June 20, 2016

The Honorable John A. Koskinen
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC  20224

The Honorable William J. Wilkins
Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Comments on Consistency in Basis Proposed Regulations [REG-127923-15]

Dear Messrs. Koskinen and Wilkins:

Enclosed please find comments on consistent basis reporting between estate and person acquiring property from decedent (“Comments”). These Comments are submitted on behalf of the American Bar Association Section of Taxation and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

The Section of Taxation would be pleased to discuss the Comments with you or your staff if that would be helpful.

Sincerely,

George C. Howell, III
Chair, Section of Taxation

Enclosure

cc: Karen Schiller, Commissioner (Small Business/Self Employed), Internal Revenue Service
William M. Paul, Deputy Chief Counsel (Technical), Internal Revenue Service
Curtis Wilson, Associate Chief Counsel (Passthroughs & Special Industries), Internal Revenue Service
Theresa M. Melchiorre, Attorney, Office of the Associate Chief Counsel (Passthroughs & Special Industries), Internal Revenue Service
Hon. Mark Mazur, Assistant Secretary (Tax Policy), Department of the Treasury
Emily McMahon, Deputy Assistant Secretary (Tax Policy), Department of the Treasury
AMERICAN BAR ASSOCIATION
SECTION OF TAXATION

COMMENTS IN RESPONSE TO PROPOSED REGULATIONS
REGARDING CONSISTENCY IN INCOME TAX BASIS

[REG-127923-15]

These comments ("Comments") are submitted on behalf of the American Bar Association Section of Taxation (the "Section") and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by representatives from the Section’s Estate and Gift Tax Committee ("EGT") and Fiduciary Income Tax Committee ("FIT"), namely, Benjamin G. Carter, Jeffrey Chadwick, Elizabeth Glasgow, George D. Karibjanian, Hannah W. Mensch, Helen Rogers and Brian Tsu. The Comments were reviewed by Laura S. Hundley, Chair of EGT, and David A. Berek, Chair of FIT. The Comments were further reviewed by John Bergner, Council Director for EGT and FIT, by Lisa M. Stern, Chair of FIT from 2011-2013, on behalf of the Committee on Government Submissions, and by Peter H. Blessing, the Section’s Vice Chair (Government Relations).

Although the members of the Section who participated in preparing these Comments have clients who might be affected by the federal tax principles addressed by these Comments, no such member or the firm or organization to which such member belongs has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments. Additionally, while the Section’s diverse membership includes government officials, no such official was involved in any part of the drafting or review of these Comments.

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Date: June 20, 2016
EXECUTIVE SUMMARY

On July 31, 2015, President Obama signed into law the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 (the “Act”). Section 2004 of the Act enacted new sections 1014(f) and 6035, which implemented new basis consistency rules for taxpayers acquiring property from a decedent and new information reporting requirements for executors of estates. In addition to these sections, the Act also enacted new section 6662(b)(8), incorporating the basis consistency rules into the accuracy-related penalties provisions, and also provided that certain returns and statements are subject to the return penalty provisions of sections 6721 and 6722 (together, these provisions shall be referred to as the “Penalty Provisions”).

Under the revised statutes, the executor of any decedent’s estate required to file a return under section 6018(a) (i.e., a United States Estate (and Generation Skipping Transfer) Tax Return, Form 706 (the “Estate Tax Return”)) shall furnish to the Secretary and to each person acquiring any interest in property included in the decedent's gross estate for federal estate tax purposes (the “Gross Estate”) a statement (as to filings to the Secretary, the “Information Return,” and as to filings to such person acquiring an interest in such property, the “Statement”) identifying the value of each interest in such property as reported on the Estate Tax Return and such other information with respect to such interest as the Secretary may prescribe (throughout this letter, this may be referenced as the “Disclosure Requirement”). With respect to any property reported on such Statement(s) that increases the decedent’s liability for the federal estate tax, the cost basis for federal income tax purposes in the hands of the recipient of such property shall not exceed the final value of which has been determined for purposes of the federal estate tax.

On December 18, 2015, the Internal Revenue Service (the “Service”) published a draft Information Return (Form 8971, “Information Regarding Beneficiaries Acquiring Property from a Decedent”), which is the required format for executors to comply with the Act. Draft instructions for Form 8971 appeared on the website for the Office of Information and Regulatory Affairs during the week of January 4, 2016. The Section submitted comments concerning draft Form 8971 and related matters in respect of sections 1014(f) and 6035 on January 25, 2016.

On March 4, 2016, Proposed Regulations (REG-127923-15) (hereinafter the “Proposed Regulations”) were published in the Federal Register. The Proposed Regulations also cross-reference Temporary Regulations published in the same Federal Register.
The time period set forth under section 6035(a)(3) for filing the Information Return and Statement(s) is 30 days after the filing of the Estate Tax Return. In Notice 2015-57, the Service extended the statutory filing deadline until February 29, 2016. Subsequently, the Service issued Notice 2016-19, which extended the statutory filing deadline until March 31, 2016, and Notice 2016-27, which further extended the statutory filing deadline until June 30, 2016.

In the March 4, 2016, Notice of Proposed Rulemaking, Treasury solicited public comments on all aspects of the proposed rules regarding basis consistency.

The Section, in conjunction with its EGT and FIT Committees, respectfully requests further guidance and/or clarification on the following eight items contained in or referenced by the Proposed Regulations:

1. Clarification to transactions removing assets from the scope of the basis consistency rules;
2. Reporting on subsequent transfers;
3. Basis assigned to after-discovered or omitted property;
4. Funding issues involving community property;
5. The executor’s obligation to disclose all remaining estate assets to a beneficiary when the executor has not determined what property will be used to satisfy that beneficiary’s interest in the estate;
6. Treatment of tangible personal property;
7. The person to whom a Statement should be issued if the probate estate pours into a revocable trust or if qualified terminable interest property is includible in the Gross Estate; and
8. The obligation for supplemental Estate Tax Returns where the original return was required to be, and was, filed, prior to July 31, 2015.
9. Remedy for beneficiaries who disagree with the value reported by the executor.

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ABA SECTION OF TAXATION

COMMENTS ON CONSISTENCY IN BASIS RULES

A. Background and Introduction

Generally, the income tax basis (hereinafter “basis”) of property “in the hands of any person acquiring the property from a decedent or to whom the property passed from a decedent” is the fair market value of the property at the date of the decedent’s death.\(^{12}\) The value reported on an Estate Tax Return is presumed to be correct for purposes of determining the recipient's basis, but the beneficiary has always been able to establish a different date-of-death (or alternate valuation date) value for the property by his or her own analysis and evidence.\(^{13}\)

In its Fiscal Year 2010 revenue proposals (the “Greenbook”), the Obama Administration began a campaign for basis consistency.\(^{14}\) The Administration considered statutory basis consistency necessary because:

\(^{12}\) I.R.C. § 1014(a)(1).

\(^{13}\) Howard Zaritsky, New Law Requires Some Estates and Their Beneficiaries to Use Consistent Valuations, ESTATE PLANNING JOURNAL at 47 (November 2015), and which states, in Endnote 17, the following:

“Treas. Reg. § 1.1014-3(a) (for purposes of Section 1014, “the value of property as of the date of the decedent’s death as appraised for the purpose of the Federal estate tax or the alternate value as appraised for such purpose, whichever is applicable, shall be deemed to be its fair market value”); Rev. Rul. 54-97, 1954-1 C.B. 113 (“the value of the property as determined for the purpose of the Federal estate tax shall be deemed to be its fair market value at the time of acquisition. Except where the taxpayer is estopped by his previous actions or statements, such value is not conclusive but is a presumptive value which may be rebutted by clear and convincing evidence”); Tech. Adv. Memo. 199933001. See also Hawkinson, T.C. Memo 1972-32 PH TCM ¶72032 31 CCH TCM 124 (upholding the validity of Treas. Reg. § 1.1014-3(a), but characterizing it as establishing only an evidentiary presumption). Courts have imposed a duty of consistency where the executor and the beneficiary are the same person or in privity. See Estate of Letts, 109 T.C. 290 (1997) (wife's estate estopped from asserting that trust did not qualify for QTIP treatment); LeFever, 78 AFTR 2d 96-7335 100 F3d 778 96-2 USTC ¶60250 (CA-10, 1996) (taxpayer was the executor of the decedent's estate); Cluck, 105 T.C. 324 (1995) (estoppel applied because the taxpayer's spouse was executor and the spouses had filed joint tax returns for the years at issue); Beltzer, 33 AFTR 2d 74-1173 495 F.2d 211 74-1 USTC ¶9373 (CA-8, 1974) (taxpayer was co-executor of the decedent's estate); Hess, 38 AFTR 2d 76-5429 210 Ct. Cl. 483 537 F.2d 457 76-2 USTC ¶9539 (Ct. Cl., 1976), cert. den. 430 U.S. 931 (1977) (testamentary trust whose trustees were executors of the estate). Courts have not estopped beneficiaries from arguing a different value than that reported on the estate tax return where such a close relationship did not exist. Ford, 5 AFTR 2d 1157 149 Ct. Cl. 558 276 F.2d 17 60-1 USTC ¶9375 (Ct. Cl., 1960) (decedent's minor beneficiaries residing outside of the U.S. were not estopped from arguing a different value because they were not fiduciaries of the decedent's estate and had no knowledge of the decedent's estate tax return); Shook, 52 AFTR 2d 83-5868 713 F.2d 662 83-2 USTC ¶9564 (CA-11, 1983) (estoppel not extended to an estate beneficiary for merely indicating approval over executor's handling of the estate over which the executor had total control and the beneficiary none).

\(^{14}\) General Explanations of the Administration’s Fiscal Year 2010 Revenue Proposals Department, Department of the Treasury, May 2009, p.119.
“Taxpayers should be required to take consistent positions in dealing with the Internal Revenue Service, whether or not principles of privity apply. If the logic underlying the determination of the new basis in property acquired on the death of the owner is that the new basis is the amount used to determine the decedent’s estate tax liability, then the law should require that the same value be used by the recipient, unless that value is in excess of the accurate value. In the case of property transferred on death or by gift during life, often the executor of the estate or the donor, respectively, will be in the best position to ensure that the recipient receives the information that will be necessary to determine the recipient’s basis in the transferred property.”

The Greenbook proposal was carried forward into each subsequent year’s proposals, including those for Fiscal Year 2016.

As stated above, on July 31, 2015, President Obama signed the Act into law, and, in Section 2004 of the Act, new sections 1014(f) and 6035 were enacted. In addition to these sections, the Act also enacted the Penalty Provisions. The EGT and FIT Committees are not submitting any comments with respect to the Penalty Provisions, so no analysis of these provisions is contained in these Comments.

(1) **New Section 1014(f)**

Section 1014(f) provides rules requiring that the basis of certain property acquired from a decedent may not exceed the value of that property as finally determined for federal estate tax purposes, or, if not finally determined, the value of that property as reported on an Information Return made under section 6035. However, this basis consistency rule will apply only to property whose inclusion in the Gross Estate increases the estate tax liability for the estate.

The value of property is considered to be “finally determined for federal estate tax purposes” if:

1. The value of such property is shown on an Estate Tax Return and such value is not contested by the Secretary within the applicable statute of limitations;
2. The value is specified by the Secretary and such value is not timely contested by the executor of the estate; or

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15 Id.
16 General Explanations of the Administration’s Fiscal Year 2011 Revenue Proposals Department, Department of the Treasury, February 2010, p.122; General Explanations of the Administration’s Fiscal Year 2012 Revenue Proposals Department, Department of the Treasury, February 2011, p.125; General Explanations of the Administration’s Fiscal Year 2013 Revenue Proposals Department, Department of the Treasury, February 2012, p.77; General Explanations of the Administration’s Fiscal Year 2014 Revenue Proposals Department, Department of the Treasury, April 2013, p.140; General Explanations of the Administration’s Fiscal Year 2015 Revenue Proposals Department, Department of the Treasury, March 2014, p.160; and General Explanations of the Administration’s Fiscal Year 2016 Revenue Proposals Department, Department of the Treasury, February 2015, p.195.
17 I.R.C. § (f)(1).
18 I.R.C. § 1014(f)(2).
(3) The value is determined by a court or pursuant to a settlement agreement with the Secretary.\(^{19}\)

(2) **New Section 6035**

While new section 1014(f) establishes the basis of property impacting the estate tax liability, new section 6035 imposes the reporting requirements for the value of property included in a decedent’s Gross Estate. These two new statutes appear to reflect two distinct regimes – whereas section 1014(f) establishes the basis for certain estate tax generating assets, the reporting requirements of section 6035 cover a broader spectrum of assets.

Under section 6035(a)(1), the executor of any estate required to file a return under section 6018(a) (i.e., an Estate Tax Return) must furnish, to both the Secretary and the person acquiring any interest in property included in the decedent’s Gross Estate, a statement identifying the value of each interest in such property as reported on such return and such other information with respect to such interest as the Secretary may prescribe (i.e., a “Statement”).

Under section 6035(a)(2), each person required to file a return under section 6018(b) (the “Beneficiary Estate Tax Return”)\(^{20}\) must furnish an Information Return to the Secretary and a Statement to each other person who holds a legal or beneficial interest in the property to which such return relates.\(^{21}\)

Under section 6035(a)(3), each required Information Return and Statement must be furnished at such time as the Secretary may prescribe, but in no case at a time later than the earlier of, (1) the date which is 30 days after the date on which the Estate Tax Return was required to be filed (including extensions, if any), or (2) the date which is 30 days after the date such return is filed.\(^{22}\) Section 6035(a)(3) also requires that if there is any adjustment to the information supplied on the Information Return and Statement(s) after filing, a supplemental Statement(s) with the adjusted information shall be filed no later than 30 days after such adjustment is made.\(^{23}\)

Finally, section 6035(b) grants the Secretary authority to issue such regulations as are necessary to carry out the provisions of section 6035, including specific references to regulations for applying section 6035 to property where no Estate Tax Return is required to be filed and situations where the surviving joint tenant or other recipient may have better information regarding the basis or fair market value of the property.\(^{24}\)

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19 I.R.C. § 1014(f)(3).
20 Unless specifically stated otherwise, all subsequent references to “Estate Tax Return” shall also include a “Beneficiary Estate Tax Return.”
21 Note that a return under section 6018(b) is required to be filed in circumstances where the decedent’s executor is unable to make a complete return of the Gross Estate because he, she or it is unable to ascertain the nature of certain property not in his, her or its possession that is includible in the decedent’s Gross Estate, and, subsequently, upon notice from the Secretary, the person in possession of such property must file a return with the Service reporting such property.
24 I.R.C. § 6035(b).
B. Proposed Regulations

The Section acknowledges that certain concerns with the new basis consistency regime stem from the plain language of the new statutory provisions themselves, and that Treasury and the Service may lack authority to address certain potential shortcomings in the statutes. The Section further notes that the Proposed Regulations reflect Treasury’s and the Service’s efforts to make the new statutory provisions function more effectively and efficiently, taking into account the practical application of these rules. The Section appreciates the thought and effort given to the Proposed Regulations and hopes that these Comments will assist Treasury and the Service to enhance the overall operation of the new statutory scheme.

(1) Proposed Regulation Section 1.1014-10

Treasury’s explanation and guidance with respect to section 1014(f) is found in new Proposed Regulation section 1.1014-10.

Proposed Regulation section 1.1014-10(a) discusses the basis consistency requirement. In Paragraph (1), the general rule set forth in the statute is repeated, i.e., that the basis is equal to the property’s final value as determined under Proposed Regulation section 1.1014-10(c). Paragraph (1) further provides that the basis must be applied whenever a taxable event occurs with respect to the property that results in the recognition of gain or loss for federal income tax purposes. In Paragraph (2), Treasury explains that the final value may be adjusted due to the operation of other provisions of the Code, such as gain recognized by the decedent’s estate or trust upon distribution of property, post-death capital improvements and depreciation, and post-death adjustments to the basis of an interest in a partnership or S corporation.

Proposed Regulation section 1.1014-10(b) discusses the property subject to the basis consistency requirement. Paragraph (1) reiterates the statutory requirement that it be property includible in the Gross Estate that generates an estate tax liability. Paragraph (2) provides for exclusions to the general rule, which are (a) property that qualifies for the marital or charitable deduction (on the theory that they do not generate an estate tax liability) and (b) tangible personal property for which an appraisal is not required under Regulation section 20.2031-6(b). Paragraph (3) states that if an estate tax liability is generated after the application of all available credits, the basis consistency requirement applies to the entire Gross Estate (other than the excluded property) because all such property is treated as generating an estate tax liability. Likewise, if no estate tax is generated after the application of all available credits, the entire Gross Estate is excluded from the basis consistency requirement.

Proposed Regulation section 1.1014-10(c) determines the “final value.” Paragraph (1) reiterates the statutory provisions in that “final value” is (a) the value reported on the Estate Tax Return after the applicable statute of limitations passes without adjustment from the Service, (b) if the Service challenges a value and the taxpayer does not challenge this value, the Service’s value after the applicable statute of limitations passes, (c) the value as determined by agreement between the Service and the taxpayer, and (d) the value as determined by a court once the court’s decision becomes final. Paragraph (2) expands on the “finality” issue by providing that even if the value is not final, the recipient may not claim a basis in excess of the value as reported on the Statement, and if the final value differs from that filed value, the taxpayer may not rely on the value as reported on the Statement.
Proposed Regulation section 1.1014-10(c)(3) introduces a new concept into the analysis, which applies to “after-discovered” or “omitted” property. Paragraph (3) is divided into two sections – where an Estate Tax Return was filed and where no Estate Tax Return was filed. If an Estate Tax Return was filed and if the statute of limitations is still open, the final value is determined under Regulation section 1.1014-10(c)(1) or (2), but only if the executor files a supplemental Estate Tax Return prior to the close of the applicable statute of limitations. If no such supplemental Estate Tax Return is filed, the final value is zero. If no Estate Tax Return was filed, and if the inclusion of the after-discovered or omitted asset would have generated an estate tax liability, then the final value of all property described in Proposed Regulation section 1.1014-10(b) is zero until the final value can be determined under Regulation sections 1.1014-10(c)(1) or (2).

Proposed Regulation section 1.1014-1(d) defines the executor as the “statutory executor” from section 2203 and also any person required to file a Beneficiary Estate Tax Return.

(2) Proposed Regulation Section 1.6035-1

Treasury’s explanation and guidance with respect to new section 6035 is found in new Proposed Regulation section 1.6035-1. Proposed Regulation section 1.6035-1(a) sets forth the basics of the Information Return and the Statement.

In Paragraph (1), an executor required to file an Estate Tax Return must file an Information Return to report the value of certain property included in the Gross Estate, which must include the final value of such property under Proposed Regulation section 1.1014-10(c). The executor is also required to furnish a Statement(s) to each beneficiary who has (or will) acquire, whether from the decedent or by reason of the death of the decedent, property reported on the Information Return. Paragraph (1) continues by providing that if any changes occur in the final value of such property, the executor must file a supplemental Information Return and Statements.

Paragraph (2) provides an exception to the general rule by stating that it only applies to an executor who is required to file an Estate Tax Return. This is clarified to exclude any Estate Tax Return filed on behalf of an estate below the filing threshold solely for portability purposes, for allocation of the generation-skipping transfer tax or for protective purposes.

Proposed Regulation section 1.6035-1(b) discusses the property for which reporting is required. The general rule is that all property reported or required to be reported on an Estate Tax Return is subject to the reporting requirement, which includes any property whose basis is determined in whole or in part by reference to that property (meaning a like-kind exchange or involuntary conversion). This also includes only the decedent’s one-half of community property. There are four exceptions to the reporting rule: cash (other than currency with numismatic value), income in respect of a decedent, tangible personal property for which an appraisal is not required under Regulation section 20.2031-6, and property sold, exchanged or otherwise disposed of by the estate in a transaction in which capital gain or loss is recognized.

Proposed Regulation section 1.6035-1(c) defines “beneficiary.” Paragraph (1) expands on what is meant by a “beneficiary.” “Beneficiary” includes the life tenant of a life estate, the remainderman who would receive property if the life tenant died immediately after the decedent, and a beneficiary of a contingent interest. Paragraph (2) provides that if the beneficiary is a trust
or another estate, the executor must send the Statement(s) to the trustee or executor of the other estate, and if the beneficiary is a business entity, the Statement(s) must be provided to the entity. Paragraph (3) discusses what happens if the executor has not determined which beneficiary receives which property. Under this instance, the executor must include in the Statement(s) all property that could be used to satisfy the beneficiary’s interest. Once the executor has determined the exact property to be used to satisfy the beneficiary’s interest, the executor may, but is not required to, file a supplemental Information Return. Finally, Paragraph (4) provides guidance as to what happens when a beneficiary cannot be located.

Proposed Regulation section 1.6035-1(d) discusses the due dates, which provides that the executor must file and furnish the Information Return and Statement(s) by the later of, (1) the date that is 30 days after the due date of the Estate Tax Return, including extensions, and (2) 30 days after the date on which the Estate Tax Return is filed with the Service. However, if the Estate Tax Return was required to be filed on or before July 31, 2015 but is not actually filed until after July 31, 2015, the reporting requirements apply to that return.

Proposed Regulation section 1.6035-1(e) contains the provisions regarding the duty to supplement. Such changes requiring a supplement include after-discovered or omitted assets, a change in the value pursuant to examination or litigation, or a change in the identity of the beneficiary to whom property is distributable.

Proposed Regulation section 1.6035-1(f) discusses subsequent transfers of reported property. In general, if reported property is transferred to a “related transferee” in a transaction in which the related transferee determines his/her basis by reference to the transferor’s basis, then the related transferee is subject to the reporting requirements. A “related transferee” is any member of the transferor’s family (as defined in section 2704(c)(2)), any controlled entity and any trust of which the transferor is deemed to be the owner for income tax purposes.

Proposed Regulation section 1.6035-1(g) provides definitions for certain terms such as “executor,” “information return” and “statement.”

C. Requests for Further Guidance and/or Clarification

The Section respectfully requests additional guidance from Treasury on the following areas within the Proposed Regulations.

(1) Clarification to transactions removing assets from the scope of the basis consistency rules

(a) Summary of Provision

Proposed Regulation section 1.1014-10(a)(1), in describing the general rule regarding the basis consistency rules, provides that the basis consistency rules continue to apply until the particular asset is “sold, exchanged, or otherwise disposed of in one or more transactions that result in the recognition of gain or loss for Federal income tax purposes.” (Emphasis added.) Further, Proposed Regulation section 1.6035-1(b)(1)(iv) provides that the reporting requirement under section 6035 does not apply to a transaction where estate property is “sold, exchanged, or otherwise disposed of (and therefore not distributed to a beneficiary) by the estate in a
transaction in which capital gain or loss is recognized.” (Emphasis added.) Such “gain or loss” provisions are referred to in this letter as the “Gain or Loss Provisions.”

(b) What if no “Gain or Loss” is recognized?

It appears that the Government’s intention is to exclude from the basis consistency rules any asset that is subject to a capital transaction. In most situations, a capital transaction will result in either gain or loss. However, when the capital transaction involves an estate, especially with a difficult to value asset, it is possible that the capital transaction will not result in a capital gain or loss because the sales price may be the date of death value of the asset, which would be the estate’s cost basis pursuant to section 1014(a) and section 1014(b)(9). In such an acquisition, the purchaser’s cost basis ordinarily would be determined by the purchaser’s purchase price. However, under Proposed Regulation section 1.1014-10(a)(1), because the estate’s basis is determined as a result of the Gross Estate includibility of the asset, the purchaser’s basis literally would still be subject to the basis consistency rules since, factually, no gain or loss was recognized in the transaction. If the purchaser disposes of the asset in a non-capital transaction, it would appear that the purchaser is still subject to the Disclosure Requirement.

We do not believe that this was the intention of the Gain or Loss Provisions. Rather, we infer that, under both Proposed Regulation section 1.1014-10(a)(1) and Proposed Regulation section 1.6035-1(b)(1)(iv), the exception is intended to be for an asset subject to a capital transaction. For this reason, we request that Treasury and the Service clarify the provisions of the Gain or Loss Provisions to also exclude the sale by an estate of a capital asset for no gain or loss.

(2) Reporting on subsequent transfers

(a) Summary of Provision

In developing the Proposed Regulations, one issue that Treasury and the Service attempted to address is the subsequent transfer of property received as a result of the death of a decedent. For example, assume that P dies, survived by C, and P’s will provides that all assets are distributable to C. One of the assets included in P’s Gross Estate and subsequently distributed to C is 100 shares of AT&T common stock. Two years after receipt of the 100 shares of AT&T common stock, C gifts such stock to her son, GS. Because C’s basis is created as a result of the inclusion of such stock in P’s Gross Estate, and since GS’s basis is a carryover basis from C, GS’s basis is technically determined as a result of the inclusion of such stock in P’s Gross Estate. Treasury and the Service, therefore, wanted to implement a mechanism to track the basis of any asset where the current basis of such asset can be traced back to gross estate inclusion, so, through Proposed Regulation section 1.6035-1(f), it imposed the Disclosure Requirement as to any such subsequent transfers (referred to in this letter as the “Subsequent Transfer Rule”).

The Subsequent Transfer Rule imposes a filing requirement on the recipient of certain property from a decedent (referred to as the “Transferor”). If, as a result of a subsequent transfer of certain estate property by the Transferor, the transferee of such property (the “Transferee”) (a) is a “related transferee” as to the Transferor, and (b) determines his/her basis, in whole or in part, by reference to the Transferor’s basis, the Transferor becomes subject to the Disclosure Requirement and is required to file and provide a “supplemental Statement” (which, as
implemented on Form 8971, is a “supplemental Schedule A”) to both the Service and the Transferee.

Proposed Regulation section 1.6035-1(f) defines “related transferee” as any one of (a) any member of the Transferor’s “family” as defined in section 2704(c)(2) (the “Family”), (b) a “controlled entity,” defined as corporation or other entity in which the Transferor and members of Transferor’s Family, whether directly or indirectly, have control within the meaning of sections 2701(b)(2)(A) or (B), and (c) any trust of which the Transferor is deemed an owner for income tax purposes.

If the Transferor is subject to the Disclosure Requirement, the Transferor must file the supplemental Statement(s) with the Service, and furnish them to the beneficiary, within 30 days of the transfer.

(b) Clarification of the definition of “related transferee” where the Transferor is a trust and the Transferee is an individual beneficiary

At the May 7, 2016 meeting of the FIT Committee during the Section’s May 2016 Meeting in Washington, DC, a panel presentation was held on the topic of the Proposed Regulations (the “ABA Panel Presentation”). Participating in the ABA Panel Presentation were two private practice practitioners and two representatives from Treasury and the Service. During the presentation, the Treasury and Service representatives stated that the purpose for the “related transferee” rule was two-fold: first, intra-family transactions are more likely to be abusive, and second, from an administrative standpoint, it is easier to require reporting for only intra-family transactions as opposed to all taxable transactions.

On the premise that the Government’s focus is on related party transactions, consider the standard testamentary provision where property passes in trust for one or more of the decedent’s descendants. While such trust can be a Transferor for purposes of the Subsequent Transfer Rule, it does not appear that any individual beneficiary of such trust would meet the definition of a Transferee. Under this analysis, distributions from a trust that received property from an estate, and for which no gain or loss is recognized on the trust’s distribution, would not be subject to the Subsequent Transfer Rule. Such a conclusion is counter-intuitive in light of the intention to track assets where the basis was determined by Gross Estate includibility.

We respectfully request guidance from Treasury and the Service as to whether distributions of property from a Trustee to the beneficiaries of such trust are included within the Subsequent Transfer Rule, which would subject the Trustee to the Disclosure Requirement.

If Treasury and the Service intended to subject such trust distributions to the Subsequent Transfer Rule, they should consider invoking the “attribution rule” of section 2701(e)(3). For this purpose, section 2701(e)(3) would deem the trust beneficiary to indirectly own the trust’s holdings. Such indirect ownership could be incorporated into the definition of “related transferee” under Proposed Regulation section 1.6035-1(f). Taken further, if Treasury and the Service wish to only capture related-party transactions, a test could be implemented whereby the “related transferee” rule would apply if more than one-half of the beneficiaries are “related or subordinate parties” (as defined in section 672(c)) as to the decedent or the trust’s grantor. In such case, the Transferor would file the supplemental Statement(s) with the Service and furnish them to the trust’s beneficiaries.
(c) Guidance regarding transfers to grantor versus non-grantor trusts

For purposes of the Subsequent Transfer Rule, a Transferee includes a trust of which the Transferor is a deemed owner for federal income tax purposes. Thus, if a Transferor receives estate assets and subsequently gifts (or perhaps sells) such property to an irrevocable grantor trust as to such Transferor, the Transferor would be subject to the Disclosure Requirement. However, a non-grantor trust is not included within the definition of a Transferee and therefore distributions from a non-grantor trust appear not to be subject to Subsequent Transfer Rule.

As stated above, during the ABA Panel Presentation, Treasury and Service representatives stated that this distinction exists for administrative convenience and because there is more potential abuse with intra-family transactions. Basis information contained in the required supplemental Statement(s), however, would only be relevant to determining the Transferor’s taxable income and, although the supplemental Schedule A would be delivered to the trustee of an irrevocable grantor trust, the disclosure is, for federal income tax purposes, made from the Transferor to the Transferor. Therefore, no immediate purpose is achieved by subjecting a transfer to an irrevocable grantor trust to the Subsequent Transfer Rule and the Disclosure Requirement.

Contrast that example with a transfer to an irrevocable non-grantor trust. As non-grantor trusts are considered to be separate taxpayers, it would seem that basis information would be extremely useful and helpful for the trustee of such trusts. However, the Subsequent Transfer Rule does not appear to apply under this scenario because an irrevocable non-grantor trust is not included within the definition of a Transferee. It is important to note that this result appears to be contrary to the language of the preamble of Proposed Regulation section 1.6035-1, which specifically references a gift to a complex (non-grantor) trust as an instance where taxpayers may circumvent the purpose of the statute.25

Accordingly, we respectfully request guidance as to whether transfers of estate property by a Transferor to a non-grantor trust should be included within the definition of “related transferee” for purposes of Proposed Regulation section 1.6035-1(f).

(d) Notice of subsequent transfer Disclosure Requirement

If the Subsequent Transfer Rule is included in the final version of Proposed Regulation section 1.6035-1, the instructions to the Form 8971 and Schedule A, and perhaps the form itself, should be revised to alert beneficiaries of the application of the Subsequent Transfer Rule and Disclosure Requirement if they become Transferors.

(e) Authority to impose the Subsequent Transfer Rule

We respect the Government’s desire for efficient administration as a tax policy objective, and its thorough examination of the issues. We further acknowledge that Treasury and the Service only issue regulations based on their understanding of the regulatory reach and would

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25 Paragraph 13 of the Preamble provides, in part, “The Treasury Department and the IRS are concerned, however, that opportunities may exist in some circumstances for the recipient of such reporting to circumvent the purpose of the statute (for example, by making a gift of the property to a complex trust for the benefit of the transferor’s family).”
not deliberately propose regulations that extend beyond that authority. Nevertheless, we would note that arguments have been raised that the authority under section 6035(b), as specifically described in section 6035(b)(2), does not extend to the creation of the Subsequent Transfer Rule. Further, it has been suggested that, if the Subsequent Transfer Rule is included in the final regulations, that challenges to such authority may result. The Section is not advocating a position on this issue, but rather believes that a reference to the discussion is warranted in its submission so that Treasury and the Service have a better understanding of the issue.

The express regulatory grant language is contained in section 6035(b), which states as follows:

(b) Regulations. The Secretary shall prescribe such regulations as necessary to carry out this section including regulations relating to –

1. the application of § 6035 with regard to a situation where no [Estate Tax Return] is required to be filed, and

2. situations in which the surviving joint tenant or other recipient may have better information regarding the basis or fair market value of the property.

The Preamble to Proposed Regulation section 1.6035-1 points to section 6035(b)(2) as the rationale for the Subsequent Transfer Rule. The potential inconsistency is, as illustrated below, that section 6035(b)(2) does not appear to relate to the underlying issues causing the creation of the Subsequent Transfer Rule.

Section 6035(b)(2) appears to relate to the initial assembly of information from surviving joint tenants or other recipients for the purpose of obtaining information regarding estate tax value, which some might say is akin to the requirement for the recipient of property to file a Beneficiary Estate Tax Return under section 6018(b). Stated differently, section 6035(b)(2) appears to refer to the gathering of information at the time of the decedent’s date of death for purposes of completing the Estate Tax Return so that the estate tax value of an asset can be determined. For example, suppose that a decedent’s estate is being administered in New York. Further suppose that the decedent’s Gross Estate includes an interest in an oil-producing parcel of real property located in a remote section of Alaska, and that the decedent held title to such interest as joint tenants with right of survivorship with another individual. Finally, suppose that the surviving joint tenant lives on or near the property and is the manager and chief operator of the facilities located on the property. In this instance, perhaps Congress was asking for further guidance as to how to apply the reporting rules to a valuation where the surviving joint tenant, and not the executor, has much better information and the capability of determining the actual value of the interest for federal estate tax purposes. Treasury and the Service indirectly acknowledge the link between section 6035(b)(2) and section 6018(b), by the definition of “executor” in Proposed Regulation section 1.6035-1(g)(1), which includes the meaning of

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26 See generally Chevron USA v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984). In addition, several commenters on the List Serve for the American College of Trust and Estate Counsel (“ACTEC”) have raised the “regulatory authority” issue, and this issue was also raised to the Treasury and Service representatives during the “Q&A” portion of the ABA Panel Presentation.
“executor” from section 2203 and any other person required under section 6018(b) to file a Beneficiary Estate Tax Return.

Contrast this to the Subsequent Transfer Rule, which is not concerned with the determination of the initial estate tax value but is related to transmitting information regarding a subsequent transfer of an asset by a recipient of property where the recipient’s cost basis has its origins from Gross Estate includibility. Since section 6035(b)(2) appears to relate to the determination of value upon the decedent’s death, the question is whether the Subsequent Transfer Rule, while well intentioned, is outside the scope of the regulatory authority described in section 6035(b)(2).

(3) Basis assigned to after-discovered or omitted property

(a) Summary of Provision

Proposed Regulation section 1.1014-10(c)(3) sets forth special rules that apply when property is discovered after an Estate Tax Return is filed, property is omitted from an Estate Tax Return, or no Estate Tax Return is filed and property is discovered that would have generated or increased federal estate taxes. Proposed Regulation section 1.1014-10(c)(3)(i) applies when an Estate Tax Return is filed; Proposed Regulation section 1.1014-10(c)(3)(ii) applies when an Estate Tax Return is not filed.

Pursuant to Proposed Regulation section 1.1014-10(c)(3)(i), if property described in Proposed Regulation section 1.1014-10(b)(1) is discovered after the Estate Tax Return is filed or otherwise omitted from the Estate Tax Return, the final value of such property depends on whether an initial or supplemental Estate Tax Return is filed prior to the expiration of the period of limitation on assessment of the tax imposed on the estate by chapter 11 (the "limitations period"). Such limitations period is generally three years from the date that the Estate Tax Return is filed.27

If an Estate Tax Return is filed before the limitations period expires, the final value of the after-discovered or omitted property is determined under the general rules of Proposed Regulation sections 1.1014-10(c)(1) or (2).28

If, however, an Estate Tax Return is not filed before the limitations period expires, the final value of the after-discovered or omitted property is zero.29 Proposed Regulation section 1.1014-10(e), Example 3 illustrates the application of this special rule.

Pursuant to Proposed Regulation section 1.1014-10(c)(3)(ii), if no Estate Tax Return has been filed and property described in Proposed Regulation section 1.1014-10(b) is later discovered that would have generated or increased federal estate taxes, then the final value of such property is zero until an Estate Tax Return is filed that includes the property or the Service determines a value for the property.

27 See I.R.C. § 6501(a).
For purposes of the remaining paragraphs of this Section 2, the special rules described above shall be referred to as the "zero basis rule."

(b) Clarification of terminology

Proposed Regulation section 1.1014-10(c)(3) attempts to use one set of defined terms to encompass scenarios where an Estate Tax Return was filed and where one was not filed. While the intentions are evident, the use of specific terminology is problematic in explaining this rule.

The preamble to Proposed Regulation section 1.1014-10(c)(3)(i) provides as follows:

“(i) Return under section 6018 filed. In the event property described in paragraph (b)(1) of this section is discovered after the estate tax return under section 6018 has been filed or otherwise is omitted from that return (after-discovered or omitted property), the final value of that property is determined under section (c)(3)(i)(A) or (B) of this section.”

In other words, this regulation defines “after-discovered or omitted property” as certain property that was discovered after the Estate Tax Return was filed or otherwise omitted from the filed Estate Tax Return.

Proposed Regulation section 1.1014-10(c)(3)(ii) attempts to adopt this phraseology into a situation where a Federal Estate Tax Return was not filed. The intentions are clear – to adopt the zero basis rule unless a Federal Estate Tax Return is thereafter filed. The problem is that, in using the phrase “after-discovered or omitted property,” the definition implies that an Estate Tax Return was previously filed. This results in an inconsistency between the intended concept and terms used to define the concept, so from a purely technical standpoint, Proposed Regulation section 1.1014-10(c)(3)(ii) cannot apply to “after-discovered or omitted property.”

We respectfully request that, if the zero basis rule is to apply to situations where an Estate Tax Return has not been filed, Treasury and the Service modify Proposed Regulation section 1.1014-10(c)(3)(ii) to better identify the property to which the zero basis rule is to apply.

(c) Clarify exceptions to zero basis rule

It is unclear how Proposed Regulation section 1.1014-10(b), which describes property subject to the basis consistency requirement, interacts with Proposed Regulation section 1.1014-10(c)(3), which sets forth the zero basis rule. This is because Proposed Regulation section 1.1014-10(c)(3)(i) refers to "property described in paragraph (b)(1) of this section" and Proposed Regulation section 1.1014-10(c)(3)(ii) refers to "all property described in paragraph (b) of this section includible in the gross estate."

A reasonable interpretation of the Proposed Regulations suggests that if after-discovered or omitted property is not subject to the basis consistency requirement, it is not subject to the zero basis rule. In other words, if such property does not generate or increase federal estate taxes, or if such property is tangible personal property for which an appraisal is not required

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30 See Prop. Reg. § 1.1014-10(b)(1).
under Regulation section 20.2031-6(b) (i.e., property having a marked artistic or intrinsic value of $3,000 or less), then such property would not be subject to the zero basis rule. Nevertheless, the language of Proposed Regulation section 1.1014-10(c)(3) leaves open the argument that when the zero basis rule applies, all property included in a decedent's gross estate is subject to such rule. The reason for this is that the reference to “all property described in paragraph (b) of this section” encompasses not only the assets ordinarily subject to the consistent basis rules, i.e., the (b)(1) assets, but also encompasses the specifically excluded assets in (b)(2).

To address this uncertainty, we respectfully request that Treasury and the Service amend the Proposed Regulations to clarify that the zero basis rule does not apply to the following property, regardless of whether an Estate Tax Return has been filed or is required to be filed as a result of such property:

(i)  **Property that does not generate or increase federal estate tax liability**

Pursuant to Proposed Regulation section 1.1014-10(b)(1), the zero basis rule should not apply to after-discovered or omitted property that does not generate or increase federal estate taxes. If property would not be subject to the basis consistency requirement if it were reported on a timely filed Estate Tax Return, it should not be subject to the zero basis rule simply because such property was omitted or discovered after the Estate Tax Return was filed. Similarly, if no Estate Tax Return is required to be filed even after including the later-discovered property, then such property should not be subject to the basis consistency requirement or the zero basis rule. In accordance with Proposed Regulation section 1.1014-10(b)(2), this first exception would apply to any property that does not generate or increase federal estate taxes, including property that qualifies for an estate tax charitable or marital deduction under sections 2055, 2056, or 2056A. The intent behind this exception is clear – Treasury and the Service are not concerned with such assets because they do not add to the estate tax liability. In such a case, the filing of an Estate Tax Return has no relevance to the premise for the exception.

(ii)  **Tangible personal property with a value of $3,000 or less**

Pursuant to Proposed Regulation section 1.1014-10(b)(2) and Regulation section 20.2031-6(b), the zero basis rule should not apply to tangible personal property having a marked or intrinsic value of $3,000 or less. This would ease the administrative application of the zero basis rule and is generally consistent with the overall approach of the Proposed Regulations.

(iii)  **Cash**

Cash, in the sense of U.S. currency held by a U.S. taxpayer, routinely is considered to have a tax basis equal to its stated value. However, under a literal reading of the Proposed Regulations, if cash is an after-discovered or omitted asset, because all such assets would be assigned a zero basis, cash could be assigned a zero basis. In light of the conventional treatment of cash, however, this clearly seems unintended. Further, it is inconsistent with Proposed

31 See Prop. Reg. § 1.1014-10(b)(2).
32 Bittker & Eustice, *Federal Income Taxation of Corporations and Shareholders*, par. 10.11 at n. “In effect, U.S. currency always has a basis equal to its face amount, hence its disposition does not result in recognition of gain or loss.” Compare the rules under §§ 985-989, which do not allow for gain or loss in respect of a functional currency, which for a U.S. taxpayer generally is the U.S. dollar.
Regulation section 1.6035-1(b)(1)(i), which specifically excepts "cash (other than a coin collection or other coins or bills with numismatic value)" from the Form 8971 reporting requirement.

(iv) Authority for the zero basis rule for after-discovered or omitted property for which an Estate Tax Return has not been filed

Some have expressed reservations whether the zero basis rule in section 1014(f) can be applied to after-discovered or omitted property for which an Estate Tax Return has not been filed, as proposed in the regime described in Proposed Regulation section 1.1014-10(c)(3)(i)(B). In an effort to give voice to those arguments and while acknowledging that Treasury and the Service believe that they have regulatory authority, we have included some discussion of those arguments.

Section 1014(f)(1) provides that:

“[t]he basis of any property to which subsection (a) applies shall not exceed – (A) in the case of property the final value of which has been determined for purposes of the tax imposed by chapter 11 on the estate of such decedent, such value, and (B) in the case of property not described in subparagraph (A) and with respect to which a statement has been furnished under section 6035(a) identifying the value of such property, such value.”

Section 1014(f)(1)(A) references the “final value” of property which “has been determined for purposes of the tax imposed by chapter 11 on the estate of such decedent …” Under section 1014(f)(3), the term “determined” refers to a value shown on a return filed under section 6018. As a commentator at the ABA Panel Presentation suggested, this language referencing the value as “determined for purposes of the tax imposed by chapter 11” does not appear to apply to after-discovered or omitted property for which an Estate Tax Return has not been filed, because such value has in fact not been “determined.”

Furthermore, section 1014(f) does not say that the basis of such property “shall” be determined as provided in section 1014(f). It merely states that the basis “shall not exceed” said value and does not reference “as reported on [an Estate Tax Return].” As a result, it appears that section 1014(f) technically applies only if an Estate Tax Return is filed. To say that section 1014(f) is the exclusive mechanism for determining the basis of such after-discovered or omitted property seems too broad based on the language of the statute.

(d) Permit the filing of a supplemental Estate Tax Return after the limitations period to avoid the zero basis rule

Putting aside the question of whether there is authority for the Proposed Regulations with respect to after-discovered or omitted property for which an Estate Tax Return has not been filed, we respectfully request a mechanism for dealing with after-discovered or omitted property for which an Estate Tax Return has not been filed after the period of limitations has expired.
The Proposed Regulations apply the zero basis rule in three situations:

(i) **Situation 1** – An Estate Tax Return is filed and the executor discovers property that was reported on the Estate Tax Return before the limitations period expires;\(^{33}\)

(ii) **Situation 2** – An Estate Tax Return is filed and the executor discovers property that was reported on the Estate Tax Return after the limitations period expires;\(^{34}\) and

(iii) **Situation 3** – No Estate Tax Return is filed and the executor discovers property that would have generated or increased federal estate taxes.\(^{35}\)

In Situations 1 and 3, an executor may avoid application of the zero basis rule to after-discovered property by filing an initial or supplemental Estate Tax Return.\(^{36}\) By contrast, in Situation 2, an executor cannot avoid application of the zero basis rule to after-discovered property, even if the Estate Tax Return was filed in good faith and the executor would otherwise file a supplemental Estate Tax Return but for the expiration of the limitations period.\(^{37}\)

We respectfully request that Treasury and the Service amend Proposed Regulation section 1.1014-10(c)(3)(i) to provide that the final value of after-discovered or omitted property shall be determined in accordance with Proposed Regulation sections 1.1014-10(c)(1) and (2), if the executor files a supplemental Estate Tax Return regardless of whether the limitations period has expired. This could be structured so that the executor could be permitted to take corrective action within 90 days after the later of (a) discovery of the asset by the executor, or (b) the final determination of any action compelling an executor to file for corrective action (i.e., to take into account any instance where an executor has been compelled by a court to file an amended Form 8971, if for example an executor has breached its fiduciary duty).

There is recent precedent for the use of regulatory authority to provide for the limited opening of a statute of limitations in furtherance of a new tax concept. Consider that Regulation section 20.2010-3(d) provides that in determining the applicable exclusion amount of a deceased individual (the “Surviving Spouse”), if the applicable exclusion amount includes any deceased spousal unused exclusion amount (“DSUE Amount”) received from a predeceased spouse (the “Deceased Spouse”), the Service may re-open the Deceased Spouse’s Estate Tax Return for the sole purpose of calculating the DSUE Amount passing to the Surviving Spouse. A similar approach could be adopted with respect to after-discovered or omitted property after the passage of the statute of limitations.

Furthermore, we respectfully request that Treasury and the Service amend Proposed Regulation section 1.1014-10(c)(3)(i)(B) to provide that the filing of a supplemental Estate Tax Return after the limitations period expires shall only reopen such limitations period with respect

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\(^{34}\) Prop. Reg. § 1.1014-10(c)(3)(i)(B).

\(^{35}\) Prop. Reg. § 1.1014-10(c)(3)(ii).


to the after-discovered or omitted property, and not with respect to all other property included on
the prior Estate Tax Return.

(4) Funding issues involving community property

(a) Summary of Provision

Proposed Regulation section 1.6035-1(b) provides that the property to be reported on an
Information Return and Statement(s) is all property included in the decedent’s gross estate
(subject to the four exceptions referenced above in Section B(2) of this letter).38

If a married decedent owns an asset as community property at the time of the decedent’s
death, then under section 1014(a) and section 1014(b)(6), if at least one-half of the entire
community property interest in the asset is includible in determining the value of the decedent's
Gross Estate, a basis adjustment is made to both the decedent’s community property interest in
the asset and the surviving spouse’s community property interest. For estate tax reporting
purposes, practices vary as to the reporting of community property. One option is to report the
full value of the asset on the estate tax return and then deduct the surviving spouse’s community
property interest (the “Full Value Approach”). Proponents of the Full Value Approach note that
by including the full value but then taking the appropriate deduction for the surviving spouse’s
interest, the Estate Tax Return includes the evidence that at least one-half of the entire
community property interest in the asset was includible in determining the value of the
decedent's Gross Estate. Another option is to only report the decedent’s community property
interest in the asset on the Estate Tax Return (the “Decedent’s Interest Approach”).

Another source of confusion is that Proposed Regulation section 1.6035-1(b) and
section 6035 are silent as to a common estate administration technique in which the community
property of a married couple is not distributed proportionally but is distributed in the discretion
of the fiduciary to satisfy the decedent’s bequests, as authorized under applicable state law
and/or the governing instrument of the decedent’s estate plan.

Given that the purpose of the Information Return and Statement(s) is to inform both the
Service and the beneficiary of the basis of an asset received from an estate, confusion exists as to
how the reporting requirements intersect with the aspects of community property described
above.

(b) Reporting the full value of community property assets

For those adopting the Full Value Approach, there may be confusion regarding the proper
completion of the Information Return and Statement(s). While the Estate Tax Return reports
the full value of the community property asset reported and subsequently deducts the surviving
spouse’s interest, the Information Return and Statement(s) technically would only be required to
report the deceased spouse’s community property interest as that would be the only “interest
passing by reason of the death of the decedent” (Prop. Treas. Reg. §1.6035-1(a)). Therefore,

38 (1) Cash; (2) income in respect of a decedent; (3) tangible personal property for which an appraisal is not required
under Regulation section 20.2031-6; and (4) property sold, exchanged or otherwise disposed of by the estate in a
transaction in which capital gain or loss is recognized. Supra p. 8.
there would be no reporting (other than on the Estate Tax Return) referencing the increased basis of the surviving spouse’s interest in the community property asset.

We respectfully request that Treasury and the Service include a provision in Proposed Regulation section 1.6035-1 to address the reporting of the surviving spouse’s interest in a community property asset if the decedent’s estate adopts the Full Value Approach. In addition, the Information Return and Statement(s) should be modified to take into account the surviving spouse’s interest in a community property asset.

(c) Reporting only the deceased spouse’s community property interest

It would appear that there is less confusion for those estates adopting the Decedent’s Interest Approach, as the Estate Tax Return and the Information Return and Statement(s) all would report the same community property interest, i.e., that belonging to the decedent spouse. However, the same issue with the Full Value Approach exists with the Decedent’s Interest Approach in that there is no reporting requirement for the adjustment to the basis of the surviving spouse’s interest in said community property.

We respectfully request that Treasury and the Service include a provision in Proposed Regulation section 1.6035-1 to address the reporting of the surviving spouse’s interest in a community property asset where the decedent’s estate adopts the Decedent’s Interest Approach. In addition, the Information Return and Statement(s) should be modified to take into account the surviving spouse’s interest in a community property asset.

(d) Non-pro-rata distribution of community property

In the administration of certain estates comprised of community property, it is not possible to equally divide each asset for community property purposes. For example, assume that D dies a resident of CP, which is a community property state, with S as her surviving spouse. D’s estate consists of two assets titled in D’s sole name and both of which are community property – a checking account with $400,000 and a 49% interest in a limited liability company with a date of death value of $1,600,000. D’s will provides for a specific cash bequest of $300,000 to her brother, B, with the balance of the estate passing outright to S. Because D’s assets are community property assets, the value of D’s estate is $1,000,000. In administering D’s estate, D’s executor must first satisfy the cash bequest to B. Yet, B’s bequest is $300,000 and D only has $200,000 of cash (D’s community property interest in the checking account). Under the laws of CP, D’s executor is authorized to satisfy B’s bequest with $300,000 in cash, and, subsequently, the $100,000 of S’s community property portion of the checking account will be credited against D’s share of the limited liability company interest, so that S’s community property share of the LLC interest is not $800,000 (which is one-half of the date of death value of $1,600,000), but rather $900,000 (the one-half interest of $800,000 plus the $100,000 credited on account of the use of S’s share of the checking account to satisfy B’s bequest).

As stated above, Proposed Regulation section 1.6035-1(b) and section 6035 are silent as to the non-pro-rata distribution of community property. Although a surviving spouse’s community property interest is an asset that may be used to satisfy a decedent’s bequest, if such property is not property that is included in the decedent’s Gross Estate within the meaning of section 6035, then it would not be included on an Information Return and Statement(s). Conversely, if a surviving spouse’s community property interest is an asset used to satisfy a
decedent’s bequest, then a corresponding value of the decedent’s community property interests will be allocated outright to the surviving spouse, which could result in a reporting of the spouse as an outright recipient, even though the terms of the decedent’s estate plan do not provide for any distribution of assets outright to the surviving spouse. If only the decedent’s community property interest is reported on the Information Return and Statement(s) and a non-pro rata distribution occurs, this may cause significant confusion because it will appear that certain bequests are underfunded (because the spouse’s community interest used to complete funding is not reflected) and/or that the surviving spouse received assets under the estate plan that the surviving spouse was not entitled to receive.

We respectfully request guidance under Proposed Regulation section 1.6035-1(b) as to the proper reporting of community property subject to non-pro-rata distributions. We recommend that the Information Return and Statement(s) (or the Regulations themselves) expressly address how to report the non-pro-rata funding of a decedent's bequests with community property.

(5) The executor’s obligation to disclose all remaining estate assets to a beneficiary when the executor has not determined what property will be used to satisfy that beneficiary’s interest in the estate

(a) Summary of Provision

Proposed Regulation section 1.6035-1(c)(3) provides that if, by the Information Return due date, the executor has not determined what property will be used to satisfy the interest of a beneficiary, the executor must report on the Statement(s) that is sent to the beneficiary “all of the property that the executor could use to satisfy that beneficiary’s interest” (the “All Property Requirement”).

Rarely, if ever, does an executor fully distribute an estate prior to the date that is 30 days after the filing of the Estate Tax Return. In many instances, little or no assets will have been distributed to the residuary beneficiaries.

For the beneficiaries of the residuary estate, they share in the balance of the estate and, under most states’ laws, they are the persons (or entities, as the case may be) to whom the executor must account and seek release and discharge (especially if the administration occurs within a revocable trust). Thus, because they are entitled to receive the report of all assets from the beginning to the end of the administration, it seems logical to invoke the All Property Requirement.

However, is not uncommon for a decedent to make a small bequest to certain individuals, such as a friend, caretaker or key employee. In many estates, there may be legitimate reasons, such as litigation, as to why no bequests could be satisfied by the time of the deadline for filing the Information Return and Statement(s). Under the Proposed Regulations, however, there is no distinction between the category of the beneficiary (i.e., cash recipient, pre-residuary, residuary, etc.) and the All Property Requirement.

(b) All Property Requirement could violate the decedent’s privacy

The imposition of the All Property Requirement raises concerns about maintaining the decedent’s privacy. Many individuals do not want all of their beneficiaries to know the extent of
their assets. As described above, an individual may provide for a friend or remote family member as a token of remembrance with no expectation that such friend or remote family member may one day receive a full report of all of the individual’s assets.

One practice that is used to avoid this outcome is for a decedent to prepare multiple revocable trusts so as to avoid giving all of their beneficiaries access to information about their entire estate. For example, a decedent might create one revocable trust that makes small bequests to friends and employees, and a second revocable trust that disposes of the bulk of his or her assets among family and other chosen beneficiaries. Yet, not all clients wish to engage in the added complexity of multiple trusts and ensuring that the smaller trust is always funded with the appropriate level of assets to satisfy those smaller bequests.

In order to maintain the decedent’s privacy, we respectfully request that Treasury and the Service consider modifying the All Property Requirement to ensure a decedent’s privacy as to his/her estate assets.

(c) All Property Requirement circumvents existing state and federal tax law

For state law purposes, as well as federal tax purposes, not every beneficiary is entitled to receive information about the decedent’s estate (or revocable trust). As stated above, in most instances it is only the residuary beneficiaries who are to receive all financial information as they are the persons or entities from whom, at the end of the administration, the executor or trustee seeks to be released. In some states, such as Florida, upon a reasonable request, an interested person shall receive from the executor information about the estate and its administration.39

For federal tax purposes, usually only those beneficiaries who may be affected by a position taken on a tax return are entitled to receive copies of such return.40

Suppose the total property passing under a decedent’s will is $100,000,000, and a family friend is named as the recipient of a $5,000 bequest. Should that beneficiary be treated the same as a residuary beneficiary? Under both state law and federal tax law principles set forth above, the answer should be “no” because nothing pertaining to the administration of the estate would affect the bequest (except if the estate is in litigation where the friend’s bequest is in danger of being eliminated). However, as a result of the Proposed Regulations, if, for whatever reason, the friend’s bequest is unpaid at the due date of the Information Return and Statement, the friend must receive a statement of all assets subject to the reporting requirement. This is a troublesome byproduct of the Proposed Regulations.

We respectfully request that Treasury and the Service modify the All Property Requirement so that it complements existing state and federal laws regarding disclosure of assets to beneficiaries.

39 See, e.g., Florida Probate Rule 5.341, “Estate Information.”
40 See, e.g., PLR 201005052 (Jan. 5, 2010), where the Service acknowledges that under section 6103(e)(3)(B), beneficiaries are entitled to see the return that the executor filed if their interest would be affected by the return.
(d) Additional and unnecessary burden placed on executors

The All Property Requirement may be burdensome for executors and confusing for beneficiaries. If an executor has not distributed the estate’s assets by the Information Return due date, the executor will need to furnish a list of all of the estate’s assets to all of the beneficiaries. This list could be extremely long, and could cause a beneficiary to misunderstand what assets he or she is entitled to receive. Such a list could also create conflict among beneficiaries, as each beneficiary will be able to assess what assets are not ultimately distributed to him or her.

We respectfully request guidance from Treasury and the Service as to a more manageable methodology and procedure for satisfying the reporting requirements when an estate has not been fully distributed by the due date of the Information Return and Statement(s).

(6) Treatment of tangible personal property

(a) Summary of Provision

The Proposed Regulations add an exclusion to the basis consistency regime and to the basis reporting regime for certain tangible personal property.

Proposed Regulation section 1.1014-10(b)(2) excludes from the definition of property subject to the basis consistency requirement “tangible personal property for which an appraisal is not required under § 20.2031-6(b).”

Similarly, Proposed Regulation section 1.6035-1(b)(1)(iii) excepts from the basis reporting requirements “tangible personal property for which an appraisal is not required under § 20.2031-6(b).” Example 1 under Proposed Regulation section 1.6035-1(b)(2) details an estate where an executor attaches a room by room itemization of a decedent’s household and personal effects, whereby all of the articles are named specifically. In each room a number of articles (none of which has a value in excess of $100) are grouped and a value is provided for each named article. Three specific items have a value in excess of $3,000 (and a qualified appraisal for these items is attached to the Estate Tax Return), and only these items are subject to the reporting requirement regime.

Regulations section 20.2031-6(b) provides that “if there are included among the household and personal effects articles having marked artistic or intrinsic value of a total value in excess of $3,000 (e.g., jewelry, furs, silverware, paintings, etchings, engravings, antiques, books, statuary, vases, oriental rugs, coin or stamp collections), the appraisal of an expert or experts, under oath, shall be filed with the return.” (Emphasis added.)

(b) Should each item of tangible personal property be considered separately?

Based on Example 1 under Proposed Regulation section 1.6035-1(b)(2), it appears that each item of tangible personal property is to be considered separately for purposes of the basis reporting regime, such that only each item of tangible personal property valued at over $3,000 is required to be reported.

However, the language of Regulation section 20.2031-6(b) discusses “total value.” This seems inconsistent with Example 1 from Proposed Regulation section 1.6035-1(b)(2).
We respectfully request clarification that this language does not require an executor to aggregate different items of tangible personal property for purposes of the basis consistency regime and the basis reporting regime. We believe that this is the intended result of the Proposed Regulations.

(c) If each item of tangible personal property is to be considered separately, how should an executor report an item over $3,000 on Form 8971 and Schedule A?

Most appraisals of tangible personal property in one location are included in a single appraisal attached to an Estate Tax Return. As a result, Schedule F of the Estate Tax Return may report “Tangible Personal Property located in decedent’s house, valued at $X.” This will often include items over $3,000, as well as items under $3,000 and smaller items grouped together.

Schedule A of Form 8971 requires that the executor indicate the item number where reported on the decedent’s Estate Tax Return.

We respectfully request clarification whether the executor is required to do more than refer to the item number for the appraisal of the entire house. For example, does the appraisal need to be attached to the Schedule A or must a separate schedule be prepared showing the appraisal of each item over $3,000?

Furthermore, we respectfully request that Treasury and the Service specify how the executor should deal with groups of items contained in an appraisal. For example, if a “Group of 48 Gold Knick-Knacks” is valued at $6,000, is the group required to be reported (since presumably no single item is worth over $3,000)?

(d) Is a partial interest worth less than $3,000 required to be reported on Schedule A of Form 8971?

Decedents frequently devise their tangible personal property to their children, in equal shares. Confusion occurs as to specific items and group bequests. For example, how would the executor report an item with a value of, for example, $5,000, that is “distributed” 50% to one child and 50% to another child? The child’s interest in such item is under the $3,000 threshold, although the value of the entire item is above the $3,000 threshold. Is that an item to be reported?

We respectfully request further guidance in Proposed Regulation section 1.6035-1 as to class gifts of tangible personal property in which the item exceeds the $3,000 threshold but the amount received by each beneficiary is less than the $3,000 threshold.

(e) Is the executor required to provide a copy of the appraisal to a beneficiary who receives a Schedule A?

We request that Treasury and the Service specify whether the executor has a duty to provide a copy of the tangible personal property appraisal (or modified schedules therefrom) to a beneficiary receiving a Schedule A that contains items of tangible personal property. If some form of appraisal is required to be sent to the beneficiary, we respectfully request clarification as to exactly what must to be included in such appraisal.
(7) To whom should a Statement(s) be issued if the probate estate pours into a revocable trust or if qualified terminable interest property is includible in the Gross Estate?

(a) Summary of Provision

Proposed Regulation section 1.6035-1(a)(1) provides, in pertinent part, that an executor “must furnish a Statement … to each beneficiary who has (or will) acquire, whether from the decedent or by reason of the death of the decedent, property reported on the Information Return to identify the property the beneficiary is to receive and to report the value of that property and other information prescribed by the Statement and instructions thereto.” (Emphasis added.)

Proposed Regulation section 1.6035-1(c)(2) provides that, if a beneficiary is a trust or another estate, the executor must furnish a Schedule A to the trustee or executor.

The two cited provisions appear to conflict with each other as to two instances: (1) when the probate estate pours over into a revocable trust, and (2) when the Gross Estate includes section 2044 property, i.e., qualified terminable interest property (“QTIP”) held in trust. In both instances, the question is who is the “beneficiary” for Statement purposes – the trust or the beneficiaries of the trust?

(b) Clarification in accordance with Treasury’s and the Service’s probable intentions

Since the issuance of the Proposed Regulations, this has been a troublesome issue. At the 2016 ACTEC National Meeting, held from March 16-20, 2016 in Las Vegas, Nevada, during the Fiduciary Income Tax Committee meeting on Friday March 18, 2016, this issue garnered much discussion, with the presentation panel concluding that a Statement(s) must only be given to the trustee and not the underlying beneficiaries. This was more in line with the provisions of Proposed Regulation section 1.6035-1(c)(2). Therefore, based on this conclusion, in the pour-over will example described above, the executor would only have one Statement as part of the Information Return and that Statement would be sent to the trustee of the revocable trust. Further, in the QTIP trust example, the executor would only be required to send a Statement to the trustee of the QTIP trust. If this were the proper interpretation, then, considering the analysis from earlier in these Comments, the trustee would not be subject to the Disclosure Requirement on transfers to the trust beneficiaries because such beneficiaries would not be “related transferees,” which would thwart the goal of tracking assets whose basis is determined by Gross Estate inclusion.

This conclusion, however, seems inconsistent with the apparent intent of section 6035, which is stated in Proposed Regulation section 1.6035-1(a)(1) as requiring, in part, that a Statement be given to persons receiving property as a result of the death of the decedent. Taken alone and without application of Proposed Regulation section 1.6035-1(c)(2), in the pour-over will example, the executor would provide Statements to each of the underlying beneficiaries of the revocable trust because they are the persons receiving property as a result of the death of the decedent. In the QTIP trust example, the executor would provide Statements to the QTIP Trust’s

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41 Supra Section C(2)(a), p. 10-11.
underlying beneficiaries because they are the persons receiving property as a result of the death of the decedent.

When considering the intentions behind the basis consistency rules, it would appear that reliance on the provisions of Proposed Regulation section 1.6035-1(c)(2) are misplaced in terms of who receives the Statements. If the goal is to provide Statements to those receiving property as a result of the death of the decedent, the trustees of a revocable trust and a QTIP trust are likely not the recipients intended by Treasury.

In addition to the above analysis, at the ABA Panel Presentation, this issue was raised and the Treasury and Service representatives on the panel stated that they believed that Statements should be served on the underlying beneficiaries and not just the trustees.

Therefore, we respectfully request that Proposed Regulation section 1.6035-1, and, in particular Proposed Regulation section 1.6035-1(c)(2), be modified to clarify the intent that the Executors serve Statements on the underlying beneficiaries of a revocable trust into which the probate estate is poured into, as well as the underlying beneficiaries of a QTIP trust included in the Gross Estate under section 2044.

(8) Obligations for supplemental Estate Tax Returns where the original return was required to be, and was, filed, prior to July 31, 2015

(a) Summary of the Provision

Public Law 114-41, which enacted section 6035, states in subsection (d) that the basis Disclosure Requirement applies to property “with respect to which an estate tax return is filed after the date of the enactment [July 31, 2015] (emphasis added).” In other words, if the due date of an Estate Tax Return is prior on or before July 31, 2015, but the filing date is extended so that such Estate Tax Return is filed after July 31, 2015, the estate is subject to the basis consistency rules.

One particular issue that is not answered concerns a supplemental Estate Tax Return where the original return was due and filed prior to July 31, 2015 but for completeness or accuracy it becomes necessary to file a supplemental Estate Tax Return after July 31, 2015 (the “Subsequent Filing”). In this instance, is the Subsequent Filing subject to the basis consistency rules?

(b) What is a “return” and is a supplemental Estate Tax Return a “return” for purposes of section 6035?

On its face, the relevant provision appears to broadly subject Subsequent Filings to the requirements of section 6035 even if the initial Estate Tax Return was due and filed prior to or on such date.

It is worth asking, however, how a “return” should be defined for this purpose.
The Service has viewed supplemental returns as equivalent to amended returns. There is no general Code definition of “return.” The term appears to be defined as appropriate for the context. For example, in the rules governing nondisclosure of confidential taxpayer information, a “return” includes any “amendment or supplement to a return.” Further, for purposes of the tax return preparer rules, a return includes “an amended or adjusted return.”

On the other hand, it may be argued that for purposes of timing, a supplemental return is not a new “return” but rather is an amendment to an existing return. Under this approach, a Subsequent Filing is simply an addendum to the original Estate Tax Return, which was filed on or prior to July 31, 2015, and the Subsequent Filing would not be subject to the basis consistency rules.

The leading case on the effect of amended or supplemental returns on timing matters is the United States Supreme Court opinion in Badaracco v. Commissioner. The focus of Badaracco was the effect of an amended return on the statute of limitations. The Supreme Court concluded that the “return” described in section 6501(c)(1) was the original, and not the amended return. The Court confirmed that “the Code does not explicitly provide for or require the filing of an amended return” and that such returns are “a creature of administrative origin and grace.” Further, in SCA 1998-024, in relying on a long line of cases, rulings, and regulations, the Office of Chief Counsel stated, with respect to a timely-filed amended return, that the statute of limitations commenced with the filing of the initial return.

On this basis, we believe that, for purposes of the effective date of section 6035, a supplemental Estate Tax Return should be disregarded as a separate “return” because it refers back to the original return and as a result, a Subsequent Filing should not be subject to the reporting requirements of section 6035.

We respectfully request clarification confirming that the basis Disclosure Requirements of section 6035 (i) apply solely to estates filing an initial Estate Tax Return after July 31, 2015, and (ii) exclude a supplemental Estate Tax Return filed after such date if the initial Estate Tax Return was filed on or prior to that date.

(9) Remedy for beneficiaries who disagree with value reported by the executor

Paragraph 16 of the Preamble to the Proposed Regulations states that there is no process for beneficiaries to challenge the value reported by the executor under Federal law. It further states that the beneficiary’s rights with regard to the estate tax valuation of property are to be governed by applicable state law.

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43 I.R.C. § 6103(b)(1).
44 Reg. § 301.7701-15(b)(4)(i).
46 Id. at 393.
A question was posed at the ABA Panel Presentation as to why Treasury and the Service could not implement a procedure whereby a beneficiary would have a right to contest a value assigned to a specific asset prior to the final determination of the value for federal estate tax purposes. The Treasury and Service representatives on the panel both responded that this was a state law issue and outside of federal authority, but that reference to the issue should be included in comments to the proposed regulations. On that basis, the Section provides the following discussion, acknowledging that a deeper analysis of the issue may be appropriate.

While it is true that internal challenges to valuation are technically a state law issue, with the implementation of the basis consistency statutes, the consistency requirement imposed under federal law can affect the state law treatment. Prior to the basis consistency rules, a recipient of property from an estate could adopt a different cost basis if the recipient believed that the asset’s final value as determined for federal estate tax purposes was incorrect. Under the basis consistency rules, the recipient must use the asset’s final value (as defined in Proposed Regulation section 1.1014-10(c)). Mandating the recipient’s cost basis can have an effect on state law aspects of the decedent’s estate and the further use of the property by the recipient. For example, under § 503 of the Uniform Principal and Income Act, a trustee is authorized to establish a reserve for depreciation. “Depreciation” is a federal tax concept, allowable as a deduction under section 167, which sets the value for depreciation purposes as the adjusted basis for gain or loss as determined under section 1011. Section 1011 provides that the adjusted basis for gain or loss is the basis determined under section 1012 and other applicable sections of this subchapter, which would include section 1014. Therefore, for state law purposes, the basis consistency rules now fix the starting value for a depreciation reserve. This interaction between federal and state law might have the effect of allowing a federal “challenge” procedure for a beneficiary to contest a value to be given effect for state law purposes.

We respectfully request that Treasury and the Service consider creating a process for beneficiaries to challenge the value reported by the executor on a Form 8971. As a commentator at the ABA Panel Presentation stated, “appraisals are an art, not a science.” It is easy to see how an executor may receive an appraisal with a value that is very different than another appraiser’s work, and this difference can have a tremendous impact on a beneficiary. There also may be competing objectives for an executor representing the estate, whereby there may be an incentive to receive a lower appraisal for estate tax purposes.

While there may be state law remedies available to a beneficiary if they bring an action against the executor in a court of law, litigation is expensive and time-consuming. Further, the litigation may not conclude until after the statute of limitations for the Disclosure Requirement has passed, thereby preventing the filing of a supplemental Information Return and Statement(s).

For these reasons, we request that Treasury and the Service consider implementing a non-adversarial recourse procedure available to beneficiaries. One suggestion is that within 90 days after receiving an Information Statement, beneficiaries could be afforded an opportunity to submit their own appraisal if they believe that the appraisal submitted by the executor is not accurate.

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48 Section 503, Transfers from Income to Principal for Depreciation, Uniform Principal and Income Act (2008).
We also note that this or any other procedure as may be considered by Treasury and the Service may be outside the scope of regulatory authority under section 6035(b) (see the analysis on this part in Section C(2)(e) of these Comments). Nevertheless, as stated above, this brief description of the issue is presented for review by Treasury and the Service at the request of the Treasury and Service representatives at the ABA Panel Presentation.