The Administration's Fiscal Year 2014 Revenue Proposals

Three Things are Certain: Death, Taxes and *nothing* is Permanent

Barely four months after the passage of the American Taxpayer Relief Act of 2012 ("ATRA") purporting to "permanently" address a volatile estate and gift tax framework, the Department of the Treasury has released the Obama Administration's Fiscal Year 2014 Revenue Proposals (the "Proposals"). Among the expected proposals modifying certain income tax provisions, the Administration lays bare its view of ATRA's estate and gift tax structure by proposing a reversal of the estate, gift and generation-skipping ("GST") tax exclusions to 2009 levels together with an increase of the maximum estate and GST tax rates from the current 40% to 45%. It is clear from the Proposals that the historically high exemptions set by ATRA (as well as the viability of other established estate planning vehicles) remain a moving target.

PERTINENT PROVISIONS:

ESTATE, GIFT AND GENERATION-SKIPPING TAXES

The 2014 Proposals provide as follows:

- The estate, generation-skipping and gift tax parameters as they existed in 2009 would be made ***permanent*.**
    - ***Top estate and GST tax rates***: 45% (currently 40%)
    - ***Estate tax exclusion***: $3.5 million (currently $5.25 million)
    - ***GST exclusion***: $3.5 million (currently $5.25 million)
    - ***Gift tax exclusion***: $1 million (currently $5.25 million)
    - There would be no indexing for inflation
- Portability as enacted would continue.
- The new parameters would be effective for estates of decedents dying and for transfers made after December 31, 2017.

GRATS

The issue of GRATs (grantor retained annuity trusts) has been debated in Congress for several years. The 2014 Proposals once again require a minimum ten-year term for a GRAT and also negate the possibility of creating a "zeroed-out" GRAT by also mandating a maximum term of the life expectancy of the annuitant plus ten years.

IDGTS

The 2014 Proposals also contain drastic new provisions concerning the assets held in Grantor Trusts. The Intentionally Defective Grantor Trust ("IDGT"), a staple of estate planning, allows a grantor to be treated as the owner of trust property for income tax purposes but excludes the trust property from a grantor's estate for ***estate*** tax purposes. The 2014 Proposals are drafted to close what the administration views as a "loophole" between the income and transfer tax rules applicable to these trusts which essentially allow a grantor to be treated as an owner of the trust for income tax purposes but permit the exclusion of the assets from the gross estate of the grantor for estate tax purposes. With regards to IDGTs, the proposed amendment would do the following:

- The assets of the trust would be included in the gross estate for estate tax purposes.
- Distributions from the trust to beneficiaries during the grantor's life would be subject to gift tax.
- If, during the life of the grantor, the grantor ceased to be treated as the owner of the trust for income tax purposes, any remaining trust assets would be subject to gift tax.

The 2014 Proposals would affect IDGTs created on or after the enactment and apply to any trust to which a contribution is made on or after the date of enactment. If passed, these provisions would radically alter the effectiveness of the IDGT's estate planning benefits.

IRA'S (AND PRESUMABLY OTHER RETIREMENT ACCOUNTS)

For the first time, the Proposals include a provision that would cap how much people could maintain in individual tax-deferred retirement accounts at $3 million. No further contributions would be permitted after the $3 million cap is reached. The cap is arrived at by estimating the amount of money that would purchase an annuity of $205,000 per year for a retiree. The $205,000 limit is the Internal Revenue Code Section 415 amount on the maximum defined benefit plan.

To be sure, the forgoing are merely proposals which cannot be effectuated without Congressional action. However, what is noteworthy is that they are a clear signal that the Administration is continuing to focus on wealth preservation strategies and estate and gift planning structures which it has long sought to modify. In light of what remains an ever-shifting landscape despite contrary assurances, this remains an optimal time to accomplish long-term estate and gift tax planning.

A copy of the General Explanations of the Administration's Fiscal Year 2014 Revenue Proposals can be found at the following link: http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2014.pdf

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