Finding Themes in Ten Decades of Tax Law Changes

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Ronald D. Aucutt

Senior Fiduciary Counsel
Bessemer Trust
www.bessemer.com

Table of Contents

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Introduction

This paper focuses on five themes found in the tax law developments of interest to estate planners over the last ten decades – (1) grantor trusts, (2) the marital unit, (3) family businesses, (4) "unifying" or "aligning" various taxes, and (5) "repealing" (or just reducing) transfer taxes. It will note how those themes weave together and sometimes clash and will provide a context for framing questions about future changes in the current political environment.

1930s

Re-enactment of the Gift Tax: The gift tax was re-enacted by the Revenue Act of 1932, after the 1924 gift tax had held been unconstitutional in *Blodgett v. Holden*, 275 U.S. 142 (1927), because of its retroactive application.

Background – The Estate Tax: In the Revenue Act of September 8, 1916, as the United States was on the brink of entering World War I, Congress enacted the current estate tax, imposed at rates of 1 percent to 10 percent on taxable estates over $50,000. In the Act of March 3, 1917, the rates were generally increased by half, to levels of 1½ percent to 15 percent. In explaining the Senate bill, which would have doubled rates to 2 percent-20 percent, the Finance Committee stated:

> **Such a tax, when used as an emergency measure, is necessarily unequal in operation.** Only if continued at the same rate for many years – the period of a generation – does it become equal for all persons in like situation**. If levied as a war tax, that is, as a temporary emergency measure, it falls only upon the estates of those who happen to die during the period of the emergency.** Particularly is it to be remembered that perhaps a majority of those dying during the war and leaving estates to be taxed will be soldiers and sailors dying in defense of our country. **On the other hand, as a permanent measure, such a tax, even at the rates already fixed by existing law, trenches in considerable degree on a sphere which should be reserved to the States.**

S. REP. NO. 103, 65TH CONG., 1ST SESS. 14 (1917) (emphasis added).

In its version of the Revenue Act of 1926, when the gross rates ranged from 1 percent to 20 percent, the House of Representatives raised the state death tax credit to 80 percent of the basic tax (that is, with rates from 0.8 percent to 16 percent), while the Senate version would have repealed the estate tax. In support of repeal, the Finance Committee quoted the excerpts from its 1917 report that are shown in bold font in the quotation above. S. REP. NO. 52, 69TH CONG., 1ST SESS. 8 (1926). Thus, the Finance Committee in 1917 and 1926 seems to have cited the same arguments in support of **doubling** the tax and in support of **repealing** the tax! The 1926 House-Senate conference, of course, accepted the House approach.

Although the state death tax credit was set at rates from 0.8 percent to 16 percent (80 percent of the gross estate tax rates) in the Revenue Act of 2026, it was locked at the same rates when the overall federal estate tax rates were increased as World War II approached. Ultimately housed in section 2011 of the Internal Revenue Code, still with rates ranging from 0.8 percent to 16 percent, it remained unchanged until it was phased out by the 2001 Tax Act. Seventy-Five Years!

Grantor Trusts: The 1932 and 1934 Revenue Acts treated the income of a trust that the grantor could revoke, or from which income could be distributed to the grantor, as income of the grantor for income tax purposes (much like sections 676 and 677 of the current Code). (The value of such trusts would also be includible in the grantor's gross estate, so there was to that extent no mismatch between the income tax and the transfer tax.) Income distributable to the grantor's spouse was not included (as it now is in section 677(a)(1)), and interests of the grantor's spouse were not treated as held by the grantor (as they now are in section 672(e)).

In the famous case of *Helvering v. Clifford*, 309 U.S. 331 (1940), *rev'g* 105 F.2d 586 (8th Cir. 1939) *and aff'g* B.T.A. Memo. 1938-335, George Clifford's wife Virginia had "substantial means of her own," as the Board of Tax Appeals stated, which in 1934 meant she had about $13,000 of investment income. That put her in a 12 percent federal income tax bracket, whereas income of $50,000, for example, would have been in a 34 percent bracket. (The rate in the top bracket, over $1,000,000, was 63 percent.) In 1934, George created an irrevocable trust, which was to pay all the income to Virginia until it terminated after five years. Upon termination, all the undistributed income was to be paid to Virginia, and the remainder was to be returned to George. George paid a gift tax on his funding of the trust. Even though the trust was irrevocable and its income was not payable to George – the two explicit conditions in the 1932 and 1934 legislation – the Bureau of Internal Revenue (the predecessor of the IRS before 1953) sought to extend grantor trust treatment to the trust. The Board of Tax Appeals (the predecessor of the U.S. Tax Court before 1942) agreed with the IRS, the Court of Appeals for the Eighth Circuit disagreed, but the Supreme Court agreed with the Bureau of Internal Revenue and the Board of Tax Appeals, stating that "[s]ince the income remains in the family and the husband retains control over the investment, he has rather complete assurance that the trust will not effect any substantial change in his economic position."

Meanwhile, the Treasury Department issued regulations under the 1932 and 1934 statutes that extended their application to irrevocable trusts with a reversion to the grantor within 15 years. The regulations were commonly referred to as the "Clifford Regulations."

1940s

Unity of a Married Couple: Partial Marital Deductions: The Revenue Act of 1948 added (1) sections 51(b) and 12(d) of the Internal Revenue Code of 1939 (now section 1(a)) to allow income-splitting through the filing of joint returns, (2) section 1000(f) of the 1939 Code (now section 2513) to allow gift-splitting between spouses, (3) section 812(e) of the 1939 Code (now section 2056) to allow a marital deduction for estate tax purposes for the estate of a U.S. citizen or resident (then limited to one-half of the value of the adjusted gross estate), and (4) section 1004(a)(3)(A) of the 1939 Code (now section 2523) to allow a marital deduction for gift tax purposes for a U.S. citizen or resident (then also limited, in this case to one-half of the value of the gift).

One of the stated objectives was to achieve rough equality of treatment of estates and gifts between common law states and community property states, where the value of only the decedent's one-half share of community property is included in the decedent's gross estate. *See* H.R. REP. NO. 1274, 80TH CONG., 2D SESS. 26 (1948); S. REP. NO. 1013, 80TH CONG., 2D SESS. 27 (1948). That explains the limitation of the deductions to one-half of the value of the adjusted gross estate and one-half of the value of the gift. Moreover, because the operation of community property law was viewed as already providing the benefits intended to be provided by the marital deduction, no marital deduction was allowed with respect to community property.

Grantor Trusts Sequel: Ironically, the trust that the Bureau of Internal Revenue successfully imputed to the grantor in the Clifford case was apparently formed merely to shift some of one spouse's income to the other spouse so it would be taxed in a lower bracket for income tax purposes. The joint return provisions enacted in the Revenue Act of 1948 largely rendered such a purpose moot and apparently made such trusts unnecessary. Nevertheless, the grantor trust rules were retained and even expanded in the 1940s, and then largely codified in sections 671-678 of the Internal Revenue Code of 1954, which the reports of the House Ways and Means and Senate Finance Committees referred to as "'Clifford' type trusts" (with the 15-year reversion period reduced to 10 years, and later, in the Tax Reform Act of 1986, changed to the 5 percent test now found in section 673(a)). In other words, Congress in 1948 affirmed the purpose George Clifford had in creating his trust (by allowing joint income tax returns), but in 1954 expanded the grantor trust features that would defeat such a purpose, thus leaving the tax treatment of grantor trusts rather untethered and schizophrenic.

1950s

Grantor Trusts Again: As noted above, the Internal Revenue Code of 1954, in sections 671-678, generally codified the "Clifford Regulations." *See* "Internal Revenue Code of 1954," H.R. REP. NO. 1337, 83D CONG., 2D SESS. 63-64, A211-A217 (March 9, 1954); "Internal Revenue Code of 1954," S. REP. NO. 1622, 83D CONG., 2D SESS. 86-87, 364-372 (June 18, 1954). (Section 679, relating to foreign trusts with U.S. beneficiaries, was added by the Tax Reform Act of 1976.)

Family Businesses: The Technical Amendments Act of 1958 added to the Code subchapter S (permitting certain corporations to elect to be treated as passthrough entities) and the original version of section 6166 (permitting deferral of the payment of estate taxes in the case of family businesses). With regard to subchapter S, the Senate Finance Committee affirmed its support of small businesses, stating:

> [P]ermitting shareholders to report their proportionate share of the corporate income, in lieu of a corporate tax, will be **a substantial aid to small business**. … In this connection it should be noted that the President's Cabinet Committee on Small Business and the President in his budget message this last January recommended a general provision of this type **for the benefit of small business**.

"Technical Amendments Act of 1958," S. REP. NO. 1983, 85TH CONG., 2D SESS. 87 (July 28, 1958) (emphasis added).

1960s

Charitable Giving Reforms: The Tax Reform Act of 1969 famously included substantial reforms of the tax treatment of private foundations, other exempt organizations, and charitable contributions. These reforms were in large part motivated by and built upon a multi-volume Treasury Department work published barely two weeks after the inauguration of President Nixon. "Tax Reform Studies and Proposals, U.S. Treasury Department," Joint Publication of the House Committee on Ways and Means and Senate Committee on Finance, 91ST CONG., 1ST SESS. (Feb. 5, 1969), especially pages 295-309. That publication heavily reflected work that had been overseen by Assistant Secretary of the Treasury for Tax Policy Stanley Surrey during the Kennedy and Johnson Administrations, and its embrace by the Nixon Administration represented a significant degree of bipartisanship. The Tax Reform Act of 1969 was passed by overwhelmingly bipartisan votes of 381-2 in the House of Representatives and 71-6 in the Senate.

Family Businesses (This Time Farms): A Caveat: The Tax Reform Act of 1969 also identified and dealt with a dance between compliance and abuse that has been a source of tension in tax enforcement in many contexts. As noted above in the context of the enactment of Subchapter S in 1958, Congress has affirmed "small business" – family businesses – and has sought to protect them from some of the burdens that the tax law might otherwise impose on them. But at times, measures Congress takes to protect family-owned businesses, including family farms, can be used by taxpayers and their advisors to achieve tax benefits in non-business settings that Congress might not have contemplated (or, conversely, measures Congress takes to curb techniques it finds abusive can inadvertently burden family businesses). The variation of the first type of those unintended consequences that Congress saw in 1969 (in the context of the favorable treatment of farming) was described this way by the House Ways and Means Committee:

> The special farm accounting rules were adopted as a means of relieving the ordinary farmer of the bookkeeping chores associated with inventories and an accrual method of accounting. These rules, however, by combining the current deduction of expenses which are capital in nature with capital gains treatment on the sale of livestock or orchards have resulted in **a tax abuse which your committee does not believe should be allowed to continue**. These rules have allowed some high-income taxpayers who carry on limited farming activities as a sideline to obtain a tax loss (but not an economic loss) which is then deducted from their high-bracket, nonfarm income. Moreover, these tax losses often arise because of the deduction of capital costs which usually would reduce capital gains on the sale of farm property, but which instead are used to offset ordinary income.

"Tax Reform Act of 1969," H.R. REP. NO. 91-413, PART 1, 91ST CONG., 1ST SESS. 63 (Aug. 2, 1969) (emphasis added). The Senate Finance Committee added:

> The provisions of present law which allow the current deduction of soil and water conservation expenditures and land clearing expenditures, combined with the capital gains treatment which is allowed upon the sale of the farm land to which the expenditures relate, **make it possible for high-income taxpayers to make short-term, tax-motivated investments in farm land. These high-income taxpayers purchase farm land, make expenditures of this type in order to obtain current deductions against their high-bracket, nonfarm income, and then receive capital gain income when the farm**

land is sold, usually within a short period of time. Thus, these high-income taxpayers are able to convert their ordinary income into capital gain income.

"Tax Reform Act of 1969," S. REP. NO. 91-552, 91ST CONG., 1ST SESS. 105 (Nov. 21, 1969) (emphasis added).

Accordingly, Congress added more precise rules in section 1251 to curb such misuse. Indeed, the 1969 Act made many similar reforms, including adding to the Code section 183, dealing with **"activities not engaged in for profit" ("hobby losses")**. (Section 1251 was repealed in 1984 as "deadwood" that "no longer serves a meaningful function." "Tax Reform Act of 1984," H.R. REP. NO. 98-432, PART 2, 98TH CONG., 2D SESS. 1589 (March 5, 1984).)

For an example of the second type of unintended consequences mentioned above ("measures Congress [or Treasury and the IRS] takes to curb techniques it finds abusive [that] can inadvertently burden family businesses"), see "Another Family Businesses Update" about the proposed section 2704 regulations in the 2010s below.

Other Proposals: Treasury's "Tax Reform Studies and Proposals" also included a number of estate and gift tax proposals, which, although they generally were not picked up in the 1969 Act, were amazingly prophetic of future congressional action. The following list of estate and gift tax proposals (see "Tax Reform Studies and Proposals, U.S. Treasury Department" at 331-409) gives the date each proposal was eventually enacted by Congress or adopted by administrative action in some form:

Taxation of appreciation at death or at the time of gifts (carryover basis enacted in 1976, repealed in 1980, and enacted again in 2001, effective, if elected, only for 2010)

Unification of the gift and estate taxes:

Same rates (1976)

Same base – tax-inclusive (1976, for gifts within three years of death)

Single exemption (1976 – until 2004 – and again in 2011)

Abolition of the "gifts in contemplation of death" rule (1976)

Unlimited marital deduction, including income interests (1981)

Amendment of section 2039 to repeal the exclusion of interests in qualified retirement plans (1984)

More explicit rules governing disclaimers (1976)

An "orphan exclusion" equal to the amount of the gift tax annual exclusion multiplied by the number of years by which the orphan is under 21 (roughly in 1976 – repealed in 1981)

Tightening of the deduction rules for transfers to charity (1969)

More rational allocation of deductions between estate tax and income tax returns (in part by the "Hubert regulations," Reg. §§20.2013-4(b)(3), 20.2055-3(b) & 20.2056(b)-4(d), in 1999)

Tax on generation-skipping transfers (1976 and 1986)

Liberalized extended payment of estate taxes (section 6166) (1976)

Discontinuance of "flower bonds" redeemable at par to pay estate tax (last issued 1971, last matured 1998)

1970s

Employee Benefits. The Economic Retirement Income Security Act of 1974 (ERISA) was passed by votes of 407-2 in the House of Representatives and 85-0 in the Senate. Notably, the House Education and Labor Committee in the Democratic-controlled House of Representatives relied significantly on one of its Republican members, Representative Al Quie of Minnesota, for leadership in the drafting of the Act, simply because he had knowledge about the subject. Another bipartisan triumph.

Unification of the Gift and Estate Taxes; Addition of the GST Tax: The Tax Reform Act of 1976 was passed by votes of 383-26 in the House of Representatives and 84-2 in the Senate. It "unified" the gift and estate taxes, in effect making the estate tax calculation a continuation of the calculation of the gift tax with reference to cumulative gifts since 1977. In the course of that unification, it lowered the top rate from the World War II rate of 77 percent to 70 percent, and over five years (1977-1981) it phased in an increase of the $60,000 estate tax exemption (and thus also the $30,000 gift tax exemption, as the two taxes had become "unified") to an "exemption equivalent" of $175,625.

The "exemption equivalent" (known today as the "basic exclusion amount") thus began its role in the calculation of a "unified credit." To explain the introduction of a credit for gift and estate tax purposes, the Senate Finance Committee stated:

> [S]ince the present estate tax exemption is a **deduction** in determining the taxable estate, it results in a greater reduction at the estate's **highest estate tax brackets**. However, a **credit** in lieu of an exemption will have the effect of reducing the estate tax at the estate's **lower estate tax brackets** since a tax credit is applied as a dollar-for-dollar reduction of the amount otherwise due. Thus, at a given level of revenue cost, a tax credit tends to confer **more tax savings on small- and medium-sized estates**, whereas a deduction tends to confer more tax savings on larger estates. The committee believes it would be **more equitable** if the exemption were replaced with a credit rather than a deduction.

"Tax Reform Act of 1976," S. REP. NO. 94-938, PART 2, 94TH CONG., 2D SESS. 13 (July 20, 1976) (emphasis added). "Estate and Gift Tax Reform Act of 1976," H.R. REP. NO. 94-1380, 94TH CONG., 2D SESS. 15 (Aug. 2, 1976) was similar. This reasoning has essentially been **moot since 2006, when the exclusion amount became equal to (and since has exceeded) the beginning of the top rate bracket**. Nevertheless, it has continued to greatly complicate the preparation of gift tax and estate tax returns (with many pages of worksheets and instructions) and to create or aggravate unintended side effects such as the potential for "clawback" that was faced in 2011 and 2013 and now again in 2026. And going back to a simple "exemption" regime might create a burden of managing or blending two types of regimes over a very long transition period.

The 1976 Act also added to the Code, in a new chapter 13, the original version of the generation-skipping transfer tax. To explain the need for the GST tax as a back-up to the gift and estate taxes, the Senate Finance Committee stated:

> The purpose of the Federal estate and gift taxes is not only to raise revenue, but also to do so in a manner which has **as nearly as possible a uniform effect, generation by generation** (taking into account as the progressive rate structure does, the differences in the utility of assets according to the value held). These policies of revenue raising and equal treatment are best served where the transfer taxes (estate and gift) are imposed, on the average, at reasonably uniform intervals. Likewise, such policies are frustrated where the imposition of such taxes is deferred for very long intervals, as is possible, under present law, through the use of generation-skipping trusts.

S. REP. NO. 94-938, PART 2 at 19 (emphasis added). H.R. REP. NO. 94-1380 at 46 was similar.

The original chapter 13 used much of the same vocabulary as the current chapter 13 (including "taxable distribution" and "taxable termination"), but it provided for a very different calculation of the tax, designed to be "substantially equivalent to the estate or gift tax which would have been imposed if the property had actually been transferred outright to each successive generation." S. REP. NO. 94-938, PART 2 at 20. H.R. REP. NO. 94-1380 at 47 was similar. It pursued that objective by identifying a "deemed transferor," often the parent of the recipient of a taxable distribution or the parent of the successive beneficiaries of a trust after a taxable termination. The deemed transferor's gift or estate tax profile (including tax brackets determined with reference to the deemed transferor's previous adjusted taxable gifts, and taxable estate if the deemed transferor has died) would be used to calculate the GST tax, but the deemed transferor would not be liable for the GST tax.

Carryover Basis: The 1976 Act also included a rule for a carryover basis at death, effective January 1, 1977, with some exceptions and, notably, with a "fresh start" new basis as of December 31, 1976. Specifically, what was then enacted as section 1023(h)(1) provided that if a marketable bond or security was owned on December 31, 1976, and its market value on that date was higher than its adjusted basis immediately before the death of the decedent, then its adjusted basis for purposes of determining gain would be that December 31, 1976, market value. For all other carryover basis property, what was then enacted as section 1023(h)(2) provided, in effect, that if the holding period for an asset at a decedent's death included December 31, 1976, a fresh start basis would be determined by adding to the historical basis an amount of the appreciation in the value of the asset prorated on a daily basis for days in the holding period before January 1, 1977, compared to the total number of days in the holding period.

The effective date of the carryover basis rule was extended to 1980 in 1978, and section 1023 was repealed in 1980 (except when elected by an executor with respect to a decedent dying after December 31, 1976, and before November 7, 1978).

Family Businesses Update: The 1976 Act added to the Internal Revenue Code the special-use valuation rules in section 2032A for real estate used in a family farm or other family business, with a limit on the reduction in value of $500,000 (now $750,000, indexed for inflation since 1999, making it $1,390,000 in 2024). Somewhat echoing the Senate Finance Committee's affirmation of small businesses in 1958, the House Ways and Means Committee explained:

> Your committee believes that, when land is actually used for farming purposes or in other closely held businesses (both before and after the decedent's death), it is inappropriate to value the land on the basis of its potential "highest and best use" especially since **it is desirable to encourage the continued use of property for farming and other small business purposes**. Valuation on the basis of highest and best use, rather than actual use, may result in the imposition of substantially higher estate taxes. In some cases, the greater estate tax burden **makes continuation of farming, or the closely held business activities, not feasible** because the income potential from these activities is insufficient to service extended tax payments or loans obtained to pay the tax. Thus, the heirs **may be forced to sell the land for development purposes**. Also, where the valuation of land reflects speculation to such a degree that the price of the land does not bear a reasonable relationship to its earning capacity, your committee believes it **unreasonable to require that this "speculative value" be included in an estate** with respect to land devoted to farming or closely held businesses.

H.R. Rep. No. 94-1380 at 21-22 (emphasis added). S. Rep. No. 94-938, Part 2 at 15 was similar. Significantly, however, despite the family-business-friendly curb appeal of special-use valuation, the Ways and Means Committee acknowledged from the beginning that it does not really reduce the estate tax **on a family farm or business as such**; it merely prevents a windfall for the IRS in the form of a tax on a **speculative prospect of development** that is faced by such businesses unevenly.

Marital Deduction Update: The 1976 Act also increased the estate and gift tax marital deduction to give relief to "small- or medium-sized" estates. S. Rep. No. 94-938, Part 2 at 14. The limit on the estate tax deduction was increased to $250,000 for adjusted gross estates less than $500,000 – in other words, the deduction would be the greater of $250,000 or one-half of the adjusted gross estate – and it would apply to community property. A similar alternative $100,000 cap on cumulative gift tax marital deductions since 1977 was included. Those provisions quickly lost significance in light of inflation, and then became moot and were repealed by the Economic Recovery Tax Act of 1981, which removed the one-half limit on the marital deduction. In addition, the 1976 Act added section 2040(b) to the Internal Revenue Code to limit the value of a joint interest between spouses included in the gross estate to one-half of the value of the interest in certain cases.

Family Business/Marital Unity Blend: Two years later, the Revenue Act of 1978 added section 2040(c) to the Code, which provided that under certain circumstances the value for estate tax purposes of a joint interest between spouses in property used in the operation of a farm or other trade or business would be reduced to reflect the surviving spouse's contribution of personal services in the operation of that farm or other trade or business. Section 2040(c) was also repealed by the Economic Recovery Tax Act of 1981.

1980s

Return to Unity of a Married Couple: Making the Marital Deduction Unlimited: As noted above, the Revenue Act of 1948 had allowed a married couple to elect in effect to be treated as one unit for income tax purposes, Treasury's 1969 "Tax Reform Studies and Proposals" had called for an unlimited transfer tax marital deduction, and the 1976 and 1978 Acts had evidenced a growing congressional unrest with the treatment of transfers between spouses. The Economic Recovery Tax Act of 1981, which was passed by votes of 282-95 in the House of Representatives and 67-8 in the Senate, removed the 1948 one-half limitation on the gift and estate tax marital deduction. The Senate Finance Committee stated:

> The committee believes that a husband and wife **should be treated as one economic unit for purposes of estate and gift taxes, as they generally are for income tax purposes**. Accordingly, no tax should be imposed on transfers between a husband and wife.
>
> Moreover, the committee believes that the taxation of jointly held property between spouses is complicated unnecessarily. Often such assets are purchased with joint funds making it difficult to trace individual contributions.

"Economic Recovery Tax Act of 1981," S. REP. NO. 97-144, 97TH CONG., 1ST SESS. 127 (July 6, 1981) (emphasis added). The House Ways and Means Committee elaborated:

Although the committee recognizes that this additional tax [when property is taxed one-half at the first spouse's death and again fully at the second spouse's death] can be minimized through proper estate planning, it believes that an individual should be free to pass his entire estate to a surviving spouse without the imposition of any additional tax. For similar reasons, the committee believes it appropriate to permit unlimited lifetime transfers between spouses without the imposition of any transfer taxes.

> In addition, the committee believes that substantial simplification of the estate and gift taxes can be achieved by allowing an unlimited deduction for transfers between spouses. Under present law, it is often extremely difficult to determine the ownership of property held by the marital unit and to determine whose funds were used to acquire that property. These problems generally will not arise with an unlimited marital deduction.

"Tax Incentive Act of 1981," H.R. REP. NO. 97-201, 97TH CONG., 1ST SESS. 159 (July 24, 1981) (footnote omitted).

But making the marital deduction unlimited was not as simple as these committee discussions might suggest. At that time, to qualify for an estate tax marital deduction, for example, a bequest to the surviving spouse would have to be outright or would have to provide the surviving spouse with income with either a general power of appointment in the spouse (section 2056(b)(5)) or a transfer to the spouse or the spouse's estate at the spouse's death or earlier termination of the income interest (Reg. §20.2056(c)-2(b)(1)). No deduction was allowed for what section 2056(b) called "terminable interests." Thus, there was significant concern about the effect of the proposed legislation on blended families, which were becoming more common, because the spouse's control of the property, either through the power of appointment or by a testamentary direction, could disinherit the decedent's children and other descendants from a previous marriage. A "credit shelter" trust could avoid that result, but, although the exclusion amount that was sheltered by the unified credit was increased on a phased-in basis by the Economic Recovery Tax Act of 1981, it was still only $225,000 in 1982 (reaching only $600,000 in 1987).

Early in 1981, there was significant doubt that this concern for blended families would permit a significant increase in the marital deduction. By about April, a solution had been developed, in the form of the "qualified terminable interest property" election that was added in sections 2056(b)(7) and 2523(f) and which has now become so common. Ironically, however, because that election is available for the entire marital deduction (not just the additional marital deduction resulting from the removal of the one-half limit), it arguably enables a deceased spouse to provide the surviving spouse with less economic interest and control than had been provided for the one-half of the adjusted gross estate deductible before 1982. With many husbands predeceasing their wives and having more wealth than their wives, this could have been a significant women's-rights issue. But I do not recall hearing a single complaint about that, and it now seems to have comfortably settled into the transfer tax structure.

The 1981 statute and committee reports used the term "qualified terminable interest property" but not the acronym "QTIP." Ward Hussey, who began working for Congress in 1947 and was Legislative Counsel from 1972 until his retirement in 1989, was highly respected for his work on the Internal Revenue Code. I asked him after his retirement if he and his colleagues realized in 1981 that the acronym "QTIP" would emerge, and that it would remind everyone who heard it of Q-Tips® (the cotton swaps that had been around since the 1920s). He said "Yeah, we knew." Meanwhile, the Tax Reform Act of 1986 used "QTIP" in the title of section 2642(b)(4), and by the mid-1990s "QTIP" was in use in many Treasury regulations.

Rates and Exemption Equivalent: The 1981 Act increased the exemption equivalent of $175,625 to $600,000, with the increase phased in over six years (1982-1987). Likewise, it reduced the top 70 percent rate to 50 percent over a four-year period (1982-1985). But the Deficit Reduction Act of 1984 postponed the last drop in the rate until 1988, keeping the top rate at 55 percent in the meantime. The Revenue Act of 1987 further postponed that drop to 50 percent until 1993. (Ultimately, the Omnibus Budget Reconciliation Act of 1993 made the 55 percent rate permanent.)

Grantor Trusts Energized: Rev. Rul. 85-13, 1985-1 C.B. 184, held that, because a grantor trust is treated as owned by its grantor, a transfer of assets from the trust to the grantor for consideration is not a sale for income tax purposes, and therefore the grantor does not receive a new cost basis in the assets. The ruling acknowledged that *Rothstein v. United States*, 735 F.2d 704 (2d Cir. 1984), had reached the opposite conclusion with respect to a transaction that was in substance identical to the facts of the ruling, but it went on the say that the IRS would not follow *Rothstein*, without even an exception for cases arising in the Second Circuit. Thus, Rev. Rul. 85-16 itself was a rather aggressive **anti-taxpayer** ruling. Nevertheless, the notion of ignoring transactions between a grantor trust and its grantor opened up many uses of sales and notes that changed grantor trusts from an IRS tool into an estate planner's tool. *See* Letter Ruling 9535026 (May 31, 1995) (and subsequent rulings); and Michael D. Mulligan, "Sale to a Defective Grantor Trust: An Alternative to a GRAT," 23 ESTATE PLANNING 3, 8 (Jan. 1996). Thus, the tax treatment of grantor trusts remained untethered and schizophrenic.

GST Tax Rebooted: The Tax Reform Act of 1986, which was passed by votes of 292-136 in the House of Representatives and 74-23 in the Senate, replaced the 1976 GST tax. The Ways and Means Committee explained:

> The committee believes, as it stated when the generation-skipping transfer tax originally was enacted in 1976, that the purpose of the three transfer taxes (gift, estate, and generation-skipping) is not only to raise revenue, but also to do so in a manner that has as nearly as possible a uniform effect. This policy is best served when transfer tax consequences do not vary widely depending on whether property is transferred outright to immediately succeeding generations or is transferred in ways that skip generations. The committee determined that the present generation-skipping transfer tax is unduly complicated. Therefore, the committee determined that this tax should be replaced with **a simplified tax, determined at a flat rate**. The bill accomplishes the committee's goal of simplified administration while ensuring that transfers having a similar substantial effect will be subject to tax in a similar manner.

"Tax Reform Act of 1985," H.R. REP. NO. 99-426, 99TH CONG., 1ST SESS. 824 (Dec. 7, 1985) (emphasis added). The Senate bill did not include a GST tax provision. The "flat rate" chosen was the top estate tax rate, at that time 55 percent. The GST exemption was set at $1,000,000.

The Marital Unit and Grantor Trusts Blended: The Tax Reform Act of 1986 added section 672(e) to the Code, providing that for purposes of determining grantor trust status, any power or interest held by the grantor's spouse shall be treated as held by the grantor, unless they are legally separated or divorced.

1990s

Another Family Businesses Update: Under the heading of "Small Business Incentives," the Omnibus [Ominous?] Revenue Reconciliation Act of 1990 included a "revision of estate freeze rules," repealing section

2036(c) (which had been enacted in 1987) and adding chapter 14 (including section 2704, which was added by the House-Senate conference and therefore did not receive the vetting the other sections received).

Regulations under chapter 14 were proposed in PS-92-90, 56 FED. REG. 14321-14341 (April 9, 1991), and PS-30-91, 56 FED. REG. 46244-46252 (Sept. 11, 1991), and finalized in T.D. 8395, 57 FED. REG. 4250-4277 (Feb. 4, 1992).

Some Family Business Relief: The Taxpayer Relief Act of 1997 added to the Code section 2033A, providing an additional exclusion with respect to certain family-owned businesses. This provision was redesignated section 2057 in 1998 and ultimately repealed in 2014.

Rates and Exclusion Amounts; the Beginning of Indexing: As noted above, the Omnibus Budget Reconciliation Act of 1993 made 55 percent the permanent top estate and gift tax rate, as well as the GST tax rate.

The Taxpayer Relief Act of 1997 phased in an increase of the exemption equivalent from $600,000 to $1,000,000 over eight years (1998-2005). It also provided for indexing of the annual gift tax exclusion, the GST exemption, the cap on the reduction in value of a family farm or business under the special use valuation rules of section 2032A, and the special exclusion for family businesses in section 2033A it had added (as noted above). But the estate and gift tax exemption equivalent, and thus the unified credit, were not indexed.

Another Step in Unifying the Gift and Estate Taxes: The Taxpayer Relief Act of 1997 also added a new section 2001(f) to the Code to overrule case law (*Estate of Smith v. Commissioner*, 94 T.C. 872 (1990) (reviewed by the Court), *acq.,* 1990-2 C.B. 1) and extend the gift tax valuation finality rule of section 2504(c) to the estate tax calculation, once the statute of limitations has run on the gift. The Act also amended section 2504(c) to drop the requirement that a current gift tax must be paid to achieve this finality of valuation, thus extending the finality of valuation provided by that statute to gifts that merely use some or all of the donor's unified credit.

Congress coupled these welcome changes with an expanded section 6501(c)(9), providing that the statute of limitations does not begin to run, even on the valuation of the gift itself, unless the gift is "disclosed in such return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature of such item." (Previously, section 6501(c)(9) had applied only to transactions subject to the valuation rules of sections 2701 and 2702 enacted in 1990.) Implementing regulations (Reg. §301.6501(c)-1(f)) were proposed in 1998 and finalized in 1999.

2000s

Attempted Repeal of the Estate, Gift, and GST Taxes: In the summer of 2000, an election year, the "Death Tax Elimination Act of 2000" (H.R. 8) was approved by the House of Representatives by a vote of 279-136 and by the Senate by a vote of 59-39, but it was vetoed by President Clinton. H.R. 8 would have repealed the estate, gift, and GST taxes and replaced them with a carryover basis regime, beginning in 2010. For the period prior to repeal, it would have converted the "unified credit" to an exemption (to allow it to be applied to the top marginal rate rather than to lower rates) and would have provided reduced rates and increased exemptions on a phased-in basis.

Actual "Repeal" of the Estate and GST Taxes: The Economic Growth and Tax Relief Reconciliation Act of 2001 (the "2001 Tax Act") did enact a repeal of the estate and GST taxes, and President Bush did sign it. But, like H.R. 8 the year before, the repeal was not effective until 2010 and was also accompanied by a carryover basis regime that seemed more complicated and burdensome than what had been unsuccessfully tried in 1976 (including the omission of any "fresh start" basis as in 1976), and then it all sunsetted in 2011 (to comply with Senate budget reconciliation rules that prohibit most revenue losses beyond the relevant budget window, typically ten years). The omission of a "fresh start" not only differed from the 1976 legislation, but it contrasted starkly with the bipartisan 1969 proposal, which stated that "[o]nly appreciation occurring after the date of enactment would be subject to tax." "Tax Reform Studies and Proposals, U.S. Treasury Department," Joint Publication of the House Committee on Ways and Means and Senate Committee on Finance, 91ST CONG., 1ST SESS. 335 (Feb. 5, 1969). Meanwhile, the Act effectively "repealed" the estate tax for many estates by raising the exclusion amount from $675,000 in 2001 to $3.5 million by 2008, while "deunifying" the gift and estate taxes in 2004 (with exclusion amounts of $1 million and $1.5 million, respectively), and phasing out the state death tax credit and replacing it with a deduction by 2005.

The votes for the 2001 Tax Act were only slightly bipartisan – 240-154 in the House with only 28 Democrats voting for it and no Republican voting against it, and 58-33 in the Senate with only 12 Democrats voting for it and only two Republicans voting against it.

After his reelection in 2004, President Bush referred to the "political capital" that he had earned and intended to "spend." He also made it clear that one of the centerpieces of his domestic agenda was to make permanent the tax cuts enacted in his first term, including the repeal of the estate and GST taxes. Also in the 2004 election, the Republicans maintained control of the House and gained four seats in the Senate. Fifty-five was more Republicans than there had been in the Senate since Herbert Hoover was President. This gain in the Senate immediately triggered a lot of speculation about the new votes that might be available for making the repeal of the estate tax permanent.

The permanent repeal of the federal estate tax was placed before the Senate when, by a more or less bipartisan vote of 272-162 on April 13, 2005, the House approved the 109th Congress's version of H.R. 8 (the "Death Tax Repeal Permanency Act of 2005") to eliminate the 2011 "sunset" that limited repeal to just the year 2010. At the end of July 2005, just before the August recess, Senate Majority Leader Bill Frist of Tennessee filed a motion of "cloture" on H.R. 8, basically the Senate form of "calling the question," which requires approval of 60 Senators, scheduled for when the Senate reconvened after Labor Day.

By Labor Day, however, Hurricane Katrina had hit the Gulf Coast. Opponents of repeal of the estate tax asked how Congress could possibly consider huge tax cuts for the nation's wealthiest families when multitudes on the Gulf Coast had been left with nothing. Supporters of repeal asserted that more than ever the economy needed stability in tax policy, especially regarding the taxation of saving and investment that would be so important in the Gulf Coast rebuilding effort. But the pressures of dealing with Katrina had become too much for the Senate, and the estate tax vote was postponed.

On June 8, 2006, the Senate considered a cloture motion to take up H.R. 8, thus returning the debate to the posture that had been expected before the hurricanes of late August 2005. The motion was only to consider H.R. 8, not necessarily to approve it but possibly to replace it with a compromise like a $5 million exemption (indexed for inflation), a 15 percent rate, a second rate of perhaps 30 percent on taxable estates over, say, $30 million, and continued stepped-up basis for appreciated assets, all effective January 1, 2010. The vote was 57-41 in favor of cloture, three votes short of the necessary 60. (The two Senators who did not vote would have voted no.) Then, in the 2006 elections, Republicans lost control of Congress. It's impossible to be sure, but Hurricane Katrina may be the reason we have an estate tax today.

2010s

"Repeal" Redefined: On December 6, 2010, President Obama announced on national television that he and certain congressional leaders had agreed on "the framework of a deal" to permit the so-called "Bush tax cuts" to be extended for two years. The President reported that the agreement included an extension of the estate tax for two years – presumably 2011 and 2012 – with a $5 million exemption and a 35 percent rate.

On December 9, the Senate released the text of an amendment to implement the agreement announced by President Obama. The Senate approved it on December 15 by a vote of 81-19, the House approved it on December 17 by a vote of 277-148, and President Obama signed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 on December 17, 2010. It provided a postponement of the 2001 Tax Act sunset for two years until December 31, 2012, the addition of section 2001(g) (now section 2001(g)(1)) to avoid recapture ("clawback") of the gift tax saving if a gift were made and the delayed sunset did occur, an estate tax exemption of $5 million and top rate of 35 percent retroactively beginning January 1, 2010, an opportunity for executors of 2010 estates to elect out of the estate tax back into the 2010 carryover basis rules, a GST exemption of $5 million beginning in 2010, a GST tax rate of zero in 2010 and 35 percent beginning in 2011, a gift tax exemption of $5 million and top rate of 35 percent beginning in 2011, and indexing of the $5 million exemption for inflation beginning in 2012.

Another Tax Reduction, This Time Permanent, and a 368-Day Year: After weeks of public and private discussions, notably between President Obama and House Speaker John Boehner (R-Ohio), then between Senate Majority Leader Harry Reid (D-Nevada) and Minority Leader Mitch McConnell (R-Kentucky), and finally between Vice President Biden and Senator McConnell, an amendment to another bill that the House had passed in August 2012 (ironically numbered H.R. 8), was introduced in the Senate by Senators Reid and McConnell. The Senate debated it on New Year's Eve and passed it in the wee hours of New Year's Day by a bipartisan vote of 89-8. The House concurred in the Senate amendment late on January 1, 2013, by a vote of 257-167, with about twice as many Democrats as Republicans supporting it. President Obama signed the "American Taxpayer Relief Act of 2012," ("ATRA" or just the "2012 Tax Act"), into law on January 2, 2013. Seriously – an Act of 2012, enacted on the second day of 2013! (Congressional terms begin on January 3 of odd-numbered years.)

The compromise in the estate tax was generally to make 2011 and 2012 law permanent, but with a compromise rate of 40 percent (the midpoint between the 2012 rate of 35 percent and the 2009 rate of 45 percent). State death taxes are still deductible. Everything else in the 2012 law was made permanent. All "sunsets" were removed. In particular, the "exemption" – technically the basic exclusion amount for estate and gift tax purposes and the GST exemption for GST tax purposes – was $5 million, permanently indexed from 2011, permanently unified (the same for gift tax purposes), and permanently portable for gift and estate (not GST) tax purposes (as discussed below). That made the 2012 exemption $5,120,000, with indexing for future years, reaching $5,490,000 by 2017.

There was no "clawback." This was addressed for gift tax purposes in the flush language in section 2505(a)(2) and to some extent for estate tax purposes in section 2001(g) (now section 2001(g)(1)) (both of which were no longer sunsetted). But the real remedy for the feared clawback was simply that the exclusion amount did not go down in 2012.

Another Return to Unity of a Married Couple: Portability and Definition of Marriage: Meanwhile, the 2010 Act had further strengthened the unity of a married couple for transfer tax purposes by adopting portability for two years, in effect extending the concept of joint returns into the estate and gift tax context and the concept of gift-splitting into the estate tax context. The 2012 Act made portability permanent (with the technical correction of changing "basic exclusion amount" to "applicable exclusion amount" in section 2010(c)(4)(B)(i)). But portability was still not extended to the GST exemption.

In addition, Supreme Court decisions expanded the availability of the entire set of marriage-related tax benefits in *United States v. Windsor*, 570 U.S. 744 (2013), and *Obergefell v. Hodges*, 576 U.S. 644 (2015). Regulations to reflect the holdings of those cases were proposed in REG-148998-13, 80 FED. REG. 64378-64381 (Oct. 23, 2015), and finalized in T.D. 9785, 81 FED. REG. 60609-60617 (Sept. 2, 2016).

Another Family Businesses Update: Proposed regulations under section 2704 scared family businesses and appraisers in 2016. REG-163113-02, 81 FED. REG. 51413-51425 (Aug. 4, 2016). The objective of the proposed regulations was to change the valuation for transfer tax purposes of interests in a family-controlled entity that are subject to restrictions on redemption or liquidation – that is, subject to limitations on the ability of the owner of the interest to require the entity or other owners to redeem or buy out that owner.

The overall effect of section 2704(b) is that specified restrictions are disregarded in valuing such an interest for estate, gift, or GST tax purposes when that interest is transferred to a family member. Under the proposed regulations, the threshold element of the new type of disregarded restriction (like the "applicable restrictions" of the statute and the current regulations) would still have been the fact that after the transfer the restriction will lapse or can be removed by the transferor or any member or members of the transferor's family. Proposed Reg. §25.2704-3(b)(1). But instead of describing the **kinds** of such lapsing or removable restrictions that will be disregarded in making such valuations, the proposed regulations defined those restrictions with reference to the **effect** they could have on the ability of the holder of an interest to be redeemed or bought out. If the **effect** of a restriction on an interest in an entity is to limit the ability of the holder of that interest to compel liquidation or redemption of that interest on no more than six months' notice for cash or property equal at least to what the proposed regulations awkwardly, and ominously, called **"minimum value,"** then that restriction would be disregarded. "Minimum value" was defined as the pro rata share of the net fair market value of the assets of the entity – that is, the fair market value of those assets reduced by the debts of the entity (but only to the extent those debts would be deductible under section 2053 if they were claims against a decedent's estate), multiplied by the share of the entity represented by that interest.

While it was arguable that the proposed regulations were not aimed at, and would not have significantly affected, family-owned businesses, the proposed regulations were not very clear on that point, and many observers were unpersuaded. Apparently feeling the pressure, Treasury and the IRS withdrew the proposed regulations 14½ months after they were proposed. 82 FED. REG. 48779-48780 (Oct. 20, 2017).

Doubling Down by Doubling Up: Then of course the legislation commonly, but not formally, called the "Tax Cuts and Jobs Act" was approved by the House of Representatives by a vote of 227-203 on December 19, 2017, approved by the Senate by a vote of 51-48 early on December 20 and by the House again by a vote of 224-201 later on December 20 to approve changes made by the Senate. This time the votes were very partisan. In the House, no Democrat voted for it and only 12 Republicans voted against it. In the Senate, all the Republicans voted for it except Senator McCain, who was not in Washington, and all the Democrats voted against it.

The only change was to double the basic exclusion amount for estate and gift tax purposes and the GST exemption for GST tax purposes – as both the House version (through 2024) and Senate version (through 2025) would have done. In the final Act, the doubling of the exemptions was made to sunset January 1, 2026, as in the Senate version, to help the Senate comply with its complex budget reconciliation rules.

The Act retained section 2001(g), redesignated section 2001(g)(1), the "anti-clawback" language added by the 2010 Tax Act to prevent, in effect, gifts exempt from gift tax under the higher exemption from being nevertheless subject to estate tax if the increased exemption were to actually "sunset" – then in 2013 and now in 2026. This is a lesson the drafters learned after the awkward failure to address such a scenario in the 2001 Tax Act, although section 2001(g)(1) standing alone arguably is insufficient because it explicitly addresses only changes in rates, not changes in the exclusion amount. In fact, the statutory drafting was apparently so daunting in 2017 that Congress simply gave up and, in a new section 2001(g)(2), left completion of the task regarding changes in the exclusion amount to Treasury Regulations. Those regulations to prevent "clawback" were proposed in November 2018 (REG-106706-18, 83 FED. REG. 59343-59348, Nov. 23, 2018) and finalized in November 2019 (T.D. 9884, 84 FED. REG. 64995-65000, Nov. 26, 2019).

2020s

Recap of Notable Themes Over a Century: The following table tracks the recurrence and sometimes interaction of the five most notable themes in transfer tax changes over the past century:

	Grantor Trusts	Marital Unit	Family Businesses	"Unifying" or "Aligning"	"Repealing" (i.e., Reducing)
1930s	1932, 1934 Acts, *Clifford*			Gift tax revived	
1940s	*Clifford* (Sup. Ct.) "Clifford Regulations"	Joint income returns Marital deduction		With community property	
1950s	"Clifford Regs" codified		Sub S, §6166		
1960s			Abuses of farm rules		

	Grantor Trusts	Marital Unit	Family Businesses	"Unifying" or "Aligning"	"Repealing" (i.e., Reducing)
1970s		Slight increase in marital deduction	§2032A	Gift & estate tax Carryover basis	$175,625/70% Credit, not deduction
1980s	Rev. Rul. 85-13	Full marital deduction		Rebooted "simplified" GST tax	$600,000/55%
	Grantor's interests and powers include spouse's				
1990s			Chapter 14	Value: Statute of limitations	$1 million exclusion Indexing
2000s					"Repeal"
2010s		*Obergefell*, etc.; Portability (not GST)	Proposed §2704 regs.	Preventing clawback	$5 million/40% Then $10 million
2020s	"Align" with transfer tax? Overrule Rev. Rul. 85-13? Payment of tax a gift? Reimbursement a gift? Basis of trust assets?		"Exceptions" for family businesses? §2032A again?	"Align" transfer tax and grantor trust status? Limit duration of GST exemption?	"Sunset" of doubled ($10 million indexed) exclusion?

The rest of this analysis touches on the questions identified in the table for the 2020s.

Selected Proposals, Especially Related to Grantor Trusts: In the Biden Administration, we have seen an increase in proposals targeting estate planning techniques and outcomes. And many of them reflect the challenging themes that have marked the previous nine decades. One theme in particular is the role and treatment of grantor trusts (and other deemed-owned trusts under section 678) – recognition of gain on transactions between a grantor and grantor trust (as in the Administration's Fiscal Year 2023, 2024, and 2025 Revenue Proposals, popularly known as the "Greenbooks"), payment of income tax by the grantor on the trust's income as an additional gift to the trust (as in the Fiscal Year 2024 and 2025 Greenbooks), and the interrelationship, integration, and alignment of the income tax and transfer tax rules (as in the "Build Back Better" bill, H.R. 5376, approved by the House Ways and Means Committee on September 15, 2021).

That Ways and Means Committee proposal, which eventually was dropped from what the House passed on November 19, 2021, would have added a new section 2901 to the Code, simply providing that, as to any trust or portion of a trust that is not otherwise includible in the grantor's gross estate, (1) the value of such portion would be included in the grantor's gross estate for estate tax purposes, (2) any distributions from such portion during the grantor's life, other than distributions to the grantor or the grantor's spouse or in discharge of an obligation of the grantor, would be subject to gift tax, (3) all of such portion at any time during the grantor's life would be treated as a gift by the grantor if the grantor ceases to be treated as the owner of such portion for income tax purposes, and (4) those three results would all be adjusted, as appropriate, to account for any amounts previously treated as taxable gifts. Thus, the proposal would effectively prevent any "intentionally defective" grantor trust that permits the grantor to pay the income tax without subjecting the trust to estate tax upon the grantor's death. That proposal would apparently not apply to a trust deemed under section 678 to be owned for income tax purposes by anyone other than the grantor. The proposal went on, however, to provide that the status of anyone as a deemed owner of a trust (even under section 678) would be "disregarded" in determining the income tax treatment of "any transfer of property" between the trust and that deemed owner, effectively nullifying Rev. Rul. 85-13, 1985-1 C.B. 184, which the first proposal alone would probably have rendered moot in most cases anyway.

But it is not as simple to figure out what to do about grantor trusts in broader contexts that have broader objectives. For example, we have seen many proposals and heard much discussion about the "deemed realization" of the appreciation in assets that are the subject of gifts or are transferred at death, a concept that can be traced, as noted above, at least to 1969. The current surge of such proposals began on March 29, 2021, when Ways and Means Committee Member Bill Pascrell, Jr. (D-New Jersey) introduced H.R. 2286, described as a bill "to amend the Internal Revenue Code of 1986 to treat property transferred by gift or at death as sold for fair market value, and for other purposes." On the same day, Senator Chris Van Hollen (D-Maryland), joined by Senators Cory Booker (D-New Jersey), Bernie Sanders (I-Vermont), Sheldon Whitehouse (D-Rhode Island), and Elizabeth Warren (D-Massachusetts), issued a statement calling "the Stepped-Up Basis Loophole" "one of the biggest loopholes in the U.S. tax code, which subsidizes America's wealthiest heirs," citing a Joint Committee on Taxation estimate that it would cause a loss of $41.9 billion of tax revenue in 2021 alone. The statement was accompanied by a 32-page "discussion draft" of statutory language titled the "Sensible Taxation and Equity Promotion ("STEP") Act of 2021," with the acronym of "STEP" evidently designed to parody the "step-up" in basis that the statement condemned. Both proposals would generally treat any property transferred by gift or at death as sold for its fair market value on the date of the gift or death. Similar proposals later appeared in the Administration's Fiscal Year 2022 (May 2021) (pages 62-64), 2023 (March 2022) (pages 30-33), 2024 (March 2023) (pages 78-81), and 2025 (March 2024) (pages 79-82) Greenbooks.

All of those proposals would tax past appreciation, not just appreciation after enactment. Like the carryover basis provisions in the 2001 Tax Act, this contrasts with the 1969 proposed "Taxation of Appreciation of Assets Transferred at Death or by Gift," which stated that "[o]nly appreciation occurring after the date of enactment would be subject to tax." "Tax Reform Studies and Proposals, U.S. Treasury Department," Joint Publication of the House Committee on Ways and Means and Senate Committee on Finance, 91ST CONG., 1ST SESS. 335 (Feb. 5, 1969).

But it is in the way the proposals dance around grantor trusts that highlights the challenges any such proposals might face. All of the proposals specifically state that in general transfers of property into a trust would be recognition events. They provide exceptions, however, for certain grantor trusts, and here is where the analysis gets awkward. The congressional proposals would apply that exception to trusts "of which the grantor or another person is treated as the owner under subpart E of part I of subchapter J of chapter 1, and is includible in the gross estate of the grantor or such other person under chapter 11" (quoting H.R. 2286). The exception in the Greenbooks would apply to "a grantor trust that is deemed to be wholly owned and revocable by the donor." Why do the congressional proposals apply this exception to trusts treated as owned by someone other than the grantor/donor, but the Greenbook proposals do not? And why do the congressional proposals define this exception in terms of trusts that are "includible in the gross estate," but the Greenbook proposals requires that the trust be "revocable by the donor"? Many powers described in sections 673, 674, and 675 will cause the value of the trust assets to be "includible" in the grantor's gross estate, but do not necessarily make the trust "revocable."

While these distinctions may have very little practical significance in the end, because they might only create timing differences in the taxation of gain, it is still natural to wonder why there are two different formulations – why there is no consensus on the way grantor trusts should be described in the landscape of transfer taxes. It may only confirm the "untethered and schizophrenic" character the tax treatment of grantor trusts has had from the very beginning, as pointed out in the discussion about the reactions to the *Clifford* case in the 1940s.

Family Businesses: Other proposals in the last few years have also reflected themes that have been developing over several decades. In the same Greenbook proposals regarding deemed realization, there are proposals for an indefinite deferral of recognition of gain attributable to a family-owned and -operated business until that interest is sold or the business ceases to be family-owned and -operated. Because basis would not be stepped up in such a case, the postponed gain might continue to grow, and the latent liability could still affect the ability of the business, for example, to raise capital or obtain loans.

Similarly, a proposal in the Fiscal Year 2024 (pages 130-132) and 2025 (pages 134-136) Greenbooks regarding the valuation of partial and fractional interests in intrafamily transfers includes what purports be an exception for family businesses, but it is very awkwardly expressed, and in any event such an exception might not protect the business's ability to maintain capital reserves for possible expansion, modernization, or other extraordinary business expenses without seeing those reserves treated as "passive assets" that invite a tax liability.

And, again, both the Ways and Means Committee's "Build Back Better" proposals and the Fiscal Year 2024 (page 118) and 2025 (page 123) Greenbooks offer to expand the availability of special use valuation under section 2032A for real property used in a family farm or other family business, without acknowledging, or even appearing to realize, what the Ways and Means Committee acknowledged from the beginning: section 2032A does not really reduce the estate tax on a family farm or business as such; it merely prevents a windfall for the IRS in the form of a tax on a speculative prospect of development that is faced by such businesses unevenly. See "Estate and Gift Tax Reform Act of 1976," H.R. REP. NO. 94-1380, 94TH CONG., 2D SESS. 21-22 (Aug. 2, 1976), discussed above in the context of the 1970s.

Limiting the Duration of the GST Exemption. Like the Fiscal Year 2023 and 2024 Greenbooks, the Fiscal Year 2025 Greenbook (at page 125) muses that "[a]t the time of the enactment of the GST provisions, the laws of most States included a common-law Rule Against Perpetuities (RAP) or some statutory version of it requiring that every trust terminate no later than 21 years after the death of a person who was alive at the time the trust was created." The Greenbook (at pages 125-126) proposes to

> make the GST exemption applicable only to: (a) direct skips and taxable distributions to beneficiaries no more than two generations below the transferor [in other words, to the transferor's children and grandchildren, even if born after the creation of the trust], and to younger generation beneficiaries who were alive at the creation of the trust; and (b) taxable terminations occurring while any person described in (a) is a beneficiary of the trust.

Other Greenbook GST tax proposals would adjust a trust's inclusion ratio upon transactions with other trusts, ignore tax-exempt organizations as "non-skip persons" that prevent taxable terminations (for example, in a "health and education exclusion trust" or "HEET"), and treat loans to trust beneficiaries as distributions (carrying out distributable net income for income tax purposes and constituting, as appropriate, either a direct skip or a taxable distribution for GST tax purposes, subject to refund of GST tax upon final payment on the loan).

Selected Actions Taken: More on Grantor Trusts: Basis of Grantor Trust Assets at the Grantor's Death: In contrast to the significant recent proposals, there have been relatively few actual law-making developments in this decade. And it is hard to tell if there will be any significant law-making developments, especially soon.

"Guidance on basis of grantor trust assets at death under §1014" was new in the Treasury-IRS 2015-2016 Priority Guidance Plan (released July 31, 2015), but it was dropped in the 2021-2022 Priority Guidance Plan (released September 9, 2021). There was reason to assume that this guidance project was simply a clarification of the rules for foreign trusts. Compare Rev. Proc. 2015-37, 2015-26 I.R.B. 1196 (published in the Internal Revenue Bulletin on June 29, 2015, adding "[w]hether the assets in a grantor trust receive a section 1014 basis adjustment at the death of the deemed owner of the trust for income tax purposes when those assets are not includible in the gross estate of that owner" to the list of "areas under study in which rulings or determination letters will not be issued until the Service resolves the issue through publication of a revenue ruling, a revenue procedure, regulations, or otherwise") to Letter Ruling 201544002 (issued the next day, June 30, 2015, concluding that assets in a **revocable** trust created by **foreign** grantors for their U.S. citizen children would receive a stepped-up basis under section 1014(b)(2) at the grantors' deaths). One month later, "Guidance on basis of grantor trust assets at death under §1014" appeared on the Priority Guidance Plan, and it continued to appear on future Plans until 2021.

On March 8, 2022, Representative Pascrell, Chair of the House Ways and Means Committee's Oversight Subcommittee, wrote to Secretary of the Treasury Yellen to urge Treasury, as his office's contemporaneous press release put it, "to expand efforts to crackdown on tax abuse by wealthy families." His letter asserted that "[t]he most glaring loophole in today's income tax base is the ability of heirs to obtain tax-free stepped-up basis on appreciated assets they inherit upon the death of a taxpayer." Citing the recent deletion of the guidance project from the 2021-2022 Priority Guidance Plan, the letter went on to state that "[o]ne of those strategies is to claim stepped-up basis for assets in an irrevocable grantor trust upon the grantor's death." In a Ways and Means Committee hearing on June 8, 2022, Representative Pascrell raised this issue with Secretary Yellen, who responded that the guidance would be implemented "Very soon. Very soon."

On November 4, 2022, Treasury and the IRS issued their 2022-2023 Priority Guidance Plan (the first annual Plan after the June 2022 hearing), including a project described as "Guidance regarding availability of §1014 basis adjustment at the death of the owner of a grantor trust described in §671 when the trust assets are not included in the owner's gross estate for estate tax purposes."

On March 29, 2023, a little over a year after Representative Pascrell's March 2022 letter and almost ten months after the June 2022 committee hearing, the IRS released Rev. Rul. 2023-2, 2023-16 I.R.B. 658, which simply went through the list in section 1014(b) of circumstances that cause property to be "considered to have been acquired from or to have passed from the decedent" for purposes of the adjusted basis at death rule of section 1014(a) and found that a decedent's power over a trust that causes the decedent to be treated as the owner of the trust under the grantor trust rules but does not cause the value of the asset held by the trust to be included in the decedent's gross estate is not on that list. Therefore, the basis of that asset is not adjusted to fair market value at the decedent's death.

The facts in the revenue ruling include the curious details that (1) the asset it addresses was transferred to the trust in a transaction that was "**a completed gift** for gift tax purposes" and that at the grantor's death (2) the trust's **liabilities did not exceed the basis** of its assets and (3) neither the trust nor the grantor "held a **note** on which the other was the obligor," thus excluding, for example, installment sales to grantor trusts, one of the most common uses of grantor trusts in estate planning. Despite those obvious limitations, Representative Pascrell's office, on the same day, issued a press release that "praised fresh action by the U.S. Treasury Department and Internal Revenue Service to curb abuse of arguably the worst loophole in the entire federal tax code, so-called stepped-up basis," adding that "[t]his action follows prodding by Pascrell to issue this guidance."

Ironically, despite the publication of Rev. Rul. 2023-2 and the subsequent omission of this item from the 2023-2024 Priority Guidance Plan, the issue of "[w]hether the assets in a grantor trust receive a § 1014 basis adjustment at the death of the deemed owner of the trust for income tax purposes when those assets are not includible in the gross estate of that owner under chapter 11 of subtitle B of the Internal Revenue Code" remains on the list of "areas under study in which rulings or determination letters will not be issued until the Service resolves the issue through publication of a revenue ruling, a revenue procedure, regulations, or otherwise." Rev. Proc. 2024-3, 2024-1 I.R.B. 143, section 5.01(10). Perhaps that means that the IRS still plans to address the issue in the context of foreign trusts, or perhaps to address the application of Rev. Proc. 2024-3 without its limitations regarding a completed gift for gift tax purposes and liabilities in excess of basis and promissory notes between the trust and the grantor at the grantor's death.

But the entire scenario certainly supports the theory that Rev. Rul. 2023-2 was merely a tactic to calm a political storm and had little or nothing to do with intentional policy-making regarding grantor trusts.

Other Selected Developments: Other developments in the first part of this decade have included the following:

- New actuarial tables, based on 2010 census data, applied in regulations proposed on May 4, 2022 (REG-122770-18, 87 FED. REG. 26806-26848, May 5, 2022) and finalized on June 1, 2023 (T.D. 9974, 88 FED. REG. 37424-37466, June 7, 2023) with revisions, including, after public pushback, elective application back to May 1, 2019, when they were due under section 7520(c)(2)
- Proposed "anti-abuse" exceptions to the anti-clawback regulations (REG-118913-21, 87 FED. REG. 24918-24923, April 27, 2022)
- Proposed regulations to require discounting of claims and expenses, including interest, paid by an estate more than three years after the decedent's death and to tighten rules for the deductibility of interest in general (REG-130975-08, 87 FED. REG. 38331-38343, June 28, 2022)
- After many years of wrestling with syndicated conservation easements, attention to charitable contributions expanded to donor advised funds (Prop. Reg. §§53.4966-1 through -6, REG-142338-07, 88 FED. REG. 77922-77941, Nov. 14, 2023), and anticipatory assignment of income (*Hoensheid v. Commissioner*, T.C. Memo. 2023-34; *Keefer v. United States*, 130 AFTR 2d 2022-5002, *motion*

for reconsideration denied, 130 AFTR 2d 2022-5406 (N.D. Tex.); *cf. Dickinson v. Commissioner*, T.C. Memo. 2020-128)

- And, reprising again the troubled status of grantor trusts, an opinion from the IRS Chief Counsel's office (likely issued in the context of a case or cases under audit and possibly headed to litigation) concluding that trust beneficiaries have made a taxable gift, in an undetermined amount, by consenting to add to the terms of an irrevocable grantor trust a discretionary power in the independent trustee to reimburse the grantor for income tax the grantor pays on the trust's income (CCA 202352018, issued Nov. 28, 2023; released Dec. 29, 2023)

Questions for the Rest of the Decade and Beyond: In conclusion, with that background, it is possible to compile, but not to answer, a few key questions for the future:

Will the doubled basic exclusion amount (in effect a "repeal" of transfer taxes for many estates) escape or survive another sunset? If not, what will?

Will the income tax treatment of grantor trusts – in some respects in search of an anchor since its inception – become more synchronized with estate and gift tax treatment?

Will the valuation and other tax features of interests in entities continue to attract the attention of lawmakers, and will overreactions threaten the accommodation and encouragement of family businesses that Congress has historically affirmed?

Will charitable giving and exempt organizations get more attention from lawmakers?

Will the GST tax ever achieve its objective of raising revenue in a unform, generation-by-generation, manner – or be made portable to better acknowledge a married couple as an economic unit?

At the end of the decade, or at any time in the future, will the transfer tax and related income tax laws look like they were designed on purpose?