

Facebook and Estate Planning

By James F. McDonough, Jr. on May 18th, 2012 Posted in Estate Planning, Social Media

Facebook has grabbed the headlines, but behind the scenes key personnel have undertaken critical estate planning, proving that they are more than just technically savvy. Here's how it worked.

The Wall Street Journal just reported that six of the insiders in *Facebook* established Grantor Retained Annuity Trusts (GRATs) last year. These trusts were established at a time when the estimated fair market value of the Initial Public Offering (IPO) was expected to be about \$29 to \$30 a share. Given that there are now reports that the IPO price may be significantly higher, this strategy would appear to be yielding an immediate benefit.

Unlike family limited partnerships, the IRS has issued detailed regulations on GRATs; therefore it offers a more predictable outcome. It is also easy to implement. A person transfers assets to a GRAT and receives an annuity for a term of years. The amount of the annuity and the length of the term are selected by the taxpayer. IRS regulations give the formula. IRS published the interest rate to be used on a monthly basis, which is 1.6% for May.

A GRAT works well if the property transferred will appreciate in value or produce a return that is higher than the interest rate that the taxpayer is required to use. Simply stated, if the value of the assets increases in excess of 1.6%, the appreciation will escape estate and gift tax. Thus, appreciating assets and a low interest rate are ideal conditions for this strategy.

One IRS requirement is that the assets have to be transferred to the GRAT at fair market value ("FMV"). Publicly-traded shares provide a FMV that is obtainable without an appraisal. No doubt the investment bankers provided the insiders with reasonable and well-supported valuations for the IPO that can also be used to support the GRAT.

The use of GRATs by *Facebook* insiders is a clear indication of the utility of the strategy in a low-interest environment and prior to the demise of the \$5,120,000 exclusion. If ever there were a sign that now is the time to engage in tax planning, this is it.