[JOINT COMMITTEE PRINT]

DESCRIPTION OF S. 2967

RELATING TO

ESTATE AND GIFT TAXES

LISTED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON TAXATION AND DEBT MANAGEMENT GENERALLY

OF THE

COMMITTEE ON FINANCE

ON AUGUST 4, 1980

PREPARED FOR THE USE OF THE

COMMITTEE ON FINANCE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This pamphlet provides a description of S. 2967, relating to estate and gift taxes, scheduled for a public hearing on August 4, 1980, by the Senate Finance Subcommittee on Taxation and Debt Management Generally.

For each provision of the bill, the pamphlet contains a discussion of present law, the issues involved, an explanation of the provision, and the effective date. The estimated revenue effect for the bill is also contained in a table presented at the end of the pamphlet.

DESCRIPTION OF THE BILL

I. Unified Credit for Estate and Gift Taxes (sec. 2 of the bill and secs. 2010, 2505, and 6018 of the Code)

Present law

Prior to the Tax Reform Act of 1976, there was a $30,000 lifetime exemption for gift tax purposes and a $60,000 exemption for estate tax purposes.[1] The Tax Reform Act of 1976 combined the separate estate and gift tax rates into a unified transfer tax system. In addition, the 1976 Act converted the prior estate and gift tax exemptions into a unified credit. With the unified credit, the gift or estate tax is first computed without any exemption and then the unified credit is subtracted to determine the amount of gift or estate tax payable before the allowance of other credits.

The amount of the unified credit when fully phased in is $47,000.[2] With a unified credit of $47,000, there is no estate or gift tax on transfers of up to $175,625. Under the 1976 Act, the unified credit against the estate tax is phased in as follows:

Estates of decedents dying in—	Unified credit	Estate tax filing requirement based on gross estate [3]
1977	$30,000	$120,000
1978	34,000	134,000
1979	38,000	147,000
1980	42,500	161,000
1981 and thereafter	47,000	175,000

[3] Under the unified estate and gift tax system adopted under the 1976 Act, the gross estate filing requirement amount is reduced by taxable gifts made after 1976.

The amount of the unified credit for gift tax purposes is increased in the same manner.

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[1] Subject to death tax conventions concluded with foreign countries, an estate tax exemption of $30,000 was provided for estates of nonresident aliens. Special rules were also provided for estates of residents of possessions of the United States.

[2] For estates of nonresident aliens, the unified credit is $3,600 (Code sec. 2102(c)(1)). Special rules are provided for the estates of residents of possessions of the United States (Code sec. 2102(c)(2)) and estates of decedents who had been expatriated to avoid tax (Code sec. 2107(c)).

Issue

The issue is whether the amount of the unified estate and gift tax credit should be increased.

Explanation of provision

Under the bill, the unified credit would be increased over a 4-year period beginning in 1982 to $155,800. With a unified credit of this amount, there would be no estate or gift tax on transfers of up to $500,000.

The increase in the unified credit against the estate tax would be phased in as follows:

Estates of decedents dying in—	Unified credit	Estate tax filing requirement based on gross estate [3]
1982	$70, 800	$250, 000
1983	96, 300	325, 000
1984	121, 800	400, 000
1985 and thereafter	155, 800	500, 000

[3] Under the unified estate and gift tax system adopted under the 1976 Act, the gross estate filing requirement amount is reduced by taxable gifts made after 1976.

The amount of the unified credit for gift tax purposes would be increased in the same manner.

The provision would not increase the unified credit with respect to estates of nonresident aliens, residents of possessions of the United States, or decedents who had expatriated to avoid tax.

Effective date

Under this provision, the increases in the unified credit would apply beginning with respect to gifts made, or decedents dying, after December 31, 1981.

II. Marital Deduction (sec. 3 of the bill and secs. 2056 and 2523 of the Code)

Present law

Under present law, an unlimited gift tax marital deduction is allowed for transfers between spouses for the first $100,000 of gifts. Thereafter, a deduction is allowed for 50 percent of the interspousal lifetime transfers in excess of $200,000.

In addition, an estate tax marital deduction is allowed for the value of property passing from a decedent to the surviving spouse for the greater of $250,000 or one-half of the decedent's adjusted gross estate. This amount is adjusted by the excess of the amount of unlimited marital gift tax deduction over one-half of the lifetime gifts to the surviving spouse.

Under these provisions, transfers of community property or terminable interests generally do not qualify for either the gift or estate tax marital deduction.

Issue

The issue is whether an unlimited marital deduction should be allowed for both gift and estate tax purposes.

Explanation of provision

The bill would provide an unlimited marital deduction for both estate and gift tax purposes. The bill would not change the present law rule that transfers of terminable interests do not qualify for the marital deduction.

Effective date

This provision would be effective for decedents dying after December 31, 1981, in the case of the estate tax marital deduction, and for gifts made after December 31, 1981, in the case of the gift tax marital deduction.

III. Annual Gift Tax Exclusion (sec. 4 of the bill and sec. 2503(b) of the Code)

Present law

Under present law, an annual exclusion of $3,000 per donee is allowed with respect to gifts of present interests in property (Code sec. 2503(b)). For example, an individual may give five different individuals $3,000 each in cash and owe no gift tax.

The annual exclusion has equalled $3,000 since January 1, 1943. When the gift tax was first enacted under the Revenue Act of 1932, the amount of the annual exclusion was $5,000. The annual exclusion was reduced to $4,000 in 1938 and was then further reduced to its present $3,000 amount under the Revenue Act of 1942.

The annual exclusion serves to eliminate gifts of small value from the gift tax system. Thus, the principal rationale for the exclusion is based on administrative and taxpayer compliance concerns. However, it is sometimes contended that the annual exclusion operates to some extent as an incentive for transfers of wealth from older to younger generations.

A gift made by a husband or wife may, with the consent of both, be treated for gift tax purposes as made one-half by each (Code sec. 2513). The full annual exclusion is allowed with respect to each spouse's one-half share of gifts of present interests in property. Thus, in these cases, a donor may make up to $6,000 in excludable transfers to a donee during a calendar year.

Issue

The principal issue is whether the annual gift tax exclusion should be increased. If it is appropriate to increase the annual exclusion, the next issue concerns the amount to which it should be increased. Another issue is whether a special exclusion should be provided for certain consumption-type transfers when the payor is not legally obligated to support the beneficiary, e.g., voluntary payments of a relative's medical and educational expenses.

Explanation of provision

Under the bill, the gift tax annual exclusion would be increased to $6,000 per donee.

Effective date

The provision would apply to gifts made after December 31, 1981.

IV. Special Valuation of Farm or Other Business Real Property (sec. 5 of the bill and secs. 2032A and 1014 of the Code)

Present law

For estate tax purposes, real property must ordinarily be valued at its highest and best use. If certain requirements are met, however, present law allows family farms and real property used in a closely held business to be included in a decedent's gross estate at current use value rather than full fair market value, provided that the gross estate may not be reduced more than $500,000 (Code sec. 2032A).

To qualify for current use valuation: (1) the decedent must have been a citizen or resident of the United States at his death; (2) the value of the farm or closely held business assets in the decedent's estate, including both real and personal property (but reduced by debts attributable to the real and personal property), must be at least 50 percent of the decedent's gross estate (reduced by debts and expenses); (3) at least 25 percent of the adjusted value of the gross estate must be qualified farm or closely held business real property;[1] (4) the real property qualifying for current use valuation must pass to a qualified heir;[2] (5) such real property must have been owned by the decedent or a member of his family and used or held for use as a farm or closely held business for 5 of the last 8 years prior to the decedent's death; and (6) there must have been material participation in the operation of the farm or closely held business by the decedent or a member of his family in 5 years out of the 8 years immediately preceding the decedent's death (Code secs. 2034A (a) and (b)).[3]

The current use value of all qualified real property may be determined under the multiple factor method (Code sec. 2032A(e)(8)). The multiple factor method takes into account factors normally used in the valuation of real estate (for example, comparable sales) and any other factors that fairly value the property.

If there is comparable land from which the average annual gross cash rental may be determined, then farm property may also be valued

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[1] For purposes of the 50 percent and 25 percent tests, the value of property is determined without regard to its current use value.

[2] The term "qualified heir" means a member of the decedent's family, including his spouse, lineal descendants, parents, and aunts or uncles of the decedent and their descendants.

[3] In the case of qualifying real property where the material participation requirement is satisfied, the real property which qualifies for current use valuation includes the farmhouse, or other residential buildings, and related improvements located on qualifying real property if such buildings are occupied on a regular basis by the owner or lessee of the real property (or by employees of the owner or lessee) for the purpose of operating or maintaining the real property or the business conducted on the property. Qualified real property also includes roads, buildings, and other structures and improvements functionally related to the qualified use.

under the formula method (Code sec. 2032A(e)(7)(A)). Under the formula method, the value of qualified farm property is determined by (1) subtracting the average annual State and local real estate taxes for the comparable land from the average annual gross cash rental for comparable land used for farming, and (2) dividing that amount by the average annual effective interest for all new Federal Land Bank loans.[4]

On July 19, 1978, the Department of the Treasury issued proposed regulations describing the circumstances under which current use valuation would be available and defining gross cash rental under section 2032A. Under the proposed regulations, the current use value was to be available only if there were some nonfarm use for the property. The proposed regulations also provided that if no comparable farm property had been leased on a cash basis, then the formula method could be applied by converting crop share rentals into cash rentals. If the crops were sold for cash in a qualified transaction, the selling price would be considered the gross cash rental. If no qualified sale occurred, then the gross cash rental would equal the cash value of the crops on the date received on an established public agricultural commodities market.

On September 10, 1979, the Department of the Treasury withdrew the proposed definition of gross cash rental and published another proposed regulation defining gross cash rental.[5] The new proposed regulation provides that crop share rentals may not be used under the formula method. Consequently, under the proposed regulation, if no comparable land is rented solely for cash, the formula method may not be used and the qualified farm property may be valued only by the multiple factor method. The Internal Revenue Service also issued on that date a news release indicating that current use value would be available with respect to any real property which satisfied the requirements of section 2032A, even if there were no other highest and best use for the property.

If, within 15 years after the death of the decedent (but before the death of the qualified heir), the property is disposed of to nonfamily members or ceases to be used for farming or other closely held business purposes, all or a portion of the Federal estate tax benefits obtained by virtue of the reduced valuation will be recaptured. A "cessation of qualified use" occurs if (1) the qualified property ceases to be used for the qualified use under which the property qualified for current use valuation or (2) during any period of 8 years ending after the date of the decedent's death and before the date of the death of the qualified heir, there have been periods aggregating 3 years or more during which there was no material participation by the qualified heir or a member of his family in the operation of the farm or other business (Code sec. 2032A(c)(7)).

The recapture provisions apply not only where the qualified real property is sold (or exchanged in a taxable transaction) to nonfamily members, but also where the property is disposed of to nonfamily members in a tax-free exchange, for example, a like-kind exchange under section 1031. If, however, an involuntary conversion of qualified real property occurs and the cost of qualified replacement property equals

[4] Each average annual computation must be made on the basis of the five most recent calendar years ending before the decedent's death.

[5] 44 Fed. Reg. 52,696 (1979).

or exceeds the amount realized on the conversion, then, in general, the adjusted tax difference will not be recaptured as a result of the involuntary conversion (Code sec. 2032A(h)). Under present law, the special rules for involuntary conversions apply only if the qualified heir makes an election in accordance with section 2032A(h)(5).

The maximum amount subject to recapture, the "adjusted tax difference," is the excess of (1) the estate tax liability which would have been incurred had the current use valuation provision not been utilized over (2) the estate tax liability based on the current use valuation provisions (Code sec. 2032A(c)(2)). In general, if a recapture event occurs within 10 years of the decedent's death, the amount of the additional or "recapture" tax imposed with respect to the interest shall be an amount equal to the lesser of (1) the adjusted tax difference attributable to this interest or (2) the excess of the amount realized with respect to the interest over the value of the interest determined with the current use valuation.[6] If the recapture event occurs more than 10, but less than 15, years after the decedent's death (but prior to the death of the qualified heir), the amount subject to recapture is reduced on a monthly basis (Code sec. 2032A(c)(3)).

Under present law, where special use valuation is elected, the basis of the property in the hands of the estate or qualified heir is the special use value, instead of its full fair market value (Code sec. 1014 (a)(3)).

Issues

The issues presented by this section of the bill include the following:

(1) Whether relief from the material participation requirement should be given where the decedent was retired or disabled.

(2) Whether special valuation should be made available to property which was not owned and used as a farm by the decedent for a substantial period before his death where the surviving spouse actively manages the property after the death of the decedent.

(3) Whether a less restrictive standard of involvement by the decedent in the operation of the land prior to his death should apply in the case of woodlands.

(4) Whether the estate tax benefit recapture period under section 2032A should be reduced from 15 years to 10 years.

(5) Whether the recapture of tax benefit can be avoided by having an agent of the qualified heir actively manage the property where the property is used for farm purposes or, in all other cases, where the qualified heir is a spouse, a minor, a student, or disabled.

(6) Whether the $500,000 limitation on the reduction of the value of the decedent's gross estate under section 2032A(a)(2) should be repealed.

(7) Whether certain like-kind exchanges should not trigger recapture of estate tax benefits under section 2032A, or trigger the recapture of only a proportionate amount of the estate tax benefits.

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[6] In cases where there is a cessation of qualifying use or a sale or exchange at other than arm's length, the amount of the additional tax imposed will be the lesser of (1) the adjusted tax difference attributable to the interest or (2) the excess of the fair market value of the interest over the current use valuation.

(8) Whether an election should be required to secure the benefits of the special rules for involuntary conversions in section 2032A(h).

(9) Whether qualified farm property may be valued under the formula method in section 2032A(e)(7)(A) by converting net crop share rents to cash if no comparable land is leased solely for cash and comparable land is leased partially or completely on a crop share basis.

(10) Whether the basis of property with respect to which there has been recapture of the estate tax benefits should be increased to its fair market value on the date of the decedent's death.

Explanation of provision

This provision would make several modificaions to the rules relating to the special valuation of farm and other business real property for estate tax purposes.

First, the bill would provide that the material paricipaion requirement for qualification for special use valuation need only be met until the date upon which the decedent retires or becomes disabled.

Second, the bill would provide an "active management" qualification test, rather than a material participation test, with respect to farm or other business real property included in the gross estate if the property had been inherited from a spouse and had qualified for special valuation in that spouse's estate. "Active management" is defined to mean the making of the management decisions of a business, other than the daily operating decisions.

Third, in the case of woodlands, the bill would provide that qualification for special valuation can be attained if the decedent or a member of his family is engaged in the "active management" of the woodlands for the 10-year period prior to his death.

Fourth, the period during which the adjusted tax difference could be recaptured would be reduced from 15 years to 10 years. The current rules applicable after the tenth year would be repealed.

Fifth, the bill would provide that recapture of the tax benefits would not occur where an agent of the qualified heir engages in the active mangement of the property in the case of all farming property or where the qualified heir was a surviving spouse of the decedent, a minor, a student or is disabled in the case of other property.

Sixth, the $500,000 limit on the reduction of the decedent's gross estate would be repealed. Consequently, the current use value, computed under section 2032A, would be substituted on the estate tax return for the full fair market value.

Seventh, the bill would expressly provide that an exchange pursuant to section 1031 of the qualified real property solely for real property to be used for the same qualified use as the original qualified real property would not trigger a recapture of the adjusted tax difference. If however, the like-kind exchange under section 1031 were not entirely for qualified property, then a proportionate amount of the recapture tax would be payable.

Eighth, a qualified heir would not be required to make an election to secure the benefits of the special rules for involuntary conversions.

Ninth, the bill would amend section 2032A to provide that if there is no comparable land from which to determine the average annual gross cash rental, then the average net share rental could be substituted for the average gross cash rental in applying the formula method. The net share rental would be (1) the value of the produce grown on the leased land received by the lessor, reduced by (2) the cash operating expenses of growing the produce that are paid, under the terms of the lease, by the lessor.

Finally, the bill would provide that, upon the recapture of the estate tax benefits, the basis of the property would be increased to its fair market value on the date of the decedent's death.[7]

Effective date

This provision would be effective for estates of decedents dying after December 31, 1981.

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[7] Technical modifications would be necessary to the bill to clarify that the basis is stepped up to its value as of the decedent's death and to insure that the special use value is not double counted in determining basis.

V. Estate Tax Treatment of Transfers Made Within Three Years of Death (sec. 6 of the bill and sec. 2035 of the Code)

Present law

Under present law, transfers made by a decedent within three years of death are included in the decedent's gross estate without regard to whether the gifts were actually made in contemplation of death. However, an exception to this rule applies for transfers of property (other than a transfer with respect to a life insurance policy) where no gift tax return was required to be filed with respect to the gift.

When a gift made within three years of the decedent's death is required to be included in the decedent's gross estate, it is valued at the time of the decedent's death. However, a credit is allowed against the estate tax for any gift tax paid by the decedent on the gift. Generally, the net effect of these two rules is to include in the gross estate the appreciation in value of the property from the date of the gift until the date of death.

There are several provisions of the Code which depend upon the amount of the decedent's gross estate. For example, qualification for special tax treatment in valuing farm real property (Code sec. 2032A), redemptions of stock of closely held corporations (Code sec. 303), and installment payment of the estate tax attributable to a closely held business interest (Code secs. 6166 and 6166A) depend upon the size of the gross estate. Consequently, the amount of gifts includible in a decedent's gross estate as gifts made within 3 years of death can affect the application of these other provisions.

Issue

The issue is whether post-gift appreciation of gifts made within three years of death should be excluded from the gross estate.

Explanation of provision

The bill would provide that the value of gifts which are includible in the gross estate by reason of being made within three years of death is to be their value on the date of gift instead of their value at the date of death. The estate will continue to receive a credit for any gift taxes imposed on the gift. Thus, the net effect of the bill would be to subject the gift to the gift tax at its value at the time of gift and to exclude any appreciation in value from the date of gift to the date of death from the estate tax. The value of the gift at the date of gift would still be included in the gross estate for purposes of determining the applicability of those other provisions (such as Code secs. 303, 2032A, 6166, and 6166A) which depend upon the amount of the decedent's gross estate.

Effective date

This provision would be effective for gifts made atfer December 31, 1980.

VI. Election to Pay Gift Tax (sec. 7 of the bill and sec. 2505 of the Code)

Present law

Under present law, any unused portion of the unified credit must be used to reduce the gift tax payable for taxable gifts made during a taxable period (Code sec. 2505(a)). Thus, a donor cannot elect not to use a portion of the unified credit that is otherwise allowable.[1]

The consequences of requiring the use of the unified credit against the gift tax, rather than using it on an elective basis, relate to finalizing the valuation of gifts made for preceding calendar years and quarters. Under present law, the valuation used for a gift made in a taxable period closed by the period of limitations for assessing deficiencies is fixed only if a gift tax has been assessed or paid for the taxable period in which the gift was made (Code sec. 2504(c)). Thus, in cases where the unified credit eliminates tax liability for a taxable period, the valuation of a gift made in an otherwise closed taxable period might be challenged on audit in subsequent taxable periods. Although no gift tax deficiency may be assessed for the prior taxable period, an increase in the valuation of the prior gift may push the taxable gifts for the subsequent taxable periods into a higher tax bracket under the progressive rate structure.

Issue

The issue is whether use of the unified credit for gift tax purposes should be elective.

Explanation of provision

Under the bill, a donor could elect to have all or any portion of the unified credit apply. The election would be required to be made no later than the due date for the return to which the election applies and in the form and manner prescribed under regulations.

Effective date

This provision would apply to gifts made after December 31, 1980.

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[1] Under prior law, any unused portion of the gift tax specific exemption could be claimed for any taxable period the donor wished (Code sec. 2521 as in effect before repeal by the Tax Reform Act of 1976).

VII. Installment Payment of Estate Tax Attributable to Closely Held Business Interests (sec. 8 of the bill and secs. 6166 and 6166A of the Code)

Present law

Code section 6166, as added by the Tax Reform Act of 1976, provides a 15-year period for the payment of the estate tax attributable to a decedent's interest in a closely held business (including a farm). Under this provision, an executor may elect to defer principal payments for up to 5 years from the due date of the estate tax return. However, interest for the first 5 years is payable annually. Thereafter, pursuant to the executor's initial election, the principal amount of the estate tax liability may be paid in from 2 to 10 annual installments. A special 4 percent interest rate is allowed on the estate tax attributable to the first $1 million of closely held business property, and interest on amounts of estate tax in excess of this amount is at the regular rate for interest on deferred payments (currently 12 percent).

In order to qualify for this deferral and installment payment treatment, the value of the closely held business (or businesses) included in the decedent's estate must exceed 65 percent of the value of the gross estate reduced by allowable expenses, indebtedness, and losses. For this purpose, the term "interest in a closely held business" means an interest as sole proprietor in a trade or business; an interest as a partner in a partnership having not more than 15 partners, or in which the decedent owned 20 percent or more of the capital; or ownership of stock in a corporation having not more than 15 shareholders, or in which the decedent owned 20 percent or more in value of the voting stock. Certain interests held by the decedent's family are treated as held by one shareholder or partner.

If a decedent's gross estate includes more than 20 percent of the value of each of two or more closely held businesses, the businesses can be treated as a single closely held business in determining whether the 65 percent test is satisfied.

Under present law, the privilege of making installment payments of the estate tax terminates if one-third or more of the value of the business is withdrawn (other than in certain redemptions for the payment of the estate tax), or if there is disposition of one-third or more of the value of decedent's interest in the business. In addition, all payments are accelerated if there is a failure to timely pay any installment payment.

A 10-year extended payment provision is also provided for estate tax attributable to a closely held business where a lesser proportion of the estate is represented by its value (Code sec. 6166A). Under this 10-year extension, the value of the business must be in excess of either 35 percent of the value of the gross estate or 50 percent of the taxable estate. Under this provision, acceleration of payments occurs if 50 percent or more of the value of the business is withdrawn, or if there is a disposition of 50 percent or more of the value of the decedent's interest in the busness. In addition, the Internal Revenue Service is authorized to permit discretionary annual extensions of up to 10 years to pay estate tax if reasonable cause for an extension exists (Code sec. 6161(a)(2)). Under both of the extensions, interest is payable at the regular rate rather than the special 4-percent rate.

Under the income tax law (Code sec. 303), a qualified redemption of stock to pay estate taxes funeral and administration expenses will be taxed as capital gain rather than as a dividend distribution taxed as ordinary income, even though a similar redemption would have been treated as a dividend if the stock had been redeemed during the decedent's lifetime. To qualify for this treatment under present law, the value of the stock redeemed, plus the value of the other stock of the redeeming corporation includible in the estate, must be more than 50 percent of the value of the gross estate reduced by allowable expenses, indebtedness and losses. Corporations, more than 75 percent of the value of which are included in the decedent's estate, may be aggregated in order to meet the 50 percent requirement.

Issues

The issue generally is whether the provisions for the deferral of estate tax payments and redemption of stock to pay the estate tax should be more closely coordinated. This includes whether a uniform set of eligibility requirements should be provided as well as a single rule for payment periods, interest rates and acceleration of payments.

Explanation of provision

Under the bill, the provision of present law allowing for the payment of estate taxes over a 15-year period would be expanded to include all estates in which the value of a closely held business (or businesses) included in the decedent's estate exceeds 35 percent of the value of the gross estate or 50 percent of the taxable estate. Also, the provision relating to the qualified redemption of stock to pay the estate tax would apply if the value of the closely held business met the same test. Likewise, the rules for aggregating two or more businesses for determining qualified redemptions would be the same as the present aggregation test for deferred payments.

The rules relating to acceleration of payments would be changed to increase from one-third to 50 percent the amount of a business interest that could be disposed of or withdrawn before payments would be accelerated. Also, a late payment made within 6 months of the due date would no longer accelerate all payments. Instead, there would be imposed a penalty of 5 percent per month on the amount of the payment, and interest on the payment would be payable at the regular interest rate.

The bill also would repeal the present 10-year estate tax extension under Code section 6166A.

Effective date

The provision would apply to estates of decedents dying after December 31, 1980.

VIII. Disclaimers (sec. 9 of the bill and sec. 2518 of the Code)

Present law

Under present law, a disclaimer is effective for federal transfer tax purposes if the requirements of Code section 2518 are satisfied. If a qualified disclaimer is made, the federal estate, gift, and generation-skipping transfer tax provisions apply with respect to the property interest disclaimed as if the interest had never been transferred to the person making the disclaimer.

A qualified disclaimer is an irrevocable and unqualified refusal to accept an interest in property that satisfies four requirements. First, the refusal must be in writing. Second, the written refusal must be received by the transferor of the interest, his legal representative, or the holder of the legal title to the property not later than 9 months after the day on which the transfer creating the interest is made. Nevertheless, the period for making the disclaimer is not to expire in any case until 9 months after the day on which the disclaimant has attained age 21. Third, the disclaimant must not have accepted the interest or any of its benefits before making the disclaimer. Fourth, the interest must pass, as a result of the refusal to accept the property, to the surviving spouse or a person other than the disclaimant. The disclaimant cannot have the authority to direct the redistribution or transfer of the property to another person.

Proposed Regulations issued on July 21, 1980, state that a disclaimer satisfies the requirements of Code section 2518 only if the disclaimer is effective under applicable local law to divest ownership of the disclaimed property in the disclaimant and to vest it in another.

Issue

The issue is whether the validity of a disclaimer for Federal tax purposes should be conditioned upon its validity under local laws.

Explanation of provision

Under the bill, a disclaimer that does not result in the passing of the interest under local law would still be a qualified disclaimer for Federal tax purposes if certain additional requirements are met. Specifically, the disclaimant, within the present time limits for making a qualified disclaimer, would be required to transfer the property interest to the person who would have received the property interest if the disclaimant had predeceased the holder of legal title to the property.

Effective date

This provision of the bill would be effective with respect to transfers creating an interest in the person disclaiming made after December 31, 1980.

REVENUE EFFECT

Table 1—Estate and Gift Tax Reduction of S. 2967

[In millions of dollars; fiscal years]

	1982	1983	1984	1985
Unified credit for estate and gift taxes		1, 231	2, 173	3, 015
Marital deduction [1]		39	29	25
Annual gift tax exclusion [1]	65	60	60	60
Special valuation of farm or other business real property [1]		155	155	155
Estate tax treatment of transfers made within 3 years of death [1]	33	37	42	46
Election to pay gift tax	([2])	([2])	([2])	([2])
Installment payment of estate tax attributable to closely held business interests [1]	13	13	13	13
Disclaimers	([2])	([2])	([2])	([2])
Total reduction	111	1, 535	2, 472	3, 314

[1] Additional loss after enactment of the unified credit proposal.
[2] Less than $5 million.

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