THE WHITE HOUSE

WASHINGTON

March 5, 1976

ADMINISTRATIVELY CONFIDENTIAL

MEMORANDUM FOR: WILLIAM F. GOROG

FROM: JAMES E. CONNOR JEC

SUBJECT: Options for Estate and Gift Tax Revisions

The President reviewed your letter of March 3 on the above subject and approved the following option:

Option 1 -
"Approve Treasury proposal to increase estate tax exemption to $150,000 with revised rate schedule and 5-year phase-in."

Please follow-up with appropriate action.

cc: Dick Cheney
Bill Seidman

Connor

THE WHITE HOUSE

WASHINGTON

March 3, 1976

MEMORANDUM FOR THE PRESIDENT

FROM: WILLIAM F. GOROG WG

SUBJECT: Options for Estate and Gift Tax Revisions

BACKGROUND

Despite three major studies of estate and gift taxes in the 1960's (the Columbia University-Brookings Institution study, the American Law Institute study, and the 1968 Treasury study) and despite repeated promises by congressional leaders to take up estate and gift taxes, Congress has deferred acting. In 1969 and 1973, the Administration side stepped the issue and made no estate and gift tax proposals. This inaction resulted for the following reasons:

-- Estate and gift taxes affect relatively few taxpayers and generate relatively little revenue.

-- The reform proposals were mainly proposals to increase taxes -- tax capital gains at death, tax death time transfers more severely by unifying the gift and estate taxes, and impose additional taxes on generation-skipping trusts. Thus, the affected taxpayers have been largely opposed to change.

-- The issues are relatively technical and complex.

There is now renewed interest in Congress in changing the estate and gift taxes. But the focus appears to have shifted to tax relief, rather than reform, and particularly tax relief for family farms and small businesses. The recent double digit inflation compounded the effect of earlier inflation in eroding the dollar value of the $60,000 estate tax exemption. Adjusting for inflation would require that the $60,000 exemption be increased to $210,000. Over one-third of the Senate has sponsored or co-sponsored legislation to increase the exemption to $100,000 or $200,000.

Ways and Means has tentatively scheduled hearings on estate and gift tax reform to begin on March 15, and the Joint Committee staff believes Ways and Means will mark up a bill this spring.

In your State of the Union speech you proposed relief for family owned farms and for owners of family owned small businesses. This proposal provided:

-- A 5-year moratorium on payment of any estate taxes for qualifying ownership interests.

-- Payment of the deferred tax in equal installments over a 20-year period after the 5-year moratorium.

-- A reduction of interest on installments from 7 to 4 percent.

-- Limitation of the 5-year moratorium and 20-year extended payment provisions to the first $300,000 in value of the family farm or business with a dollar for dollar reduction in the value of the qualifying farm or business between $300,000 and $600,000.

Treasury has studied the overall question of estate tax exemption in preparation for upcoming Ways and Means hearings. On February 24, 1976, these recommendations were reviewed by the EPB and the following Administration position was proposed:

-- Increase the estate tax exemption from $60,000 to $150,000. To minimize the potential revenue impact of $1.6 billion, Treasury proposes to:

  . Eliminate the lower rate brackets (3 to 28 percent) on the first $90,000 and establish a new rate schedule starting at 30 percent.

  . Phase in the change over 5 years, resulting in a $1.16 billion annual cost, with a first year cost of $155 million.

REVENUE IMPACT

The recommendation for raising the estate tax exemption to $150,000 and making the minimum tax rate 30 percent reflects a concern to avoid creating an overly large revenue loss as a result of this initiative. A proposal involving a larger revenue loss might trigger an attempt to recoup these funds through institution of a new program to tax unrealized capital gains at death.

The revenue losses which will result from alternate proposals are as follows:

Size of exemption	Revenue loss with current rates	Revenue loss with new beginning rates	Beginning rate
$ 75,000	$500 million	$120 million	14%
$100,000	$900 million	$430 million	22%
$150,000	$1.6 billion	$1.16 billion	30%
$210,000	$2.1 billion	$1.9 billion	30%

EFFECTIVE TAX REDUCTIONS

It is important to recognize that these two initiatives when coupled would provide very significant benefits to the farmer or small businessman.

The following example takes a typical farm estate to show the relative impact of the combination of the recommended $150,000 estate tax exemption and your extended payment proposal. Together they provide greater tax relief than the $200,000 or $210,000 estate tax exemption proposed by many members of Congress.

Example: Father leaves 500 acre farm worth $1000 per acre to son. Other assets are sufficient to pay debts and administrative expenses.

Present law

$500,000 Adjusted gross estate
- 60,000 Exemption
440,000 Taxable estate

$125,500 Estate tax

Proposal

$500,000 Adjusted gross estate
-150,000 Exemption [1]
350,000 Taxable estate — REVENUE COST: $1.16 billion

$109,700 Estate tax
60,335 Estate tax burden [2]

Simple exemption increase [3]

$500,000 Adjusted gross estate
210,000 Exemption
290,000 Taxable estate — REVENUE COST: $2.1 billion

$ 78,500 Estate tax

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[1] Also eliminate lower estate tax brackets, with new beginning rate of 30 percent.

[2] Five-year moratorium and 20-year installment payments reduce tax burden, on a discounted cash basis, by 45 percent.

[3] No change in rate structure; beginning rate is 3 percent.

GIFT TAX CHANGES

Whatever changes are made in the estate tax exemption or rate structure, conforming changes will be required in the gift tax. For example, if the estate tax exemption is increased from $60,000 to $150,000 with a 30 percent starting rate, the gift tax exemption would be increased from $30,000 to $75,000 with a 22.5 percent starting rate. The revenue cost of the gift tax changes will be about $100 million to $150 million.

OPTIONS

Option 1: Approve Treasury proposal to increase estate tax exemption to $150,000 with revised rate schedule and 5-year phase-in.

Option 2: Increase estate tax exemption to a figure higher than $150,000, such as $210,000, with revised rate schedule and 5-year phase-in.

Option 3: Increase estate tax exemption to a figure higher than $150,000, such as $210,000, with a 5-year phase-in but without revision of the rate schedule.

Discussion:

Support of the $210,000 exemption:

-- maximizes support from affected taxpayers but also maximizes opposition from some tax reform quarters.

. Total estate and gift tax collections are currently about $5.1 billion so that the larger exemption increase proposals imply about a 40 percent reduction in collections. Many tax reformers regard the estate and gift taxes as very progressive taxes on the wealthy and will seek to maintain their revenue potential.

-- increases chances of a tax on capital gains at death, which would adversely affect family farms and small businesses.

. However, any such tax would be the responsibility of Congress, and actual enactment of major estate and gift tax changes in this Congress is unlikely.

Support of the $150,000 exemption:

-- reduces revenue cost while still putting Administration in position of advocating very substantial relief.

-- enhances the prospects for Ways and Means approval of a package of estate and gift tax changes that loses revenue, yet does not include a tax on capital gains at death.

RECOMMENDATION:

Option 1 should be approved. The combination of the $150,000 exemption and the deferred payment for farmers and small businesses is a generous estate tax revision. A larger amount is not necessary. Furthermore, greater 1977 receipt losses would seriously impair our budget position. Jim Lynn strongly objects to increasing the exemption and would like to speak to you personally if you are considering Options 2 or 3.

I Approve:

Option 1 ___ *HRF*

Option 2 ________

Option 3 ________

THE PRESIDENT HAS SEEN....

THE WHITE HOUSE

WASHINGTON

March 2, 1976

MEMORANDUM FOR THE PRESIDENT

FROM: WILLIAM F. GOROG

SUBJECT: Estate and Gift Tax Proposals

Attached is a memorandum from Treasury summarizing the EPB Estate and Gift Tax Proposals.

A question has been raised as to why a recommendation was made for establishing the estate tax exemption at $150,000 rather than at a higher level such as $185,000. Treasury points out that the basis for this decision was that such a higher level would build revenue loss from $1.16 billion to $1.46 billion. Treasury has been very concerned that the larger revenue loss may trigger an attempt to recoup these losses through a tax on unrealized capital gain on property transferred at death.

Attachment

OFFICE OF THE SECRETARY OF THE TREASURY
WASHINGTON, D.C. 20220

March 2, 1976

MEMORANDUM TO: THE HONORABLE
WILLIAM GOROG
Deputy Director, Economic Policy Board

FROM: Dale S. Collinson
Tax Legislative Counsel

SUBJECT: Estate and Gift Tax Proposals

Attached are page three of the February 24, 1976, memorandum summarizing for the President the tax policy recommendations of the EPB Executive Committee, together with pages eight and nine of the accompanying discussion memorandum. These materials summarize the estate and gift tax recommendations.

A question has been raised why the estate tax exemption was set at $150,000 rather than some higher amount such as $185,000. The answer is revenue considerations. The $150,000 exemption will cost $1.16 billion annually when fully effective. This is true even though we would be eliminating the lower rate brackets and adopting a beginning estate tax of 30 percent. (There will also be an additional revenue loss, not reflected in the memoranda, of about $100 million annually for conforming structural changes in the gift tax -- $75,000 exemption and 22-1/2 percent beginning rate.) Increasing the exemption to $185,000 would cost an additional $300 million.

Attachments

C. OTHER CAPITAL FORMATION MEASURES

We support the integration proposal outlined last July and recommend continuing to advance the proposal. Given the existing budget constraints we recommend that no other new capital formation measures be suggested to the Senate Finance Committee.

D. ENERGY TAXES

We oppose any changes in the area of oil and gas taxation until price controls are fully removed. We do support the home insulation credit and the six-point utilities relief package.

E. ESTATE AND GIFT TAX REVISIONS

We recommend:

-- Increasing the estate tax exemption to $150,000.

-- Opposing any tax on unrealized capital gain on property transferred at death.

-- Allow free interspousal transfers without imposition of estate or gift taxes.

-- Reaffirming the Administration's proposal to relieve the liquidity problems of family farms and business by liberalizing the provisions for installment payment of estate tax.

-- Taking no position on the other principal issues of estate and gift taxes--unification of estate and gift taxes and additional taxes on generation-skipping trusts.

William E. Simon

William E. Simon

E. ESTATE AND GIFT TAX REVISIONS

Over the past decade there has been much discussion of estate and gift tax reform but little action. There are a number of reasons.

-- Estate and gift taxes affect relatively few taxpayers and generate relatively little revenue.

-- The reform proposals are mainly proposals to increase taxes, for example by taxing capital gains on property transferred at death.

-- The issues are relatively technical and complex.

During this period pressures have been building up for tax relief rather than reform. From a tax on the rich, the estate tax has become a broad-based tax with 11 percent of decedents' estates required to file returns (7.6 percent pay estate tax). Adjusting the $60,000 estate tax exemption for inflation since 1942 would require a $210,000 exemption. Small business and farm interests have been particularly vocal in complaining about the impact of estate taxes, and the pressures for relief have been brought to a head by the Administration's proposal to liberalize the installment payment provisions.

We recommend:

-- Increasing the estate tax exemption to $150,000. To minimize the revenue impact, the lower rate brackets (3 percent to 28 percent) on the first $90,000 of taxable estate would be eliminated and the new rate schedule would start with a 30 percent rate.

  o The revenue cost would be $1.16 billion annually but would be phased in over five years, with a first year cost of $155 million.

-- Opposing any tax on capital on property transferred at death. Any such tax would in reality simply increase death taxes and would attract strong opposition from small business and farming interests.

-- Allow free interspousal transfers without imposition of estate or gift taxes.

  o Present law allows a deduction for transfers to a spouse under the gift tax equal to one-half of the amount transferred to a spouse and under the estate tax equal to the amount transferred to the spouse but with a maximum limit on the estate tax deduction of one-half of the adjusted gross estate.

  o Free interspousal transfer rule supported by most prior studies and by women's organizations; it comports with the tendency of many couples to common management of their assets without regard to nature of ownership as joint property, separate property, etc.

  o The revenue cost, in addition to a $150,000 estate tax exemption, would be about $500 million, which could be phased in over a period of years.

-- Reaffirming the Administration's proposal to relieve the liquidity problems of family farms and business by liberalizing the provisions for installment payment of estate tax.

-- Taking no position on the other principal issues of estate and gift taxes--unification of estate and gift taxes and additional taxes on generation-skipping trusts.

  o These are more technical issues, the solution of which can impinge on estate plans unless carefully handled with adequate transition rules.

  o Our testimony would discuss the issues and the pitfalls.

  o There would be a limited technical recommendation dealing with a particular abuse through gifts in contemplation of death to utilize the existence of a separate gift tax structure to minimize total estate and gift taxes.

William E. Simon

William E. Simon

THE WHITE HOUSE
WASHINGTON

Trudy,

Jim says this doesn't make any difference - do you want to put it with your backup material?

E.

3/13

THE WHITE HOUSE

WASHINGTON

March 10, 1976

MEMORANDUM FOR JAMES CONNOR

FROM: WILLIAM F. GOROG WFG

SUBJECT: Error in March 3, 1976, Estate and Gift Tax Options Memorandum

Treasury miscalculated the estate tax in an example cited on page 4.

Attached is corrected calculation.

Attachment

to: William Gorog

room: OEOB 200 date: 3-9-76

Department of the Treasury

Office of the Secretary

Office of Tax Legislative Counsel

Attached are (1) corrected copy for the example used in the March 3 paper and (2) a new example using an estate of $300,000.

cc: Metz
Penner
Davie
Walker
Goldstein

Dale S. Collinson
Tax Legislative Counsel

room 3064
ext. 8024

Example: Father leaves 300 acre farm worth $1,000 per acre to son. Other assets are sufficient to pay debts and administrative expenses.

Present law

$300,000	Adjusted gross estate
- 60,000	Exemption
240,000	Taxable estate

$62,700 Estate tax

Proposal

$300,000	Adjusted gross estate
-150,000	Exemption [1]
150,000	Taxable Estate

REVENUE COST: $1.16 billion

$46,000 Estate tax [2]
$25,300 Estate tax burden [3]

Simple exemption increase [4]

$300,000	Adjusted gross estate
-210,000	Exemption
90,000	Taxable estate

REVENUE COST: $2.1 billion

$ 17,900 Estate tax

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[1] Also eliminate lower estate tax brackets, with new beginning rate of 30 percent

[2] $100,000 taxed at 30% = $30,000
50,000 taxed at 32% = $16,000
$46,000

[3] Five-year moratorium and 20-year installment payments reduce tax burden, on a discounted cash basis, by 45 percent.

[4] No change in rate structure; beginning rate is 3 percent.

Example: Father leaves 500 acre farm worth $1,000 per acre to son. Other assets are sufficient to pay debts and administrative expenses.

Present law

$500,000 Adjusted gross estate
- 60,000 Exemption
440,000 Taxable estate

$126,500 Estate tax

Proposal

$500,000 Adjusted gross estate
-150,000 Exemption [1]
350,000 Taxable estate — REVENUE COST: $1.16 billion

$113,000 Estate tax [2]
$100,570 Estate tax burden [3]

Simple exemption increase [4]

$500,000 Adjusted gross estate
210,000 Exemption
290,000 Taxable estate — REVENUE COST: $2.1 billion

$ 78,500 Estate tax

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1 Also eliminate lower estate tax brackets, with new beginning rate of 30 percent.

2 $100,000 taxed at 30% = $30,000
$150,000 taxed at 32% = $48,000
$100,000 taxed at 35% = $35,000
$113,000

3 Five-year moratorium and 20-year installment payments reduce tax burden, on a discounted cash basis, by 45 percent for portion of tax attributable to $100,000 (benefits are phased out dollar for dollar for interests valued over $300,000).

4 No change in rate structure; beginning rate is 3 percent.