

Report for Congress

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Estate Tax Legislation in the 108th Congress

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Summary

Under provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA, P.L. 107-16, enacted June 7, 2001), the estate tax is scheduled to be repealed in 2010 but reinstated in 2011. All tax cut provisions of EGTRRA are scheduled to sunset on December 31, 2010. This report tracks actions in the 108th Congress to permanently repeal the estate tax or to retain but alter the tax.

Thus far in the 108th Congress, eight bills involving the estate tax have been introduced in the House and five in the Senate. The bills can be grouped under four broad categories. First, three House bills, H.R. 25 (Linder), H.R. 269 (English), and H.J.Res. 15 (Paul) would repeal the estate tax as part of a major overhaul of the federal tax system. Second, three other House bills, H.R. 57 (Dunn), H.R. 139 (McGinnis), and H.R. 158 (Pitts), would make the repeal of the estate tax permanent after 2010, by removing the sunset provision for the estate tax provisions of EGTRRA. The revenue cost for FY2012 from permanent repeal has been estimated at \$48 billion by the U.S. Treasury Department and \$58 billion by the Joint Committee on Taxation.

Third, four bills – one in the House and three introduced by Senator Kyl – would accelerate the repeal of the estate tax sooner than the 2010 date scheduled by EGTRRA. H.R. 51 (Cox) would repeal the gift tax along with the estate tax effective in 2003. S. 13 (Kyl) and S. 169 (Kyl) would accelerate the repeal of the estate tax to 2005 and make the repeal permanent by removing the sunset provision solely with respect to the estate tax provisions of EGTRRA. S. 96 (Kyl) would accelerate the repeal of the estate tax to 2005 as well. In addition, it would repeal the sunset for all provisions of EGTRRA; accelerate the scheduled income tax rate reductions; and introduce other provisions favorable to investments and retirement plans.

Fourth, three bills – one in the House and two in the Senate – would retain but alter the estate tax. Two would increase the exclusion amount for all estates; two would repeal the estate tax for qualified family-owned business interests; one would do both. H.R. 396 (DeFazio) would retain the estate tax but increase the exclusion amount to \$5 million starting in 2004, keep the maximum estate tax rate at its 2003 level of 49%, and repeal the modified carryover basis (and keep stepped-up basis). It would also freeze EGTRRA's reduction of the top individual income tax marginal rate at its 2003 level of 38.6%. S. 34 (Lincoln) would immediately and permanently repeal the estate tax on family-owned businesses and farms. Carryover (not stepped-up) basis would be used to calculate the capital gain if the beneficiary later sold the family-owned business interest. In contrast, S. 135 (Dayton) would eliminate EGTRRA's institution of carryover basis (and retain stepped-up basis). It would immediately increase the exclusion amount for all estates to \$4 million and provide a complete estate tax exclusion for family-owned businesses. It would also expand the 10% tax individual income tax bracket, freeze the rate decline for the top income tax brackets, and address other income tax issues.

This report will be updated as events warrant.

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Estate Tax Legislation in the 108th Congress

Background

The estate tax and generation-skipping transfer (GST) taxes are scheduled to be repealed effective January 1, 2010, under Title V of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA, P.L. 107-16). However, under Title IX of the tax cut Act, the estate tax repeal, and all other provisions of EGTRRA (pronounced egg-tra), are scheduled to sunset as of December 31, 2010. If the sunset provision is not repealed, in 2011 tax law would return to the law in place prior to the enactment of EGTRRA on June 7, 2001. For the estate tax, the exclusion amount would have risen to \$1 million under prior law.¹

During 2002, estate tax proposals offered by Republican Members in both houses focused on making the repeal of the estate tax permanent. The Bush Administration supported permanent repeal. Alternative proposals offered by Democratic Members in the House and Senate would have retained the estate tax but made some changes, such as making special exceptions for qualified family-owned business interests (QFOBI) and/or accelerating an increase in the exclusion amount for all estates.

In 2002, efforts to permanently repeal the estate tax focused on removing the sunset provision of EGTRRA with respect to the estate tax provisions of the Act. The estate and generation-skipping transfer taxes would thus be eliminated from 2010 onward. Other changes made by Title V of EGTRRA also would continue, such as replacing the step-up in basis with a modified carryover basis for assets transferred at death and retaining the gift tax on transfers made during one's lifetime even when the estate tax is repealed.

On April 18, 2002, the House passed H.R. 586, part of which would have removed the sunset provision of EGTRRA and thereby made permanent the repeal of the estate tax and all other provisions of the tax cut law. On June 6, 2002, the House passed H.R. 2143 which would have removed the sunset provision solely from the estate tax provisions of EGTRRA. On September 19, 2002, the House approved a resolution, H.Res. 524, which called upon the Senate to approve the Permanent Death Tax Repeal Act of 2002 (H.R. 2143) before the 107th Congress adjourned. The Senate did not act on the bill. In June 2002 the Senate considered three amendments offered to H.R. 8 regarding the estate tax. None of the amendments received the 60

¹ For additional information, see CRS Report RL31061, *Estate and Gift Tax Law: Changes Under the Economic Growth and Tax Relief Reconciliation Act of 2001*, by Nonna A. Noto.

votes needed to waive the budget point of order as established by a unanimous consent agreement.²

Bush Administration's FY2004 Revenue Proposal

One of the revenue proposals offered by the Bush Administration in conjunction with its FY2004 budget proposal was to “permanently extend provisions expiring in 2010.” This proposal would permanently extend all of the provisions of EGTRRA, which would otherwise sunset on December 31, 2010.³ One effect of this extension of EGTRRA would be to make the repeal of the estate tax and the generation-skipping transfer tax permanent for 2010 and beyond. However, the repeal of the sunset was not included as part of H.R. 2 (Thomas) and S. 2 (Nickles), the Jobs and Growth Tax Act of 2003, introduced on February 27, 2003. These companion bills in the House and Senate are the legislative vehicles for the economic growth package portion of the Administration's FY2004 tax cut and economic growth proposals. H.R. 2 and S. 2 do not include any provision regarding the estate tax and do not remove the sunset on tax provisions expiring in 2010.

The estimated revenue loss for FY2012⁴ from permanent repeal of the estate and generation-skipping transfer taxes, and modification of gift taxes, is \$48 billion according to the U.S. Treasury Department⁵ and \$58 billion according to the Joint Committee on Taxation.⁶

² For additional information, see CRS Report RS21224, *Estate Tax: Legislative Activity in 2002*, by Nonna A. Noto.

³ U.S. Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2004 Revenue Proposals* (referred to as the “Blue Book”), Washington, Feb. 2004, 129. U.S. Congress, Joint Committee on Taxation, *Description of Revenue Provisions Contained in the President's Fiscal Year 2004 Budget Proposal*, Joint Committee Print JCS-7-03, 108th Cong., 1st Sess., March 2003 (Washington, U.S. Govt. Print. Off., 2003), 239.

⁴ FY2012 is the first full fiscal year that would reflect the extension of EGTRRA's expiring provisions beyond December 31, 2010.

⁵ U.S. Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2004 Revenue Proposals*, 152.

⁶ U.S. Congress, Joint Committee on Taxation, *Estimated Budget Effects of the Revenue Provisions Contained in the President's Fiscal Year 2004 Budget Proposal*, JCS-15-03, 108th Cong., 1st Sess., March 4, 2003, 4.

The March 2003 estimate of \$58 billion is close to the Joint Committee's estimate of \$56 billion for FY2012, made in June 2002. U.S. Congress, Joint Committee on Taxation, *Estimated Revenue Effects of H.R. 2143, “Permanent Death Tax Repeal Act of 2001,”* JCS-51-02, 107th Cong., 2d Sess., June 4, 2002.

Overview of Bills Introduced in the 108th Congress

To date, 13 bills involving the estate tax have been introduced in the 108th Congress, eight in the House and five in the Senate. The bills can be grouped under four broad categories.

First, three House bills would repeal the estate tax as part of a major overhaul of the federal tax system. H.R. 25 (Linder) would repeal the estate, income, and payroll taxes and replace them with a national sales tax. H.R. 269 (English) would repeal the estate and income taxes and replace them with a “simplified USA tax,” an adaptation of the current individual and corporate income taxes. H.J. Res. 15 (Paul) proposes an amendment to the U.S. Constitution that would abolish the estate and gift taxes, along with the personal income tax, and prohibit the U.S. Government from engaging in business in competition with its citizens.

Second, three other House bills would make the repeal of the estate tax permanent after 2010. H.R. 57 (Dunn) would remove the sunset provision of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA, P.L. 107-16) solely with respect to the estate tax provisions (Title V) of EGTRRA. H.R. 139 (McGinnis) and H.R. 158 (Pitts) are equivalent in substance to H.R. 57.

Third, four bills would accelerate the repeal of the estate tax, currently scheduled for 2010 under EGTRRA. One bill is in the House and the three others in the Senate, introduced by Senator Kyl. H.R. 51 (Cox) would repeal the gift tax, along with the estate and generation-skipping transfer taxes, effective in 2003. S. 13 (Kyl) and S. 169 (Kyl) would accelerate the repeal of the estate and GST taxes to 2005. S. 13 and S. 169 (like H.R. 57, H.R. 139, and H.R. 158 in the House) would make the repeal permanent by removing the sunset provision solely with respect to the estate tax provisions of EGTRRA. S. 96 (Kyl), like S. 13 and S. 169, would accelerate the repeal of the estate and GST taxes to 2005. In contrast to S. 13 and S. 169, S. 96 would make the repeal permanent by repealing the sunset for all provisions of EGTRRA (not just the estate tax provisions). In addition, S. 96 would accelerate the income tax rate reductions scheduled under EGTRRA and introduce other provisions favorable to investments and retirement plans.

Fourth, three bills would retain but alter the estate tax. One is in the House and two in the Senate. Two would repeal the estate tax for qualified family-owned business interests. Two would increase the applicable exclusion amount (exemption) for all estates.⁷ One would do both. As revenue offsets to the other provisions of

⁷ The amount of a decedent’s assets that may be transferred free from estate tax is commonly referred to as the “exemption amount” or simply the “exemption.” Formally, however, in the Internal Revenue Code, the exemption is called the “applicable exclusion amount.” EGTRRA calls it the “unified credit effective exemption amount,” referring to the unified estate and gift tax credit. Under the law prior to EGTRRA, the applicable exclusion amount was scheduled to rise from \$675,000 in 2001, in steps, to \$1 million in 2006. Thus, \$1 million would be the exemption amount in effect if EGTRRA sunsets as scheduled on December 31, 2010. EGTRRA raised the applicable exclusion amount to \$1 million for

(continued...)

H.R. 396 (DeFazio), section 602 of the bill would repeal EGTRRA's repeal of the estate and GST taxes. It would increase the applicable exclusion amount to \$5 million starting in 2004; keep the maximum estate tax rate at its 2003 level of 49%, applied to taxable estate amounts over \$2 million; and repeal the carryover basis that is scheduled to take effect in 2010 under EGTRRA (keeping stepped-up basis). In addition, section 601 would freeze EGTRRA's reduction of the top individual income tax marginal rate at its 2003 level of 38.6%.

S. 34 (Lincoln) would keep the estate tax but immediately and permanently repeal the tax on family-owned businesses and farms. These would be classified as carryover business interests (COBIs) and carryover (not stepped-up) basis would apply in any subsequent sale by the heir. S. 34 would also eliminate several restrictive requirements included under the current QFOBI rules. In contrast, S. 135 (Dayton) would eliminate both EGTRRA's repeal of the estate tax and its institution of carryover basis. It would immediately increase the applicable exclusion amount for all estates to \$4 million and provide a complete estate tax exclusion for family-owned businesses. It would also expand the 10% (lowest) tax bracket under the individual income tax, freeze the rate decline for the top income tax brackets, and address other income tax issues.

In the descriptions below related to provisions of EGTRRA, references to the estate tax include the generation-skipping transfer tax, but not the gift tax. Under EGTRRA, the gift tax would continue after the estate tax is repealed. Also under EGTRRA, the repeal of the estate and GST taxes is accompanied by replacing the step-up in basis treatment by a "modified carryover basis" for inherited assets. Any exceptions to these conventions are noted in the bill descriptions that follow.

House

H.R. 25 (Linder). Fair Tax Act of 2003. H.R. 25 would repeal the federal estate and gift taxes, along with the income and payroll taxes. In their stead, would institute a national sales tax, to be administered largely by the states. Three of the four negative findings listed in the bill in relation to the estate tax are statements about the detrimental effects the tax has on small businesses and farms. Introduced January 7, 2003. Referred to the Committee on Ways and Means.

H.R. 51 (Cox). Family Heritage Preservation Act. H.R. 51 would repeal the federal death tax, including gift taxes as well as the estate tax and the tax on generation-skipping transfers, effective in 2003. Lists seven findings related to death

⁷ (...continued)

2002 and 2003, \$1.5 million for 2004 and 2005, \$2 million for 2006-2008, and \$3.5 million for 2009, before the tax is repealed in 2010. See CRS Report RL31061, *Estate and Gift Tax Law: Changes Under the Economic Growth and Tax Relief Reconciliation Act of 2001*, by Nonna A. Noto, 4-5. For further explanation of the relationship between the applicable exclusion amount and the applicable credit amount, see CRS Report RL31092, *Calculating Estate Tax Liability During the Estate Tax Phasedown Period 2001-2009*, by Nonna A. Noto, 1-2.

taxes and saving, investments, and other taxes. Introduced January 7, 2003. Referred to the Committee on Ways and Means.

H.R. 57 (Dunn). Death Tax Permanency Act of 2003. H.R. 57 would make the repeal of the estate tax and generation-skipping transfer tax permanent. Would remove the sunset provision solely from the estate tax provisions (Title V) of EGTRRA. Equivalent in substance to H.R. 139 and H.R. 158. Introduced January 7, 2003. Referred to the Committee on Ways and Means.

H.R. 139 (McInnis). Permanent Death Tax Repeal Act of 2003. Equivalent in substance to H.R. 57. H.R. 139 introduced January 7, 2003. Referred to the Committee on Ways and Means.

H.R. 158 (Pitts). Equivalent in substance to H.R. 57. H.R. 158 introduced January 7, 2003. Referred to the Committee on Ways and Means.

H.R. 269 (English). Simplified USA Tax Act of 2003. H.R. 269, Title V would repeal the gift tax as well as the estate and GST taxes. Would also repeal the existing individual income tax and corporate income tax but replace them with a simplified USA tax for individuals and for businesses, based on a new definition of taxable income and a reduced number of deductions. Introduced January 8, 2003. Referred to the Committee on Ways and Means.

H.R. 396 (DeFazio). Emergency Anti-Recession Act of 2003. H.R. 396, Section 602 would retain the estate and GST taxes by repealing EGTRRA's repeal. It would also increase the applicable exclusion amount to \$5 million starting in 2004; keep the maximum estate tax rate at its 2003 level of 49% (for taxable estate amounts over \$2 million); and repeal the carryover basis that is scheduled to take effect in 2010 under EGTRRA. These estate tax provisions, together with freezing the reduction of the top individual income tax marginal rate at its 2003 level of 38.6% (Sec. 601), are revenue offsets to the other provisions of the bill. Introduced January 28, 2003. Referred to the Committee on Ways and Means and, in addition, to the Committees on Transportation and Infrastructure; Education and the Workforce; Energy and Commerce; Agriculture; Financial Services; and Armed Services.

H.J.Res. 15 (Paul). H.J.Res. 15 is a joint resolution proposing an amendment to the Constitution of the United States relative to abolishing personal income, estate, and gift taxes and prohibiting the United States Government from engaging in business in competition with its citizens. Would require the liquidation of activities and sale of affected properties and facilities of the United States government which violate the intent and purposes of the amendment. Would repeal the sixteenth amendment to the Constitution (which grants Congress the power to impose and collect income taxes). Introduced January 28, 2003. Referred to the Committee on the Judiciary.

Senate

S. 13 (Kyl). Death Tax Fairness Act of 2003. S. 13 would accelerate the repeal of the estate and generation-skipping transfer taxes to 2005 (compared to 2010

under EGTRRA). Would make permanent the repeal of the estate and GST taxes by removing the sunset provision solely with respect to the estate tax provisions of EGTRRA (Title V) after 2010. S. 13 is equivalent in substance to S. 169 (Kyl). Introduced February 14, 2003. Read the second time and placed on the calendar February 24, 2003.

S. 34 (Lincoln). Estate Tax Repeal Acceleration (ExTRA) for Family-Owned Businesses and Farms Act. S. 34 would immediately and permanently repeal the estate tax on family-owned businesses and farms. Would repeal section 2057 of the Internal Revenue Code (IRC) regarding the deduction for qualified family-owned business interests. In its stead, would introduce a new section 2059 of the IRC providing for a dollar-unlimited deduction from the gross estate of the “carryover business interests” of the decedent. Carryover (not stepped-up) basis would apply in any subsequent sale by the beneficiary. No spousal property basis increase could be allocated to a COBI. The COBI deduction could not apply to property acquired by the decedent by gift, or for less than adequate and full consideration, during the three-year period before the decedent’s death.

The bill would eliminate several requirements under the current QFOBI rules: that the business represent at least 50% of the decedent’s gross estate; that the heir materially participate in the business; that the tax benefit be recaptured if the heir does not participate over the next 10 years; and that not more than 35% of a business’s adjusted gross income be passive income. The exempt COBI would be permitted to hold cash or marketable securities, or both, up to “reasonably anticipated business needs,” a term that is expected to encompass funds needed to retire debt or expand the business. This is in contrast to current law which limits exempt cash and marketable securities to the “reasonably expected day-to-day working capital needs” of the business.

The executor would have the option to allow family-owned business interests to pass under ordinary estate tax law, as would the other taxable assets in the estate. Under ordinary law, the (net) taxable estate would be free from estate tax for amounts up to the applicable exclusion amount plus property transferred to a surviving spouse under the unlimited marital deduction. Assets would receive a step-up in basis, with the exception that the aggregate spousal basis increase would be limited to \$3 million.

These amendments would apply to the estates of decedents dying and gifts made 1) after December 31, 2003, and before January 1, 2010, and 2) after December 31, 2011 [*sic*]. (Presumably, December 31, 2010, is intended. If this presumption is correct, the bill assumes that the estate tax will remain in effect except for 2010, as provided by EGTRRA and its sunset provision.) No estate tax would be due on the estates of decedents who die in 2010, the year of repeal under current law. Introduced January 7, 2003. Referred to the Committee on Finance.

S. 96 (Kyl). Contract With Investors. S. 96 would repeal the sunset for all tax provisions of EGTRRA, including those applying to the estate tax. Would accelerate the repeal of the estate and generation-skipping transfer taxes to 2005 (compared to 2010 under current law). In addition, would accelerate the scheduled reductions in individual income tax rates. Would reduce the maximum capital gains tax rate for

individuals to 10% (from 20%). Would increase the limit on capital losses applicable to individuals to \$10,000 (from \$3,000), indexed for inflation. Would accelerate the scheduled increase in contributions to certain retirement plans. Would increase the age for beginning mandatory distributions from qualified pension and retirement plans to 75 (from 70 1/2). Would exclude from income taxation dividends received by individuals. Includes a sense of the Senate resolution endorsing action by Congress to safeguard American workers' pension and retirement accounts; to modernize this country's international tax provisions in order to enhance the international competitiveness of U.S. companies; to repeal redundant, outdated, and unscientific regulatory burdens on investors and U.S. companies and perform a cost-benefit analysis before enacting new burdens; to enact meaningful tort reform; and to enact meaningful tax reform that simplifies the federal tax code and reduces the cost recovery periods that businesses must use to recover the cost of capital (the number of years over which depreciation deductions must be spread). Introduced January 7, 2003. Referred to the Committee on Finance.

S. 135 (Dayton). Dayton Fair Tax Cut Act. S. 135 would eliminate EGTRRA's repeal of the estate tax and its institution of carryover basis. Instead, would immediately increase the applicable exclusion amount to \$4 million and provide a complete estate tax exclusion for family-owned businesses. Would also expand the 10% (lowest) tax bracket under the income tax and freeze the rate decline for the top income tax brackets. Also addresses tax shelter transactions; expatriate corporations; acceleration of increase in child tax credit; acceleration of marriage penalty relief; and extension of alternative minimum tax relief. Introduced January 9, 2003. Referred to the Committee on Finance.

S. 169 (Kyl). Permanent Death Tax Repeal Act of 2003. S. 169 would accelerate the repeal of the estate and generation-skipping transfer taxes and the implementation of the modified carryover basis to 2005 (compared to 2010 under EGTRRA). Would make permanent the repeal of the estate and GST taxes by removing the sunset provision solely with respect to the estate tax provisions of EGTRRA (Title V) after 2010. S. 169 is equivalent in substance to S. 13 (Kyl). Introduced January 15, 2003. Referred to the Committee on Finance.

For Additional Information

CRS Electronic Briefing Book, *Taxation*, "Federal Estate and Gift Tax," available at [<http://www.congress.gov/brbk/html/ebtxr35.html>].

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

CRS Report RS20609, *Economic Issues Surrounding the Estate and Gift Tax: A Brief Summary*, by Jane G. Gravelle.

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

CRS Report RL31061, *Estate and Gift Tax Law: Changes Under the Economic Growth and Tax Relief Reconciliation Act of 2001*, by Nonna A. Noto.

CRS Report RS21224, *Estate Tax: Legislative Activity in 2002*, by Nonna A. Noto.

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