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PRINCIPLES FOR EFFECTIVE USE OF MARITAL DEDUCTIONS

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I. INTRODUCTION

Most estate planning has two primary tax objectives. The first is to reduce estate and gift tax liability. The second is to defer such liability until the death of a surviving spouse. From 1948 through 1976, interspousal transfers of property which qualified for gift and estate tax marital deductions were the most common method for accomplishing tax deferral and, to a lesser extent, constituted a tool for reducing total transfer taxes. The changes in the federal gift and estate tax laws made by the Tax Reform Act of 1976,[1] effective January 1, 1977, generally expand the maximum amounts allowable as gift and estate tax marital deductions for medium-sized estates, but also increase the risks of improper use of such deductions. Such improper use may needlessly increase aggregate gift and estate tax liability. For example, suppose that the spouse with the larger estate (usually referred to in this article as S-1) has a prospective adjusted gross estate of $250,000 and the other (S-2) an estate of $120,000. If S-1 made a new will in 1977, leaving a maximum marital deduction bequest to S-2, and then S-1 dies shortly before S-2, under the new law, the increased maximum marital deduction of $250,000 reduces S-1's taxable estate to zero.[2] However, if S-2's taxable estate remains intact, S-1's use of the maximum marital deduction bequest will increase S-2's estate to $370,000, $120,000 from S-2's former estate and $250,000 from the assets passed by S-1. Assuming both spouses died in 1977, the federal estate tax liability of S-2's estate after applying the new unified transfer tax credit[3] was $81,600.[4] S-1 accordingly has achieved complete deferral[5] of estate tax but at the cost

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[1] The Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1853 [hereinafter generally cited as the Act].

[2] The date is significant because in 1977 the new "unified" transfer tax credit available for each estate was $30,000. In later years, the credit increases. I.R.C. §2010(b).

[3] I.R.C. § 2010 specifies the amount of the new unified credit for estate tax purposes and I.R.C. § 2505 specifies such amount for gift tax purposes. The credit reduces total transfer tax payable (gift or estate tax) dollar for dollar up to the amount of tax equal to the credit. The credit increases from $30,000 in 1977, to $47,000 in 1981 and thereafter.

The calculations made in this introductory section are based on the 1977 unified credit of $30,000, and do not take into account the credit for state death taxes; its omission here is simply for purposes of clarity and arithmetic simplicity. The bulk of the article assumes that the unified credit available is the amount allowable in 1981.

[4] The tax imposed by § 2001(b) on a $370,000 estate is $70,800 on the first $250,000 plus 34% of the amount over $250,000, or $70,800 plus $40,800 = $111,600. In 1977 the available unified credit was $30,000, which leaves $81,600, disregarding any state death tax credits.

[5] In the case of spouses dying soon after one another, any benefit from tax deferral is virtually nonexistent.

of increasing S-2's estate law liability. S-1 could have achieved the same complete deferral with a lesser increase in S-2's estate and estate tax liability if S-1 had used a marital deduction large enough to reduce his or her adjusted gross estate only to the amount at which the unified transfer tax credit would be exactly equal to the tax due on the estate. In 1977, that amount was $120,000. That is, the unified credit allowable in estates of decedents dying in 1977 is equivalent to an exemption from tax for a taxable estate of $120,000. A $130,000 marital deduction bequest which would have left a taxable estate of $120,000 would equal the so-called "exemption equivalent" of the available unifed credit. Accordingly, an alternative to leaving a maximum marital deduction is making a marital gift which leaves a taxable estate equal to the exemption equivalent and applying the credit to eliminate tax on that taxable estate.

A plan which uses the smaller marital deduction in order to have remaining an estate large enough to utilize the entire available credit not only achieves complete tax deferral in S-1's estate, but also results in a reduction in the aggregate taxes imposed on both estates. If, in the example above, S-1 had left S-2 a marital bequest of property worth $130,000 his taxable estate would be $120,000, or the exemption equivalent of the federal tax credit available to him. By placing the entire $120,000 taxable estate in a trust which gives S-2 the income for life, with, for example, the remainder interest to their children, the estate plan gives S-2 the beneficial enjoyment of the entire estate for life, while transferring to S-2's prospective taxable estate only the $130,000 of marital deduction property. S-2 will then have a taxable estate of $250,000, consisting of $120,000 of previously-owned assets plus $130,000 of the marital bequest, S-1's trust of $120,000 not being included in S-2's gross estate.[6] If S-2 died in 1977 there would be $70,800 tax due on S-2's estate, leaving, after application of the $30,000 credit, a tax of $40,800. As noted above, had S-2 died in 1977 with a taxable estate of $370,000, including a marital bequest of $250,000 transferred from S-1, after application of the unified credit, the tax payable would have been $81,600, an amount twice the $40,800 owed when the smaller marital deduction is used. Thus, in this instance, the goal of complete deferral and the goal of tax minimization can both be achieved through careful use of the marital deduction.

If, in this example, S-2 survives until 1981, when the unified credit rises to $47,000, by proper use of the estate tax marital deduction, federal estate tax liability in both estates could be eliminated almost entirely.[7] In this case too, there would be no conflict between the objectives of tax deferral and reduction. In many instances, however, it is possible to achieve maximum tax reduction only by sacrificing maximum deferral, and vice versa. Suppose, for example, that S-2, instead of owning an estate of $120,000, had an estate of $1,500,000 and S-2 in fact survives S-1. Maximum tax reduction (i.e. the lowest total tax in both estates) clearly will be attained if S-1 with an estate of $250,000 makes no marital deduction transfer to S-2, since any property transferred to S-2 ultimately will be taxed at the much higher rates operating on S-2's estate, rather than at the

[6] *See* I.R.C. §§ 2033-2038.

[7] That is, the total of marital property which S-1 must pass to S-2 in order to keep S-1's estate within the exemption equivalent will cause S-2's estate to exceed by only a small amount the exemption equivalent of S-2's unified credit.

lower rates imposed on S-1's estate. Specifically, if S-1 did make a marital deduction bequest to S-2 of approximately $130,000, S-1's estate would incur no transfer tax, just as was the case in the preceding example. S-2's estate, however, since it is much larger, will be taxed at higher marginal rates. By virtue of its being increased to $1,630,000 by the addition of the property passing from S-1, S-2's estate will pay a tax, when reduced by the credit available, of $584,300. Had no property passed from S-1 to S-2, S-2's tax, on an estate of $1,500,000 would have been only $525,800. Thus, the complete deferral achieved in S-1's estate costs almost $60,000 in additional estate taxes in S-2's estate.

On the other hand, if S-1 had died in 1977 without making any marital deduction, his or her estate would have incurred a substantial federal estate tax liability. With no marital deduction, the tax due on a taxable estate of $250,000, even when reduced by the unified credit, is $40,800. In this case, there is a clear conflict between deferral of tax and tax reduction. The cost of deferring $40,800 tax on S-1's estate is the increase of tax on S-2's estate of about $60,000. This choice of whether to defer or to minimize tax must turn on nontax considerations, including the liquidity of the assets, the availability of lucrative investment opportunities, and the life expectancy and state of health of both spouses. After considering such factors, the tax deferred may or may not be worth the resulting tax increase, either in monetary terms or in terms of other objectives of the spouses.

The purpose of this article is to help estate planners deal with the reduction-deferral quandary and other similar problems. It will analyze the changes in the law as they relate to both the gift and estate tax marital deductions and will develop certain general principles for effective use of such deductions in current estate planning. In the course of its analysis this article will relate these general principles to specific categories of estates based on their size. The first such category consists of the smallest estates in which total adjusted gross estates of both spouses combined do not exceed $200,000 to $250,000. The second or medium-sized category consists of combined estates larger than those in the first category but not exceeding $250,000 plus the exemption equivalent of unified credit and any other credits against tax available to one spouse, or combined estates not exceeding approximately $428,000, when the new unified credit has been fully implemented. Combined estates between $428,000 and just over $600,000[8] constitute the third category. The final category considered is where combined assets of both spouses exceed $600,000. In this category, the general principles for effective use of marital deductions have changed the least.

This article will first discuss changes made by the 1976 Tax Reform Act which affect the use of the marital deduction. It will then treat estate planning under the new law, dealing specifically with effective use of the gift tax and then effective use of the estate tax marital deduction. It will be shown that consistent use of the principles outlined in this article can aid the estate planner in confronting the transfer tax problems associated with any of the categories of estates.

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[8] These figures are based on the sum of the exemption equivalents of credits for both spouses, plus $250,000.

II. TAX REFORM ACT CHANGES AFFECTING MARITAL DEDUCTIONS

A. *The New Unified Credit*

The Tax Reform Act made several major changes in transfer taxation. The most important and new features are the unified credit, a different rate structure, and different maximum gift and estate tax marital deductions. These changes will be discussed in turn.

Under prior law, all estates were entitled to an exemption for $60,000 worth of the taxable estate, and, for $30,000 worth of the total taxable gifts. These exemptions have been replaced by a unified credit provided in sections 2010 and 2505 applicable against all taxable transfers. Instead of exempting any part of the taxable estate or gift from tax, this credit, in effect, treats the tax due on a particular estate as paid to the extent of the credit.

It should be noted that tax reduction resulting from the credit is uniform for all taxpayers, whereas under prior law the amount of tax reduction from exemptions depended on the marginal or highest bracket rate applicable to a particular taxpayer. Thus, the prior $30,000 gift tax exemption could reduce taxes by as little as $2,250 at the starting gift tax rates and as much as $17,325 at the maximum gift tax rates. That is, absent the exemption, a $30,000 taxable gift resulted in a tax of $2,250. The $30,000 gift exemption thus saved a taxpayer $2,250 in tax. However, a gift of more than $10,000,000 where the marginal rate was 57.75%, resulted in a savings of $17,325 on account of the same $30,000 exemption.[9] Similarly, the $60,000 estate tax exemption reduced federal estate tax liability by as little as $3,000 in the lowest rate brackets and $37,440 at the top bracket rate applicable after credit for state death taxes. A tax credit, on the other hand, reduces tax by the amount of the credit regardless of the rate at which the taxpayer is paying tax. The $47,000 credit scheduled to be effective as of January 1, 1981, will be worth $47,000 in tax reduction to all taxpayers whose tax would equal or exceed $47,000 in the absence of the credit.

In all but the largest estates the new unified credit represents substantially greater tax reduction potential than both of the old exemptions combined. In smaller and medium-sized estates, the new credit has a tax reduction potential several times greater than the former exemptions.[10] For a husband and wife with combined estates of more than $350,000, the separate credit for each estate offers potential tax savings of more than $90,000 and a very significant percentage increase in the assets available to the objects of their bounty. As compared with the exemptions, the new credit affords a vastly increased opportunity for minimizing transfer taxes in smaller and medium-sized estates where tax savings can be most important to the clients.

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[9] I.R.C. § 2502, prior to amendment by the Tax Reform Act of 1976.

[10] For example, consider two taxable estates of $178,289, one of which was taxed in 1976, and one in 1981. The 1976 estate, after an exemption of $60,000 paid $26,187. By 1981, a $178,289 estate will pay no federal estate tax as the result of credits. The relative advantage offered by the unified credit is evident.

Similar savings are applicable to taxable gifts. In 1977, the unified credit allowed the taxpayer to make four times the amount of otherwise taxable gifts without incurring immediate gift tax liability than could be made under prior law; by 1981, that amount will be nearly six times as much as, and $145,000 more than, was allowed under prior law. That is, from $30,000 of tax free gifts, the Act raises the amount, protected now by the unified credit, to approximately $175,000.

The schedule by which the new unified credit is to be introduced covers a five year period beginning in 1977 with a credit of $30,000. The credit will increase in $4,000 increments until 1980 and 1981 in each of which years a $4,500 increase will occur, bringing the credit to its maximum of $47,000.

The exemption equivalent of available credits is further expanded when the credit for state death taxes is combined with the unified credit. The credit for state death taxes, provided for in section 2011, remains the same as under prior law. It allows a credit against federal estate tax for "estate, inheritance, legacy or succession taxes actually paid to any State . . . ."[11] The credit ranges from .8% of the excess of the adjusted taxable estate over $40,000, to $1,082,800 plus 16% of the excess over $10,040,000. The combined effect of the unified tax credit of $47,000 and the credit for state death taxes is an exemption equivalent in 1981 and later in excess of $178,000. Equivalents for the unified credit separately and when combined with the credit for state death taxes applicable to decedents whose death occurs in 1977 and later years are set forth in the following table:[12]

		Exemption Equivalents	
Calendar Year of Death	Unified Credit	Unified Credit Only	Unified Credit Plus Credit for State Death Taxes
1977	$30,000	$120,000	$121,233
1978	34,000	134,000	134,932
1979	38,000	147,000	148,630
1980	42,500	162,000	163,487
1981 and thereafter	47,000	175,625	178,289

These credits are the cornerstone of estate planning under the Act, and can be used as a starting point in the calculations necessary to full understanding of the tax consequences of the credit.

In sum, then, the increased tax protection afforded by the unified credit assures that many small to medium sized estates which formerly were subject to tax now can pass without incurring tax. Plainly, it behooves the estate planner to assure that the provisions do what they are designed to do, especially when planning the estate of clients with moderate assets.

[11] I.R.C. § 2011.

[12] I.R.C. § 2010(b).

B. *Increased Gift and Estate Tax Rates in Lower Brackets*

The corollary to the enlarged protection created by the unified credit is an increase in rates applicable in lower brackets in which the credit is used. Whereas the effective tax rate on the first taxable dollars after the specific exemptions under prior law was quite modest,[13] the new unified gift and estate tax rate before applying the unified credit commences at 18% and rises to 30% at the $100,000 level of taxable gifts and estates. Although the technical differences between an exemption and a credit create conceptual difficulties with the following table, the comparisons of prior and new law illustrate the impact of new higher estate tax rates on modest-sized estates:

Size of Taxable Estate (before $60,000 exemption)	Prior Law		New Law[14]		
	Tax	Rate on Excess	Tax before Credit	Rate on Excess	Tax after Credit
$ 60,000	0	3%	$13,000	26%	0
80,000	$1600	14%	18,200	28%	0
100,000	4800	22%	23,800	30%	0
120,000	9500	28%	29,800	30%	0
160,000	20,700	30%	42,000	32%	0
200,000	32,700	30%	59,800	32%	$7,800
250,000	47,700	30%	70,800	34%	$23,800

These figures reemphasize what has already been said concerning the dollar effect of the new unified credit. The new rate structure with effective federal rates of 30% and more on each taxable dollar in excess of available credits dictates that the tax planner should consider and in general fully utilize the tax reduction opportunities arising from the existence of available credits. The higher rates dramatically increase the potential tax cost of bad tax planning.

C. *Changes in Maximum Marital Deductions*

In addition to introducing the new unified credit and increasing transfer tax rates, the Tax Reform Act substantially modifies the limits, and, hence, the planning significance, of the marital deductions for transfers, either by gift or bequest, from one spouse to another. For both gift and estate tax purposes, the maximum marital deduction under prior law had a 50% limitation, that is, 50% of the taxable interspousal gifts was deductible, as was any marital bequest up to 50% of the value of the adjusted gross estate.[15] However, for each tax the base to which this 50% limitation applies was and remains quite different. For estate tax purposes, it is

[13] The marginal rate specified by § 2001(c) did not exceed 30% until the taxable estate surpassed $250,000.

[14] Amounts of tax and rates are before credit for state death taxes. Percentage rates apply to first dollars of excess only. Figures do not apply in all instances to decedents dying prior to 1981.

[15] I.R.C. §§ 2056, 2523, prior to amendment by the Tax Reform Act of 1976.

applied to the total adjusted gross estate without regard to whether the other 50% passes to the surviving spouse or to third persons.[16] For gift tax purposes, however, the limitation is applied only against the total interspousal gifts otherwise eligible for the deduction.

The new law eliminates this 50% limitation from the maximum marital deduction for the first $250,000 of marital bequests so that the maximum marital deduction is now the greater of $250,000 or 50% of the adjusted gross estate. Only where the adjusted gross estate exceeds $500,000 will the 50% figure produce the maximum marital deduction.[17] The maximum estate tax marital deduction thus is now able to eliminate entirely any tax liability in an estate of $250,000 plus the exemption equivalent of credits, whereas under prior law the combined effect of both the maximum marital deduction and the specific exemption was to eliminate tax only if the adjusted gross estate did not exceed $120,000.[18] The new maximum of $250,000 enables a spouse to defer tax on an entire estate of $428,289 if death occurs after 1980 when the exemption equivalent of available credits becomes $178,289. Thus, the estate planning opportunities presented by the new maximum marital deduction are considerable.

In addition to changing the 50% limit on the deductibility of marital bequests, the Act also eliminates the 50% limitation of the deductibility of the first $100,000 of lifetime interspousal gifts. Thus, all interspousal gifts up to a total of $100,000 are now fully deductible.[19] Every dollar of the second $100,000 is taxed fully.[20] For all gifts over $200,000, 50% of the amount in excess of $200,000 is also subject to tax.[21] The consequences of this arrangement are that $100,000 of gifts incurs no tax, $200,000 of gifts incurs tax on the second $100,000, $300,000 of gift incurs tax on $150,000, i.e., the second $100,000, plus 50% of the third $100,000 or $50,000.

The final change of note in the two marital deductions is the provision in section 2056 that requires a downward adjustment in the available estate tax marital deduction under section 2056 to reflect the gift tax marital deductions taken in excess of 50% of lifetime interspousal gifts.[22] Specifically, the law requires that the maximum estate tax marital deduction otherwise available be reduced by the amount by which total gift tax marital deductions taken exceed 50% of the total value of the gifts.[23] Since all gifts up to $100,000 are fully deductible, the estate tax maximum marital deduction otherwise available will be reduced by 50% of lifetime marital gifts so long as the total of such gifts is not more than $100,000. Thus an $80,000 gift will reduce the maximum available marital bequest deduction by $40,000. Gifts in the range of $100,000 to $200,000, not being eligible for deductions beyond the first $100,000, reduce the downward adjustment

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[16] I.R.C. § 2056(c)(1)(A).

[17] *Id.*

[18] A specific exemption of $60,000 was available to all estates. The maximum marital deduction was 50% of the adjusted gross estate; or, in the case of a $120,000 estate, $60,000. Thus, all tax on a $120,000 estate could be deferred. Any estate over $120,000 would have possessed nondeductible property in excess of the specific exemption of $60,000, and such property accordingly would be subject to tax.

[19] I.R.C. § 2523(a)(1).

[20] I.R.C. § 2523(a)(2).

[21] *Id.*

[22] I.R.C. § 2056(c)(1)(B).

[23] *Id.*

of the estate tax marital deduction only by the amount by which $100,000 exceeds 50% of the gift. For example, lifetime gifts of $150,000 will reduce the available marital bequest deduction by $25,000 since the total gift deductions taken ($100,000) exceeds 50% of the total of lifetime gifts ($75,000) by $25,000. Clearly, this adjustment to the estate tax marital deduction raises important problems in relating lifetime and testamentary dispositions which must be carefully examined by the estate planner.

The Tax Reform Act, by introducing the unified credit, altering, and to some extent relating the deductions applicable to marital lifetime gifts and marital bequests, expands the planning options available to the planner, and increases the risks involved in poor planning. The Act does not, however, change some of the most basic principles which planners used before the Act. Credits and exemptions should, as before, be fully utilized and the marital deduction utilized to the extent necessary. Finally the importance both of careful calculation of all tax consequences, and of full consideration of the nontax goals and aspirations of clients are critical to effective planning.

III. ESTATE PLANNING UNDER THE NEW LAW

A. *The Cardinal Rules*

In the past, the estate tax marital deduction has been the chief method of deferring tax on medium-sized estates. A bequest to a spouse, either outright or in trust with sufficient incidents of ownership to the spouse so as to constitute, in effect, the spouse's property[24] was deductible from the estate of the deceased spouse to a limit of 50% of the deceased spouse's adjusted gross estate. The 50% limit now applies only to estates larger than $500,000. In smaller estates a limit of $250,000 is applicable.

At first glance, it would appear that the provision for a $250,000 marital deduction provides a means which generally could be used to defer tax in the decedent's estate. In fact, however, as has been noted,[25] use of the maximum marital deduction may not be the most appropriate planning technique. To illustrate this, suppose that S-1 has an estimated adjusted gross estate of $300,000, and that S-2 has assets of $100,000. Suppose further that S-1's will includes a $250,000 maximum marital deduction bequest, placing the remaining $50,000 in a nonmarital trust, in which S-2 has a life estate, and after S-2's death their children receive the remainder free of the trust. If S-1 predeceases S-2, S-1's taxable estate will be only $50,000 which is a great deal less than the exemption equivalent of the unified credit, and hence no tax would be paid. Unfortunately, however, S-2's estate has now grown to $350,000, a good deal greater than the exemption equivalent of credits against tax. Assuming death in 1981 or later, S-2's es-

[24] Thus, for example, a life income interest in a trust with a general power of appointment by will, would qualify for the marital deduction under I.R.C. § 2056(b)(5), whereas an identical gift which prohibited the surviving spouse from exercising the power in favor of the spouse, the spouse's estate or creditors would not so qualify.

[25] See text at notes 2-5 *supra*.

tate will pay taxes of approximately $57,800.[26] If, on the other hand, S-1 had established the nonmarital trust with a fund equal to the exemption equivalent of $175,000, and had made a marital deduction bequest of only $125,000 ($300,000 minus the $175,000 exemption equivalent used to fund the nonmarital trust), S-1 would have preserved the tax free treatment of his or her own estate while at the same time reducing S-2's taxable estate to $225,000 (composed of S-2's original $100,000 of assets plus $125,000 marital deduction bequest) on which approximately $62,800 tax would be due. S-2's $47,000 credit would eliminate all but $15,800 of this tax obligation. Under this plan, then, S-1 and S-2 realize a tax savings on their combined estate of approximately $42,000 as compared with the first plan.

This example pinpoints the first cardinal rule of estate planning under the Tax Reform Act, which may be stated as follows:

> Fully utilize any available credit against federal tax liability, particularly the new unified credit.

The corollary to this rule is also clear from the example above. The corollary is, in reality, a restatement of the familiar principle under prior law which required avoiding gifts which would qualify for the marital deduction (hence increasing the surviving spouse's taxable estate), but which exceeded the maximum dollar amount permitted by the marital deduction. This resulted in "overfunding" of the deduction with property which could have been kept from S-2's estate through a nonmarital bequest. This rule may now be rephrased as follows:

> The unified credit (or other credits) should be applied against transfers which will not qualify for a deduction.

That is, the unified credit should be used to absorb the tax burden on property which will not be included in the surviving spouse's estate.

Thus, our "cardinal rules" require us to utilize fully all credits, by applying them against property which will not be includible in the surviving spouse's estate, and by making marital gifts and bequests only to the extent that the estate of the first spouse to die will exceed the exemption equivalent of all available credits. With these principles in mind, the appropriate uses which can be made of the gift tax marital deduction, and the estate tax marital bequest deduction will now be examined.

B. *Using the Gift Tax Marital Deduction*

1. General Rules

Under prior law, the tax objectives of lifetime interspousal gifts were increased tax deferral if the donee survived the donor or reduced transfer taxes in the two estates combined if the donor survived the donee. Under the new law, the objectives are the same, but the rules of the game have been significantly altered. Thus, if the donee survives the donor, the amount on which tax deferral is attainable with zero transfer tax liability to

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[26] The tax on a $350,000 estate is $104,800. Disregarding the state death tax credit, the unified credit in 1981 will be $47,000, which, when subtracted from the tax owed leaves $57,800 in tax to be paid.

the donor or the donor's estate has been greatly increased, but the price of maximum deferral in increased estate tax in the donee's estate has become so high as to make such giving relatively unattractive unless the donee plans to leave his or her estate to charity, thereby reducing or eliminating the estate tax cost.

The problems involved in using lifetime marital gifts to defer tax may be illustrated by examining the assertion widely circulated among lawyers after the passage of the Act to the effect that it was possible, by means of full use of the lifetime gift deduction, to pass $600,000 tax free to a surviving spouse. For example, if by 1981, S-1 makes lifetime gifts to S-2 of $350,000, one half of such gifts will come within the gift tax marital deduction and the other half will use up S-1's unified credit. If S-1 predeceases S-2, S-1's estate will still have a $250,000 marital deduction[27] available for estate tax purposes.[28] Thus, $600,000 will have passed tax free from S-1 to S-2.[29] Generally, of course, this would not represent good estate planning because the unified credit has been used against marital gifts to S-2, which will be taxable later in S-2's estate. Accordingly, S-2 will have the largest possible estate taxed at the new higher marginal rates, consisting of all the property transferred from S-1 plus any property originally owned by S-2. The use of this scheme violates the rule requiring utilization of credits against property not includible in S-2's estate, since S-1's unified credit was used against gifts to S-2 of property which will be included in S-2's taxable estate at death. The transfers could have been more effective if made in a

[27] Note that there is no loss of maximum marital deduction because the total gift tax deductions taken ($175,000) do not exceed 50% of the value of the total gifts made ($350,000).

[28] As will be discussed more fully, in an estate of $600,000 there is no tax difference between transferring $300,000 by deductible marital bequest, or transferring $100,000 by deductible gift and the remaining $200,000 by marital deduction. This occurs because if a $100,000 gift is made, the marital bequest deduction will be reduced by $50,000. Since S-1's taxable estate is now $500,000 instead of $600,000, the maximum marital deduction is $250,000, minus $50,000 or $200,000. In short, S-1 can make $300,000 of fully deductible gifts. Whether they are all made by bequest, or by making $100,000 by gifts and $200,000 by bequest is, for tax purposes, immaterial.

[29] In fact, by utilizing the gift tax annual exclusion and the state death tax credit, it will be possible to make tax free transfers of $607,250 after 1981. The calculations required to transfer this amount tax free are as follows:

Assuming that a donor has made no gifts prior to 1981, if he makes a qualified gift to his spouse of $357,250 in 1981 or thereafter, no net gift tax results. The gift tax is computed as follows:

	$357,250	value of gift
less:	3,000	annual exclusion under § 2503(b)
less:	178,625	marital deduction under § 2523
	$175,625	taxable gift
Tax on $175,625 under § 2502 is:		
	$47,000	gross gift tax
less:	47,000	unified credit under § 2505
	0	net gift tax

form which would not have qualified for a marital gift or estate tax deduction and therefore would not have been included in S-2's taxable estate—for example, by using a trust in which S-2 would have been entitled only to income for life.

The inclusion in S-2's estate of all the property transferred in the illustration above carries a very high tax cost because of the higher rates now imposed on property not protected from tax. In this case, the tax on S-2's $600,000 estate, when reduced by the unified credit, will be $145,800. Had S-1 avoided using any unified credit against transfers to S-2, the maximum marital deduction available of $300,000 would have increased S-2's taxable estate to that amount and S-2's estate would be liable for about $40,000 in tax. S-1's remaining estate also would be liable for about $40,000 in tax. However, the aggregate taxes of $80,000 on the two estates is still about $65,000 less than the aggregate taxes owed ($145,000) if S-1 transferred all his property tax-free to S-2. Thus, it can readily be seen that lifetime transfers based on the assumption that the donee will survive the donor may be costly if they unduly increase the donee spouse's estate beyond the available transfer tax credits. It therefore may be generally said that under the new law, tax deferral is a less important objective of lifetime interspousal gifts than the tax reduction which may be obtained if the donee predeceases the donor.

While it is important not to increase S-2's estate unnecessarily, there are certain circumstances in which limited gifts to S-2 will be advisable. In fact, the major potential tax advantage of lifetime marital gifts under the new Act is that they can increase the taxable estate of the donee spouse (S-2) to an amount sufficient to utilize fully all credits available to the donee's estate against federal estate tax in the event that the donee spouse predeceases the donor (S-1). This goal has the virtue of enabling S-2 to utilize his or her unified credit which otherwise would be wasted if S-2 predeceases S-1, without adverse results if the order of death is reversed. One attractive technique for accomplishing this augmentation of S-2's estate

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If the donor dies more than three years later with a gross estate of $250,000 and leaves $250,000 to his wife so that it qualifies for the estate tax marital deduction under § 2056, no net estate tax will result:

	$250,000	gross estate
less:	250,000	marital deduction under § 2056(c)(1)(A)
	0	taxable estate
plus:	175,625	adjusted taxable gifts
	175,625	tentative taxable amount

The tentative tax under § 2001(b) is:

	$ 47,000	
less:	47,000	unified credit under § 2010(a)
	0	net estate tax

Lifetime tax free gifts	= 357,250
Marital bequest	= 250,000
Total tax free transfers	$607,250

would be for S-1 by inter vivos gifts to increase S-2's estate to the exemption equivalent of S-2's credits against tax (again, without using any of S-1's credit against property includible in S-2's estate). S-2's estate plan would provide by will that the money received by inter vivos gifts be placed in trust for S-1 for life, with a remainder to third parties. The tax consequences of this arrangement should S-2 die first are simple enough: S-1 has beneficial use of property insulated from tax by S-2's credit, and the property will pass tax free to third parties on S-1's death. S-1's estate, reduced by the lifetime gifts is subject to less tax than it would have incurred had no such gifts been made. The tax consequences to S-1's estate, if S-1 should predecease S-2 are more complex. However, it can be generally said that S-1's estate can lose nothing, and may gain a small amount of tax reduction if the adjusted gross estate as reduced by the lifetime gifts is less than $500,000 but more than $328,289. Thus, for example, if S-1's estate would have been $700,000 but for the gifts, and S-1 makes $100,000 of gifts to S-2 to enable S-2 to utilize the unified credit, S-1 will, if he or she dies first, lose $50,000 of his or her marital deduction because of the adjustment required by section 2056(c)(1). Since S-1's adjusted gross estate is now only $600,000, his or her maximum marital deduction is only $300,000, minus the section 2056(c) adjustment, or $250,000. Thus, the taxable estate of S-1, having made the $100,000 of gifts, is $350,000. This is, of course, what the taxable estate would have been had S-1 not made any gifts, and had died with a $700,000 estate against which had been taken a marital deduction of $350,000 to reduce the estate to $350,000. Thus, in such large estates there are no tax consequences if S-1 should die first resulting from the use of this technique to augment S-2's estate.

Similarly, in much smaller estates, the use of this technique produces results which are, from a tax standpoint, a matter of indifference if the donee survives the donor. To illustrate, for decedents dying after 1981, an estate equal to a maximum marital bequest deduction of $250,000 plus the exemption equivalent of all available credits ($178,289) can be passed tax free. Lifetime transfers in estates of less than such a total ($428,289) accordingly have no tax impact so long as the donor dies first. A $400,000 estate, disposed of with $221,711 in a marital bequest, and $178,289 in nonmarital property is for tax purposes no different from an estate of $300,000 which has been reduced by lifetime gifts of $100,000 and against which is taken a marital bequest deduction of $121,711 and a nonmarital property bequest of $178,289. In both cases S-1's estate is subject to no tax, and in both cases, S-2's estate will ultimately be $221,711.

Thus, in very large and relatively small estates, there are no ultimate tax savings or losses in S-1's estate incident to making $100,000 of lifetime gifts from the larger estate to the smaller in order to assure full use of the credits available to the smaller estate. The use of lifetime gifts, not exceeding $100,000, however, will, when S-1's prospective estate is in the range of $428,000 to $600,000, actually enable S-1's estate to save taxes on transfers of property to S-2 if S-1 dies before S-2. Further, with the use of lifetime marital gifts of $100,000, it is possible to eliminate entirely federal transfer tax in adjusted gross estates of up to $478,289. This is so because the lifetime marital gifts of $100,000 decrease the adjusted gross estate to only $378,289. Taking the maximum estate tax marital deduction of $200,000 will leave a taxable estate of $178,289, which is the exemption equivalent of the unified credit of $47,000 plus the credit for state death taxes. Thus, using gifts to reduce estates to no more than $378,289 can result in the entire estate passing tax free. If lifetime gifts equal $100,000, this means tax free treatment for $478,289 of transfers.

Making gifts which reduce estates in the range of $528,289 to $600,000 to taxable estates in the range of $428,289 to $500,000 will yield some tax savings, since the maximum marital bequest deductions will never be reduced by more than 50% of the gifts made. Thus a $100,000 gift reducing a $550,000 estate to $450,000, will, after subtracting the reduced marital deduction of $200,000, produce a taxable estate of $250,000. If no gift had been made, the $550,000 estate reduced by a 50% marital bequest of $275,000 leaves a taxable estate of $275,000. When, however, the maximum estate tax marital deduction becomes tied not to the flat $250,000 figure, but is calculated as 50% of the adjusted gross estate, which occurs when the estate reaches $500,000; there ceases to be any tax benefit to the $100,000 gift. This is so because each dollar of inter vivos gift will lower the estate tax marital deduction by 50%. Thus, there will be no tax difference between S-1 dying with an estate of $600,000, against which a $300,000 marital deduction is taken, and dying with a $500,000 estate, following a $100,000 marital gift, against which a $200,000 marital bequest deduction is taken.

Clearly, then, use of the $100,000 fully deductible lifetime gift makes considerable sense for medium sized estates, assuming that nontax factors do not militate against it.[30] If S-1 dies first, the tax reduction in his or her estate represents a deferral of tax until the death of S-2. If S-2 dies first with a taxable estate less than available credits, the assets removed from S-1's estate by this lifetime gift to S-2 represent a net tax reduction in both estates combined. Thus there are tax advantages regardless of the order of death.

2. Marital Deduction Gifts Versus Annual Exclusion Gifts

Given that the primary purpose of lifetime interspousal gifts is to increase the donee spouse's estate to a level which will utilize the spouse's entire available unified credit, the question still remains whether the gifts should be made by fully deductible interspousal gifts, or by annual exclusion gifts.[31] Annual exclusion gifts from S-1 to S-2 provide a supplement, and to some extent an alternative to marital deduction gifts for the purpose of increasing the size of S-2's estate. Such annual exclusion gifts avoid a reduction in the maximum estate tax marital deduction available in S-1's estate. The disadvantage of relying on such annual exclusion gifts is that they are limited to $3,000 per year and the number of years until either S-1's or

[30] Plainly, one such nontax factor is the willingness of the donee spouse to cooperate in the estate plan. In order for the gift to be effective, the donor must retain no power to direct the use, or misuse, of the property transferred. If the donor mistrusts the donee's willingness to invest and dispose of the property in accordance with the estate plan, the donor's making the gift may not be advisable.

[31] I.R.C. § 2503(b) provides that the donor may exclude $3,000 of gifts to each donee each year.

S-2's death is unknowable. Thus, while the goal in either case is augmentation of S-2's estate, the planner must decide whether to accomplish this by annual exclusion gifts, or marital gifts or a combination of both. The two major guidelines available for the planner are rather general. Probably the best that can be said is that (1) the choice depends on a number of nontax facts and circumstances and (2) in many cases the best result may be achieved by using partly marital deduction gifts and partly annual exclusion gifts.

It is doubtful whether it would be possible to list all the facts and circumstances that might be relevant to the choice between annual exclusion and marital deduction gifts. A great deal may depend on S-1's attitude with respect to making gifts to S-2. Planners therefore must remind the prospective donor spouse of nontax considerations, such as the possibility of separation or divorce. Thus, where S-1 suspects that a divorce is a realistic possibility, gifts in excess of the $3,000 annual exclusion may transfer to S-2 more property more rapidly than S-1, given the instability of the marriage, may desire. Among less personal considerations which a planner would have to consider are the relative ages and health of the spouses, the present assets of the donee spouse, and the projected increase to the worth of these assets resulting from earned and unearned income and from appreciation in value.

The planner also should consider other means of increasing S-2's estate besides the use of annual exclusion gifts. For example, if both spouses have earned income, ordinary expenses clearly should be paid by the spouse with the larger amount of assets, and the earnings of the other spouse should be saved since these savings increase the size of his or her estate. Similarly, gifts to third persons should be made solely by the spouse with the larger estate and any joint and several tax liabilities, such as income and gift taxes, should be paid by that spouse.

Where nontax factors such as a short life expectancy of the donor spouse do not militate against it, the use of annual exclusion gifts instead of marital deduction gifts represents the most significant tax savings where the donor's estate without making any gifts exceeds $600,000. To illustrate, assume that prior to making lifetime marital deduction gifts S-1 has a potential adjusted gross estate in excess of $600,000, and that S-1 makes lifetime marital deduction gifts not exceeding $100,000. If S-1 dies first, although these lifetime gifts will reduce the estate tax marital deduction for S-1's estate by an amount equal to one half the value of the lifetime gift, that reduction could have been avoided to the extent that annual exclusion gifts had been substituted for the marital deduction gifts. In other words, had S-1 used annual exclusion gifts to augment S-2's estate, S-1 would have lost no marital deduction.

While there are thus tax advantages of using annual exclusion gifts in large estates, it is probable that in most estate planning situations where S-1 has a gross estate above $600,000 and S-2 has no significant amount of assets, S-1's life expectancy will not permit increasing S-2's estate to the exemption equivalent of available credits solely by making annual exclusion gifts. Under such circumstances, the estate planner certainly should suggest that S-1 consider using in whole or in part the 100% marital deduction for the first $100,000 of lifetime marital deduction gifts. On the other hand, if S-1 and S-2 are both young and apparently in good health, S-1 may wish to gamble on S-2's estate being increased to the exemption equivalent of available credits by means of annual exclusion gifts, and from other sources where possible. There also may be an opportunity to augment annual exclusion gifts with a marital deduction gift shortly prior to S-2's death where the death can be foreseen. By thus supplementing the annual exclusion gifts, such a gift would effectively utilize the credits in S-2's estate.

The preceding analysis assumes, of course, that S-1 is not a multimillionaire whose estate will be taxed at something like 50% or more if he or she should outlive S-2. Under such circumstances, and again solely from the standpoint of the tax objectives of estate planning, a marital deduction gift of at least $100,000 should be considered as early as possible. This is so because by causing an amount equal to the exemption equivalent to pass through S-2's estate, that much is wholly excluded from S-1's estate. Such amounts, if included in S-1's estate, could be taxed at a 70% rate. Annual exclusion gifts each year also would be indicated, in order to assure that S-2's estate will utilize the exemption equivalent if S-2 should die first.

3. Lifetime Marital Gifts in Excess of $100,000

Thus far, the discussion generally has assumed that lifetime marital gifts, if made, should not exceed either $100,000 in total transfers, or such lesser amount as will increase the estate of the spouse with the lesser assets to an amount equal to that spouse's exemption equivalent. Will lifetime interspousal gifts in excess of $100,000 ever be advantageous to accomplish either tax deferral or tax reduction objectives? The answer appears to be in the negative except in the following situations of rather limited application.

First, as discussed above, it is possible to obtain 100% deferral of tax on an estate slightly in excess of $600,000 by a combination of using the gift and estate tax marital deductions and giving lifetime gifts in excess of $100,000. However, this method involves using up S-1's unified credit on gifts to S-2. The gifts so made will be subject to tax in S-2's estate. Yet, if S-1's unified credit had been used against nonmarital gifts the property so protected could have been kept from S-2's estate. The resultant increase in S-2's taxable estate from transferring a large amount of marital property causes a significant increase in total tax. Therefore, such a program would be desirable from a tax standpoint only if the survivor's estate is being left to charity. If the estate will be left to charity, the complete deferral of tax on S-1's estate enables S-2 to enjoy the property fully, without reduction for tax on S-1's death. Since the remainder will pass tax free to charity, there is no increase in tax to reduce the remainder.

Second, gifts in excess of $100,000 may be in order where S-1 owns property expected to appreciate very rapidly prior to S-1's death and it is reasonably probable that S-2 will survive S-1. The use of such gifts can permit the spouses to defer tax on future appreciation for the longest possible period. Obviously, it is rarely certain that any property will appreciate in value to any extent. However, where the appreciation is likely to occur, and is likely to be substantial, deferring tax on it by putting the property in the estate of the spouse most likely to survive can be desirable, although gifts to third persons or gifts in trust which do not qualify for the marital deduction could be more advantageous solely from a tax standpoint.

Apart from these relatively limited circumstances, lifetime marital gifts in excess of $100,000 generally will not be advisable. Nevertheless, as in all things, the planner must be guided by the particular facts and circumstances confronting each client.

4. Marital Deduction Gifts Within Three Years Prior to Death

The Tax Reform Act made three major changes in the rules regarding gifts in contemplation of death. These changes reduce certain preexisting incentives to deathbed transfers. First, a rule inserted in section 2035 treats all gifts made within three years of death (other than gifts of less than $3000 to any donee) as gifts in contemplation of death and brings such gifts into the donor's estate.[32] Second, prior law, which encouraged deathbed transfers because of the estate tax credit allowed for gift taxes paid on gifts in contemplation of death has been changed to eliminate the credit.[33] A final disincentive, which serves to discourage making gifts to spouses which may be deemed to be in contemplation of death stems from the fact that, as passed, the Act allows no offset to the reduction in the maximum marital bequest deduction under section 2056(c)(1)(B) for gifts which are included in the gross estate by section 2035.

Ordinarily these changes in the rules should not cause the possible death of the donor spouse within three years to be an actual deterrent to making lifetime marital deduction gifts. First, the automatic inclusion of the gift in the decedent's estate, leaves the donor's gross estate in the same position as if no gift had been made, and a marital deduction gift which incurs no gift tax could not give rise to a loss of unified credit. Second, if the Technical Corrections Bill currently pending in Congress is enacted,

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[32] I.R.C. § 2035 provides for inclusion in the gross estate of "the value of all property of which the decedent has at any time made a transfer" within three years of death. For a full discussion of the new § 2035 see in this issue, Note, *Section 2035: Gifts Made Within Three Years of Death*, p. 577 *infra*.

[33] The following example will illustrate the economics of a death bed gift before 1977. Assume an unmarried decedent has a gross estate and taxable estate of $10,000,000. His federal estate tax would have been $6,042,600 leaving $3,957,400 to pass to heirs. If he gave away $3,000,000 of property on his death bed which was subsequently included in his gross estate, the tax consequences would be as follows. A gift tax of $947,400 would be paid by him or his estate. His gross and taxable estate would be $9,052,600 ($10,000,000 less $947,400) producing an estate tax of $4,375,176 (gross estate tax of $5,322,576 less credit of $947,400 for gift tax). This would produce a savings for the heirs of $720,024 (difference between $6,042,600 of tax due without the gift and $5,322,576 of tax owed after making the gift) resulting from both the credit for the gift tax paid, and the difference between the estate and gift tax rates.

any downward adjustment in the estate tax maximum marital deduction which otherwise would result from such gifts will be eliminated when the transfers are included in the gross estate under section 2035.[34]

The operation of section 2035 can, however, cause problems if S-2 as donee unexpectedly dies prior to S-1, who dies thereafter within three years of making the transfer to S-2. The gift property will be included in the gross estate of S-2 and because of the operation of section 2035, will also be included in S-1's estate. If, however, S-2 predeceases S-1 by less than two years, the Code softens the impact of this double inclusion by granting S-1's estate a credit for any tax attributable to inclusion in S-2's estate.[35] This may be small comfort if in fact S-2's estate had no estate tax liability, but under such circumstances, although nothing will have been gained by the gift, neither will any tax loss be incurred. S-1's estate is in the same position in which it would have been had no transfer been made and S-2's estate still incurs no tax. On the other hand, if any tax is incurred in S-2's estate, and if S-1 dies more than two years after S-2's death but within three years of making the gift to S-2, estate tax on the same property will be incurred by both estates. Such double taxation of the property would be unfortunate, but nothing is ever certain in estate planning. Hence it would be unreasonable not to make lifetime gifts, where otherwise indicated, because of the slim possibility that the donor will die more than two years after S-2 dies but before escaping the effects of section 2035. Consequently, given the limited circumstances in which tax disadvantages will result from section 2035 treatment once the Technical Corrections Bill adjusts the anomalous treatment of the marital deduction, there is little reason for possible section 2035 treatment to discourage the making of lifetime gifts.

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[34] The following example illustrates the problem. If the donor has total assets of $500,000, and gives $100,000 to his spouse one month before his death to take advantage of the unlimited $100,000 gift tax marital deduction, and dies leaving a will containing a maximum marital deduction clause, his taxable estate will be $300,000 computed as follows:

Ordinary		$400,000
Contemplation of death assets	§ 2035 assets	100,000
	gross & adjusted gross estate	500,000
Less: Marital Deduction Maximum	$250,000	
Adjustment for gift tax deduction	50,000	200,000
	taxable estate	$300,000

If no gift had been made the taxable estate would be $250,000, thus producing a lower tax. That is, the gross estate of $500,000 would be reduced by the available $250,000 maximum marital deduction to produce a taxable estate of $250,000.

Since the purpose of section 2035 is simply to tax the decedent as if the gift in contemplation of death had not been made, there is no reason to reduce the available marital deduction. Section 2035 is not designed to act as a penalty but merely seeks to assure that no tax benefits result from death bed transfers as occurred under prior law.

[35] I.R.C.§ 2013(a).

5. Kinds of Property to Use for Lifetime Marital Gifts

Given the desirability of augmenting S-2's estate to the exemption equivalent by lifetime gifts, the question remains what kinds of property which can be used for such gifts will best aid in the process of increasing S-2's estate. Since in many cases the value of a marital gift to S-2 at the time of the gift may be insufficient to utilize fully the credits expected to be available in S-2's estate, such a gift should be made in property which will appreciate as rapidly as possible. If S-2 in fact survives S-1, the tax on this rapidly appreciating property will have been effectively deferred. If S-2 should predecease S-1, maximum tax reduction can be achieved by using tax credits to pass the property to third persons without incurring transfer tax liability. As is often the case, however, there is a danger that this plan may succeed too well. If S-2 survives S-1 by many years, S-2's estate may be so swollen by the appreciation on the property that the estate tax due on S-2's death will be inordinately high. The effect would be the same as if S-1 had made unnecessarily large marital gifts—that is, deferral is achieved but at the cost of a greater total tax burden than would have been incurred had S-1 retained the rapidly appreciating property and had it placed in a nonmarital trust for S-2's life with a remainder to third parties. This would have subjected the property to tax on S-1's death, when the property had less worth, while giving S-2 the benefit of its income for life without it ever being included in S-2's taxable estate.

In some cases the uncertainty of the order of death militates strongly against the use of certain property for marital deduction gifts. For example, gifts to S-2 of life insurance policies or of cash to pay premiums on policies on S-1's life are not necessarily the most desirable kind of property for marital deduction gifts particularly in the case of term as distinguished from whole life policies. Term policies are especially unhelpful because they have virtually no value unless the insured dies. Whole life policies, which may accumulate some equity by premium payments are less objectionable but even whole life policies are generally to be avoided as marital gift property. This is so because while the appreciation which occurs at the instant of S-1's death for all life insurance policies creates a significant tax deferral if S-2 survives S-1, such gifts fail to contribute to full utilization of S-2's unified credit if the order of deaths is reversed since the policies have little value until S-1 dies. Therefore, life insurance policies and premium payments thereon may be far more suitable for annual exclusion gifts than for marital deduction gifts, since the payments of premiums are not designed to be the chief means of augmenting S-2's estate.

Creation of joint property interests is even more unsatisfactory for marital deduction gifts than are life insurance policies because if S-2 dies first the jointly owned property simply becomes part of S-1's assets as the surviving joint tenant, and S-1 has not removed the property from his or her own taxable estate at all.

Under new provisions of section 2040, added by the Tax Reform Act of 1976, only 50% of the value of the property is included in the estate of each joint tenant, provided one spouse supplied the entire consideration, and an election was made at the creation of the tenancy to treat the acquisition of the noncontributory spouse's interest as a gift under section 2515.[36] Thus, it is now possible to avoid the inclusion of the entire property in the estate of both spouses in the case of joint tenancies created after 1976.

On the other hand, severance of pre-1976 joint tenancies in personal property, as distinguished from real property, may be an effective means of eliminating property from S-1's estate with or without making a current marital deduction gift. If the property was acquired entirely from S-1's contribution and the severance is accomplished by a division in proportion to the respective interests of the spouses, S-2's share is eliminated from S-1's estate without any current gift to S-2 since the creation of S-2's interest was taxed as a gift on creation. Thus, if a true joint tenancy, as distinguished from a tenancy by the entirety, was created when personal property was transferred into joint ownership, upon severance, both S-1 and S-2 will have a 50% interest in the property. If instead of dividing the property in proportion to their respective interests, S-1 then gives up his or her 50% undivided interest by transferring it to S-2, thereby making S-2 the sole owner, 100% of the value of the property is eliminated from S-1's estate, but S-1's current marital deduction gift is only the 50% interest in the property held as joint tenants. The severance of personal property joint interests accordingly may be an important estate planning device, where clients possess substantial assets as joint tenants.

In addition to considering the desirability of severing such personal property joint tenancies, the estate planner should also consider severing and recreating pre-1977 joint interests in real property for which S-1 furnished the entire or major consideration. This technique is authorized by the legislative history,[37] and by carrying out the necessary transactions a husband and wife can assure that half the value of the property is included in each spouse's estate, by making a section 2515 election. Reconstituting such joint tenancies is useful primarily when S-1 is unwilling to make outright marital deduction gifts to S-2, or when S-2's assets are already sufficient to utilize available credits against tax in his or her estate. Although no tax savings will result if S-2 dies first causing the property to pass entirely to S-1 as the survivor, if S-2 is the survivor, maximum tax deferral has been achieved and if S-1's estate is less than $500,000, some tax reduction may have been achieved by reducing S-1's estate after the estate tax marital deduction.

The property used to increase S-2's estate can be critical in achieving the goal of raising S-2's assets to a level equal to the exemption equivalent. While it is generally advisable to use property with some prospect of appreciating and while certain types of gifts, such as the creation of joint tenancies and transfers of life insurance policies are generally not advised, there is no substitute for careful analysis of the particular goals and circumstances of particular clients.

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[36] I.R.C. §2040(b). Section 2515 specifies the procedure for making the election.

[37] H.R. Rep. No. 1380, 94th Cong., 2d Sess. 20, *reprinted in* [1976] U.S. Code Cong. & Ad. News 3330, 3356.

6. Summary of Principles Relating to Lifetime Marital Deduction Gifts

The preceding discussion has been of necessity adumbrated. Nevertheless, the principles discussed reflect the consistent application to marital deduction gifts of the cardinal rules developed earlier. At this point, however, a brief summary of the application of the principles to various estate sizes may be in order.

First, in the case of spouses whose combined estates do not and are not likely to exceed significantly an amount equal to the exemption equivalent of one spouse's available credits against federal estate tax, the gift tax marital deduction plays no appreciable role in either deferring or reducing transfer taxes. This is true, of course, since no matter in which estate the assets are found, they will be tax free in both estates without using any marital deductions. The assets are all protected by available credits regardless of the estate in which they are located and regardless of the order of death.

If the combined assets of the spouses significantly exceed the exemption equivalent of one person's credits against estate tax and the assets of one spouse are appreciably less than that amount, marital deduction gifts within the $100,000 amount which qualify for 100% deduction should be seriously considered to increase the assets of the spouse having the smaller estate to an amount not greater than the exemption equivalent of the unified credit. The objectives are deferring transfer tax liability if S-1 dies first and reducing tax if S-1 is the survivor. If the estate from which the marital gift is to be made is in the range of $428,000 to $600,000 before the gifts are made, gifts not exceeding $100,000 will result in some total tax savings for the donor. If the combined estates of both spouses exceed $600,000, but the estate of one spouse is less than the exemption equivalent of available credits, marital deduction gifts from the spouse with the larger estate to the spouse with the smaller estate sufficient to bring the smaller estate up to the exemption equivalent of credits against tax will decrease aggregate tax liability on the two estates combined if the donee spouse should die first. On the other hand, if the donor dies first and if the donor's estate alone in the absence of the marital deduction gifts would have been $600,000 or more, the tax in the donor's estate will be the same as it would have been without making the lifetime marital deduction gifts and there will be no tax deferred until the death of the survivor. By the same token, however, the reduction of the estate tax marital deduction in the donor's estate, which made the tax in the donor's estate the same as it would have been in the absence of the gift, means that the gift has not increased tax when the donee survives the donor.

Finally, proper choice of property to be used for lifetime marital gifts can significantly improve the success of the plan; improper choice of property may severely impair its effectiveness.

It would be impossible, in concluding this section, to overstress two principles of planning which have nothing directly to do with tax laws. They are, of course, that the estate planner in all cases, must scrupulously assess the financial, personal, family, and tax consequences of all planning options. Second and perhaps more important, the planner must communicate these options clearly and fully to the client, so the client can take an intelligent role in the planning process.

C. *Using the Estate Tax Marital Deduction*

1. The Minimum Marital Deduction Versus the Maximum Marital Deduction

The new maximum estate tax marital deduction equal to the greater of $250,000 or one half of the adjusted gross estate[38] offers as many traps for the unwary as opportunities for new planning techniques. Although heralded as furthering the concept of free transferability among spouses, the cost of such transferability may be extremely high. Thus, if S-1 with an adjusted gross estate of $250,000 dies after 1980 leaving all property to S-2, there will be no estate tax. If S-2 dies soon thereafter without having consumed any of the bequest, there will be a tax of $21,400. If S-1's adjusted gross estate had been $350,000, again, there will be no tax on S-1's death, but the tax on S-2's death will be $52,600. S-1's estate must exceed $428,300 before there is a tax on S-1's death. This does indicate "free transferability". However, on S-2's death, the tax on $428,300 would be $76,700.

Using these same examples, but following our first rule, making the marital bequest to S-2 equal only to the excess of S-1's adjusted gross estate over the amount of the exemption equivalent of credits available to S-1's estate, will result in the smallest combined federal tax. Assuming S-2's estate consists solely of the assets received from S-1, in the first two examples where S-1's estate was, respectively, $250,000 and $350,000, there would have been no tax on S-2's death. In the third example, by following this technique the tax would have been $21,400, not $76,700.[39] A formula written into the instrument creating the marital deduction gift designed to achieve a marital deduction which is exactly equal to the excess of the decedents adjusted gross estate over the credits available to the decedent is here called a "minimum marital deduction" formula.

Usually, the familiar marital deduction formula provides for a marital deduction bequest which will produce the maximum marital deduciton allowable. The inclusion of a minimum marital deduction formula, however, provides for a reduction in the marital bequest to the extent required to utilize available credits against the federal estate tax liability of the decedent's estate. Such a reduction may be expressed in various ways, but the typical formula is one which will cause no reduction in the marital deduction bequest in those cases in which the adjusted gross estate plus adjusted taxable gifts exceeds $250,000 plus the exemption equivalent of credits. In other words, for a decedent dying after 1980 who has made no adjusted taxable gifts and whose estate is entitled only to the unified credit and the credit for state death taxes, the minimum marital deduction under the formula is the same as the maximum marital deduction unless the adjusted

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[38] I.R.C. § 2056(c)(1)(A)(i)-(ii).

[39] Thus, in example one, S-1's marital deduction would have been $250,000 less S-1's exemption equivalent of $178,000 or $72,000. This $72,000 would constitute S-2's taxable estate at death, and would be entirely shielded from tax by S-2's credits. Similarly, in example two, $350,000 less the exemption equivalent $178,000 produces S-1's marital bequest of $172,000, includible in S-2's estate, but fully shielded by the credits available to S-2. Finally, in example three, $428,300 less the same $178,000 produces marital bequest property of $250,000. The tax on $250,000 is $70,800 reduced by S-2's credits to $21,400.

gross estate is less than $428,289. When the estate is smaller than this figure, the minimum formula language operates to reduce the marital bequest to the amount needed to utilize the credits fully.

This new minimum marital deduction affords greater opportunity for tax savings than the new maximum. In fact, as compared with prior law, use of the new maximum in small or medium-sized estates will produce the most advantageous tax result only in two situations. The first is when the combined value of the estates of both spouses does not appreciably exceed the value of the exemption equivalent of credits for a single decedent so that no tax will be due in either estate if all assets pass from one spouse to the other regardless of the order of death. The advantage of the new maximum in this situation is that it dispenses with the need for a nonmarital trust in order to reduce or eliminate federal estate tax. The entire estate can, in these cases, pass directly to the surviving spouse without incurring tax.

The second situation where taking the maximum marital deduction is advantageous is where one spouse owns substantially all of the assets and the value of that spouse's adjusted gross estate is less than $500,000 but greater than the sum of $250,000 and the exemption equivalent of all available credit.[40] The advantage, as opposed to prior law, however, is not in tax savings but rather in deferral of payment. For example, if S-1 dies after 1980 with an adjusted gross estate of $450,000, and leaves a marital bequest of $225,000, equal to one half of the adjusted gross estate allowed under prior law, the federal estate tax due will be $14,000. Yet, the tax will be only $6,600 if the amount of the bequest is equal to the new maximum of $250,000. On S-2's death, however, assuming that the value of S-1's estate remains intact, the smaller marital bequest of $225,000 will be subject to a tax of $14,000 whereas the maximum bequest of $250,000 will be subject to a tax of $21,400. Total taxes of $28,000 are, therefore, the same under either plan. However, use of the maximum marital deduction permits deferral of $7,600 in taxes until S-2's death. In such situations, taking a maximum marital deduction may accomplish significant tax deferral.

Although there are only two instances in small or medium sized estates where the maximum deduction results in tax benefits, these are not the only circumstances under which the maximum deduction can and should be used. In fact, nontax factors may mandate use of a maximum deduction even in situations where it will result in an increase in tax liability. In those estates described at the outset of this article as the "smallest," where the combined assets of both spouses do not exceed $200,000 to $250,000, an estate plan that provides for outright bequests from each spouse to the other is often the only practical one. If substantially all the assets are owned by one of the spouses, the new maximum marital deduction will mean no estate tax in the estate of the first to die. The likelihood of consumption of those assets by the surviving spouse is so great that there probably will be little or no tax due when that spouse dies. Transferring only the minimum marital deduction, on the other hand, would mean placing the assets designed to be shielded by the credits in a trust where the

[40] Ordinarily, this means estates between $428,289 and $500,000, unless taxable lifetime gifts have been made.

costs of administration may well exceed any tax savings. Where extensive consumption of assets is not only likely but necessary, an outright bequest using the $250,000 maximum deduction may be the only appropriate estate plan.

Similarly, for medium sized estates, where combined assets do not exceed the sum of the exemption equivalent of one spouse's unified credit plus $250,000, use of the maximum marital deduction may still be appropriate for either or both spouses, particularly if the estates are at the lower end of this range. This is so because a large portion of the assets may be held jointly and their value will exceed the amount of the minimum marital deduction. Additional factors also may encourage use of a maximum deduction in medium sized estates. First, the surviving spouse may need to consume the estate. Finally, and probably most important, each spouse may want the survivor to have the entire estate regardless of tax costs.

Many families with medium sized estates for whom maximum tax savings are a paramount consideration have substantial death benefits from retirement plans that will not be subject to tax in the estate of the spouse for whom the benefits have accrued, but will be available for the survivor. Here the maximum marital deduction becomes less attractive. Where the taxable estate of the first spouse who dies is not large, but it is unlikely that the estate will have to be consumed in order to provide for the surviving spouse, planning for the appropriate sized marital deduction becomes important. As a general rule, when in medium sized estates, where the combined assets of both spouses do not exceed approximately $425,000, the choice facing each spouse will be between a minimum marital deduction and no deduction. For the spouse with the larger estate, the minimum marital deduction will always produce maximum deferral and minimum tax, since the combination of the marital deduction and the credit will protect the entire estate. Whether or not the spouse with the smaller estate should use a minimum marital deduction to protect from tax that portion of the assets that are not shielded by the credits will require a choice between the deferral of tax accomplished by using the deduction and the added tax that will be imposed on the surviving spouse's estate as a result of the inclusion of the marital deduction property in that estate.

Finally, it should be noted that when it has been decided to use a marital deduction, there are more ways to create the deduction than the familiar plan involving an outright gift or a trust which qualifies for the marital deduction and is includible in the surviving spouse's estate, and a trust created for the benefit of the surviving family or spouse, that is not included in the surviving spouse's estate. Many clients do wish to avail themselves of the marital deduction but fear that the administrative cost of sheltering assets from a second tax by using a separate nonmarital trust for assets protected by the credit is too great. Furthermore, such clients often want the survivor to have the sole beneficial interest in the trust. A single specific portion trust, rather than the two-trust plan may be the appropriate disposition in such case.

The essential elements of a specific portion trust are that a specified portion of a single trust composed of the entire estate is designed to qualify for the marital deduction. To achieve this, the spouse should receive all income at least annually and must also have a testamentary power to appoint that fraction of the property that is to produce the desired marital deduction. It is possible to require revision of the fraction subject to the spouse's power of appointment to account for inter vivos distributions of principal to the surviving spouse. In its simplest form, the formula will be determined at the first death, and if distributions of principal are made during the survivor's lifetime, the fraction will then be larger than was necessary to obtain the desired marital deduction. The choice of whether to require adjustment of the fraction to reflect lifetime distributions must be made in terms of the likelihood of the survivor's needing principal and the size of the survivor's potential estate. In either form, the specific portion trust will undoubtedly be more widely used than in the past.

In summary, the new unified credit which is equivalent to a substantially larger exemption than that provided by prior law has made proper utilization of the marital deduction more delicate. Although the amount of the available deduction has been increased, correct utilization of the deduction requires careful planning. The appropriate amount for the deduction may, according to circumstances be the maximum, the minimum, or none. The job of the planner must be to explain the options so that the clients may choose the plan that properly meets their personal goals.

2. Effect of State Death Taxes

The discussion thus far has been confined solely to federal estate tax consequences. In those states where death taxes do not exceed the federal credit or are computed as a percentage of the applicable federal estate tax, there is no need for further planning. In other cases, however, use of a minimum marital deduction formula may have serious adverse consequences in terms of the state tax. Ironically, this will often be the case in those estates which are small enough to escape federal estate tax. The principal consideration must then be the rate at which the state will tax property in excess of the minimum marital deduction. For example, in Massachusetts, which has one of the highest rates for death taxes and a marital deduction equal to one half of the Massachusetts adjusted gross estate,[41] a minimum marital deduction formula for such small estates will produce the worst possible result on the death of the first spouse. Thus, if the adjusted gross estate is $150,000 so that a "minimum" formula produces no bequest qualifying for the marital deduction, the Massachusetts estate tax on the entire estate will be $7,800. However, the tax would be only $2,250 if a bequest of one half the adjusted gross estate were made to the surviving spouse. Accordingly, when planning estates where a minimum deduction formula will produce either no deduction, or a negligible one, the total federal tax reduction achieved by this plan should be balanced against the possible increase in state death taxes.

In states other than Massachusetts, the difference between utilizing a minimum marital deduction for federal purposes, and a maximum for state purposes may not produce as expensive a tax result as occurs in Massachusetts, but there may be other problems. For example, in some states a marital deduction is available only for certain property passing to a surviving

[41] MASS. GEN. LAWS ANN. ch. 65C § 3.

spouse, such as life insurance or residential real estate. Conflicts may then arise between the desire to transfer property qualifying for the deduction and the need for cash in the residue to pay expenses and taxes. One may be left with an unhappy choice; but an unhappy choice is far preferable to a choice by default.

3. Planning when the Maximum and the Minimum Marital Deduction are Equal

In some estates, the problem of what size marital deduction to use, as has been indicated, is relatively simple. In larger estates, after the crossover point at which the minimum marital deduction becomes the same as the maximum, the answer to the question of how much marital deduction should be used is to be found in a consideration of the marginal federal estate tax rates. Using deaths after 1980 and taking into account the credit for state death taxes, as well as the uniform credit, the effective federal rate is 31.4%.[42] The marginal rate does not increase by more than three percentage points until the taxable estate exceeds $750,000. In fact, for taxable estates between $900,000 and $1 million, it drops to 33.4% due to an increase in the rate of credit allowed for state death taxes. In taxable estates between $1 million and $1,500,000, the effective marginal rate of 36.6% is only 20% higher than the beginning rate of 30.4%.

These figures mean that for one dollar of tax deferred at the lowest net federal tax payable after fully utilizing the exemption equivalent of all available credits, the increase in the federal estate tax cost in the estate of the surviving spouse attributable to the $1 deferral will be no more than $1.20. This rule applies so long as the marital bequests to the surviving spouse do not cause that estate to exceed $1,500,000. That is, the marginal rate on the dollar deferred into the survivor's estate will be taxed at rates no more than 20% higher than would have been imposed in the first decedent's estate. Under such circumstances, the deferral of tax is clearly worth more than the increased cost in the survivor's estate if the survivor lives for more than three or four years.

Some examples will illustrate the low cost of deferral just described in general terms. Assume that S-1 and S-2 each has an adjusted gross estate of $1 million, that neither has made taxable gifts and that neither dies until after 1980. If S-1 uses the maximum marital deduction, the net federal estate tax drops from $265,000 without any marital deduction to $98,800, a deferral of $168,000. On S-2's death, the tax will be $444,400 rather than $265,000 as a result of the increase in that estate attributable to the marital deduction property. Thus, the cost in S-2's estate of deferring payment of $168,800 of tax at S-1's death will be only about $13,000.[43]

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[42] The actual marginal rate from the tentative tax tables is 34%. However, when reduced by credits, each additional dollar above the crossover level will be subject only to 30 cents tax.

[43] That is, rather than paying $265,000 tax on each estate or a total of $531,200 for both estates, $98,800 is paid from S-1's estate. The subsequent tax on S-2's estate of $444,400, plus the $98,800 previously paid is only $12,000 more than the total tax which would have been paid by not deferring any tax from S-1.

However, if S-1's estate was $1 million but S-2's was $500,000, there is no question but that S-1 should take advantage of the maximum marital deduction. The harder decision is in regard to S-2. If S-2 uses a maximum marital deduction, estate tax will be $37,200, not $98,800. The "cost" on S-1's subsequent death, however, would be $352,000 less $265,600 or $86,400. The deferral of $61,600 is at an ultimate cost of $86,400, an increase of $24,800 or more than 40 percent. As the difference between estates increases, the cost of deferral increases and, again, there is a dilemma that can be solved only after consideration of all other facts and circumstances and the inclinations of the clients.

4. Effect of Generation-Skipping Transfers

The analysis thus far has been based solely on transfers of a decedent's own property. If, however, the decedent is the deemed transferor of a generation-skipping transfer[44] occurring at his death or within nine months thereafter the maximum marital deduction in his estate is to be measured by the value of his own adjusted gross estate and adjusted taxable gifts, plus the value of the generation-skipping property even though the estate is not liable for the tax on the generation-skipping property.[45] Furthermore, under section 2602(c)(3), any part of the unified credit not used in calculating the tax on the decedent's estate may be applied to the generation-skipping transfer. These provisions create planning possibilities as well as additional "traps."

The planning possibilities can best be illustrated by an example. If S-1 has an adjusted gross estate of $400,000 and is also the deemed transferor of a generation-skipping transfer of $400,000 (after giving effect to the grandchild exclusion provided by section 2613(b)(5)), use of a maximum marital deduction formula that includes the generation-skipping property will mean no tax on S-1's estate. That is, the estate of $400,000 is totally protected by the increased $400,000 marital deduction that results from treating the generation-skipping property as part of the estate. Under section 2602, the tax on the generation-skipping transfer would be calculated by adding the property to the deemed transferor's estate, and determining the amount of additional tax the deemed transferor would have paid if the property had been a part of the estate. The unified credit would be applied to the generation-skipping tax and the tax payable on the transfer would be $74,800. On the other hand, if instead of the maximum deduction of $400,000 made possible by the inclusion of the generation-skipping property in the estate, the will excluded that property and provided for a minimum marital deduction of $225,000, there would still be no tax on S-1's estate. The tax on the generation-skipping transfer would be $121,800 since none of S-1's unified credit will be available to absorb the tax on the generation-skipping transfers. On the death of S-2, assuming S-2 has no other assets, the tax on the first example would be $68,000 and the combined tax would be $189,800. In the second example, the tax on S-2's es-

[44] The tax on generation-skipping transfers is imposed by I.R.C. §§ 2601-2622. For a discussion of the generation-skipping tax, see in this issue Belknap, *Planning Under the Generation-Skipping Tax*, p. 433 *infra*.

[45] I.R.C. § 2602(c)(5)(A).

tate would be $15,600 and combined taxes $137,400. The choice thus appears to be between deferral of tax on S-1's death and tax reduction on the combined taxes on the estates of S-1 and S-2. The problem is, however, more complex since the surviving spouse is never, under the generation assignment rules of section 2601(c), the beneficiary of a generation-skipping transfer of which the decedent is the deemed transferor. Therefore, the deferral of tax on the death of S-1 will benefit the beneficiaries of S-2's estate at the expense of the beneficiaries of the generation-skipping trust. Unless it is known then whether the client is to be a deemed transferor, the conservative approach will be to specify in any formula that the marital deduction is to be computed without regard to generation-skipping transfers of which the decedent is a deemed transferor.

5. Effect of Prior Taxable Gifts

In the analysis of estate tax marital deduction thus far, it has been assumed that there have been no taxable gifts, either to the spouse or to others, since 1976. Does the fact that the decedent made lifetime gifts require a change in the "Rules"? The answer is negative as to gifts to a spouse for which a marital deduction was allowed and for gifts to third persons within the annual exclusion for charitable gifts. In all other cases, lifetime gifts must be considered because the estate tax is computed by adding to the value of the adjusted gross estate the value of the adjustable taxable gifts[46] and subtracting from the tentative tax on that amount any gift taxes previously paid.[47] The maximum allowable estate tax marital deduction, however, is computed solely in terms of the adjusted gross estate,[48] without regard to the higher figure produced by adding back lifetime gifts. It is entirely possible for the adjusted gross estate to be less than $428,300, the theoretical crossover point where the maximum and minimum marital deduction become the same, but if the sum of adjusted gross estate and adjusted taxable gifts exceeds this amount, use of a minimum marital formula which directs that an amount equal to the remaining exemption equivalent be left in the taxable estate, will produce a larger tax on the estate than a maximum formula bequest. The tax on the S-2's estate will then be smaller. Total taxes may also be less although this is not necessarily so, since the result depends on the value of the gifts to third persons and the size of the adjusted gross estate. Whenever there are gifts to third persons, there is no rule that can automatically produce the optimum result. Again, a decision as to the appropriate plan can be made only on the basis of estimates of estate tax liability in terms of the actual gifts made and the estimated value of the adjusted gross estate.

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[46] I.R.C. § 2001(b)(1)(B).
[47] I.R.C. § 2001(b)(2).
[48] I.R.C. §§ 2056(c)(1)(A)(ii) and (2).

6. Effect of Credit for Foreign Death Taxes and Prior Transfer and Deduction for Gifts to Charities

All of the examples thus far have assumed that the only credits available were the unified credit and the credit for state death taxes. The Code also allows credits for prior transfers under section 2013[49] and for foreign death taxes under section 2014.[50] A minimum marital deduction formula that ignores these credits may have serious adverse consequences. Thus, if S-1 has an estate of $600,000 that includes property inherited just prior to death for which a credit equivalent to the tax on $200,000 is available under section 2013, a maximum marital deduction will leave a taxable estate of $300,000, but all available credits will offset the tax on an estate of $378,300. On S-2's death, $78,300 will be subject to tax at a marginal rate of 30.8%, resulting in a tax of $24,100 that could have been avoided if the marital deduction bequest had been reduced to permit full utilization of the credit. This result can be achieved by using a formula that requires consideration of all available credits. It may lead to mathematical complexity, but for those who do not fear algebra, it is well worth considering.

Many of the "minimum" formulas that have been suggested direct that the marital deduction be reduced to the extent that the reduction will result in no estate tax being paid. However, a reduction only if it leaves the tax at zero will not permit use of the property previously taxed whenever the credit is less than 100% of the tax in the second decedent's estate attributable to inclusion in the estate of the previously taxed property. This will always occur when either (1) the amount of the credit is limited because the transferor's estate was in a lower bracket than the estate of the second decedent or (2) the credit is less than 100% by reason of the number of years since the death of the prior decedent. In such a situation, increasing the taxable estate by decreasing the available marital deduction will increase the available credit. This results because the larger taxable estate increases the marginal rate at which the tax is calculated, thus utilizing the available credit. A tax will still be payable, but reduction of the marital deduction will not necessarily increase the tax after giving effect to the credit for property previously taxed if the adjusted gross estate exceeds the sum of the exemption equivalent of other credits plus $250,000. To achieve this result, the formula must direct reduction to the extent it does not *increase* the taxes payable on account of the testator's death.

If the decedent's estate is less than the sum of $250,000 plus the exemption equivalent of the unified credit and state death tax credit and if the decedent has made no adjusted taxable gifts or lifetime marital deduction gifts which reduce the estate tax maximum marital deduction, it is always possible to reduce the marital deduction by some amount which will eliminate federal estate tax liability. In such cases, if any credit for property previously taxed which would otherwise be available is less than 100% of

[49] I.R.C. § 2013 allows a credit for property previously taxed, to the extent of the previously paid tax, or the tax imposed on the property in the second estate, whichever is less, and reduced in proportion to the time between the imposition of the respective taxes.

[50] I.R.C. § 2014 allows a credit to the extent of taxes paid on property in foreign countries, but not in excess of the tax attributable to the property for estate tax purposes.

the tax in the decedent's estate, it is impossible to obtain such credit even by a formula which directs reduction of the marital gift to the extent that it does not increase the federal estate tax. In such cases, if it is desired to take advantage of the credit for property previously taxed by reducing the marital deduction transfer at the cost of a small increase in federal estate tax payable, other means must be used to accomplish the result.

A final caveat is in order. If a minimum marital deduction formula is combined with a bequest to charity, the amount of which is to be determined as a fraction of the after-tax residue, there will be three amounts that are dependent upon each other and the computations cannot be made. Pecuniary bequests of a fixed dollar amount are the only available alternative if the testator wishes to make a minimum marital bequest.

CONCLUSION

The changes in the estate and gift tax laws made by the Tax Reform Act have complicated the estate planners' problems in making the most effective use of marital deductions. Two major points have been developed in this article.

First, the estate planner should avoid the trap of wasting the new unified credit and other credits against federal transfer taxes which may occur by utilizing the maximum marital deduction. Second, in most, if not all, planning situations, it is more essential than ever to compute estimated transfer tax liability with respect to various planning options, taking into account both alternatives as to the order of death of the spouses as well as possible changes in the estates of both spouses.