

## **Estate And Gift Tax Exam**

**Fall 2021**

### **Issue Outline**

#### **Question 1**

The full value of the five years' worth of annuity payments due to Finn is included in Emma's gross estate under section 2039 of the Code. The value is determined as of the date of Emma's death (or the alternate valuation date, if elected).

Nothing is included in Emma's gross estate with respect to Pops's trust. Emma's income interest expires when she dies, and her power of appointment is not a general power of appointment.

The fair market value of the corpus of the late husband's trust is includible in Emma's gross estate, but only if the trust was subject to a QTIP election by the late husband's executor under section 2056(b)(7) of the Code. In that case, the corpus is included in Emma's gross estate under section 2044. The trust meets the requirements for the election; Emma had a qualifying income interest for life. The value is determined as of the date of Emma's death (or the alternate valuation date, if elected). Absent a QTIP election, none of the trust corpus is includible in Emma's gross estate, because her interest in the trust terminated.

The taxes paid by the estate are deductible under sections 2053 and 2058 of the Code, except for the income taxes on the income received by Rose. IRC § 2053(c)(1)(B).

The full proceeds of the life insurance policy are includible in Emma's estate because they are payable to Rose as executor of Emma's estate.

Because of Emma's substantial gifts, the unified credit may not be much of a factor in computing her gift and estate taxes. Emma may have had some unused unified credit "ported" from her late husband. There are no GST tax consequences to Dana or Dana's estate from the transactions discussed in this question.

#### **Question 2**

The establishment of the Family Trust is a completed gift of the remainder to Bob, but an incomplete gift of the income interest to Ada. Dana has the right to divert the income by invading the corpus for Bob. The fact that Dana must get Taj's consent to invade the corpus does not render the gift to Ada complete, because Taj does not have an adverse interest.

Bob's interest is not a present interest and thus is ineligible for the annual exclusion. Dana and Sam may elect to split the gift under section 2513 of the Code, in which case it is treated as being made one half by each of them.

Bob's remainder interest is valued using the tables promulgated under section 7520 of the Code based on Ada's life expectancy at the time of the establishment of the trust. The section 7520 valuation factor is multiplied by the fair market value of the Corp stock at the time of the transfer of the stock in trust.

The fair market value of the Corp stock, which starts with the market price of the stock (indicating a fair market value of \$10 million) may be subject to value adjustments. Specifically, the value may be subject to a discount for blockage because of the large size of the block. On the other hand, the 30 percent block may possess effective control of Corp, warranting a control premium.

As the trustee of the Family Trust distributes income to Ada, the gift of that income by Dana to Ada becomes complete. These gifts are eligible for the annual exclusion.

When Dana dies, the entire value of the corpus of the Family Trust is included in her gross estate under Section 2036(a)(2) because her invasion power gives her the right to determine who gets the income from the trust. The fair market value of the Corp stock, which starts with the market price of the stock (indicating a fair market value of \$12 million) may be subject to a blockage discount and control premium, as discussed earlier. The value is determined as of the date of death (or if elected, the alternate valuation date).

The gift of the remainder previously given to Bob will not be an adjusted taxable gift in calculating Dana's estate tax under section 2001(b) of the Code. In effect, the estate will get credit for the gift tax paid on Bob's remainder.

The 800 shares of XYZ stock are included in Dana's gross estate under Section 2033. Their value is determined as of the date of death (or if elected, the alternate valuation date).

The value of the XYZ stock transferred to the Marital Trust is eligible for the estate tax marital deduction because Sam has the right to all of the income payable annually, and Sam has the power to appoint the entire corpus to Sam's estate at death. IRC § 2056(b)(5). The value of the XYZ stock transferred to the university is eligible for the estate tax charitable contribution deduction.

However, the value of the XYZ stock is likely to be greater for inclusion purposes than for deduction purposes. In the gross estate, the stock is valued as a controlling block (80 percent). In contrast, for deduction purposes, the deductible transfers are valued separately, as noncontrolling blocks (40 percent each). Through a control premium or minority discount, or both, some of the value of the XYZ stock is likely to be taxable to the estate.

For both inclusion and deduction purposes, however, the stock is likely to be valued taking into account a discount for lack of marketability.

Any gift taxes paid on gifts Dana made within three years prior to her death are included in her gross estate under section 2035(b) of the Code. The estate may be eligible for the alternate valuation date election.

There are no GST tax consequences to Dana or Dana's estate from the transactions discussed in this question.

### **Question 3**

Joy's transfer to the trust for Gary is a completed gift. The trustee's power to accumulate income does not prevent the gift from being complete. It does, however, render the gift ineligible for the annual exclusion. The amount of the gift is the fair market value of the property at the

time it is transferred to the trust. Joy and her estate may be entitled to the unified credit for gift and estate tax purposes, respectively.

When Joy dies, the corpus of the trust is not includible in Joy's gross estate under section 2036(a)(2) of the Code. The power to control the timing of distributions to a sole beneficiary is a power described in section 2036(a)(2). *Estate of O'Connor*. However, the trustee's powers to accumulate income and distribute corpus are not imputed to Joy because she could not name herself as trustee in case of a vacancy.

Joy's transfer of funds to the joint checking account is not a completed gift because it may be revoked by Joy's withdrawing funds from the account. Whenever Maya withdraws money from the account, a completed gift from Joy to Maya, potentially reduced by the annual exclusion, takes place. When Joy dies, the balance in the account is included in her gross estate under section 2040 of the Code.

The creation of the tenancy in common was a gift of a one-half interest from Joy to Zia when Blackacre was acquired. Joy's retained one-half undivided interest in Blackacre is included in her gross estate under section 2033. In valuing each half-interest, a discount may be available for the shared control that comes with a co-tenancy.

Joy's transfer to the trust she established for Gary is a direct skip, because the trust is a skip person. No nonskip persons have any interest in the trust, and a skip person is the only beneficiary. Joy is liable for the GST tax, subject to any allocation of her GST tax exemption.

If Maya's disclaimer is a qualified disclaimer, the transfer of the interest in Blackacre is treated as being made by Joy to Gary, and thus is a direct skip. Joy's estate is liable for the GST tax, subject to any allocation of her GST tax exemption.

The estate may be eligible for the alternate valuation date and special use valuation elections.