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February 2, 2009

Congressional Research Service

Report RL31061

Estate and Gift Tax Law: Changes Under the Economic Growth and Tax Relief Reconciliation Act of 2001

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Updated January 29, 2002

Abstract. The first section of this report emphasizes the three distinct time phases under the Act. The second section describes the major changes from prior law regarding estate and gift taxes.

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Order Code RL31061

CRS Report for Congress
Received through the CRS Web

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Updated January 29, 2002

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Estate and Gift Tax Law: Changes Under the Economic Growth and Tax Relief Reconciliation Act of 2001

Summary

The Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16, EGTRRA) was enacted on June 7, 2001. Title V of the Act contains the provisions addressing estate, gift, and generation-skipping transfer (GST) taxes. These take effect in three distinct time phases. During the phasedown period – calendar years 2002 through 2009 – the Act reduces estate, gift, and generation-skipping transfer tax liabilities by raising the exempt amount of a taxable estate (the applicable exclusion amount) and lowering the maximum tax rate. In 2010, the estate and GST taxes will be repealed; the step-up in basis will be replaced with a modified carryover basis for assets transferred at death; and the gift tax will remain in effect, with the maximum gift tax rate lowered to the maximum income tax rate. On December 31, 2010, all provisions of the Act are scheduled to sunset. Unless future legislation extends the estate tax provisions of EGTRRA or enacts new ones, on January 1, 2011, estate and gift tax law will revert to the law in place prior to June 7, 2001.

During the phasedown period, the exemption per decedent under the estate tax is scheduled to rise (from $675,000 in 2001) to $1 million in 2002; $1.5 million in 2004; $2 million in 2006; and $3.5 million in 2009. The GST exemption ($1,100,000 in 2002 and indexed for 2003 under prior law) will be equal to the estate tax exemption from 2004 through 2009. For the gift tax, the lifetime gift exemption increased to $1 million in 2002 and will remain there. Exemptions claimed for lifetime gifts will continue to be subtracted from the exemption remaining for the estate tax at death. The maximum tax rate for both the estate and gift taxes is scheduled to fall (from 55%, plus a 5% surcharge for a certain range over $10 million, in 2001) to 50% in 2002; 49% in 2003; 48% in 2004; 47% in 2005; 46% in 2006; and 45% in 2006-2009. The GST tax rate will be the maximum estate tax rate in effect for the year. In 2010, when the estate tax and GST tax are repealed, the gift tax will remain in effect, but the maximum gift tax rate will be lowered to 35%. The credit for state death taxes will be reduced to 75% of its prior-law value in 2002, 50% in 2003, 25% in 2004, and repealed and replaced with a full deduction in 2005.

In 2010, the step-up in basis for inherited assets will be replaced with a carryover basis, with two exceptions. A basis increase of up to $1.3 million per decedent may be allocated among assets transferred to any beneficiary. An additional basis increase of up to $3 million may be allocated to assets transferred to a surviving spouse. Instead of filing an estate tax return, executors of estates with more than $1.3 million in assets (other than cash) will be required to file a "return relating to large transfers" with the IRS, to help document the carryover basis of each asset transferred to heirs.

As a consequence of the year-by-year changes in the tax law prescribed by EGTRRA, the law that will apply to a particular individual's estate will vary substantially, depending upon the year of death. Because the new law is scheduled to sunset at the end of 2010, knowledge of prior law remains relevant for long-term estate tax planning. This report may be updated as the new law is clarified.

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Estate and Gift Tax Law: Changes Under the Economic Growth and Tax Relief Reconciliation Act of 2001

The Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16, henceforth referred to EGTRRA or the Act)[1] was approved by Congress on May 26, 2001, and signed by President George W. Bush on June 7, 2001. Title V of the Act contains the provisions addressing estate, gift, and generation-skipping transfer (GST) taxes – often referred to simply as estate and gift taxes.

The first section of the report emphasizes the three distinct time phases under the Act. The second section describes the major changes from prior law regarding estate and gift taxes. There are many other detailed provisions in Title V that are not addressed here.[2] This report may be updated as the new law is clarified.

Three Phases of the Act

The effective dates for the estate and gift tax provisions in EGTRRA fall into three distinct time periods:

- phasedown period, from calendar year 2002 through 2009;
- repeal year for the estate tax and generation-skipping transfer tax, 2010; and
- post-sunset period, 2011 and after.

Table 1 on the next page summarizes the major changes in estate and gift tax law scheduled by the Act, for each year from 2002 to 2011. As a consequence of the year-by-year changes, the tax law that will apply to a particular individual's estate will vary substantially, depending upon the year of the person's death, the year in which a gift is made, or the year the generation-skipping transfer is made.[3]

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[1]H.R. 1836, P.L. 107-16, 115 Stat. 38.

[2]For a detailed summary of provisions in the new tax law, see Robert F. Manning and David F. Windish, "Tax Analysts' Guide to the Economic Growth and Tax Relief Reconciliation Act of 2001," *Tax Notes*, vol. 91, no. 12, June 11, 2001.

[3]For purposes of estate and gift taxes, the effective dates formally apply to "estates of decedents dying, gifts made, or generation skipping transfers" after the effective date. In the law, the effective date is usually expressed as "after December 31" of a particular year (e.g., after December 31, 2001). For simplicity, this text refers to that effective date as the next calendar year, which begins the next day on January 1 (the year 2002, in this example).

Table 1. Year-by-Year Changes in Estate and Gift Tax Law: 2002-2011

Effective Date (For the estates of decedents dying, and gifts or generation-skipping transfers made, in calendar year)	**Major Changes in Estate and Gift Tax Law**
2002	5% surtax repealed. Tax rates above 50% repealed. Unified estate and gift exemption increased to $1 million; lifetime gift exemption will remain at $1 million.[a] State death tax credit decreased to 75% of its prior-law level.
2003	Tax rates above 49% repealed. State death tax credit decreased to 50% of its prior-law level.
2004	Tax rates above 48% repealed. Estate[a] and GST exemption amount increased to $1.5 million. Family-owned business deduction repealed. State death tax credit decreased to 25% of its prior-law level.
2005	Tax rates above 47% repealed. State death tax credit repealed and replaced by a deduction for all state death taxes actually paid.
2006	Tax rates above 46% repealed. Estate[a] and GST exemption amount increased to $2 million.
2007	Tax rates above 45% repealed.
2008	No additional changes.
2009	Estate[a] and GST exemption amount increased to $3.5 million.
2010	Estate and generation-skipping transfer taxes repealed. Gift tax remains in effect; maximum gift tax rate is lowered to 35%, the maximum individual income tax rate; lifetime exemption for gifts remains at $1 million. Repeal of step-up in basis for assets transferred at death. Replaced with modified carryover basis that permits an added basis increase of $1.3 million per decedent, plus $3 million for assets transferred to a surviving spouse. Reporting requirements introduced for assets other than cash transferred during life or at death.
2011	Sunset of all provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 on December 31, 2010. Unless the new law is extended or changed, return to tax law in place prior to June 7, 2001, effective January 1, 2011.

a. Of the total unified estate and gift exemption amount, up to $1 million may be used for lifetime gifts.

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Phasedown Period, 2002-2009

During the phasedown period for the estate tax – calendar years 2002 through 2009 – EGTRRA reduces estate, gift, and generation-skipping transfer (GST) tax liabilities by raising the exempt amount of taxable estate (the applicable exclusion amount) and lowering the maximum marginal tax rate.

Repeal of Estate Tax and GST Tax, 2010

In calendar year 2010, the estate tax and the generation-skipping transfer (GST) tax are repealed. For assets transferred at death, the step-up in basis is replaced with a modified carryover basis. For gifts made during one's lifetime, the gift tax will remain in effect with a lifetime exemption of $1 million, but the maximum gift tax rate will be lowered to the maximum income tax rate in 2010.

Sunset, 2011 and After

Under the terms of Title IX of EGTRRA, all provisions of the Act are scheduled to sunset on December 31, 2010. In particular, provisions of the Act shall not apply "... in the case of title V, to estates of decedents dying, gifts made, or generation skipping transfers, after December 31, 2010." As a result of this sunset provision, on January 1, 2011, estate and gift tax law is scheduled to revert to the law that was in place prior to June 7, 2001.

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Changes Relative to Prior Law

This section emphasizes the major changes in estate and gift tax law made by the Economic Growth and Tax Relief Reconciliation Act of 2001. Because the new law is scheduled to sunset on December 31, 2010, knowledge of prior law remains relevant for long-term estate and gift tax planning. Also, for most provisions, prior law continued to apply until year-end 2001.[4]

The order of presentation here does not follow the sequence in the Act. However, to make it easier to refer to the Act, the subheadings indicate the subtitle of Title V that contains the provision being discussed.

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[4]A few provisions in EGTRRA were effective retroactively, beginning after December 31, 2000. These include the modifications to the treatment of generation-skipping transfers and repealing the geographic restrictions on conservation easements.

Exemption Amount Increased during Phasedown (Subtitle C)

The amount of a decedent's[5] assets that may be transferred free from estate tax is commonly referred to as the "exemption amount" or simply the "exemption." Formally, in the Internal Revenue Code, the exemption is called the "applicable exclusion amount." EGTRRA calls it the "unified credit effective exemption amount," referring to the unified estate and gift tax credit.

Under prior law, the unified estate and gift tax exemption amount was scheduled to rise from $675,000 in 2001, to $700,000 in 2002 and 2003, $850,000 in 2004, $950,000 in 2005, and finally $1 million in 2006. Instead, EGTRRA raised the exemption amount to $1 million for 2002 and 2003. The lifetime gift exemption is to remain at $1 million thereafter, while the unified estate and gift exemption continues to rise during the tax phasedown period.

Under prior law, the generation-skipping transfer (GST) tax exemption was set at $1 million, indexed for inflation after 1998. The GST exemption was $1,060,00 in 2001 and is $1,100,000 for 2002. For 2003, the GST exemption will have its indexed value, to be determined under prior law.

Starting in 2004, EGTRRA sets the GST exemption equal to the applicable exclusion amount for the estate tax. The exemption for both the estate tax and the GST tax will rise together: to $1.5 million in 2004, $2 million in 2006, and $3.5 million in 2009. The applicable exclusion amount for the estate tax, by calendar year, is shown in the middle column of **Table 2**.

The estate and gift tax are still unified from 2002 through 2009, in the sense that the exemption available at death will be reduced by the amount of lifetime gifts that claimed the gift tax exemption. As an illustration, assume that a person had given cumulative gifts of $1 million or more during their lifetime and claimed the maximum permitted lifetime gift exemption of $1 million. If the person died in 2002 or 2003, there would be no exemption remaining for the estate at death because the unified credit effective exemption for 2002 and 2003 of $1 million would already be fully used. However, if the person died in 2009, the exemption amount still available to the estate at the time of death would be $2.5 million, equal to the unified credit effective exemption for 2009 of $3.5 million minus the lifetime gift exemption of $1 million. In 2010, the estate tax is repealed but the gift tax remains in place with a lifetime exemption of $1 million.

The exemption amount continues to apply per decedent. Thus, for a couple to take full advantage of two times the estate tax exemption amount ($2 million instead of $1 million in 2002; $7 million instead of $3.5 million in 2009), they must take the

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[5]Decedent is the word used in the law to refer to a deceased or dead person. People planning ahead for their own affairs could substitute the word "person" or "individual" for "decedent." It is important to understand that the estate tax provisions apply to each person individually and not to a married couple as a unit.

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necessary estate tax planning steps. This includes assigning ownership of some assets to each spouse independently, rather than jointly.[6]

Table 2. Applicable Exclusion Amount and Maximum Tax Rate Under the Estate Tax, 2002-2011

Calendar Year (In the case of estates of decedents dying during)	**Applicable Exclusion Amount** [a, b]	**Maximum Tax Rate on Taxable Estate in Excess of** [c]
2002	$1 million	50% over $2.5 million
2003	$1 million	49% over $2 million
2004	$1.5 million	48% over $2 million
2005	$1.5 million	47% over $2 million
2006	$2 million	46% over $2 million
2007-2008	$2 million	45% over $2 million
2009	$3.5 million	45% over $2 million
2010	N/A Tax repealed for 2010	N/A Tax repealed for 2010
2011 and thereafter (New law sunsets December 31, 2010. Unless extended or changed, return to law prior to June 7, 2001.)	$1 million	55% over $3 million, plus 5% surtax on $10 million to $17,184,000

a. The unified exemption or applicable exclusion amount may include up to $1 million in lifetime gifts.
b. The same exemption amount applies to the generation-skipping transfer (GST) tax as to the estate tax from 2004 through 2009, under EGTRRA. The GST exemption is $1,100,000 for 2002 and will be indexed for inflation again in 2003, under prior law.
c. As under prior law, the GST tax rate is the maximum estate tax rate in effect for the year.

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[6]The new law did not adopt the proposal (offered in some of the estate tax reform bills introduced in the 106th and 107th Congresses) that a surviving spouse be able to use any remaining exemption amount unused by the first spouse to die.

The new law retains the system of a tax credit to deliver the tax benefits of the exemption. Under EGTRRA, the applicable exclusion amount is still converted into a tax credit, known as the "applicable credit amount" or the "unified credit" (where "unified" refers to the unified estate and gift tax).[7], [8]

Family-owned Business Deduction Repealed. Under prior law, there is a special deduction for family-owned business interests (Section 2057 of the Internal Revenue Code or IRC). That special deduction of $675,000 (maximum), in combination with the applicable exclusion amount (available to all estates), can protect up to $1.3 million in estate value from taxation.[9] Because the exemption available to all decedents will reach $1.5 million in 2004, the $1.3 million deduction would no longer offer an advantage. EGTRRA repealed the special deduction for estates with family-owned businesses as of 2004.

Maximum Tax Rates Lowered during Phasedown (Subtitle B)

From 2002 through 2009, during the phasedown period, the same reductions in the maximum tax rate apply to both estate and gift tax rates. The reductions in the maximum tax rate affect taxable estate values above $2 million. The graduated rates established by prior law continue to apply to estate values up to $2 million. In 2010, when the estate tax is repealed, the gift tax will remain. At that time, the maximum gift tax rate will be lowered (from 45%) to 35%. This is equal to the maximum rate of the income tax in 2010, under other provisions of EGTRRA.

Information about the maximum tax rates in effect each year, and the level of taxable estate values above which they will apply, is summarized on the preceding page, in the last column of **Table 2**. The two tables in the appendix at the end of this report were created by the Congressional Research Service to present the full schedule of graduated estate and gift tax rates for each year from 2002 through 2011.

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[7]The applicable credit amount (the unified credit) is equal to the estate tax that would be due on the applicable exclusion amount (the exemption). The tax credit is subtracted from the tentative tax that would otherwise be due on the entire taxable estate. Both the exemption and its corresponding credit amount will vary according to the particular calendar year of a person's death. For a given year, the maximum dollar amount of the permitted credit is the same for all estates, regardless of their size. For further explanation, see CRS Report RL31092, *Calculating Estate Tax Liability During the Estate Tax Phasedown Period 2001-2009*, by Nonna A. Noto.

[8]In contrast, H.R. 8, the *Death Tax Elimination Act of 2001*, passed by the House on April 4, 2001, would have converted the applicable credit amount or unified credit into a "true exemption." Under that system, the exemption amount would be subtracted from the value of the taxable estate before applying the graduated tax rate schedule. For the same dollar amount of exemption, larger estates facing higher marginal tax rates would receive a bigger tax saving that smaller estates facing lower marginal rates.

[9]For further explanation of the criteria to qualify for the deduction and the mathematical interaction between the qualified business deduction and the applicable credit amount, see CRS Report 95-416 A, *Federal Estate, Gift, and Generation-Skipping Taxes: A Description of Current Law*, by John R. Luckey, section on "Deductions from the Gross Estate: Reaching the Taxable Estate," p. 5.

Because the new law is scheduled to sunset on December 31, 2010, the column for 2011 reflects the law in place prior to enactment of EGTRRA on June 7, 2001. In the appendix**, Table A.1** presents the schedule of federal estate tax rates. **Table A.2** presents the schedule of federal gift tax rates. In both tables, the changes in the maximum tax rate are highlighted in bold type.

Under prior law, the maximum rate of estate and gift tax was 55% on taxable estate values over $3 million. In addition, a 5% "bubble" surtax was levied on estate values from $10 million to $17,184,000. (The surtax was intended to phase out the benefit of the graduated rates – the rates below 55% – for large estates.)

Under EGTRRA, the 5% surtax is repealed in 2002. Also in 2002, tax rates in excess of 50% are repealed. (These include the rates of 55% on taxable estate value over $3 million and 53% on values from $2.5 million to $3 million.) Thus, in 2002, the maximum rate is 50% on taxable amounts over $2.5 million.

In 2003, estate and gift tax rates in excess of 49% are repealed. This means that the tax rate on taxable estate values over $2.5 million will fall from 50% to 49%.

The remaining four rate reductions lower the tax rate on all taxable estate values over $2.0 million. The maximum marginal tax rate will fall from 49% in 2003, by one percentage point per year, down to 45% by 2007. This means that the tax rate on estate values over $2.0 million will be 48% in 2004, 47% in 2005, 46% in 2006, and 45% in 2007 through 2009. Under prior law, the tax rate already was 45% on taxable estate values from $1.5 million to $2.0 million. The graduated tax rates in the tax brackets below $2.0 million will remain the same as under prior law.

As of December 31, 2010, all of the changes made by EGTRRA are scheduled to sunset. Unless future legislation extends the provisions of EGTRRA or enacts new ones, on January 1, 2011, estate and gift tax law will revert to the law in place prior to June 7, 2001. Under provisions of prior law, the exemption amount under the estate tax would have risen (from $675,000 in 2001) to $1 million for 2006 and subsequent years. Tax rates would revert to their prior-law levels, with a maximum rate of 55% and the 5% surtax to phase out the benefits of the graduated rates. (See appendix **Table A.1** for a year-by-year schedule of estate tax rates.)

Estate Tax Repealed in 2010, Gift Tax Retained (Subtitle A)

In 2010, when the estate tax and the generation-skipping transfer tax are repealed, the gift tax will remain in effect.

Under prior law, the estate tax and gift tax were completely unified and faced a single exemption amount. (They will continue to be treated this way for 2002 and 2003 under EGTRAA.) With regard to tax liability, it did not matter whether a person transferred assets to another individual as a gift while still alive, or as a bequest after death. For each person, the applicable exclusion amount was a cumulative lifetime exemption that encompassed both taxable gifts during life and the estate remaining at death. The gift tax only became due on a current basis once a person

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had given away taxable gifts[10] over their lifetime that cumulatively exceeded the applicable exclusion amount in effect for the year of the gifts (in 2001, cumulative taxable gifts exceeding $675,000; under EGTRRA, in 2002 and 2003, cumulative taxable gifts exceeding $1 million). At the time of death, lifetime taxable gifts were counted as part of the estate in calculating the tentative estate tax due. In determining the net estate tax due after death, the estate was credited for any gift taxes already paid. Hence the name "unified credit." The same graduated tax rate schedule applied to both estate and gift taxes.

Under EGTRRA, the same reduction in the maximum tax rate that applies to the estate tax also applies to the gift tax during the entire phasedown period, from 2002 through 2009. For 2002 and 2003, the unified credit effective exemption increases to $1 million for both the estate and gift taxes. However, EGTRRA gradually separates the estate tax from the gift tax after 2003. The lifetime exemption under the gift tax will remain at $1 million. In contrast, the estate tax exemption is scheduled to rise to $1.5 million in 2004, $2 million in 2006, and $3.5 million in 2009.

In 2010, when the estate tax is repealed, the gift tax remains in effect with an exemption of $1 million.[11] However, the maximum gift tax rate will be lowered from 45% to 35% – the maximum individual income tax rate by that time, under other provisions of EGTRRA. The 35% maximum marginal tax rate would apply to cumulative taxable gift transfers above $500,000. In the brackets up to $500,000, the lower graduated marginal tax rates will remain as under prior law.[12]

The maximum value of the lifetime gift tax credit would be $330,800, the tax otherwise due on the first $1 million in taxable gifts. The total lifetime credit can be allocated in portions to separate gifts, to protect them from gift tax. Cumulative gifts in excess of $1 million would be subject to gift tax on a current basis, for the year the gift is made.

If the new tax law sunsets as scheduled on December 31, 2010, the cumulative lifetime exemption under the unified estate and gift tax would remain at $1 million, because it would have risen to $1 million for 2006 and thereafter under provisions of prior law. However, the maximum gift tax rate would revert to its former higher level, rising from 35% in 2010 back to 55% in 2011. (See appendix **Table A.2** for a year-by-year schedule of gift tax rates.)

In short, any lifetime gifts beyond the first $1 million would be subject to gift tax on a current basis under all of the scenarios: during the phasedown period from 2002

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[10]There are some exclusions from the gift tax, described near the end of this section. Gifts covered by these exclusions are not considered taxable and are not counted against the lifetime exemption.

[11]Beginning in 2010, a transfer to a trust will be treated as a taxable gift, unless the trust is treated as wholly owned by the donor or the donor's spouse under the grantor trust provisions of the Internal Revenue Code.

[12]The graduated rates below 35% affect the calculation of the total tentative gift tax and the tax credit on the first $1 million in gifts.

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through 2009, in 2010 when the estate tax is repealed, and in 2011 and beyond under either prior law or an extension of EGTRRA.

Three exclusions from the gift tax remain as under prior law. Gifts covered by these exclusions do not count against the donor's lifetime gift exemption. There is still an annual exclusion for gifts from an individual donor to an individual beneficiary, up to a certain dollar amount. Under prior law, the exclusion amount of $10,000 per person per year was indexed for inflation after 1998, with a minimum increment of $1,000[13] (IRC Section 2503(b)). The annual exclusion increased for the first time, from $10,000 to $11,000, effective January 1, 2002. There is also an exclusion from the gift tax for qualified transfers of payments for tuition or medical expenses on behalf of another individual (IRC Section 2503(e)).

In addition, there is a special exclusion from the gift tax for contributions to qualified tuition programs (IRC Section 529). A contributor may give, on behalf of an individual beneficiary, up to five times the annual exclusion amount at one tim, but have the amount treated for gift tax purposes as divided over 5 years. As of 2002 this exclusion would cover a gift contribution to a qualified tuition program of up to $55,000 (five times the annual exclusion of $11,000), made in the first year of a 5-year period.[14] (Additional gifts to, or on behalf of, that beneficiary during the 5-year period would be subject to the gift tax.)

Unless covered by these exclusions, gifts from an individual to the same beneficiary, within a calendar year, that are in excess of the standard annual exclusion ($11,000 as of 2002) would be considered taxable gifts and counted against the donor's lifetime gift exemption of $1 million.

As under prior law, assets transferred as gifts continue to receive a carryover basis (the donor's adjusted basis) for the recipient. The carryover basis is used to calculate the capital gain, or loss, under the income tax when the gift is sold by the recipient. The carryover basis for gifts will continue in 2010, when the estate tax is repealed and assets transferred at death receive a modified carryover basis, and in 2011 and beyond, under either prior law or an extension of EGTRRA.

Retaining the gift tax is intended to help protect income tax revenues. H.R. 8, the *Death Tax Elimination Act of 2001*, which passed the House on April 4, 2001, would have repealed both the estate tax and the gift tax. Like EGTRRA, H.R. 8 created a potential capital gains tax liability for some heirs by replacing the step-up in basis with a carryover basis for assets transferred at death.[15] In discussions

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[13]Inflation-adjustments that are not exact multiples of $1,000 are to be rounded down to the next lowest multiple of $1,000.

[14]For further explanation of qualified tuition programs, and the tax treatment and restrictions on contributions to them, see CRS Report RL31214, *Saving for College Through Qualified Tuition (Section 529) Programs*, by Linda Levine, particularly the section on "Coordination of Contributions with Estate, Gift, and Generation-Skipping Transfer Taxes," p. 7-8.

[15]This is explained in the section below on "Step-up in Basis Replaced with Modified Carryover Basis for Inherited Assets in 2010 (Subtitle E)." For further explanation of the (continued...)

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surrounding the passage of H.R. 8, tax practitioners pointed out a strategy to reduce the income taxes due on the capital gains when the assets are eventually sold. Absent a gift tax, wealthy people could transfer assets during their lifetime, without tax cost, to friends and relatives in lower income tax brackets, who could sell the assets subject to a lower capital gains tax rate, and possibly no tax liability at all. The original owner could then receive back the proceeds from the other person's sale of the asset, through either gift or inheritance. In an effort to discourage this potential means of evading income tax liability on capital gains, EGTRRA retained the gift tax on transfers of assets in excess of $1 million during one's lifetime.

Generation-Skipping Transfer Tax Lowered, then Repealed

Under prior law, the generation-skipping transfer (GST) tax is levied, in addition to the estate tax, on amounts transferred, either indirectly or directly, to a "skip person." A skip person is a person assigned to a generation two or more generations below the transferor (a grandchild or more distant generation).[16] Each person transferring assets (transferor) has a cumulative exemption to allocate to generation-skipping transfers made either during life or at death. The GST tax is levied at a flat rate of tax equal to the maximum estate tax rate (55% under prior law), multiplied by the "inclusion ratio." The inclusion ratio that applies to a particular transfer of property reflects the amount of the total GST tax exemption allocated to that property.[17] The GST tax is levied on the value of the taxable property at the time of the taxable event (the transfer).

The GST exemption amount of $1 million was indexed for inflation after 1998. The GST exemption is $1,100,000 for 2002 and will be adjusted by the index for 2003, under prior law. Under provisions of EGTRRA, from 2004 through 2009, during the phasedown period, the exemption under the generation-skipping transfer tax will be the same as the applicable exclusion amount under the estate tax. Thus, the GST exemption is scheduled to rise to $1.5 million in 2004, $2 million in 2006, and $3.5 million in 2009. (See the middle column of **Table 2** earlier in the report.)

As under prior law, the tax rate on generation-skipping transfers will be the highest estate and gift tax rate in effect for the year of the transfer. Under EGTRRA, the maximum tax rate will decline, first to 50% for 2002 and then gradually to 45% for 2007-2009. (See the last column of **Table 2** and appendix **Table A.1**.)

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[15](...continued)
potential capital gains tax liability, see CRS Report RL30875, *Step-Up vs. Carryover Basis for Capital Gains: Implications for Estate Tax Repeal*, by Nonna A. Noto.

[16]An indirect skip occurs where the generation one level below the decedent (e.g., the decedent's son or daughter) receives some beneficial interest in the property before the property passes to the generation two or more levels below (e.g., the decedent's grandchildren). A direct skip occurs where the property passes directly to the generation two or more levels below the decedent. The GST tax applies to both types of transfers. For additional explanation, see CRS Report 95-416, *Federal Estate, Gift, and Generation-Skipping Taxes: A Description of Current Law*, by John R. Luckey.

[17]The inclusion ratio is explained in more detail in a footnote to the subsection near the end of this report on Modifications of Generation-Skipping Transfer Tax (Subtitle G).

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The generation-skipping transfer tax will be repealed in 2010, at the same time as the estate tax. The repeal of the GST tax is scheduled to sunset in 2011, with prior law being reinstated.

Other changes to the GST tax are described in the subsection near the end of this report on Modifications of Generation-Skipping Transfer Tax (Subtitle G).

Step-up in Basis Replaced with Modified Carryover Basis for Inherited Assets in 2010 (Subtitle E)

Under prior law, assets transferred at death receive a "step-up in basis."[18] This includes assets transferred to a spouse under the unlimited marital deduction.[19] The step-up treatment will continue to apply under EGTRRA during the phasedown period from 2002 through 2009. For the heir or recipient, the basis becomes the fair market value of the asset on the decedent's date of death (or the alternative valuation date, six months later, if the value was lower). For income tax purposes, when the heir sells the asset, the capital gain is calculated as the difference between the heir's selling price and the stepped-up basis of the asset as of the decedent's date of death. The step-up practice means, in effect, that the capital gain on the asset during the decedent's period of ownership is not subject to income taxation, for either the decedent or the heir. Only the capital gain (or loss) on the asset after the decedent's death is taxable to the heir when the heir sells the asset.

In contrast, assets transferred by gift, during the donor's lifetime, retain a carryover basis. The carryover basis is the decedent's adjusted basis – the decedent's acquisition cost with certain permitted adjustments, such as adding the cost of capital improvements or subtracting depreciation. The use of carryover basis for gifted assets remains unchanged under the new law.[20]

Under EGTRRA, when the estate tax is repealed in 2010, the step-up in basis provision for inherited assets will be repealed and replaced by a modified carryover basis. In 2010, assets transferred at death generally will be treated like assets transferred by gift, with certain exceptions. As with gifts, the carryover basis to the recipient of the asset will be the lesser of the decedent's adjusted basis or the fair market value of the property – on the date of the decedent's death. Unlike with gifts, however, a limited "basis increase" to the decedent's adjusted basis will be permitted for certain inherited property.

Basis Increase Allowances. EGTRRA provides two basis-increase allowances. An "aggregate basis increase" of $1.3 million is permitted per decedent. This $1.3 million limit may be increased by the amount of unused "built-in" losses associated with assets in the decedent's estate. These are losses that could have been

[18]IRC Section 1014, basis of property acquired from a decedent.

[19]Under the unlimited marital deduction, any assets left to a surviving (U.S. citizen) spouse are free from the estate tax at the time of the first spouse's death.

[20]For further explanation, see CRS Report RL30875, *Step-Up vs. Carryover Basis for Capital Gains: Implications for Estate Tax Repeal*, by Nonna A. Noto.

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claimed on the deceased person's income tax return, if he or she were still alive.[21] (In the case of a decedent who is a non-resident non-citizen – a non-resident alien – the aggregate basis increase is limited to $60,000 and the provision to add unused built-in losses and loss carryovers does not apply.) In addition, a $3 million basis increase is permitted for assets transferred to a surviving spouse.[22] Thus, $4.3 million in basis increase could be assigned to property transferred to a surviving spouse ($1.3 million plus $3.0 million).[23]

These basis-increase amounts are counted in addition to the decedent's adjusted cost basis in order to determine the maximum total basis for all of the appreciable assets[24] in the estate. For example, if the adjusted cost basis of the assets were $1 million, then $2.3 million in assets – $1 million plus $1.3 million – could be transferred to beneficiaries without any potential liability for income taxes on capital gains when the assets are sold. That is, the gross value of assets protected from possible capital gains income taxation to heirs is more than the $1.3 million and $3.0 million (spousal) basis-increase amounts.

The basis-increase limits of $1.3 million (per decedent), $60,000 (for non-resident aliens), and $3.0 million (for spouses) are indexed for inflation after 2010. The permissible inflation adjustment amounts are rounded down to increments of the nearest $100,000, $5,000, and $250,000, respectively.

The executor of the estate is given the responsibility for allocating portions of the basis increase or, alternatively, a strict carryover basis, to particular assets and, consequently, to particular heirs. Different heirs could thus receive assets with comparable current market value, but very different basis and consequently very different capital gains tax implications upon sale of those assets.[25]

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[21]The built-in losses include capital loss carryovers, net operating loss carryovers, and losses not compensated by insurance. The losses need not be assigned to the particular assets from which they originated. Rather, the aggregate dollar amount of these losses can be added to the total basis increase available to be allocated.

[22]Qualified spousal property includes both outright transfer property and qualified terminable interest property (QTIP). QTIP is property in which the surviving spouse has a qualifying income interest for life, but which passes to others when the second spouse dies, under terms set forth by first spouse to die. The new law also establishes rules relating to the treatment of jointly held property for purposes of the basis increase.

[23]The basis increase provisions in EGTRRA will hold most heirs harmless relative to prior law with respect to the amount of assets they may inherit free from either the estate tax or capital gains tax.

[24] Not all assets are appreciable and therefore candidates to receive part of the basis increase allowance. For example, bank accounts or U.S. savings bonds are not subject to a capital gain (or loss).

[25]For discussion of possible difficulties in administering a carryover basis regime, see: Stefan F. Tucker, "Thoughts on Radical Estate and Gift Tax Reform," Testimony before the Senate Finance Committee, Subcommittee on Taxation and IRS Oversight, March 15, 2001, *Tax Notes*, vol. 91, no. 1, April 2, 2001, 163-70; Joseph M. Dodge, "What's Wrong with

(continued...)

The basis of any particular asset may not be increased above its fair market value at the date of the decedent's death (the former stepped-up basis value). Assets not assigned any basis increase at all will receive their carryover basis – the lesser of the decedent's adjusted cost basis or the fair market value of the asset at date of death. In between are assets that receive some amount of the total basis-increase allowance, but not enough to bring their modified carryover basis up to their date-of-death fair market value.

Exclusion for Capital Gain on Principal Residence. In addition to the basis increase allowance, the income tax exclusion of up to $250,000 of capital gain on the sale of a principal residence is extended to the estate or person inheriting the decedent's residence. There is still a requirement that the property have been used as a principal residence for 2 or more years during the 5-year period before the sale, to qualify for the exclusion. If the decedent met the residency requirement before death, the exclusion may be claimed when the residence is sold by the estate or the heir. If the decedent had not met the residency requirement and if the heir takes occupancy of the property as a principal residence, then the decedent's period of occupancy may be added to the heir's subsequent period of occupancy to satisfy the 2-year residency requirement for the exclusion.

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Property Ineligible for Basis Increase. The new law enumerates several categories of property that may not receive a basis increase. These include property acquired by the decedent by gift within 3 years of death and the stock of several types of foreign investment companies.

In addition, the new law specifically provides that the basis-increase provisions "... do not apply to property which constitutes a right to receive an item of income in respect of a decedent under Section 691." One implication of this provision is that the basis increase allowance cannot be applied to assets that the decedent held in tax-deferred retirement plans such as traditional (not Roth) IRAs and 401(k) plans. As under prior law, heirs will owe income taxes on any assets they withdraw from these inherited plans. Furthermore, any withdrawals, including investment earnings from capital gains, will be taxed at the heir's ordinary income tax rate – not the lower capital gains tax rate.[26]

Reporting Requirements and Penalties for Failure to Report. The purpose of returns filed with the IRS will change. Under prior law, the emphasis is on determining the value of the taxable estate of the decedent. Under the new law in

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[25](...continued)
Carryover Basis Under H.R. 8," *Tax Notes*, vol. 91, no. 6, May 7, 2001, 961-73; Lee Sheppard, "Debt in Contemplation of Death," *Tax Notes*, vol. 91, no. 11, June 4, 2001, 1655-60.

[26]In general, withdrawals of capital gains from tax-deferred retirement accounts, whether during one's lifetime or by heirs after one's death, are taxed at ordinary income tax rates and not at the lower capital gains tax rate that applies to capital gains on assets held outside such accounts.

2010, the emphasis is on establishing the carryover basis for assets transferred at death.[27]

Under prior law, the executor of an estate with gross assets in excess of the applicable exclusion amount ($675,000 for 2001) is required to file an estate tax return (Form 706) with the Internal Revenue Service, whether or not the estate has a tax liability.[28] Under EGTRRA, the rules regarding filing an estate tax return will continue to apply during the phasedown period from 2002 through 2009 (to estates of decedents dying up to December 31, 2009). However, the filing threshold will rise to the much higher applicable exclusion amounts set by EGTRRA ($1 million in 2002 and 2003, rising in steps to $3.5 million in 2009). If the new law sunsets in 2011, the filing threshold would be $1 million in gross assets for 2011 and subsequent years, as scheduled under prior law.

Under EGTRRA, the language in Section 6018 of the IRC referring to estate tax returns is replaced by language on "Returns Relating to Large Transfers at Death."[29] For deaths occurring in 2010, when the estate tax is repealed, the executor of the estate (or the trustee of a revocable trust) is required to report to the IRS regarding all non-cash assets transferred at death – if the gross fair market value of the property (in the aggregate) exceeds $1.3 million. If the estate exceeds this threshold, all of the non-cash assets must be reported, even those assets whose capital gains will be shielded from future income taxation by the basis-increase allowances.[30]

Property that constitutes a right to receive an item of income in respect of a decedent (IRD) under Section 691 is not considered to be property acquired from a decedent for purposes of the carryover basis rules. Consequently, IRD property (including traditional IRAs and 401(k) plans) is not eligible for a step-up in basis (as previously explained) and need not be reported to the IRS on the Section 6018 return relating to large transfers.

The executor also must report to the IRS on appreciated property received by the decedent within 3 years of death which was required to be included on a gift tax return. (Such recently-gifted property is not eligible to receive a basis increase.) The Section 6018 return is to be filed with the decedent's last income tax return, unless a later date is specified in IRS regulations.

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[27]If it can be retrieved and matched, this basis information could be used to help the IRS determine the capital gains subject to income tax, if and when the asset is eventually sold by the heir.

[28]Over half of estate tax returns filed during the late 1990s were not taxable because eligible deductions reduced the value of the net taxable estate below the applicable exclusion amount.

[29]In certain other parts of the Code, references to the term "estate tax return" will be replaced by "section 6018 return."

[30]Different rules apply to the estates of non-resident aliens.

The executor must report the following information for each asset to the IRS:

- name and taxpayer identification number (TIN) of the recipient;
- accurate description of the property;
- adjusted basis for the property in the hands of the decedent and its fair market value at the time of death;
- decedent's holding period;
- sufficient information to determine whether any gain on the sale of the property would be treated as ordinary income;
- amount of basis increase (aggregate and spousal) allocated to the property; and
- any other information prescribed by the IRS.

If unable to file a complete return on a particular property, the executor is to include a description of the property and the name of every person holding a legal or beneficial interest in it.

Within 30 days of filing the return with the IRS, the executor is required to provide the same information in writing to the individuals receiving each property, along with the executor's name, address, and phone number.

There are penalties on the executor for failure to provide the required information to the IRS by the required date. The penalty for each violation is $10,000 for failure to report on the transfer of noncash assets at death; $500 for failure to provide the required information to the IRS on appreciated property acquired by the decedent within 3 years of death; and $50 for each failure to report the information to a beneficiary.

For gift transfers made during life, the donor is required to provide recipients of the property the information reported on the donor's gift tax return (including the property's fair market value and its basis). There is a penalty of $50 for each failure to provide information to recipients.

There is no penalty for a failure due to reasonable cause. However, if the failure to report is due to intentional disregard of the rules, then there is a penalty of 5% of the fair market value of the property at the date of the decedent's death or the time of the gift (for a lifetime gift).

Credit for State Death Taxes Phased Out, Replaced with Deduction (Subtitle D)

Under prior law, a limited tax credit was permitted against the federal estate tax for death taxes (including estate, inheritance, legacy, or succession taxes) actually paid to any state or the District of Columbia, on any property included in the decedent's gross estate. The maximum amount of the credit was determined based on the size of the decedent's adjusted taxable estate[31] in conjunction with a table of graduated tax

[31]For purposes of the state tax credit, the adjusted taxable estate is equal to the federal taxable estate minus $60,000.

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rates.[32] Under EGTRRA, a declining fraction of the prior state tax credit will be available for 2002-2004.

The state death tax credit is nonrefundable. It may only be claimed against the federal estate tax liability remaining after subtracting the unified credit from the tentative tax on the estate. Consequently, the credit only has value to estates with a net taxable value that is larger than the applicable exclusion amount in effect for the year of death ($675,000 in 2001, corresponding to a unified tax credit of $220,550; $1 million in 2002 and 2003, corresponding to a unified credit of $345,800, and rising through 2009 under EGTRRA).

In the aggregate, for estate tax returns filed in 1995 through 1998, claims for state death tax credits equaled approximately 20% of the federal tentative tax liability on estates before claiming the state death tax credit, with the federal government retaining the other 80%.[33, 34]

As a result of the dollar-for-dollar federal tax credit under prior law, there was no increase in the combined federal-state tax burden on an estate for state death taxes levied up to the maximum federal credit. Consequently, as of 2001, every state had at least a "pick-up" tax that enabled the state to take full advantage of the federal estate tax credit. In most states, the estate tax was equal to the federal credit. A few states have an independent estate or inheritance tax.[35] The laws of those states provide for the state tax liability to rise to the maximum federal credit if the tax liability under the state tax formula is lower. For some estates, the liability for the independent state tax could exceed the federal credit.

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[32]The rates range from 0.8% on the first taxable amounts, to 16.0% on amounts over $10,040,000. IRC Section 2011(b).

[33]Average nationwide percentages. Calculated by the Congressional Research Service from aggregate Internal Revenue Service data on net estate tax due before state credits, state death tax credits, and net federal estate tax after state credits, for estate tax returns filed in 1995-98. Data from: Barry W. Johnson and Jacob M. Mikow, "Federal Estate Tax Returns, 1995-97," Internal Revenue Service, *Statistics of Income (SOI) Bulletin*, Summer 1999, Tables 5a, 5b, and 5c, p. 118-20. Unpublished data for 1998 obtained from the authors.

[34]This is in reverse proportion to the value of the credit at the time of its last revision, in 1926. At that time, the credit for state death taxes was increased to 80 percent of the federal tax. This was implemented through the introduction of the rate structure for the state tax credit still present in Section 2011 of the IRC. Subsequently, federal estate tax rates were changed but the state tax credit was not and the relative value of the state credit declined. U.S. Congress, Joint Committee on Taxation, *Description and Analysis of Present Law and Proposals Relating to Federal Estate and Gift Taxation*, 107th Congress, 1st session, JCX-14-01, March 14, 2001, p. 12.

[35]As of 2001, 38 states and the District of Columbia provided that their only state death tax is a pick-up tax equal to the federal credit for state death taxes. Of that group, Louisiana and Connecticut have enacted laws to have a pure pick-up tax by 2004 and 2005, respectively. Ten of the remaining states have a separate inheritance tax and two a separate estate tax. Federation of Tax Administrators, Repeal of Federal Estate Tax Would Have Effect on States, FTA Bulletin B-07/01, Washington, February 22, 2001. Available on the FTA Web site [http://www.taxadmin.org/fta/rate/b-0701.html]

Under EGTRRA, the state death tax credit is phased out over four years, beginning in 2002. In 2002, the credit is 75% of its former level; in 2003, 50% of its former level; and in 2004, 25% of its former level. In 2005, the credit will be repealed and replaced with a deduction.

In states whose tax is specifically linked to the federal credit, the state tax would disappear in 2005 when the federal credit is repealed, unless the state enacted a new estate tax law.[36] States that already have independent tax structures may still have state death taxes after the repeal of the federal credit.

For most estates still facing state taxes, the combined federal-state tax bill would be higher with the deduction during 2005-2009 than with the prior credit. The deduction would reduce federal estate taxes in proportion to the estate's marginal tax rate. The maximum estate tax rate on taxable estate values above $2 million is 47% in 2005, 46% in 2006, and 45% in 2007-2009. These percentages are lower than the dollar-for-dollar reduction in federal taxes provided by the federal credit under prior law, and lower than the 75% credit available in 2002 and 50% credit in 2003 under EGTRRA, but higher than the 25% credit available in 2004.[37]

Estates with state tax bills in excess of the prior federal credit may receive some offsetting benefit from the deduction. For 2005-2009, estates may deduct their state taxes in full from the federal gross estate, not subject to the dollar limit of the former federal tax credit.

For estates not subject to the federal estate tax because they are smaller than the exemption amount, the deduction would be worthless, as would a credit. Likewise, the deduction for state taxes will be worthless to all estates when the estate tax is repealed in 2010. The prior-law credit for state death taxes would be reinstated if the provisions of EGTRRA sunset as scheduled in 2011.

Other Changes

EGTRRA made the following other changes in the tax code relating to estate, gift, and generation-skipping taxes. Like all other provisions in the Act, these are scheduled to sunset on December 31, 2010, with a return to prior law in 2011.

Conservation Easements (Subtitle F). Under prior law, a qualified conservation easement was geographically restricted to be in, or within 25 miles of, a metropolitan area, national park, or wilderness area, or in, or within 10 miles of, an Urban National Forest (IRC Section 2031(c)(8)(A)). Under provisions of EGTRRA, a qualified conservation easement may now be claimed with respect to any land

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[36]For additional information about state taxes, see CRS Report RS20853, *State Revenue from Estate, Inheritance, and Gift Taxes*, by Steven Maguire.

[37]For state taxes up to the federal credit amount, the increase in combined federal-state taxes (with the new deduction, in contrast to the prior credit) would be equal to the state taxes multiplied times one minus the federal marginal estate tax rate. For estates facing a marginal rate of 45% that would be 1.00-0.45= 0.55. That is, their combined federal-state tax bill would be higher by approximately 55% of the state tax bill.

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located in the United States or its possessions. The Act clarified that the values are the values as of the date of the contribution. These amendments took effect after December 31, 2000.

Modifications of General-Skipping Transfer Tax (Subtitle G). The modifications to the law on generation-skipping transfer taxes described in this subsection took effect after December 31, 2000. In general, these changes enhance the transferor's or trustee's ability to allocate the GST tax exemption in order to achieve an inclusion ratio of zero for assets transferred in indirect skips,[38] so that those particular assets are not subject to the GST tax.[39] The changes in the law under EGTRRA provided for:

- deemed allocation of the GST tax exemption to lifetime transfers (subject to the gift tax) made to GST trusts that are indirect skips (defined in the Act); an individual may elect not to have the automatic allocation rules apply by making that election on a timely filed gift tax return;
- retroactive allocation of the GST tax exemption is now permitted when there is an unnatural order of death;
- permission for a trustee to sever a trust holding property having an inclusion ratio of greater than zero but less than one into one trust with an inclusion ratio of zero, and another with an inclusion ratio of one, at any time; under prior law, the trust could not be severed after it had been created;
- modification of the rules determining the point in time in the transfer tax process at which the value of the inclusion ratio is determined;
- authorizing the IRS to grant extensions of time to allocate a GST tax exemption based on the value of the property at the time the transfer was made; under prior law this allocation had to be made on a timely filed gift tax return, otherwise, the value on the date of allocation had to be used; and
- substantial compliance with the requirements for allocating a GST tax exemption will suffice to establish that the exemption was allocated to a

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[38]An indirect skip occurs when the generation one level below the decedent receives some beneficial interest in the property before the property passes to the generation two or more levels below. For additional explanation, see CRS Report 95-416, *Federal Estate, Gift, and Generation-Skipping Taxes: A Description of Current Law*, by John R. Luckey.

[39]An inclusion ratio of zero means that no GST tax applies. An inclusion ratio of one means that no portion of the exemption is allocated to the particular transfer and the full tax applies. An inclusion ratio between zero and one means that that particular fraction of the GST tax applies.

In algebraic terms, the inclusion ratio is equal to 1 (one) minus the "applicable fraction" which is the ratio of (a) the dollar portion of the total available exemption allocated to that transfer, to (v) the value of the property transferred; that is, 1 - (a/v). The inclusion ratio becomes zero, and no tax applies, when a sufficient amount of exemption can be allocated to fully cover the value of the property transferred. That is, when a = v, then the applicable fraction is one (a/v = 1), and the inclusion ratio is zero [1-(a/v) = 1 - 1 = 0]. If no amount of the exemption is allocated to the particular property transfer, then a = 0, the applicable fraction is zero (0/v = 0), and the inclusion ratio is one (1 - 0/v = 1 - 0 = 1), and the full tax applies. In between are cases where the allocated exemption covers part of the property's value.

particular transfer or trust; then the transferor's unused GST exemption will be allocated to produce the lowest possible inclusion ratio; under prior law, there was no statutory rule regarding substantial compliance.

Extension of Time for Payment of Estate Tax (Subtitle H). EGTRRA increased from 15 to 45 the number of allowable partners and shareholders in closely held businesses, for purposes of the 15-year extension-of-time to pay the estate tax. In addition, the Act made a special installment payment method available to estates with interests in a qualifying lending and finance business (defined in the Act) by treating such a business as an active (not passive) trade or business company. The Act permitted those estates a 5- (not 10-) year installment payment plan but did not allow a 5-year deferral for principal. The Act also limited to 5 (rather than 10) years the number of estate tax installment payments permitted for holding company stock that is non-readily-tradable. These amendments to IRC Section 6166 applied to the estates of decedents dying after December 31, 2001.

Waiver on Statute of Limitations for Taxes on Certain Farm Valuations (Subtitle J). EGTRRA gave taxpayers one year from the date of enactment to be granted a refund or credit for overpayment of tax under IRC Section 2032A(c)(7)E which addresses renting the property to lineal descendants.

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Table A.1. Estate Tax Rate Schedule, 2002-2011

Taxable Estate Bracket		Calendar Year							
Over	**But Not Over**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007-2009**	**2010 Tax repealed**	**2011 & After (prior law, unless new law is extended)**
$ 0	$10,000	18	18	18	18	18	18	N/A	18
10,000	20,000	20	20	20	20	20	20	N/A	20
20,000	40,000	22	22	22	22	22	22	N/A	22
40,000	60,000	24	24	24	24	24	24	N/A	24
60,000	80,000	26	26	26	26	26	26	N/A	26
80,000	100,000	28	28	28	28	28	28	N/A	28
100,000	150,000	30	30	30	30	30	30	N/A	30
150,000	250,000	32	32	32	32	32	32	N/A	32
250,000	500,000	34	34	34	34	34	34	N/A	34
500,000	750,000	37	37	37	37	37	37	N/A	37
750,000	1,000,000	39	39	39	39	39	39	N/A	39
1,000,000	1,250,000	41	41	41	41	41	41	N/A	41
1,250,000	1,500,000	43	43	43	43	43	43	N/A	43
1,500,000	2,000,000	45	45	45	45	45	45	N/A	45
2,000,000	2,500,000	49	**49**	**48**	**47**	**46**	**45**	N/A	49
2,500,000	3,000,000	**50**	**49**	**48**	**47**	**46**	**45**	N/A	53
3,000,000		**50**	**49**	**48**	**47**	**46**	**45**	N/A	**55**
10,000,000	17,184,000	N/A	N/A	N/A	N/A	N/A	N/A	N/A	5% surtax

Source: CRS adaptation of estate and gift tax rate schedule under prior law adapted according to the information presented in Section 2001(c) of the Internal Revenue Code as of June 7, 2001. For 2011 and after, as well as 2001, Section 2001(c) of the Internal Revenue Code.

Notes: The maximum estate tax rate scheduled to take effect each year is highlighted in **bold type**. The two leftmost columns identify the level of taxable estate at which the reduction in the maximum marginal rate will take effect.

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Table A.2. Gift Tax Rate Schedule, 2002-2011

Taxable Estate Bracket		Calendar Year							
Over	But Not Over	2002	2003	2004	2005	2006	2007-2009	2010	2011 & After (prior law, unless new law is extended)
$ 0	$ 10,000	18	18	18	18	18	18	18	18
10,000	20,000	20	20	20	20	20	20	20	20
20,000	40,000	22	22	22	22	22	22	22	22
40,000	60,000	24	24	24	24	24	24	24	24
60,000	80,000	26	26	26	26	26	26	26	26
80,000	100,000	28	28	28	28	28	28	28	28
100,000	150,000	30	30	30	30	30	30	30	30
150,000	250,000	32	32	32	32	32	32	32	32
250,000	500,000	34	34	34	34	34	34	34	34
500,000	750,000	37	37	37	37	37	37	35	37
750,000	1,000,000	39	39	39	39	39	39	**35**	39
1,000,000	1,250,000	41	41	41	41	41	41	**35**	41
1,250,000	1,500,000	43	43	43	43	43	43	**35**	43
1,500,000	2,000,000	45	45	45	45	45	45	**35**	45
2,000,000	2,500,000	49	**49**	**48**	**47**	**46**	**45**	**35**	49
2,500,000	3,000,000	**50**	**49**	**48**	**47**	**46**	**45**	**35**	53
3,000,000		**50**	**49**	**48**	**47**	**46**	**45**	**35**	**55**
10,000,000	17,184,000	N/A	N/A	N/A	N/A	N/A	N/A	N/A	5% surtax

Source: For 2002-2009, CRS adaptation of estate and gift tax rate schedule under prior law adapted according to the information presented in Section 2001(c) of the Internal Revenue Code as of June 7, 2001. For 2010, Section 2502(a) of the Internal Revenue Code as of June 7, 2001.

Notes: The maximum gift tax rate scheduled to be in effect each year is highlighted in **bold type**. From 2002 to 2009, the reduction in maximum rate for the gift tax mirrors the estate tax, shown in **Table A.1**. In 2010, when the estate tax is repealed, the gift tax is retained, but its maximum rate is lowered to 35%. The taxable estate brackets in the two leftmost columns identify the level of gifts at which the reduction in the maximum marginal rate will take effect.

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For Additional Information

CRS Reports

CRS Report RL31092. *Calculating Estate Tax Liability During the Estate Tax Phasedown Period 2001-2009*, by Nonna A. Noto.

CRS Report RL30600. *Estate and Gift Taxes: Economic Issues*, by Jane G. Gravelle and Steven Maguire.

CRS Report 95-416. *Federal Estate, Gift, and Generation-Skipping Taxes: A Description of Current Law*, by John R. Luckey.

CRS Report RS20989. *Federal Estate, Gift, and Generation-Skipping Transfer Taxes: Modification, Phase Out and Repeal Under the Economic Growth and Tax Relief Reconciliation Act of 2001*, by John R. Luckey.

CRS Report 95-444. *A History of Federal Estate, Gift, and Generation-Skipping Taxes*, by John R. Luckey.

CRS Report RL30912. *H.R. 8: The Death Tax Elimination Act of 2001*, by Nonna A. Noto.

CRS Report RS20853. *State Revenue from Estate, Inheritance, and Gift Taxes*, by Steven Maguire.

CRS Report RL30875. *Step-Up vs. Carryover Basis for Capital Gains: Implications for Estate Tax Repeal*, by Nonna A. Noto.

Congressional Documents

U.S. Congress. House. *Death Tax Elimination Act of 2001. Report together with Dissenting Views to accompany H.R. 8*. H.Rept. 107-37, 107th Congress, 1st session, April 3, 2001.

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