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# Grantor Retained Annuity/ Uni Trust
# Questions and Answers

**Question 1: What is a Grantor Retained Annuity Trust (GRAT)?**

Answer: A GRAT is a trust that permits you to: (1) transfer property to it, (2) receive an annuity interest for a term of years from it, and (3) direct who receives the balance at the end of the trust term. In a low interest-rate environment it is effective for transferring assets that are expected to appreciate at a relatively low or no transfer-tax cost.

**Question 2: What is a Grantor Retained Uni-Trust (GRUT)?**

Answer: A GRUT is similar to a GRAT except that the grantor receives periodic payments equal to a predetermined percentage of the annual value of the trust principal. Thus, the dollar value of periodic payments may increase or decrease depending on the performance of the trust investments.

**Question 3: How are annuity payments figured?**

Answer: Annuity payments are determined with reference to the term of the trust, a predetermined percentage or dollar amount, and the IRC 7520 interest rate. The value of periodic payments does not change as would the value of a uni-interest.

**Question 4: What kind of property should I transfer to my trust?**

Answer: You may fund the trust with any property, but the trust is most effective when funded with assets that are expected to appreciate in value at a greater percentage than the applicable IRC 7520 rate. This is so, because the property value used for determining transfer tax cost is the fair market value at the time the property is transferred to the trust.

**Question 5: What is the transfer tax?**

Answer: Anytime you give property in excess of $12,000.00 per year to any one person, the United States government imposes a tax on the gift. The tax rate is currently 45%. However, each taxpayer has a one million dollar lifetime exemption that reduces your estate tax exclusion. The GRAT/GRUT can help to leverage this exemption.

**Question 6: How do you determine the transfer tax cost?**

Answer: The tax payable is based on the current value of the property interest that passes at the end of the trust term. Simply stated, the value of the gift is equal to the value of the

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property transferred to the trust minus the value of the periodic payments that you will receive.

**Question 7: How does this leverage my gift-tax exemption?**

Answer: Assume that you transfer shares of stock into the trust. The shares are worth $100,000.00 at the time of the transfer into trust. You reasonably expect the shares to appreciate at 20% per year. The trust term is 10 years. The 7520 rate is 5.2%. You retain an annual annuity payment equal to 13% of 100,000.00, i.e. $13,000.00. At the end of the ten-year period you will have received $130,000.00 and your beneficiary receives about $280,000.00, yet the value of the gift is only $600.00. You have given almost $300,000.00 at a transfer-tax cost of $300.00.

**Question 8: What is a "zeroed-out" GRAT?**

Answer: If you have an asset that will almost certainly appreciate rapidly and drastically in the relatively near future, you may do a short-term GRAT that gives you a return of principal and transfers the appreciation of the asset to your beneficiary. The GRAT is "zeroed out" in that there is absolutely no gift tax due, yet your beneficiary has received a substantial gift. In this case there is no transfer-tax cost.

**Question 9: How might this work?**

Answer: Assume that your shares are reasonably expected to appreciate by 50% per year. You transfer your $100,000.00 worth to the GRAT and take a 53.93137% annuity for two years. At the end of the two years you have received $107,862.74. Your beneficiary receives shares worth over $90,000.00, yet there is no tax because there is no present value to the gift.

**Question 10: You wrote in the answer to question 1 that the GRAT is effective in a low interest rate environment. How much would a greater 7520 rate affect the example above?**

Answer: If the 7520 rate were 10.2% rather than 5.2%, you would receive $115,545.74 back at the end of two years, and your beneficiary would receive $80,567.83. The technique is still effective, just a bit less so.

**Question 11: Why can't I just give my daughter a gift in return for her promise to pay to me all income for life?**

Answer: You can, but the gift tax will be figured based on the full fair market value of the gift without any reduction in value for the value of your periodic payments. Further, at your death, the value of the transferred property will be included in your taxable estate, because you retained an interest for life. This is definitely not the desired result. The GRAT of GRUT is recognized and accepted by the IRS, because it provides "qualified" payments to you.

**Question 12: Can the trust give me a promissory note instead of cash or stock?**

Answer: No. Regulations do not permit the trust to issue a debt instrument in lieu of actual payment. This is why it is a good idea to fund the trust with cash equivalents along with illiquid assets.

**Question 13: What happens if I die during the trust term?**

Answer: If you die during the trust term and the governing instrument provides that periodic payments shall continue beyond your death (paid to your estate), then the periodic payments will be valued according to the trust term, not up to the date of your death. This is good, but a portion of date of death value of the trust principal will be included in your taxable estate. This is not so good. It is important to consider your life expectancy when selecting a trust term. A series of short-term GRATs might be better than one long-term GRAT. On the other hand, the reduced value of the principal included in your estate under IRS regulations may make the risk of a long-term GRAT worthwhile. But this depends on the circumstances.

**Question 14: Does a GRAT or GRUT offer any asset protection?**

Answer: Yes. Since you have irrevocably transferred the asset to the trust and have given your beneficiary an enforceable interest in the trust asset, the asset is not subject to the claims of your creditors. However, your periodic payments are open to attachment.