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A Guide to the Estate and Gift Tax Amendments of 1970

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The Excise, Estate, and Gift Tax Adjustment Act of 1970 [Pub. L. No. 91-614 (Dec. 31, 1970), hereinafter referred to as "the 1970 Act"], made a number of amendments to the federal estate and gift tax laws.

The estate tax laws were amended to shorten the period of time for filing estate tax returns

and for the alternate valuation date and for several related items. In addition, for income tax purposes, the holding period of property that was included in a decedent's gross estate and that was acquired from the decedent was altered; and fiduciaries were granted additional means of obtaining a discharge of their personal liability for estate

EDITOR'S NOTE: This article is based on Professor Kahn's recently prepared supplement to the ALI-ABA Practice Handbook, *FEDERAL TAXATION OF ESTATES, GIFTS, AND TRUSTS*, by Douglas A. Kahn, Earl M. Colson, and George Craven (ALI-ABA Joint Committee on Continuing Legal Education, 4025 Chestnut Street, Philadelphia, Pa., 1970); paperbound, 366 pp., \$9.98 (including postage and handling charges).

taxes or other taxes owed by the decedent at his death.

The gift tax laws were amended to require that, beginning with the year 1971, gift tax returns be filed and the gift tax paid on a quarterly basis rather than annually, which had been the procedure prior to the 1970 Act.

This article will discuss only those changes affecting estate and gift taxes. The 1970 Act also contained amendments concerning excise taxes and other matters that will not be covered here.

ESTATE TAX

Estate Tax Returns

Due Date

The estate tax return for the estate of a decedent dying after December 31, 1970, is due nine months after the decedent's death. 1970 Act §101(b), amending INT. REV. CODE OF 1954 [hereinafter cited, IRC] §6075(a).

Prior to the 1970 Act, the estate tax return was due 15 months after the decedent's death. According to the Senate Finance Committee report, the 1970 Act shortened the period for filing in order to accelerate the collection of revenue, to decrease the period of estate administration, and to expedite the distribution of the estate's assets to the beneficiaries. S. REP. No. 1444, 91st Cong., 2d Sess. (Dec. 15, 1970).

Place of Filing

The 1970 Act authorizes the Treasury to determine in its promulgated regulations whether the estate tax return for the estate of a decedent dying after December 31, 1970, is to be filed:

- In the Internal Revenue district in which the decedent was domiciled at the time of his death, or
- At a service center serving that Internal Revenue district. 1970 Act §101(i), amending IRC §6091(b).

The purpose of this amendment is to expedite the Service's examination of estate tax returns.

In any event, an estate tax return can be filed by hand-carrying it to the office of the Internal Revenue district in which the decedent was domiciled at the time of his death. 1970 Act §101(i), amending IRC §6091(b). This provision will be helpful to an executor who desires verification of timely filing to avoid penalties for filing late. If a decedent was not domiciled in an Internal Revenue district at his death (that is, if he was a non-resident citizen or alien), the estate tax return shall be filed in such place as the Treasury shall designate in its regulations. *Id.* Since that provision merely restates the prior law, presumably the place designated by the Treasury for filing the return will continue to

be the Director of International Operations, Internal Revenue Service, Washington, D.C. Treas. Reg. §20.6091-1.

Preliminary Notice

Prior to the 1970 Act, a preliminary notice (Form 704 for citizens and residents, and Form 705 for nonresident aliens) was required to be filed if the gross estate of a United States citizen or resident exceeded \$60,000 or if it exceeded \$30,000 for a nonresident alien. The preliminary notice was due within two months of the decedent's death.

Because of the shortening of the period for filing an estate tax return from 15 months to nine months, the Internal Revenue Service announced that it will not require a preliminary notice (Form 704 or 705) for estates of persons who died after December 31, 1970, and that it is preparing an appropriate amendment to the Estate Tax Regulations. News Release, Jan. 27, 1971. See P-H FEDERAL TAXES, ESTATE & GIFT TAXES ¶142, 352.

This announcement implements the understanding expressed in the Senate Finance Committee's report [cited above] that the Internal Revenue Service would eliminate the requirement of filing a preliminary notice. The report also states that, henceforth, the Service will give a high priority to the classification and audit of estate tax

returns and that instructions to executors will be promulgated regarding the supporting material to be filed with the estate tax return. If the required supporting material is not filed with the return, the audit may be delayed.

Payment of Estate Tax

The payment of the estate tax is due on the same date that the estate tax return is due, but there are several provisions of the Code under which a taxpayer may obtain an extension of time for the payment of the tax.

Extensions Already Available

IRC §6166 permits an extension of up to 10 years if a substantial portion of the decedent's gross or taxable estate constitutes a closely held business and certain conditions are satisfied, and this provision was not amended by the 1970 Act.

Section 6163 provides an extension of time for the payment of an estate tax on the value of a reversionary or remainder interest in property that is included in the decedent's gross estate, and this provision was likewise not amended by the 1970 Act.

Alternatively, IRC §6161(a)(2) also permits an extension of time for payment of all or part of the estate tax for a reasonable period of up to 10 years if the taxpayer can demonstrate that payment of such part of the estate tax would

result in an undue hardship to the estate. The maximum extension of time for payment of an estate tax deficiency (in contrast to the estate tax shown as due on the estate tax return) is four years. IRC §6161(b).

In addition, prior to the 1970 Act, IRC §6161(a)(1) permitted the Internal Revenue Service to grant an extension of time for the payment of various taxes, including the estate tax, for a reasonable period of up to six months. The extension can exceed six months for a taxpayer who lives abroad. Prior to the 1970 Act, IRC §6161(a)(1) was not employed frequently to extend the time for estate tax payments, but it was administered more liberally than was the "undue hardship" provision in IRC §6161(a)(2). See S. REP. NO. 1444, above.

New 12-Month Extension

In order to alleviate the hardship that might be imposed upon an estate by requiring it to pay the estate tax nine months after the decedent's death when liquid assets are not readily available, the 1970 Act amended IRC §6161(a)(1) to permit an extension of time of up to 12 months for the payment of the estate tax liability of a decedent who died after December 31, 1970. 1970 Act §101(h), amending IRC §6161(a)(1). Consequently, while the 1970 Act shortened the period of time for

filing an estate tax return and paying the estate tax by six months, the Act also lengthened the period of time for which the payment of the estate tax may be extended by six months.

Examples

The Senate Finance Committee report on the 1970 Act [cited above] stated the Committee's understanding with the Treasury Department that henceforth extensions of time under IRC §6161(a)(1) will be made "on a more liberal basis than in the past and that in the future they will be available whenever there is reasonable cause." The report lists six situations in which the Treasury will grant extensions under IRC §6161(a)(1) as examples of the types of requests that will be granted extensions. Those six examples cover the following situations:

- A farm (or a closely held business) comprises a significant portion of a decedent's gross estate, but the percentage requirements for automatic extension of time under IRC §6166 where a closely held business constitutes a specific percentage of either the gross estate or the taxable estate are not satisfied. The estate does not have sufficient liquid funds to pay the estate tax. Even though the farm, or other closely held business, could be sold to a third party for a sum that is sufficient to provide

ample liquidity to pay the estate tax, the executor will be granted an extension of time under IRC §6161(a)(1) to facilitate the raising of funds from other sources.

- The decedent's gross estate contains sufficient liquid assets to pay the estate tax. An extension of time nevertheless will be granted where the liquid assets cannot be marshalled by the executor, even with due diligence, within the time period for payment of the tax because the assets are located in several jurisdictions and thus are not immediately subject to the executor's control.

- An extension will be granted to an estate where a substantial part of the estate's assets is the right to receive payments in the future—for example, copyright royalties, annuities, contingent fees, or accounts receivable. These assets do not provide immediate cash value, and the estate usually cannot borrow against them except upon harsh terms that would cause a substantial loss to the estate.

- An extension will be granted where the estate includes a claim to a substantial amount of assets, which claim must be litigated successfully to collect the assets. In that case, the size of the taxable estate—and thus the amount of estate tax owing—cannot be ascertained.

- An extension will be granted where otherwise assets of the estate will have to be sold in a depressed market or at a sacrifice price.

- An extension will be granted where the estate lacks sufficient funds to provide a reasonable allowance for the period of administration of the estate to the decedent's widow and dependent children and to satisfy legitimate claims against the estate if the estate tax is paid when the return is filed. The extension will be granted even though the estate could borrow sufficient funds if the loans could be obtained only at a rate of interest higher than that which is generally available. However, the executor must have made a reasonable effort to convert assets in his possession to cash, other than an interest in a closely held business to which IRC §6166 applies.

The extensions granted under IRC §6161(a)(1) will be limited to the period of cash shortage. The committee report states that the above six examples are not exclusive and that an extension will be granted whenever an examination of the facts and circumstances discloses that the request is reasonable.

Appeal Procedure

The committee report further states that the Internal Revenue

Service will establish an appeal procedure so that when a district director's office denies a request for an extension of time for payment of the estate tax under IRC §6161(a)(1), the executor can have his request reviewed by the office of the Regional Commissioner for the region that includes that district.

Interest Rates

If the period for payment of an estate tax is extended under IRC §6161(a)(1), the estate must pay simple interest at a rate of six per cent per annum on the unpaid amount. IRC §6601(a). If the period for payment of an estate tax is extended under IRC §6161(a)(2) (the "undue hardship" provision) or under IRC §6166 (the closely held business provision), the rate of simple interest on the unpaid amount is only four per cent per annum.

Consequently, an executor might prefer to obtain an extension of time under the latter two provisions rather than under IRC §6161(a)(1) where that is possible. Also, time may be extended under those two provisions for up to 10 years, and the extension of time under section 6161(a)(1) cannot exceed 12 months. But in many instances, an executor may be able to obtain an extension only under IRC §6161(a)(1).

In this connection, it is noteworthy that the necessity to sell

assets at a sacrifice price or in a depressed market, or to sell a family business to unrelated persons, constitutes an undue hardship under IRC §6161(a)(2). Treas. Reg. §20.6161-1(b). It should be noted that the provisions for extending the time for payment of the estate tax do not authorize any delay in the filing of the estate tax return.

Alternate Valuation Date

Under IRC §2032, the executor of a decedent's estate may elect to have the assets that are included in the decedent's gross estate valued at a specified date after the decedent's death instead of the date of the decedent's death, which would otherwise be the valuation date. IRC §2031 establishes the date of the decedent's death as the valuation date where the executor does not elect to use the alternate valuation date.

Prior to the 1970 Act, the alternate valuation date for property included in the decedent's gross estate that was distributed, sold, exchanged, or otherwise disposed of within one year after the decedent's death was the date of such distribution, sale, exchange, or other disposition; and the alternate valuation date for such property that was *not* distributed, sold, exchanged, or otherwise disposed of during the one-year period following the decedent's death was the date one year after the de-

cedent's death. IRC §2032(a).

Since the election for the alternate valuation date is made on the estate tax return [IRC §2032(c)], the 1970 Act's shortening of the period for filing the estate tax return from 15 months after the decedent's death to nine months after the decedent's death would have required the executor to elect the alternate valuation date at a time when the period for valuing undistributed and unsold assets had not yet expired, and consequently the executor would have had to speculate as to the desirability of making the election. Accordingly, the 1970 Act amended IRC §2032 so that for the estates of decedents dying after December 31, 1970, the relevant date for alternate valuation is six months after the decedent's death. 1970 Act §101(a), amending IRC §2032.

Illustration. X died on January 5, 1971. At the time of his death, X owned 1,000 shares of stock of Win All, Inc., a publicly held corporation, and he owned Blackacre. In addition, one year prior to his death, X gave Whiteacre to Y, and that gift was held to be in contemplation of death.

At the date of X's death, the fair market value of the 1,000 shares of Win All stock was \$100,000; the fair market value of Blackacre was \$50,000; and the fair market value of White-

acre was \$25,000.

On March 13, 1971, Y sold Whiteacre to an unrelated party for its then value of \$26,500. On May 26, 1971, the executor distributed Blackacre to the Friendly National Bank, who is serving as the testamentary trustee of the residue of X's estate, and the fair market value of Whiteacre on that date is \$52,000. The fair market value of Win All stock on July 5, 1971 (six months after X's death) is \$80,000, and the Win All stock is distributed by the executor to the Friendly National Bank on August 2, 1971.

The executor elects to use the alternate valuation date. The estate tax values of these three assets are as shown in Table 1 on the following page.

Power of Appointment Exercised in Favor of Charity

IRC §2055(b) provides a limited exception to the general rule that no charitable deduction is allowed to a decedent unless the transfer to the charitable organization was made by the decedent. This exception extends the charitable deduction to certain situations where a power of appointment that was created by the decedent is exercised by the decedent's surviving spouse in favor of a charity.

To begin with, there must be a bequest to a trust, all the income from which is payable to the de-

cedent's surviving spouse for her life and the corpus of which is subject to a power of appointment by the surviving spouse. To the extent that the surviving spouse's power is exercised in favor of a charitable organization, the bequest will be treated as a bequest of the remainder interest from the decedent to such charitable organization, if certain requirements are met.

Statutory Requirements

Among the statutory requirements are the conditions that:

- The surviving spouse be over 80 years of age at the date of the decedent's death; and
- The surviving spouse must execute an affidavit within *one year* after the decedent's death specifying the organizations in whose

TABLE 1—ILLUSTRATION OF ESTATE TAX VALUES AND ALTERNATE VALUATION DATES

| <i>Asset</i> | <i>Estate tax value</i> | <i>Date of valuation</i> |
|-------------------------------|-------------------------|---|
| Whiteacre | \$26,500 | Date Y sold Whiteacre, since that was within six months of X's death. |
| Blackacre | \$52,000 | Date distributed to the testamentary trustee.* |
| 1,000 shares of Win All, Inc. | \$80,000 | The date six months after the decedent's death, since it was not distributed or sold prior to that date.* |

*The date of valuation may be on a day earlier than the actual date of distribution or sale in some cases—for example, where there was a prior entry of an order or decree of distribution that became final, the entry of the order or decree would be the date of valuation. Treas. Reg. §20.2032-1(c)(2). For a list of the circumstances where an asset may be valued at a date prior to the actual sale or distribution, see KAHN, COLSON & CRAVEN, FEDERAL TAXATION OF ESTATES, GIFTS, AND TRUSTS 82 (ALI-ABA Joint Committee on Continuing Legal Education, Philadelphia, 1970).

favor he or she plans to exercise the power and the amount or proportion of the trust to be so appointed.

- As to decedents dying after December 31, 1970, the period of time for the surviving spouse to file the required affidavit was shortened from one year to *six months* after the date of the decedent's death. 1970 Act §101(c), amending IRC §2055(b)(2)(c). This change was needed because of the shortening of the period of time for filing the decedent's estate tax return. If the affidavit were not executed prior to the filing of the estate tax return, the executor could not claim the charitable deduction.

It is noteworthy that under the changes adopted by the Tax Reform Act of 1969, a bequest of a remainder interest in a trust to a charity would not qualify for an estate tax deduction where the surviving spouse has a right to all the income from the trust, since the remainder interest does not qualify as a charitable remainder annuity trust or a charitable remainder unitrust. IRC §2055(e). However, IRC §2055(b) is clearly intended to permit a charitable deduction in the limited and unusual circumstances described therein, and in view of the 1970 Act's amendment of that provision, it would appear that Con-

gress intends to retain that deduction, notwithstanding the inconsistent language in IRC §2055(e).

Holding Period for Income Tax Purposes

One consequence of shortening the time period for filing the decedent's estate tax return and paying the tax is that an executor may have to sell estate assets within a few months after the decedent's death in order to obtain sufficient liquid funds to pay the tax.

Prior to the 1970 Act, the holding period of assets that comprised part of the decedent's probate estate commenced with the date of the decedent's death, and consequently the gain or loss on capital assets sold by the executor within six months of the decedent's death was characterized as short-term gain or loss. IRC §1222(1)-(2). As for assets that were not owned by the decedent at his death but which nevertheless were included in his gross estate for estate tax purposes (for example, transfers made by the decedent in contemplation of death and transfers to a revocable trust), the holding period of such assets was not free from doubt, but it appears that the holding period of such assets commenced with the date on which the decedent transferred the property rather than on the date of the decedent's death. Rev. Rul. 59-86, 1959-1 CUM. BULL. 209. But see

Fifth Avenue Bank v. United States, 41 F. Supp. 428 (Ct. Cl. 1941), cert. denied, 315 U.S. 820 (1942).

In view of the 1970 Act's change described below, any doubts as to the holding period of such property has been mooted.

Six-Month Treatment

In order to expedite the sale of the estate's assets, section 101(g) of the 1970 Act [amending IRC §1223] provides that the holding period of the property is deemed to be in excess of six months where:

- The property was acquired from or passed from a decedent who died after December 31, 1970 [IRC §1014(b) describes the types of acquisitions that are deemed to have passed from or been acquired by a decedent];
- The basis of such property is determined by its value at the date of the decedent's death or, if an election is made under IRC §2032, by its value at the alternate valuation date [IRC §1014(b) describes the types of property whose basis is determined by its value at the decedent's death or alternate valuation date, including property owned by decedent at the time of death, property transferred by him prior to his death but included in his gross estate for estate tax pur-

poses, jointly held property for which the decedent furnished the consideration, and, in most cases, the surviving spouse's share of community property]; and

- The property is sold or otherwise disposed of within six months after the decedent's death by the person who acquired the property from the decedent or his estate.

Thus, where the distributee of a capital asset from a decedent who died after December 31, 1970, which property was included in the decedent's gross estate for estate tax purposes, recognizes a gain or loss on the sale of such property, the gain or loss will be characterized as a long-term capital gain or a long-term capital loss. (Indeed, this provision apparently also applies to the surviving spouse's share of community property, and that application might be significant if the community property were acquired shortly before the decedent's death and were sold shortly after his death.)

If the property the distributee acquired from a decedent dying after December 31, 1970 or from his estate was property described in IRC §1231(b) or if the distributee's disposition of such property was of the type described in IRC §1231(a)—for example, an involuntary conversion caused by a fire or by a theft—then, IRC §1231 will apply to such sale or

other disposition even if it should occur within six months after the decedent's death.

Fiduciary's Personal Liability for Estate Tax

Executors, trustees, and other fiduciaries may be held personally liable under section 3467 of the Revised Statutes (31 U.S.C. §192), or under IRC §6324, or under local state law for the payment of taxes owed the United States by the person or estate they represent, if in their fiduciary capacity they make payment of a debt or a distribution to a beneficiary that results in the remaining assets administered by them being insufficient to pay the taxes owing to the United States.

Discharge of Executor's Liability

IRC §2204 permits an executor to obtain a discharge of his personal liability for the payment of estate taxes by requesting the district director to make a determination of the estate tax owing, which determination must be made within one year after the request is filed (or one year after the estate tax return is filed if that is a later date). If the executor pays the full amount of the tax so determined by the district director, the executor will not be personally liable for any tax deficiency that might subsequently be assessed. IRC §2204; Treas. Reg. §20.2204-1.

As used in the Internal Revenue

Code, the term "executor" refers to an executor or an administrator of a decedent, or if none is appointed, qualified, and acting in the United States, it refers to any person having actual or constructive possession of the decedent's property. IRC §2203.

Prior to 1970, IRC §2204 applied only to the executor, and there was no comparable relief for other fiduciaries, such as trustees, who held assets that were included in a decedent's gross estate, even though they also might be personally liable for the payment of the estate tax. Moreover, even as to executors, the relief afforded by IRC §2204 was available only after the entire amount of estate tax was paid, and consequently an executor remained personally liable for estate taxes during the period that the payment of the estate tax liability was extended and being paid in installments.

More Liberal Relief

The 1970 Act made several important amendments to IRC §2204 that substantially liberalized the relief available under that provision. 1970 Act §101(d), (f), amending IRC §2204.

Under the 1970 Act, an executor of an estate of a decedent who died after December 31, 1970, will be discharged from personal liability upon payment of the amount of estate tax determined by the district director to be currently

owing (exclusive of any amount of the estate tax the payment of which is extended under IRC §§6161, 6163, or 6166), provided that if the district director requests it, the executor must furnish a bond for any amount the time for payment of which has been extended. Thus, the executor may utilize IRC §2204, even though the payment of the estate tax is deferred.

The executor is required to furnish a bond for the satisfaction of the unpaid tax liability only if the Service requests it. The report of the Senate Committee [cited above] expressed the committee's belief that it is desirable to permit a discharge of personal liability where the payment of tax is deferred, if the Service is satisfied that the transferee of the estate's assets will make the appropriate payments or where a bond has been provided that assures the payment of the unpaid tax.

Trustees and Other Fiduciaries

In addition, the 1970 Act amended IRC §2204 to provide relief for trustees or other fiduciaries who are not executors, provided that the executor of the decedent also requests a discharge of his personal liability under IRC §2204.

A fiduciary (other than a fiduciary when the decedent was a non-resident) who is not an executor may apply to the Service for

a determination of the amount of estate tax liability for which he is personally liable and for discharge of that personal liability. Upon the determination of the executor's personal liability pursuant to a request made by the executor under IRC §2204, or upon the expiration of six months from the fiduciary's request, whichever is later, the Service shall then notify the fiduciary of the amount of estate tax for which the fiduciary is personally liable.

Upon the fiduciary's payment of that amount of the estate tax for which he is determined to be personally liable (exclusive of any amount the time for payment of which has been extended under IRC §§6161, 6163, or 6166), the fiduciary will be discharged from any tax found thereafter to be due, provided that, if the Service requests it, the fiduciary must furnish a bond for any amount the time for payment of which has been extended. 1970 Act §101(d), adding IRC §2204(b).

The language actually employed in the 1970 Act reads: "On payment of the amount of such tax for which it has been determined the fiduciary is liable (other than any amount the time for payment of which has *not* been extended under section 6161, 6163, or 6166)" [emphasis added]. The word "not" clearly does not belong in that sentence and must have been included by inadvertence. The

sentence makes no sense when the word "not" is included, and the Senate Committee's report [cited above] demonstrates the intention to exclude that part of the estate tax for which payment had been deferred.

This provision applies only to fiduciaries for decedents who died after December 31, 1970.

A fiduciary has a legitimate concern as to the extent of his personal liability, and Congress granted this relief so that fiduciaries would not be subjected to a greater risk than is necessary for the protection of the revenue. S. REP. NO. 1444, above. It should be noted that these relief provisions serve only to discharge fiduciaries from *personal* liability and do not affect their fiduciary obligation to pay taxes that are subsequently determined to be owing.

Accelerated Audit

Since the 1970 Act shortened the period for filing estate tax returns and for payment of the estate tax, and thus increased the burden imposed on the executor to complete the administration of the estate, Congress decided that in fairness a correlative obligation should be imposed on the Service to complete its audit on the estate tax return within a shorter time period. *Id.* Accordingly, for estates of decedents dying after December 31, 1973, where an executor re-

quests a determination of the estate tax and a discharge of his personal liability, the estate tax must be determined nine months after the request is made or nine months after the estate tax return is filed, whichever is later. 1970 Act §101 (f), amending IRC §2204. Thus, the period for determining the estate tax liability will be shortened from one year to nine months.

The effective date of this provision was postponed until 1974 in order to provide the Service with adequate time to make appropriate administrative adjustments in its audit procedures.

Executor's Liability for Income and Gift Taxes

Under section 3467 of the Revised Statutes [31 U.S.C. §192], an executor may incur personal liability for the payment of any income or gift taxes that were owed by the decedent. Prior to the 1970 Act, there was no procedure by which the executor could obtain a discharge from his personal liability for those taxes.

Congress determined that the threat to an executor of personal liability for such taxes was a deterrent to the rapid administration of the estate and the distribution of the estate's assets, and therefore that a procedure should be established to permit the executor to obtain a discharge from that potential liability. S. REP. NO. 1444, above. Accordingly, Con-

gress added section 6905 to the Code. 1970 Act §101(e).

Section 6905 provides that where an executor makes a written application for release from personal liability for a decedent's income and gift taxes, the Service may notify the executor of the amount of such taxes. Upon the executor's payment of the amount of tax of which he is notified (or, if no notification is sent to the executor, upon the expiration of one year from the date on which the executor's written application was received), the executor shall be discharged from any personal liability for any additional tax found to be due.

Thus, if the Service cannot or does not choose to determine the tax within the requisite one-year period, the executor will have no further personal liability, but that does not remove the Government's lien on the estate's assets or relieve the executor from fiduciary liability. For executors of decedents dying after December 31, 1973, this one-year period is reduced to nine months. 1970 Act §101(f).

Presumably, the written application of the executor will have to request notice of the liability for specific taxes for specific years [compare Treas. Reg. §301.6501(d)-1], but the statute does not expressly resolve that question and leaves it to be resolved by the regulations. The application must be made after the return with

respect to such income or gift taxes is made and filed, and that requirement suggests that it may not be possible for the executor to obtain a discharge from taxes owing for a year for which no tax return was filed. The manner and form of the written application will be prescribed by regulations to be promulgated.

As used in IRC §6905, the term "executor" refers only to "the executor or administrator of the decedent appointed, qualified, and acting within the United States." IRC §6905(b).

GIFT TAXES

Gift Tax Returns

Prior to the 1970 Act, gift taxes were paid on gifts made during a calendar year, and the gift tax return (Form 709) and the gift tax payment were due on or before the 15th day of April following the close of the calendar year in which the gifts were made. A gift tax return was required whenever an individual donor either:

- Made a gift of a future interest in any amount; or
- Made a gift or gifts to any one donee (including a donee who is a charitable organization) of a total value in excess of \$3,000.

Quarterly Basis

Thus, if a large gift were made

on January 2, 1965, no gift tax would be owing on that gift until April 15, 1966. Congress viewed this procedure as an unreasonable deferral of the gift tax payment [S. REP. No. 1444, above], and accordingly amended the gift tax laws to require that, for gifts made after December 31, 1970, gift tax returns shall be filed and gift tax payments made on a quarterly basis. 1970 Act §102, amending IRC §§2501-4, 6019, and 6075(b).

The 1970 Act retained the \$3,000 annual exclusion of gifts of present interests made to one donee, but the exclusion must be used in the earliest available quarter of such year. The 1970 Act also retained the \$30,000 lifetime exemption.

Where a donor makes a gift of a future interest in a calendar quarter, or where a donor makes a gift in a calendar quarter of a present interest in excess of his unused annual exclusion for that donee, the donor must file a gift tax return for that calendar quarter on or before the 15th day of the second month following the close of the calendar quarter. IRC §§6075(b), 6019, and 2503(b), as amended by the 1970 Act §102.

Illustration. X had made no gifts prior to 1971. In 1971, X made the following gifts:

On February 4, 1971, X gave \$2,500 cash to A. On April 3, 1971, X gave \$2,800 cash to B.

On June 10, 1971, X gave a remainder interest in Blackacre valued at \$2,600 to C. On August 10, 1971, X gave \$1,200 cash to A.

In the first quarter of 1971, X did not make a transfer that was to be included in the total amount of gifts made by him, since he gave less than \$3,000 to A, and the property transferred to A was not a future interest. (IRC §2503(b) excludes from consideration of taxable gifts transfers to a donee of a present interest of up to \$3,000, less the aggregate value of present interests transferred to that donee in prior calendar quarters of that calendar year.) Consequently, X will not file a gift tax return for the first calendar quarter.

In the second calendar quarter (April-June), X's gift to B was less than \$3,000 and therefore is not to be reported, but X's gift to C was a transfer of a future interest and therefore is not excluded under IRC §2503(b). Accordingly, X must file a gift tax return by August 15, 1971, and report the \$2,800 gift to B, but X may elect to deduct \$2,800 of his \$30,000 lifetime exemption under IRC §2521 and thus pay no gift tax.

In the third calendar quarter (July-September), X gave \$1,200, to A, which was \$700 more than the difference between

\$3,000 and the \$2,500 given to *A* in the first calendar quarter. Accordingly, *A* must file a gift tax return by November 15, 1971, and report a \$700 gift to *A*, which gift will be taxable unless *X* elects to use part of his lifetime exemption.

Reporting Charitable Transfers

Under the 1970 Act, where a donor makes a gift to a qualified charity (that is, a transfer that qualifies for a charitable deduction under IRC §2522), no return shall be required unless the gift to the charity is a future interest or unless the aggregate amount given by the donor to that charity for the calendar quarter and the preceding calendar quarters of that calendar year exceed \$3,000. IRC §6019(a). Thus, even though the total amount given to a charity in excess of the \$3,000 annual exclusion is deductible as a charitable deduction, the donor must file a gift tax return; and this requirement in the 1970 Act merely restates the same requirement that existed under prior law.

Where a gift tax return is required for a transfer to a charity that is fully deductible under IRC §2522 as a charitable deduction, the 1970 Act requires that the gift tax return be filed for the fourth calendar quarter for the calendar year in which the gift was made (that is by February 15 of the following year) unless a quarterly

gift tax return must otherwise be filed (because of a non-charitable gift) on an earlier date after the quarter in which the charitable gift was made. In that latter event, the charitable gift shall be reported on the earliest gift tax return filed by the donor after making the charitable gift. IRC §6019.

(Literally read, section 6019 would require that the charitable transfer be included in the first return filed for a calendar quarter of the calendar year in which the charitable transfer was made, but it would be more reasonable to construe that provision as requiring that the charitable transfer be so included only if such return is filed after the date on which the charitable transfer was made.)

Deferred Filing

Since no gift tax will be payable on a qualified charitable transfer because of the charitable deduction allowed, the 1970 Act does not require the donor to file a return for that transfer until the end of the calendar year (that is, by February 15 of the following calendar year). But if the taxpayer must otherwise file a gift tax return in the calendar year in which the charitable transfer was made, he will not be inconvenienced by including the charitable transfers in that earlier return (and indeed that avoids the inconvenience of filing a second return at the end of the year), and consequently the

transfer is to be reported on the earlier return. S. REP. No. 1444, above.

According to the report of the Senate Finance Committee, this special provision for charitable transfers does not apply where the donor makes a gift in which the beneficial interests are split between charitable and non-charitable beneficiaries, even though the interest of the charitable beneficiary is deductible as a charitable gift under IRC §2522. Where the special provisions for qualified charitable transfers are inapplicable, a gift tax return must be filed for the quarter in which the gift was made.

According to the committee, the statutory definition of the term "qualified charitable transfer" as a transfer by gift with respect to which a charitable deduction is allowed for the full amount transferred [IRC §6019] requires that the entire amount of the gift must be transferred to a qualified charity to obtain the special benefit of deferring the filing of a tax return. The reference in section 6019 to the amount "transferred by gift" refers to the amount so transferred in excess of the annual exclusion allowed on account of the gift. IRC §2503(b). Thus, if *X* gave \$10,000 cash to a qualified charity on January 5, 1972, and made no other gifts in that year, *X* would file a gift tax return for that gift by February 15, 1973,

even though of the \$10,000 transferred by *X*, \$3,000 was excluded under IRC §2503(b) and only the remaining \$7,000 was deductible under IRC §2522.

Examples of Filing

The following examples illustrate the procedure for filing gift tax returns for charitable gifts:

Illustration a. *X* gave \$10,000 cash to *Z*, a qualified charity, on March 3, 1971, and *X* made no other gifts in that year. *X* must file a gift tax return no later than February 15, 1972. In that return, *X* will utilize a \$3,000 exclusion [IRC §2503(b)] and a \$7,000 charitable deduction, and consequently he will have no gift tax liability.

Illustration b. The same facts as in *Illustration a*, except that *X* also gave \$4,500 cash to *Y*, an individual, on April 10, 1971 (the second calendar quarter of that year). Since *X* must file a gift tax return on August 15, 1971, to report the gift to *Y* (which was in excess of \$3,000), *X* must also report the charitable gift made to *Z* on that same return.

Illustration c. On January 10, 1972, *X* transferred \$40,000 cash in trust for the life of his son, *S* who is paid an annuity from the trust. The remainder

interest in the trust belongs to a qualified charity, and *X*'s transfer of the remainder interest qualified for a gift tax charitable deduction under IRC §2522, because the remainder interest constituted a charitable remainder annuity trust. IRC §2522(c)(2)(A). *X* made no other gifts in 1972.

According to the Senate Finance Committee's report, *X* must file a gift tax return reporting the charitable gift by May 15, 1972 (that is, the return must be filed for the calendar quarter in which the charitable gift was made), because the amount transferred in trust is greater than the amount deductible under IRC §2522, on account of the charity's interest in the transfer.

While the Committee's report discussed in detail the exception shown in Illustration *c*, it does not appear to have much significance. If (as is likely) the value of *S*'s annuity interest exceeds \$3,000, *X* will have to file a gift tax return for the first calendar quarter in any event, and consequently, as noted in Illustration *b*, *X* would then have to report the charitable gift by May 15, 1972, regardless of the applicability of this additional exception.

If the value of *S*'s annuity interest were less than \$3,000 so that the full amount of *S*'s interest were

excluded under IRC §2503(b), then it would appear that the amount transferred by *X* in trust (the full amount transferred less the annual exclusion allowed) would equal the amount allowed as a charitable deduction so that this special exception will not apply. The report of the Senate Finance Committee does not discuss that situation.

It should be emphasized that the 1970 Act's amendments to the gift tax laws apply only to gifts made after December 31, 1970. 1970 Act §102(e).

Payment of Gift Taxes

The gift tax is computed and paid when a gift tax return is filed, so that for gifts made after December 31, 1970, the gift tax will be paid on a quarterly basis. IRC §§6151, 2501-04, and 2521, as amended by the 1970 Act.

The rate of the gift tax, the annual exclusions and allowable gift tax deductions, and the procedure for computing the gift tax were not changed by the 1970 Act, other than by requiring the computation of tax to be made quarterly rather than annually. S. REP. No. 1444, above. Thus, the cumulative effect of the prior gift tax law is preserved.

Of course, a gift tax return filed for one calendar quarter will commence the running of the period of limitations for assessing a gift tax deficiency only for that quarter

and not for any other quarter of that calendar year. IRC §6501.

Split Gifts

The gift tax laws permit a husband and wife to divide the gifts made by either or both of them to third parties during a taxable period equally between themselves if certain conditions are met. IRC §2513. The gifts to third parties are not physically divided, but are treated for gift purposes as if each spouse had made one-half of all the gifts actually made by either or both spouses during the taxable period, provided that only gifts made after the spouses marry are split.

Prior to the 1970 Act, the election to split gifts was made on the return or returns filed by the spouses for the calendar year in which the gifts were made, and the election applied to all gifts made during that calendar year by the spouses while they were married. That is, the spouses could not select some gifts for splitting and treat others as the gift of the actual donor. IRC §2513(a)(2); Treas. Reg. §25.2513-1 and -2.

Election

The 1970 Act changed the taxable period for gifts from the calendar year to the calendar quarter, and accordingly section 102(b)(2) of the 1970 Act amended IRC §2513 so that the split-gift election is made on a quarterly rather than

on an annual basis for gifts made after December 31, 1970. Thus, the election is made on a gift tax return for a calendar quarter, and all gifts made by the married spouses during that quarter must be split. Spouses may elect split-gift treatment for one or more quarters of a calendar year and not elect split-gift treatment for the other quarters of that year. The consent to split-gift treatment may not be made prior to the close of the calendar quarter in which the gifts were made. IRC §2513(b)(2), as amended by the 1970 Act.

The election may be made at any time between the close of the calendar quarter in which the gifts were made and the 15th day of the second month following the close of that calendar quarter, and indeed the election may even be made after the 15th day of the second month following the close of that calendar quarter, provided that prior to making the election:

- No gift tax return was filed by either spouse for that calendar quarter; and
- Neither spouse had received a notice of deficiency with respect to the gift tax for such calendar quarter. IRC §2513(b)(2), as amended by the 1970 Act.

An election to split gifts cannot be revoked after the 15th day of the second month following the

close of the calendar quarter in which the gifts were made; but if an election to split gifts is made on or prior to that date (the 15th day of the second month), it may be revoked by the spouses, provided that the revocation is made prior to the 16th day of the second month following the close of such calendar quarter. IRC §2513(c), as amended by the 1970 Act.

Joint Tenancies between Spouses in Real Property

Generally, the creation of a joint tenancy [or, for the purposes of this article, a tenancy by the entirety] between spouses, where one spouse provided a disproportionate amount of the consideration for the property, would cause gift tax consequences. Similarly, one spouse's adding to the value of jointly held property by making additions or improvements or by reducing the debt on the property would also cause gift tax consequences. However, where the jointly held property is *realty*, the gift tax laws permit the donor spouse to elect whether or not to treat the transfer as a gift for gift

tax purposes. IRC §2515.

If the donor spouse does nothing, the transfer is not treated as a gift. If the donor spouse wishes to have the transfer treated as a gift, he must file a gift tax return for the taxable period during which the transfer was made; and to make the election, the gift tax return must be filed irrespective of whether the amount transferred exceeds the annual exclusion. That is, even though a gift tax return would not otherwise be required because the amount transferred to the donee spouse is a present interest having a value less than \$3,000, a gift tax return must be filed to have the transfer treated as a gift.

Prior to the 1970 Act, the taxable period for gift taxes was the calendar year, and consequently the election was made by filing a gift tax return for the calendar year in which the transfer was made. Where such transfers are made after December 31, 1970, the election must be made on a return for the calendar quarter in which the transfer occurred. 1970 Act §102(b)(3), amending IRC §2515(c).

I cannot resist interposing the old story of the young lawyer who reported to his father, when the latter returned from vacation, that he had finally closed out the Smith estate, whereupon the horrified father said: "Good heavens—we have been living on that estate for years."

RENE A. WORMSER, THE PLANNING AND ADMINISTRATION OF ESTATES 225 (Practising Law Institute, New York, 1961).