The Curious Case of Dr. Jekyll and the Estate Tax Marital Deduction: Should Prenuptial Agreements Alter the Relationship?

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I. INTRODUCTION

With the enactment of the Economic Recovery Tax Act of 1981 (ERTA), Congress established a deduction for 100% of the value of transfers between spouses from imposition of the estate and gift taxes, provided the transfers are either outright or in appropriate form. The marital deduction feature of ERTA was the culmination of a policy shift in the transfer taxation of married individuals. Although a married taxpayer would still be taxed as an individual (for purposes of the rate table, for instance), the trans-
ried couple would now be treated as a unit in other transfer code provisions.\textsuperscript{5} When the modern estate tax was enacted in 1916 and the modern gift tax was established in 1932, the taxes did not provide special treatment for transfers from one spouse to the other.\textsuperscript{6} This changed in 1948\textsuperscript{7} with the provision of a 50\% deduction for transfers between spouses, enacted in an attempt to equalize the transfer tax treatment of married couples in separate property states with those in community property states.\textsuperscript{8} ERTA embodied the most recent shift in the transfer tax policy toward married individuals, evincing the congressional determination that married individuals form economic units and that the transfer taxes should not tax transfers between spouses but only transfers outside of the economic unit to a third party.\textsuperscript{9}

The gift tax marital deduction is provided in section 2523 of the Internal Revenue Code.\textsuperscript{10} Section 2523 provides that the value of transfers made from one spouse to another are deductible, resulting in their subtraction from gross gifts during the calculation of the individual spouse’s annual taxable gifts, again, provided they are either outright transfers or made in an appropriate form.\textsuperscript{11} Similarly, section 2056 of the Estate Tax Code provides that the value of transfers made from a decedent’s gross estate to a surviving spouse are deductible, resulting in their removal from the decedent’s taxable estate.\textsuperscript{12} Thus, whether property is transferred to a spouse in life or as a result of death, a taxpayer is forgiven tax liability on the value of such transfers.\textsuperscript{13} As a result of the 100\% deduction for transfers between spouses, married individuals may avail themselves of a benefit in the tax

6. Id.
7. Congress also attempted to address the imposition of the estate tax on married individuals in community property states in 1942, but this effort was abandoned in favor of the initial marital deduction effort in 1948. See infra notes 84-100 and accompanying text.
9. Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, § 403, 95 Stat. 172, 301; S. REP. No. 97-144, at 127 (1981) (“[H]usband and wife should be treated as one economic unit for purposes of estate and gift taxes, as they generally are for income tax purposes.”); H.R. REP. NO. 97-201, at 159 (1981) (reflecting fear that inadequate tax planning could result in spousal property being subjected to tax more than once in a spousal generation, the determination that spouses should be able to transfer property between themselves without imposition of the tax, and that the 100\% deduction would avoid administrative difficulties of accounting for jointly held property of spouses).
14. See, e.g., I.R.C. § 2051 (2006) (defining taxable estate as the gross estate minus allowable deductions); see also I.R.C. § 2503(a) (2006) (defining taxable gift as transfers of property by gift minus allowable deductions and exclusions).}
code that unmarried individuals may not. Indeed, many estate planning techniques minimize or defer transfer tax liability by utilizing the marital deduction provisions.

The marital deduction provisions are part of the Dr. Jekyll and Mr. Hyde approach to married individuals in the Transfer Tax Code. On the one hand, and in addition to the marital deduction provisions, married individuals receive favorable treatment denied to unmarried individuals, such as the ability to split gifts made by one spouse as if each spouse had made half the value of the total gift, and, added most recently to the Code, the ability of a surviving spouse to avail himself of any unused applicable exemption amount of his most recent spouse to pass away. On the other hand, suspicion that a married couple may abuse certain valuation techniques otherwise available to taxpayers led to the enactment of section 2702, which prohibits family units, including spouses, from using vulnerable valuation techniques.

The transfer tax’s focus on married taxpayers is similar to that of the income tax. For instance, again in 1948, in an attempt to equalize the tax treatment of married couples in separate property states with those in community property states, married individuals were provided the option to file

15. See Gutman, supra note 5, at 1219.


17. See generally ROBERT LOUIS STEVENSON, THE STRANGE CASE OF DR. JEKYLL AND MR. HYDE 1 (1888) (Dr. Henry Jekyll was the upstanding citizen with the horrible alter ego, Mr. Hyde).

18. I.R.C. § 2513 (2006); Treas. Reg. § 25.2513-1(b) (2006) (providing a consent procedure for married couples, under which a gift made by either spouse to a third person can be reported as though each spouse made a gift of one-half of the transferred property).

19. Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, I.R.C. §§ 2010(c)(4)-(6) (2010). With the enactment of TRA 2010, the unused applicable exclusion amount of a married individual became portable but only to the surviving spouse. In this way, a married individual’s remaining unified credit will not evaporate at death but instead will possibly shield his spouse’s assets from the estate tax. The provision of portability is currently set to sunset January 1, 2013. Notwithstanding the uncertainty stemming from the sunset provision, estate planners have been evaluating the changes portability may trigger in standard estate planning for married individuals. See, e.g., Deborah L. Jacobs, Married with Assets, FORBES, Jan. 26, 2011 (pondering whether married individuals should forgo certain trust-based estate planning); see also Bridget J. Crawford, One Flesh, Two Taxpayers: A New Approach to Marriage and Wealth Transfer-Taxation, 6 FLA. TAX REV. 757, 768 (2004) (mentioning that the disclaimer provisions favor married taxpayers).

20. I.R.C. § 2702 (2006) (providing that the retained interest in a trust in which the grantor retains the income or remainder interest is valued at zero if the interest given is given to a family member, including the grantor’s spouse, unless one of two detailed current beneficiary terms are used in the trust).
their taxes jointly. Initially, the result of the 1948 enactment was beneficial to married taxpayers with different income levels in common law states, allowing them to split the income equally between them and take advantage of the lower levels of the progressive rate table. Single taxpayers were denied such income splitting. The act placed singles at a serious tax disadvantage, sometimes imposing a tax burden as much as 41% greater on a single individual with an income level equal to that of a married couple. Eventually, in an effort to alleviate the relative burdens placed on single and married taxpayers by the various rate tables that had subsequently been developed for the income tax, the rate tables were adjusted, resulting in the higher rate burden potentially falling upon the married taxpayers instead of the single taxpayer: the so-called marriage penalty. Currently, the code provides relief from the marriage penalty at the lower end of the rate table. The current rate structure for married taxpayers also provides the possibility for a marriage bonus in situations where married couples with significantly different income levels are allowed to jointly file.

21. In 1948, Congress enacted the predecessor to current section 6013 in the Revenue Act of 1948, which permitted married individuals to file a joint tax return. Revenue Act of 1948, Pub. L. No. 80-471, 62 Stat. 110. Congress was reacting to the Supreme Court’s decision in Poe v. Seaborn, 282 U.S. 101 (1930), in which the Court held that a wife was taxable on one-half of the community income, even if it was earned solely by the husband. This introduced a “geographical inequality [to the tax code], since it gave married couples in community property states a large tax advantage over similarly situated married couples with the same aggregate income in common law states.” Druker v. Comm'r, 697 F.2d 46, 48 (2d Cir. 1982). As a consequence of Poe, “marriage usually reduced a couple’s tax burden if they resided in a community property state but was a neutral tax event for couples in common law states.” Id. In addition, “in community property states all married couples with the same aggregate income paid the same tax, whereas in common law states a married couple’s [total] tax liability depended on the amount of income each spouse earned.” Id. The Supreme Court eventually limited the Poe holding by denying the same treatment to people living in states which had allowed them to elect into community property treatment, as opposed to mandating such. Id. (citing Comm’r v. Harmon, 323 U.S. 44 (1944)). But, such limitation did not eliminate states’ consideration of switching to a community property system in order to attain the associated tax benefits. Id.; see also I.R.C. § 66 (2006).

22. Druker, 697 F.2d at 48 (providing geographical uniformity for married people in community property states and common law states and promoting horizontal equity when comparing the aggregate income levels of married individuals in community and common law states).

23. Id. at 48-49.

24. Id. at 49.


Other examples of the Jekyll and Hyde approach taken to married individuals in the Income Tax Code include section 267, which denies loss deductions in transfers between related parties, including husband and wife, and section 132(h), which defines employee to include the employee’s spouse, allowing the exclusion of certain benefits bestowed on the spouse from the actual employee’s income. In addition, certain provisions of subchapter J of the Code, which provides the grantor trust rules, also focus on the tax treatment of married individuals.

Some have argued that marriage should not be accounted for in the Code. Such arguments include the assertion that because married individuals tend to have more money, the tax code should not heap additional benefits upon them. Similarly, it is argued that tax benefits subsidize marriage, encouraging marginal couples to get married to obtain the tax benefits. Further, it is asserted the focus on marriage deviates from the basic principle that the tax code should interfere as little as possible in people’s

27. I.R.C. § 267 (2006) (“No deduction shall be allowed in respect of any loss from the sale or exchange of property, directly or indirectly, between persons specified [in the statute].”).
30. I.R.C. § 132(h)(2)(A) (2006) (“Any use by the spouse or a dependent child of the employee shall be treated as use by the employee.”).
32. See, e.g., I.R.C. § 672(e) (2006) (treating interests held by a grantor’s spouse as interests held by the grantor); I.R.C. § 677(a)(1) (2006). Section 677(a)(1) treats the grantor as the owner of a trust for income tax purposes if the income of the trust, without the consent of an adverse party, or in the discretion of a non-adverse party, may be distributed to the grantor’s spouse. This is intended to discourage married taxpayers from gaming the income tax system through clever trust planning. The grantor trust rules are now more commonly triggered purposefully by taxpayers to achieve desirable estate planning results. See, e.g., Michael D. Milligan, Sale to a Defective Grantor Trust: An Alternative to a GRAT, 23 EST. PLAN. 1 (1996) (discussing an estate planning technique to avoid transfer tax restrictions by conducting transactions with a trust intentionally termed as a “grantor trust”).
34. Puckett, supra note 33, at 1417-19.
35. Id.
behavior.\textsuperscript{36} It has also been argued that allocating tax burdens based on an individual’s marital status undermines the United States’s democratic ideals.\textsuperscript{37}

In an article proposing the elimination of the marital deduction provisions entirely, Professor Bridget J. Crawford described the transfer tax’s approach as “one flesh, one taxpayer.”\textsuperscript{38} Professor Crawford deemed this approach as “undesirable because [the transfer tax benefits] are based on gender stereotypes and because [it denies] estate and gift tax benefits to socially important non-marital relationships.”\textsuperscript{39} Professor Crawford proposed that gratuitous transfers between spouses be fully taxable, but the amount an individual may transfer free of transfer tax considerations be increased to eliminate the associated complexity of such an approach from the Code.\textsuperscript{40} Professor Crawford also observed that removing the marital deduction provisions from the Code would eliminate a “powerful incentive” for spousal transfers that would not otherwise be made, which would tend to simplify and ease the costs of administration of the tax system.\textsuperscript{41}

Others have embraced the use of marriage as a factor in allocating tax burdens,\textsuperscript{42} arguing that if we were to eliminate marriage benefits in the code, we would invite a flood of potential interspousal tax avoidance schemes.\textsuperscript{43} The argument continues that, because of the complexity of the tax code and budgetary constraints on the IRS, it would be difficult to detect the schemes and enforce the code.\textsuperscript{44}

Still others are either neutral toward the use of marriage in the tax code or call for further study.\textsuperscript{45} For instance, Great Britain has an individual taxation system, not allowing married taxpayers to aggregate their tax attributes.\textsuperscript{46} It has been proposed that a comparative study between the U.S. sys-

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  \item \textsuperscript{36} Motro, supra note 26, at 1529 n.67.
  \item \textsuperscript{37} See Jessica Knouse, Civil Marriage: Threat to Democracy, 18 MICH. J. GENDER & L. 361 (2012).
  \item \textsuperscript{38} Crawford, supra note 19, at 760 & n.8.
  \item \textsuperscript{39} Id. at 760 (amount that can pass tax free is referred to as the Unified Credit); see id. at 787 & n.160.
  \item \textsuperscript{40} Id. Professor Crawford further observed that the increased Unified Credit amount would alleviate the disparities between married individuals in community property states and common law property states. Id. at 803.
  \item \textsuperscript{41} Id. at 801-02.
  \item \textsuperscript{43} See id.; Motro, supra note 26, at 1551.
  \item \textsuperscript{44} See McMahon, supra note 42, at 741.
  \item \textsuperscript{46} McMahon, supra note 45, at 170.
\end{itemize}
tem and the individual system be conducted to determine the consequences
that may stem from shifting to an individual system.\textsuperscript{37} For instance, does an
individual taxation system tend to trigger a redistribution of property within
the marital unit?\textsuperscript{48} Further, do we want a system that promotes such redis-
tribution?\textsuperscript{49} A discussion of the income tax provisions related to marriage is
beyond the scope of this Article.\textsuperscript{50}

A primary justification for bestowing benefits on married taxpayers in
the income and transfer tax systems, currently, is the policy pronouncement
that married individuals constitute economic units and should not be re-
quired to account for intramarriage transfers, but only for transfers outside
of the economic unit.\textsuperscript{51} The characterization of married individuals as eco-
nomic units is the subject of much criticism, including the assertion that
married couples do not always function as economic units.\textsuperscript{52} No baseline of
economic activity has been legislated by which to measure whether married
individuals are functioning as an economic unit. The mere fact of marriage
acts as a proxy, leading to the presumption that the married taxpayers are
functioning as an economic unit.\textsuperscript{53} Once presumed, the tax code bestows
certain benefits and imposes certain restrictions on the married taxpayers.\textsuperscript{54}
Professor Crawford’s conclusion includes the observation that “[t]reating
husband and wife—or any two taxpayers—as a single economic unit is
inconsistent with the privileges and responsibilities of citizenship as they
have evolved over time.”\textsuperscript{55}

To be considered an economic unit, there is no requirement that the
secondary earner in the marriage have a legal entitlement to the primary
earner’s money.\textsuperscript{56} The married individuals may maintain separate bank ac-
counts, and the marriage may be governed by a prenuptial agreement.\textsuperscript{57} In
the sense that the economic unit presumption allows transfer tax benefits to
married individuals who are not actually functioning as an economic unit,
however measured, the economic unit justification is applied too broadly.\textsuperscript{58}

\textsuperscript{47} See id. at 165.
\textsuperscript{48} See id. at 207.
\textsuperscript{49} See id.
\textsuperscript{50} For a discussion of a proposal to remove marriage as a proxy for economic unit
status for purposes of joint filing provisions, see Motro, supra note 26, at 1543-53.
\textsuperscript{51} See H.R. REP. NO. 90-1274.
\textsuperscript{52} See Motro, supra note 26, at 1512; Richards, supra note 33, at 621.
\textsuperscript{53} See Crawford, supra note 19, at 805; Motro, supra note 26, at 1541.
\textsuperscript{54} See Crawford, supra note 19, at 805.
\textsuperscript{55} Id.
\textsuperscript{56} Richards, supra note 33, at 621; Motro, supra note 26, at 1532.
\textsuperscript{57} Richards, supra note 33, at 621.
\textsuperscript{58} See id.
The use of only marriage as a proxy for an economic unit has also been criticized. To the extent unmarried (by choice or otherwise), yet committed couples actually function as an economic unit, they are denied these tax benefits, even though they may qualify under the underlying economic unit justification. In that sense, the justification is applied too narrowly. Given the lack of a baseline of economic activity by which to measure whether a couple is functioning as an economic unit, these unmarried, yet committed couples are unable to prove they are otherwise entitled to the related benefits.

To be sure, the Jekyll approach is more generous than the Hyde approach is restrictive. The focus on marriage and reliance on the economic unit presumption is firmly entrenched in the tax code. This Article joins the chorus of those criticizing the use of the economic unit presumption, using a song sheet involving prenuptial agreements to do so. To make this criticism, this Article considers a discrete question: Should married individuals be able to avail themselves of the 100% estate tax marital deduction when their marriage is governed by a prenuptial agreement? Put another way, should the existence of a prenuptial agreement ever rebut the economic unit presumption? Or, do the elements of simplicity and administrative ease gained through the use of the economic unit presumption still support the presumption even if there is a written agreement undercutting, in some fashion, the existence of an economic unit? The 100% marital deduction provides a benefit to married individuals. Should they be allowed this benefit if they have avoided the burdens associated with marriage, in some manner, by executing a prenuptial agreement?

59. See id. at 636. In Mueller v. Commissioner, the Supreme Court affirmed that reliance on state-sanctioned marriage for joint filing purposes did not violate the due process clause. Mueller v. Comm’r, 537 U.S. 1003 (2002). The court agreed with the Tax Court’s findings that Congress had a rational basis for determining that married units had greater financial burdens. Mueller v. Comm’r, 82 T.C.M. (CCH) 764 (T.C. 2001). However, the Tax Court’s focus was on contemporary economic considerations and left open the possibility that these considerations could lead Congress eventually to extend the benefits of joint filing to unmarried economic units: “[W]hether policy considerations warrant narrowing of the gap between the tax treatment of married taxpayers and homosexual and other nonmarried economic partners is for Congress to determine in light of all relevant legislative considerations.” Id. at 2.

60. See Motro, supra note 26, at 1512.

61. See id.

62. See id.

63. For convenience, although the questions may be similar, this Article references only prenuptial agreements, not post nuptial agreements. See generally Sean Hannon Williams, Postnuptial Agreements, 2007 Wis. L. Rev. 827 (2007).

sumption is accepted. Given the lack of a baseline of economic activity between spouses with which to determine if they actually function as economic units, the use of marriage as a proxy for the economic unit presumption adds an element of simplicity to the Transfer Tax Code and eases enforcement concerns associated with determining the transfer tax consequences of intramarriage transfers.\textsuperscript{65} For discussion purposes, the use of the economic presumption is accepted, generally, outside of the context of marriages governed by prenuptial agreements.

It is recognized that the discussion herein may be applicable to the broader question of whether any of the marriage-related benefits should be allowed to individuals married pursuant to a prenuptial agreement. As a corollary question, it could be asked whether the valuation restrictions of section 2702, for instance, should apply to individuals married pursuant to a prenuptial agreement.\textsuperscript{66} The article’s conclusion regarding the discrete question presented suggests these two questions should be answered in the negative.

Parts III, IV, and V of the Article discuss the evolution, basic mechanics, and related estate planning uses of the 100% estate tax marital deduction. Part V discusses the use of marriage as the proxy for the economic unit presumption. Part VI briefly discusses the history of prenuptial agreements and common tax-related terms of such agreements. Part VII discusses whether the economic unit presumption should be treated as rebutted if there is a prenuptial agreement, leading to a disallowance of the estate tax marital deduction. Part VIII concludes that, although such a disallowance may be justifiable for certain policy reasons, it would add too much complexity to the tax code, with attendant compliance difficulties, to do so.

II. ESTATE TAX MARITAL DEDUCTION: HISTORY

The modern estate tax was enacted in 1916 to raise revenue as America prepared to enter World War I.\textsuperscript{67} Congress enacted the gift tax in 1932 to prevent avoidance of the estate tax through inter vivos giving.\textsuperscript{68} Despite the revenue-raising rationale that gave rise to the estate tax and the complementary gift tax,\textsuperscript{69} the stronger historic and long-stated primary purpose of the

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  \item \textsuperscript{65} See McMahon, \textit{supra} note 42, at 718.
  \item \textsuperscript{66} See Motro, \textit{supra} note 26, at 1551 (marriage-based tax restrictions should not apply if the taxpayers may not jointly file).
  \item \textsuperscript{67} Revenue Act of 1916, Pub. L. No. 271, §§ 200-12, 39 Stat. 756, 777-80.
  \item \textsuperscript{69} The generation-skipping transfer tax, enacted in 1986, was designed to prevent avoidance of the estate tax through trust devices that allowed a decedent to leave a series of
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The estate tax has been to break up large concentrations of wealth. One scholar articulated this goal as: “The purpose of [the transfer taxes] is not to raise revenue (release resources to the government) but gradually and continually to correct the distribution of wealth and to prevent concentrations of power detrimental to the fair value of political liberty and fair equality of opportunity.”

The estate tax and gift tax were in pari materia, but they were not united, initially, as each had its own rules, regulations, and rate tables. Though not united, generally, they did share a common feature: neither tax provided special treatment for transfers between spouses. The absence of such provisions led to disparate treatment of the estates of deceased individuals leaving a surviving spouse in community property estates with the estates of such individuals in common law property states. The disparate treatment was the result of the split of community property at death, allowing half of the decedent’s wealth to pass to his surviving spouse by operation of law, outside of the transfer tax system. If a decedent in a common law state wanted half of his property to pass to his surviving spouse, he could arrange his affairs to accomplish such, but the property would pass through his gross estate and be subjected to the estate tax system.

For example, assuming an estate tax regime with a flat 50% estate tax rate and without any available credits or deductions, a decedent in a community property state could have half of his property pass through his gross estate and be subjected to the estate tax system, thereby providing descendants with the fruit of the family fortune, but never giving them enough of an interest in it to subject the trust property to the estate tax at the death of each generation. Tax Reform Act of 1986, Pub. L. No. 99-514, §§ 1431-33, 100 Stat. 2085, 2717-32. The passage of the generation-skipping transfer tax completed the transfer tax triumvirate.

70. JOHN RAWLS, A THEORY OF JUSTICE 277 (1971) (alteration in original). This statement is consistent with the testimony of U.S. Representative Robert Kean before the Ways and Means Committee, where he approved of the tax solely because it functioned to “prevent[] the piling up of too big estates.” Louis Eisenstein, The Rise and Decline of the Estate Tax, 11 TAX L. REV. 223, 224 (1955) (quoting Hearings Before the Comm. on Ways and Means on Revenue Revision of 1950, 81st Cong. 125 (1950)). He repeated this sentiment in 1951 by saying, “[The estate tax] was not chiefly for the production of revenue, but rather for a social benefit, in order not to allow these great piles of capital to grow and grow.” Id. at 224 n.6 (quoting Hearings Before the Comm. on Ways and Means on Revenue Revision of 1951, 82d Cong. 68 (1951)).

71. Statutes in pari materia are those related to the same person or thing or having a common purpose. BLACK’S LAW DICTIONARY 711 (5th ed. 1979); see Burnet v. Guggenheim, 288 U.S. 280, 286 (1933) (“The two statutes are plainly in pari materia.”).

72. Eisenstein, supra note 70, at 224.


74. See Eisenstein, supra note 70, at 224; Crawford, supra note 19, at 762-64.

75. See Eisenstein, supra note 70, at 224; Crawford, supra note 19, at 762-64.

76. Eisenstein, supra note 70, at 224.
community property state with title to community property valued at $2,000,000 would only have a taxable estate for estate tax purposes of $1,000,000. This is because the community property laws provide that half of his community property belongs to his surviving spouse, passing not from the decedent’s gross estate but by operation of state law.\textsuperscript{77} The $1,000,000 taxable estate would be subjected to the estate tax, resulting in a $500,000 estate tax liability. By contrast, an individual in a common law state with title to $2,000,000 would have a taxable estate of $2,000,000, as nothing would be deemed the property of his surviving spouse by operation of law.\textsuperscript{78} This $2,000,000 estate would be subjected to the estate tax, resulting in an estate tax liability of $1,000,000. Considering the estate tax rates were progressive, the benefit of this disparate treatment to estates in community property states was even greater.\textsuperscript{79}

This disparity also manifested itself in imposition of the gift tax and income tax. A transfer of community property as a gift was treated as if each spouse had made half of the gift, allowing the value of half of the gift to be taxed at lower marginal rates by each spouse.\textsuperscript{80} By contrast, again, a gift of separately titled property in a common law state was taxed solely to the person making the transfer.\textsuperscript{81} In income tax, the income earned by one spouse in a community property state was split between husband and wife, allowing each spouse to pay taxes based on half of the amount of the total income, taking twice the advantage of the lower marginal rates.\textsuperscript{82} If both spouses in either jurisdiction had similar wealth levels and income levels, the imposition of the tax laws was more or less neutral, but otherwise couples in community property systems were favored over those in common law jurisdictions.\textsuperscript{83}

Congress attempted to resolve the associated estate tax disparities in 1942.\textsuperscript{84} The 1942 estate tax amendments required all of a decedent’s community property, including the portion that passed to the surviving spouse by operation of law, to be included in the estate of the first spouse to die, unless the property was attributable to the services or property of the surviving spouse.\textsuperscript{85} This approach ordinarily required all of the community property to be included in the gross estate of the husband.\textsuperscript{86} If the wife


\textsuperscript{78} See id.

\textsuperscript{79} See id.

\textsuperscript{80} See id.

\textsuperscript{81} See id.

\textsuperscript{82} Druker v. Comm'r, 697 F.2d 46, 48 (2d Cir. 1982).

\textsuperscript{83} See id.


\textsuperscript{85} Price & Donaldson, supra note 77, § 5.2.1.

\textsuperscript{86} Id.
passed first, one-half of the community property was included in her gross estate given that she held a power of testamentary disposition over her half of the community property.\textsuperscript{87}

The 1942 estate tax amendments were unpopular in community property states, not surprisingly given the amendments subjected more of their property transfers to imposition of the tax and did not address the treatment of taxpayers in common law states.\textsuperscript{88} In addition, the 1942 enactment did not alleviate the disparate treatment associated with the imposition of the income tax.\textsuperscript{89} The income tax advantages offered to community property couples eventually influenced six jurisdictions to adopt community property systems between 1945 and 1947 (Hawaii, Michigan, Nebraska, Oklahoma, Oregon, and Pennsylvania).\textsuperscript{90} As a result of congress’s 1948 adoption of the limited marital deduction and related modifications to the gift and income taxes, each of these six states reverted to common law property systems.\textsuperscript{91}

The 1948 enactment established a deduction for transfers to surviving spouses, limited to 50\% of the deceased spouse’s adjusted gross estate.\textsuperscript{92} The adjusted gross estate was the result of subtracting from the gross estate the value of any community property included in the gross estate and the portion of deductions under sections 2053\textsuperscript{93} and 2054\textsuperscript{94} attributable to the noncommunity property.\textsuperscript{95} As a general matter, a deduction was allowed if the property was transferred to a surviving spouse in a manner that would make it includible in the survivor’s gross estate when he or she died.\textsuperscript{96}

The 1948 enactment also created a deduction for 50\% of the value of gifts made from one spouse to the other and introduced split gifts to the gift tax system, allowing a spouse to treat a gift made by one as if made one-

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\item \textsuperscript{87} Id.
\item \textsuperscript{88} Id.
\item \textsuperscript{89} Id.
\item \textsuperscript{90} PRICE & DONALDSON, supra note 77, § 5.2.
\item \textsuperscript{91} Id.
\item \textsuperscript{92} Id. § 5.2.2.
\item \textsuperscript{93} I.R.C. § 2053 (2006) (providing deduction from the gross estate for administrative expenses).
\item \textsuperscript{94} I.R.C. § 2054 (2006) (providing deduction for the estate for certain losses, such as those caused by fire).
\item \textsuperscript{95} See Revenue Act of 1948, I.R.C. § 2506(c) (amended 1976). As an example, assume a decedent left a gross estate of $800,000 in noncommunity property. The decedent’s estate was allowed a total of $40,000 of deductions under section 2053. The decedent left $25,000 to a charity, for which a deduction under section 2055 was allowable, and the balance of the estate to his wife. The maximum allowable marital deduction was limited to $380,000 (one-half of the decedent’s adjusted gross estate) calculated as follows: gross estate of $800,000 less the section 2053 deduction of $40,000 resulted in an adjusted gross estate of $760,000, multiplied by 50\%, determining that the maximum marital deduction amount was $380,000. PRICE & DONALDSON, supra note 77, ex. 5-1.
\item \textsuperscript{96} Revenue Act of 1948, I.R.C. § 2506(c) (amended 1976).
\end{itemize}
half by each.\footnote{97}{\textit{Estate planning use of split gifts is discussed infra} at notes 194-97 and accompanying text.} In community property states, a gift of community property by one spouse to a third party was treated as if each spouse had made half of the gift. For example, assuming there were no deductions or exclusions available, if a husband had title to and transferred property valued at $100,000 to a third party, the wife would be treated as having made a $50,000 taxable gift, and the husband would be treated as if he transferred a taxable gift of only $50,000, allowing each to take advantage of the lower portions of the progressive rate schedule. By contrast, a spouse making a $100,000 gift in a common law state would be taxed on the entire transfer.\footnote{98}{\textit{I.R.C.} § 2513 (2006). Section 2513(a)(1) provides: A gift made by one spouse to any person other than his spouse shall, for the purposes of this chapter, be considered as made one-half by him and one-half by his spouse, but only if at the time of the gift each spouse is a citizen or resident of the United States. \textit{I.R.C.} § 2513(a)(1) (2006). The split gift provision only applies if both spouses consent to so sharing the value of all gifts to third parties made in a given tax year. \textit{I.R.C.} § 2513(a)(2) (2006).} The split gift provisions, currently contained in section 2513,\footnote{99}{\textit{Price \\& Donaldson, supra} note 77, § 5.2.2.} afford the married taxpayers in common law states to elect the same treatment provided as a result of underlying property law to the married taxpayers in community property states.\footnote{100}{\textit{Id.}} From a theoretical standpoint, the split gift provisions were rendered unnecessary by the eventual enactment of the 100% marital deduction: one could transfer half of the value of the intended gift to a third party to his spouse, transfer tax free, and then the spouse could make the actual transfer to the third party, rather than only elect to be treated as if she had done so. Perhaps for reasons of practicality, however, the provision persists.\footnote{101}{\textit{Id.}}

Regarding transfer taxes, the purpose of the 1948 amendments was to “equalize the effect of the estate taxes in community property and common-law jurisdictions.”\footnote{102}{\textit{United States v. Stapf,} 375 U.S. 118, 128 (1963).} While it is true the estate tax marital deduction was available to estates of decedents where separate property had been held in a community property state, the guiding objective involved providing decedents in common law states with the ability to mimic the advantages of “estate splitting” allowed to decedents in community property states.\footnote{103}{\textit{Id.}} A key feature of the 50% estate tax marital deduction was that it allowed taxes to be deferred, not avoided. The deduction was only available if the subject property transferred to the surviving spouse was transferred in a manner...
that would render it includible in the surviving spouse’s gross estate.\textsuperscript{103} In that manner, the tax was deferred, not avoided, and the value would potentially be subjected to the estate tax upon the death of the surviving spouse. The income tax disparity was addressed by allowing married individuals to file joint returns, aggregating their gross income and applying preferential tax rates.\textsuperscript{104}

In 1976, Congress tinkered with the marital deduction, increasing the quantitative limit of the deduction to either $250,000 or half of the decedent’s gross estate, whichever was higher.\textsuperscript{105} In effect, to the extent of $250,000, married individuals were treated as an economic unit for estate tax purposes at this time. With the Tax Reform Act of 1976,\textsuperscript{106} Congress endeavored to unify the separate estate and gift tax systems.\textsuperscript{107} The 1976 Act equalized the rate structures, created the unified credit,\textsuperscript{108} and updated the transfer tax consequences of gifts made within three years of death.\textsuperscript{109} The purpose of unification was to equalize the transfer tax burden on transfers of the same amount of wealth, whether made inter vivos or at death.\textsuperscript{110}

The 1976 Act did not completely unify the estate and gift taxes. Among other disparities between the estate and gift tax were the different marital-deduction provisions under each.\textsuperscript{111} Recognizing these disparities, Congress enacted ERTA in 1981.\textsuperscript{112} ERTA introduced the unlimited marital deduction to both taxes, thereby further unifying the two taxes.\textsuperscript{113}

\begin{itemize}
\item \textsuperscript{103} Id.
\item \textsuperscript{104} See supra notes 22-25 and accompanying text.
\item \textsuperscript{105} Gutman, supra note 5, at 1220 n.128.
\item \textsuperscript{106} Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520.
\item \textsuperscript{108} See infra notes 166-70 and accompanying text.
\item \textsuperscript{113} Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, § 403, 95 Stat. 172 (codified as amended at I.R.C. § 2056 (2006)); David Jouiaian, Office of Tax Analysis, U.S. Dep’t of Treasury, O.T.A. Paper 100, The Federal Gift Tax: History, Law, and Economics 6 (2007). At the same time, however, the 1981 Act disunified the taxes further by increasing the annual exclusion from $3,000 to $10,000 under the gift tax and creating unlimited gift-tax exclusions for transfers made on behalf of another as payment for his education or healthcare. Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, § 441, 95 Stat. 172 (codified as amended at I.R.C. § 2503(b), (e)). In order to “qualify” for the deduction, the transferor must make the payment directly to the beneficiary’s educational institu-
Congress stated the 100% marital deduction was justified because husband and wife constitute one economic unit and should not be required to account independently for transfers made between the members of the unit. Further, Congress believed a 100% marital deduction would alleviate certain difficulties associated with imposing the estate tax on property that had been held jointly by the spouses. As with the 50% marital deduction, property received by the surviving spouse for whom the value was allowed a 100% marital deduction was required to be transferred in a manner that would make it includible in the survivor’s gross estate.

Congress first addressed the concern regarding jointly held spousal property in the Tax Reform Act of 1976, with the enactment of section 2040(b), but refined its approach in the ERTA. Section 2040(b) provides special gross estate inclusion rules for married taxpayers in regards to property the decedent held with his surviving spouse in joint names with right of survivorship or in tenancies by the entirety. Section 2040(b) allows married taxpayers to avoid the general approach to such properties provided in section 2040(a).

The standard approach regarding gross estate inclusion of property in which the decedent was a joint owner with right of survivorship instructs the inclusion of the portion of the date-of-death value of such property according to the percentage of the consideration the decedent had provided. For instance, if the decedent provided the entire purchase price for the property, the value of the entire property is in his estate. If the decedent provided no part of the consideration but one of the other joint owners provided the entire consideration, no part of the value of the property is included in the decedent’s gross estate. If the decedent and his two brothers, for example, acquired the property via gift, only one-third of the property would be included in his gross estate.

Section 2040(b) allows married taxpayers to avoid the general approach to such properties provided in section 2040(a).
difficult tracing problems. For example, in situations where the decedent provided the other joint owner via gift with part of the consideration paid by the other joint owner, some portion of that prior gift may be deemed consideration paid by the decedent, triggering a proportionate inclusion of the date-of-death value of the property in the decedent’s gross estate.\textsuperscript{124}

Congress enacted section 2040(b) because it determined the necessary tracing was particularly vexing when the joint property was held within the marriage.\textsuperscript{125} If the decedent held property jointly with only his surviving spouse or in tenancies by the entirety, section 2040(b) provides that only half of the property is in the decedent’s gross estate, alleviating the need to trace the source of the consideration.\textsuperscript{126} Section 2040(b) treats married taxpayers as economic units and was enacted to “implicitly recognize the services furnished by a spouse toward the accumulation of jointly owned property even though the monetary value of the services cannot be accurately determined.”\textsuperscript{127}

The economic unit justification is a presumption that husband and wife own and control all of the income and share the burdens of marriage equally, regardless of who earns the income or who incurs the burdens.\textsuperscript{128} In considering the 100% marital deduction features as part of the potential unification of the transfer tax systems in 1969, the Treasury Department stated:

It does not appear, then, that transfers of property between husband and wife are appropriate occasions for imposing the tax. An especially difficult burden may be imposed by the tax when property passes to a widow, particularly if there are minor children. The present system of taxing

\begin{footnotes}
\item[124.] Treas. Reg. § 20.2040-1(c)(4)-(5) (1958); see, e.g., Estate of Goldsborough v. Comm’r, 70 T.C. 1077 (1978), aff’d, 673 F.2d 1310 (4th Cir. 1982).
\item[126.] I.R.C. § 2040(b) (2006).

The committee believes that a husband and wife should be treated as one economic unit for purposes of estate and gift taxes, as they generally are for income tax purposes. Accordingly, no tax should be imposed on transfers between a husband and wife.

Moreover, the committee believes that the taxation of jointly held property between spouses is complicated unnecessarily. Often such assets are purchased with joint funds making it difficult to trace individual contributions. \ldots Accordingly, the committee believes it appropriate to adopt an easily administered rule under which each spouse would be considered to own one-half of jointly held property regardless of which spouse furnished the consideration for the property.

\item[128.] Motro, supra note 26, at 1512, 1518.
\end{footnotes}
transfers between spouses does not accord with the common understanding of most husbands and wives that the property they have accumulated is “ours.” Furthermore, the distinctions drawn by existing law between transfers which qualify for the marital deduction and those which do not qualify have generated drafting complexities, artificial limitations upon dispositions, and considerable litigation.\textsuperscript{129}

The recognition of this economic unit initially extended to individuals with foreign spouses.\textsuperscript{130} In 1988, however, Congress enacted the Technical and Miscellaneous Revenue Act, limiting the deduction amount and availability for transfers to non-citizen spouses to insure subsequent transfers out of the unit would be taxed.\textsuperscript{131}

III. ESTATE TAX MARITAL DEDUCTION: BASIC MECHANICS OF THE 100% MARITAL DEDUCTION

The estate tax marital deduction is provided in section 2056.\textsuperscript{132} Section 2056(a) provides a deduction for 100% of the value of interests in property passing from a decedent to his surviving spouse to the extent the value is included in the decedent’s gross estate and subject to various limitations.\textsuperscript{133} These limitations render the value of an interest passing to a surviving spouse either deductible or nondeductible.\textsuperscript{134} An interest passing to a surviving spouse will be deemed deductible, unless the interest was not included in the decedent’s gross estate; the subject interest was otherwise deductible under either sections 2053 (deduction for administrative expenses) or 2054 (loss deductions), or the interest is a terminable interest, as defined by section 2056(b) and Treasury Regulation 20.2056(b)-1.\textsuperscript{135}

The most difficult of these limitations is the terminable interest rule.\textsuperscript{136} The terminable interest rule provides that “[w]here, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or

\textsuperscript{130} I.R.C. § 2523 (1986).
\textsuperscript{132} I.R.C. § 2056 (2006).
\textsuperscript{133} Id.
\textsuperscript{134} Treas. Reg. § 20.2056(a)-2(a) (1958) (“Property interests which passed from a decedent to his surviving spouse fall within two general categories: (1) Those with respect to which the marital deduction is authorized, and (2) Those with respect to which the marital deduction is not authorized,” referred to as “deductible interests” and on “deductible interests.”).
\textsuperscript{135} Treas. Reg. § 20.2056(a)-2(b) (1958).
contingency to occur, an interest passing to the surviving spouse will termi-
nate or fail, no deduction shall be allowed . . . with respect to such interest,”
if (i) an interest in the property passes for less than adequate consideration
from the decedent to any person other than the surviving spouse and (ii)
such other person or his heirs or assigns may possess such interest after
such failure.137 This rule has been referred to as a “thicket.”138 The purpose
of the terminable interest rule is to assure that an interest in property, the
value of which was granted a deduction in the estate of the first spouse to
die, is given in a manner that makes it includible in the estate of the surviv-

ying spouse.139 The IRS has been admonished not to exalt literal statutory
arguments regarding the terminable interest rule over an inquiry into
whether the interest will be includible in the survivor’s estate.140

Not all terminable interests are nondeductible.141 For example, if a de-
cedent bequeaths a patent to his surviving spouse and a third party as ten-
ants in common, the decedent’s estate will be allowed a deduction for the
value of the patent interest passing to the surviving spouse.142 The interest
in the surviving spouse will terminate upon the expiration of the patent, but
it will not pass to the third party as a result.143 Because the property will not
pass to the third party upon this expiration, it is not a nondeductible termi-
nable interest.144

137. Id.
139. Estate of Smith v. Comm’r, 565 F.2d 455, 459 (7th Cir. 1977).
140. Id.

A property interest passing to decedent’s surviving spouse is deductible .
. . even though it is a terminable interest, and even though an interest
therein passed from the decedent to another person, if it is a terminable
interest only because—
(1) It is conditioned on the spouse’s surviving for a limited period in
the manner described in 20.2056(b)-3;
(2) It is a right to income for life with a general power of appointment,
meeting the requirements set forth in20.2056(b)-5;
(3) It consists of life insurance or annuity payments held by the insurer
with a general power of appointment in the spouse, meeting the require-
ments set forth in 20.2056(b)-6;
(4) It is a qualified terminable interest property, meeting the require-
ments set forth in 20.2056(b)-7; or
(5) It is an interest in a qualified charitable remainder trust in which the
spouse is the only non-charitable beneficiary, meeting the requirements
set forth in20.2056(b)-8.

142. See Treas. Reg. § 20.2056(b)-1(g), ex. 6 (1958).
143. Id.
144. Id.
The following is an example of a nondeductible terminable interest. A deceased spouse devised real property to a trust for the lifetime benefit of his surviving spouse, with the remainder to his heirs. The decedent passed an interest in the property to both his surviving spouse and another person, terminating the trust at the occurrence of the surviving spouse’s death and allowing the remainder person to enjoy and possess the property as a result of the survivor’s death.\textsuperscript{145} Also, upon the surviving spouse’s death, there will be no attributes associated with this trust that would trigger gross estate inclusion.

Section 2056(b), in addition to providing the terminable interest rule, also provides exceptions to the terminable interest rule\textsuperscript{146} For instance, section 2056(b)(5) provides that if the surviving spouse is given a general power of appointment over the property in the trust described above to appoint the property either to herself or her estate, the trust will be a deductible interest.\textsuperscript{147} If such a power is given, the trust will be in the estate of the survivor by virtue of section 2041, which includes property over which a decedent possessed a general power of appointment in his or her gross estate.\textsuperscript{148} In addition to granting the surviving spouse a general power of appointment, to claim a deduction by virtue of 2056(b)(5) the terms of the trust must satisfy the following:

\begin{enumerate}
\item The surviving spouse must be entitled for life to all of the income from the entire interest of a specific portion of the entire interest, or to a specific portion of all the income from the entire interest.
\item The income payable to the surviving spouse must be payable annually or at more frequent intervals.
\item . . .
\item . . .
\item The power in the surviving spouse must be exercisable by her alone and (whether exercisable by will or during life) must be exercisable in all events.
\item The entire interest or the specific portion must not be subject to any power in any other person to appoint any
\end{enumerate}

\textsuperscript{145} See Treas. Reg. § 20.2056(b)-1(g), ex. 1 (1958).
\textsuperscript{146} See Treas. Reg. § 20.2056(b)-1(d) (1958).
\textsuperscript{147} I.R.C. § 2056(b)(5) (2006).
\textsuperscript{148} I.R.C. § 2041 (2006).
Another exception to the terminable interest rule is to elect to designate property as qualified terminable interest property (QTIP).\textsuperscript{150} QTIP is property that passes from the decedent in which the surviving spouse has a qualifying income interest for life\textsuperscript{151} and regarding which an appropriate election is made.\textsuperscript{152} The required election must be made by the executor of the decedent’s estate. If such an election is made, the property interest will be includible in the estate of the surviving spouse pursuant to section 2044.\textsuperscript{153} The above-described trust could be the subject of the marital deduction, therefore, if the decedent’s executor so elects. As a result, the date-of-death value of the trust would be includible in the survivor’s estate pursuant to section 2044 upon her death.\textsuperscript{154}

The QTIP exception to the terminable interest rule was added to the Code in 1981.\textsuperscript{155} It was enacted due to Congress’s concern that the only methods available by which a decedent could avail the marital deduction entailed relinquishing dispositive power to the surviving spouse, perhaps to the detriment to the decedent’s descendants.\textsuperscript{156} Congress stated:

\begin{quote}
[T]he limitations on the nature of interests [currently] qualifying for the marital deduction should be liberalized to permit certain transfers of terminable interests to qualify for the marital deduction. Under [existing] law, the marital deduction is available only with respect to property passing outright to the spouse or in specified forms [providing] the spouse control over the transferred property. Because the
\end{quote}

\textsuperscript{149} Treas. Reg. § 20.2056(b)-5(a) (1958).
\textsuperscript{150} I.R.C. § 2056(b)(7) (2006).
\textsuperscript{151} This is defined in section 2056(b)(7)(B)(i) as an income interest granting the surviving spouse an entitlement to all of the income from the property, payable annually or in more frequent intervals, or as a usufruct interest for life in the property, and over which no person has a power to appoint any of the property to a person other than the spouse (not including a power exercisable only after the surviving spouse has died). I.R.C. § 2056(b)(7)(B)(i) (2006).
\textsuperscript{153} I.R.C. § 2044 (2006). If the surviving spouse attempts to relinquish her qualifying income interest during life, section 2519 increases the value of her gross gifts by the date-of-gift value of the trust interest beyond the value of the income interest. I.R.C. § 2519 (2006); see also I.R.C. § 2519 (triggering gift tax consequences if the surviving spouse divests herself of the income interest inter vivos).
\textsuperscript{154} I.R.C. § 2044 (2006) (providing that the gross estate includes the value of property in which the decedent had a qualifying income interest that had been the subject of a section 2056(b)(7) deduction (QTIP deduction)).
surviving spouse [must] be given control over the property, the decedent [was not certain] that the spouse will subsequently pass the property to his children. Because the maximum marital deduction is limited under current law to one-half of decedent’s adjusted gross estate, a decedent at least could control the [ultimate] disposition of one-half of his estate and still maximize current tax benefits. However, unless certain interests which do not grant the spouse total control are eligible for the unlimited marital deduction, a decedent would be forced to choose between surrendering control of his entire estate to avoid imposition of the estate tax at his death or reducing his tax benefits at his death to insure inheritance by the children. The committee believes that the tax laws should be neutral and that tax consequences should not control an individual’s disposition of property.157

As the forgoing makes clear, a host of complex rules and regulations must be considered when planning to obtain an estate tax marital deduction. If a transfer runs afoul of the terminable interest rule or fails to satisfy one of the exceptions to that rule, an estate may lose the benefit of the deduction. If the rules and regulations are satisfied, however, married taxpayers are given beneficial estate planning options that single taxpayers are not.158

IV. ESTATE TAX MARRITAL DEDUCTION: GENERAL ESTATE PLANNING CONSIDERATIONS

A discussion of the use of the marital deduction provisions in estate planning requires a review of the unified credit provisions of the taxes.159 Section 2010 provides a credit of the “applicable credit amount” against the estate tax.160 The applicable credit amount is equal to the amount of the tentative tax that would be determined on the “applicable exclusion amount,” currently $5,000,000.161 Section 2505 provides a credit against the gift tax, also currently based on the applicable exclusion amount of $5,000,000.162 Effectively, the two credits work within the framework of the transfer tax system to allow a taxpayer to transfer a cumulative total of

157. Id.
property valued at $5,000,000 (currently)—in life or at death—free of the transfer tax.163 Once the unified credit amount, also known as the exemption equivalent or exclusion, is exhausted, any taxable transfer of property thereafter generates a transfer tax liability.164

The credit was introduced into the estate and gift taxes in 1976, replacing exemptions that had previously existed in both the estate and gift taxes, as part of an effort to unify the two taxes.165 From 1977 to 2004, the credit was the same for both the estate and gift tax.166 Initially, in 1977, the credit allowed an exemption equivalent of $120,667. The exemption equivalent rose significantly over the years until 2001 when the amount was set at $1,000,000 for both the gift and estate taxes.167

The Economic Growth and Tax Relief and Reconciliation Act (EGTRRA) set in motion a separation of the estate tax and the gift tax, eventually leading to the temporary repeal of the estate tax in 2010.168 As part of this separation, EGTRRA uncoupled the unified credit amounts of the estate tax and gift tax.169 The EGTRRA set the gift tax unified credit at a constant $1,000,000.170 The estate tax amount was set at $1,000,000 for 2002-2003, $1,500,000 for 2004-2005, $2,000,000 for 2006-2008, and $3,500,000 for 2009.171 The increase in the estate tax unified credit from 2002-2009 was based on the desire to incentivize taxpayer saving, capital formation, and entrepreneurial activity.172

Pursuant to the EGTRRA, the estate tax was repealed in 2010, but for obscure parliamentary reasons, the repeal was only for one year, and the estate tax was to be revived at 2001 levels, effective January 1, 2011.173 After the repeal was triggered in 2010, Congress debated various approach-
es to preventing a reimposition of the tax at 2001 levels, ranging from outright repeal to a return to the 2009 levels.\textsuperscript{174} Congress eventually passed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (TRA 2010) which reinstated the estate tax for 2011 and 2012 with a $5,000,000 unified credit for both estate and gift taxes and put off to 2013 the possibility of a reversion to the 2001 estate tax levels.\textsuperscript{175} The TRA 2010 also introduced the concept of portability of the unified credit amount between spouses.\textsuperscript{176} In general, a taxpayer’s unified credit amount can be availed by only the taxpayer.\textsuperscript{177} If a taxpayer dies without consuming his entire unified credit, the amount evaporates.\textsuperscript{178} For 2011 and 2012, a surviving spouse of a taxpayer may file an estate tax return upon the death of their spouse, claiming the spouse’s remaining unified credit.\textsuperscript{179} In essence, and assuming away inflation adjustments, a surviving spouse can combine her unified credit with that of her most recent spouse to pass away, effectively shielding $10,000,000 from the estate tax at her death.\textsuperscript{180} Though the portability provisions were initially set to expire on January 1, 2013, they were made permanent by the American Taxpayer Relief Act of 2012.\textsuperscript{181}

Disregarding portability, a standard estate plan for married taxpayers seeks to utilize a decedent’s unified credit amount and to only employ the marital deduction to the extent the value of a decedent’s gross estate exceeds the available unified credit.\textsuperscript{182} For example, assuming the first spouse to die’s gross estate is $10,000,000, that the decedent had made no taxable gifts, and that no other deductions or credits are available, the estate of the first spouse to die might be split pursuant to a formula clause,\textsuperscript{183} as follows:

\begin{itemize}
  \item \textsuperscript{175} Id.
  \item \textsuperscript{176} Id.
  \item \textsuperscript{178} Id.
  \item \textsuperscript{179} Id.
  \item \textsuperscript{180} Moy, supra note 177, at 851.
  \item \textsuperscript{183} For a discussion of formula clauses, see Detzel, supra note 16, ¶ 1600.
\end{itemize}
$5,000,000 to a credit shelter trust, free of estate tax liability due to the unified credit; the other $5,000,000 would fund a marital deduction trust, free from estate tax liability in the estate of the first spouse to die due to the marital deduction. The first spouse to die has passed $10,000,000, therefore, transfer tax free. If we further assume the surviving spouse in this scenario has never had any separate assets of her own, only the $5,000,000 marital deduction trust (assuming no inflation) will be in her gross estate upon her death. The $5,000,000 in this trust will pass upon her death, also free of estate tax due to the surviving spouse’s unified credit. The credit shelter trust will not be included in the surviving spouse’s estate upon her death, as the estate plan will not give her any interests in the trust to trigger such inclusion. In this scenario, a total of $10,000,000 has passed unburdened by the transfer taxes.

If we assume away the fact of marriage in this scenario, at least $5,000,000, the amount passed to the surviving spouse in a marital deduction trust, would have been subjected to the transfer tax upon the death of the first spouse to die. Even if an unmarried, but long-term, couple employed a similar plan, they would be denied the marital deduction and the attendant tax savings.\(^{184}\)

Estate planning pursuant to the 50% marital deduction also required formula planning.\(^{185}\) Estate plans would call for a division of the estate of the first spouse to die into a share that was eligible for the marital deduction and a second share for the property not so eligible.\(^{186}\) The estate planning provisions related to both the 50% and 100% marital deduction added complexity to estate planning documents.

There are numerous other estate planning options available to married individuals that are not provided to unmarried taxpayers.\(^{187}\) For instance, married individuals may use the gift tax marital deduction to equalize the value of the estates in order to insure the utilization of both spouse’s unified credit amount.\(^{188}\) For example, if one spouse has property with a total value of $10,000,000 and the other spouse has no property, the wealthy spouse may make a transfer of $5,000,000 to the poor spouse, free of gift taxation due to the gift tax marital deduction. Assuming no appreciation occurs and the unified credit amount remains at $5,000,000, upon the death of each spouse no estate tax will be due as a result of the application of each of their unified credit amounts. Even assuming the unified credit amount goes down and a more progressive rate table is established, such equalization will al-

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184. See supra notes 52-59 and accompanying text.
185. Crawford, supra note 19.
186. Id.
188. See, e.g., PRICE & DONALDSON, supra note 77, § 5.9.
low both spouses to take advantage to the fullest extent possible of the lowest portions of the rate table.

The possibility of portability may negate the need for estate equalization planning and for the trust arrangement described above. Under portability, the surviving spouse could receive all of the assets pursuant to the marital deduction and then shield all of the assets upon her death from the estate tax via the combination of the two unified credits. Given the long-term uncertainty regarding the provision of portability and other concerns, however, the basic plan presented remains a viable approach to estate planning. If portability persists in the law, it is offered to only married taxpayers, justified by the same economic unit presumption as the estate tax marital deduction.

The ability to split gifts pursuant to section 2513 also provides married individuals with an estate planning option denied to unmarried taxpayers. Not all non-deductible transfers of property by gift are deemed taxable gifts. Section 2503(b), for example, provides an exclusion from the definition of taxable gift of a transfer at or below a specified amount, currently $13,000, if the transfer is of a present interest. Typically, if a taxpayer transfers a present interest of $26,000, $13,000 of the transfer is excluded from the determination of the taxable gift, leaving a taxable gift of $13,000. If a married taxpayer makes such a transfer and his spouse elects to split the gift with him, each spouse will be treated as if they transferred $13,000, allowing each spouse to exclude their share of the gift. As a result, $26,000 has been transferred by someone that will never be the subject of a taxable gift.

189. Moy, supra note 177, at 851-54.
190. Id.
191. Id.
192. Id.
194. See I.R.C. § 2503 (2006) (providing exclusion from the gift tax of certain types of gifts); I.R.C. § 2502 (2006) (providing for the calculation of the annual gift tax liability by multiplying the taxable gifts of an individual by the rate table provided in section 2502).
196. A present interest is an interest over which the recipient has a current economic benefit. See United States v. Pelzer, 312 U.S. 399 (1941). The committee report explained that the exclusion should be denied unless the donees of the transfer were ascertainable at the time of the transfer and in the case of a transfer of a future interest due to the difficulties “in many instances, of determining the number of eventual donees and the values of their respective gifts.” H.R. REP. NO. 72-708, at 29 (1932).
197. Price & Donaldson, supra note 77, § 5.9. The annual exclusion was added to the gift tax code in 1932 “to obviate the necessity of keeping an account of and reporting numerous small gifts” made during the course of a year. H.R. REP. NO. 72-708, at 29 (1932). The exclusion was “to fix the amount sufficient[ly] . . . to cover in most cases wedding and
V. MARRIAGE AS THE PROXY FOR ECONOMIC UNIT

Marriage is the only proxy for an economic unit for purposes of the estate tax marital deduction. In order to obtain the deduction, in addition to the statutory requirements discussed in Section 3, the estate will be required to establish the testator was married at the time of his death and that the property being made the subject of the deduction is passing to the surviving spouse. Once the fact of marriage is established, however, the IRS will not inquire into whether the married couple was functioning as an economic unit. This is a good thing, as there is no guidance suggesting the contours of such an inquiry.

Marital status questions turn on state law, typically, though the federal Defense of Marriage Act currently limits the application of tax benefits, such as the marital deduction, to hetero couples. As a general matter, if the taxpayer’s marriage is honored for state law purposes, it will be honored for estate tax deduction purposes. Even if a taxpayer is legally separated from his spouse or functioning under a judicial order short of a state law issued divorce decree at the time of his death, the status of his spouse for purposes of a marital deduction is unaffected.

Christmas gifts and occasional gifts of relatively small amounts.” Id. Although established to reduce administrative and compliance burdens associated with such transfers, estate planners eventually hijacked the annual exclusion and use it as an estate planning device. Kelly Moore, Proposal for Estate Tax Exclusion Provisions, 35 OHIO N. U. L. REV. 37, 44 (2009). Such use is consistent with the view of some that the annual exclusion is designed as an incentive for making lifetime gifts. Id.; H.R. REP. NO. 94-1380 (1976), reprinted in 1976 U.S.C.C.A.N. 3356.

201. Indeed, the court will not inquire even in the face of an obvious breakdown of the economic unit. See, e.g., Rev. Rul. 56-368, 1956-2 C.B. 1027 (allowing a marital deduction despite legal separation).
202. See Crawford, supra note 19, at 792 & n.196; Motro, supra note 26, at 1523. (In discussing an income tax proposal, “statistical evidence of marital sharing is subject to much dispute. Data on income pooling within couples is scarce, is likely to be unreliable, and has been interpreted as supporting as well as debunking the marital unity paradigm.”).
205. Id. There have been recent attempts to repeal DOMA, but none came to a vote in Congress. The Supreme Court recently granted cert in U.S. v. Windsor, 699 F.3d 169 (2d Cir. 2012), cert. granted, 133 S. Ct. 786 (2012).
For instance, in *Estate of Steffke v. Commissioner*, the court held that a decedent’s bequest to the woman he had most recently married before his death did not qualify for the marital deduction because his divorce from his prior wife was invalid.\(^\text{208}\) The divorce had not been challenged whilst the decedent was alive, but the supreme court of his state determined that the divorce, which had been obtained in Mexico, was invalid after his death, disqualifying his supposed widow from inheriting under state law.\(^\text{209}\) The tax court determined this was dispositive for estate tax purposes as well.\(^\text{210}\) Similarly, in *Estate of Goldwater v. Commissioner*,\(^\text{211}\) the court determined that a New York court’s refusal to honor a divorce granted in Mexico rendered the no-longer-divorced spouse the surviving spouse of the decedent for estate tax purposes.\(^\text{212}\)

Once the fact of marriage is established, the presumption that the taxpayer and his spouse are functioning as an economic unit is accepted.\(^\text{213}\) The basis for the economic unit presumption is found in various general statements, such as “husband and wife should be treated as one economic unit for purposes of the estate and gift taxes, as they generally are for income tax purposes.”\(^\text{214}\) If the IRS were to inquire into the actual economic relationship of a married taxpayer, there is no baseline provided of what level of economic relationship is required. A policy determination to allow cohabiting couples, in general, to utilize this benefit if they prove to be functioning as economic units would beg the broader question: what level of economic sharing and related activity is required to prove such status? The focus of this Article is not on this broader question. Instead, this Article asks the discrete question of whether the presumption and related benefit of the estate tax marital deduction should be rebutted and/or disallowed if a married taxpayer’s economic relationship with his spouse is defined by a prenuptial agreement. The absence of a baseline makes such a discussion

\(^{208}\) *Estate of Steffke v. Comm’r*, 64 T.C. 530, 530 (1975), *aff’d*, 538 F.2d 733 (7th Cir. 1976).

\(^{209}\) *Id.*

\(^{210}\) *Id.*

\(^{211}\) *Estate of Spalding v. Comm’r*, 537 F.2d 666 (2d Cir. 1976).

\(^{212}\) *Estate of Goldwater v. Comm’r*, 64 T.C. 540 (1975), *aff’d*, 539 F.2d 878 (2d Cir. 1976) (estate allowed a deduction for the value of the forced share received by a no-longer-divorced spouse).

\(^{213}\) Motro, *supra* note 26, at 1523.

\(^{214}\) S. REP. NO. 97-144, at 127 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 228; *see also*, H.R. REP. NO. 97-201, at 159 (1981) (reflecting fear that inadequate tax planning could result in spousal property being subjected to tax more than once in a spousal generation, the determination that spouses should be able to transfer property between themselves without imposition of the tax, and that the 100% deduction would avoid administrative difficulties of accounting for jointly held property of spouses).
difficult. For purposes of discussion, however, the state law provided protections against disinheriting spouses will be used as the baseline.

Marriage impacts the legal rights of each spouse by creating an obligation of support and placing some restrictions on the right to transfer property during life and at death.\(^\text{215}\) Whether a jurisdiction is a community property state or a separate property state, state law provides protections against disinheriting a surviving spouse.\(^\text{216}\) In community property jurisdictions, generally, property earned during the marriage becomes the community property of each spouse.\(^\text{217}\) For example, if a deceased individual had $1,000,000 of community property titled in his name at death, $500,000 of this property passed to his surviving spouse by operation of law.\(^\text{218}\) In this way, the surviving spouse is protected from disinheriting and impoverishment.\(^\text{219}\)

In common law states, spouses are provided an elective share to protect them from disinheriting and impoverishment.\(^\text{220}\) The spouse is given the option of either taking what the decedent provided for in his will or a statutorily defined share of the decedent’s estate.\(^\text{221}\) The elective share varies from state to state, and the nature of the property interest allowed to the surviving spouse may differ as well.\(^\text{222}\) There are also issues regarding whether the statutory share applies to property passing outside of probate via a will substitute or perhaps transfers that had been made in fraud of marital rights.\(^\text{223}\) Whatever the contours of a given state’s elective share statute and related case decisions, however, after marriage the property of each spouse is potentially subjected to an elective share claim upon his or her death.\(^\text{224}\)

Both the community property regime and an elective share regime are premised on the fact that, for state law purposes, husband and wife form a unit, both equally contributing to the economy of the unit.\(^\text{225}\) State law al-

\(^{\text{215}}\) Motro, supra note 26, at 1517.


\(^{\text{217}}\) See, William A. Reppy, Jr & Cynthia A. Samuel, Community Property in the United States (2d ed. 1982).

\(^{\text{218}}\) Id.

\(^{\text{219}}\) Id.


\(^{\text{221}}\) Id.

\(^{\text{222}}\) Id.


allows couples to deviate, however, from their property regimes by entering into a prenuptial agreement.226 As will be discussed in Part VI, not all prenuptial agreements contain the same terms. For purposes of discussion, a prenuptial agreement that alleviates the taxpayer from the state provided protections against impoverishing the spouse will be considered a possible instance where the economic unit presumption is rebutted.227

VI. Prenuptial Agreements

Marriage impacts the legal rights of each spouse by creating an obligation of support and placing some restrictions on the right to transfer property during life and at death.228 These obligations and restrictions may be abrogated, however, by entering a valid prenuptial agreement.229

Prenuptial agreements are hardly a new legal device as they date back to the sixteenth century.230 Early prenuptial agreements were notably different from those often seen today in that their primary focus was on what would happen to the couple’s assets at death, not upon divorce.231 Furthermore, they were drawn up not to protect the assets of the husband, but rather to ensure the return of the wife’s assets to her family should she die without issue.232

At common law, prenuptial agreements were limited to governing the distribution of property upon the death of a spouse and did not apply in the case of a divorce.233 This was due to the commonly held view that allowing prenuptial agreements to include provisions dealing with the disposition of assets upon divorce was against public policy as it would undermine the stability of the marriage.234 American courts continued to decline to enforce prenuptial agreements contemplating divorce in deference to this policy view up through the 1960s.235 The past forty years have seen significant change in how American courts have addressed the validity of prenuptial

226. Sherman, supra note 64, at 365-66.
227. The gift tax marital deduction could also be the subject of such a discussion, perhaps focusing instead on any deviation from the state-provided rights and burdens upon dissolution of the marriage.
228. Motro, supra note 26, at 1517.
229. Id.
230. Sherman, supra note 64, at 365-66.
231. Id. at 365.
232. Id. at 366.
234. Difonzo & Stern, supra note 233, at 33-34.
235. Sherman, supra note 64, at 375.
Court enforcement of prenuptial agreements containing provisions that address divorce stems from a changing view of marriage from that of a sacred union to a form of secular legal relationship.\textsuperscript{237} This is evidenced by the fact that the first cases to find prenuptial agreements contemplating divorce to be enforceable coincided with the advent of no-fault divorce.\textsuperscript{238}

The rate at which couples execute prenuptial agreements is currently on the rise. Depending on which study one examines, it has either increased to 5% in the mid-1990s from 1% in the mid-1970s or to 3% in 2010 from 1% in 2002.\textsuperscript{239} The increase in the popularity of prenuptial agreements is partially due to a shift in judicial preferences when it comes to divorce settlements toward favoring property division rather than granting alimony.\textsuperscript{240} Moreover, high profile divorce cases illustrating the savings that could be had through the use of a premarital agreement are also a siren song for those possessing significant wealth.\textsuperscript{241}

\begin{itemize}
\item \textsuperscript{236} Id. at 375-83.
\item \textsuperscript{237} Id. at 392.
\item \textsuperscript{238} See, e.g, Posner v. Posner, 233 So. 2d. 381 (Fla. 1970), rev’d on other grounds, 257 So. 2d 530 (Fla. 1972); id. at 380-81. Public acceptance of the institution of divorce and increased rates thereof have led to a change in how the public perceives prenuptial agreements providing for the disposition of property upon divorce in that they are now viewed as legitimate contracts. Difonzo & Stern, supra note 233, at 35. Although most courts continue to view prenuptial agreements as distinct from ordinary contracts, others take a more extreme position and treat prenuptial agreements just like any other contract. Brian Bix, Bargaining in the Shadow of Love: The Enforcement of Premarital Agreements and How We Think About Marriage, 40 WM. & MARY L. REV. 145, 162-182 (1998); Sherman, supra note 64, at 381-82. The 1983 Uniform Premarital Agreement Act (UPAA) provides an enforceable structure for premarital agreements and more certainty than the case-by-case approach many state courts had been using in lieu of a controlling statute on the enforceability of prenuptial agreements. Dennis I. Belcher, How to Tie a Tight Knot with a Marital Agreement, 35 INST. ON EST. PLAN. 4-3, 401.1 (2001). Thus far, the UPAA has been adopted by twenty-six states and the District of Columbia. UNIF. PREMARITAL AGREEMENT ACT (1983), Table of Jurisdictions Wherein Act Has Been Adopted (Supp. 2009).
\item \textsuperscript{239} Laura Petrecca, Unromantic? Maybe, but Prenups Make Sense: Nearly One-Third of Those Surveyed Would Ask for One, USA TODAY, Mar. 11, 2010, at 6A; Sherman, supra note 64, at 372.
\item \textsuperscript{240} Sherman, supra note 64, at 374.
\item \textsuperscript{241} Bix, supra note 238, at 146; Sherman, supra note 64, at 375. In addition to those wedding for the first time, prenuptial agreements are also popular among those embarking upon their second or a subsequent marriage. Sherman, supra note 64, at 373. In fact, individuals age 40-60 account for 65% of those who request their prospective spouses to sign prenuptial agreements. Misty Harris, Couples Seek Made-to-Order Unions: Everything from Petcare to Housekeeping Provisions Requested in Prenups, CANWEST NEWS SERVICE (Oct. 12, 2006), http://www.aaml.org/sites/default/files/couples%20seek%20made%20to%20order.pdf. This is due, at least in part, to the fact that older individuals usually have accumulated more wealth than those marrying for the first time and the benefits in terms of familial harmony that can be had when children from a prior relationship are assured that they will still take
In addition to the tax concerns inherent in the execution of a prenuptial agreement, prenuptial agreements contain provisions detailing the tax arrangement of the parties during the course of the marriage. For instance, prenuptial agreements often provide for how income taxes are to be filed. This can be addressed in a simple fashion by a provision agreeing to cooperate in filing joint tax returns or by a considerably more complex set of provisions. Couples contemplating filing jointly may even dictate the allocation of any refund received. In addition, the parties may agree to indemnify each other if an audit determines that they owe additional funds on their joint return. Irrespective of filing status, the parties may choose from their parent’s estate. Andre Katz & Amanda Clayman, *When Your Elderly Clients Marry: Prenuptial Agreements and Other Considerations*, 16 J. AM. ACAD. MATRIMONIAL LAW 445, 451 (2000); Sherman, supra note 64, at 373.

242. Unless a transfer in contemplation of marriage is actually made at the time when the prenuptial agreement is signed, there will be no tax consequences due to the act of signing the prenuptial agreement. Linda J. Ravdin & Marcia C. Fidis, *Tax Aspects of Marital Agreements*, PDPA MD-CLE 6-1, § 6.16 (2009). Couples executing prenuptial agreements should exercise care though when it comes to the timing of transfers envisioned by the agreement because their transfers can determine whether or not the transfers qualify for the marital deduction. Belcher, supra note 238, at 406.3. This point is illustrated by *Farid-Es-Sultaneh v. Commissioner* which states that releasing one’s marital rights does not count as consideration for transfers made in anticipation of marriage and that such transfers will therefore be subject to the gift tax. *Farid-Es-Sultaneh v. Comm’r*, 160 F.2d 812, 816 (2d Cir. 1947); Rev. Rul. 69-347, 1969-1 C.B. 227. However, it is possible to condition transfers on the marriage actually occurring, which provides an avenue by which to skirt the timing issue and qualify for the marital deduction. Belcher, supra note 238, at 406.3.


244. GARY N. SKOLOFF, RICHARD H. SINGER, JR. & RONALD L. BROWN, DRAFTING PRENUPTIAL AGREEMENTS, IV-71 (Supp. 1999). A prenuptial agreement may require joint filing. Katz & Clayman, supra note 241, at 460; SKOLOFF, supra note 244, at IV-70. Or, the parties may agree in the prenuptial agreement to give one of the spouses the responsibility for determining whether they will file jointly or separately. SKOLOFF, supra note 244, at IV-97. A prenuptial agreement can even prohibit joint filing if the parties separate without divorcing. Id. at IV-93. The prenuptial agreement may require one spouse to shoulder the entire income tax burden. Id. at IV-85. Alternatively, a prenuptial agreement may require each spouse to pay the portion of income tax liability which would be owed on their earnings had the couple filed separately should they elect to file jointly. Cenovic v. Cenovic, No. A-09-238, 2010 WL 4237928, *10 (Neb. Ct. App. Jan. 12, 2010). Additionally, if the parties are combining households, they may include provisions related to the capital gains taxes owed upon the sale of the home belonging to the spouse who moves into the other’s home. SKOLOFF, supra note 244, at VIII-69. For example, the high-earning spouse may agree to pay the entire amount due on their joint income tax return, except for taxes stemming from the sale of the home of the less wealthy spouse. Id. at VIII-69.

245. Cenovic, 2010 WL 4237928, at *10; SKOLOFF, supra note 244, at IV-85 to -86.

246. SKOLOFF, supra note 244, at IV-86 to -87. While it is often advantageous to file jointly, the parties may, for one reason or another, agree to a provision in their prenuptial agreement stipulating that they must file their tax returns separately. Id. at IV-95. When filing separately, both spouses must either elect to itemize or they must both file jointly. As
to include a provision in their prenuptial agreement stipulating that income taxes traceable to items of separate property shall be paid out of separate property assets and that which is traceable to marital property be paid out of marital property assets.\textsuperscript{247}

Even though an annual election has to be made on one’s gift tax return, a couple may include a provision in their prenuptial agreement consenting in advance to splitting gifts to third parties.\textsuperscript{248} In addition to establishing a gift-splitting regime, a prenuptial agreement may also contain a provision compensating the less wealthy spouse for the use of his or her unified credit if issues later arise relating to the valuation of gifts, which would push the value of the gifts beyond the annual exclusion amount.\textsuperscript{249}

Prenuptial agreements provide an avenue to protect an individual’s probate estate from their surviving spouse’s elective share claim.\textsuperscript{250} As such, prospective spouses may choose to include a provision in their prenuptial agreement mutually waiving their elective share claims.\textsuperscript{251} Limiting the surviving spouse’s access to his or her elective share can also serve to assure children from a prior relationship that the motivation of the prospective spouse in entering the marriage is not their parent’s wealth, thereby enhancing familial harmony.\textsuperscript{252} Furthermore, “a ‘marriage condition’ is included to provide that the death provisions are superseded by the divorce provisions contained in the marital agreement in the event that the parties are not living together at the death to one spouse or if divorce proceedings had been already commenced by either party.”\textsuperscript{253}

VII. REBUTTING THE ECONOMIC UNIT?

The use of marriage as a proxy for economic unit status offers efficiencies to the tax system.\textsuperscript{254} As it is only a proxy, its use triggers the possibility that a tax benefit may be provided to taxpayers who do not satisfy the underlying requirement of functioning as an economic unit. It is accepted

\textsuperscript{247} Coleman, supra note 243, at 165; Mary H. Schmidt & Christopher H. Suh, \textit{Marital Agreements, in 2 A Practical Guide to Estate Planning in Massachusetts} § 12, § 12.6.6 (2009).

\textsuperscript{248} Coleman, supra note 243, at 200.

\textsuperscript{249} Belcher, supra note 238, at 400.2.

\textsuperscript{250} Katz & Clayman, supra note 241, at 453.

\textsuperscript{251} Belcher, supra note 238, at 400.2; Katz & Clayman, supra note 241, at 451-52.

\textsuperscript{252} Schmidt & Suh, supra note 248, § 12.6.6.

\textsuperscript{253} See, e.g., supra notes 43-44.
for this Article that, generally, the efficiencies justify the toleration of such possibility.

The economic unit presumption is based on an underlying belief that married individuals share the economic burdens associated with the marriage.\textsuperscript{255} For discussion purposes, this Article explores this presumption based on the restriction the act of marriage places upon a decedent’s testamentary freedom, either as a result of community property laws or the elective share. As a result of the presumption, married individuals are provided the benefit of a 100% estate tax marital deduction that is not provided to single individuals.\textsuperscript{256} Based on the premise that marriage is a set package of rights and responsibilities, it is fair to assert that if one accepts the burdens, they are entitled to the benefits.\textsuperscript{257} If, however, they deny the burdens, by enacting a prenuptial agreement, arguably they are not entitled to the benefits. This is an old concept; the idea that one who refuses to sustain a burden ought not to derive its benefit dates to the Justinian code.\textsuperscript{258} From this perspective, the benefit of the estate tax marital deduction should be denied if a prenuptial agreement is executed limiting the burdens associated with marriage. As such, burdening the wealthier spouse by placing a cost on ending a marriage (i.e., denying marriage-related tax benefits) ought to be one of the burdens of this benefits and burdens package.\textsuperscript{259} As a counter-argument, however, it has been posited that marriage is more than economics, more than a legal fiction: it is an intimate and reciprocal relationship.\textsuperscript{260}

The mere possibility that a prenuptial agreement could exist has been offered as one of the reasons for jettisoning the economic unit presumption for bestowing tax benefits.\textsuperscript{261} When a prenuptial agreement does exist, this argument is made stronger. As the above discussion of possible prenuptial agreement terms indicates, parties may abrogate whatever level of property sharing and burdening that is attendant to a marriage under state law, in the first place, while at the same time divvying up the tax benefit spoils.\textsuperscript{262} Should these benefits be allowed when the agreement arguably removes their underlying justification?

Allowing married individuals to obtain the benefit of a marital deduction without exposing their estates to possible control by their surviving spouses runs counter to the general purpose of the estate tax of breaking up accumulations of wealth. It is true the QTIP provisions allow a decedent to

\begin{itemize}
\item \textsuperscript{255} Id. at 384-86.
\item \textsuperscript{256} Id. at 389.
\item \textsuperscript{257} Id. at 388.
\item \textsuperscript{258} See supra Parts III, IV, VI.
\end{itemize}
avail the estate tax marital deduction without providing the surviving spouse privately with such control, but the underlying state laws persistently provide for such control, unless contracted away in a prenuptial agreement.

To the extent the marital deduction provisions were motivated by the desire to simplify the gross estate issues involving property held in the entirety or in right of survivorship between just the spouses, this Article posits such issues will be the province of the prenuptial agreement. Even if the prenuptial agreement does not provide the answers for these types of issues, section 2040(b) will. Although section 2040(b) is based on the same economic unit presumption, if such property is held by the spouses outside of the terms of the prenuptial agreement, this Article’s acceptance of marriage as a proxy, generally, suggests there is no need to rebut the presumption for such uncovered property.

Using the state-provided rules against disinheriting a spouse as the baseline for the existence of an economic unit, a prenuptial agreement deviating from this baseline rebuts the presumption. If rebutted, the 100% marital deduction seems inappropriate. Accepting that other baselines are possible, once established, deviation from any baseline rebuts the justification for the presumption, arguably rendering the 100% deduction inappropriate.

If the 100% marital deduction is disallowed in the face of certain prenuptial agreements, what is the result for the taxpayer? The 50% marital deduction was not created based on the economic unit presumption. Instead, it was enacted in response to inequities between married taxpayers in community property states and those in common law states. Perhaps a reenactment of some version of the 50% deduction would be necessary for those who are denied the 100% deduction. As discussed earlier, the current marital deduction provisions are complex. The concurrent existence of a 50% marital deduction would add further complexity.

Use of marriage as a proxy for bestowing tax benefits is a simple approach. The lack of a baseline, in the first place, and the reliance on a proxy allow for a less complex imposition of the estate tax than would a regime requiring a detailed inquiry into whether the married couple is acting as an economic unit, however defined. Should this simplicity be abandoned in some or all situations involving prenuptial agreements?

Not all prenuptial agreements contain the same terms. Should the estate tax marital deduction be disallowed based on the mere existence of a

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264. See supra text accompanying notes 234-67.
265. See supra notes 104-06 and accompanying text.
266. See supra notes 104-06 and accompanying text.
267. See, e.g., supra notes 248-53 and accompanying text.
prenuptial agreement without reviewing the terms of the agreement? In
addition, a prenuptial agreement acts as a floor regarding what a spouse
must leave to the survivor. Should the IRS be required to compare the
actual terms of the agreement with what the deceased individual finally
provided for his surviving spouse? Requiring the IRS to make any of these
types of inquiries as a result of limiting the marital deduction when a pre-
nuptial agreement is involved would most likely be administratively ineffi-
cient. Given that administrative efficiency concerns may provide the
strongest argument against requiring the IRS to determine if a married cou-
ple is actually functioning as an economic unit, requiring such inquiries as a
result of a possible denial of the deduction seems equally objectionable.

If a detailed inquiry into the precise terms of a prenuptial agreement or
actual property distribution is not to be made, an alternative would be to
deny the deduction based on the mere existence of the prenuptial agree-
ment, perhaps based on the presumption that such an agreement tends to
deviate too much from the burdens and obligations otherwise provided by
state law. Just as the grant of benefits based on the economic unit presump-
tion may tend to grant such benefits too broadly, a denial of this sort may
deny them too broadly. Whereas it may be appropriate to bestow a tax ben-
efit too broadly as a result of a presumption, it seems too harsh to deny said
benefits too broadly based on a counter presumption.

Another alternative would be to establish a hybrid approach between
requiring a case-by-case analysis of each situation involving a prenuptial
agreement and having an irrebuttable presumption that the existence of a
prenuptial agreement precludes treating the married couples as economic
units. Perhaps, a rebuttable presumption could be employed. This Article
posits this would trigger the same types of factual inquiries the current ap-
proach evinces intent to avoid.

It is true the surviving spouse will obtain the bargained-for benefits
upon the death of the first spouse. If the benefits are presented to the sur-
viving spouse in the appropriate form, the current marital deduction provi-
sions shield the benefit from estate taxation upon the death of the first
spouse. Why not deem the married couple an economic unit to the extent
of such a benefit, no matter its scope? This would result in an allowance of
the deduction, as is currently the case. This seems appropriate, given the
artificial construct of relying on spousal inheritance rights to determine
economic unit status, but ignores the broader policy justification of bestow-
ing the deduction on married couples because they are functioning as eco-
nomic units. Most prenuptial agreements deal with divorce and other rights

268. See supra notes 257-58.
269. See supra notes 257-58.
270. See supra note 4.
beyond inheritance rights, which, though not discussed in this Article, would necessitate a broader set of inquiries to determine a baseline of economic unit status.\(^{271}\)

The canons of just taxation include “[t]he [c]anon of [s]implicity, which dictates the tax system should be simple, plain and intelligible to the common taxpayer. The tax should not be complicated. It should be simple to understand as to how it is to be calculated and how much is to be paid.”\(^{272}\) Many of the arguments to repeal the transfer tax focused on the complexity of the tax, compliance difficulties, and other inefficiencies caused by the tax.\(^{273}\) The use of marriage as a proxy for the economic unit, forestalling the need to conduct any inquiries into the actual economic relationship between the married couple, avoids complexity and limits the compliance concerns. The state-imposed burdens on a married individual’s property are not overly burdensome, in the first place, and the use of marriage as a proxy evinces intent to avoid such inquiries. If such inquiries were to be conducted in cases involving prenuptial agreements, even if justified by the underlying policy arguments, the introduction of additional complexity and related compliance pressures would be unacceptable insults to the canon of simplicity and efforts to reduce compliance burdens associated with the tax code.

It is true that, given the current unified credit amount of $5,000,000, any attendant complexities would be foisted upon the small percentage of taxpayers who have wealth levels sufficient to trigger a transfer tax liability.\(^{274}\) For the vast majority of taxpayers, whether they are married pursuant to a prenuptial agreement or not, a transfer tax liability is not currently on the horizon.\(^{275}\) However, given the uncertainty surrounding the amount of the unified credit in the future and the absence of a well-defined baseline

\(^{271}\) See Jeffrey A. Baskies, *A Practical Guide to Preparing and Using Premarital Agreements*, 27 EST. PLAN. 347 (2000); see, e.g., Weisfeld-Ladd v. Estate of Ladd, 920 So. 2d 1148, 1149 (Fla. Dist. Ct. App. 2006) (finding language in a prenuptial agreement that a wife agreed to “not claim or acquire any interest in any [of her husband’s] property during the marriage or in the event of dissolution of the marriage” was a waiver of both dissolution rights and elective share rights).


\(^{274}\) Steve Wamhoff, *State-by-State Estate Tax Figures: Number of Deaths Resulting in Estate Tax Liability Continues to Drop*, CITIZENS FOR TAX JUSTICE (OCT. 20, 2010), http://www.ctj.org/pdf/estatetax2010.pdf (state-by-state estate tax figures show that the President’s plan is too generous to millionaires, indicating that in 2009, only 0.6% of deaths triggered an estate tax liability when the unified credit amount was 3,500,000).

\(^{275}\) Id.
with which to measure the economic unit presumption, the efficiencies offered by the status quo are stronger than any benefit to be gained by more precisely matching the award of the benefits of the 100% marital deduction with couples actually satisfying the underlying presumption. Even if a baseline could be crafted, the underlying inquiries would be too great to justify the abandonment of marriage as a proxy.

VIII. CONCLUSION

Using the state law protections against spousal disinheretance as the baseline for determining the existence of an economic unit, it is defensible to consider a prenuptial agreement deviating from the baseline as rebutting the existence of the economic unit. So rebutted, the attendant estate tax marital deduction seems unwarranted. Concerns over estate tax issues involving jointly held spousal property also seem minimized when the affairs of the parties are governed by a prenuptial agreement. Allowing a wealthy spouse via contract to maintain control over his wealth, without exposing it to the possibility his spouse may elect or otherwise obtain the property, seems counter to the estate tax goal of breaking up large concentrations of wealth. There would be efficiency concerns associated with such an inquiry, however, and, admittedly, other baseline measurements would need to be considered.

If we accept the economic unit justification for the provision of a 100% marital deduction in the estate tax code, generally, the current approach of not attempting to account for the existence of prenuptial agreements remains the most efficient approach. It is true that prenuptial agreements tend to move away from state-imposed obligations toward customized requirements, theoretically undercutting the basis for the economic unit justification. All prenuptial agreements are not created equally, however, and to fully determine if they deviate from the underlying state law requirements to a sufficient extent to warrant denial of the deduction presents administrative burdens. In addition, the absence of a legislated baseline indicating precisely what constitutes an economic unit in the first place, and the fact that the state-imposed obligations are not as onerous as the economic unit presumption suggests to begin with, would vex any attempt to determine if the deviation justifies denial of the deduction.

The tautology used in this Article for discussion purposes belies the complexity associated with evaluating and tracking the economic relation-

276. See Difonzo & Stern, supra note 233.
277. See, e.g., supra notes 44-45 and accompanying text.
ship between spouses.\textsuperscript{278} It is this complexity that some have relied upon to justify the marriage as a proxy approach to begin with.\textsuperscript{279} This Article criticizes the use of the economic unit presumption and suggests a baseline be developed but offers no such baseline. If a baseline could be determined and evaluated with administrative ease, not only would certain prenuptial agreements lead to a conclusion that the economic unit does not exist, but marriages in general could be so evaluated. Moreover, if the marital deduction provisions were repealed altogether, this baseline could provide the necessary guide to judge whether gratuitous transfers had been made between spouses. Until such a baseline is developed, however, the simplicity of using marriage as a proxy is justified. A discussion of the Federal DOMA and various state laws barring same-sex marriage is beyond the scope of this Article. Given these bars to same-sex marriage, however, consideration of additional proxies seems appropriate.\textsuperscript{280}

\textsuperscript{278} Not discussed in the Article is the possibility of defining economic unit more broadly, perhaps including the entire nuclear family as part of the unit. See Crawford, \textit{supra} note 19, at 792-94; Motro, \textit{supra} note 26, at 1549 (such a discussion is beyond the scope of this Article).

\textsuperscript{279} See McMahon, \textit{supra} note 42, at 718.

\textsuperscript{280} Crawford, \textit{supra} note 19, at 795-96; Motro, \textit{supra} note 26, at 1556-57.