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Some of the Best Estate Planning Ideas We See Out There That I Have Not Already Talked About©

(That Also Have the Merit of Playing Havoc With Certain "Conventional Wisdom")

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Some of the Best GRAT Planning Ideas We See Out There (Pages 1 through 26 of the Paper)

Conventional Wisdom:

- "Using a short term GRAT to transfer a family limited partnership interest does not work;"
- "GRATs only work in good markets;" or
- "You can use the leverage of a GRAT for gift tax purposes, but you cannot use that leverage for generation-skipping purposes."

This "conventional wisdom," under the circumstances discussed below, is incorrect.

What is a GRAT:
(Pages 1 – 3 of the Paper)

- A GRAT (a grantor retained annuity trust) is an irrevocable trust to which the grantor transfers an asset in exchange for the right to receive a fixed amount annuity for a fixed number of fiscal years (the "Annuity Period").
- When the trust term expires, any GRAT balance remaining is transferred tax-free to a designated remainder beneficiary (*e.g.*, the grantor's issue or a "defective grantor trust" for the benefit of the issue).
- If a grantor makes a gift of property in trust to a member of the grantor's family while retaining an interest in such property, the taxable gift generally equals the fair market value of the gifted property without reduction for the fair market value of the retained interest.
- However, I.R.C. Section 2702 provides that for a gift of the remainder of a GRAT in which the grantor retains a "qualified interest", defined to include a guaranteed annuity, the taxable gift will be reduced by the present value of the qualified interest, as determined pursuant to a statutory rate determined under I.R.C. Section 7520(a)(2) (the "Statutory Rate").

What is a GRAT: (Continued)

- In general, the Statutory Rate requires an actuarial valuation under prescribed tables using an interest rate equal to 120 percent of the Federal midterm rate in effect for the month of the valuation.
- A grantor's ability to determine the size of the guaranteed annuity and the annuity period at the outset allows the GRAT to be constructed so that the present value of the grantor's retained interest approximately equals the value of the property placed in the GRAT, resulting in a "zeroed out" GRAT.
- Thus, a GRAT could be structured, where there is no, or a relatively modest, taxable gift.

Advantages of a GRAT
(Pages 4 – 9 of the Paper)

- Valuation advantages – annuity automatically adjusts on asset revaluation
- Grantor may pay for income taxes associated with GRAT gift tax-free
- Grantor may substitute assets of the GRAT income tax-free
- Synergy with other techniques
- Comparatively low hurdle rate
- High leverage
- Non-recourse risk to remaindermen

Disadvantages of a GRAT
(Pages 9 – 13 of the Paper)

- Financial reasons why a GRAT may not succeed:
  - We'll see below that a GRAT transfers value to the remainder beneficiaries when its assets are sufficiently volatile – that is, when the assets contributed have the potential for large swings in value.
  - When a client contributes an asset outright to a GRAT (financial engineers say the client is "long" the asset), the GRAT succeeds only if the asset appreciates above the 7520 rate. The pressure is on the client or the advisor to select just the right asset for the GRAT term.
  - Financial engineering expands the possibilities for successful GRAT.
- If a GRAT is not administered properly, the retained interest by the grantor may not be deemed to be a qualified interest:

Disadvantages of a GRAT (Continued)

- The *Atkinson* worry: The U.S. Court of Appeals for the Eleventh Circuit (*see Atkinson*, 309 F.3rd 1290 (11th Cir. 2002), cert denied, 540 U.S. 945)), has held that an inter vivos charitable remainder annuity trust's (CRAT's) failure to comply with the required annual payment regulations during the donor's lifetime resulted in complete loss of the charitable deduction. The Court found that the trust in question was not properly operated as a CRAT from its creation. Even though the subject CRAT prohibited the offending acts of administration, the Court held that the CRAT fails.
- In a similar fashion, the Internal Revenue Service could take the position that if the regulations under IRC Section 2702 are violated by the trustee of the GRAT's administrative practices, then the interest retained by the grantor will not be a qualified interest.

- The annuity amount must be paid annually.

Disadvantages of a GRAT (Continued)

- Paying the grantor in satisfaction of his retained annuity interest with hard to value assets may disqualify his retained interest from being a qualified interest, if the assets are valued improperly.
- The contribution of assets to the GRAT must be made at the exact point of the creation of the GRAT.
- The retained annuity interest is valued using the valuation principles under IRC Section 7520.
- A successful GRAT could regress to the mean by the end of the term of the GRAT.
- The GRAT may not satisfy a client's stewardship goals because the investments of the GRAT may have been too successful.
- The GST tax exemption may be difficult to leverage through the use of a GRAT.
- A GRAT will not be successful in transferring assets if the grantor does not survive until the end of the term of the GRAT.

Possible Structural Solutions to Address Certain Administrative and Certain Stewardship Disadvantages of a GRAT (Pages 13 – 14 of the Paper)

- Structural solutions to prevent the inadvertent additional contribution of assets to a GRAT:
  - When creating the GRAT, the grantor may wish to consider a provision that prohibits any additional contributions to the GRAT and if any additional contribution is made, a new GRAT must be created specifically to hold that contribution.
  - The grantor of the GRAT may wish to consider initially making the trust revocable. Once all assignments to the trust have been completed, the grantor could amend the trust to make it an irrevocable GRAT.
- Structural solutions to ensure that the annuity amount is always deemed to be paid on a timely basis:
  - The grantor of the GRAT may wish to consider a provision in the trust document that provides (pursuant to a formula) a portion of the trust that is equal to the Annuity Amount due to the grantor shall not be subject to the trust.

Possible Structural Solutions to Address Certain Administrative and Certain Stewardship Disadvantages of a GRAT (Continued)

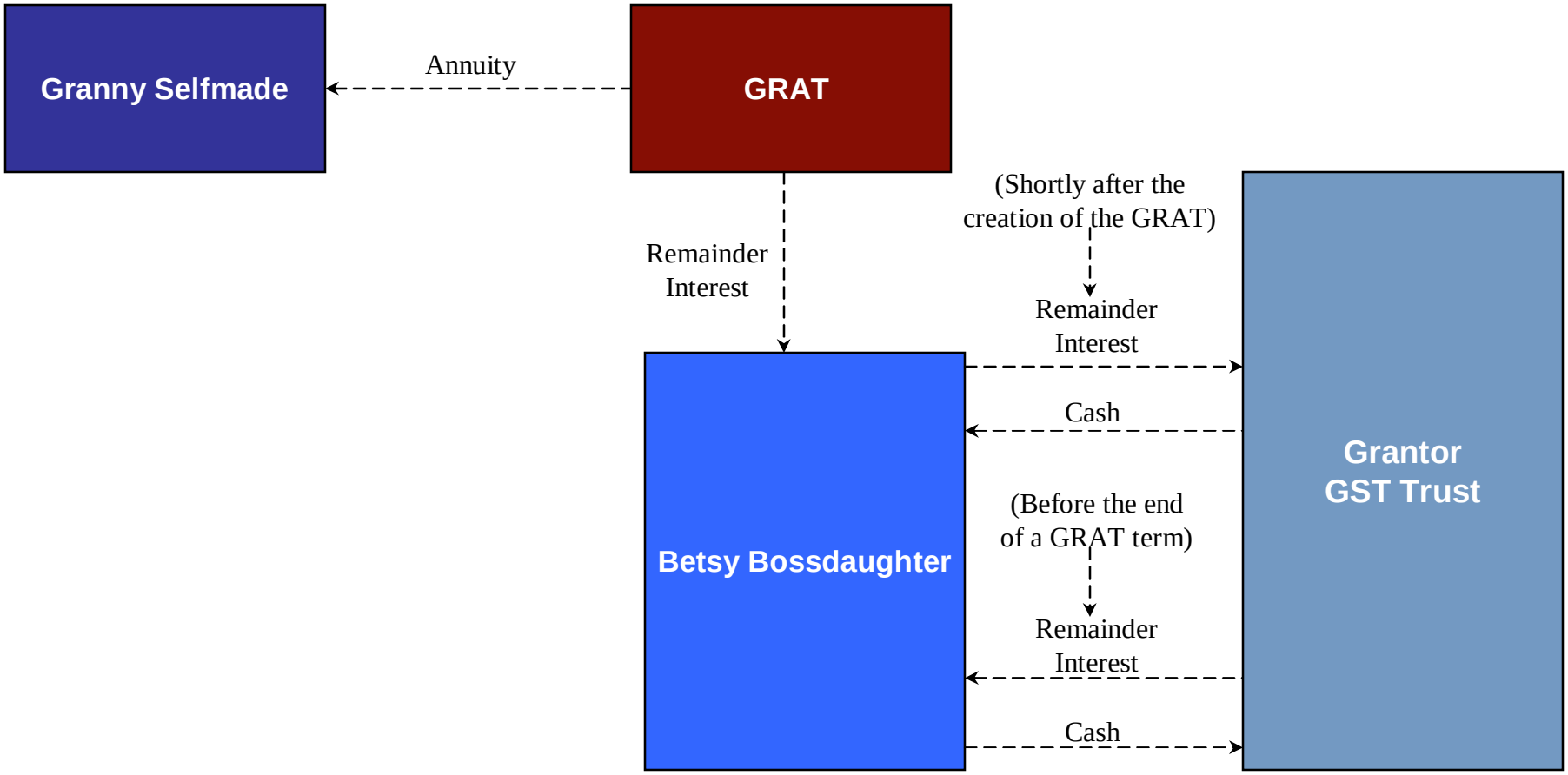
- If that portion remains in the hands of the trustee after the annuity payment date, the trustee shall hold such property only as a nominee or agent for the grantor.

- Structural solutions to limit the amount that is received by the remainderman of the GRAT:
  - A structural solution is to put a cap on the amount left in the trust for the benefit of his descendants at the end of the annuity term.
  - To the extent that the value of the assets of the GRAT on its termination exceeds that cap, there could be a provision that requires that excess to revert back to the donor.
  - Spouse could be named as a discretionary beneficiary and the spouse could be given a special power of appointment.

Possible Structural Solutions to Address Certain Administrative and Certain Stewardship Disadvantages of a GRAT (Continued)

- Solutions to reduce the mortality risk in GRATs:
  - The grantor could sell her retained annuity interest.
  - The grantor could create and fund an insurance trust that would have an "estate planning windfall" if the grantor dies before the GRAT term terminates.
  - The grantor could contribute mortgaged property to the GRAT and the leverage from the note payable to the grantor may not have the same IRC Section 2036 issue.
  - The grantor could purchase the remainder interest in a profitable GRAT from the remainder beneficiaries.
  - The GRAT could be created by the grantor in consideration of full and adequate consideration:
  - If the remainder interest of a GRAT is not created by gift, but is created for full consideration, IRC Section 2036 should not apply to the GRAT assets, if the grantor dies before the end of the term of the trust.

Example: Using the Leverage of a GRAT to Indirectly Profit a GST Trust – Non-Skip Person Exception



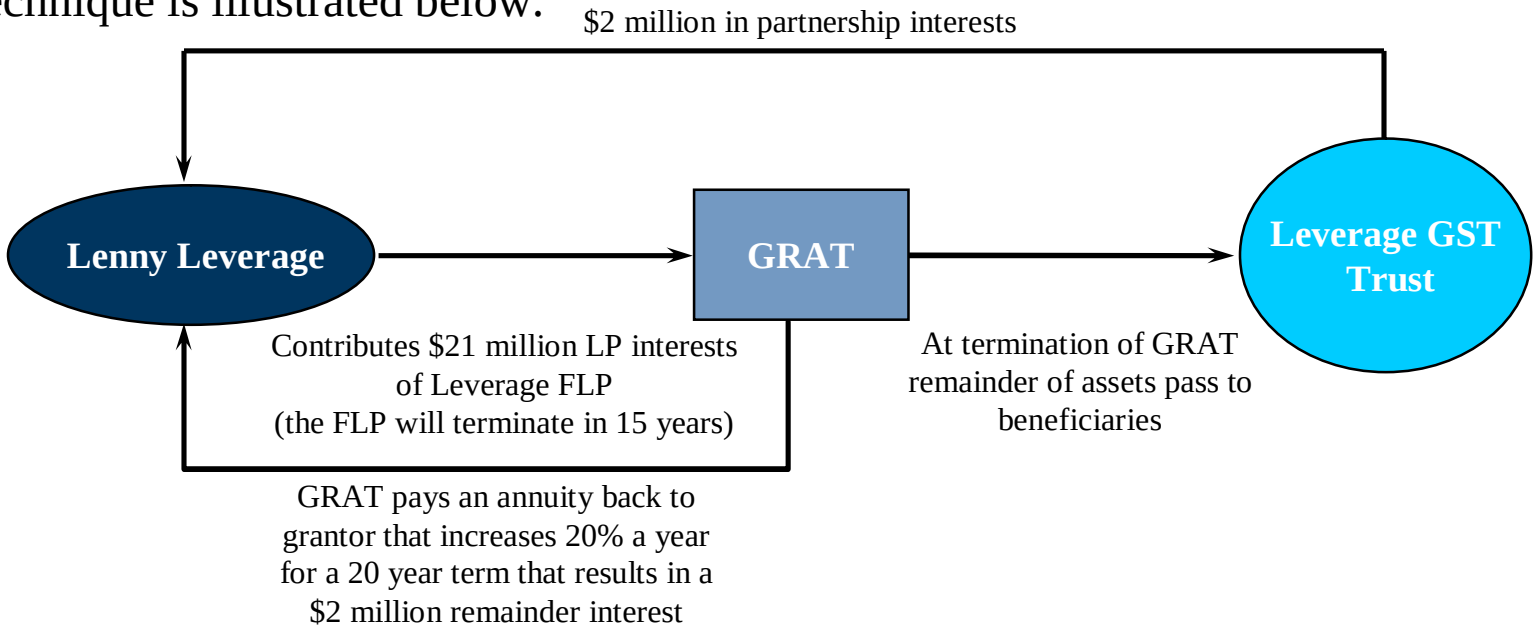
Using the Leverage of a GRAT to Indirectly Profit a GST Trust – Non-Skip Person Exception

- See private letter ruling 20010705. The private letter ruling's basic holding can be viewed as uniquely applicable to the charitable lead annuity trust. However, it is clear that the IRS will look for other opportunities to apply equitable doctrines in similar contexts. Stated differently, the ruling's reasoning could apply just as easily to a GRAT, if the reader substituted the phrase "ETIP rules" for "I.R.C. Section 2642(e)."
- Using the same logic, the Service could find that a gift by a GRAT remainderman is avoidance of the Congressional intent in enacting the ETIP rules. However, would the equitable doctrines inherent in the ruling apply to a sale by Betsy? It would appear that the answer should be no.
- In using a sale for full and adequate consideration, the issue is not whether Granny or Betsy is the transferor of the property that moves from the GRAT to the dynasty trust. The issue is whether there is an addition to the dynasty trust for GST purposes. There should not be an addition to the dynasty trust for GST purposes when Betsy transfers the remainder interest to the GST trust for full and adequate consideration and when Betsy buys the remainder interest back for full and adequate consideration.

Possible Solutions to Allow a GRAT to Leverage the GST Exemption: Creation of a GRAT For Full and Adequate Consideration

- Consider a GRAT that is created with a substantial remainder interest, however, because of a purchase of a remainder interest of the GRAT, there is not a gift. That is, instead of making a gift of the remainder interest, what if the grantor of a GRAT sold it for full and adequate consideration to a pre-existing trust? IRC Section 2036 inclusion does not apply if the grantor dies before the GRAT term ends, and as a consequence, the ETIP limitation may also not apply and the creation of the GRAT may not constitute a transfer to the GST trust.

The technique is illustrated below:



Possible Solutions to Allow a GRAT to Leverage the GST Exemption: Creation of a GRAT For Full and Adequate Consideration (Continued)

Please note the table below, which delineates the amount that is projected to be transferred to Lenny's children, grandchildren and great grandchildren pursuant to this technique in comparison to not doing any further planning with respect to the partnership. The table assumes Lenny's death at the end of year 20, Lenny consumes $100,000 a year with a 3% inflation rate, an 8% pre-tax rate of return with 2% being taxed at ordinary income rates (35%) and 6% at capital gains rates (15%, with a 30% turnover). The table assumes Lenny has $1,500,000 of assets outside the partnership. Assume that the partnership, at the time of the creation of the split purchase GRAT, has only 15 years remaining and that the valuation discount is 30%.

Technique	Leverage Children	Leverage GST Trust	Consumption – Direct Cost	Consumption – Investment Opportunity Cost	IRS – Income Tax	IRS – Investment Opportunity Cost	IRS – Estate Tax (at 45%)	Total
No Further Planning; Bequeaths Estate To Family	$55,282,583	$13,317,021	$2,687,037	$3,022,654	$20,916,430	$19,680,241	$45,231,204	$160,137,171
Hypothetical Integrated Income and Estate Tax Plan With a Partnership and GRAT; Bequeaths Estate To Family	$9,687,257	$98,772,116	$2,687,037	$3,022,654	$20,778,989	$17,263,179	$7,925,938	$160,137,171

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Possible Solutions to Allow a GRAT to Leverage the GST Exemption: Creation of a GRAT For Full and Adequate Consideration (Continued)

- The results are obviously very significant. Will this work? An argument can certainly be made that the creation of the split purchase GRAT is not subject to the ETIP rules and the creation of the GRAT does not constitute a transfer to the GST trust. If Lenny died during the 20 year term of the GRAT, the GRAT property will not be includible in his gross estate, only the value of the remaining annuity payments would be included. Alternatively, the GRAT annuity period could be set for the shorter of 20 years or the death of Lenny. Obviously, the GRAT annuity payment would have to be set at a higher amount in order to provide adequate and full consideration to Lenny. If Lenny died earlier than 20 years there would be significant income tax and estate tax advantages in structuring the GRAT term in that manner.
- There could be abusive situations where the remainder interest is very small and the logic of the *Wheeler*, *D'Ambrosio* and *Magnin* cases would not be applied.
- However, under the facts assumed under this case, the remainder interest is significant and would seem to be analogous to the remainderman values considered in the above Circuit Court cases.

Possible Solutions to Increase the Likelihood of a Successful GRAT Even When the Investment Results of a Client's Portfolio Are Flat or Decrease

Leveraged Reverse Freeze With a GRAT (Pages 26 – 38)

Use of a leveraged reverse freeze – consider the following example, which illustrates the potential of contributing a high yielding preferred partnership interest to a GRAT:

Ian and Inez Inverse Wish to Transfer $30,000,000
of Their Financial Assets to Their Children in the
Most Efficient Transfer Tax Manner Possible

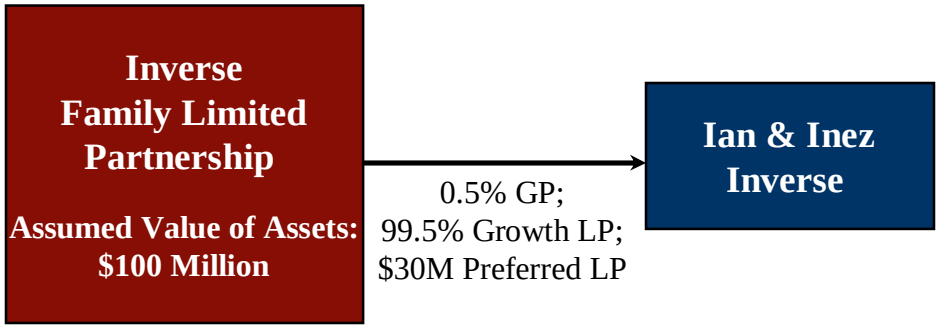
Ian and Inez Inverse own significant financial assets, $103,000,000. They are not fond of paying substantial gift taxes. Ian and Inez want their tax planner, Pam Planner, to devise a plan in which their consumption needs are addressed and in which their stewardship goals are met. Their stewardship goals are to give, within 10 years, $30,000,000 to trusts for their children and eventually give the rest of their estate to their favorite charitable causes.

Ian and Inez tell Pam that they are both in excellent health. Ian and Inez ask Pam to assume that the assets will earn 6% pre-tax, with 3% of the 6% being taxed at ordinary income rates and 3% being taxed at capital gains rates, with a 30% turnover in capital gains investments.

Ian and Inez desire for Pam to develop a plan in which there are minimum gift tax consequences and, which eliminates, as much as possible, their gift and/or estate taxes on their planned $30,000,000 gift to their children.

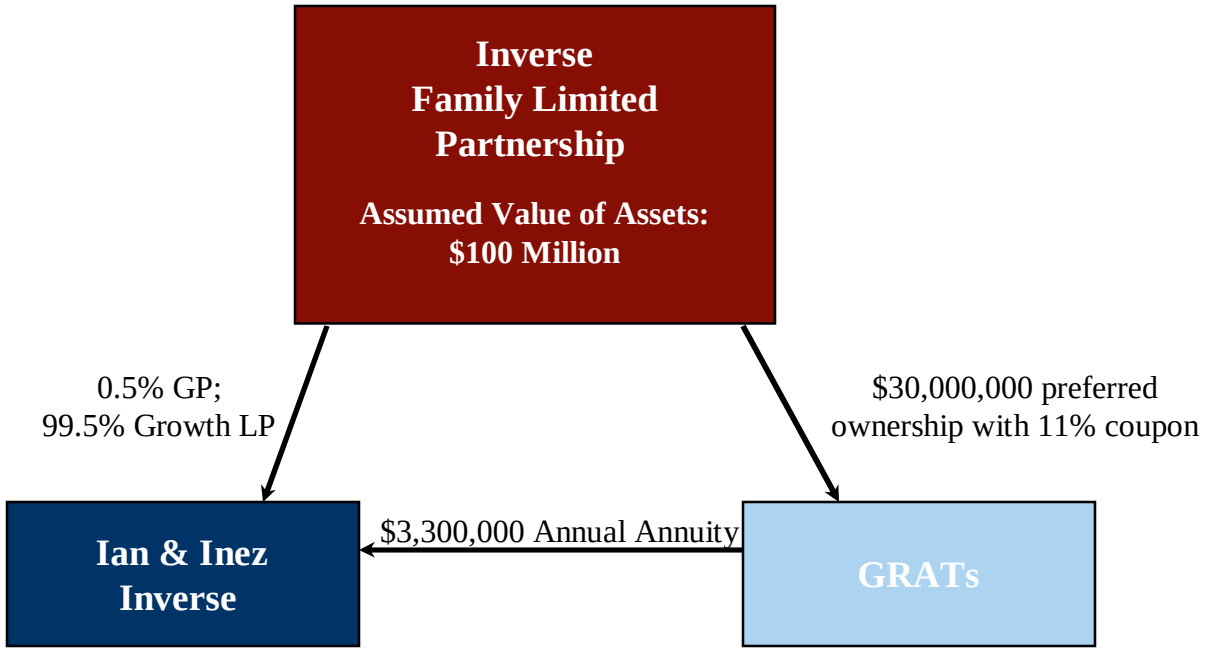
This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Leveraged Reverse Freeze With a GRAT
(Pages 26 – 38 of the Paper)



Partner	Ownership (%)
Ian & Inez Inverse	0.5% GP; 99.5% Growth LP; $30M Preferred LP

Leveraged Reverse Freeze With a GRAT (Continued)



- Assuming the partnership earns 3% to 4% before income taxes, there will be enough income to satisfy the preferred coupon of $3,300,000.
- Valuation advantage: IRS concedes in Rev. Rul. 83-120 preferred partnership interests should have a high coupon.

Leveraged Reverse Freeze With a GRAT (Continued)

- IRC Section 2036 advantage of a multi-economic class partnership: Strong legislative history suggests IRC Section 2036 should not apply to partnerships with significant preferred interests.
- The valuation rules of IRC Section 2701 should not apply, if one generation transfers the preferred partnership interests to the second generation.
- What is the comparative outcome under the proposed plan?
  - If Mr. and Mrs. Inverse create GRATs that last 10 years, with the payouts described above, the gift will be $2,135,460, assuming the IRC Section 7520 rate is 3.2%, even though trusts for their children will receive $30,000,000 of preferred partnership interests at the end of 10 years.
  - If the term of the GRAT is 11 years, assuming the IRC Section 7520 rate is 3.2%, the gift will be zero.

Leveraged Reverse Freeze With a GRAT (Continued)

- If the appraisers find that the rate of return on the preferred interests should be equal to 11.843% in order to support par value of the preferred interests, and the 10 year GRATs are created with $30,000,000 of preferred interest paying all of that coupon in satisfaction of the retained annuity, the GRATs will be near zeroed out GRATs.
- Thus, in each of these scenarios, Mr. and Mrs. Inverse could be in the position to receive substantial cash flows for a 10 year or 11 year period, and assuming the gift tax exemption that they each have is $1,000,000, they will each transfer preferred interests that are equal in value to over $30,000,000 to trusts for the benefit of their children by paying little or no gift taxes.
- All of this is accomplished, even though their investment portfolio only earns 4% to 5% annually, after taxes.

Financial Engineering With a GRAT
(Pages 38 – 62 of the Paper)

What is a Call Option?

- The buyer of a call option has the right to purchase stock from the seller of a call option at a certain price in the future (the "exercise price").
- The purchase price of a call (the "premium") is generally a portion of the value of the stock at the time the buyer purchases the call.
- If the stock price is at or above a specified value (the "target value") on a specified date (the "target date"), the buyer can purchase the stock from the seller of the call option at the exercise price.
- If the stock price is less than the target value on the target date, the buyer will not purchase the stock from the seller. That means that the buyer loses the premium paid for the call option to the seller.
- If the stock price is at or above the target value on the target date, the seller must sell the stock to the buyer for the exercise price (or could enter into a cash settlement). The seller keeps the premium and the exercise price, but the sum of those two is less than the stock's value on the target date.

Please note that options involve risk and are not suitable for all investors.

Simplified Call Option Example

When XYZ Company stock is $50 per share, the buyer of a call option pays the seller a $7 premium for the right to buy XYZ Company stock for $55 (the exercise price) at a future date.

Buyer's net worth increases: On the target date, the XYZ stock is trading at $65. The buyer will pay the seller the exercise price of $55 to get the stock. The seller will have the original call option premium of $7 and the exercise price of $55, but that is $3 less than the value of the XYZ Company stock. The buyer will have paid $62 (the $7 premium and the $55 exercise price) to own a $65 stock. The buyer's net worth increases by $3.

Seller's net worth increases: On the target date, the XYZ stock is trading at $52. The buyer will not pay $55 to purchase the stock, so the seller keeps the $7 premium. The seller's net worth increases by $7 and his stock is now trading $2 higher.

The most the buyer can lose is the $7 premium.

Theoretically, the seller can lose an unlimited amount if the price of XYZ Company skyrockets, unless the seller owns the same amount of stock in XYZ Company (a so-called "covered call").

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What is a Call Spread Option?

- When we described a call option on the previous page, we looked at the buyer's perspective. But the seller might do more than just sell a call option. The seller might buy a call option too.
- In a call spread option, the seller invests a portion (or all) of the purchase price the buyer paid for the call option to buy a different call option. This call option that the seller purchases for herself has a target value below the target value of the call option she sold.
- On the target date, the seller makes money if the stock price is between the higher value of the call option the seller sold and the lower target value of the call option the seller purchased.
- It's important to know that a call spread option limits losses, but it also limits gains.

Please note that options involve risk and are not suitable for all investors.

Simplified Call Spread Option Example

When XYZ Company stock is $50 per share, the buyer of a call option pays the seller a $7 premium for the right to buy XYZ Company stock for $55 (the exercise price) at a future date and that buyer then sells a call option for $3 to another buyer for the right to buy XYZ Company stock for $65 at the same future date.

Buyer's net worth increases: On the target date, the XYZ stock is trading at $65. Assume the call spread contract is cash settled. The buyer will gross $10 on his $4 net investment.

The most the buyer of the call spread option can lose is the $4 net premium.

Theoretically, the seller of a call spread option, under the above assumed facts, cannot lose more than $6 after the net premium received is considered.

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What is a Put Option?

- The buyer of a put option has the right to sell stock to the seller of a put option at a certain price in the future (the "exercise price").
- The purchase price of a put (the "premium") is generally a portion of the value of the stock at the time the buyer purchases the put.
- If the stock price is at or below a specified value (the "target value") on a specified date (the "target date"), the buyer of the put option can require the seller to purchase the stock from the buyer at the exercise price.
- If the stock price is more than the target value on the target date, the seller does not have to purchase the stock from the buyer. That means that the buyer loses the premium paid for the put option to the seller.
- If the stock price falls to target value or below on the target date, the seller must purchase the stock from the buyer for the exercise price or settle the difference in value for cash.

Please note that options involve risk and are not suitable for all investors.

Simplified Put Option Example

When XYZ Company stock is $50 per share, the buyer of a put option pays the seller $7 (the "premium") for the right to sell XYZ Company stock to the seller for $40 (the exercise price) at a future date.

Buyer's net worth increases: On the target date, the XYZ stock is trading at $30. The buyer will sell the stock to the seller of the put option for the $40 exercise price. The buyer of the put option will have $40 from the seller, less the $7 premium previously paid. The buyer's stock was only worth $30 when the buyer exercised the put option, so the buyer nets $33 ($40 stock price less the $7 premium) and the buyer's net worth increases by $3.

Seller's net worth increases: On the target date, the XYZ stock is trading at $45. The buyer won't sell the stock to the seller of the put option for $40, so the seller keeps the $7 premium. The seller's net worth increases by $7.

The most the buyer of the put option can lose is the $7 premium.

Theoretically, the seller can lose the entire $40 exercise price of the stock if the stock price falls to zero, but the seller will still get to keep the $7 premium (for a $33 potential loss).

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What is a Put Spread Option?

- When we described a put option on the previous page, we looked at the buyer's perspective. But the seller might do more than just sell a put option. The seller might buy a put option too.
- In a put spread option, the seller invests a portion (or all) of the purchase price the buyer paid for the put option to buy a different put option. This put option that the seller purchases for herself has a target value above the target value of the put option she sold.
- On the target date, the seller makes money if the stock price is between the lower value of the put option the seller sold and the higher target value of the put option the seller purchased.
- It's important to know that a put spread option limits losses, but it also limits gains.

Please note that options involve risk and are not suitable for all investors.

Simplified Put Spread Option Example

When XYZ Company stock is $50 per share, the buyer of a put option pays the seller $7 (the "premium") for the right to sell XYZ Company stock to the seller for $40 (the exercise price) at a future date and that buyer then sells a put option for $3 to another buyer for the right to sell XYZ Company stock for $30 at the same future date.

Buyer's net worth increases: On the target date, the XYZ stock is trading at $30. Assume the call spread contract is cash settled. The buyer will gross $10 on his $4 net investment.

The most the buyer of the put spread option can lose is the $4 net premium.

Theoretically, the seller of a put spread option, under the above assumed facts, cannot lose more than $6 after net premium received is considered.

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Financial Engineering With a GRAT: Purchasing Derivatives From an Investment Bank Solely for the Purpose of Using That Investment for Contribution to a GRAT (Page 41 of the Paper)

- Use of derivatives purchased from an investment bank solely for the purpose of using that investment for contribution to a GRAT:
  - The friend of the GRAT technique is a volatile investment.
  - Put spread options and call spread options are very leveraged financial instruments.
  - Very small movements in the underlying asset on which the derivative is based can produce significant gains for any GRAT to which the derivative is contributed.
  - On the other hand, if the asset on which the derivative is based moves in the opposite direction, the derivative could expire worthless.
  - One way to ameliorate the risk of purchasing a volatile derivative is to also purchase a derivative that will similarly profit if the underlying asset moves in the opposite direction.

Financial Engineering With a GRAT (Continued)

- The safest way to use the power of the offsetting derivative transactions and have them recognized with use of the GRAT technique is to use one GRAT.
- The donor could keep the potential profit from one of the derivatives with the other derivative being contributed to a GRAT.
- If the donor keeps the derivative in which there is greater potential profit because of a greater investment in that derivative, one of two outcomes should be present: either (i) the client makes a small profit from the two derivative purchases, which more than pays for the legal cost of creating the unsuccessful GRAT or (ii) the client and his family collectively lose a modest amount of money on the derivative purchases, but the economic loss is more than offset by the gift tax savings of the transfer to the client's family with the successful GRAT.

Financial Engineering With a GRAT: Client Purchases Derivatives From an Investment Bank for Reasons Independent of Estate Planning (Pages 41 – 47 of the Paper)

- The creation of a GRAT or GRATs when a client is purchasing derivatives for reasons independent of estate planning increases the attractiveness of using derivatives:
  - Of course, many clients have a strong view about the direction of the value of their stock and/or would like to hedge or partially hedge the value of their stock and they use "cashless" derivatives to implement their views.
  - One derivative strategy that clients use when they have a strong view that their stock will increase, and if it does increase they are prepared to sell their stock, is the Enhanced Price Selling Strategy ("EPSS"):
    - This derivative strategy involves a "cashless" purchase of one at the money call.
    - The purchase is funded by a sale of two out of the money calls.
      - For instance, two 53 week out of the money (e.g., 27.00% above current market price) calls are sold.
      - The proceeds of that sale are used to purchase one 53 week at the money call.

Financial Engineering With a GRAT (Continued)

- One derivative strategy that clients use when they wish to hedge their stock and achieve a significant return within a range is the so-called "TWIN-WIN" strategy:
  - This derivative strategy involves a "cashless" purchase of one at the money call and two modified at the money puts.
  - The purchases are funded by a sale of two out of the money calls.
    - For instance, two 13 month out of the money (e.g., 23.50% above current market price) calls are sold.
    - The proceeds of that sale are used to purchase one 13 month at the money call and two 13 month at the money puts. However, the puts are designed to have no value if the stock declines by more than 25%.

Financial Engineering With a GRAT (Continued)

These strategies and their inter-relationship with the GRAT technique may perhaps be best illustrated with an example:

Dede Derivative Wishes to Enhance and Hedge the Return
of Her Stock and Also Wishes to Engage in Estate Planning

Dede Derivative owns Dow Chemical stock. On February 6, 2009, she decides to engage in both the EPSS strategy and the Twin-Win strategy. Dede also wishes to engage in estate planning using the GRAT technique. Dow is priced at $10.88 on that date and the statutory rate for GRATs is at 2%.

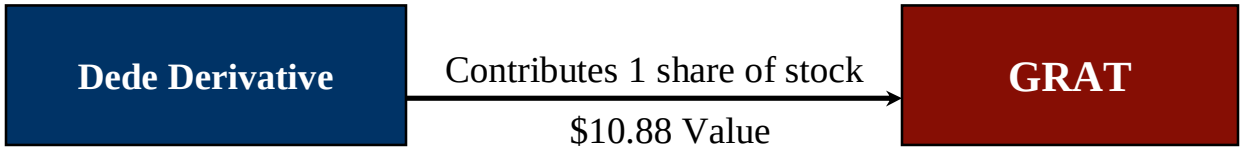
Thirteen month European style at-the-money calls will cost $2.94. An out-of-the-money 13 month European style call with an upper call strike of $13.82 will sell for $1.47 or two such calls will sell for $2.94. Two 13 month European style at-the-money puts cost $0.16 that would protect the value of the stock until it decreased below $8.16 (a 25% drop in the value of the stock). Two 13 month European style out-of-the-money calls with an upper call strike at $13.44 would sell for $3.10 (enough to pay for one at-the-money call and two modified at-the-money puts).

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

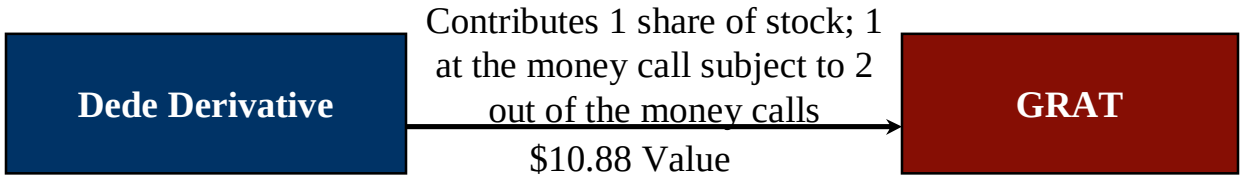
Financial Engineering With a GRAT (Continued)

Assuming Dede is contemplating for financial reasons the EPSS strategy for part of her stock, Dede's attorney, Dan Devine, designs three GRAT strategies for Dede to consider and compare, which are illustrated below:

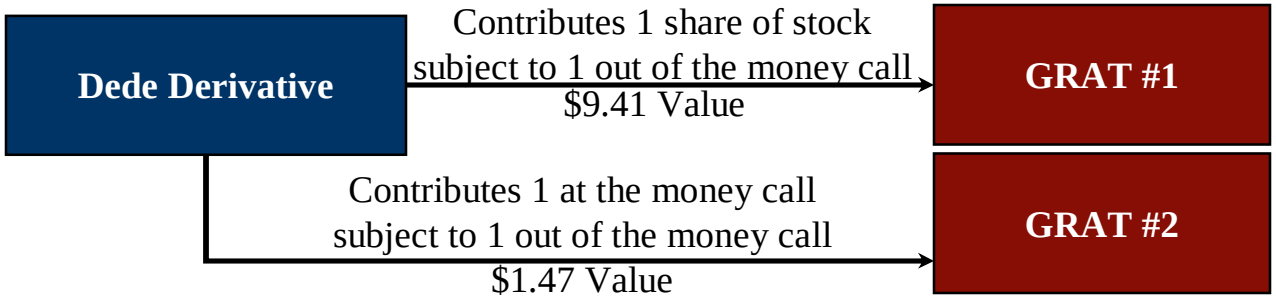
Strategy #1: Conventional GRAT funded with stock:



Strategy #2: GRAT funded with stock and EPSS strategy:



Strategy #3: 2-GRAT strategy (GRAT #1 – stock subject to call; GRAT #2 – call spread):



Financial Engineering With a GRAT (Continued)

The results of the three strategies, with respect to certain assumed stock prices in 13 months, are delineated in the table below:

Stock Value	Percentage Increase or Decrease in Value of Stock	Percentage of Beginning GRAT Assets to Remainderman at the End of One Year		
		Strategy #1	Strategy #2	Strategy #3
$9.38	-13.79%	0.00%	0.00%	0.00%
$9.63	-11.49%	0.00%	0.00%	0.28%
$10.88	0.00%	0.00%	0.00%	11.77%
$11.13	2.30%	0.30%	2.60%	14.07%
$12.38	13.79%	11.79%	25.57%	25.57%
$13.88	27.57%	25.57%	52.00%	52.00%
$16.63	52.85%	50.85%	52.00%	52.00%
$16.88	55.15%	53.15%	52.00%	52.00%

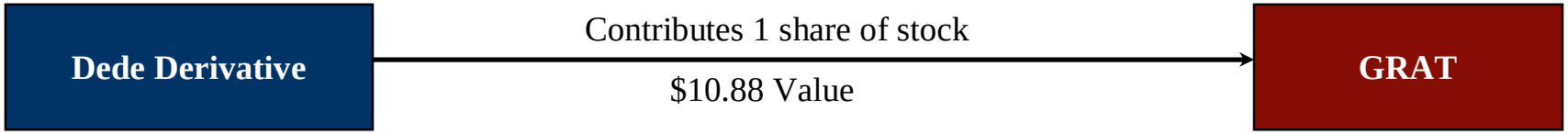
Strategy #1: Conventional GRAT Funded With Stock
Strategy #2: GRAT Funded With Stock and EPSS Strategy
Strategy #3: 2-GRAT Strategy (GRAT #1 - Stock Subject to Call; GRAT #2 - Call Spread)

This material is based on the assumptions stated herein. In the event any of the assumptions used do not prove to be true, results are likely to vary substantially from the examples shown herein. These examples are for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown. Simulated, modeled, or hypothetical performance results have certain inherent limitations. Simulated results are hypothetical and do not represent actual trading, and thus may not reflect material economic and market factors, such as liquidity constraints, that may have had an impact on actual decision-making. Simulated results are also achieved through retroactive application of a model designed with the benefit of hindsight.

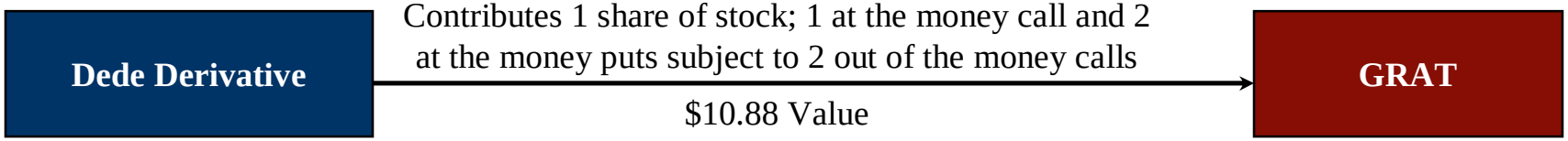
Financial Engineering With a GRAT (Continued)

Assuming Dede is also contemplating, for financial reasons for part of her stock, the Twin-Win derivative strategies, Dede's attorney, Dan Devine, also designs three GRAT strategies for Dede to consider and compare, which are illustrated below:

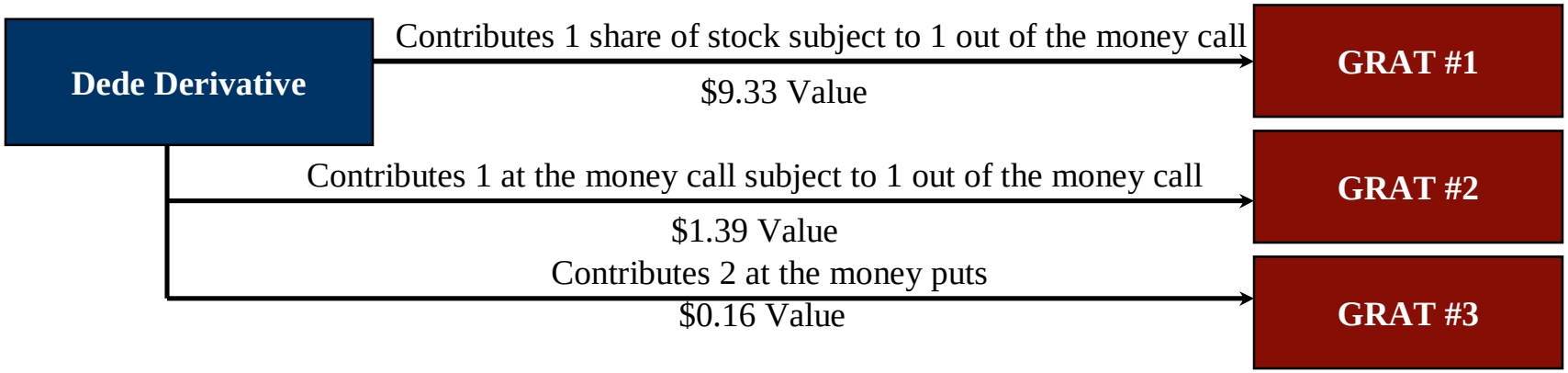
Strategy #1: Conventional GRAT funded with stock:



Strategy #2: GRAT funded with stock and Twin-Win derivatives:



Strategy #3: 3-GRAT strategy (GRAT #1 – stock subject to call; GRAT #2 – call spread; GRAT #3 – 2 puts):



Financial Engineering With a GRAT (Continued)

The results of the three strategies, with respect to certain assumed stock prices in 13 months, are delineated in the table below:

Stock Value	Percentage Increase or Decrease in Value of Stock	Percentage of Beginning GRAT Assets to Remainderman at the End of One Year		
		Strategy #1	Strategy #2	Strategy #3
$8.13	-25.28%	0.00%	0.00%	0.00%
$8.38	-22.98%	0.00%	20.98%	44.43%
$10.63	-2.30%	0.00%	0.30%	13.30%
$10.88	0.00%	0.00%	0.00%	12.54%
$11.13	2.30%	0.30%	2.60%	14.83%
$13.38	22.98%	20.98%	43.96%	45.49%
$13.63	25.28%	23.28%	45.00%	46.53%
$16.13	48.25%	46.25%	45.00%	46.53%
$16.38	50.55%	48.55%	45.00%	46.53%

Strategy #1: Conventional GRAT Funded With Stock

Strategy #2: GRAT Funded With Stock and Twin-Win Derivatives

Strategy #3: 3-GRAT Strategy (GRAT #1 - Stock Subject to Call; GRAT #2 - Call Spread; GRAT #3 - 2 Puts)

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Using Private Intra-Family Derivatives and GRATs to Hedge Grantor Trust Investments and to Transfer Wealth (Pages 47 – 50 of the Paper)

Example: A Trust Wishes to Hedge its ETF Investment By Entering Into a Twin-Win Derivative With its Grantor

Tom Trustee enters into a cashless derivative with Connie Counterparty who is the grantor of the trust and Connie contributes her position to a GRAT.

Tom Trustee is trustee of a grantor trust that was created many years ago by Connie Counterparty. The trust has a significant position in an ETF that mimics the S&P 500 stock index. On March 2, 2009, Tom decides to hedge the ETF position. Tom approaches a big investment bank and sells two out of the money calls with respect to his S&P 500 index ETF that are 13% out of the money. These two call positions are a 53 week European style options. The proceeds of the sale of those two out of the money call positions are then utilized to buy one at the money call position that is also a 53 week option and two knock out puts that protect the ETF for any decrease that does not exceed 20% of the position of the ETF in 53 weeks. Thus, Tom is in a position to enjoy a $2.00 profit for every dollar increase in the value of the ETF position until it increases more than 13% and will enjoy $1.00 increase every time the ETF position decreases by $1.00 until it decreases by more than 20%. Tom will not regret the trade unless the stock index grows by more than 26% in the 53 week period.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using Private Intra-Family Derivatives and GRATs to Hedge Grantor Trust Investments and to Transfer Wealth (Continued)

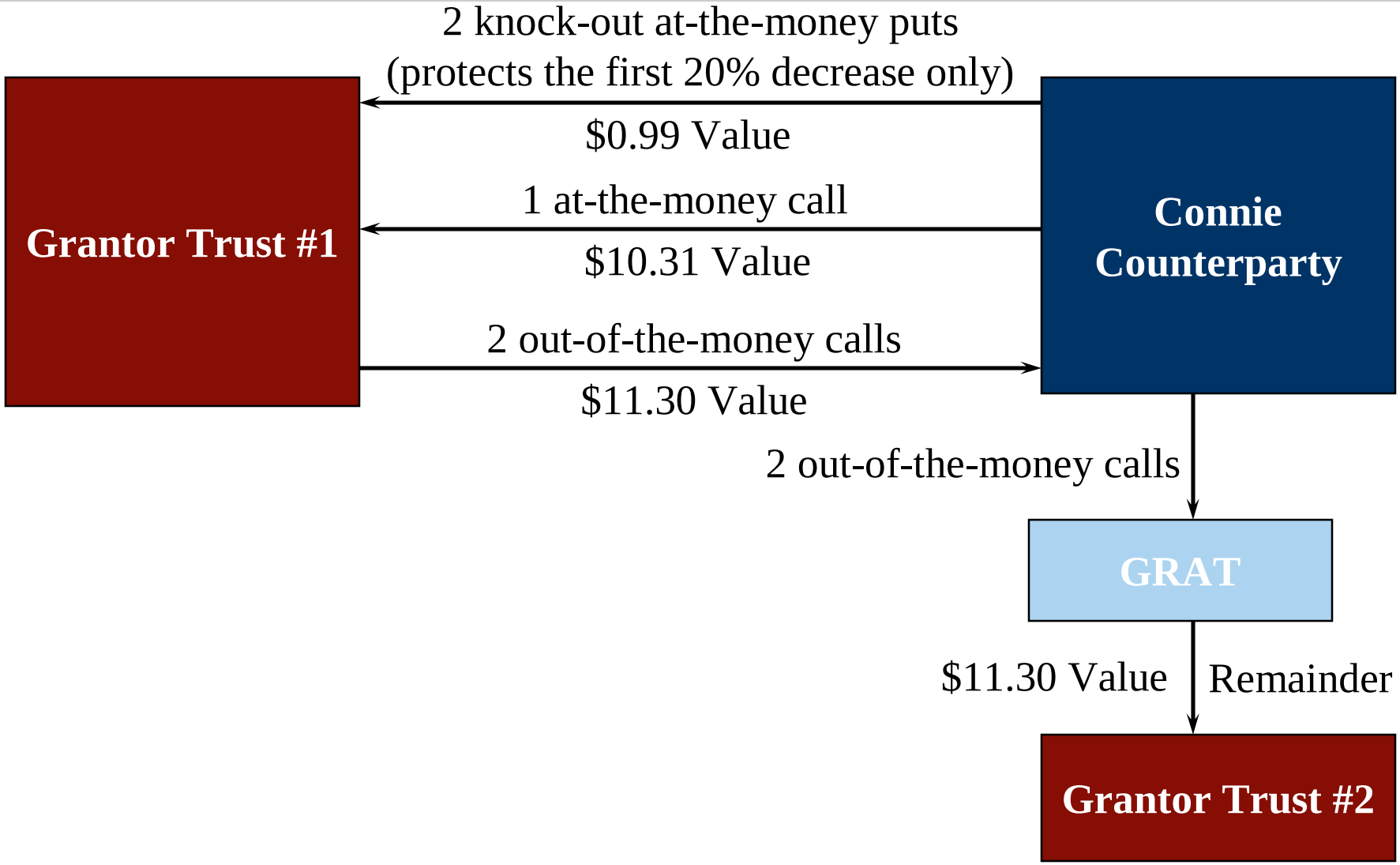
Connie Counterparty learns about the trade that Tom Trustee is entering into with the investment bank. Connie suggests to Tom that she would like to do the same trade with Tom. That is, Connie will purchase two out of the money call positions from Tom, as trustee, and Tom, as trustee, can use those proceeds to buy from her at the money call position and two knock out puts. All of the positions with Connie will also be 53 week options.

The ETF simulating the S&P 500 on March 2, 2009 is worth $70.60. The sale of two out of the money call positions that are 13% above that $70.60 price (or $79.78) will bring to Tom $11.30 for each share of the ETF. That $11.30 can be redeployed to buy one at the money call, which is worth $10.31 and two at the money knock out puts, which will protect the first 20% of downside of the ETF (the downside knock out level is $56.48). The knock out at the money puts will cost 99¢.

After Connie enters into the transaction with Tom, she decides to transfer her two out of the money call positions to a new GRAT. The GRAT could have as it remainderman a different grantor trust (Grantor Trust #2) with different provisions.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

The Proposed Transaction With Connie Counterparty is Graphically Demonstrated Below



The Potential Outcomes of the Proposed Transaction With Connie Counterparty Are Shown In the Chart Below

Numeric Summary Comparison of Results from the Perspective of Connie Counterparty's Family

Assumptions:		Status Quo with Grantor Trust Holding One Share of ETF		Hypothetical Plan With Grantor Trust Holding Derivatives Strategy and a GRAT Funded with 2 Out-of-the-Money Calls		
Estimated ETF Value	**Percentage Increase or Decrease in Value of ETF**	Estimated Profit/(Loss) Realized at the End of One Year Grantor Trust (Holding 1 Share of ETF)	**ESTIMATED TOTAL ASSETS TO BENEFICIARIES** **Trust Total ($)**	Estimated Profit/(Loss) Realized at the End of One Year Grantor Trust #1 (Derivatives Grantor Trust)	Estimated Profit/(Loss) Realized at the End of One Year Grantor Trust #2 (2 OTM Call GRAT Beneficiary)	**ESTIMATED TOTAL ASSETS TO BENEFICIARIES** **Trust Total ($)**
$56.10	-20.54%	($14.50)	**$56.10**	($14.50)	$0.00	**$56.10**
$56.60	-19.83%	($14.00)	**$56.60**	$14.00	$0.00	**$84.60**
$70.10	-0.71%	($0.50)	**$70.10**	$0.50	$0.00	**$71.10**
$70.60	0.00%	$0.00	**$70.60**	$0.00	$0.00	**$70.60**
$71.10	0.71%	$0.50	**$71.10**	$1.00	$0.00	**$71.60**
$79.60	12.75%	$9.00	**$79.60**	$18.00	$0.00	**$88.60**
$80.10	13.46%	$9.50	**$80.10**	$18.36	$0.00	**$88.96**
$85.60	21.25%	$15.00	**$85.60**	$18.36	$0.08	**$89.03**
$89.10	26.20%	$18.50	**$89.10**	$18.36	$7.08	**$96.03**
$91.10	29.04%	$20.50	**$91.10**	$18.36	$11.08	**$100.03**
$91.60	29.75%	$21.00	**$91.60**	$18.36	$12.08	**$101.03**
$94.10	33.29%	$23.50	**$94.10**	$18.36	$17.08	**$106.03**
$94.60	33.99%	$24.00	**$94.60**	$18.36	$18.08	**$107.03**
$111.60	58.07%	$41.00	**$111.60**	$18.36	$52.08	**$141.03**

* This derivative strategy involves a "cashless" purchase of one at the money call and two modified at the money puts. The purchases are funded by a sale of two out of the money calls. More specifically, two 53 week out of the money (13% above current market price) calls are sold. The proceeds of that sale are used to purchase one 53 week at the money call and two 53 week at the money puts. However, the puts are designed to have no value if the stock declines by more than 20%.

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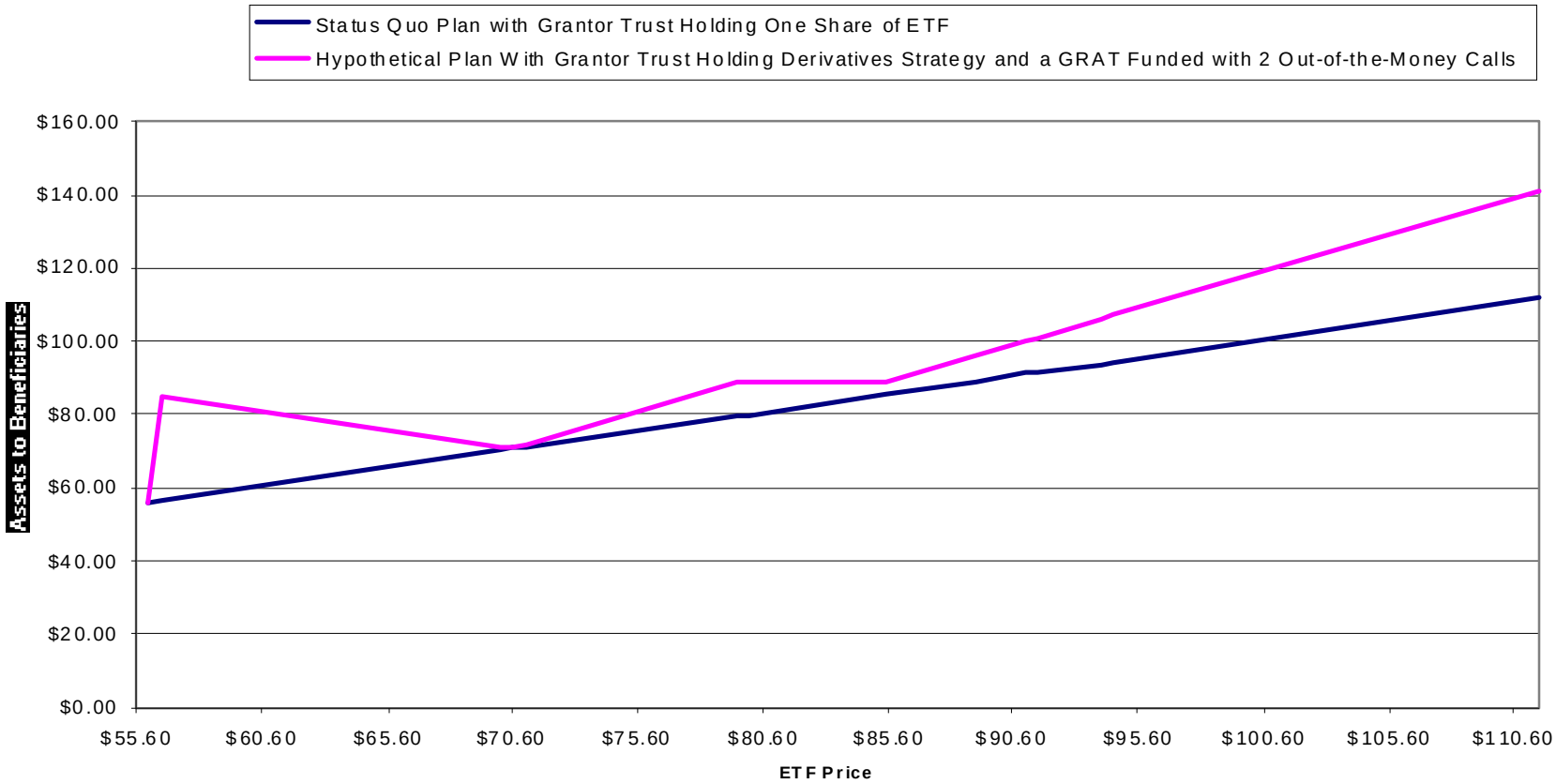
The Potential Outcomes of the Proposed Transaction With Connie Counterparty Are Shown In the Diagram Below

Graphic Summary Comparison of Results from the Perspective of Connie Counterparty's Family



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Example: Grantor of GRAT Enhances the Likelihood of Exceeding the Statutory Rate By Contributing a Private Derivative to a GRAT, Which is the Result of a Private Intra-Family Transaction (Pages 50 – 62 of the Paper)

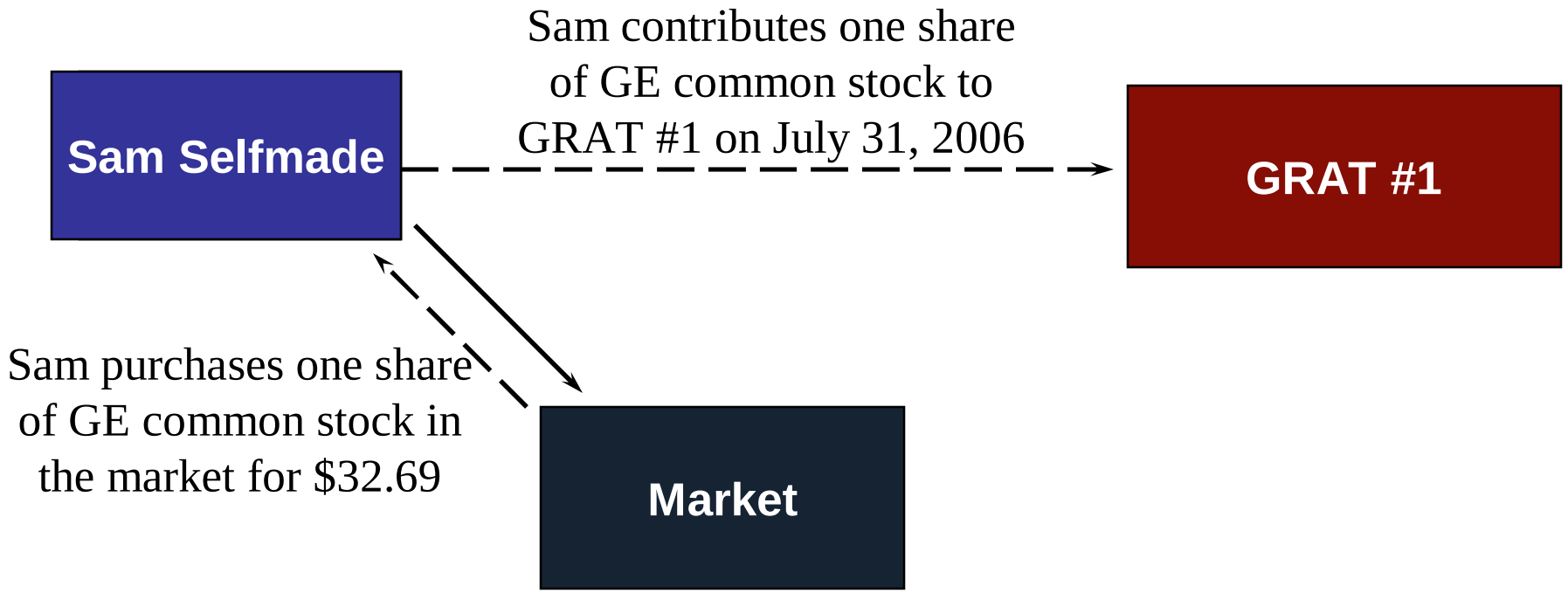
Many years ago, Sam Selfmade's company merged with General Electric. Sam received General Electric stock as a result of that merger. In 2005, Sam, with his wife Sally and their children put some of their General Electric stock in a family limited partnership. Sam and Sally still own a significant part of their General Electric stock outside of the partnership.

Sam Selfmade, on July 31, 2006, wishes to compare over a one year period the possible results from entering into a variety of private derivative transactions involving GE stock with either his spouse, Sally Selfmade, or a marital deduction trust he created for her benefit, acting as the financial counterparty, and contributing his derivative to a GRAT.

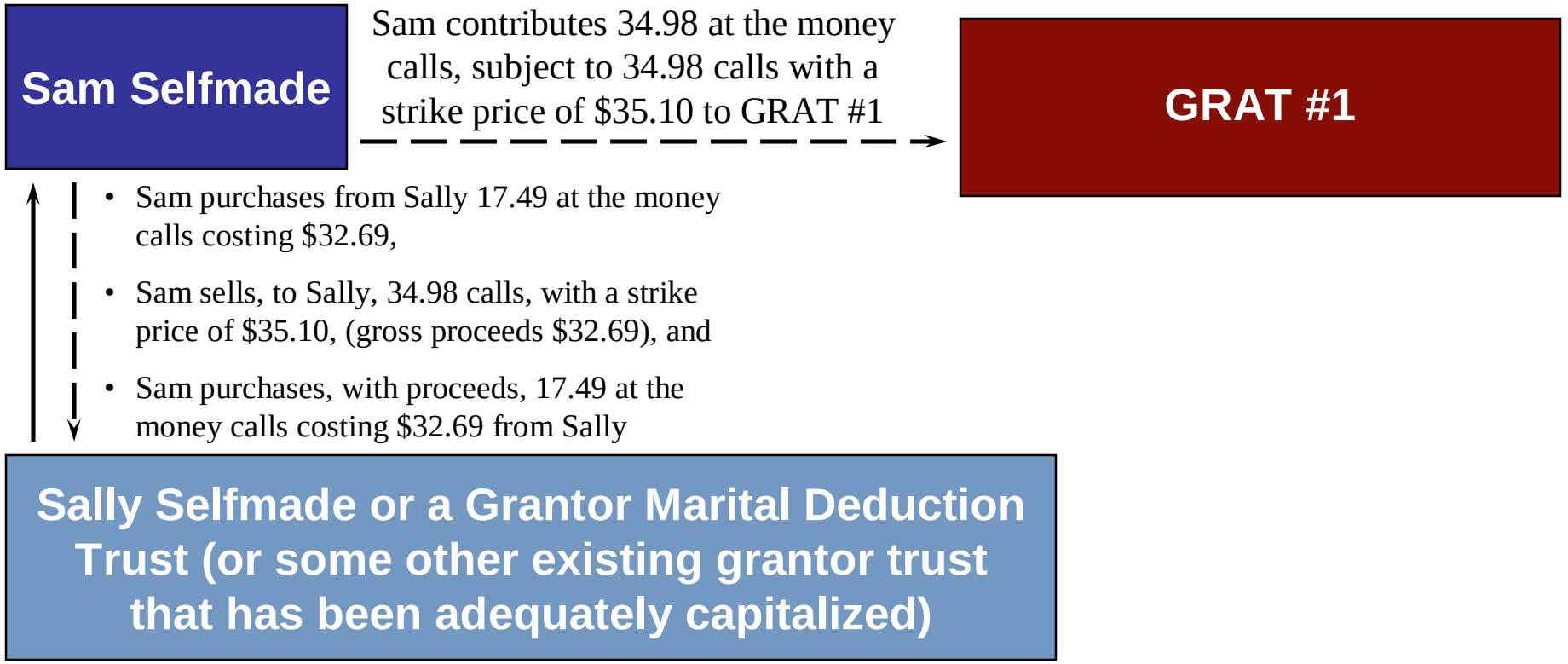
Sam wishes to compare the various results if he simply contributes his GE stock to a traditional GRAT.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Transaction 1 (Traditional Investment GRAT, No Options): Sam Selfmade Purchases a Share of GE Common Stock for $32.69 and Contributes it to GRAT #1



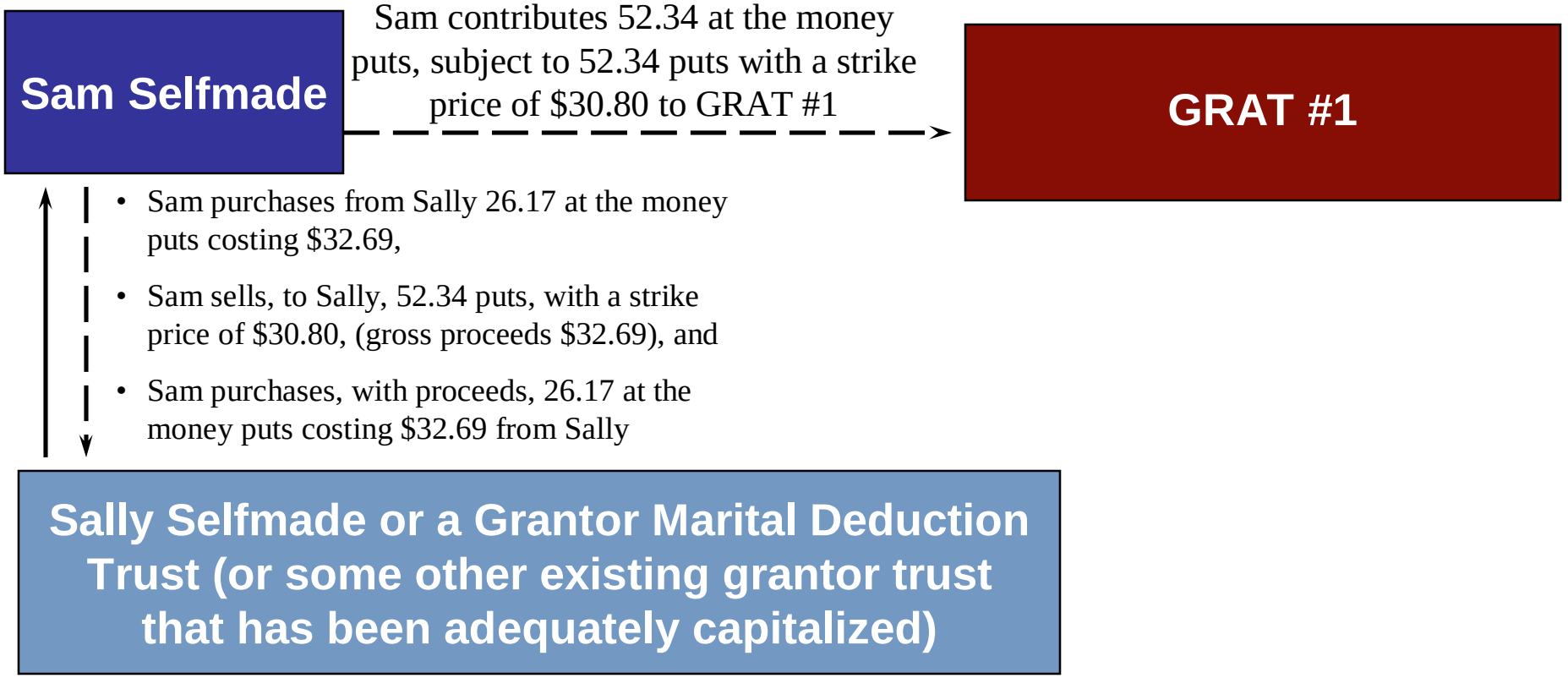
Transaction 2 (Call Option Spread, One GRAT): Sam Selfmade Purchases, from Sally Selfmade, 17.49 at the Money Calls; Sam Selfmade Sells 34.98 Calls, with Strike Prices of $35.10, to Sally Selfmade; Sam Selfmade Contributes the 17.49 at the Money Calls, Subject to 34.98 Calls with a Strike Price of $35.10, to GRAT #1



Assuming that Sam Selfmade is willing to contribute, to a GRAT, assets that have a net value of $32.69. Transactions are assumed to take place on July 31, 2006.

The premium paid for the option and/or the settlement of the option could be with Sam Selfmade's partnership units or the marital deduction trust's partnership units.

Transaction 3 (Put Option Spread, One GRAT): Sam Selfmade Purchases, from Sally Selfmade, 52.34 at the Money Puts; Sam Selfmade Sells 52.34 Puts, with Strike Prices of $30.80, to Sally Selfmade; Sam Selfmade Contributes the 52.34 at the Money Puts, Subject 52.34 Puts with a Strike Price of $30.80, to GRAT #1



Assuming that Sam Selfmade is willing to contribute, to a GRAT, assets that have a net value of $32.69. Transactions are assumed to take place on July 31, 2006.

The premium paid for the option and/or the settlement of the option could be with Sam Selfmade's partnership units or the marital deduction trust's partnership units.

GRAT Remainderman's Return at the End of One Year as a Percentage of the Initial Contribution to the GRAT

Stock Price	Increase (Decrease) in the Value of GE Stock	Transaction 1	Transaction 2	Transaction 3
$10.00	-69.41%	0.00%	0.00%	196.44%
$15.00	-54.11%	0.00%	0.00%	196.44%
$20.00	-38.82%	0.00%	0.00%	196.44%
$25.00	-23.52%	0.00%	0.00%	196.44%
$27.00	-17.41%	0.00%	0.00%	196.44%
$28.00	-14.35%	0.00%	0.00%	196.44%
$29.00	-11.29%	0.00%	0.00%	196.44%
$30.00	-8.23%	0.00%	0.00%	196.44%
$30.80	-5.78%	0.00%	0.00%	196.44%
$31.00	-5.17%	0.00%	0.00%	164.42%
$32.00	-2.11%	0.00%	0.00%	4.29%
$33.00	0.95%	0.00%	0.00%	0.00%
$35.00	7.07%	0.87%	140.99%	0.00%
$35.10	7.37%	1.17%	151.69%	0.00%
$41.00	25.42%	19.22%	151.69%	0.00%
$50.00	52.95%	46.75%	151.69%	0.00%
$55.00	68.25%	62.05%	151.69%	0.00%
$60.00	83.54%	77.34%	151.69%	0.00%

Transactions are assumed to take place on July 31, 2006.

This table is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

For a Single GRAT, Why Do Call Option Spreads (Option 2) Work So Well? The Answer is Extreme Leverage as Noted Below For GE Stock (Assuming the GRAT was Created on July 31, 2006)

Transaction	Assets of the GRAT, Which Are Worth $32.69 on July 31, 2006	The Amount of Growth in Value That GE Must Achieve Before GRAT Remaindermen Receive Value (Breakeven Point)	The Amount GRAT Remaindermen Will Receive For Every Dollar of Growth of a Share of GE Stock Once Breakeven Point is Achieved
Transaction 1	One share of GE stock	$2.03	$1
Transaction 2	34.98 at the money call, subject to 34.98 calls with a strike price of $35.10	$0.99	$34.99

This table is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Goldman Sachs

Refinements of the Technique

- What if Sam Selfmade purchases both a call spread option and a put spread option from the marital deduction trust for Sally's benefit, and then contributes each option to different GRATs with different annuity payouts and different remainderman provisions? Investors sometimes make that purchase (the so-called "winged-tip" strategy) when they are betting on market volatility. There are circumstances when neither strategy would work (because that stock is flat or the markets are flat). Even so, in most instances one of the GRATs will always work and the failure of the other will be costless (apart from administrative costs). This bothers the practitioner who applies a "too good to be true" test.

- A more conservative approach, and just as an effective approach in the long term, would be for Sam Selfmade to use his judgment as to whether GE stock is going to be higher or lower and purchase a call spread or put spread option, but not both. If Sam's judgment is incorrect, he could do another transaction at a later time. Eventually, Sam's judgment will presumably be correct, and at that time he will have a successful GRAT with this cascading GRAT strategy.

Refinements of the Technique (Continued)

- Assuming Sam's judgment is eventually correct, Sam and his family will not be disadvantaged by the cascading GRAT strategy except for the continuing legal costs in creating the GRATs. One way to ameliorate that concern, and to create evidence as to the fair market value of the private call spread option or put spread option, is for Sally Selfmade, or her marital deduction trust, to sell, for a premium, a very small part (e.g. 5%) of the transaction to an independent third party. If the private call spread option expires worthless, the independent third party call spread option will also expire worthless. The Selfmade family will, under those circumstances, "pocket" the third party premium, which could pay for the legal costs of creating the unsuccessful GRAT that holds the private call spread option.
- The annuity payout percentage of a two year GRAT that is funded with a private derivative should be around 90% of the original fair market value in first year and around 12% in the second year. The result, or success of the transaction, will be known by the end of year one. In effect, the large annuity payout in year one creates a GRAT that performs similar to a one year GRAT. It should be noted that there is not any express support or prohibition in the treasury regulations with respect to decreasing annuity payouts for GRATs.

Refinements of the Technique (Continued)

- As noted above, the payment of the premium by Sam to the grantor marital trust could be "in kind" (e.g., shares of a subchapter S trust or family limited partnership units). Likewise, the marital deduction trust could settle the option contract "in kind". In this manner, the technique could be used to transfer, assuming a successful GRAT, any of the client's assets.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Pages 62 – 68 of the Paper)

- Private equity fund managers or hedge fund managers often participate in their funds in two different manners.
- The fund manager often invests in his managed fund along with other investors and receives the same return and rights that the other investors receive.
- Additionally, the fund manager also receives a right to "carried" interest from the fund that participates in the profits of the fund after a certain minimum amount of profits have been allocated to the investors.
- Many of these mangers would like to do estate planning solely on their "carried" interest because of its greater growth potential.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

- However, because managers have two different types of equity interests in their funds, and because they are in control of the funds, many worry that the special valuation rules of IRC Section 2701 may apply to any transfers of the "carried" interest and those valuation rules may be applied in a manner that is disadvantageous in comparison to the hypothetical willing buyer, willing seller standard that is normally applied for gift tax transfers.

Example: Iam A. Carrier Engages in
Estate Planning With Respect to His Carried Interest

Iam A. Carrier is a private equity fund manager, along with his partners of a $1 billion private equity fund. Mr. Carrier is interested in estate planning with respect to certain of his interests in a private equity fund in which he invests and co-manages. Mr. Carrier owns a .2% investment interest in the $1 billion private equity fund. Mr. Carrier also has a 10% interest in the entity that owns the general partner of the private equity fund. The general partner is entitled to the "carried interest" as further described below.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

The profits and cash flow of the private equity fund are to be divided as follows:

- First, to the investment owners in proportion to their unreturned capital contributions until all capital contribution amounts have been returned.
- Second, to the investment owners until they have received an 8% return on their unreturned capital contribution amounts. This 8% "preference" return is cumulative and compounds annually.
- Third, to the carried interest owners until they have received distributions totaling 20% of the total profits of the private equity hedge fund on a cumulative basis.
- Fourth, to the carried interest owners and the investment owners so that the carried interest owners receive 20% of the "residual" cash flow and profits and the remaining 80% of the "residual" cash flow and profits are allocated among the investment owners in proportion to their respective membership interests.

There are many investment reasons for Mr. Carrier to create a LLC to hold the carried interest before he engages in estate planning, including certain control aspects inherent with his other co-managers.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

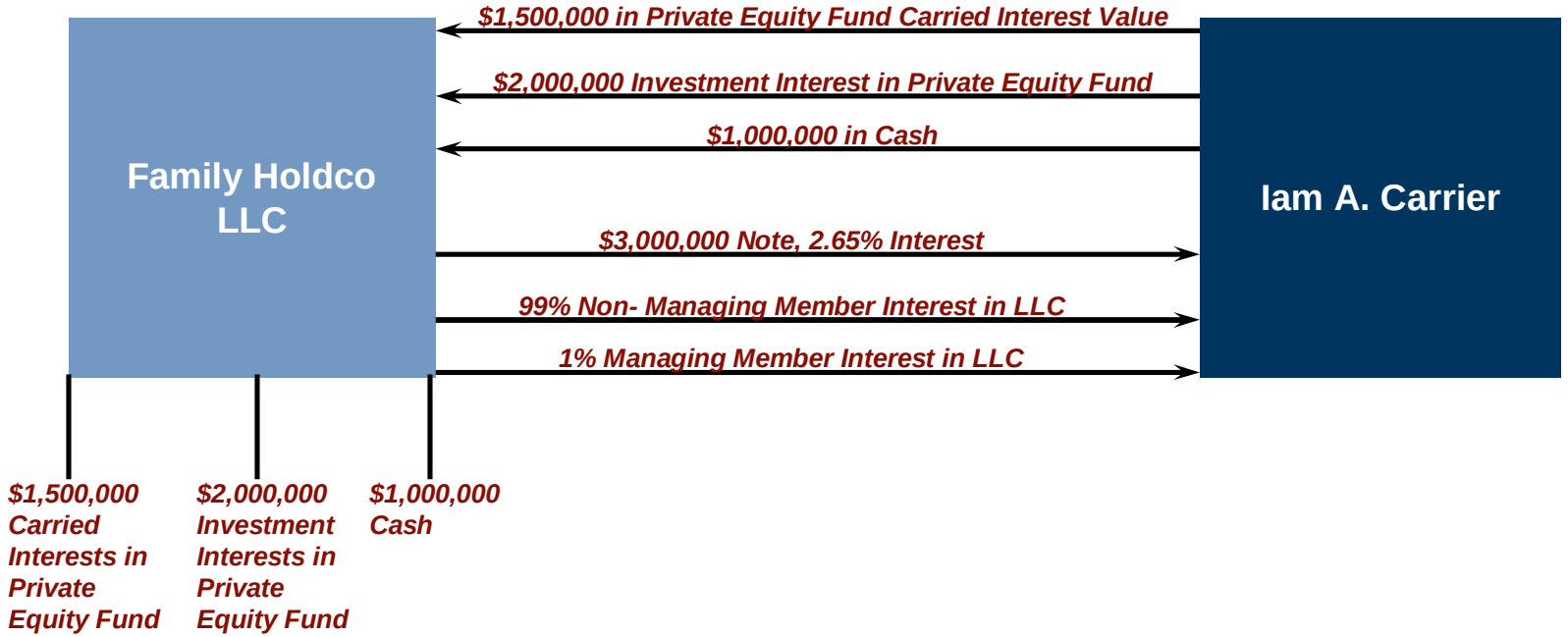
Mr. Carrier has asked his attorney, Connie Careful, to develop planning ideas based on the following assumptions about the growth of the private equity fund:

	Beginning of Year	Distributed Income	Unrealized Growth	End of Year
Year 1	1,000,000,000	20,000,000	101,353,392	1,101,353,392
Year 2	1,101,353,392	22,027,068	111,625,902	1,212,979,294
Year 3	1,212,979,294	24,259,586	122,939,566	1,335,918,860
Year 4	1,335,918,860	26,718,377	135,399,908	1,471,318,768
Year 5	1,471,318,768	29,426,375	149,123,148	1,620,441,915
Year 6	1,620,441,915	32,408,838	164,237,285	1,784,679,200
Year 7	1,784,679,200	35,693,584	180,883,290	1,965,562,490
Year 8	1,965,562,490	39,311,250	199,216,425	2,164,778,916

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

Ms. Careful believes that if Mr. Carrier creates a family LLC to hold his interests, she would then be in a position to plan for Mr. Carrier's estate, without the investment interest "diluting" the planning opportunity for the carried interest. More specifically, Ms. Careful believes that if Mr. Carrier receives a note from the family holding entity that is equal to the value of the investment interest in the private equity fund contribution and contributed cash, there will be no dilution in her planning for the carried interest contribution to the family holding entity. The initial Holdco structure would be organized as follows (Scenario #1: Hypothetical Transaction #1):



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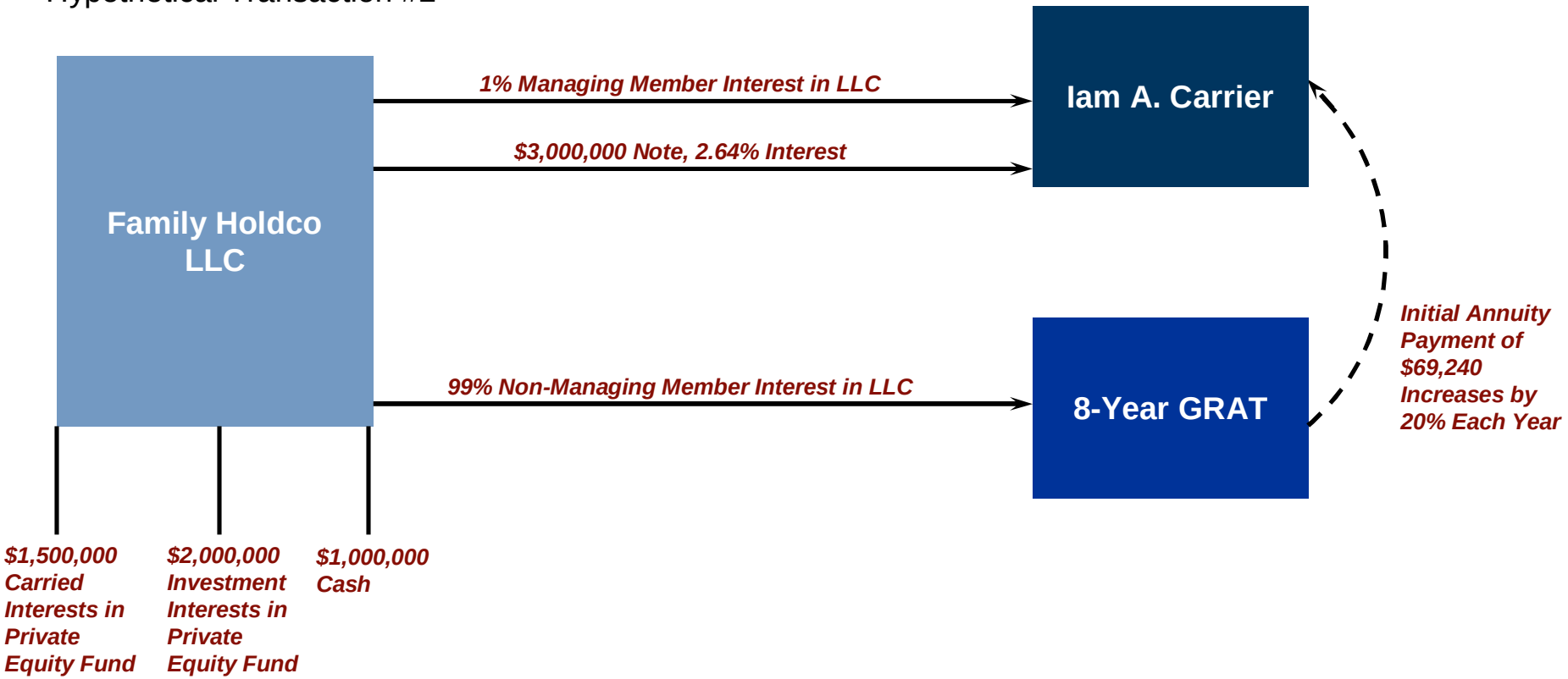
Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

Scenario #1:
Hypothetical Transaction #2

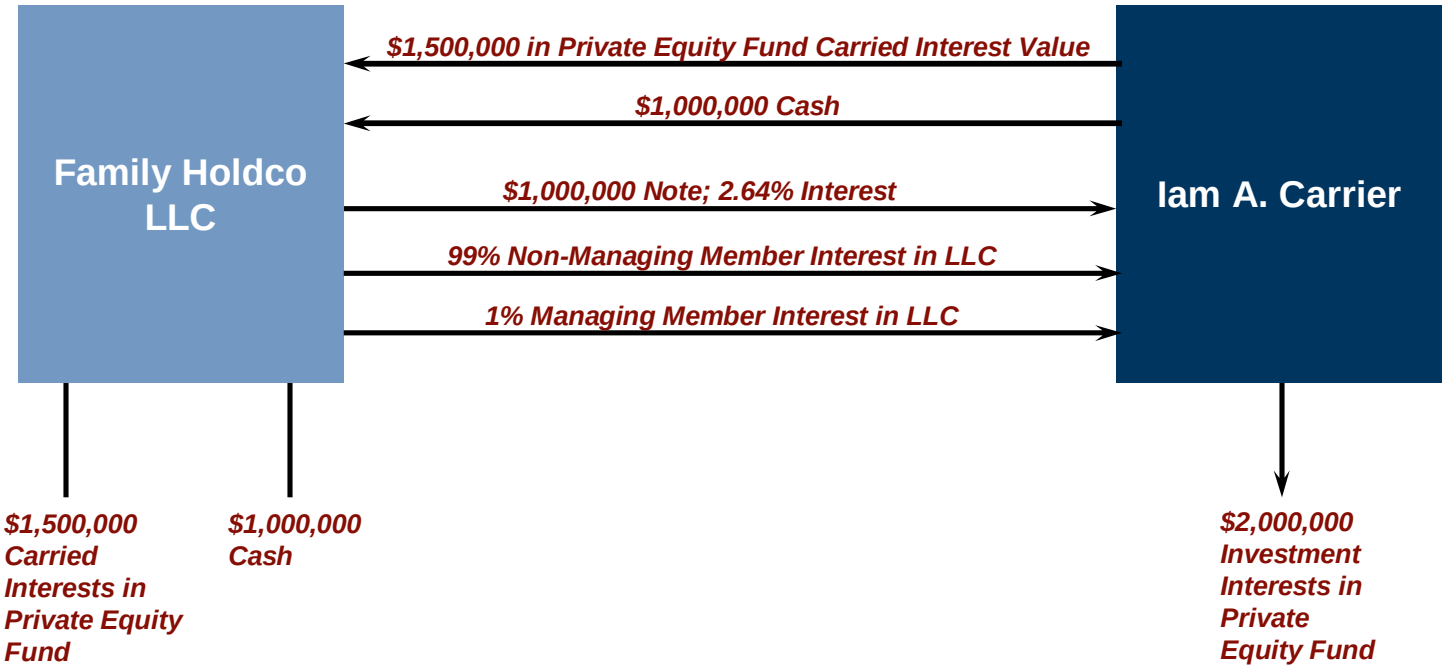


This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

An alternative structure, which may be subject to the valuation rules under IRC Section 2701, would be for Iam Carrier to contribute $1,000,000 along with the carried interest to Holdco. Iam A. Carrier would continue to individually own the investment interest in the private equity fund. The structure would be similar to the illustration below:

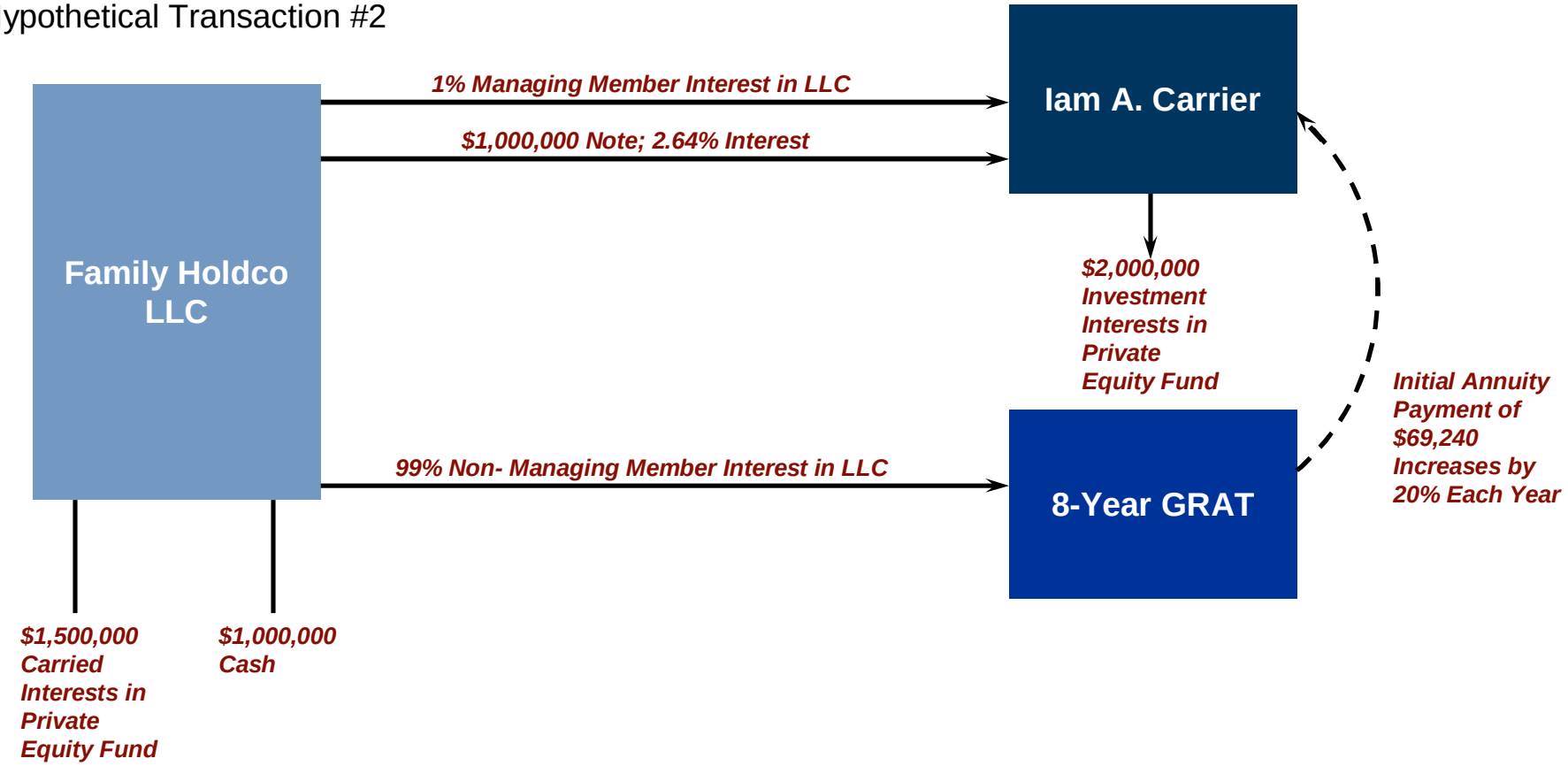
Scenario #2:
Hypothetical Transaction #1



This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

Scenario #2:
Hypothetical Transaction #2



This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

Under the assumptions of this example, the estate planning results of scenario one and scenario two in comparison to each other and in comparison to no further planning are delineated below:

Technique	Carrier Family	IRS - Income Tax	IRS - Investment Opportunity Cost	IRS - Gift Tax (at 45%)	Total
No Further Planning; Transfers Estate to Family at the End of 8 Years	14,092,544	3,755,759	68,598	11,530,263	29,447,164
Planning Scenario #1: Iam A. Carrier Creates a Family Partnership and Contributes $1,000,000 Cash, Carried Interest and a $2,000,000 Investment Interest in a Private Equity Fund that he Co-Manages; and the Partnership Issues $3,000,000 in Notes to Iam A. Carrier with an Interest Rate Equal to the Federal Mid-Term Rate; Iam A. Carrier then Contributes Partnership Units to a GRAT; Iam A. Carrier Gives His Remaining Assets to His Family in 8 Years	24,886,627	3,769,157	68,598	722,783	29,447,164
*Planning Scenario #2: Iam A. Carrier Creates a Partnership and Contributes $1,000,000 Cash and the Carried Interest; Iam A. Carrier Returns the Investment Interest in the Private Equity Fund; the Partnership Issues $1,000,000 in Notes to Iam A. Carrier with an Interest Rate Equal to the Federal Mid-Term Rate; Iam A. Carrier Contributes Partnership Units to a GRAT; Iam A. Carrier Gives His Remaining Assets to His Family in 8 Years	24,447,268	3,497,229	68,598	1,434,069 *	29,447,164

* This scenario may also be subject to additional gift taxes because of the valuation rules under IRC Section 2701.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Using a 20% Annual Increasing Annuity GRAT, and Using "Proportionality" and "Debt" Exceptions of IRC Section 2701 to Plan for Private Equity Fund Managers and Hedge Fund Managers (Continued)

- Observations:
- Using two of the exceptions to the valuation rules of IRC Section 2701, (i) the proportionality exception (client contributes all of his interests (both his investment interest and his carried interest) in the private equity fund to the Holding Family Limited Partnership) and (ii) the debt exception (the investment interest is contributed in exchange for a note), in combination with a 20% annual increasing annuity GRAT, the results attained are similar to or enhanced over the results of contributing a partnership that solely owns a carried interest to a 20% annual increasing annuity GRAT, without the IRC Section 2701 valuation concerns.

Some of the Best Family Limited Partnership Planning Ideas We See Out There (Pages 74 – 136 of the Paper)

Conventional Wisdom:

- "For the passive trustee investor, there does not exist any substantive non-tax investment reason to invest in a family limited partnership;" or
- "Do not engage in family limited partnership planning unless it can be demonstrated that the partnership uniquely solves a substantive non-tax problem;" or
- "Discounting a client's assets is a much better estate planning tool than grantor trusts or freezing a client's estate."

This "conventional wisdom," under the circumstances discussed below, is incorrect.

Best Non-Tax Planning Idea – or Why Investment Professionals Have Limited Liability Companies and/or Limited Partnerships (Pages 74 – 106 of the Paper)

Marvin and Maggie Modern wish to give $300,000 to separate trusts for each of their grandchildren. Marvin and Maggie understand modern portfolio theory and the importance of diversification. They want the grandchildren's trusts to invest for the greatest risk-adjusted return and are concerned that the trusts will not be large enough to meet SEC limitations on who may invest in certain alternative asset classes.

In addition to current gift planning, Marvin and Maggie want to provide a qualified terminal interest marital deduction trust ("QTIP") for the surviving spouse under their estate plans. Many of their personal alternative asset investments are held in private equity partnerships now. Marvin and Maggie worry that these investments could cause income tax fairness issues for the QTIP trust – that is, they worry that the surviving spouse, as income beneficiary, may bear a disproportionate amount of income tax liability on the alternative investments - but still feel strongly that the QTIP trust should have exposure to alternative asset classes.

Marvin and Maggie ask their attorney, Pam Planner, how to structure their investment portfolio so the trustees for their grandchildren's individual trusts and the survivor's QTIP trust can invest in the broad array of asset classes necessary to maximize risk-adjusted return under modern portfolio theory.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Best Non-Tax Planning Idea – Or Why Investment Professionals Love Limited Liability Companies and/or Limited Partnerships (Continued)

- The first investment reason certain trusts are benefited by the creation of family limited partnerships: closely held family limited partnerships may facilitate a trust holding alternative investments and the trust's ability to follow modern portfolio theory.
  - Certain exceptions to the registration requirements under the Securities Exchange Act of 1933, the Securities Exchange Act of 1934 and the Investment Company Act of 1940 are important to many issuers of alternative investments (e.g., investments such as oil and gas, real estate and other private equity investment funds).
  - It is important that those alternative investment funds be held by "accredited investors" and/or "qualified purchasers".
  - If the Moderns first create a family limited partnership, and then give family limited partnership units to the trusts for the grandchildren, then the accredited investor and qualified purchaser exceptions may apply. In that manner the trust investments would follow modern portfolio theory.

Best Non-Tax Planning Idea – Or Why Investment Professionals Love Limited Liability Companies and/or Limited Partnerships (Continued)

- The second investment reason certain trusts are benefited by the creation of family limited partnerships: closely held family limited partnerships facilitate income only (so-called simple) trusts to be fully diversified, as modern portfolio theory seems to require.
  - Closely held family limited partnerships could be a tool to manage distribution fairness issues for income only trusts associated with distributions (or lack of distributions) from alternative investments.
    - Unitrust conversion does not help because of valuation issues with hedge funds and private equity investments.
    - Distributions of private equity and fund investment units cannot be made because of securities concerns.
    - If other assets are distributed it could potentially distort the overall asset allocation.
  - Closely held family limited partnerships could be a tool to manage income tax fairness issues associated with alternative investments for income only trusts.
    - One cash distribution could be made from a family limited partnership to an income only trust and designated as trust accounting income.
    - A second cash distribution could be made from a family limited partnership to an income only trust and designated as corpus to pay trust income taxes.

Best Non-Tax Planning Idea – Or Why Investment Professionals Love Limited Liability Companies and/or Limited Partnerships (Continued)

- The third investment reason certain trusts are benefits by family limited partnerships: the closely held family limited partnership has the management capacity to carry out the partnership's capital gains income to the income only beneficiary for income tax purposes.
  - Under UPIA Section 401, a distribution of cash from an entity to a trust may be deemed to have carried out capital gain income as trust accounting income, if a trustee does not have distribution control over a family limited partnership.
  - A trustee can only allocate receipts from the entity between income and principal according to the trust agreement or UPIA Section 401.

One of the Best Family Limited Partnership Planning Ideas – Sell It (Pages 106 – 136 of the Paper)

Example: The Sweet Deal

Cal Client is in his office when Dan Deal knocks on his door and tells Cal that he has "a heck of a deal for him." Dan states that he would like to sell most of his assets to Cal for 65¢ on the dollar. Cal tells Dan that he likes the price, but he does not want to buy any of the assets for cash. Cal wonders if Dan would still be willing to sell his assets for 65¢ on the dollar, if it was all for a seller financed note from Cal. Dan tells Cal that because he likes him so much he will be happy to accept a note from Cal. Cal then informs Dan that while he likes the 65¢ on the dollar, he likes the fact that he can buy all the assets for a seller financed note, he does not like to pay much interest on the note and wonders if Dan will still offer that deal if the interest rates are comparable to US Treasury interest rates. Again, Dan tells Cal that because he likes him so much he will be happy to do that deal. Cal then informs Dan that while he likes the price of 65¢ on the dollar, and he also likes the fact that he can purchase the assets for a seller financed note at US Treasury interest rates, he will only buy the assets if he will have no personal liability on the note (i.e., the note will be non-recourse). Dan, once again agrees to Cal demands. An increasingly impatient Dan asks Cal if there are any other deal points. Cal says there is just one more. Cal tells Dan that he does not like paying income taxes. Cal will only do the deal if Dan will agree to pay all of the income taxes associated with the assets he is purchasing from Dan. Dan agrees.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

If a Sale of a Partnership Interest Occurs During a Client's Lifetime, the Gift Tax Equivalent of I.R.C. Section 2036 Does Not Exist (i.e., There is No I.R.C. Section 2536 Under Chapter 12 of the Code)

Example: Lacy Lucky Sells Her Partnership Interest During Her Lifetime

Lacy Lucky lives in the great state of Nirvana. In the state of Nirvana, plaintiff's lawyers have been banned. In this enlightened state, wealthier spouses always receive all of the marital assets, if there is a failed marriage. Because this state is so enlightened, the SEC is very impressed and has waived its qualified purchaser and accredited investor rules with respect to trusts created under this state's laws. Because of all of these reasons (and because all children in this state are born with above average intelligence), Lacy Lucky is worried that a substantive non-tax reason may not exist for the creation of her family limited partnership. After the creation of the partnership, Lacy will own a 1% general partnership interest and a 98% limited partnership interest. Lacy asks her attorney, Tom Taxadvisor, what she could do to avoid the application of I.R.C. Section 2036(a)(1) other than avoiding behavior that might constitute an implied agreement to use the partnership asset income?

- Tom may advise Lacy to sell all of her limited partnership interest for adequate and full consideration.
- Even if the sale is not for adequate and full consideration (e.g. part sale, part gift or all a gift), if Lacy lives longer than three years after the transfer, then I.R.C. Section 2036(a)(1) should not apply to the resulting note (assuming the note is a note for state law property purposes) and/or cash she receives from that sale.

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Best Family Limited Partnership Idea – Sell It (Continued)

- If a sale of a partnership interest occurs during a client's lifetime the gift tax equivalent of IRC Section 2036 may not exist.
- The valuation principles of Revenue Ruling 93-12 apply to lifetime transfers, but they do not apply to transfers at death.
- Growth of the underlying assets of the partnership, if a transfer occurs during the lifetime of a taxpayer, will not be subject to estate tax.
- A future Congress could change the current law with respect to valuation discounts associated with family limited partnerships.
- The taxpayer may have the ability to indirectly access all of the partnership distributable cash flow for consumption needs.
- Generally, the sale of a family limited partnership interest to a trust, is a flexible arrangement that can be modified to changed circumstances.
- The sale of a limited partnership interest for a note facilitates testamentary charitable planning, because the note is a more attractive asset for a charity to receive than family limited partnerships interests.
- There is a significant transfer tax advantage for the taxpayer who transfers his partnership interests during his lifetime to a grantor trust in exchange for a note.

Best Family Limited Partnership Idea – Sell It (Continued)

Example: Mimi Minimum Wonders What Additional Transfer Tax Benefit Accrues From a Partnership Valuation Discount Over Her Life Expectancy

Mimi Minimum is a very healthy 50 year old female. Both of her parents are still alive and she has only recently buried her grandparents. Her doctor assures her that she easily has a 30 year life expectancy. Mimi likes the relative simplicity of making a $2,000,000 gift of some of her highly appreciated stock to fund a grantor trust and then selling her highly appreciated stock worth $18,000,000 to that grantor trust for a low interest note after the sale for the note is completed, the grantor trust would then sell all $20,000,000 of its stock ("Technique One" below). Mimi asks her estate planner, Les Rates what is gained by transferring a family limited partnership (which holds $18,000,000 of her stock) to a grantor trust from a transfer tax standpoint, assuming she does live a 30 year period ("Technique Two" below). Mimi is concerned about the costs of creating a family limited partnership (legal costs, accounting costs, administrative costs and valuation expert costs). Mimi tells Les Rates to assume that she will earn 8% pretax return with respect to the proceeds of the sale of the appreciated stock (with 2% being taxed at ordinary income rates and 6% being taxed at capital gains rates with a 30% turnover) and that her consumption needs will be $350,000 a year before inflation. What does Les Rates' analysis demonstrate?

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Summary of Results For $20 Million of Asset With "0" Basis Growing at 8% Per Year (Pre-Tax) – No Further Planning vs. Two Hypothetical Integrated Income and Estate Tax Plans; 30 Year Future Values; Post-Death Scenarios (assuming client dies in 30 years)

Technique	Minimum Family	Consumption – Direct Cost	Consumption – Investment Opportunity Cost	IRS– Income Tax	IRS– Investment Opportunity Cost	IRS– Estate Tax (at 45%)	Total
No Further Planning; Bequeaths Estate To Family (Without Discount)	$38,798,412	$16,651,395	$36,796,365	$19,551,445	$57,711,366	$31,744,155	$201,253,138
No Further Planning; Bequeaths Estate To Family (With Discount)	$49,908,866	$16,651,395	$36,796,365	$19,551,445	$57,711,366	$20,633,701	$201,253,138
Technique #1: Hypothetical Integrated Income and Estate Tax Plan With a Gift/Sale to a GST; Bequeaths Estate To Family	$68,269,192	$16,651,395	$36,796,365	$21,308,079	$57,711,366	$516,740	$201,253,138
Technique #2: Hypothetical Integrated Income and Estate Tax Plan With a Partnership and With a Gift/Sale to a GST; Bequeaths Estate To Family	$68,399,886	$16,651,395	$36,796,365	$21,796,365	$57,711,366	$298,954	$201,253,138

This is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Summary of Results For $20 Million of Asset With "0" Basis Growing at 8% Per Year (Pre-Tax) – No Further Planning vs. Two Hypothetical Integrated Income and Estate Tax Plans; 10 Year Future Values; Post-Death Scenarios (assuming client dies in 10 years)

Technique	Minimum Family	Consumption – Direct Cost	Consumption – Investment Opportunity Cost	IRS – Income Tax	IRS – Investment Opportunity Cost	IRS – Estate Tax (at 45%)	Total
No Further Planning; Bequeaths Estate To Family (Without Discount)	$14,857,342	$4,012,358	$1,692,703	$6,076,989	$4,383,101	$12,156,007	$43,178,500
No Further Planning; Bequeaths Estate To Family (With Discount)	$19,111,945	$4,012,358	$1,692,703	$6,076,989	$4,383,101	$7,901,405	$43,178,500
Technique #1: Hypothetical Integrated Income and Estate Tax Plan With a Gift/Sale to a GST; Bequeaths Estate To Family	$20,869,217	$4,012,358	$1,692,703	$6,780,213	$4,383,101	$5,440,909	$43,178,500
Technique #2: Hypothetical Integrated Income and Estate Tax Plan With a Partnership and With a Gift/Sale to a GST; Bequeaths Estate To Family	$23,931,861	$4,012,358	$1,692,703	$6,635,610	$4,383,101	$2,522,868	$43,178,500

This table is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Some of the Best Synergistic Planning Ideas That Incorporate the Use of Life Insurance (Pages 136 – 157 of the Paper)

Conventional Wisdom:

- "Using a family limited partnership always creates administrative problems, it does not solve them;" or
- "Life insurance will be included in an insured's estate if the insurance is owned by a partnership in which he is a partner."
- "Using a preferred partnership interest is dead after the passage of I.R.C. Section 2701;" or
- "It is impossible, after the split dollar reform, for a trust to pay for premiums on a significant life insurance policy without paying significant gift taxes."

This "conventional wisdom," under the circumstances discussed below, is incorrect.

Best Post Mortem Planning Idea (and a Good Insurance Planning Idea) – The Note "Freeze" Partnership (Pages 136 – 151 of the Paper)

Please consider the following example:

Connie Confused Wishes to Simplify Her Post-Mortem Administrative Life and Also Accomplish Some Estate Planning Goals

Carl Confused dies in a year in which the estate tax exemption and the GST exemption are $2,000,000. Carl and Connie live in a community property state. The financial assets of their community property estate equal $12,000,000. Carl and Connie, at Carl's death, have not created a family limited partnership. Connie is 70 years of age and is in very good health. Connie is the lifetime beneficiary of the by-pass trust, which is also a generation-skipping trust that Carl created under his will. Connie also wishes to create a generation-skipping trust using her $1,000,000 gift tax exemption. In order to help defray the cost of paying estate taxes, Connie is contemplating purchasing a $2,500,000 life insurance policy on her life that is a guaranteed universal life policy.

Connie asks her estate planner, Pam Planner, if there is any way to organize the multiple trusts and her financial assets where there is a simplified structure that consolidates the community estate assets and saves future estate taxes. She asks Pam to assume that she will spend $250,000 a year, after income taxes, with a 3% inflation adjustment.

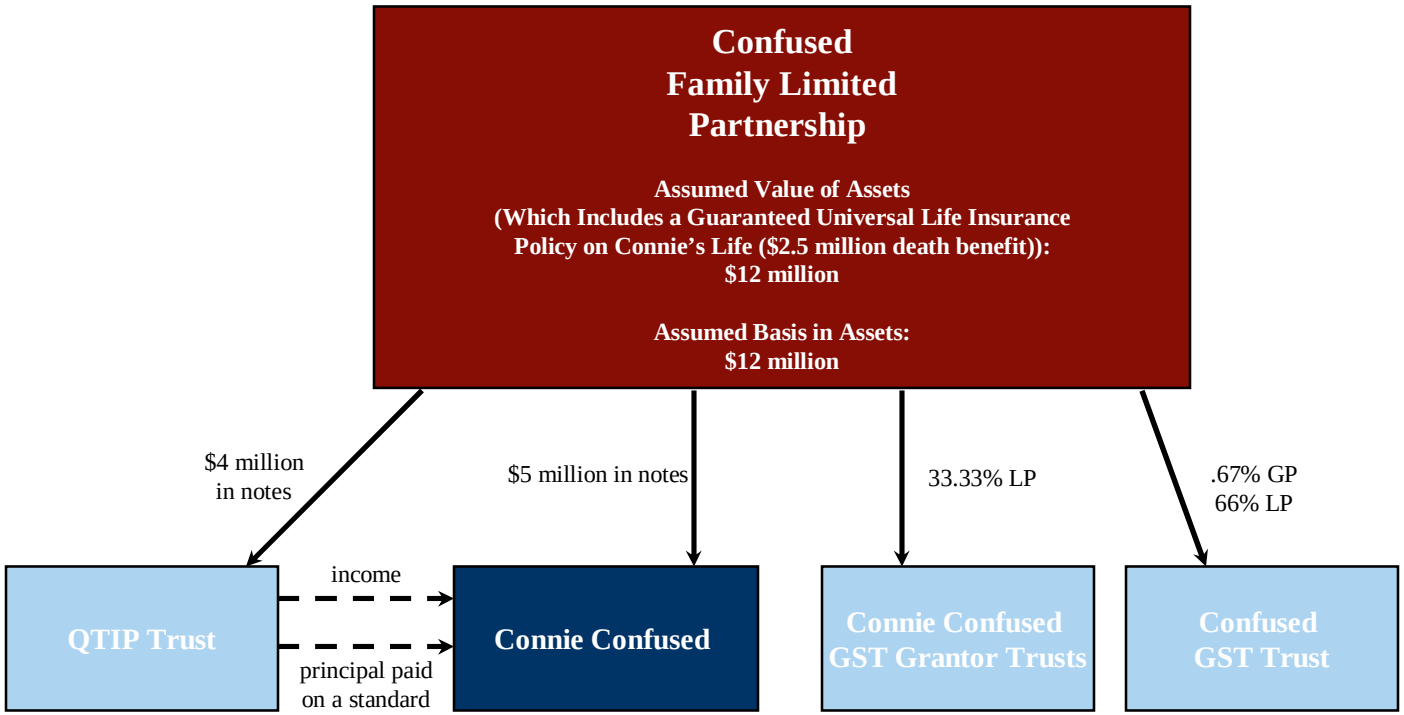
This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Best Post Mortem Planning Idea (and a Good Insurance Planning Idea) – The Note "Freeze" Partnership (Continued)

- Pam suggests that Connie and the various trusts form a partnership with the various parties either receiving a note for their contribution to the partnership or receiving partnership interests for their contribution to the partnership.
- The $2,000,000 GST trust, in which Connie is a lifetime beneficiary, receives a partnership interest for its $2,000,000 contribution. The $1,000,000 GST trust that Connie creates will receive a partnership interest for its $1,000,000 contribution. Connie receives a note for the contribution of her assets. The various QTIP trusts receive notes for their contribution to the partnership. The notes pay the AFR interest rate.

Best Post Mortem Planning Idea (and a Good Insurance Planning Idea) – The Note "Freeze" Partnership (Continued)

The diagram below illustrates the concept:



Non-Tax Reasons For the Creation of a Note Freeze Partnership

- Simplifies the administration of the estate.
- Takes advantage of the step-up in basis of estate assets.
- Life insurance proceeds will not be subject to I.R.C. Section 2042.
- Note freeze partnership is not subject to valuation rules of I.R.C. Section 2701.
- The historic low yields on treasuries accentuate the result of note freeze partnership.

Comparative Result of the Note Freeze Partnership

Please note the following table, which compares the result that would have accrued had Connie not done any further planning with the hypothetical plan (assuming she lives 20 years, consumes $250,000 a year, after inflation) the family assets earn 8% before taxes, with 2% being taxed as ordinary income and 6% being taxed as capital gains rates with an assumed 30% turnover.

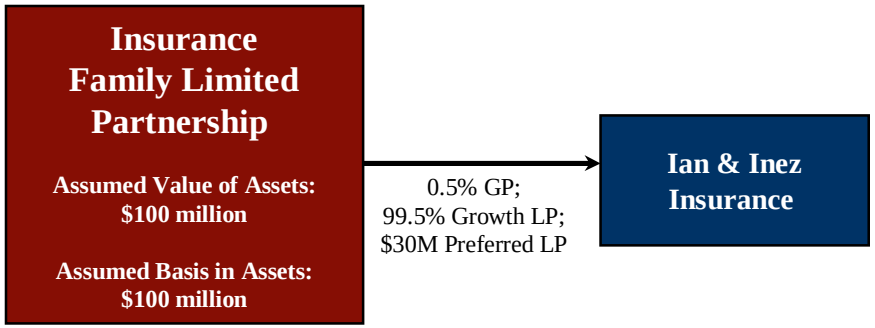
Technique	Confused Children	Confused GST Trust	Consumption – Direct Cost	Consumption – Investment Opportunity Cost	Investment Opportunity Cost/(Benefit) of Buying Life Insurance	IRS – Income Tax	IRS – Investment Opportunity Cost	IRS – Estate Tax (at 45%)	Total
No Further Planning; Bequeaths Estate To Family	$14,538,178	$7,041,630	$6,717,594	$7,556,636	$0	$5,569,070	$5,477,142	$9,031,236	$55,931,486
Hypothetical Integrated Income and Estate Tax Plan With a Partnership; Bequeaths Estate To Family	$3,701,671	$25,629,169	$6,717,594	$7,556,636	$377,325	$5,777,962	$5,187,944	$983,185	$55,931,486

Not only does the proposed structure greatly simplify the administration problems for Connie, but it also has the potential of saving considerable transfer taxes. If Connie should die early (e.g., in 5 years) the life insurance policy forms a substantial "hedge" against an early death.

This table is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Best Insurance Planning Idea (and a Very Good Partnership Planning Idea) – The Leveraged Reverse Freeze With a Cascading Sale of Growth Partnership Interests (Pages 151 – 157 of the Paper)

- Consider the following example, which illustrates the potential of combining a leveraged sale of a high yielding preferred to a grantor trust with the trust using its excess cash flow to purchase life insurance and make cascading purchases of the growth partnership interests:



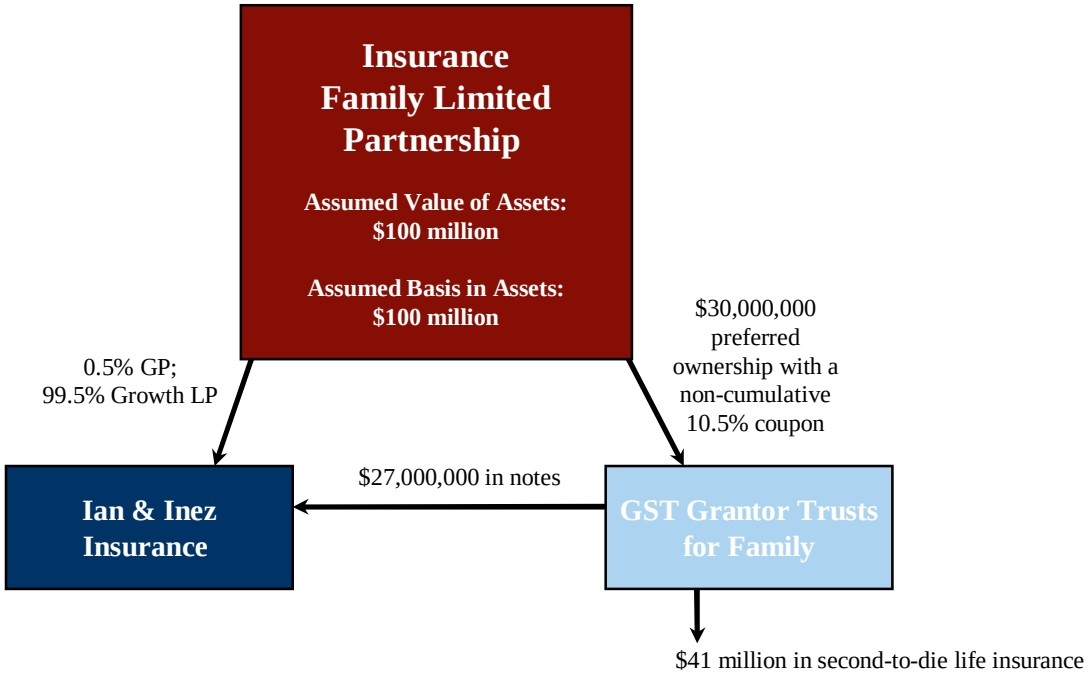
Partner	Ownership (%)
Ian & Inez Insurance	0.5% GP; 99.5% Growth LP; $30M Preferred LP

- After the partnership has been created Ian and Inez Insurance transfers, by gift, a $3,000,000 preferred partnership interest with a non-cumulative 10.5% coupon to some generation-skipping transfer trusts for the benefit of their children, grandchildren and future descendants.

Best Insurance Planning Idea (and a Very Good Partnership Planning Idea) – The Leveraged Reverse Freeze With a Cascading Sale of Growth Partnership Interests (Continued)

- Ian and Inez also sell the remaining $27,000,000 preferred interests to those trusts in exchange for notes that will pay a blended AFR rate of 2.06%.

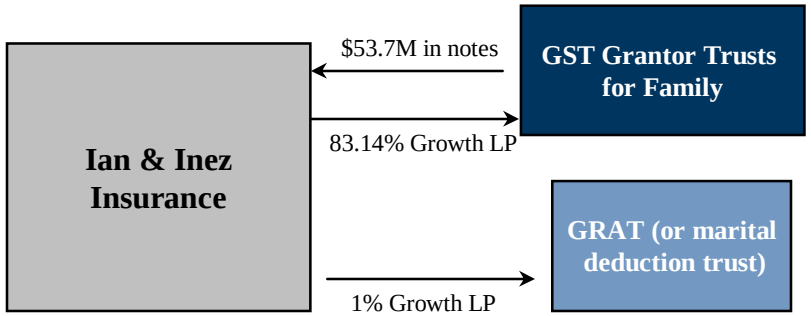
  See the illustration below:



Best Insurance Planning Idea (and a Very Good Partnership Planning Idea) – The Leveraged Reverse Freeze With a Cascading Sale of Growth Partnership Interests (Continued)

- Approximately three years after the transfer of the preferred partnership interests, the GST grantor trust could purchase from Ian and Inez their remaining growth interests that have not been sold in prior years in exchange for notes (on which, it is again assumed there will be a blended 2.06% interest rate).
- During the interim three year period, it is assumed that around 16% of the growth limited partnership units will have been purchased. The purchase of the remaining growth interests could occur in a manner in which there is a defined value sale and in which a stated dollar amount (around $54M) of the value of the transferred growth limited partnership interest, as finally determined for federal gift tax purposes, passes to the generation-skipping trusts and any excess in value passes to a near zero GRAT or a marital deduction trust.

See the illustration below:



Owner	Ownership (%)
Ian & Inez Insurance	0.5% GP; $80.7 M note receivable
GST Grantor Trusts for Family	98.5% Growth LP; $80.7M note payable; $30M Preferred LP
GRAT (or marital deduction trust)	1% Growth LP

Best Insurance Planning Idea (and a Very Good Partnership Planning Idea) – The Leveraged Reverse Freeze With a Cascading Sale of Growth Partnership Interests (Continued)

Advantages:

- With the use of life insurance, there is a hedge against early deaths.
- In Revenue Ruling 83-120 the IRS concedes preferred partnership interests in a closely held partnership should have a high coupon.
- Currently, there exists a significant arbitrage between high yielding private preferred partnership interests in a closely held partnership and treasury interest rates.
- Strong legislative history suggests I.R.C. Section 2036 should not apply to partnerships with significant preferred interests.
- The valuation rules of I.R.C. Section 2701 should not apply if one generation transfers its ownership of preferred partnership interests to the second generation.
- A later transfer of the growth partnership interests will not be affected by the valuation rules of I.R.C. Section 2701.

Best Insurance Planning Idea (and a Very Good Partnership Planning Idea) – The Leveraged Reverse Freeze With a Cascading Sale of Growth Partnership Interests (Continued)

The tables below indicate the results that could accrue under the assumptions given to Pam Planner by Ian and Inez and also assuming a $400,000 a year premium and a 40% discount on the growth partnership interests (because of the effect of the preferred partnership interests). The results are extremely powerful. Assuming that Ian and Inez die in 10 years, the 30 year future values of the hypothetical integrated plan in comparison to not doing any further planning is as follows:

30 Year Future Values (Death in 10 Years)

Technique	Insurance Children	Insurance Children & Grandchildren	Consumption – Direct Cost	Consumption – Investment Opportunity Cost	IRS – Income Tax	IRS – Investment Opportunity Cost	IRS – Estate Tax (at 45%)	Investment Opportunity Cost/(Benefit) of Buying Life Insurance	Total
No Further Planning; Bequeaths Estate To Family	$417,679,967	$0	$22,927,759	$168,266,209	$94,874,217	$580,465,509	$82,357,221	$0	$1,366,570,882
Hypothetical Integrated Income and Estate Tax Plan With a Partnership; Bequeaths Estate To Family	$173,319,917	$572,273,337	$22,927,759	$168,266,209	$159,136,543	$432,194,150	$34,174,842	($195,721,874)	$1,366,570,882

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Best Insurance Planning Idea (and a Very Good Partnership Planning Idea) – The Leveraged Reverse Freeze With a Cascading Sale of Growth Partnership Interests (Continued)

If the survivor of Ian and Inez Insurance dies in 30 years, the future value in 30 years of what their descendants will receive under the hypothetical plan in comparison to no further planning is as follows:

Future Value (Death in 30 Years)

Technique	Insurance Children	Insurance Children & Grandchildren	Consumption – Direct Cost	Consumption – Investment Opportunity Cost	IRS – Income Tax	IRS – Investment Opportunity Cost	IRS – Estate Tax (at 45%)	Investment Opportunity Cost/(Benefit) of Buying Life Insurance	Total
No Further Planning; Bequeaths Estate To Family	$337,941,016	$0	$95,150,831	$266,196,369	$124,662,541	$266,122,930	$276,497,195	$0	$1,366,570,882
Hypothetical Integrated Income and Estate Tax Plan With a Partnership; Bequeaths Estate To Family	$7,205,005	$586,008,373	$95,150,831	$266,196,369	$133,704,220	$258,888,064	$5,895,004	$13,523,015	$1,366,570,882

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Some of the Best Charitable Planning Ideas We See Out There (Pages 157 – 171 of the Paper)

Conventional Wisdom:

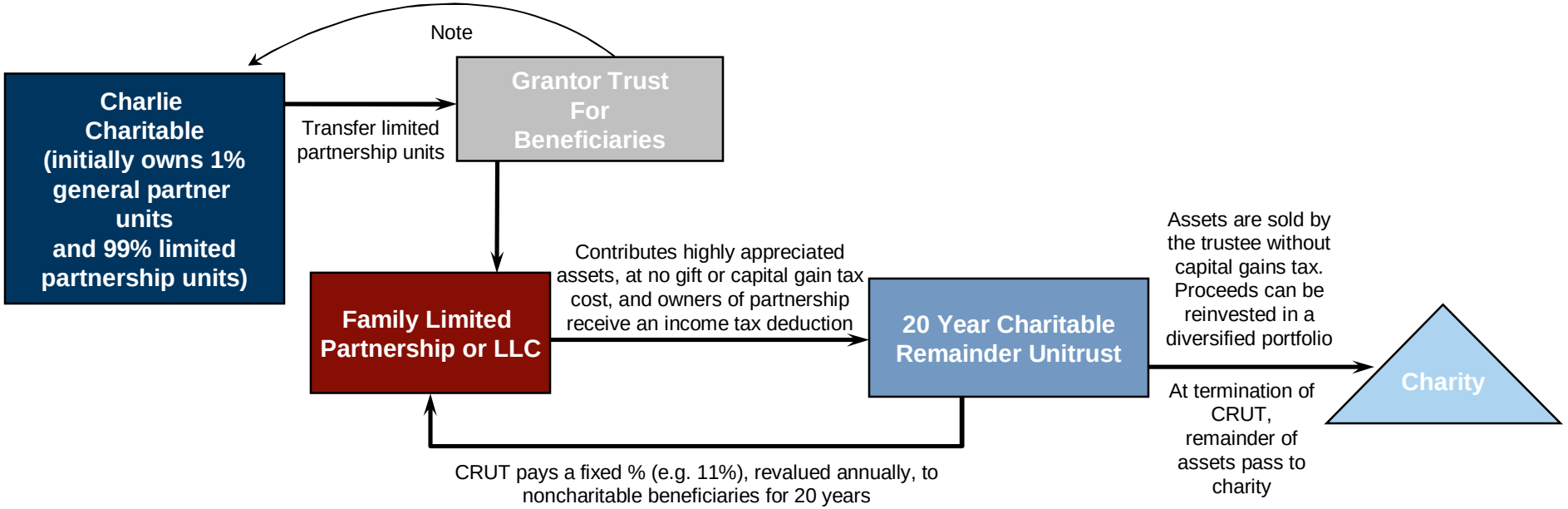
- "You can no longer use the CRUT technique and benefit your family;"
- "The problem with charitable planning is that it will greatly decrease what a client's family will receive;"
- "One can never self-deal, even on a fair basis, with a foundation or a CLAT;"
- "The problem with testamentary gifts to charity is that the decedent's family always ends up with substantially less;" or
- "The problem with testamentary CLATs is that the decedent's family has to wait a long time to have access to the decedent's assets."

This "conventional wisdom," under the circumstances discussed below, is incorrect.

Best Lifetime Charitable Planning Idea – Partnership, or a Limited Liability Company, Creates a Charitable Remainder Trust With the Partnership Units Eventually Being Sold to a Grantor Trust (Pages 157 – 166 of the Paper)

- Charitable remainder trusts, particularly charitable remainder uni-trusts ("CRUTs") are a very popular planning technique for the charitably inclined client. While the technique has significant benefits to the client and his favorite charitable causes, one downside is the perception that it is difficult to benefit a client's family with the technique. Perhaps that is not true, if the technique is used synergistically with certain other estate planning techniques, that is, sale of limited liability company or limited partnership units to a grantor trust. What if that synergistic planning simulated a capital gains tax and estate tax holiday for the client and his family with the client's family charity receiving 23% of his death on his death?

Best Lifetime Charitable Planning Idea – Partnership, or a Limited Liability Company, Creates a Charitable Remainder Trust With the Partnership Units Eventually Being Sold to a Grantor Trust (Continued)



Advantages

- Generation of current income tax deduction (10% or more of value placed in CRUT)
- Depending on investment performance, approximately 40% to 60% of inherent capital gains in the asset contributed to the CRUT will not be subject to capital gains tax
- The remaining inherent capital gains will be subject to tax, but is tax-deferred (over 20 years)
- Production of relatively steady cash flow over time
- Tax-efficient satisfaction of charitable desires
- Economic participation in growth of assets

Considerations

- Limit on certain investment alternatives
- Certain prohibited related-party transactions (even if fair)
- In the early years, access to capital is limited
- Capital gains tax rates may increase in the future
- Administrative costs in connection with formation of partnership

The Comparative Results

To show Charlie the difference that taxes play in accumulating family wealth over time, Pam projects what would happen if there were no initial capital gains taxes when Charlie sells his stock and no estate taxes She also projects what would happen if Charlie sold partnership interests to a grantor trust without including the CRUT component. If the investment plan produced smooth returns until Charlie's death (which the group agrees to project twenty-five into the future), the results would look like this:

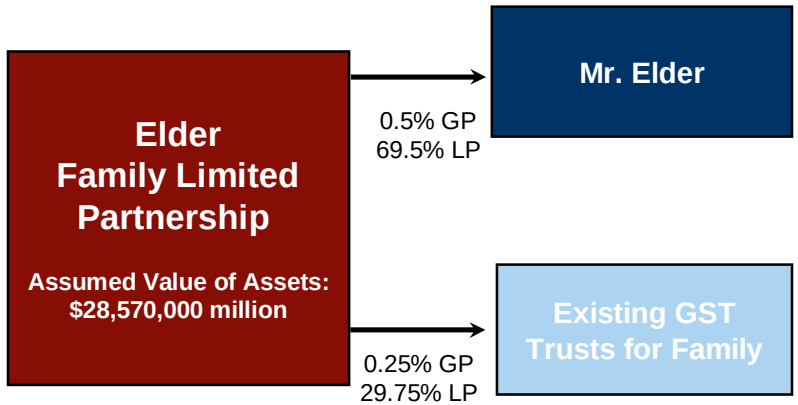
Scenario	Charlie's Children	Charlie's Descendants (GST Exempt)	Charity	Charlie's Consumption Direct Costs	Consumption Investment Opportunity Costs	IRS – Income Taxes	IRS – Investment Opportunity Costs	IRS – Estate Taxes	Total
Stock Sale, No Planning	14,795,841	2,000,000	-	5,468,890	8,795,202	7,413,154	16,269,613	13,742,052	68,484,752
Simulated Tax Holiday (No Initial Capital Gains Tax and No Estate Tax) 72% - 28% Split Between Family and Charity	-	28,053,477	8,510,849	5,468,890	8,795,202	8,008,304	9,648,029	-	68,484,752
FLP/CRUT/ Grantor Trust Sale, Charlie gives remaining estate to charity	-	27,731,762	8,510,849	5,468,890	8,795,202	7,685,158	10,292,890	-	68,484,752
FLP/ Grantor Trust Sale, Charlie gives remaining estate to family	-	29,698,713	-	5,468,890	8,795,202	8,117,016	16,269,613	135,318	68,484,752

This example is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

Best Testamentary Charitable Planning Idea For the Family Limited Partnership – The Leveraged Buy-Out Charitable Lead Annuity Trust (Continued) (Pages 166 – 171 of the Paper)

- Assume a client, at his death, wishes for part of his estate to go to his family and the rest to his favorite charitable causes. One technique that is generally considered under those circumstances is the testamentary charitable lead annuity trust ("CLAT"):

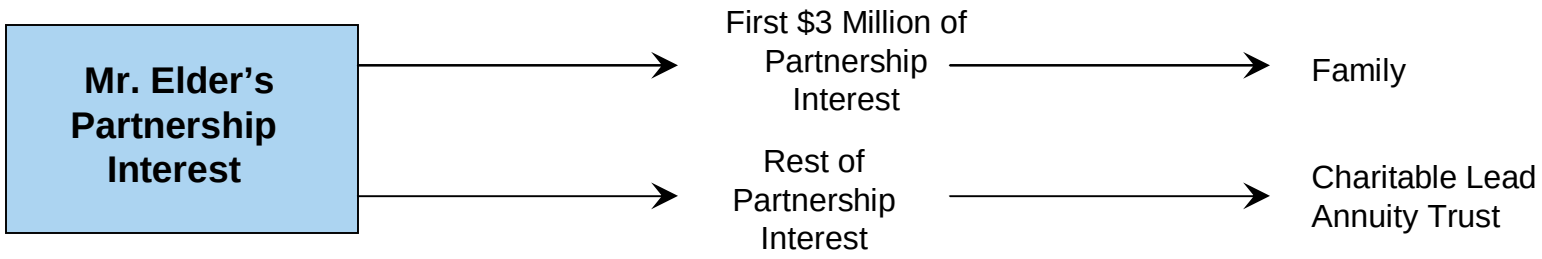
During Ed's lifetime he creates a partnership with his family:



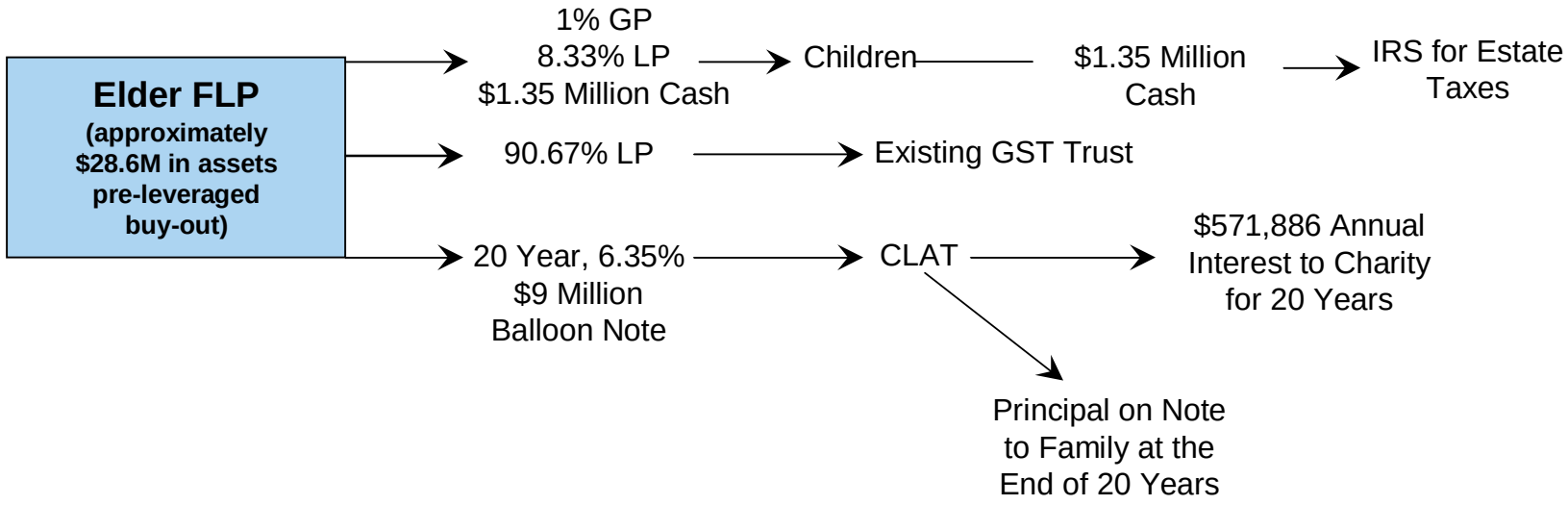
Partner	Ownership (%)
Mr. Elder	0.5% GP; 69.5% LP
Existing GST Trusts for Family	0.25% GP; 29.75% LP

Best Testamentary Charitable Planning Idea For the Family Limited Partnership – The Leveraged Buy-Out Charitable Lead Annuity Trust (Continued)

After Ed's death his will conveys his partnership interest as follows:



After a probate hearing Ed's testamentary CLAT is redeemed as follows:



What Are the Comparative Results of the Leveraged Buy-Out CLAT?

Summary of Results For $28.57 Million of Assets Growing at 8% Per Year (Pre Tax) – No Further Planning vs. 20 Year Testamentary CLAT Technique; 30 Year Future Values; Post-Death Scenarios (assuming Mr. Elder dies in year 1)

Technique	Elder Children	Elder GST Trust	Charity	IRS – Income Tax	IRS – Investment Opportunity Cost	IRS – Estate Taxes	Total
No Further Planning Without a Discount 8%, 30 Years	74,723,823	55,481,827	-	29,497,788	118,801,049	9,000,000	287,504,487
No Further Planning With a Discount 8%, 30 Years	84,904,303	55,481,827	-	33,691,823	108,026,533	5,400,000	287,504,487
CLAT Redemption With a Discount and $3 Million to Family 8%, 30 Years	46,374,710	92,379,335	56,500,420	30,013,402	60,886,619	1,350,000	287,504,487
CLAT Redemption With a Discount and $10 Million to Family 8%, 30 Years	74,166,232	65,866,823	12,555,671	32,874,812	97,540,948	4,500,000	287,504,487

This table is for illustrative purposes only and no representation is being made that any client will or is likely to achieve the results shown.

What Are the Comparative Results of the Leveraged Buy-Out CLAT? (Continued)

- The primary reason the leveraged buy out CLAT technique has a good result for both the client's family and the client's favorite charities, is that, in effect, the client's family is getting two tax deductions for the interest payments that they are making on the note. There is an estate tax deduction (i.e., the zeroed out CLAT annuity payments) and the family owners of the partnership are also receiving an income tax deduction on the interest payments.
- The secondary reason the technique has a good result for the family is that they are not out-of-pocket cash to pay the principal of the note to a third party.
- From the family's perspective, the principal of the note is, in effect, paid to themselves.
- From the family's perspective, they have the assets now subject to the interest obligations of the note held by the CLAT (which could be satisfied with a sinking fund of laddered bonds).

Additional Information

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