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Marital Sharing of Transfer Tax Exemptions

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Abstract: This Article analyzes portability and its antecedents in order to distill a positive account of marital sharing of transfer tax exemption amounts. Prior to 2010, the estate and gift tax exemption equivalent was a non-transferable, separate tax attribute of each spouse. A spouse could only access his or her spouse's effective exemption by shifting property into the other spouse's tax base. With the enactment of portability, Congress decoupled tax-free availability of a spouse's unified credit from the necessity of a prior intra-spousal transfer. All that is required is an election by the decedent spouse, via the executor, to share the decedent's unused exemption equivalent with the surviving spouse. This Article argues that a logical extension of this progression in the law, presaged by several early proposals by the American Law Institute and the U.S. Treasury, would be a regime that authorized elective sharing of estate and gift tax exemption amounts between spouses, in any proportion, during life or at death.

INTRODUCTION

This Symposium celebrating the one-hundredth anniversary of the estate tax provides an opportunity to reflect on where the law has been and where it may be heading. Accordingly, this Article analyzes portability and its antecedents (marital deduction and gift-splitting) in order to distill a positive account of the transfer tax exemptions of married persons.[1] This Article argues that the move to portability, justified largely on simplification grounds, may signal a more fundamental change in the nature of spousal exemption equivalents. The Article then considers the contours of the law with full realization of this new spousal exemption conception. In more colloquial terms, the goal of this piece is to describe the proverbial can of

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[1] As such, the author takes no normative view on its appropriateness. In addition, given the focus of this symposium, the discussion solely focuses on the estate and gift tax unified credit and not the generation-skipping transfer ("GST") tax exemption.

worms, open up the lid, and peek inside. The author plans to unpack the normative underpinnings of this account in future work.

Prior to 2010, the only way that one spouse could access the benefit of the other spouse's effective exemption amount was via a prior marital deduction transfer, actual or deemed (per a gift-splitting election). With the enactment of portability, Congress decoupled tax-free availability of a decedent spouse's applicable exclusion amount from the requirement of a prior shift in the tax base to that spouse. All that is required is an election by the decedent spouse, via the executor, to share the decedent's unused exemption equivalent with the surviving spouse. Evaluation of this progression in the law suggests that Congress may be moving towards a model of elective sharing of unified credits between spouses, during life or at death.

Part I of this Article provides a brief history of the transfer taxation of married couples.[2] Part II details the evolution in how spouses access or share each other's unified credits.[3] Part III articulates a paradigm of marital sharing of transfer tax exemptions and envisions its operationalization.[4] Lastly, Part IV raises several potential implications of adoption of such a regime.[5]

I. Brief History of Transfer Taxation of Married Couples

This Part provides a brief legislative history of the federal estate and gift taxes focusing primarily on those transfer tax provisions specifically aimed at married couples. The Revenue Act of 1916[6] imposed an excise tax on the transfer of a decedent's estate at death. A modestly progressive rate schedule applied to the net estate.[7] Concerned about the erosion of the estate tax base presented by inter vivos gifts, Congress adopted the first federal gift tax in 1924 with its own separate tax base, rates, and exemption amounts.[8] In 1976, Congress integrated the two taxes by establishing a unitary rate schedule cumulatively applied to all gratuitous transfers of property during life or at death, and a single unified credit, which was equal to the

[2] *See infra* notes 6–35 and accompanying text.

[3] *See infra* notes 36–68 and accompanying text.

[4] *See infra* notes 69–94 and accompanying text.

[5] *See infra* notes 95–103 and accompanying text.

[6] Revenue Act of 1916, Pub. L. No. 64-271, 39 Stat. 756.

[7] Darien B. Jacobson et al., *The Estate Tax: Ninety Years and Counting*, 27 STAT. INCOME BULL., no. 1, Summer 2007, at 118, 120, https://www.irs.gov/pub/irs-soi/ninetyestate.pdf [https://perma.cc/79MR-AETF] (defining net estate as the gross estate less certain deductions and less an exemption of $50,000).

[8] Revenue Act of 1924, ch. 234, §§ 319–24, 43 Stat. 253, 313–16 (repealed 1926); Jacobson et al., *supra* note 7, at 121–22 & n.17. This was retroactively repealed and replaced with the modern gift tax in 1932. Revenue Act of 1932, Pub. L. No. 72-154, §§ 501–32, 47 Stat. 169, 245–59 (codified as amended in scattered sections of 26 U.S.C.).

tax saved on exempting the applicable exclusion amount ("AEA") from taxation, in lieu of separate exemptions under each tax.[9]

Prior to 1942, no special tax provisions applied to transfers of property between spouses or transfers from one spouse to a non-spouse beneficiary. The U.S. Treasury occasionally pushed Congress to equalize the taxation of married individuals in community property and common law states.[10] State community property law automatically treated each spouse as owning one half of any community property. This was advantageous from a transfer tax perspective because it included only half the value of the marital property in the estate of the first spouse to die.[11] The Revenue Act of 1942[12] ("the 1942 Act") attempted to bring uniformity by rejecting state law as the touchstone for estate and gift taxation in community property states, and instead applied common law notions of ownership and control to community property transferors.[13]

Dissatisfaction with the 1942 Act from the community property states led to a repeal of the 1942 gift and estate tax revisions.[14] In the Revenue Act of 1948,[15] Congress implemented a regime that attempted to produce equal transfer tax results in common law states and community property jurisdictions.[16] To operationalize this new version of uniformity, Congress enacted two new transfer tax provisions: (1) a deduction for estate and gift tax purposes for qualifying transfers to a spouse, limited to one half (fifty percent) of the decedent's adjusted gross estate (so-called "marital deduction"),[17] and (2) an election to treat a gift made by either spouse to a third-party beneficiary as if one half of the gift was made by each spouse (so-called "gift-splitting").[18] In light of the fact that the half-interest of a spouse in community property was an outright interest, Congress intended to restrict the types of transfers qualifying for the marital deduction to fee simple interests

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[9] Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat 1520; Jacobson et al., *supra* note 7, at 122–23. This Article uses the terms applicable exclusion amount, effective exemption amount, exemption equivalent, and unified credit interchangeably.

[10] REGIS W. CAMPFIELD ET AL., THE STUDY OF FEDERAL TAX LAW: ESTATE AND GIFT TAXES INCLUDING INCOME TAXATION OF ESTATES AND TRUSTS 600 (1984).

[11] At the time, rates were progressive so each spouse got his or her own run through the brackets.

[12] Revenue Act of 1942, Pub. L. No. 77-753, 56 Stat. 798.

[13] Norman A. Sugarman, *Estate and Gift Tax Equalization—The Marital Deduction*, 36 CALIF. L. REV. 223, 225 (1948); Stanley S. Surrey, *Federal Taxation of the Family—The Revenue Act of 1948*, 61 HARV. L. REV. 1097, 1117–19 (1948).

[14] Surrey, *supra* note 13, at 1118–19.

[15] Revenue Act of 1948, Pub. L. No. 80-471, 62 Stat. 110.

[16] Surrey, *supra* note 13, at 1121.

[17] *Id.* (explaining how the adjusted gross estate was a new estate tax concept that equaled the gross estate less certain deductions, but excluded the $60,000 exemption, charitable bequests and the deduction for property previously taxed, and any community property).

[18] Sugarman, *supra* note 13, at 228.

or to the rough equivalent of a fee simple interest if the property passed into a trust (a life estate coupled with control over the ultimate disposition of the trust property).[19]

After a limited expansion of the amount deductible in 1976,[20] Congress enacted an unlimited gift and estate marital deduction in the Economic Recovery Tax Act of 1981.[21] Sections 2056 and 2523 allowed qualifying spousal transfers to pass free from the imposition of estate or gift tax.[22] The policy reason for the marital deduction shifted from attempting to equate the common law and community property results to allowing intra-spousal gifts without the imposition of transfer tax.[23] According to the legislative history, Congress "believe[d] that a husband and wife should be treated as one economic unit for purposes of the estate and gift taxes."[24]

Rather than achieving the community property result, the qualification rules were designed to ensure that any property transferred tax-free between spouses was taxed when it passed outside the marital unit.[25] Fee simple or fee simple equivalent interests still qualified under this new standard because such interests were includable in the gross estate of the surviving spouse ("SS").[26] Moreover, Congress authorized a new type of qualifying interest, so-called qualifying terminable interest property ("QTIP").[27] A QTIP election by the transferor spouse allowed a deduction for the full value of property passing into a trust even though the transferee spouse only received a life interest, with the remainder passing to non-spouse beneficiaries.[28] Congress also added a new provision designed to ensure that the QTIP trust property (which otherwise would not be includable) was taxed in the transferee spouse's estate.[29]

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[19] Surrey, *supra* note 13, at 1127–28.

[20] Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520.

[21] Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, 95 Stat. 172.

[22] *See* I.R.C. § 2523 (2012) (gift tax); I.R.C. § 2056 (2012) (estate tax).

[23] RICHARD B. STEPHENS ET AL., FEDERAL ESTATE AND GIFT TAXATION: INCLUDING THE GENERATION-SKIPPING TRANSFER TAX ¶ 5.06[1], at 5-119 (9th ed. 2013).

[24] S. REP. NO. 97-144, at 127 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 228.

[25] STEPHENS ET AL., *supra* note 23, ¶ 5.06[7][a], at 5-151.

[26] *See* I.R.C. § 2033 (2012) (regarding property in which the decedent had an interest); I.R.C. § 2041 (2012) (involving the powers of appointment); *id.* § 2056(a)–(b)(5) (providing guidance on bequests, etc., to surviving spouse).

[27] *See id.* § 2056(b)(7) (regarding election of life estate for the surviving spouse in a bequest to the surviving spouse); *id.* § 2523(f) (discussing election of life estate for the donee spouse in a gift to spouse context).

[28] *Id.* §§ 2056(b)(7), 2523(f).

[29] *See* I.R.C. § 2044 (2012) (providing guidance about property for which the marital deduction was previously allowed). Absent this provision, the qualifying terminable interest trust property ("QTIP") would not otherwise be included in the SS gross estate because the SS's income interest terminated at death and the SS exercised no dispositive control over the property.

Until 2010, the applicable transfer tax provisions for married couples (marital deduction and gift-splitting) remained relatively stable. In the Tax Relief Act of 2010,[30] Congress enacted a new provision that allowed a deceased spouse ("DS") to port or transfer such spouse's unused unified credit to the SS (so-called portability).[31] In order to implement this provision, Congress redefined the AEA as the sum of the basic exclusion amount ($5 million, adjusted for inflation) and in the case of a SS, the deceased spousal unused exclusion amount ("DSUEA").[32] The DSUEA is defined as the lesser of: (1) the basic exclusion amount, or (2) the excess of (A) the applicable[33] exclusion amount of the SS's last DS, over (B) the amount of such last DS's taxable estate plus adjusted taxable gifts.[34] A DSUEA is not automatically ported, but requires the DS's executor to file an estate tax return (even if one would not otherwise be required) on which the DSUEA is calculated and an election is made.[35]

II. EVOLUTION OF SPOUSAL EXEMPTION EQUIVALENT UTILIZATION—WHERE THE LAW IS

This Part details the evolution in how spouses access or share each other's effective exemption amounts. Section A establishes that prior to the introduction of portability, the AEA was a non-transferable, separate tax attribute of each spouse. The only way that one spouse could obtain the benefit of the other spouse's exemption equivalent was by shifting property into the other spouse's tax base via a prior marital deduction transfer. With

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[30] Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296.

[31] *See* I.R.C. § 2010(c) (2012, Supp. II) (regarding the applicable unified credit amount against the estate tax).

[32] *See id.* § 2010(c)(2) (stating the applicable exclusion amount of the applicable unified credit amount against the estate tax). Use of the word "last" was intentional so that if a SS has more than one DS, only the most recent DS's DSUEA may be utilized by the SS. *See* TRACY BLAKE DEVLIEGER & TIFFANY B. CARMONA, REAL PROP., TR. & ESTATE LAW SECTION, AM. BAR ASS'N, THE RULES OF PORTABILITY 1, 5–6 (2011), http://www.americanbar.org/content/dam/aba/publications/rpte_ereport/2011/Dec_2011/te_articles.authcheckdam.pdf [https://perma.cc/A2VC-ZUEP] (explaining the "last" deceased spouse restriction).

[33] The 2010 Act used the word "basic" instead of "applicable" but that error was corrected by subsequent legislation. *See* American Taxpayer Relief Act of 2012, Pub. L. No. 112-240, § 101 (c)(2), 126 Stat. 2313, 2318 (2013) (stating the correction).

[34] I.R.C. § 2010(c)(4).

[35] *Id.* § 2010(c)(5)(A). Under the regulations, upon the timely filing of a complete and properly prepared estate tax return, an executor of the estate of a decedent survived by a spouse will have elected portability of the decedent's DSUEA, unless the executor validly opts out of making the portability election. Treas. Reg. § 20.2010-2(a) (2015). This can be time-consuming and expensive if an estate tax return would not otherwise. *See generally* Howard M. Zaritsky, *The DSUE Amount as an Estate Asset with Value*, 41 EST. PLAN. 46 (2014) (suggesting that the DS's estate may need to be compensated by the SS for this additional cost).

the enactment of portability's elective transfer tax exemption sharing regime, section B claims that Congress decoupled tax-free availability of a spouse's unified credit from the requirement of a prior intra-spousal transfer. All that is required is an election by the decedent spouse, via the executor, to share the decedent's unused exemption equivalent with the surviving spouse. Finally, section C argues that gift-splitting is actually a hybrid between the marital deduction method of sharing of spousal exemptions and portability.

A. Prior Marital Deduction Transfer

As described above, the marital deduction exempts intra-spousal gifts, devises, and bequests from estate and gift taxation. There is also a secondary transfer tax effect of a marital deduction gift—it shifts property from the tax base of the donor spouse to the tax base of the donee spouse.[36] As a result, it will be the donee spouse who will bear the tax burden (consumption of AEA or payment of transfer tax) when that same property passes outside of the marital unit. Under this model, a marital deduction transfer by one spouse is a necessary prerequisite to tax-free availability of the other spouse's effective exemption.[37]

For example, assume that husband ("*H*") and wife ("*W*") are married with one child ("*C*").[38] Also assume that the basic exclusion amount is $5 million. *H* has $1 million in assets, with his full unified credit intact. *W* owns property worth $2 million but had previously exhausted her $5 million AEA making taxable gifts to *C*. *W* would like to gift $1 million to *C* without the imposition of transfer tax. In order to accomplish this, *W* would need to first transfer the $1 million to *H* in a form that qualifies for the marital deduction.[39] By doing this interim marital deduction step, *H* will be treated as the transferor of the $1 million when it ultimately passes to *C*, so that *H*'s AEA will be available to shelter the gift to *C* from taxation.

The marital deduction is automatic for qualifying transfers,[40] with control over satisfying the requirements for qualification vested in the hands of

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[36] *Accord* Joseph M. Dodge, *A Feminist Perspective on the QTIP Trust and the Unlimited Marital Deduction*, 76 N.C. L. REV. 1729, 1744 (1998) (noting that the marital deduction shifts all or a portion of a spouse's tax). In reality, the marital deduction shifts all or a portion of a one spouse's tax base to the other spouse's tax base thereby deferring "not the tax but rather a portion of the aggregate tax base." *See id.*

[37] Of course, if the transferor is willing to pay a transfer tax, he or she can also shift assets into any transferee's tax base, including a spouse.

[38] This is a first marriage for *H* and *W*.

[39] A § 2513 election would not result in a tax-free transfer to *C* because *W* had no unified credit available. *See infra* note 67 and accompanying text.

[40] STEPHENS ET AL., *supra* note 23, ¶ 5.06[1], at 5-120. The term "qualifying transfers" is meant to include only those QTIP transfers where a proper election is made. *See* I.R.C.

the transferor spouse. As a result, power to access the transferee spouse's unified credit via a prior marital deduction transfer also sits largely with the donor spouse. Prior to 1981, the cost for this access was relinquishment of dispositive control to the donee spouse. Intuitively, it appears that this is the proper matching of costs and benefits. Since the donee spouse bears the ultimate tax burden (use of AEA or tax due) on the transfer of the property to a non-spouse beneficiary, the donee spouse should be able to exercise dispositive power over the property.

In 1981, Congress altered this intuitive result with the introduction of QTIP. Under QTIP, as long as the donor spouse is willing to provide a qualifying income interest to the donee spouse, the donor spouse can shift the underlying property to the donee's tax base, thereby consuming the donee spouse's AEA, without relinquishing dispositive control and without the donee's consent. In effect, access to the donee spouse's exemption equivalent is unrestricted and costless to the donor spouse. Commentators continue to critique this aspect of QTIP.[41]

B. Portability

At the first death, a DS can utilize his or her SS's available exemption by making a marital deduction transfer to such SS. But, prior to 2010, there was no way that a SS could potentially consume his or her DS's unused unified credit amount. As a separate, non-transferable tax attribute, it simply died along with the DS. Of course, a prescient SS could make a pre-death shift in the tax base to a DS in order to access the DS's available unified credit at the DS's death. This would, however, require much advance planning and a bit of luck in terms of the order of deaths.

As a second example, assume husband ("*H*") died with his full $5 million AEA intact and an estate valued at $1 million left entirely to his only child, a son ("*S*"). At the time of *H*'s death, his wife ("*W*") owned $2 million worth of assets, having previously exhausted her unified credit by making taxable gifts to her only child, a daughter ("*D*"). Absent portability, *W* would have needed to transfer her $2 million to *H* prior to his death in order to take advantage of his available exemption at his death. Given their differing ultimate beneficiaries, presumably *W* would create an inter vivos QTIP trust, giving *H* the life interest, with the assets passing to *D* at *H*'s death. By

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§ 2056(b)(7) (2012) (requiring an election for any property to be considered "qualified terminable interest property").

[41] *See, e.g.*, Joseph M. Dodge, *Norms and Transfer Taxes*, *in* CONTROVERSIES IN TAX LAW: A MATTER OF PERSPECTIVE 217, 233 (Anthony C. Infanti ed., 2015) (noting that "as far as the ultimate control of wealth by women . . . the real culprit is the QTIP trust"); Wendy C. Gerzog, *The Marital Deduction QTIP Provisions: Illogical and Degrading to Women*, 5 UCLA WOMEN'S L.J. 301, 306–25 (1995) (critiquing the QTIP for demeaning women).

doing this, *W* could utilize *H*'s unused unified credit at his death to shelter the transfer of *W*'s $2 million to *D* from taxation.

With a portability election, *H*'s $4 million DSUEA becomes available to *W* to shelter her future gratuitous transfers to D or anyone else.[42] No pre-death shift in the tax base from *W* to *H* is necessary. Of course, *W* could still make the QTIP transfer, but it would be purely because that was her donative intent, not because she was attempting to achieve a particular tax result.[43] Portability essentially decouples tax-free availability of a spouse's AEA from the requirement of a prior marital deduction transfer to that spouse. All that is required is an election by the DS's executor to share the decedent's DSUEA with the SS.[44]

Hailed "as a paradigm shift,"[45] portability promised to reduce the cost and complexity of estate planning for married couples.[46] Prior to portability, estate tax planning for married individuals involved maximizing the amount that could pass tax-free in both spouses' estates (amount sheltered by the spouses' unified credits), and then passing the remainder at the first death in a form that deferred inclusion in the tax base until the second death (marital deduction) (the "Optimum Plan"). Given that the marital deduction is automatic for qualifying transfers,[47] and reduces the gross estate prior to application of the unified credit, it took a bit of planning to reverse this order and achieve the desired tax result.[48]

This usually necessitated splitting the estate into two shares at the first death: a non-marital and a marital share. The non-marital share received an amount equal to the decedent's estate tax effective exemption amount (so-called bypass, or credit shelter amount or trust). This share purposely did not qualify for the marital deduction, so it could soak up the available credit

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[42] In this example, the DSUEA is calculated as the lesser of: (1) $5 million, or (2) $4 million. *See supra* note 34 and accompanying text (explaining how the DSUEA is calculated). *W* may utilize the DS's DSUEA so long as *H* remains her last deceased spouse. *See* I.R.C. § 2010(c)(4) (2012, Supp. II) (defining the DSUEA in reference to the "last such deceased spouse of such surviving spouse").

[43] Indeed, under the facts of this second example, it is extremely unlikely that *W* would have engaged in the pre-death QTIP transaction, as it would have left her destitute.

[44] *See supra* note 35 and accompanying text (describing the filing process to elect DSUEA portability).

[45] Jonathan G. Blattmachr et al., *Portability or No: The Death of the Credit-Shelter Trust?*, 118 J. TAX'N 232, 233 (2013).

[46] *Tax Code Complexity: New Hope for Fresh Solutions: Hearing Before the S. Comm. on Fin.*, 107th Cong. 45 (2001) (statement of Richard M. Lipton, Chair, Section on Taxation, American Bar Association); *see also* Dennis L. Belcher & Mary Louise Fellows, *Report on Reform of Federal Wealth Transfer Taxes*, 58 TAX LAW. 93, 200–03 (2004) [hereinafter *2004 Task Force Report*] (suggesting portability alternatives to estate and generation-skipping transfer taxes).

[47] *See supra* note 40 (defining qualifying transfers).

[48] *See, e.g.*, KATHRYN G. HENKEL, ESTATE PLANNING AND WEALTH PRESERVATION 4-1 to 4-26 (2003) (providing fundamentals on optimizing the tax attributes of married couples).

amount. Any part of the decedent spouse's gross estate in excess of the credit shelter amount passed in a form that qualified for the marital deduction, with inclusion in the transfer tax base deferred until the SS's death.

The earliest mention of portability can be found in a 1988 report by the American Bar Association's Task Force on Transfer Tax Restructuring,[49] and a 2004 report by the Task Force on Federal Wealth Transfer Taxes.[50] These reports identified the cost and complexity in drafting and administering the Optimum Plan as problematic.[51] Furthermore, given the uncertainty as to the order of deaths, the Optimum Plan required each spouse to own enough assets in his or her own name to fully fund the non-marital (bypass) share at the first death.[52] This created a burden for spouses who were unable or unwilling to engage in the necessary inter vivos asset equalization.[53] According to the 2004 report, the losers in this scheme were couples "who [did] not engage in sophisticated planning or whose assets [did] not lend themselves to appropriate allocation."[54] After a failed attempt in 2006,[55] Congress temporarily enacted portability in 2010 and made it permanent in 2012.[56]

Although proponents of portability generally asserted that portability simply allowed spouses to achieve the results that otherwise would have been achievable through costly tax planning and re-titling of assets, portability allowed spouses to obtain better tax results than they could have with the best estate planning.[57] Notice in the second example above, that without portability, *H* and *W* could shelter only $8 million in assets from transfer taxation; whereas, with portability they can shelter up to $10 million. Importantly, Congress was aware of this result, as the Joint Committee on Taxation highlighted this in a 2008 report to the Senate Finance Committee.[58] The Joint Committee suggested that if Congress viewed this as problematic it could limit the DSUEA to the lesser of: (1) the combined value of the spouses' assets at the first death, or (2) the unused exemption amount of the

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[49] K. Jay Holdsworth et al., *Report on Transfer Tax Restructuring*, 41 TAX LAW. 395, 398–99 (1988) [hereinafter *1988 Task Force Report*].

[50] *See 2004 Task Force Report*, *supra* note 46, at 200–03.

[51] *See 1988 Task Force Report*, *supra* note 49, at 396 (analyzing the complexity of the then-current system); *see also* Robert B. Smith, *Unifying the Unified Credit*, 39 FLA. L. REV. 1153, 1163–70 (1987) (listing as complexities the need to educate clients, trustee selection issues, expenses, tensions between the SS and other trust beneficiaries, problem assets, and increased income taxes).

[52] *1988 Task Force Report*, *supra* note 49, at 396.

[53] *Id.*

[54] *2004 Task Force Report*, *supra* note 46, at 201.

[55] Estate Tax and Extension Tax Relief Act of 2006, H.R. 5970, 109th Cong. § 102.

[56] American Taxpayer Relief Act of 2012, Pub. L. No. 112-240, § 101 (c)(2), 126 Stat. 2313, 2318 (2013).

[57] JOINT COMM. ON TAXATION, TAXATION OF WEALTH TRANSFERS WITHIN A FAMILY: A DISCUSSION OF SELECTED AREAS FOR POSSIBLE REFORM 10 (2008).

[58] *Id.*

first to die.[59] By failing to implement either option, it appears that Congress intended to allow the SS to benefit from the DS's entire unused exemption, regardless of the value of the combined spousal assets at the DS's death and regardless of to whom those assets will ultimately pass.[60]

C. Gift-Splitting[61]

Although this is clearly a new development in the estate area, a limited form of elective spousal lifetime exemption sharing has existed under the gift tax since 1948 in the form of gift-splitting. The so-called split-gift provision was enacted in 1948 at the same time as the limited (fifty percent) marital deduction.[62] A valid gift-splitting election treats a gift by a married person to a non-spouse as if made one half by each of the spouses instead of as a transfer made entirely by the actual donor spouse. Both spouses must agree to split all gifts made by either spouse during the calendar year.[63]

Section 2513 deems each spouse as transferor of one half of the value of a gift, regardless of who actually owned the property (the "deemed transferor rule"). Gift-splitting does not require the non-donor spouse to have any interest whatsoever in the gift property.[64] If both spouses have unequal interests in the gift property, § 2513 equalizes their interests solely for tax computation purposes.[65] In the words of one learned treatise, "The section must be viewed simply as permitting an artificial assumption quite contrary to fact as a part of the determination of gift tax liability."[66] The assumption is that the spouses owned the gift property equally immediately prior to the gift.

Once the deemed transferor rule is applied, the gift tax computation is calculated separately for each individual spouse, with each spouse applying his or her own gift tax attributes to the deemed transfer. The gift tax consequences of an election may differ as between the spouses. For example, an election by a transferor spouse with no available unified credit to split gifts with a consenting spouse with full credit intact will not relieve the transferor spouse from gift tax payable on one half of the value of the gift property.[67]

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[59] *Id.* (recognizing that such a limit raised complexity and administrability concerns).

[60] *See* I.R.C. § 2010(c)(4) (defining the DSUEA as the last deceased spouse's unused unified credit amount without any limitation).

[61] I.R.C. § 2513 (2012).

[62] Revenue Act of 1948, Pub. L. No. 80-471, § 372, 62 Stat. 110, 127.

[63] I.R.C. § 2513 (a)(2); Treas. Reg. § 25.2513-1(b)(5) (as amended in 1983). "In other words, the consent to gift-splitting is bilateral." Diana S.C. Zeydel, *Gift-Splitting—A Boondoggle or a Bad Idea? A Comprehensive Look at the Rules*, 106 J. TAX'N 334, 335 (2007).

[64] STEPHENS ET AL., *supra* note 23, ¶ 10.03[2][a], at 10-90.

[65] *Id.*

[66] *Id.*

[67] *Id.*

In other words, § 2513 is not an authorization to share transfer tax exemptions, as is the case with portability.[68] Although in effect the spouses are sharing unified credits, in operation gift-splitting is actually more akin to the marital deduction method of accessing a spouse's effective exemption amount. Section 2513 implicitly deems a transfer of one half of the value of the gift property from the donor spouse to the consenting spouse (tax free due to marital deduction), and explicitly deems a transfer of that same amount from the consenting spouse to the ultimate non-spouse donee. The consenting spouse then calculates his or her gift tax liability as if the deemed transfers were real. So implicitly, the ability of the donor spouse to access the consenting spouse's gift tax credit relies on a prior marital deduction transfer. The statute merely relieves the parties from having to actually engage in the interim marital deduction step. Portability, on the other hand, allows spousal AEA sharing with no prerequisite transfer (actual or deemed).

III. POSITIVE ACCOUNT—WHERE THE LAW MAY BE HEADING

This Part argues that a logical extension of the progression in the law described in Part II above[69] would be congressional adoption of a provision authorizing elective sharing of exemption equivalents between spouses, in any proportion, during life or at death, without the necessity of a prior marital deduction transfer ("Positive Account"). Section A claims that the Positive Account is actually grounded in early proposals made by both the American Law Institute ("ALI") and Treasury to extend the then-existing gift-splitting regime. Sections B through D articulate the various components of the Positive Account and independently justify each based on arguments made by the ALI, Treasury, and proponents of portability.

A. ALI-Treasury Proposal

The Positive Account is not a completely novel suggestion—it is related to a 1969 proposal made by both the ALI and Treasury to extend gift-splitting in two ways: (1) to allow other than a fifty-fifty split, and (2) to allow gift-splitting at death.[70] Combined with its other recommendation for an unlimited marital deduction,[71] Treasury reasoned that:

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[68] *Id.*

[69] *See supra* notes 36–68 and accompanying text.

[70] U.S. TREASURY DEP'T, 91ST CONG., TAX REFORM STUDIES AND PROPOSALS: UNLIMITED MARITAL DEDUCTION 357–60, 377–81 (Comm. Print 1969), *reprinted in* GERSHAM GOLDSTEIN, READINGS IN DEATH AND GIFT TAX REFORM 114–21 (1971); AM. LAW INST., FEDERAL ESTATE AND GIFT TAXATION RECOMMENDATIONS OF THE AMERICAN LAW INSTITUTE, AND REPORTERS' STUDIES 38–39 (1969).

[71] AM. LAW INST., *supra* note 70, at 36; GOLDSTEIN, *supra* note 70, at 115.

> Because property passing to a spouse by gift will also be excludable, a couple could arrange to have taxed to either husband or wife the full amount, or any portion, of gifts to third persons, by use of prior transfers between themselves. To make such artificial circuity unnecessary, an option will be available to have any portion of any lifetime gift taxed as a transfer by the non-donor spouse, if the non-donor spouse consents. The rule will apply to transfers at death as well as during life.[72]

Although the ALI-Treasury proposal was never adopted, all of its components are integrated into and extended under the Positive Account, as detailed below.

B. Any Proportion

Recall that a gift-splitting election treats the spouses as equal co-transferors of any transfer to a third party by either spouse for gift tax calculation purposes. In 1948, this deemed allocation made sense, working in conjunction with the then-existing fifty-percent marital deduction, to roughly achieve the community property result in common law states.[73] In 1981, however, Congress enacted the current unlimited marital deduction and embraced the married couple as one economic unit for federal transfer tax purposes.[74] As a corollary, it should have adopted the related ALI-Treasury recommendation to revise § 2513 to remove the deemed fifty-fifty split on electing spouses' gifts.[75]

Similarly, the ALI-Treasury proposal would have allowed sharing of exemptions in any proportion at death. In contrast, portability is an all-or-nothing proposition—either the entire DSUEA is ported or none of it is. One could imagine a spouse wanting to limit the amount of the DSUEA to something less than all of the spouse's unused unified credit.[76] Accordingly,

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[72] GOLDSTEIN, *supra* note 70, at 120.

[73] *See supra* note 17 and accompanying text (discussing the enactment of transfer tax provision).

[74] *See supra* note 21 and accompanying text (discussing enactment of unlimited gift and estate marital deduction).

[75] *See Where the Bodies Are Buried—Why Reform: Hearings on Tax Reform Act of 1969 Before the H. Comm. on Ways & Means*, 91st Cong. 3977–85 (1969) (statement of Jerome Kurtz, former Tax Legislative Counsel, Treasury Department), *reprinted in* GOLDSTEIN, *supra* note 70, at 74 (explaining Treasury's proposed treatment of gift-splitting between spouses).

[76] One could imagine a DS limiting the DSUEA to only the value of marital deduction transfers to SS. *Cf.* Joseph M. Dodge, *Comparing a Reformed Estate Tax with an Accessions Tax and an Income-Inclusion System, and Abandoning the Generation-Skipping Tax*, 56 SMU L. REV. 551, 568 (2003) (opining that a bequest-neutrality rationale supports allowing a decedent's unused exemption to pass to the SS "only to the extent that it would have been used by the decedent spouse in the absence of the marital deduction," thereby limiting the DSUEA to the extent of

a complete implementation of the Positive Account would allow spouses to share their available AEAs *in any proportion*.

C. At Death

The ALI and Treasury also suggested extending gift-splitting to transfers at death.[77] Under this proposal, a SS could elect to be treated as the transferor of any portion of a DS's estate, thereby making the SS's exemption equivalent available to the DS's estate. As noted by the ALI, the DS could have achieved the same result by making a marital deduction transfer at death to the SS, who in turn, could give it to the ultimate beneficiary.[78] Gift-splitting at death removed the need for this "artificial circuity."[79]

There is some fallacy in this argument. The artificial circuity characterization only applies in a harmonious family setting where both spouses agree on the identity of the ultimate beneficiaries of marital wealth and that identity remains constant throughout both spouses' lifetimes. Absent this, the same dispositive plan may not be achievable when the SS elects gift-splitting at the DS's death as compared to when the DS makes a death-time marital deduction transfer to the SS.

There are also real economic differences between the DS transferring property to or for the benefit of the SS to access the benefit of the SS's AEA, versus the SS electing to allow the DS to utilize the SS's exemption equivalent without a related property transfer. With an interim marital deduction transfer, inclusion in the tax base is delayed until the SS's death. This timing difference can affect the amount of transfer tax levied and the property value that ultimately passes to the non-spouse beneficiary.[80] Furthermore, the SS will have at least a beneficial interest for life in any marital deduction property.[81] This can be important if the SS needs access to the property to maintain his or her standard of living. In contrast, property transferred tax-free at the DS's death to a non-spouse beneficiary via gift-splitting will be completely unavailable to the SS during his or her lifetime.

Notice that the ALI-Treasury proposal is the exact opposite of the carryforward of the DS's DSUEA to the SS under portability—it effectively

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marital deduction transfers to the SS (emphasis omitted)). Or a DS may want to limit carryover of his or her unused unified credit to the combined level of the marital assets at the first death. *Cf. supra* notes 57–59 and accompanying text (discussing the use of portability to enhance tax outcomes and proposed methods of fixing this outcome).

[77] AM. LAW INST., *supra* note 70, at 38–39; GOLDSTEIN, *supra* note 70, at 114–21.

[78] AM. LAW INST., *supra* note 70, at 37.

[79] *See supra* note 72 and accompanying text (quoting a Treasury report on the unlimited marital deduction).

[80] For example, there may be an increase or decline in the value of the asset or the amount of the SS's available exemption between the two deaths.

[81] This would depend on the form of the qualifying marital deduction transfer.

allows the carryback of the SS's AEA to the DS's estate. Given that these are mirror images of each other, the arguments made by the proponents of portability should apply with equal force to the proposal to allow the SS to elect gift-splitting at the DS's death.

Advocates argued that "portability promotes the federal tax policies of simplifying estate planning . . . and treating married individuals as a single economic unit, consistent with . . . gift-splitting, the unlimited marital gift and estate tax deductions, and . . . joint income tax returns."[82] In practice, portability merely adds an additional element to the already exceedingly complex decision matrix that applies to planning for a married couple.[83] The decision as to whether to rely on the Optimum Plan or utilize portability raises a host of new issues.[84] Nonetheless, one could interpret the "simplicity" claim as something akin to furthering "transfer tax neutrality." The Optimum Plan forces transfers into certain patterns or imposes disproportionately large transfer taxes if those patterns are not followed.[85] Portability removes one transfer-tax-driven motivation to own and dispose of a couple's assets in a certain way.

Portability advocates also argued that there were legitimate non-tax reasons for the bulk of a couple's wealth to be titled in only one spouse's name.[86] For example, transfer restrictions imposed by law or contract may prevent asset-shifting between spouses.[87] Portability provides relief from any transfer tax penalty for failing to equalize marital asset ownership, at least if the less-propertied spouse died first. The ALI-Treasury version of

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[82] DEVLIEGER & CARMONA, *supra* note 32, at 2.

[83] Blattmachr et al., *supra* note 45, at 232 (making this point); *accord* Doug H. Moy, *Unused Spousal Exemption Amount: 'There You Go Again,'* 33 TAX NOTES 847 (2011).

[84] Considerations include: expected length of time between spousal deaths, expected appreciation or decline in the value of marital assets between deaths, benefit of two income basis step-ups with portability versus only one with the Optimum Plan, likelihood and cost of an election by the executor of the estate of the first spouse to die, GST considerations because the GST exemption is not portable, asset protection concerns, state death taxes, and others. *See generally* Marc S. Bekerman, *Credit Shelter Trusts and Portability: Does One Exclude the Other?*, PROB. & PROP., May/June 2011, at 10 (discussing the factors that affect the choice between a portability election and traditional credit shelter trust planning); Blattmachr et al., *supra* note 45 (discussing the advantages and disadvantages of portability as compared to traditional marital planning); Paul S. Lee et al., *Venn Diagrams: Meet Me at the Intersection of Estate & Income Tax*, *in* 48 HECKERLING INSTITUTE ON ESTATE PLANNING 3-1 (2014) (comparing estate tax advantages of traditional estate planning with income tax advantages of portability). In addition, a SS who inherits a DSUEA now needs to plan to preserve that tax benefit in the event of remarriage. *See generally* Austin W. Bramwell & Leah Socash, *Preserving Inherited Exclusion Amounts: The New Planning Frontier*, 50 REAL PROP. TR. & EST. L.J. 1 (2015) (analyzing various techniques to preserve the DSUEA for the SS).

[85] *Accord* GOLDSTEIN, *supra* note 70, at 74 (Kurtz's statement making the same point with regard to Treasury's 1969 Proposal to allow unlimited gift-splitting).

[86] *See 2004 Task Force Report*, *supra* note 46, at 201.

[87] *Id.*

carryback of spousal AEAs would provide similar relief if the wealthier spouse died first.

Proponents also cited portability as promoting Congress's normative view that "a husband and wife should be treated as one economic unit for purposes of estate and gift taxes."[88] With an election, no matter who owns what property, as between the spouses, the couple is collectively entitled to take advantage of two times the individual AEA.[89] In Senate testimony supporting portability, one advocate noted that portability "would permit the actual result for a married couple to match the way the exemption is often viewed . . . [as] '$2 million per person, and $4 million for a married couple.'"[90] Elective sharing of spousal transfer tax exemptions at the first death (carryback and carryforward) would more closely comport to this view.

The ALI-Treasury form of gift-splitting at death only worked when the wealthier spouse died first. It could not be implemented in the manner suggested if the poorer spouse died first. Highlighting this problem in an article critiquing the 1969 Treasury proposals, one scholar suggested extending gift-splitting "to transfers by the surviving spouse during some limited period, such as six months, after the death of the first spouse."[91] This would have given the SS a limited opportunity to take advantage of a DS's unused unified credit after the DS's death. Notice this is essentially a more limited form of portability. It appears that portability's true origins lie in this proposal.

D. Transfer

Prior to portability, the AEA was a non-transferable, separate tax attribute of each spouse. The only way that one spouse could access the other

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[88] S. REP. NO. 97-144, at 127 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 228. A full implementation of this ideal would require, at a minimum, cumulating the spouse's assets for purposes of gross estate inclusion. Harry L. Gutman, *Reforming Federal Wealth Transfer Taxes After ERTA*, 69 VA. L. REV. 1183, 1225–35 (1983) (providing a comprehensive articulation of full implementation of the marital unit ideal); Anne-Marie Rhodes, *Individual, Couple or Family? The Unit of Taxation for Transfer Tax Purposes: A Shifting Focus*, 17 AKRON L. REV. 575, 599–600 (1984). *But see* Bridget J. Crawford, *One Flesh, Two Taxpayers: A New Approach to Marriage and Wealth Transfer Taxation*, 6 FLA. TAX REV. 757, 784–805 (2004) (arguing against the conception of the marital couple as the transfer taxable unit because it is based on gender stereotypes and denies estate and gift tax benefits to socially important non-marital relationships).

[89] *But see* Bridget J. Crawford & Wendy C. Gerzog, *Portability, Marital Wealth Transfers, and the Taxable Unit*, *in* CONTROVERSIES IN TAX LAW: A MATTER OF PERSPECTIVE, *supra* note 41, at 247, 252 (noting that "portability's 'merger' of the . . . exemption [of DS with that of SS] resembles coverture").

[90] *Outside the Box on Estate Tax Reform: Reviewing Ideas to Simplify Planning: Hearings Before the S. Fin. Comm.*, 110th Cong. 123 (2008) (statement of Shirley L. Kovar, Attorney, Branton & Wilson APC). The AEA at the time of this testimony was $2 million.

[91] David Westfall, *Revitalizing the Federal Estate and Gift Taxes,* 83 HARV. L. REV. 986, 999 (1970). Gift-splitting is not effective for gifts made by the SS after the death of the DS. Treas. Reg. § 25.2513-1(b)(1) (1983).

spouse's effective exemption amount was by shifting property into the other spouse's tax base. With the enactment of portability, Congress decoupled tax-free availability of a decedent spouse's unified credit from the requirement of a prior marital deduction transfer. Instead, Congress authorized elective sharing of a DS's exemption equivalent with a SS.

From this perspective, the current gift-splitting regime seems anachronistic because it still implicitly relies on a marital deduction transfer to allow a donor spouse to utilize a consenting spouse's unified credit. Recall that a gift-splitting election deems spouses as equal co-transferors of any gift made by either spouse, with each spouse limited to accessing his or her own unified credit to shelter the deemed transfers. Because the ALI and Treasury modeled their proposals after § 2513, they too utilize the deemed transferor model of marital exemption sharing.

Although it would be a step towards full implementation, the ALI-Treasury proposal falls short because it utilizes the deemed transferor approach and fails to account for the situation of the poorer spouse dying first.[92] A proposed extension of the ALI-Treasury proposal would partially deal with that problem; however, it too is rejected as a less effective, more cumbersome version of portability.[93] The existing gift-splitting regime is lacking because it is only available for inter vivos transfers, clings to the deemed transferor model, and splits gifts in only a fifty-fifty proportion.[94] With portability, AEA sharing flows only one way at the first death—from the DS to the SS. There is no way for the SS to share his or her exemption equivalent with the DS's estate. Accordingly, to completely operationalize the Positive Account, Congress would need to repeal the current gift-splitting and portability regimes, and enact a provision that allows elective sharing between spouses of their respective unified credits, in any proportion, during life or at death.

IV. Implications

Although this Article does not provide a full-blown analysis, this Part sketches out some likely implications of full implementation of the Positive Account. Elective sharing of AEAs between spouses would substantially increase complexity in planning for married couples, even beyond that introduced by gift-splitting[95] and portability.[96] Each spouse would need to determine whether, when (during life or at death), and in what amount (be-

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[92] *See supra* notes 70–72 and accompanying text.
[93] *See supra* note 91 and accompanying text.
[94] *See supra* notes 61–68 and accompanying text.
[95] *See* Zeydel, *supra* note 63, at 334–35, 339.
[96] *See supra* note 84 and accompanying text.

tween 0% and 100%) to share a unified credit with the other spouse. These decisions may be made at a time when future uncertainties abound (e.g., relative spousal wealth, marriage or family status, tax law changes, order of deaths, etc.). Demand for professional advice would substantially increase. As a result, any potential tax savings realized from utilizing elective exemption sharing between spouses may be captured by estate-planning advisors.[97]

Under the Positive Account, the unified credit of a married person transforms from an individual tax attribute that shelters gifts from taxation into something akin to property itself—it has economic value[98] and would be transferable during life or at death to one's spouse. As a result, the use (or non-use) of each spouse's AEA would need to be addressed in marital agreements, estate planning documents, separation agreements, and divorce agreements, to name a few.[99] The stakes would be high because sharing of an AEA with a spouse would be an irrevocable act. A SS's exemption equivalent utilized by a prior DS would not be available to shelter any unexpected future increases in the SS's wealth. If a marriage ends in divorce, there is no direct method to recapture any previously shared unified credit.[100]

Complete implementation of elective sharing of unified credits between spouses may require repeal of the QTIP provisions. Recall that under QTIP, one spouse (the tax-benefited spouse) may utilize the other spouse's (the tax-burdened spouse) AEA without the tax-burdened spouse's consent. This is incompatible with the Positive Account that vests control over the use of a spouse's AEA with that spouse.

Enactment of elective marital exemption sharing may reduce the number of purely tax-motivated transfers between spouses because a prior marital deduction gift would no longer be a necessary prerequisite to tax-free availability of a spouse's AEA.[101] Electivity may also act as a hedge against impoverishment of the less-propertied spouse[102] by providing bargaining leverage in marital negotiations. A shrewd spouse could demand compensa-

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[97] *Accord* Crawford & Gerzog, *supra* note 89, at 257 (noting that portability may result in a transfer of wealth to estate-planning advisors in the form of fees).

[98] Value would be equal to the transfer tax saved upon its application. *See* Zaritsky, *supra* note 35, at 48 (suggesting that the DSUEA should be viewed as an asset of the estate and that the estate should be compensated by the SS for its transfer).

[99] *See id.* (suggesting that a decedent should direct in a will or revocable trust whether the executor should elect portability or not).

[100] This problem exists under gift-splitting as well. Query whether a spouse should or could demand compensation for a previously shared AEA in the event of divorce. *Cf. id.* (suggesting that the SS should compensate the DS's estate for access to the DS's DSUEA).

[101] Crawford & Gerzog, *supra* note 89, at 247 (observing that portability will likely reduce the frequency of QTIP transfers).

[102] *Id.* at 251–52 (noting that in a heterosexual marriage, the female spouse often lives longer and is less wealthy than the male spouse).

tion for the use of his or her exemption in the form of a property transfer.[103] On the other hand, if the power dynamics are such that the poorer spouse is susceptible to undue pressure by the wealthier spouse, the family, or advisors, then control over the unified credit may be illusory.

CONCLUSION

Prior to 2010, the only way that one spouse could access the benefit of the other spouse's AEA was via a prior marital deduction transfer (actual or deemed). This Article views the introduction of portability as signaling congressional intent to move towards a model of elective marital sharing of unified credits without the necessity of a prior shift in the tax base between the spouses. Full realization of this principle would require Congress to repeal the current gift-splitting and portability regimes, and in their place, enact a provision that allows elective sharing of exemption equivalents between spouses, in any proportion, during life or at death. Although the Article raises several possible effects of such an extension of current law, the desirability of such a move remains to be explored in future work.

[103] *See supra* note 100 and accompanying text. Of course, the existence of the QTIP option substantially weakens the poorer spouse's negotiating leverage.