ACTEC

THE AMERICAN COLLEGE OF TRUST AND ESTATE COUNSEL

ADDRESSING TECHNICAL ISSUES RELATING TO THE ESTATE AND GST TAXES

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In February 2010, the Washington Affairs Committee of the American College of Trust and Estate Counsel ("ACTEC") presented congressional staff members a paper ("Issues Paper") outlining technical issues raised by the one-year suspension of the federal estate and generation-skipping transfer ("GST") taxes as provided by the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"). The basic theme of the Issues Paper was that statutory language written in 2001 creates many challenging problems in the context of a one-year statutory interruption of federal estate and GST taxes. This paper follows up with specific statutory suggestions for bridging that short-term gap in the clearest and least disruptive manner consistent with the policy judgments Congress has made and may make about these taxes.

ACTEC is a national professional association of approximately 2,600 lawyers elected to membership by their peers on the basis of professional reputation and ability in the field of trusts and estates and on the basis of having made substantial contributions to these fields through lecturing, writing, teaching, and bar activities. Fellows of ACTEC have extensive experience in rendering advice to taxpayers on matters of federal taxes, with a focus on estate and gift tax planning and compliance. ACTEC offers technical comments about the law and its effective administration, but does not take positions on matters of policy or political objectives.

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A. BACKGROUND OF THE PROBLEMS

In general, the practical problems for individuals and fiduciaries in interpreting and applying the changes made by EGTRRA in 2010 and 2011, including those identified in the Issues Paper, stem from two sources. The first source of problems is the uncertainty about what tax obligations and rules will apply in the future or might even be imposed retroactively to the present and whether and when that uncertainty might be resolved. This uncertainty will be eliminated or reduced by congressional action or, to some extent, by the passage of time even if Congress does not act. Any solutions will be provided by the judgments Congress makes about the level of transfer taxation. Other than acknowledging the general need for clarity, this paper does not address those judgments. For purposes of providing a fixed and objective framework (without recommendation or endorsement), this paper assumes that Congress will reinstate the estate and GST taxes, and possibly amend the gift tax, effective on or before January 1, 2011, with a limited retroactivity to January 1, 2010, and an executor of an estate of a decedent dying after December 31, 2009 will be able to elect current 2010 law, either as is or as modified. If Congress chooses a different outcome, these suggestions can be adapted.

The second source of problems is the "shall not apply" language of sections 2210(a) and 2664 applicable in 2010 and the "shall not apply" and "as if [EGTRRA] had never been enacted"

sunset language of section 901 of EGTRRA. The former suspends not only taxation in 2010 but also all of the definitions and rules that affect both the dispositions (*e.g.*, formula bequests) and the tax treatment (*e.g.*, the long-term GST tax profile) of estates and trusts. The sunset language creates uncertainty for 2011 and beyond. These two issues of statutory language are closely related, have common solutions, and will be addressed together in this paper. The 2010 "shall not apply" issues may appear moot if Congress acts in 2010 or even if we get to 2011 with no congressional action, but that language will still aggravate the uncertainty for 2011 and beyond if it is not addressed. Therefore, some of the suggestions in this paper will be necessary (perhaps as eventual "technical corrections" to EGTRRA) even if no action is taken regarding the level of tax.[1]

In that framework and spirit, the following congressional responses are suggested.

B. SUGGESTIONS FOR BRIDGING THE 2010 GAP: PROVIDE CLARITY FOR THE PERIOD WHEN THERE IS NO ESTATE OR GST TAX

1. ***Estate Tax.*** We encourage Congress to amend section 2210(a) to preserve the estate tax definitions and rules, even during any period that the estate tax is not imposed. Section 2210(a) currently reads "Except as provided in subsection (b), this chapter [the estate tax chapter] shall not apply to the estates of decedents dying after December 31, 2009." It could be changed to something like **"Except as provided in subsection (b), the tax computed under this chapter, after all credits allowed by this chapter, shall not be payable with respect to the estate of any decedent dying after December 31, 2009."**

    a. If feasible, it would be simpler and clearer if "after December 31, 2009" were changed to "after December 31, 2009, and before _____, 2010". Even if no action is taken in 2010 regarding the level of tax, it would be simpler and clearer to eventually amend section 2210(a) to "after December 31, 2009, and before January 1, 2011" or perhaps simply "in 2010".

    b. Subsection (b) provides special rules for distributions from QDOTs. It should be possible to simplify subsection (b), because there should be no need now for rules that purport to apply through 2020 when those rules terminate no later than January 1, 2011.

2. ***GST Tax.*** Similarly, we encourage Congress to amend section 2664 to preserve the GST tax definitions and rules, even during any period in which the GST tax is not imposed. Section 2664 currently reads "This chapter [the GST tax chapter] shall not apply to generation-skipping transfers after December 31, 2009." It could be changed to something like **"The tax imposed by section 2601 shall not be payable with respect to generation-skipping transfers after December 31, 2009."**

    a. Again, if feasible, it would be simpler and clearer if "after December 31, 2009" were changed to "after December 31, 2009, and before _____, 2010" or

[1] Although the details of the carryover basis rules in section 1022 also present technical issues, many of which might be addressed in regulations or other administrative guidance contemplated by section 1022(h), this paper is limited to the more comprehensive and more urgent estate, gift, and GST tax issues for which administrative guidance will not work and legislative attention is therefore crucial.

perhaps simply "in 2010". And, again, this action would eventually be needed even if Congress takes no action regarding the level of tax.

b. The reference is to "the tax imposed by section 2601," because, unlike the estate tax, the GST tax is imposed by only one section. This amendment could be reworded and placed in section 2601 itself, although it is doubtful that anyone affected by this amendment would not be aware of it and know how to find it.

c. The GST tax is also different from the estate tax in that it is imposed not only with respect to transfers from decedents but also with respect to (i) inter vivos transfers (direct skips), (ii) changes in the generation level of the beneficiaries of an ongoing trust by reason of a death (taxable terminations), (iii) other taxable terminations not involving a death, and (iv) taxable distributions from an ongoing trust. But the simple fix suggested seems to work for all cases. During 2010, in the case of a direct skip, the donor or executor will not have to allocate GST exemption to the transfer. In the case of a taxable termination or taxable distribution, where before 2010 the tax treatment would have been determined with reference to the inclusion ratio of the trust, that inclusion ratio would not be affected.[2]

3. ***Separate Steps and Severability.*** We encourage Congress to enact the above two actions separately (even if the provisions in question, as so amended, are immediately re-amended by the same Act) and explicitly make all steps and parts of the legislation severable. That should ensure the affirmation of the necessary landmarks of the estate and GST tax law, even, for example, if other legislative amendments are unclear, are subject to an election, or are even subject to judicial challenge. See the technical comments about retroactivity, elections, and interpretation of documents in part E below.

C. CONFORMING AND RELATED CHANGES

1. ***GST Exemption.*** We encourage Congress to amend sections 2001(c) and 2010(c) to provide the desired rate and exemption structure for the year 2010.

a. Congress would presumably do this in connection with any action establishing the level of the estate tax, but even if Congress does not address the level of the estate tax it will still be necessary to prescribe an "applicable exclusion amount" in section 2010(c) for the year 2010, because that is needed to determine the GST exemption amount under section 2631(c) for transfers made in the year 2010. (Alternatively, section 2631 itself could be amended to specify the GST exemption amount for allocations of GST exemption in the year 2010.)

b. If the GST exemption for 2010 or 2011 and beyond is lower than the pre-2010 $3.5 million GST exemption (either as a current congressional choice or because no change is made and pre-2002 law returns in 2011), then it is possible that some trusts have been allocated GST exemption in excess of the exemption available on a long-term basis, and the status of those trusts would be in doubt. See Issues

[2] For example, it is not contemplated that a trustee of a trust with an inclusion ratio greater than zero could treat a 2010 taxable distribution as coming entirely from the "taxable portion" (albeit excused from tax) so as to reduce the inclusion ratio of the trust.

Paper part D1. In that case, technical legislation would be needed to clarify (i) the effect of pre-2010 over-allocations, (ii) the remedies available to trustees to address such effects (such as "qualified severances" under section 2642(a)(3), which currently are not available after 2010 under section 901 of EGTRRA), and (iii) the post-2009 availability, if any, of GST exemption.

2. ***GST Tax Rate.*** We encourage Congress to amend section 2641(b) to clarify the GST tax rate applicable in 2010, or until the estate tax is reinstated. Section 2641(b) currently reads "For purposes of subsection (a), the term 'maximum Federal estate tax rate' means the maximum rate imposed by section 2001 on the estates of decedents dying at the time of the taxable distribution, taxable termination, or direct skip, as the case may be." This could be amended by adding something like **"without regard to section 2210"** at the end, or after "section 2001", or in some other appropriate place, perhaps in parentheses, or by setting forth the rate in section 2641(b) itself.

    a. Although this result might go without saying in light of the change to section 2210(a) suggested above, the clarification of the GST tax rate is so fundamental that it seems appropriate to make it explicit.

    b. If Congress chooses not to apply the GST tax during any period when the estate tax is unambiguously not applicable, then this change may not be necessary.

3. ***"Transferor," etc.*** We encourage Congress to amend sections 2612(c)(1) (defining "direct skip"), 2651(e)(1)(B) (relating to the predeceased parent rule), and 2652(a)(1)(A) (defining "transferor") by changing "tax imposed by chapter 11" to something like **"tax imposed by chapter 11 (without regard to section 2210)"**.

    a. The amendment to the definition of "transferor" in section 2652 is particularly important, because it appears that in the absence of such an amendment a generation-skipping trust created at death in 2010 has no "transferor," has no "skip persons," and is exempt from GST tax forever, regardless of amount and without the need for allocation of GST exemption. See Issues Paper part C. There appears to be no policy reason for that result.

    b. There are other references to the provisions of chapter 11 in the GST tax rules, such as references to the alternate valuation and special-use valuation rules of sections 2032 and 2032A (sections 2624(b) & (c) and 2663(1)), administration expenses deductible under section 2053 (section 2622(b)), charitable deductions under section 2055 (sections 2642(a)(2)(B)(ii)(II), (d)(2)(B)(i)(II), (e)(2)(A) & (e)(3)(B) and 2652(c)(1)(B) & (C)), the marital deduction under section 2056 (section 2652(a)(3)(A)), and the definition of "executor" in section 2203 (section 2652(d)). These references appear to be sufficiently clarified by the change to section 2210(a) suggested above, although individual amendments of each reference or a global provision covering all such references might be thought desirable. It might be questioned whether an alternate valuation date election for taxable terminations under section 2624(c) is appropriate if the estate tax does not apply (or is elected out of), but it seems both appropriate and workable, in the absence of a contrary policy judgment.

c. Similarly, the normal operation of the "nontaxable gift" rule in section 2642(c) (see Issues Paper part B3) and the "move down rule" in section 2653 (see Issues Paper part B2) in 2010 would be confirmed by the change to section 2210(a) suggested above.

4. ***Estate Tax Inclusion Period.*** We encourage Congress to amend the first sentence of section 2642(f)(3) to clarify that any suspension of the estate tax in 2010 will not by itself cause the close of an estate tax inclusion period ("ETIP") and permit the allocation of GST exemption to a trust that will become subject to estate tax again. The first sentence of section 2642(f)(3) currently reads "For purposes of this subsection, the term 'estate tax inclusion period' means any period after the transfer described in paragraph (1) during which the value of the property involved in such transfer would be includible in the gross estate of the transferor under chapter 11 if he died." This could be amended by adding something like **"(without regard to section 2210)"** after "chapter 11".

   a. A change of this sort is necessary if Congress does not intend to permit mid-term allocations of GST exemption to pre-2010 trusts that have been subject to estate tax and will be subject to estate tax again. It would reconcile the potential ambiguity created by the references to includibility in the gross estate "immediately after" the transfer and to "the close of the estate tax inclusion period" in section 2642(f)(1) and the reference to "any period" in section 2642(f)(3). See Issues Paper part D5. If the transferor actually dies during 2010, section 2642(f)(3)(B) provides that the ETIP closes at that time in any event.

   b. If Congress concludes that even a trust created in 2010 should be subject to the ETIP rules after 2010, then something like **"(without regard to section 2210)"** should be added after "chapter 11" in section 2642(f)(1)(B) also.

5. ***No 2010 Estate Tax Legislation.*** All the changes suggested in this part C are necessary to make the GST tax rules unambiguous and workable in 2011 and beyond and therefore would be appropriate even if no other changes were made to the estate tax.

D. OTHER NECESSARY OR DESIRABLE CHANGES

1. ***Section 2511(c).*** Congress should specifically consider the policy objectives, if any, that section 2511(c) should serve in the future and clarify, amend, or repeal it accordingly. See Issues Paper part E.

2. ***Other Changes in EGTRRA.*** Congress should make permanent the other provisions of Title V of EGTRRA, except in any case where it sees a policy reason otherwise.

   a. Those other provisions of EGTRRA (that is, provisions not dealing directly with the core policy issues of rates, exemptions, carryover basis, and effective dates) are section 551 (relating to conservation easements), sections 561, 562, 563, and 564 (relating to the allocation of GST exemption and to the inclusion ratio), and sections 571 and 572 (relating to the extension of time to pay estate tax under section 6166). See Issues Paper part H1.

   b. Such action would also solve most of the remaining continuity problems relating to the GST tax, including deemed allocations, late allocations, and qualified severances. See Issues Paper parts D2 through D4.

3. ***Relief from the Consequences of Uncertainty***

   a. As described in the Issues Paper (parts G and H2), the unprecedented uncertainty in federal transfer tax law, including uncertainty about both tax obligations and the identity of beneficiaries under formula dispositions, has prompted a number of remedies. These include state statutes,[3] court proceedings, and nonjudicial settlements, as well as use of more accessible but less flexible techniques such as disclaimers and spousal elections.

   b. Although the IRS is expected to be understanding in its view of such self-help and state-assisted measures, these unprecedented circumstances have created circumstances where beneficiaries and fiduciaries have to assume interpretation risks that go beyond what is historically "safe" by known and accepted standards of IRS review. The unintended and unwelcome consequences could include an indefinite marital or charitable bequest, gift or income tax consequences to beneficiaries viewed as redirecting or exchanging their interests, and uncertainty about the GST tax status of a trust.

   c. For those situations, Congress could help, for example, by directing the IRS to respect any interpretation or calibration of a decedent's estate plan or a donor's gift that is permitted by state law.[4]

   d. This help could be reinforced by explicit federal legislation to confirm that a **rescission** of a 2010 transfer or trust distribution in accordance with applicable state law on or before the due date (including extensions) of the gift tax return or other appropriate return for 2010 would not be regarded as a taxable gift or other transfer for purposes of subtitle B, even if the applicable state law requires the consent to the rescission or other affirmative act by the transferee and even if the transferee continues to be a beneficiary of the distributing trust or becomes a beneficiary of a trust that is an alternate transferee. Such legislation could probably be patterned after section 2518, without the detailed requirements of section 2518(b), but would apply only to rescission of transfers or distributions made in 2010 or in such shorter or longer period in which the meaning and durability of federal tax law were uncertain.

   e. Congress could also help by giving attention to the need for appropriate extensions of due dates for filing returns, paying tax, making relevant tax elections and allocations (including the allocation of GST exemption), and also

[3] States in which such statutes are known to have been enacted include Florida (H.B. 1237 and S.B. 998), Idaho (H.B. 472 enacted March 18, 2010), Indiana (S.B. 65 enacted March 12, 2010), Maryland (S.B. 337 enacted April 13, 2010), Minnesota (S.F. 2427 enacted May 13, 2010), Nebraska (L.B. 1047 enacted April 12, 2010), South Dakota (H.B. 1201 enacted March 11, 2010), Tennessee (S.B. 3045, enacted March 17, 2010), Utah (S.B. 121 enacted March 26, 2010), Virginia (H.B. 755 enacted April 7, 2010), Washington (S.B. 6831 enacted March 10, 2010), and Wisconsin (S.B. 670 enacted May 13, 2010). With some exceptions and variations, and with substantial differences in the Florida statute, a typical approach in these state statutes is to create a presumption that references to federal estate or GST tax law in formulas during the 2010 period in which those laws do not apply mean those laws as they applied on December 31, 2009, and/or to allow or expand access to state courts to determine whether the decedent would have intended a different result.

[4] An alternative approach is illustrated in the suggested legislative finding in paragraph (9) on pages 10-11.

taking less obvious but clearly relevant actions such as making qualified disclaimers under section 2518, including transfer disclaimers under section 2518(c)(3) where necessary.

f. Because such topics are not normally addressed in tax legislation, there may be compelling reasons to accompany such legislation with a broad grant of authority to Treasury to issue appropriate guidance.

E. TECHNICAL COMMENTS ABOUT RETROACTIVITY, ELECTIONS, AND INTERPRETATION OF DOCUMENTS

1. *Interpretation of Formula Clauses in Estate Planning Documents*

a. *The Model of the Economic Recovery Tax Act of 1981*

In the past, Congress has been sensitive to the effect of federal tax legislation on the application of formula dispositions in wills and trusts. For example, in enacting the unlimited marital deduction in the Economic Recovery Tax Act of 1981 ("ERTA") –

> "The Congress understood that many existing wills and trusts include a maximum marital deduction formula clause under which the amount of property transferred to the surviving spouse is determined by reference to the maximum allowable marital deduction. Because the maximum estate tax marital deduction under prior law was limited to the greater of $250,000 or one-half of the decedent's adjusted gross estate, the Congress was concerned that many testators, although using the formula clause, may not have wanted to pass assets valued at more than the greater of $250,000 or one-half of the adjusted gross estate (recognizing the prior law limitation) to the spouse—a result which might otherwise occur because of the enactment of an unlimited marital deduction. For this reason, a transitional rule provides that the increased estate tax marital deduction, as provided by the Act, does not apply to transfers resulting from a will executed or trust created before the date which is 30 days after the date of enactment (i.e., September 12, 1981), which contains a maximum marital deduction clause, provided that (1) the formula clause is not amended before the death of the decedent to refer specifically to an unlimited marital deduction and (2) there is not enacted a State law, applicable to the estate, which would construe the formula clause as referring to the increased marital deduction as amended by the Act."[5]

The transitional rule was in section 403(e)(3) of ERTA, which provided:

> "(3) If—
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> "(A) the decedent dies after December 31, 1981,
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> "(B) by reason of the death of the decedent property passes from the decedent or is acquired from the decedent under a will executed before the

[5] STAFF OF THE JOINT COMMITTEE ON TAXATION, GENERAL EXPLANATION OF THE ECONOMIC RECOVERY TAX ACT OF 1981 (H.R. 4242, 97th Cong; Public Law 97-34) 239-40 (JCS-71-81, Dec. 31, 1981), drawing from similar statements in S. REP. NO. 97-144, 97TH CONG., 1ST SESS. 128 (July 6, 1981) and H. REP. NO. 97-201, 97TH CONG., 1ST SESS. 163-64 (July 24, 1981).

date which is 30 days after the date of the enactment of this Act, or a trust created before such date, which contains a formula expressly providing that the spouse is to receive the maximum amount of property qualifying for the marital deduction allowable by Federal law,

"(C) the formula referred to in subparagraph (B) was not amended to refer specifically to an unlimited marital deduction at any time after the date which is 30 days after the date of enactment of this Act, and before the death of the decedent, and

"(D) the State does not enact a statute applicable to such estate which construes this type of formula as referring to the marital deduction allowable by Federal law as amended by subsection (a),

"then the amendment made by subsection (a) shall not apply to the estate of such decedent."

In short, in 1981, while the unlimited marital deduction was an important part of the legislation, it was withheld in cases where its application would have distorted an estate plan. Where the federal tax rule clashed with the integrity of the formula bequest, the federal tax rule yielded. Nevertheless, there are clear and material differences between the context of ERTA and the conditions faced today. First, ERTA was not retroactive; it was enacted August 13, 1981, and the marital deduction changes were effective January 1, 1982, giving individuals, in effect, an opportunity to elect the unlimited marital deduction by amending the formula as provided in subparagraph (C). Second, the marital deduction changes made by ERTA bestowed an unambiguous benefit, not the mixed (at best) outcome resulting from either carryover basis or a restoration of the estate tax, and therefore presented a simpler option. Third, the marital deduction changes in ERTA were important, but they did not represent the replacement of an entire tax system, thereby again presenting simpler choices. So while ERTA, like similar legislation over the years,[6] provides a precedent for "doing something" to relieve the burden of tax changes on tax-sensitive formula drafting, it is not a model that can simply be cut and pasted into 2010 legislation.

b. ***The Utility and Limitations of the Suggested Amendments***

In that light, the suggested amendment to remove the broad "shall not apply" cloak from the estate and GST tax chapters will go a long way toward restoring the framework in which many formula dispositions are drafted and many exercises of fiduciary discretion are determined. For a decedent's estate there will be a gross estate, an adjusted gross estate, a taxable estate, an applicable exclusion amount, a unified credit, and eligibility criteria relating to includibility, valuation, deductions, and other tax attributes. For generation-skipping dispositions, there will be a transferor, skip persons, and a GST exemption. The amendments suggested in parts B and C above will leave in place most of the variables that drafters of estate planning documents have come to rely on. For example, it is anticipated that a bequest of "the applicable exclusion amount" or "the largest value of the trust assets that can pass free of federal estate tax by reason of the unified credit" or "my unused GST exemption" will mean the same under the suggested

[6] *E.g.*, section 2002(d)(1)(B) of the Tax Reform Act of 1976.

amendment as it would have meant on December 31, 2009 (assuming that 2009 law is what Congress decides to use to fill in the gap).

What these amendments will not do is guarantee clarity and an appropriate outcome where, for example, instead of a bequest of "the largest value of the trust assets that can pass free of federal estate tax by reason of the unified credit," the governing instrument refers simply to "the largest value of the trust assets that can pass free of federal estate tax" or "the largest value of the trust assets that can pass to the _____ trust without incurring a federal estate tax." While the amendment preserves an amount that passes tax-free "by reason of the unified credit," it also produces an amount that passes tax-free in some other way, namely the entire balance of the estate.

The final challenge is posed by the possibility that Congress may empower the executor to elect between a taxable regime that makes formulas work and a carryover basis or other non-estate tax regime. This can be a tough burden to impose on a fiduciary whom the law requires to treat all beneficiaries impartially, especially when the election can change the interests of the beneficiaries under a "free of federal estate tax" formula.

While guidance and protection for fiduciaries is ordinarily a matter of state law, there arguably are more measures Congress could consider to help fiduciaries. As an illustration (not in any way intended as a recommendation), it would be possible to draft a statute under which, even if an executor elects "out" of a retroactively reinstated estate tax, the amended statute could provide a nominal estate tax of, say, the estate tax computed in the usual way divided by 100,000 or some other suitably large number. The idea would be to make "free of federal estate tax" and "free of federal estate tax by reason of the unified credit" mean the same thing, because there would be enough tax above the applicable exclusion amount to trigger the formula, but presumably not enough to provoke a constitutional challenge. But such an approach would be complicated and difficult to understand, and would likely be perceived as gimmicky and weird.

Alternatively, instead of amending section 2210(a) to read "Except as provided in subsection (b), the tax computed under this chapter, after all credits allowed by this chapter, shall not be payable with respect to the estate of any decedent dying after December 31, 2009," Congress could consider a variation such as **"With respect to the estate of any decedent dying after December 31, 2009, the credit allowed by section 2010 or 2102(b) shall be equal to the tax computed under section 2001 or 2101, after all other credits allowed by this chapter."** Such an amendment (which could also be made directly to sections 2010 and 2102(b)) would ensure that any amount that is "free of federal estate tax" is indeed free of federal estate tax "by reason of the unified credit." Because this approach would bias the disposition of an estate under a formula clause in favor of a "bypass" or "credit shelter" disposition – often a trust for the ultimate benefit of descendants – rather than a marital disposition, it would achieve a result that many would find optimal in the absence of a federal estate tax. In other cases, though, this approach might materially reduce or eliminate the surviving spouse's interest in a manner that is not as easy to address through post-mortem techniques such as disclaimers and therefore might be viewed as striking the balance in a riskier way.[7] And like the approach described in the preceding paragraph, this approach would be complicated and could be confusing.

[7] Significantly, the state legislatures that have addressed references to inapplicable federal estate or GST tax law in formula dispositions have generally chosen to strike the balance more conservatively by creating a presumption that

These are tough issues, there may be no easy answers, and in any event legislation that is ultimately agreed to should probably not be held up by an effort to find perfect solutions.

c. ***Perhaps the Best That Can Be Done***

Although the interpretation of estate planning documents is also a matter of state law, it cannot hurt, given the background of the current uncertainty, for Congress to try to do what it can. One option is the use of legislative findings to provide reassurance that Congress does not intend to disturb the operation of estate planning formulas. For example:

> "Congress finds and declares as follows:
>
> "(1) For many years drafters and users of wills and trusts have defined dispositions of interests in property with reference to federal estate tax terms and outcomes.
>
> "(2) The use of such formulas permits the disposition of assets, particularly at death, in a manner that best suits the needs and priorities of transferors and beneficiaries, consistently with the payment of tax obligations in a timely and orderly way.
>
> "(3) The ability of transferors and beneficiaries to rely on such formulas is important both to the maintenance of harmony among beneficiaries and to the public support for the tax system.
>
> "(4) Federal tax policy should be directed to collecting tax revenue and appropriately allocating the responsibility for that tax revenue, with the least possible interference with the legitimate expectations of transferors and beneficiaries regarding dispositive formulas.
>
> "(5) Neither the estate, gift, and generation-skipping transfer tax changes made in the Economic Growth and Tax Relief Reconciliation Act of 2001 nor the changes made in this Act are intended to disturb the disposition of estates and trusts or the legitimate expectations of beneficiaries regarding those dispositions.
>
> "(6) It best serves the ability to rely on dispositive formulas if the elements in the tax law that could affect the disposition of estates and trusts, as much as possible, change predictability from year to year.
>
> "(7) Congress recognizes that the interpretation and administration of wills and trust instruments, including dispositive formulas therein, is a matter of State law.
>
> "(8) Congress does not intend that changes in Federal tax law should necessarily result in differences in the identification and treatment of beneficiaries beyond the differences intended by transferors and decedents themselves and determined under State law.
>
> "(9) Congress intends that, to the extent permitted by sound tax administration, the Secretary of the Treasury administer this Act and the

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such references mean those laws as they applied on December 31, 2009. See footnote 3.

estate, gift, and generation-skipping transfer taxes in a manner that permits and encourages transferors, beneficiaries, fiduciaries, and State courts to interpret and administer wills and trust instruments, including dispositive formulas therein, consistently with these findings."[8]

Such clear signals in legislative findings would maximize the likelihood that state legislatures would close the gaps regarding both interpretations and fiduciary elections in a rational and helpful way, which occurred for the most part regarding the unlimited marital deduction after ERTA.

2. ***Retroactivity and Elections***

Whether any legislation should have a retroactive effective date is a policy judgment for Congress to make, as is any decision to mitigate retroactivity by providing elections, such as an executor's election between the current carryover basis and a reinstated estate tax. The following observations, however, seem relevant to both the choice of method and the details of making that choice most workable.

a. Application, for example, of 2009 law (including section 1014) in 2010 could avoid a tax increase for estates with a value less than $3.5 million but with significant holdings of appreciated assets.[9] For that reason and perhaps others, in any such election between the estate tax and carryover basis, the estate tax should be the default, with an opportunity to elect out of the estate tax into carryover basis. That would place the burden on those executors that are most likely to recognize the need for, and to be able to afford, the analysis needed to determine whether it would be beneficial to elect the carryover basis alternative.

b. An election that keeps the carryover basis rules of section 1022 on the books may require technical corrections, regulations, and other guidance, and will require the development of forms and instructions.

c. An election in the context of the estate tax would give relief from retroactivity to executors, who some would say most need it in the face of the involuntary act of death and the unique need, not generally faced by individuals and continuing trusts, to promptly identify beneficiaries and make distributions. Those who have taken inter vivos action in 2010 are viewed by some as intentionally taking advantage of an uncertain tax climate and by others as simply relying on the law as Congress wrote it. Proponents of all these views invoke principles of fundamental fairness.

d. An election between estate tax and carryover basis would appear administrable because of the general rule that when there is an estate tax there is a date-of-death value for all assets subject to the estate tax. Because the imposition of a gift or GST tax, standing alone, generally does not produce such adjustments to basis, it is less apparent how an election would be administered in the context of those taxes.

[8] As to this final bullet point, see part D3 above.

[9] Such a tax increase could also be avoided by increasing the general basis increase of section 1022(b) from $1.3 million to $3.5 million.

e. An exception is the GST tax on a direct skip occurring at death. Such GST taxes are typically computed and paid in connection with the payment of the estate tax, and the inclusion in the gross estate results in a basis step-up that could be traded for the election out of GST tax with roughly the same administrative ease.

f. Another exception is a taxable termination caused by the death of a trust beneficiary. An ongoing trust might not have as great a need as an executor for certainty, because it does not necessarily terminate upon a beneficiary's death or even if it does it would be rare that the identity and shares of trust beneficiaries would depend on tax-sensitive formulas. But in such a case there actually is a basis step-up (section 2654(a)(2)) and thus an election between the GST tax and the carryover basis would also appear to be administrable.

g. It might be argued that avoidance or mitigation of a retroactive increase in the gift tax rate is less necessary, because it would only be a rate change and not the revival of an entire tax system. On the other hand, because a mere change in the gift tax rate is less revolutionary than suspending the estate and GST taxes and generally does not create the structural and continuity problems identified above with respect to the estate and GST taxes, it might be argued that there has been even more reason to expect that change to survive and therefore more reason to protect the expectations of those who relied on it.

h. Elections are sometimes not as easy to administer as they are expected to be,[10] again suggesting the need for broad discretion in Treasury and the IRS and liberal relaxation of deadlines, interest, and penalties.

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[10] In the view of some, it took ten years, until the October 1991 revision of the estate tax return, to remove all of the kinks in the QTIP election for estate tax purposes enacted in ERTA in 1981.