

By Steven J. Oshins & Kristen E. Simmons

The SCIN-GRAT

A hedging technique takes the mortality risk out of estate planning

Estate planners can learn from financial planners. For years, financial planners have used hedging techniques to reduce risk or to guarantee a desired outcome. This is done by entering into a transaction that moves in the opposite direction as the first transaction in order to avoid or minimize a loss.

Estate planners often recommend life insurance as a hedging tool because it's the ideal solution for handling mortality risk. But what if life insurance is unavailable because the proposed insured is either too old or too unhealthy to qualify for a reasonably priced policy? What if a person wants to reduce the insurance need by handling part of the mortality risk with an advanced estate-planning strategy that leverages the assets removed from the taxable estate without a mortality risk?

Such individuals should consider a SCIN-GRAT, a hedging technique that combines a bet-to-die strategy with a bet-to-live strategy. More specifically, it combines a self-cancelling installment note (SCIN) with a grantor retained annuity trust (GRAT), enhanced with a few additional twists.

SCIN SALE

The first phase of the transaction is to create a generation-skipping transfer (GST) tax-exempt dynasty trust funded with a gift sufficient enough to substantiate a large installment sale to the trust. The trust is drafted as an income tax defective trust, or grantor trust, in order

to make the settlor the owner of the trust for income tax purposes. This is accomplished by intentionally violating one or more of the grantor trust rules.¹ Because the settlor is the owner of the trust for income tax purposes, he can sell assets to the trust without income tax ramifications.²

Traditionally, the seller sells a discounted asset, such as a limited partnership (LP) interest, a non-controlling limited liability company (LLC) membership interest or a non-controlling stock interest, to the dynasty trust. The trust typically purchases the discounted asset from the seller in exchange for an interest-only promissory note at that month's applicable federal rate (AFR) with a balloon payment due at the end of a term of years.

The twist with the SCIN-GRAT technique is that the promissory note is structured as a SCIN instead of a traditional note.

A SCIN is a promissory note that pays the seller until the first to occur of a selected term of years or the seller's death. When either event occurs, all remaining payments due on the SCIN are cancelled. With an interest-only SCIN, the seller's death before the end of the selected term of years cancels not only the remaining interest payments but also the large balloon payment of principal payable at the end of the term of years. The term of years selected must be within the seller's life expectancy using the Internal Revenue Service tables.³ Because the SCIN cancels when the seller dies, the value of the note (other than the payments received by the seller before the seller's death) should not be included in the seller's estate.⁴

A SCIN is a bet-to-die strategy for the buyer. The buyer is betting that the seller will die before the end of the SCIN's term of years, canceling the remaining payments. An early death creates a windfall for the buyer (in this case, the dynasty trust).



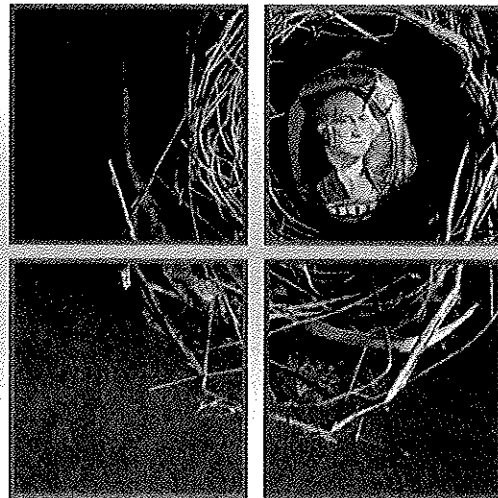
Steven J. Oshins and Kristen E. Simmons are members of the Law Offices of Oshins & Associates, LLC in Las Vegas

To avoid the SCIN being recharacterized by the IRS as a taxable gift from the seller to the buyer, an interest rate premium or a principal premium must be applied to the note. This premium also legitimizes the sale for a SCIN because it applies adequate and bargained-for consideration for the cancellation feature. The premium amount depends on the seller's age and the note's term. Generally, the older the seller, the larger the premium that must be used to avoid a gift. (See "SCIN Term and Premium Analysis," p. 20.) The sale in exchange for the SCIN should be an arm's length transaction between the seller and the trustee of the dynasty trust. It should be properly documented and enforceable by the seller/owner in all events. Also, the trust should pay the required interest and principal payments when due.⁵ If the SCIN is structured properly and paid as required, and if the seller has no reasonable expectation of a shortened life expectancy, the SCIN should be upheld even if the seller dies before the SCIN term expires.⁶ When structuring the sale for a SCIN, it is important to analyze the cash flow of the asset to be sold to determine whether it will be sufficient to make the required SCIN payments. If there is a shortfall, payments can be made in-kind using non-cash assets.

To provide the greatest amount of mortality leverage, the SCIN's term should be as long as possible within the seller's life expectancy, determined using the IRS mortality tables. Because the mortality tables often are outdated and include in the sample the lives of people who cannot afford quality medical care, most wealthy clients live beyond the term of years selected. Therefore, without hedging the SCIN sale with the second leg of the transaction, the SCIN option may

cause more wealth to be returned to the estate than the amount that would be paid to the estate using a traditional non-SCIN promissory note.

To hedge against this risk of a SCIN overpayment, the SCIN-GRAT technique combines the initial leg of the transaction (the SCIN sale) with a bet-to-live



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strategy (a GRAT). The combination of a bet-to-die strategy and a bet-to-live strategy insures a successful end result.

SCIN GIFT

After the SCIN sale has been consummated, the owner of the SCIN sets up a single member LLC that is taxed as a disregarded entity for income tax purposes. The SCIN owner contributes the SCIN, along with other assets, to the LLC. Because the LLC is a disregarded entity for income tax purposes, contributing the SCIN to the LLC does not trigger a taxable event. The LLC generally is structured with a 1 percent voting interest and a 99 percent non-voting interest in contemplation of the owner transferring non-voting interests.

Next, the LLC owner establishes one or more *Walton*⁷ GRATs for the benefit of his spouse and/or children.⁸ The LLC owner then transfers by gift a portion of his non-voting or minority LLC interests to the GRAT(s) in exchange for an annuity of substantially equal value. An appropriate valuation discount, based upon an independent appraisal, is applied to the gift of the non-voting or minority LLC interests. Because the GRAT(s) is (are) structured as a grantor trust(s) for income tax purposes, even after the transfer of the non-voting LLC interests to the GRAT(s), the LLC continues to be taxed as a disregarded entity.⁹

A GRAT is a trust to which the settlor gifts an asset in exchange for an annuity that is generally payable for a term of years. If structured as a qualified annuity, the value of the annuity may be subtracted from the value of the asset transferred to the GRAT to determine the value of the gift.¹⁰ After the *Walton* case, it's possible to structure the annuity so that the total taxable gift by the settlor is zero or close to zero.

A GRAT has several benefits. First, it's a strategy sanctioned by the Internal Revenue Code, and therefore acceptable to the IRS, if structured properly. Also, the annuity amount paid can be structured as a percentage of the initial fair market value (FMV) of the trust, rather than a dollar figure. Therefore, if the IRS challenges the value of the asset transferred to the GRAT, the annuity automatically adjusts itself and should not cause a significant gift tax exposure for the settlor.

A GRAT has two main drawbacks: (1) For it to be successful in transferring assets outside of the settlor's

SCIN Term and Premium Analysis

The maximum term of a SCIN depends upon the settlor's age and the mortality risk premium applied to the SCIN depends upon the term selected

Age	Note's Maximum Term of Years	Mortality Risk Premium	
		Principal	Interest
40	42	\$316,020.99	0.1570%
45	37	828,886.27	0.4230
50	33	1,564,474.49	0.8180
55	28	2,291,064.20	1.2670
60	24	3,305,246.84	1.9220
65	19	4,075,221.36	2.6650
70	16	5,658,254.22	3.9940
75	12	6,623,909.97	5.5210
80	9	11,295,147.44	9.5980
85	6	10,654,639.29	13.2690

Notes

- Calculations were done using NumberCruncher Software.
- The Principal Mortality Risk Premium amounts listed here are in addition to the base principal amount; and the Interest Rate Mortality Risk Premium will be in addition to the minimum applicable federal rate (AFR).
- This chart assumes an Internal Revenue Code Section 7520 rate of 3.40 percent, a mid-term AFR of 2.87 percent and a long-term AFR of 4.40 percent, the rates provided by the Internal Revenue Service for transfers made in April of 2008. For purposes of the Mortality Risk Premium for Principal, it assumes a fair market value (FMV) of \$10 million of property transferred in exchange for the self-cancelling installment note (SCIN).
- All numbers assume that the SCIN is structured to pay interest-only for the term, with a balloon payment of principal (including the principal premium, if applicable) at the end of the SCIN's term.

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estate, the settlor needs to survive the term of years selected for the GRAT. If the settlor dies during the GRAT's term, part or all of the GRAT assets are included in the settlor's estate. (2) A GRAT generally cannot generation-skip.¹¹ Therefore, the assets remaining in the GRAT after the GRAT term usually are included in the estates of the settlor's children.

In the SCIN-GRAT strategy, the GRAT is used as a

hedging tool in case the settlor outlives the SCIN's term. If the settlor dies prior to the expiration of the GRAT term, the settlor will not have outlived the SCIN term and the remaining SCIN payments will be cancelled. Because the main asset of the GRAT is a non-voting membership interest in an LLC that has as its primary asset the SCIN obligation, if the settlor dies during the term of the GRAT, there will be little value remaining in the GRAT for inclusion in the settlor's estate. Therefore, the survivorship requirement inherent in a traditional GRAT is not as strong a concern in the GRAT portion of the SCIN-GRAT strategy.

The settlor (LLC owner) establishes a GRAT term that is as short as possible, based on an analysis of the SCIN payments attributable to the portion of the LLC transferred to the GRAT(s). This figure is known in advance because the SCIN payments already have been set. The GRAT's term should generally be much shorter than the SCIN's term because the value of the non-voting or minority LLC interests gifted to the GRAT should be subject to a valuation discount for lack of marketability and control. (See "SCIN-GRAT Diagrammed," p. 24.)

SCIN-GRAT Results

The benefits of the SCIN-GRAT depend on when the settlor dies. There are three possibilities:

- (1) the settlor dies before the end of the GRAT term and before the end of the SCIN term;
- (2) the settlor dies after the end of the GRAT term, but before the end of the SCIN term; and
- (3) the settlor dies after the end of both the GRAT term and the SCIN term.

• **Scenario One: The settlor dies before the GRAT term ends and before the SCIN term ends.** If the settlor dies before the GRAT term ends and before the SCIN term ends, the settlor's family receives a windfall in the dynasty trust because the balance of the interest payments and the SCIN balloon payment are

cancelled pursuant to the SCIN's terms. The GRAT is unsuccessful because the settlor failed to outlive its term of years. But the GRAT's failure is insignificant because its primary asset is an LLC interest with an unsuccessful SCIN as its underlying primary asset. Although no one wishes for the settlor to die, on paper, that creates the best economic result for the family because it results in a significant value in the generation-skipping dynasty trust.

Example—Using the fact pattern in "See How It Works" on p. 23, assume the settlor dies three years after the SCIN and GRAT transactions have been executed.¹²

Payment trail—In Year 1 through Year 3, the dynasty trust makes three interest payments to the owner of the SCIN (now the LLC), totaling \$3,740,400. The GRAT in turn pays back to the settlor annuity payments totaling \$3,421,643.40 (assuming a 10 percent growth/income rate, the settlor has included in his estate from the GRAT annuity payments an amount equal to \$3,775,213.22). This leaves a balance in the LLC of \$1,017,194.78 (the value of the additional \$500,000 worth of assets contributed to the LLC along with the SCIN (including 10 percent growth/income) plus the value of the difference (including growth) between the SCIN interest payments made to the LLC from the dynasty trust and the value of the annuity paid back from the GRAT to the settlor).

To the extent possible, the SCIN payments will be made from the dynasty trust to the LLC using cash flow from the underlying asset sold to the dynasty trust. The LLC will in turn distribute the cash received in satisfaction of the SCIN payment to its members (the settlor and the GRAT) and the GRAT will use this cash to make the required annuity payment back to the settlor. If the cash flow of the underlying asset is insufficient to make the required SCIN payment, a portion or all of the payment can be made in-kind. The drawbacks of an in-kind payment are that: (1) it may require an additional independent appraisal of the underlying asset; and (2) if the underlying asset is discountable, it may result in leakage of the discount amount back into the settlor's estate.

Results—The settlor's death at the end of Year 3 creates an immediate windfall to the dynasty trust because

See How It Works

Using a likely set of facts and assumptions, these are the benefits of the SCIN-GRAT

FACT PATTERN / ASSUMPTIONS

Age of Seller/Settlor **80 years**
 Life Expectancy of Seller/Settlor **9.5 years**
 Gift to Dynasty Trust **\$1,000,000**
 Non-Discounted Value of Asset Sold to Dynasty Trust **\$15,000,000**
 Discounted Value of Asset Sold to Dynasty Trust **\$10,000,000**
 Assumed Growth/Income of Underlying Asset **10%**
SCIN
 Principal Amount **\$10,000,000**
 Term of Note **9 years**
 Section 7520 Rate **3.40%**
 Mid-Term Applicable Federal Rate **2.87%**

Mortality Risk Premium (Interest) **9.5980%**
 Total Interest Rate **12.4680%**
 Annual SCIN Interest Payment **\$1,246,800**
GRAT
 Non-Discounted Value of LLC (SCIN note plus \$500,000 other assets) **\$10,500,000**
 Value of Discounted 99 % Non-voting LLC Interest Contributed to GRAT **\$7,000,000**
 Term of Annuity **7 years**
 Percentage Payout **16.29354%**
 Annuity Amount (assumes level GRAT payments) **\$1,140,547.80**
 Gift Amount **\$1.93**

RESULTS

	If Settlor Dies 3 years into Sample Transaction (Before GRAT ends)	If Settlor Dies 7 years into Sample Transaction (After GRAT ends but before SCIN ends)	If Settlor Dies 10 years after Sample Transaction (After GRAT and SCIN end)
Amount Includible from GRAT Annuity Payments	\$3,775,213.22	\$10,820,572.01	\$14,402,181.35
Amount Includible from GRAT (because settlor did not survive term)	1,017,194.78	0	0
Total Included in Settlor's Estate	4,792,408.00	10,820,572.01	14,402,181.35
Total Transferred to GRAT Remainder Trust (Outside of Settlor's Estate)	0	1,982,391.34	16,518,670.87
Total Transferred to Dynasty Trust (Outside of Settlor's Estate)	17,169,092.00	19,350,868.80	11,875,898.37
Total Transferred Outside of Settlor's Estate	17,169,092.00	21,333,260.14	28,394,569.24

Notes

- The life expectancy of the seller/settlor is based on the tables outlined in Treasury Regulations Section 1.72.
- The amounts listed as included in the settlor's estate do not take into account income taxes paid by the settlor on behalf of the dynasty trust and on behalf of the GRAT. Because the dynasty trust and GRAT are structured as grantor trusts, the settlor's estate will be further reduced by any income taxes paid on income earned in the GRAT and dynasty trust.

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the dynasty trust does not have to pay the LLC the \$10 million cancelled SCIN principal payment, and does not have to pay six cancelled SCIN interest payments totaling \$7,480,800. Assuming a 10 percent growth/income rate of the underlying asset sold to the dynasty trust, at the end of Year 3, the total value of the dynasty trust is \$17,169,092. Because the SCIN obligation is cancelled by reason of the settlor's death, the entire \$17,169,092 passes to the dynasty trust without an additional transfer tax. Therefore, the SCIN portion of the SCIN-GRAT strategy effectively transfers \$17,169,092 outside of the settlor's estate.

If the settlor dies at the end of Year 3, the GRAT fails because the settlor died before its seven-year term expires. The settlor will have included in his estate the value of the annuity payments paid back to him from the GRAT, totaling \$3,421,643.40 (assuming a 10 percent growth/income rate, \$3,775,213.22 should be includible in the settlor's estate as a result

of the annuity payments). Also, because the settlor did not survive the term of the GRAT, some or all of the 99 percent LLC interest (\$1,017,194.78) will be included in the settlor's estate under IRC Section 2036¹³. This results in a total amount includible in the settlor's estate of \$4,792,408.00.

Because both the dynasty trust and the GRAT are structured as grantor trusts (the settlor pays the income tax on the income earned in each trust), the settlor's estate is further reduced by any income tax liability paid on behalf of the dynasty trust or GRAT during the three years from the inception of the transaction. If the income tax payments are factored into the analysis, the results are even more staggering.

• **Scenario Two: The settlor dies after the GRAT ends, but before the SCIN term ends.** If the settlor dies after the GRAT term ends, but before the SCIN term ends, there's a windfall partially in the dynasty trust and partially in the GRAT remainder trust, the continuing trust that receives all GRAT assets remaining at the end of the GRAT term. The sooner the settlor dies, the greater the value of assets in the dynasty trust and the less the value of assets in the GRAT remainder trust. Regardless, there is a combined windfall between the two trusts because the remaining interest payments and SCIN balloon payment cancel pursuant to the terms of the SCIN.

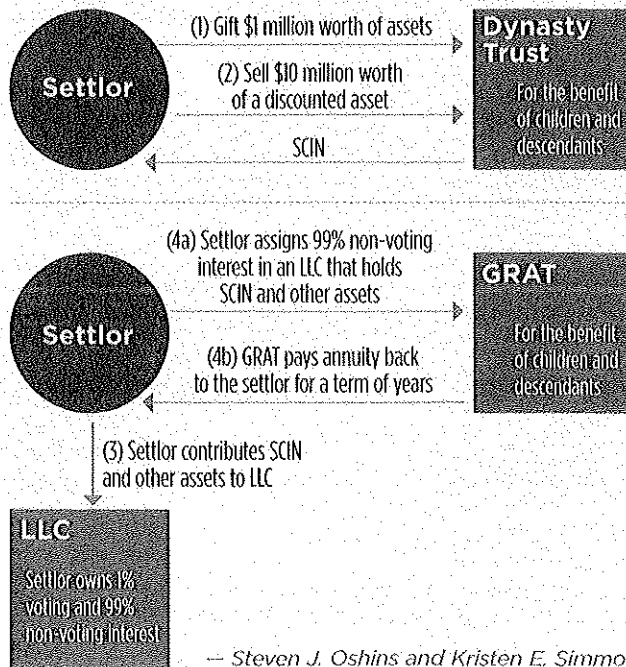
Example—Using the same fact pattern, assume the settlor dies seven years after the SCIN and GRAT transactions have been executed.

Payment trail—In Years 1 through Year 7, the dynasty trust makes seven interest payments to the owner of the SCIN (now the LLC), totaling \$8,727,600. The GRAT in turn pays back to the settlor all of the required annuity payments, totaling \$7,983,834.60 (assuming a 10 percent growth/income rate, after Year 7 the settlor will have included in his estate from the GRAT annuity payments an amount equal to \$10,820,572.01). This leaves a balance in the LLC of \$1,982,391.34.

Results—The settlor's death at the end of Year 7 cancels the \$10 million SCIN principal payment and cancels the two remaining SCIN interest payments (totaling

SCIN-GRAT Diagrammed

These are the steps involved



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\$2,493,600). Assuming a 10 percent growth/income rate of the underlying asset sold to the dynasty trust, at the end of Year 7 the total value of the dynasty trust is \$19,350,868.80. Because the SCIN obligation is cancelled by reason of the settlor's death, the entire \$19,350,868.80 passes to the dynasty trust without an additional transfer tax. Therefore, the SCIN portion of the SCIN-GRAT strategy effectively transfers \$19,350,868.80 outside of the settlor's estate.

If the settlor dies at the end of Year 7, the GRAT succeeds because the settlor outlived the seven-year term. The settlor has included in his estate the value of the annuity payments paid back to him from the GRAT (assuming the 10 percent growth/income rate, at the end of Year 7, \$10,820,572.01 should be includible in the settlor's estate as a result of the annuity payments). The balance of the portion of the LLC transferred to the GRAT passes to the GRAT remainder trust without any additional gift tax and is not included in the settlor's estate. Assuming the same rate of growth/income as given in our fact pattern, the total amount transferred through the LLC to the GRAT remainder trust at the end of Year 7 should be \$1,982,391.34. Thus, the net result of the SCIN-GRAT transaction if the settlor dies after Year 7 is inclusion of \$10,820,572.01 (from the GRAT annuity payments) in the settlor's estate, reduced further by any income taxes paid by the settlor on behalf of the dynasty trust and GRAT during the seven-year term, and a wealth transfer of \$21,333,260.14.

• **Scenario Three: The settlor dies after the SCIN term ends.** If the settlor dies after the SCIN term ends, because of the GRAT hedge, the GRAT remainder trust receives a huge amount of assets. It receives SCIN interest payments made after the GRAT term plus the large SCIN balloon payment because that payment is due upon the settlor surviving the SCIN term.

Example—Using the same fact pattern, assume the settlor dies at the end of Year 10, after the final SCIN payment was made.

Payment trail—At the end of Year 9 the dynasty trust has paid the LLC (owner of the SCIN) all of the SCIN interest payments as well as the SCIN principal payment outlined in the SCIN obligation. The GRAT in

turn has paid back to the settlor all of the required annuity payments, totaling \$7,983,834.60 (assuming a 10 percent growth/income rate, the settlor has included in his estate from the GRAT annuity payments an amount equal to \$14,402,181.35). This leaves a balance in the LLC of \$16,518,670.87 (again, because the LLC has received all of the SCIN interest payments and the SCIN principal payment).

Results—Because the settlor died after the SCIN term, the value of the dynasty trust is reduced by the total obligations under the SCIN. Assuming a 10 percent growth/income rate of the underlying asset sold to the dynasty trust, after the SCIN obligations are paid, the total value of the dynasty trust at the end of Year 10 should be \$11,875,898.37.

Because the settlor survived the GRAT term, the GRAT succeeds in transferring assets to the GRAT remainder trust. The settlor has included in his estate the value of the annuity payments paid back to him from the GRAT (assuming the 10 percent growth/income rate, \$14,402,181.35 should be includible in the settlor's estate as a result of the annuity payments). The balance of the portion of the LLC transferred to the GRAT passes to the GRAT remainder trust without an additional gift tax, and is not included in the settlor's estate. Assuming the same rate of growth/income as outlined in our fact pattern, the total amount transferred through the LLC to the GRAT remainder trust at the end of Year 10 should be \$16,518,670.87 (because the value of the remaining SCIN interest and principal payments is held in the LLC). Thus, the net result of the SCIN-GRAT transaction if the settlor dies at the end of Year 10 is inclusion of \$14,402,181.35 (from the GRAT annuity payments) in the settlor's estate, reduced further by any income taxes paid by the settlor on income earned by the dynasty trust and the GRAT, and a total of \$28,394,569.24 transferred outside of the settlor's estate (\$16,518,670.87 to the GRAT remainder trust and \$11,875,898.37 to the dynasty trust).

Summary and Warning

Regardless of whether the settlor dies before the GRAT term ends or before or after the SCIN term

ends, there is a significant wealth shift and estate tax savings using the SCIN-GRAT technique. But care must be taken to ensure that the settlors retain sufficient wealth or access to wealth in case they survive the GRAT term because the GRAT annuity stream stops at the end of the GRAT term—and the cash flow the settlors were receiving as a result of the transaction ceases at such time.

The SCIN-GRAT technique was originally developed for older clients, but it's also a tool that can shift wealth out of a younger client's estate. For a younger client, the number of years between the end of the GRAT term and the end of the SCIN term is much larger. This longer period allows more wealth to shift to the client's beneficiaries. Regardless of the client's age, by combining the bet-to-die strategy of a SCIN with the bet-to-live strategy of a GRAT, the client's estate can be reduced and the savings can inure to the benefit of the client's beneficiaries. ■

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The purpose of this article is to advance the exchange of ideas. A taxpayer interested in implementing any of the techniques discussed should seek advice from an independent tax advisor based on that taxpayer's particular circumstances. To the extent this article expresses an opinion on one or more federal tax issues, that opinion was not written to be used, and cannot be used, for the purpose of avoiding penalties.

Endnotes

1. Customarily, the grantor trust rules violated to create grantor trust status for income tax purposes, but not for transfer tax purposes, are: the power of a non-adverse party to add beneficiaries to the trust (See Internal Revenue Code Section 674(c)); the power of the settlor, in a non-fiduciary capacity, to reacquire trust assets by substituting property of an equivalent value (See IRC Section 675(4)(C)); and sometimes including the settlor's spouse as a permissible beneficiary of income and principal (See IRC Section 677(a)(1)).
2. See Revenue Ruling 85-13, 1985-1 CB 184.
3. If the term of the note exceeds the seller's life expectancy, it could cause recharacterization of the sale transaction as a private annuity. See General

Counsel Memorandum (GCM) 39503 (June 28, 1985).

4. See *Estate of Moss v. Commissioner*, 74 TC 1239 (1980), acq. in result 1981-1 CB 2 (holding that the remaining note balance due under a self-cancelling installment note was not includible in the decedent's gross estate under IRC Section 2033 because the cancellation provision was part of the bargained-for consideration); See also *Estate of Frane v. Comm'r*, 98 TC 341 (1992) (reviewed by the court), *aff'd in part, rev'd in part*, 998 F.2d 597 (8th Cir. 1993).
5. See *Estate of Buckwalter v. Comm'r*, 46 TC 805 (1966) (self-cancelling feature accomplished through a scheme in which donee controlled whether to extinguish the debt, which was the equivalent of a testamentary disposition that would have been taxable).
6. See *Estate of Costanzo v. Comm'r*, 998 F.2d 597 (8th Cir. 1993) (upholding a self-cancelling note arrangement even though the transferor died within five months of the transaction, because at the time of the transaction his life expectancy was longer than the term of the self-cancelling arrangement); see also Rev. Rul. 86-72, 1986-1 CB 253; GCM 39503 (May 7, 1986), Issue 2(B); Tax Management Portfolio, 805-2nd T. M., Private Annuities and Self-Canceling Installment Notes, at pp. A-37 (2002).
7. *Walton v. Comm'r*, 115 T.C. 589 (2000), acq. in Notice 2003-72, 2003-44 Internal Revenue Bulletin 964.
8. There are several ways to structure the grantor retained annuity trust (GRAT) portion of the SCIN-GRAT strategy. For other examples, see generally Richard A. Oshins, Steven J. Oshins and Robert S. Keebler, "The SCIN/GRAT: An Innovative Strategy to Hedge Your Bet," *Estate Planning* (September 2007), at p. 3.
9. See Rev. Rul. 2004-77, I.R.B. 2004-31, 119, Aug. 2, 2004.
10. See IRC Section 2702.
11. See IRC Section 2642(f). The estate tax inclusion period (ETIP) rule prohibits a settlor's generation-skipping transfer (GST) tax exemption from being allocated to a transfer while it is possible that the transferred asset could be included in the settlor's estate, except by reason of the three-year rule provided by IRC Section 2035. Because the IRS takes the position that the assets transferred to the GRAT may be includible in the settlor's estate if the settlor dies during the GRAT's term, the settlor's GST tax exemption cannot be allocated to the assets transferred to the GRAT until the end of the GRAT's term. At the end of the GRAT's term, the assets transferred to the GRAT generally will have grown. Therefore, the GRAT generally is not known as a tool to leverage a settlor's GST tax exemption.
12. Note that this example is an oversimplification of the strategy, as it is prudent not to fund the GRAT on the same date as the date of the SCIN sale so as to reduce the possibility that the series of transfers will be recast as one transfer under a step-transaction theory.
13. See Proposed Treasury Regulations Section 20.2036-1, 119097-05 72 F.R. 31487-31491 (June 7, 2007). Note that the \$1,017,194.78 figure assumes that the limited liability company (LLC) interest is included in the settlor's estate with no valuation discount, assuming the IRS concludes that it should be aggregated with the 1 percent voting LLC interest that is included in the settlor's estate under IRC Section 2033.