



Agricultural Law Press

Publisher/Editor

Robert P. Achenbach, Jr.

Contributing Editor

Dr. Neil E. Harl, Esq.

* * * *

Issue Contents

Adverse Possession

Driveway **75**

Bankruptcy

Federal Taxation

Discharge **75**

Federal Agricultural Programs

Crop insurance **75**

Soybeans **75**

Federal Estate and Gift Taxation

GSTT **75**

Transfers with retained interests **75**

Federal Income Taxation

Accounting method **76**

Alternative fuel vehicle refueling
property credit **76**

Annuity **76**

Business expenses **76**

Cooperatives **76**

Court awards and settlements **76**

Deductions **77**

Dependents **77**

Disaster losses **77**

Domestic production deduction **77**

Hybrid vehicle tax credit **77**

IRA **77**

Legal Fees **77**

Medical savings accounts **77**

Pension plans **77**

S Corporations

Depreciation **78**

Tax practitioners **78**

Tax shelters **78**

Travel expenses **78**

Probate

Life estate **78**

Property

Public road **79**

In the News 79

Agricultural Law Digest

Volume 18, No. 10

May 11, 2007

ISSN 1051-2780

Proposed Regulations Issued on Effects of Post-Death Events on Deductibility

From the Gross Estate

-by Neil E. Harl*

The Internal Revenue Service, with the issuance of proposed regulations on April 22, 2007,¹ took the first step toward resolving a long-running dispute in authority on the extent to which post-death events are to be considered in the computation of the amounts deductible for federal estate tax purposes.² The issuance of the regulations was surprising in light of the fact that repeal of the federal estate tax is just over 30 months away, and would be effective for deaths after December 31, 2009,³ although the repeal is subject to a “sunset” provision for decedents dying, gifts made and generation-skipping transfers after December 31, 2010.⁴ Moreover, few now believe the federal estate tax will be repealed at the end of 2009 with many betting that the provisions applicable in 2009 will be continued indefinitely by Congressional action this year or next year.

The controversy

The dispute dates back more than 75 years to a 1929 U.S. Supreme Court decision⁵ that established the “date of death” rule for determining deductibility of amounts for federal estate tax purposes. That case involved the calculation of the federal estate tax charitable deduction for a remainder interest (following a life estate for the surviving spouse) with the amount of the deduction determined as of the date of death even though the spouse died within six months after the death of the decedent in question.⁶ In later cases following that decision, courts have generally held that post-death events may not be considered in determining the amount deductible for federal estate tax purposes.⁷ Thus, the Ninth Circuit Court of Appeals has held that the deduction allowable with respect to a lien on real property was the amount of the claim due and owing on the date of the decedent’s death, not the lesser amount later paid in settlement of the claim.⁸ The same court later held that the amount deductible for a claim consisting of an annuity payable to the decedent’s ex-spouse was the actuarial value as of the date of death even though the ex-husband died seven months later so the amount actually paid was substantially less than the date of death actuarial value.⁹ The Tenth Circuit Court of Appeals, in reversing the Tax Court,¹⁰ in a case involving an estate tax deduction for federal and state income tax owed at the time of the decedent’s death, even though the decedent later was entitled to a refund for the tax year at issue, held that events occurring after death are not to be considered in valuing a claim taken as an estate tax deduction.¹¹ Likewise, the Eleventh Circuit Court of Appeals, in a case involving the estate’s reimbursement of federal gift tax liability paid by the heirs

* Charles F. Curtiss Distinguished Professor in Agriculture and Emeritus Professor of Economics, Iowa State University; member of the Iowa Bar.

of the decedent, was to be valued at the date of death, without regard to any post-death events.¹² The Fifth Circuit Court of Appeal has also held that post-death events are not relevant in determining the amount of the deduction.¹³

On the other hand, the Eighth Circuit Court of Appeals in *Jacobs v. Commissioner*,¹⁴ in which the court considered but rejected the date-of-death valuation rule in determining the amount of a claim against the estate that would be deductible in a situation involving an election to take under the will and trust by the surviving spouse rather than to take what was provided under an antenuptial agreement.¹⁵ The Eighth Circuit adopted the view that only claims that are valid against the estate *and that are actually paid by the estate in satisfaction of the claim* could be deducted as claims against the estate.¹⁶

The IRS position has been that post-death events should be considered in determining the amount of a claim that was deductible.¹⁷

The proposed regulations

The proposed regulations clarify that events occurring after a decedent's death are to be considered in determining the amount deductible under all provisions of the federal estate tax law allowing deductions for expenses, indebtedness and taxes.¹⁸ Thus, deductions are limited to amounts actually paid by the estate in satisfaction of deductible expenses and claims.¹⁹ Final court decisions as to the amount and enforceability of the claim or expense are accepted in determining the deductible amount.²⁰ Settlements are acceptable if reached in bona fide negotiations between adverse parties with valid claims that are recognizable under and not inconsistent with state law.²¹

A protective claim for refund may be filed before the expiration of the period of limitations for the claim if the amount of the claim is not ascertainable by the time of expiration of the period of limitations for refunds.²² No deduction can be claimed for a claim that is potential, unmatured or contested at the time the return is filed although, again, a protective claim for refund can be filed.²³

Under the proposed regulations, claims of related parties are subject to a rebuttable presumption that claims by a family member of the decedent, a related entity or a beneficiary of the decedent's estate or revocable trust are not legitimate and bona fide and, therefore, are not deductible.²⁴ Evidence sufficient to rebut the presumption may include evidence that the claim arose from circumstances that would reasonably support a similar claim by unrelated persons or non-beneficiaries.²⁵

Footnotes

¹ NPRM REG 143316-03, April 22, 2007; 72 Fed. Reg. 20080 (April 23, 2007); Prop. Treas. Reg. §§ 20.2053-1, 20.2053-3, 20.2053-4, 20.2053-6, 20.2053-9, 20.2053-10.

² I.R.C. § 2053. See generally 5 Harl, *Agricultural Law* § 44.01 (2007); Harl, *Agricultural Law Manual* § 5.04 (2007).

³ See Pub. L. No. 107-16, § 521(b), 115 Stat. 38 (2001).

⁴ Pub. L. No. 107-16, § 901, 115 Stat. 38 (2001).

⁵ *Ithaca Trust Co. v. United States*, 279 U.S. 151 (1929).

⁶ *Id.*

⁷ See, e.g., *Propstra v. United States*, 680 F.2d 1248 (9th Cir. 1982).

⁸ *Id.*

⁹ *Estate of Van Horne v. Comm'r*, 720 F.2d 1114 (9th Cir. 1983).

¹⁰ *Estate of McMorris*, T.C. Memo. 1999-82.

¹¹ *Estate of McMorris v. Comm'r*, 243 F.3d 1254 (10th Cir. 2001).

¹² *Estate of O'Neal v. United States*, 258 F.3d 1265 (11th Cir. 2001), *aff'g in part and vac'g and rem'g in part*, 99-2 U.S. Tax Cas. (CCH) ¶ 60,365 (N.D. Ala. 1999), *related opinion*, 291 F. Supp. 2d 1253 (N.D. Ala. 2003).

¹³ *Estate of Smith v. Comm'r*, 108 T.C. 412 (1997), *rev'd and rem'd*, 198 F.3d 515 (5th Cir. 2000), *non-acq.*, 2000-1 C.B. xvi, *on remand*, 115 T.C. 342 (2000), *supp. opinion*, T.C. Memo. 2001-303, *aff'd*, 2002-2 U.S. Tax Cas. (CCH) ¶ 60,453 (5th Cir. 2002).

¹⁴ 34 F.2d 233 (8th Cir. 1929), *cert. denied*, 280 U.S. 603 (1929).

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ Rev. Rul. 60-247, 1960-2 C.B. 272 (deduction not allowed for claims against estate where creditor waives payment). See FSA Ltr. Rul. 200217022, Jan. 17, 2002 (estate allowed to deduct claim for wrongful death lawsuits where estate denied claim but later settled its portion of the claim which was the deductible amount; reference to the "two distinct and irreconcilable lines of cases").

¹⁸ I.R.C. § 2053. See Prop. Treas. Reg. § 20.2053-4(a)(2).

¹⁹ Prop. Treas. Reg. § 20.2053-4(a)(1)(iii).

²⁰ Prop. Treas. Reg. §§ 20.2053-1(b)(2)(i), 20.2053-4(d), Ex. 2.

²¹ Prop. Treas. Reg. §§ 20.2053-1(b)(3); 20.2053-4(d), and Ex. 3.

²² See Prop. Treas. Reg. § 20.2053-4(d).

²³ Prop. Treas. Reg. § 20.2053-4(d).

²⁴ Prop. Treas. Reg. § 20.2053-4(b)(4).

²⁵ *Id.*