CUMMINGS & LOCKWOOD LLC

HOW DOES THE GRAT WORK?

The tax advantage of this technique results from the way the taxable value of the gift to the GRAT is calculated. The value of the Donor's taxable gift is not the value of the assets transferred to the GRAT, but the current value of the beneficiaries' right to receive the assets remaining in the GRAT upon the end of the GRAT Term after payment to the Donor of the required annuity payments. The duration of the GRAT and the amount of the annuity payments are fixed to reduce the taxable gift to zero or a nominal amount. This form of GRAT is commonly called a "zeroed-out" GRAT.

If the total investment return of a GRAT exceeds the anticipated return based on the rate prescribed by the IRS for the month the GRAT is funded (the "7520 rate"), this "excess" investment return will pass gift and estate tax-free to the Donor's beneficiaries at the end of the GRAT. If the total investment return is less than the 7520 rate, no assets will remain to be transferred to the Donor's beneficiaries upon the expiration of the GRAT, but as long as the taxable gift upon funding the GRAT is zero, nothing will be lost other than the expense of establishing and administering the GRAT.