a(b), added by Pub. L. No. 104-62, §6.

[1141] 15 U.S.C. §80a-3a(c), added by Pub. L. No. 104-62, §6.

[1142] *See, e.g.*, Va. Code Ann. §13.1-514.2.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXIX. Planning Considerations

A pooled income fund permits donors with less than substantial amounts of accumulated wealth to make split-interest gifts while retaining an income interest in the transferred property. The pooled income fund was designed as a vehicle to accept transfers too small to justify establishment of a charitable remainder trust. As a general rule of thumb, in the case of contemplated gifts of less than $100,000, the cost of establishment and administration of a charitable remainder trust suggests that the donor consider a gift to a pooled income fund instead.

Planning considerations for a pooled income fund are similar to the planning considerations discussed at II., above, with respect to charitable remainder trusts, specifically a charitable remainder unitrust. The additional advantages and disadvantages are discussed below.

A. Advantages

The pooled income fund is an alternative to the charitable unitrust, particularly for taxpayers of intermediate wealth. Both inter vivos and testamentary contributions can be made to a pooled income fund. In addition, the donor to an established pooled income fund may have greater income security because the fund's assets are likely to be invested in a diversified portfolio. The donor receives the benefit of this "instant diversification" without the adverse tax consequences that can arise from a sale or exchange of long-term capital gain property.

The donor also may retain a considerable degree of latitude in determining the final disposition of the income interest. As in a charitable remainder trust, the donor is able to retain the testamentary power to terminate or revoke the income interest of any designated beneficiary except the charitable remainder beneficiary. In each case, this feature permits the donor to avoid making a completed gift and, therefore, avoid gift tax on the initial transfer.

One difference is that, unlike in a charitable remainder annuity trust, the income payments are not fixed with a pooled income fund. Accordingly, the income payments can keep pace with inflation. With a successful investment strategy that includes at least some growth, the beneficiary's annual income payments can increase with the appreciation of the fund's assets in a manner comparable to the charitable remainder unitrust. In addition, the donor to a pooled income fund is not required to assume an active role in the management of the trust assets as he or she may with a charitable remainder trust. Of course, the prohibition on a donor's acting as the trustee would be a drawback if the donor desires active participation in the investment policies of the fund.

B. Disadvantages

The donor to a pooled income fund makes an irrevocable gift of the transferred assets and retains the ability to receive only ordinary income. In contrast, with a careful investment strategy, the trustee of a charitable remainder trust may be able to ensure that the income payable to the beneficiary is in the form of capital gains, tax-exempt income, or even a return of capital.

The initial charitable deduction for a gift to a pooled income fund that has either been in existence for three years or less or has a historically high rate of return may be significantly lower than the charitable deduction resulting from a similar gift to a charitable remainder trust.

C. Practical Considerations

The policies of a pooled income fund should focus on procedures that favorably affect the functioning of the fund. For example, it may be helpful to establish a minimum value for both initial contributions and additional contributions by donors. In addition, trustees of pooled income funds may not wish to be constrained by non-income-producing investments that are not readily marketable; the governing instrument could, therefore, contain a provision stating that the trustee has the power to decline to accept any property transferred. As a practical matter, the trustee should consider rejecting all contributions of personalty and perhaps real estate. The acceptance of low-income or non-income-producing property will reduce the rate of return of the fund until the property is sold.

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXX. Drafting Considerations

Rev. Proc. 88-53 provides a sample declaration of trust for a pooled income fund and instruments of transfer. The sample provisions satisfy §642(c)(5) and the requirements for pooled income funds. The IRS stated in the revenue procedure that if the public charity creating the fund makes specific reference in the governing instrument to Rev. Proc. 88-53 and adopts substantially similar terms, the IRS will recognize the trust as satisfying the requirements of §642(c)(5). Rev. Rul. 85-57 includes provisions for the selection of an alternative charitable remainder beneficiary in the event that the designated public charity fails to qualify as such at the termination of an income interest.

Comment: In now-superseded Rev. Proc. 88-54,[1143] the IRS announced that it will no longer ordinarily issue advance rulings on the qualification of pooled income funds or whether a transfer to a pooled income fund will qualify for an income, gift, or estate tax deduction. It is the intent of the IRS that charities use the format provided in Rev. Proc. 88-53. This IRS ruling position on pooled income funds is now contained in the third annual revenue procedure published in the first annual Internal Revenue Bulletin.[1144] This no-ruling policy presents difficulties for drafters of pooled income funds for which the sample language in Rev. Proc. 88-53 is not appropriate.[1145]

[1143] *Superseded by* Rev. Proc. 89-3.

[1144] *See* Rev. Proc. 2026-3, §4.01(16), §4.01(36), §4.01(52), §4.01(58).

[1145] *See, e.g.*, PLR 9027036, PLR 9026017 (declining to rule on qualification of pooled income funds with depreciation reserves, citing Rev. Proc. 88-54). *Cf.* PLR 9136026, PLR 9135046, PLR 9126011 (rulings on qualification of pooled income funds). *See also* PLR 9642037 (approving both trust agreement and gift agreement for pooled income fund that contained provisions not found in Rev. Proc. 88-53). The IRS stated that it will rule on fund instruments that contain provisions not addressed in Rev. Proc. 88-53. *See, e.g.*, PLR 200252066 (ruling on qualification of pooled income funds because issue presented was not addressed by sample trust in Rev. Proc. 88-53), PLR 200608002–PLR 200608003, PLR 201450016 (ruling that certain provisions of governing instruments not contained in Rev. Proc. 88-53 are consistent with the requirement of §642(c)(5), without ruling on whether the governing instruments meet all requirements of §642(c)(5)).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

XXXI. Filing Requirements

Pooled income funds may be required to file the following forms: (1) Form 1041, *U.S. Income Tax Returns for Estates and Trusts*; (2) Form 4720, *Return of Certain Excise Taxes on Charities and Other Persons Under Chapters 41 and 42 of the Internal Revenue Code* (only if there is a Chapter 42 excise tax liability); and (3) Form 5227, *Split-Interest Trust Information Return*.[1146] Forms 1041-A and 5227 must be filed by April 15 following the close of the calendar year.[1147] Rev. Proc. 83-32[1148] contains a table summarizing the pooled income fund filing requirements.

Any claim for a deduction for the value of the remainder interest transferred to a pooled income fund must be supported by a statement attached to the return showing the computation of the present value of such interests.[1149] The method of calculating a pooled income fund's yearly rate of return must also be supported by such statement.[1150] In addition, a donor claiming a deduction for a noncash gift to a pooled income fund in excess of $500 must complete the applicable portion of Form 8283, *Noncash Charitable Donations*. The donor must also receive a written acknowledgment of the gift from the fund, although the acknowledgment is not filed with the return.

[1146] Effective for returns for taxable years beginning after 2006, §6034(a), amended by the Pension Protection Act of 2006, Pub. L. No. 109-280, §1201(b)(1), §1201(c)(2), no longer contains an exception to the information return filing requirement for years in which a pooled income fund is required to distribute all net income currently. Section 6034(a), as amended, requires a pooled income fund to furnish such information concerning its taxable year as required by the IRS (regardless of whether the fund is required to distribute all its net income in that year). See VI.E., above, for more information on the §6034 requirements. For taxable years beginning after 2006, a pooled income fund's §6034 filing requirements are satisfied with Form 5227. For taxable years beginning before 2007, a pooled income fund also filed Form 1041-A, *U.S. Information Return — Trust Accumulation of Charitable Amounts*. The instructions to Form 1041 indicate that 1041-A is no longer filed by pooled income funds.

[1147] See VI.E., above, for a discussion on using Form 8868 to request an extension of time to file these forms. Upon filing Form 8868, taxpayers are entitled to a single, automatic six-month extension for filing Form 4720, Form 1041-A, and Form 5227. *See* Reg. §1.6081-9, T.D. 9892, 85 Fed. Reg. 5323 (Jan. 30, 2020). Upon filing Form 7004, taxpayers are entitled to a 5 ½-month extension for filing Form 1041, which would be September 30 for calendar year taxpayers. *See* Reg. §1.6081-6, T.D. 9892.

[1148] For further discussion, see 452 T.M., *Tax-Exempt Organizations — Reporting, Disclosure, and Other Procedural Aspects*.

[1149] Reg. §1.642(c)-6(a)(3). For a sample pooled income fund statement, see *Trust: Pooled Income Fund Statement (§642(c)(5))* in the Bloomberg Tax Elections & Compliance Statements.

[1150] Reg. §1.642(c)-6(c)(4).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7

TABLE OF WORKSHEETS

	LEGISLATIVE HISTORY
Worksheet 1	Conference Report to the Taxpayer Relief Act of 1997, H.R. Rep. No. 220, 105th Cong., 1st Session, 605–608 (for the Amendment of §664).
	SAMPLE DOCUMENTS, ELECTION STATEMENTS, AND CHARTS
Worksheet 2	Sample Charitable Remainder Trust Forms.
Worksheet 3	Sample Contribution Statement. (As required by Reg. §1.664-4(c) for unitrusts and Reg. §1.664-2(d) for annuity trusts).
Worksheet 4	Sample Memorandum to Individual Trustee of Newly Created Charitable Remainder Unitrust.
Worksheet 5	Pooled Income Fund Disclosure Statement.
Worksheet 6	Approximate Charitable Deduction Factors for Charitable Remainder Unitrusts at Various Payout Rates (5% to 10%) for One and Two Lives.
Worksheet 7	Maximum Suggested Gift Annuity Rates.
Worksheet 8	Model One-Life Gift Annuity Agreement.
Worksheet 9	Model Two-Life Gift Annuity Agreement for Spouses.
Worksheet 10	Model Deferred Payment One-Life Gift Annuity Agreement.
Worksheet 11	Model One-Life Flexible Deferred Payment Gift Annuity Agreement.

Working Papers for this Portfolio can be found at https://bloombergtax.com.

Additional Resources:

- Ron Shoemaker & David Jones, Charitable Remainder Trusts: *The Income Deferral Abuse and Other Issues, IRS Exempt Organizations Continuing Education Technical Instruction Program for FY 1997* (available at https://www.irs.gov/pub/irs-tege/eotopick97.pdf).
- IRS Form 5227, *Split-Interest Trust Information Return*, is available at http://www.irs.gov/pub/irs-pdf/f5227.pdf.
- *Prior Month Rate Election for Valuing Charitable Remainder or Lead Interests (§7520(a)).*
- Pooled Income Funds, Exchange Act Release No. 33-6175, No. 34-16478, IC-11016 (Jan. 10, 1980).

© 2026 Bloomberg Industry Group, Inc., Arlington, VA
ISBN 978-1-63359-295-7