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Charitable Trust: Examination Of A (Sometimes) Counterintuitive Term

Charitable planning is an essential part of any estate planner’s toolbox. Clients are drawn to charitable planning by different motivations—for many there is an altruistic desire to give back, while others are drawn to the prospect of lowering or even eliminating income or estate taxes. While charitable planning often takes the form of making an outright gift to an existing charitable organization, many gifts are made through trust planning—the creation of a trust specifically to fulfill charitable intentions, a charitable devise to create an ongoing trust after someone’s death to benefit a charitable organization or mission, or even naming a charitable organization to receive the assets of a trust in the case of a failure of beneficiaries. All of these planning situations can be captured in the term “charitable trust.”

Statutory Guidance

But what is a charitable trust? It is a seemingly simple question with a far less simple answer. Philosophically, the term indicates a charitable purpose to some degree. When we look at the statute, we find helpful guidance. Understanding charitable trusts is important for all planners; understanding how to help clients effectuate their charitable intentions—and knowing the implications of the structures that are created to do so—allows planners to help clients make the best decisions.

The Revised Code gives us two definitions of “charitable trust” depending on whether one is reviewing the provisions of the Revised Code regarding the powers of the Attorney General or the Ohio Trust Code. [R.C. 109.23](#) provides that a charitable trust is “any fiduciary relationship with respect to property arising under the law of this state or of another jurisdiction as a result of a manifestation of intention to create it, and subjecting the person by whom the property is held to fiduciary duties to deal with the property within this state for any charitable, religious, or educational purpose.” The statute further provides that the definition “includes the fiduciary relationship, the entity serving as trustee, the status as trustee, the corpus of such trust, or a combination of any or all of such meanings, regardless of the primary meaning of any use of the term, that is necessary in any circumstances to effect the purposes of [[R.C. sections 109.23 through 109.33](#)].” These provisions implicate the Ohio Attorney General in circumstances that are not always intuitive.

Under the Trust Code,¹ a charitable trust is “a trust, or portion of a trust, created for a charitable purpose described in [division \(A\) of section 5804.05 of the Revised Code](#).”² The purposes under [R.C. 5804.05](#) include “the relief of poverty, the advancement of education or religion, the promotion of health, governmental or municipal purposes, or other purposes the achievement of which is beneficial to the community.”³ In other words, the definition of charitable trust, by providing that any trust with a charitable beneficiary of any kind, no matter how remote, no matter how contingent, is expansive, and captures far more trusts than many practitioners anticipate.

Types of Charitable Trusts

While [R.C. 109.23](#) to [R.C. 109.33](#) and the Trust Code do not always draw distinctions between the types of charitable trusts, there are subtypes, and understanding the subtypes can help understand when a trust that otherwise meets the definition of charitable trust might be exempted from requirements under [R.C. 109.23](#) to [R.C. 109.33](#) or the Trust Code.

It is helpful to think of charitable trusts on a spectrum: at one end are wholly charitable trusts, while at the other are “charitable trusts” that are charitable only in the sense that there is either (a) a charitable devise after the settlor’s death or (b) a remote, contingent remainder beneficiary that happens to be a charity. As with much of the law concerning estate planning more generally, charitable trusts are the intersection of different bodies of law (we have already seen the Trust Code and the Attorney General’s regulatory powers); notably it is an area of law where state law intersects with federal tax law. While these bodies of law do not always speak to each other well, the Ohio legislature made an effort to make state law accommodating to avoid foot faults that would jeopardize tax planning undertaken in effectuating a settlor’s charitable intentions.

Starting at one end of the spectrum with the most intuitive and colloquial type of charitable trust, a wholly charitable trust is one where the entire beneficial interest is vested in one or more charitable organizations exempt from taxation under I.R.C. § 501(c)(3) of the Internal Revenue Code of 1986, as amended (the “I.R.C.”), or held in furtherance of supporting one or more such organizations. It is important to note that while “charitable trust” often is equated with “tax-exempt charitable organization,” this is not always the case. There are wholly charitable trusts that are not tax-exempt,⁴ though as a general rule, wholly charitable trusts are eligible to petition the Internal Revenue Service for recognition under I.R.C. § 501(c)(3).⁵ From an income tax standpoint, charitable trusts exempt under I.R.C. § 501(c)(3) are not subject to income tax, and nonexempt charitable trusts are entitled to a income tax charitable deduction for all amounts paid out to qualified charitable organizations.⁶

In the middle of the spectrum are split-interest trusts—charitable remainder trusts (CRTs) and charitable lead trusts (CLTs)—so termed because the lead interest is vested in one party, while the remainder interest is vested in another.⁷ Here the names of the trusts are helpfully descriptive and are in reference to the charitable organization’s interest in the trust. A charitable organization⁸ holds the remainder interest in a CRT, while the charitable organization holds the lead interest in a CLT. Both CRTs and CLTs can provide income and estate tax planning advantages, but in general the popularity of CRTs and CLTs often corresponds with then-prevailing interest rates. CRTs⁹ are more popular when interest rates are higher, while CLTs are favored with lowered interest rates. CRTs are afforded more favorable income tax treatment during the term of the trust as they are considered tax-exempt under I.R.C. § 664(c), while the income tax treatment of CLTs depends on whether the trust is structured as a grantor or non-grantor trust (which in turn often depends on whether the CLT is created during life to maximize income tax planning or at death to maximize estate tax planning).

Finally, at the other end of the spectrum are the trusts that are “charitable” because the statutes define them to be, but not trusts that would generally be thought of as charitable. Common situations that lead to classification of trusts as “charitable trusts” include incorporating a charity into a failure clause (often a family foundation or donor advised fund, but not uncommonly a charity important to the settlor of the trust), including one or more charitable gifts after death, or even providing that some portion of a trust be distributed to unnamed charitable organizations in the discretion of the trustee. The intentions of a settlor should be paramount in a drafting attorney’s mind, but the attorney should also understand that naming a charitable organization in a failure clause may have consequences that are unintended (and certainly differ from the default of heirs-at-law). The income tax treatment of these trusts depends on whether the trust is a grantor or non-grantor trust, but in general the trust would be subject to income tax, but eligible to take a charitable deduction for any amount paid to a charitable organization.

Role of Ohio Attorney General

Understanding the implication of being classified as a “charitable trust” (regardless of the extent of the charitable interest involved) is important. Perhaps the most important implication is that the Ohio Attorney General has broad investigative and enforcement powers with respect to charitable trusts.¹⁰ In general, the Ohio Attorney General may investigate transactions and relationships of a charitable trust to determine whether the property held for charitable, religious, or educational purposes has been properly administered in accordance with fiduciary principles under Ohio law.¹¹ The statute does not differentiate between types of charitable trusts—the Ohio Attorney General has broad investigative powers for *any* charitable trust, including those that name a charitable organization in a failure clause but otherwise have no charitable interest.¹²

Pursuant to its powers under the statute, the Ohio Attorney General is a required party in any judicial proceeding that might arise with respect to the trust, even if the court proceeding does not have any impact on the charitable provisions of the trust.¹³ The required involvement of the Ohio Attorney General can also extend to private settlement agreements under the Trust Code when the private settlement agreement construes or modifies any term of a trust that relates to estate or generation-skipping

transfer tax or any division of property related to the imposition of any transfer tax.¹⁴ This can be a trap for the unwary because the statute applies even if the trust is a charitable trust only by virtue of an “off the top” devise of a small monetary amount or even its failure clause when statistically is borderline impossible for the failure clause to be invoked.

Practitioners should also be aware that the Ohio Attorney General is a necessary party in many trust termination actions involving charitable trusts. Although the Trust Code allows termination of trusts having a total value of less than \$100,000 after the trustee has concluded that the value of the trust property is insufficient to justify the cost of administration, the Trust Code also provides that termination is not permitted under this section for certain charitable trusts.¹⁵ Helpfully, the Trust Code limits the definition of charitable trust to those with “qualified beneficiaries,”¹⁶ so the definition is less expansive and a failure clause naming a charitable organization will not complicate terminating a trust that is not otherwise charitable under the Trust Code if it otherwise meets the criteria of [R.C. 5804.14](#) (in terms of the spectrum above, the counterintuitive charitable trusts are largely exempted). For most charitable trusts (wholly charitable trusts and split interest trusts), though, termination would be effectuated under either [R.C. 5804.12](#) (change in circumstances) or [R.C. 5804.13](#) (charitable purpose frustrated). In both instances, the Ohio Attorney General would be a required party to the judicial proceedings under [R.C. 109.25](#).

Charitable trusts are also required to register and annually report with the Ohio Attorney General’s office.¹⁷ Various types of charitable trusts are (helpfully) exempted from this obligation—CRTs, any trust in which a charitable interest is contingent and the conditions for vesting have not yet occurred, and estates with charitable bequests.¹⁸ For charitable trusts with contingent charitable beneficiaries, registration is required with the Ohio Attorney General within six months of the charitable interests becoming vested.¹⁹ While estates are not required to register as charitable trusts to become part of the Ohio Attorney General’s register, if an estate includes a bequest of more than \$1,000, notice must be given to the Ohio Attorney General’s office.²⁰ Failure to comply with the registration and annual reporting requirements can cause the imposition of penalties.

Conclusion

It is a generally good practice to review the Trust Code and [R.C. 109.23](#) before taking any action with respect to a trust when a charitable organization is named in a trust agreement in any capacity. Understanding what constitutes a charitable trust under the Trust Code and for purposes of the Ohio Attorney General’s regulatory powers is valuable for any estate planning practitioner. Doing so can help avoid inadvertent noncompliance with applicable statutes, as well as unintended hiccups in administering, modifying, or terminating a charitable trust, especially one that seems on its face to not be charitable but that is nevertheless captured into the statutory definitions.

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Footnotes

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- 1 The Trust Code was enacted effective January 1, 2007.
- 2 [R.C. 5801.01\(E\)](#).
- 3 [R.C. 5804.05\(A\)](#).
- 4 [I.R.C. § 4947\(a\)\(1\)](#).
- 5 Administration of wholly charitable trusts that are subject to the private foundation rules under the Code are addressed in [R.C. 109.231](#). This statute is particularly helpful for trusts (often created under

wills) that predate the enactment of the private foundation rules in 1969 or otherwise were drafted without contemplating the importance of the various obligations and prohibitions applicable to charitable organizations subject to the private foundation rules.

6 Charitable trusts that are classified as private foundations under [I.R.C. § 509\(a\)](#) are subject to a net income investment tax (currently levied at 1.39%). Nonexempt charitable trusts often will not be subject to income tax because the charitable deduction will obviate the income tax liability. However, this is not always the case, especially in years where the trust recognizes capital gain income.

7 A lead interest can be structured as either an annuity interest or unitrust interest. Practically, it is most common to see CRUTs and CLATs, though CRATs and CLUTs are possible.

8 All references are to organizations exempt from taxation under [I.R.C. § 501\(c\)\(3\)](#).

9 Like [R.C. § 109.231](#), the statute also provides a savings clause to ensure that trusts intended to be CRTs will qualify under [I.R.C. § 664\(D\)](#)—see [R.C. 109.232](#).

10 [R.C. 109.24](#).

11 See [R.C. 109.23](#) to [R.C. 109.33](#).

12 As a practical matter, it is difficult to see how the Ohio Attorney General would become involved with a charitable trust that did not have a registration obligation under [R.C. § 109.30](#) or was not the subject of a judicial proceeding where the Ohio Attorney General was a required party; however, the statute does allow the Ohio Attorney General to intervene sua sponte.

13 [R.C. 109.25](#). For a discussion of charitable trust modification more generally, see Spievack, [Charitable Trusts: A Practical Approach To Avoiding Cy Pres Or Deviation Actions](#), 30 No. 3 Ohio Prob. L.J. NL 8 (January/February 2020); Burke et al., [The Use of Liberal Construction, Deviation, and Cy Pres to Adapt Charitable Trusts to Changing Circumstances](#), 18 Ohio Prob. L.J. 202 (July/August 2008).

14 [R.C. 5801.10\(B\)\(2\)](#). Note that even if the private settlement agreement does not require the Ohio Attorney General as a party, a named charitable organization would still be a required party under [R.C. 5801.10\(B\)\(1\)\(b\)](#). If there is no named charitable organization but the assets are to be distributed for charitable purposes (e.g., a failure provision that the trustee should distribute the assets to charitable causes supported by the settlor), it is unclear whether the Ohio Attorney General should be included, but arguably the better approach is to do so.

15 [R.C. 5804.14\(A\)\(2\)](#).

16 See [R.C. 5801.01\(Q\)](#). In general, to be qualified, a beneficiary must have a current interest, or must have an interest that would become current if the current beneficial interest holders' interests were terminated.

17 This requirement extends to nonprofit corporations that are charitable as well as “trust” is not used in a literal sense in the [R.C. 109.23](#) definition.

18 [R.C. 109.26](#). The reporting obligations under [R.C. 109.31](#) further exempt certain types of charitable organizations (e.g., those organized solely for religious purposes, certain educational institutions, and those which receive less than \$25,000 per year in revenue).

19 [R.C. 109.26](#). See also [Ohio Admin. Code § 109:1-1-02\(B\)](#).

20 [R.C. 109.30](#). The notice to the Ohio Attorney General should be given in accordance with the requirements of [R.C. 2107.09\(A\)\(1\)](#).