# Advance planning for business sales

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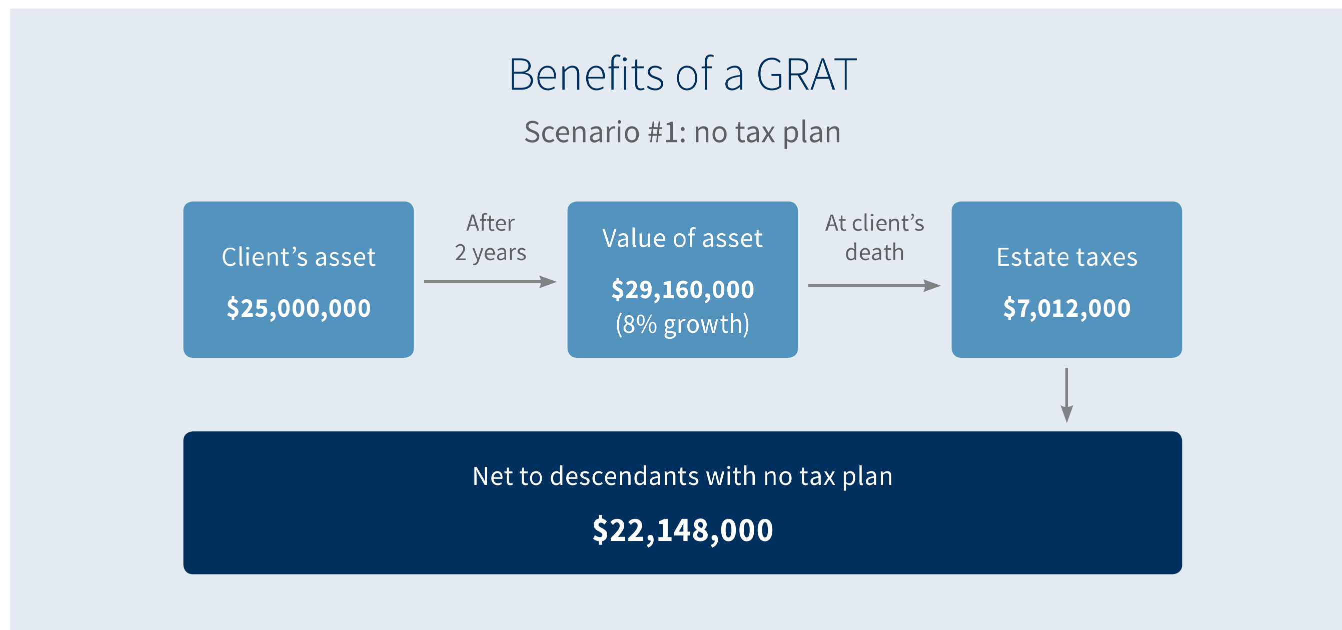
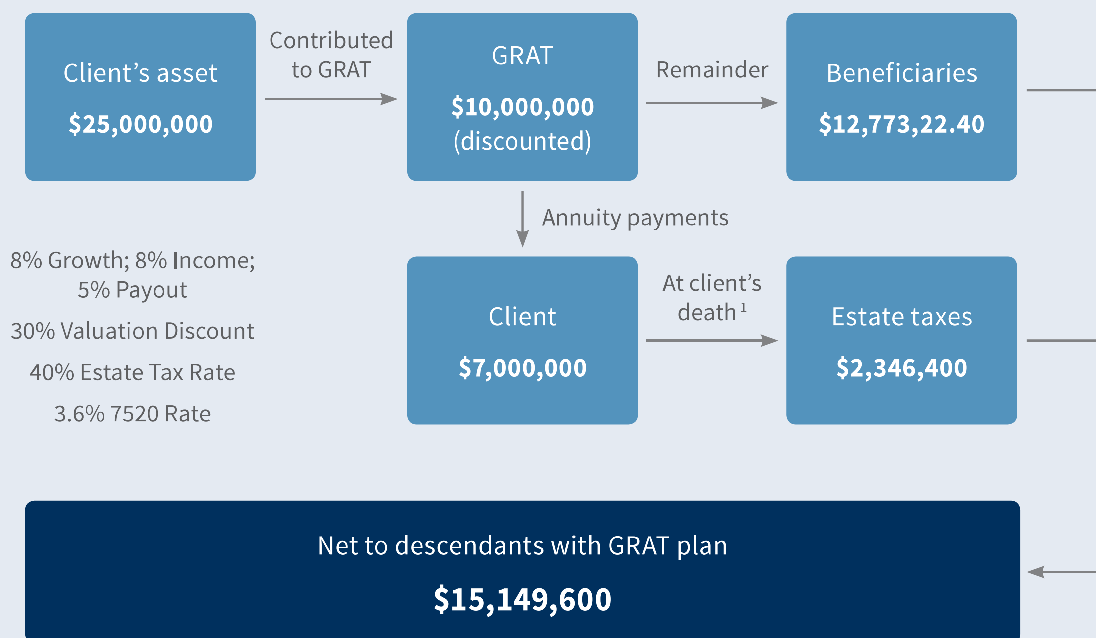
Individuals who experience significant increases in net worth typically consider estate planning after the wealth creation event occurs. However, the best opportunity to transfer wealth and reduce tax exposure often is prior to wealth expansion, such as a business sale, an IPO or merger transaction. A grantor retained annuity trust (GRAT) is one technique that can transfer wealth with little practical impact on the underlying transaction yet deliver results.

For example, if a GRAT is funded with shares from a closely held business, there is the possibility that substantial wealth can be passed to the children tax free. When a minority interest in closely held shares is placed in a GRAT, the shares may be assigned a value that is less than their fair market value because of the inherent lack of liquidity and marketability at the time. If the owner later decides to sell the business and receives a price higher than that previously assigned value, the beneficiaries (typically the children) reap the benefits of the sale premium free of transfer tax. For income tax purposes, though, the grantor is treated as the owner of all of the assets in the GRAT during the GRAT term. Accordingly, income earned on any GRAT asset during the GRAT term is taxable to the grantor. Any transfers between the grantor and the GRAT (such as when assets are contributed to the GRAT or annuity payments are made to the grantor) during the GRAT term are not treated as taxable events for income tax purposes.

A GRAT can be a powerful wealth transfer tool for an asset expected to rapidly appreciate and can create a meaningful difference in net proceeds for family business owners contemplating a sale or transfer.






[1] If the grantor dies during the GRAT term, then all of the remaining GRAT assets (including appreciation) return to the grantor's taxable estate. If the grantor survives the GRAT term, then only the value of the annuity payments remain part of the grantor's taxable estate.

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