

### ARE YOUR CLIENTS

### LOOKING FOR SMART

### WAYS TO GIFT

### THEIR HEIRS?

If you have clients interested in transferring assets to their children at a reduced tax cost, a grantor-retained annuity trust (GRAT) may be able to help your clients maximize the wealth they leave to their loved ones, especially in a low-interest-rate environment. Based primarily on interest rate assumptions, clients can create GRATs to pass the appreciation in assets to the next generation with little or no gift and estate tax.

For many investors, all assets in their name—stocks, bonds, business interests, real estate, and valuable objects—are considered wholly taxable parts of their estate. However, by establishing a GRAT, an individual or family can develop a powerful wealth-transfer strategy that shifts these assets and will present heirs with much more favorable tax consequences.

Among its benefits, a GRAT minimizes or eliminates the gift tax the IRS levies on money you give your heirs. Currently, the IRS will let individuals gift up to \$13,000 a year per recipient without any tax consequences. And if the total amount an individual gifts to heirs over a lifetime is less than \$1 million, the IRS will assess no tax, but will reduce that individual's unified credit for estate tax purposes. However, anything given above these amounts is subject to gift tax, payable upon filing a gift tax return.

### The ABCs of GRATs

A GRAT is an irrevocable trust into which your clients can transfer appreciating assets. Once established, a GRAT provides your clients (the grantors) with an income—in the form of annuity payments—throughout the trust's lifetime, usually a specified number of years. At the end of the trust term (so long as they are still living), the trust beneficiaries receive whatever is left. Upon creation of the GRAT, the IRS allows your client a gift tax deduction for the actuarial value of the income interest they retain. The value of that interest depends on their life expectancy and the value at which money is expected to grow (determined by using the interest rate specified in IRC Section 7520, which changes monthly). This estate planning technique actually “freezes” the current value of the assets transferred into the trust; if the assets appreciate at a rate greater than the stated IRS rate, your clients' beneficiaries will receive the appreciation amount free of gift or estate tax obligations.

### The Time is Now—But Why?

The current low-interest-rate environment is favorable to GRATs because it serves to decrease the retained value of your clients' annuity interest while increasing the value of the remainder interest that will pass to their heirs. The IRS Section 7520 interest rate for October 2008 was 3.8 percent. This rate is called the “hurdle” rate because the goal is for your clients' assets' appreciation to “jump over” or exceed it.

Your clients can structure the annual payout to match the IRS-projected value of the assets in hopes their trust will appreciate more than the IRS projection, leaving the remainder tax-free to their heirs. By creating this kind of “zeroed-out” GRAT, in which the value of the annuity equals the value of the property put into the trust, your clients can avoid using their federal gift tax exclusion or paying gift tax.

### Getting The Most Out of a GRAT

The optimal GRAT includes a single stock with short annuity terms (typically two to three years). If your client has multiple stocks, it's better to isolate them in separate GRATs so that the stocks with less appreciation don't pull down the overall performance. However, if your client sets up a longer-term GRAT, a single volatile stock could work against him or her. This makes a more diversified portfolio preferable.

Funding GRATs with your clients' personal assets works well because it helps ease gift and estate taxes with little downside.

Likewise, business owners planning to sell can benefit by funding GRATs with their company stock. On the date of the gift, the IRS determines a value of the stock and computes the gift tax, “freezing” the market value of the company. If the business sells within the term of the GRAT at a higher value, the business owner's heirs receive the proceeds.

### Some Points to Consider

You and your clients should discuss their options in detail to determine if a GRAT serves their wealth transfer needs. Before creating a GRAT, consider your clients' age and health. Their assets will be returned and taxed back to their estate if they pass away before the end of the GRAT's term—as though the GRAT never existed. That risk can be mitigated by purchasing life insurance to cover the amount of any anticipated federal estate tax that would be levied if they did not survive the term of the GRAT. Another reality of GRATs is that your client, as the grantor, is responsible for paying all income and capital gains taxes on the trust during its term. Also, assets placed in a GRAT become the property of the trust; regardless of the amount of appreciation, they will receive only the predetermined annuity payments.

Although not the simplest of trusts to fully understand, a GRAT may be helpful in your clients' estate planning, especially in the current low-interest-rate environment. GRATs require careful analysis of your clients' own personal circumstances. But with the assistance of an estate planning attorney, you can make this sometimes complex tool the foundation of your clients' wealth management program

Adapted from an article originally authored by Lynn A. Brickman, CTFA, Vice President and Senior Fiduciary Advisor, Wilmington Trust, FSB, Pennsylvania; and, Jeanette Madaya, CFP, CTFA, Vice President and Senior Fiduciary Advisor, Wilmington Trust FSB, Pennsylvania, for WEALTHtoday—Fall 2008.

© Wilmington Trust Corporation.

## ADVISORY TRUST

The Advisory Trust Company of Delaware

2710 Centerville Road, Suite 101  
Wilmington, Delaware 19808  
800.258.6334

2800 North Central Avenue, Suite 900  
Phoenix, Arizona 85004

[www.advisorytrustco.com](http://www.advisorytrustco.com)

© 2009 Wilmington Trust Corporation.

# ADVISORY TRUST

The Advisory Trust Company of Delaware

2710 Centerville Road, Suite 101  
Wilmington, Delaware 19808  
800.258.6334

2800 North Central Avenue, Suite 900  
Phoenix, Arizona 85004

[www.advisorytrustco.com](http://www.advisorytrustco.com)

© 2009 Wilmington Trust Corporation.

## Conclusion

The Advisory Trust Company of Delaware (Advisory Trust) provides directed trustee, trust administration, and back-office services for high-net-worth individuals and families. We work exclusively with professional advisors, assisting them in helping their clients achieve their financial goals by using the full range of trust strategies available under Delaware law.

Advisory Trust is comfortable working with you and your clients to administer a GRAT in a way that is most advantageous to your clients. Sometimes, only investment decisions are controlled by an external financial advisor, in which case Advisory Trust serves solely as administrative trustee. In addition, with Advisory Trust, your clients may be able to use Delaware's many favorable trust laws and maximize The Delaware Advantage.

In the end, a GRAT with Advisory Trust may be able to provide you and your clients with the flexibility and freedom needed to overcome many hurdles in their estate planning process.

## About Advisory Trust

Advisory Trust is part of the Wilmington Trust corporate family, which has been in the wealth management business for 105 years, serving as trustee and advisor for prominent individuals, families, and foundations. Founded in Wilmington, Delaware, in 1903 by T. Coleman du Pont, one of the great industrialists and entrepreneurs in our nation's history, the Wilmington Trust corporate family currently serves wealth advisory clients in all 50 states and 36 countries.

Advisory Trust has offices in Wilmington, Delaware, and Phoenix, Arizona, and currently oversees approximately \$1.3 billion in assets for more than 1,200 personal trust accounts, providing tax and administration services.

Call us toll-free at **800.258.6334, ext. 8531** or email us today at **[inquiries@advisorytrustco.com](mailto:inquiries@advisorytrustco.com)** to learn more about how we can help you and your clients take advantage of Delaware directed trusts and our other trust services.

Advisory Trust works exclusively with advisors and we take the relationship between advisors and their clients seriously. Our mission is to assist you in achieving your goals and your clients' financial goals by utilizing trust strategies and the full benefits of Delaware law.

We can help you with all types of personal trusts including GRATs. For more information and assistance in setting up trusts for your clients, email us today at **[inquiries@advisorytrustco.com](mailto:inquiries@advisorytrustco.com)** or call toll-free **800.258.6334, ext. 8531**.

THE FOREGOING IS PROVIDED FOR INFORMATIONAL PURPOSES ONLY. It is not designed or intended to provide financial, tax, legal, accounting, or other professional advice since such advice always requires consideration of individual circumstances. If professional advice is needed, the services of a professional advisor should be sought.