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TITLE: Estate Tax Planning for the Transfer of Business Interests

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PANEL: Estate Tax Planning for the Transfer of Business Interests: Structuring Transfers of Businesses for Estate Tax Planning Purposes

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Estate Tax Planning for the Transfer of Business Interests

American Bar Association
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Sample Wealth Transfer Illustrations

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Agenda

- Assumptions
- Transfer to Grantor Retained Annuity Trust (GRAT)
- Sale to a grantor trust for promissory note
- Sale to a grantor trust for a Self-Canceling Installment Note (SCIN)
- Transfer for private annuity

Assumptions

- Grantor’s entire estate is composed of a $2.7mm family business (organized as a Subchapter S Corporation) and $300,000 in cash
- Grantor has $300,000 of lifetime exemption remaining
- Grantor’s is 60 years old with a 24.2 year life expectancy (rounded to 24 years for the purposes of our illustrations)
- Grantor transfers all assets to next generation via (1) a GRAT, (2)sale to a grantor trust for a note, (3) a sale to a grantor trust for a SCIN, or (4) a sale to a child for a private annuity
- Only federal income taxes are considered; income and capital gains taxes are based on current schedules
- Estate and gift tax rates are 45% for all relevant years
- Goal is to transfer the business to the next generation to operate the business, no current intention to sell the business to a third party
- Distribution of S Corporation is treated as ordinary income

Note: This material is distributed with the understanding that we are not providing accounting, legal or tax advice. You should consult with your independent advisors concerning such matters.

Sample economic flows of GRAT

Example			
Value of initial transfer to GRAT[1]	$ 2,700,000	Growth of special asset	12.0%
Assets' basis	$ -	Growth of liquid assets (post-tax)	6.0%
7520 rate	6.00%	Annuity	$ 396,960
Gift to side trust (cash)	$ 300,000	Annual distribution from special assets	$ 500,000
Gift tax exemption available	$ 300,000	Growth of distributions	0.0%
Grantor's life expectancy	24	Term of trust	9

	GRAT/Side Trust[2]		Grantor[3]	Net to Beneficiaries
Year	Value of Transferred Assets	Annuity	After-Tax Annuity Re-investment	After Estate Tax
1	$3,445,040	($396,960)	$221,960	$2,159,950
2	$3,936,222	($396,960)	$457,238	$2,568,089
3	$4,478,648	($396,960)	$706,632	$3,012,691
4	$5,078,006	($396,960)	$970,990	$3,497,382
5	$5,740,636	($396,960)	$1,228,209	$4,013,525
6	$6,473,614	($396,960)	$1,500,862	$4,577,462
7	$7,284,830	($396,960)	$1,789,874	$5,194,077
8	$8,183,090	($396,960)	$2,096,226	$5,868,793
9	$9,178,221	($396,960)	$2,420,960	$10,509,749
24	$56,672,644	$0	$1,193,329	$57,328,975

1 Assets are shares of stock in a family Subchapter S Corporation.

2 Previous year's FMV of special asset + appreciation of special asset + yield of special asset + previous year's FMV of liquid assets + appreciation of liquid assets - annuity payments. (yr1: $2.70 + $0.32 + $0.50 + $0.30 + $0.02 - $0.40 = $3.45)

3 Grantor receives annuity payments and reinvests in liquid assets. Liquid assets are paid out first in satisfaction of annuity and special assets second (if needed). Grantor pays tax on yield of assets in the grantor trust through the grantor's life expectancy. ($0.40 - $0.18{$0.50 * 35%} = $0.22)

Note: Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind. Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax or accounting advice. You should consult with your independent advisors concerning such matters. NumberCruncher 2006.00 software (610-924-0515) has been used to determine the annual payment requirements.

Snapshot of a GRAT, death after year 9, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use GRAT	
Year		Hold asset	Grantor	GRAT/ side trust
0	Assets held/gifted/transferred	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
9	Value of asset	11,599,181	2,420,960	9,178,221
	Estate tax	(5,084,631)	(1,089,432)	-
	Net wealth to beneficiaries	6,514,549	1,331,528	9,178,221
	Total value to beneficiaries	$6,514,549	$10,509,749	
	Value added by transaction		**$3,995,200**	

Assumptions: Initial funding value = $3,000,000; special asset growth rate: year 1-9=12%; IRS discount rate = 6%; annuity rate = 14.7%: liquid growth rate (after-tax) = 6%; yield of special asset = $500,000; transfer tax rate (for transfers at the end of year 9) = 45%. Annuity escalation rate = 0%. If grantor does not survive term, all assets in the GRAT are includable in grantor's estate. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.

Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. GRATs involve complex tax and, in the case of insiders, securities laws issues that should be discussed with your own advisors and company counsel. Annuity will be paid for full term to the grantor or, in case of the grantor's death, to the grantor's estate. Calculation is based on 2000 Tax Court ruling in Walton v. Commissioner (115 T.C. No. 41 (Dec. 22, 2000)).

Snapshot of a GRAT, death after year 2, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use GRAT	
Year		**Hold asset**	**Grantor**	**GRAT/ side trust**
0	Assets held/gifted/transferred	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
2	Value of asset	4,393,460	457,238	3,936,222
	Estate tax	(1,842,057)	(205,757)	(1,619,614)
	Net wealth to beneficiaries	2,551,403	251,481	2,316,608
	Total value to beneficiaries	$2,551,403	$2,568,089	
	Value added by transaction		**$16,686**	
	Year 9 value if grantor dies in year 2*	**$8,855,557**	**vs**	**$10,509,749**

* $1,825,371 estate tax in year 2, is paid with the $1,006,580 available liquid assets, and remaining $818,791 paid with loan proceeds at a 7% interest rate.
Assumptions: Initial funding value = $3,000,000; special asset growth rate: year 1-9=12%; IRS discount rate = 6%; annuity rate = 14.7%: liquid growth rate (after-tax) = 6%; yield of special asset = $500,000; transfer tax rate (for transfers at the end of year 2) = 45%. Annuity escalation rate = 0%. If grantor does not survive term, all assets in the GRAT are includable in grantor's estate. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon.
Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.
Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice.
You should consult with your independent advisors concerning such matters. GRATs involve complex tax and, in the case of insiders, securities laws issues that should be discussed with your own advisors and company counsel. Annuity will be paid for full term to the grantor or, in case of the grantor's death, to the grantor's estate. Calculation is based on 2000 Tax Court ruling in Walton v. Commissioner (115 T.C. No. 41 (Dec. 22, 2000)).

Snapshot of a GRAT, death after year 24, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use GRAT	
Year		Hold asset	Grantor	GRAT/ side trust
0	Assets held/gifted/transferred	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
24	Value of asset	57,865,973	1,193,329	56,672,644
	Estate tax	(25,904,688)	(536,998)	-
	Net wealth to beneficiaries	31,961,285	656,331	56,672,644
	Total value to beneficiaries	$31,961,285	$57,328,975	
	Value added by transaction		**$25,367,690**	

Assumptions: Initial funding value = $3,000,000; special asset growth rate: year 1-24=12%; IRS discount rate = 6%; annuity rate = 14.7%: liquid growth rate (after-tax) = 6%; yield of special asset = $500,000; transfer tax rate (for transfers at the end of year 24) = 45%. Annuity escalation rate = 0%. If grantor does not survive term, all assets in the GRAT are includable in grantor's estate. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.

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Sample economic flows of a sale to a grantor trust

Example			
FMV of assets sold for Installment Note[1]	$ 2,700,000	Growth of special asset	12.0%
Assets' basis	$ -	Growth of liquid assets (post-tax)	6.0%
Mid-term AFR	5.01%	Year 1 payment	$ 435,270
Seed gift to trust (cash)	$ 300,000	Annual distribution from special assets	$ 500,000
Gift tax exemption available	$ 300,000	Growth of distributions	0%
Face value of note	$ 2,700,000	Term of note	9

	Sale[2]		Grantor[3]	Net to Beneficiaries
Year	Value of Transferred Assets	Note Payment	After-Tax Note Re-investment	After Estate Tax[4]
1	$3,406,730	($435,270)	$260,270	$2,028,393
2	$3,872,334	($420,240)	$521,126	$2,851,325
3	$4,402,677	($405,210)	$782,604	$3,732,575
4	$5,004,256	($390,180)	$1,044,740	$4,678,660
5	$5,684,271	($375,150)	$1,284,574	$5,651,152
6	$6,450,707	($360,120)	$1,523,769	$6,744,199
7	$7,312,418	($345,090)	$1,762,285	$7,925,385
8	$8,279,234	($330,060)	$2,000,082	$9,204,515
9	$9,362,064	($315,030)	$2,237,117	$10,592,478
24	$57,113,233	$0	$752,739	$57,527,240

1 Assets are shares of stock in a family Subchapter S Corporation.

2 Previous year’s FMV of special asset + appreciation of special asset + yield of special asset + previous year’s FMV of liquid assets + appreciation of liquid assets - principal and interest payments. (yr1: $2.70 + $0.32 + $0.50 + $0.30 + $0.02 - $0.44 = $3.41)

3 Grantor receives principal and interest payments and reinvests in liquid assets. Liquid assets are paid out first in satisfaction of note repayment and special assets second (if needed). Grantor pays tax on yield of assets in the grantor trust through the grantor's life expectancy. (yr1: $0.44 - $0.18 = $0.26)

4 Model assumes proportionate income tax recognition if death occurs before term of note. The income tax consequences on death of grantor before term of note, are not free from doubt.

Note: Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind. Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax or accounting advice. You should consult with your independent advisors concerning such matters. NumberCruncher 2006.00 software (610-924-0515) has been used to determine the annual payment requirements.

Snapshot of a sale, death after year 9, for illustrative purposes only

Cash flow example: $3,000,000 asset

Year		Scenario 1 Hold asset	Scenario 2: Sale to a grantor trust Grantor	Sale
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
9	Value of asset	11,599,181	2,237,117	9,362,064
	Estate tax	(5,084,631)	(1,006,703)	-
	Net wealth to beneficiaries	6,514,549	1,230,414	9,362,064
	Total value to beneficiaries	$6,514,549	$10,592,478	
	Value added by transaction		**$4,077,929**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-9=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; Year 1 payment = $435,270; transfer tax rate (for transfers at the end of year 9) = 45%. If grantor does not survive term, remaining note principal is includable in the estate. Grantor-type trust, year 1 income tax = 35%; year 1 long-term capital gains = 15%.
Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.
Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. Calculations were made on NumberCruncher 2006.00.

Snapshot of a sale, death after year 2, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Sale to a grantor trust		
Year		Hold asset	Grantor		Sale
0	Assets held/gifted/sold	$3,000,000			$3,000,000
	Gift tax incurred at transfer		$0		
2	Value of asset	4,393,460	521,126		3,872,334
	IRD	-	(315,000)		-
	Estate tax	(1,842,057)	(234,507)		(1,134,378)
	Net wealth to beneficiaries	2,551,403	(28,381)		2,737,956
	Total value to beneficiaries	$2,551,403		$2,709,575	
	Value added by transaction		**$158,172**		
	Year 9 value if grantor dies in year 2*	**$9,050,987**	**vs**	**$ 10,592,478**	

* $1,368,885 estate tax in year 2, is paid with the $691,580 available liquid assets, and $677,305 with loan proceeds at a 7% interest rate.

Assumptions: Initial value = $3,000,000; asset growth rate: year 1-9=12%; asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; Year 1 payment = $435,270; transfer tax rate (for transfers at the end of year 2) = 45%. If grantor does not survive term, remaining note principal is includable in the estate. Grantor-type trust, year 1 income tax = 35%; year 1 long-term capital gains = 15%. Model assumes proportionate income tax recognition at death. Under scenario 1, special asset is held until death and grantor's heirs receive a stepped up basis. The income tax consequences on death of grantor before term of note are not free from doubt; above illustration does not account for any potential 691(c) deduction. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.

Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. Calculations were made on NumberCruncher 2006.00.

Snapshot of a sale, death after year 24, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Sale to a grantor trust	
Year		**Hold asset**	**Grantor**	**Sale**
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
24	Value of asset	57,865,973	752,739	57,113,233
	Estate tax	(25,904,688)	(338,733)	-
	Net wealth to beneficiaries	31,961,285	414,006	57,113,233
	Total value to beneficiaries	$31,961,285	$57,527,240	
	Value added by transaction		**$25,565,955**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-24=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; Year 1 payment = $435,270; transfer tax rate (for transfers at the end of year 24) = 45%. If grantor does not survive term, remaining note principal is includable in the estate. Grantor-type trust, year 1 income tax = 35%; year 1 long-term capital gains = 15%.
Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.
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Sample economic flows of Self-Canceling Installment Note (SCIN)

Example			
FMV of assets sold to grantor trust for SCIN[1]	$ 2,700,000	Growth of special asset	12.0%
Assets' basis	$ -	Growth of liquid assets (post-tax)	6.0%
Adjusted interest rate	7.40%	Year 1 payment	$ 499,800
Seed gift to trust (cash)	$ 300,000	Annual distribution from special assets	$ 500,000
Gift tax exemption available	$ 300,000	Growth of distributions	0%
Initial face amount of note[2]	$ 2,700,000	Term of note	9
7520 rate	6.0%		

	SCIN[3]		Grantor[4]	Net to Beneficiaries
Year	Value of Transferred Assets	Note Payment	After-Tax Note Re-investment	After Estate Tax
1	$3,342,200	($499,800)	$324,800	$3,342,200
2	$3,746,572	($477,600)	$646,888	$3,929,110
3	$4,219,179	($455,400)	$966,101	$4,602,035
4	$4,766,728	($433,200)	$1,282,267	$5,348,225
5	$5,396,642	($411,000)	$1,572,203	$6,129,354
6	$6,117,140	($388,800)	$1,857,336	$7,039,674
7	$6,937,328	($366,600)	$2,137,376	$8,046,884
8	$7,867,298	($344,400)	$2,412,018	$9,160,908
9	$8,918,242	($322,200)	$2,680,939	$10,392,758
24	$56,049,587	$0	$1,816,385	$57,048,599

1 Assets are shares of stock in a family subchapter S Corporation.

2 Based on purchase price adjustment for self cancellation feature, alternatively, initial principal amount could be adjusted to $2,832,947 and the interest rate could be 6%.

3 Previous year's FMV of special asset + appreciation of special asset + yield of special asset + previous year's FMV of liquid assets + appreciation of liquid assets - principal and interest payments. (yr1: $2.70 + $0.32 + $0.50 + $0.30 + $0.02 - $0.50 = $3.34)

4 Grantor receives principal and interest payments and reinvests in liquid assets. Liquid assets are paid out first in satisfaction of note repayment and special assets second (if needed). Grantor pays tax on yield of assets in the grantor trust through the grantor's life expectancy. (yr1: $0.50 - $0.18 = $0.32)

Note: Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind. Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax or accounting advice. You should consult with your independent advisors concerning such matters. NumberCruncher 2006.00 software (610-924-0515) has been used to determine the annual payment requirements.

Snapshot of a SCIN, death after year 9, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use Self-Canceling Installment Note	
Year		Hold asset	Grantor	SCIN
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
9	Value of asset	11,599,181	2,680,939	8,918,242
	Estate tax	(5,084,631)	(1,206,423)	-
	Net wealth to beneficiaries	6,514,549	1,474,517	8,918,242
	Total value to beneficiaries	$6,514,549		$10,392,758
	Value added by transaction		**$3,878,209**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-9=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; Year 1 payment = $499,800; transfer tax rate (for transfers at the end of year 9) = 45%. Grantor-type trust, year 1 income tax = 35%; year 1 long-term capital gains = 15%.

Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.

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Snapshot of a SCIN, death after year 2, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use Self-Canceling Installment Note		
Year		Hold asset	Grantor		SCIN
0	Assets held/gifted/sold	$3,000,000			$3,000,000
	Gift tax incurred at transfer		$0		
2	Value of asset	4,393,460	646,888		3,746,572
	IRD	-	(315,000)		-
	Estate tax	(1,842,057)	(291,100)		-
	Net wealth to beneficiaries	2,551,403	40,788		3,746,572
	Total value to beneficiaries	$2,551,403		$3,787,360	
	Value added by transaction		**$1,235,957**		
	Year 9 value if grantor dies in year 2	**$10,687,831**	**vs**	**$ 10,392,758**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-9=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; Year 1 payment = $499,800; transfer tax rate (for transfers at the end of year 2) = 45%. Grantor-type trust, year 1 income tax = 35%; year 1 long-term capital gains = 15%. Model assumes proportionate income tax recognition at death. Under scenario 1, special asset is held until death and grantor's heirs receive a stepped up basis. The income tax consequences on death of grantor before term of note are not free from doubt. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.
Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. Payment calculations were made on NumberCruncher 2006.00.

Snapshot of a SCIN, death after year 24, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use Self-Canceling Installment Note	
Year		Hold asset	Grantor	SCIN
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
24	Value of asset	57,865,973	1,816,385	56,049,587
	Estate tax	(25,904,688)	(817,373)	-
	Net wealth to beneficiaries	31,961,285	999,012	56,049,587
	Total value to beneficiaries	$31,961,285	$57,048,599	
	Value added by transaction		**$25,087,314**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-24=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; Year 1 payment = $499,800; transfer tax rate (for transfers at the end of year 24) = 45%. Grantor-type trust, year 1 income tax = 35%; year 1 long-term capital gains = 15%.
Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.
Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. Payment calculations were made on NumberCruncher 2006.00.

Sample economic flows of Private Annuity

Example			
FMV of assets sold for Private Annuity[1]	$ 2,700,000	Growth of special asset	12.0%
Assets' basis	$ -	Growth of liquid assets (post-tax)	6.0%
7520 rate	6.00%	Annuity	$ 249,356
Gift to side trust (cash)	$ 300,000	Annual distribution from special assets	$ 500,000
Gift tax exemption available	$ 300,000	Growth of distributions	0.0%
Grantor's life expectancy	24		

	Private Annuity[2]		Grantor[4]	Net to Beneficiaries
Year	Value of Transferred Assets	Annuity[3]	After-Tax Annuity Re-investment	After Estate Tax
1	$3,417,644	($249,356)	$184,866	$3,519,320
2	$3,879,787	($249,356)	$380,824	$4,089,240
3	$4,391,431	($249,356)	$588,540	$4,715,128
4	$4,958,159	($249,356)	$808,719	$5,402,954
5	$5,563,202	($249,356)	$1,030,182	$6,129,803
6	$6,235,138	($249,356)	$1,264,933	$6,930,851
7	$6,981,650	($249,356)	$1,513,769	$7,814,222
8	$7,811,323	($249,356)	$1,777,535	$8,788,967
9	$8,733,752	($249,356)	$2,057,128	$9,865,172
24	$45,194,803	($249,356)	$8,955,375	$50,120,260

1 Assets are shares of stock in a family Subchapter S Corporation.

2 Previous year's FMV of special asset + appreciation of special asset + yield of special asset – tax on yield of special asset + previous year's FMV of liquid assets + appreciation of liquid assets - annuity payments. ($2.70 + $0.32 + $0.50 - $0.18 + $0.30 + $0.02 - $0.25 = $3.42)

3 Tax on annuity is as follows: $0 tax-free, $113,924 long-term capital gains, $135,432 ordinary income. ($0.11 * 15% + $0.14 * 35% = $0.06)

4 Grantor receives annuity, pays applicable ordinary and capital gains tax and reinvests net in liquid assets. Annuity pays out liquid assets first in satisfaction of annuity, and special assets second (if needed). (yr1: $0.25 - $0.06 = $0.18)

Note: Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind. Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax or accounting advice. You should consult with your independent advisors concerning such matters. NumberCruncher 2006.00 software (610-924-0515) has been used to determine the annual payment requirements. In the event seller dies before life expectancy, basis is adjusted to the sum of the payments made.

Snapshot of Private Annuity, death after year 9, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use Private Annuity	
Year		Hold asset	Grantor	PA/side trust
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
9	Value of asset	11,599,181	2,057,128	8,733,752
	Estate tax	(5,084,631)	(925,707)	-
	Net wealth to beneficiaries	6,514,549	1,131,420	8,733,752
	Total value to beneficiaries	$6,514,549	$9,865,172	
	Value added by transaction		**$3,350,623**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-9=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; annuity = $249,356; transfer tax rate (for transfers at the end of year 9) = 45%. Year 1 income tax = 35%; year 1 long-term capital gains = 15%. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.

Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. Annuity calculations were made on NumberCruncher 2006.00.

Snapshot of Private Annuity, death after year 2, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use Private Annuity	
Year		Hold asset	Grantor	PA/side trust
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
2	Value of asset	4,393,460	380,824	3,879,787
	Estate tax	(1,842,057)	(171,371)	-
	Net wealth to beneficiaries	2,551,403	209,453	3,879,787
	Total value to beneficiaries	$2,551,403	$4,089,240	
	Value added by transaction		**$1,537,837**	
	Year 9 value if grantor dies in year 2	**$11,141,747**	**vs**	**$ 9,865,172**

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-9=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; annuity = $249,356; transfer tax rate (for transfers at the end of year 2) = 45%.Year 1 income tax = 35%; year 1 long-term capital gains = 15%. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.
Note: Above example is for illustrative purposes only. These materials should not be construed as providing legal, tax, or accounting advice. You should consult with your independent advisors concerning such matters. Annuity calculations were made on NumberCruncher 2006.00.

Snapshot of Private Annuity, death after year 24, for illustrative purposes only

Cash flow example: $3,000,000 asset

		Scenario 1	Scenario 2: Use Private Annuity	
Year		**Hold asset**	**Grantor**	**PA/side trust**
0	Assets held/gifted/sold	$3,000,000		$3,000,000
	Gift tax incurred at transfer		$0	
24	Value of asset	57,865,973	8,955,375	45,194,803
	Estate tax	(25,904,688)	(4,029,919)	-
	Net wealth to beneficiaries	31,961,285	4,925,456	45,194,803
	Total value to beneficiaries	$31,961,285	$50,120,260	
	Value added by transaction		**$18,158,975**	

Assumptions: Initial value = $3,000,000; special asset growth rate: year 1-24=12%; special asset yield = $500,000; liquid assets growth (after-tax) = 6%; IRS discount rate = 6%; annuity = $249,356; transfer tax rate (for transfers at the end of year 24) = 45%. Year 1 income tax = 35%; year 1 long-term capital gains = 15%. Numbers have been rounded for convenience, are only estimates for illustrative purposes and should not be relied upon. Corporate insiders should consult with securities counsel as to any reporting issues under SEC Section 16 of the Securities Exchange Act of 1934 associated with receiving shares in-kind.

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