



## Grantor Retained Annuity Trust

The Grantor Retained Annuity Trust (“GRAT”) is one of the leading wealth transfer techniques. It is ideal for clients who want to move wealth out of their estate without paying taxes, and it is a remarkably simple concept. Now may be the best time to incorporate a GRAT into your estate plan.

A GRAT is a trust into which the grantor makes a gift and retains a stream of annuity payments for a term of years. Most GRATs are for a term of between 2 and 10 years. At the end of the term of years of the GRAT, if there are any assets remaining, those assets pass to the remainder beneficiaries free of any gift tax or estate tax.

### A Successful GRAT

In order to be successful, the GRAT assets will generally need to outperform the Applicable Federal Rate (called the Section 7520 rate) that exists as of the month the assets are transferred to the GRAT. The current Applicable Federal Rate for August 2020 is the lowest in history, at only *four tenths of one percent* (.4%). This means that a GRAT is successful if the assets inside the GRAT grow at more than .4% annually. The amount by which the assets in the GRAT exceed the Applicable Federal Rate is the amount that is transferred estate and gift tax free to the beneficiaries. Since the current applicable rate (.4%) is so low, virtually all of the growth inside the GRAT can be transferred tax free.

### Short-Term “rolling” GRATs

One strategy is for the grantor to gift publicly-traded stock to a short-term two-year GRAT in order to take advantage of the higher volatility of a short-term GRAT, as opposed to that of a long-term GRAT. As the annuity payments are made to the grantor using stock to make those payments in-kind, the grantor will often re-GRAT that stock into new two-year GRATs, a technique called “rolling GRATs.” By continuing to do this, the grantor will often have some successful GRATs in strong two-year periods and some unsuccessful GRATs during weak two-year periods. If just some of the GRATs are successful, the strategy works well.

There are several reasons the GRAT strategy is particularly appealing right now:

1. GRAT rate is the lowest in history. The applicable GRAT rate is now only *four tenths of one percent* (.4%). This is the lowest in history.



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2. No downside. There is really no downside to utilizing a GRAT. A grantor can put any amount in the GRAT, and if the growth of the assets in the GRAT do not exceed the low applicable rate, the grantor receives the assets back and is in the same position as if no GRAT was ever created. No gift tax is due.
  3. November Election. The 2020 election has tremendous financial implications, one of which is Joe Biden's proposal to significantly reduce the current (historically high) estate tax exemption for Americans. Also, former President Barack Obama's administration sought to significantly limit the use and efficiency of the GRAT technique. It is therefore possible that the GRAT technique would be similarly scrutinized or limited under Joe Biden's administration, if elected. Accordingly, individuals should consider implementing plans to mitigate estate taxes by using a GRAT before November 2020.

### **Conclusion**

A GRAT is a simple, yet powerful, tool. In light of the current interest rate environment and the uncertainty regarding future estate and gift taxes, right now might be the best time to consider using a GRAT to save taxes.

