Estate Tax Strategies **Franklin Karibjanian & Law PLLC**

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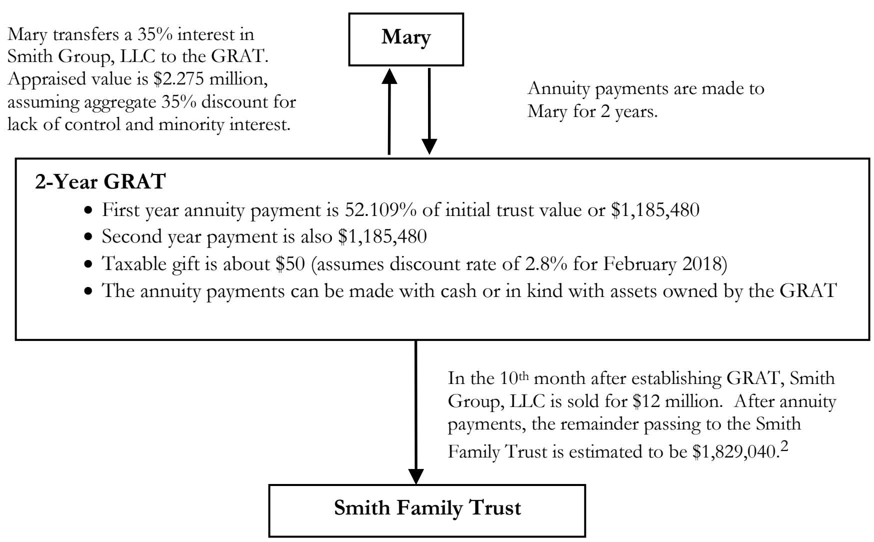
Grantor Retained Annuity Trust (GRAT)

A GRAT is used to transfer future appreciation of an asset to family members free of gift and estate taxes. In general, the grantor transfers property to an irrevocable trust and receives back an annuity (often once a year for two years). The annuity is typically equals 100% the value of the transferred property on the date of transfer, plus interest at the applicable IRS rate. Because the value of the property retained by the grantor is equal to the value of the property initially transferred to the trust plus interest, the value of the "remainder" interest which passes to the family members at the end of the trust term is actuarially calculated at near zero. Therefore, the gift tax value of the asset transferred to the GRAT is "frozen" at the value of the annuity retained by the grantor, and the actual gift for gift tax purposes upon establishing the GRAT will be nominal, often $100 or less.

Future appreciation in the value of the asset transferred to the GRAT that exceeds the applicable IRS rate (i.e., currently 2.8% in February 2018) will be transferred to the remainder beneficiaries (the grantor's family members, or trust for the family members) of the GRAT without gift or estate tax. (This is assuming the grantor survives the retained term of years). If the asset does not appreciate greater than the applicable IRS rate (e.g., 2.8%), the entire asset is returned to the grantor, but he or she has only used a nominal amount of his or her gift tax exclusion or paid a nominal gift tax for enjoying the opportunity to pass appreciation to the family members.

A GRAT is commonly created with publicly traded stock or interests in family or private companies that the grantor anticipates will appreciate. The following is an illustration of how a GRAT works:

Example: Mary owns 85% of Smith Group, LLC, a computer security services firm. Smith Group is currently worth $10 million. Mary expects that Smith Group will be sold within one year for a handsome profit, but currently no buyer has been identified. Mary previously created the Smith Family Trust, an irrevocable trust to benefit her spouse and descendants. The Trust is exempt from estate taxes upon Mary's death.



A GRAT provides protection against a disagreement with the IRS over the value of the asset transferred to the GRAT. In Mary's case, even if the IRS could sustain a higher value for the 35% membership interest in Smith Group, LLC, the annuity payments to Mary would increase – i.e., the new annuity payments would be recomputed as 52.109% of the increased value. The gift to the family members would still remain

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[1] This is merely an illustration using certain assumptions. Actual results will vary.

at a nominal amount. Therefore, the GRAT strategy mitigates the risk of a valuation adjustment on audit when using a hard to value asset, such as an interest in a family or private company.

The ability to establish a GRAT began in 1990 when Congress enacted statutes specifically providing for this type of trust. Since that time the GRAT technique has proved to be effective at transferring wealth at a minimal cost for gift and estate tax purposes. This is another intelligent method of transferring significant sums to younger generations and other family members.

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