



## Market conditions and pending legislation:

Why now is the time to review your wealth transfer strategies.

The summer of 2009 may be the best time to address wealth transfer planning in the past 20 years:

- It is highly likely new estate tax legislation will be enacted later this year.
- Proposed legislative changes, including proposals from the Obama Administration, target key wealth transfer strategies—such as GRATs and transfers—that make use of valuation discounts.
- Current economic conditions such as depressed asset values and low interest rates lend themselves to strategic planning.

Wealth transfer planning ensures that assets pass to family members, charities, and other intended beneficiaries with the lowest transfer tax cost possible. While this aspect should be part of your overall financial strategy, the formulation and reevaluation of wealth transfer planning goals and strategies will be very important over the next three to four months.

### **Understand why Grantor Retained Annuity Trusts (GRATs) are a highly effective wealth transfer strategy in this economy**

Implementing a GRAT involves a grantor who transfers highly appreciating property into a trust while retaining an annuity stream for a stated period of years. At the expiration of the term, the property remaining in the trust is transferred to the GRAT remainder beneficiaries.

Because the grantor retains an annuity stream, GRATs are appealing to people who are cautious about giving away their current wealth.

The transfer of assets to a GRAT creates a taxable gift equal to the fair market value of the assets minus the actuarially determined present value of the retained annuity stream. To the extent that the amount actually transferred as the remainder interest exceeds the value calculated for gift tax purposes, the excess is transferred gift-tax free. At the end of the GRAT term, the remainder interest that passes to heirs is removed from the grantor's estate. Because the present value of the remainder interest is calculated based on the interest rate at the time the trust is established, GRATs can be especially effective during periods of low interest rates.

GRATs have been legislatively sanctioned since 1990, with the typical GRAT term running for as little as two or three years. However, if passed this fall, an Obama Administration proposal would require a 10- year minimum term for GRATs. While a zeroed-out gift (an annuity stream that is valued equal to the value of the property contributed to the GRAT) would still be permitted, the impact a GRAT could have on your transfer of wealth could be negatively impacted by the 10-year minimum-term requirement.

For this reason, prudent planning calls for considering the creation of one or more new GRATs in 2009, before the 10-year minimum-term requirement is enacted.

### **Be aware of proposed changes to estate and gift tax rates**

Due to rules enacted several years ago, the US estate and gift tax system is currently in a state of flux. Gift taxes (not scheduled to be repealed) have a maximum tax rate of 35% for 2010. For 2011 and thereafter, the gift tax exemption is scheduled to remain at \$1 million, while the highest tax rate increases to 55%.

Those dying in 2009 are entitled to an estate tax exemption of \$3.5 million, with the highest estate tax rate set at 45%. Under current law, the estate tax is scheduled to be repealed for one year for persons dying in 2010 and then reinstated in 2011. For 2011 and thereafter, the estate tax exemption is scheduled to be \$1 million, with the highest tax rate set at 55%.

Although it is uncertain how issues caused by the scheduled, one-year repeal of the estate tax will be resolved, the general consensus is that some action will be taken before the temporary estate tax repeal takes effect.

### **Do you have a family-controlled entity? Consider action before changes in valuation discounts**

An appraisal of a family business entity determines the value of an owner's interest, essentially estimating the price a willing buyer would pay to a willing seller. The same approach is used to determine the value for gift and estate tax purposes. Currently, one technique often used in wealth transfer planning involves the creation of a family-owned business entity with voting and non-voting interests. A transfer of non-voting interests is typically valued by taking minority and lack-of-marketability discounts into account.

In such instances, an Obama Administration proposal would change situations where a valuation discount is available by ignoring restrictions imposed on the transferred interest for wealth transfer purposes. Now is the time to evaluate whether the transfer of a family business entity should be implemented before any new rules take effect.

Wealth planning is an area in which you can benefit from the recent economic downturn. In today's otherwise difficult and uncertain economic environment, depressed asset values and low interest rates create tremendous wealth transfer

opportunities that should be explored before the environment changes and new laws are enacted.

Want to know more about applying GRATs and other wealth planning strategies? Please contact your local PricewaterhouseCoopers partner or:

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