

Wealth transfer planning strategies for the current time



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While news about the pandemic and all the ways it is impacting us dominate our daily lives, those who give attention to the future may be able to find some attractive wealth transfer opportunities. The combination of depressed asset values and extraordinarily low interest rates suggests certain potentially effective strategies.

Brief discussions of some of these strategies follow:

Grantor Retained Annuity Trust (GRAT)

A GRAT involves a transfer to a trust with the transferor retaining an annuity payment from the trust for a specified time period, usually two to ten years. The annuity is set at an amount computed to return to the transferor the value of the asset(s) transferred to the trust (at the time the trust is funded) plus an investment return. Each month the IRS publishes an investment return rate (the “7520 rate”) that it is assumed the GRAT will realize over the GRAT’s term. For June, the rate is an exceptionally low 0.6%. Because the annuity’s value (according to the IRS) at the time the GRAT is funded is the same as the value of the property transferred to the GRAT, no gift results. However, if the return on the GRAT’s property exceeds the 7520 rate over the GRAT’s term, value (possibly considerable value) passes to the next generation or trusts for their benefit when the GRAT terminates. As you probably can discern, the greater the investment return during the GRAT’s term, the greater the amount passing transfer tax free when the GRAT terminates.

The following table shows the amount that can be transferred at the GRAT’s termination using the June 7520 rate; two and, alternatively, ten year GRAT terms; a GRAT funded with \$1 million; and an assumed 10% total return on the GRAT’s property over the GRAT term:

GRAT Term	Annual Annuity	Total Annuity Payments	Value at Termination
2 years	\$504,515	\$1,009,030	\$150,518
10 years	\$103,329	\$1,033,290	\$946,941

Gifts

If you believe currently depressed asset values are not representative of future higher values, making gifts now may be a good means of efficiently transferring wealth. Gifts have the effect of transferring future appreciation from the donor’s taxable estate. Gifts not exceeding \$15,000 per donee per year (annual exclusion gifts) do not consume transfer tax exemptions. Gifts with values exceeding those qualifying for the annual exclusion reduce the exemption available, which for this year is \$11.58 million. This exemption is indexed for inflation through 2025, then under current law is reduced by one-half beginning in 2026. Owners of substantial wealth will want to consider the prospects of a reduced

exemption in their transfer tax planning.

When an owner decides to make a gift, an important consideration is what property to transfer. Among the main considerations are:

- transferring assets believed to have the greatest appreciation potential;
- transferring assets with relatively low gain (in order to benefit under current law from a stepped-up-basis for assets retained until death rather than transferred by lifetime gift); and
- the impact on the owner's income of giving away assets with different yields.

Low Interest Loans or Sales

Just as the 7520 rate is extraordinarily low currently (0.6% in June), so are the Applicable Federal Rates (AFRs) for loans. Effectively, loans made at or above the AFR rate will not result in any imputed interest that would be treated as a gift. For AFR purposes, tax law provides three categories of term loans: short (less than three years), mid (three to nine years), and long (nine or more years). For loans made in June (AFR rates are subject to monthly adjustments), the AFRs are:

Short	0.18%
Mid	0.43%
Long	1.01%

With interest rates being so low and asset values being depressed, loans the proceeds of which the borrower (usually a descendant of the lender or a new or existing trust for a descendant) can use to make investments or reduce higher cost debt have the potential to efficiently transfer wealth.

Just as low-interest loans may be an attractive wealth transfer strategy, so also can be a sale to a family member. Capital gain from a sale of appreciated property may be an obstacle to this strategy, but a sale to a trust which has a feature that makes it a grantor trust for income tax purposes can overcome this obstacle.

These are just some of the features of a few strategies that deserve consideration under current circumstances. We are glad to discuss your planning with you.

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