Miller Wealth Advisors

CASE STUDY | VOLUME 112

PLANNING FOR THE IMPACT OF CORONAVIRUS ON ESTATE TAXES

GRAT and Life Insurance used in strategy to mitigate client's potential estate tax exposure

THE SITUATION

Joe White*, age 65, is a successful real estate attorney planning to retire this year. He is in a second marriage with Judy, age 60, and has three sons from his first marriage. Joe has a net worth of approximately $12M, the majority of which is held in cash or cash equivalents. Joe's current estate plan leaves all of his assets equally to Judy and his three sons.

THE PROBLEM

In light of the coronavirus pandemic, and ensuing massive government stimulus spending, Joe is more concerned than ever about mitigating future estate taxes at death. Under his current plan, Judy will receive $3 million of his estate and thus any estate taxes will be deferred under the unlimited marital deduction. The remaining $9 million will pass equally to his sons. Joe has already gifted his sons $10M against his $11.58M lifetime estate tax exemption in contemplation that this amount would sunset after 2025 to $5.49M per person. Even after such gifts, we reminded Joe that he would incur an estate tax at death of 40% on $9M.

TAX LAW DEVELOPMENT

Last November, the IRS finalized proposed regulations confirming that there would be no "clawbacks" for individuals who want to take advantage of the increased gift and estate tax exemptions.

THE SOLUTION

While there are many ways to reduce Joe's taxable estate, we focused on the combined use of a zeroed-out Grantor Retained Annuity Trust (GRAT) and Life Insurance. Since stock prices have sharply declined, we proposed that Joe convey $3M of cash to a 9-year GRAT invested in large cap growth stocks (i.e., S&P 500 Index). The concept is one of arbitrage to take advantage of the potential spread between the expected 7% annual investment return and the low IRC Sec 7520 rate (0.80% midterm for 5/20) that is used to determine the annuity payment. The total sum of the zeroed-out GRAT used to repay the estate would be just over $3.1M with the excess market appreciation used to pay the premium on a $1.8M Guaranteed Universal Life Insurance policy (assumes standard nonsmoker).

THE OUTCOME

- Joe places $3M of cash with the GRAT.
- Joe and Judy receive back $3.1M over nine years.
- After the GRAT is complete, $1.8M of life insurance will be removed from Joe's estate and will be able to be used for additional estate tax and liquidity needs.

CONTACT US | BILL MILLER, CFP® CLU, ChFC, AEP® | 561.613.0130 | BILL@MILLERWEALTHADVISORS.COM