Permanent? That's five years under Obama estate tax plan

Bid to lower exemption after January deal unexpected; advisers sitting tight for now

By **Darla Mercado**
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Apparently, permanent works out to be about five years in Washington time.

At least that would seem to be the case when it comes to President Barack Obama's plan to alter the estate tax drastically mere months after a “permanent” deal on the marital exclusion was reached.

In the White House budget released Wednesday, the president proposed lowering the death tax exclusion to $3.5 million, from the $5 million figure agreed on in January.

The swift move to rejigger has not gone over well with some planners. “I can't believe that they'd revisit that,” said Martin M. Shenkman, an estate planning attorney at an eponymous firm in Tenafly, N.J. “Why would they put themselves and everyone through that again?”

It's a fair question. Clients went into panic mode during the fiscal cliff negotiations in December, when the White House and legislators wrangled over reducing the estate tax exclusion to as little as $1 million. Indeed, scores of the wealthy made last-minute changes in their estate plans with the expectation that this year would bring harsher tax treatments.

Ultimately, estates, gifts and generation-skipping trusts ended up being taxed at a maximum rate of 40%, with the federal estate tax exclusion set permanently at an inflation-indexed $5 million — or $5.25 million for this year.

That would all change if the president's plan is approved as is — a scenario that, while worrying to clients, seems unlikely. Indeed, estate experts are telling advisers to sit tight for now. “Practitioners shouldn't jump the gun,” said David Pratt, a partner in the personal planning department at Proskauer Rose LLP. “This is a wish list. It's a starting point for negotiations.”

Where the plan ends up is anybody's guess. But here's what the White House is currently proposing:

The estate, gift and generation-skipping trust tax parameters would go back to 2009 levels: Estates and GSTs will be taxed at a maximum rate of 45%, with a lifetime exclusion of $3.5 million. Gifts would be taxed at a maximum rate of 45% with a lifetime exclusion of $1 million. The estate provision would become effective in 2018, as would transfers. The exclusions will not be indexed for inflations.

Grantor retained annuity trusts will be subject to minimum terms. GRATs are a great estate-planning tool because they permit wealthy individuals to pass large assets to family members and save on taxes. Grantors, meanwhile, can receive an annuity for a fixed period of years, funded by the assets within the trust.

GRAT terms are typically brief — less than two years — because if the grantor dies within the term, the assets will be counted as part of his or her estate. Mr. Obama's proposal would require that all trusts have a minimum term of 10 years and a maximum term of 10 years beyond the annuitant's life expectancy. The value of the remainder must be greater than zero, and the annuity must not decrease during the term of the GRAT.

The duration of the generation-skipping trust tax exemption would be limited. Currently, each person has a lifetime GST tax exemption of $5.25 million, which can be allocated to the benefit of younger relatives who are receiving asset transfers (a wealth transfer from a grandparent to a grandchild). The grantor can also allocate his or her GST exemption to shield the assets transferred and future appreciation from GST taxes. The limits proposed by Mr. Obama on the duration of the GST tax exemption would take effect on the 90th anniversary of the creation of the trust. The 90 year limit is a big deal, considering some states have abolished rules against perpetuity — which limit the duration of a trust — while others have lengthy periods, according to Mr. Pratt. Florida, for instance, permits trusts to last as long as 360 years.

Estate planners, for now, are taking a wait-and-see approach. “It all depends on which provisions pass,” Mr. Pratt said. “Some of them have prospective effects, and others could require some changes in trusts that already exist.” GRATs that are in place now, for instance, would likely be grandfathered if these proposals came to pass. GSTs that already exist, however, could be affected if that 90-year provision goes through, he added.

Mr. Shenkman noted that this might be a good time for people to think about the gifts they could've made last year. “The ones who need to be most concerned are the people who are very ill or in their late 80s,” he said. “Even if the proposal doesn't happen, you might save on taxes by making your gifts now.”

“We wouldn't do anything different now just because of this,” said Gavin Morrissey, vice president of wealth management at **Commonwealth Financial Network**. “If it does anything, it'll make those people who missed the boat last year [on tax and estate planning] act while those structures are still available. But I don't put a lot of stock into this proposal.”

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