

[Date]

[Client Name]

[Client Address]

[City, State, Zip Code]

Re: Tax Implications of Your Grantor Retained Annuity Trust (GRAT)

Dear [Client Name],

This letter outlines the primary federal tax implications associated with the establishment and operation of your Grantor Retained Annuity Trust (GRAT).

1. Gift Tax Considerations

When you fund the GRAT, you are making a gift of the "remainder interest" to your beneficiaries. The value of this gift is calculated using the IRS Section 7520 interest rate. If the trust is structured as a "zeroed-out" GRAT, the value of the retained annuity equals the value of the assets transferred, resulting in little to no usage of your lifetime gift tax exemption.

2. Income Tax Status

For federal income tax purposes, a GRAT is typically classified as a "Grantor Trust." This means that you, as the Grantor, are responsible for reporting all items of income, gain, loss, and credit generated by the trust assets on your personal Form 1040. The trust itself does not pay separate income taxes.

3. Estate Tax Inclusion

To successfully remove the asset appreciation from your taxable estate, you must survive the designated term of the GRAT. If you pass away during the term, the assets remaining in the trust may be included in your gross estate for federal estate tax purposes.

4. Generation-Skipping Transfer (GST) Tax

GST exemption cannot be allocated to a GRAT until the end of the Estate Tax Inclusion Period (ETIP), which occurs when the trust term expires. Therefore, GRATs are generally not the preferred vehicle for direct long-term transfers to grandchildren.

5. Asset Basis

Assets remaining in the trust at the end of the term that pass to beneficiaries do not receive a "step-up" in basis at your death. The beneficiaries will take a carryover basis in the assets.

Please contact our office if you have any questions regarding these tax treatments.

Sincerely,

[Your Name/Firm Name]

[Title]