MANY UNHAPPY RETURNS: ESTATE TAX RETURNS OF MARRIED DECEDEENTS

Richard Schmalbeck & Jay A. Soled

TABLE OF CONTENTS

I. INTRODUCTION ................................................................. 361

II. OVERVIEW OF THE ESTATE TAX RETURN FILING REQUIREMENT AND A SHORT HISTORY OF THE ESTATE TAX ................................................................. 365

III. THE PROPOSAL AND REASONS FOR ITS ADOPTION .... 369

IV. CRITICISMS OF THE PROPOSAL ........................................ 371
   A. Collection of Estate Tax .................................................. 372
   B. Ability to Monitor Future Tax Events .............................. 378
      1. Date of Death Values of the Predeceased Spouse’s Assets .................................................. 379
      2. Beneficiaries’ Names and the Value of Assets That Pass to or on Their Behalf ....................... 380
      3. Generation-Skipping Transfer Tax Exemption Allocation .................................................. 382
      4. Estate Administration Expenses .................................. 383

IV. CONCLUSION ..................................................................... 385

I. INTRODUCTION

High on any American’s list of tax-related annoyances is the process of completing and filing tax returns. In most cases, however, the return is an essential part of revenue collection; without it, the Internal Revenue Service (Service) would have difficulty verifying that the computation and declaration of tax liabilities were accurate. Occasionally, however, the Internal Revenue Code (Code) compels a

* Richard Schmalbeck is a professor at the Duke University School of Law, and Jay A. Soled is a professor at the Rutgers University School of Business. The authors thank Martha Eller and Jacob M. Mikow of the Statistics of Income Bureau of the Internal Revenue Service for their assistance in accessing data on estate tax returns. Of course, the views presented in this article are exclusively those of the authors.
taxpayer to file a return that has little or no connection to the payment of a tax.¹

Where clear instances of this phenomenon can be identified, they should be closely reviewed because they may impose heavy burdens pointlessly.

This article demonstrates that the imposition of an automatic estate tax return-filing requirement, based exclusively on the size of the gross estate, imposes such pointless burdens in many cases. In particular, because the use of the unlimited marital deduction is so extensive, and so effective in eliminating estate tax liabilities for married decedents, the estates of such decedents should only be required to file estate tax returns in the relatively unusual case in which the estate actually has an estate tax liability.

It will be useful to preface our argument with a brief consideration of the most familiar tax return, the Form 1040. Some 125 million 1040s (and their close relatives, the 1040A and the 1040EZ) were filed by individual taxpayers in 1998, the most recent year for which such data are available.² Most of these returns—about 93 million, or 74% reported positive tax liabilities.³ Of the 32 million tax returns that showed no positive tax liability, some 27 million returns were filed by taxpayers who were entitled to refunds, either because they were eligible for a refundable credit (such as the earned income credit), or because they had had income tax withheld, or both. Less than 4% of income tax returns were filed, as it were, simply to satisfy the curiosity of the Service, having no effect on either the payment of a tax or the generation of a refund.

The fact that most income tax returns actually relate to payments of tax or refunds is not an accident. The obligation to file a return is calibrated to produce this result in most cases. If a person enjoys income that is potentially taxable, but in amounts that are less than

¹ Some returns are not meant to accompany any final declaration or payment of a tax liability. For example, a partnership files annually a Form 1065 but computes no tax liability and pays no tax. Predicated on the Form 1065, however, a partnership distributes to each partner a Schedule K-1, on which that partner’s share of partnership income and deduction items are shown. The Form 1065, then, does play a vital role in the computation and payment of tax liabilities by a partnership’s partners.


³ Id. This is not to say that they had net liabilities after accounting for tax withholding; in fact, most taxpayers with positive tax liabilities have had sufficient tax withheld so that they are in a position to receive refunds upon the filing of their returns.
the sum of the personal exemption(s) and standard deduction for which she would be eligible, then there is ordinarily no obligation to file a return.\footnote{The amounts involved depend on the taxpayer's age, marital status, and a few other variables. For example, in 1998 a single taxpayer under the age of sixty-five would normally have been required to file a return only if his income had been greater than $6,950, the sum of his personal exemption ($2,700) plus his standard deduction ($4,250). This general rule is subject to a number of exceptions; for example, if the taxpayer can be claimed as a dependent by another taxpayer, then the taxpayer would be obligated for that year to file a return if either the taxpayer's total income exceeded $4,250 or the taxpayer's unearned income exceeded $700.} This simply recognizes the fact that the gross income in such cases will be canceled by the subtraction of the exemption and the standard deduction, resulting in zero or negative taxable income, and, hence, no net tax liability.

The return obligation in the case of a decedent's estate superfi-
cially resembles the rules of the income tax, in the sense that the ob-
ligation to file an estate tax return is imposed only if the value of the
gross estate exceeds the amount that is effectively exempted from
taxation by the "unified credit," or, as some prefer, the "applicable
credit amount."\footnote{An estate tax return must be filed for a U.S. citizen (wherever resident) or U.S. resident if the gross estate exceeds the "applicable exclusion amount" (i.e., the amount excluded by the applicable credit amount) in effect for the calendar year that includes the date of death. I.R.C. § 6018(a)(1). The caption of section 2010, which provides the rules sheltering wealth transfers below certain thresholds, is "Unified Credit Against Estate Tax." The legally operative words of that section use the phrase "applicable credit amount." Id. § 2010.} This credit imposes a threshold prior to the imposition estate tax which, in recent years for which tax return data are available, has been about $600,000.\footnote{The Taxpayer Relief Act of 1997 mandated a series of uneven increases in this threshold, until it reached a level of $1,000,000 in 2006. H.R. 2014, 105th Cong., 111 Stat. 788 § 501 (1997). This schedule has been supplanted for years after 2001 by the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001, which provides thresholds of $1,000,000 for estates of decedents dying in 2002-03; $1,500,000 for estates of decedents dying in 2004-05; $2,000,000 for estates of decedents dying in 2006-08; and $3,500,000 for estates of decedents dying in 2009. H.R. 1836, 107th Cong., 115 Stat. 38 § 521 (2001). In 2010, the estate tax temporarily ceases to exist, but in 2011, the threshold will return to $1,000,000, unless there is further Congressional action on this point, before this date.} The resemblance is more in form than in effect, however, because a high percentage of estates above the filing threshold have deductions or credits that eliminate any net estate tax liability. In 1997, the latest year for which complete data are available, only about 43,000 (or about 47.7\%) of the roughly 90,000 estate tax returns filed showed any net tax liability.\footnote{Internal Revenue Service. Statistics of Income Bulletin, vol. 19, no. 1, at 102}
The obvious converse should be emphasized: *the majority of estate tax returns showed no estate tax liability.*\(^8\) As a practical matter, because there is no withholding of estate tax obligations nor any refundable estate tax credits, the 47,000 estate tax returns that showed no net estate tax liability—about 52.3% of the total—cannot be said to relate to the computation or payment of any positive tax liability. They exist primarily for the purpose of demonstrating to the Service that no tax is due.

There are many reasons why an estate which exceeds the filing threshold of taxability may nevertheless ultimately owe no estate tax, having to do generally with the various deductions that are available to estates. For example, a decedent may leave a great deal of her wealth to charity, generating a sufficient deduction to reduce her otherwise taxable estate to an amount below the threshold of taxability.\(^9\) But there is one deduction, taken by one particular category of decedent, that explains most of the nontaxable estate tax returns: since 1981, section 2056 has provided an unlimited deduction for transfers to a surviving spouse.

To say that most married decedents take advantage of this deduction would be a considerable understatement. On the contrary, it is only a slight overstatement to say that the estate tax does not apply at all to the estates of married decedents. Among decedents who died in 1995 (the most recent year for which full breakdowns of data by marital status are available), deductions for bequests to surviving spouses amounted to nearly $41 billion of the roughly $69 billion left by married decedents.\(^{10}\) Together with other deductions and the unified credit, this produced a remarkably low estate tax impact on married decedents, as measured by the percentage of estate tax returns that showed a positive tax liability. More precisely, only about one out of seven estates of married decedents that were subject to an estate tax filing obligation actually owed any estate tax liability.\(^{11}\) In contrast, despite having slightly smaller average gross estates, unmarried decedents whose estates were subject to filing requirements ended up having estate tax liabilities three-quarters of the time.\(^{12}\) The marital status of the decedent is, thus, a powerful predictor of

---

\(^8\) *Id.*

\(^9\) The charitable deduction for estate tax purposes under section 2055 is unlimited in amount; even a very wealthy decedent can completely avoid the estate tax if she gives all or most of her estate to charity.


\(^11\) *Id.*

\(^12\) *Id.*
whether any estate tax will be due from a decedent’s estate—much more so than the size of the gross estate, which is currently the sole determinant of the existence of an estate tax filing obligation.

When six out of seven estates in a particular category are obligated to file estate tax returns just to satisfy the Service that no estate tax is owed, a review of the filing obligation seems clearly indicated. Imaginably, some extraordinary considerations could exist to support the imposition of filing estate tax returns on a category of estates that is largely nontaxable. After examination of the arguments militating in that direction, however, we conclude that the benefits of a general estate tax filing requirement for estates of married decedents having gross estates above the threshold of taxability are significantly outweighed by the burdens of such a requirement. Accordingly, we propose that Congress modify the current rules on mandated estate tax filing so that the estates of married decedents be obligated to file estate tax returns only if the executor or administrator determines that there will be a net estate tax liability.

In advocating this proposal, we divide our analysis into several parts. First, we present an overview of the estate tax return filing requirement and an abridged history of the estate tax. Second, we set forth the fundamental elements of this proposal and delineate the affirmative arguments against retention of the current general filing requirement with respect to married decedents. Third, we defend against anticipated criticisms of this proposal. A brief concluding section summarizes our position.

II. OVERVIEW OF THE ESTATE TAX RETURN FILING REQUIREMENT AND A SHORT HISTORY OF THE ESTATE TAX

From the inception of the estate tax, there has been a concomitant requirement that estates above a certain size file an estate tax return.\(^\text{13}\) The reason for instituting a return requirement is obvious: it provides the government with the means to monitor compliance and collect revenue.

Since the estate tax return must mirror the considerable intricacies of the estate tax, compliance comes at a price. For example, a Form 706 (U.S. Estate (and Generation-Skipping Transfer) Tax Return) includes twenty-one schedules and covers forty-four pages. Its instructions alone are a daunting twenty-five pages. Executors who

\(^{13}\) Revenue Act of Sept. 8, 1916, Pub. L. No. 64-271, § 205, 39 Stat. 756 ("The executor shall...file...a return...where the gross estate at the death of the decedent exceeds $60,000....").
must complete this form almost invariably retain professional assistance in dealing with this morass. The Service itself estimates that a typical estate tax return requires over thirty hours to complete.14 With professional fees ranging from $200 to $600 an hour, compliance costs running into five figures are presumably the norm.

Perhaps even more important than the direct costs of compliance is the delay associated with the current estate tax return-filing requirement. Many executors choose not to make estate distributions until they receive a closing letter from the Service that verifies the accuracy of the estate tax return. Because estate tax returns are not due until nine months after the death of a taxpayer (fifteen months if the executors file for an extension),15 and because the Service usually does not issue an estate tax closing letter until six months after submission of the return, this precautionary stance can create significant hardships on the estate’s beneficiaries, delaying the enjoyment of their inheritances by anywhere from fifteen months to two years from the date of the decedent’s death.16

The expense and delay associated with estate tax return compliance do not end with the taxpayer, however. Even though there is rarely any revenue at stake, the Service must still process these returns and, in some cases, audit them for their accuracy using rela-

---

15 I.R.C. § 6075(a) (setting forth the requirement that estate tax returns are due nine months after a decedent’s death); Treas. Reg. § 6081-1 (using a Form 4768, an executor can request an extension of up to six months to file the Form 706). More often than not, executors file an extension. This is because if the surviving spouse dies during the intervening six months, significant estate tax dollars may be saved as the predeceased spouse’s executors take advantage of the graduated rate structure of the estate tax and do not fully utilize the estate tax marital deduction. The estates of both spouses thereby incur a combined estate tax rate that is lower than if the asset value of their combined estates all had been subject to higher graduated estate tax rates in the estate of the surviving spouse. See, e.g., Michael M. Mariani, Understanding Estate, Gift & Fiduciary Income Tax Returns: Strategies for Maximum Advantage with the “706”, “709” & “1041”, PRACTICING LAW INSTITUTE no. D0-006N (Jan. 2001) (“The executor should give serious consideration to securing an extension of time to file the estate tax return when assets pass to a QTIP trust. If the surviving spouse dies or becomes seriously ill within the six month extension period, the executor may wish to make a partial QTIP election (or elect not to make a QTIP election) to reduce the combined estate taxes.”).
16 It may be that executors are excessively cautious, and in some cases might imaginably be ordered to make some distributions in advance of receipt of the closing letter. But estate administration is and has always been a conservative field, so this idea would likely be even less warmly received than our suggestion that filing requirements be truncated for married decedents.
tively expensive personnel with expertise in the complexities of the estate tax.\textsuperscript{17}

While the estate tax return requirement has remained essentially constant from its inception, the underlying estate tax has undergone several fundamental changes. Introduced in 1916, the first estate tax formally applied to the estates of all taxpayers.\textsuperscript{18} An exemption of $50,000 (in the form of a deduction),\textsuperscript{19} however, shielded most taxpayers from paying estate tax and from filing estate tax returns. During the following years, Congress periodically changed the amount of the exemption,\textsuperscript{20} settling in 1942 at $60,000,\textsuperscript{21} where it remained unchanged for the next three decades.

In 1976, Congress fundamentally reformed the U.S. transfer tax system. It replaced the dual estate and gift tax rate schedules with a single, unified one, supplanted the dual estate and gift tax exemptions with a “unified credit” that taxpayers could use during life or upon death to shelter otherwise taxable transfers from tax, and increased to $175,625 the amount that taxpayers could transfer tax-free.\textsuperscript{22} In 1981, Congress significantly raised the amount of the unified credit, enabling taxpayers to shelter from transfer tax up to $600,000.\textsuperscript{23} In 1997, Congress renamed the unified credit the “applicable credit amount” and instituted a gradual increase in the amount that a taxpayer could shelter so that by 2006 taxpayers would be able to transfer up to a $1,000,000 of their assets free of transfer tax.\textsuperscript{24}

In 2001, Congress voted to raise the amount taxpayers could shelter from estate tax gradually over the next nine years to

\textsuperscript{17} Audit rates are believed to be much lower for returns from the estates of married decedents, though data on this point does not appear to be publicly available.


\textsuperscript{19} Id. § 203.

\textsuperscript{20} The amount of the exemption in effect for the following tax years was as follows:

<table>
<thead>
<tr>
<th>Years</th>
<th>Exemption Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1916-1926</td>
<td>$50,000</td>
</tr>
<tr>
<td>1926-1932</td>
<td>$100,000</td>
</tr>
<tr>
<td>1932-1935</td>
<td>$50,000</td>
</tr>
<tr>
<td>1935-1942</td>
<td>$40,000</td>
</tr>
<tr>
<td>1942-1976</td>
<td>$60,000</td>
</tr>
</tbody>
</table>


$3,500,000. In addition, Congress voted to eliminate the estate tax entirely in 2010. However, because the Congressional leadership decided it could not count on the votes of sixty Senators necessary to make changes to the Code that would increase the deficit in the “out years” (beyond 2010), the Economic Growth and Tax Relief Reconciliation Act of 2001 will expire in 2011, causing the law to revert to its 2001 contours. Thus, another affirmative Congressional enactment will be necessary to truly repeal the estate and gift tax. In view of projected budget deficits, the Social Security funding problems that loom on the horizon, and the amount of revenue the estate tax generates, the permanent repeal is far from certain. Indeed, many commentators in the academic and political community doubt that it will be enacted within the foreseeable future.

The estate tax marital deduction has also undergone several important changes over the past half century. When the estate tax was first introduced, it contained no marital deduction. In 1948, however, in an attempt to achieve parity between community and noncommunity property states, Congress introduced a limited estate tax marital deduction. Executors were allowed to deduct up to one-half of the value of their estate with respect to assets that passed to a surviving spouse. Then, as part of its 1976 reforms, Congress expanded the estate tax marital deduction to 50% of the value of a taxpayer’s adjusted gross estate or $250,000, whichever was greater. Finally, in 1981, in an endeavor to treat married taxpayers as a single economic

---

26 Id.
28 See, e.g., Tom Herman, Nothing Is Sure About ‘Death Tax’, WALL ST. J., May 25, 2001, at C1 (reporting that there is nearly unanimous agreement among all law makers that the length of the phase out virtually ensures that estate tax repeal will not come into being).
unit, Congress instituted the unlimited estate tax marital deduction.\textsuperscript{31} This law entitles estates to a full deduction of the value of any property passing to a surviving spouse.\textsuperscript{32} Of course, assets qualifying for this deduction which are not consumed by the surviving spouse will normally end up in the surviving spouse's gross estate.\textsuperscript{33} Thus, for large estates, in which the income from the inherited property is sufficient to support the surviving spouse, the marital deduction tends to defer estate tax obligations rather than eliminate them altogether.

The introduction of the unlimited estate tax marital deduction has had a significant effect on estate planning strategy, and in turn, on the kind of estate tax returns that taxpayers file. Of particular importance, it has dramatically reduced the number of taxable returns filed by estates of married decedents.\textsuperscript{34}

If Congress had written the return requirements contemporaneously with the enactment of the marital deduction, it seems likely (at least to us, at any rate) that they would have been reluctant to impose a general return requirement on the estates of married decedents, the vast majority of which would not in fact have an estate tax liability. In the actual event, of course, Congress does not appear to have considered the impact of the estate tax marital deduction on the likelihood that estate tax returns filed for married decedents would be taxable. Our modest proposal is simply that Congress should correct this oversight by eliminating the general obligation to file estate tax returns on the basis of the size of the gross estate in the case of estates of married decedents.

III. THE PROPOSAL AND REASONS FOR ITS ADOPTION

The salient elements of this proposal would be as follows: the Code would set forth a general rule that no estate tax return needs to be filed when no estate tax is due with respect to the estate of a decedent who is married at the time of death. In the simplest case, Congressional adoption of this rule would mean that if a married dece-

\begin{footnotes}
\footnote{I.R.C. § 2056(a).}
\footnote{I.R.C. §§ 2033, 2044(a). Of course, the surviving spouse may pursue more aggressive estate planning measures than the decedent spouse did, using such techniques as annual gifts, grantor retained annuity trusts, and the like, to reduce the estate. So the pattern described in the text is far from inevitable.}
\footnote{Internal Revenue Service, Statistics of Income Bulletin, vol. 19, no. 1, at 102 (Summer 1999).}
\end{footnotes}
dent left his entire estate outright to his spouse, the estate would not be obligated to file an estate tax return.

This general rule would extend well beyond outright bequests to surviving spouses, however. It could also apply in cases where taxpayers bequeathed assets in any form of trust that qualified for the estate tax marital deduction, if such bequests left the taxable estate at or below the exemption level.

Consider prototypical wills for married taxpayers—the terms of which are so common that virtually every lawyer with an estate planning practice has the appropriate boilerplate language to effectuate them. The terms of each will establish a “by-pass trust,” funded with assets equal in value to the taxpayer’s unused unified credit exemption amount,\(^{35}\) and a “QTIP trust,” that qualifies for the estate tax marital deduction, funded with assets equal to the balance of the taxpayer’s estate.\(^{36}\) Because the combination of these bequests does not—indeed, cannot—generate any estate tax, under our proposal, the Code would not require that an estate tax return be filed for estates planned in this way.

Two corollaries of this general rule would be as follows. First, an executor would have to file an estate tax return if the aggregate value of bequests passing to nonspousal beneficiaries exceeded the amount of the taxpayer’s unused unified credit exemption amount. For example, suppose a decedent leaving a gross estate of $10 million bequeathed $3 million to the children of his first marriage rather than to his surviving spouse. In this case, the taxpayer’s executor would have to file an estate tax return.

Second, an executor would have to file an estate tax return in cases where a taxpayer bequeathed assets to or for the benefit of the taxpayer’s surviving spouse in a fashion that did not qualify for the estate tax marital deduction.\(^{37}\) For example, if a taxpayer established

\(^{35}\) As noted above, see supra note 6, Congress has from time to time phased in larger effective exemptions, so estate planners typically refer simply to the maximum exemption amount, rather than specify particular dollar amounts. For decedents dying in 2001, the maximum exemption amount is $675,000. I.R.C. § 2010(a).

\(^{36}\) To illustrate, suppose a married taxpayer dies in 2001, leaving a taxable estate of $2 million, and suppose further the taxpayer had executed a prototypical will. His executor would bifurcate the assets held in the taxpayer’s estate into two trusts, a by-pass trust funded with $675,000 and a qualified terminable interest property (QTIP) trust funded with $1,325,000.

\(^{37}\) If there were questions whether a particular bequest qualifies for the estate tax marital deduction, a taxpayer can always request a private letter ruling from the Service on the issue of qualification.
a testamentary trust for the benefit of his spouse intending for it to qualify for the marital deduction, but the trust terms failed to meet a statutory requirement for qualification (e.g., it did not provide the surviving spouse with a lifetime annual income right\textsuperscript{38}), the taxpayer's executor would have to file an estate tax return.\textsuperscript{39}

There would only be one exception to the rule allowing executors of estates of married decedents not to file estate tax returns if there was no estate tax liability: an executor would have to file an estate tax return whenever the surviving spouse was not a U. S. citizen. Bequests to noncitizen spouses do not qualify for the estate tax marital deduction.\textsuperscript{40} While it is true that a the bequest to a noncitizen spouse may qualify for a marital deduction if made to a qualified domestic trust,\textsuperscript{41} the elements of a qualified domestic trust are numerous and highly technical.\textsuperscript{42} Thus, failure to retain the filing requirement in this instance could frustrate the Service's ability to monitor compliance.

Under the proposal, the number of estate tax return filings would decline significantly. As Table 1 from the Statistics of Income Bulletin shows, only about one of seven married decedents has any net estate tax liability, and less than 1% of estate tax returns shows bequests to noncitizens.\textsuperscript{43}

IV. CRITICISMS OF THE PROPOSAL

The primary objections to this proposal would be that its adoption might jeopardize the collection of estate tax at the demise of the surviving spouse and also hamper the Service's ability to monitor future income tax events. A thorough analysis of these objections, however, suggests that they are not entitled to great weight.

\textsuperscript{38} I.R.C. § 2056(b)(7)(B)(i)(II).
\textsuperscript{39} Failure to institute this rule could thwart congressional intent, for taxpayers might take the liberty to devise their own form of "marital trust" that they would assert qualified for the estate tax marital deduction.
\textsuperscript{40} I.R.C. § 2056(d)(1).
\textsuperscript{41} Id. § 2056(d)(2).
\textsuperscript{43} For example, in 1999 only 0.7% of estate tax returns indicated bequests made to noncitizen spouses. Internal Revenue Service, Statistics of Income Bulletin, vol. 20, no. 2, at 26 (Fall 2000).
At first blush, one might object to our proposal on grounds that the absence of a return to examine would diminish the Service's opportunity to contest an executor's determination that no tax was owed. While that cannot be flatly denied, it is clear on reflection that this argument suffers from overbreadth. Under current law, more than 95% of decedents' estates are not obligated to file estate tax returns. This is because the executor determines that the size of the estate is below the filing threshold. That determination may involve errors or bad faith, yet this filing decision is insulated from the direct scrutiny of the Service because no return is filed. But this very general problem of tax administration (which has counterparts in the income and gift tax rules) is mitigated by the presence of penalties that may be imposed if the Service, by one means or another, should later find that an executor's determination was erroneous or fraudulent. In the case of estate tax returns, willful failure to file is criminally punishable under section 7203, and civil penalties are available under section 6651. While there is no doubt some revenue loss that results from the fact that the estate tax return obligation is not universal, Congress's choice to forego such a filing requirement indicates its willingness to tolerate a modest revenue leakage in the interest of lightening the burdens of compliance. That reasoning should apply with equal force to the imposition of automatic filing burdens on the estates of married decedents possessing assets, the aggregate value of which triggers application of the filing requirement.

A. Collection of Estate Tax

Some background on how the marital deduction is actually used by estate planners illuminates the likely concerns regarding our proposal. The marital deduction is by a wide margin the most important of the several deductions permitted by the estate tax provisions, accounting for more than two-thirds of all deductions in typical years.44 Through its use, taxpayers are able to defer estate tax until the death

---

44 For example, on returns filed in 1997, marital deductions accounted for over $49 billion of the $73 billion of deductions claimed. Internal Revenue Service, Statistics of Income Bulletin, vol. 19, no. 1, at 105 tbl.1c (Summer 1999). For an article stressing the importance of the estate tax marital deduction and the role it plays in estate planning, see Joel C. Dobris, Marital Deduction Estate Planning: Variations on a Classic Theme, 20 SAN DIEGO L. REV. 801, 801 (1983) (“Property transfers between spouses—marital deduction transfers—which take effect when the first spouse dies are the linchpin of most tax-oriented estate plans.”).

Dispositions that qualify for the estate tax marital deduction come in many forms. An outright bequest made to a surviving spouse is the most common.\footnote{I.R.C. § 2056(a). Recent surveys indicate that most husbands generally desire to leave all their property to their widows. \textit{See} Jesse Dukeminier & Stanley M. Johanson, \textit{Wills, Trusts, and Estates} 70-71 (5th ed. 1995); Henry M. Or- dower, \textit{Trusting Our Partners: An Essay on Resetting the Estate Planning Defaults in an Adult World}, 31 PROP. PROP. & TRUST J. 313, 318-19 (1996).} Other forms of disposition that qualify for the estate tax marital deduction include the following: (1) general power of appointment trusts,\footnote{\textit{Id.} § 2056(b)(5).} (2) life insurance settlements,\footnote{Treas. Reg. § 20.2056(c)-2(b)(1) (as amended in 1994); Rev. Rul. 56-26, 1956-1 C.B. 447; Rev. Rul. 68-554, 1968-2 C.B. 412.} (3) so-called “estate trusts”;\footnote{I.R.C. § 2056(b)(7).} and (4) qualified terminable interest property trusts (QTIP trusts).\footnote{Chris J. Prestopino, \textit{Strategies Recommended by Experienced Estate Planners}, 133 TR. & EST. 47, 50-51 (Jan. 1994); Mark B. Edwards, \textit{When to Use a QTIP Trust and How to Structure It}, 41 N.Y.U. ANN. INST. FED. TAX’N 49.01-49.07, at 49-1 to 49.16 (1983). The leading text on drafting marital deduction clauses prefers the QTIP trust and includes only QTIP provisions in the forms section. \textit{See} Richard B. Covey, \textit{Marital Deduction And Credit Shelter Dispositions And The Use Of Formula Provisions} 147-48, 195-204 (1984).} The last of these—the QTIP trust—has emerged as the clear favorite of most estate planners, probably because QTIP trusts allow the predeceased spouse to control the ultimate disposition of their assets, while the other forms effectively cede that control to the surviving spouse.\footnote{\textit{See} Estate of Clayton v. Comm’r, 976 F.2d 1486, 1491 (5th Cir. 1992), rev’g 97 T.C. 327 (1991) ("An essential feature of the marital deduction from its very beginning...[is] that any property of the first spouse to die that passed untaxed to the surviving spouse should be taxed in the estate of the surviving spouse.").} As a general matter, upon the surviving spouse’s demise, assets held by or for the benefit of the surviving spouse, including those that formerly qualified for the estate tax marital deduction (to the extent they are not exhausted), are includible in the estate of the surviving spouse.\footnote{\textit{Id.}} Thus, as noted above, at least as to assets not consumed by
the surviving spouse during his or her life, the marital deduction defers estate tax liabilities but does not make them disappear. QTIP trusts present a potential difficulty in this regard, because the assets in such trusts would ordinarily be excluded from the surviving spouse's estate on grounds that such spouse had no control over the trust. Congress therefore added section 2044, which requires that any property held in a QTIP trust be included in the estate of the surviving spouse.\(^{53}\)

Given the significance of the estate tax marital deduction, the single most important schedule on the estate tax return for estates of married decedents is Schedule M, on which bequests qualifying for the marital deduction are reported. Failure to list a particular asset on this schedule means that it does not qualify for the estate tax marital deduction.\(^{54}\) A corollary to this rule is that assets owned by the predeceased spouse that are not listed on Schedule M are generally not included in the surviving spouse's gross estate.

This situation creates—both presently and under our proposal—potential opportunities for taxpayers to "whipsaw" the government by taking inconsistent positions on the respective estate tax returns of the two spouses. On the one hand, the executors of the predeceased spouse's estate could assert that assets held in a QTIP trust established under the terms of the predeceased spouse's will qualified for the estate tax marital deduction. On the other hand, the executors of the surviving spouse's estate could argue that the assets held in the QTIP trust should not be included in the surviving spouse's estate on grounds that the trust was somehow technically flawed (e.g., failed to pay all the trust income to the surviving spouse) or, alternatively, on a theory that a valid QTIP election was not made. On the basis of either theory, section 2044 would not be triggered and the assets held in the QTIP trust would escape inclusion in the surviving spouse's estate. Were the statute of limitations closed with respect to the predeceased spouse's estate (which typically occurs three years following the filing of the return), the government would be stymied in collecting estate tax from either estate.

The whipsawing issue is a legitimate concern. Indeed, several litigated cases have addressed the issue of whether the estates of two spouses could take inconsistent positions with respect to whether property of the predeceased spouse qualified for the estate tax marital deduction and whether such property should be included in the surviving spouse's estate. Taxpayers met with some initial success in

---

\(^{53}\) I.R.C. § 2044(a).

\(^{54}\) Treas. Reg. § 20.2056(b)-7(b)(4).
the lower courts\textsuperscript{55} but have uniformly failed to sustain the inconsistent positions when their cases were heard on appeal.

In \textit{Estate of Shelfer v. Commissioner},\textsuperscript{56} for example, the taxpayer established a QTIP trust for the benefit of his surviving spouse that ostensibly qualified for the estate tax marital deduction. Upon the death of the surviving spouse, however, the executor of her estate pointed out that the terms of the putative QTIP trust did not pay the surviving spouse income that accrued between the date of the last distribution and the date of the surviving spouse’s death (the so-called “stub income”). That being the case, the terms of this trust arguably fail in a fundamental respect to meet one of the central requirements of a QTIP trust, namely that the surviving spouse have a “qualifying income interest for life.”\textsuperscript{57}

In a reviewed decision, the Tax Court upheld the executor’s position. It read the controlling section of the Code literally and declared that the failure of the surviving spouse to receive the stub income did invalidate the QTIP election made at the predeceased spouse’s death. On the basis of this factual finding, the court held that “[a]n erroneous election by the executor certainly cannot override the terms of the statute and make a trust that otherwise would not qualify as QTIP into a QTIP trust.”\textsuperscript{58} The majority opinion averred that the jurists had no choice but to adhere to the written words of the Code, even if those words produced a windfall that could not have been intended by Congress.

The taxpayer’s success, however, was short-lived. The Eleventh Circuit reversed and ruled in favor of the government.\textsuperscript{59} In interpreting the Code’s ambiguous language—that is, whether “qualifying income interest for life” meant the surviving spouse must receive or control the so-called stub income—the Eleventh Circuit held that a QTIP trust requirements were met as long as the QTIP trust distributed its income annually.\textsuperscript{60} There was no implicit statutory requirement that income be distributed on what would amount to a daily basis.

The Eleventh Circuit cited three practical advantages that would flow from upholding the government’s position: (1) greater certainty

\textsuperscript{55} \textit{See}, e.g., Estate of Howard v. Comm’r, 91 T.C. 329, 333 (1988) (“If the trust was never a QTIP trust, the election to treat it as such was not valid.”), \textit{rev’d} 910 F.2d 633 (9th Cir. 1990).
\textsuperscript{56} 103 T.C. 10 (1994).
\textsuperscript{57} I.R.C. § 2056(b)(7)(B)(i)(II) (as amended in 1998).
\textsuperscript{58} \textit{Shelfer}, 103 T.C. at 14.
\textsuperscript{59} Estate of Shelfer v. Comm’r, 86 F. 3d 1045 (11th Cir. 1996).
\textsuperscript{60} \textit{Id.} at 1053-54.
in estate planning, (2) greater consistency with standard trust practices, and (3) furthering Congressional intent that all previously deducted property be taxed.\(^{61}\) Aside from the practical advantages of adopting the government’s position, the court pointed out that the Service’s reading of the language in question was consistent with the legislative history behind the QTIP election. More specifically, the legislative history reflected the balance Congress tried to strike between meeting the control preferences of the predeceased spouse and the support needs of the surviving spouse.\(^{62}\) While the payment of stub income was likely to be immaterial to the support needs of the surviving spouse, failure to include assets held in the QTIP trust would undermine Congressional intent of treating a husband and wife as a single economic unit.\(^{63}\)

By deciding that there was in fact a valid QTIP election, the court in Sheller avoided a more general question of whether the respective estates of two spouses are subject to a duty of consistency. That more general question was presented the following year by Estate of Letts v. Commissioner.\(^{64}\) In Letts, the executor of the predeceased spouse mistakenly forgot to check the box on Schedule M on the predeceased spouse’s estate tax return—required under prior law—that indicated that the assets to be held in the QTIP trust would qualify for the estate tax marital deduction.\(^{65}\) On the computational part of the estate tax return, however, the executor of the predeceased spouse deducted the value of the assets passing to this putative QTIP trust. When the surviving spouse died, her executors took the position that the trust assets were not includable in her estate because a valid QTIP election had not been made on the predeceased spouse’s return.

In general, the duty of consistency doctrine prevents a taxpayer from benefiting in a later year from an error or omission in an earlier year that cannot be corrected because the time to assess tax for the

\(^{61}\) Id. at 1053.

\(^{62}\) Id. at 1049.


\(^{65}\) Under prior law, taxpayers had to elect which assets qualified for the estate tax marital deduction and reflect this election by checking a box located on Schedule M. Estate of Higgins, 91 T.C. 61 (1988), aff’d. 899 F.2d 1199 (6th Cir. 1990); see also Spohn v. United States, No. H89-232, 1990 U.S. Dist. LEXIS 7426 (N.D. Ind. June 4, 1990).
earlier year has expired.\textsuperscript{66} The first question the Tax Court had to
decide was whether sufficient identity of interests existed between
the predeceased and surviving spouse for their estates to be treated as
though they were a single taxpayer. On the basis of the taxpayers'
mariage and the similarity of their testamentary goals, the Tax Court
held that the two estates could be considered as one.\textsuperscript{67}

After making this determination, the Tax Court reviewed
whether the requisite elements of the duty of consistency doctrine
were present. The elements are as follows:

(i) the taxpayer made a representation of fact or reported
an item for tax purposes in one tax year;
(ii) the Commissioner acquiesced in or relied on that fact
for that year; and
(iii) the taxpayer desires to change the representation previ-
ously made in a later tax year after the earlier year has been
closed by the statute of limitations.\textsuperscript{68}

The court then found that each of these elements was present in
the facts of the case, in that the executor of the predeceased spouse’s
estate represented inferentially that the trust qualified for the estate
tax marital deduction (even though no QTIP election was made);\textsuperscript{69}
the Commissioner accepted that representation;\textsuperscript{70} and, finally, the
executors of the surviving spouse’s estate claimed the erroneous
submission by the executors of the predeceased spouse’s estate, now
barred by the statute of limitations, should not bind them to the repre-
sentation that the trust qualify for the estate tax marital deduction.\textsuperscript{71}
Because all the elements of the duty of consistency doctrine were

\textsuperscript{66} Herrington v. Comm’r, 854 F.2d 755, 757 (5th Cir. 1988), aff’g. Glass v.
Comm’r, 87 T.C. 1087 (1986); S. Pac. Transp. Co. v. Comm’r, 75 T.C. 497, 838-
39 (1980). Put differently, the duty of consistency prevents a taxpayer who has
benefited from a past representation from adopting a position inconsistent with that
taken in a year barred by the statute of limitations; this doctrine prevents a taxpayer
from avoiding the present tax by claiming that he or she should have paid more tax
before. \textit{See} Eagan v. United States, 80 F.3d 13, 16 (1st Cir. 1996); Lewis v.
Comm’r, 18 F.3d 20, 26 (1st Cir. 1994) (vacating and remanding in part T.C.
Memo. 1992-391). For an excellent exposition of the duty of consistency, see Steve

\textsuperscript{67} \textit{Letts}, 109 T.C. at 298 – 99.

\textsuperscript{68} \textit{Id.} at 297 (citing LeFever v. Comm’r, 103 T.C. 525, 543 (1994), \textit{aff’d}.
100 F.3d 778 (10th Cir. 1996)).

\textsuperscript{69} \textit{Id.} at 299-300.

\textsuperscript{70} \textit{Id.} at 300-01.

\textsuperscript{71} \textit{Id.} at 301.
present, the Tax Court ruled that the taxpayer could not exclude the value of assets held in the putative QTIP trust from the surviving spouse’s estate under section 2044.\textsuperscript{72}

Eliminating any return requirement in the case of a married decedent whose estate claims that no tax is due might imaginably exacerbate the whipsaw possibility, because the first element of the duty of consistency doctrine (i.e., a taxpayer making a representation) might be somewhat more difficult for the government to establish.

Under our proposal, however, estate executors would have a choice. The predeceased spouse’s executors would be obligated to file an estate tax return (assuming the value of the predeceased spouse’s estate exceeded the amount exempt from estate tax) if they did not want the assets held in the QTIP trust to qualify for the estate tax marital deduction. Conversely, they would not file an estate tax return if they wanted the assets held in the QTIP trust to qualify for the estate tax marital deduction. If the predeceased spouse’s executors chose not to file an estate tax return, and if the executors of the surviving spouse’s estate subsequently dispute the qualification of the QTIP trust for the estate tax marital deduction, then the executors of the surviving spouse’s estate would be unlikely to achieve any more success than the estates in the \textit{Shelfer} and \textit{Letts} cases.

In any event, the legal posture of cases of this sort would be similar to what it is under present law: the estate of the first spouse to die must make an affirmative representation (i.e., not filing an estate tax return would indicate that assets to be held in a QTIP trust qualified for the estate tax marital deduction), which would, under the case law described, ordinarily suffice to bind the estate of the second spouse to die.

\textbf{B. Ability to Monitor Future Tax Events}

Our proposal might also be subject to criticism on grounds that its adoption would result in the loss of valuable tax information. A predeceased spouse’s estate tax return normally provides the Service with four ostensibly useful pieces of tax information: (1) date of death values of the predeceased spouse’s assets; (2) a list of beneficiaries’ names and the value of assets passing to or on their behalf; (3) an allocation of the predeceased spouse’s generation skipping transfer tax exemption; and (4) a delineation of estate administration expenses deducted on the predeceased spouse’s estate tax return.

\textsuperscript{72} \textit{Id.}
In the following subsections 1.–4., we explain why each of these pieces of tax information is not as useful as it may first appear, and suggest alternative means for the Service to gather the same and perhaps more useful tax information.

1. Date of Death Values of the Predeceased Spouse’s Assets

One of the most critical features of an estate tax return is that it establishes a record of the decedent’s assets and their date of death values. This record is important for income tax purposes because recipients will hold assets passing to them with a tax basis equal to the asset value reported on the decedent’s estate tax return.\(^\text{73}\)

For example, suppose a spouse purchased raw land for $100,000 and that the land was worth $2,000,000 on the date of the spouse’s death. In most instances, reporting the $2,000,000 value on the predeceased spouse’s estate tax return will establish the asset’s tax basis for purposes of computing gain or loss on the land’s subsequent sale or disposition.\(^\text{74}\) From a theoretical point of view, the estate tax return thus serves as an information return of sorts to track recipients’ tax basis in the assets they acquire.

As a practical matter, however, the Service does not appear to use estate tax returns as information returns. Information returns (e.g., Form W-2s and Form 1099s) are typically submitted by third-party payors to the Service, which enters that data into its central computing center in West Virginia and uses them to crosscheck the

\(^{73}\) I.R.C. § 1014(a)(1). The Economic Growth and Tax Relief Reconciliation Act of 2001 has modified this rule for tax years after 2009, providing instead a general carryover basis rule, with important exceptions. See I.R.C. § 1014(f). The date-of-death (or alternate valuation date) basis rules of section 1014 will, however, continue to be effective until 2010, and perhaps beyond that, depending on what Congress does about the long-term future of the federal wealth transfer tax system.

\(^{74}\) Hess v. United States, 537 F.2d 457, 464 (Ct. Cl. 1976) (government accepted the value of stock as reported by an estate on the federal estate tax return and the estate did not seek to raise the issue of the stock’s value until after the statute of limitations had run on assessment; held, the duty of consistency doctrine required estate beneficiaries to use the same value of the stock as reported on the federal estate tax return as the basis for computing gain on subsequent redemption of the stock by beneficiaries). See also Ford v. United States, 270 F.2d 17 (Ct. Cl. 1960) (decedent's minor beneficiaries residing outside of the United States were not estopped from arguing a different value because they were not fiduciaries of the decedent's estate and had no knowledge of the decedent's estate tax return); Shook v. United States, 713 F.2d 662 (11th Cir. 1983) (estoppel not extended to an estate beneficiary for merely indicating approval of executor's handling of the estate over which the executor had total control and the beneficiary none).
accuracy of taxpayers’ income tax returns.\textsuperscript{75} In contrast, valuation information that taxpayers supply on their estate tax returns does not appear to play the same vital role in helping the Service monitor compliance because an estate tax return does not indicate who receives particular assets. This information vacuum precludes the Service from determining whether estate beneficiaries properly report an asset’s basis in accordance with the asset’s value as reported on the decedent’s estate tax return. Thus, short of conducting an income tax audit of an estate beneficiary, the Service has no way to verify the tax basis of bequeathed assets.

Consider, too, the fact that estate returns are filed by the estates of less than 5\% of all decedents.\textsuperscript{76} Even though those decedents generally own more property than decedents whose estates are not required to file returns, it is nevertheless the case that a good deal of inherited property subject to the fair-market-value at death basis rules will not have been reported on any estate tax return.

Together, the facts that the Service does not appear to make much use of the basis information it does get, and, in any event, is not in a position to receive comprehensive information about the basis of inherited property, suggest that this information-producing function of estate tax returns does not loom large in present estate administration practices. Perhaps the information on estate tax returns could be better and more extensively used; but, at least at the moment, the very limited usefulness of the information on the estate tax return of a married decedent who has no tax liability would not seem to be sufficient to justify the burden that the current filing requirement imposes.

2. Beneficiaries’ Names and the Value of Assets that Pass to or on Their Behalf

Estate tax return submissions ostensibly play another important role. They indicate the name of the decedent’s beneficiaries and the overall value of property that passes directly to and in trust for their


\textsuperscript{76} Staff of the Joint Committee on Taxation, Present Law and Background Relating to the Estate and Gift Taxes, 105\textsuperscript{th} Cong., 2\textsuperscript{nd} Sess. (1998).
benefit (but, as previously pointed out, not the specific assets that pass to or for their benefit).

From the perspective of the Service, this information is theoretically very useful, particularly when it comes to trusts established for the surviving spouse’s benefit. For example, suppose a spouse dies with a gross estate of $5,000,000. Suppose further that the terms of the spouse’s will carve out a by-pass trust, with assets equal in value to the decedent’s unused unified credit exemption amount, say $675,000, and the value of the balance of the spouse’s assets, or $4,325,000, pass into a QTIP trust.\footnote{This arrangement follows the framework of a prototypical estate plan. See supra Part III.} The $675,000 and $4,325,000 dollar figures, along with the trust designations, would be indicated on Part 4 and Schedule M, respectively, on the predeceased spouse’s estate tax return. This information supposedly enables the Service to track trust funding and serves as a mechanism to police later the estate tax return of the surviving spouse.

But because the Service receives no verification that the predeceased spouse’s executors actually fund the trusts in question with assets equal to the values delineated on the predeceased spouse’s estate tax return, this information is much less useful than it may first appear.\footnote{See generally Jay A. Soled, Dena L. Wolf & Nathan E. Arnell, Funding Marital Trusts: Mistakes and Their Consequences, 31 REAL PROP. PROP. & TRUST J. 89 (1996).} In fact, in situations that involve related parties (e.g., husbands, wives, and children) there is a tremendous transfer tax-savings incentive to overfund the trust that will not be included in the surviving spouse’s estate (i.e., the by-pass trust, say with assets equal in value to $2,000,000) and to underfund the trust that will be included in the surviving spouse’s estate (i.e., the QTIP trust, say with assets equal in value to $3,000,000).\footnote{Id. at 90-91.} Given the fact that testamentary trusts are often funded many years after the receipt of a Service closing letter, this chicanery is not as unlikely as it may seem.

Upon closer examination, a predeceased spouse’s estate tax return thus provides information that proves to be of little practical utility and may actually facilitate deception. Eliminating a predeceased spouse’s estate tax return may not result in the anticipated loss of much meaningful information.

The Service would certainly be in a far better position to monitor taxpayer compliance if Congress mandated an information return requirement in lieu of the current estate tax return filing requirement.
Imaginably, at the time an estate is closed, executors might be obliged to file an information return that indicated the exact dollar amount and value of assets then held by any testamentary trust established by a predeceased spouse. Receipt of this information would be far more beneficial than receipt of a predeceased spouse’s Form 706. This is because such information would provide a picture of what actually happened instead of a picture of what was supposed to have happened.

3. Generation-Skipping Transfer Tax Exemption Allocation

In addition to the estate tax, the Code imposes a secondary tax on every generation-skipping transfer (GST).\(^{80}\) This is not the place for a full description of this rather complicated tax. It will suffice for our purposes to note that the federal wealth transfer taxes are intended to tax the movement of wealth between each pair of succeeding generations. If not for the GST tax, gifts and bequests from grandparents to their grandchildren would only be burdened by the estate tax every other generation. Very roughly, then, the GST tax is intended to reach transfers to grandchildren (and more remote generations) but not transfers to spouses and children.

To shield relatively modest wealth transfers from the imposition of GST tax, the Code provides a GST tax exemption of, currently, $1,060,000.\(^{81}\) On an estate tax return, executors may allocate this exemption to any property transferred by the decedent.\(^{82}\) This allocation may be made at any time on or before the date prescribed for filing the estate tax return (determined with regard to extensions).\(^{83}\)

In determining a decedent’s immediate GST tax burden (in the case of gifts going directly to grandchildren) and ultimate GST tax burden (in cases of transfers in trust, or the like, in which the grandchild’s interest is deferred), the GST tax exemption allocation proc-

\(^{80}\) I.R.C. § 2601. Like the estate tax, this provision has been repealed by the Economic Growth and Relief Reconciliation Act of 2001, effective after 2009. Also like the estate tax, however, it will come back to life in 2011, unless further Congressional enactment provides otherwise.

\(^{81}\) I.R.C. § 2631(a). This exemption is annually adjusted by a cost-of-living adjustment. \textit{Id.} § 2631(c).

\(^{82}\) \textit{Id.} § 2631(a).

\(^{83}\) \textit{Id.} § 2632(a)(1). In the absence of an allocation, the Code imposes a default rule. The Code deems the unused exemption to be allocated as follows: (A) first, to property which is the subject of a direct skip occurring at such individual’s death, and (B) second, to trusts with respect to which individual is the transferor and from which a taxable distribution or a taxable termination might occur at or after such individual’s death. \textit{Id.} § 2632(c)(1).
ess serves an important role. This is particularly true in cases involving the death of the first spouse. This is because the executors of a predeceased spouse who establish QTIP trusts can elect to treat—for GST purposes—all of the property in such a trust as if a QTIP election with respect to such property had not been made. By making this so-called "reverse QTIP election" the Code deems the predeceased spouse the transferor of property held in the QTIP trust, even though such property will ultimately be taxed in the surviving spouse’s estate.

Only a very small percentage of executors make GST exemption allocations, however, and even a smaller proportion of those do so at the death of the first spouse. Again, to gather the same information, Congress could instead require executors to submit an information return that reflects executors’ GST tax exemption allocations at the death of the first spouse. This information would serve as a record to taxpayers, trustees, and the Service of how predeceased spouses deployed their GST tax exemption and the inclusion ratio (a technical term that indicates percentage of trust property subject to GST tax) of any testamentary trust established by a predeceased spouse.

4. Estate Administration Expenses

Certain expenses that estates incur (e.g., executors’ commissions) are deductible on either the estate tax return or on the estate’s income tax return, but not on both. In light of the unlimited estate tax marital deduction and the fact that no estate tax is normally due at

---


85 I.R.C. § 2652(a)(3). The importance of this election is that otherwise the surviving spouse would be considered the transferor of such property (I.R.C. § 2652(a)(1)) and the predeceased spouse’s GST exemption might otherwise go to waste. John B. Atkins, Balancing the GSTT Exemption and the Marital Deduction, 14 REAL PROB. & PROB. TR. J. 16 (2000) ("By virtue of the reverse QTIP election, the first spouse to die is treated as the "transferor" of the marital trust for GSTT purposes only, which allows the trust to qualify for the marital deduction and to use the first spouse’s excess GSTT exemption."). Examples 3 and 6 in Treas. Reg. § 26.2652-1(a)(5) demonstrate the effect of the reverse QTIP election.

86 I.R.C. § 642(g).
the death of the first spouse, common sense might indicate that executors of a predeceased spouse would deduct estate administration expenses on the estate’s income tax return. Assuming the predeceased spouse’s estate had taxable income, using the administration expense deduction in this fashion would result in immediate income-tax savings. There would be a long-term disadvantage, however, in using this deduction on the predeceased spouse’s estate income tax return. This is because the monies used to pay these administration expenses would not qualify for the estate tax marital deduction. That being the case, the terms of most prototypical wills specify that the value of the so-called by-pass trust be reduced by an amount equal to the estate administration expenses if such expenses are otherwise not deductible on the estate tax return.\textsuperscript{87} While a reduction of the amount passing into the by-pass trust has no immediate transfer tax consequences, it usually means that a larger estate tax will be due at the surviving spouse’s demise.

Instead of weighing the consequences involved in a choice between the two returns, many executors intentionally or mistakenly skirt the law. That is, they often deduct estate administration expenses on both the decedent’s estate tax return and the estate’s income tax return, but they do not reduce the value of assets that pass into the by-pass trust.\textsuperscript{88} Thus, as in several other situations described in this section, potentially useful information on the estate tax return is not actually being used by the Service. Under these circumstances, defending a general return requirement on the basis of the ancillary (but unused) information it may contain has a distinctly hollow ring.

Given the current sorry state of affairs, Congress should require that all taxpayers deduct estate administration expenses on a decedent’s estate income tax return. By instituting this mandate, the majority of estates (which are nontaxable because the value of their as-

\textsuperscript{87} Suppose a spouse worth $5,000,000 dies and the estate incurs administration expenses of $100,000. Suppose further the estate administration expenses are deducted on the estate’s income tax return. The by-pass trust would be funded with $575,000, rather than $675,000, had the administration expenses been deducted on the predeceased spouse’s estate tax return.

\textsuperscript{88} See Boris Bittker & Lawrence Lokken, \textit{3 Federal Taxation Of Income, Estates, And Gifts} ¶ 81.2.6 (2d ed. 1992) (“Indeed, it is not usual to deduct the same item on both returns (with appropriate disclosure of this fact) if, when the returns are due, the fiduciary is uncertain of the more advantageous treatment, and then to abandon the claim on one of the returns (by filing or refraining from filing the requisite waiver) when the uncertainty is clarified by audit or otherwise.”); Stephens et. al., \textit{Federal Estate And Gift Taxation} ¶ 5.03[3][d] (6th ed. 1992) (referring to the “sensible practice of deferring the filing of the waiver until the time of audit of the estate tax return.”).
sets do not exceed the unified credit exemption amount) will still be able to deduct administration expenses on the estate's income tax return, as they generally have in the past. In cases where the estate is taxable, the executors will simply reduce by the amount of these administration expenses the value of assets to be held under the terms of the by-pass trust, if any, established by the terms of the predeceased spouse's will.

In sum, it is not entirely incorrect that the Service would lose some valuable information were this proposal adopted. But when the advantages of this proposal are weighed against the value of the information that would be lost at a predeceased spouse's death, particularly in light of the limited actual use of this information under current law and administrative practice, the balance clearly favors adoption of our proposal. Some may disagree with our assessment of this. If Congress ultimately disagrees, we would encourage it to consider, in any event, whether the legitimate information needs of the Service could be better served by instituting more targeted information returns of the sorts that we have suggested as a substitute for the full estate tax return the Code demands in cases of nontaxable estates of married decedents.

IV. CONCLUSION

The burdens of filing tax returns ought not to be imposed lightly. The estate tax return is a particularly complex and demanding one, as to which unnecessary filing requirements are especially noisome. Yet current law does indeed impose an apparently unnecessary filing requirement on the estates of six-sevenths of the married decedents who exceed the filing thresholds, but owe no tax. For this group of estates, the returns obviously generate no government revenue and only a modest amount of useful tax information. Further, it appears that the Service's current procedures do not make optimal use of even the modest information provided. Overall, these are truly unnecessary returns, imposing significant financial costs on estates and resulting in significant delays in the distribution of the affected estates' assets.

The Economic Growth and Tax Relief Reconciliation Act of 2001 may eventually relieve this problem to some degree; by phasing in higher thresholds of estate tax liability, it will reduce the number of estate tax returns across the board.\textsuperscript{89} It will presumably remain

\textsuperscript{89} Of course, those higher thresholds are not permanent, with the reversion to 2001 law in 2011. The authors' best guess about the future of the federal wealth
true, however, that there will be many estates of married decedents that will exceed the filing thresholds yet owe no tax. And, during the transitional period over which higher thresholds are being phased in, the case for relief from filing for estates that owe no tax is especially compelling since it is unlikely that the surviving spouses in such cases will owe any estate tax either.\textsuperscript{90}

This analysis advances a relatively simple reform—namely, the elimination of estate tax returns for predeceased spouses’ in instances when there is no estate tax due. This would benefit primarily those estates that are relieved of their filing obligations, but this reform would also relieve the Service from having to process approximately half the number of estate tax returns that are currently filed. Finally, it would contribute to greater acceptability of the wealth transfer system among the public at large, many of whom have been beneficiaries of an estate of a married decedent and have had occasion to be annoyed at the costs and delays associated with unnecessary filing requirements.

This reform is long overdue: Congress should have amended the estate tax return requirements when it adopted an unlimited marital deduction in 1981. The fact that they did not is no defense of the status quo; what may not have been obvious then—that estates of married taxpayers would rely heavily on that unlimited marital deduction—has become obvious over the succeeding two decades. Mandatory estate tax filing for married decedents based solely on the size of the gross estate is a relic of the pre-1981 estate tax rules. Replacing that rule with the more sensible one that we propose is, quite simply, the right thing to do.

\textsuperscript{90} The higher exemption levels being phased in over the next several years increase the urgency of the reforms we advocate. Because nearly 90\% of estate tax returns report gross estates of less than $2,500,000 (i.e., 79,921 of the 90,006 estate tax returns filed in 1997 showed less than $2,500,000 as the gross estate (Internal Revenue Service, \textit{Statistics of Income Bulletin}, vol. 19, no. 1, at 102 (Summer 1999)), the odds are very good that the estates of surviving spouses of married decedents who die in the next few years will themselves be subject to neither the estate tax itself nor the burden of filing an estate tax return.