Trust Connection

Building Lasting Relationships for the Benefit of our Mutual Clients

TRUST NEWS AND INFORMATION
FROM YOUR TRUST REPRESENTATIVE OFFICE

Welcome to ***Trust Connection***, a regular communication from Valley National Trust Services.

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Trust Planning Techniques When Interest Rates are Low

Given the recent events in the world over the past few weeks and the unprecedented actions by the Federal Reserve to drastically lower interest rates to near zero in an attempt to stimulate a shaken global economy, now is the time to discuss the trust planning opportunities that exist for families when interest rates are low. Here's why…interest rates influence how wealth transfers are valued for tax reporting purposes. There are several estate planning strategies that can be especially beneficial in a low interest rate environment, including GRATs (Grantor Retained Annuity Trusts), IDGTs (Intentionally Defective Grantor Trusts), CLATs (Charitable Lead Annuity Trusts), Intrafamily Loans, and FLPs (Family Limited Partnerships). Let's examine a couple of these strategies.

GRATs - Grantor Retained Annuity Trusts

A GRAT is an irrevocable trust into which the grantor transfers assets and receives payment of a fixed dollar amount (the annuity) for a specified number of years. At the end of the GRAT term, the remaining assets in the trust, minus the interest, then pass tax-free to the designated beneficiaries.

The GRAT works great in a low interest rate environment because the IRS sets an interest rate at which they believe the GRAT will grow at the time the trust is established (in low interest periods these rates are low). The IRS does not consider the actual growth of the assets, so any apprecia-

tion above the IRS set interest rate is passed on to trust beneficiaries free of gift and estate taxes. The lower the interest rate, the larger the potential tax-free gift.

Another benefit of a GRAT is that it is a "grantor trust." The grantor is considered the owner of the trust from an income tax perspective, so all the income tax is paid by the grantor. The payment of income taxes by the grantor allows the trust assets to grow tax free, and, becomes a tax-free gift to the trust beneficiaries. A GRAT can be an especially great wealth transfer strategy when interest rates are low.

CLATS - Charitable Lead Annuity Trusts

CLATs are similar to GRATs, except, instead of the annuity payment being made to the grantor, it is made to a charity. Like the GRAT, the CLAT annuity payment must be paid at least annually for a specified number of years. At the end of the CLAT term, the remainder interest must be distributed to one or more non-charitable beneficiaries. These remainder beneficiaries are most often family members.

The assets contributed to a CLAT are assumed to grow at a rate equal to the IRS established rate in effect at the time of the transfer of asset into the trust. A CLAT works best in a low interest rate environment because any investment performance in excess of the hurdle rate passes tax-free to the family members at the expiration date of the CLAT. The lower the interest rate, the larger the potential tax-free transfer.

Another feature of a CLAT is that the grantor (donor) can take a charitable deduction on the value of the annuity payments paid to the charity. Only the calculated remaining assets when the CLAT terminates are subject to a gift tax. When a CLAT is structured to be zero at termination, there is little to no gift tax.

Based on what your client is trying to achieve, there are many trust planning options that can be employed when interest rates are low. This is just an overview of GRATs and CLATs. There are many more details and items to consider with each option. Please consult with estate planning attorneys and financial planning professionals to determine the path that is best for the families you serve.

About Trust Connection

As a Trust Representative Office of National Advisors Trust, we represent the largest federally-chartered trust company created by Registered Investment Advisors (RIAs). Our trust service model is built on the strength of the local support and responsiveness provided by you—the local estate planning professional, Valley National Advisers— the local and trusted investment advisor and National Advisors Trust serving as the trust administrator. This combined expertise allows us to excel in the services we provide delivering the best possible outcomes for our mutual clients.