

USING FAMILY LIMITED PARTNERSHIPS, SALES TO GRANTOR TRUSTS AND GRAT'S TO MINIMIZE TRANSFER TAXATION AND TO FUND LARGE INSURANCE PREMIUMS

I. INTRODUCTION AND CIRCULAR 230 NOTICE

A. Introduction – This outline briefly summarizes several advanced estate planning concepts including the use of Family Limited Partnerships (“FLP’s”), Sales to Intentionally Defective Grantor Trusts (“IDGT”) and the use of Grantor Retained Annuity Trusts (“GRAT”). These vehicles can accomplish numerous estate planning and asset protection objectives. This outline will present a brief substantive discussion of family wealth transfer techniques and illustrates the advantages and disadvantages of using the various structures outlined above.

These structures are commonly referred to as “estate freezing” techniques in that they attempt to shift the future expected appreciation in the value of the asset to the next generation in a manner that will allow the expected appreciation to escape liability from transfer taxation. These structures are very complicated and require careful planning and expert guidance in order to achieve successful attainment of the client’s objectives.

B. Circular 230 Notice – Pursuant to Internal Revenue Service Circular 230, I am required to advise you that this outline involves a discussion of various tax matters and an analysis of one or more significant tax issues. We believe that the conclusions reached in the memorandum are based on substantial authority and relate to tax benefits in a manner consistent with applicable statutes and

congressional intent. Our conclusions, however, are not intended to be relied on and cannot be relied on for the purposes of avoiding penalties that may be imposed by the Internal Revenue Service. In addition, the ideas described in the outline should be considered as merely preliminary tax advice. If the reader of this outline determines to proceed with any of these ideas, or if the reader wants more information before deciding on proceeding with any of these ideas, we can provide you with a more complete and formal description of the tax effects of the specific transaction you may wish to consider. Because preparation of that more formal tax advice may require additional facts and research regarding the reader's individual situation, the reader should not rely on the preliminary ideas described in the memorandum as a basis for implementing a transaction based on those ideas.

II. GOALS OF FAMILY WEALTH PLANNING

A. Wealth Disposition – An experienced estate planning attorney has many tools available to assist their clients in meeting their wealth transfer objectives. This may involve the use of wills, trusts, life insurance, charitable planning, family limited partnerships, GRATS, Captive Insurance Companies, and other advanced planning opportunities.

B. Wealth Protection Concepts – The preservation of a client's wealth, both during their lifetime and at death may involve asset protection planning, the management of assets and the minimization of costs associated with the transfer of wealth including the reduction of transfer taxes. The ideal estate plan will involve all of these concepts so that we can protect our clients' assets from seizure by creditors, allow them to control their assets

to a substantial degree and reduce the costs and taxes associated with the transfer of wealth.

III. WEALTH PRESERVATION

A. Lifetime Gifting – Transfer tax reduction through lifetime gifts. Lifetime gifting allows a client to minimize estate and gift taxation through various available means that are allowed by the IRS. Each person is allowed to donate \$13,000.00 (for 2009) per year, to as many people as they want, every calendar year. This is referred to as the “Annual Exclusion” and this amount is adjusted for inflation annually. As an example, a married couple with three children \$78,000.00 to their children on January 1, 2009 and every year thereafter.

In addition, clients can pay an unlimited amount for education or medical expenses as long as the checks are written directly to the institution and not to the individuals that are involved.

In addition to the annual exclusion, educational and medical gifting exemptions that are available to our clients, each person is allowed to transfer up to \$3,500,000.00 free of the estate tax (commonly referred to as the “Unified Credit”) so that a married couple could transfer \$7,000,000.00 to their descendants free of the estate tax. However, under current law, a person can only gift \$1,000,000.00 of their unified credit during their lifetime.

The advantage of using these various exemptions during a client’s lifetime is that the appreciation of those assets is removed from the estate. As you will see later, it is also possible to have the client continue to pay the income tax liability associated with that

appreciation even though the underlying assets have been moved to lower generations. This is accomplished through the use of an intentionally defective grantor trust (“IDGT”) which is discussed in further detail later in this outline. By having the parents continue to pay the income taxes on the earnings of the assets held by the trust for the benefit of their descendants, the parent’s estate is further reduced thereby decreasing the estate taxation on their assets.

Further, in certain circumstances, it may be beneficial to exceed the above limitations, and in particular the \$1,000,000.00 lifetime gift tax exemption and have the client pay gift taxes on the excess above the \$1,000,000.00 exemption since the payment of the gift tax is not in and of itself subject to taxation. To provide a fairly simple illustration, and forgetting about the unified credit for a moment, the client dies owning \$10,000,000.00 and the estate tax rate is 50%, his heirs will inherit \$5,000,000.00. If, on the other hand, the client chooses to transfer his wealth while he was alive, he could donate \$6,600,000.00 and pay the 50% gift tax of \$3,330,000.00 so that his heirs inherit \$1,660,000.00 more by utilizing lifetime gifting. Again, this is a result of the fact that the dollars used to pay the \$3,330,000.00 gift tax are not in and of itself subject to estate tax.

B. Disadvantages of Lifetime Gifting. Lifetime gifting does have several disadvantages, however, including the potential loss of control of the gifted property and the fact that once an asset is gifted, it is typically an irrevocable transaction. An additional problem with lifetime gifting is that many clients are not only reluctant to lose control, but they are concerned about becoming

financially destitute if they gift too much of their wealth while they are alive. However, there are ways to minimize these concerns.

However, the use of the annual exclusion and the \$1,000,000.00 lifetime gift tax exemption can yield extraordinarily substantial transfer tax benefits, in particular when used with an IDGT (“See exhibit “A” at the end of this outline”).

C. What does the future hold for the unified credit amount?

Under the law in effect on January 1, 2009, the exemption is \$3,500,000 per person in 2009, there is no estate tax in 2010 and in 2011 the estate tax returns but at a \$1,000,000.00 exemption level.

IV. GIFTING STRATEGIES INVOLVING FAMILY LIMITED PARTNERSHIPS

A. General Concepts - A common objective of many clients is to have their assets protected from seizure by creditors and to maintain control to the greatest extent possible while they are alive. Obviously, this can lead to some clients not wanting to transfer assets directly to their descendants since they would lose control over those assets. Since many clients want to maintain some degree of control over the assets they gift, the use of Family Limited Partnerships (“FLP’s”) has become increasingly popular (See chart on Exhibit B).

B. What is a FLP? The FLP is an entity that is structured so that the ownership is divided between a small number of Class A voting shares and a much larger number of Class B non-voting shares. Further, restrictions are placed on the transferability of the ownership of the entity so that ownership cannot be transferred

without first offering it to the remaining owners. Typically, the parents will retain all of the voting rights of the company and the non-voting ownership interest will be gifted or sold to the descendants or trusts for their benefit. The fact that the Class B ownership interests have very little voting rights and the fact that they cannot be easily transferred, results in the Class B ownership valuation being discounted relative to the underlying assets of the entity. For transfer tax purposes, the value of an asset is determined by defining the price at which the asset would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or the sell, and both having reasonable knowledge of the facts. Valuation discounts occur due to the fact that the Class B ownership interest are not worth as much as their proportionate share of the underlying assets held by the entity since they lack marketability and control.

Depending on a number of factors, the discounts can range between 15% - 50% of the underlying assets of the company.

C. Types of Entities that can be used for the Transaction – While commonly referred to as a Family Limited Partnership, this structure can be used with “C” corporations, “S” corporations, limited liability companies and partnerships. Further, this structure can be used for an ongoing business that has been operating for years as well as an entity that is newly created to hold assets owned by the parents’ generation.

D. Example of Gifting using a FLP Structure – Assume Archie and Olivia own an operating business that they believe is worth \$10,000,000.00. Archie and Olivia have three grown sons who are

successful in their own right and seven grandchildren who hold a special place in their hearts. Archie wants to make sure that he maintains control of the business for as long as he is alive and, if he died, that Olivia would continue to control the company until her passing. The limited liability company that they own was established many years ago, and had a very simple Operating Agreement. After several meetings, the clients decide that an FLP structure makes sense for their family. We would amend the Operating Agreement and recapitalize the ownership into two (2) Class A voting units and nine hundred ninety-eight (998) Class B non-voting units. We would then obtain a valuation of the underlying assets of the company as well as an additional valuation of the Class B non-voting units that would have lack of marketability and lack of control discounts. By retaining the Class A units, Archie and Olivia would make all of the important decisions regarding the management and operation of the LLC. If the appraisal of the 998 Class B units indicates a discount for lack of marketability and lack of control of 30%, then the Class B units would be valued at approximately \$7,000,000.00.

At this point, Archie and Olivia could do any of the following. First, they could gift sufficient Class B units to each of their three children and each of their seven grandchildren to fully utilize the \$13,000.00 annual exclusion. With ten (10) descendants, Archie and Olivia could gift Class B units that would have a total value of \$260,000.00 ($\$13,000.00 \times 2 \times 10$) so that they could fully utilize their annual exclusion gifting capacity. Further, next year and every year thereafter, they could make an additional gift of Class B units \$260,000.00 ($\$13,000.00 \times 2 \times 10$) to fully utilize their annual exclusion gifting capacity.

However, Archie and Olivia realize that their business is growing at a very rapid pace and, consequently, they realize that their annual exclusion gifting alone will not be sufficient to remove the growth of their business from their estate. As a result, Archie and Olivia agree to transfer an additional \$1,000,000.00 each of the Class B interests which they are permitted to gift under the federal gift tax exemption amount. Consequently, Archie and Olivia are allowed to gift over \$2,500,000.00 worth of discounted Class B units of their company between now and the beginning of next year (\$2,000,000.00 unified credit gift plus current year annual exclusion gift of \$260,000.00 plus next year's annual exclusion gift of \$260,000.00). As a result of this transaction we will have transferred 35.71% ($\$2,500,000/\$7,000,000$) of their business, representing \$3,571,000.00 of underlying assets for a discounted value of \$2,500,000.00, without paying any gift taxes. The difference ($\$3,571,000.00 - \$2,500,000.00 = \$1,071,000.00 \times 45\%$ estate tax rate), will result in the children saving \$481,195.00 as a result of this transaction plus the appreciation on the transferred "B" units will also be removed from the estate and not subject to the estate tax when the clients eventually pass away.

E. What do we do with the balance of the Class B shares? With regard to the remaining 65% of the Class B units, the clients will have several options. If they retain these Class B units in their estate, the future appreciation on those assets will result in additional estate taxes being levied at their death on that appreciation. One option would be for Archie and Olivia to gift the balance of those shares, but there would be a substantial gift tax since they would have already utilized their annual exclusion gifts

thru the following year and their \$1,000,000.00 unified credit exemption that can be used during their lifetime. However, again, it is more efficient to pay gift tax rather than estate tax for the reasons detailed previously herein. Having said that, most clients refuse to pre-pay transfer taxes if they can avoid having to do so. An additional option would be to sell the remaining Class B shares to an Intentionally Defective Grantor Trust (“IDGT”) in exchange for a Promissory Note.

V. A SALE TO AN INTENTIONALLY DEFECTIVE GRANTOR TRUST

A. In General – A primary advantage to utilizing lifetime gifting is the ability to shift some or all of the future appreciation of an asset to the donor’s family and remove the appreciation from estate taxation. If Archie and Olivia sell the balance of the Class B shares to an IDGT, there will be no capital gains tax on the sale since the IDGT is indistinguishable from Archie and Olivia for income tax purposes even though the assets are removed from their estate for estate tax purposes.

B. Grantor Trust Rules – Under the Internal Revenue Code, the trust can be structured in a manner that will allow the creator (referred to as a “Grantor”) to retain certain powers in a manner that will result in the trust income being taxed to the Grantor as if the trust did not exist for income tax purposes. Common IDGT’s include a revocable trust, or an irrevocable trust that allows the grantor to exchange assets with the trust, in a non-fiduciary capacity, for assets of equal value. It is referred to as an intentionally defective grantor trust because it is intentionally drafted in a manner that

causes the income to be taxed to the grantor even though the assets were removed from the grantor's estate.

C. IDGT Tax Consequences – Because an IDGT is not recognized as a separate entity for income tax purposes, despite the fact that the trust can be structured in a manner so that the assets are not included in the grantor's estate for federal estate tax purposes, several positive tax results will occur. First, all of the trust income and expenses will be reflected on the grantor's personal income tax return. Having the grantor pay the income taxes on income earned by the assets held within the trust results in the grantor indirectly making a tax free gift to the trust beneficiaries. However, pursuant to Revenue Ruling 2004-64, the payment of income taxes by the grantor on the trust assets is not considered a gift by the grantor to the trust. Further the payment of income tax by the grantor on the trust income removes the dollars used to pay the income tax from estate taxation in the grantor's estate. Based on Bernstein's analysis, as demonstrated on Exhibit C, significant wealth transfer results will occur due to the grantor paying the income tax rather than the beneficiaries. As a simple example, if the trust assets yield a ten percent (10%) income stream, the beneficiaries realize the full ten percent (10%) growth rather than paying a forty percent (40%) combined state and federal income tax which would result in a net six percent (6%) growth of the trust assets. Additionally, due to the fact that the trust is not recognized as a separate entity for income tax purposes, transactions between the grantor and the trust are disregarded. As a result, if a grantor sells assets to the IDGT, the grantor is considered as having made the sale to himself, which is not recognized for federal income tax purposes and, consequently, no capital gains will be recognized on

the sale to the IDGT. Finally, a federal gift tax return is typically required to be filed with this transaction. Most commentators feel that it is necessary to gift at least ten percent (10%) of the value of the sold assets to ensure that there is sufficient collateral which would be necessary in an arm's length transaction. This gift will necessitate the filing of a gift tax return by April 15th of the year following the donation.

D. Disadvantages to Lifetime Gifting – Beyond the issues relating to potential loss of control, and the ability to access the assets transferred, an additional consideration involves the loss of the so called “step up” in basis that typically occurs when someone dies. In other words, if a client purchased stock for \$10 a share, retained it for their life and at their death the stock was worth \$100 per share, his beneficiaries would inherit the stock and be able to sell it for \$100 a share without incurring any additional capital gains taxes due to the “step up” provisions of the internal revenue code. However, when a lifetime gift is made, the children do not receive a “step up” basis and instead get a carryover basis that is equal to the \$10 that their parents purchased the stock for originally. However, the estate tax savings at higher tax rates typically outweigh the loss of the “step up” at the lower capital gains tax rates. Further, if the children do not intend to sell the asset, this issue has no impact.

E. Illustration of Benefits of Sale of Family LLC to an IDGT – Continuing with our previous example, if Archie and Olivia have sixty-five percent (65%) of the remaining Class B units, they could sell those units to the IDGT in exchange for a Promissory Note of equal value. The Promissory Note will bear interest at a rate equal

to the rate published by the IRS on a monthly basis. The note can be structured as a balloon note with interest only payments spread out over Archie and Olivia's life expectancy. Thus, Archie and Olivia can gift \$2,500,000.00 of discounted Class B shares and the remaining \$5,500,000.00 would be sold to the IDGT in exchange for a Promissory Note of \$5,500,000.00 bearing interest, payable in annual installments of interest only. As a result of these transactions, Archie and Olivia will have transferred ninety-nine percent (99%) of their business, while retaining substantial voting control, in exchange for a Promissory Note of \$5,500,000.00 growing at a nominal interest rate. If the business would have doubled in value to \$20,000,000.00 over their lifetime, the estate tax savings between the amount that would have been subject to estate taxes (\$20,000,000.00) and the amount included in their estate (\$5,500,000.00) results in a savings of approximately \$6,500,000.00 to the children.

A substantial shift in wealth to the next generation will occur if the growth of the trust assets on an after income tax basis exceeds the interest rate payable on the note. A balloon installment payment will further enhance the wealth transfer since all of the trust assets are appreciating. The trust is only paying interest on the note and not on the entire assets of the trust.

F. Use Extreme Caution – It is critical that an experienced expert be involved in the planning of this transaction. If clients have a family attorney that handles all of their legal affairs, it is imperative that they go to an expert in estate planning. There are numerous tax traps that must be accounted for in structuring these transactions. For example, under Internal Revenue Code

§2702, if the grantor retains certain interests in the property transferred, then the property could be included back in the grantor's estate. Further, great care must be exercised in the structure of the entity, the design of the trust, the administration of the company on an ongoing basis, the type of assets contributed to the company and similar problems that can result in substantial audit risks, litigation, penalties and attorneys fees if this structure is not designed correctly. Additionally, certain tax risks are associated with the use of an IDGT. Sales to IDGT's are not blessed by statute and instead owe their existence to IRS rulings and court cases. As a result, a sale to an IDGT could be eliminated by an act of congress or a change in IRS position. Further if a grantor dies before the entire installment obligation is paid, the balance of the Promissory Note is an asset included in the grantor's estate. This can be avoided through the use of a self-cancelling installment note ("SCIN"), but the use of a SCIN requires adroit planning to avoid a gift when the sale is made. It is absolutely critical that the assets of the company, as well as the Class B non-voting units, be appraised by a qualified appraiser. Do not subject yourself to the audit risks associated with someone who wants to value the company who doesn't possess the requisite training and expertise to properly value the assets. Finally, there is a risk associated with a decline in the value of the trust assets. As with any transfer planning, if the assets ultimately decrease in value, then much of the tax advantages of doing these types of transactions will be eliminated.

G. Recent Rulings – The IRS will frequently challenge FLP's if they are not structured or administered properly. It is important that the family home not be placed into the company, that the company

not be used as a pocket book for the parents, that the client retain sufficient assets in their own name and that there be substantial non-tax purposes for the establishment of the FLP. For example, in estate of Mirowski vs. Commissioner, the tax court upheld the FLLC discounts and held that legitimate and significant non-tax reasons were present for the creation of the entity. These purposes included joint management of the family assets, maintenance of the bulk of the family assets in a single pool, providing for each of the descendants on an equal basis and asset protection. The court rejected the IRS contention that a business purpose was needed to validate the transaction. In Holman vs. Commission, the taxpayer created a FLP and funded it with Dell Corporation stock. A week later, the taxpayer made gifts of limited partnership interests to family members and filed a gift tax return taking a discount on the value of the stock. The IRS argued that the discount was not appropriate and instead should have been treated as an indirect gift of the Dell Corporation stock itself and not of limited partnership interests. The court rejected the IRS's position that there was an indirect gift of the assets of the FLP and thus the discounts were warranted. Further, due to the fact that there was a "material economic risk" of a change in value, it wasn't necessary to wait months between the creation and funding of the partnership and the transfer of the limited partnership interests. However, it is uncertain that if the taxpayer had funded the FLP with bonds, more time may have been required before the transfer of the limited partnership interests. While the court in Holman refused to allow discounts for transfer restrictions in the partnership agreement, it still allowed a total discount of 22.5% for lack of control. This is one of the most restrictive valuation cases to date. While extreme caution should be used when

contemplating funding a FLP with publically traded securities, Holman should provide some relief to concerned taxpayers. Again, it is critical that an expert be hired to ensure that the establishment of the FLP is properly conducted. The non-tax reasons for establishing the entity should be substantial and documented. Further, the taxpayer should never place all of their assets inside the FLP and instead should retain sufficient assets to pay taxes and living expenses. In another taxpayer victory, the tax court in Astleford vs. Commissioner, held that multi-level discounts can be taken when a parent subsidiary structure is in effect, but there should not be an artificial stacking of shell entities. Some common non-tax reasons to establish a FLP include asset protection, to educate descendants about the importance of investments and wealth, introducing them to the management and time commitment required to manage wealth, to facilitate and manage pooled resources and to achieve various economies of scale. Another case that was favorable to a client that established a FLP by funding it solely with marketable securities is Bianca Gross, donor, vs. Commissioner in which the mother transferred only marketable securities to a FLP and made a gift to her daughter's of a 44.5% limited partnership interest. She took a 35% valuation discount on her gift tax return. Here, the tax court rejected IRS arguments that there was an indirect gift of the underlying assets and that the "step transaction" doctrine should be followed. The court did, however, warn that the step transaction argument may have application in other cases. Here, the court found that months prior to signing the FLP, the mother and her daughters reached an oral agreement on the same terms and provisions, and the asset transfers were completed over

several months to the FLP with the last transfer occurring 11 days prior to the gift.

VI. GRANTOR RETAINED ANNUITY TRUST

A. Introduction - A grantor retained annuity trust (“GRAT”) is a structure that allows taxpayers to remove a certain amount of the growth of the assets from their estate on a transfer tax free basis. The client would contribute assets to the GRAT and would retain the right to receive an annuity for a term of years, while the remainder interest, if any, will pass to their children or an IDGT in which the children are beneficiaries. Typically, the client’s retained annuity interest will reduce the value of the transfer so that there are no or little gift tax consequences upon creation of the GRAT. If the investment performance of the assets held by the GRAT exceeds the rate published by the IRS under §7520, in effect at the time of the funding of the GRAT, the excess value will be passed to the children free of gift tax. If the investment performance does not exceed the 7520 rate, all of the GRAT assets will be returned to the client in satisfaction of their interest, and the trust will owe no further payments to the client so that the grantor is in the same position economically as if the GRAT had never been established. In order to shift wealth to the remainder beneficiaries, the grantor must survive the trust term. If the grantor dies during the trust term, the assets of the GRAT will be included in the grantor’s estate and subject to estate taxation.

B. Income, Gift and Estate Tax Issues Relating to GRATS – A GRAT is a “grantor trust” for income tax purposes and the result is that the grantor will be taxed on all GRAT income. As stated previously, this is an additional benefit for wealth transfer

purposes since the grantor will pay income tax on property that remains in the trust. This enhances the value of the property passing to the remainder beneficiaries without being considered a gift that would be subject to gift tax. For gift tax purposes, the GRAT can be structured so that the actuarial value of the remainder interest is nominal or eliminated. This was allowed in the Walton case. Relative to estate taxes, if the grantor does not survive the term of the trust, some or all of the GRAT assets will be included in their estate, but if the grantor does survive the termination of the trust, then any appreciation above the 7520 rate will be removed from the grantor's estate and will not be subject to gift taxes either.

C. Considerations Regarding The Duration Of The GRAT –

Historically, many people viewed the ideal GRAT as being a long term trust and, ideally, the trust would terminate immediately prior to the grantor's death. Again, this was critical in that if the grantor died before the termination of the GRAT, some or all of the assets held by the GRAT would be included in the grantor's estate which would negate the transfer tax benefit. However, the key is to have the grantor transfer assets that they believe will significantly appreciate in value and to survive the term of the trust. One possibility would be to structure a series of two year GRATs so that the leverage can continue as long as it is economically feasible. In essence, the grantor would establish a trust in year one that would have a two year duration. After the end of the first year, GRAT #1 would make an annuity payment to the Grantor and the grantor would then contribute that annuity payment into new GRAT #2. Every year thereafter, the client would continue to establish GRATs and the payments being received from the previous GRATs would

be contributed into a new GRAT. This is commonly referred to as a “Rolling GRAT” or a “Cascading GRAT” since the grantor will continue to roll his annuity payments into new GRATs, although this can be discontinued at any point. (See Exhibit “D”).

D. Primary Advantages Of A GRAT – The primary advantages of a GRAT are that it will typically result in a small taxable gift, if any. The GRAT is an instrument that is specifically authorized by the Internal Revenue Code, and if the assets actually depreciate in value, the grantor will receive all of the assets held by the GRAT and the grantor is no worse off than if they had done nothing except for the transaction costs. Further, if the IRS challenges the value of the assets contributed to the GRAT, this will not dramatically affect the value of the gift. To the extent that the assets will continue to appreciate in value, the grantor can continue to roll those annuity payments into a new GRAT, but the excess appreciation from the prior GRATs will be removed from the estate regardless of when the grantor dies. Finally, since the GRAT is a grantor trust for income tax purposes, the GRAT will not be required to file a separate income tax return.

E. Primary Disadvantages of A GRAT – In order to be successful, in other words in order to transfer wealth without triggering gift taxes, the trust assets must generate a rate of return that is in excess of the §7520 Rate, which is 3.6% for November 2008. If the assets fail to achieve a rate of return in excess of the 7520 rate, other wealth shifting transactions may have been more beneficial. Second, the GRAT is not an effective tool for generation skipping transfer tax planning. Third, as previously stated, a grantor must survive for the term of the GRAT. Finally, if the GRAT assets do

not generate sufficient cash flow to satisfy the annual annuity payments, the trustee must either borrow funds from a third party lender or make an in-kind distribution of assets in order satisfy those payments. If the assets contributed to the GRAT are difficult to value, a formal appraisal will need to be done every year.

F. Additional Considerations – It is important that the grantor contribute only their separate property and not the community property of the grantor and their spouse. This can be achieved through a partition of the assets so that the grantor will contribute their separate property to the GRAT. If the assets contributed to the GRAT are publically traded securities, an appraisal is not required but rather the trust would value the assets at the average between the high and low selling prices on the date of the contribution. Based on some extensive research that Bernstein has prepared relative to the benefits of using Rolling GRATs compared to a series of long term GRATs or a sale to an IDGT, substantial wealth transfer results can be achieved (See Exhibit “E”).

G. Sample GRAT Transaction – Assume John owns 1,000,000 shares of ABC stock which is a publically traded company that is trading for \$10 per share on the date that he contributes the stock to the GRAT. The contribution is of John’s separate property and the 7520 Rate is 3.8%. The GRAT is established for a 2 year term. John contributes the million shares of ABC stock and \$100 in cash to the GRAT. The cash can be used to make up any excess in the amount of an annuity payment over the value of the stock distributed in satisfaction of that annuity payment so that the number of shares will be a whole number. John retains the right

to receive a payment each year of the GRAT term and the payment for the second year will be 20% greater than the first year. The annuity payments can be established so that John's retained annuity interest in the GRAT is equal to the fair market value of the ABC stock and the cash transfer to the GRAT. John can then create a separate IDGT for the benefit of his children. The IDGT will receive whatever value remains in the GRAT at the expiration of the two year GRAT term. Now assume that the ABC stock appreciates at a rate of 10% per year, and that the remainder in the GRAT will be distributed to the IDGT for John's children. The result of this is that John will be deemed to have made a gift of \$1 since the value of his retained annuity interest is almost equal to the fair market value of the stock transferred to the GRAT plus the interest factor that was applicable based on the 7520 Rate. This \$1 gift should be reported on a gift tax return which will start the statute of limitations. The first annuity payment, due one year from the establishment and funding of the GRAT will be 48.14404% of the fair market value of the assets contributed to the GRAT, or \$4,814,452.00. The second annuity payment, due at the end of the second year, will be 20% greater than the first payment which results in a second year annuity payment of \$5,777,343.00. If John survives the two year term and the ABC stock performs as expected with a 10% annual increase, John will receive payments totaling \$10,591,795.00 from the GRAT. The assets remaining in the GRAT at the end of the trust term will pass to the IDGT that was established for John's children and that amount would be \$1,026,881.00. Consequently, John will have shifted \$1,026,881.00 of value to his descendants with a deemed taxable gift of \$1.

Year	Beginning Trust Property	Appreciation At 10%	Annuity	Ending Trust Property
1	\$10,000,100	\$1,000,010	(\$ 4,814,452)	\$6,185,658
2	\$ 6,185,658	\$ 618,566	(\$ 5,777,343)	\$1,026,881
Total			(\$10,591,795)	\$1,026,881

H. Final Consideration – Please keep in mind that the structures detailed above are not mutually exclusive. As seen on Exhibit “F”, a client with substantial wealth can use a family limited partnership, a sale to IDGT and a GRAT in a manner that will transfer substantial amounts of wealth given sufficient time. By leveraging these transfers, additional income producing assets will be available to assist in paying premiums to hedge the payment of the estate tax. Again, please make sure that you consult with a qualified expert in estate planning to make sure that all of the requirements imposed by the Internal Revenue Code are met.

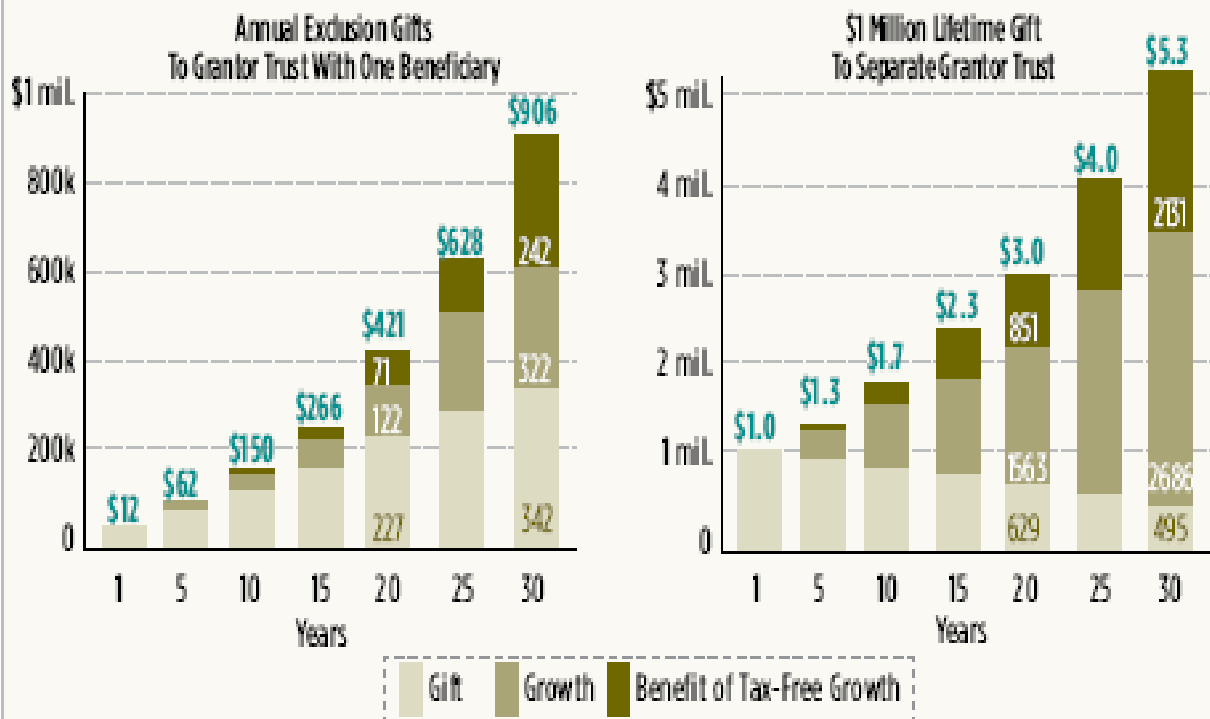
Exhibit "A"

The Grantor Trust Benefit

Making gifts to grantor trusts can significantly enhance their benefit

Make an annual exclusion gift each year to a grantor trust for one beneficiary and transfer \$906,000 in 30 years. Make a gift of \$1 million (the gift tax applicable exclusion amount) to a separate grantor trust—and transfer a whopping \$5.3 million in the same time!

*Total Wealth Transferred**



*Median results, inflation-adjusted.

NOTE: All accounts are invested in globally diversified equities.

Based on Bernstein estimates of the range of returns for the applicable capital markets over the duration of the analysis. Data does not represent past performance and isn't a promise of actual future results or a range of results.

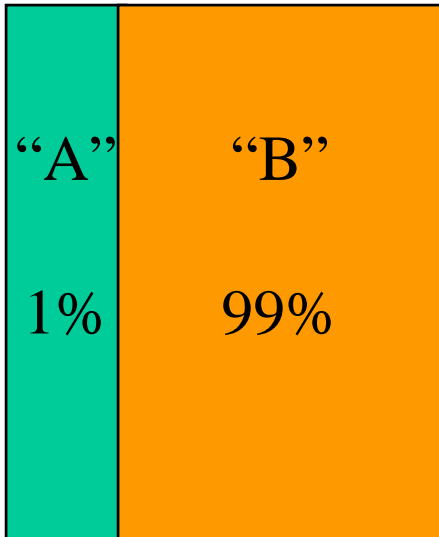
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Exhibit "B"

FLP ILLUSTRATION

FLP

**"B" Shares
Gifting**



\$2,000,000 Unified Credit



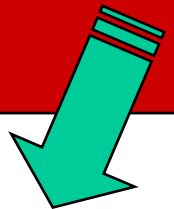
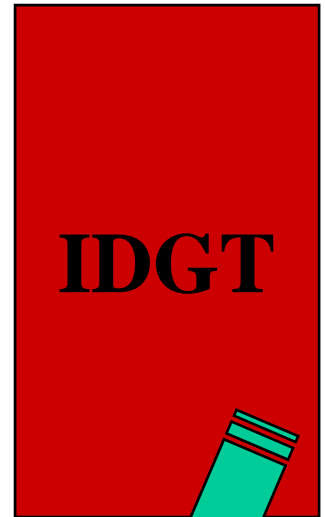
Annual Exclusion



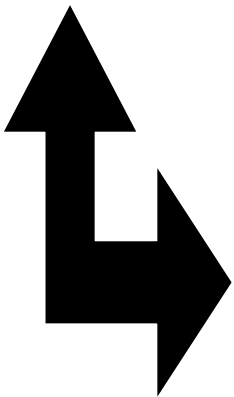
Sale to Trust



Promissory Note



Children and/or grandchildren
are the beneficiaries



"A" Shares retained by Parents

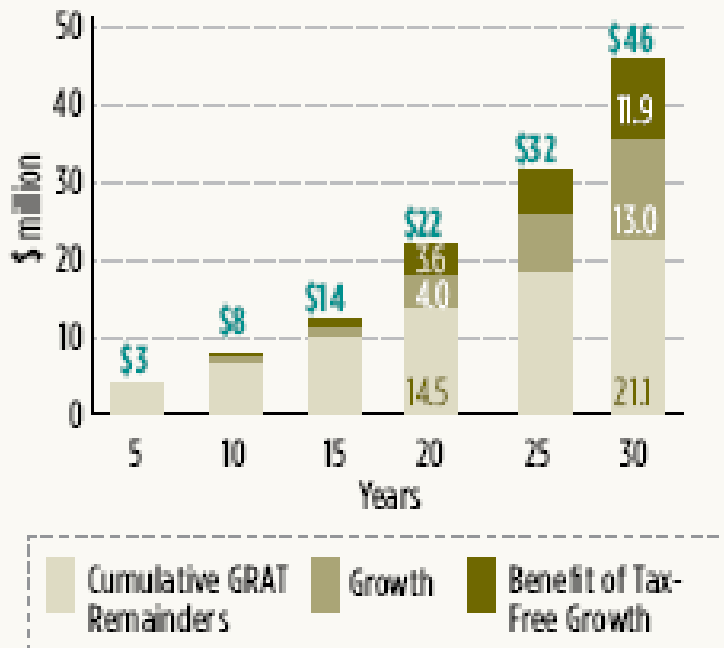
Exhibit “C”

A Powerful Combination

Combining rolling GRATs with a grantor trust can move a great deal of money out of an estate

The total wealth reflected in each bar comprises the aggregate value of the assets received from the GRATs, the subsequent growth of the assets, and the portion of that growth that is attributable to the grantor’s payment of the income taxes on the income from those assets.

Wealth Transfer to Grantor Trust for Children
(*\$10 million rolling GRATs with two-year term**)



* Median results, after inflation.

NOTE: All accounts are invested in globally diversified equities.

Based on Bernstein estimates of the range of returns for the applicable capital markets over the duration of the analysis. Data does not represent past performance and is not a promise of actual future results or a range of results.

— *AllianceBernstein*

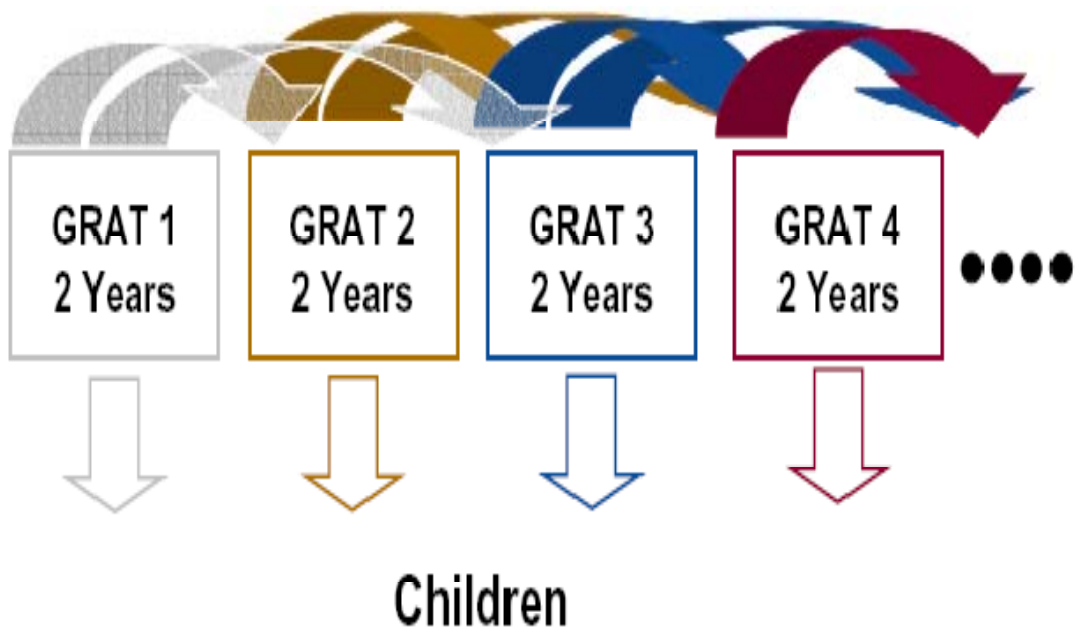
Exhibit “D”

Short-Term Rolling GRATs Offer an Alternative

Rolling GRATs

- Contribute initial assets to a two-year trust
- Annual payout is contributed to a new two-year GRAT every year
- Any appreciation above 7520 rate in each trust transfers tax-free to children*

Annuity Stream Annuity Stream Annuity Stream Annuity Stream

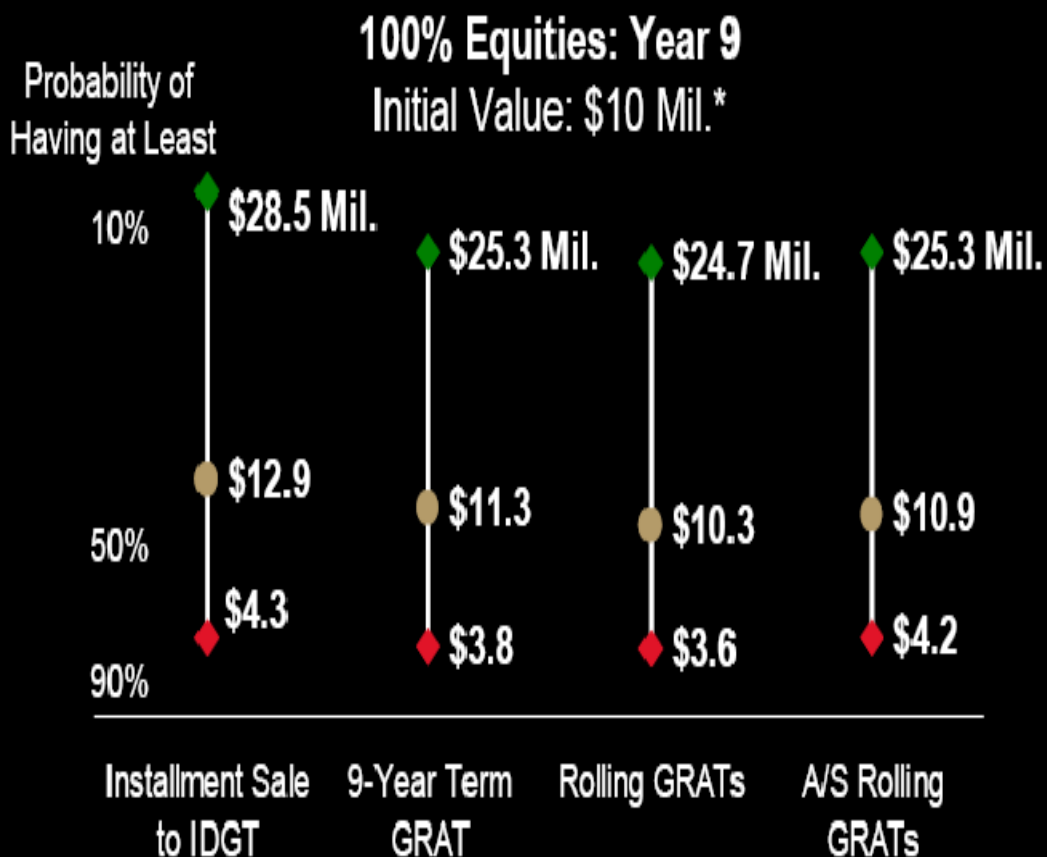


*Assuming the GRAT is “zeroed out” so that the present value of the annuity stream, discounted by the Section 7520 rate, equals the original contribution, and assuming grantor survives the term of the GRAT

Exhibit "E"

Wealth-Transfer Comparisons: Remainder to Children

Rolling GRAT strategies with no discount assumed are almost as effective as Installment Sales and long-term GRATs with a 30% valuation discount



*Based on Bernstein's estimates of the range of returns for the applicable capital markets over the next nine years. Data do not represent any past performance and are not a promise of actual future results. See Notes on Wealth Forecasting System at the end of this presentation for further details. 100% equities are allocated 35% to US Value, 35% to US Growth, 25% to Developed Foreign, 5% to Emerging Markets.