

**MODELING THE FEDERAL REVENUE EFFECTS  
OF CHANGES IN ESTATE AND GIFT TAXATION**

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of the  
JOINT COMMITTEE ON TAXATION



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## INTRODUCTION

This document<sup>1</sup> describes the economic modeling that the staff of the Joint Committee on Taxation (“Joint Committee staff”) undertakes to estimate the Federal revenue effects of estate and gift tax proposals. The Joint Committee staff welcomes comments on its modeling of the Federal estate and gift taxes.

The Federal transfer tax system is composed of three taxes: the estate tax, the gift tax, and the generation skipping transfer tax.

The estate tax is levied on the estate of any person who was a citizen or resident of the United States at the time of death and on certain property of nonresidents that is situated in the United States. The estate tax is generally based on the fair market value of the estate at the time of death. In computing the taxable value of the estate, certain deductions, including deductions for charitable bequests and bequests to a surviving spouse, are allowed against the value of the gross estate.

A gift tax is imposed on the cumulative lifetime gifts made by U.S. citizens and residents and on certain gifts of U.S. property by nonresidents. This tax is imposed whether the gift is made directly or indirectly (*e.g.*, through a trust). The gift tax is imposed on the donor and is based on the fair market value of the gift at the time the gift is made. Deductions are generally allowed for gifts to spouses and to charities and for certain transfers for educational or medical expenses. Also, donors may exclude certain gifts of up to \$13,000 (for 2012) per donee annually, for both the tax and reporting requirements.

In addition to the estate and gift taxes, a separate transfer tax is imposed on generation skipping transfers, whether made at death or while living. Generation skipping transfers are generally transfers made to a beneficiary more than one generation below that of the transferor. For example, a transfer from a grandparent to a grandchild is generally a generation skipping transfer whereas a transfer from a parent to a child is not. The generation skipping transfer tax is imposed at the highest estate tax rate on transfers in excess of the estate tax exemption in effect for the year.

For estate and gift tax returns filed in 2008<sup>2</sup> approximately \$277 billion in value, including taxes paid, was reported transferred. Of this \$277 billion, \$229 billion was transferred at death (reported on an estate tax return) while \$48 billion was transferred during life (reported on a gift tax return). More than half of the \$277 billion in value transferred, approximately \$145 billion, was transferred to persons other than the spouse of the transferor; \$69 billion was

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<sup>1</sup> This document may be cited as follows: Joint Committee on Taxation, *Modeling the Federal Revenue Effects of Changes in Estate and Gift Taxation* (JCX-76-12), November 9, 2012. This document may also be found on our website at [www.jct.gov](http://www.jct.gov).

<sup>2</sup> Returns filed in 2008 generally represent transfers made in 2007 and, to a lesser extent, 2006. In 2006 and 2007 the exemption amount was \$2 million. The maximum marginal tax rate in 2006 was 46 percent; in 2007 it was 45 percent.

transferred to a spouse;<sup>3</sup> \$35 billion was donated to charitable entities; and \$28 billion was paid in Federal transfer taxes. Almost \$25 billion of this \$28 billion in transfer taxes arose from the estate tax; less than \$150 million was attributable to the generation skipping transfer tax.

Most estates of decedents who died in 2007 were not required to file estate tax returns because they did not have gross estates in excess of the exemption amount for that year, \$2 million. Of the approximately 2.5 million people who died in 2007, about 36,700 estates filed estate tax returns.<sup>4</sup> Less than half of those 36,700 estate tax returns, approximately 16,600, reported an estate tax liability. That is, about 1.5 percent of estates of decedents who died in 2007 filed estate tax returns and 0.66 percent of such estates had an estate tax liability. Returns of married 2007 decedents comprised about 49 percent of returns filed. Because of the unlimited marital deduction, significantly fewer returns of married decedents reported an estate tax liability. Only 10 percent of the estate tax returns of married 2007 decedents reported an estate tax liability, while nearly 80 percent of the estate tax returns of unmarried 2007 decedents reported an estate tax liability.

Approximately 257,000 gift tax returns were filed in 2008.<sup>5</sup> Of these returns, approximately 172,000 reported a gift in excess of the gift tax annual exclusion amount,<sup>6</sup> which was \$12,000 in 2007.<sup>7</sup> Gifts other than annual exclusion gifts generally were subject to a lifetime exemption amount of \$1 million. Approximately 9,600 gift tax returns filed in 2008 reported some gift tax liability aggregating to \$2.8 billion.

The remainder of this document is organized as follows. Because the estate and gift tax laws are complex and have been in flux for more than a decade, the first section lays out a brief description of estate and gift tax law as it presently stands and its recent history. The next section describes the economic issues and the model used to address them. The third section illustrates the modeling techniques described in the previous section by describing the Joint

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<sup>3</sup> Generally, transfers to a spouse during life are not required to be reported on a gift tax return. More than 98 percent of reported transfers to a spouse were made at death.

<sup>4</sup> 2007 is the latest year for which complete estate tax information is available by year of death instead of filing year.

<sup>5</sup> Gift tax returns filed in 2008 are generally representative of gifts given in 2007.

<sup>6</sup> Spouses may elect to “split” annual exclusion gifts with one another; that is, they may treat one-half of a gift made by one spouse as having been made by the other spouse for purposes of the gift tax annual exclusion. For example, in 2012 when the annual exclusion is \$13,000, one spouse can make a gift of \$26,000 to a single recipient and, if her spouse consents and a proper election is made, treat the gift as having been made \$13,000 by herself and \$13,000 by her spouse. Of the approximately 85,000 returns filed in 2008 that did not report a gift in excess of the annual exclusion amount, it appears that a significant majority were filed for the purpose of electing to split gifts with a spouse.

<sup>7</sup> The total number of gifts made in 2007 is not known since there is no filing requirement for most gifts under the gift tax exclusion amount.

Committee staff's estimate of the President's fiscal year 2013 estate and gift budget proposal.<sup>8</sup> Finally, the appendix contains information related to the distribution of estate tax liabilities under different estate tax policies.

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<sup>8</sup> For a complete description of the President's fiscal year 2013 budget proposals, see Joint Committee on Taxation, *Description of Revenue Provisions Contained in the President's Fiscal Year 2013 Budget Proposal* (JCS-2-12), June 2012.

## **I. DESCRIPTION OF THE LAW**

### **A. Basic Structure of Estate and Gift Taxation**

#### **Rates and exemption amounts**

Under present law, a unified credit is available with respect to taxable transfers made during life and at death. This credit offsets any tax liability accruing to transfers up to the applicable exclusion amount, or exemption amount. For example, the exemption amount in 2012 is \$5.12 million. The tax due on a transfer of \$5.12 million is \$1,772,800, which is the unified credit amount. The unified credit will cover the tax on a transfer of up to \$5.12 million, but a transfer of more than this amount could generate a tax liability larger than the unified credit amount, depending upon other available exclusions, deductions, or credits. This unified credit is non-refundable; therefore, for example, a taxpayer who died in 2012 with a taxable estate valued at \$750,000 and made no lifetime taxable gifts would owe no transfer taxes and would not be entitled to a refund of the unused portion of the unified credit.

Before the passage of the Economic Growth and Tax Relief Reconciliation Act of 2001 (“EGTRRA”),<sup>9</sup> the estate and gift taxes were unified with a common exemption amount and a common rate structure. The estate and gift tax exemption amount was scheduled to rise to \$1 million in 2006 and remain at \$1 million thereafter. The graduated tax rate structure provided for a maximum tax rate of 55 percent on taxable transfers of more than \$3 million. However, the law provided for a five-percent surtax on taxable transfers between \$10 million and \$17.184 million to recapture the benefit of the increasing graduated tax rate structure.<sup>10</sup> Therefore, estates with taxable values of at least \$17.184 million faced a flat estate tax of 55 percent on taxable estate values in excess of \$1 million.

Under EGTRRA, the estate, gift, and generation skipping taxes were gradually reduced from 2002 through 2009 through reductions in the maximum marginal tax rates and increases in the exemption amounts. In 2002, the exemption amount for both estate and gift (and, therefore, generation skipping) tax purposes increased to \$1 million and the highest estate and gift tax marginal tax rate fell to 50 percent. In 2003, the highest estate and gift tax marginal tax rate was 49 percent. In 2004, the exemption amount increased to \$1.5 million for estate and generation skipping transfer tax purposes<sup>11</sup> while the maximum marginal tax rate applied to estates and gifts fell to 48 percent. In 2005, the maximum estate and gift tax marginal tax rate fell to 47 percent. In 2006, the exemption amount increased to \$2 million for estate and generation skipping transfer tax purposes and the highest marginal tax rate applied to estates and gifts fell to 46

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<sup>9</sup> Pub. L. No. 107-16.

<sup>10</sup> Therefore, the effective maximum marginal tax rate was 60 percent on taxable transfers between \$10 million and \$17.184 million.

<sup>11</sup> EGTRRA decoupled the estate and gift tax exemption amounts. As the estate tax exemption amount rose, the credit exemption amount for gift tax purposes remained at \$1 million for 2004 and years thereafter. Estates and gifts still faced a common rate structure.

percent. In 2007, the maximum marginal tax rate applied to estates and gifts fell to 45 percent. In 2009, the exemption amount for estate and generation skipping transfer tax purposes rose to \$3.5 million.

EGTRRA repealed the estate and generation skipping taxes for decedents dying and gifts made after 2009. EGTRRA retained a gift tax after 2009 with a 35-percent tax rate on lifetime gifts in excess of \$1 million.

However, the provisions of EGTRRA that modified the estate, gift, and generation skipping transfer taxes were scheduled to expire at the end of 2010. Therefore, the repeal of the estate and generation skipping taxes would not apply to decedents dying or gifts made after 2010. The estate, gift, and generation skipping transfer tax rates and exemption amounts scheduled to be in effect prior to EGTRRA were to apply to the estates of decedents dying after 2010 and for gifts made after 2010. In 2011 and later years the estate and gift taxes were to be reunified so that a common exemption amount of \$1 million and a common graduated rate schedule with a maximum rate of 55 percent<sup>12</sup> were to apply for purposes of determining the tax on cumulative taxable transfers made by a taxpayer during life and at death.

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the “Tax Relief Act”)<sup>13</sup> generally extended and modified the estate and gift tax framework enacted under EGTRRA for two years, through 2012. The Tax Relief Act generally reinstated the estate and generation skipping transfer taxes for 2010 with a \$5 million estate tax exemption amount and a maximum tax rate of 35 percent. The Tax Relief Act provided that executors of decedents dying in 2010 could elect to have EGTRRA apply.<sup>14</sup> Also, the Tax Relief Act specified that the generation skipping transfer tax rate was zero in 2010 with a \$5 million exemption amount. The Tax Relief Act also increased the gift tax exemption amount to equal the estate tax exemption amount (or reunified the exemptions) after 2010. The \$5 million estate and gift tax exemption amount is indexed for inflation for years after 2011. The Tax Relief Act also generally allows the unused exemption amount of a spouse to be used by (or ported to) the surviving spouse.

After 2012, the Tax Relief Act’s extension and modification of EGTRRA expire and the estate, gift, and generation skipping transfer tax rates and exemption amounts scheduled to be in effect prior to EGTRRA apply to the estates of those dying after 2012 and for gifts made after 2012. Therefore, in 2013 and later years the estate and gift taxes are unified with a common

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<sup>12</sup> Again, there was to be a five-percent surtax on taxable estate values between \$10 million and \$17.184 million to recapture the benefit of the graduated rates. Thus, the highest effective marginal tax rate was to be 60 percent.

<sup>13</sup> Pub. L. No. 111-312.

<sup>14</sup> If the executor of a 2010 decedent so elected, the estate of that decedent would follow the EGTRRA estate and gift tax laws for 2010. That is, the decedent’s estate would not be subject to the estate tax and assets acquired from the decedent would not receive a step up in basis but rather would receive the modified carryover basis described in section 1022.

exemption amount of \$1 million and a common graduated rate schedule with a maximum rate of 55 percent<sup>15</sup> applies for purposes of determining the tax on cumulative taxable transfers made by a taxpayer during life and at death. The changes under EGTRRA and the Tax Relief Act are summarized in Table 1 below.

**Table 1.—Estate and Gift Exemption Amounts and Tax Rates  
Under EGTRRA and the Tax Relief Act**

| <b>Calendar Year</b> | <b>Estate (and GST) Tax Exemption Amount</b> | <b>Gift Tax Exemption Amount</b> | <b>Highest Estate and Gift Tax Rates</b> |
|----------------------|----------------------------------------------|----------------------------------|------------------------------------------|
| 2001                 | \$675,000                                    | \$675,000                        | 60% <sup>1</sup>                         |
| 2002                 | \$1,000,000                                  | \$1,000,000                      | 50%                                      |
| 2003                 | \$1,000,000                                  | \$1,000,000                      | 49%                                      |
| 2004                 | \$1,500,000                                  | \$1,000,000                      | 48%                                      |
| 2005                 | \$1,500,000                                  | \$1,000,000                      | 47%                                      |
| 2006                 | \$2,000,000                                  | \$1,000,000                      | 46%                                      |
| 2007                 | \$2,000,000                                  | \$1,000,000                      | 45%                                      |
| 2008                 | \$2,000,000                                  | \$1,000,000                      | 45%                                      |
| 2009                 | \$3,500,000                                  | \$1,000,000                      | 45%                                      |
| 2010                 | \$5,000,000 <sup>2</sup>                     | \$1,000,000                      | 35%                                      |
| 2011                 | \$5,000,000                                  | \$5,000,000                      | 35%                                      |
| 2012                 | \$5,120,000 <sup>3</sup>                     | \$5,120,000 <sup>3</sup>         | 35%                                      |
| After 2012           | \$1,000,000                                  | \$1,000,000                      | 60% <sup>1</sup>                         |

<sup>1</sup> Including the 5 percent surtax on estates with taxable values between \$10 million and \$17.184 million.

<sup>2</sup> Executors of estates of decedents dying in 2010 could elect out of the estate tax (and into EGTRRA). Also, the GST tax rate was zero in 2010.

<sup>3</sup> The Tax Relief Act indexed the exemption amounts after 2011 for inflation.

### **Basis in property received**

Gain or loss on the disposition of property is measured by the amount realized on the sale of the asset less the taxpayer's basis in the asset. The basis generally represents the taxpayer's investment in the property, with certain adjustments. For example, basis is increased by the cost of capital improvements made to the property and decreased by any depreciation deductions taken with respect to the property.

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<sup>15</sup> Therefore, the effective maximum marginal tax rate is 60 percent on taxable transfers between \$10 million and \$17.184 million.

Under present law, the basis in property received from a donor of a lifetime gift generally is carried over. Carryover basis means that the basis of property in the hands of the donee is the same as it was in the hands of the donor. The basis of property transferred by a lifetime gift is increased by any gift tax paid by the donor. However, the basis of a lifetime gift generally cannot exceed its fair market value on the date of the gift. Therefore, a donor's unrealized capital loss on an asset given to a donee cannot be recognized by the donee. Carryover basis generally preserves the character of the gain so that, for example, real estate that has been depreciated and would be subject to recapture if sold by the donor is subject to recapture if sold by the donee.

Property acquired from a decedent generally receives stepped-up basis.<sup>16</sup> Stepped-up basis means that the basis for property in the hands of an heir is not the same as the basis in the hands of a decedent but rather the fair market value of the property on the date of the decedent's death.<sup>17</sup> This step-up in basis eliminates the recognition of income on any appreciation of the property that may have occurred during the lifetime of the decedent. Conversely, if the value of the property on the date of the decedent's death is less than the basis of the property to the decedent then the property takes a "step-down" in basis. This step-down eliminates any income tax benefit from the unrealized loss.

### **Treatment of State death taxes**

Prior to 2005, a credit was allowed against the Federal estate tax for any estate, inheritance, legacy, or succession taxes ("death taxes") paid to any State or the District of Columbia with respect to any property included in the decedent's gross estate. The maximum amount of credit allowed for State death taxes was determined under a graduated rate table.<sup>18</sup>

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<sup>16</sup> As discussed above, EGTRRA provided for the elimination of the estate and generation skipping transfer taxes in 2010. Upon the repeal of the estate and generation skipping transfer taxes, EGTRRA provided for a modified carryover basis regime. Under this modified carryover basis regime, the executor of an estate could allocate up to \$1.3 million (\$4.3 million in the case of a married decedent) in basis to property in the decedent's estate. Certain unused losses could also be allocated to the decedent's property. Otherwise, property acquired from a decedent upon the decedent's death was treated as if the property were acquired by gift. That is, under the modified carryover basis regime, the basis of the property in the hands of an heir generally was the lesser of the decedent's basis or the fair market value at the time of the decedent's death.

<sup>17</sup> An alternative valuation date may be elected provided such date is the earlier of six months after the decedent's death or the date the property is sold or distributed by the estate.

<sup>18</sup> See Sec. 2011 of the Internal Revenue Code. The State death tax credit was enacted as part of the Revenue Act of 1924. It was limited to the lesser of State death taxes paid or 25 percent of Federal estate tax liability. In 1926, the credit was set so that it would equal 80 percent of Federal estate tax liability under the 1926 estate tax schedule. The credit was unchanged until it was phased out by EGTRRA. Unless otherwise stated, all section references are to the Internal Revenue Code of 1986, as amended.

The maximum credit rate was 16 percent. States imposed an estate tax at least equal to the maximum Federal credit allowed.<sup>19</sup>

EGTRRA phased out this credit for State death taxes paid from 2002 through 2004. After 2004, the State death tax credit was repealed and replaced with a deduction for death taxes paid to any State or the District of Columbia with respect to any property included in the decedent's gross estate. The deduction for State death taxes paid was scheduled to expire in 2010 under EGTRRA with the State death tax credit reinstated beginning in 2011; however, the Tax Relief Act extended the State death tax deduction through 2012. For decedents dying in 2013 and later years the credit for State death taxes paid is reinstated as it existed prior to EGTRRA.

### **Portability of unused exemption between spouses**

Under the Tax Relief Act, any estate tax exemption that remains unused as of the death of a spouse who dies after December 31, 2010, generally is available for use by the surviving spouse as an addition to the surviving spouse's own exemption. A surviving spouse may use the predeceased spouse's carryover, or ported, exemption in addition to the surviving spouse's own exemption for transfers made by gift or at death. Like the other provisions of the Tax Relief Act, portability of unused exemption is effective only through 2012, for spouses dying after 2010, and does not apply to the estates of decedents dying after December 31, 2012.

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<sup>19</sup> Thus, this credit served as a mechanism to transfer revenue from the Federal government to the State governments.

## **B. Exclusions and Deductions**

### **Gift tax annual exclusion**

For 2012, donors of lifetime gifts are provided an annual exclusion of \$13,000 (this amount is indexed for inflation) on transfers of present interests in property to each donee.

### **Exclusion for educational and medical expenses**

Qualified transfers for educational or medical purposes on behalf of an individual are not considered gifts. For purposes of this exemption, qualified transfers are tuition paid to an educational organization or payments made to any person providing medical care.

### **Transfers to a surviving spouse**

Generally, a 100-percent marital deduction is available for the value of property transferred between spouses for both estate and gift tax purposes.<sup>20</sup> Furthermore, this marital deduction is permitted even when the surviving spouse cannot control the disposition of the property after the surviving spouse's death as long as the surviving spouse has an income interest in the property and the property is subject to the estate or gift tax when transferred from the surviving spouse (property of this kind is referred to as "qualified terminable interest property").

### **Transfers to charity**

Generally, transfers made to charities, governmental units, and certain other eligible donees by gift during life are completely deductible for gift tax purposes. Likewise, such transfers made by bequest at death are completely deductible against the total gross estate.

### **Conservation easements**

An executor generally can elect to exclude from the taxable estate 40 percent of the value of any land subject to a qualified conservation easement, up to a maximum exclusion of \$500,000. EGTRRA expanded the availability of qualified conservation easements by eliminating certain geographic restrictions on qualifying conservation easements. The Tax Relief Act extended this geographic expansion. The expansion expires along with the other estate and gift tax provisions of the Tax Relief Act on December 31, 2012.

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<sup>20</sup> This complete marital deduction is generally denied for surviving spouses who are not citizens of the United States. However, a marital deduction is allowed for property passing to a domestic trust of which the noncitizen surviving spouse is a beneficiary. Estate tax is then imposed on distributions of corpus from the trust and on the value of the property remaining in the trust upon the death of the noncitizen surviving spouse.

## **C. Provisions Affecting Small and Family-Owned Businesses and Farms<sup>21</sup>**

### **Special-use valuation**

Under certain circumstances, an executor can elect to value certain property used in farming or in another closely held business at its current-use value, rather than at its fair market value.<sup>22</sup> The maximum reduction in value is currently \$1,040,000 and is adjusted annually for inflation.

### **Family-owned business deduction**

Prior to 2004, under certain conditions, an estate was permitted to deduct the adjusted value of a qualified family-owned business interest of the decedent, up to a maximum deduction of \$675,000.<sup>23</sup> To qualify for the exclusion, the decedent (or a member of the decedent's family) must have owned and materially participated in the trade or business for at least five of the eight years preceding the decedent's date of death.<sup>24</sup> Also, at least one qualified heir (or member of the qualified heir's family) was required to materially participate in the trade or business for at least 10 years following the decedent's death.

This provision was repealed by EGTRRA. The Tax Relief Act extended the repeal through December 31, 2012. This provision applies to decedents dying after December 31, 2012.

### **Installment payment of estate tax for closely held businesses**

Under present law, the estate tax is generally due within nine months of a decedent's death. However, an executor may elect to pay estate tax attributable to an interest in a closely held business in up to 10 installments. If the election is made, the estate may defer payment of principal and pay only interest for the first five years, followed by 10 annual installments of

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<sup>21</sup> For a fuller description of some of these provisions see Joint Committee on Taxation, *Taxation of Wealth Transfers Within a Family: A Discussion of Selected Areas for Possible Reform* (JCX-23-08), April 2008. See also sec. 2032A.

<sup>22</sup> Sec. 2057.

<sup>23</sup> After 2012, the qualified family-owned business deduction amount and the unified credit effective exemption amount are coordinated. If the maximum deduction amount of \$675,000 is elected then the unified credit effective exemption amount is \$625,000, for a total exemption amount of \$1.3 million. If the qualified family-owned business deduction is less than \$675,000 then the unified credit effective exemption amount is equal to \$625,000 plus the difference between \$675,000 and the amount of the qualified family-owned business deduction. Because the maximum total exemption amount when claiming the qualified family-owned business deduction is \$1.3 million, the qualified family-owned business deduction provides no benefit in any year in which the applicable exclusion amount is \$1.3 million or more.

<sup>24</sup> There are also certain other provisions concerning the citizenship of the decedent, his or her ownership of the business, and the decedent's ownership of the assets.

principal and interest.<sup>25</sup> This provision effectively extends the time for paying estate tax by 14 years from the original due date. Furthermore, a special two-percent interest rate applies to a portion of the deferred estate tax.<sup>26</sup>

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<sup>25</sup> Secs. 6161(a)(2) and 6166.

<sup>26</sup> The portion eligible for the special interest rate is adjusted annually for inflation. In 2012, this amount is the first \$1.39 million of deferred tax.

## II. MODELING ESTATE AND GIFT TAX PROPOSALS

All revenue estimates prepared by the Joint Committee staff begin with the 10-year projection of baseline Federal receipts prepared by the Congressional Budget Office (the “CBO”). The CBO bases the estate and gift tax baseline receipts forecast on samples of estate and gift tax returns as well as data from the Federal Reserve’s Survey of Consumer Finances (“SCF”).<sup>27</sup> The estate tax return data provides information about gross estates with values above the filing threshold and the SCF provides information on household wealth for households below that threshold. The CBO uses these data, along with their economic and demographic projections, to generate estimates of population wealth. These wealth estimates are then used to forecast estate tax receipts in each year of the budget window. Gift tax receipts are projected based on the historical relationship between gift tax receipts and wealth, with adjustments for taxpayer responses to changing estate and gift tax laws.

The revenue estimates produced by the Joint Committee staff are the expected changes in Federal revenues, relative to the CBO baseline, resulting from proposed tax law changes. The Joint Committee staff generally incorporates microeconomic behavioral effects into its revenue estimates. However, for purposes of conventional revenue estimates, the Joint Committee staff generally assumes that changes in the tax law do not cause changes in aggregate economic activity. Therefore, changes in the estate and gift tax rates are assumed not to generate changes in the total output of the economy.<sup>28</sup>

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<sup>27</sup> The SCF is generally administered every three years. The most recent year for which data is available is 2010. More information may be found at [www.federalreserve.gov/econresdata/scf/scfindex.htm](http://www.federalreserve.gov/econresdata/scf/scfindex.htm).

<sup>28</sup> Conventional revenue estimates of estate and gift tax legislation attempt to account for microeconomic behavioral effects but assume that the proposal does not change the underlying macroeconomic environment. For more information on the revenue estimating methods of the Joint Committee staff, see Joint Committee on Taxation, *Testimony of the Staff of the Joint Committee on Taxation Before the House Committee on Ways and Means Regarding Economic Modeling* (JCX-48-11), September 2011; Joint Committee on Taxation, *Exploring Issues in the Development of Macroeconomic Models for Use in Tax Policy Analysis* (JCX-19-06), June 2006; Joint Committee on Taxation, *Overview of Revenue Estimating Procedures and Methodologies Used by the Staff of the Joint Committee on Taxation* (JCX-1-05), February 2005; and Joint Committee on Taxation, *Overview of the Work of the Staff of the Joint Committee on Taxation to Model the Macroeconomic Effects of Proposed Tax Legislation to Comply with House Rule XIII.3(h)(2)* (JCX-105-03), December 2003.

## A. Economic and Behavioral Considerations

### The tax base

The estate tax generally is levied upon the terminal wealth of the decedent, that is, the value of the decedent's assets minus the value of the decedent's liabilities at the time of death.<sup>29</sup> Under present law, some assets are fully included in the estate tax base, some assets are partially included in the tax base, and some assets are fully excluded from the estate tax base, as shown in Table 2.

**Table 2.—The Estate Tax Base**

|                           |                                                                                                                                                                                                                        |
|---------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Fully Included</b>     | Personal Residences<br>Other Real Estate<br>Publicly Traded Stock<br>Bonds<br>Mutual Funds<br>Life Insurance on the Decedent Owned by the Decedent<br>Pension and Annuity Assets<br>Cash<br>Collectibles               |
| <b>Partially Included</b> | Family Owned Business Assets<br>Farming Property<br>Closely Held Business Assets<br>Conservation Easements                                                                                                             |
| <b>Fully Excluded</b>     | All Assets Transferred to a Surviving Spouse<br>All Assets Transferred to Charity<br>Certain Estate Administrative Expenses<br>( <i>e.g.</i> , funeral expenses)<br>Certain Assets Transferred to a Trust <sup>1</sup> |

<sup>1</sup> Assets transferred in a testate transfer that is a completed gift for transfer tax purposes are not includable in the gross estate (for example, as under sections 2035 through 2038).

A different way to conceptualize the tax base is to consider how the assets of a decedent would appear on the estate tax return itself. The estate tax form (IRS Form 706) is laid out substantially as below to facilitate the computation of estate tax liability.

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<sup>29</sup> The executor of the estate may also elect to use the value of the decedent's assets at the date of sale or six months after the decedent's date of death, whichever is earlier.

| Estate Tax Computation |                                                            |
|------------------------|------------------------------------------------------------|
| <b>Estate Value</b>    |                                                            |
| -                      | <u>(Valuation Discounts)</u>                               |
| -                      | <u>(Conservation Easements)</u>                            |
| =                      | Gross Estate                                               |
| -                      | <u>(Deductions)</u>                                        |
| =                      | Taxable Estate                                             |
| +                      | <u>Adjusted taxable gifts (generally, post-1976 gifts)</u> |
| =                      | Sum of taxable estate & adjusted taxable gifts             |
| x                      | <u>Estate tax rates</u>                                    |
| =                      | Tentative tax                                              |
| -                      | <u>(Gift tax attributable to post-1976 gifts)</u>          |
| =                      | Gross estate tax                                           |
| -                      | <u>(Credits)</u>                                           |
| =                      | <u>Estate tax liability</u>                                |

A summary of estate tax returns filed in 2008 is presented in Table 3 below.<sup>30</sup>

**Table 3.—Summary of Estate Tax Returns Filed in 2008**

(Number of Returns; Dollar Amounts in Millions)

|                                                  | <u><b>Taxable Estates</b></u> |               | <u><b>Nontaxable Filing Estates</b></u> |               |
|--------------------------------------------------|-------------------------------|---------------|-----------------------------------------|---------------|
|                                                  | <b>Number</b>                 | <b>Amount</b> | <b>Number</b>                           | <b>Amount</b> |
| Estate Value                                     | 17,172                        | \$139,572     | 21,202                                  | \$103,523     |
| Valuation Discounts                              | 3,807                         | (\$10,869)    | 3,333                                   | (\$3,336)     |
| Conservation Easements                           | 43                            | (\$17)        | 0                                       | \$0           |
| Gross Estate                                     | 17,172                        | \$128,685     | 21,202                                  | \$100,187     |
| Total Deductions                                 | 17,166                        | (\$42,405)    | 21,198                                  | (\$69,928)    |
| Funeral Expenses                                 | 16,287                        | \$183         | 16,987                                  | \$190         |
| Executor Commissions                             | 10,085                        | \$1,144       | 2,392                                   | \$156         |
| Attorneys Fees                                   | 14,851                        | \$770         | 7,718                                   | \$264         |
| Bequests to Surviving Spouse                     | 1,479                         | \$10,891      | 16,647                                  | \$56,719      |
| Charitable Deduction                             | 4,009                         | \$20,932      | 3,206                                   | \$7,440       |
| Debts and Mortgages                              | 14,604                        | \$3,868       | 13,032                                  | \$4,588       |
| State Death Tax Deduction                        | 7,698                         | \$3,145       | 3,863                                   | \$330         |
| Other Deductions                                 | 16,767                        | \$1,472       | 11,110                                  | \$242         |
| Taxable Estate                                   | 17,172                        | \$86,281      | 19,641                                  | \$30,687      |
| Adjusted Taxable Gifts                           | 6,211                         | \$6,521       | 4,000                                   | \$2,142       |
| Sum of Taxable Estate and Adjusted Taxable Gifts | 17,172                        | \$92,802      | 19,703                                  | \$32,829      |
| Tentative Tax                                    | 17,172                        | \$39,825      | 19,699                                  | \$12,608      |
| Post-1976 Gift Adjustment                        | 1,700                         | (\$1,497)     | 588                                     | (\$241)       |
| Gross Estate Tax                                 | 17,172                        | \$38,328      | 19,695                                  | \$12,367      |
| Credits                                          | 17,172                        | (\$13,458)    | 21,202                                  | (\$16,309)    |
| Estate Tax Liability                             | 17,172                        | \$24,870      | 0                                       | \$0           |

<sup>30</sup> Some estates hold sufficient assets in combination with gifts to meet the filing threshold but do not have a tax liability after factoring in credits and deductions. These estates would be “Nontaxable Filing Estates” in the table.

The tax base for the gift tax includes the total gifts for the calendar year,<sup>31</sup> less the gift tax annual exclusion and less deductions for charitable gifts and gifts to a spouse. The gift tax computation is as follows. First, compute a tentative tax by applying the current year tax rate table to the sum of all taxable gifts for the current calendar year and all prior calendar years. Second, compute a tentative tax by applying this same current year tax rate table to the sum of all taxable gifts for prior calendar years only. Third, subtract the result of the second calculation from the result of the first calculation to determine the tax due on current calendar year gifts. Finally, subtract any remaining unified credit to determine the gift tax payable on current calendar year gifts. A summary of gift tax returns filed in 2008 is presented in Table 4 below.<sup>32</sup>

**Table 4.—Summary of Gift Tax Returns Filed in 2008**  
(Number of Returns; Dollar Amounts in Millions)

|                               | <u>Taxable Returns</u> |            | <u>Nontaxable Returns</u> |            |
|-------------------------------|------------------------|------------|---------------------------|------------|
|                               | Number                 | Amount     | Number                    | Amount     |
| Gift Value                    | 9,553                  | \$12,895   | 247,932                   | \$35,781   |
| Valuation Discounts           | 1,528                  | (\$853)    | 25,542                    | (\$2,576)  |
| Total Value of Gifts          | 9,553                  | \$12,042   | 247,932                   | \$33,205   |
| Annual Exclusions             | 9,151                  | (\$896)    | 235,196                   | (\$8,557)  |
| Marital Deduction             | 137                    | (\$142)    | 1,218                     | (\$1,035)  |
| Charitable Deduction          | 752                    | (\$3,445)  | 7,022                     | (\$3,075)  |
| Current Year Gifts            | 9,553                  | \$7,559    | 157,714                   | \$20,538   |
| Gifts from Prior Years        | 9,033                  | \$26,036   | 108,323                   | \$47,877   |
| Total Taxable Gifts           | 9,553                  | \$33,595   | 196,629                   | \$68,416   |
| Tax on Total Taxable Gifts    | 9,553                  | \$14,041   | 195,727                   | \$23,404   |
| Tax on Gifts from Prior Years | 9,033                  | (\$10,761) | 107,457                   | (\$17,056) |
| Balance                       | 9,553                  | \$3,280    | 157,592                   | \$6,348    |
| Unified Credit <sup>1</sup>   | 3,410                  | (\$437)    | 157,592                   | (\$6,348)  |
| Gift Tax Due                  | 9,553                  | \$2,843    | 0                         | \$0        |

<sup>1</sup> Includes a small amount of credit for foreign gift taxes paid.

Once the tax base has been determined, the estate and gift microsimulation model is used to calculate preliminary forecasts of estate and gift tax revenue in each calendar year in the budget period. Details of this microsimulation model are described below in part B of this section.

<sup>31</sup> Certain gifts for educational and medical purposes and to certain political organizations are statutorily excluded from the gift tax base.

<sup>32</sup> Similarly to Estate Tax returns, Gift Tax returns may have a filing requirement but not a tax liability. In the case of Gift Tax returns, this is often due to the gift amount exceeding the annual exclusion amount but not exceeding the donor's unused exemption amount.

## **Behavior**

Taxpayer responses to changes in the estate and gift tax laws can lead to changes not only in estate and gift tax receipts, but also in income tax receipts. Generally, changes in estate and gift tax rates and exemption amounts are expected to change estate, gift, and income tax receipts in the following ways:

- Changing the timing and amount of *inter vivos* giving
- Changing the timing and amount of charitable contributions claimed on income and estate tax returns
- Changing the amount of capital gains realized on income tax returns
- Shifting various deductions between the estate and income tax returns
- Expanding or contracting opportunities for the use of tax planning and mitigation techniques

The first three of these effects, generally known as “life-time planning,” are influenced by the income tax rates on ordinary income, the capital gains tax rates, the estate and gift tax rates, and the estate and gift tax exemption amounts. The fourth item concerns efforts by the taxpayer to maximize the tax benefit of any particular activity. Shifting deductions between the estate and income tax returns, sometimes called “form shopping,” is primarily influenced by the income and estate tax rates and exemption amounts. The final consideration, tax planning, concerns the ease with which taxpayers may remove their assets from the transfer or income tax bases. These are discussed in turn below.

### **Changing the timing and amount of *inter vivos* giving**

Wealthy individuals are sensitive to changes in tax rates and to differences between the estate and gift tax rates.<sup>33</sup> For example, after the enactment of EGTRRA, taxable giving fell substantially; the CBO projected a large increase in taxable gifts in 2010 when the generation skipping tax was scheduled to be repealed and the highest tax rate applied to gifts was to fall to 35 percent.<sup>34</sup> That is, the highest tax rate applied to gifts in 2010 was scheduled to be 20

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<sup>33</sup> See David Joulfaian, “The Federal Estate and Gift Tax: Description, Profile of Taxpayers, and Economic Consequences,” *U.S. Department of the Treasury*, OTA Paper 80, December 1998. Joulfaian argues that taxable gift giving increased substantially in 1976 in response to the passage of the Tax Reform Act of 1976 which increased gift rates from 57.75 percent to 70 percent effective in 1977. He also argues that the growth in gift tax receipts in the late 1980s may have been a response to the fall in maximum gift tax rate from 70 percent to 50 percent. See James Poterba, “Estate and Gift Taxes and Incentives for Inter Vivos Giving in the United States,” *NBER Working Paper* 6842, December 1998. Poterba discusses the sensitivity of *inter vivos* giving to the estate tax. Also, see Kathleen McGarry, “Behavioral Responses to the Estate Tax: Inter Vivos Giving,” *National Tax Journal*, vol. 53, no. 4, Part 1, December 2000, pp. 913-931. Finally, for anecdotal evidence, see Arden Dale, “A Rush to Value Gifts for Tax Savings,” *Wall Street Journal*, October 26, 2012, <http://online.wsj.com/article/SB10001424052970203922804578080562098642722.html>.

<sup>34</sup> Congressional Budget Office, *Federal Estate and Gift Taxes*, December 2009.

percentage points lower than the highest rate to be applied in 2011 (55 percent) and 10 percentage points lower than the highest gift tax rate in 2009 (45 percent). This predicted surge of gift giving in 2010 was consistent with the deferral of taxable gifts in the years leading up to 2010 to take advantage of the relatively favorable gift tax regime in that year. However, the enactment of the Tax Relief Act in late 2010 mitigated the incentive to give gifts in 2010;<sup>35</sup> instead, the Tax Relief Act increased the gift and generation skipping transfer tax exemption amounts to \$5 million and maintained a 35-percent top tax rate through 2012. Due to the scheduled expiration of the estate and gift tax provisions of the Tax Relief Act at the end of 2012, the Joint Committee staff expects a large amount of gift giving during 2012.

Changes in the estate and gift tax rate structure may also alter the relative advantages of lifetime giving versus bequests at death. While many factors affect a taxpayer's decision between lifetime gifts and bequests at death, generally a reduction in the estate tax rate reduces the tax incentive to make lifetime taxable gifts. Gifts are generally taxed less heavily than estates, even when the tax rate is the same, because the gift tax is levied on a tax-exclusive basis and the estate tax is levied on a tax-inclusive basis.<sup>36</sup> That is, the estate tax is paid out of the funds to be transferred to an heir whereas the gift tax is paid out of funds that are not part of the gift.<sup>37</sup> As the common tax rate on estates and gifts falls, the advantage of the tax exclusive gift tax versus the tax inclusive estate tax diminishes and so lifetime transfers become less favored.<sup>38</sup> These considerations are part of every estimate performed by the Joint Committee staff.

For revenue estimating purposes, the Joint Committee staff generally assumes a relatively stable amount of giving over the 10-year budget window and that this giving may be shifted from year to year to take advantage of temporarily low tax rates and/or high exemption amounts.

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<sup>35</sup> Even so, the data on gift tax returns filed in 2010, which are generally representative of gifts made in 2009 when the top gift tax rate was 45 percent, show approximately \$38 billion in gifts while gift tax returns filed in 2011, which are generally representative of gifts made in 2010 when the top gift tax rate was 35 percent, report gifts of \$51 billion.

<sup>36</sup> However, the basis rules granting assets acquired from a decedent a step-up in basis generally favor bequests at death over lifetime gifts for appreciated property.

<sup>37</sup> As an example, consider a taxpayer who has exhausted her full exemption amount. This taxpayer has an additional \$1 million in assets that she will transfer to an heir either in life or at death. With a common tax rate of 35 percent, at death this taxpayer pays a tax of \$350,000 on the gross transfer of \$1 million and the heir receives \$650,000. On the other hand, if the taxpayer makes this transfer during life, then the taxpayer makes a taxable gift of approximately \$740,741. The recipient receives approximately \$740,741 and the taxpayer pays tax of approximately \$259,259.

<sup>38</sup> See David Joulfaian, "Choosing Between Gifts and Bequests: How Taxes Affect the Timing of Wealth Transfers," *Journal of Public Economics*, vol. 89, 2005, pp. 2069-2091. Joulfaian demonstrates that the advantages of bequests rise with the capital gains and gift tax rates, and decline with the estate tax rate.

### Changing the timing and amount of charitable contributions

Charitable bequests are deducted from the gross estate, and economic analysis shows that this estate tax deduction provides an incentive to make charitable bequests.<sup>39</sup> When estate tax rates are reduced, there are two competing effects. As estate tax rates fall, the tax benefit of making a charitable bequest is reduced. This is known as the price effect. However, a lower estate tax rate generally increases net wealth, and charitable giving is positively correlated with wealth. This is known as the wealth effect. Empirical studies have generally found that the price effect dominates the wealth effect so that, as estate tax rates fall, fewer charitable bequests are made.<sup>40</sup> Furthermore, there is evidence that total lifetime charitable giving (the sum of lifetime charitable gifts and charitable bequests at death) is reduced as the estate tax rate falls.<sup>41</sup> Although charitable contributions, which decline as tax rates decline, are deductible from the gross estate and are not subject to gift tax, estate and gift tax collections generally fall as tax rates decline. On the other hand, a reduction in charitable giving reduces the size of the pool of assets from which charities may derive income, thus reducing the income available to nontaxable charitable entities. Dividend and interest income that would accrue to charities under a tax regime with higher estate tax rates accrues instead to the taxable sector of the economy and is subject to the income tax.

Revenue estimates produced by the Joint Committee staff account for changes in the size and timing of charitable bequests, the amount of charitable deductions claimed on income and estate tax returns, and the amount of dividend and interest income accruable to the taxable economy. For proposals that reduce estate taxes, the net effect of these considerations is generally an increase in Federal income tax revenues, partially offsetting the reduction in Federal estate taxes. That is, the reduction in Federal estate tax revenues from the reduction in estate tax rates is partially offset by an increase in Federal income tax receipts attributable to a decrease in the amount of charitable deductions claimed on income tax returns and an increase in taxable interest and dividends resulting from a decrease in lifetime charitable gifts.

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<sup>39</sup> See Michael J. Boskin, 1976. "Estate Taxation and Charitable Bequests," *Journal of Public Economics*, vol. 5, Jan-Feb 1976, pp. 27-56. Also, Charles T. Clotfelter, *Federal Tax Policy and Charitable Giving*, University of Chicago Press, 1985. See also David Joulfaian, "Estate Taxes and Charitable Bequests: Evidence from Two Tax Regimes," *U.S. Department of the Treasury*, OTA Paper 92, March 2005, and also Jon Bakija, William Gale, and Joel Slemrod, "Charitable Bequests and Taxes on Inheritances and Estates: Aggregate Evidence from across States and Time," *American Economic Review*, vol. 93, no. 2, May 2003, pp. 366-370.

<sup>40</sup> See David Joulfaian, "Charitable Bequests and Estate Taxes," *National Tax Journal*, vol. 44, June 1991, pp. 169-180. Also, David Joulfaian, "Estate Taxes and Charitable Bequests by the Wealthy," *National Tax Journal*, vol. 53, September 2000, pp. 743-764.

<sup>41</sup> See David Joulfaian, "Charitable Giving in Life and at Death," in Gale, Hines, and Slemrod (eds.), *Rethinking Estate and Gift Taxation*, Brookings Institution, 2001. See also Auten and Joulfaian, "Charitable Contributions and Intergenerational Transfers," *Journal of Public Economics*, vol. 59, 1996, pp. 55-68. And Pamela Greene and Robert McClelland, "The Effects of Federal Estate Tax Policy on Charitable Contributions," *Congressional Budget Office*, Technical Paper 2001-2, 2001.

### Changing capital gains realizations

Capital gains realizations are affected by the capital gains tax rate, the estate tax rate, and the amount of step-up in basis provided to assets transferred from a decedent.<sup>42</sup> Estate tax law generally provides a step-up in basis for assets acquired from a decedent.<sup>43</sup>

There are several interactions between the estate and gift taxes and the individual income tax that are influenced by the capital gains tax rates and the amount of step-up in basis afforded assets in an estate. Under present law, holding gain assets until death shields them from income taxation as a result of the step-up in basis. However, these gain assets do not escape taxation entirely as they are taxed as part of the decedent's estate. The estate tax functions as a toll that must be paid to shield capital gains from income taxation. As this toll falls (*i.e.*, the estate tax rate is reduced and/or the estate tax exemption amount increases), it is relatively more attractive to pay the estate tax to avoid the income tax on capital gains realizations. Similarly, as capital gains taxes rise (fall), paying the estate tax toll becomes more (less) attractive because the step-up in gains at death is more (less) valuable. High estate tax rates make the transmission of wealth to heirs less efficient and so encourage the realization of capital gains.

A taxpayer subject to potentially high marginal estate tax rates may weigh several tax-related considerations when considering the disposition of a capital asset before death. For wealthy taxpayers, the effective capital gains tax rate is not the statutory rate but instead something lower because for this taxpayer taxes paid on capital gains before death reduce the amount of wealth subject to estate and gift taxation. For example, consider a taxpayer whose estate will be subject to the highest marginal estate tax rate of 55 percent in 2013.<sup>44</sup> If, in 2012, the taxpayer sells the capital asset and realizes a \$100 gain, he pays \$15 of capital gains tax. However, the payment of the tax reduces the taxpayer's estate by \$15, reducing the taxes that will be levied against his estate by \$8.25. Thus, ignoring the time value of money, the effective income tax on capital gains for this taxpayer is 6.75 percent. There are at least three tax-related considerations for certain wealthy taxpayers making decisions about whether to realize capital gains: 1) the amount of step-up in basis available at death; 2) estate tax rates; and 3) the *de facto* reduction in income tax rates on capital gains realized before death. Depending upon the preferences of any specific taxpayer, the availability of a step-up in basis at death could encourage the retention of gain assets until death (the so-called "lock-in effect") while the other two factors, high estate tax marginal rates and the *de facto* reduction in effective capital gains tax

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<sup>42</sup> See Gerald Auten and David Joulfaian, "Bequest Taxes and Capital Gains Realizations," *Journal of Public Economics*, vol. 81, no. 2, August 2001, pp. 213-229. Also, Athiphat Muthitacharoen, "The Impact of the Estate Tax on Capital Gains Realizations: Evidence from the Taxpayer Relief Act of 1997," *Congressional Budget Office*, Working Paper 2010-08, 2010. Also, see David Joulfaian, "Taxing Wealth Transfers and Its Behavioral Consequences," *National Tax Journal*, vol. 53, no. 4, December 2000, pp. 933-957.

<sup>43</sup> As previously note, decedents dying in 2010 could have opted to be treated under EGTRRA estate tax law, which provides for a modified carryover basis.

<sup>44</sup> For purposes of this example, the five percent surtax on taxable estates of between \$10 million and \$17.184 million is disregarded.

rates could encourage the disposition of gain assets before death. A taxpayer whose estate will be subject to high estate tax rates at death has an incentive to realize more capital gains relative to a taxpayer whose estate will be more lightly taxed at death, if both taxpayers face similar capital gains tax rates.

Estimation of the capital gains effect of a proposal to modify the estate tax depends significantly on the treatment of the basis of the asset and the applicable estate and capital gains tax rates. Proposals that maintain a step-up in basis but reduce estate tax rates will result in fewer capital gains realizations because they diminish the importance of factors two and three (those that encourage the disposition of gain assets before death) in the preceding paragraph. Likewise, economic theory suggests that, if estate tax rates remain unchanged but step-up in basis is eliminated, capital gains realizations increase. In the event that the ability to step up the basis of assets held at death is reduced along with a reduction in estate tax rates, the net effect on capital gains realizations is ambiguous and depends upon the various circumstances of individual taxpayers.

For heirs, the treatment of the basis of inherited assets has the opposite effect compared to the effect on decedents. While a step-up in basis on assets held at death encourages the locking-in of gains during the decedent's life, the heirs are generally free to dispose of those gain assets as they wish because no capital gains tax is due on any appreciation that occurred prior to that transfer. Likewise, reducing or eliminating the step-up in basis on assets held at death encourages capital gains realizations during the decedent's life but produces a lock-in effect for those assets in the hands of the heirs.

For proposals that repeal, or substantially reduce, the estate tax while reducing or eliminating the step-up in basis on assets held at death, the Joint Committee staff models both the deferral of capital gains realizations that results from the repeal of the estate tax and the switch to carryover basis and the taxation of capital gains on inherited assets, some of which may now be subject to capital gains taxation as a result of carryover basis. For proposals that retain some step-up in basis,<sup>45</sup> the Joint Committee staff considers the amount of additional basis that might be allocated to estates and how heirs might dispose of assets that have increased in value. The results of the Joint Committee staff's models indicate that the increased lock-in effect on capital gains realizations from the elimination of the estate tax tends to dominate the increased capital gains realization by heirs as a result of elimination of basis step-up.

#### Shifting deductions between the estate and income tax returns

Some expenses such as attorney's fees, medical expenses, and some executor's commissions are allowable as deductions on either the estate tax return or the final income tax return of the decedent. These deductions are usually taken on the decedent's estate tax return because a greater tax benefit is derived from the deduction at the generally higher marginal estate tax rates rather than the generally lower marginal income tax rates. Proposals that reduce the applicable marginal estate tax rates below the applicable marginal income tax rates or that

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<sup>45</sup> For example, the modified carryover basis regime in place for 2010 electing estates.

increase the estate tax exemption amount may result in shifting these deductions from the estate tax return to the final income tax return of the decedent. For example, consider a proposal that increases the estate tax exemption amount. An increase in the estate tax exemption amount automatically removes some estates from the estate tax base (alternatively, one could say that the marginal estate tax rate on these estates is reduced to zero). Thus, deductions migrate from the estate tax return to the decedent's final income tax return.

### Opportunities for tax planning

The wealth transfer tax system serves a role in preserving the income tax base by making it costly to transfer assets among persons to obtain more favorable income tax treatment. In the absence of a transfer tax system, it would be easier to use the progressive rate structure of the income tax to reduce income tax liabilities with strategic transfers of assets to persons in lower marginal tax brackets. For example, in the absence of a gift tax, assets could be shuffled among family members to reduce income taxes on investment income.<sup>46</sup> Without a gift tax, there would generally be no limit on the amounts that could be transferred among adult family members to take advantage of the increasing graduated marginal tax rate structure of the income tax. For proposals that eliminate or substantially reduce the gift tax, the Joint Committee staff assumes that high-income persons who have substantial amounts of interest and dividend income will seek to shift some of these assets to lower income family members to obtain the benefit of the lower income tax brackets.

Additionally, the parameters of the estate and gift taxes may affect the aggressiveness with which various planning techniques, such as marketability and minority discounts, are used by taxpayers to reduce the estate or gift tax base. Often, these discounts result in substantial reductions in the estate or gift tax base, as shown in Table 5. In computing the fair market value of assets transferred, minority discounts lower the value of a minority interest in a business to compensate for the lack of control as the holder of a minority interest cannot make decisions regarding the operation of the entity nor the timing and amount of income distributions from the entity to its owners. Marketability discounts compensate for limitations upon free exit inherent in interests for which no public market exists. As these discounts are dependent upon the actual facts and circumstances of the taxpayer, many analysts believe that they may be inappropriately applied in many cases.<sup>47</sup> With relatively high marginal estate tax rates, there is a substantial

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<sup>46</sup> Code section 1(g), sometimes known as the "kiddie tax," prevents the shifting of unearned income to children who are under 18 years of age or who are under 19 years of age (24 years old if a student) and are still dependents of their parents.

<sup>47</sup> Commentators have referred to this discounting as the "disappearing wealth" phenomenon: Wealth disappears from the transfer tax base even though no (or little) actual economic value is lost. See Mary Louise Fellows and William H. Painter, "Valuing Close Corporations for Federal Wealth Transfer Taxes: A Statutory Solution to the Disappearing Wealth Syndrome," *Stanford Law Review*, vol. 30, 1978, p. 895; James Repetti, "Minority Discounts: The Alchemy in Estate and Gift Taxation," *Tax Law Review*, vol. 50, 1995; Laura E. Cunningham, "Remember the Alamo: The IRS Needs Ammunition in its Fight Against the FLP," *Tax Notes*, March 13, 2000, p. 1461. *Church v. United States*, 85 A.F.T.R. 2d (RIA) 804 (W.D. Tex. 2000), aff'd without published opinion, 268 F.3d 1063 (5th Cir. 2001), provides a simple example of the creation of discounts shortly before death. Mrs. Church, who was the mother of the plaintiff and was suffering from a terminal illness, and her two children

benefit to the aggressive application of valuation discounts that, as long as the taxpayer acts in good faith and has a reasonable basis for the discount, results in few consequences.<sup>48</sup>

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together formed a limited partnership. In exchange for limited partnership interests, Mrs. Church contributed to the partnership her interest in a Texas ranch (valued at \$380,038) together with \$1,087,710 in publicly traded securities, while her two children contributed their undivided interests in the ranch. A corporation owned equally by the two children was the general partner of the partnership. Two days after the formation of the partnership, Mrs. Church died. The District Court found that the date-of-death value of Mrs. Church's limited partnership interest was \$617,591, despite the fact that Mrs. Church transferred assets to the partnership worth \$1,467,748 just two days earlier. The court upheld a 58-percent discount based upon the noncontrolling and illiquid nature of Mrs. Church's limited partnership interest.

<sup>48</sup> See Joint Committee on Taxation, *Options to Improve Tax Compliance and Reform Tax Expenditures* (JCS-02-05), January 29, 2005, pages 396-404, for a more thorough description of the application of marketability and minority discounts.

**Table 5.—Valuation Discounts by Size of Estate or Current Year Gifts**  
**Valuation Discounts by Size of Estate**  
**(2008 Estate Tax Return Filers; Dollar Amounts in Millions)**

| Size of Estate                                  | Total Estate of Filers | Returns Claiming Discount | Total Discount | Total Estate of Those Claiming a Discount | Discount as Percent of Total Estate of Filers | Discount as Percent of Total Estate of Those Claiming a Discount |
|-------------------------------------------------|------------------------|---------------------------|----------------|-------------------------------------------|-----------------------------------------------|------------------------------------------------------------------|
| Less than \$2 million                           | \$2,449                | 157                       | \$25           | \$245                                     | 1%                                            | 10%                                                              |
| At least \$2 million but less than \$5 million  | \$80,462               | 3,803                     | \$1,125        | \$12,426                                  | 1%                                            | 9%                                                               |
| At least \$5 million but less than \$10 million | \$41,358               | 1,711                     | \$1,284        | \$11,678                                  | 3%                                            | 11%                                                              |
| \$10 million or more                            | \$118,825              | 1,469                     | \$11,770       | \$64,601                                  | 10%                                           | 18%                                                              |
| All Estates                                     | \$243,094              | 7,140                     | \$14,205       | \$88,950                                  | 6%                                            | 16%                                                              |

**Valuation Discounts by Size of Gift**  
**(2008 Gift Tax Return Filers; Dollar Amounts in Millions)**

| Size of Current Year Gifts                      | Total Current Year Gift Value of Filers | Returns Claiming Discount | Total Discount | Total Current Year Gift Value of Those Claiming a Discount | Discount as Percent of Total Current Year Gift Value of Filers | Discount as Percent of Total Current Year Gift Value of Those Claiming a Discount |
|-------------------------------------------------|-----------------------------------------|---------------------------|----------------|------------------------------------------------------------|----------------------------------------------------------------|-----------------------------------------------------------------------------------|
| Less than \$100,000                             | \$6,296                                 | 10,914                    | \$124          | \$460                                                      | 2%                                                             | 27%                                                                               |
| At least \$100,000 but less than \$500,000      | \$15,339                                | 9,786                     | \$695          | \$2,538                                                    | 5%                                                             | 27%                                                                               |
| At least \$500,000 but less than \$1 million    | \$8,718                                 | 3,680                     | \$760          | \$2,613                                                    | 9%                                                             | 29%                                                                               |
| At least \$1 million but less than \$2 million  | \$6,252                                 | 2,297                     | \$1,079        | \$3,153                                                    | 17%                                                            | 34%                                                                               |
| At least \$2 million but less than \$5 million  | \$2,745                                 | 270                       | \$221          | \$783                                                      | 8%                                                             | 28%                                                                               |
| At least \$5 million but less than \$10 million | \$1,530                                 | 60                        | \$97           | \$395                                                      | 6%                                                             | 25%                                                                               |
| \$10 million or more                            | \$7,796                                 | 63                        | \$452          | \$1,906                                                    | 6%                                                             | 24%                                                                               |
| All Gifts                                       | \$48,676                                | 27,070                    | \$3,429        | \$11,848                                                   | 7%                                                             | 29%                                                                               |

Various transfers of assets into trusts before death can be used to reduce estate tax liability at death. For example, a taxpayer may give assets to a trust structured so that it is separate from the grantor for transfer tax purposes, but treated as owned by the grantor for income tax purposes. Such trusts are sometimes referred to as intentionally defective grantor trusts (“IDGTs”), because the taxpayer intentionally includes in the trust agreement a right that causes the trust to be treated as a grantor trust under sections 671 through 679 of the Internal Revenue Code (the “Code”).<sup>49</sup> The taxpayer essentially “freezes” the value of certain assets by transferring them to an IDGT, sometimes by means of a taxable gift during his or her lifetime. The transfer tax value is measured at the time of the gift, and any subsequent appreciation

<sup>49</sup> See Daniel L. Ricks, “I Dig It, But Congress Shouldn’t Let Me: Closing the IDGT Loophole,” *ACTEC Law Journal*, vol. 36, Winter 2010, pp. 641-644.

accrues to the trust (which is not a part of the taxpayer's estate). As the owner of the trust for income tax purposes, the grantor satisfies the income tax liability of the trust out of the grantor's separate assets, thereby managing and preserving trust assets for the beneficiary and reducing the grantor's taxable estate. The additional payments of income tax are not treated as additional taxable gifts for transfer tax purposes.

Taxpayers may also reduce tax liability through grantor retained annuity trusts ("GRATs").<sup>50</sup> In a typical GRAT transaction, a taxpayer (the grantor of the trust) funds a trust with a completed gift under which he or she retains an annuity interest in the trust. For gift tax purposes, the value of the gift is the value of the assets transferred to the trust minus the value of the retained annuity interest at prevailing interest rates. In practice, the value of this taxable gift is often quite small relative to the value of assets transferred to the trust (or is zero). When the grantor's retained annuity interest expires, any remaining trust assets are transferred to one or more beneficiaries. If the trust property has increased at a faster rate than the interest rate used to value the retained annuity interest then the excess appreciation passes to the trust beneficiaries without further transfer tax.

Another planning technique is to use lapsing trust powers to leverage the gift tax annual exclusion amount. Trusts that use this method are often called Crummey trusts.<sup>51</sup> To qualify for the gift tax annual exclusion, the transfer to the beneficiary must be a transfer of a present (not a future) interest. Accordingly, if the trust beneficiaries have no right to present enjoyment of the transferred property then the annual exclusion does not apply. However, a temporary right of withdrawal of trust property on the part of a beneficiary may create a present interest, thereby qualifying such a gift for the annual exclusion. The holder of a lapsing withdrawal right need not even be a vested beneficiary of the trust, which creates the possibility of using multiple annual exclusions for what is ultimately a gift to a single beneficiary.

Other forms of avoidance may seek to exploit the step-up in basis for gains at death. For example, in the absence of a gift tax, an individual may transfer appreciated assets to elderly relatives not subject to the estate tax to obtain the step-up in basis upon that person's death. Also, some other income-tax-advantaged assets may become more advantageous in the absence of a transfer tax system.<sup>52</sup>

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<sup>50</sup> See sec. 2702.

<sup>51</sup> See *Crummey v. Commissioner*, 397 F.2d 82 (9<sup>th</sup> Cir. 1968); Rev. Rul. 73-405, 1973-2 C.B.

<sup>52</sup> For example, life insurance held by the person whose life is insured.

## **B. The Estate and Gift Tax Microsimulation Model**

### **Data**

To calculate estate tax liability in any given year the Joint Committee staff needs to determine the number of estates that must file an estate tax return and the value and composition of those estates. An estate tax return is required when the aggregate of the total gross estate for tax purposes and adjusted taxable gifts is greater than the exemption amount. As previously discussed, under EGTRRA, the estate tax exemption amount rose incrementally from \$675,000 in 2001 to \$3.5 million in 2009. The Tax Relief Act provides for a \$5 million exemption amount in 2010, 2011, and 2012.<sup>53</sup> Under present law, the estate tax exemption amount falls to \$1 million after 2012.

The Joint Committee staff begins with a sample of estate tax returns filed in 2008. This 2008 Estate Tax file has been edited by the Statistics of Income division of the Internal Revenue Service (“SOI”). It contains 11,726 records representing the estates of 38,373 decedents. The sample is stratified by three variables: year of death, age at death, and size of total gross estate plus adjusted taxable gifts. Sampling rates range from one percent to 100 percent with approximately half of the strata selected at the 100 percent rate. The estate tax files prepared by SOI contain a wealth of information on the composition of assets held by the decedent at death and the disposition of those assets. For example, the data show the value of the decedent’s publicly traded stock, closely held stock, farming assets, real estate, and other holdings as well as the deductions claimed for assets transferred to a surviving spouse or to charity and even the discounts claimed on various classes of assets.

The 2008 Estate Tax file generally represents decedents who died in 2006 and 2007, when the exemption amount was \$2 million. Therefore, to model present law after 2012, the Joint Committee staff needs information on estates whose sum of total gross estate plus taxable gifts is between \$1 million and \$2 million. If one assumes that these \$1 million to \$2 million estates are the same fraction of the filing population in 2008 as they were for 2001 decedents,<sup>54</sup> then these returns comprise approximately 65 percent of the filing population with a total gross estate plus taxable gifts of at least \$1 million. Furthermore, beginning with the 2005 Estate Tax file, the SOI provided additional information concerning valuation discounts. Therefore, the 2005 Estate Tax file is a source of information both on valuation discounts and on estates with total gross estates plus taxable gifts of between \$1 million and \$2 million. The 2005 Estate Tax file contains 796 observations (representing 5,899 estates) of decedents dying in either 2002 or 2003 (when the estate tax exemption amount was \$1 million) with a total gross estate plus taxable gifts of between \$1 million and \$2 million. After examining these records along several

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<sup>53</sup> This \$5 million amount is indexed for inflation after 2011 and is currently \$5.12 million.

<sup>54</sup> In addition to the estate tax files that represent returns filed in a given year, every three years the SOI produces a “year of death” file which represents the estates of decedents dying in a given year. The Joint Committee staff has this file for 2001, 2004, and 2007. The 2001 file is the last file on which estates of \$1 million are represented.

dimensions, the Joint Committee staff determined that they differ in no significant way from similar estate tax returns of 2001 decedents in the 2001 “year of death” estate tax file.<sup>55</sup> Therefore, the Joint Committee staff adds these \$1 million to \$2 million estate tax returns from 2002 and 2003 decedents who filed estate tax returns in 2005 to the 2008 Estate Tax file and adjusts the weights to produce a file representative of all decedents with estates worth at least \$1 million. In particular, the additional 2002 and 2003 returns are reweighted so that estates with an aggregate of total gross estate and taxable gifts of between \$1 million and \$2 million are 65 percent of the sample population.

Tables 6 through 9, below, show the total gross estate for tax purposes and the number of returns filed by total gross estate and marital status for several relevant Estate Tax populations. Table 10 shows this same information for the final synthetic cohort created by blending the 2008 and 2005 Estate Tax files that is used in the Joint Committee’s estate tax model.

**Table 6.—Number of Estate Tax Returns and Total Gross Estate for Tax Purposes, 2001 Decedents With a Total Gross Estate Plus Taxable Gifts of at Least \$1 Million**

| All Estate Tax Returns                                  |                        |                                              | Married Estate Tax Returns |                                              | Unmarried Estate Tax Returns |                                              |
|---------------------------------------------------------|------------------------|----------------------------------------------|----------------------------|----------------------------------------------|------------------------------|----------------------------------------------|
| Total Gross Estate (TGE) for Tax Purposes (\$ millions) | Returns Filed (number) | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)     | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)       | Aggregate TGE for Tax Purposes (\$ millions) |
| Less than 1                                             | 1,280                  | 1,023                                        | 226                        | 177                                          | 1,054                        | 846                                          |
| 1 to 1.5                                                | 29,247                 | 35,276                                       | 12,873                     | 15,517                                       | 16,374                       | 19,760                                       |
| 1.5 to 2                                                | 12,746                 | 21,901                                       | 6,508                      | 11,203                                       | 6,238                        | 10,698                                       |
| 2 to 3.5                                                | 12,879                 | 33,129                                       | 6,608                      | 17,066                                       | 6,271                        | 16,063                                       |
| 3.5 to 5                                                | 4,037                  | 16,645                                       | 2,048                      | 8,455                                        | 1,989                        | 8,190                                        |
| 5 to 10                                                 | 3,656                  | 24,962                                       | 1,861                      | 12,718                                       | 1,795                        | 12,243                                       |
| 10 to 20                                                | 1,302                  | 17,729                                       | 694                        | 9,455                                        | 608                          | 8,274                                        |
| More than 20                                            | 695                    | 42,493                                       | 393                        | 27,308                                       | 302                          | 15,185                                       |
| All                                                     | 65,842                 | 193,158                                      | 31,210                     | 101,900                                      | 34,632                       | 91,259                                       |

<sup>55</sup> For example, some of these dimensions are marital status, holding assets in a family limited partnership, claiming a valuation discount, claiming a special-use valuation, and estate tax liability.

**Table 7.—Number of Estate Tax Returns and Total Gross Estate for Tax Purposes,  
2008 Filers**

| All Estate Tax Returns                                  |                        |                                              | Married Estate Tax Returns |                                              | Unmarried Estate Tax Returns |                                              |
|---------------------------------------------------------|------------------------|----------------------------------------------|----------------------------|----------------------------------------------|------------------------------|----------------------------------------------|
| Total Gross Estate (TGE) for Tax Purposes (\$ millions) | Returns Filed (number) | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)     | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)       | Aggregate TGE for Tax Purposes (\$ millions) |
| Less than 1                                             | 196                    | 166                                          | 43                         | 36                                           | 153                          | 129                                          |
| 1 to 1.5                                                | 539                    | 683                                          | 180                        | 235                                          | 359                          | 448                                          |
| 1.5 to 2                                                | 953                    | 1,693                                        | 338                        | 603                                          | 616                          | 1,090                                        |
| 2 to 3.5                                                | 20,954                 | 54,113                                       | 9,843                      | 25,686                                       | 11,111                       | 28,427                                       |
| 3.5 to 5                                                | 6,562                  | 27,025                                       | 3,440                      | 14,191                                       | 3,122                        | 12,834                                       |
| 5 to 10                                                 | 5,895                  | 39,936                                       | 3,067                      | 20,755                                       | 2,828                        | 19,180                                       |
| 10 to 20                                                | 2,096                  | 28,643                                       | 1,078                      | 14,763                                       | 1,018                        | 13,880                                       |
| More than 20                                            | 1,178                  | 76,613                                       | 634                        | 35,906                                       | 543                          | 40,708                                       |
| All                                                     | 38,373                 | 228,872                                      | 18,624                     | 112,176                                      | 19,750                       | 116,697                                      |

**Table 8.—Number of Estate Tax Returns and Total Gross Estate for Tax Purposes,  
2005 Filers**

| All Estate Tax Returns                                  |                        |                                              | Married Estate Tax Returns |                                              | Unmarried Estate Tax Returns |                                              |
|---------------------------------------------------------|------------------------|----------------------------------------------|----------------------------|----------------------------------------------|------------------------------|----------------------------------------------|
| Total Gross Estate (TGE) for Tax Purposes (\$ millions) | Returns Filed (number) | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)     | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)       | Aggregate TGE for Tax Purposes (\$ millions) |
| Less than 1                                             | 796                    | 660                                          | 257                        | 219                                          | 539                          | 441                                          |
| 1 to 1.5                                                | 4,795                  | 5,958                                        | 1,957                      | 2,481                                        | 2,837                        | 3,476                                        |
| 1.5 to 2                                                | 13,954                 | 24,046                                       | 5,931                      | 10,294                                       | 8,023                        | 13,751                                       |
| 2 to 3.5                                                | 14,842                 | 38,162                                       | 7,248                      | 18,624                                       | 7,594                        | 19,538                                       |
| 3.5 to 5                                                | 4,445                  | 18,386                                       | 2,258                      | 9,357                                        | 2,187                        | 9,030                                        |
| 5 to 10                                                 | 4,122                  | 28,001                                       | 2,053                      | 13,898                                       | 2,069                        | 14,103                                       |
| 10 to 20                                                | 1,358                  | 18,650                                       | 691                        | 9,578                                        | 667                          | 9,072                                        |
| More than 20                                            | 760                    | 50,833                                       | 423                        | 25,858                                       | 336                          | 24,975                                       |
| All                                                     | 45,070                 | 184,696                                      | 20,818                     | 90,310                                       | 24,253                       | 94,387                                       |

**Table 9.--Number of Estate Tax Returns and Total Gross Estate for Tax Purposes,  
2005 Filers of 2002 & 2003 Decedents with Total Gross Estate Plus Adjusted  
Taxable Gifts Between \$1 million and \$2 million**

| All Estate Tax Returns                                  |                        |                                              | Married Estate Tax Returns |                                              | Unmarried Estate Tax Returns |                                              |
|---------------------------------------------------------|------------------------|----------------------------------------------|----------------------------|----------------------------------------------|------------------------------|----------------------------------------------|
| Total Gross Estate (TGE) for Tax Purposes (\$ millions) | Returns Filed (number) | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)     | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)       | Aggregate TGE for Tax Purposes (\$ millions) |
| Less than 1                                             | 90                     | 80                                           | 38                         | 37                                           | 52                           | 43                                           |
| 1 to 1.5                                                | 3,997                  | 4,929                                        | 1,745                      | 2,206                                        | 2,252                        | 2,723                                        |
| 1.5 to 2                                                | 1,812                  | 3,125                                        | 934                        | 1,625                                        | 878                          | 1,500                                        |
| 2 to 3.5                                                | -                      | -                                            | -                          | -                                            | -                            | -                                            |
| 3.5 to 5                                                | -                      | -                                            | -                          | -                                            | -                            | -                                            |
| 5 to 10                                                 | -                      | -                                            | -                          | -                                            | -                            | -                                            |
| 10 to 20                                                | -                      | -                                            | -                          | -                                            | -                            | -                                            |
| More than 20                                            | -                      | -                                            | -                          | -                                            | -                            | -                                            |
| All                                                     | 5,899                  | 8,134                                        | 2,717                      | 3,867                                        | 3,182                        | 4,266                                        |

**Table 10.--Number of Estate Tax Returns and Total Gross Estate  
for Tax Purposes, Synthetic Cohort**

| All Estate Tax Returns                                  |                        |                                              | Married Estate Tax Returns |                                              | Unmarried Estate Tax Returns |                                              |
|---------------------------------------------------------|------------------------|----------------------------------------------|----------------------------|----------------------------------------------|------------------------------|----------------------------------------------|
| Total Gross Estate (TGE) for Tax Purposes (\$ millions) | Returns Filed (number) | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)     | Aggregate TGE for Tax Purposes (\$ millions) | Returns Filed (number)       | Aggregate TGE for Tax Purposes (\$ millions) |
| Less than 1                                             | 1,161                  | 1,026                                        | 446                        | 431                                          | 715                          | 596                                          |
| 1 to 1.5                                                | 47,561                 | 58,670                                       | 20,711                     | 26,183                                       | 26,850                       | 32,487                                       |
| 1.5 to 2                                                | 22,273                 | 38,456                                       | 11,327                     | 19,724                                       | 10,946                       | 18,733                                       |
| 2 to 3.5                                                | 20,954                 | 54,113                                       | 9,843                      | 25,686                                       | 11,111                       | 28,427                                       |
| 3.5 to 5                                                | 6,562                  | 27,025                                       | 3,440                      | 14,191                                       | 3,122                        | 12,834                                       |
| 5 to 10                                                 | 5,895                  | 39,936                                       | 3,067                      | 20,755                                       | 2,828                        | 19,180                                       |
| 10 to 20                                                | 2,096                  | 28,643                                       | 1,078                      | 14,763                                       | 1,018                        | 13,880                                       |
| More than 20                                            | 1,178                  | 76,613                                       | 634                        | 35,906                                       | 543                          | 40,708                                       |
| All                                                     | 107,681                | 324,483                                      | 50,548                     | 157,638                                      | 57,133                       | 166,845                                      |

After constructing the synthetic cohort to adequately represent the filing population, the base data in the microsimulation model is adjusted in three ways. The Joint Committee staff makes certain adjustments to the magnitude of charitable bequests. The Joint Committee staff also makes adjustments for both the credit or deduction for State death taxes and the deduction for certain family-owned business interests.

## **Changes in charitable bequests**

Under present law, in 2013, estate and gift tax rates are higher and the applicable exemption amounts lower than was the case for much of the data comprising the Joint Committee staff's base data (the synthetic cohort containing data from the 2005 and 2008 Estate Tax file). Because charitable bequests are sensitive to these tax parameters, the Joint Committee staff adjusts the levels of charitable bequests in the base data to arrive at levels more appropriate for the law as scheduled to be in effect in 2013 and beyond.

As discussed in the previous subsection, the deduction from the estate tax of charitable bequests provides an incentive to make such bequests. Generally, as estate tax rates fall, fewer charitable bequests are made.<sup>56</sup> To calculate the expected change in each taxpayer's charitable bequests, the Joint Committee staff applies a price elasticity of -1.6 and a wealth elasticity of 1.2 in determining each taxpayer's response to changes in the estate tax.<sup>57</sup>

In performing these calculations, the Joint Committee staff first determines the decedent's initial wealth, which is calculated as the post-tax wealth of the decedent if he or she made no charitable bequests. The initial price of a charitable bequest is one minus the estate tax rate at the decedent's initial wealth.<sup>58</sup> The Joint Committee staff then determines the decedent's initial wealth under the baseline and the price of a charitable bequest under the baseline. The wealth and price elasticities are applied to the changes in wealth and the price of charitable bequests, respectively. For this purpose of determining wealth, it is assumed that a married decedent will bequeath all of his or her assets to a surviving spouse. Because of this assumption and the unlimited marital deduction, changes in estate tax rates and exemption amounts do not affect the charitable bequests of married decedents. This same method is used by the model to estimate and account for changes in charitable bequests resulting from proposed estate tax policy changes.

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<sup>56</sup> See footnote 40.

<sup>57</sup> An elasticity is a measure of the sensitivity of some behavior to changes in an economic variable. In this case, the elasticities measure the sensitivity of charitable bequests with respect to the estate tax price of a charitable bequest (the estate tax price of a charitable bequest is one minus the effective marginal estate tax rate) and the decedent's wealth. The price elasticity of -1.6 implies that a 10-percent increase in the price of a charitable bequest will result in a 16-percent decrease in the amount donated to charity at death. Similarly, the wealth elasticity of 1.2 implies that a 10-percent increase in a decedent's wealth will result in a 12-percent increase in the amount donated to charity at death. For comparison, Joulfaian finds a price elasticity of between -1.7 and -2.5 and a wealth elasticity of between 1.2 and 1.6. See David Joulfaian, "Taxing Wealth Transfers and Its Behavioral Consequences," *National Tax Journal*, vol. 53, no. 4, Part 1, December 2000, pp. 933-957.

<sup>58</sup> If the decedent makes a large enough charitable bequest, then he or she may increase the tax price of making a charitable bequest to more than one minus the estate tax rate at the decedent's initial wealth. However, the estate tax rate schedule is flat above relatively low values and therefore this is unlikely to have much effect. This is especially true for decedents after 2005 whose estates have been taxed at a single rate above the exemption amount. Also, if the decedent makes a bequest larger than that required to reduce estate tax liability to zero, the Joint Committee staff assumes that the amount of the bequest does not vary in response to changes in the estate tax.

## **State death taxes**

As previously noted, EGTRRA phased out the credit for State death taxes paid and replaced it after 2004 with a deduction for State death taxes paid. The credit was determined according to a rate schedule in the Code<sup>59</sup> with a maximum credit rate of 16 percent. As the credit for State death taxes effectively created a transfer from the Federal to the State governments, before EGTRRA all States assessed an estate tax at least as large as the State tax credit amount. Therefore, for years after 2012 when the State death tax credit is scheduled to be in effect, the Joint Committee staff assumes that every decedent claims the credit amount according to the rate schedule set forth in the Code.

For years when the State death tax deduction is scheduled to be in effect and for proposals which would replace the State death tax credit with a State death tax deduction, the Joint Committee staff uses the actual reported deduction for those observations in the base data from years in which there is a State death tax deduction. For those observations in the base data from decedents before 2005, when there was a credit for State death taxes paid, the Joint Committee staff estimates the State death tax deduction by assuming that the deduction is equal to the credit they would be entitled to claim according to the rate schedule in the Code.

## **Qualified family-owned business interests**

Another aspect of the law affected by EGTRRA is the deduction for qualified family-owned business interests (“QFOBI”). The QFOBI deduction was repealed after 2003 but will apply again after 2012 when the exemption amount will be \$1 million.<sup>60</sup> Estates are eligible for the QFOBI deduction if farm and business assets account for at least one-half the value of the total gross estate. However, the QFOBI provision imposes certain other conditions on the decedent and the heir, particularly the requirement that the heir continue in the business for a period of 10 years after the decedent’s death. These conditions tend to reduce the number of estates claiming benefits under the provision. Therefore, when modeling the provision after 2012 the Joint Committee staff assumes the percentage of eligible estates claiming benefits under the provision to be the same percentage as in 2001. The data show that the estates of married decedents do not claim the deduction when they are apparently qualified to do so, perhaps because of the unlimited marital deduction.

All other credits and adjustments are unchanged from the amount reported on the tax return filed by the executor of the decedent’s estate.<sup>61</sup>

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<sup>59</sup> See sec. 2011(b)(1).

<sup>60</sup> See sec. 2057. The QFOBI deduction has no value when the estate tax exemption amount is at least \$1.3 million. \$1.3 million is the sum of the \$625,000 estate tax exemption amount available for those claiming the deduction plus maximum deduction amount of \$675,000.

<sup>61</sup> For example, the credit for foreign death taxes, the credit for tax on prior transfers, etc.

The base data are then reweighted so that the Joint Committee staff’s model of present law reproduces the CBO’s baseline estate tax revenue projections in each model year.<sup>62</sup> The reweighting takes into consideration estimates of nominal GNP growth and population growth as well as trends on the distribution of wealth. The model applies present law and proposed law in each calendar year of the 10-year budget window to produce estimates of the changes in estate and gift taxes.<sup>63</sup> The baseline is shown in Table 11.<sup>64</sup>

**Table 11.—Estate Tax Returns and Transfer Tax Liability Under Present Law, CY 2012-21**

|                                          | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   | 2020   | 2021   |
|------------------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Number of Estate Tax Returns (thousands) | 8.6    | 107.5  | 113.7  | 122.2  | 131.4  | 141.2  | 151.7  | 162.2  | 173.0  | 185.1  |
| Number of Taxable Returns (thousands)    | 3.6    | 55.2   | 58.4   | 62.7   | 67.5   | 72.5   | 77.8   | 83.2   | 88.8   | 95.0   |
| Estate Tax Liability (\$ millions)       | 10,031 | 37,728 | 39,908 | 42,900 | 46,136 | 49,565 | 53,237 | 56,932 | 60,709 | 64,971 |
| Gift Tax Liability (\$ millions)         | 5,027  | 3,151  | 4,428  | 5,269  | 6,181  | 6,511  | 6,835  | 7,147  | 7,467  | 7,794  |

<sup>62</sup> The CBO provides only fiscal year estimates of estate and gift tax receipts. The Joint Committee staff converts these fiscal year revenue forecasts into the calendar year revenue forecasts that are presented in Table 11. These calendar year forecasts are the basis of the model because the relevant parameters of the law generally change with the calendar year. However, the Joint Committee staff reports the estimated effects of proposals upon Federal fiscal year receipts. To do this, the Joint Committee staff must reconvert the calendar year effects reported by the model into fiscal year effects.

<sup>63</sup> For purposes of Tables 11, 12, and 15, the generation skipping transfer tax is not separately listed, but instead is included in the estate tax or gift tax, respectively, according to whether the tax is levied on a transfer at death or during life.

<sup>64</sup> See the Appendix for the distribution of estate tax revenues.

### **III. A REVENUE ESTIMATING EXAMPLE: THE PRESIDENT'S FISCAL YEAR 2013 ESTATE AND GIFT BUDGET PROPOSAL**

One of the President's fiscal year 2013 budget proposals permanently reinstates the estate, gift, and generation skipping transfer tax parameters as they applied in 2009, modified to allow the portability of the unused estate tax exemption amount between spouses. Therefore, under the President's proposal, the estate and gift taxes have the same rate structure as under present law but with a top tax rate of 45 percent. The estate and generation skipping transfer tax exemption amount is \$3.5 million while the gift tax exemption amount is \$1 million (*i.e.*, the estate and gift taxes are no longer unified). Furthermore, some aspects of the estate and gift tax changes made by EGTRRA pertaining to qualified conservation easements, various technical aspects of the generation skipping transfer tax, and the installment payment of estate taxes are permanently extended.<sup>65</sup>

This proposal does not make changes to the tax base.<sup>66</sup> That is, the proposal does not change the present law treatment of assets as fully taxable, partially taxable, or exempt as described previously in Table 2. Furthermore, the proposal maintains a gift tax with a relatively small exemption amount and a high tax rate so that there are virtually no changes in opportunities or motives for tax avoidance. Also, the proposal does not change the contours of the gift tax regime. Under both the baseline and the proposal, the gift tax exemption amount falls from \$5.12 million in 2012 to \$1 million in 2013 while the top tax rate rises from 35 percent in 2012 to either 55 percent or 45 percent under the baseline and the proposal, respectively. With no change in the fundamental incentives, the Joint Committee staff estimates no substantial difference in the pattern or amount of giving under the proposal as compared to the baseline.

The Joint Committee staff uses the estate and gift tax calculator to produce preliminary estimates of the estate and gift tax revenues under the proposal. The results of this model for calendar years 2012 through 2021 without taking into account changes in charitable bequests are shown in Table 12a.

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<sup>65</sup> See Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2013 Revenue Proposals*, February 2012, available at <http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2013.pdf> and Joint Committee on Taxation, *Description of Revenue Provisions Contained in the President's Fiscal Year 2013 Budget Proposal* (JCS-2-12), June 2012, pp. 229-255.

<sup>66</sup> The President's budget proposals include other proposals to change the estate and gift tax base (*e.g.*, requiring a 10-year minimum term for a GRAT) that are beyond the scope of this document.

**Table 12a.--Transfer Tax Revenue Under the President's Proposal Without Changes  
in Charitable Bequests, CY 2012-21 (millions of dollars)**

|                                   | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   | 2020   | 2021   |
|-----------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Estate Tax Liability from Model   | 10,031 | 17,655 | 18,635 | 19,979 | 21,435 | 22,979 | 24,627 | 26,288 | 27,996 | 29,923 |
| Additional EGTRRA Revenue Changes | 0      | -427   | -542   | -572   | -605   | -639   | -615   | -586   | -552   | -518   |
| Total Estate Tax Liability        | 10,031 | 17,228 | 18,093 | 19,407 | 20,830 | 22,340 | 24,012 | 25,702 | 27,444 | 29,405 |
| Gift Tax Liability                | 5,027  | 2,688  | 3,778  | 4,495  | 5,273  | 5,553  | 5,828  | 6,094  | 6,365  | 6,644  |

The results of the model including changes in charitable bequests are shown in Table 12b. For example, in 2013, the difference between the estate tax liability from the model in Tables 12a and 12b is due to the modeled changes in charitable bequests resulting from the proposed policy change. The model shows charitable bequests falling by approximately five percent, from \$32.3 billion to \$30.6 billion, in 2013 with similar changes in subsequent years. Also, the President's proposal extends some aspects of EGTRRA relating to conservation easements, various technical aspects of the generation skipping transfer tax, and the installment payment of estate taxes that are better modeled outside of the estate and gift tax calculator; these are shown in the tables. The results shown in Table 12b, which both account for changes in charitable bequests and include some of the technical aspects of EGTRRA, are the foundation of the revenue estimate.

**Table 12b. --Transfer Tax Revenue Under the President's Proposal With Changes  
in Charitable Bequests, CY 2012-21 (millions of dollars)**

|                                   | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   | 2020   | 2021   |
|-----------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Estate Tax Liability from Model   | 10,031 | 18,214 | 19,225 | 20,614 | 22,118 | 23,713 | 25,415 | 27,131 | 28,895 | 30,884 |
| Additional EGTRRA Revenue Changes | 0      | -427   | -542   | -572   | -605   | -639   | -615   | -586   | -552   | -518   |
| Total Estate Tax Liability        | 10,031 | 17,787 | 18,683 | 20,042 | 21,513 | 23,074 | 24,800 | 26,545 | 28,343 | 30,366 |
| Gift Tax Liability                | 5,027  | 2,688  | 3,778  | 4,495  | 5,273  | 5,553  | 5,828  | 6,094  | 6,365  | 6,644  |

The Joint Committee staff then considers the potential income tax effects that may result from the proposed change in estate and gift tax policy. These include changes in lifetime charitable giving, capital gains realizations, and the form shopping of deductions between a decedent's final income tax return and estate tax return.

As discussed in the previous section, changes in the tax price of noncharitable bequests have effects beyond charitable bequests. Lifetime giving is also affected. The Joint Committee staff assumes that taxpayers use income and estate tax parameters to derive a giving and bequest plan. The Joint Committee staff uses charitable giving on the decedent's income tax returns for his final full year of life (that is, the decedent's penultimate income tax return) as a proxy for the giving part of this plan. The Joint Committee staff then extrapolates the plans of these decedents to those of older, wealthier taxpayers whose lifetime giving is likely influenced by the estate tax. This information is then used to estimate the revenue effects of decreasing the marginal estate

tax rates under the proposal from 55 percent to 45 percent.<sup>67</sup> The estimated increase in income tax revenues resulting from changes in lifetime charitable giving are shown in Table 13 below.

**Table 13.—Income Tax Effects of Changes in Lifetime Charitable Giving, CY 2012-22**  
(millions of dollars)

| 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|------|------|------|------|------|------|------|------|------|------|------|
| 0    | 141  | 149  | 161  | 173  | 186  | 199  | 213  | 227  | 243  | 260  |

The proposal's reduction in the top estate tax rate from 55 percent to 45 percent increases the *de facto* effective capital gains tax rate for individuals projected to have estates subject to the estate tax, resulting in fewer capital gains realizations (because, as discussed previously, the estate tax price of not realizing capital gains before death has decreased). This reduction in capital gains realizations leads to reduced income tax receipts. While the effect on capital gains realizations is small, the amount of capital gains realized in any given year is substantial so that even small effects on capital gains realizations may produce relatively large revenue effects when compared to estate tax receipts. The CBO capital gains baseline, the projected change in that baseline, and the projected revenue effects from the expected change in capital gains realizations are shown in Table 14.

**Table 14.—Capital Gains Baseline and Revenue Effects, CY 2012-22**  
(millions of dollars)

|                                       | 2012    | 2013    | 2014    | 2015    | 2016    | 2017    | 2018    | 2019    | 2020    | 2021    | 2022    |
|---------------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Capital Gains Realization Baseline    | 651,232 | 419,688 | 619,195 | 644,629 | 674,860 | 705,619 | 736,856 | 769,724 | 804,036 | 840,036 | 877,098 |
| Change in Capital Gains Realizations  | -3,397  | -2,746  | -4,052  | -4,218  | -4,416  | -4,617  | -4,822  | -5,037  | -5,263  | -5,497  | -5,739  |
| Change in Capital Gains Tax Liability | -510    | -645    | -952    | -991    | -1,038  | -1,085  | -1,133  | -1,184  | -1,237  | -1,292  | -1,349  |

Note: The capital gains realization baseline is produced by the Congressional Budget Office.

Finally, by increasing the estate tax exemption amount and by lowering the estate tax rate, the proposal may be expected to reduce the amount of deductions claimed on estate tax returns and increase deductions claimed on income tax returns. The Joint Committee staff estimates the deductions claimed on estate tax returns which would be taxable under the baseline but not under the President's budget proposal and the income tax rate that may be applied to those deductions if they were to be transferred to the decedent's final income tax return. This effect is generally quite small when the estate tax rate remains above the highest income tax rate as long as the estate tax exemption amount is not so large as to affect the use of these deductions against high-value estates. In the case of this proposal, the Joint Committee staff considers this

<sup>67</sup> For ease of exposition, in this section the five percent surtax on taxable estates of between \$10 million and \$17.184 million is disregarded.

effect to be negligible. Finally, the complete revenue estimate, after converting the calendar year revenue estimates to fiscal year revenue estimates, is shown in Table 15.

**Table 15. –Total Revenue Estimate of the President's Budget Proposal, CYs & FYs 2012-22**  
(millions of dollars)

|                                                                                 | 2012                             | 2013    | 2014    | 2015    | 2016    | 2017    | 2018    | 2019    | 2020    | 2021    | 2022    |
|---------------------------------------------------------------------------------|----------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Change in Estate Tax Liability (CY)                                             | 0                                | -19,942 | -21,225 | -22,859 | -24,623 | -26,492 | -28,438 | -30,388 | -32,366 | -34,604 | -       |
| Change In Gift Tax Liability (CY)                                               | 0                                | -463    | -650    | -774    | -908    | -958    | -1,007  | -1,053  | -1,102  | -1,150  | -       |
| Change in Income Tax Revenue from<br>Changes in Lifetime Charitable Giving (CY) | 0                                | 141     | 149     | 161     | 173     | 186     | 199     | 213     | 227     | 243     | 260     |
| Change in Income Tax Revenue from<br>Changes in Capital Gains Realizations (CY) | -510                             | -645    | -952    | -991    | -1,038  | -1,085  | -1,133  | -1,184  | -1,237  | -1,292  | -1,349  |
| Change in Income Tax Revenue from<br>Shifting Deductions (CY)                   | <i>Negligible Revenue Effect</i> |         |         |         |         |         |         |         |         |         |         |
| Total Fiscal Year Revenue Effect                                                | -38                              | -547    | -19,389 | -22,558 | -24,328 | -26,249 | -28,207 | -30,231 | -32,264 | -34,328 | -36,633 |

Note: Revenue from estate and gift tax liabilities incurred in CY2022 are not expected until at least FY2023. Therefore, the effects of the proposal on transfer tax liabilities in that year are not modeled.

## **APPENDIX: DISTRIBUTION OF THE ESTATE TAX UNDER THREE ESTATE AND GIFT TAX POLICIES**

This appendix describes the expected distribution of the estate tax burden as well as the total estimated revenue effects by calendar year for three different estate and gift tax policies. Table A1 shows the estate tax revenue by the size of the gross estate as well as the total expected number of returns filed and the number of taxable returns filed expected under present law. This is the baseline case. Tables A2 and A3 show this same estate tax information expected under the President's budget proposal and under a permanent extension of the Tax Relief Act, respectively.

Table A4 contains information on the taxable status of all returns and those returns identified by the Joint Committee staff as "Farm Estates" and "Small Business Estates" under the same three policies.<sup>68</sup> For this presentation, the Joint Committee staff defines farm estates as estates reporting positive values of farm assets or farm land if the sum of the values of the farm assets, farm land, improved real estate, vacant land, and mortgages and notes is at least one-half of the value of the total gross estate. Similarly, for this presentation, the Joint Committee staff defines small business estates as nonfarm estates reporting positive values for noncorporate business assets, closely held stock, or real estate partnerships and where the sum of the values of these assets plus cash is less than \$10 million and at least one-half the value of the total gross estate (*i.e.*, by this definition, one cannot have a small business worth \$10 million or more).<sup>69</sup>

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<sup>68</sup> There is no single definition of a "farm" or "small business" in Federal law. These terms are defined arbitrarily in the text for the purpose of presenting certain data to the reader.

<sup>69</sup> For purposes of identifying farm estates and small business estates, the valuation discounts claimed are eliminated from the computation of the numerator and the denominator to measure the economic activity of the relevant estates more accurately.

**Table A1.—Distribution of Estate Tax Liability by Return Type Under Present Law, CY2013-2017**  
**(Size of Gross Estate, Gross Estate, and Tax Liability in millions of dollars)**

|                      | 2013    |              |               | 2014    |              |               | 2015    |              |               | 2016    |              |               | 2017    |              |               |
|----------------------|---------|--------------|---------------|---------|--------------|---------------|---------|--------------|---------------|---------|--------------|---------------|---------|--------------|---------------|
| Size of Gross Estate | Nbr     | Gross Estate | Tax Liability | Nbr     | Gross Estate | Tax Liability | Nbr     | Gross Estate | Tax Liability | Nbr     | Gross Estate | Tax Liability | Nbr     | Gross Estate | Tax Liability |
| ALL RETURNS          |         |              |               |         |              |               |         |              |               |         |              |               |         |              |               |
| Less than 1.0        | 900     | 822          | 35            | 1,000   | 869          | 37            | 1,100   | 935          | 40            | 1,100   | 1,005        | 43            | 1,200   | 1,080        | 46            |
| 1.0 - 2.0            | 68,000  | 94,781       | 2,400         | 72,000  | 100,259      | 2,539         | 77,400  | 107,778      | 2,730         | 83,200  | 115,907      | 2,935         | 89,400  | 124,529      | 3,154         |
| 2.0 - 3.5            | 21,800  | 56,258       | 7,190         | 23,000  | 59,486       | 7,606         | 24,800  | 63,947       | 8,175         | 26,600  | 68,744       | 8,791         | 28,600  | 73,857       | 9,445         |
| 3.5 - 5.0            | 6,800   | 28,085       | 4,351         | 7,200   | 29,708       | 4,603         | 7,800   | 31,936       | 4,947         | 8,400   | 34,344       | 5,320         | 9,000   | 36,899       | 5,716         |
| 5.0 - 10.0           | 6,400   | 42,924       | 7,215         | 6,700   | 45,404       | 7,632         | 7,200   | 48,809       | 8,204         | 7,800   | 52,491       | 8,823         | 8,400   | 56,395       | 9,479         |
| 10.0 - 20.0          | 2,300   | 30,855       | 5,443         | 2,400   | 32,638       | 5,757         | 2,600   | 35,085       | 6,189         | 2,800   | 37,732       | 6,656         | 3,000   | 40,538       | 7,151         |
| More than 20.0       | 1,300   | 90,900       | 11,008        | 1,400   | 96,153       | 11,644        | 1,500   | 103,365      | 12,517        | 1,600   | 111,161      | 13,461        | 1,700   | 119,430      | 14,462        |
| All Returns          | 107,500 | 344,625      | 37,642        | 113,700 | 364,517      | 39,817        | 122,200 | 391,855      | 42,802        | 131,400 | 421,385      | 46,030        | 141,200 | 452,727      | 49,452        |
| TAXABLE RETURNS      |         |              |               |         |              |               |         |              |               |         |              |               |         |              |               |
| Less than 1.0        | 300     | 294          | 35            | 300     | 311          | 37            | 400     | 335          | 40            | 400     | 360          | 43            | 400     | 387          | 46            |
| 1.0 - 2.0            | 22,300  | 33,092       | 2,400         | 23,600  | 35,004       | 2,539         | 25,400  | 37,629       | 2,730         | 27,300  | 40,468       | 2,935         | 29,300  | 43,478       | 3,154         |
| 2.0 - 3.5            | 17,700  | 45,831       | 7,190         | 18,700  | 48,480       | 7,606         | 20,100  | 52,115       | 8,175         | 21,600  | 56,046       | 8,791         | 23,200  | 60,215       | 9,445         |
| 3.5 - 5.0            | 5,900   | 24,375       | 4,351         | 6,300   | 25,783       | 4,603         | 6,700   | 27,717       | 4,947         | 7,200   | 29,808       | 5,320         | 7,800   | 32,025       | 5,716         |
| 5.0 - 10.0           | 5,700   | 38,202       | 7,215         | 6,000   | 40,410       | 7,632         | 6,400   | 43,441       | 8,204         | 6,900   | 46,717       | 8,823         | 7,400   | 50,192       | 9,479         |
| 10.0 - 20.0          | 2,000   | 27,910       | 5,443         | 2,200   | 29,523       | 5,757         | 2,300   | 31,737       | 6,189         | 2,500   | 34,131       | 6,656         | 2,700   | 36,670       | 7,151         |
| More than 20.0       | 1,200   | 78,523       | 11,008        | 1,300   | 83,060       | 11,644        | 1,400   | 89,290       | 12,517        | 1,500   | 96,025       | 13,461        | 1,600   | 103,167      | 14,462        |
| All Returns          | 55,200  | 248,227      | 37,642        | 58,400  | 262,572      | 39,817        | 62,700  | 282,264      | 42,802        | 67,500  | 303,554      | 46,030        | 72,500  | 326,133      | 49,452        |
| NON-TAXABLE RETURNS  |         |              |               |         |              |               |         |              |               |         |              |               |         |              |               |
| Less than 1.0        | 600     | 528          | 0             | 600     | 558          | 0             | 700     | 600          | 0             | 700     | 645          | 0             | 800     | 693          | 0             |
| 1.0 - 2.0            | 45,700  | 61,689       | 0             | 48,400  | 65,254       | 0             | 52,000  | 70,148       | 0             | 55,900  | 75,440       | 0             | 60,100  | 81,051       | 0             |
| 2.0 - 3.5            | 4,100   | 10,427       | 0             | 4,300   | 11,006       | 0             | 4,600   | 11,832       | 0             | 5,000   | 12,697       | 0             | 5,300   | 13,642       | 0             |
| 3.5 - 5.0            | 900     | 3,710        | 0             | 1,000   | 3,924        | 0             | 1,000   | 4,219        | 0             | 1,100   | 4,537        | 0             | 1,200   | 4,874        | 0             |
| 5.0 - 10.0           | 700     | 4,721        | 0             | 700     | 4,994        | 0             | 800     | 5,369        | 0             | 900     | 5,774        | 0             | 900     | 6,203        | 0             |
| 10.0 - 20.0          | 200     | 2,945        | 0             | 200     | 3,115        | 0             | 300     | 3,348        | 0             | 300     | 3,601        | 0             | 300     | 3,869        | 0             |
| More than 20.0       | 100     | 12,378       | 0             | 100     | 13,093       | 0             | 100     | 14,075       | 0             | 100     | 15,137       | 0             | 100     | 16,263       | 0             |
| All Returns          | 52,300  | 96,398       | 0             | 55,400  | 101,945      | 0             | 59,500  | 109,591      | 0             | 64,000  | 117,830      | 0             | 68,700  | 126,594      | 0             |

Note: Details may not add to totals due to rounding. Number of returns ("Nbr") is rounded to the nearest 100.

**Table A2.—Distribution of Estate Tax Liability by Return Type Under President’s Budget Proposal, CY2013-2017**  
**(Size of Gross Estate, Gross Estate, and Tax Liability in millions of dollars)**

|                      | 2013   |              |               | 2014   |              |               | 2015   |              |               | 2016   |              |               | 2017   |              |               |
|----------------------|--------|--------------|---------------|--------|--------------|---------------|--------|--------------|---------------|--------|--------------|---------------|--------|--------------|---------------|
| Size of Gross Estate | Nbr    | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability |
| ALL RETURNS          |        |              |               |        |              |               |        |              |               |        |              |               |        |              |               |
| Less than 1.0        | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             |
| 1.0 - 2.0            | [1]    | 30           | 0             | [1]    | 32           | 0             | [1]    | 34           | 0             | [1]    | 37           | 0             | [1]    | 40           | 0             |
| 2.0 - 3.5            | 500    | 1,653        | 17            | 600    | 1,748        | 17            | 600    | 1,879        | 17            | 700    | 2,021        | 17            | 700    | 2,171        | 17            |
| 3.5 - 5.0            | 6,300  | 26,016       | 421           | 6,700  | 27,519       | 434           | 7,200  | 29,583       | 452           | 7,700  | 31,814       | 472           | 8,300  | 34,181       | 495           |
| 5.0 - 10.0           | 6,300  | 42,742       | 3,020         | 6,700  | 45,212       | 3,177         | 7,200  | 48,603       | 3,392         | 7,700  | 52,269       | 3,626         | 8,300  | 56,157       | 3,874         |
| 10.0 - 20.0          | 2,300  | 30,855       | 3,836         | 2,400  | 32,638       | 4,051         | 2,600  | 35,085       | 4,346         | 2,800  | 37,732       | 4,665         | 3,000  | 40,538       | 5,003         |
| More than 20.0       | 1,300  | 90,900       | 10,866        | 1,400  | 96,153       | 11,490        | 1,500  | 103,365      | 12,346        | 1,600  | 111,161      | 13,272        | 1,700  | 119,430      | 14,254        |
| All Returns          | 16,700 | 192,196      | 18,160        | 17,700 | 203,303      | 19,168        | 19,000 | 218,550      | 20,553        | 20,500 | 235,035      | 22,052        | 22,000 | 252,517      | 23,643        |
| TAXABLE RETURNS      |        |              |               |        |              |               |        |              |               |        |              |               |        |              |               |
| Less than 1.0        | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             |
| 1.0 - 2.0            | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             |
| 2.0 - 3.5            | 100    | 435          | 17            | 100    | 409          | 17            | 100    | 418          | 17            | 100    | 445          | 17            | 100    | 478          | 17            |
| 3.5 - 5.0            | 1,700  | 7,160        | 421           | 1,700  | 7,389        | 434           | 1,800  | 7,812        | 452           | 1,900  | 8,033        | 472           | 2,000  | 8,596        | 495           |
| 5.0 - 10.0           | 2,900  | 20,435       | 3,020         | 3,100  | 21,616       | 3,177         | 3,300  | 23,222       | 3,392         | 3,600  | 24,973       | 3,626         | 3,800  | 26,814       | 3,874         |
| 10.0 - 20.0          | 1,500  | 20,553       | 3,836         | 1,600  | 21,740       | 4,051         | 1,700  | 23,371       | 4,346         | 1,800  | 25,134       | 4,665         | 2,000  | 27,003       | 5,003         |
| More than 20.0       | 900    | 71,591       | 10,866        | 1,000  | 75,728       | 11,490        | 1,100  | 81,408       | 12,346        | 1,100  | 87,548       | 13,272        | 1,200  | 94,060       | 14,254        |
| All Returns          | 7,200  | 120,174      | 18,160        | 7,500  | 126,882      | 19,168        | 8,000  | 136,230      | 20,553        | 8,600  | 146,133      | 22,052        | 9,200  | 156,951      | 23,643        |
| NON-TAXABLE RETURNS  |        |              |               |        |              |               |        |              |               |        |              |               |        |              |               |
| Less than 1.0        | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             |
| 1.0 - 2.0            | [1]    | 30           | 0             | [1]    | 32           | 0             | [1]    | 34           | 0             | [1]    | 37           | 0             | [1]    | 40           | 0             |
| 2.0 - 3.5            | 400    | 1,217        | 0             | 400    | 1,339        | 0             | 500    | 1,462        | 0             | 500    | 1,576        | 0             | 600    | 1,693        | 0             |
| 3.5 - 5.0            | 4,600  | 18,855       | 0             | 4,900  | 20,130       | 0             | 5,400  | 21,771       | 0             | 5,800  | 23,781       | 0             | 6,300  | 25,585       | 0             |
| 5.0 - 10.0           | 3,400  | 22,307       | 0             | 3,600  | 23,596       | 0             | 3,900  | 25,381       | 0             | 4,200  | 27,295       | 0             | 4,500  | 29,343       | 0             |
| 10.0 - 20.0          | 800    | 10,302       | 0             | 800    | 10,897       | 0             | 900    | 11,715       | 0             | 900    | 12,598       | 0             | 1,000  | 13,535       | 0             |
| More than 20.0       | 400    | 19,309       | 0             | 400    | 20,425       | 0             | 400    | 21,957       | 0             | 500    | 23,613       | 0             | 500    | 25,370       | 0             |
| All Returns          | 9,600  | 72,022       | 0             | 10,200 | 76,421       | 0             | 11,000 | 82,320       | 0             | 11,900 | 88,902       | 0             | 12,800 | 95,566       | 0             |

Notes: Details may not add to totals due to rounding. Number of returns (“Nbr”) filed is rounded to the nearest 100 and does not include those who file solely to preserve the exemption amount of a spouse.  
[1] = less than 50 returns

**Table A3.—Distribution of Estate Tax Liability By Return Type Under A Permanent Extension of the Tax Relief Act, CY2013-2017**  
**(Size of Gross Estate, Gross Estate, and Tax Liability in millions of dollars)**

|                      | 2013  |              |               | 2014  |              |               | 2015   |              |               | 2016   |              |               | 2017   |              |               |
|----------------------|-------|--------------|---------------|-------|--------------|---------------|--------|--------------|---------------|--------|--------------|---------------|--------|--------------|---------------|
| Size of Gross Estate | Nbr   | Gross Estate | Tax Liability | Nbr   | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability | Nbr    | Gross Estate | Tax Liability |
| ALL RETURNS          |       |              |               |       |              |               |        |              |               |        |              |               |        |              |               |
| Less than 1.0        | [1]   | 1            | 0             | [1]   | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             |
| 1.0 - 2.0            | [1]   | 5            | 0             | [1]   | 5            | 0             | [1]    | 5            | 0             | [1]    | 6            | 0             | [1]    | 6            | 0             |
| 2.0 - 3.5            | [1]   | 72           | 0             | [1]   | 76           | 0             | [1]    | 82           | 0             | [1]    | 88           | 0             | [1]    | 85           | 0             |
| 3.5 - 5.0            | 200   | 1,056        | 1             | 200   | 936          | [2]           | 200    | 899          | [2]           | 200    | 732          | 0             | 100    | 599          | 0             |
| 5.0 - 10.0           | 5,400 | 37,755       | 846           | 5,500 | 38,935       | 830           | 5,800  | 41,082       | 831           | 6,000  | 42,742       | 821           | 6,100  | 44,208       | 797           |
| 10.0 - 20.0          | 2,300 | 30,842       | 2,244         | 2,400 | 32,624       | 2,330         | 2,600  | 35,057       | 2,461         | 2,800  | 37,702       | 2,590         | 3,000  | 40,506       | 2,712         |
| More than 20.0       | 1,300 | 90,900       | 8,284         | 1,400 | 96,153       | 8,733         | 1,500  | 103,365      | 9,358         | 1,600  | 111,161      | 10,025        | 1,700  | 119,430      | 10,722        |
| All Returns          | 9,200 | 160,630      | 11,375        | 9,500 | 168,730      | 11,894        | 10,100 | 180,492      | 12,650        | 10,500 | 192,432      | 13,436        | 11,000 | 204,834      | 14,232        |
| TAXABLE RETURNS      |       |              |               |       |              |               |        |              |               |        |              |               |        |              |               |
| Less than 1.0        | 0     | 0            | 0             | 0     | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             |
| 1.0 - 2.0            | 0     | 0            | 0             | 0     | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             |
| 2.0 - 3.5            | 0     | 0            | 0             | 0     | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             | 0      | 0            | 0             |
| 3.5 - 5.0            | [1]   | 113          | 1             | [1]   | 52           | [2]           | [1]    | 42           | [2]           | 0      | 0            | 0             | 0      | 0            | 0             |
| 5.0 - 10.0           | 1,700 | 12,792       | 846           | 1,700 | 12,868       | 830           | 1,700  | 13,122       | 831           | 1,700  | 13,206       | 821           | 1,700  | 13,401       | 797           |
| 10.0 - 20.0          | 1,100 | 15,514       | 2,244         | 1,200 | 16,361       | 2,330         | 1,300  | 17,453       | 2,461         | 1,400  | 18,702       | 2,590         | 1,500  | 19,983       | 2,712         |
| More than 20.0       | 700   | 62,149       | 8,284         | 800   | 65,716       | 8,733         | 800    | 70,498       | 9,358         | 900    | 75,816       | 10,025        | 1,000  | 81,325       | 10,722        |
| All Returns          | 3,600 | 90,568       | 11,375        | 3,700 | 94,998       | 11,894        | 3,900  | 101,115      | 12,650        | 4,000  | 107,724      | 13,436        | 4,200  | 114,709      | 14,232        |
| NON-TAXABLE RETURNS  |       |              |               |       |              |               |        |              |               |        |              |               |        |              |               |
| Less than 1.0        | [1]   | 1            | 0             | [1]   | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             | [1]    | 1            | 0             |
| 1.0 - 2.0            | [1]   | 5            | 0             | [1]   | 5            | 0             | [1]    | 5            | 0             | [1]    | 6            | 0             | [1]    | 6            | 0             |
| 2.0 - 3.5            | [1]   | 72           | 0             | [1]   | 76           | 0             | [1]    | 82           | 0             | [1]    | 88           | 0             | [1]    | 85           | 0             |
| 3.5 - 5.0            | 200   | 943          | 0             | 200   | 883          | 0             | 200    | 857          | 0             | 200    | 732          | 0             | 100    | 599          | 0             |
| 5.0 - 10.0           | 3,700 | 24,963       | 0             | 3,800 | 26,067       | 0             | 4,100  | 27,961       | 0             | 4,300  | 29,537       | 0             | 4,400  | 30,807       | 0             |
| 10.0 - 20.0          | 1,100 | 15,328       | 0             | 1,200 | 16,263       | 0             | 1,300  | 17,604       | 0             | 1,400  | 18,999       | 0             | 1,500  | 20,523       | 0             |
| More than 20.0       | 600   | 28,751       | 0             | 600   | 30,437       | 0             | 600    | 32,866       | 0             | 700    | 35,345       | 0             | 800    | 38,104       | 0             |
| All Returns          | 5,600 | 70,062       | 0             | 5,800 | 73,733       | 0             | 6,200  | 79,377       | 0             | 6,500  | 84,708       | 0             | 6,800  | 90,126       | 0             |

Notes: Details may not add to totals due to rounding. Number of returns ("Nbr") filed is rounded to the nearest 100 and does not include those who file solely to preserve the exemption amount of a spouse.

[1] = less than 50 returns

[2] = less \$500,000

**Table A4.—Number of Estates of Decedents Dying in Calendar Years 2013 Through 2021**

|                                              | 2013    | 2014    | 2015    | 2016    | 2017    | 2018    | 2019    | 2020    | 2021    |
|----------------------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| <u>Present Law</u>                           |         |         |         |         |         |         |         |         |         |
| Filers                                       | 107,500 | 113,700 | 122,200 | 131,400 | 141,200 | 151,700 | 162,200 | 173,000 | 185,100 |
| Taxable Estates                              | 55,200  | 58,400  | 62,700  | 67,500  | 72,500  | 77,800  | 83,200  | 88,800  | 95,000  |
| Farming Taxable Estates                      | 2,400   | 2,500   | 2,700   | 2,900   | 3,100   | 3,400   | 3,600   | 3,800   | 4,100   |
| Small Business Taxable Estates               | 2,700   | 2,800   | 3,000   | 3,200   | 3,500   | 3,700   | 4,000   | 4,300   | 4,600   |
| <u>President's Budget Proposal</u>           |         |         |         |         |         |         |         |         |         |
| Filers                                       | 16,700  | 17,700  | 19,000  | 20,500  | 22,000  | 23,600  | 25,300  | 27,000  | 28,800  |
| Taxable Estates                              | 7,200   | 7,500   | 8,000   | 8,600   | 9,200   | 9,800   | 10,400  | 11,100  | 11,800  |
| Farming Taxable Estates                      | 300     | 300     | 300     | 300     | 300     | 300     | 400     | 400     | 400     |
| Small Business Taxable Estates               | 400     | 500     | 500     | 500     | 600     | 600     | 700     | 700     | 700     |
| <u>Permanent Extension of Tax Relief Act</u> |         |         |         |         |         |         |         |         |         |
| Filers                                       | 9,200   | 9,500   | 10,100  | 10,500  | 11,000  | 11,400  | 11,800  | 12,100  | 12,500  |
| Taxable Estates                              | 3,600   | 3,700   | 3,900   | 4,000   | 4,200   | 4,300   | 4,400   | 4,500   | 4,600   |
| Farming Taxable Estates                      | 100     | 100     | 100     | 100     | 100     | 100     | 100     | 100     | 100     |
| Small Business Taxable Estates               | 200     | 200     | 200     | 200     | 200     | 200     | 200     | 200     | 200     |