REPEAL OF THE DEATH TAX? SHOVING ASIDE THE RHETORIC TO DETERMINE THE CONSEQUENCES OF THE ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001

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I. INTRODUCTION

"For centuries, philosophers and economists have debated whether governments should curtail inherited wealth."[1] The debate centers on whether states should protect their citizens' property after death.[2] One side considers it a "natural" or "fundamental" right of parents to bequeath property to their children at death.[3] The other side weighs social concerns more heavily by placing more importance on the interests of society.[4] These philosophers proclaim: "'It is not the fortunes which are earned, but those which are unearned, that it is for the public good to place under limitation.'"[5] Regardless of the view you share, an estate tax does exist, at least until December 31, 2009.[6]

The estate tax is a tax on the transfer of property at death, and is levied on the decedent's estate, not on the recipients of the estate.[7] Although there is disagreement as to when the estate tax originated, it likely drew its first breath in 1797, during our early days as a nation, when the Republic faced uncertain international relations and the constant possibility of war.[8] However, the newly enacted tax was repealed in 1802.[9] The tax was reinstated in 1862 in the midst of the Civil War, repealed in 1870, and enacted once "again in 1802 [sic] during the Spanish-American War."[10] The tax was repealed shortly thereafter, but has been

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1. James R. Repetti, *Democracy, Taxes, and Wealth*, 76 N.Y.U. L. REV. 825, 828 (2001).

2. *Id.*

3. *Id.* (citing JOHN LOCKE, TWO TREATISES OF GOVERNMENT 206-07, 210 (Peter Laslet ed., Cambridge Univ. Press 1988) (1690)).

4. *Id.* at 828-29.

5. *Id.* (citing JOHN STUART MILL, PRINCIPLES OF POLITICAL ECONOMY 808 (W.J. Ashley ed., Longmans, Green & Co. 1923) (1848)); *see also* HOWARD M. ZARITSKY, PRACTICAL ESTATE PLANNING AND DRAFTING AFTER THE ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001 ¶ 1.01[3] (2001) (providing that the Conference Committee believes, and thus sides with, those philosophers who believe decedents should be able to pass their property on to their heirs free of tax consequences, "that it is inappropriate to impose a tax by reason of the death of a taxpayer").

6. *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16 [hereinafter 2001 Tax Act], § 501(a), 115 Stat. 69 (2001) (to be codified at I.R.C. § 2210(a)).

7. W. LESLIE PEAT & STEPHANIE J. WILLBANKS, FEDERAL ESTATE AND GIFT TAXATION: AN ANALYSIS AND CRITIQUE 4 (2d ed. 1995).

8. *Compare* E.E. Anderson, *Estate Taxes*, 14 No. 4 COMPLEAT LAW. 58 (1997) ("Many say that estate tax was created in 1916, but in reality it was originally enacted in 1797 . . . ."), *with* Stephanie A. Weber, *Re-Thinking the Estate Tax: Should Farmers Bear the Burden of a Wealth Tax?*, 9 ELDER L.J. 109, 112-13 (2001) (noting that the estate tax was first instituted in 1787) (footnotes omitted).

9. Anderson, *supra* note 8, at 58.

10. *Id.* (Spanish-American War actually took place during 1902, not 1802.); *see also* Weber, *supra* note 8, at 113 (noting that the estate tax appeared again in 1898, during the Spanish-American War).

with us since its latest restoration in 1916, during World War I.[11] The current rationale for the tax is not to raise revenue for war,[12] but rather, as President Theodore Roosevelt reasoned, "'to put out of the power of the owner of one of these enormous fortunes' . . . amassed by an elite few . . . ."[13] Over the years, the tax has undergone a number of "face changes."[14] These changes represent perhaps the most alluring characteristic of the estate-planning field—it is continually evolving.[15] Estate planners are consistently in a state of instability due to these changes in tax law, but were daunted when President Bush signed landmark tax legislation on June 7, 2001.[16] The Economic Growth and Tax Relief Reconciliation Act of 2001 (2001 Tax Act) "represent[s] the biggest reduction in federal taxes since 1981."[17] The Bush Administration and Republicans alike touted the 2001 Tax Act as a sweeping reform "that would eliminate the 'death tax,' eliminate 'double taxation,' save the 'family farm,' and save the 'small business' while at the same time stimulate the slowing economy."[18] "However, if one looks beyond the rhetoric to the text of the [2001 Tax A]ct it is apparent that it is not a panacea for all."[19]

Leading up to "repeal," there was a growing opposition to transfer taxes, not just by philosophers and economists, but also by the average American.[20]

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11. Anderson, *supra* note 8, at 58.
12. Weber, *supra* note 8, at 113.
13. *Id.* at 114 (citing Lori Nitschke, *Eager to Hack At Estate Tax, Foes Welcome New Allies*, CONG. Q., *available at* http://www.deathtax.com/deathtax/cq91199.html (Sept. 11, 1999)).
14. *See* Anderson, *supra* note 8, at 58 (noting that there have been a number of changes to the law since its enactment).
15. Jeffrey L. Burr, *Recent Legislative Changes Impacting Trusts and Estates*, 9 NEV. LAW., July 2001, at 11.
16. *See id.* (noting that practitioners have heralded the 2001 Tax Act as "landmark"). It has been cleverly asserted: "On June 7, 2001, the Federal Estate Tax suffered an untimely death at the age of eighty-five. The tax's demise marks the passing of a controversial figure in American public life." M.C. Mirow & Bruce A. McGovern, *An Obituary of the Federal Estate Tax*, 43 ARIZ. L. REV. 625, 625 (2001).
17. Burr, *supra* note 15, at 12.
18. William S. Forsberg, *Icarian Estate Planning: Risks and Opportunities in the 2001 Tax Act*, BENCH & B. MINN., Aug. 2001, at 23. Mirow and McGovern note that former President Clinton twice saved the estate tax from repeal by exercising his veto power. Mirow & McGovern, *supra* note 16, at 626. Its new "lease on life" was short-lived, however, as President Bush signed the 2001 Tax Act shortly after taking office. *See id.* The 2001 Tax Act, however, does more than the Bush Administration has advertised. The 2001 Tax Act "ended the current stepped-up basis rule and implemented a complex carryover basis regime whose burdensome administrative, tracing, record keeping, and reporting requirements have been described by one commentator as 'the four horsemen of the carryover basis apocalypse.'" *Id.* (quoting Stefan F. Tucker, *Thoughts on Radical Estate and Gift Tax Reform*, 91 TAX NOTES 163, 165-66 (2001)).
19. Forsberg, *supra* note 18, at 23.
20. Karen C. Burke & Grayson M.P. McCouch, *Death Without Taxes?*, 20 VA. TAX REV. 499, 500-02 (2001).

This passion for repeal remains something of a conundrum.[21] "After all, these taxes produce relatively little revenue; they are paid by a select group of wealthy taxpayers; and the average effective transfer tax rate is less than half of the stated top marginal rate of fifty-five percent."[22] Moreover, the estate tax is clearly the most progressive element in our tax system, affecting only the wealthiest two to three percent of Americans.[23] The average American will never have to agonize over the complex estate tax regime.[24] For example, in 2002 the applicable exclusion amount was $1 million.[25] This means that a person could have died with up to $1 million in his or her taxable estate and not have to pay any estate taxes. "When all is said and done, only about 1% of decedents leave an estate with *any* estate tax liability."[26] "Perhaps, as Michael Graetz has suggested, the explanation lies in an irrational optimism that leads a majority of Americans to believe that they will rank among the wealthiest one or two percent when they die."[27]

Several factors may explain the recent growth in opposition to estate taxes.[28] A greater percentage of estates have been pushed above the applicable exclusion amount in recent years due to inflation and real economic growth.[29] Additionally, since implementation of the marital deduction in 1981, many taxable estates in the hands of surviving spouses exceed the applicable exclusion amount.[30] According to one expert, the remarkable growth in stock prices over the last decade has "swollen the expectations of baby boomers who stand to receive a massive intergenerational wealth transfer over the next twenty years."[31]

Which beliefs are most rational can be debated without end. The focus should be on whether the federal estate tax is meeting its objectives and the effect of the 2001 Tax Act. In Part II of this Note, I discuss the objectives of the estate tax, and, with impartiality, decide in Part III whether these objectives are being

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21. *Id.*
22. *Id.* at 501-02.
23. Krisanne M. Schlachter, *Repeal of the Federal Estate and Gift Tax: Will It Happen and How Will It Affect Our Progressive Tax System?*, 19 VA. TAX REV. 781, 788 (2000) (citing PHILIP D. OLIVER & FRED W. PEEL, JR., TAX POLICY 103 (1996)).
24. Edward J. McCaffery, *The Uneasy Case for Wealth Transfer Taxation*, 104 YALE L.J. 283, 297 (1994).
25. 2001 Tax Act, § 521(a), 115 Stat. 71 (2001) (to be codified at I.R.C. § 2010(c)).
26. McCaffery, *supra* note 24, at 298 (footnotes omitted).
27. Burke & McCouch, *supra* note 20, at 502 (citing Michael J. Graetz, *To Praise the Estate Tax, Not to Bury It*, 93 YALE L.J. 259, 285 (1983)).
28. *Id.* at 501.
29. *Id.*; *see also* I.R.C. § 2010(c) (2000) (providing applicable exclusion amounts for specific taxable years).
30. Burke & McCouch, *supra* note 20, at 501; *see also* I.R.C. § 2056 (providing a deduction for certain property interests bequeathed to a surviving spouse).
31. Burke & McCouch, *supra* note 20, at 501.

met. Part IV provides a summary of the 2001 Tax Act. Finally, Part V examines the effects of the 2001 Tax Act on a hypothetical decedent, states, charities, and the estate planning industry.

II. OBJECTIVES OF THE ESTATE TAX

Thomas Jefferson wrote to James Madison in 1789: "'The earth belongs in usufruct to the living; . . . the dead have neither powers nor rights over it. The portion occupied by any individual ceases to be his when [he] ceases to be[,] and [it] reverts to the society.'"[32] Generally, advocates of the estate tax declare there to be three major goals of the estate tax.[33] The first goal, which received particular attention in the 1930s, is to reduce concentrations of wealth.[34] The second goal of the estate tax is to produce revenue.[35] The final goal, which has been promulgated recently, is to add "an element of progressivity to the overall federal tax system."[36] An examination of each of these goals follows.

A. *Reducing Concentrations of Wealth*

"Redistribution of wealth is a concept related to the notion of equality of opportunity."[37] Politicians, philosophers, and academics disagree on the effects of wealth concentration.[38] However, for the most part, "[e]conomic studies are remarkably unanimous in suggesting that high concentrations of wealth correlate with poor economic performance in the long run."[39] Most studies have suggested that greater inequality reduces the rate of growth.[40] "Published studies that have examined twenty-five year periods have found that high income concentration at the beginning of the twenty-five year period correlates with poor economic

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32. Repetti, *supra* note 1, at 830-31 (alteration in original) (quoting Letter from Thomas Jefferson to James Madison (Sept. 6, 1789), *in* 5 THE WRITINGS OF THOMAS JEFFERSON 115-16 (Paul Leicester Ford ed., 1895)).

33. *Compare* John E. Donaldson, *The Future of Transfer Taxation: Repeal, Restructuring and Refinement, or Replacement*, 50 WASH. & LEE L. REV. 539, 541 (1993) (citing Louis Eisentstein, *The Rise and Decline of the Estate Tax*, 11 TAX L. REV. 223, 231, 235-36 (1956) (noting three goals of the estate tax)), *with* Schlachter, *supra* note 23, at 788-89 (suggesting the estate and gift tax have two main objectives) (footnotes omitted).

34. Donaldson, *supra* note 33, at 541.

35. *Id.*

36. *Id.*

37. Schlachter, *supra* note 23, at 790 (citing Mark L. Ascher, *Curtailing Inherited Wealth*, 89 MICH. L. REV. 69, 70-71, 88 (1990)).

38. Repetti, *supra* note 1, at 828-29 (citing RONALD CHESTER, INHERITANCE, WEALTH, AND SOCIETY 11-33 (1982) (citing Ascher, *supra* note 37, at 76-84)).

39. *Id.* at 831.

40. *Id.* at 832 (citing Philippe Aghion et al., *Inequality and Economic Growth: The Perspective of the New Growth Theories*, 37 J. ECON. LIT. 1615, 1617 (1999)).

growth in the subsequent twenty-five years."[41] These long-term studies strongly challenge those once prominent idealists who believed "inequality is good for incentives and therefore good for growth . . . ."[42] Modern economists make arguments that are simply more solid. For example, one study performed by Roberto Perotti found that higher marginal tax rates correlate with higher growth.[43] On the other hand, some economists proclaim failure to invest in education is the likely cause of the "wealth concentration-low growth correlation."[44] Explanations for the correlation between wealth concentration and the failure to invest in education have generally taken two forms.[45] One explanation is that "[t]he inability to invest in human capital traps many families in intergenerational poverty, thus slowing the nation's economic growth."[46] Other experts suggest "[a]n increase in family wealth leads to lower fertility rates and to higher investment in human capital."[47] Therefore, "[w]hen wealth is highly concentrated, higher fertility rates may result in lower investment in education, and as a result, lower productivity growth."[48] James Repetti notes:

> The statistics are strikingly consistent. Children who grow up in poor households are more likely to become teen mothers, to drop out of high school, to accumulate fewer years of education, and to perform worse on cognitive tests. Children whose parents did not complete high school are much more likely to become dropouts themselves. The adult children of the poor are more likely to be unemployed as young adults and more likely to be on welfare.[49]

In short, the deprivations suffered by one generation seem to be having a grim impact on future generations.[50]

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41. *See id.* (citing a number of studies showing that high concentrations of wealth have adverse effects on the growth rate of countries).

42. *Id.* at 835 (quoting Aghion, *supra* note 40, at 1615) ("The conventional wisdom was that inequality should contribute to increased growth because: (1) the wealthy had a higher marginal propensity to save than the poor; (2) only the wealthy could make the large capital commitments necessary for industrial growth; and (3) the poor would be motivated to work harder than the wealthy.")).

43. *Id.* at 837 (citing Roberto Perotti, *Growth Income Distribution and Democracy: What the Data Say*, 1 J. ECON. GROWTH 149, 170-71 (1996)).

44. *Id.* at 838 (footnotes omitted).

45. *Id.* at 839.

46. *Id.* (citing Oded Galor & Josehp Zeira, *Income Distribution and Macroeconomics*, 60 REV. ECON. STUD. 35, 41, 43 (1993)).

47. *Id.* (citing Perotti, *supra* note 43, at 177-82).

48. *Id.* at 839-40 (footnotes omitted).

49. *Id.* at 838.

50. *Id.* at 839.

In his studies on wealth concentration, Perotti was also able to conclude that "large disparities of wealth cause sociopolitical instability, which impedes growth."[51] Uncertainty due to sociopolitical instability disrupts market behavior and labor relations.[52] "One need only look to the effect of social unrest in some American urban areas to appreciate the impact of such unrest on investment in those areas."[53] Finally, Perotti asserts that high concentrations of wealth have an adverse effect "on the effectiveness of democracies to the extent that an objective of a democracy is to give all participants an equal voice."[54]

B. *Production of Revenue*

The second goal of the estate tax is to produce revenue.[55] Historically, in comparison to breaking up concentrations of wealth, production of revenue may be the more important goal.[56] In its early days, the estate tax contributed a significant amount of revenue to the total tax system.[57] For example, "In the mid to late 1930s, the transfer tax system . . . produce[d] more than six percent of total revenues and in one year, 1936, ten percent."[58] In 1934, transfer tax revenues were twenty-seven percent of individual income tax revenues.[59] "In 1936, the $379 million produced in transfer taxes amounted to more than fifty-six percent of the $674 million produced by the individual income tax."[60] Although historical residue is often relevant, the more important inquiry is whether the estate tax is producing a significant amount of revenue today. This examination follows in Part III.B.

C. *Contribution to Progressivity*

Some commentators proclaim that a third goal of the estate tax is to add an element of progressivity to the federal tax system.[61] The estate tax acts as a backdrop to the income tax system by taxing wealth from "tax-preferred

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51. *Id.* at 840 (citing Perotti, *supra* note 43, at 173-77).
52. *Id.*
53. *Id.*
54. *Id.* (citing Edward B. Foley, *Equal-Dollars-Per-Voter: A Constitutional Principle of Campaign Finance*, 94 COLUM. L. REV. 1204 (1994); David A. Strauss, *Corruption, Equality, and Campaign Finance Reform*, 94 COLUM. L. REV. 1369, 1382 (1994)).
55. Donaldson, *supra* note 33, at 541 (citing Eisentstein, *supra* note 33, at 231); Schlachter, *supra* note 23, at 789 (footnotes omitted).
56. Donaldson, *supra* note 33, at 542 (citing Eisentstein, *supra* note 33, at 231).
57. *Id.*
58. *Id.*
59. *Id.*
60. *Id.*
61. *See, e.g.*, *id.* at 541 (citing Graetz, *supra* note 27, at 272).

sources."[62] Many believe the most efficient way to add progressivity to a tax system is to simply change the marginal income tax rates.[63] However, "high marginal tax rates may have unacceptable efficiency costs."[64] On the other hand, estate taxes, levied upon death, have less effect on an individual's decision-making regarding savings and investment in comparison to income taxes, which are levied annually.[65] In sum, experts assert that the greatest testimonial to the progressivity of estate taxes is that these taxes only impinge on those in the "top tier" of income distributions.[66]

III. ARE THESE OBJECTIVES BEING MET?

A. *Are the Rich Getting Richer?*

Inter vivos transfers and bequests account for nearly half of all wealth accumulations.[67] Consequently, taxing wealth transfers should aid in breaking up concentrations of wealth.[68] However, the transfer tax regime has failed to play a meaningful role in the disintegration of wealth concentration.[69] One commentator noted: "[I]t is hard to imagine that a system could have any significant effect on the redistribution of wealth without raising more than a modest amount of revenue."[70] For example, "in 1992 transfer taxes produced revenues of approximately $12 billion from the wealthiest one percent of the population," however, "that amount is relatively minuscule in relation to the objective."[71] Additionally, total wealth held by the richest one percent of our nation has remained remarkably stable.[72] From 1958 until 1972, the richest one

62. Burke & McCouch, *supra* note 20, at 504.

63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.* (citing William G. Gale & Joel B. Slemrod, *A Matter of Life and Death: Reassessing the Estate and Gift Tax*, 88 TAX NOTES 927, 930 (2000)).

67. Repetti, *supra* note 1, at 856.

68. *Id.*

69. Donaldson, *supra* note 33, at 542.

70. Schlachter, *supra* note 23, at 791.

71. Donaldson, *supra* note 33, at 542.

72. Graetz, *supra* note 27, at 271 (citing *Federal Estate and Gift Tax: Public Hearings and Panel Discussions Before the House Comm. on Ways and Means*, 94th Cong., 2d Sess. 390, at 1311, 1315 (1976) [hereinafter *Public Hearings and Panel Discussions*]). Christopher Erblich also analyzed the effects of the estate tax on redistribution of wealth and provided the following table:

SHARES OF NET WORTH HELD BY TOP WEALTHHOLDERS, 1962-1989

Percent of Population	1962	1983	1986	1989
0.5	24.8	24.3	23.9	28.8
1.0	32.2	31.5	31.7	37.1

percent of the population possessed approximately one-quarter of the national wealth.[73] This statistic saw a decline from one-quarter to one-fifth in the period between 1972 and 1976,[74] however, there is nothing pointing to the estate tax as playing the causal role for this decline.[75]

Moreover, while reduction in concentrations of wealth is a stated goal of the estate tax, "most estate and gift tax legislation in recent years has substantially undermined this objective by reducing the overall progressivity of the estate and gift tax system."[76] Congress knowingly lessened the tax burden of the rich when it passed the Tax Reform Act of 1976,[77] which unified the estate and gift tax systems.[78] In 1981, Congress again moved contrary to the goal of breaking up concentrations of wealth by passing the Economic Recovery Tax Act of 1981.[79] This Act expanded the unified credit, permitted an unlimited marital deduction, and phased in a reduction of the maximum rate bracket from seventy percent to fifty percent.[80] The 2001 Tax Act, which features a gradually increasing applicable exclusion amount,[81] decreasing maximum marginal tax rates,[82] and eventual repeal in 2010,[83] is yet another contributor in a string of tax legislation that has caused the estate tax to fail in breaking up concentrations of wealth. "Absent a significant change in the political climate, which appears unlikely in the foreseeable future, it is improbable that the system will be called upon to more effectively address perceived problems of wealth concentration."[84]

However ineffective the recent trend in estate tax legislation has been at reducing concentrations of wealth, a recent study has determined that eliminating the estate tax "would increase the percentage of national wealth held by the top one percent from a conservative estimate of a ten percent increase to an

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Christopher E. Erblich, *To Bury Federal Transfer Taxes Without Further Adieu*, 24 SETON HALL L. REV. 1931, 1938 (1994) (footnotes omitted) (copyright 1994, Seton Hall Law Review, reprinted with permission of the publisher).

73. *Id.* (citing *Public Hearings and Panel Discussions*, *supra* note 72, at 1317 (1976)).

74. *Id.* (citing J. Smith, Trends in Concentration of Personal Wealth in the United States (Draft Paper for Meeting of the Int'l Ass'n for Research on Income and Wealth (Aug. 1981))).

75. *Id.*

76. Schlachter, *supra* note 23, at 790-91.

77. Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520 (1976) (codified as amended in scattered sections of 26 U.S.C.).

78. Donaldson, *supra* note 33, at 541 (citing Tax Reform Act of 1976).

79. Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, 95 Stat. 172 (1981) (codified as amended in scattered sections of 26 U.S.C.).

80. Donaldson, *supra* note 33, at 541 (citing Economic Recovery Tax Act of 1981).

81. 2001 Tax Act, § 521(a), 115 Stat. 70 (2001) (to be codified at I.R.C. § 2010(c)).

82. 2001 Tax Act, § 511(c)(2)(B), 115 Stat. 70 (to be codified at I.R.C. § 2001(c)(2)).

83. 2001 Tax Act, § 501(d), 115 Stat. 69 (to be codified at I.R.C. § 2210(a)).

84. Donaldson, *supra* note 33, at 542.

aggressive estimate of a two-fold increase."[85] Additionally, the estate tax also encourages charitable contributions, which reduces wealth transferred within a family, while at the same time aiding those in need.[86] A 1994 study examining decedents who died in 1982 found that on average, charitable bequests, estate expenses, and taxes account for forty-one percent of the net worth of decedents with gross estates over $10 million.[87] In conclusion, due to recent trends in tax legislation, the estate tax has failed to significantly reduce concentrations of wealth. However, total repeal, without some alternative transfer tax levied at death, would simply make the problem even worse.

B. *Does the Estate Tax Raise a Significant Amount of Revenue?*

Since World War II, transfer tax revenues have rarely exceeded two percent of total federal tax revenues,[88] and due to recent tax legislation,[89] these

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85. Repetti, *supra* note 1, at 856 (citing John Laitner, Simulating the Effects on Inequality and Wealth Accumulation of Eliminating the Federal Gift and Estate Tax, at 2 (Apr. 17, 2000) (unpublished manuscript, on file with New York University Law Review)).

86. *Id.*

87. *Id.* at 857 (footnotes omitted).

88. Christopher Erblich provided the following table in his article:

Year	Total Federal Receipts ($ billions)	Transfer Tax Receipts ($ billions)	Transfer Tax Receipts—% of Total Fed. Receipts
1959	90.6	1.4	1.55
1960	97.0	1.8	1.86
1961	99.0	2.0	2.02
1962	107.2	2.1	1.96
1963	115.5	2.2	1.90
1964	116.2	2.6	2.24
1965	125.8	2.8	2.23
1966	143.5	3.0	2.09
1967	152.6	3.1	2.03
1968	176.8	3.1	1.75
1969	199.6	3.6	1.80
1970	195.2	3.7	1.90
1971	202.6	4.6	2.27
1972	232.0	5.4	2.33
1973	263.7	5.1	1.93
1974	294.0	4.8	1.63
1975	194.8	4.9	1.66
1976	339.9	5.6	1.65
1977	384.0	7.2	1.88
1978	441.2	5.2	1.18

revenues have diminished to 1.1%.[90] This decline may also reflect the greater importance of other taxes to the federal government with respect to raising revenue.[91] In 1992, transfer taxes were budgeted to be $12 billion, while income taxes were budgeted to be $479 billion.[92] Income tax revenues in 1998 alone were greater than the total transfer taxes levied over the last century.[93] "In terms of revenue significance, transfer taxes have evolved from a role of major importance to that of virtually a de minimis component."[94] Stunningly, in 1992, "revenues from taxes on alcohol and tobacco (excise taxes) exceeded those from transfer taxes by more than $1 billion."[95] Moreover, some experts believe the estate tax "might actually be losing money for the government."[96] The Internal Revenue Service (IRS) incurs costs administering the tax, while taxpayers incur costs complying with it and trying to avoid it.[97] Additionally, even if it were desirable for transfer taxes to produce a significant amount of revenue, it is doubtful the system could ever be transformed into any type of revenue-

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1979	504.7	5.5	1.09
1980	553.0	6.5	1.18
1981	639.0	6.9	1.08
1982	635.4	7.5	1.18
1983	660.0	5.8	0.88
1984	725.8	6.0	0.83
1985	788.6	6.4	0.81
1986	827.2	7.0	0.85
1987	913.8	7.2	0.79
1988	972.3	7.6	0.78
1989	1,059.3	8.9	0.84
1990	1,107.4	11.6	1.05
1991	1,122.2	11.0	0.98

Erblich, *supra* note 72, at 1935 (footnotes omitted) (copyright 1994, Seton Hall Law Review, reprinted with permission of the publisher).

89. *See supra* notes 77, 79, 81-83 and accompanying text.

90. Donaldson, *supra* note 33, at 542-43 (citing COMMERCE DEP'T, STATISTICAL ABSTRACT OF THE UNITED STATES 316 (1992)).

91. *Id.* at 543.

92. *Id.*

93. Weber, *supra* note 8, at 125.

94. Donaldson, *supra* note 33, at 543.

95. *Id.*

96. McCaffery, *supra* note 24, at 300-01.

97. Repetti, *supra* note 1, at 869; *see also* Weber, *supra* note 8, at 125 ("Furthermore, the estate tax actually causes the government to lose money annually when one takes into account not only the administrative burden of collecting one of the 'costliest taxes for the IRS to administer,' but also the numerous loopholes that currently exist.").

producing machine.[98] In fact, no country realizes a significant amount of revenue from their transfer tax system.[99]

In sum, empirical data suggests that a tax on transfers at death is not, and probably will never become, a major source of revenue.[100] However, with the federal government constantly operating with insufficient revenues and large deficits,[101] along with the chance of the war on terrorism lasting long into the future, it is doubtful that total repeal will be achieved (or at least should be achieved) without some type of supplementation.[102]

C. *Does the Estate Tax Add a Sufficient Amount of Progressivity to the Overall Tax System?*

Unlike the first two goals of the estate tax,[103] which have almost universally been proclaimed to have failed their objectives,[104] some commentators believe the estate tax has contributed a significant amount of progressivity to the tax system.[105] However, its contribution to the progressivity of the federal tax system is hampered by the narrowness of the transfer tax base.[106] Despite this narrow focus, the estate tax acts as a backdrop to the federal income tax, which has traditionally favored the wealthy, by "reaching wealth accumulated from tax-preferred sources."[107] Moreover, there appears to be "a

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98. Donaldson, *supra* note 33, at 543 (citing Henry J. Aaron & Alicia H. Munnell, *Reassessing the Role for Wealth Transfer Taxes*, 45 NAT'L TAX J. 121, 133 (1992)).

99. *Id.*

100. Graetz, *supra* note 27, at 270.

101.
> About $150 billion pass at death each year. Yet in 1988, the federal wealth transfer taxes raised less than $8 billion. Obviously, these taxes could raise much more. If, to take the extreme example, we allowed the government to confiscate all property at death, we could almost eliminate the deficit with one stroke of a Presidential pen.

Ascher, *supra* note 37, at 72-73.

102. *See* Donaldson, *supra* note 33, at 543.

103. *See supra* text accompanying notes 34 and 35.

104. *See* discussion *supra* Part III.A-B.

105. *See* Graetz, *supra* note 27, at 272. Graetz further noted:
> [T]he estate and gift taxes—despite their low revenue yield—contributed nearly one-third as much to the progressivity of our tax structure as did rates in excess of the average individual income tax even though the estate tax imposed a smaller levy on inheritances than would have been imposed if bequests had been taxed as ordinary income.

Graetz, *supra* note 27, at 272.

106. Burke & McCouch, *supra* note 20, at 503-04 (citing Harry L. Gutman, *Reforming Federal Wealth Transfer Taxes After ERTA*, 69 VA. L. REV. 1183, 1194 (1983); William G. Gale & Joel B. Slemrod, Rethinking the Estate and Gift Tax: Overview 35 tbl.7 (July 2000) (unpublished manuscript, on file with Virginia Tax Review)).

107. *Id.*

strong prima facie case for the progressivity of" the estate tax, "for [it] fall[s] primarily on taxpayers in the top tier of wealth and income distributions."[108] One commentator has noted that "households in the top one percent of the income distribution bear sixty-four percent of the federal estate tax burden, and those in the top five percent bear ninety-one percent of the burden."[109] A study of returns filed in 1970 found that transfer taxes, despite their low revenue yield, contributed "nearly one-third as much to the progressivity of our tax structure as did rates in excess of the average individual income tax rate . . . ."[110] However, data from recent years paints a different picture.[111] "The average income tax rate[s] ha[ve] not changed greatly," while "the revenue raised by the estate tax amounted to only about twelve percent of that raised by [the] income tax," causing "a far smaller contribution to progressivity than before."[112]

In short, the estate tax once provided a significant amount of progressivity to the overall tax system.[113] However, its contribution to progressivity has been shrinking consistently over the years.[114] With studies confirming that there is a growing inequality in distributions of wealth and that the estate tax is contributing much less to the progressivity of the tax system than it once did, one can only wonder why the federal government continues to pass tax legislation that weakens the progressivity of the tax system.[115] Does the 2001 Tax Act aid or hinder the estate tax in reaching its stated objectives? A summary of the 2001 Tax Act and its effect on relevant parties follows.

IV. A SUMMARY OF THE ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001

A. *Introduction*

Repeal of the "death tax"! This was one of the advertised objectives of the 2001 Tax Act.[116] The Bush Administration further proclaimed that the 2001 Tax

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108. *Id.* (citing William G. Gale & Joel B. Slemrod, *A Matter of Life and Death: Reassessing the Estate and Gift Tax*, 20 VA. TAX REV. 500, 504 (2001)).

109. *Id.* (citing JULIE-ANNE CRONIN, U.S. TREASURY DISTRIBUTIONAL ANALYSIS METHODOLOGY 24 tbl.12 (U.S. Dep't of the Treasury, OTA Paper No. 85, 1999)).

110. *Id.*

111. *Id.*

112. Graetz, *supra* note 27, at 272 (citing Harry C. Gutman, *Federal Wealth Transfer Taxes After the Economic Recovery Act of 1981*, 35 NAT'L TAX J. 253, 261-62 (1982)).

113. *See supra* note 110 and accompanying text.

114. *See supra* note 112 and accompanying text.

115. Burke & McCouch, *supra* note 20, at 506 (citing JOEL B. SLEMROD & JON BAKIJA, DOES GROWING INEQUALITY REDUCE TAX PROGRESSIVITY? SHOULD IT? 1 (Nat'l Bureau of Econ. Research, Working Paper No. 7576, 2000)).

116. James F. Gulecas & Alan S. Gassman, *The Economic Growth and Tax Relief Reconciliation Act of 2001: Practical Estate Planning*, PRAC. TAX LAW., Summer 2001, at 37.

Act would save family farms and other family-owned businesses, while at the same time stimulate a slowing economy.[117] For most estate planning clients, the 2001 Tax Act is better characterized as a "poorly crafted, politically motivated two-edged sword."[118] It will undoubtedly wreak havoc on most existing estate plans.[119] Additionally, the estate tax is repealed for only one year, specifically, for those decedents dying after December 31, 2009, but before January 1, 2011.[120] The 2001 Tax Act also contains a "sunset provision," which ensures that all changes made by the Act will not apply to decedents dying after 2010.[121] Critics have suggested that this may be one of the most deceptive tax acts ever enacted, "particularly in view of applicable legislation that would also require the budget to remain balanced during the years in question."[122] One commentator proclaimed: "All the oil in Alaska and Antarctica is not going to pay for the tax savings that would truly apply if all application of this rule were phased in!"[123]

The inability of the estate tax to meet its objectives led to its demise.[124] Those who opposed repeal called the federal estate tax an efficient and "sensible balance of competing goals."[125] In addition, opponents of repeal called the estate tax a "voluntary tax," that is, only "those who amass capital with complete indifference about whether to pass it on intergenerationally" pay the tax.[126] Edward McCaffery, like the Bush Administration, did not accept this latter reasoning for several reasons.[127] First, the estate tax is hardly voluntary due to its binding effect on the very rich, a small but important class with regard to aggregate capital stock.[128] Second, there are significant costs incurred to avoid the tax.[129] A final consideration weighing in favor of repeal is that a voluntary tax is a "limited tool for furthering equal opportunity and redistribution, both in theory and in practice."[130] "The estate tax's very low revenue yield and the continuing inequality of the distribution of wealth suggest that the estate tax is

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117. Forsberg, *supra* note 18, at 23.
118. *Id.*
119. *Id.*
120. 2001 Tax Act, § 501(d), 115 Stat. 69 (2001) (to be codified at I.R.C. § 2210(a)).
121. 2001 Tax Act, § 901(a)(1), (b), 115 Stat. 150.
122. Gulecas & Gassman, *supra* note 116, at 36.
123. *Id.*
124. *See* discussion *supra* Part III.A-C (noting that the estate tax has failed to meet at least two of its stated objectives, while losing ground on its third objective).
125. McCaffery, *supra* note 24, at 358.
126. *Id.*
127. *Id.*
128. *See id.* at 358-59 (arguing that private individuals make better capital decisions than those in public office, and that by taxing the very wealthy, the estate tax discourages personal savings and favors consumption).
129. *Id.* at 359.
130. *Id.* at 360.

doing little, if anything, to level playing fields."[131] McCaffery further argues that, if only wealthy individuals—at least those unconcerned with passing on large amounts of wealth to their heirs—pay the tax, how does this make the world better?[132]

Proponents of the estate tax argue that the tax is at least symbolic, ensuring that all believe they have the opportunity to realize the American Dream—not just those who have amassed great wealth.[133] Proponents argue: "So long as we continue to tolerate inheritance by healthy, adult children, what we as a nation actually proclaim is, 'All men are created equal, except the children of the wealthy.'"[134]

There are credible arguments in support of and against the estate tax. In fact, this seems to be a basic political preference question.[135] The Bush Administration opted for repeal, and thus the question becomes how repeal is accomplished.

B. *How "Repeal" Is Accomplished*

In 2001, the applicable exclusion amount was $675,000[136] and the highest marginal tax rate was fifty-five percent.[137] "Repeal" is accomplished through phased-in reductions of the maximum marginal tax rate and increases in the applicable exclusion amount.[138] Under the 2001 Tax Act, the applicable exclusion amount will increase in stages until 2009, while the top marginal tax rate will decrease in stages until 2007, at which time it will remain at forty-five percent.[139] For example, in 2002 the applicable exclusion amount will increase to

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131. *Id.* (citing Donaldson, *supra* note 33, at 541).

132. *Id.*

133. *See id.* ("Perhaps the estate tax is mostly symbolic, a nod in the direction of liberal egalitarian ideals.").

134. Ascher, *supra* note 37, at 71 (footnote omitted).

135. As is well known, Republicans usually favor lower taxes, while Democrats have traditionally favored more government, which generally means higher taxes.

136. I.R.C. § 2010(c) (2000), *repealed by* 2001 Tax Act, § 521(a), 115 Stat. 71 (2001).

137. I.R.C. § 2001(c), *repealed by* 2001 Tax Act, § 511(c)(2)(B), 115 Stat. 70.

138. *See* 2001 Tax Act, §§ 511(c)(2)(B), 521(a), 115 Stat. 70, 71 (to be codified at I.R.C. §§ 2001(c)(1)-(2), 2010(c)).

139. *Id.* The following table represents the exemption equivalent amounts and the top marginal tax rates that will be in effect through "repeal":

Year	Applicable Exclusion Amount	Top Marginal Rate*
2002	$1,000,000	50%
2003	$1,000,000	49%
2004	$1,500,000	48%
2005	$1,500,000	47%
2006	$2,000,000	46%

$1 million,[140] while the top marginal tax rate will decrease to fifty percent.[141] In 2009, the applicable exclusion amount increases to $3.5 million,[142] while the top tax rate remains at its 2007 level, forty-five percent.[143] Finally, for the year 2010, the estate tax is repealed.[144]

C. *Sunset Provision*

"One of the most important aspects of the [2001 Tax A]ct that is not widely known, publicized or reported is that the [2001 Tax A]ct 'sunsets' in 2011."[145] Section 901 is a "sunset provision," which repeals all the provisions of the 2001 Tax Act after December 31, 2010.[146] In short, this means that if Congress fails to take action, everything will return to the levels of 2002, or a $1 million applicable exclusion amount and a fifty percent top marginal tax rate.[147] "This provision was added to avoid application of the arcane 'Byrd rule' in the Senate, but is as much a part of the law as any other provision."[148] The inclusion of this provision nearly guarantees that at some point in the future Congress will have to revisit the 2001 Tax Act.[149] However, it is likely some provisions of the 2001 Tax Act will be revisited by Congress and changed before they ever go into effect.[150]

2007	$2,000,000	45%
2008	$2,000,000	45%
2009	$3,500,000	45%

* Applicable to taxable estates in excess of $2,500,000.

Id.

140. 2001 Tax Act, § 521(a), 115 Stat. 72 (to be codified at I.R.C. § 2010(c)).

141. 2001 Tax Act, § 511(c)(2)(B), 115 Stat. 70 (to be codified at I.R.C. § 2001(c)(2)).

142. 2001 Tax Act, § 521(a), 115 Stat. 71 (to be codified at I.R.C. § 2010(c)).

143. 2001 Tax Act, § 511(c)(2)(B), 115 Stat. 70 (to be codified at I.R.C. § 2001(c)(2)).

144. 2001 Tax Act, § 501(d), 115 Stat. 69 (to be codified at I.R.C. § 2664).

145. Forsberg, *supra* note 18, at 23.

146. Gulecas & Gassman, *supra* note 116, at 37. Zaritsky asserts that if the 2001 Tax Act is allowed to sunset, "[c]arryover basis would disappear and the present basis rules would be returned . . . [while] . . . the state death tax credit . . . would be resurrected . . . ." ZARITSKY, *supra* note 5, ¶ 1.10.

147. 2001 Tax Act, § 901(b), 115 Stat. 150.

148. Gulecas & Gassman, *supra* note 116, at 36; *see also* ZARITSKY, *supra* note 5, ¶ 1.10 (stating that "[t]his change was required to comply with the Congressional Budget Acts of 1974 and 1990, which require a vote of 60 senators to pass a bill that would decrease revenues for a fiscal year more than 10 years after the present fiscal year").

149. ZARITSKY, *supra* note 5, ¶ 1.10. Zaritsky further notes: "A subsequent session of Congress, however, might find that economic or political conditions have changed sufficiently to decline an extension of these provisions." *Id.*

150. *Highlights of the Estate, Gift, and Generation Skipping Tax Provisions in the Economic Growth and Tax Relief Reconciliation Act of 2001*, EST. PLANNER'S ALERT 1 (2001) [hereinafter *Highlights of the 2001 Tax Act*].

D. *Carryover Basis Implementation*

After "repeal," the current law's step-up in basis rule[151] will be replaced with a modified carryover basis rule.[152] The effect of the new basis rule is that the basis in property for income tax purposes will be the lower of: (1) the decedent's adjusted basis in the property, or (2) "the fair market value of the property on the date of the decedent's death."[153] Stated simply, "the decedent's basis will carry over to the heir, except for property whose value at death was lower than the decedent's basis, in which case the heir will receive a basis equal to the fair market value of the property at death."[154] This new basis rule mandates that a beneficiary's basis in bequeathed property will be zero unless the beneficiary has receipts to prove the decedent's basis in the property.[155] However, three exceptions will allow executors to increase the basis of a significant amount of assets.[156] First, "each estate will receive $1.3 million of basis to be added to the carryover basis of any one or more of the assets held at death."[157] For example, if a decedent dies owning stock worth $10 million that she purchased for $8.7 million, this exception allows the basis to be increased to $10 million.[158] Secondly, an estate may receive additional basis equal to the aggregate of: "(a) the decedent's unused capital loss carryforwards; (b) the decedent's unused net operating loss carryforwards; and (c) the amount of losses that would have been allowable under Code Sec. 165 if the property acquired from the decedent had been sold at fair market value immediately before death."[159] The third exception allows assets passing to the surviving spouse an

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151. *See* I.R.C. § 1014(a)(1) (2000).

152. 2001 Tax Act, §§ 541, 542, 115 Stat. 76 (to be codified at I.R.C. §§ 1014(f), 1022(a)).

153. 2001 Tax Act, § 542, 115 Stat. 76 (to be codified at I.R.C. § 1022(a)(2)(A)-(B)).

154. *Highlights of the 2001 Tax Act*, *supra* note 145, at 4.

155. The 2001 Tax Act states that the basis will be the lower of the decedent's adjusted basis "or the fair market value of the property at the date of the decedent's death." 2001 Tax Act, § 542, 115 Stat. 76 (to be codified at I.R.C. § 1022(a)(2)(A)-(B)). Therefore, if you cannot prove the basis of your assets with receipts, the basis in the property will be assumed to be zero, and this is surely lower than the assets' fair market value.

156. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4.

157. *Id.*; *see also* 2001 Tax Act, § 542(a), 115 Stat. 76 (to be codified at I.R.C. § 1022(b)(2)(B)).

158. *See Highlights of the 2001 Tax Act*, *supra* note 150, at 4 (providing a similar example). The significance of this increase is that when the beneficiary goes to sell the property, he or she will realize no gain on the sale. *See* I.R.C. § 1001(b)-(c) (2000) (providing the calculation for the amount realized and recognized on the sale of property).

159. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4; *see also* 2001 Tax Act, § 542(a), 115 Stat. 76 (to be codified at I.R.C. § 1022(b)(2)(C)).

additional $3 million of basis.[160] However, "[n]o addition to basis may increase the new basis of any asset above its fair market value on the date of [the decedent's] death."[161] Significantly, the executor will be able to choose to which assets the basis increase should be allocated.[162] However, basis can be added to property only if the property was owned, or treated as owned, by the decedent at death.[163] The 2001 Tax Act provides that basis may not be allocated to "(1) property acquired by the decedent by gift (other than from a spouse) during the 3-year period ending on the date of the decedent's death; (2) property that constitutes a right to receive income in respect of a decedent under Code Sec. 691 . . .; or (3) stock of certain foreign entities."[164] Finally, the allowable amounts of additional basis are indexed for inflation after 2010.[165]

Implementation of a carryover basis scheme was attempted in 1976,[166] but was such an "administrative nightmare"[167] that it was repealed in 1980.[168] Opponents of carryover basis contend the unfairness of the scheme lies in the fact that those receiving property from a decedent have to rely on the records of the decedent to prove the basis in property.[169] If beneficiaries are unable to prove basis in the property, or if there is a disagreement regarding the actual basis in such property, the IRS will win on the burden of proof issue.[170] Due to the allocation of basis rules under the 2001 Tax Act, the new law's carryover basis rules are even more complex than those in effect in 1976.[171] One commentator contends: "Given the dubious history of carryover basis at death, it may very

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160. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4; *see also* 2001 Tax Act, § 542(a), 115 Stat. 77 (to be codified at I.R.C. § 1022(c)(2)(B)).

161. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4; *see also* 2001 Tax Act, § 542(a), 115 Stat. 80 (to be codified at I.R.C. § 1022(d)(2)).

162. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4; *see also* 2001 Tax Act, § 542(a), 115 Stat. 80 (to be codified at I.R.C. § 1022(d)(2)).

163. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4; *see also* 2001 Tax Act, § 542(a), 115 Stat. 80 (to be codified at I.R.C. § 1022(d)(2)).

164. *Highlights of the 2001 Tax Act*, *supra* note 150, at 5.

165. *Id.* at 4; *see also* 2001 Tax Act, § 542(a), 115 Stat. 80 (to be codified at I.R.C. § 1022(d)(4)).

166. *See* Tax Reform Act of 1976, Pub. L. No. 94-455, §§ 1901(a)(126)(A), 2005(a), 90 Stat. 1784, 1872 (1976) (codified as amended in scattered sections of 26 U.S.C.) (repealing the step-up in basis rules and implementing carryover basis rules).

167. Gulecas & Gassman, *supra* note 116, at 42; *see also* Graetz, *supra* note 27, at 261 ("The complexities and technical difficulties that haunted the carryover-basis provision from the outset prompted a delay in its effective date in 1978 and ultimately were a major cause of its demise in the Crude Oil Windfall Profit Tax Act of 1980.") (footnotes omitted).

168. Crude Oil Windfall Profit Tax Act of 1980, Pub. L. No. 96-223, § 401(a), 94 Stat. 299 (1980).

169. Gulecas & Gassman, *supra* note 116, at 42-43.

170. *Id.* at 43.

171. *Id.*

well be that this carryover basis law will be repealed before its effective date, particularly if outright repeal of the estate tax is rescinded at some point."[172]

E. *Phase-Out of the State Death Tax Credit*

The 2001 Tax Act also phases out the state death tax credit.[173] Under § 2011, a credit is allowed for any state estate, inheritance, legacy, or succession taxes paid by the decedent.[174] This section ensures that a taxpayer is not responsible for any "extra" estate taxes to the federal government because of the state tax.[175] Typically, "[t]he state tax acts as a 'pick-up' or 'sponge' tax, merely imposing tax up to the amount of the allowable federal credit, thereby shifting revenue from the federal government to the states."[176] Under the 2001 Tax Act, the state death tax credit is reduced to seventy-five percent of its current amount in 2002, fifty percent in 2003, and twenty-five percent in 2004.[177] "[I]n 2005, the [state death tax] credit is replaced by a federal estate tax *deduction* for state death taxes" paid.[178]

F. *Reporting Requirements*

The 2001 Tax Act also mandates specific reporting requirements after repeal.[179] The executor is required to file a return if the fair market value of all property (other than cash) exceeds the dollar amount provided for in I.R.C. § 1022(b)(2)(B)—$1.3 million.[180] Furthermore, the executor will need to provide the following information on the federal estate tax return:

> (1) [T]he name and TIN of the recipient of such property; (2) an accurate description of such property; (3) the adjusted basis of such property in the hands of the decedent and its fair market value at the time of death; (4) the decedent's holding period for such property; (5) sufficient information to determine whether any gain on the sale of the property would be treated as ordinary income; (6) the amount of basis increase allocated to the property .

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172. *Id.*
173. 2001 Tax Act, § 531, 115 Stat. 72 (2001) (to be codified at I.R.C. § 2011(b)(2)).
174. I.R.C. § 2011 (2000); *see also* Schlachter, *supra* note 23, at 799.
175. Schlachter, *supra* note 23, at 799.
176. *Id.*
177. 2001 Tax Act, § 531, 115 Stat. 72 (to be codified at I.R.C. § 2011(b)(2)).
178. Gulecas & Gassman, *supra* note 116, at 39 (emphasis added); *see also* 2001 Tax Act, § 532(d), 115 Stat. 73 (to be codified at I.R.C. § 2058).
179. 2001 Tax Act, § 542, 115 Stat. 81, 82 (to be codified at I.R.C. § 6018).
180. 2001 Tax Act, § 542, 115 Stat. 81 (to be codified at I.R.C. § 6018(b)(1)).

. .; (7) such other information as the Secretary may by regulations prescribe.[181]

The estate tax return is to be filed with the decedent's final income tax return, or at a later date that may be specified by regulation.[182] Furthermore, the executor will be required to provide the recipient of bequeathed property a written statement providing everything above that was disclosed to the IRS.[183] There are stiff penalties for failure to provide this information. The penalty for failure to furnish information is $10,000 for each failure, except that the penalty is $500 for each failure to furnish information regarding gifts within three years of death, and failure to furnish information to beneficiaries is $50 for each failure.[184] However, if the executor can show the failure to provide such information was "reasonable," no penalty will be imposed.[185]

V. EFFECTS OF THE 2001 TAX ACT AND THE PROSPECT OF TOTAL REPEAL

After opting for repeal of the estate tax, Congress essentially had two options at its disposal: (1) outright repeal, or (2) phase-out.[186] Some experts have suggested that outright repeal could in fact enhance federal revenues.[187] These experts predict that outright repeal would cause an $11 billion increase in economic output per year.[188] Additionally, personal incomes would increase up

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181. 2001 Tax Act, § 542, 115 Stat. 82 (to be codified at I.R.C. § 6018(c)(1)-(7)).

182. 2001 Tax Act, § 542, 115 Stat. 83 (to be codified at I.R.C. § 6075(a)).

183. 2001 Tax Act, § 542, 115 Stat. 82 (to be codified at I.R.C. § 6018(e)).

184. 2001 Tax Act, § 542, 115 Stat. 83 (to be codified at I.R.C. § 6716(a)-(b)).

185. 2001 Tax Act, § 542, 115 Stat. 83 (to be codified at I.R.C. § 6716(c)).

186. Weber, *supra* note 8, at 134.

187. *Id.* (citing Prepared Testimony of William W. Beach, John M. Olin Senior Fellow in Economics and Director of the Center for Data Analysis, the Heritage Foundation, 105th Cong. 1 (1998)). Christopher Erblich examined the effect of repealing transfer taxes on economic growth and provided the following table in his article:

ECONOMIC GROWTH WITHOUT TRANSFER TAX, 1993-2000

Year	Change in GDP ($ billions)	Change in Jobs (thousands)	Change in Capital ($ billions)
1993	6.6	12	64.5
1994	19.3	44	180.8
1995	33.2	84	301.4
1996	45.6	128	401.6
1997	57.5	171	492.6
1998	65.7	203	547.7
1999	73.0	225	595.8
2000	79.2	228	638.9

Erblich, *supra* note 72, at 1948 (footnotes omitted) (copyright 1994, Seton Hall Law Review, reprinted with permission of the publisher).

188. Weber, *supra* note 8, at 134 (footnotes omitted).

to as much as $8 billion per year and 145,000 new jobs would be created.[189] Weber further notes that the federal debt may be reduced due to an increase in the federal income tax base.[190] Regardless of the method chosen to accomplish repeal, it was estimated that "the federal government would initially loose $11 to $15 million during the transition phase."[191]

As previously noted, repeal of the estate tax is accomplished through a phase-out program and not outright repeal.[192] Does the phase-out of the estate tax do what the Bush Administration and supporters of repeal proclaim? An examination regarding the effect the phase-out of the death tax will have on a hypothetical decedent, states, charities, and the estate planning industry follows.

A. *On a Hypothetical Decedent*

In order to appreciate the effects of the 2001 Tax Act, one must examine the consequences to a hypothetical decedent under the Act. Jane Smith, an eighty-two year-old widow, has a taxable estate of $2 million. If Mrs. Smith had died in 2001, the year before implementation of the 2001 Tax Act, Mrs. Smith would have paid $560,250 in estate taxes.[193] If Mrs. Smith dies in 2002, under the 2001 Tax Act she will pay $435,000 in estate taxes, in comparison to $551,000 before enactment.[194] If Mrs. Smith dies in 2005, under the 2001 Tax Act she will pay only $225,000 in estate taxes, in comparison to $454,500 before its enactment.[195] If Mrs. Smith dies in 2010, the year of repeal, she will pay no estate taxes, in comparison to the $435,000 she would pay if the 2001 Tax Act

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189. *Id.*
190. *Id.*
191. *Id.*
192. *See supra* text accompanying notes 139-44.
193. Calculations were performed as follows: 2001 Calculations—pre-2001 Tax Act—the gross estate value was plugged into the rate table of I.R.C. § 2001(c) (2000) to determine gross taxes due. The "applicable exclusion amount" of I.R.C. § 2010(c) was then plugged into the rate tables of I.R.C. § 2001(c) to determine the "unified credit." Finally, the unified credit was subtracted from the gross taxes due, to arrive at an estimated tax liability. 2002-2010 Calculations—same as above, but with the appropriate figures under the 2001 Tax Act, §§ 521(a), 511(c)(2)(B), 115 Stat. 71, 70 (to be codified at I.R.C. §§ 2010(c), 2001(c)(2)). 2011 Calculations—I used the 2002 figures under the 2001 Tax Act, §§ 521(a), 511(c)(2)(B), 115 Stat. 71, 70 (to be codified at I.R.C. § 2010(c), 2001(c)(2)), as provided for in the "sunset provision" of the 2001 Tax Act, § 901. These calculations do not reflect available deductions from the gross estate or factor in adjusted taxable gifts.
194. *See supra* note 193 and accompanying text. This represents a tax savings of $116,000 ($551,000 - $435,000).
195. *See supra* note 193 and accompanying text. This represents a tax savings of $229,500 ($454,500 - $225,000).

were not passed.[196] However, if she lives until 2011, the year the 2001 Tax Act "sunsets," everything will revert back to the 2002 levels, or a $1 million applicable exclusion amount and a fifty percent top marginal tax rate, and Mrs. Smith will pay $435,000 in estate taxes.[197] In sum, wealthy clients are likely to reap large tax savings under the 2001 Tax Act.

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196. *See supra* note 193 and accompanying text. This represents a tax savings of $435,000 ($435,000 - $0).

197. *See supra* notes 193-94 and accompany text. The following tables provide the amount of estate taxes payable for the relevant years on taxable estates of $2 million, $3 million, $5 million, and $10 million under the 2001 Tax Act, the taxes payable before enactment, and the tax savings due to the 2001 Tax Act.

*Taxable Estate of $2 Million:

Year	Taxes Payable Under 2001 Tax Act	Taxes Payable Before Enactment	Tax Savings
2001	$ 560,250	$ 560,250	$ 0
2002	$ 435,000	$ 551,000	$ 116,000
2003	$ 435,000	$ 551,000	$ 116,000
2004	$ 225,000	$ 493,500	$ 268,500
2005	$ 225,000	$ 454,500	$ 229,500
2006	$ 0	$ 435,000	$ 435,000
2007	$ 0	$ 435,000	$ 435,000
2008	$ 0	$ 435,000	$ 435,000
2009	$ 0	$ 435,000	$ 435,000
2010	$ 0	$ 435,000	$ 435,000
2011 & later	$ 435,000	$ 551,000	$ 116,000

*Taxable Estate of $3 Million:

Year	Taxes Payable Under 2001 Tax Act	Taxes Payable Before Enactment	Tax Savings
2001	$1,070,250	$1,070,250	$ 0
2002	$ 930,000	$1,061,000	$ 131,000
2003	$ 930,000	$1,061,000	$ 131,000
2004	$ 705,000	$1,003,500	$ 298,500
2005	$ 695,000	$ 964,500	$ 269,500
2006	$ 460,000	$ 945,000	$ 485,000
2007	$ 450,000	$ 945,000	$ 495,000
2008	$ 450,000	$ 945,000	$ 495,000
2009	$ 0	$ 945,000	$ 945,000
2010	$ 0	$ 945,000	$ 945,000
2011 & later	$ 930,000	$1,061,000	$ 131,000

*Taxable Estate of $5 Million:

Year	Taxes Payable Under 2001 Tax Act	Taxes Payable Before Enactment	Tax Savings
2001	$2,170,250	$2,170,250	$ 0
2002	$1,930,000	$2,161,000	$ 231,000
2003	$1,905,000	$2,161,000	$ 256,000
2004	$1,665,000	$2,103,500	$ 438,500

B. *On States*

"Although the phase-out of the state death tax credit will not affect the total amount of estate taxes paid by taxpayers themselves, the effect upon state revenues will be significant."[198] The phase-out of the state death tax credit simply means a greater portion of the federal estate tax will go to the federal government and less to the states.[199] In order to properly analyze the effect that the 2001 Tax Act will have on the states, a distinction must be drawn between those states that "peg" their state's inheritance tax to the state death tax credit, and those that do not. If a state's inheritance tax is not "pegged" to the state death tax credit, "then part of the benefit of lower federal estate taxes will be lost if the state retains its current rates and a lower (or no) state death tax credit is available."[200]

Due to this lost revenue sharing between the states and the federal government, the sole responsibility of taxing estates will fall on the states.[201] States will be forced to increase other taxes and possibly enact or reenact their own transfer tax systems.[202] The enactment of a new transfer tax scheme could pose administrative problems for states, which would need to draft new

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2005	$1,635,000	$2,064,500	$ 429,500
2006	$1,380,000	$2,045,000	$ 665,000
2007	$1,350,000	$2,045,000	$ 695,000
2008	$1,350,000	$2,045,000	$ 695,000
2009	$ 675,000	$2,045,000	$1,370,000
2010	$ 0	$2,045,000	$2,045,000
2011 & later	$1,930,000	$2,161,000	$ 231,000

*Taxable Estate of $10 Million:

Year	Taxes Payable Under 2001 Tax Act	Taxes Payable Before Enactment	Tax Savings
2001	$4,920,250	$4,920,250	$ 0
2002	$4,430,000	$4,911,000	$ 481,000
2003	$4,355,000	$4,911,000	$ 556,000
2004	$4,065,000	$4,853,500	$ 788,500
2005	$3,985,000	$4,814,500	$ 829,500
2006	$3,680,000	$4,795,000	$1,115,000
2007	$3,600,000	$4,795,000	$1,195,000
2008	$3,600,000	$4,795,000	$1,195,000
2009	$2,925,000	$4,795,000	$1,870,000
2010	$ 0	$4,795,000	$4,795,000
2011 & later	$4,430,000	$4,911,000	$ 481,000

198. Gulecas & Gassman, *supra* note 116, at 39.
199. *Highlights of the 2001 Tax Act*, *supra* note 150, at 3.
200. *Id.*
201. Schlachter, *supra* note 23, at 799-800 (footnotes omitted).
202. Gulecas & Gassman, *supra* note 116, at 39.

legislation and establish collection mechanisms.[203] Furthermore, permanent repeal may "invite competition among the states."[204] As one commentator put it, there could be a race to the bottom, "[s]ince all but fourteen states have repealed or substantially modified their inheritance taxes."[205]

If total repeal becomes a reality, states with a "sponge" estate tax[206] "will suffer a drastic and immediate reduction in their revenues from these taxes."[207] In 2000, the White House Office of Management and Budget estimated that the federal government would transfer $28.4 billion in estate taxes to the states over the next five years due to the state death tax credit.[208] This represents a significant amount of potentially lost revenue, and could prove harmful to the states.[209]

The state of Iowa "pegs" a portion of its death taxes to the federal estate tax,[210] but unlike some states, Iowa has a state inheritance tax that applies to non-lineal descendents and unrelated beneficiaries.[211] In short, Iowa will lose less

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203. Schlachter, *supra* note 23, at 800; *see also* ZARITSKY, *supra* note 5, ¶ 1.04 (observing that states employing only "soak-up" taxes "will need to find other sources of state revenues to replace the state death tax or adopt their own forms of state inheritance or estate taxes").

204. Schlachter, *supra* note 23, at 800.

205. *Id.* (footnotes omitted); *see also* ZARITSKY, *supra* note 5, ¶ 1.04 (asserting that repeal of the state death tax credit "will create a disparity between and among state death taxes, and may actually become a significant factor in the decision of some clients as to their residence").

206. A "sponge" estate tax refers to the imposition of inheritance taxes up to the amount of the state death tax credit.

207. Gulecas & Gassman, *supra* note 111, at 39; *see also* ZARITSKY, *supra* note 5, ¶ 1.04 (stating that repeal of the state death tax credit "is likely to have a serious adverse effect on the revenues of many states because most states impose a state death tax equal only to the federal credit"). Zaritsky further notes that some states claim they have a "soak-up" death tax credit, when actually they do not. *See* ZARITSKY, *supra* note 5, ¶ 1.04 (noting that many states that are viewed as having a "soak-up" estate tax "do not automatically adopt changes in the federal estate tax"). Zaritsky uses Virginia as an example of such a state. *Id.* ¶ 1.04 n.56 (quoting VA. CODE ANN. § 58.1-901 (Michie 2002) ("'In no event, however, shall such amount be less than the federal credit allowable by § 2011 of the Internal Revenue Code as it existed on January 1, 1978.'")).

208. Schlachter, *supra* note 23, at 800 (citing White House, Office of Management and Budget, Budget of the U.S. Government, Fiscal Year 2000, at 272 (Doc. 1999-4577), *available at* http://www.access.gpo.gov/usbudget).

209. *See id.* (arguing repeal will require states to draft new legislation in order to establish collection mechanisms, thereby causing increased competition among the states to enact the lowest estate tax burden); *see also* ZARTISKY, *supra* note 5, ¶ 1.04 (noting that the resulting disparity among state death taxes may be "a significant factor in the decision of some clients as to their residence").

210. IOWA CODE ch. 451 (2001).

211. *Id.* ch. 450; *see also* Mike Lipsman, Manager of the Tax Research and Program Analysis, Iowa Department of Revenue and Finance, State Death Tax Credit Phase-Out Estimate (2001) (on file with author).

money than those states with a "sponge" estate tax.[212] According to Mike Lipsman, manager of the Tax Research and Program Analysis section of the Iowa Department of Revenue and Finance, the State of Iowa was projected to receive approximately $110 million in "death" taxes in 2001, of which roughly fifty percent is attributable to the state death tax credit.[213] Additionally, Lipsman projects Iowa will lose $383.448 million over the period in which the state death tax credit is phased out.[214] This figure represents a significant amount of lost revenue for a state that has been struggling with budget issues.[215] Clearly, Iowa will miss the money it was to receive from the state death tax credit and, in fact, may need to increase other state taxes to compensate for the projected loss in revenue.[216] What could Iowa do with this lost revenue?[217] Such possibilities include: raising teacher salaries, investing in technological classrooms, putting more police officers on city streets and highways, halting what seems to be the consistent ease with which our state employees are being laid off. A January 12,

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212. This will occur because the State of Iowa does not rely solely on revenue from the state death tax credit—the state has an additional inheritance tax. *See* IOWA CODE ch. § 450.

213. Telephone Interview with Mike Lipsman, Manager of the Tax Research and Program Analysis Section of the Iowa Department of Revenue and Finance (Jan. 15, 2002).

214. Mike Lipsman provided the following table representing Iowa's projected loss in revenue due to the phase-out of the state death tax credit:

Estimated Impact of State Death Tax Credit Phase-Out:

Year	Impact ($ millions)
2001	0
2002	–9.922
2003	–20.462
2004	–31.647
2005	–43.508
2006	–44.861
2007	–46.256
2008	–47.694
2009	–49.178
2010	–50.707
2011	–39.213
Total	–383.448

Lipsman, *supra* note 211 (reprinted with permission of author).

215. *See* Lynn Okamato, *Iowa State Revenue Down Millions*, DES MOINES REGISTER, May 8, 2002, at 1A (noting that Iowa had a $219 million shortfall in state revenue for 2002). Okamato went on to provide: "Iowa state government must make more budget cuts, drain much of its emergency money, and perhaps eliminate entire programs." *Id.*

216. *See* Gulecas & Gassman, *supra* note 116, at 39 (noting that Florida will likely have to increase state taxes to make up for the loss in revenue from the phase-out of the state death tax credit).

217. *See* William G. Gale & Peter Orszag, *Keeping the Existing Tax Cuts, but Freeze New Ones*, DES MOINES REGISTER, Feb. 2, 2002, at 11A (noting that the freezing of future tax cuts could have several benefits, including funding health and child care programs, as well as cutting future budget deficits).

2003, *Des Moines Register* article provided other examples of services not being performed due to budget troubles, including: (1) continued waiting lists at the state's mental-health hospitals; (2) refund delays for tax returns of up to twelve weeks; (3) regulations for adult day care have not been updated since 1995 due to lack of money; (4) "Iowa's long-term care ombudsman doesn't have the money to respond to all questions and complaints from assisted-living residents as required by federal law"; (5) more than one hundred positions are vacant at the Department of Human Services due to lack of resources; and (6) more than one hundred troubled and abused children are on waiting lists for group homes.[218]

Phase-out of the state death tax credit will also prove harmful to the State of Florida. Gulecas and Gassman analyzed the effect total repeal would have on Florida.[219] Florida's revenue from the federal estate tax was estimated to be $800 million in 2001.[220] That number was expected to rise to over $1 billion as an aging and well-off population dies.[221] Due to the 2001 Tax Act, "Florida will lose over $7 billion in revenue . . . over the next ten years and, unlike other states, is precluded under their state constitution from enacting any state estate or inheritance tax that is not creditable against a federal estate tax."[222] Suffice to say, the State of Florida will likely see an increase in other state taxes, including property and sales taxes, to make up for this dramatic loss in revenue.[223] In sum, the 2001 Tax Act gives a tax break to the wealthiest two to three percent of Americans—the only segment of the population who actually pay the tax—and will force the general public to pick up the tab for the loss in revenue in the form of higher state taxes.[224]

C. *On Charities*

The 2001 Tax Act may have a dampening effect on charitable giving. Under I.R.C. § 2055 and its gift tax counterpart, I.R.C. § 2522, "bequests to certain charitable organizations are fully deductible from a decedent's gross

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218. Jonathan Roos, *Leaders to Reach for New Tools in Effort to Fix Iowa Economy*, DES MOINES REGISTER, Jan. 12, 2003, at 15A.

219. Gulecas & Gassman, *supra* note 116, at 39.

220. *Id.*

221. *Id.*

222. *Id.* The Florida Constitution provides:

> No tax upon estates or inheritances or upon the income of natural persons who are residents or citizens of the state shall be levied by the state, or under its authority, in excess of the aggregate of amounts which may be allowed to be credited upon or deducted from any similar tax levied by the United States or any state.

FLA. CONST. art. VII, § 5(a).

223. Gulecas & Gassman, *supra* note 116, at 39.

224. *Id.*; *see also* Schlachter, *supra* note 23, at 788 (noting that the estate tax only affects the wealthiest two to three percent of Americans).

estate."[225] One commentator asserts: "The combination of lower tax rates with the possibility of the repeal of the estate tax means that there is likely to be somewhat of . . . [a reduction] in charitable gifts."[226] Some experts have estimated that repeal of the estate tax would curve charitable giving by $15 to $20 billion.[227] This fear of decreased charitable giving is "supported by evidence that the amount of gifts donated to nonprofit organizations over the past thirty years is significantly higher in the United States than in countries, such as Canada, which do not allow tax deductions for charitable gifts."[228] However, tax incentives are certainly not the only reasons why Americans give more than their Canadian counterparts.[229] After all, most decisions to give are not motivated by tax incentives, but rather, one's desire to give.[230] Schlachter further notes:

> Under the current system, it is often more advantageous to donate to charities at death than during life since the donation is deductible from both the decedent's final income tax return and from the decedent's gross estate. However, gifts to charities would still be deductible from income under section 170 if the estate tax were repealed. Thus, in some cases, a repeal of the estate tax would merely shift charitable giving from bequests at death to contributions during life.[231]

Jerry McCoy believes the following five often overlooked factors will serve to moderate some experts' gloomy predictions:

> (1) People have left bequests to charity since long before there was an estate tax . . .; (2) Removal of the estate tax would leave decedents' estates with more property to distribute to beneficiaries, including charity; (3) Income tax factors, which are a more potent incentive for charitable transfers, would continue . . .; (4) Research suggests that, while tax savings are important, they are not generally the motivating factor for charitable transfers; and (5) Carryover basis property would create a new incentive for bequests of affected property.[232]

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225. Schlachter, *supra* note 23, at 800 (footnote omitted); *see also* I.R.C. §§ 2055, 2522 (2000) (allowing deductions for certain types of charitable gifts).

226. B. Howard Pearson, *Charitable Planning in 2001*, *in* 32ND ANNUAL ESTATE PLANNING INSTITUTE 451, 454 (PLI Estate Planning & Admin. Course, Handbook Series No. D-309, 2001).

227. Schlachter, *supra* note 23, at 801 (footnote omitted).

228. *Id.*

229. *Id.*

230. Pearson, *supra* note 226, at 454.

231. Schlachter, *supra* note 23, at 801-02 (footnotes omitted).

232. Jerry J. McCoy, *Nontrust Giving Techniques (Or, Charitable Giving Without Trusts)*, SF 91 ALI-ABA 237, 242 (2001).

In short, there appears to be no consensus on how the 2001 Tax Act will affect charitable giving, however, there is likely to be a "steady flow" of charitable giving.[233]

D. *On the Estate Planning Industry*

The 2001 Tax Act "both entices and threatens the client seeking to safeguard an estate."[234] The 2001 Tax Act "gives estate tax planning lawyers and other professionals the opportunity to help position clients for the eventuality of increased exemptions, potential repeal of the tax and potential loss of a stepped-up basis for all assets in the event of death."[235] Due to the implementation of a carryover basis regime, estate planners will need to advise clients to maintain all records of their assets' bases, which are generally the original purchase prices.[236] Moreover, because the executor will be able to use discretion as to which assets the additional basis allotments are allocated, the executor will want to determine which assets are likely to be sold by heirs.[237] By adding bases to those assets likely to be sold, heirs may be able to avoid paying income taxes on the sale.[238] Additionally, because an executor (other than the surviving spouse) may not add basis to property acquired by the decedent by gift during the three-year period before the decedent's death, one should "make the transfers as early as possible to increase the likelihood that the transferee will survive the 3-year period."[239]

Although repeal will not occur until 2010, clients should act now to best position themselves for whatever action Congress may take next.[240] At the very least, estate plans should be modified by clients to plan "for the possibility that they may die before 2010 while there is still an estate tax, in 2010 when there is no estate tax, and after 2010 if the estate tax is reinstated."[241] Undoubtedly, estate planning is easier when there is certainty in the law.[242] However, the 2001 Tax Act is anything but certain; rather, it "is a moving target for clients and the best way to effectively plan is to incorporate as much flexibility into estate plans as possible."[243]

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233. Pearson, *supra* note 226, at 454-55.
234. Forsberg, *supra* note 18, at 23.
235. Gulecas & Gassman, *supra* note 116, at 35.
236. *Id.* at 43.
237. *Highlights of the 2001 Tax Act*, *supra* note 150, at 4.
238. *Id.*
239. *Id.* at 5.
240. Gulecas & Gassman, *supra* note 116, at 41.
241. Forsberg, *supra* note 18, at 24.
242. *Id.*
243. *Id.*; *see also* ZARITSKY, *supra* note 5, at 0-1 ("The Tax Act of 2001 will dramatically alter the practice of estate planning during the next eight years . . . .").

The sunset provision is one particular source of uncertainty in the 2001 Tax Act. This provision provides uncertainty about the future of tax benefits recognized under the 2001 Tax Act, and therefore estate planners must exercise diligence and foresight to ensure they make solid decisions for their clients.[244] Many clients have been misled by the "popular press into thinking that the [2001 Tax] Act permanently repeals the estate tax . . . ."[245] These clients "need to be educated about this fact so that they can make informed decisions regarding their estate planning."[246] Estate planners should warn their clients to be skeptical of those promising permanent repeal.[247] The consensus from practitioners and academics seems to be that total repeal is unlikely.[248] "The fact that there is a nine-year phase-out, a $1 million gift tax exclusion, and a sunset provision is a clear admission that the country cannot afford such a repeal"[249] and at the same time, balance the budget, provide for the aggressive tax cuts President Bush has signed into law, and finance the war on terrorism.[250] Although no one knows for certain what Congress will do when it acts, if total repeal were affordable, Congress would have made it happen.[251] Keep in mind the unpopularity of the carryover basis regime in 1976[252] and that "[r]epeal will not occur, if at all, until 2010. With four Congressional elections and two Presidential elections between now and then, many believe it unlikely that the law will retain its present form for

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244. Gulecas & Gassman, *supra* note 116, at 36.

245. *Id.* at 38; *see also* ZARITSKY, *supra* note 5, ¶ 2.01[1] ("Politicians and the press have announced the repeal of the estate tax, and while most news articles state somewhere in the late paragraphs that actual repeal will occur only in 2010, many clients will read the headlines, listen to the sound bites, and believe that the estate tax has been eliminated."). Zaritsky further notes that the biggest problem facing estate planners as a result of the 2001 Tax Act will be "explaining to clients that the estate tax has not in fact been repealed presently, that it may never be repealed permanently, and that even if it is repealed permanently, good estate planning remains a necessary part of a client's overall financial plan." ZARITSKY, *supra* note 5, ¶ 2.01.

246. Gulecas & Gassman, *supra* note 116, at 38.

247. *Id.* at 43.

248. *See, e.g.*, Burr, *supra* note 15, at 13 (opining "that we shall never see a full and permanent repeal of the estate tax").

249. Gulecas & Gassman, *supra* note 116, at 43.

250. *See* ZARITSKY, *supra* note 5, ¶ 2.01[1][a] (providing that "[t]he first session of the 107th Congress supported repeal, but an economic downturn before 2010 could erase the present budget surpluses, create budget deficits, and make repeal of the estate . . . tax[] economically impossible"). Zaritsky goes on to assert that "a slight leftward shift in the political composition of Congress could make elimination of the estate tax politically impossible because the estate tax currently affects only the largest 2 percent of all estates and will, in 2008, likely affect less than the largest one percent of all estates." *Id.*

251. Gulecas & Gassman, *supra* note 116, at 43.

252. *See* Crude Oil Windfall Profit Tax Act of 1980, Pub. L. No. 96-223, § 401(a), 94 Stat. 269 (1980) (noting the unpopularity of the carryover basis regime and its eventual repeal in 1980).

long."[253] Richard Gans asserted: It is unlikely that estate planners will suffer the same fate Lenny Brown suffered in The Boost,[254] however, "[t]he only thing that is certain is uncertainty."[255] Finally, estate planning is big business, and repeal of the estate tax would adversely affect a thriving industry.

For now, "estate planners who advise or allow their clients to forgo or defer tax-sensitive estate planning based on supposed repeal under the [2001 Tax] Act do their clients a great disservice and risk potential malpractice liability."[256] Experts suggest estate planners should advise their clients to take measures to reduce their taxable estates by sufficiently using their applicable exclusion amount,[257] by taking advantage of the $11,000 annual exclusion on gifts,[258] by sufficiently using the marital deduction,[259] and by using other valuation discount vehicles.[260] The other alternative is to die in 2010, in which case there will be no federal estate tax levied on your taxable estate.[261] For those suffering from a terminal illness, this may be a noble goal.[262] However, if the client ends up living beyond 2010, the tax consequences may be significant.[263] Gulecas and Gassman said it best:

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253. Richard R. Gans, *Waiting for Estate Tax Repeal: What Do You Tell Your Clients in the Meantime?*, FLA. B.J. Nov. 2001, at 67; *see also* ZARITSKY, *supra* note 5, ¶ 2.01[1][a] (proclaiming that "actual repeal of the estate . . . tax[] in 2010 is uncertain because there will be three Congresses (the 108th, 109th, and 110th) and at least one more president elected before 2010, and any of them can muster the forces required to delay or eliminate the repeal of the estate . . . tax[]"). "Some worry Congress could take action well before then, and not to taxpayers' advantage." Nkiru Askika Oluwasanmi, *The Best Laid Plans*, SMART MONEY, Mar. 2002, at 128. "'This law was passed before Sept. 11, before the economy took a nosedive, and that which Congress giveth, Congress taketh away.'" *Id.* (quoting Mel Warshaw, head of the estate planning department for the Boston-based firm McDermott, Will & Emery).

254. *See id.* ("In the 1988 film 'The Boost,' Lenny Brown makes a handsome living selling interests in tax-shelter limited partnerships to affluent investors. He has the world by the tail until the day Congress closes the tax shelter loop-hole: Almost overnight, demand for Lenny's limited partnership interests disappears. Deprived of his livelihood by the stroke of a pen, Lenny loses everything.").

255. *Id.*

256. Gulecas & Gassman, *supra* note 116, at 38.

257. *See* I.R.C. § 2010(c) (2000).

258. *See id.* § 2503(b)(2) (providing an inflation adjustment for the annual exclusion on gifts); *see also* 2002 MASTER TAX GUIDE ¶ 2908 (2001) (stating that in 2002 the annual exclusion amount is likely to increase to $11,000).

259. *See* I.R.C. § 2056.

260. Gulecas & Gassman, *supra* note 116, at 43.

261. *See supra* note 144 and accompanying text.

262. *See id.* (stating that dying in 2010 may be a noble goal for clients in their mid-to-late eighties).

263. *Id.*

> Without being too ghoulish, we can only hope that the perverse incentives under the new law will not result in estate tax planning by means of homicide at that time. Police who would otherwise be celebrating that New Year's Eve may instead be on duty and stationed by electrical outlets powering heart-lung machines![264]

VII. CONCLUSION

The estate tax is failing to meet its objectives.[265] Studies conclude that the estate tax is not effectively combating wealth concentration, and that this high wealth concentration correlates with poor economic performance.[266] However ineffective the estate tax is at breaking up concentrations of wealth, total repeal would only compound the problem.[267] In fact, I submit that tax legislation from 1976 to the present has played a significant role in the inability of the estate tax to achieve this objective.[268] The solution may be to increase the applicable exclusion amount to an amount sufficient to reach the wealthy—the target of the estate tax.

The estate tax also fails to produce a significant amount of revenue.[269] One solution may be to repeal or reduce some of the credits and deductions to the current estate tax. This proposal may have only a modest effect on revenue production, but with the federal government constantly operating with insufficient revenues and large deficits, along with the chance of the war on terrorism lasting long into the future, it would provide much needed revenue.

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264. *Id.*; *see also* ZARITSKY, *supra* note 5, ¶ 1.10 n.71 (stating that "[w]ealthy persons with families that are less than totally harmonious may wish to employ bodyguards and tasters during calendar year 2010, if Congress does not eliminate the sunset rules or make the estate tax permanent before that date").

265. *See* discussion *supra* Part III.A-C (noting that the estate tax has failed to meet at least two of its stated objectives, while losing ground on its third objective).

266. *See* Repetti, *supra* note 1, at 828-29 (asserting that studies confirm that high levels of wealth concentration correlate with poor economic performance); *see also* Donaldson, *supra* note 33, at 542 (stating that the estate tax has failed to play a significant role in the disintegration of wealth concentration).

267. *See* Repetti, *supra* note 1, at 856 (noting that experts believe total repeal of the estate tax would increase wealth held by the richest one percent of Americans anywhere from ten percent to two hundred percent).

268. *See supra* notes 77-83 and accompanying text (providing a summary of the recent tax acts and how they have contributed to the estate tax's failure to achieve its objective of reducing concentrations of wealth).

269. *See* Donaldson, *supra* note 33, at 543 (stating that in 1992, transfer taxes were budgeted to be $12 billion).

At one time, the estate tax provided a significant contribution to the ideal of progressivity in the federal tax system.[270] Recently, the estate tax has been contributing far less to the progressivity of the federal tax system.[271] A solution may lie in ensuring that the estate tax does what it was designed to do—tax that segment of society that has amassed great fortunes.[272]

President Bush's platform as a presidential candidate was geared toward tax breaks. Among the cuts signed into law by President Bush on June 7, 2001, was the "repeal" of the estate tax.[273] The 2001 Tax Act, like many of its predecessors, causes the estate tax to once again fail in meeting its objectives. Shoving aside the rhetoric, the 2001 Tax Act is not what the Bush Administration claims it is. The 2001 Tax Act, while in reality repealing the estate tax for only one year, complicates the transfer tax system and wreaks havoc on most existing estate plans.[274] States will likely have to increase other state taxes, including property and excise taxes, to make up for the loss in revenue which will result from the phase-out of the state death tax credit.[275] Who will be the lucky recipient of these higher taxes? The middle class. Moreover, charitable giving will likely be curbed, adversely affecting that segment of the population who needs help the most.[276] Unfortunately, the public has been misled into believing in the hype of total repeal. The consensus among practitioners and academics seems to be that total repeal is unlikely.[277] The following factors weigh against the prospect of total repeal: (1) the fact that the 2001 Tax Act contains a nine year phase-out, a sunset provision, a complicated and unpopular carryover basis regime, (2) the multitude of elections—both congressional and presidential—between now and actual repeal, (3) the economic circumstances of the nation, and (4) the uncertainty surrounding the war on terrorism.[278] The public needs to

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270. *See* Burke & McCouch, *supra* note 20, at 506-07 (noting that in 1970, transfer taxes contributed nearly one-third as much to the progressivity of the tax system as did the federal income tax).

271. *Id.* at 507.

272. *See* discussion *supra* Part II.A.

273. *See supra* note 6 and accompanying text.

274. Forsberg, *supra* note 18, at 23.

275. *See* Gulecas & Gassman, *supra* note 116, at 39 (noting that the State of Florida will likely see an increase in state taxes due to the phase-out of the state death tax credit).

276. Pearson, *supra* note 226, at 454.

277. *See, e.g.*, Burr, *supra* note 15, at 13.

278. Gulecas & Gassman, *supra* note 116, at 43; *see also* Gale & Orszag, *supra* note 211, at 11A (noting that a compromise may be to make the tax cuts that are already in place permanent, but delay others until they are affordable). Gale and Orszag further note that when the tax cuts of June 7, 2001, were signed, the projected surplus outside of Social Security and Medicare was $2.7 trillion. Gale & Orszag, *supra* note 217, at 11A. By February of 2002, there was a projected deficit outside Social Security and Medicare of $1 trillion. *Id.* Finally, Gale and Orszag assert: "The tax cuts plainly are not as affordable now." *Id.*

be properly informed of these prospects so they may safeguard their estates accordingly, thus, ensuring that money needed during retirement years does not vanish. No one has all the answers. In fact, in article after article, experts debate the proper alternative to the current transfer tax regime. The proper solution can be endlessly debated. I submit that total repeal is not the answer, rather, restructuring, refinement, and reprioritizing of estate tax objectives is. The 2001 Tax Act does more than "repeal" the death tax. It also secures a tax break for the wealthy and ensures that the adverse effects of wealth concentration will continue, while at the same time causing a government, in the midst of a deficit crisis, to take in less revenue. If none of these considerations have convinced you that repeal of the death tax is the wrong decision, perhaps the following parable will:

> [J]ust the other day, I heard today's version of thoughtful estate planning advice in the office of a well-known New York practitioner. A client had asked with great anxiety what he might do to minimize the estate taxes of his ninety-year-old widowed mother who had a large fortune, composed of extremely valuable art and cash. The lawyer thought for a great long while, no doubt running through his bag of estate planning tricks, when all of a sudden, with a gleam in his eye, looked up and said calmly, 'marry her.' It would be a shame if a tax which produces such creative advice were to disappear.[279]

*Tye J. Klooster**

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279. Graetz, *supra* note 27, at 286 (footnotes omitted).

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VERITAS

1881