

## SHOULD YOU CONSIDER A GRAT THIS YEAR?

### Low Interest Rates Create GRAT Funding Opportunities



*If you are planning on making a gift to a family member, take advantage of historically low rates that:*

- Allow you to reduce your tax burden and
- Remove future appreciation from your estate.

#### WHAT IS A GRAT?

A grantor retained annuity trust (GRAT) is an irrevocable trust designed to transfer property to beneficiaries (often the grantor's children) with little to no gift tax. The grantor retains the right to receive payments for a term of years. At the end of the term, any remaining property in the GRAT passes to the remainder beneficiaries. A GRAT is generally funded with rapidly appreciating or high income-producing assets, and the main goal is the removal of appreciation and/or income from the grantor's estate.

#### HOW DOES A GRAT WORK?

Since a GRAT is an irrevocable trust, the property transferred to the GRAT becomes a taxable gift to the remainder beneficiaries. The value of the gift is reduced by the value of the retained right to receive annuity payments over the trust term. The value of the retained interest is calculated using a discount rate determined by the IRS known as the section 7520 rate, or the "hurdle rate." If the property in the trust grows faster than the section 7520 rate, the excess growth will pass to the remainder beneficiaries estate tax free.

#### WHY IS NOW AN OPPORTUNE TIME TO FUND A GRAT?

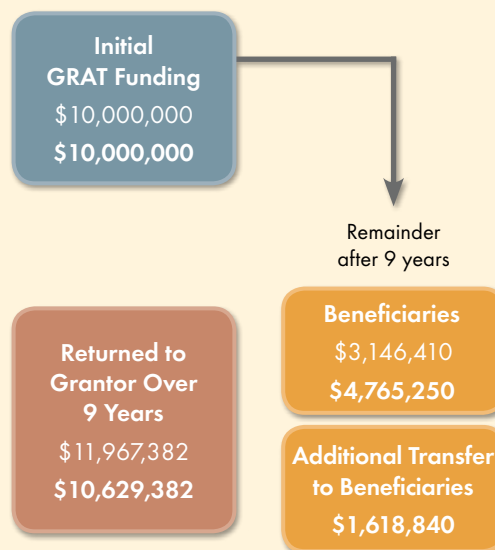
The tax benefit of setting up a GRAT is the greatest when the asset's growth rate exceeds the section 7520 rate. Since the current section 7520 rate is at an all-time low of 1% (November 2012), there is a likely opportunity to remove appreciation and/or income from the grantor's estate.

#### LET'S TAKE A LOOK AT THE DIFFERENCE BETWEEN FUNDING A GRAT ASSUMING TWO DIFFERENT 7520 RATES.

Suppose a nine-year GRAT is funded with property valued at \$10 million with an expected annual growth rate of 6.5%. Also, suppose the annuity payments are structured such that they increase 20% annually over the nine-year term.

The illustration at right demonstrates the significant impact that a low section 7520 rate has on the amount that will be transferred to the beneficiaries. The figures on top assume a 3% section 7520 rate, while the numbers on bottom assume a 1% section 7520 rate.

As you can see in this example, an additional \$1,618,840 would be transferred to the beneficiaries given the current section 7520 rate of 1% compared to the higher 3% rate.



### HOW DO I KNOW IF THIS PLANNING TECHNIQUE IS APPROPRIATE FOR ME?

Northern Trust advisors can help you determine how funding a GRAT might help you accomplish your specific wealth accumulation and wealth transfer objectives. We have the experience and resources to provide clients with the proper education to help them make informed decisions. We also work together with tax, legal and investment professionals to help construct a thoughtful plan and guide clients through implementation.

### FOR MORE INFORMATION

Northern Trust is a leading global financial institution founded more than 120 years ago on the principles of service, expertise and integrity. We are one of the nation's strongest, most secure financial institutions and a recognized leader in wealth management. To learn more, contact a Northern Trust professional at a location near you or visit us at [northerntrust.com/taxcenter](http://northerntrust.com/taxcenter).

IRS CIRCULAR 230 NOTICE: To the extent that this communication or any attachment concerns tax matters, it is not intended to be used, and cannot be used by a taxpayer, for the purpose of avoiding any penalties that may be imposed by law. For more information about this notice, see <http://www.northerntrust.com/circular230>.

LEGAL, INVESTMENT AND TAX NOTICE: This information is not intended to be and should not be treated as legal advice, investment advice or tax advice. Readers, including professionals, should under no circumstances rely upon this information as a substitute for their own research or for obtaining specific legal or tax advice from their own counsel.



**Northern Trust**

© NORTHERN TRUST 2012

[northerntrust.com](http://northerntrust.com) | Should you consider a grat this year? | 1 of 2

Q52209 (11/12)