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Moderator: I, again, like everybody else, would like to thank you for coming. I know it's raining and it's a tough day and I actually lost a bet. I bet there would be 26 people here tonight. You got to 28 so I lost a dollar to Mike over there. I appreciate everybody showing up. It just would have been nice if you stopped at 26 (laughter). My name is Jerry Citroela as Guy said. My role is as a financial adviser by practice, but tonight, I'm a volunteer. I'm a volunteer for an organization called Philanthropy International. Philanthropy International is a national community foundation dedicated to helping organizations teach tax exempt planning strategies. We help teach tax exempt planning strategies to CPA's, attorneys, individuals like yourself and we help charities through marketing for their own personal efforts. A lot of that will be explained as we go through this, but just know, my capacity tonight is as a volunteer speaker for an organization called Philanthropy International, helping North Ridge Hospital spread the word of a strategy that we feel is very valuable.

The title of this speech is actually called, "What a 1031 Exchange Won't Do." We're here to talk about something a little bit different, which is actually exiting real estate. You're not exiting real estate as a deferral strategy, which is what a 1030 Exchange will do, but exiting real estate altogether. Because at some point, I think people are ready to get out. But before I get started, how many people here own investment real estate? How many people here have owned that investment real estate for more than 10 years? 15? 20? Okay, good news is you have lots of gain. Bad news is have you looked at the numbers of what it would cost you to sell it? Taxes are pretty big. So we're going to talk about some tax favored strategies for exiting real estate. Now, I need you all to be open minded with me because I'm going to talk about some things here that you may have heard of before and you may have some misconceptions about. So my role tonight is to educate on a strategy that makes a lot of sense for a lot of people, but in our opinion is greatly under utilized. We do this for CPA's and attorneys, not only locally, but around the country and you'd be surprised how many of them have heard of this, but have never recommended it to their clients because they're not comfortable, but it is very valid tax law and very useful ways of exiting real estate.

So first question is why real estate? Why are you in real estate? Because it makes lots of money for you, produces a nice passive income, has some nice appreciation and it's something that people are comfortable with and in California, it never goes down, right? Well, not recently – well, it has gone down, but there's an impression out there that it's a wonderful investment and we're not here to say real estate is bad. We're just here to say maybe we have a strategy when you're ready to get out. But real estate has been great. I'm a real estate investor myself. We all believe in it, so real estate can make us all some money. But the question is what are the exit

strategies, because at some point in your life, you might want to say, “I’m done” or “I’m done with some of it.” Maybe you’ve just accumulated a couple of properties over your lifetime and you’ve retired recently and dealing with toilets and tenants and repairs just isn’t as exciting as was any more. And you just think, “I’m just ready to be out of it.” Somebody’s laughing. You have a leaky toilet in your property, don’t you? Okay, so you know what I’m talking about.

So what are the exit strategies? We’re going to go through that and talk about your options and let you know some of the best ways to do that. What are the tax implications? As David said a little while ago, I think you’ve got up to 34% or 39% potential tax. I like to use the number of 25%. So as I’m going through this illustration and the presentation, you’re going to see me talk about the tax on the sale of investment real estate or other appreciated assets and I’m talk about 25% because that’s a pretty realistic expectation. So for every million dollars in gain, you’re going to pay a quarter million in tax. Painful. Most people don’t make a quarter million over a 2- or 3-year period. And that’s the tax you’d have to pay on just that one multi-unit building you have.

That all came about in 1913 with the 16th amendment when it was put into law that we all get to pay taxes. It was supposed to be something small and it’s grown way out of proportion, but we’re not here to say taxes are bad because without taxes, we wouldn’t have defense. We wouldn’t have emergencies – emergency care. We wouldn’t have freeways. Who enjoys the freeways? Imagine how bad they’d be if we had a lower tax rate and they couldn’t repair them ever. So taxes are good. We understand that. We know it’s a necessary thing out there. What we want to do, though, is teach you how maybe you can defer some money that would otherwise go to tax somewhere else that’s more in line with your personal beliefs.

Ask you a question. Would you be surprised if tomorrow Congress passed a law letting you reduce, delay or even completely eliminate your tax?

Respondent: No.

Respondent: No.

Moderator: No. You wouldn’t be surprised?

Respondent: No.

Moderator: Why is that?

Respondent: They get their money sooner or later.

Moderator: Well, actually, they already did this in 1969. In 1969, there were some laws passed, code section 664, that says clearly “If you are willing to plan a gift, the IRS is willing to forgive a tax.” Now, we’re going to go more into this, but I want you to understand. What I’m going to talk about today is not one of these tax schemes. This is as we like to say, “right down the middle of the main street”. It’s just an under utilized strategy that because it’s fairly specific, and more importantly, very flexible, a lot of people in the world of planning, just stay away from it and just say, “I can’t figure it out. So it’s bad.” Understand, it’s been around since ’69. It’s been rewritten in the ‘80’s. We’re going to go through this as the taxes are written very clearly and will help you understand it.

First thing we need to realize is there’s something called personal capital. Now what is personal capital? Everybody reaches into your pocket or your purse and you pull out what’s in there and it’s green. That would be money. That’s personal capital. If you own a car that you drove in here – personal capital. If you have a house, rental properties, IRA accounts – whatever you have. That’s your personal capital. But there’s a piece of that that goes away occasionally called social capital. And what is the default for social capital?

Where does most of your social capital end up? As someone said over here, “They’re going to get it sooner or later”, right? Most of your default capital or social capital goes to tax because you do your taxes with a wonderful tax person that we just heard speak and at the end of the year, they say, “This is what you owe.” So that’s what you do.

Now, I’m assuming some of you are charitable and you donate some money occasionally. Maybe some of you more than others – that’s your personal business. But usually, the charitable stuff is either a cute little girl comes up and talks you into buying some cookies or your church passes around a basket or you just bump into something that sounds good or there’s a cause or something that you latch on to, but it’s usually a small portion of your social capital.

What I’d like to show you is you have the opportunity to take this charitable portion of your social capital, expand it, limiting what part of it goes to government, goes to tax and, here’s the important part, at the same time, increase your current income, your net worth and your overall estate size. So I’m going to repeat that. I want to show you how you can help charity and increase your personal situation in terms of income and estate size.

Who’s a great philanthropist? Anybody that gives of their time, effort, income, property and taxes. Why is taxes up there?

Respondent: It goes to charity.

Moderator: It goes to charity. What’s the number one nonprofit organization in the world?

Respondent: The United States Government.

Moderator: Our IRS. Okay, so you are already a great philanthropist. So some people say, “Well, I’m not charitable.” I beg to differ. If you could take all of your charitable contributions that you’ve given to IRS over the years and figured out what they’ve earned on those in interest and totaled that – you’re laughing – this is a scary number. Figure out what you’ve paid in tax over you lifetime, add some interest to it and imagine if you can back now. It’s a big number. So we are all great philanthropists. What I suggest to you is why not explore some options where you can direct your philanthropy rather than go with the default method?

Tax and charity are realistically 2 parts of the same system. We like to say 2 hands of the same system. Tax is the default. Charity is an option. Unfortunately, most people think charity is the little stuff left over at the end. Realistically, it can be the first option.

Let me explain something here. Does anybody believe that charity is needed?

Respondent: I do.

Moderator: Okay. Do you think the IRS believes that charity is needed? Without charity – before charities were around, who had to take care of our social issues?

Respondent: The Government.

Moderator: Think of other countries. Who takes care of health care?

Respondent: The Government.

Moderator: The Government. Who would have – we do a lot of work with the March of Dimes on a national basis doing some of this stuff. If March of Dimes hadn’t cured polio, do you think there’d be polio still if the Government was responsible for curing polio?

Respondent: It would be there.

Moderator: Who takes care of your kids after school? The Boys and Girls Clubs. Government knows there’s a need for charity. Now, who used to fund charity before the fund raiser was invented.

Respondent: The Government.

Moderator: The Government. The Government still funds charity, but who was solely responsible for it? Charity. I’m sorry, Government. If Government gave \$1 to charity to

support them, what would that cost them? Easy math divided by $1 - 1$ minus nothing, 1 plus nothing. I'm helping you out here.

Respondent: 1

Moderator: 1 divided by $1 - 1$. So if Government gave \$1 charity, it would cost them \$1. If the Government said to you I will allow you to give \$1 to charity and I will forgive you a tax for that \$1, if you're in the highest possible tax bracket, what does that cost the Government?

Respondent: 35%.

Moderator: 35% - 42%, State and Federal maybe. So it's cost them less than 50¢. Let's just call it 50¢. So if Government gives money to charity, it costs them \$1. If they allow you to do it, it only costs them 50¢ or less. So these plans are fully supported by them because we know a few things – we know charities are necessary and Government supports them completely; we know they have to be funded; and we know it's a great deal for the IRS if they let you fund them rather than them. The decision is which way do you want to go with your money – IRS or charity because you truly do have that option.

I have a simple equation for you regarding your appreciated asset – your real estate. If you sold it, you can pay 25% now in tax, right? We understand that. Capital gains tax on the gain, or you can pay 10% later to charity. When I say later, it's a term of years or the end of your life. If I told you nothing else, which would you choose?

Respondent: Later.

Respondent: Later.

Moderator: So 25% to tax or 10% to charity – later. What if I said it was 25% now in tax or 10% now to charity, which would you choose? What if it was 25 and 25 now? Don't answer that. What if it was 25% to tax now or 26% to charity now? Would you give up an extra 1% if you were allowed to give it all to charity instead of tax? See, you're all charitable here by the nods. It's even better though. It's 25% now or 10% at the end of your life to charity and that's a choice you're given clearly written in the tax code. So we're going to talk about that.

Let's have some fun though. Everybody has a penny. If you had a penny and it doubled every day for 30 days. So one penny turns into 2, into 4, 8, 16, 32, 64 – that's as far as I'm going. What would that be worth at the end of 30 days?

Respondent: Quite a bit.

Moderator: Quite a bit is not the appropriate answer (laughter). It's accurate, I guess, but it's not appropriate.

Respondent: I'd have to have my calculator.

Moderator: Somebody throw a number out there. What do you think?

Respondent: \$900,000.

Moderator: \$900,000 – close. What did you say? A million something. Close. Close. \$5,368,709. That's power of compounding interest and your money growing on your money. But what happens when you have to pay a tax on it? The same story – we have a penny that doubles. But instead of doubling it again, instantly, we have to take 20% of that out. So we turns into 2 minus 20% and then that doubles. And then we take 20% out and then that doubles and so on for 30 days. So it's \$5.3 million without the tax, without the 20%, what is it when this happens?

Respondent: A lot less.

Moderator: A lot less. You're very decisive.

Respondent: I haven't had time to *.

Moderator: Where do you live? Over there (laughter). \$252,873. Now, I'm not here to tell you we can double a penny every day for 30 days, but this is just a good example of what the effects of tax are and how much they can hurt your earnings.

Common options for exiting your real estate: first one is real obvious – it's called a typical sale. What does that mean? Put a sign in the ground, * list it for you, you sell it. Everybody's happy. What happens? You pay some tax. But also here to tell you that might not be such a bad option. A lot of people won't even consider it. But you might have to think about what you're getting in your rentals, what the hassles are, what you're dealing with and what you might end up with after the tax. Sometimes it's not a bad option just to sell the darn thing if you're done with it. Again, tax is bad if you don't want to – tax isn't bad if you understand the benefits of it, but sometimes, it's just time to get out.

You can do a gift during life. Pretty simple. You can gift it to your children or somebody else. Not recommended, but an option.

You can do a bequest at death, which means you're going to give it to somebody or a charity at the time of your death.

You can do a TIC. Anybody hear of a TIC? Okay. Tenants in Common, Tenancy in Common – it's a way for you to exit your real estate and actually, in a lot of cases, 1031 into a Tenancy in Common situation where you're actually owner of the real estate. You do hold title to it, but you're now no longer in action. You're no longer managing it. It's like a limited partnership. Like a partnership, but Tenancy in Common allows you to get out of the business of real estate, but still own real estate. Less control, less options, but some people like that opportunity to still be in, but kind of be out.

Anybody here hear of a private annuity trust? Okay, I'm going to touch on that for one second. There are red lines through of it. You've heard of one. There are red lines through it because it's not longer in existence. It's a good example of abuse. A private annuity trust was not a law was an interpretation of the law and a use of a law and an abuse of it. People were promoting ways to get out of real estate saying this was the perfect fit. I'm surprised nobody here has heard of it because there were a lot of seminars going around with a lot of people that weren't doing things right. I won't tell you any more other than if you have anybody telling you to do a private annuity trust or you're in one or in the process of one, please call me or someone else who knows the situation because it's not legal any more and you need to make sure that you're not involved in. So private annuity trust – no good.

1031 Exchange – David talked about that a little bit. And that is simply a way to exit one piece of real estate and get into another piece of real estate. We're going to talk more about that.

And then the last thing is a split interest trust. What the heck is a split interest trust? Well, we're going to get to that. That's the big meat of this thing.

What will a 1031 Exchange do? And I know we've been through this a little bit, but I want to recap it. It will defer – big important word – defer capital gains. You're going to get to pay them eventually. You're just going to extend that period of time. It will avoid recapture of depreciation as long as you keep 1031'ing, but eventually, you're going to have to deal with that. It allows you to consolidate equity – allows you to diversify equity, whichever you want to go. And it could potentially increase your leverage. What won't it do? It will not reduce your capital gains tax. It will not reduce your current tax liability. It will not reduce your estate tax liability and it will not give you a tax deduction. Now, why in the world would I even say that? No one ever thought that doing a 1031 would give you a tax deduction. Well, you'll understand when we talk about that in just a minute.

It also will not, in some cases, increase your current income stream. And I'd like to touch on this for a second. Why would do a 1031? Either you're in a horrible property you need to get out of or you're trying to improve your situation. I think everybody in the room own their property for at least 10 years by the show of hands, so you all have what? A low basis. You also all have a

property tax bill that's based on the purchase price 10, 15 or 20 years ago. If you 1031 that property you bought for \$200,000 that's now worth \$1 million and you have to buy something that's worth a million or more, what would just the property tax bill alone look like?

Respondent: About \$12,000.

Moderator: There goes all of your profits. 1031's aren't making a lot of sense in a lot of cases right now just because of the new tax bill. So you may not be able to increase your current income stream. In fact, you may limit it. You can't protect your assets against creditors and in big, bold hefty letters up there, you see a 1031 Exchange does not provide an exit strategy. It does not get you out of real estate if that's what you're looking to accomplish.

Challenges with a 1031 Exchange – we talked about this again, but finding a replacement property. Again, you have 45 days to identify it. Your ability to negotiate – you have 180 days to close that property. What if you're on the 175th and you find out that there was some termite damage that they didn't know about or it just popped up and you tell the seller who knows that you're doing a 1031 and knows you have to close in 5 days that you want him to pay to have that fixed? Do you think he's going to do it?

Respondent: No.

Moderator: A lot of your ability to negotiate is limited because of the time frames that are there. So getting the best prices, getting work done – these things can be hurt. Your ability to walk away – again, you're not leaving the real estate. Selling and buying in the same market – it's a high market. You're selling high and buying high. Wouldn't it be nice to be able to get out and by low or you're buying low and selling market there? New problems – who here knows everything that's wrong with the properties they own now? Who here knows everything that's wrong with the property 3 doors down from here? You know your problems in your real estate. You don't know what you're getting yourself into. Why is that person selling it if it's such a good deal? Could be some problems there. And the new property tax basis is the big issue.

Now, if you love real estate and you want to take 4 properties and move them into one or take one and move them into 4, the 1031 can be a great opportunity for you. This is not a "We have to exit real estate. We can't do a 1031" seminar.

Respondent: It's got to be like property.

Moderator: Like property. A lot of rules that go around it. Yes. It has to be like property. So, if you're interested in staying in real estate, a 1031 can be an option. Just know the parameters. Know the rules. What I'm here more specifically to talk about is what we really want sometimes. We want to actually sell our investment real estate. We'd like to avoid or

delay the taxes. How's that? Who wants to increase their cash flow? You can have a higher income. Do you want it? Don't say no. You'll look really silly (laughter). We want to simplify our lives. Real estate is great, but is managing your own properties really a simple task?

Respondent: No.

Moderator: Sometimes. It depends on the property, right? You can get into those things that are a little difficult. Just do what I do. Buy them in Arizona and pay somebody to handle it. I don't even want to see a tenant.

Respondent: Yeah.

Moderator: Take care of your loved ones. Any planning you do, obviously, you want to make sure that your loved ones are taken care of or at least not hurt. If this anything that you're interested in, stay for another few minutes. What I'd like you to do – this is the open minded part – is consider what is called a charitable trust, also known as a qualified split interest trust or more popularly known in this scenario as a charitable remainder trust. As I mentioned before, if you want to look it up, it's Section 664 of the Internal Revenue Code put into place in 1969, revisited in the 80's and made even stronger. Nothing I'm about to tell you is one of these things that you kind of have to hide while you're doing it. This is right down the middle of main street, IRS approved, right in the code.

What are the basics of the trust? Does anybody here own a revocable living trust – your basic living trust?

Respondent: I do.

Moderator: Pretty simple, right? You put your – you set up. You get a big thick book. When you open a bank account, you bring them the book and the book owns your bank account. Right? But you're still in control over it. And it's just a simple little document. The same thing here. There's something called a grantor. Now what is a grantor? A grantor is somebody that has something and gives it. You're granting it. So the grantor puts something into the trust. There's a trustee. A trustee is simple. The trustee is the person who controls the trust. That can you be you or somebody you assign. And there's the beneficiary. We all know what beneficiaries are because we love to be them, but a beneficiary is somebody or something or an entity that benefits from the trust. Okay, simple – three parts – someone puts something in, somebody controls it and somebody gets something at some point in the future.

Split interest trust adds one little piece to that. Grantor is the same. Trustee is the same. The difference is now we have a split beneficiary. So before where there was basically one party getting something out of it, this one has 2 parties sharing in the 2 pieces of any trust. One is

income, so there's something in the trust creating income. One party gets that. And then at the end of the term of the trust or the end of the life, what is there? There's the remainder – whatever is left in it. Another party gets that. Clear enough? Put something in, somebody controls it. At the end of the term, somebody gets what's left. In the meantime, somebody receives income from it.

How a charitable remainder trust works is the assets are transferred to the trust. So you have your real estate. You transfer it to the trust. Just like you did when you opened up your living trust. See that? The little house moved over there. Pretty simple to understand? That's the easy part. There's a cash flow to the beneficiary. So while this trust is in tact, somebody will receive some income from it. At the end of the trust, the remainder goes to charity.

Now, this is the part where everybody says, "Thanks. I'm out of here." We're going to go a little bit further and explain how this really does make sense. Benefits of a CRT, charitable remainder trust, is you can completely avoid capital gains tax. This is what's called a qualified split interest tax exempt trust, meaning any sales inside of this trust do not pay capital gains tax regardless of the size of the gain. If you bought it for \$1 and it's worth a billion, you can sell it in here and pay no tax. You can receive a cash flow for your lives or term of years. Typically, we see 6% to 9%. The laws are you can take as little as 5 – you have to take at least 5 and you can take as much as 50%. The rules say there has to be a remainder for charity, which we'll talk about. But the rules are as little as 5, as much as 50% on an annual basis.

You get an income tax deduction now. Let's stop for a second. When did we say you have to give this gift? End of your life.

Respondent: When you die.

Moderator: End of a term. When do you get the deduction for that?

Respondent: Now.

Moderator: Today. If you have 30 years left, you get a deduction today for what you're going to give away 30 years from now. That's a pretty good deal. You get to earn on the savings from that deduction for the rest of your life. Big deal here. Assets also go tax deferred. Now, if you have produced income in your real estate, can you say, "Wait a minute. I don't need it this year, so I'm not going to pay any taxes on it". It can't happen. In this, you only pay taxes on what you get out of it, not what is growing inside if you don't take that distribution.

Who's in control? This is a big question. We talked about this a little bit, but one of the big concerns about these types of trusts is people feel, "I lost control of my asset." In this trust, you are the grantor. You put the asset in. You can be the trustee or you choose the trustee and tell

them how to run this trust. So you're in control of what happens in the trust. You choose the beneficiaries. You choose the investments inside the trust. Those investments can be any typical investments – mutual funds, stocks, bonds, real estate – you can actually have real estate inside this trust as well if you absolutely love it. You choose the pay-out rate and you choose the length, as long as it qualifies according to the IRS rules which are clearly stated, redefined every month by the rate that they're giving us to determine if this makes sense. As long as you qualify, as long as you abide by those rules, you have a qualified trust and you get to choose all of these things accordingly.

Okay, so what do we have? We have an opportunity to place our real estate in a trust, sell it tax free, receive an income. At the end of the life, the charity gets the remainder. We're going to explain that a little bit more, but first let's look at what it looks like if you just sell the property.

You all have assets – retirement assets, residence, investment, business and right here, you have your real estate assets. And you've just decided time to sell that \$2 million piece of property. Now, for our purposes, we're going to assume you have 0 basis, meaning you bought it a long time ago. You did a good job of depreciating it and it's all gain. It makes my math easier. So there's \$2 million that's all gain. Okay? We're also going to assume 25% tax as I discussed earlier.

You sell that property and you'll notice the \$2 million is no longer real estate. It's now an investment because it's turned into cash, which means you can do whatever you want with it. Unfortunately, you're going to get hit with a \$500,000 tax. Ouch. Who wants to write a check for \$500,000? The wrong direction – that's it - \$500,000 tax, that's if it's only 25%. It can go higher. At this point, then, assuming a rate of return of 7% - it could be higher, it could be lower – we're just assuming 7 – a pretty safe, realistic number. You're going to receive an income of \$105,000 a year for the rest of your life, retaining the principle. So the \$1.5 million stays in tact. You get \$105,000 a year for the rest of your life. With a 30-year life expectancy, that would mean over your lifetime, you've received \$3.15 million. Your children get – wait a minute. This was \$1.5 million. How did they just end up with \$750? Good old estate taxes. Not quite half, but it can chop it nearly in half. So worst scenario, your \$1.5 million turns into \$750. The best scenario, they get the \$1.5 million. But potentially, that asset you were planning on leaving them could be cut in half to one and a half million. So the tax becomes \$1.25 million potentially. So if you were to sell this property outright, you could have a lifetime income of \$3.15 million, your children will receive \$750 and you would pay the Government \$1.25 million. Okay? Pretty simple to understand?

What I'd like to show you is the charitable remainder trust strategy. The same asset, real estate – the same value, \$2 million, except this time, we're not going to sell it right away. We're going to get it appraised and we're going to drop it into a charitable remainder trust or gift it to the charitable remainder trust or assign it – whatever word you want to use. We're going to give it

to the charitable remainder trust. At that point, you've now committed to a future gift. The gift is at the end of your life, but you're going to get a tax deduction worth at least \$200,000 for this gift. The tax deduction could be higher. It's dependent upon what the rules say you're going to leave to the IRS.

And we'll stop here for one second. The IRS gives us a couple of things. Not three things – they give us two things. They give us the number saying how much you're going to earn in this. Currently, they say if you set up a trust today, you're going to earn about 5.8%. It doesn't matter what you earn. That's what they say you're going to earn. They also tell us how long you're going to live. It's big power on their part, but they actually tell us how long you're going to live. It's called life expectancy. We tell them how much money we want to take out each year. If, using those three numbers, if it's going to earn 5.8 and you say you want to take 7 and you're going to live another 30 years, will there be 10% of what you put into it left at the end? Do you follow me? If the answer to that is yes, this is a qualified trust. So we can look at it taking out the most you possibly can or if you're very charitable, we can look at it taking out less. If you commit to a lower number for you in the terms of income, you get a higher deduction because you're going to leave more to charity. If you want more during your lifetime, that's fine. You can take up to 50%, but that's if you have 1½ years left to live, but your deduction is lower the higher you go because you're committing less to charity. Okay? So potentially a \$200,000 tax deduction.

At this point, then, we list the property for sell and we sell it. Now, the difference here is instead of having \$1.5 million left after taxes, here you have \$2 million left because you paid no tax. So you're now earning on a higher income. That 7% now pays you \$140,000 per year. What was the number last time? See who was paying attention - \$105,000. \$105,000 – so you just received a \$35,000 a year raise for promising charity a gift of 10% of what you put into it at the end of your life.

Now, this is going to assume that it earns 7 and you take 7. Obviously, your earnings could be 9, they could be 4, they could be wherever you invest it. So this number may not be accurate, but if you were to earn 7 and take 7, at the end of your life, there would be \$4.25 million that was given to you in the form of income. There would be \$2 million given to charity – now remember, that number could be less if you take more or earn less. That doesn't have to be. This is just the scenario. And 0 went to tax. So your income is higher and the IRS got nothing. Does it sound good?

Respondent: Yeah.

Moderator: Do you love your kids?

Respondent: * kids..

Moderator: Bad news. You just disinherited your children. Alright. I'm done. Let's talk about that for a second. We understand that that is a big concern of this plan and that's one of the main reasons that these plans stop. Everybody thinks I can't do this because my kids get disinherited. There's 2 very, very simple ways to take care of that. The first is we continue the trust. The rest of this trust could be your life for a term of years. It could also be multiple lives. So you can have this trust pay you and then continue on through your children's lives. Obviously, some rules that apply to that, it may reduce what you can get during your life, but the numbers could still make sense. Or we could do it for your life and a number of years. So you get it for your life and then another 15 years, which in a lot of cases, is equal to what they would have gotten with the typical sale. All we have to do is match what they would have gotten.

And I always hear a lot of people say, "You know, I'd rather give them an income anyway." If I give my kids \$4 million, it's going to be \$1 million in one time. So a lot of people would choose to give them an income because they know it's less chance that they'll blow that money.

That's the first option. The other one is simple. You just replace what's lost with insurance. We're going to talk about that in a little bit more detail, because it's a little bit more complex, but it is sometimes a more efficient form of planning. And don't think, "Oh, my God. Life insurance – that's horrible." Who cares what the product is? We care what the result is. So I'm going to show you how that works. So children do not have to get disinherited.

Two ways – first, we continue the trust; second, is we can replace that asset with what is called an irrevocable life insurance trust. Is there a question? Oh, you're yawning – a stretch.

Okay, same scenario – we have the \$2 million asset. We put it in the trust again. We do the same thing with the tax deduction. We sell the property again. The difference is this time, we have to put a life insurance policy in place, which means part of the income you would have received goes towards insurance premium. So the \$2 million at 7% gets split between you and your insurance policy. Okay? If you notice, if you sold the property, what was your income - \$105,000? We're still at \$123,00 here – maybe it's lower, maybe it's higher, depending on your age and insurability, but this number does make sense. So what's the end result here? Lifetime income to you for \$3.69 million. Children receive \$2 million – they get the whole asset. Estate and federal and state tax free – so the \$2 million stays \$2 million. It doesn't get reduced by estate taxes. Charity gets the same \$2 million and IRS still gets their nothing. I'm always tempted to say what they deserve, but this is not a "We hate the IRS" meeting at all. It's wonderful, but let's just reposition some of those assets that would normally go there.

How does it look next to each other? If you sell your property right now, you're going to get a lifetime income of \$3.15 million using the numbers we just talked about. If you do the strategy I just showed you, you're going to get a lifetime income of \$3.69 million. Your children would

get \$750,000 in the sale, potentially a million and a half if there's no estate tax, but it's still less than the \$2 million you give them in this scenario. Charity gets nothing with the sale, \$2 million here, tax is \$1.25 million and 0 here. I told you earlier on that if you're willing to plan a gift, you can increase your income, your net worth and your estate size. This is how we do it.

Respondent: Question?

Moderator: Yes.

Respondent: How would you give out the \$123,000 a year? By checks every month?

Moderator: The question is how would we give out the \$123,000 a year or whatever the income is.

Respondent: Yes.

Moderator: I personally come to your house (laughter). I expect that and I require dinner (laughter). It can be set up annually, quarterly – monthly is a little ridiculous because of the accounting, but wherever you invest money normally, you probably have some investments now – whether it's Fidelity, Schwab, an investment advisor – you would just have a distribution from that account each year. It would be calculated at the end of the year. Whatever the trust value is, you get a percentage of that that year distributed according to how you decided at the beginning of the year. Usually, we see semiannual or annual, but you can make it quarterly. You can make it monthly. It's just a little more difficult for accounting.

Respondent: Is it taxable income?

Moderator: Taxable income, but – the question is, “Is it taxable income?” It is taxable, but here's something interesting about it. If you receive income from your rentals, what kind of tax is that? Ordinary income – the highest possible tax.

Respondent: You have expenses. You're having income, but you've got expenses.

Moderator: Of course, over and above what you can't write off. But whatever you receive is ordinary income. In this plan, because of the rules in it, which are called 4 tiered accounting methods, there's some tax efficiencies that we can benefit from. And over time, we can turn the income into the most favorable long-term capital gain or potentially tax free income to you. Okay, not to tell you that you put this in as tax free. There's going to be some tax that comes out, but once we use up some of the original stuff and it grows above the original amount, we can have some better tax efficiencies in it. So, yes, it is taxable, but no different than if you had your rental income or if you sold the property an invested it. Tax, tax, tax – what you get to

avoid here is the capital gain, giving you a larger number to earn on. There are some tax efficiencies we can use inside of this and then you get the deduction as well. We can't forget what that deduction is worth.

Respondent: So what if you're supposed to live 30 years, get in an accident and die next year?

Moderator: Question was "What if you're supposed to live 30 years, you get in an accident and you die next year?" The trust ends at that point if it's a lifetime trust. So the charity gets their money. If you have the life insurance set up, your beneficiaries just get their money then. If you have it set up to go your life plus your children's lives, then it just continues on after you. Whenever you're gone, whatever is supposed to happen at that point, happens. Okay? So if you have it set up to replace money to your children, that just kicks in that much earlier for them. Okay?

Respondent: What would happen if the market goes down?

Moderator: If the market goes down, well after the – do you mean the stock market or real estate market?

Respondent: Real estate market – just like 1990.

Moderator: Relating to what?

Respondent: The assets.

Moderator: The assets – well, if you're invested in real estate inside of this, your value would go down. If you're invested in the stock market, your value would go down. It's not different than keeping it in real estate or selling it and buying investments. It goes up. It goes down. That's why I said, "We're going to use a number of 7%. It's just an assumption. We don't know what you're going to earn, but if you sell the property and invest it, it's going to be invested in the same fashion. So whatever you earn outside of this trust, you'd earn the same thing inside." So I don't know what you'll earn. If the market goes down, that means that you'll have less income the next year. But you would have had the same thing without the trust. In the trust, out of the trust, the market is the market. Okay?

Alright, this is the part that I love the most. This is where everybody says, "This is great, but if I'm out of real estate, I'd actually like to have some cash because I've been sitting on this asset", which is an asset but it's not really something you can take money out and go on a cruise or take money out and buy something. It's an income for you. So if you're in a position where you'd

like to get out and actually get some cash out of it, we have a strategy here called the Cash Out CRT. If you're relating this to an infomercial, this is the part where we say, "And there's more."

Okay, the same family asset - \$2 million. Except this time, we're not going to gift it completely to the trust. We're actually going to take the deed and we're going to split it in two. Pretty simple process if anybody's had a partner or gifted something, you're going to take the deed to that property and you're going to split it in two. Whatever numbers make sense. But in this scenario, I'm keeping 25% of it and I'm giving 75% of it to the trust. Okay? So I have a property worth \$2 million. I've just split the deed. I've given \$1.5 million in value or 75% of it to the trust and I've kept \$500,000 in value or 25% for myself. There's no maximums. This can be any percentage you want - 50/50, 60/40 - it can be whatever it needs to be. For this example, I'm just going to use this simple 25/75 number. Okay, but you can split it any way you want. And when I show you the end of this, you'll understand why I say that.

Okay. So now 25% stays with you and 75% is in the charitable remainder trust. You now sell the property like you did before. But now, \$500,000 stays with you after the sale and \$1.5 million stays in the trust. The \$500,000 becomes cash in your estate again - your family assets. And because you retained that portion of the deed, what has to happen? You pay tax on it. So there is a capital gains tax for that portion. The \$500,00 you kept, you'll pay capital gains tax on. The \$1.5 million, however, you pay no capital gains tax and if you remember correctly, we also get a tax deduction for that. Right?

So we have \$1.5 million earning 7%. Does that number sound familiar? That's the same number as if you sold the property outright, paid the tax and kept what's left. That produces \$105,000 a year in income for you. So, so far, it's just the same as if you just sold the property. But you have \$500,000 in your pocket. Unfortunately, there's a capital gains tax.

But what do we have here from the gift to the charitable remainder trust? We have a tax deduction. The tax deduction can offset that tax, putting the \$500,000 tax free in your pocket to remain in your estate.

Respondent: The tax deduction would be the exemption?

Moderator: The tax deduction on the gift can offset the tax owed on the sale portion that you keep in your hands.

Respondent: What's the tax deduction?

Moderator: The tax deduction is giving the money to the charitable remainder trust. It depends on how your trust is set up. So the reason I say it can be different numbers, depending on your tax situation, your age, how much you want in income, there is a number that we can

say, “This is exactly how much you can split and receive it tax free.” It may only be \$100,000. It might be \$700,000. It depends on your personal situation. But the moral of the story is you can get some cash out of this thing and pay no tax on it.

Respondent: What formula would I use to determine how much I could get?

Moderator: What do we use to determine that?

Respondent: Yes.

Moderator: Well, we’d have to look at your age – the question is how do we determine that. It’s computer programs that do that. We say how old you are, what your tax situation is, how much of this deduction you can use. So the simple story is we can sell the property, we can take some tax out cash free – tax out, cash free – I kind of said that backward. In this scenario, you get to put the cash in your pocket that’s equal to what you would have paid in tax. Again, it may not be the exact number but conceptually sound. We use it all of the time. And it’s a great way to get out of your real estate, keep your income the same as if you would have just sold it and paid the tax, travel around the world, buy a Harley Davidson or – how about this, take cash out, put it on the side, wait for the market to do whatever you think it might do if you think it’s declining a little bit, or just wait to find the perfect property and then use that half million in this scenario to get back into real estate.

Respondent: When I said exemption, I was thinking of joint. Then you have \$500,000.

Moderator: Yeah, this has nothing to do with that. That’s only if it’s primary residence. We’re talking about investment real estate. Exemption doesn’t apply to investment real estate. Right. So this gives you the opportunity – one of the problems with the 1031 is you’re buying in a like market. You’re going to sell high and buy high. This could give you the opportunity to sell high and – I’m not saying the market is going down, but if you believe it is, sit on the sidelines with \$500,000 cash and get back in later without all of the 1031 Exchange rules.

Respondent: Why can’t you do that on residential property?

Moderator: You can do it on residential property. The question was why can’t you do it on residential property. You can if it exceeds those exemption amounts. So if you have a property worth \$6 million and it’s \$5 million in gain and that’s your primary residence, well, then you can only exempt \$500,000. Everything else would be taxable so you could use it.

Respondent: That’s what I was thinking.

Moderator: Yes. Primary residence, if you have gain above the exemption amount, you can use this. Yes?

Respondent: What determines the amount of the cash that's not deductible – that's free.

Moderator: What determines the amount of the cash that can be free to you? That's determined by your personal tax situation. There's a certain amount based on your income that you're allowed to deduct, but this – this capital gain will increase that amount. So we just have to take a look at what your tax situation would be assuming you took the \$5000 capital gain and how much of that deduction you can use, based on the income you're going to get out of this, and see if they completely wipe it out. I may come back to you after analyzing this and say, "If you want \$500,000, you're still going to have to pay \$364 in tax, based on my calculations". There is a magic number that works out perfectly. The question is, "How much would you like? Would you like to just what's free, a little bit less, a little bit more, and we can do those calculations for you." So it's different for everybody, but the calculations are based on the income out of the trust and your personal tax situation.

Respondent: * the money if you reinvest something * gain or *?

Moderator: So did you ask the money that you get out tax free?

Respondent: Yeah.

Moderator: After you invest it again?

Respondent: Uh huh.

Moderator: It would be the same as any other money you currently have invested. It's just – then it becomes cash and you can do with it whatever you want. If you invest in income producing bonds, you have higher tax. If you're doing tax-free bonds, you have no tax. If you do it typical investments, you put it into an annuity, you have tax deferral. You can put it back in real estate and you all know that one. Okay, so again, get a little bit of cash out, sell your real estate, pay no tax, have a nice income, get some cash out, the numbers are whatever they need to be for you personally. One more question.

Respondent: Is there a minimum amount of what you can do with CRT's? Can you have multiple ones or is it just one?

Moderator: Okay, the question is are there minimum amounts that you can put into a CRT and can you have multiple CRT's?

Respondent: One more question.

Moderator: I should write these down.

Respondent: Who sets them up and how costly are you?

Moderator: I was actually going to answer that one as part of the first one. Minimum amounts you can put in – technically, there are no minimums, but it has to make sense for the legal fees. Legal fees on these, depending on which area code or zip code you go in, can be anywhere from \$1700 to up to maybe \$6000. Typical, pretty basic CRT, we can get you for right around \$2200, maybe \$2500.

Respondent: Per year.

Moderator: One time – not per year. Now, there is an additional tax return. The tax return, depending on your accountant, they have a CRT trust return.

Respondent: It would be probably \$400 or \$500.

Moderator: How much?

Respondent: \$400 to \$500.

Moderator: \$400 to \$500 a year. So that's an average – so that's an annual basis. So what's the minimum? As little as you can do and make it make sense. The smallest one I've done personally was \$228,000. The second part of the question was can you have multiple trusts. The answer to that is yes. But the question is why. There are some reasons, but you can have one trust set up. You can sell the property this year. You can put another one in next year, put another one in the following year. You can have some appreciated stock and put that in. You can have a piece of art and put that in. Everything can go into the same trust unless you decide in the future, you'd like to have some different terms. Maybe you do one now and you only want 6% out, but you do one 2 years from now and you happen to have a great year in your business, had a high income and you need a bigger deduction. So you know you do a trust that gives you a larger deduction. So, yes, you can have more, but you don't need more. You can add to the same one. Yes?

Respondent: Just one question. I was a little puzzled on this insurance policy that you had mentioned in regard to children being the beneficiaries as a solution. What is that insurance?

Moderator: The question was regarding the insurance that makes the children the beneficiaries. In the charitable remainder trust, at the end of your life, if it's set up for lifetime,

whatever's in that trust goes to the charity. Okay? So what that means is that your children will get nothing. So if we care about our children, we need to make sure that we replace that asset. If you don't care, no big deal. If you just want to give this to charity, that's okay. But if you decide that you don't want all of that money going to charity and you want to replace it to your children, then you can purchase a life insurance policy that is specifically designed to replace the asset that goes to charity. So simply put, if you have a dollar you're intending to give your children, but for you personally, it makes sense to give it to charity, but you still want to replace it to your children, here's a way that you can do that. As long as the numbers make sense and you can still come out ahead, then we go that route. The other option is you discontinue the trust for your children's life. So it's a life insurance policy structured to replace the asset that charity received by using this plan.

Respondent: The ILIT doesn't add to your estate.

Moderator: The irrevocable life insurance trust is where we put it. It keeps it out of the estate so we don't have to pay estate taxes. Okay?

Some other solutions for this, you can sell or transfer a business. So if anybody here owns a business, the founder of my company did a – I think it was a \$46 million business sale. I think \$45 million of it was gain and not only did they pay no tax, they actually got a little over a million dollar tax credit using a combination of these strategies. If you have children or grandchildren, you can use this stuff for education trusting. You can get money out of a family business. You can do some IRA stuff. Also, if you're in a situation where you've maxed funded – if you're younger and you've maxed funded all of your potential retirement plans – your 401K's, your IRA's – what a great way that you can actually fund a retirement plan for yourself using what we call a NIMCRT, net income make-up charitable remainder trust, which defers the payments to you. We won't go into that, but it's a great opportunity for some retirement planning and also, any other appreciated asset – stock options, individual stocks, business, art – whatever it might be.

To get started, really the first thing is the most important. You need to customize your plan. I just threw a bunch of numbers up here that I guarantee make sense for nobody in this room. But for illustration purposes, they're pretty powerful, I think. But what we need to do is we need to look at your personal situation. You need to talk to your loved ones. Let them know it's going to look like I'm disinherit you, but here's how you get yours back to make sure they're on board with this. And then you need to meet with your professional advisers.

This does not have to be done through me. It doesn't have to be done through anybody in this room. What I will tell you is we do kind of specialize in this. So meet with your advisers. If they tell you, "No, that CRT thing is wrong. It's illegal. It's not good." Please leave them. Come talk to us. We have too many CPA's and attorneys out there who actually say these things

aren't legal, which is wrong. One client we were meeting with last year, we were going to save him about – big tax situation – probably about \$4.5 million in taxes – year end real quick tax strategy. His CPA said, “No, no, no. That's not legal.” What ends up happening is his CPA just never heard of it. It costs this guy \$4 million in taxes and now he's going through the process of letting his accountant know that he's realizing that it actually was a true strategy. So, far too often, your personal advisers may not be aware of these things, because I have a room full of people here that own real estate and a lot of you have probably thought about exiting it and how many of you really knew how a CRT worked or ever had anybody advise you to do it? Everybody here in this room should have heard of it as an exit strategy at some point. We teach classes for CPA's and attorneys. 95% of them in the room usually say, “Well, I've heard of it, but I never recommend them because they're kind of confusing.” Just know, this is very real. We can help you. We can help your CPA or attorney or your other advisers.

We have some worksheets we'll put together. A lot of the questions were what if this, what if that, how do I do this, how do we calculate this – we put it all down on paper.

Respondent: What is the right time – before sale or after sale?

Moderator: The question is what is the right time – before or after sale? To do the charitable remainder trust strategy, you have to give it to the trust before you list the property. It can be listed and then put into the trust. It can't be sold and put into the trust. This a presale process. There's an appraisal of the property. There's a gift to the trust. Then it gets listed.

Respondent: It has to be sold eventually.

Moderator: It doesn't have to be sold. You can leave it in the trust. Take the tax deduction and keep the property if you want to. You don't have to sell it immediately.

Respondent: So it's before sale.

Moderator: Before the sale, it has to go into the trust, yes. Otherwise, it doesn't qualify.

Respondent: But you don't have to actually sell it.

Moderator: You don't have to sell it. Now, usually people do these because they want to do the tax free sale. Now, if you have a big need for a tax deduction, maybe you can – so yes, you can still keep it. So we'll figure out all of the numbers for you.

Respondent: You can rent it, too.

Moderator: You can rent it.

Respondent: You can sell the property.

Moderator: Yeah, you can do whatever you want to do with that in terms of selling properties, keep it rented. We'll put together the plan that makes sense for you. Now, just so you know, this is one of many solutions. We're going to give you a DVD at the end of this if you fill out our little survey, which is this one here. There are a number of other DVD's and other programs and other educational pieces that we have. What I just told you about is really, I think, interesting and there's some great uses for it. There are a lot of other strategies like this that you can use for just a simple tax deduction. Anybody here that gives money to charity and you're planning on doing it for the next 15 years, how would you like to take all of those deductions today? There's a strategy for that. How would you like to completely avoid estate tax, regardless of the size of the estate? We could talk about that for 5 or 10 minutes if you guys would like to. If not, we'll skip over it, but I'll take a survey. And a lot of other strategies here you can use using these some type of solutions.

We have something called a living balance sheet that we can help you out with which will put all of your assets in one place, whether they're with the same company or not. Your bank accounts, your Schwab account, your Fidelity account, your Morgan Stanley account – you can view them all in one place. We can put your real estate values in there. You can truly see your net worth and determine whether or not this stuff makes sense for you. We can vault all of your deeds. We can vault all of your living trusts. We can vault anything you want including your passport that you can view any time, anywhere you have access to a computer in any country. So we can put you on the living balance sheet as well and help you get your stuff in line there.

This is the DVD I was just telling you about that you can take a look at. You notice here it says, "March of Dimes". Philanthropy International works with the March of Dimes on a national basis. We do this around the country for them. Brian and I, who you're going to meet in a second – Brian just got back from Florida doing a presentation to 140 or so commercial real estate investors. This has been endorsed and supported and obviously budgeted and marketed by the March of Dimes.

Now, what does that mean to you? March of Dimes is a pretty big name and they're pretty involved in charitable planning and charitable giving and they did a pretty big audit on what we're talking about and the way we do business. That's not to say that this is the perfect plan, but if March of Dimes put their stamp of approval on it, you can feel pretty comfortable that we're doing things pretty safely because they're not going to allow us to ruin their name. We really do stay right down the middle of main street and make sure that we don't do any of those abuses and create exits through plans that you saw on the private annuity trust.

You're here today at North Ridge Hospital because we're doing this presentation for them today. You have an option at the end of your trust planning. Okay? If at some point you decide this makes sense for you, you're going to draw up a trust. And at the end, they're going to say, "Who do you want to leave it to?" You can choose any charity you like. It doesn't have to be anything specific. You can also change that charity. So if you don't like a charity 10 years from now, you can take them off if you do a revocable beneficiary. If you make it irrevocable, you have to stick to that and the charity truly does appreciate the irrevocable trust because they can count that as a current gift. But just know, you can choose the charity you want. What we ask is because you're here tonight and North Ridge Hospital Foundation invited you, got you a dinner – a good dinner, right? Pretty good. It's the typical chicken. I know the rubber chicken dinner thing. But they bought you dinner. You spent some time here. They gave you an education. If you guys look at this and you say, "You know what? That kind of makes sense for me" and we do some planning for you and there is a gift needed, what I would just simply ask is that you remember North Ridge Hospital for part of that gift because they were the ones that got you here and we're going to hear a little bit more about them in the future. On a national level, we'd love for you to remember March of Dimes, because March of Dimes ... Is there a question? Everybody's pointing.

Respondent: Can you have more than one charity?

Moderator: The question is can you have more than one charity? Yes. You can have multiple charities as well.

Respondent: In the same CRT?

Moderator: Yes. One CRT, multiple charities – and in fact, we usually set them up with a contingent charity because let's say, you're with your local school – the school you went to and your kids went to and that school could go out of business. So we always like to do a contingent – usually a national charity, just in case the local one goes away so there's a contingency plan in place as well.

Philanthropy International is the national community foundation. We have people like me, charitable planning specialists, all across the country doing this right now. This is a real thing. We are supported by a lot of top attorneys in the country. Gerard Bostwick was rated in the top 100 attorneys in estate planning in the entire country by Worth magazine. He's on our team. We have a lot of people that really know what they're doing. We now have a national relationship with a company called CB Richard Ellis doing some stuff on commercial real estate nationally. So we have some support. And the only reason I tell you that is just please understand that we're experienced in this and we can really help you go the right direction.

We're going to give you an evaluation in a second. Please fill out for us. It will help us improve these in the future and kind of give us an idea of who's here. You're going to put your phone number on there. There's a spot for you on there. It's a white spot all over the place. If you don't want anyone to call you, just write "no" and circle it and we promise we won't call you, but just know the call will be simply, "Thanks for coming. Is there anything else we can help you with?" We like to talk to people and see if we can assist them in their planning, but if you don't want to be bothered, just simply write "no" and circle it.

I'm going to say thank you now and then I'm going to ask before we pass out the surveys, would anybody like to quickly hear how you can completely avoid estate taxes? One no.

Respondent: What time is it and I'll tell you *.

[End of recording]