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CPA's basic guide to proven estate planning strategies to protect client wealth

David Thomas III

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A CPA's Basic Guide to Proven Estate Planning Strategies to Protect Client Wealth

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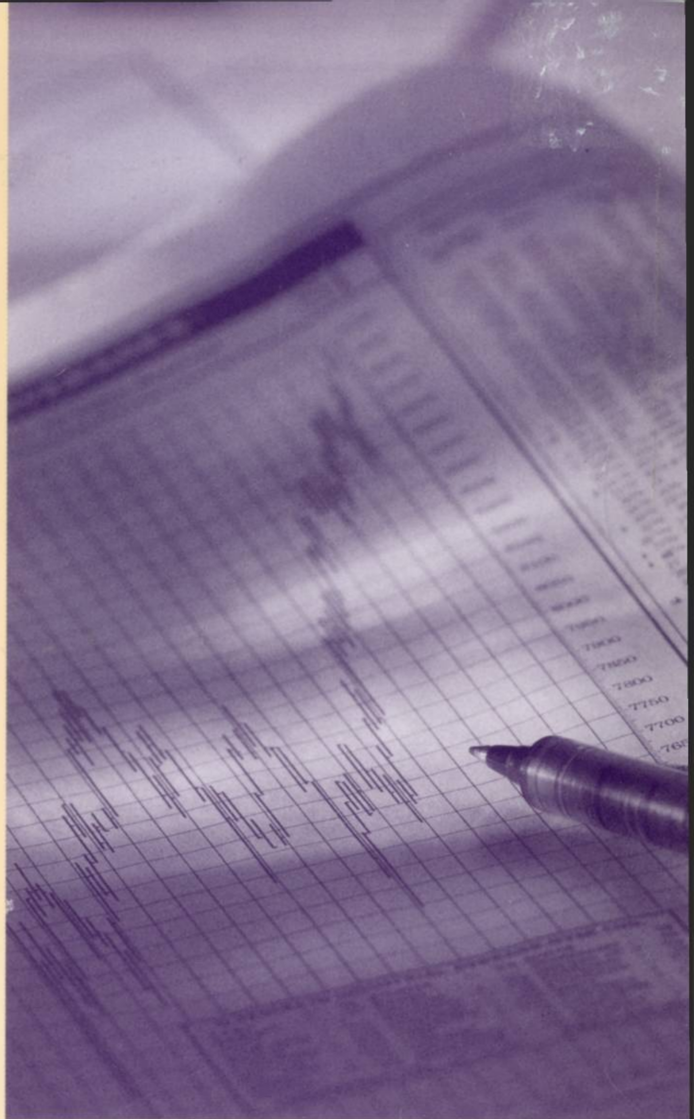

A CPA's Basic Guide to Proven Estate Planning Strategies to Protect Client Wealth

David Thomas, III, Esq.
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AICPA

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

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FOREWORD

This book provides a strong foundation for accountants who want to assist their clients with their estate plans. It is designed for practitioners with some experience in estate planning and emphasizes the integration of their client's estate plans with their lifestyle, which may include gifting strategies and business plans.

David Thomas, III, Esq. of Sherman & Howard, Denver, CO, and Margaret L. Toal, Esq., of Hutchinson Black and Cook, Boulder, CO, have written an informative and practical book. I would also like to thank Julia B. Fisher, Esq. of Erskine, Wolfson, Gibbon and Fisher, Esqs., Philadelphia, PA, who served as a technical reviewer of the course on which this book is based.

Linda Prentice Cohen, Publisher
Professional Publications and Technology Products

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Chapter 1

Tax Rules

FEDERAL ESTATE TAX

The federal estate tax is a tax imposed on the transfer of the taxable estate of every person who is a citizen or resident of the United States upon death.

DEFINITION OF ESTATE

General Definition

The federal estate tax is a graduated tax and it is imposed on the net fair market value of the deceased person's estate. This includes not only the probate estate but also non-probate assets such as life insurance, pension and retirement assets, and property owned in joint tenancy. The effective rates begin at 37% and increase to 55% (§2001).

The probate estate is the property which is administered by the state probate court process for the payment of administrative expenses and for the distribution of property to creditors and to beneficiaries of the decedent. The distribution of probate property is controlled by the decedent's will, or if none, by the state laws of intestacy and by the probate laws of the state or states in which the probate estate is administered. Probate property may include real property (land, buildings) or personal property (stocks, bonds, etc.).

Unified Credit

The federal estate tax is imposed after the application of the unified credit. The credit permits a person to transfer a certain amount tax free. Under the Taxpayer Relief Act of 1997, the amount of the unified credit is being increased each year in steps. The estate tax is integrated with taxes on lifetime giving.

- The estate tax is imposed upon not only the amount of the taxable estate, but also the amount of adjusted taxable gifts which have been made during the decedent's lifetime.

Adjusted taxable gifts are gifts made by the decedent after December 31, 1976, other than gifts which are includable in the gross estate of the decedent. There are exclusions from taxable gifts and these will be discussed below. The applicable credit amount is applied both to adjusted taxable gifts which are made during lifetime and the taxable estate which passes at death.

TABLE A — Unified Rate Schedule

Column A Taxable amount over	Column B Taxable amount not over	Column C Tax on amount in Column A	Column D Rate of tax on excess over amount in Column A
			(Percent)
0	$10,000	0	18
$10,000	20,000	$1,800	20
20,000	40,000	3,800	22
40,000	60,000	8,200	24
60,000	80,000	13,000	26
80,000	100,000	18,200	28
100,000	150,000	23,800	30
150,000	250,000	38,800	32
250,000	500,000	70,800	34
500,000	750,000	155,800	37
750,000	1,000,000	248,300	39
1,000,000	1,250,000	345,800	41
1,250,000	1,500,000	448,300	43
1,500,000	2,000,000	555,800	45
2,000,000	2,500,000	780,800	49
2,500,000	3,000,000	1,025,800	53
3,000,000	. . . .	1,290,000	55

For estates between $10 million and $21,040,000, there is a 5% surcharge.

The liability for the payment of the estate tax is imposed on the executor (also known as personal representative in many states) or administrator of the estate (§2002). The taxable estate, for estate tax purposes, includes assets which are titled in the decedent's name, retirement benefits, life insurance and other interests such as revocable transfers, transfers with a retained interest, joint tenancy property, community property, property subject to a general power of appointment, and certain transfers of interests made within three years of death.

Revocable Transfers

If, on the date of death, the decedent alone, or in conjunction with another person, retained the power to alter, amend, revoke or terminate a transfer of property, then that property is included in the gross estate of the transferor for estate tax purposes. Also included in the gross estate is any property to which the decedent has such power but is relinquished of within three years of his death (§2038).

The rules on revocable transfers are one reason that property placed in a revocable living trust, for example, is included in the decedent's estate.

Transfers of Retained Interests

The gross estate includes the value of all property (to the extent of an interest of the decedent in the property) of which the decedent has made a transfer by trust or otherwise but has retained a life estate, an interest for any period which is not ascertainable without reference to death, or an interest for any period which does not in fact end before death.

The interest would be for the possession or enjoyment of, or right to income from the property, or the right, either alone or in conjunction with another person, to designate the persons who shall possess or enjoy the property or the income. The retention of the right to vote directly or indirectly the shares of stock of a controlled corporation is considered retention of enjoyment of transferred property.

A controlled corporation is one which, at the time of transfer of the property or during a three-year period ending on the date of the decedent's death, the decedent owned (with the application of §318) or had the right, alone or in conjunction with another person, to vote stock possessing at least 20% of the total combined voting power of all classes of stock. The relinquishment of voting rights is treated as a transfer of property made by the decedent (§2036).

EXAMPLE 1-1:

- George "gives" 1000 shares of General Motors stock to his daughter, Sally, but George retains the right to the dividends each year.
- When George dies, the value of the General Motors stock will be included in his taxable estate.
- Why? - because he retained the right to income from the property.

EXAMPLE 1-2:

- Hank transfers a $100,000 investment account into trust for his granddaughter, Molly. Hank is the trustee.
- The trust provides for the distribution of income and principal, in the trustee's discretion, for Molly's health, support, and education. Hank retains no right to income or principal. The transfer is irrevocable.
- When Hank dies, the trust estate will be included in Hank's taxable estate because he retains the right to designate when Molly will benefit from the trust.

EXAMPLE 1-3:

- Roberta transfers certain valuable paintings to her son, Malcolm. She makes the transfer of legal title by a valid bill of sale. Roberta keeps the paintings on the walls in her home.
- When Roberta dies, the paintings will be included in her taxable estate because she retained the enjoyment of the property.

Joint Tenancy Property

Property which is owned in joint tenancy with right of survivorship passes automatically to the surviving joint tenant. It does not pass under the will. This type of ownership is in contrast to property owned as tenants in common. A decedent's interest in property owned as a tenant in common does not pass automatically to the surviving tenant or tenants but rather is subject to disposition under the decedent's will.

Property which is owned in joint tenancy is also included in the gross estate, at least to the extent of decedent's ownership in the joint tenancy property.

Excluded from the gross estate is the part of the jointly held property which is shown to have originally belonged to the other joint tenant and never to have been received or acquired by the other joint tenant from the decedent for less than adequate and full consideration.

If the property or part of the property has been acquired by the other joint tenant from the decedent, then the value does not include, in the estate, the amount that is proportionate to the consideration given by the other joint tenant. If the property was acquired by gift, bequest, devise, or inheritance,

as a tenancy by the entirety or as joint tenants by the decedent and spouse, then one-half is included in the estate of the first spouse to die. If property is acquired by gift, bequest, devise, or an inheritance by the decedent and a non-spouse as joint tenants with right of survivorship, then the value included is calculated by dividing the value by the number of joint tenants, with right of survivorship, and that fractional part is included in the estate, unless the interests are otherwise fixed by law.

A qualified joint interest is any interest in property held by the decedent and the decedent's spouse as tenants by the entirety or joint tenants with right of survivorship, but only if the decedent and the spouse are the only joint tenants. When spouses own a qualified joint interest, then one-half of the value of the qualified joint interest property is included in the first estate (§2040). Unless sold or otherwise disposed of by the surviving spouse prior to his or her death, the value of all the joint property is included in the surviving spouse's estate.

EXAMPLE 1-4:

- Grandmother has $100,000 in a bank account. She changes the form of ownership so the account is owned in joint tenancy with grandmother, her son, and her daughter.
- Assume son dies. No part of the joint tenancy property will be included in the son's estate for federal estate tax purposes (because he provided no consideration).
- Assume grandmother dies. 100% of the value of the joint tenancy property will be included in grandmother's estate for federal estate tax purposes because she provided 100% of the consideration.

EXAMPLE 1-5:

- Wife earns $150,000 which she transfers to a brokerage account in her own name. Later she transfers the brokerage account into joint tenancy with her husband. Wife and husband are the only two joint tenants.
- Husband dies. The ownership interest of the husband is a qualified joint interest. Accordingly, one-half of the value of the property will be included for federal estate tax purposes in the husband's estate.

General Power of Appointment

A power of appointment is an authority, usually granted in a trust, to designate (to "appoint") which person(s) will be the beneficiaries or successor beneficiaries—that is, who will receive the property, most commonly, upon termination of the trust. A **general** power of appointment is a power which

may be exercised by a person (the "holder" of the power) in favor of himself, his estate, his creditors or the creditors of his estate. Property which is subject to a general power of appointment is included in the taxable estate of the "holder" of the power (§2041).

EXAMPLE 1-6:

- Grandfather establishes a trust for his son. The trust provides that the trust income will be distributed to the son during the son's lifetime and that upon the son's death the son may name, by the son's will, who should receive the trust property.
- The trust imposes no restriction on the persons to whom the son may bequeath (appoint) the property. The power granted in the trust to the son—to name (appoint) the eventual recipients of the property—is a power of appointment.
- Because the power may be exercisable by the son (decedent) without restriction, the power is considered a "general power of appointment" for federal estate tax purposes and therefore the property subject to the power is included in the son's estate.

Excluded from the definition of a general power of appointment is a power to consume, invade or appropriate property for the benefit of the decedent which is limited by an **ascertainable standard**. The ascertainable standard is defined as health, education, support or maintenance (§2041(b)(1)(A)).

EXAMPLE 1-7:

- Husband dies and establishes a Credit Shelter Trust (this type of trust is discussed in Chapters 2 and 3) for his wife, with the wife as trustee.
- If the trust provides that the wife may distribute (appoint) the principal to herself for her general welfare and happiness, then the wife is deemed to have a general power of appointment over the trust property.
- Upon the wife's death, the property in the Credit Shelter Trust will be included in the taxable estate of the wife.
- If, however, the wife's authority as trustee to make distributions of principal to herself only permitted distributions of principal for her health, education, support or maintenance, then the wife would **not** be deemed to have a general power of appointment (because the distributions were subject to the ascertainable standard—health, education, support or maintenance) and the property in the Credit Shelter Trust would **not** be included in the wife's taxable estate at her death.

This is a very important distinction for estate planning purposes. Consider a Credit Shelter Trust established for a surviving wife which permits the trustee to make principal distributions to the wife. There are three key scenarios:

Scenario One

If there is an independent trustee (not the wife) with the authority to make distributions to the wife for her general welfare and happiness (not limited by the ascertainable standard of health, education, support or maintenance), the property is not deemed subject to a general power of appointment and the property in the Credit Shelter Trust will not be subject to estate tax later in the wife's estate.

Scenario Two

If the wife is the trustee and has the authority to make distributions to herself for her general welfare and happiness, then the wife is deemed to have a general power of appointment and the property in the Credit Shelter Trust will be included in the wife's taxable estate.

Scenario Three

If the wife is the trustee but distributions of principal to her are limited to health, education, support or maintenance, the wife is not deemed to have a general power of appointment and the property in the Credit Shelter Trust will not be included in the wife's taxable estate.

Note: If wife can distribute principal to satisfy her legal obligation to support her children, even with ascertainable standards, it is a general power of appointment (Reg. §20.2041-1(c)(i)).

There are numerous rules concerning the possession, exercise, or release of a general power of appointment which must be considered in determining the value of the property subject to the power which is included in the estate for estate tax purposes.

This is important when dealing with larger estates with multigenerational wealth. The rules and limitations to the powers created on or before October 21, 1942, differ greatly from the rules and limitations for those created after October 21, 1942 (§2041).

Section 2041 and the Ascertainable Standard

The application of §2041 to powers of appointment excludes those that are limited by an ascertainable standard. The ascertainable standard is defined as health, support, maintenance, and education.

These limitations are basic to the creation of Credit Shelter Trusts which will be discussed in Chapters 2 and 3 of this book.

Transfers Made Within Three Years of Death

Before 1981, gifts made within three years of the date of death were considered in "contemplation of death" and were included in the decedent's taxable estate.

For example, the decedent made a gift of $7,500 of cash to each of his children within one week prior to his death. The old law required the "undoing" of these transfers. That is, although the decedent no longer owned the cash, the cash gifts were considered gifts in contemplation of death and each of the $7,500 amounts became part of the decedent's taxable estate.

Now, transfers made prior to death are generally not included in the decedent's taxable estate (§2035). If a father makes gifts of $7,500 of cash to his children on Monday (assuming he has made no prior gifts that year) and he dies on Tuesday, the $7,500 amounts are not included in his estate. The making of pre-mortem gifts in amounts of up to $10,000 can be an effective estate planning strategy.

There are exceptions. A transfer of a life insurance policy on the decedent's life is includable in the decedent's estate if the decedent first owned the policy and then transferred it within three years of death. Transfers of interests are also included in the gross estate under §2036 (transfers with a retained life estate) and §2037 (transfers taking effect at death).

Additionally, a relinquishment of powers to amend, revoke or terminate trusts, within three years of death are included, such as where an individual changes a revocable trust benefiting his children into an irrevocable trust and that change occurs within three years of death, then that trust property is included in the decedent's estate (§2038). Also, for the purposes of determining the estate's eligibility for §303(b) distributions in redemption of stock to pay death taxes, special valuations under §2032(a) and installment payment of estate taxes under §6166, the three-year rule applies for certain purposes.

For large estates, it is sometimes an effective estate planning strategy to make **taxable gifts**. For maximum benefits, gifts must be made more than three years prior to the decedent's death. The amount of gift tax which is paid by the decedent or his estate on gifts made within three years of death is included in the gross estate whether or not the gift is includable in the gross estate. The purpose is to eliminate an incentive to make a deathbed transfer which would remove from the tax base the amount of the gift tax liability. (An extended discussion of taxable gifts is beyond the scope of this book.)

Community Property

Nine states currently have community property laws: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington and Wisconsin. Several states have had them for brief periods of time. Most states recognize that community property retains its character even when the owners move to another state. Later-acquired assets can be traced back to community property funds and may retain community property character.

The rules can be complicated and vary by state. In general, one-half of community property is deemed owned by the decedent spouse and one-half by the surviving spouse, without regard to legal title. The decedent spouse is required to include one-half of the community property in the gross estate.

EXAMPLE 1-8:

- Husband and wife were married in California and had no assets at the time of the marriage.
- During the course of the marriage the husband earns a substantial income and the wife earns no income.
- Due to those earnings an estate of $2,000,000 is accumulated.
- The estate consists of a residence, a mountain cabin, and an investment account. All of these assets are in the husband's name.
- If the wife predeceases the husband, one-half of this property ($1,000,000) is considered the wife's interest in community property and is included in her estate for federal estate tax purposes, even though she does not have the legal title to the property.
- This is generally the rule for community property states.

Family-Owned Business Deduction

The Taxpayer Relief Act of 1997, P.L. 105-34, enacted a family-owned business exclusion for federal estate tax purposes as §2033A. The Internal Revenue Service Restructuring and Reform Act of 1998 (H.R. 2676) ("1998 Reform Act") redesignated this provision as §2057 and converted the exclusion into a deduction. Under former §2033A and new §2057, the executor of the estate of a citizen or resident of the United States who dies after 1997 may elect special treatment for qualified family-owned business interests. In general, §2057 now operates, along with the applicable credit amount, to allow the deduction of $1.3 million of closely held business interests from the decedent's gross estate. Section 2057 has many similarities to §2032A, special use valuation, another provision applicable to family farms and small businesses. Many of the definitions are applicable to both sections (§2057(i)).

Deduction and Unified Credit

The deduction of $1.3 million is coordinated with the value of the unified credit. That is, a qualifying taxpayer may not exclude $1.3 million from the decedent's gross estate **and** shield an additional $650,000 (in 1999) from federal estate tax. Rather these are combined and a qualifying taxpayer in 1999 may exclude up to $1.3 million from the decedent's gross estate. The Reform Act of 1998 added that the estate can take a maximum $675,000 qualified business deduction if it owns that much in qualified business interests, and take the applicable exclusion from the unified credit amount up to $1.3 million (rather than have the deduction reduced each year as the exclusion amount increases as prior law provided) (§2057(a)). This deduction is not applicable to generation-skipping transfers (§2057).

To qualify for §2057 treatment, the decedent must have been a U.S. citizen or a resident of the United States at death; the executor must make an election and file a recapture agreement; the adjusted value

(§2057(d)) of the family-owned business interest in the estate and which were gifts to family members must exceed 50% of the decedent's gross estate; and there must have been a material participation as defined in §2032A(e)(6) in the operation of the business in at least five of the eight years ending on the decedent's death. The decedent's participation qualifies for these purposes.

The deduction applies to a sole proprietorship interest, as well as to other types of entities. The decedent and family members must own at least 50% of the entity, at least 30% of an entity in which two families own 70% of interests, or at least 30% of an entity in which three families own 90%. In a corporation, the family must own the stated percentage of the total voting power of all classes of voting stock and the required percentage of the total value of shares of all classes.

Partnerships are measured by the percentage of the capital interest earned. Section 2057 sets forth rules for the ownership of tiered entities which must be tested separately. Individual ownership of entities must be proportionally owned by shareholders, partners, or beneficiaries having a present interest.

The adjusted value of the qualified family-owned business interests includes those interests which are part of the decedent's gross estate, and those which were acquired by or passed to a qualified heir from a decedent, as long as they have been held continuously by the decedent's family other than the decedent's spouse between the date of the gift and date of death (§2057(b)(3)).

Excluded Business Interests

There are certain types of business interests which are excluded from §2057. These include those in which the principal place of business is located outside the United States, those where the stock is readily tradeable on an established securities market or secondary market within three years of death, an interest in a business where in the year of the decedent's death more than 35% of the adjusted ordinary gross income was personal holding company income (except for certain family leases on a net cash basis, banks or domestic building and loan associations), and finally those where the proportion of business interests attributable to cash or marketable securities is in excess of the day-to-day working capital needs of the business or of certain passive interests.

Recapture

The benefit of the deduction may be recaptured if, within ten years after the decedent's death and before the heir's death, participation requirements are not met, the heir disposes of the interest other than to another family member or pursuant to a qualified conservation contribution under §170(h), or the qualified heir no longer maintains the principal place of business inside the United States. The entire benefit is recaptured if these events occur within six years of the decedent's death and they are reduced in increments after the sixth year (§2057(f)).

Qualified Heirs

If the qualified heir is not a United States citizen, the interest must pass to a qualified trust. Under §2057(i)(1), a qualified heir is defined to include active employees who have been employed in the

business for at least ten years at the death of the decedent, in addition to the family members who might be considered qualified heirs.

VALUATION

General Definition

The value of an asset is generally determined for estate tax purposes as of the date of death. Regulations govern the method of valuing stocks and bonds, interests in businesses, notes, cash on hand or on deposit, household and personal effects, annuities, interests for a term of years, remainder or reversionary interests, valuation of certain life insurance and annuity contracts and shares in open-ended investment companies. All other property is valued as set out in Reg. §20.2031-1. In general, value is the net fair market value of the property of the date of decedent's death. The executor may elect to use the alternate valuation date which is described below.

Fair market value is defined by the regulations as the price at which the property would change hands between a willing buyer and willing seller, neither being under any compulsion to buy or to sell, and both having reasonable knowledge of relevant facts. Specifically excluded is any valuation determined by a forced sale price or a sale price of the item in a market other than that in which the item is most commonly sold to the public, taking into account the location of the item wherever appropriate. Property is not valued as assessed for local tax purposes unless it can be shown that that value represents the fair market value as of the applicable valuation date. Items which were held by the decedent for sale in the course of business generally are reflected in the value of the business.

Alternate Valuation

The value of the gross estate may be valued on an alternate valuation date which is allowed under §2032. If property is distributed, sold, exchanged or disposed of within six months after the decedent's death, the property would be valued as of the date of the distribution, sale, exchange or other disposition. If the property has not been distributed, sold, exchanged or otherwise disposed of, within six months after the decedent's death, the property may be valued as of the date six months after the decedent's death (when the alternate valuation date is elected).

The election of the alternate valuation date is made by the executor on the federal estate tax return and is irrevocable once it is made. The election is not allowed if the federal estate tax return is filed more than one year after its due date including extensions. The estate tax return is normally due nine months after the date of death.

All property must be valued as of the alternate valuation date if such an election is made. Property which passes for purposes of the charitable deduction under §2055 or §2106(a)(2), or the marital deduction under §2056, must be adjusted in value as of the date six months after the decedent's death or the date of sale, exchange or other disposition if the executor elects the alternate valuation date.

The election is not allowed to be made unless the election will accomplish a decrease in the value of the gross estate and a decrease in the sum of the tax imposed generally. Consider the estate of a husband which is valued at the date of death at $900,000 and which all passes under the will to his surviving wife (and, thus, no estate tax is due because of the marital deduction). If the assets in the estate are worth $1,100,000 six months after the date of death, the estate **may not** elect the alternative valuation date—in order to receive a step-up in basis for the assets to $1,100,000.

EXAMPLE 1-9:

- At date of death, in 1999, Zelda's estate, which passes to her daughter, is valued at $700,000. Securities are valued at $400,000, and real estate is valued at $300,000.
- Her estate's executor sells one-half of the securities three months after her death for $235,000.
- Six months after death the real estate is valued at $250,000 and the rest of the securities are valued at $195,000.
- Assuming no other deductions or credits, on the federal estate tax return the executor may use date of death values of $700,000 and pay tax on $50,000 (see Table B, page 17), or the executor may elect the alternate valuation date which results in the following:

One-half securities on date of sale:	$ 235,000
One-half securities six months after death:	$ 195,000
Real estate six months after death:	$ 250,000
	$ 680,000

In electing the alternate valuation date, the estate pays estate tax on $30,000.

In 1999, the applicable credit amount is $650,000.

Valuation of Real Property in Certain Farms and Closely Held Businesses

Under §2032A, a special valuation is allowed for certain property. In order to qualify to use this section of the Code, the decedent must at the time of death be a U.S. citizen or a resident of the United States, the executor of the estate must elect the application of the section and file the required Refunding Agreement. Generally, valuation is made on either a capitalization of rent formula or the multiple factor method. The aggregate reduction in fair market value (after 1982) is limited for any one decedent to no more than $760,000. This amount was raised from $750,000 as an adjustment for inflation pursuant to §2032A.

This section may be applied to an interest in a partnership, corporation or trust which is a closely held business with respect to the decedent. Real estate is eligible for special use valuation if a qualified heir receives a present interest from the decedent. All of the beneficiaries of a discretionary trust

must be qualified heirs. Real property in such a trust is treated as a present interest if all beneficiaries are qualified heirs [Reg. §20.2032A-3(b)(1)].

Definitions in Section 2032A

"Qualified use" means the property is used as a farm for farming purposes or is used in a trade or business [§2032A(b)(2)].

"Qualified real property" for purposes of this section is real property located in the United States which was acquired from or passed from a decedent to a qualified heir of the decedent and which on the date of the decedent's death was being used for a qualified use by the decedent or a member of the family if 50% or more of the adjusted value of the gross estate consists of the value of such property which was acquired from or passed from the decedent to a qualified heir.

Twenty-five percent or more of the adjusted value of the gross estate consisting of the adjusted value of the real property must, during the eight-year period ending on the date of the decedent's death, have periods aggregating five years in which the real property was owned by the decedent or a member of his family and used for a qualified use by the decedent or a member of his family, was acquired from or passed from the decedent to a qualified heir.

There must have been material participation by the decedent or a member of his family in the operation of a farm or other business. The real property must be designated in the Refunding Agreement.

"Material participation" is determined in a manner similar to the manner used for the purposes of §1402(a) relating to net earnings from self-employment.

"Qualified heir" is a member of the decedent's family who acquired property or to whom the property passed from the decedent. If the qualified heir disposes of the interest in qualified real property to any member of his family, then such member of his family is thereafter treated as the qualified heir with respect to that interest. A member of the family means an ancestor, spouse, lineal descendant, lineal descendant of such individual spouse or parent of such individual, and spouse of any lineal descendant.

"Farming purposes" means cultivating soil or raising or harvesting any agricultural or horticultural commodity (including raising, shearing, feeding, caring for, training, and management of animals) on a farm and handling, drying, packing, grading or storing on a farm any agricultural or horticultural commodity in its unmanufactured state, but only if the owner, tenant, or operator of the farm regularly produces more than one-half of the commodity so treated and the planting, cultivating, caring for or cutting of trees or the preparation, other than milling, of trees for market.

"Active management" means making management decisions of a business other than daily operating decisions.

Recapture

The benefits of the valuation are recaptured if within ten years after the decedent's death and before the death of a qualified heir, the qualified heir disposes of any interest in the qualified real property other than to a member of his family or the qualified heir ceases to use it for the qualified use which was passed from the decedent. The benefits are recovered pro rata if there is a partial disposition of the interest acquired by the qualified heir or a predecessor to the qualified heir or there is a cessation of the qualified use of the portion.

Real property ceases to be used for a qualified use if the property is no longer used for the qualified use or during any years after the decedent's death and before the death of the qualified heir, if there are periods of more than three years in which there has been no material participation by the decedent or any member of his family in the operation of the farm or other business.

In the case of periods during which the property was held by the qualified heir but there was no material participation by the qualified heir or any member of the qualified heir's family, then the qualified use ceases.

The qualified heir is personally liable for any amount which must be refunded under the ten-year rules and may post a bond in order to be discharged from personal liability.

The qualified heir may begin to use the qualified real property within two years after the decedent's death and no tax is imposed by the failure of the qualified heir to use the property before that date. The ten-year period is then extended by the period of time between the decedent's death and the date (within two years) that the qualified heir begins to use the property.

Eligible Qualified Heir

Another term defined in §2032A is the "**eligible qualified heir**." This is either:

- A surviving spouse,
- One who has not attained the age of 21,
- One who is disabled, or
- One who is a student.

For an eligible qualified heir, active management by the eligible qualified heir or by the fiduciary of an eligible qualified heir qualifies as material participation for purposes of this section. These "eligible qualified heirs" may rent the real property to a family member on a net cash basis and not lose the qualified use criteria.

Certain accommodations for decedents who were retired or disabled for a continuous period as of the date of the decedent's death are made. There are also special rules for situations in which the surviving spouse is active in the management of the farm or other business.

Valuation

Farms are valued by dividing the excess of the average annual gross cash rental for comparable land used for farming purposes over the average annual state and local real estate taxes for such comparable land by the average annual effective interest rate for all new federal land bank loans.

The average annual computation is made on the basis of the five most recent calendar years and ending before the date of death. If there is no comparable land from which the average annual gross cash rental may be determined, but there is comparable land from which the average net share rental may be determined, average annual net share rental may be substituted for average annual gross cash rental. Net share rental is the value of the produce received by the lessor of the land on which the produce is grown over the cash operating expenses of growing such produce which under the lease are paid by the lessor.

Qualified conservation contributions receive special treatment under the section (§2032A(c)(8); See §2057(f)(1)(B)).

Five Factors

Where the method described above is not used for valuing farms, then the following factors are applied in determining the value of qualified real property:

- Capitalization of income which the property can be expected to yield for farming or closely held business purposes over a reasonable period of time under prudent management using traditional cropping patterns for the area, taking into account soil capacity, terrain configuration and similar factors.
- Capitalization of the fair rental value of the land for farm land or closely held business purposes.
- Assessed land values in a state which provides a differential or use value assessment law for farm land or closely held businesses.
- Comparable sales of other farm land or closely held businesses in the same geographical area far enough removed from the metropolitan or resort area so that non-agricultural use is not a significant factor in the sales price.
- Any other factor which fairly values the farm or closely held business value of the property.

Removal of standing timber on qualified woodland has specific rules. Trees cannot be treated as a crop on qualified woodland. Qualified woodland means any real property which is used in timber operations and is an identifiable area of land such as an acre or other area for which records are normally maintained in conducting timber operations. Timber operations means planting, cultivating, caring for or cutting of trees or the preparation, other than milling, of trees for market.

EXAMPLE 1-10:

- Gene and Gert own a farm on which both of them have worked for thirty years. They have two adult sons who have each worked on the farm as their sole adult employment for more than ten years. Gert died.
- Both sons plan to continue working on the farm for the rest of their lives.
- Gene dies in 2006. Gene's interest in the farm land is valued at $1.5 million and he owns other assets valued at about $250,000. The marital trust which Gert left for Gene held assets valued at $500,000 (but no farm land). No special use valuation election was made at her death. Gene's net estate after expenses of $50,000, is $2,200,000.
- With no special use valuation, the taxable estate is as follows:

Estate		2,200,000
Credit in 2006		1,000,000
Taxable Estate	1,200,000	

Approximate Estate Tax $ 427,800.

- If a special use valuation is made and the use value of the farm land is, for example, $600,000, then the estate cannot utilize the entire use valuation. It is limited to the total reduction from fair market value set out in§ 2032A, adjusted for inflation. In 1999, this number is $760,000. Unless this amount is adjusted significantly for inflation by 2006 when Gene dies, Gene's estate cannot use the value of $600,000 because that reduces the estate by $900,000.

  - Using the 1999 §2032A amount of $760,000, Gene's estate is $1,460,000 [comprised of $760,000 for the farmland, other assets of $250,000, the marital trust of $500,000 less the $50,000 of expenses]

Estate	$1,460,000
Credit in 2006	1,000,000
Taxable Estate	460,000

Approximate Estate Tax $142,200

Miscellaneous

The section allows for a qualified replacement property which is real property acquired in a §1031 exchange or the acquisition of which results in non-recognition of gain under §1033. It may only include property which is used for the same qualified use as the replaced property which was being used before the exchange.

The statute of limitations for the cessation of use for qualified use is no less than three years after the date the Secretary of the Treasury is notified of the disposition or cessation of use, or three years from the date the Secretary is notified of replacement of property or of an intention not to replace or exchange property.

There are additional rules for involuntary conversion of property. There are also rules for treatment of qualified exchanges of property.

FEDERAL ESTATE TAX PAYMENTS

The estate tax is paid with the filing of Form 706, the federal estate tax return. The tax is due nine months after the date of death. Upon approval, an estate may extend the date of filing the Form 706 to fifteen months after the date of death, but such extension to file does not constitute an extension to pay the federal estate tax. In certain cases, the executor may elect to pay the tax in installments pursuant to §6166. The rates are set out in Table A (page 2).

APPLICABLE CREDIT AMOUNT

The unified credit is increasing each year, beginning in 1998 and ending in 2006. The applicable exclusion amount to the increasing credit is set forth in Table B. §2010. The unified credit is not per recipient but per transferor. For example, a single parent who dies in 2003 with two children may transfer $350,000 free of federal estate tax to each child (not $700,000 per child).

TABLE B

INCREASE IN APPLICABLE EXCLUSION AMOUNT (1997 STATUTORY CHANGE)	
1998	$ 625,000
1999	650,000
2000	675,000
2001	675,000
2002	700,000
2003	700,000
2004	850,000
2005	950,000
2006	1,000,000

MARITAL DEDUCTION

A deduction is allowed for the value of property which passes from the decedent to the decedent's surviving spouse under §2056. This is the unlimited marital deduction. This deduction applies to gifts which are made outright from the decedent to his or her spouse, as well as to certain interests that can be placed in trust for the benefit of the spouse during the spouse's lifetime as allowed under §2056. If the spouse is a U.S. citizen and the interest qualifies as a deductible interest, the marital deduction is an unlimited deduction against the estate tax for federal purposes.

The idea behind the unlimited marital deduction is that the interest received by the surviving spouse will be included in the spouse's estate at the spouse's subsequent death unless spent by the spouse during his or her lifetime. However, as we shall see in the discussion of the Credit Shelter Trust, the maximum use of the unlimited marital deduction is not always appropriate.

Property which passes outright to the surviving spouse—for example, as surviving joint tenant or as named beneficiary under an insurance policy or pension plan—qualifies for the marital deduction. In addition, there are three types of trusts which qualify for the marital deduction, although only two are used with frequency. These trusts which qualify for the marital deduction are the QTIP Trust, the General Power of Appointment Trust, and the Estate Trust.

QTIP

A QTIP Trust has been allowed since Congress amended §2056 in 1981. The trust holds Qualifying Terminable Interest Property, thus the name QTIP. The trust must provide that there is a mandatory distribution of income to the surviving spouse at least annually, for his or her lifetime, but upon the death of the surviving spouse the trust property may pass to the children or others. The QTIP qualifies for the unlimited marital deduction if the executor elects to claim the marital deduction for the QTIP Trust. The election is irrevocable.

There must be a mandatory payment of income without any conditions during the lifetime of the surviving spouse. Principal may or may not be distributed to the surviving spouse. However, no one other than the surviving spouse may receive any income or principal distributions. During the surviving spouse's lifetime, no one, not even the surviving spouse, may appoint or distribute the QTIP property to anyone other than the surviving spouse.

The QTIP Trust may provide the surviving spouse with a limited power of appointment on death. This is not a necessary feature. The popularity of the QTIP Trust derives from the fact that upon the death of the surviving spouse the property may be distributed to the original decedent's descendants or other beneficiaries named by the original decedent (and the first of two parents to die). That is, a QTIP Trust may be structured so that the surviving spouse (the beneficiary of the QTIP Trust) has no authority to govern the disposition of the remaining QTIP Trust estate on the subsequent death of the surviving spouse. This feature makes it very popular, especially in case where there are children of a first marriage and the QTIP is created for the spouse in a subsequent marriage.

General Power of Appointment Trust

The General Power of Appointment Trust, as its name indicates, qualifies for the unlimited marital deduction because the spouse is given a general power of appointment over the entire trust corpus. It also must include mandatory payment of income to the surviving spouse during the lifetime of the surviving spouse without any conditions.

Like the QTIP, the General Power of Appointment Trust may provide for principal distributions to the surviving spouse or it may preclude the principal distribution to the surviving spouse, but no one other than the surviving spouse may receive distributions of income or principal during the lifetime of the surviving spouse. Given the General Power of Appointment (and unlike the QTIP Trust), the surviving spouse has the power to appoint the remaining trust estate to anyone (even the surviving spouse's new spouse!).

Estate Trust

Less often used is the estate trust, which is the type of marital trust which permits income to be accumulated rather than paid out to the surviving spouse. At the death of the surviving spouse, the accumulated income and principal must be distributed to the surviving spouse's estate.

The estate trust was used in situations where the surviving spouse had substantial income from independent sources and income from the trust was not needed and would be subject to a very high income tax rate. Under the current income tax rates, this benefit is rarely or little realized and this trust is not seen often in today's estate planning.

Other Issues

As noted above, the QTIP Trust was not a trust that was allowed until after §2056 was amended by Congress in 1981. It is further noteworthy that prior to 1981, the marital deduction was not an unlimited deduction, but was limited to one-half of the decedent's estate or $250,000, whichever was larger, under various types of formulas. It is important that any pre-1981 estate plan be updated to qualify for the (post-1981) unlimited marital deduction.

Non-Citizen Spouses

The unlimited marital deduction is not allowed for property passing to a surviving spouse who is not a United States citizen. For property to pass free of federal estate tax to a surviving spouse who is not a U.S. citizen, the property must pass to a Qualified Domestic Trust (commonly called a QDOT).

A QDOT is a trust which requires that at least one of the trustees be a U. S. citizen or a domestic corporation and that the trustee have the right to withhold taxes imposed under §2056A(b). The property remaining in the QDOT at the surviving spouse's death must be subject to estate tax.

Further, trust distributions to the surviving spouse during the surviving spouse's lifetime (except for income and hardship disbursements) must be subject to United States estate tax. This is a heavy financial burden for a surviving non-U.S. citizen spouse. The principal distributions from a QTIP

trust to a U.S. citizen-spouse are not subject to estate tax. The principal distributions to a non-U.S. citizen-spouse from a QDOT are subject to estate tax.

There is no requirement to provide for all trust income to be paid annually to the surviving spouse as there is with the Power of Appointment Trusts and QTIP trusts. The U.S. trustee requirement has been modified by the Taxpayer Relief Act of 1997 in certain situations.

The executor of the decedent's estate must make an irrevocable election on the federal estate tax return to treat a trust as a QDOT. There are strict security requirements on QDOTs which contain assets in excess of $2 million and there is a two-tiered structure which is imposed in order to assure that the §2056A tax is collected.

If there is value exceeding $2 million, determined without regard to indebtedness on the assets, the trust document must require that at least one trustee be a U.S. bank or the U.S. branch of a foreign bank or that the U.S. trustee furnish a bond in favor of the IRS or a Letter of Credit in an amount equal to 65% of the fair market value of the trust assets, again determined without regard to indebtedness. Also, the investment in offshore real estate may be limited in a QDOT. Value is determined as it would be for federal estate tax purposes.

OTHER DEDUCTIONS—CREDITS

Administration Expenses

Under §2053 reasonable administration expenses are a deduction for purposes of determining the amount of the taxable estate. The executor has the choice whether to take these deductions on the estate's income tax return or on the federal estate tax return. Refer to §642(g).

Expenditures actually incurred in connection with the funeral and burial are deductible and include such items as casket, burial vault, clothing purchased for burial, flowers provided by the estate, and the cost of transporting the body to the place of burial. Tombstone monuments and mausoleum burial plots are also deductible. The expenses are limited by a test of reasonableness and whether or not they are properly allowable out of the probate estate under state law. Generally, the expenses must actually have been paid from the decedent's estate. These are deductible on Form 706.

Other administrative expenses which are deductible are the executor's commissions, attorney's and accountant's fees for the estate, and other expenses incurred in the collection of assets, payment of debts, and distribution of property to the persons entitled to it from the estate.

Debts

The estate may deduct from the taxable estate claims which were personal obligations of the decedent which were enforceable against the decedent at the time of death. It may also include contingent claims against the decedent if there is a possibility that the liability will actually arise.

In general, taxes are deductible in the estate to the extent that they were an enforceable obligation against the decedent at the time of death. Unpaid gift taxes on gifts made by the decedent before his or her death are deductible. (State death taxes and possibly some foreign taxes are credits against the federal estate tax.)

Taxes on income earned by the decedent prior to death are deductible. This does not include income of the surviving spouse. Nor does it include taxes on income received after death. The estate may elect to treat state death taxes and some foreign taxes which are imposed upon charitable bequests as deductions.

Casualty Losses

The estate may deduct casualty losses incurred (§2054). The type of casualties which may be deducted are those which are defined under §165(c).

State Death Taxes

The federal estate tax is credited with the amount of any estate, inheritance, legacy, or succession taxes actually paid to any state, which does not exceed the statutory amounts (§2011). The credit may not exceed the amount determined under the following table [§2011(b)].

TABLE C

Computation of Maximum Credit for State Death Taxes (Based on Federal adjusted taxable estate)							
(1) Adjusted taxable estate equal to or more than B	(2) Adjusted taxable estate less than B	(3) Credit on amount in column (1)	(4) Rate of credit on excess over amount in column (1)	(1) Adjusted taxable estate equal to or more than B	(2) Adjusted taxable estate less than B	(3) Credit on amount in column (1)	(4) Rate of credit on excess over amount in column (1)
			(Percent)				(Percent)
0	$40,000	0	None	2,040,000	2,540,000	106,800	8.0
$40,000	90,000	0	0.8	2,540,000	3,040,000	146,800	8.8
90,000	140,000	$400	1.6	3,040,000	3,540,000	190,800	9.6
140,000	240,000	1,200	2.4	3,540,000	4,040,000	238,800	10.4
240,000	440,000	3,600	3.2	4,040,000	5,040,000	290,800	11.2
440,000	640,000	10,000	4.0	5,040,000	6,040,000	402,800	12.0
640,000	840,000	18,000	4.8	6,040,000	7,040,000	522,800	12.8
840,000	1,040,000	27,600	5.6	7,040,000	8,040,000	650,800	13.6
1,040,000	1,540,000	38,800	6.4	8,040,000	9,040,000	786,800	14.4
1,540,000	2,040,000	70,800	7.2	9,040,000	10,040,000	930,800	15.2
				10,040,000	....	1,082,800	16.0

Many states impose a state estate tax which equals the state death tax credit under the federal estate tax provisions. The effect is to allocate the fraction of the tax to state government and reduce the

amount which is being paid to the federal government while not increasing the total tax liability of the decedent's estate.

There are numerous systems of state death taxes which are imposed by the various states. Currently, most states have an estate or inheritance tax system which takes the full amount allowed for federal estate purposes (and only that amount). A few states impose estate taxes which exceed the federal credit. A few cities collect a transfer tax at death.

Charitable Deduction

An unlimited charitable deduction for property donated to a qualified charity is allowed (§2005). This value of the donated property is a deduction against the gross estate when calculating the taxable estate and ultimately reduces the estate tax liability.

Form 706

Included in the Appendix is Form 706. This is the United States Estate Tax return and Generation-Skipping Transfer Tax return. Form 706 is due within nine months after the date of the decedent's death unless the estate receives an extension of time to file. The estate would use Form 4768 to apply for an extension of time to file the return and pay Federal Estate and Generation-Skipping Transfer taxes. There is no provision for filing an amended Form 706. If a Form 706 has been filed, and something must be changed, then a Form 706 marked "Supplemental Information" must be filed.

Form 706 must be filed by the executor of the estate of every citizen or U.S. resident whose gross estate, plus adjusted taxable gifts, is more than the applicable credit amount ($650,000 in 1999).

As you will see the estate tax is set up as follows:

- Calculate gross estate
- Calculate and Subtract allowable deductions
- Result is the *taxable estate*
- Calculate and add adjusted taxable gifts (made after 1976)
- Calculate *tentative tax* on taxable estate plus adjusted taxable gifts
- Add 5% surcharge, if applicable
- Result is the *total tentative tax*
- Subtract gift tax paid on gifts made after 1976
- Result is *gross estate tax*
- Subtract adjusted appreciable credit amount
- Subtract credit for state death tax

- Subtract the total amount of the credits for pre-1977 gift taxes, foreign death taxes, and prior transfer taxes
- The result is the *net estate tax*
- *Add* generation-skipping taxes and §4980A taxes to net estate tax
- *Subtract* prior payments and certain Treasury bonds redeemed in a payment of tax.

FEDERAL GIFT TAX

UNIFIED SYSTEM

The federal gift tax system has been integrated with the federal estate tax system. Prior to 1981, they were separate systems rather than a unified transfer tax system. The gift tax is effectively imposed at the same rates as the estate tax [§2502(a)].

DEFINITION OF GIFT

Gratuitous transfers are taxable. Donative intent is not necessary as long as the transfer is complete and the donor has parted with dominion and control (§2511).

ANNUAL EXCLUSION AND QUALIFIED TRANSFER EXCLUSIONS

The first $10,000 of gifts to each donee in each calendar year is not included in the total amount of gifts made during that year for gift tax purposes. Beginning in 1999, the $10,000 amount is increased by a cost of living adjustment and rounded to a multiple of $1,000, under the provisions of the Taxpayer Relief Act of 1997. The annual exclusion has not been increased for 1999 since the cost of living adjustment has not warranted it.

Also excluded from the transfer of property as gift is a "**qualified transfer.**" A qualified transfer is an amount paid on behalf of an individual as tuition to an educational organization for the education or training of such individual, or to any person who provides medical care with respect to such individual as payment for such medical care. These transfers must be made directly to the educational organization or to the person who provides medical care and not indirectly or in trust. (§2503(e)).

APPLICABLE CREDIT AMOUNT

The unified credit was described previously in the estate tax discussion. The same unified credit, which is applied against the estate tax, is integrated with the gift tax provisions. The unified credit applies an exclusion amount of $650,000 for those who die in 1999 and increases to $1,000,000 in 2006. The unified credit may be used for transfers by gift during lifetime and for transfers from the estate after death. (See Table B page 17.)

MARITAL DEDUCTION

There is an unlimited marital deduction for gift tax purposes. If the donor transfers an interest in property to a donee, who, at the time of the gift, is the donor's spouse, it is not included as a taxable gift. §2523(a). If the donor's spouse is not a U.S. citizen, the marital deduction is limited to $101,000 annual exclusion gifts (§2523(i) Rev. Proc. 98-61).

CHARITABLE DEDUCTION

There is an unlimited charitable deduction for gift tax purposes. There is allowed, as a deduction in the case of a citizen or resident, the amount of all gifts made to, or for the use of, the United States, any state, any political subdivision, or any qualified charitable organization [§2522(a)].

There is also a deduction for income tax purposes for charitable gifts, but that deduction is not unlimited.

INCOME TAX

GENERAL RULE

"Gross income does not include the value of property acquired by gift, bequest, devise or inheritance." §102(a).

Generally there is no income tax imposed on the transfer of property through a transfer at death or by gift during lifetime. Income tax will be imposed on the income generated by that property.

IRA AND RETIREMENT PLAN CONSIDERATIONS

Withdrawals from qualified retirement plans and IRAs ordinarily trigger taxable income when the withdrawal or distribution is made. However, a surviving spouse can roll over funds into an IRA and defer income tax on the assets in the IRA.

The surviving spouse may be able to postpone withdrawals until age 70 and then pay the income tax over many years rather than having the income tax paid in one lump sum at the decedent's death. This is generally the recommended course for an IRA or other qualified retirement plan where the spousal rollover is possible.

Funds from a qualified retirement plan or IRA passing to an individual other than a surviving spouse (such as a child) also trigger income. That is, a distribution from a qualified retirement plan or IRA to a non-spouse constitutes income (although in some instances, the income may be deferred over the recipient's life expectancy). This rule—that such funds passing to a non-spouse constitute taxable income—is a major *exception* to the *general rule* that an inheritance does not constitute income.

IRD CONSIDERATIONS

Income in respect of a decedent is any item of gross income earned by the decedent or his or her assets but paid after death and not properly includable in the taxable income of the decedent. Reg. §1.691(a). It is basically a receivable not subject to income tax until actually received. Under the general rule, income in respect to the decedent is taxed for income tax purposes to the person who actually receives it, even where it is included in the estate for estate tax purposes. This could be the estate of the decedent, a person who receives a distribution of that right from the estate, or a person who receives the right to receive the income by reason of the decedent's death even if it does not pass through the estate.

For example, assume wife dies prior to the date her employer makes a contribution for her to the company (nonqualified) profit-sharing plan. The employer, many months after her death, makes the contribution to the plan based upon the company's formula for the amount earned by her for the plan prior to her death. The recipient of the right to that contribution, such as her husband, receives it as income in respect of a decedent. He would incur any income tax liability associated with it when the income is actually received by him (§691).

BASIS CONSIDERATIONS

In general, the basis of the property in the hands of a person who acquired the property from a decedent, if the property is not sold, exchanged or otherwise disposed of before the decedent's death, is the fair market value of the property at the date of the decedent's death. §1014(a)(1). Thus, property which passes through the decedent's estate receives, in many cases, a step-up in the basis of the property.

EXAMPLE 1-11:

- Fred acquired 100 shares of ABC stock for $6,000. Assume that the stock appreciated to $30,000 during Fred's lifetime.
- If Fred sold the stock the day before he died there would be a capital gain of $24,000 (and a resulting federal capital gains tax of approximately $4,800).
- If, instead, Fred held the stock until the date of death when it was worth $30,000, the stock would receive a new (stepped-up) basis equal to $30,000.
- If Fred's executor sold the stock the day after Fred's death for $30,000, there would be no taxable gain (the sale price of $30,000 minus new basis of $30,000).

In effect, the capital appreciation for income tax purposes is deleted at the time of death by the step-up in basis. This is not true for transfers by gift; the donee of a gift receives a "carry-over basis"—a basis in the hands of the donee equal to the basis in the hands of the donor.

INCOME TAX RETURNS FILED BY THE ESTATE

The estate not only files the final income tax returns for the decedent, but is an independent taxpayer required to file fiduciary income tax returns itself. The same is usually true of trusts or custodial accounts in that they are independent taxpayers and are required to file fiduciary income tax returns.

Chapter 2

Marital Planning—Credit Shelter Trust

BASIC STRUCTURE

ESTATE PLANNING FOR MODERATE ESTATES (LESS THAN $650,000 IN 1999)

For a couple or a single person with a net worth less than the applicable exclusion amount due to the unified credit, no tax planning is needed to minimize the federal estate tax; the entire estate is protected by the applicable exclusion amount.

In a typical situation, the couple will have a simple will which transfers the entire estate outright to the surviving spouse and then in equal shares to adult children, or if there are minor children, in trusts (embodied in the will) for the minor children.

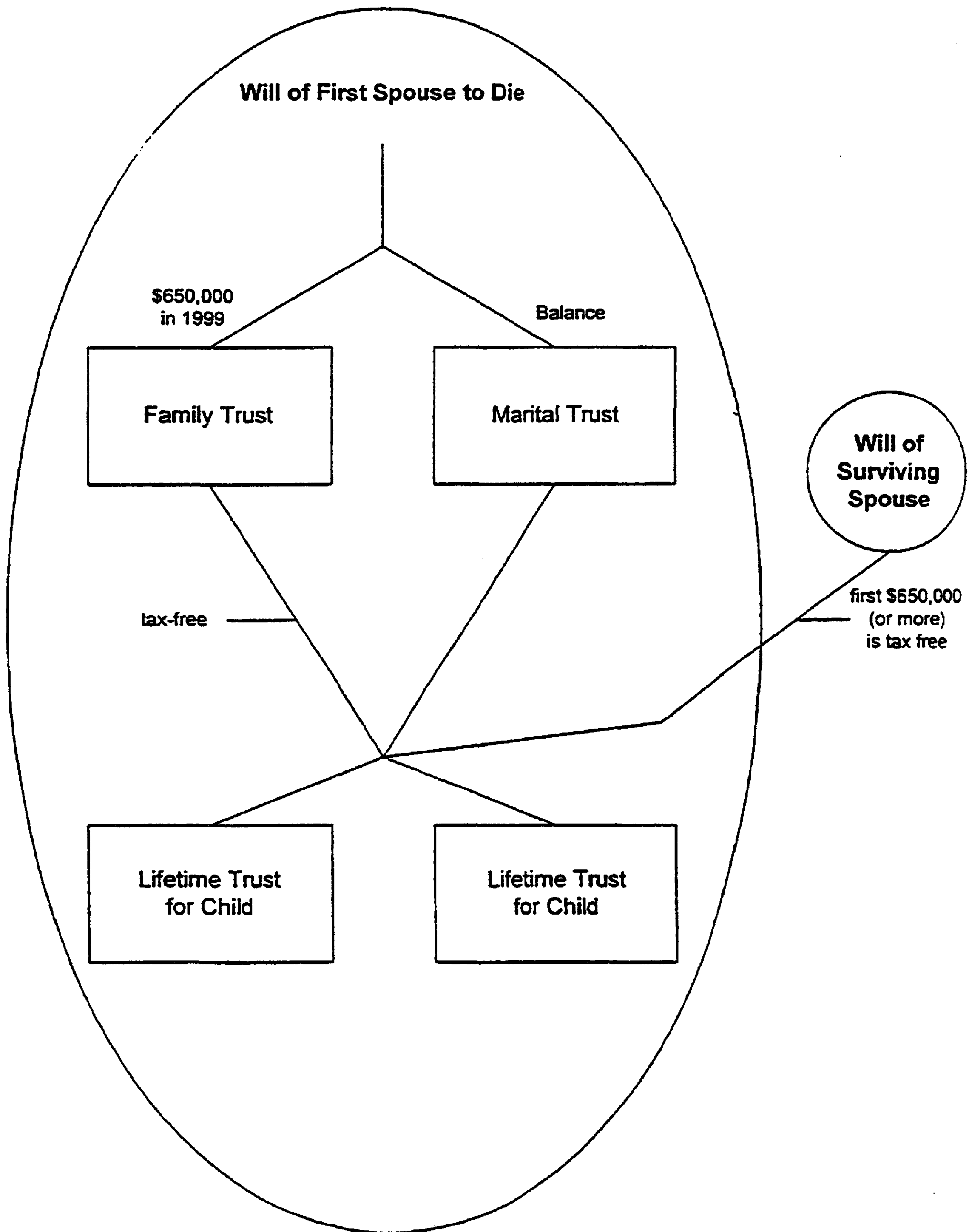
More extensive trust planning may be used for adult children who have particular problems according to the parents, such as being a spendthrift, having drug problems, being under the influence of a manipulative spouse, or being otherwise at risk for dissipation of the family funds.

More complex trust planning is often used as well for second marriages—to provide for the surviving spouse and children from prior and current marriages. Also, trusts or other more sophisticated techniques are sometimes used in planning for the care of a parent, sibling or other family members.

To reiterate, for couples or for a single individual with a net worth of less than the applicable exclusion amount under the unified credit ($650,000 in 1999), trust planning is not needed to shield the estate from federal estate tax.

PLANNING TO PROTECT COMBINED APPLICABLE CREDIT AMOUNT (APPROXIMATELY $1.3 MILLION)

The classic way to minimize federal estate tax for a couple with a combined net worth in excess of the applicable credit amount is what is known as **A/B planning**. This planning is illustrated by the following graphic.


Will of First Spouse to Die
$650,000
in 1999
Balance
Family Trust
Marital Trust
Will of
Surviving
Spouse
tax-free
first $650,000
(or more)
is tax free
Lifetime Trust
for Child
Lifetime Trust
for Child

The terms of the will for husband and wife each typically provide as follows:

> *If I die and my spouse survives me, I set aside the applicable credit amount into a credit shelter trust for the benefit of my surviving spouse and family. My (husband/wife) shall be the trustee. The trustee shall distribute the income and principal for the health, support, maintenance and education of my (husband/wife) and descendants. This trust shall terminate on the death of my surviving spouse. Upon termination, the trust estate of the credit shelter trust shall be distributed to my children in equal shares with the share of a deceased child being given in equal shares to his or her children. I give the balance of my estate (after setting aside the exclusion amount in the credit shelter trust) to my (husband/wife).*

Credit Shelter Trust

The assets in the Credit Shelter Trust are generally wholly available to the surviving spouse and the children. Typically the surviving spouse is the trustee, with the authority to make decisions about the investment and distribution of the assets.

From a federal estate tax point of view, the key is that the assets in the Credit Shelter Trust are not included in the estate of the surviving spouse. The assets escape federal estate taxation at the death of the first spouse and later at the death of the surviving spouse.

The assets in the Credit Shelter Trust (including the appreciation during the lifetime of the surviving spouse) pass free of federal estate tax to the children.

The surviving spouse also has his or her own applicable credit amount to protect property from estate tax. The structure of the plan then permits the couple to use **both** exclusion equivalents and to pass at least $1,300,000 free of federal estate tax to the children.

The Credit Shelter Trust is sometimes known as the B Trust or the Family Trust. Sometimes the Credit Shelter Trust is called the Bypass Trust because the property in the trust bypasses the taxable estate of the surviving spouse.

Single persons may also want to utilize a Credit Shelter Trust for children, grandchildren, nephews and nieces, or others for whom they want to provide trust benefits and protections over a period of time.

EXAMPLE 2-1:

- Husband owns $1 million of property, wife owns 0.
- Husband dies in 1999, leaving all property to wife.
- No federal estate tax at husband's death because of marital deduction and unified credit.
- Wife dies in 2000 with $1 million of property.
- Part of wife's estate shielded by her $675,000 unified credit. Approximate estate tax at wife's death: $130,000.

EXAMPLE 2-2:

- Husband owns $1 million of property. Wife owns 0.
- Husband creates a Credit Shelter Trust in his will, leaving the balance of the property to wife outright.
- Husband dies first, in 1999. No federal estate tax at his death.
- Wife dies in 2000 with $350,000 in her name and $650,000 in the Credit Shelter Trust.
- Estate tax at wife's death: **0**

NATURE OF THE CREDIT SHELTER TRUST

DEFINITION OF A TRUST

A trust is a legal entity in which a trustee holds property on behalf of one or more beneficiaries. The person who holds the legal title to the trust property and administers the trust according to the terms of the trust agreement is the trustee who is then in a fiduciary relationship to deal with the property for the benefit of the beneficiaries.

The trust is created by one or more settlors or grantors. Usually there is a written agreement which sets forth the terms of the trust and is known as the Trust Agreement or the Trust Instrument, and sometimes as the Trust Deed. It is also possible, and common, to establish a trust in a will. The trust (or trusts) is in effect "embodied" in the will.

The four defining elements of a trust are:

- Trust Instrument,
- Settlor or grantor,
- One or more beneficiaries, and
- One or more trustees.

TRUST AGREEMENT

There are various types of trust agreements. The trust agreement may establish a single trust. The trust agreement may also be a single trust agreement which then in turn establishes numerous trusts for numerous beneficiaries.

Single Trusts Agreement

> *I, Gilbert Grandfather, grantor, by this written agreement establish a trust to provide for my grandson, Ben. The trustee shall distribute the income and principal of the trust to pay for Ben's health, support, maintenance, and education, including tuition, books, supplies, and educational expenses which he may incur while attending undergraduate or graduate college and university. This trust shall terminate when Ben attains the age of thirty years or dies, whichever first occurs. Upon termination, the trust estate shall be distributed to Ben or if he is not then living, to my niece, Jenny Smith, if she is then living, or if she is not then living to the University of Illinois for use for its general purposes.*

Here Grandfather has established a single trust under his Trust Agreement.

Subordinate Trust Agreements

Alternatively, Grandfather might want to enter into one Trust Agreement and establish separate trusts under that Trust Agreement for each of his five grandchildren. The five trusts are each governed by the same type of language.

> *The trustee shall divide the trust property into five equal trusts, one for each of my grandchildren. The trustee shall distribute the income and principal of this trust to the grandchild of mine for whom this trust is created to provide for such grandchild's undergraduate and graduate education. This trust shall terminate when the grandchild for whom this trust is created attains the age of thirty years or dies, which ever first occurs. Upon termination, the trust estate shall be distributed to the grandchild for whom this trust is created or if he or she is not then living, to my niece, Jenny Smith, if she is then living, or if she is not then living to the University of Illinois for use for its general purposes.*

Within a Will Trust Agreements

Trusts may be, and often are, created within a will. In a trust established under the will, the same type of language is incorporated within the will. For example, the will might state

> *If any of my grandchildren survive me, my personal representative shall distribute $200,000 to the trustee of the trust established under Article 1.8 of this will. The balance of my estate shall be distributed to my nieces and nephews in equal shares.*

Revocable/Irrevocable

A trust may be revocable or irrevocable. If it is revocable, the settlor or another person may later amend or revoke its provisions. An irrevocable trust cannot be revoked or amended. Testamentary trusts become irrevocable, usually, when the testator dies because at that time there is no one who is permitted to change the terms of the trust which is established under the will.

The settlor may also establish an irrevocable trust during lifetime. **For example**, the settlor may establish an irrevocable trust during his lifetime to own a life insurance policy—in order to exclude

the eventual life insurance proceeds from the settlor's taxable estate. This will be discussed later in the book.

Trustee

The trustee is the person who holds **legal** title to the assets. The trustee is the legal owner; the beneficiary is the **beneficial owner**. The trustee is required by law to follow the terms of the trust agreement. Trustees may be individuals or corporations such as banks or trust companies. There may be one or more trustees who act alone or together making decisions about the administration of the trust.

Beneficiaries

The beneficiaries of a trust typically include:

- Income beneficiary,
- Principal beneficiary,
- Future (remainder) beneficiary, and
- Contingent beneficiary.

Income Beneficiary

The income beneficiary is entitled to receive some or all of the income. The trust agreement may mandate that all income or a portion of it be distributed to the beneficiary. Alternately, the trust agreement may grant discretion to the trustee as to whether or not to distribute income to that beneficiary.

Principal Beneficiary

Similarly, the principal beneficiary is entitled to the distributions of principal pursuant to the provisions for distribution included within the trust agreement.

Future Beneficiary

A future beneficiary is a beneficiary who will receive benefits of the trust, either income or principal, at some future time, but who does not have a present interest to receive trust income or principal.

Contingent Beneficiary

The contingent beneficiary is a person who may, but not necessarily, receive property based upon some future contingency. In the examples, the niece, Jenny Smith, is a contingent beneficiary because she only receives a distribution if the grandchild for whom the trust is created is not living at the time it terminates.

Similarly, the University of Illinois is a contingent beneficiary because it only receives trust property in the event that neither the grandchild for whom the trust is created nor niece Jenny Smith is living at the time the trust terminates.

Powers of Appointment

There are two types of powers of appointment. One is the **General Power of Appointment** and the other is a **Special Power of Appointment**.

The tax consequences of a General Power of Appointment is that the property subject to the power is included in the taxable estate of the holder of the General Power of Appointment. Prior to 1981, a General Power of Appointment was required as part of a marital trust in order to qualify it under the federal estate tax marital deduction. Many wills still include a Marital Trust with a General Power of Appointment (although QTIP marital trusts without such powers are very common now).

As defined in the tax code, the General Power of Appointment includes any authority which allows a person to include as a transferee of the property interest:

- Holder of the power,
- Creditors of the holder of the power,
- Estate of holder of the power, or
- Creditors of the estate of the holder of the power (§§2041, 2514).

The Special Power of Appointment is a legal authority which allows a person to appoint property or trust corpus to anyone other than:

- Himself or herself,
- His or her estate,
- His or her creditors, or
- Creditors of his or her estate (§§2041, 2514).

When included in a trust, a power of appointment allows the holder of the power to deal with future changes in needs and circumstances. The holder of the Special Power of Appointment does not have the property subject to that power included in his or her estate for estate tax purposes.

CREDIT SHELTER TRUST

Trust Agreement

The Credit Shelter Trust is often set forth within the wills of a married couple. The Credit Shelter Trust is established upon the death of the first spouse. In the event that the husband and wife have established revocable living trusts during their lifetimes, the Credit Shelter Trust may be included as a trust within that trust document.

In that circumstance, the will would "pour over" into the revocable living trust at the first death. The will would be a relatively brief document which would provide that all assets would be distributed to the trustee of the revocable living trust.

The provisions of the revocable living trust would then direct the trustee of the trust to set aside property into the Credit Shelter Trust. The property in excess of the Credit Shelter amount typically would be distributed outright to the surviving spouse or set aside in a marital trust.

The Trustee

The trustee of the Credit Shelter Trust may be the surviving spouse. The trustee could also be a bank or third party. It is possible to have co-trustees. The trustee has the authority to govern the investments of the Credit Shelter Trust and to make income and principal distributions, consistent with the terms of the trust agreement (or will).

Income Distributions

The Credit Shelter Trust may provide that all income is paid to the surviving spouse. (In the event that the surviving spouse is the sole trustee, it is likely that all income would be taxable to the surviving spouse, and so a mandatory distribution of income to the surviving spouse often makes sense under current tax laws.)

Alternatively, the Credit Shelter Trust may also provide that income is distributed to the surviving spouse and to children for the health, support, maintenance, and education of those family members within the discretion of the trustee.

The trustee may then decide to distribute all income and "sprinkle it" among the spouse and children or the trustee may decide to distribute only a portion of the income as needed for those purposes to the spouse and children. The rest of the income would be accumulated and added to the principal.

Principal Distributions

The trustee may be given power to distribute principal for the health, support, maintenance, and education of the spouse, or the spouse and the children. The principal could be distributed for only one or more of those purposes, again for either the spouse or the spouse and the children.

The trust agreement may also provide that there is no distribution of principal for any purposes. Also, the trust agreement may provide for a much broader standard for the distribution of principal, such as comfort, luxury, welfare and happiness.

However, if the surviving spouse is the trustee, then distributions of principal must be limited to the ascertainable standard of §2041. The ascertainable standard is health, support, maintenance, and education.

If the distributions of principal are not so limited, and the surviving spouse is the trustee, then the surviving spouse is deemed to have a General Power of Appointment over the trust principal and the trust estate of the Credit Shelter Trust would be taxed in the estate of the surviving spouse.

There is an exception to the General Power of Appointment provisions. The surviving spouse (or any beneficiary) may be given the authority to withdraw in any year the greater of $5,000 or 5% of the trust estate without regard to trust purposes or the ascertainable standard.

This limited "5 and 5 power" is not deemed to be a General Power of Appointment under the current tax code, and, therefore, it does not cause the Credit Shelter Trust to be taxed in the estate of the surviving spouse when he or she dies.

Special Power of Appointment

Often the provisions of the Credit Shelter Trust grant a Special Power of Appointment to the surviving spouse which allows the surviving spouse to name persons who will receive the remaining trust estate in the Credit Shelter Trust upon the death of such spouse.

For example, each trust might include the following:

> *In addition to other authorized distributions in this trust, the trustee shall make distributions to any person or corporations as my spouse directs, by a provision in my spouse's will specifically identifying this special power of appointment, provided that no such distribution shall benefit, directly or indirectly, my spouse, my spouse's estate, my spouse's creditors or the creditors of my spouse's estate.*

Generally, the Special Power of Appointment is exercised by the will of the surviving spouse. The Credit Shelter Trust may provide, for example, that the surviving spouse has a Special Power of Appointment exercisable among the decedent's descendants. The surviving spouse may then do a new will which provides as follows:

> *I am granted a Special Power of Appointment under the Credit Shelter Trust established by my husband at his death. I hereby exercise such Special Power of Appointment to provide that the remaining trust of the estate shall be distributed in equal shares to my two younger children. No property shall be distributed to my older child. I love my older child dearly, but he is independently wealthy and my two younger children (both of whom are teachers) have much greater financial need.*

A Special Power of Appointment, then, may grant to the surviving spouse the **flexibility** to treat children and grandchildren differently, responding to personal and financial situations which develop after the death of the first parent.

Such a power of appointment does not cause the trust estate of the Credit Shelter Trust to be subject to federal estate tax at the death of the surviving spouse.

Only if the power of appointment may be exercised in favor of:

- Surviving spouse,
- Surviving spouse's estate,
- Surviving spouse's creditors, or
- Creditors of the surviving spouse's estate,

would the trust estate be included in surviving spouse's estate.

If the power may be exercised in favor of one of those prohibited four donees, then the power of appointment is a General Power of Appointment causing the trust estate to be included in the taxable estate of the surviving spouse (the holder) (§2041).

Remainder Beneficiaries

Generally the Credit Shelter Trust is distributed to the decedent's descendants upon the death of the surviving spouse. This would occur at the surviving spouse's death if there is no special power of appointment or in the event that the special power of appointment is not exercised by the surviving spouse.

If the children or grandchildren are less than the designated age of maturity, the remaining trust estate of the Credit Shelter Trust is typically held in continuing trust for those younger family members.

The Credit Shelter Trust may provide, for example, that upon the death of the surviving spouse there shall be distribution of the Credit Shelter Trust "to my descendants, by representation, provided that the share of any descendant who is has not attained thirty-five years of age shall be held in trust for such descendant under Article 1.9."

MARITAL SHARE

For a couple with a net worth substantially more than the applicable credit amount, the typical estate plan provides for a set-aside of the applicable credit amount into a Credit Shelter Trust. The balance of the estate typically passes to the surviving spouse.

EXAMPLE 2-3:

- Husband has an estate of $1,600,000 and a traditional will providing for a Credit Shelter Trust.
- If the husband dies in 2003, the will would set aside $700,000 into the Credit Shelter Trust.
- The balance of the estate, namely $900,000 would pass to the surviving spouse.

The transfer of the property to the surviving spouse may occur in a number of ways.

OUTRIGHT DISTRIBUTIONS

Joint Tenancy

By operation of law, all property which is titled in the spouses' names as joint tenants with rights of survivorship (or as tenants by the entirety in states which recognize that title) passes directly to the surviving spouse and the provisions of wills and trusts have no effect upon that passing of property interest to the surviving spouse.

The interests in joint tenancy which are included in the estate of the decedent for estate tax purposes are automatically transferred to the surviving spouse at death. Property passing to the spouse as surviving joint tenant is shielded from federal estate tax by the marital deduction.

Insurance: Named Beneficiary

Any life insurance benefits on the decedent's life which name the surviving spouse as the beneficiary of the policy upon the decedent's death will be distributed automatically to the surviving spouse. Again, this occurs by operation of the insurance policy and contract law without any will provisions or trust provisions having any effect upon that disposition.

Qualified Pension Benefits and IRAs: Named Beneficiary

Similar to the insurance benefits, the retirement plans usually will have a beneficiary designation which has been completed by the participant; the named beneficiary may be (and usually is) the spouse. The decedent's will has no effect on the beneficiary designation and the recipient of the proceeds.

QTIP TRUST

As noted above, the QTIP Trust is a very popular means of qualifying assets left in trust for the marital deduction. The QTIP Trust qualifies for the marital deduction but the surviving spouse does not have the flexibility to appoint the trust assets, upon trust termination, to third parties (such as a new spouse). For example, the QTIP Trust assures the (deceased) husband that upon the subsequent death of the wife, the QTIP assets will pass to his children. This "assurance" does not attach to a General Power of Appointment type Marital Trust.

Mandatory Income

The QTIP Trust must provide mandatory payment of the trust income to the surviving spouse at least annually.

Principal

The QTIP Trust may, but is not required to, provide for the payment of trust principal to the surviving spouse, such as for health, support, and maintenance.

Spouse as Only Beneficiary

The surviving spouse must be the only beneficiary of income or principal from the QTIP Trust. No one, including the surviving spouse, may have the power to distribute income or principal or trust estate during the surviving spouse's lifetime to any one other than the surviving spouse.

Before 1981, a distribution into a trust for a surviving spouse qualified for the marital deduction (so that no federal estate tax was due) only if the surviving spouse had the authority upon his or her later death to leave the property to any person.

In that mode, the surviving spouse could leave the remaining trust estate of the marital trust to a new spouse, or to children from a prior marriage, or to any third party.

In 1981, Congress introduced the QTIP Trust. The transfer of property to a QTIP Trust does qualify for the marital deduction, but the QTIP Trust can be structured so that the surviving spouse has no authority with respect to the eventual disposition of the QTIP Trust estate.

In effect, the decedent may provide:

> I leave the balance of my estate, in excess of the applicable credit amount in a QTIP Trust for my surviving spouse. The trust shall distribute all of the net income each year to my spouse. The trust shall terminate upon the death of my spouse. Upon termination, the remaining trust estate shall pass to my children from my first marriage in equal shares.

LESSER-USED TECHNIQUES OF OBTAINING MARITAL DEDUCTION

General Power of Appointment Trust

Prior to 1981, this was a well-known means of setting up a marital deduction qualifying trust. It is still a method of qualifying for the marital deduction. Pursuant to the terms of the trust, the spouse must receive all income and must be given a General Power of Appointment either during life or at death to distribute the assets in the trust at least to:

- Himself or herself,
- His or her estate,
- Creditors of his or her estate,
- His or her own creditors.

Estate Trust

The Estate Trust is a lesser used technique for qualifying for the Federal Estate Tax Marital Deduction. It requires that the assets remaining at the surviving spouse's death be distributed directly to the surviving spouse's estate. There is no requirement for mandatory distribution of income in the estate trust.

QDOT Trust for Non-U.S. Citizen Spouse

As noted in Chapter 1, if the surviving spouse is not a U.S. citizen, then the techniques used above for obtaining the marital deduction are not available. The only way that the marital deduction can be obtained for assets left to a non-U.S. citizen spouse is for the assets to be placed in a qualifying domestic trust (QDOT) [§2056(d)(2)].

COMMUNITY PROPERTY

There are nine states which are community property states in the United States. The laws in these states derive from the Spanish tradition or the original French law that applied. Each state's laws are slightly different, and, in some cases, dramatically different, from the laws of the other states.

In general, property in a community property estate is divided into separate property and community property. Separate property is property which the individual brought to the marriage or which the spouse received by gift or inheritance (after the marriage). The community property is property which was acquired during the term of the marriage (other than by gift or inheritance).

Typically each spouse "owns" 50% of the community property, even though the title to the property may be held in one spouse's name.

EXAMPLE 2-4:

- Couple was married in California and neither had significant property entering the marriage.
- Husband was employed and the wife was a homemaker.
- If the couple accumulated $900,000 during the course of the marriage by reason of the husband's earnings, all held in the husband's name, the property would nevertheless be community property.
- If the husband died, he would have the right to direct distribution of his share of the community property, namely $450,000.
- To reiterate, the wife would "own" $450,000 of the community property even though all of the property was in the husband's name.

In a community property estate, it nevertheless is advisable to follow the traditional AB planning. That is, the husband's will (or will and revocable trust) might typically provide:

> *This will governs the disposition of my interest in community property and my separate property. Upon my death, there shall be set aside from such property an amount equal to the unified credit exclusion amount. Such amount shall be distributed to the Credit Shelter Trust, with my wife as trustee, pursuant to Article 1.6. The balance of the estate shall be distributed outright to my wife.*

This will language is over-simplified, but it illustrates the main point—the set-aside of a Credit Shelter Trust from the first estate is sound planning in all 50 states including the community property states.

Chapter 3

Marital Planning—Additional Issues

REVOCABLE TRUST (LIVING TRUST)

As previously noted, there are two common approaches in providing for the disposition of property. The estate plan may be embodied in a will only, or the estate plan may contain a will and a revocable living trust. This second structure—a "two document structure"—is described below. The revocable living trust achieves similar goals, described below, for married couples, as well as single persons.

PROBATE AND PROBATE AVOIDANCE

States With Uniform Probate Code (UPC)

In states that have adopted the Uniform Probate Code (UPC), the probate system has been simplified and is generally much less expensive than in states which have not adopted the UPC.

The **probate** of a will is the presentation of the will to the court, the acceptance of the will, the appointment of the personal representative (or executor) and the approval of the distribution of assets. The process is simple and economical in states which have adopted the UPC. It is typically accomplished by the filing of pre-printed forms without a hearing. Generally, then, probate avoidance is not an appropriate goal in states which have adopted the UPC.

States Without Uniform Probate Code

In states without the Uniform Probate Code, probate is lengthy and expensive. Then probate avoidance through use of a revocable living trust should be recommended. The client establishes a revocable living trust during his or her lifetime.

In a state without the UPC, it is generally advisable to transfer the client's assets to the revocable living trust during lifetime—to "fund" the trust. When the client dies, no (or little) property passes under the will of the decedent (because the property has previously been transferred to the revocable trust). Therefore, the property does not pass "through probate." This method avoids the delays, expense and hearings of the difficult probate process.

CONFIDENTIALITY

Whether or not someone lives in a state that has the Uniform Probate Code or in a state which has high expenses for probate, the revocable trust is often recommended because it allows the client to maintain confidentiality about the disposition of assets upon his or her death. A will becomes a public record. The revocable living trust document is not public. When there is a funded revocable trust, the only public information available at death would be a will which would essentially name the executor of the estate, guardians of minor children, and a clause which "pours over" into the revocable living trust.

For example, Clause Seventh of President Eisenhower's will is such a "pourover."

> *SEVENTH: All the rest, residue and remainder of the property, both real and personal and wheresoever situate, of which I may die seized or possessed and to which I may be entitled at the time of my death, and all property over which I have power of appointment and disposition, which powers I hereby exercise in favor of my general Estate, I give, devise, and bequeath to the MERCANTILE-SAFE DEPOSIT AND TRUST COMPANY of Baltimore, Maryland, and JOHN S. D. EISENHOWER, and their successors, as Trustees, of a certain Indenture of Trust bearing date September 27, 1961, and as amended by Indenture dated May 5, 1965, between me, as Settlor, and said MERCANTILE-SAFE DEPOSIT AND TRUST COMPANY and JOHN S.D. EISENHOWER, as Trustees, as an addition to the principal of said Trust, to be held by said Trustees upon the trusts, terms and conditions set forth in said Indenture of Trust as amended.*

If the revocable living trust has been funded, there are no assets which are disclosed to the court because they are included within the trust rather than within the probate estate. In a state without the UPC, to the extent that the revocable living trust is not funded, then the assets which have not been placed in the revocable living trust would generally be disclosed as public records in inventories and accountings filed with the probate court.

In a state which has adopted the UPC, there is a requirement that an inventory of probate assets be prepared, but, generally, there is no requirement that the inventory be filed with the court. A result of using a will and an unfunded revocable trust in a UPC state is to keep the disposition confidential (the value of assets is automatically confidential because no inventory need be filed).

VEHICLE FOR MANAGEMENT OF PROPERTY

Another use for the revocable living trust is to assist with the management of property. The settlor of the trust may retain complete control of the assets during his or her lifetime, but vest management of the property in a co-trustee if the settlor wishes to remain as trustee, or in someone else as sole trustee to manage the property.

The revocable living trust can serve as a focused and organized way for the property to be managed when a client owns property but has little management experience, little skill in this area, little

interest, or, there are other circumstances (illness, incapacity) for which it is not advisable to retain the management of the property either temporarily or for lifetime.

Since the trustees can sign on behalf of the trust and hold legal title to the assets, the trustee has control over the assets and authority to deal with the assets consistent with the provisions of the trust agreement.

Durable Financial Power of Attorney

In contrast to a revocable living trust, another vehicle for management of property is the durable financial power of attorney. Under a durable power of attorney, as allowed by state law, the person (principal) names someone else (agent) who has full power over financial affairs and the financial power over his or her assets.

The power is not terminated in the event of incapacity or disability, so it is "durable." It terminates upon the death of the grantor of the power, or when he or she decides to terminate it. This is a useful device. It may be used in addition to, or even in place of, a revocable living trust. However, it is not always convenient to use because sometimes financial institutions or third parties are reluctant to recognize the durable power of attorney. Historically, a funded revocable living trust is a more readily accepted technique to manage property for an incapacitated person.

Conservatorship

If there is no trust or durable financial powers of attorney, and a person becomes incompetent to handle his or her financial affairs, then a court proceeding may be initiated to name a conservator or guardian. The management process in a conservatorship is similar to the probate process.

NEUTRALITY

Neutral for Tax Purposes

The revocable living trust is neutral for tax purposes. Because the settlor retains power to amend, revoke, name trustees, etc., the trust is treated as though the settlor is the legal title holder and owner for tax purposes. It is disregarded for tax purposes (§§2038, 671).

Neutral for Creditor Purposes

In most states the fact that the settlor retains complete control over the assets in the revocable living trust means that the assets are not protected from the settlor's creditors either during lifetime or at death.

SPECIAL POWER OF APPOINTMENT

GENERAL DEFINITION

The special power of appointment, as noted above, is a power which is exercisable by the holder in favor of any person or persons other than to the "prohibited four":

- Holder of the power,
- Holder's estate,
- Creditors of the holder, and
- Creditors of the holder's estate (§§2041, 2514).

PURPOSE

The purpose in allowing a special power of appointment is to let someone, usually the surviving spouse, provide for unusual and unforeseen future developments. A power of appointment is a provision, usually in a trust, which permits a beneficiary (the "holder" of the power of appointment) to specify which beneficiaries will later receive the trust property. That is, the power of appointment grants an individual the right to "appoint" the trust property to beneficiaries.

As previously noted, for tax purposes, powers of appointment are generally divided into a general power of appointment and a special power of appointment. If a beneficiary of a trust has a general power of appointment (which permits appointment of property to any of the "prohibited four" noted above), then the trust assets generally are subject to federal estate tax in the estate of the holder. If a beneficiary has a more limited "special power of appointment," then the trust estate is not subject to federal estate tax in the estate of the holder.

TYPES

Limited

In many cases the special power of appointment is limited to its exercise among the descendants. In this circumstance, the settlor of the trust or the testator protects his or her assets from new husbands or wives of surviving spouses, stepchildren, and charities or other interests. For example, each will might state:

> *In addition to other distributions authorized in this trust, the trustee shall make distributions to anyone or more of my descendants as my spouse may direct by a writing delivered to the trustee during her lifetime or by a provision in her will specifically identifying this special power of appointment, provided that no such distribution shall benefit, directly or indirectly, my spouse, my spouse's estate, my spouse's creditors, or the creditors of my spouse's estate.*

The assets are protected for the descendants but there is some flexibility in the event that unforseen circumstances occur. These circumstances might be a serious illness of a child or a grandchild which

requires more assets to be devoted to that child or grandchild, the spendthrift descendant, a child with a difficult spouse, or even one with a drug problem.

The surviving spouse can pick and choose among the descendants in a way that would protect assets and distribute them as the settlor or testator might have chosen had he or she been alive to do so. For example, the husband may die and the wife may survive for a period of 30 years. During that period of survivorship she may see her oldest child become very wealthy but the younger two children remain school teachers of modest means. Therefore she might exercise the special power of appointment over the Credit Shelter Trust and the Marital Trust as follows:

> *I was granted a testamentary special power of appointment over the trust estate of the Credit Shelter Trust and the Marital Trust. At my death, the remaining trust estate in the Credit Shelter Trust and the Marital Trust shall be distributed in equal shares to my two younger children (or to the descendants, by representation, of the younger child if mine predeceases me). I am exercising this testamentary special power of appointment in this manner because my oldest child, whom I love dearly, has become independently wealthy.*

Broad

The other option of the special power of appointment is to allow the holder of the power, again usually a surviving spouse, the right to appoint assets among **any** person or entity, other than the prohibited four, for any purpose. This, of course, bestows enormous discretion in the holder of the power.

For example, each will might include the following:

> *In addition to other authorized distributions in this trust, the trustee shall make distributions to any person or corporations as my spouse directs, by a provision in my spouse's will specifically identifying this special power of appointment, provided that no such distribution shall benefit, directly or indirectly, my spouse, my spouse's estate, my spouse's creditors or the creditors of my spouse's estate.*

Balanced Approach

The first two types set forth opposite poles for the usual discretion granted in a special power of appointment. Any group of interests can be selected in between those two poles.

For example, the power of appointment could be exercised among children, the spouses of children, and other descendants as well as any charities that the surviving spouse may select.

Most clients provide that Special Power of Appointment may be exercised only in favor of the client's descendants (children and grandchildren).

The major point to keep in mind is that there is an enormous amount of flexibility which can be granted either broadly or in a more limited manner. Factors to consider include the age of the settlor or testator and his or her surviving spouse, whether or not they have young children or grown children, whether grown children have already been given substantial assets or are successful and have substantial assets in their own right, health problems, and children with addictions or under undesirable influences.

Also, note that special powers of appointment do not have to be given to spouses. For example, a single person may want to give a special power of appointment to a trusted brother or sister, so that he or she could have the flexibility to appoint among a widower's descendants, as one example.

COORDINATION—OWNERSHIP OF PROPERTY

It is very important that the ownership of property be coordinated with the dispositive plan built into the will (or will and revocable trust). Indeed, one of the most common estate planning problems is that the ownership of property (the legal title) is not coordinated with the estate planning documents.

For a couple who own assets in joint tenancy with a right of survivorship, the property will pass automatically by operation of state law to the surviving joint tenant. The decedent's interest in the joint property does not pass under the decedent's will. Husband and wife may have a $1,000,000 investment account held in joint tenancy. It may be the intent that, if, for example, husband dies, his $500,000 interest in the account pass under his will --- to be used to help fill the Credit Shelter Trust. However if the $1,000,000 investment account is held in joint tenancy, the entire $1,000,000 account will pass automatically to the surviving wife (as surviving joint tenant) and will not be available to help fill up the Credit Shelter Trust.

EXAMPLE 3-1:

- A couple has an estate of $2,200,000.
- Couple has established an estate plan with traditional AB planning—the set-aside of the applicable credit amount from the first estate.
- All of the couple's assets are owned in joint tenancy.
- If the husband dies, all of the property will pass automatically to the surviving wife as joint tenant.
- No funds will be available to fund the Credit Shelter Trust (and to make possible the federal estate tax saving at the second death).

Ownership as Tenants in Common

It is generally preferable for a couple with AB estate planning to own property as tenants in common. If property is owned as tenants in common, the property is owned 50% by each person.

Upon the death of a tenant in common, the decedent's one-half interest does not pass automatically to the survivor but rather passes under the will (or will and revocable trust) of the decedent. That is, the decedent's interest in the property **can** pass to the Credit Shelter Trust.

Positioning Each Spouse to Use Applicable Credit Amount

One of the common issues facing a married couple as they prepare an estate plan is to create ownership and title of property so that each spouse effectively uses his or her applicable credit amount. This is necessary so that, whichever spouse dies first, the full amount which can be placed in the Credit Shelter Trust and avoid federal estate tax is available to be put into the Credit Shelter Trust. In 1999, the ideal would be if each spouse owned at least $650,000 in his/her name—so that if a spouse died the surviving spouse could fully use the $650,000 exclusion amount from the unified credit, allocating these assets to the Credit Shelter Trust.

EXAMPLE 3-2:

- Husband and wife have combined assets worth $2.1 million, but $2.0 million of it is in the husband's name.
- If the wife predeceases the husband, there can only be $100,000 allocated to her Credit Shelter Trust. The Credit Shelter Trust is "underfunded."
- In 1999, this creates a lost opportunity for placing an additional $550,000 into the trust which eventually would pass free of federal estate tax to the children.

The **tax effectiveness** can be shown as follows:

Husband's Estate:	$2,000,000
Wife's Estate:	$100,000

- **Scenario 1**:

Wife dies first in 1999: No federal estate tax at her death. $100,000 passes to her Credit Shelter Trust.

Husband dies second in 2000: Gross estate is $2,100,000.
Taxable estate is $1,325,000.

Approximate total tax on husband and wife = $530,000

- **Scenario 2:**

Husband gives wife $550,000.

Husband's estate:	$4,250,000
Wife's estate:	$650,000

Wife dies first, using marital deduction and credit shelter trust in 1999. $650,000 passes to Credit Shelter Trust established under her will.

Federal estate tax: 0

Husband dies in 2000.

Gross estate:	$1,450,000
Taxable estate:	$775,000
Federal estate tax:	$310,000
Federal Estate Tax Savings	$220,000

COORDINATION OF BENEFICIARY DESIGNATIONS

LIFE INSURANCE

When life insurance is included in the estate of the insured, it is often a problem to name the spouse as the beneficiary. Such a beneficiary designation limits the assets which may be allocated to the Credit Shelter Trust. The amount of life insurance is often large compared to the other assets and there will be an overfunding of the marital share and lost opportunities to fully fund the Credit Shelter Trust.

In the situation described above, the estate, or better yet, a revocable living trust created for that purpose, should be named as beneficiary of the life insurance. If a revocable living trust has been created, then the trust should be the beneficiary of the life insurance policy. This gives maximum flexibility to the executor, personal representative or trustee to properly fund the Credit Shelter Trust.

Often children are named as contingent beneficiaries after the spouse of the life insurance. This creates another problem if the children are not adults at the time of death; it will be necessary to set up a mechanism under state law to manage these assets for minors and they are often not as flexible or as convenient as the trusts that the decedent could have set up in a will or in a revocable living

trust. Often the life insurance is a substantial asset and it may be required to be distributed to the child at age 18, and in all cases no later than at age 21; it is often unwise to distribute assets, particularly cash, to someone so young.

For example, husband and wife have a relatively modest estate of $500,000 which includes $100,000 in investment assets and $400,000 in a term life insurance policy on husband's life. The beneficiary designation on the husband's life insurance policy is: wife, or if wife is not surviving, the children in equal shares. Husband and wife each have a will which would channel the eventual estate into trusts for the children, to be managed by a family member as trustee with eventual distribution to the child at age 30. Husband and wife both die and the two children are 19 and 18 years old. The $400,000 of life insurance proceeds will pass directly to each child. This can be a destructive influence.

To reiterate, where the insured owns the policy, the estate of the insured or the trustee of the revocable living trust is the recommended beneficiary for life insurance proceeds in most cases. This beneficiary designation will channel the life insurance proceeds into the provisions of the will or revocable trust. In the example above, this beneficiary designation would channel the proceeds into the trusts for the children and to be managed by a family member until each child reached age 30.

QUALIFIED RETIREMENT PLANS

This same issue—the importance of beneficiary designations in the estate plan—is also seen in qualified retirement plans, 401(k) plans, and IRAs. The disposition of these assets is not governed by the will (or will and revocable trust). Rather the disposition of these assets is governed by the beneficiary designation.

For these qualified plan assets, income tax considerations must be addressed. If a qualified plan asset is withdrawn, it is considered a "distribution" and triggers the income tax. However, if the qualified plan assets are paid to the surviving spouse as the named beneficiary, then there may be no income tax due. If the qualified plan assets are paid to a beneficiary other than the surviving spouse, income tax is due (although in some cases it may be deferred).

Stated differently, Qualified Retirement Plans, 401(k)s and IRAs are all eligible for a spousal rollover. They should not be used to fund the Credit Shelter Trust. The estate planner should verify that the beneficiary of these types of plans is the surviving spouse. The goal is to defer the payment of income taxes on the plans for as long as possible.

If any other beneficiary, such as the estate or a trust or children, is named as beneficiary of these types of plans, then at the time of death the income tax has to be paid on the entire amount in these plans and the chance to obtain the deferral of the income tax is lost.

Generally the estate of the plan participant, or a revocable living trust set up by the participant is named as the contingent beneficiary if the spouse does not survive the participant.

In most cases, this implements the true wishes of the participant in that all of the assets, if there is no surviving spouse, are subject to the directions of the will or the trust and are placed in trust for beneficiaries if that is appropriate or distributed outright if the beneficiaries are then old enough to handle the type and size of assets that the proceeds may represent.

POSTMORTEM PLANNING—DISCLAIMER

FUNDING THE CREDIT SHELTER TRUST

In the event that the ownership of the property and the beneficiary designations on life insurance and retirement plans have not been implemented effectively before death, it is sometimes possible to have the surviving spouse or other beneficiaries **disclaim** assets in order that they become part of the estate and available to fund the Credit Shelter Trust fully.

The time period for making an effective disclaimer is governed by state law and state law requirements for making an effective disclaimer must be followed. Since the federal estate tax return is due nine months after death, as a practical matter the disclaimer usually has to be made prior to the nine-month deadline. Disclaimers are voluntary actions by the beneficiaries.

EXAMPLE 3-3:

- Husband and wife have estate planning documents which set aside the applicable credit amount in a Credit Shelter Trust, with the rest in a Marital Deduction Trust.
- Couple's entire estate is composed of $2,000,000 of assets held in joint tenancy.
- If the husband dies, in most states the wife as surviving joint tenant may **disclaim** the husband's interest in joint tenancy property which would otherwise pass to her.
- That interest, namely $1,000,000, then passes as part of the husband's estate—that is under the husband's will.
- Of the $1,000,000 of assets, the appropriate amount may be allocated to the Credit Shelter Trust.
- In effect, the wife disclaims the right to enjoy the property as the surviving joint tenant, but later claims the right to enjoy the property as beneficiary under the Credit Shelter Trust.

In Example 3-3, absent a disclaimer, the entire $2,000,000 estate will pass to the wife as the surviving joint tenant. No property will pass under the husband's will and there will be no assets allocated to the Credit Shelter Trust. The result of disclaimer will be (in 1999) that $650,000 will be allocated to the Credit Shelter Trust and $350,000 to the Marital Trust. This disclaimer will enable the family

to take advantage of the deceased husband's $650,000 unified credit, positioning these assets so that they will eventually pass free of federal estate tax to the children.

The postmortem technique—disclaimer—often makes it possible to fill the Credit Shelter Trust where the ownership of property in joint tenancy or the naming of the spouse as beneficiary under a life insurance policy jeopardizes the couple's tax planning.

Chapter 4

Gifts

BASIC RULES

UNIFIED SYSTEM

The federal estate tax and the federal gift tax systems are a unified system. With some exceptions for gifts which are described below, the applicable credit (or exclusion) amount for making gifts during lifetime and the applicable credit (or exclusion) amount for transfers at death are the same. The exclusion amount can be used during lifetime or at death. The unified system has been in effect since the Tax Reform Act of 1976 (§§2001, 2502).

Valuation

The value of the gift is determined at the time of the gift and is established with Form 709, the federal gift tax return. There is a three-year statute of limitations for gift tax returns. When the statute of limitations has run, the value of the gift is firmly established if a gift tax has been paid or assessed.

Before TRA'97 the IRS had taken the position that it could revalue gifts for purposes of federal estate tax. However TRA'97 established the value of the gift on Form 709 as its value and once the statute of limitations has expired, the gift cannot be revalued [§2001(f)].

The value of the gift is an important factor to consider in an estate plan because the future appreciation of an asset (gift) can be shifted to the beneficiary and removed from the donor's estate. Also, the associated future income (and income taxes) can be shifted from the donor to the donee by transfers of income generating property.

Rate

Technically, the unified rates in effect for 1987 and subsequent years range from 18% to 55%. However, because the applicable credit amount must be applied against the first transfers, the effective minimum rate is actually 37%. The actual rate at which a transfer is taxed depends upon the aggregate amount of transfers which were previously made by the donor.

The most important principle to keep in mind is that the federal gift tax rates are the same as the federal estate tax rates. In prior years (prior to 1976) the federal gift tax rates were lower so that there was an incentive to make taxable gifts during lifetime to obtain the lower federal gift tax rates. This is no longer the case.

What Is a Gift?

Gifts, whether in trust or outright, are transfers of property that can be tangible or intangible, real or personal. Generally taxable gifts are taxable to the donor (§2511).

The donor must part with dominion and control over the property in order for a gift to be complete [Reg. §25.2511-2(b)]. An incomplete gift is not a gift for federal gift tax purposes.

For example, placing assets into a joint tenancy bank or brokerage account in which either of the joint tenants may sign to make withdrawals or transfers without the consent of the other represents an incomplete gift—the donor has not relinquished dominion and control over the property. Similarly, writing a check to the donee, without the delivery and cashing of the check, generally constitutes an incomplete gift.

Contrary to many other state laws and common law, donative intent is not a required element of the definition of a gift in determining whether or not the transfer is taxable as a gift.

Gift-Splitting

Under current federal gift tax law, a donor and his or her spouse can split the value of a gift between them even though the property is titled in the name of only one of the spouses (§2513). The effect of this is to double the annual exclusion, which is described below, and to double the amount of available unified credit amounts which are available for lifetime gifts.

If the spouse consents to split any gifts in any particular year, then all gifts made within that year by either spouse must be split.

Gift-splitting requires the consent of both spouses on a gift tax return, Form 709. This must be done before a notice of deficiency is sent to either spouse. In practice, many spouses who agree to gift-splitting do not file returns for gift-splitting annual exclusion gifts. They count on a notice from the IRS prior to the filing of a notice of deficiency.

Applicable Credit Amount

As noted above, the credit amount for federal gift tax purposes is the same as the credit amount for federal estate tax purposes and is being increased each year. The 1999 applicable credit exclusion equivalent amount is $650,000. (See Table B in Chapter 1.)

If an individual makes gifts during his lifetime and uses $300,000 of his applicable credit exclusion amount, then (in 1999) only $350,000 of applicable credit amount protection remains to shield additional gifts from gift tax and testamentary transfers from the federal estate tax.

MARITAL DEDUCTION

There is an unlimited interspousal marital deduction which is available for gifts. This is available for gifts made after 1981. It is available only if the donee spouse is a U.S. citizen. If the gift is in trust, the trust must meet the requirements which are similar to those trusts which are qualified for a federal estate tax marital deduction (mandatory income, spouse as only beneficiary, etc.). Gifts to spouses in trust may require that a gift tax return be filed claiming the marital deduction; outright gifts do not (§2523). (There is a $101,000 annual exclusion for a gift to a spouse who is not a U.S. citizen.)

INCOME TAX CONSIDERATIONS

A gift is not income to the donee of the gift (§102).

Gifts to Charity

Outright gifts to charity may be made without any imposition of federal gift tax. However, there are income tax considerations.

General Rule

The charitable deduction is limited to a percentage of the individual's "**contribution base**." "Contribution Base" is the donor's AGI (adjusted gross income) computed ignoring any net operating loss carryback [§170(b)(1)(F); §172]. Such percentage is determined by two factors: the type of organization (50% or 30%) and the type of property donated. Any charitable gift in excess of the percentage limitation for the tax year may be carried forward (but not back) for a period of five years [§170(b)(1)].

50% Charity

The contribution to a 50% organization (church, educational institution, etc.) qualifies for the maximum deduction of 50% of a taxpayer's contribution base for the taxable year [§170(b)(1)]. Even for such a public charity, there is a special 30% limitation on the contribution of certain capital gain property (§170).

30% Charity

The deduction associated with a contribution to a 30% charity (like a private non-operating foundation) is limited to the lesser of:

- 30% of the taxpayer's contribution base, and
- Excess of 50% of the taxpayer's contribution base for the tax year over the amount of charitable contributions qualifying for the 50% deduction ceiling, including carryovers [§170(b)(1)].

Gifts of capital gain property to these organizations are subject to a 20% limitation.

EXAMPLE 4-1:

- James had a contribution base of $1 million and made charitable contributions to a public charity in that year of $420,000.
- He also wants to make a cash contribution to a private foundation.
- The deduction limitation on cash contributions to the private foundation would be the lesser of:
  - 30% of the taxpayer's contribution base ($300,000), or

Excess of 50% of the taxpayer's contribution base for the tax year ($500,000) over the amount of the contributions qualifying for the 50% deduction ($420,000).

  - Only $80,000 of the contributions to the private foundation would qualify for a charitable deduction in that tax year.

For these purposes, ordinary income property is property that, if sold at its fair market value on the date of contribution, would give rise to ordinary income or short-term capital gain. Capital gain property includes any assets in which a long-term capital gain would have been realized if the taxpayer had sold the asset for its fair market value on the date of contribution.

A deduction equal to the **fair market value** (not basis) of qualified appreciated stock contributed to a private non-operating foundation is allowed for contributions made during certain periods, since the law has been extended and is now permanent [§170(e)(5)].

Qualified appreciated stock is unrestricted publicly traded stock that is capital gain property. There are family attribution rules and no more than 10% of the corporation's outstanding stock may be given.

A charitable contribution may be deducted against capital gain income. If a person's only income in the tax year was $5,000,000 of capital gain income and the person contributed $2,000,000 of cash to a public charity, then the person would have $3,000,000 of taxable income, resulting in income tax of $840,000.

Basis Considerations

With respect to property transferred by way of gift, the basis of the property in the hands of the donee is the same as the basis of the property in the hands of the donor. That is, the donee takes a "**carryover basis.**"

By contrast, when a person dies the property which is part of the decedent's taxable estate for federal estate tax purposes receives a new basis equal to the net fair market value at the date of death. Accordingly, the recipients of testamentary transfers acquire property with a "**step-up**" in basis. This distinction—that property received by gift has a carryover basis but property received by testamentary transfer has a stepped-up basis—is critically important in structuring a gift program. Particularly for an older donor with highly appreciated property, the planner must give careful attention to the basis consequences of gifts. The gifts of property to children and grandchildren may remove the donated property from the donor's taxable estate, and hence save federal estate tax, but the gifts lose the opportunity to obtain a step-up in basis which would occur if the property were transferred by will. For older donors, it is often preferable to make gifts of cash or high-basis property.

ANNUAL EXCLUSION AND QUALIFIED TRANSFERS

Amount

In general, each year each donor may exclude from what would otherwise be taxable gifts $10,000 of present interest gifts to as many donees (who may or may not be related to the donor) as the donor wishes [§2503(b)]. For example, a grandfather with three children and six grandchildren may give $90,000 each year of present interest annual exclusion gifts to his family members. Under the Taxpayer Relief Act of 1997 this $10,000 amount is due to be adjusted beginning in 1999 to the nearest thousand, based upon a cost of living adjustment.

A program of annual exclusion gifts is often advisable for a couple with substantial estates.

EXAMPLE 4-2:

- Grandmother and grandfather have a combined estate of $5,000,000. If both grandparents live until 2006, and use AB planning, there will be at least $3,000,000 of property subject to federal estate tax in the second estate.
- To reduce that amount and the eventual federal estate tax, the classic strategy is for the grandparents to make $10,000 a year gifts to each family member.
- For grandparents with three children and six grandchildren, the couple together may give $180,000 each year free of federal gift tax.
- Pursued over a course of ten years, this would shift $1,800,000 (plus the income and appreciation associated with such assets) from the taxable estate(s) of the grandparents.

Although a program of annual exclusion gifts often is advisable for a couple with a large estate, it is important to keep in mind at least two other factors:

- A couple should not make gifts which jeopardize long-term financial security. Generally a systematic program of annual exclusion gifts is advisable for a couple (or individuals) who are very rich or very old.
- The financial/emotional impact on the recipient should be considered carefully. Will annual gifts influence the recipient to abandon a program of education or a good employment opportunity? How will systematic gifts to the adult child affect his or her spouse?

TUITION

Payments of tuition for any donee made directly to a qualifying educational institution for the education of a donee are also exempt from gift taxes. Such a tax-free gift is a so-called qualified transfer; it is in addition to the $10,000 annual exclusion. The payment cannot be made to the donee but must be made directly to the institution [§2503(e)].

HEALTH CARE

Payment for the medical expenses of anyone may be made directly to the caregiver and again the exclusion is unlimited [§2503(e)]. Such a payment is also a qualified transfer.

RETURNS

There is no gift tax return required for annual exclusion gifts, provided there is no gift-splitting (§6019). However, some people prefer to file a gift tax return even when none is due, in order to start the running of the statute of limitations.

PRESENT INTEREST REQUIREMENT

ANNUAL EXCLUSION ONLY ALLOWED FOR GIFTS OF PRESENT INTEREST

Any possible delay in the enjoyment of the property by the donee results in a future interest and future interests do not qualify for the annual exclusion [§2503(b)]. This factor often applies to gifts in trust.

For example, assume a grandfather established a trust for his ten-year-old granddaughter. Assume the trust provides:

> *The trustee shall accumulate the income and principal until my granddaughter is registered in an accredited college. Thereafter the trustee shall use the income and principal to pay for the tuition, room,*

> *board, books, supplies and transportation incurred in the undergraduate college education of my granddaughter. This trust shall terminate when my granddaughter attains 25 years of age or upon her death, whichever first occurs. Upon termination the remaining trust estate shall be distributed to Iowa State University.*

If the grandfather were to make $10,000 gifts each year to this trust, the gifts would not qualify for the annual exclusion. The granddaughter has no "present interest" in the property; she will not be entitled to receive distributions of income and principal until many years in the future.

A gift can be split between the gift of the present interest and the future interest. The right to income from a trust, for instance, may be a gift of present interest but the value of the remainder interest which is distributed sometime in the future is not a present interest. Even if the income interest qualifies, the remainder interest would not qualify for the exclusion.

Trusts

There is an exception to the present interest requirement which permits establishment of a certain type of trust which does qualify for the $10,000 annual exclusion even though the beneficiary does not have a present interest [§2503(c)]. There are two types of trusts which qualify under the Internal Revenue Code, each trust is one established for a minor and one which meets certain requirements.

In a 2503(c) trust, the minor is not required to receive benefits from the trust until age 21. The funding of this type of trust can qualify for the gift tax annual exclusion. Many 2503(c) trusts which hold significant assets allow the beneficiary to make a demand for a limited time period at age 21, and if he or she fails to do so, the trust continues until the beneficiary is older, or for the beneficiary's lifetime.

The Uniform Transfers to Minors Act is also known as Uniform Gifts to Minors Act (UTMA or UGMA). Accounts established under UTMA or UGMA are also known as "Statutory Trusts."

Gifts can be made to minors which are set up under UTMA or UGMA for the benefit of a minor. State law controls UTMA and UGMA. Most banks and many stock brokers have UTMA accounts which are set up as allowed under state law. The beneficiary alone must receive the benefit of the assets. Distribution of all of the assets must be made at age 21. Someone other than the donor should be the custodian of the account. A gift to a UTMA or UGMA account qualifies for the $10,000 annual exclusion.

Crummey Withdrawal Rights

It is often the wish of the donor to create a trust for a family member which does not terminate when the beneficiary reaches age 21. Such a trust may provide, for example, that the income and principal may be used for the college and graduate education of the donee and later for the health and support of the donee.

Since the donee is not to receive property immediately, the gift would not ordinarily qualify as a "present interest" and therefore would not be eligible for the $10,000 annual exclusion. To create a present interest (and qualify for the $10,000 annual exclusion) such a trust is often structured by giving the donee (or other family members) the right to withdraw the donated amount for a 30-day period subsequent to the gift.

This technique was first developed by the Crummey Family and was approved by the Tax Court. These rights of withdrawal (Crummey rights) are discussed in Chapter 5.

PLANNING STRATEGIES

ANNUAL GIFTS

Substantial assets may be transferred to the donor's family tax-free through a plan using the annual exclusion amount each year over a number of years. If spouses agree to gift-split, $20,000 per year, per donee, as adjusted in the future for inflation, may be transferred without gift or estate tax.

LARGE GIFT—APPLICABLE CREDIT

The use of the applicable credit amount for gifts is often advisable in large estates. Future appreciation of the asset can be removed from the donor's estate and transferred to younger family members. Such a gift—using the applicable credit amount—may be a major element in the estate plan of a wealthy family. The father and mother may not only make annual gifts of $20,000 per family members but may also make gifts using the applicable unified credit amount. In 1999 two parents together could transfer a total of $1,300,000 to family members (in addition to $20,000 a year annual exclusion gifts). As noted below, such large gifts might be of stocks and bonds, of interests in appreciating real estate, or of interest in a family partnership. To reiterate, the key to this planning is that a large gift of property shifts the appreciation on that property to the second generation (and often to the third generation) free of any federal transfer tax.

In very large estates, it may be good planning to use the applicable credit amount, and then continue to make gifts and pay the gift tax. The amount of the gift tax paid is then removed from the taxable estate at death (except within three years of death). The advantage of a taxable gift may be illustrated by the following (slightly oversimplified) example.

Consider a single parent who has already used her unified credit amount with prior gifts. If she makes a gift of $3,000,000 to her son, there will be federal gift tax of approximately $1,000,000. The $3,000,000 transfer will result in $2,000,000 to her son and $1,000,000 to the IRS.

By contrast, if the single parent keeps the $3,000,000 and the funds are included in her eventual taxable estate, the $3,000,000 will be subject to federal estate tax. The federal estate tax will be approximately $1,500,000. The testamentary transfer will result in $1,500,000 to her son and $1,500,000 to the IRS.

The reason for this difference is noteworthy—the funds used to pay federal gift tax are not themselves subject to federal gift tax. The funds used to pay federal estate tax are subject to federal estate tax. Given this difference, there are circumstances (generally older clients with very large estates) in which the making of a taxable gift is a sound strategy.

VALUATION STRATEGIES—DISCOUNTING

FAMILY LIMITED PARTNERSHIPS

Family limited partnerships are often used to hold the parents' investments. In some states limited liability companies and limited liability partnerships are also used. The LLC and LLP are not recognized in all states, so we will discuss only the family limited partnership (FLP).

A major purpose of the FLP is to discount the value of the investments for federal gift and estate tax purposes.

EXAMPLE 4-3:

- Alan and Alice each own $500,000 of stocks and bonds and other assets of substantial value.
- If Alan makes a gift of $20,000 of IBM stock to his daughter, the value for gift tax purposes is $20,000.
- If either Alan or Alice die without making gifts, $500,000 of securities is included in the estate.

EXAMPLE 4-4:

- Alice and Alan each contribute $500,000 to an FLP, each retaining a 5% general partnership interest and a 45% limited partnership interest.
- Alan then makes a gift of a 3% limited partnership interest to his daughter. However, the minority interest in the FLP is discounted for valuation purposes.
- The daughter receives a nonvoting minority interest in the partnership. Usually it is nonmarketable. The IRS usually allows a discount of 15% to 35%.
- The 3% interest, nominally worth $30,000, is discounted and valued at closer to $20,000 for federal gift tax purposes.
- If either Alan or Alice die without making gifts, the 45% limited partnership interest is nominally worth $450,000.
- However, the same discount is applied, and the value for estate taxes would be more in the range of $250,000 to $350,000.

Creditor Concerns

A limited partnership interest in an FLP may also serve as a barrier to future creditors and protect the assets. If a creditor obtained a judgment against Alan and Alice's daughter, the limited interest can be attached by the creditor with a judgment against the limited partner, but the creditor cannot foreclose upon and take title in the limited partnership interest. The creditor becomes an assignee of but not the owner of the interest, and the creditor may be required to pay income tax on his or her share without necessarily being entitled to cash distributions from the partnership. Sometimes this feature can encourage a favorable settlement.

FLP Structure

The FLP agreement could name Alan and Alice, or either of them, as managing partners. Ownership of partnership interests could be restricted to family members. If a child were to be divorced, there could be restrictions in the FLP agreement to protect ownership from passing to the child's spouse.

Alan and Alice can make the management and investment decisions and use their annual exclusions and unified credits to transfer the securities at a discounted value to children or other family members and reduce their taxable estates. Or, if either dies, and gifts have not been made, the discounted value in the estate may be transferred with less tax cost.

Personal Residence Trusts

An individual may transfer a residence to a trust while retaining the right to use the residence for a specific term of years and directing distribution of the residence to his or her children on termination of the trust (§2702).

At the time of the transfer to the trust, the owner is treated as having made a gift to the beneficiaries. The amount of the gift is the fair market value of the residence on the date of the transfer reduced by the value of the right to use the residence for the trust term and the right to receive ownership of the residence if death occurs during the trust term. A gift tax return is required. The owner continues to be treated as the owner of the residence for income tax purposes.

If the owner outlives the trust (and if the owner may still reside in the residence after trust termination), the value of the residence is not included in the value of the "owner's" estate for federal estate tax purposes. Only the value of the gift, as of the time of the transfer, is part of the calculation of the estate tax.

If the owner dies during the trust term, the residence is returned to the estate and included in the estate at its value on the date of death. The potential estate tax savings are lost, with the owner in the same position for estate tax purposes as he or she would have been if the trust had not been created.

If the owner no longer wishes to live in the residence on termination of the trust, the children, as the new owners, may sell the residence and use the proceeds as they wish. If the owner wants to

continue to live in the residence, he or she may lease the residence from his or her children at a fair market value rent. The lease payments reduce the assets in the owner's estate.

On termination of the trust, the children receive ownership of the house without any income, estate or gift tax consequences to them. The children's basis in the residence is the basis of the owner on the date of the transfer to the trust.

An individual can contribute a primary residence or vacation residence to a personal residence trust. Each individual may have two personal residence trusts.

EXAMPLE 4-5:

- Dan and Deborah own a home in which they wish to live now, but leave to their children. Dan was born in 1935 and Deborah was born in 1938.
- They own the home as tenants in common and the home is worth $300,000.
- They each put their share of the home into a qualified personal residence trust in November 1997, retaining a term of 15 years.
- The value of the gift for federal gift tax purposes was approximately $35,900 for Dan and $32,600 for Deborah, rather than $150,000 each.
- (The gift is valued in accordance with §7520 taking into account present value, term and remainder or reversing interest.)

CHARITIES

Most outright charitable gifts received income tax, gift tax and estate tax deductions.

In addition, certain gifts in trust and gifts of remainder interests receive favorable tax treatment. These include charitable remainder annuity trusts, charitable remainder unitrusts, pooled income funds, and private foundations.

The detailed methods of structuring these types of gifts is outside the scope of this book.

STATUTE OF LIMITATIONS GENERALLY

In general, the statute of limitations is three years from the date a gift tax return is filed and any gift tax is paid.

Disclosure Requirement/Statute of Limitations

For any gift which is valued under either §2701 or §2702, the transferor must not only file a gift tax return but disclose the transfer on the return in "a manner adequate to apprise the Secretary of the nature of the transaction" to start the statute of limitations running. This is true even for gifts which qualify for the annual exclusion.

In general, §2701 applies to a transfer of a junior equity interest to or for the benefit of the transferor's family, where the transferor, his or her spouse, or a "senior family member" retains a preferred interest to distributions. It is applied to determine whether a gift has been made and the value of the gift.

Section 2702, in summary, applies to transfers in trust to a family member where the transferor retains an interest in the trust.

PREMORTEM STRATEGY

NO THREE-YEAR RULE

There is no disadvantage to making gifts within three years of death in most cases. The gifts remove assets from the donor's estate and save estate taxes.

EXAMPLE 4-6:

- Assume grandmother is 84 years old and has an estate of $2,100,000 but has done little estate planning. Further, assume grandmother has been diagnosed with a terminal illness.
- If the grandmother has 15 family members (including children, grandchildren, and in-laws), she may make a $10,000 gift to each family member, taking advantage of the $10,000 annual exclusion. Even if grandmother makes the gifts on Monday and dies on Tuesday, the $150,000 has successfully been removed from her estate; the associated federal estate tax saving would be approximately $70,000.

Exceptions

Gifts of insurance policies, certain powers of appointment, and certain transfers involved with §303(b) and §2032A are brought back into the estate at death, if given within three years of death. Also, amounts paid as gift tax within three years of death are brought back into the estate at death.

Durable Power of Attorney

If an incompetent person has made a durable power of attorney prior to becoming incompetent, then the agent under the power of attorney may make gifts for the incompetent person, if expressly allowed by the terms of the durable power of attorney and state law. The IRS has taken a particularly intransigent position on this issue. If the power of attorney permits the agent to "take any legal steps which I may take," the IRS finds that is not sufficient to authorize the agent to make gifts which are binding for federal gift tax purposes. The power of attorney must expressly permit the agent "to make gifts."

Chapter 5

Insurance Planning

BASIC RULE

INCIDENTS OF OWNERSHIP

The full amount of the proceeds of any life insurance policy in which the insured owned any incident of ownership is included in the insured's estate at death for federal estate tax purposes (§2042).

The incident of ownership may be possessed by the insured either alone or in conjunction with another.

The incidents of ownership include:

- Right to name a beneficiary,
- Right to surrender the policy,
- Right to change the beneficiary,
- Right to assign the policy, and
- Right to borrow against cash values in the policy.

Incidents of ownership may also be broader than these listed issues. A reversionary interest in the policy would also bring all of the proceeds of the policy into the decedent's estate (§2042).

If the corporation owns the life insurance policy on the shareholder, and that shareholder owns more than 50% of the total combined voting power of the corporation, then the incidents of ownership are attributed to the shareholder. This would cause the insurance policy to be included in the estate to the extent that the proceeds are not paid directly to the corporation or to a third party for a valid business purpose.

Right to Purchase

The right to purchase a policy which is payable to the insured or the insured's spouse may also be an incident of ownership. This situation arises where the employer has decided to cancel a policy or to stop paying the premiums and the insured would like to continue to have the policy in place.

The typical buy/sell or key man provisions are usually excepted from this inclusion because the employer is the owner and the beneficiary of the policy (PLR8049002). Also if the corporation exercises a right to acquire the shareholder's stock and the insured shareholder then exercises the right to purchase the policy, under PLR 8049002 this is not an incident of ownership.

The ownership of life insurance by the insured can result in significant federal estate tax.

EXAMPLE 5-1:

- Couple has a net worth of $3,000,000, including a $750,000 term life insurance policy on the husband's life.
- If the couple has traditional AB planning documents, there will be no federal estate tax on the first estate. If both die, there will be federal estate tax on the amount which exceeds the combined applicable credit amounts.
- Even if the couple survives until 2006, there will be federal estate tax on at least $1,000,000 of assets. The substantial federal estate tax bill results, in part, because the husband owns the $750,000 term policy on his life.
- It would be preferable if there were independent ownership of the policy. It is not necessarily an advantage, however, for the wife to own the policy.
- Assume the husband transfers ownership of the $750,000 policy to the wife and then the husband dies. The proceeds will be payable to the wife (otherwise she has made a taxable gift).
- The $750,000 of proceeds and the associated investment assets become part of her estate.
- There is no federal estate tax saving associated with the wife owning the policy on the husband's life (if the husband dies first).

In addressing this insurance planning, consideration should be given to the independent ownership of the life insurance policy by an independent person.

IRREVOCABLE LIFE INSURANCE TRUST—POLICY ON ONE LIFE

PURPOSE

The purpose of the irrevocable life insurance trust is to obtain the benefit of the life insurance proceeds for the beneficiaries of the irrevocable life insurance trust without subjecting the proceeds to federal estate taxes in the estate of the decedent-insured or in the estate of the surviving spouse. Proceeds held in an irrevocable life insurance trust, and the associated investment assets, escape federal estate tax on the eventual transfer to the children.

For the couple in the example above, AB planning may enable the couple eventually to shield $2,000,000 from the reach of the federal estate tax. Ownership of the $750,000 life insurance policy in an irrevocable insurance trust will make it possible for the couple to protect an additional $750,000 from the federal estate tax.

STRUCTURE OF TRUST

Trust

An irrevocable life insurance trust is an irrevocable trust established during the lifetime of the insured. Typically the insured person is the settlor of the trust.

Trustee

The trustee must be someone other than the insured because the insured may not have incidents of ownership in the policy. Typically, the spouse or an adult child is the trustee.

Operation During Lifetime

During the lifetime of the insured-settlor, an irrevocable life insurance trust is typically relatively passive. The trust owns the policy. The premiums may be paid on an annual basis. Generally there are no distributions of income or principal to the family.

Income and Principal Distributions During Surviving Spouse's Lifetime

The irrevocable life insurance trust generally provides that upon the death of the insured, the proceeds (and associated investment assets) will be held in trust for the surviving spouse and often for the children.

After the death of the insured, the irrevocable trust is much like a Credit Shelter Trust. There may be distribution of income and principal for the health, support, maintenance, and education of the surviving spouse and children. The surviving spouse may have a special power of appointment—to provide the flexibility to adjust to later developments in the personal and family circumstances of the children.

Upon the death of the surviving spouse, the trust estate is distributed to the remainder beneficiaries, typically the children and grandchildren, and usually in trust. Distributions to the grandchildren can present significant generation skipping transfer taxes which will be discussed in the next chapter.

From a federal estate tax perspective, the key is that the investment proceeds held in the irrevocable insurance trust are **not** included in the taxable estate of the surviving spouse. Like a Credit Shelter Trust, the irrevocable insurance trust makes it possible to pass assets to the second and third generation free of federal estate tax. This can be powerful planning.

PAYMENT OF PREMIUMS

Present Interest Requirement

To make possible the annual premium payments, the settlor-insured generally makes gifts each year to the trust. Depending on the structure of the trust, these gifts may qualify for the annual exclusion. As noted above in the chapter on gifts, in order to obtain the annual exclusion for gifts, the gifts must be a gift of present interest [§2503(b)].

In order to pay the premiums on the policy during the insured's lifetime, gifts must be made to the trust of assets from which the trustee can pay the premiums on the policy. Because there are no current income or principal distributions during the lifetime of the insured, the enjoyment of rights under the trust are postponed. Therefore, "Crummey powers" are needed so that the gifts of the amounts to pay the premiums each year are qualified as annual exclusions.

Crummey Withdrawal Rights

In the *Crummey* case [397 F.2d 82 (9th Cir. 1968)], beneficiaries were given an immediate right to withdraw assets which were added to a trust. The right of withdrawal extended for a period of 30 days and then lapsed. The beneficiaries did not demand or withdraw any of the contributions to the trust, but the court held that the gifts to the trust were gifts of present interests. This resulted because the beneficiaries had a legally enforceable right to demand and withdraw the contributions to the trust under the terms of the trust document.

Eventually the Internal Revenue Service acquiesced to the holding in *Crummey* provided that in the cases involving minor beneficiaries there is "no impediment under the trust or local law to the appointment of a guardian and the minor donee has a right to demand distribution" (Rev. Rul. 73-405, 1973-2 C.B. 321; *see* Rev. Rul. 80-261, 1980-2 C.B. 279).

Crummey withdrawal rights are structured so that the power to withdraw will be limited and that there is adequate notice given to the beneficiaries who have the withdrawal rights. The beneficiaries are notified immediately in writing at any time assets are added to the trust and then at least a thirty-day time period is given in order for the beneficiaries to demand their withdrawal rights over the assets which are contributed and described in that notice.

The Crummey withdrawal right and the lapse or failure to exercise the withdrawal right is a general power of appointment [§2514(b),(c)]. To avoid a taxable gift under the power of appointment rules, the withdrawal right is often limited to the greater of $5,000 or 5% of the trust principal [§2514(e)].

Sample Language

The withdrawal rights in trust would be established by language similar to the following:

ARTICLE 8: WITHDRAWAL RIGHTS

8.1 Withdrawal Right. In each calendar year in which a transfer or transfers are made by me to the trust, each descendant of mine who is living on the date of such transfer shall have the right to withdraw from the principal of such trust the lesser of (a) the full amount of such transfer or transfers divided by the number of my descendants living on the date of such transfer; (b) Twenty Thousand Dollars ($20,000), if my wife and I notify the trustee at the time of such transfer or transfers that my wife and I intend to consent under Section 2513 of the Code to treat such transfer as having been made one-half by each of us; or (c) $10,000, if my wife and I do not so notify the trustee.

8.2 Notice. The trustee shall promptly give notice to the person(s) with the right to withdraw under 8.1 with respect to any transfer or property specifying the date of transfer, the amount he or she may withdraw, and the date the withdrawal right terminates. The trustee may give such timely notice annually by furnishing to such person(s) a schedule of the anticipated gift transfers to such trust and the periods in which he or she may exercise such withdrawal rights if such gift transfers are made as scheduled. If such person(s) is a minor or legally incapacitated person, such timely notice shall be given to his or her parents, legal guardian or conservator.

8.3 Provisions Relating to Withdrawal Rights. The transfers referred to under the preceding provisions of this Article shall not include any transfers made at my death. Any right of withdrawal under 8.1 shall apply only against the principal of this trust and shall take precedence over any other distribution or application of principal directed or permitted under this trust agreement. Each such right of withdrawal shall be noncumulative and must be exercised within thirty days following the transfer which gave rise to such right by a written notice delivered to the trustee, provided in all events such right must be exercised by the last day of the calendar year in which a transfer is made. Exercise of any right to withdraw principal, in whole or in part, shall be by written notice to the trustee. To the extent a right to withdraw principal is not timely exercised, no further right of withdrawal shall exist with respect to such transfer. Any beneficiary entitled to demand a withdrawal from this trust may make such demand even though such beneficiary is a legally incapacitated person, in which event such demand may be made by such beneficiary's conservator, if any. The specific dollar amounts permitted to be withdrawn from this trust during any calendar year under 8.1 are limited to some extent in accordance with certain sections of the Internal Revenue Code to cause the lowest federal gift and estate tax liabilities. If any one or more of Sections 2041, 2503, 2513, and 2514 of the Code is amended after execution of this agreement by me to increase the amount or amounts permitted to be

transferred during a calendar year without incurring any federal estate or federal gift tax liabilities, then the dollar limitations set forth under 8.1 shall be correspondingly adjusted to accomplish the tax planning objectives embodied in this agreement.

8.4 Mandatory Distributions to Maintain Insurance. The trustee shall apply the principal of this trust not required to make distributions under 8.1 first to maintaining the insurance policies which are trust assets.

Payment of Premiums—Use of Applicable Credit Amount

For large policies and/or older insured clients, the premiums may exceed the annual exclusion, even after gift-splitting is applied. The applicable credit amount is then available for use for gifts of the premiums. This is often a good use of the applicable credit amount because its use for premium gifts makes possible the eventual transfer of a much larger amount in insurance proceeds for the beneficiaries.

Trust as Owner and First Beneficiary

After the transfer of policy to the irrevocable insurance trust, the trust must be the owner of the policy. The trust is also the beneficiary of the policy and as noted above receives all of the proceeds of the policy upon the death of the insured.

Three-Year Rule

The transfer of life insurance policies is included in the three-year rule and if the insured dies within three years of transferring the policy to the irrevocable life insurance trust, then the entire value of the life insurance proceeds is included in the decedent's estate even though the policy is owned by the irrevocable life insurance trust (§2035).

Accordingly, when a client is considering the purchase of a new insurance policy, it is preferable that the irrevocable insurance trust be established first and that the trust be the initial owner of the policy. If the irrevocable life insurance trust is the initial owner of the policy and the insured dies within three years of the purchase, the insurance proceeds will not be included in the taxable estate of the decedent-insured. If, by contrast, the insured person acquires a policy and then transfers the policy to an irrevocable insurance trust, the insured-settlor must survive the transfer by three years in order to remove the proceeds from the estate.

Purchase of Assets From Estate

One of the major uses of life insurance for estate planning purposes is to provide liquidity for an estate for the payment of taxes and other expenses of the estate. The terms of the irrevocable life

insurance trust will provide that the trustee may purchase assets from the estate of the insured at fair market value.

The life insurance provides the estate with the cash it needs for liquidity purposes. The irrevocable insurance trust continues after such transaction, now holding assets purchased from the estate. The purchase of the assets from the estate generally does not trigger taxable gain to the estate (on the sale of assets to the insurance trust) because the assets have received a step-up in basis at the decedent insured's death.

IRREVOCABLE LIFE INSURANCE TRUST—SURVIVORSHIP POLICY

PURPOSE

Another way of purchasing a life insurance policy is the second-to-die policy. This is frequently a less expensive policy to purchase than a policy on a single life. The decedent and his or her spouse would purchase the policy and the proceeds would be realized at the death of the second of the spouses to die. Thus, the liquidity is available for taxes and other expenses at the surviving spouse's death at a much lower cost than the purchase of a policy on one life.

Due to the unlimited marital deduction and the use of the credit shelter trust, an estate plan can be created in which no federal estate taxes are paid at the first spouse's death. At the second death, estate taxes are paid, liquidity is needed and the second-to-die policy provides the cash to accomplish this.

STRUCTURE OF TRUST

Trustee

The spouse and the decedent are now both insured under the second-to-die policy and therefore neither can act as trustee of the irrevocable life insurance trust.

Remainder Beneficiaries

After purchase of any estate assets to provide liquidity for payment of any taxes and expenses of the estate, the remaining proceeds may be held in trust for children (or anyone else) or distributed outright to adult beneficiaries.

PAYMENT OF PREMIUMS—PRESENT INTEREST REQUIREMENT

The same present interest requirement is involved in the second-to-die irrevocable life insurance trust as in the single death life insurance trust.

OWNERSHIP BY CHILDREN

ADVANTAGE

Another technique for removing life insurance from the estate of the decedent or in the case of a second-to-die policy the decedent and the decedent's spouse is to have the adult children own the policy. This is a simple technique for shielding the proceeds from federal estate tax.

DISADVANTAGES

The disadvantages of ownership of insurance policies by children directly are:

- Children must work together as co-owners of the policy;
- No generation-skipping techniques are available which may be used by the children who receive the proceeds outright;
- No technique is in place requiring that the proceeds be made available to the surviving spouse; and
- If a child predeceases the insured, the child's ownership rights become part of the estate and difficulties may arise if there are minor beneficiaries of the child's estate or uncooperative beneficiaries of the child's estate.

LARGE ESTATE—CHILDREN FROM A PRIOR MARRIAGE

The use of the irrevocable life insurance trust is one technique for handling an equalization of children from a current marriage with children from a prior marriage. The children from the prior marriage could be the beneficiaries of the irrevocable life insurance trust or the owners of the life insurance for which the insured funds the premiums. The insured can pass substantial value to the children from the first marriage through the insurance proceeds, without reduction for federal estate taxes.

EXAMPLE 5-2:

- Henry has an estate of $3,500,000, three children from a prior marriage, and a second wife. If he adopts traditional A/B planning, the estate plan may provide for a $650,000 unified credit transfer to the children and the balance of $2,850,000 to his wife.
- This may not seem to be a "fair" balance to the husband (or the children).
- If, however, he chose to make a distribution of his estate 50% to children and 50% to wife, the $1,750,000 passing to the children would attract federal estate tax of approximately $550,000.

An alternative strategy for the husband, and one which would eliminate federal estate tax, would be to establish an irrevocable life insurance trust with the children as trust beneficiaries and have the trust purchase a $1,000,000 policy on the husband's life. If the husband died, there would be the tax-free transfer of $1,650,000 (in 1999) to the children, namely $650,000 protected by the unified credit and $1,000,000 from the irrevocable insurance trust. The wife would receive $2,850,000. There would be no federal estate tax due.

This, if planned carefully, might equalize the assets that are passed to the surviving spouse in a second marriage (and presumably would then be passed on to the children of the second marriage by the surviving spouse or through the surviving spouse's marital trust) with the assets made available to children of a prior marriage.

Chapter 6

Generation–Skipping Tax

BASIC RULES

Since 1986 there has been a separate generation-skipping tax that is imposed on transfers that are not subject to estate tax at each generation. The generation-skipping tax is in addition to any federal estate tax.

A basic definition is that of the **skip person**. A skip person is a person assigned to a generation that is two or more generations below that of the transferor. A trust where all of the beneficiaries are skip persons is also referred to as a **skip person** (§2613).

THREE TYPES OF TRANSFERS

There are three types of transfers which are generation-skipping transfers:

- Taxable termination,
- Taxable distribution, and
- Direct skip (§2611).

Taxable Distribution

A taxable distribution occurs when income or principal is distributed from a generation-skipping trust to a skip person [§2612(b)].

EXAMPLE 6-1:

- Distributions of income or principal from the credit shelter trust during the surviving spouse's lifetime to a grandchild or a great-grandchild would be a taxable distribution.

Taxable Termination

A taxable termination occurs when all of the beneficial interests possessed by non-skip persons in a trust terminate and there are only remaining beneficiaries who are skip persons (§2612).

EXAMPLE 6-2:

- Settlor or testator creates a trust for his child as sole income and principal beneficiary. The trust terminates upon the child's death.
- The distribution of the remaining trust estate to the grandchildren, at the termination of the trust, is a taxable termination.

Direct Skip

The direct skip occurs when a transfer is made to a skip person and the transfer is subject to federal gift or estate tax (§2613). If a transfer is both a direct skip and a taxable termination, then it is considered a direct skip only.

EXAMPLE 6-3:

- Grandfather's will provides for a transfer of $500,000 to his 24-year-old granddaughter, even though the granddaughter's parents are living. The transfer is a direct skip.

There is an exception to the direct skip when a transfer is made to a grandchild when the grandchild's parent is not living at the time of the transfer. This exception does not apply to a transfer from a trust if the child survives the donor.

If a transfer skips more than one generation, e.g., where a gift is made to a great-grandchild, only one direct skip occurs.

TRA'97 broadened the exception to include transfers made to a grandniece or grandnephew where their parent (niece or nephew) is deceased and the transferor has no lineal descendants (children nor grandchildren) [§2651(e)].

Applicable Rate

The generation-skipping tax is imposed at the maximum federal estate tax rate, normally a 55% tax rate. The tax is imposed after application of the GST exemption. The tax is charged against the transferred property, unless other provisions are made for its payment.

With a direct skip or taxable distribution, the amount of the transfer is the amount received by the transferee. With a taxable termination, the amount of the transfer is the value of the property when the termination occurred (§§2621, 2622, 2623).

Maximum Federal Estate Tax Rate Inclusion Ratio

In determining the federal generation-skipping tax due on a generation-skipping transfer, under §2641, the tax equals the **product** of the maximum federal estate tax rate imposed under §2001 on the estates of decedents dying at the time of the taxable distribution, taxable termination or direct skip, and the **inclusion ratio** with respect to the transfer.

Inclusion Ratio

The inclusion ratio is 1.0 minus the applicable fraction determined for the trust from which the transfer is made (or 1.0 minus the applicable fraction determined for a direct skip) (§2642).

The numerator of the applicable fraction is the amount of GST exemption allocated to the trust or to the property transferred in a direct skip. The denominator of the applicable fraction is the value of the property transferred to the trust or involved in the direct skip, reduced by the sum of federal estate tax or state death tax recovered from the trust attributable to such property and any allowable charitable deduction (§2055 or §2522). See Example 6-4 on page 80.

The values determined for federal estate tax purposes generally govern for purposes of the federal generation-skipping tax. Special rules apply to valuation of property given special use valuation under §2032A. Other specific valuation rules should be reviewed; see §2624 and its regulations and proposed regulations.

Valuation for gifts made during lifetime for the GST exemption is the value of such property made on the appropriately filed gift tax return, Form 709, included in Appendix A. Form 706GS(D-1) is used to report a taxable distribution. The recipient may report on Form 706GS(D). Taxable terminations are reported on Form 706GS(T).

Exemption Amount

Each individual has a $1 million amount which is exempt from the generation-skipping tax, which must be allocated to the transfers. Therefore the typical couple may create generation-skipping trusts for their children which combine their $2 million exempt amount from the generation-skipping tax. After 1998, the $1 million will be indexed for inflation, rounded to the next multiple of $10,000

(§2631(c)). In 1999, the exemption amount has been increased to $1,010,000 (Rev. Proc. 98-61, §2642).

Different rules and exceptions may exist for trusts and wills in specific circumstances made prior to 1986.

EXAMPLE 6-4:

- Grandfather dies and after payment of the federal estate tax, there remains a net estate of $3,000,000 for distribution. The will stipulated that the entire remainder of the estate go into a trust for his only child.
- The trust provides for the distribution of income and principal to the child for health, support, maintenance, and education. Upon the child's death, the remaining trust estate is to be distributed to the grandchildren (the child's children).
- Upon the subsequent death of the child, there will be federal generation-skipping tax imposed equal to the inclusion ratio times 55% times the value of the trust estate.
- The inclusion ratio will be one minus the applicable fraction. The numerator of the applicable fraction is $1,000,000 (the grandfather's generation-skipping tax exemption). The denominator is the total value of the trust upon creation, namely $3,000,000. Therefore the inclusion ratio is two-thirds,

$$1 - \frac{1{,}000{,}000 = \text{exemption}}{3{,}000{,}000 = \text{value of trust on creation}}$$

If the trust has a value of $5,100,000 on the child's death, then the federal generation-skipping tax will be $1,870,000, namely two-thirds times 55% x $5,100,000.

EXAMPLE 6-5:

- Bill and Betty, who have three children, have a total estate of $4,000,000. Their revocable living trusts each divide the first estate into a Credit Shelter Trust and a Marital Trust.
- Upon the death of the surviving spouse, both $1,000,000 GST exemptions, one for Bill and one for Betty, will be used.
- Assume Betty dies first in 1998. No federal estate tax is due.
- At Bill's death in 1999, there is federal estate tax of approximately $1,300,000.
- The after-tax amount of $2,700,000 will be divided in equal shares for the three children.

(continued)

EXAMPLE 6–5 (continued):

- Of that total amount, $2,000,000 (using both $1,000,000 GST exemptions) may be put in separate lifetime trusts for the children.
  - These amounts held in trust will be "exempt" from federal estate tax and from general generation-skipping tax upon the later death of each of the children.

Allocation of First $1,000,000 GST Exemption

- The $1,000,000 GST exemption of the first decedent, Betty, must be allocated to property in Betty's estate.
  - Usually an amount of the GST exemption equal to the applicable credit amount is allocated to property passing to the Credit Shelter Trust.
- To preserve Betty's remaining GST exemption of $375,000 (in 1998), it is traditional that $375,000 of property will be placed in an Exempt Marital Trust.
  - That is, the excess of Betty's estate over $625,000 is allocated to the Marital Trust which qualifies for the unlimited marital deduction and which in turn is be divided into "sub-trusts."
- The Exempt Marital Trust for Bill will hold property to which has been allocated the balance of Betty's GST exemption ($375,000 in this 1998 example).
- The Non-Exempt Marital Trust for Bill will hold the balance of Betty's estate. Betty's estate, then, is effectively allocated into three trusts:
  - The Credit Shelter Trust with $625,000,
  - The Exempt Marital Trust with $375,000 (in 1998), and
  - The Non-Exempt Marital Trust with the balance of Betty's estate.
- On Bill's subsequent death there is payment of federal estate tax of approximately $1,300,000. In Bill's estate, there would also be allocation of his $1,010,000 generation-skipping tax exemption.
- Therefore of the $2,700,000 passing to the children, $2,000,000 would be "exempt" for federal generation-skipping purposes. This $2,000,000 would be composed of the funds in the Credit Shelter Trust ($625,000 or more or less) depending on the appreciation or depreciation of assets, the funds in the Exempt Marital Trust established at Betty's death, and $1,010,000 of exempt property in Bill's estate.
- Each child inherits $900,000 of which approximately $666,666 is "exempt" for generation-skipping purposes and $233,333 is non-exempt.

(continued)

EXAMPLE 6–5 (continued):

- Ordinarily these amounts are allocated to an Exempt Trust for a child (holding $666,666) and a separate but essentially identical Non-Exempt Trust for a child (holding $233,333).
- (Administratively this is generally a more simple alternative than cashing the child's entire inheritance into one trust which has an inclusion ratio of more than zero. In this structure, the Exempt Trust has an inclusion ratio of zero and the Non-Exempt Trust has an inclusion ratio of one.)

Exempt Trust

- Usually each child's $666,666 exempt share would be held in an exempt lifetime trust for the child.
- Each trust might provide as follows:

> *My trustee shall distribute the income and principal to my child and such child's descendants as my trustee may determine to be necessary and advisable to provide for their health, support, maintenance, and education. When my child reaches 30 years of age, my trustee shall distribute one-half of the net income to my child at least quarterly. My trustee shall distribute all of the net income to my child, at least quarterly, when she reaches 35 years of age. The trustee shall be my sister, Bonnie. If Bonnie ceases to act, the trustee shall be my brother, Bart. Notwithstanding the above provision, when my child reaches 35 years of age my child shall become the sole trustee of this trust. This trust shall terminate upon my child's death, when it shall be distributed to her descendants as provided in Section 6 of this trust.*

Non-Exempt Share

- There is no federal estate tax or federal generation-skipping tax advantage to holding the $233,333 non-exempt share in trust.
- However, it may be held in trust to protect the property in a divorce, in a lawsuit, or to protect the child with an independent trustee until the child reaches an appropriate age of maturity.

TYPICAL GENERATION-SKIPPING TRUST ELEMENTS

TRUSTEE

The child can be trustee of the lifetime generation-skipping trust of the child. The child serving as trustee may affect the efficacy of the trust as an entity to protect the property from creditors, as later noted. However the child serving as trustee does not jeopardize the generation-skipping feature of the trust.

Beneficiary

The beneficiary of the trust during the child's lifetime is typically the child and after his or her death the descendants of that child.

Trust Agreement

The trust agreement is established either at death or during the lifetime of the donor.

Corpus

The advantage of the generation-skipping trust is that the principal of the trust is then protected from estate tax at succeeding generations until the assets are actually distributed.

Special Power of Appointment

By definition, a lifetime generation-skipping trust for a child will continue for the child's entire lifetime. The death of the child may be many years in the future (many years after the drafting of the governing instrument).

Therefore it is very common to include a special power of appointment for the child in the lifetime trust—granting the child the flexibility to govern the disposition of assets by the child's later will. This flexibility can be very important in the context of a generation-skipping trust.

NON-TAX FEATURES OF LIFETIME TRUST

DIVORCE

In addition to the tax reasons for setting up a lifetime trust for children and other descendants, there are additional reasons including protection of the assets from a divorcing spouse. This protection varies from state to state but usually provides at least some measure of protection. That is, inherited property which is held in trust generally retains its character as the child's "separate property" and accordingly is beyond the reach of a divorcing spouse.

CREDITORS

Likewise, the creditors of the child or the other beneficiaries of the trust may in some instances not attach the assets of the trust. To the extent that interest and principal are distributed, of course, those distributions would be subject to creditor claims. However, as long as the assets are being held in the trust and not distributed outright to the beneficiary of the trust, they are generally protected from creditors.

State law varies on this point but the general rule is that the creditors may not attach the assets of a "discretionary trust." This is a trust with an independent trustee which has the authority to make income and principal distributions to the beneficiary as the trustee deems necessary or advisable. In many states if the beneficiary serves as co-trustee, the trust is still a "discretionary trust" and beyond the reach of creditors.

SPENDTHRIFT ISSUES

In the event that there are concerns about the ability of the child or other beneficiary of the trust to manage trust assets, an independent trustee can be named who would manage the assets, invest them and distribute them according to the terms of the trust agreement. In this way, the grantor of the trust is assured that the assets will be protected from the beneficiary's own poor choices.

An example of a spendthrift trust and the reasons for establishing one can be found in President Thomas Jefferson's will quoted below:

Considering the insolvent state of the affairs of my friend & son in law Thomas Mann Randolph, and that what will remain of my property will be the only resource against the want in which his family would otherwise be left, it must be his wish, as it is my duty, to guard that resource against all liability for his debts, engagements or purposes whatsoever, and to preclude the rights, powers and authorities over it which might result to him by operation of law, and which might, independently of his will, bring it within the power of his creditors, I do hereby devise and bequeath all the residue of my property real and personal, in possession or in action, whether held in my own right, or in that of my dear deceased wife, according to the powers vested in me by deed of settlement for that purpose, to my grandson Thomas J. Randolph, & my friends Nicholas P. Trist, and Alexander Garrett & their heirs during the life of my sd. son in law Thomas M. Randolph, to be held & administered by them, in trust, for the sole and separate use and behoof of my dear daughter Martha Randolph and her heirs, and, aware of the nice and difficult distinctions of the law in these cases, I will further explain by saying that I understand and intend the effect of these limitations to be, that the legal estate and actual occupation shall be vested in my said trustees, and held by them in base fee, determinable on the death of my sd. son in law, and the remainder during the same time be vested in my sd. daughter and her heirs, and of course disposable by her last will, and that at the death of my sd. son in law, the particular estate of the sd. trustees shall be determined, and the remainder, in legal estate, possession and use become vested in my sd. daughter and her heirs, in absolute property, for ever.

STRUCTURE OF EXEMPT AND NON-EXEMPT TRUST

The entire exempt share would be held in trust for the lifetime of a child. The entire value of the exempt share, plus any appreciation, would then pass free of generation-skipping tax (GST) and free of federal estate tax to the grandchildren.

EXAMPLE 6-6:

- Gina and George create an exempt trust for their son, Gabe. Gabe lives to be 83 years old.
- He has had the use of the income and principal, when needed, of the exempt trust for his lifetime. The trust assets have appreciated to $6,000,000 at Gabe's death.
- Gabe's children receive the entire $6,000,000 at Gabe's death without reduction for federal estate tax or generation-skipping tax.

There is no GST reason to hold the nonexempt share in trust. There may be non-tax reasons. If held in trust, usually its assets are distributed before using the assets of the exempt share trust.

Chapter 7

Small Business Considerations

PLANNING WITH FAMILY-OWNED BUSINESS DEDUCTION

TRA '97 created an additional estate tax exclusion for qualified family-owned businesses (§2033A). An estate with a qualified family-owned business can exclude up to $1,300,000 (including the unified credit) of assets otherwise includible in the estate. The 1998 Reform Act changed this provision from an exclusion to a deduction, and it is now located at §2057.

The deduction is coordinated with the unified credit. An estate cannot qualify for both a $1,300,000 business deduction and the protection of $650,000 (in 1999) by the unified credit. They must together total no more than $1.3 million.

KEY REQUIREMENTS

The key requirements for the §2057 family-owned business deduction are as follows:

1. The decedent was a citizen or resident of the United States.
2. The adjusted value of the qualified family-owned business interest plus the amount of such gifts exceeds 50% of the adjusted gross estate.
3. During the eight-year period ending on the date of the decedent's death, there have been periods of at least five years during which such interests were owned by the decedent or a member of the decedent's family and there was "material participation" by the decedent or a member of the decedent's family in the operation of the business.
4. The qualified family-owned business interests passed to a "qualified heir"—a family member or any active employee who has been employed by the trade or business for a period of at least ten years before the date of the decedent's death.

Recapture

Section 2057 provides for recapture. There is additional estate tax imposed if within ten years after the date of the decedent's death and before the date of the qualified heir's death:

- Material participation requirements are not met, or
- Qualified heir disposes of any portion of a qualified family-owned business interest.

If the additional estate tax is imposed in years one through six, there is federal estate tax equal to 100% of what would otherwise have been the federal estate tax (plus interest). If the recapture occurs thereafter, the applicable percentage is as follows:

Year 7	80%
Year 8	60%
Year 9	40%
Year 10	20%

Some have called the new provision the "young Frankenstein" because it carries with it many of the rigid technical requirements of §2032A. Note that unlike other planning arenas, gifts of business interests made by the business owner are aggregated in the estate (so that the making of gifts does not penalize qualification for the $1,300,000 business deduction).

PLANNING CONSIDERATIONS

Gifts

If the client has one or more children who are interested in continuing the family farm or the family business, then gifts within the annual exclusion or sometimes using the applicable unified credit amount are possible during the lifetime of the client to those children.

This slow transfer of ownership to the child is an excellent method of making gifts because:

- It allows the donor to review and work with the child in the business with the child having the incentive of having a partial ownership.
- The minority interest in the entity may be valued at a heavily discounted rate for purposes of the gift tax.
- The appreciation in the business has been transferred to the child to the extent of the ownership which has been transferred and removed from the donor's estate.

EQUALIZATION AMONG CHILDREN

The other issue which arises when some but not all of the children are interested in being involved in the family business is the equalization with gifts of other assets to other children.

For children who are not interested in being involved in the family business, it may not be advisable to make them shareholders or partners with the child or children who are interested in the business. Giving all children gifts of business interests could be a source of family conflict in the future.

The children who are not part of the business will not be receiving salaries or other benefits from the business. Moreover it is often the case that it is not possible to sell the interest of a child who is not active in the management of the business. The non-active child may have, in effect, a "non-spendable inheritance."

A non-active child typically receives no salary, no dividend, and no benefit.

This can be a particularly vexing situation where the other assets in the decedent's estate must be used to pay federal estate tax.

EXAMPLE 7-1:

- Dan and Doris have a total estate of $3,000,000, including a closely held business with a value of approximately $1.6 million. Dan and Doris have three children, a son who works in the business and two daughters who live out of state.
- If Dan and Doris die in 1999 and 2000 with A/B planning, approximately $1,275,000 will be shielded from federal estate tax (assuming the business deduction does not apply).
- This will leave approximately $1,725,000 subject to federal estate tax, resulting in federal estate tax of approximately $750,000. Assuming the business is maintained intact, there would be approximately $650,000 of net assets for distribution (other than the family business).
- If the son's inheritance is composed entirely of interests in the family business, then each daughter will inherit approximately $325,000 of spendable assets and approximately $400,000 of stock in the family business. For the daughter, that stock may be a "worthless asset."

Three Alternatives

- There are at least three alternatives the family may consider in this circumstance:
  - Purchase of a life insurance policy, particularly a second-to-die life insurance policy, to be paid to the daughters—helping to equalize the estate distribution.
- If possible without a negative income tax result, distribute the business real property to the daughters so they may then lease the real property back to the brother's family business.
  - The granting of a partial "put" right to each daughter—granting the daughter the right to sell at least part of their stock in the family business to the brother. Such a transaction is often structured with a relatively modest down payment and a secured promissory note. It may provide more "spendable funds" to the daughter but it obviously can result in family tensions. If the business goes through a difficult period, do the sisters foreclose upon their brother?

S CORPORATION ISSUES

An S corporation may be disqualified as an S corporation if the shareholders in the S corporation are not qualified. Only certain types of trusts qualify to be a shareholder of an S corporation stock. These include:

- Limited voting trusts,
- Testamentary trusts and grantor trusts which are limited in duration,
- QSSTs, and
- ESBTs.

QSST

The qualified subchapter S trust (QSST) may be a shareholder in an S corporation. A QSST has only one income beneficiary who must be a citizen or resident of the United States. Income must be distributed currently to the income beneficiary. (It may be possible to elect annually to have the trustee retain income. PLR8836057.) Any distribution of principal during the beneficiary's life may be made only to the income beneficiary. If the trust terminates during the life of the beneficiary, then all of the assets must be distributed to the beneficiary [§1361(d)]. The beneficiary must elect QSST treatment for the trust.

Accordingly, few Credit Shelter Trusts (which often have several family beneficiaries and continue beyond the life of a single income beneficiary) qualify as a QSST.

A QSST may be structured so that it qualifies for the gift tax and estate tax marital deduction as a QTIP (qualified terminable interest property trust) or general power of appointment marital trust.

ESBT

The electing small business trust (ESBT) is allowed as a subchapter S shareholder under the Small Business Job Protection Act of 1996 [§1361(e)]. The ESBT must meet three main requirements:

- All trust beneficiaries must be individuals or estates who are eligible to be S Corporation shareholders. (A charity may hold a contingent remainder interest.)
- No interest in the ESBT may be acquired by purchase. (Purchase is defined as any acquisition where the basis is determined under §1012.)
- Finally, the ESBT must elect to be a small business trust.

The portion of an ESBT which consists of S Corporation stock pays the highest rate for trusts and estates income except capital gains [§641(d)]. None of the items of income, loss, or deduction may

be passed through to the ESBT beneficiaries and capital losses are allowed only to the extent of capital gains.

The Credit Shelter Trust may be structured to be an ESBT.

The introduction of the ESBT provides an opportunity for more flexible estate planning. With a QSST, as noted, there may be only one beneficiary. Further, there is the requirement that there be the mandatory distribution of income. If a parent died and the property passed into a QSST for a child (particularly a young child) the distribution of income to a minor for many years may be inconvenient or the income may be more than one would want to give to a young person. With an ESBT, income may be accumulated and trust distributions may be "sprinkled" among family members who are trust beneficiaries.

DEFERRAL OF TAX

SECTION 6166

Section 6166 covers the federal estate tax and to a more limited extent the generation-skipping tax. It allows for a payment of federal estate tax which is attributable to a substantial interest in a closely held business to be paid over two to ten equal annual installments. Part of the interest of the unpaid balance of the tax may be paid at the rate of 4%.

For decedents who die after 1997, the interest rate is 2% for tax attributable to the first $1 million in taxable value in qualified closely held businesses which is included in the estate. This $1 million is indexed for inflation and rounded to the next $10,000 under the Taxpayer Relief Act of 1997. For decedents dying in 1999, the amount available for a 2% interest rate on its tax due, has been increased to $1,010,000. (Rev. Proc. 98-61) The interest on the remaining tax attributable to the closely held business is payable at 45% of the underpayment rate (§6601(j)). Interests in holding companies and non-readily-tradeable businesses do not qualify for the 2% interest rate under new provisions of the 1998 Reform Act [§6166(b)].

Section 6166 applies to corporations, partnerships and sole proprietorships.

The benefits of §6166 are only made available to the estates of decedents who are U.S. citizens or resident aliens at the time of death. The interest in the closely held business must exceed 35% of the decedent's adjusted gross estate for federal estate tax purposes.

Because the first installment of a §6166 deferral of payment does not need to be made until a date selected by the executor, which is not more than five years after the date prescribed in Section 6151(a) for payment of the tax, the estate tax may be spread over a period as long as 14 years from the decedent's death. During the first five years interest only need be paid.

The election for a §6166 deferral is made on the federal estate tax return or on the last date of the extension of time granted for filing the estate tax return. There are provisions which allow the election to apply to the estate tax as finally determined or agreed to following any audit.

Appendix—IRS Forms

Form **706**

(Rev. July 1999)

Department of the Treasury
Internal Revenue Service

United States Estate (and Generation-Skipping Transfer) Tax Return

Estate of a citizen or resident of the United States (see separate instructions).
To be filed for decedents dying after December 31, 1998
For Paperwork Reduction Act Notice, see page 1 of the separate instructions.

OMB No. 1545-0015

Part 1.—Decedent and Executor

1a Decedent's first name and middle initial (and maiden name, if any)	1b Decedent's last name		2 **Decedent's Social Security No.**
3a Legal residence (domicile) at time of death (county, state, and ZIP code, or foreign country)	3b Year domicile established	4 Date of birth	5 Date of death
6a Name of executor (see page 4 of the instructions)	6b Executor's address (number and street including apartment or suite no. or rural route; city, town, or post office; state; and ZIP code)		
6c Executor's social security number (see page 4 of the instructions)			
7a Name and location of court where will was probated or estate administered			7b Case number

8 If decedent died testate, check here ▶ ☐ and attach a certified copy of the will. 9 If Form 4768 is attached, check here ▶ ☐

10 If Schedule R-1 is attached, check here ▶ ☐

Part 2.—Tax Computation

Line	Description		
1	Total gross estate less exclusion (from Part 5, Recapitulation, page 3, item 12)		1
2	Total allowable deductions (from Part 5, Recapitulation, page 3, item 23)		2
3	Taxable estate (subtract line 2 from line 1)		3
4	Adjusted taxable gifts (total taxable gifts (within the meaning of section 2503) made by the decedent after December 31, 1976, other than gifts that are includible in decedent's gross estate (section 2001(b)))		4
5	Add lines 3 and 4		5
6	Tentative tax on the amount on line 5 from Table A on page 12 of the instructions		6
7a	If line 5 exceeds $10,000,000, enter the lesser of line 5 or $17,184,000. If line 5 is $10,000,000 or less, skip lines 7a and 7b and enter -0- on line 7c	7a	
b	Subtract $10,000,000 from line 7a	7b	
c	Enter 5% (.05) of line 7b		7c
8	Total tentative tax (add lines 6 and 7c)		8
9	Total gift tax payable with respect to gifts made by the decedent after December 31, 1976. Include gift taxes by the decedent's spouse for such spouse's share of split gifts (section 2513) only if the decedent was the donor of these gifts and they are includible in the decedent's gross estate (see instructions)		9
10	Gross estate tax (subtract line 9 from line 8)		10
11	Maximum unified credit (applicable credit amount) against estate tax	11	
12	Adjustment to unified credit (applicable credit amount). (This adjustment may not exceed $6,000. See page 4 of the instructions.)	12	
13	Allowable unified credit (applicable credit amount) (subtract line 12 from line 11)		13
14	Subtract line 13 from line 10 (but do not enter less than zero)		14
15	Credit for state death taxes. Do not enter more than line 14. Figure the credit by using the amount on line 3 less $60,000. See Table B in the instructions and **attach credit evidence** (see instructions)		15
16	Subtract line 15 from line 14		16
17	Credit for Federal gift taxes on pre-1977 gifts (section 2012) (attach computation)	17	
18	Credit for foreign death taxes (from Schedule(s) P). (Attach Form(s) 706-CE.)	18	
19	Credit for tax on prior transfers (from Schedule Q)	19	
20	Total (add lines 17, 18, and 19)		20
21	Net estate tax (subtract line 20 from line 16)		21
22	Generation-skipping transfer taxes (from Schedule R, Part 2, line 10)		22
23	Total transfer taxes (add lines 21 and 22)		23
24	Prior payments. Explain in an attached statement	24	
25	United States Treasury bonds redeemed in payment of estate tax	25	
26	Total (add lines 24 and 25)		26
27	Balance due (or overpayment) (subtract line 26 from line 23)		27

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer other than the executor is based on all information of which preparer has any knowledge.

Signature(s) of executor(s) Date

Signature of preparer other than executor Address (and ZIP code) Date

Cat. No. 20548R

Form 706 (Rev. 7-99)

Estate of:

Part 3—Elections by the Executor

Please check the "Yes" or "No" box for each question. (See instructions beginning on page 5.)		Yes	No
1 Do you elect alternate valuation?	1		
2 Do you elect special use valuation? If "Yes," you must complete and attach Schedule A-1.	2		
3 Do you elect to pay the taxes in installments as described in section 6166? If "Yes," you must attach the additional information described on page 8 of the instructions.	3		
4 Do you elect to postpone the part of the taxes attributable to a reversionary or remainder interest as described in section 6163?	4		

Part 4—General Information

(**Note:** *Please attach the necessary supplemental documents.* **You must attach the death certificate.**) *(See instructions on page 9.)*

Authorization to receive confidential tax information under Regs. sec. 601.504(b)(2)(i); to act as the estate's representative before the IRS; and to make written or oral presentations on behalf of the estate if return prepared by an attorney, accountant, or enrolled agent for the executor:

Name of representative (print or type)	State	Address (number, street, and room or suite no., city, state, and ZIP code)

I declare that I am the ☐ attorney/ ☐ certified public accountant/ ☐ enrolled agent (you must check the applicable box) for the executor and prepared this return for the executor. I am not under suspension or disbarment from practice before the Internal Revenue Service and am qualified to practice in the state shown above.

Signature	CAF number	Date	Telephone number

1 Death certificate number and issuing authority (attach a copy of the death certificate to this return).

2 Decedent's business or occupation. If retired, check here ▶ ☐ and state decedent's former business or occupation.

3 Marital status of the decedent at time of death:

☐ Married

☐ Widow or widower—Name, SSN, and date of death of deceased spouse ▶

☐ Single

☐ Legally separated

☐ Divorced—Date divorce decree became final ▶

4a Surviving spouse's name	4b Social security number	4c Amount received (see page 9 of the instructions)

5 Individuals (other than the surviving spouse), trusts, or other estates who receive benefits from the estate (do not include charitable beneficiaries shown in Schedule O) (see instructions). For Privacy Act Notice (applicable to individual beneficiaries only), see the Instructions for Form 1040.

Name of individual, trust, or estate receiving $5,000 or more	Identifying number	Relationship to decedent	Amount (see instructions)
All unascertainable beneficiaries and those who receive less than $5,000 ▶			
Total			

Please check the "Yes" or "No" box for each question.	Yes	No
6 Does the gross estate contain any section 2044 property (qualified terminable interest property (QTIP) from a prior gift or estate) (see page 9 of the instructions)?		

(continued on next page)

Form 706 (Rev. 7-99)

Part 4—General Information *(continued)*

Please check the "Yes" or "No" box for each question.	Yes	No
7a Have Federal gift tax returns ever been filed? If "Yes," please attach copies of the returns, if available, and furnish the following information:		
7b Period(s) covered — **7c** Internal Revenue office(s) where filed		
If you answer "Yes" to any of questions 8–16, you must attach additional information as described in the instructions.		
8a Was there any insurance on the decedent's life that is not included on the return as part of the gross estate?		
b Did the decedent own any insurance on the life of another that is not included in the gross estate?		
9 Did the decedent at the time of death own any property as a joint tenant with right of survivorship in which **(a)** one or more of the other joint tenants was someone other than the decedent's spouse, and **(b)** less than the full value of the property is included on the return as part of the gross estate? If "Yes," you must complete and attach Schedule E		
10 Did the decedent, at the time of death, own any interest in a partnership or unincorporated business or any stock in an inactive or closely held corporation?		
11 Did the decedent make any transfer described in section 2035, 2036, 2037, or 2038 (see the instructions for Schedule G beginning on page 11 of the separate instructions)? If "Yes," you must complete and attach Schedule G		
12 Were there in existence at the time of the decedent's death:		
a Any trusts created by the decedent during his or her lifetime?		
b Any trusts not created by the decedent under which the decedent possessed any power, beneficial interest, or trusteeship?		
13 Did the decedent ever possess, exercise, or release any general power of appointment? If "Yes," you must complete and attach Schedule H		
14 Was the marital deduction computed under the transitional rule of Public Law 97-34, section 403(e)(3) (Economic Recovery Tax Act of 1981)? If "Yes," attach a separate computation of the marital deduction, enter the amount on item 20 of the Recapitulation, and note on item 20 "computation attached."		
15 Was the decedent, immediately before death, receiving an annuity described in the "General" paragraph of the instructions for Schedule I? If "Yes," you must complete and attach Schedule I		
16 Was the decedent ever the beneficiary of a trust for which a deduction was claimed by the estate of a pre-deceased spouse under section 2056(b)(7) and which is not reported on this return? If "Yes," attach an explanation		

Part 5—Recapitulation

Item number	Gross estate		Alternate value	Value at date of death
1	Schedule A—Real Estate	1		
2	Schedule B—Stocks and Bonds	2		
3	Schedule C—Mortgages, Notes, and Cash	3		
4	Schedule D—Insurance on the Decedent's Life (attach Form(s) 712)	4		
5	Schedule E—Jointly Owned Property (attach Form(s) 712 for life insurance)	5		
6	Schedule F—Other Miscellaneous Property (attach Form(s) 712 for life insurance)	6		
7	Schedule G—Transfers During Decedent's Life (att. Form(s) 712 for life insurance)	7		
8	Schedule H—Powers of Appointment	8		
9	Schedule I—Annuities	9		
10	Total gross estate (add items 1 through 9)	10		
11	Schedule U—Qualified Conservation Easement Exclusion	11		
12	Total gross estate less exclusion (subtract item 11 from item 10). Enter here and on line 1 of Part 2—Tax Computation	12		

Item number	Deductions		Amount
13	Schedule J—Funeral Expenses and Expenses Incurred in Administering Property Subject to Claims	13	
14	Schedule K—Debts of the Decedent	14	
15	Schedule K—Mortgages and Liens	15	
16	Total of items 13 through 15	16	
17	Allowable amount of deductions from item 16 (see the instructions for item 17 of the Recapitulation)	17	
18	Schedule L—Net Losses During Administration	18	
19	Schedule L—Expenses Incurred in Administering Property Not Subject to Claims	19	
20	Schedule M—Bequests, etc., to Surviving Spouse	20	
21	Schedule O—Charitable, Public, and Similar Gifts and Bequests	21	
22	Schedule T—Qualified Family-Owned Business Interest Deduction	22	
23	Total allowable deductions (add items 17 through 22). Enter here and on line 2 of the Tax Computation	23	

Page 3

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE A—Real Estate

- *For jointly owned property that must be disclosed on Schedule E, see the instructions on the reverse side of Schedule E.*
- *Real estate that is part of a sole proprietorship should be shown on Schedule F.*
- *Real estate that is included in the gross estate under section 2035, 2036, 2037, or 2038 should be shown on Schedule G.*
- *Real estate that is included in the gross estate under section 2041 should be shown on Schedule H.*
- *If you elect section 2032A valuation, you must complete Schedule A and Schedule A-1.*

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1				
Total from continuation schedules or additional sheets attached to this schedule . . .				
TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 1.)				

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)

(See the instructions on the reverse side.)

Schedule A—Page 4

Form 706 (Rev. 7-99)

Instructions for Schedule A—Real Estate

If the total gross estate contains any real estate, you must complete Schedule A and file it with the return. On Schedule A list real estate the decedent owned or had contracted to purchase. Number each parcel in the left-hand column.

Describe the real estate in enough detail so that the IRS can easily locate it for inspection and valuation. For each parcel of real estate, report the area and, if the parcel is improved, describe the improvements. For city or town property, report the street and number, ward, subdivision, block and lot, etc. For rural property, report the township, range, landmarks, etc.

If any item of real estate is subject to a mortgage for which the decedent's estate is liable; that is, if the indebtedness may be charged against other property of the estate that is not subject to that mortgage, or if the decedent was personally liable for that mortgage, you must report the full value of the property in the value column. Enter the amount of the mortgage under "Description" on this schedule. The unpaid amount of the mortgage may be deducted on Schedule K.

If the decedent's estate is NOT liable for the amount of the mortgage, report only the value of the equity of redemption (or value of the property less the indebtedness) in the value column as part of the gross estate. Do not enter any amount less than zero. Do not deduct the amount of indebtedness on Schedule K.

Also list on Schedule A real property the decedent contracted to purchase. Report the full value of the property and not the equity in the value column. Deduct the unpaid part of the purchase price on Schedule K.

Report the value of real estate without reducing it for homestead or other exemption, or the value of dower, curtesy, or a statutory estate created instead of dower or curtesy.

Explain how the reported values were determined and attach copies of any appraisals.

Schedule A Examples

In this example, alternate valuation is not adopted; the date of death is January 1, 1999.

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1	House and lot, 1921 William Street NW, Washington, DC (lot 6, square 481). Rent of $2,700 due at end of each quarter, February 1, May 1, August 1, and November 1. Value based on appraisal, copy of which is attached			$108,000
	Rent due on item 1 for quarter ending November 1, 1998, but not collected at date of death			2,700
	Rent accrued on item 1 for November and December 1998			1,800
2	House and lot, 304 Jefferson Street, Alexandria, VA (lot 18, square 40). Rent of $600 payable monthly. Value based on appraisal, copy of which is attached			96,000
	Rent due on item 2 for December 1998, but not collected at date of death . . .			600

In this example, alternate valuation is adopted; the date of death is January 1, 1999.

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1	House and lot, 1921 William Street NW, Washington, DC (lot 6, square 481). Rent of $2,700 due at end of each quarter, February 1, May 1, August 1, and November 1. Value based on appraisal, copy of which is attached. Not disposed of within 6 months following death	7/1/99	90,000	$108,000
	Rent due on item 1 for quarter ending November 1, 1998, but not collected until February 1, 1999	2/1/99	2,700	2,700
	Rent accrued on item 1 for November and December 1998, collected on February 1, 1999	2/1/99	1,800	1,800
2	House and lot, 304 Jefferson Street, Alexandria, VA (lot 18, square 40). Rent of $600 payable monthly. Value based on appraisal, copy of which is attached. Property exchanged for farm on May 1, 1999	5/1/99	90,000	96,000
	Rent due on item 2 for December 1998, but not collected until February 1, 1999 .	2/1/99	600	600

Schedule A—Page 5

Instructions for Schedule A-1. Section 2032A Valuation

The election to value certain farm and closely held business property at its special use value is made by checking "Yes" to line 2 of Part 3, Elections by the Executor, Form 706. Schedule A-1 is used to report the additional information that must be submitted to support this election. In order to make a valid election, you must complete Schedule A-1 and attach all of the required statements and appraisals.

For definitions and additional information concerning special use valuation, see section 2032A and the related regulations.

Part 1. Type of Election

Estate and GST Tax Elections. If you elect special use valuation for the estate tax, you must also elect special use valuation for the GST tax and vice versa.

You must value each specific property interest at the same value for GST tax purposes that you value it at for estate tax purposes.

Protective Election. To make the protective election described in the separate instructions for line 2 of Part 3, Elections by the Executor, you must check this box, enter the decedent's name and social security number in the spaces provided at the top of Schedule A-1, and complete line 1 and column A of lines 3 and 4 of Part 2. For purposes of the protective election, list on line 3 all of the real property that passes to the qualified heirs even though some of the property will be shown on line 2 when the additional notice of election is subsequently filed. You need not complete columns B–D of lines 3 and 4. You need not complete any other line entries on Schedule A-1. Completing Schedule A-1 as described above constitutes a Notice of Protective Election as described in Regulations section 20.2032A-8(b).

Part 2. Notice of Election

Line 10. Because the special use valuation election creates a potential tax liability for the recapture tax of section 2032A(c), you must list each person who receives an interest in the specially valued property on Schedule A-1. If there are more than eight persons who receive interests, use an additional sheet that follows the format of line 10. In the columns "Fair market value" and "Special use value," you should enter the total respective values of all the specially valued property interests received by each person.

GST Tax Savings

To compute the additional GST tax due upon disposition (or cessation of qualified use) of the property, each "skip person" (as defined in the instructions to Schedule R) who receives an interest in the specially valued property must know the total GST tax savings on all of the interests in specially valued property received. This GST tax savings is the difference between the total GST tax that was imposed on all of the interests in specially valued property received by the skip person valued at their special use value and the total GST tax that would have been imposed on the same interests received by the skip person had they been valued at their fair market value.

Because the GST tax depends on the executor's allocation of the GST exemption and the grandchild exclusion, the skip person who receives the interests is unable to compute this GST tax savings. Therefore, for each skip person who receives an interest in specially valued property, you must attach worksheets showing the total GST tax savings attributable to all of that person's interests in specially valued property.

How To Compute the GST Tax Savings. Before computing each skip person's GST tax savings, you must complete Schedules R and R-1 for the entire estate (using the special use values).

For each skip person, you must complete two Schedules R (Parts 2 and 3 only) as worksheets, one showing the interests in specially valued property received by the skip person at their special use value and one showing the same interests at their fair market value.

If the skip person received interests in specially valued property that were shown on Schedule R-1, show these interests on the Schedule R, Parts 2 and 3 worksheets, as appropriate. Do not use Schedule R-1 as a worksheet.

Completing the Special Use Value Worksheets. On lines 2–4 and 6, enter -0-.

Completing the Fair Market Value Worksheets. *Lines 2 and 3, fixed taxes and other charges.* If valuing the interests at their fair market value (instead of special use value) causes any of these taxes and charges to increase, enter the increased amount (only) on these lines and attach an explanation of the increase. Otherwise, enter -0-.

Line 6—GST exemption. If you completed line 10 of Schedule R, Part 1, enter on line 6 the amount shown for the skip person on the *line 10 special use allocation schedule* you attached to Schedule R. If you did not complete line 10 of Schedule R, Part 1, enter -0- on line 6.

Total GST Tax Savings. For each skip person, subtract the tax amount on line 10, Part 2 of the special use value worksheet from the tax amount on line 10, Part 2 of the fair market value worksheet. This difference is the skip person's total GST tax savings.

Part 3. Agreement to Special Valuation Under Section 2032A

The agreement to special valuation by persons with an interest in property is required under section 2032A(a)(1)(B) and (d)(2) and must be signed by all parties who have any interest in the property being valued based on its qualified use as of the date of the decedent's death.

An interest in property is an interest that, as of the date of the decedent's death, can be asserted under applicable local law so as to affect the disposition of the specially valued property by the estate. Any person who at the decedent's death has any such interest in the property, whether present or future, or vested or contingent, must enter into the agreement. Included are owners of remainder and executory interests; the holders of general or special powers of appointment; beneficiaries of a gift over in default of exercise of any such power; joint tenants and holders of similar undivided interests when the decedent held only a joint or undivided interest in the property or when only an undivided interest is specially valued; and trustees of trusts and representatives of other entities holding title to, or holding any interests in the property. An heir who has the power under local law to caveat (challenge) a will and thereby affect disposition of the property is not, however, considered to be a person with an interest in property under section 2032A solely by reason of that right. Likewise, creditors of an estate are not such persons solely by reason of their status as creditors.

If any person required to enter into the agreement either desires that an agent act for him or her or cannot legally bind himself or herself due to infancy or other incompetency, or due to death before the election under section 2032A is timely exercised, a representative authorized by local law to bind the person in an agreement of this nature may sign the agreement on his or her behalf.

The Internal Revenue Service will contact the agent designated in the agreement on all matters relating to continued qualification under section 2032A of the specially valued real property and on all matters relating to the special lien arising under section 6324B. It is the duty of the agent as attorney-in-fact for the parties with interests in the specially valued property to furnish the IRS with any requested information and to notify the IRS of any disposition or cessation of qualified use of any part of the property.

Form 706 (Rev. 7-99)

Checklist for Section 2032A Election. *If you are going to make the special use valuation election on Schedule A-1, please use this checklist to ensure that you are providing everything necessary to make a valid election.*

To have a valid special use valuation election under section 2032A, you must file, in addition to the Federal estate tax return, **(a)** a notice of election (Schedule A-1, Part 2), and **(b)** a fully executed agreement (Schedule A-1, Part 3). You must include certain information in the notice of election. To ensure that the notice of election includes all of the information required for a valid election, use the following checklist. The checklist is for your use only. Do not file it with the return.

1. Does the notice of election include the decedent's name and social security number as they appear on the estate tax return?

2. Does the notice of election include the relevant qualified use of the property to be specially valued?

3. Does the notice of election describe the items of real property shown on the estate tax return that are to be specially valued and identify the property by the Form 706 schedule and item number?

4. Does the notice of election include the fair market value of the real property to be specially valued and also include its value based on the qualified use (determined without the adjustments provided in section 2032A(b)(3)(B))?

5. Does the notice of election include the adjusted value (as defined in section 2032A(b)(3)(B)) of **(a)** all real property that both passes from the decedent and is used in a qualified use, without regard to whether it is to be specially valued, and **(b)** all real property to be specially valued?

6. Does the notice of election include **(a)** the items of personal property shown on the estate tax return that pass from the decedent to a qualified heir and that are used in qualified use and **(b)** the total value of such personal property adjusted under section 2032A(b)(3)(B)?

7. Does the notice of election include the adjusted value of the gross estate? (See section 2032A(b)(3)(A).)

8. Does the notice of election include the method used to determine the special use value?

9. Does the notice of election include copies of written appraisals of the fair market value of the real property?

10. Does the notice of election include a statement that the decedent and/or a member of his or her family has owned all of the specially valued property for at least 5 years of the 8 years immediately preceding the date of the decedent's death?

11. Does the notice of election include a statement as to whether there were any periods during the 8-year period preceding the decedent's date of death during which the decedent or a member of his or her family did not **(a)** own the property to be specially valued, **(b)** use it in a qualified use, or **(c)** materially participate in the operation of the farm or other business? (See section 2032A(e)(6).)

12. Does the notice of election include, for each item of specially valued property, the name of every person taking an interest in that item of specially valued property and the following information about each such person: **(a)** the person's address, **(b)** the person's taxpayer identification number, **(c)** the person's relationship to the decedent, and **(d)** the value of the property interest passing to that person based on both fair market value and qualified use?

13. Does the notice of election include affidavits describing the activities constituting material participation and the identity of the material participants?

14. Does the notice of election include a legal description of each item of specially valued property?

(In the case of an election made for qualified woodlands, the information included in the notice of election must include the reason for entitlement to the woodlands election.)

Any election made under section 2032A will not be valid unless a properly executed agreement (Schedule A-1, Part 3) is filed with the estate tax return. To ensure that the agreement satisfies the requirements for a valid election, use the following checklist.

1. Has the agreement been signed by each and every qualified heir having an interest in the property being specially valued?

2. Has every qualified heir expressed consent to personal liability under section 2032A(c) in the event of an early disposition or early cessation of qualified use?

3. Is the agreement that is actually signed by the qualified heirs in a form that is binding on all of the qualified heirs having an interest in the specially valued property?

4. Does the agreement designate an agent to act for the parties to the agreement in all dealings with the IRS on matters arising under section 2032A?

5. Has the agreement been signed by the designated agent and does it give the address of the agent?

Form 706 (Rev. 7-99)

Estate of: | **Decedent's Social Security Number**

SCHEDULE A-1—Section 2032A Valuation

Part 1. Type of Election (Before making an election, see the checklist on page 7.):

☐ **Protective election (Regulations section 20.2032A-8(b)).** Complete Part 2, line 1, and column A of lines 3 and 4. (See instructions.)

☐ **Regular election.** Complete all of Part 2 (including line 11, if applicable) and Part 3. (See instructions.)

Before completing Schedule A-1, see the checklist on page 7 for the information and documents that must be included to make a valid election.

The election is not valid unless the agreement (i.e., Part 3—Agreement to Special Valuation Under Section 2032A)—

- Is signed by each and every qualified heir with an interest in the specially valued property, and
- Is attached to this return when it is filed.

Part 2. Notice of Election (Regulations section 20.2032A-8(a)(3))

Note: *All real property entered on lines 2 and 3 must also be entered on Schedules A, E, F, G, or H, as applicable.*

1 Qualified use—check one ▶ ☐ Farm used for farming, or
▶ ☐ Trade or business other than farming

2 Real property used in a qualified use, passing to qualified heirs, and to be specially valued on this Form 706.

A Schedule and item number from Form 706	B Full value (without section 2032A(b)(3)(B) adjustment)	C Adjusted value (with section 2032A(b)(3)(B) adjustment)	D Value based on qualified use (without section 2032A(b)(3)(B) adjustment)
Totals			

Attach a legal description of all property listed on line 2.

Attach copies of appraisals showing the column B values for all property listed on line 2.

3 Real property used in a qualified use, passing to qualified heirs, but not specially valued on this Form 706.

A Schedule and item number from Form 706	B Full value (without section 2032A(b)(3)(B) adjustment)	C Adjusted value (with section 2032A(b)(3)(B) adjustment)	D Value based on qualified use (without section 2032A(b)(3)(B) adjustment)
Totals			

If you checked "Regular election," you must attach copies of appraisals showing the column B values for all property listed on line 3.

(continued on next page)

Schedule A-1—Page 8

Form 706 (Rev. 7-99)

4 Personal property used in a qualified use and passing to qualified heirs.

A Schedule and item number from Form 706	B Adjusted value (with section 2032A(b)(3)(B) adjustment)	A (continued) Schedule and item number from Form 706	B (continued) Adjusted value (with section 2032A(b)(3)(B) adjustment)
		"Subtotal" from Col. B, below left	
Subtotal		**Total adjusted value** . . .	

5 Enter the value of the total gross estate as adjusted under section 2032A(b)(3)(A). ▶ ______

6 **Attach a description of the method used to determine the special value based on qualified use.**

7 Did the decedent and/or a member of his or her family own all property listed on line 2 for at least 5 of the 8 years immediately preceding the date of the decedent's death? . . . . ☐ **Yes** ☐ **No**

8 Were there any periods during the 8-year period preceding the date of the decedent's death during which the decedent or a member of his or her family:

	Yes	No
a Did not own the property listed on line 2 above?		
b Did not use the property listed on line 2 above in a qualified use?		
c Did not materially participate in the operation of the farm or other business within the meaning of section 2032A(e)(6)?.		

If "Yes" to any of the above, you must attach a statement listing the periods. If applicable, describe whether the exceptions of sections 2032A(b)(4) or (5) are met.

9 **Attach affidavits describing the activities constituting material participation and the identity and relationship to the decedent of the material participants.**

10 Persons holding interests. Enter the requested information for each party who received any interest in the specially valued property. **(Each of the qualified heirs receiving an interest in the property must sign the agreement, and the agreement must be filed with this return.)**

	Name	Address
A		
B		
C		
D		
E		
F		
G		
H		

	Identifying number	Relationship to decedent	Fair market value	Special use value
A				
B				
C				
D				
E				
F				
G				
H				

You must attach a computation of the GST tax savings attributable to direct skips for each person listed above who is a skip person. (See instructions.)

11 **Woodlands election.** Check here ▶ ☐ if you wish to make a woodlands election as described in section 2032A(e)(13). Enter the Schedule and item numbers from Form 706 of the property for which you are making this election ▶______

You must attach a statement explaining why you are entitled to make this election. The IRS may issue regulations that require more information to substantiate this election. You will be notified by the IRS if you must supply further information.

Schedule A-1—Page 9

Form 706 (Rev. 7-99)

Part 3. Agreement to Special Valuation Under Section 2032A

Estate of:	Date of Death	Decedent's Social Security Number

There cannot be a valid election unless:

- The agreement is executed by each and every one of the qualified heirs, and
- The agreement is included with the estate tax return when the estate tax return is filed.

We (list all qualified heirs and other persons having an interest in the property required to sign this agreement)

____

____,

being all the qualified heirs and ____

____,

being all other parties having interests in the property which is qualified real property and which is valued under section 2032A of the Internal Revenue Code, do hereby approve of the election made by ____,

Executor/Administrator of the estate of ____,

pursuant to section 2032A to value said property on the basis of the qualified use to which the property is devoted and do hereby enter into this agreement pursuant to section 2032A(d).

The undersigned agree and consent to the application of subsection (c) of section 2032A of the Code with respect to all the property described on line 2 of Part 2 of Schedule A-1 of Form 706, attached to this agreement. More specifically, the undersigned heirs expressly agree and consent to personal liability under subsection (c) of 2032A for the additional estate and GST taxes imposed by that subsection with respect to their respective interests in the above-described property in the event of certain early dispositions of the property or early cessation of the qualified use of the property. It is understood that if a qualified heir disposes of any interest in qualified real property to any member of his or her family, such member may thereafter be treated as the qualified heir with respect to such interest upon filing a Form 706-A and a new agreement.

The undersigned interested parties who are not qualified heirs consent to the collection of any additional estate and GST taxes imposed under section 2032A(c) of the Code from the specially valued property.

If there is a disposition of any interest which passes, or has passed to him or her, or if there is a cessation of the qualified use of any specially valued property which passes or passed to him or her, each of the undersigned heirs agrees to file a **Form 706-A,** United States Additional Estate Tax Return, and pay any additional estate and GST taxes due within 6 months of the disposition or cessation.

It is understood by all interested parties that this agreement is a condition precedent to the election of special use valuation under section 2032A of the Code and must be executed by every interested party even though that person may not have received the estate (or GST) tax benefits or be in possession of such property.

Each of the undersigned understands that by making this election, a lien will be created and recorded pursuant to section 6324B of the Code on the property referred to in this agreement for the adjusted tax differences with respect to the estate as defined in section 2032A(c)(2)(C).

As the interested parties, the undersigned designate the following individual as their agent for all dealings with the Internal Revenue Service concerning the continued qualification of the specially valued property under section 2032A of the Code and on all issues regarding the special lien under section 6324B. The agent is authorized to act for the parties with respect to all dealings with the Service on matters affecting the qualified real property described earlier. This authority includes the following:

- To receive confidential information on all matters relating to continued qualification under section 2032A of the specially valued real property and on all matters relating to the special lien arising under section 6324B.
- To furnish the Internal Revenue Service with any requested information concerning the property.
- To notify the Internal Revenue Service of any disposition or cessation of qualified use of any part of the property.
- To receive, but not to endorse and collect, checks in payment of any refund of Internal Revenue taxes, penalties, or interest.
- To execute waivers (including offers of waivers) of restrictions on assessment or collection of deficiencies in tax and waivers of notice of disallowance of a claim for credit or refund.
- To execute closing agreements under section 7121.

(continued on next page)

Form 706 (Rev. 7-99)

Part 3. Agreement to Special Valuation Under Section 2032A *(Continued)*

Estate of:	Date of Death	Decedent's Social Security Number

- Other acts (specify) ▶ ____________________

By signing this agreement, the agent agrees to provide the Internal Revenue Service with any requested information concerning this property and to notify the Internal Revenue Service of any disposition or cessation of the qualified use of any part of this property.

Name of Agent	Signature	Address

The property to which this agreement relates is listed in Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, and in the Notice of Election, along with its fair market value according to section 2031 of the Code and its special use value according to section 2032A. The name, address, social security number, and interest (including the value) of each of the undersigned in this property are as set forth in the attached Notice of Election.

IN WITNESS WHEREOF, the undersigned have hereunto set their hands at ____________________,

this ________ day of ________ .

SIGNATURES OF EACH OF THE QUALIFIED HEIRS:

Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir

Signatures of other interested parties

Signatures of other interested parties

Schedule A-1—Page 11

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE B—Stocks and Bonds

(For jointly owned property that must be disclosed on Schedule E, see the instructions for Schedule E.)

Item number	Description including face amount of bonds or number of shares and par value where needed for identification. Give 9-digit CUSIP number.	CUSIP number	Unit value	Alternate valuation date	Alternate value	Value at date of death
1						
Total from continuation schedules (or additional sheets) attached to this schedule . . .						
TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 2.)						

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(The instructions to Schedule B are in the separate instructions.)

Schedule B—Page 12

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE C—Mortgages, Notes, and Cash

(For jointly owned property that must be disclosed on Schedule E, see the instructions for Schedule E.)

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1				
	Total from continuation schedules (or additional sheets) attached to this schedule . .			
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 3.)			

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(See the instructions on the reverse side.)

Schedule C—Page 13

Form 706 (Rev. 7-99)

Instructions for Schedule C.— Mortgages, Notes, and Cash

Complete Schedule C and file it with your return if the total gross estate contains any:

- mortgages,
- notes, or
- cash.

List on Schedule C:

- Mortgages and notes payable **to the decedent** at the time of death.
- Cash the decedent had at the date of death.

Do not list on Schedule C:

- Mortgages and notes payable **by the decedent.** (If these are deductible, list them on Schedule K.)

List the items on Schedule C in the following order:

- mortgages,
- promissory notes,
- contracts by decedent to sell land,
- cash in possession, and
- cash in banks, savings and loan associations, and other types of financial organizations.

What to enter in the "Description" column:

For mortgages, list:

- face value,
- unpaid balance,
- date of mortgage,
- date of maturity,
- name of maker,
- property mortgaged,
- interest dates, and
- interest rate.

Example to enter in "Description" column:

"Bond and mortgage of $50,000, unpaid balance: $24,000; dated: January 1, 1981; John Doe to Richard Roe; premises: 22 Clinton Street, Newark, NJ; due: January 1, 1999; interest payable at 10% a year--January 1 and July 1."

For promissory notes, list:

- in the same way as mortgages.

For contracts by the decedent to sell land, list:

- name of purchaser,
- contract date,
- property description,
- sale price,
- initial payment,
- amounts of installment payment,
- unpaid balance of principal, and
- interest rate.

For cash in possession, list:

- such cash separately from bank deposits.

For cash in banks, savings and loan associations, and other types of financial organizations, list:

- name and address of each financial organization,
- amount in each account,
- serial or account number,
- nature of account--checking, savings, time deposit, etc., and
- unpaid interest accrued from date of last interest payment to the date of death.

Important: If you obtain statements from the financial organizations, keep them for IRS inspection.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE D—Insurance on the Decedent's Life

You must list **all** policies on the life of the decedent and attach a Form 712 for each policy.

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1				
Total from continuation schedules (or additional sheets) attached to this schedule . .				
TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 4.)				

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)

(See the instructions on the reverse side.)

Schedule D—Page 15

Instructions for Schedule D—Insurance on the Decedent's Life

If you are required to file Form 706 and there was any insurance on the decedent's life, whether or not included in the gross estate, you must complete Schedule D and file it with the return.

Insurance you must include on Schedule D. Under section 2042 you must include in the gross estate:

- Insurance on the decedent's life receivable by or for the benefit of the estate; and
- Insurance on the decedent's life receivable by beneficiaries other than the estate, as described below.

The term "insurance" refers to life insurance of every description, including death benefits paid by fraternal beneficiary societies operating under the lodge system, and death benefits paid under no-fault automobile insurance policies if the no-fault insurer was unconditionally bound to pay the benefit in the event of the insured's death.

Insurance in favor of the estate. Include on Schedule D the full amount of the proceeds of insurance on the life of the decedent receivable by the executor or otherwise payable to or for the benefit of the estate. Insurance in favor of the estate includes insurance used to pay the estate tax, and any other taxes, debts, or charges that are enforceable against the estate. The manner in which the policy is drawn is immaterial as long as there is an obligation, legally binding on the beneficiary, to use the proceeds to pay taxes, debts, or charges. You must include the full amount even though the premiums or other consideration may have been paid by a person other than the decedent.

Insurance receivable by beneficiaries other than the estate. Include on Schedule D the proceeds of all insurance on the life of the decedent not receivable by or for the benefit of the decedent's estate if the decedent possessed at death any of the incidents of ownership, exercisable either alone or in conjunction with any person.

Incidents of ownership in a policy include:

- The right of the insured or estate to its economic benefits;
- The power to change the beneficiary;
- The power to surrender or cancel the policy;
- The power to assign the policy or to revoke an assignment;
- The power to pledge the policy for a loan;
- The power to obtain from the insurer a loan against the surrender value of the policy;
- A reversionary interest if the value of the reversionary interest was more than 5% of the value of the policy immediately before the decedent died. (An interest in an insurance policy is considered a reversionary interest if, for example, the proceeds become payable to the insured's estate or payable as the insured directs if the beneficiary dies before the insured.)

Life insurance not includible in the gross estate under section 2042 may be includible under some other section of the Code. For example, a life insurance policy could be transferred by the decedent in such a way that it would be includible in the gross estate under section 2036, 2037, or 2038. (See the instructions to Schedule G for a description of these sections.)

Completing the Schedule

You must list every policy of insurance on the life of the decedent, whether or not it is included in the gross estate.

Under "Description" list:

- Name of the insurance company and
- Number of the policy.

For every policy of life insurance listed on the schedule, you must request a statement on **Form 712,** Life Insurance Statement, from the company that issued the policy. Attach the Form 712 to the back of Schedule D.

If the policy proceeds are paid in one sum, enter the net proceeds received (from Form 712, line 24) in the value (and alternate value) columns of Schedule D. If the policy proceeds are not paid in one sum, enter the value of the proceeds as of the date of the decedent's death (from Form 712, line 25).

If part or all of the policy proceeds are not included in the gross estate, you must explain why they were not included.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE E—Jointly Owned Property

(If you elect section 2032A valuation, you must complete Schedule E and Schedule A-1.)

PART 1.—Qualified Joint Interests—Interests Held by the Decedent and His or Her Spouse as the Only Joint Tenants (Section 2040(b)(2))

Item number	Description For securities, give CUSIP number.	Alternate valuation date	Alternate value	Value at date of death
	Total from continuation schedules (or additional sheets) attached to this schedule			
1a	Totals	**1a**		
1b	Amounts included in gross estate (one-half of line **1a**)	**1b**		

PART 2.—All Other Joint Interests

2a State the name and address of each surviving co-tenant. If there are more than three surviving co-tenants, list the additional co-tenants on an attached sheet.

	Name	Address (number and street, city, state, and ZIP code)
A.		
B.		
C.		

Item number	Enter letter for co-tenant	Description (including alternate valuation date if any) For securities, give CUSIP number.	Percentage includible	Includible alternate value	Includible value at date of death
		Total from continuation schedules (or additional sheets) attached to this schedule			
2b		Total other joint interests			
3		**Total includible joint interests** (add lines 1b and 2b). Also enter on Part 5, Recapitulation, page 3, at item 5			

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(See the instructions on the reverse side.)

Schedule E—Page 17

Instructions for Schedule E. Jointly Owned Property

If you are required to file Form 706, you must complete Schedule E and file it with the return if the decedent owned any joint property at the time of death, whether or not the decedent's interest is includible in the gross estate.

Enter on this schedule all property of whatever kind or character, whether real estate, personal property, or bank accounts, in which the decedent held at the time of death an interest either as a joint tenant with right to survivorship or as a tenant by the entirety.

Do not list on this schedule property that the decedent held as a tenant in common, but report the value of the interest on Schedule A if real estate, or on the appropriate schedule if personal property. Similarly, community property held by the decedent and spouse should be reported on the appropriate Schedules A through I. The decedent's interest in a partnership should not be entered on this schedule unless the partnership interest itself is jointly owned. Solely owned partnership interests should be reported on Schedule F, "Other Miscellaneous Property."

Part 1—Qualified joint interests held by decedent and spouse. Under section 2040(b)(2), a joint interest is a qualified joint interest if the decedent and the surviving spouse held the interest as:

- Tenants by the entirety, or
- Joint tenants with right of survivorship if the decedent and the decedent's spouse are the only joint tenants.

Interests that meet either of the two requirements above should be entered in Part 1. Joint interests that do not meet either of the two requirements above should be entered in Part 2.

Under "Description," describe the property as required in the instructions for Schedules A, B, C, and F for the type of property involved. For example, jointly held stocks and bonds should be described using the rules given in the instructions to Schedule B.

Under "Alternate value" and "Value at date of death," enter the full value of the property.

Note: *You cannot claim the special treatment under section 2040(b) for property held jointly by a decedent and a surviving spouse who is not a U.S. citizen. You must report these joint interests on Part 2 of Schedule E, not Part 1.*

Part 2—Other joint interests. All joint interests that were not entered in Part 1 must be entered in Part 2.

For each item of property, enter the appropriate letter A, B, C, etc., from line 2a to indicate the name and address of the surviving co-tenant.

Under "Description," describe the property as required in the instructions for Schedules A, B, C, and F for the type of property involved.

In the "Percentage includible" column, enter the percentage of the total value of the property that you intend to include in the gross estate.

Generally, you must include the full value of the jointly owned property in the gross estate. However, the full value should not be included if you can show that a part of the property originally belonged to the other tenant or tenants and was never received or acquired by the other tenant or tenants from the decedent for less than adequate and full consideration in money or money's worth, or unless you can show that any part of the property was acquired with consideration originally belonging to the surviving joint tenant or tenants. In this case, you may exclude from the value of the property an amount proportionate to the consideration furnished by the other tenant or tenants. Relinquishing or promising to relinquish dower, curtesy, or statutory estate created instead of dower or curtesy, or other marital rights in the decedent's property or estate is not consideration in money or money's worth. See the Schedule A instructions for the value to show for real property that is subject to a mortgage.

If the property was acquired by the decedent and another person or persons by gift, bequest, devise, or inheritance as joint tenants, and their interests are not otherwise specified by law, include only that part of the value of the property that is figured by dividing the full value of the property by the number of joint tenants.

If you believe that less than the full value of the entire property is includible in the gross estate for tax purposes, you must establish the right to include the smaller value by attaching proof of the extent, origin, and nature of the decedent's interest and the interest(s) of the decedent's co-tenant or co-tenants.

In the "Includible alternate value" and "Includible value at date of death" columns, you should enter only the values that you believe are includible in the gross estate.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE F—Other Miscellaneous Property Not Reportable Under Any Other Schedule

(For jointly owned property that must be disclosed on Schedule E, see the instructions for Schedule E.)
(If you elect section 2032A valuation, you must complete Schedule F and Schedule A-1.)

		Yes	No
1	Did the decedent at the time of death own any articles of artistic or collectible value in excess of $3,000 or any collections whose artistic or collectible value combined at date of death exceeded $10,000? . . . . If "Yes," submit full details on this schedule and attach appraisals.		
2	Has the decedent's estate, spouse, or any other person, received (or will receive) any bonus or award as a result of the decedent's employment or death? . . . . If "Yes," submit full details on this schedule.		
3	Did the decedent at the time of death have, or have access to, a safe deposit box? . . . . If "Yes," state location, and if held in joint names of decedent and another, state name and relationship of joint depositor. If any of the contents of the safe deposit box are omitted from the schedules in this return, explain fully why omitted.		

Item number	Description For securities, give CUSIP number.	Alternate valuation date	Alternate value	Value at date of death
1				
Total from continuation schedules (or additional sheets) attached to this schedule . .				
TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 6.)				

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(See the instructions on the reverse side.)

Schedule F—Page 19

Instructions for Schedule F—Other Miscellaneous Property

You must complete Schedule F and file it with the return.

On Schedule F list all items that must be included in the gross estate that are not reported on any other schedule, including:

- Debts due the decedent (other than notes and mortgages included on Schedule C)
- Interests in business
- Insurance on the life of another (obtain and attach **Form 712,** Life Insurance Statement, for each policy)

Note for single premium or paid-up policies: *In certain situations, for example where the surrender value of the policy exceeds its replacement cost, the true economic value of the policy will be greater than the amount shown on line 56 of Form 712. In these situations, you should report the full economic value of the policy on Schedule F. See Rev. Rul. 78-137, 1978-1 C.B. 280 for details.*

- Section 2044 property (see **Decedent Who Was a Surviving Spouse** below)
- Claims (including the value of the decedent's interest in a claim for refund of income taxes or the amount of the refund actually received)
- Rights
- Royalties
- Leaseholds
- Judgments
- Reversionary or remainder interests
- Shares in trust funds (attach a copy of the trust instrument)
- Household goods and personal effects, including wearing apparel
- Farm products and growing crops
- Livestock
- Farm machinery
- Automobiles

If the decedent owned any interest in a partnership or unincorporated business, attach a statement of assets and liabilities for the valuation date and for the 5 years before the valuation date. Also attach statements of the net earnings for the same 5 years. You must account for goodwill in the valuation. In general, furnish the same information and follow the methods used to value close corporations. See the instructions for Schedule B.

All partnership interests should be reported on Schedule F unless the partnership interest, itself, is jointly owned. Jointly owned partnership interests should be reported on Schedule E.

If real estate is owned by the sole proprietorship, it should be reported on Schedule F and not on Schedule A. Describe the real estate with the same detail required for Schedule A.

Line 1. If the decedent owned at the date of death articles with artistic or intrinsic value (e.g., jewelry, furs, silverware, books, statuary, vases, oriental rugs, coin or stamp collections), check the "Yes" box on line 1 and provide full details. If any one article is valued at more than $3,000, or any collection of similar articles is valued at more than $10,000, attach an appraisal by an expert under oath and the required statement regarding the appraiser's qualifications (see Regulations section 20.2031-6(b)).

Decedent Who Was a Surviving Spouse

If the decedent was a surviving spouse, he or she may have received qualified terminable interest property (QTIP) from the predeceased spouse for which the marital deduction was elected either on the predeceased spouse's estate tax return or on a gift tax return, Form 709. The election was available for gifts made and decedents dying after December 31, 1981. List such property on Schedule F.

If this election was made and the surviving spouse retained his or her interest in the QTIP property at death, the full value of the QTIP property is includible in his or her estate, even though the qualifying income interest terminated at death. It is valued as of the date of the surviving spouse's death, or alternate valuation date, if applicable. Do not reduce the value by any annual exclusion that may have applied to the transfer creating the interest.

The value of such property included in the surviving spouse's gross estate is treated as passing from the surviving spouse. It therefore qualifies for the charitable and marital deductions on the surviving spouse's estate tax return if it meets the other requirements for those deductions.

For additional details, see Regulations section 20.2044-1.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE G—Transfers During Decedent's Life

(If you elect section 2032A valuation, you must complete Schedule G and Schedule A-1.)

Item number	Description For securities, give CUSIP number.	Alternate valuation date	Alternate value	Value at date of death
A.	Gift tax paid by the decedent or the estate for all gifts made by the decedent or his or her spouse within 3 years before the decedent's death (section 2035(b))	X X X X X		
B.	Transfers includible under section 2035(a), 2036, 2037, or 2038:			
1				
	Total from continuation schedules (or additional sheets) attached to this schedule . .			
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 7.)			

SCHEDULE H—Powers of Appointment

(Include "5 and 5 lapsing" powers (section 2041(b)(2)) held by the decedent.)

(If you elect section 2032A valuation, you must complete Schedule H and Schedule A-1.)

Item number	Description	Alternate valuation date	Alternate value	Value at date of death
1				
	Total from continuation schedules (or additional sheets) attached to this schedule . .			
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 8.)			

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(The instructions to Schedules G and H are in the separate instructions.)

Schedules G and H—Page 21

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE I—Annuities

Note: *Generally, no exclusion is allowed for the estates of decedents dying after December 31, 1984 (see page 15 of the instructions).*

		Yes	No
A	Are you excluding from the decedent's gross estate the value of a lump-sum distribution described in section 2039(f)(2)?		
	If "Yes," you must attach the information required by the instructions.		

Item number	Description Show the entire value of the annuity before any exclusions.	Alternate valuation date	Includible alternate value	Includible value at date of death
1				
	Total from continuation schedules (or additional sheets) attached to this schedule . .			
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 9.)			

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)

(The instructions to Schedule I are in the separate instructions.)

Schedule I—Page 22

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE J—Funeral Expenses and Expenses Incurred in Administering Property Subject to Claims

Note: *Do not list on this schedule expenses of administering property not subject to claims. For those expenses, see the instructions for Schedule L.*

If executors' commissions, attorney fees, etc., are claimed and allowed as a deduction for estate tax purposes, they are not allowable as a deduction in computing the taxable income of the estate for Federal income tax purposes. They are allowable as an income tax deduction on Form 1041 if a waiver is filed to waive the deduction on Form 706 (see the Form 1041 instructions).

Item number	Description	Expense amount	Total amount
	A. Funeral expenses:		
1			
	Total funeral expenses . . . . ▶		
	B. Administration expenses:		
	1 Executors' commissions—amount estimated/agreed upon/paid. (Strike out the words that do not apply.)		
	2 Attorney fees—amount estimated/agreed upon/paid. (Strike out the words that do not apply.). .		
	3 Accountant fees—amount estimated/agreed upon/paid. (Strike out the words that do not apply.).		
	4 Miscellaneous expenses:	Expense amount	
	Total miscellaneous expenses from continuation schedules (or additional sheets) attached to this schedule		
	Total miscellaneous expenses . . . . ▶		
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 13.) . . . . ▶		

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(See the instructions on the reverse side.)

Schedule J—Page 23

Instructions for Schedule J—Funeral Expenses and Expenses Incurred in Administering Property Subject to Claims

General. You must complete and file Schedule J if you claim a deduction on item 13 of Part 5, Recapitulation.

On Schedule J, itemize funeral expenses and expenses incurred in administering property subject to claims. List the names and addresses of persons to whom the expenses are payable and describe the nature of the expense. **Do not list expenses incurred in administering property not subject to claims on this schedule. List them on Schedule L instead.**

The deduction is limited to the amount paid for these expenses that is allowable under local law but may not exceed:

1. The value of property subject to claims included in the gross estate, plus

2. The amount paid out of property included in the gross estate but not subject to claims. This amount must actually be paid by the due date of the estate tax return.

The applicable local law under which the estate is being administered determines which property is and is not subject to claims. If under local law a particular property interest included in the gross estate would bear the burden for the payment of the expenses, then the property is considered property subject to claims.

Unlike certain claims against the estate for debts of the decedent (see the instructions for Schedule K in the separate instructions), you cannot deduct expenses incurred in administering property subject to claims on both the estate tax return and the estate's income tax return. If you choose to deduct them on the estate tax return, you cannot deduct them on a Form 1041 filed for the estate. Funeral expenses are only deductible on the estate tax return.

Funeral Expenses. Itemize funeral expenses on line A. Deduct from the expenses any amounts that were reimbursed, such as death benefits payable by the Social Security Administration and the Veterans Administration.

Executors' Commissions. When you file the return, you may deduct commissions that have actually been paid to you or that you expect will be paid. You may not deduct commissions if none will be collected. If the amount of the commissions has not been fixed by decree of the proper court, the deduction will be allowed on the final examination of the return, provided that:

- The District Director is reasonably satisfied that the commissions claimed will be paid;
- The amount entered as a deduction is within the amount allowable by the laws of the jurisdiction where the estate is being administered;
- It is in accordance with the usually accepted practice in that jurisdiction for estates of similar size and character.

If you have not been paid the commissions claimed at the time of the final examination of the return, you must support the amount you deducted with an affidavit or statement signed under the penalties of perjury that the amount has been agreed upon and will be paid.

You may not deduct a bequest or devise made to you instead of commissions. If, however, the decedent fixed by will the compensation payable to you for services to be rendered in the administration of the estate, you may deduct this amount to the extent it is not more than the compensation allowable by the local law or practice.

Do not deduct on this schedule amounts paid as trustees' commissions whether received by you acting in the capacity of a trustee or by a separate trustee. If such amounts were paid in administering property not subject to claims, deduct them on Schedule L.

Note: *Executors' commissions are taxable income to the executors. Therefore, be sure to include them as income on your individual income tax return.*

Attorney Fees. Enter the amount of attorney fees that have actually been paid or that you reasonably expect to be paid. If on the final examination of the return the fees claimed have not been awarded by the proper court and paid, the deduction will be allowed provided the District Director is reasonably satisfied that the amount claimed will be paid and that it does not exceed a reasonable payment for the services performed, taking into account the size and character of the estate and the local law and practice. If the fees claimed have not been paid at the time of final examination of the return, the amount deducted must be supported by an affidavit, or statement signed under the penalties of perjury, by the executor or the attorney stating that the amount has been agreed upon and will be paid.

Do not deduct attorney fees incidental to litigation incurred by the beneficiaries. These expenses are charged against the beneficiaries personally and are not administration expenses authorized by the Code.

Interest Expense. Interest expenses incurred after the decedent's death are generally allowed as a deduction if they are reasonable, necessary to the administration of the estate, and allowable under local law.

Interest incurred as the result of a Federal estate tax deficiency is a deductible administrative expense. Penalties are not deductible even if they are allowable under local law.

Note: *If you elect to pay the tax in installments under section 6166, you may* **not** *deduct the interest payable on the installments.*

Miscellaneous Expenses. Miscellaneous administration expenses necessarily incurred in preserving and distributing the estate are deductible. These expenses include appraiser's and accountant's fees, certain court costs, and costs of storing or maintaining assets of the estate.

The expenses of selling assets are deductible only if the sale is necessary to pay the decedent's debts, the expenses of administration, or taxes, or to preserve the estate or carry out distribution.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE K—Debts of the Decedent, and Mortgages and Liens

Item number	Debts of the Decedent—Creditor and nature of claim, and allowable death taxes	Amount unpaid to date	Amount in contest	Amount claimed as a deduction
1				
Total from continuation schedules (or additional sheets) attached to this schedule				
TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 14.)				

Item number	Mortgages and Liens—Description	Amount
1		
Total from continuation schedules (or additional sheets) attached to this schedule		
TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 15.)		

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(The instructions to Schedule K are in the separate instructions.)

Schedule K—Page 25

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE L—Net Losses During Administration and Expenses Incurred in Administering Property Not Subject to Claims

Item number	Net losses during administration (**Note:** *Do not deduct losses claimed on a Federal income tax return.*)	Amount
1		
	Total from continuation schedules (or additional sheets) attached to this schedule	
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 18.)	

Item number	Expenses incurred in administering property not subject to claims (Indicate whether estimated, agreed upon, or paid.)	Amount
1		
	Total from continuation schedules (or additional sheets) attached to this schedule	
	TOTAL. (Also enter on Part 5, Recapitulation, page 3, at item 19.)	

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)

Schedule L—Page 26 (The instructions to Schedule L are in the separate instructions.)

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE M—Bequests, etc., to Surviving Spouse

Election To Deduct Qualified Terminable Interest Property Under Section 2056(b)(7). If a trust (or other property) meets the requirements of qualified terminable interest property under section 2056(b)(7), and

a. The trust or other property is listed on Schedule M, and

b. The value of the trust (or other property) is entered in whole or in part as a deduction on Schedule M,

then unless the executor specifically identifies the trust (all or a fractional portion or percentage) or other property to be excluded from the election, the executor shall be deemed to have made an election to have such trust (or other property) treated as qualified terminable interest property under section 2056(b)(7).

If less than the entire value of the trust (or other property) that the executor has included in the gross estate is entered as a deduction on Schedule M, the executor shall be considered to have made an election only as to a fraction of the trust (or other property). The numerator of this fraction is equal to the amount of the trust (or other property) deducted on Schedule M. The denominator is equal to the total value of the trust (or other property).

Election To Deduct Qualified Domestic Trust Property Under Section 2056A. If a trust meets the requirements of a qualified domestic trust under section 2056A(a) and this return is filed no later than 1 year after the time prescribed by law (including extensions) for filing the return, and

a. The entire value of a trust or trust property is listed on Schedule M, and

b. The entire value of the trust or trust property is entered as a deduction on Schedule M,

then unless the executor specifically identifies the trust to be excluded from the election, the executor shall be deemed to have made an election to have the entire trust treated as qualified domestic trust property.

			Yes	No
1	Did any property pass to the surviving spouse as a result of a qualified disclaimer? . . . . *If "Yes," attach a copy of the written disclaimer required by section 2518(b).*	1		
2a	In what country was the surviving spouse born? ____________			
b	What is the surviving spouse's date of birth? ____________			
c	Is the surviving spouse a U.S. citizen?	2c		
d	If the surviving spouse is a naturalized citizen, when did the surviving spouse acquire citizenship? ____________			
e	If the surviving spouse is not a U.S. citizen, of what country is the surviving spouse a citizen? ____________			
3	**Election Out of QTIP Treatment of Annuities**—Do you elect under section 2056(b)(7)(C)(ii) **not** to treat as qualified terminable interest property any joint and survivor annuities that are included in the gross estate and would otherwise be treated as qualified terminable interest property under section 2056(b)(7)(C)? (see instructions)	3		

Item number	Description of property interests passing to surviving spouse	Amount
1		
	Total from continuation schedules (or additional sheets) attached to this schedule	

4	**Total** amount of property interests listed on Schedule M			4	
5a	Federal estate taxes payable out of property interests listed on Schedule M . .	5a			
b	Other death taxes payable out of property interests listed on Schedule M . . .	5b			
c	Federal and state GST taxes payable out of property interests listed on Schedule M	5c			
d	Add items 5a, b, and c			5d	
6	Net amount of property interests listed on Schedule M (subtract 5d from 4). Also enter on Part 5, Recapitulation, page 3, at item 20			6	

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(See the instructions on the reverse side.)

Schedule M—Page 27

Form 706 (Rev. 7-99)

Examples of Listing of Property Interests on Schedule M

Item number	Description of property interests passing to surviving spouse	Amount
1	One-half the value of a house and lot, 256 South West Street, held by decedent and surviving spouse as joint tenants with right of survivorship under deed dated July 15, 1957 (Schedule E, Part I, item 1)	$132,500
2	Proceeds of Gibraltar Life Insurance Company policy No. 104729, payable in one sum to surviving spouse (Schedule D, item 3)	200,000
3	Cash bequest under Paragraph Six of will	100,000

Instructions for Schedule M—Bequests, etc., to Surviving Spouse (Marital Deduction)

General

You must complete Schedule M and file it with the return if you claim a deduction on item 20 of Part 5, Recapitulation.

The marital deduction is authorized by section 2056 for certain property interests that pass from the decedent to the surviving spouse. You may claim the deduction only for property interests that are included in the decedent's gross estate (Schedules A through I).

Note: *The marital deduction is generally not allowed if the surviving spouse is* ***not*** *a U.S. citizen. The marital deduction is allowed for property passing to such a surviving spouse in a "qualified domestic trust" or if such property is transferred or irrevocably assigned to such a trust before the estate tax return is filed. The executor must elect qualified domestic trust status on this return. See the instructions that follow, on pages 29–30, for details on the election.*

Property Interests That You May List on Schedule M

Generally, you may list on Schedule M all property interests that pass from the decedent to the surviving spouse and are included in the gross estate. However, you should not list any "Nondeductible terminable interests" (described below) on Schedule M unless you are making a QTIP election. The property for which you make this election must be included on Schedule M. See "Qualified terminable interest property" on the following page.

For the rules on common disaster and survival for a limited period, see section 2056(b)(3).

You may list on Schedule M only those interests that the surviving spouse takes:

1. As the decedent's legatee, devisee, heir, or donee;

2. As the decedent's surviving tenant by the entirety or joint tenant;

3. As an appointee under the decedent's exercise of a power or as a taker in default at the decedent's nonexercise of a power;

4. As a beneficiary of insurance on the decedent's life;

5. As the surviving spouse taking under dower or curtesy (or similar statutory interest); and

6. As a transferee of a transfer made by the decedent at any time.

Property Interests That You May Not List on Schedule M

You should not list on Schedule M:

1. The value of any property that does not pass from the decedent to the surviving spouse;

2. Property interests that are not included in the decedent's gross estate;

3. The full value of a property interest for which a deduction was claimed on Schedules J through L. The value of the property interest should be reduced by the deductions claimed with respect to it;

4. The full value of a property interest that passes to the surviving spouse subject to a mortgage or other encumbrance or an obligation of the surviving spouse. Include on Schedule M only the net value of the interest after reducing it by the amount of the mortgage or other debt;

5. Nondeductible terminable interests (described below);

6. Any property interest disclaimed by the surviving spouse.

Terminable Interests

Certain interests in property passing from a decedent to a surviving spouse are referred to as *terminable interests.* These are interests that will terminate or fail after the passage of time, or on the occurrence or nonoccurrence of some contingency. Examples are: life estates, annuities, estates for terms of years, and patents.

The ownership of a bond, note, or other contractual obligation, which when discharged would not have the effect of an annuity for life or for a term, is not considered a terminable interest.

Nondeductible terminable interests. A terminable interest is *nondeductible,* and should not be entered on Schedule M (unless you are making a QTIP election) if:

1. Another interest in the same property passed from the decedent to some other person for less than adequate and full consideration in money or money's worth; and

2. By reason of its passing, the other person or that person's heirs may enjoy part of the property after the termination of the surviving spouse's interest.

This rule applies even though the interest that passes from the decedent to a person other than the surviving spouse is not included in the gross estate, and regardless of when the interest passes. The rule also applies regardless of whether the surviving spouse's interest and the other person's interest pass from the decedent at the same time.

Property interests that are considered to pass to a person other than the surviving spouse are any property interest that: **(a)** passes under a decedent's will or intestacy; **(b)** was transferred by a decedent during life; or **(c)** is held by or passed on to any person as a decedent's joint tenant, as appointee under a decedent's exercise of a power, as taker in default at a decedent's release or nonexercise of a power, or as a beneficiary of insurance on the decedent's life.

For example, a decedent devised real property to his wife for life, with remainder to his children. The life interest that passed to the wife does not qualify for the marital deduction because it will terminate at her death and the children will thereafter possess or enjoy the property.

However, if the decedent purchased a joint and survivor annuity for himself and his wife who survived him, the value of the survivor's annuity, to the extent that it is included in the gross estate, qualifies for the marital deduction because even though the interest will terminate on the wife's death, no one else will possess or enjoy any part of the property.

The marital deduction is not allowed for an interest that the decedent directed the executor or a trustee to convert, after death, into a terminable interest for the surviving spouse. The marital deduction is not allowed for such an interest even if there was no interest

in the property passing to another person and even if the terminable interest would otherwise have been deductible under the exceptions described below for life estate and life insurance and annuity payments with powers of appointment. For more information, see Regulations sections 20.2056(b)-1(f) and 20.2056(b)-1(g), Example (7).

If any property interest passing from the decedent to the surviving spouse may be paid or otherwise satisfied out of any of a group of assets, the value of the property interest is, for the entry on Schedule M, reduced by the value of any asset or assets that, if passing from the decedent to the surviving spouse, would be nondeductible terminable interests. Examples of property interests that may be paid or otherwise satisfied out of any of a group of assets are a bequest of the residue of the decedent's estate, or of a share of the residue, and a cash legacy payable out of the general estate.

Example: A decedent bequeathed $100,000 to the surviving spouse. The general estate includes a term for years (valued at $10,000 in determining the value of the gross estate) in an office building, which interest was retained by the decedent under a deed of the building by gift to a son. Accordingly, the value of the specific bequest entered on Schedule M is $90,000.

Life Estate With Power of Appointment in the Surviving Spouse. A property interest, whether or not in trust, will be treated as passing to the surviving spouse, and will not be treated as a nondeductible terminable interest if: **(a)** the surviving spouse is entitled for life to all of the income from the entire interest; **(b)** the income is payable annually or at more frequent intervals; **(c)** the surviving spouse has the power, exercisable in favor of the surviving spouse or the estate of the surviving spouse, to appoint the entire interest; **(d)** the power is exercisable by the surviving spouse alone and (whether exercisable by will or during life) is exercisable by the surviving spouse in all events; and **(e)** no part of the entire interest is subject to a power in any other person to appoint any part to any person other than the surviving spouse (or the surviving spouse's legal representative or relative if the surviving spouse is disabled. See Rev. Rul. 85-35, 1985-1 C.B. 328). If these five conditions are satisfied only for a specific portion of the entire interest, see the section 2056(b) regulations to determine the amount of the marital deduction.

Life Insurance, Endowment, or Annuity Payments, With Power of Appointment in Surviving Spouse. A property interest consisting of the entire proceeds under a life insurance, endowment, or annuity contract is treated as passing from the decedent to the surviving spouse, and will not be treated as a nondeductible terminable interest if: **(a)** the surviving spouse is entitled to receive the proceeds in installments, or is entitled to interest on them, with all amounts payable during the life of the spouse, payable only to the surviving spouse; **(b)** the installment or interest payments are payable annually, or more frequently, beginning not later than 13 months after the decedent's death; **(c)** the surviving spouse has the power, exercisable in favor of the surviving spouse or of the estate of the surviving spouse, to appoint all amounts payable under the contract; **(d)** the power is exercisable by the surviving spouse alone and (whether exercisable by will or during life) is exercisable by the surviving spouse in all events; and **(e)** no part of the amount payable under the contract is subject to a power in any other person to appoint any part to any person other than the surviving spouse. If these five conditions are satisfied only for a specific portion of the proceeds, see the section 2056(b) regulations to determine the amount of the marital deduction.

Charitable Remainder Trusts. An interest in a charitable remainder trust will **not** be treated as a nondeductible terminable interest if:

1. The interest in the trust passes from the decedent to the surviving spouse; and

2. The surviving spouse is the only beneficiary of the trust other than charitable organizations described in section 170(c).

A "charitable remainder trust" is either a charitable remainder annuity trust or a charitable remainder unitrust. (See section 664 for descriptions of these trusts.)

Election To Deduct Qualified Terminable Interests (QTIP)

You may elect to claim a marital deduction for qualified terminable interest property or property interests. You make the QTIP election simply by listing the qualified terminable interest property on Schedule M and deducting its value. You are presumed to have made the QTIP election if you list the property and deduct its value on Schedule M. If you make this election, the surviving spouse's gross estate will include the value of the "qualified terminable interest property." See the instructions for line 6 of General Information for more details. **The election is irrevocable.**

If you file a Form 706 in which you do not make this election, you may not file an amended return to make the election unless you file the amended return on or before the due date for filing the original Form 706.

The effect of the election is that the property (interest) will be treated as passing to the surviving spouse and will not be treated as a nondeductible terminable interest. All of the other marital deduction requirements must still be satisfied before you may make this election. For example, you may not make this election for property or property interests that are not included in the decedent's gross estate.

Qualified terminable interest property is property **(a)** that passes from the decedent, and **(b)** in which the surviving spouse has a qualifying income interest for life.

The surviving spouse has a *qualifying income interest for life* if the surviving spouse is entitled to all of the income from the property payable annually or at more frequent intervals, or has a usufruct interest for life in the property, and during the surviving spouse's lifetime no person has a power to appoint any part of the property to any person other than the surviving spouse. An annuity is treated as an income interest regardless of whether the property from which the annuity is payable can be separately identified.

Amendments to Regulations sections 20.2044-1, 20.2056(b)-7 and 20.2056(b)-10 clarify that an interest in property is eligible for QTIP treatment if the income interest is contingent upon the executor's election even if that portion of the property for which no election is made will pass to or for the benefit of beneficiaries other than the surviving spouse.

The QTIP election may be made for all or any part of qualified terminable interest property. A partial election must relate to a fractional or percentile share of the property so that the elective part will reflect its proportionate share of the increase or decline in the whole of the property when applying sections 2044 or 2519. Thus, if the interest of the surviving spouse in a trust (or other property in which the spouse has a qualified life estate) is qualified terminable interest property, you may make an election for a part of the trust (or other property) only if the election relates to a defined fraction or percentage of the entire trust (or other property). The fraction or percentage may be defined by means of a formula.

Qualified Domestic Trust Election (QDOT)

The marital deduction is allowed for transfers to a surviving spouse who is not a U.S. citizen only if the property passes to the surviving spouse in a "qualified domestic trust" (QDOT) or if

such property is transferred or irrevocably assigned to a QDOT before the decedent's estate tax return is filed.

A QDOT is any trust:

1. That requires at least one trustee to be either an individual who is a citizen of the United States or a domestic corporation;

2. That requires that no distribution of corpus from the trust can be made unless such a trustee has the right to withhold from the distribution the tax imposed on the QDOT;

3. That meets the requirements of any applicable regulations; and

4. For which the executor has made an election on the estate tax return of the decedent.

Note: *For trusts created by an instrument executed before November 5, 1990, paragraphs 1 and 2 above will be treated as met if the trust instrument requires that all trustees be individuals who are citizens of the United States or domestic corporations.*

You make the QDOT election simply by listing the qualified domestic trust or the **entire value** of the trust property on Schedule M and deducting its value. You are presumed to have made the QDOT election if you list the trust or trust property and deduct its value on Schedule M. **Once made, the election is irrevocable.**

If an election is made to deduct qualified domestic trust property under section 2056A(d), the following information should be provided for each qualified domestic trust on an attachment to this schedule:

1. The name and address of every trustee;

2. A description of each transfer passing from the decedent that is the source of the property to be placed in trust; and

3. The employer identification number (EIN) for the trust.

The election must be made for an entire QDOT trust. In listing a trust for which you are making a QDOT election, unless you specifically identify the trust as not subject to the election, the election will be considered made for the entire trust.

The determination of whether a trust qualifies as a QDOT will be made as of the date the decedent's Form 706 is filed. If, however, judicial proceedings are brought before the Form 706's due date (including extensions) to have the trust revised to meet the QDOT requirements, then the determination will not be made until the court-ordered changes to the trust are made.

Line 1

If property passes to the surviving spouse as the result of a qualified disclaimer, check "Yes" and attach a copy of the written disclaimer required by section 2518(b).

Line 3

Section 2056(b)(7) creates an automatic QTIP election for certain joint and survivor annuities that are includible in the estate under section 2039. To qualify, only the surviving spouse can have the right to receive payments before the death of the surviving spouse.

The executor can elect out of QTIP treatment, however, by checking the "Yes" box on line 3. Once made, the election is irrevocable. If there is more than one such joint and survivor annuity, you are not required to make the election for all of them.

If you make the election out of QTIP treatment by checking "Yes" on line 3, you cannot deduct the amount of the annuity on Schedule M. If you do not make the election out, you must list the joint and survivor annuities on Schedule M.

Listing Property Interests on Schedule M

List each property interest included in the gross estate that passes from the decedent to the surviving spouse and for which a marital deduction is claimed. This includes otherwise nondeductible terminable interest property for which you are making a QTIP election. Number each item in sequence and describe each item in detail. Describe the instrument (including any clause or paragraph number) or provision of law under which each item passed to the surviving spouse. If possible, show where each item appears (number and schedule) on Schedules A through I.

In listing otherwise nondeductible property for which you are making a QTIP election, unless you specifically identify a fractional portion of the trust or other property as not subject to the election, the election will be considered made for all of the trust or other property.

Enter the value of each interest before taking into account the Federal estate tax or any other death tax. The valuation dates used in determining the value of the gross estate apply also on Schedule M.

If Schedule M includes a bequest of the residue or a part of the residue of the decedent's estate, attach a copy of the computation showing how the value of the residue was determined. Include a statement showing:

- The value of all property that is included in the decedent's gross estate (Schedules A through I) but is not a part of the decedent's probate estate, such as lifetime transfers, jointly owned property that passed to the survivor on decedent's death, and the insurance payable to specific beneficiaries.
- The values of all specific and general legacies or devises, with reference to the applicable clause or paragraph of the decedent's will or codicil. (If legacies are made to each member of a class; for example, $1,000 to each of decedent's employees, only the number in each class and the total value of property received by them need be furnished.)
- The date of birth of all persons, the length of whose lives may affect the value of the residuary interest passing to the surviving spouse.
- Any other important information such as that relating to any claim to any part of the estate not arising under the will.

Lines 5a, b, and c—The total of the values listed on Schedule M must be reduced by the amount of the Federal estate tax, the Federal GST tax, and the amount of state or other death and GST taxes paid out of the property interest involved. If you enter an amount for state or other death or GST taxes on lines 5b or 5c, identify the taxes and attach your computation of them.

Attachments. If you list property interests passing by the decedent's will on Schedule M, attach a certified copy of the order admitting the will to probate. If, when you file the return, the court of probate jurisdiction has entered any decree interpreting the will or any of its provisions affecting any of the interests listed on Schedule M, or has entered any order of distribution, attach a copy of the decree or order. In addition, the District Director may request other evidence to support the marital deduction claimed.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE O—Charitable, Public, and Similar Gifts and Bequests

		Yes	No
1a	If the transfer was made by will, has any action been instituted to have interpreted or to contest the will or any of its provisions affecting the charitable deductions claimed in this schedule? If "Yes," full details must be submitted with this schedule.		
b	According to the information and belief of the person or persons filing this return, is any such action planned? If "Yes," full details must be submitted with this schedule.		
2	Did any property pass to charity as the result of a qualified disclaimer? If "Yes," attach a copy of the written disclaimer required by section 2518(b).		

Item number	Name and address of beneficiary	Character of institution	Amount
1			
Total from continuation schedules (or additional sheets) attached to this schedule			

3	Total		3	
4a	Federal estate tax payable out of property interests listed above	4a		
b	Other death taxes payable out of property interests listed above	4b		
c	Federal and state GST taxes payable out of property interests listed above	4c		
d	Add items 4a, b, and c		4d	
5	Net value of property interests listed above (subtract 4d from 3). Also enter on Part 5, Recapitulation, page 3, at item 21		5	

(If more space is needed, attach the continuation schedule from the end of this package or additional sheets of the same size.)
(The instructions to Schedule O are in the separate instructions.)

Schedule O—Page 31

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE P—Credit for Foreign Death Taxes

List all foreign countries to which death taxes have been paid and for which a credit is claimed on this return.

If a credit is claimed for death taxes paid to more than one foreign country, compute the credit for taxes paid to one country on this sheet and attach a separate copy of Schedule P for each of the other countries.

The credit computed on this sheet is for the .... (Name of death tax or taxes)

.... imposed in .... (Name of country)

Credit is computed under the .... (Insert title of treaty or "statute")

Citizenship (nationality) of decedent at time of death

(All amounts and values must be entered in United States money.)		
1 Total of estate, inheritance, legacy, and succession taxes imposed in the country named above attributable to property situated in that country, subjected to these taxes, and included in the gross estate (as defined by statute)	1	
2 Value of the gross estate (adjusted, if necessary, according to the instructions for item 2)	2	
3 Value of property situated in that country, subjected to death taxes imposed in that country, and included in the gross estate (adjusted, if necessary, according to the instructions for item 3)	3	
4 Tax imposed by section 2001 reduced by the total credits claimed under sections 2010, 2011, and 2012 (see instructions)	4	
5 Amount of Federal estate tax attributable to property specified at item 3. (Divide item 3 by item 2 and multiply the result by item 4.)	5	
6 Credit for death taxes imposed in the country named above (the smaller of item 1 or item 5). Also enter on line 18 of Part 2, Tax Computation	6	

SCHEDULE Q—Credit for Tax on Prior Transfers

Part 1—Transferor Information

	Name of transferor	Social security number	IRS office where estate tax return was filed	Date of death
A				
B				
C				

Check here ▶ ☐ if section 2013(f) (special valuation of farm, etc., real property) adjustments to the computation of the credit were made (see page 18 of the instructions).

Part 2—Computation of Credit (see instructions beginning on page 18)

Item	Transferor			Total A, B, & C
	A	B	C	
1 Transferee's tax as apportioned (from worksheet, (line 7 ÷ line 8) × line 35 for each column)				
2 Transferor's tax (from each column of worksheet, line 20)				
3 Maximum amount before percentage requirement (for each column, enter amount from line 1 or 2, whichever is smaller)				
4 Percentage allowed (each column) (see instructions)	%	%	%	
5 Credit allowable (line 3 × line 4 for each column)				
6 TOTAL credit allowable (add columns A, B, and C of line 5). Enter here and on line 19 of Part 2, Tax Computation				

Schedules P and Q—Page 32 (The instructions to Schedules P and Q are in the separate instructions.)

Form 706 (Rev. 7-99)

SCHEDULE R—Generation-Skipping Transfer Tax

Note: *To avoid application of the deemed allocation rules, Form 706 and Schedule R should be filed to allocate the GST exemption to trusts that may later have taxable terminations or distributions under section 2612 even if the form is not required to be filed to report estate or GST tax.*

The GST tax is imposed on taxable transfers of interests in property located ***outside the United States*** *as well as property located inside the United States.*

See instructions beginning on page 19.

Part 1—GST Exemption Reconciliation (Section 2631) and Section 2652(a)(3) (Special QTIP) Election

You no longer need to check a box to make a section 2652(a)(3) (special QTIP) election. If you list qualifying property in Part 1, line 9, below, you will be considered to have made this election. See page 21 of the separate instructions for details.

1	Maximum allowable GST exemption	1	
2	Total GST exemption allocated by the decedent against decedent's lifetime transfers	2	
3	Total GST exemption allocated by the executor, using Form 709, against decedent's lifetime transfers	3	
4	GST exemption allocated on line 6 of Schedule R, Part 2	4	
5	GST exemption allocated on line 6 of Schedule R, Part 3	5	
6	Total GST exemption allocated on line 4 of Schedule(s) R-1	6	
7	Total GST exemption allocated to intervivos transfers and direct skips (add lines 2–6)	7	
8	GST exemption available to allocate to trusts and section 2032A interests (subtract line 7 from line 1)	8	
9	Allocation of GST exemption to trusts (as defined for GST tax purposes):		

A Name of trust	B Trust's EIN (if any)	C GST exemption allocated on lines 2–6, above (see instructions)	D Additional GST exemption allocated (see instructions)	E Trust's inclusion ratio (optional—see instructions)
9D Total. May not exceed line 8, above		9D		

10	GST exemption available to allocate to section 2032A interests received by individual beneficiaries (subtract line 9D from line 8). You must attach special use allocation schedule (see instructions)	10	

(The instructions to Schedule R are in the separate instructions.)

Schedule R—Page 33

Form 706 (Rev. 7-99)

Estate of:

Part 2—Direct Skips Where the Property Interests Transferred Bear the GST Tax on the Direct Skips

Name of skip person	Description of property interest transferred	Estate tax value

1 Total estate tax values of all property interests listed above	1	
2 Estate taxes, state death taxes, and other charges borne by the property interests listed above	2	
3 GST taxes borne by the property interests listed above but imposed on direct skips other than those shown on this Part 2 (see instructions)	3	
4 Total fixed taxes and other charges (add lines 2 and 3)	4	
5 Total tentative maximum direct skips (subtract line 4 from line 1)	5	
6 GST exemption allocated	6	
7 Subtract line 6 from line 5	7	
8 GST tax due (divide line 7 by 2.818182)	8	
9 Enter the amount from line 8 of Schedule R, Part 3	9	
10 **Total GST taxes payable by the estate** (add lines 8 and 9). Enter here and on line 22 of Part 2—Tax Computation, on page 1	10	

Schedule R—Page 34

Form 706 (Rev. 7-99)

Estate of:

Part 3—Direct Skips Where the Property Interests Transferred Do Not Bear the GST Tax on the Direct Skips

Name of skip person	Description of property interest transferred	Estate tax value

1 Total estate tax values of all property interests listed above	1	
2 Estate taxes, state death taxes, and other charges borne by the property interests listed above.	2	
3 GST taxes borne by the property interests listed above but imposed on direct skips other than those shown on this Part 3 (see instructions)	3	
4 Total fixed taxes and other charges (add lines 2 and 3).	4	
5 Total tentative maximum direct skips (subtract line 4 from line 1)	5	
6 GST exemption allocated	6	
7 Subtract line 6 from line 5	7	
8 GST tax due (multiply line 7 by .55). Enter here and on Schedule R, Part 2, line 9	8	

Schedule R—Page 35

SCHEDULE R-1 (Form 706)
(Rev. July 1999)
Department of the Treasury
Internal Revenue Service

Generation-Skipping Transfer Tax

Direct Skips From a Trust
Payment Voucher

OMB No. 1545-0015

Executor: File one copy with Form 706 and send two copies to the fiduciary. Do not pay the tax shown. See the separate instructions.
Fiduciary: See instructions on the following page. Pay the tax shown on line 6.

Name of trust		Trust's EIN
Name and title of fiduciary	Name of decedent	
Address of fiduciary (number and street)	Decedent's SSN	Service Center where Form 706 was filed
City, state, and ZIP code	Name of executor	
Address of executor (number and street)	City, state, and ZIP code	
Date of decedent's death	Filing due date of Schedule R, Form 706 (with extensions)	

Part 1—Computation of the GST Tax on the Direct Skip

Description of property interests subject to the direct skip	Estate tax value

		Line	
1	Total estate tax value of all property interests listed above	1	
2	Estate taxes, state death taxes, and other charges borne by the property interests listed above	2	
3	Tentative maximum direct skip from trust (subtract line 2 from line 1)	3	
4	GST exemption allocated	4	
5	Subtract line 4 from line 3	5	
6	**GST tax due from fiduciary** (divide line 5 by 2.818182) **(See instructions if property will not bear the GST tax.)**	6	

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete.

Signature(s) of executor(s) — Date

Date

Signature of fiduciary or officer representing fiduciary — Date

Schedule R-1 (Form 706)—Page 36

Form 706 (Rev. 7-99)

Instructions for the Trustee

Introduction

Schedule R-1 (Form 706) serves as a payment voucher for the Generation-Skipping Transfer (GST) tax imposed on a direct skip from a trust, which you, the trustee of the trust, must pay. The executor completes the Schedule R-1 (Form 706) and gives you 2 copies. File one copy and keep one for your records.

How to pay

You can pay by check or money order.

- Make it payable to the "United States Treasury."
- Make the check or money order for the amount on line 6 of Schedule R-1.
- Write "GST Tax" and the trust's EIN on the check or money order.

Signature

You must sign the Schedule R-1 in the space provided.

What to mail

Mail your check or money order and the copy of Schedule R-1 that you signed.

Where to mail

Mail to the Service Center shown on Schedule R-1.

When to pay

The GST tax is due and payable 9 months after the decedent's date of death (shown on the Schedule R-1). You will owe interest on any GST tax not paid by that date.

Automatic extension

You have an automatic extension of time to file Schedule R-1 and pay the GST tax. The automatic extension allows you to file and pay by 2 months after the due date (with extensions) for filing the decedent's Schedule R (shown on the Schedule R-1).

If you pay the GST tax under the automatic extension, you will be charged interest (but no penalties).

Additional information

For more information, see Code section 2603(a)(2) and the instructions for Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return.

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE T—Qualified Family-Owned Business Interest Deduction

For details on the deduction, including trades and businesses that do not qualify, see page 22 of the separate Instructions for Form 706.

Part 1—Election

Note: *The executor is deemed to have made the election under section 2057 if he or she files Schedule T and deducts any qualifying business interests from the gross estate.*

Part 2—General Qualifications

1 Did the decedent and/or a member of the decedent's family own the business interests listed on line 5 of this schedule for at least 5 of the 8 years immediately preceding the date of the decedent's death? . ☐ **Yes** ☐ **No**

		Yes	No
2	Were there any periods during the 8-year period preceding the date of the decedent's death during which the decedent or a member of his or her family:		
a	Did not own the business interests listed on this schedule?		
b	Did not materially participate, within the meaning of section 2032A(e)(6), in the operation of the business to which such interests relate?.		

If "Yes" to either of the above, you must attach a statement listing the periods. If applicable, describe whether the exceptions of sections 2032A(b)(4) or (5) are met.

Attach affidavits describing the activities constituting material participation and the identity and relationship to the decedent of the material participants.

3 Check the applicable box(es). The qualified family-owned business interest(s) is:

☐ An interest as a proprietor in a trade or business carried on as a proprietorship.

☐ An interest in an entity, at least 50% of which is owned (directly or indirectly) by the decedent and members of the decedent's family.

☐ An interest in an entity, at least 70% of which is owned (directly or indirectly) by members of 2 families and at least 30% of which is owned (directly or indirectly) by the decedent and members of the decedent's family.

☐ An interest in an entity, at least 90% of which is owned (directly or indirectly) by members of 3 families and at least 30% of which is owned (directly or indirectly) by the decedent and members of the decedent's family.

4 Persons holding interests. Enter the requested information for each party who received any interest in the family-owned business. If any qualified heir is not a U.S. citizen, see the line 4 instructions beginning on page 23 of the separate instructions.

(Each of the qualified heirs receiving an interest in the business must sign the agreement that begins on the following page 40, and the agreement must be filed with this return.)

	Name	Address
A		
B		
C		
D		
E		
F		
G		
H		

	Identifying number	Relationship to decedent	Value of interest
A			
B			
C			
D			
E			
F			
G			
H			

Schedule T (Form 706)—Page 38

Form 706 (Rev. 7-99)

Part 3—Adjusted Value of Qualified Family-Owned Business Interests

5 Qualified family-owned business interests reported on this return.
Note: *All property listed on line 5 must also be entered on Schedules A, B, C, E, F, G, or H, as applicable.*

A Schedule and item number from Form 706	B Description of business interest and principal place of business	C Reported value

Line	Description			
6	**Total** reported value			6
7	Amount of claims or mortgages deductible under section 2053(a)(3) or (4) (see separate instructions)		7	
8a	Enter the amount of any indebtedness on qualified residence of the decedent (see separate instructions)	8a		
b	Enter the amount of any indebtedness used for educational or medical expenses (see separate instructions)	8b		
c	Enter the amount of any indebtedness other than that listed on line 8a or 8b, but do not enter more than $10,000 (see separate instructions)	8c		
d	Total (add lines 8a through 8c)		8d	
9	Subtract line 8d from line 7			9
10	Adjusted value of qualified family-owned business interests (subtract line 9 from line 6)			10

Part 4—Qualifying Estate

Line	Description			
11	Includible gifts of qualified family-owned business interests (see separate instructions):			
a	Amount of gifts taken into account under section 2001(b)(1)(B)		11a	
b	Amount of such gifts excluded under section 2503(b)		11b	
c	Add lines 11a and 11b			11c
12	Add lines 10 and 11c			12
13	Adjusted gross estate (see separate instructions):			
a	Amount of gross estate	13a		
b	Enter the amount from line 7	13b		
c	Subtract line 13b from line 13a		13c	
d	Enter the amount from line 11c	13d		
e	Enter the amount of transfers, if any, to the decedent's spouse (see inst.)	13e		
f	Enter the amount of other gifts (see inst.)	13f		
g	Add the amounts on lines 13d, 13e, and 13f	13g		
h	Enter any amounts from line 13g that are otherwise includible in the gross estate	13h		
i	Subtract line 13h from line 13g		13i	
j	Adjusted gross estate (add lines 13c and 13i)			13j
14	Enter one-half of the amount on line 13j			14
	Note: *If line 12 does not exceed line 14, stop here; the estate does not qualify for the deduction. Otherwise, complete line 15.*			
15	Net value of qualified family-owned business interests you elect to deduct (line 10 reduced by any marital or other deductions)—**DO NOT** enter more than $675,000—(see instructions) (attach schedule)—enter here and on Part 5, Recapitulation, page 3, at item 22			15

Schedule T—Page 39

Form 706 (Rev. 7-99)

Part 5—Agreement to Family-Owned Business Interest Deduction Under Section 2057

Estate of:	Date of Death	**Decedent's Social Security Number**

There cannot be a valid election unless:

- The agreement is executed by each and every one of the qualified heirs, and
- The agreement is included with the estate tax return when the estate tax return is filed.

We (list all qualified heirs and other persons having an interest in the business required to sign this agreement)

____

____ ,

being all the qualified heirs and ____

____ ,

being all other parties having interests in the business(es) which are deducted under section 2057 of the Internal Revenue Code, do hereby approve of the election made by ____ ,

Executor/Administrator of the estate of ____ ,

pursuant to section 2057 to deduct said interests from the gross estate and do hereby enter into this agreement pursuant to section 2057(h).

The undersigned agree and consent to the application of subsection (f) of section 2057 of the Code with respect to all the qualified family-owned business interests deducted on Schedule T of Form 706, attached to this agreement. More specifically, the undersigned heirs expressly agree and consent to personal liability under subsection (c) of 2032A (as made applicable by section 2057(i)(3)(F) of the Code) for the additional estate tax imposed by that subsection with respect to their respective interests in the above-described business interests in the event of certain early dispositions of the interests or the occurrence of any of the disqualifying acts described in section 2057(f)(1) of the Code. It is understood that if a qualified heir disposes of any deducted interest to any member of his or her family, such member may thereafter be treated as the qualified heir with respect to such interest upon filing a new agreement and any other form required by the Internal Revenue Service.

The undersigned interested parties who are not qualified heirs consent to the collection of any additional estate tax imposed under section 2057(f) of the Code from the deducted interests.

If there is a disposition of any interest which passes or has passed to him or her, each of the undersigned heirs agrees to file the appropriate form and pay any additional estate tax due within 6 months of the disposition or other disqualifying act.

It is understood by all interested parties that this agreement is a condition precedent to the election of the qualified family-owned business deduction under section 2057 of the Code and must be executed by every interested party even though that person may not have received the estate tax benefits or be in possession of such property.

Each of the undersigned understands that by making this election, a lien will be created and recorded pursuant to section 6324B of the Code on the interests referred to in this agreement for the applicable percentage of the adjusted tax differences with respect to the estate as defined in section 2057(f)(2)(C).

As the interested parties, the undersigned designate the following individual as their agent for all dealings with the Internal Revenue Service concerning the continued qualification of the deducted property under section 2057 of the Code and on all issues regarding the special lien under section 6324B. The agent is authorized to act for all the parties with respect to all dealings with the Service on matters affecting the qualified interests described earlier. This authority includes the following:

- To receive confidential information on all matters relating to continued qualification under section 2057 of the deducted interests and on all matters relating to the special lien arising under section 6324B.
- To furnish the Service with any requested information concerning the interests.
- To notify the Service of any disposition or other disqualifying events specified in section 2057(f)(1) of the Code.
- To receive, but not to endorse and collect, checks in payment of any refund of Internal Revenue taxes, penalties, or interest.
- To execute waivers (including offers of waivers) of restrictions on assessment or collection of deficiencies in tax and waivers of notice of disallowance of a claim for credit or refund.
- To execute closing agreements under section 7121.

(continued on next page)

Form 706 (Rev. 7-99)

Part 5. Agreement to Family-Owned Business Interest Deduction Under Section 2057 (continued)

Estate of:	Date of Death	**Decedent's Social Security Number**

- Other acts (specify) ▶ ______________________

By signing this agreement, the agent agrees to provide the Internal Revenue Service with any requested information concerning the qualified business interests and to notify the Internal Revenue Service of any disposition or other disqualifying events with regard to said interests.

Name of Agent	Signature	Address

The interests to which this agreement relates are listed in Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, along with their fair market value according to section 2031 (or, if applicable, section 2032A) of the Code. The name, address, social security number, and interest (including the value) of each of the undersigned in this business(es) are as set forth in the attached Schedule T.

IN WITNESS WHEREOF, the undersigned have hereunto set their hands at ______________________,

this __________ day of __________.

SIGNATURES OF EACH OF THE QUALIFIED HEIRS:

Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir
Signature of qualified heir	Signature of qualified heir

Signature(s) of other interested parties

Signature(s) of other interested parties

Schedule T, Part 5—Page 41

Form 706 (Rev. 7-99)

Estate of:

SCHEDULE U. Qualified Conservation Easement Exclusion

Part 1—Election

Note: *The executor is deemed to have made the election under section 2031(c)(6) if he or she files Schedule U and excludes any qualifying conservation easements from the gross estate.*

Part 2—General Qualifications

1 Describe the land subject to the qualified conservation easement (see separate instructions) ______________

2 Did the decedent or a member of the decedent's family own the land described above during the 3-year period ending on the date of the decedent's death? . . . . ☐ **Yes** ☐ **No**

3 The land described above is located (check whichever applies) (see separate instructions):

☐ In or within 25 miles of an area which, on the date of the decedent's death, is a metropolitan area.

☐ In or within 25 miles of an area which, on the date of the decedent's death, is a national park or wilderness area.

☐ In or within 10 miles of an area which, on the date of the decedent's death, is an Urban National Forest.

4 Describe the conservation easement with regard to which the exclusion is being claimed (see separate instructions).

Part 3—Computation of Exclusion

Line	Description		Amount		Amount
5	Estate tax value of the land subject to the qualified conservation easement (see separate instructions)			5	
6	Date of death value of any easements granted prior to decedent's death and included on line 11 below (see instructions)	6			
7	Add lines 5 and 6	7			
8	Value of retained development rights on the land (see instructions)	8			
9	Subtract line 8 from line 7	9			
10	Multiply line 9 by 30% (.30).	10			
11	Value of qualified conservation easement for which the exclusion is being claimed (see instructions)	11			
	Note: *If line 11 is less than line 10, continue with line 12. If line 11 is equal to or more than line 10, skip lines 12 through 14, enter ".40" on line 15, and complete the schedule.*				
12	Divide line 11 by line 9. Figure to 3 decimal places (e.g., .123) . .	12			
	If line 12 is equal to or less than .100, stop here; the estate does not qualify for the conservation easement exclusion.				
13	Subtract line 12 from .300. Enter the answer in hundredths by rounding any thousandths up to the next higher hundredth (i.e., .030 = .03; but .031 = .04).	13			
14	Multiply line 13 by 2	14			
15	Subtract line 14 from .40	15			
16	Deduction under section 2055(f) for the conservation easement (see separate instructions).	16			
17	Amount of indebtedness on the land (see separate instructions)	17			
18	Total reductions in value (add lines 8, 16, and 17)			18	
19	Net value of land (subtract line 18 from line 5)			19	
20	Multiply line 19 by line 15			20	
21	Enter the smaller of line 20 or the exclusion limitation (see instructions). Also enter this amount on item 11, Part 5, Recapitulation, Page 3.			21	

Schedule U—Page 42

Form 706 (Rev. 7-99) (Make copies of this schedule before completing it if you will need more than one schedule.)

Estate of:

CONTINUATION SCHEDULE

Continuation of Schedule ______________
(Enter letter of schedule you are continuing.)

Item number	Description For securities, give CUSIP number.	Unit value (Sch. B, E, or G only)	Alternate valuation date	Alternate value	Value at date of death or amount deductible
TOTAL. (Carry forward to main schedule.)					

See the instructions on the reverse side.

Continuation Schedule—Page 43

Form 706 (Rev. 7-99)

Instructions for Continuation Schedule

When you need to list more assets or deductions than you have room for on one of the main schedules, use the Continuation Schedule on page 43. It provides a uniform format for listing additional assets from Schedules A through I and additional deductions from Schedules J, K, L, M, and O.

Please keep the following points in mind:

- Use a separate Continuation Schedule for each main schedule you are continuing. Do not combine assets or deductions from different schedules on one Continuation Schedule.
- Make copies of the blank schedule before completing it if you expect to need more than one.
- Use as many Continuation Schedules as needed to list all the assets or deductions.
- Enter the letter of the schedule you are continuing in the space at the top of the Continuation Schedule.
- Use the *Unit value* column only if continuing Schedule B, E, or G. For all other schedules, use this space to continue the description.
- Carry the total from the Continuation Schedules forward to the appropriate line on the main schedule.

If continuing	Report	Where on Continuation Schedule
Schedule E, Pt. 2	*Percentage includible*	*Alternate valuation date*
Schedule K	*Amount unpaid to date*	*Alternate valuation date*
Schedule K	*Amount in contest*	*Alternate value*
Schedules J, L, M	*Description of deduction continuation*	*Alternate valuation date* **and** *Alternate value*
Schedule O	*Character of institution*	*Alternate valuation date* **and** *Alternate value*
Schedule O	*Amount of each deduction*	*Amount deductible*

Continuation Schedule—Page 44

Form **706-A**
(Rev. August 1999)
Department of the Treasury
Internal Revenue Service

United States Additional Estate Tax Return

(To report dispositions or cessations of qualified use under section 2032A of the Internal Revenue Code)

For Privacy Act and Paperwork Reduction Act Notice, see page 4 of the separate instructions.

OMB No. 1545-0016

Part I General Information

1a Name of qualified heir	2 **Heir's social security number**
1b Address of qualified heir (number and street, including apartment number, P.O. Box, or rural route)	3 Commencement date (see instructions)
1c City, town or post office, state, and ZIP code	

4 Decedent's name reported on Form 706	5 Decedent's social security number	6 Date of death

Part II Tax Computation (First complete Schedules A and B—see instructions.)

Line	Description				
1	Value at date of death (or alternate valuation date) of all specially valued property that passed from decedent to qualified heir:				
a	Without section 2032A election	1a			
b	With section 2032A election	1b			
c	Balance (subtract line 1b from line 1a)			1c	
2	Value at date of death (or alternate valuation date) of all specially valued property in decedent's estate:				
a	Without section 2032A election	2a			
b	With section 2032A election	2b			
c	Balance (subtract line 2b from line 2a)			2c	
3	Decedent's estate tax:				
a	Recomputed without section 2032A election (attach computation)	3a			
b	Reported on Form 706 with section 2032A election	3b			
c	Balance (subtract line 3b from line 3a)			3c	
4	Divide line 1c by line 2c and enter the result as a percentage			4	%
5	Total estate tax saved (multiply line 3c by percentage on line 4)			5	
6	Value, without section 2032A election, at date of death (or alternate valuation date) of specially valued property shown on Schedule A of this Form 706-A	6			
7	Divide line 6 by line 1a and enter the result as a percentage			7	%
8	Multiply line 5 by percentage on line 7			8	
9	Total estate tax recaptured on previous Form(s) 706-A (attach copies of 706-A)			9	
10	Remaining estate tax savings (subtract line 9 from line 5) (do not enter less than zero)			10	
11	Enter the lesser of line 8 or line 10			11	
12	Enter the total of column D, Schedule A, page 2	12			
13	Enter the total of column E, Schedule A, page 2	13			
14	Balance (subtract line 13 from line 12) (but enter the line 12 amount in the case of a disposition of standing timber on qualified woodland)			14	
15	Enter the lesser of line 11 or line 14			15	

If you completed Schedule B, complete lines 16–19. If you did not complete Schedule B, skip lines 16–18 and enter the amount from line 15 on line 19.

Line	Description		
16	Enter the total cost (or FMV) from Schedule B	16	
17	Divide line 16 by line 12 and enter the result as a percentage (do not enter more than 100%)	17	%
18	Multiply line 15 by percentage on line 17	18	
19	**Additional estate tax,** subtract line **18** from line **15** (do not enter less than zero)	19	

Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer other than taxpayer is based on all information of which preparer has any knowledge.

Signature of taxpayer/qualified heir — Date

Signature of preparer other than taxpayer/qualified heir — Date

Address (and ZIP code)

Cat. No. 10141S — Form **706-A** (Rev. 8-99)

Form 706-A (Rev. 8-99) Page 2

Schedule A.—Disposition of Specially Valued Property or Cessation of Qualified Use

List property in chronological order of disposition or cessation

A Item number	B Description of specially valued property and schedule and item number where reported on the decedent's Form 706	C Date of disposition (or date qualified use ceased)	D Amount received (or fair market value if applicable) (see instructions)	E Special use value (see instructions)
1	Form 706, Schedule ...., Item .... Description—			
Totals: Enter total of column D on line 12 of the Tax Computation, and total of column E on line 13 of the Tax Computation.				

Form **706-A** (Rev. 8-99)

Form 706-A (Rev. 8-99) Page 3

Schedule B.—Involuntary Conversions or Exchanges Check if for: ☐ Involuntary conversion ☐ Exchange

Qualified replacement (or exchange) property

A Item	B Description of qualified replacement (or exchange) property	C Cost (or FMV)
1		
Total cost (or FMV) (enter here and on line 16 of the Tax Computation)		

Form **706-A** (Rev. 8-99)

Form 706-A (Rev. 8-99) Page 4

Schedule C.—Dispositions to Family Members of the Qualified Heir

Each transferee must enter into an agreement to be personally liable for any additional taxes imposed by section 2032A(c) and the agreement must be attached to this Form 706-A. (See instructions.)

Transferee #1:	Last name	First name	Middle initial
	Social security number	Relationship to the qualified heir	

Description of property transferred

A Item number	B Description of specially valued property and schedule and item number where reported on the decedent's Form 706	C Date of disposition
1	Form 706, Schedule ...., Item .... Description—	

Transferee #2:	Last name	First name	Middle initial
	Social security number	Relationship to the qualified heir	

Description of property transferred

A Item number	B Description of specially valued property and schedule and item number where reported on the decedent's Form 706	C Date of disposition
1	Form 706, Schedule ...., Item .... Description—	

If there are more than two transferees, attach additional sheets using the same format. Form **706-A** (Rev. 8-99)

Form **706-GS(D)**
(Rev. June 1999)
Department of the Treasury
Internal Revenue Service

Generation-Skipping Transfer Tax Return For Distributions

For calendar year ....

OMB No. 1545-1144

Attach a copy of all Forms 706-GS(D-1) to this return.

Part I **General Information**

1a Name of skip person distributee	1b **Social security number of individual distributee** (see instructions)
2a Name and title of person filing return (if different from **1a**, see instructions)	1c **Employer identification number of trust distributee** (see instructions)

2b Address of distributee or person filing return (see instructions) (number and street or P.O. box; city, town, or post office; state; and ZIP code)

Part II **Distributions**

a Trust EIN (from line **2a**, Form 706-GS(D-1))	b Item no. (from line **3**, column **a**, Form 706-GS(D-1))	c Amount of Transfer (from Tentative transfer, line **3**, column **f**, Form 706-GS(D-1))

3	Total transfers (add amounts in column **c**)	3

Part III **Tax Computation**

4	Adjusted allowable expenses (see instructions)			4	
5	Taxable amount (subtract line 4 from line 3)			5	
6	Maximum Federal estate tax rate (see instructions)			6	%
7	Gross GST tax (multiply line 5 by line 6)			7	
8	Creditable state GST tax (if any)	8			
9	Multiply line 7 by 5% (.05)	9			
10	Allowable credit (enter the smaller of line 8 or line 9)			10	
11	Net GST tax (subtract line 10 from line 7)			11	
12	Payment, if any, made with Form 2758			12	
13	**TAX DUE**—if line 11 is larger than line 12, enter amount owed ▶ *(Make the check payable to the United States Treasury.)*			13	
14	**Overpayment**—if line 12 is larger than line 11, enter amount to be refunded ▶			14	

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer other than taxpayer is based on all information of which preparer has any knowledge.

Please Sign Here	▶ Signature of taxpayer or person filing on behalf of taxpayer	Date
Paid Preparer's Use Only	Preparer's signature ▶	Date
	Firm's name (or yours if self-employed) and address ▶	ZIP code ▶

For Privacy Act and Paperwork Reduction Act Notice, see page 3 of separate instructions. Cat. No. 10327Q Form **706-GS(D)** (Rev. 6-99)

Form **706-GS(D-1)**
(Rev. June 1999)
Department of The Treasury
Internal Revenue Service

Notification of Distribution From a Generation-Skipping Trust

(Complete for each skip person distributee—see separate instructions.)
For calendar year ....

OMB No. 1545-1143

Copy A—Send to IRS

Part I **General Information**

1a Skip person distributee's identifying number (see instructions)	2a **Trust's employer identification number** (see instructions)
1b Skip person distributee's name, address, and ZIP code	2b Trust's name, address, and ZIP code

Part II **Distributions**

3 Describe each distribution below (see instructions).

a Item no.	b Description of property	c Date of distribution	d Inclusion ratio	e Value (see instructions)	f Tentative transfer (multiply col. **e** by col. **d**)
1					

Part III **Trust Information** (see instructions)

4 If this is not an explicit trust, check the box and attach a statement describing the arrangement that makes its effect substantially similar to an explicit trust . . . . ▶ ☐

		Yes	No
5	Has any property been contributed to this trust since the last Form 706-GS(T) or (D-1) was filed? If "Yes," attach a schedule showing how the trust's inclusion ratio has been refigured		
6	Have any contributions been made to this trust since the last Form 706-GS(T) or (D-1) was filed that were not included in calculating the trust's inclusion ratio? If "Yes," attach a statement explaining why the contributions were not included		
7	Has any exemption been allocated to this trust by reason of the deemed allocation rules?		

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer other than trustee is based on all information of which preparer has any knowledge.

Signature of trustee ▶ .... **Date** ▶ ....

Signature of preparer other than trustee ▶ .... **Date** ▶ ....

Address ▶

For Paperwork Reduction Act Notice, see page 5 of the separate trustee's instructions. Cat. No. 10328B Form **706-GS(D-1)** (Rev. 6-99)

Form **706-GS(D-1)**
(Rev. June 1999)
Department of The Treasury
Internal Revenue Service

Notification of Distribution From a Generation-Skipping Trust
(Complete for each skip person distributee—see separate instructions.)
For calendar year ....

OMB No. 1545-1143

Copy B—For Distributee

Part I **General Information**

1a Skip person distributee's identifying number (see instructions)	2a **Trust's employer identification number** (see instructions)
1b Skip person distributee's name, address, and ZIP code	2b Trust's name, address, and ZIP code

Part II **Distributions**

3 Describe each distribution below (see instructions).

a Item no.	b Description of property	c Date of distribution	d Inclusion ratio	e Value (see instructions)	f Tentative transfer (multiply col. **e** by col. **d**)
1					

Skip Person Distributee—To report this distribution, you must file Form 706-GS(D), Generation-Skipping Transfer Tax Return for Distributions, at the following Internal Revenue Service Center. ▶

For Paperwork Reduction Act Notice, see page 5 of the separate trustee's instructions. Form **706-GS(D-1)** (Rev. 6-99)

Instructions for Skip Person Distributee

General Instructions

Purpose of form.—Form 706-GS(D-1) is used by a trustee to report to the distributee and to the Internal Revenue Service distributions from a trust that are subject to the generation-skipping transfer tax. The skip person distributee uses the information on Form 706-GS(D-1) to complete **Form 706-GS(D),** Generation-Skipping Transfer Tax Return for Distributions.

Attach a copy of each Form 706-GS(D-1) you received during the year to your Form 706-GS(D). You should also keep a copy for your records.

Errors.—If you believe the trustee has made an error on your Form 706-GS(D-1), notify the trustee and ask for a corrected Form 706-GS(D-1). Do not change any items on your copy. Be sure that the trustee sends a copy of the corrected Form 706-GS(D-1) to the IRS.

Specific Instructions

Part I

Line 2a.—Enter the trust's employer identification number from Part I of this form in Part II, column **a,** of your Form 706-GS(D).

Part II

Column a.—Use the same item number used here for the corresponding entry in Part II, column **b,** of your Form 706-GS(D).

Column c.—The date of distribution is the date the title to the property distributed passed from the trustee to the distributee. This is the date used to determine the value of the distribution.

Column f.—Enter the tentative transfer amount in Part II, column **c,** of your Form 706-GS(D).

Form **706-GS(T)**
(Rev. July 1999)
Department of the Treasury
Internal Revenue Service

Generation-Skipping Transfer Tax Return For Terminations

For calendar year ......

OMB No. 1545-1145

Part I General Information

1a Name of trust

1b Trust's employer identification number (see instructions)

2a Name of trustee

2b Trustee's address (number and street or P.O. box; apt. or suite no.; city, town or post office; state and ZIP code)

Part II Trust Information (see page 3 of the instructions)

		Yes	No	Sch. A number(s)
3	Has any exemption been allocated to this trust by reason of the deemed allocation rules of section 2632 (b) and (c)? If "Yes," describe the allocation on the line 7, Schedule A attachment showing how the inclusion ratio was calculated			
4	Has property been contributed to this trust since the last Form 706-GS(T) or 706-GS(D-1) was filed? If "Yes," attach a schedule showing how the inclusion ratio was calculated			
5	Have any terminations occurred that are not reported on this return because of the exceptions in section 2611(b)(1) or (2) relating to medical and educational exclusions and prior payment of GST tax? If "Yes," attach a statement describing the termination.			
6	Have any contributions been made to this trust that were not included in calculating the trust's inclusion ratio? If "Yes," attach a statement explaining why the contribution was not included .			
7	Has the special QTIP election in section 2652(a)(3) been made for this trust?.			

8 If this is not an explicit trust (see page 1 of the instructions under **Who Must File**), check box and attach a statement describing the trust arrangement that makes its effect substantially similar to an explicit trust . . . . ▶ ☐

Part III Tax Computation

9a Summary of attached Schedules A (see instructions for line 9b on page 6)

Schedule A No.			Net GST tax (from Sch. A, line 14)
1	. . . .	9a1	
2	. . . .	9a2	
3	. . . .	9a3	
4	. . . .	9a4	
5	. . . .	9a5	
6	. . . .	9a6	
9b	Total from all additional Schedules A attached to this form. . . . . ▶	9b	
10	**Total** net GST tax (add lines 9a1–9b)	10	
11	Payment, if any, made with Form 2758	11	
12	**TAX DUE**—if line 10 is larger than line 11, enter amount owed	12	
13	**Overpayment**—if line 11 is larger than line 10, enter amount to be refunded.	13	

Please Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer other than fiduciary is based on all information of which preparer has any knowledge.

▶ Signature of fiduciary or officer representing fiduciary | Date

Paid Preparer's Use Only

Preparer's signature ▶ | Date

Firm's name (or yours if self-employed) and address ▶ | ZIP code

For Paperwork Reduction Act Notice, see page 1 of separate instructions. Cat. No. 10329M Form **706-GS(T)** (Rev. 7-99)

Form 706-GS(T) (Rev. 7-99) Page 2

Name of trust	EIN of trust

Schedule A No.

Note: *Make copies of this schedule before completing it if you will need more than one Schedule A.*

Schedule A—Taxable Terminations

(See page 4 of the instructions before completing this schedule.)

1	a Name of skip persons	b SSN or EIN of skip person	c Item no. from line 4 below in which interest held

2 Describe the terminating power or interest. If you need more space, attach an additional sheet.

3 If you elect alternate valuation, check here (see page 4 of the instructions) . . . . ▶ ☐

4 Describe each taxable termination below (see page 4 of the instructions)

a Item no.	b Description of property subject to termination	c Date of termination	d Valuation date	e Value
1				
Total . . . . ▶				4

5	Total deductions applicable to this Schedule A (from attached Schedule B, line 5)		5
6	Taxable amount (subtract line 5 from line 4)		6
7	Inclusion ratio (attach separate schedule showing computation)		7
8	Maximium Federal estate tax rate (see page 6 of the instructions)		8 %
9	Applicable rate (multiply line 7 by line 8)		9
10	Gross GST tax (multiply line 6 by line 9)		10
11	Creditable state GST tax, if any (attach credit evidence)	11	
12	Multiply line 10 by 5% (.05)	12	
13	Allowable credit (enter the smaller of line 11 or line 12)		13
14	Net GST tax (subtract line 13 from line 10) (enter here and on line 9, Part III, page 1)		14

Schedule A (Form 706-GS(T)) (Rev. 7-99)

Form 706-GS(T) (Rev. 7-99) Page **3**

Name of trust	**Schedule A No.** ▶
	EIN of trust

Note: *Make copies of this schedule before completing it if you will need more than one Schedule B.*

Schedule B(1)—General Trust Debts, Expenses, and Taxes

(Section 2622(b)) (Enter only items related to the entire trust; see page 4 of the instructions.)

a Item no.	b Description	c Amount
1		

1	Total of Schedule B(1)	1	
2	Percentage allocated to corresponding Schedule A	2	%
3	Net deduction (multiply line 1 by line 2)	3	

Schedule B(2)—Specific Termination-Related Debts, Expenses, and Taxes

(Section 2622(b)) (Enter only items related solely to terminations appearing on corresponding Schedule A; see page 5 of the instructions.)

a Item no.	b Description	c Amount
1		

4	Total of Schedule B(2)	4	
5	**Total**—Add lines 3 and 4 (enter here and on line 5 of the corresponding Schedule A)	5	

Schedules B(1) and B(2) (Form 706-GS(T)) (Rev. 7-99)

Form **706-QDT**
(Rev. January 1996)
Department of the Treasury
Internal Revenue Service

U.S. Estate Tax Return for Qualified Domestic Trusts

Calendar Year 19 ...
▶ See separate instructions.

OMB No. 1545-1212

Part I General Information

1a Name of surviving spouse (see "Definitions" in instructions)	**1b SSN of surviving spouse**
2a Name of designated filer/trustee (see instructions)	**2b SSN or EIN of designated filer/trustee**
2c Address of designated filer/trustee	
3a Surviving spouse's date of death (if applicable)	**3b** Surviving spouse's current marital status
4a Name of decedent	**4b SSN of decedent**
4c Service center where Form 706 for decedent's estate was filed	**4d** Decedent's date of death

Part II Elections by the Designated Filer/Trustee (see instructions)

Please check the "Yes" or "No" box for each question.	Yes	No
1 Do you elect alternate valuation?		
2 Do you elect special use valuation? If "Yes," you must complete and attach Schedule A-1 of Form 706.		
3 Do you elect to pay the taxes in installments as described in section 6166? If "Yes," you must attach the additional information described in the instructions.		
4 If the surviving spouse has become a U.S. citizen, does he or she elect under Code section 2056A(b)(12)(C) to treat all prior taxable distributions as taxable gifts and to treat any of the decedent's unified credit applied to the QDOT tax on those distributions as the surviving spouse's unified credit used under section 2505? (If not a U.S. citizen, enter "N/A")		

Part III Tax Computation

1	Current taxable trust distributions (total from Part II of Schedule A)	1	
2	Value of taxable trust property at date of death (if applicable) (total from Part III of Schedule A)	2	
3	Add lines 1 and 2	3	
4	Charitable and marital deductions (see Schedule B instructions) (total from col. d, Part IV of Sch. A)	4	
5	Net tentative taxable amount (subtract line 4 from line 3)	5	
6	Prior taxable events (total from Part I of Schedule A)	6	
7	Taxable estate of the decedent (see instructions)	7	
8	Add lines 6 and 7.	8	
9	Add lines 5 and 8	9	
10	Recomputation of decedent's estate tax based on the amount on line 9 (see instructions) (attach computation)	10	
11	Recomputation of decedent's estate tax based on the amount on line 8 (see instructions) (attach computation)	11	
12	Net estate tax (subtract line 11 from line 10)	12	
13	Payment made with request for extension, if any, and credit under section 2056A(b)(2)(B)(ii).	13	
14	TAX DUE—(If the amount on line 12 exceeds the amount on line 13, enter the difference here.) ▶	14	
15	Overpayment—(If the amount on line 13 exceeds the amount on line 12, enter the difference here.)	15	

Under penalties of perjury, I declare that I have examined this return, along with accompanying schedules and statements, and to the best of my knowledge and belief it is true, correct, and complete. Declaration of preparer (other than trustee or designated filer) is based on all information of which preparer has any knowledge.

Trustee's or designated filer's signature ▶ Date ▶

Preparer's signature (other than trustee or designated filer) ▶ Date ▶

Preparer's address (other than trustee or designated filer) ▶

For Paperwork Reduction Act Notice, see page 1 of the separate instructions for this form. Cat. No. 12292E Form **706-QDT** (Rev. 1-96)

Form 706-QDT (Rev. 1-96) Page 2

SCHEDULE A—Complete Schedule A **only** if you are a designated filer filing this return for multiple trusts.

Part I Summary of Prior Taxable Distributions

(a) Year	(b) Amount	(c) Year	(d) Amount
19.....	$	19.....	$
19.....	$	19.....	$
19.....	$	19.....	$
19.....	$	19.....	$
19.....	$	19.....	$
19.....	$	19.....	$
19.....	$	19.....	$
19	$	19	$

Total—Combine columns **(b)** and **(d)** ▶

Part II Summary of Current Taxable Distributions

(a) EIN of QDOT	(b) Total Taxable Distributions for the Year	(c) EIN of QDOT	(d) Total Taxable Distributions for the Year
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$
	$		$

Total—Combine columns **(b)** and **(d)** ▶

Part III Summary of Property Remaining in QDOTs at Death of Surviving Spouse

(a) EIN of QDOT	(b) Alternate Valuation Date (if applicable)	(c) Value	(d) EIN of QDOT	(e) Alternate Valuation Date (if applicable)	(f) Value
		$			$
		$			$
		$			$
		$			$
		$			$
		$			$
		$			$
		$			$

Total—Combine columns **(c)** and **(f)** ▶

Part IV Summary of Marital and Charitable Deductions

(a) EIN of QDOT	(b) Total Marital Deduction	(c) Total Charitable Deduction	(d) Total Deductions (add cols. **(b)** and **(c)**)
	$	$	$
	$	$	$
	$	$	$
	$	$	$
	$	$	$
	$	$	$
	$	$	$
	$	$	$

Total ▶

Form 706-QDT (Rev. 1-96) Page 3

SCHEDULE B

Part I General Information (see instructions)

1a Name of trust	1b EIN of trust
2a Name of trustee	2b SSN or EIN of trustee
2c Address of trustee	
3 Name of designated filer, if applicable	
4a Name of surviving spouse	4b SSN of surviving spouse
4c Surviving spouse's date of death (if applicable)	4d Surviving spouse's current marital status (or at death, if applicable)
5a Name of decedent	5b SSN of decedent
5c Service center where Form 706 (or 706-NA) for decedent's estate was filed	5d Decedent's date of death

Part II Taxable Distributions From Prior Years

(a) Year	(b) Amount	(c) Year	(d) Amount
19......	$	19......	$
19......	$	19......	$
19......	$	19......	$
19......	$	19......	$
19......	$	19......	$
19......	$	19......	$
19......	$	19......	$
19......	$	19......	$
19	$	19	$
Total—Combine columns **(b)** and **(d)** ▶			

Part III Current Taxable Distributions

(a) Date of Distribution	(b) Description	(c) Value	(d) Amount of Hardship Exemption Claimed (see instructions)	(e) Net Transfer (col. (c) minus col. (d))
TOTAL ▶				

Form 706-QDT (Rev. 1-96) Page 4

Schedule B (cont.)

Part IV Taxable Property in Trust at Death of Surviving Spouse

(a) Item No.	(b) Description	(c) Alternate Valuation Date	(d) Value
1			
TOTAL . . . . ▶			

Part V Marital Deductions

(a) Item No.	(b) Description of property interests passing to spouse	(c) Value
1		
TOTAL . . . . ▶		

Part VI Charitable Deductions

(a) Item No.	(b) Description	(c) Name and address of beneficiary	(d) Character of institution	(e) Amount
1				
TOTAL . . . . ▶				

Printed on recycled paper

Form **709**

Department of the Treasury
Internal Revenue Service

United States Gift (and Generation-Skipping Transfer) Tax Return

(Section 6019 of the Internal Revenue Code) (For gifts made during calendar year 1999)

▶ **See separate instructions. For Privacy Act Notice, see the Instructions for Form 1040.**

OMB No. 1545-0020

1999

Part 1—General Information

1 Donor's first name and middle initial	2 Donor's last name	3 **Donor's social security number**
4 Address (number, street, and apartment number)		5 Legal residence (domicile) (county and state)
6 City, state, and ZIP code		7 Citizenship

		Yes	No
8	If the donor died during the year, check here ▶ ☐ and enter date of death ...., ...		
9	If you received an extension of time to file this Form 709, check here ▶ ☐ and attach the Form 4868, 2688, 2350, or extension letter		
10	Enter the total number of separate donees listed on Schedule A—count each person only once. ▶		
11a	Have you (the donor) previously filed a Form 709 (or 709-A) for any other year? If the answer is "No," do not complete line 11b .		
11b	If the answer to line 11a is "Yes," has your address changed since you last filed Form 709 (or 709-A)?		
12	Gifts by husband or wife to third parties.—Do you consent to have the gifts (including generation-skipping transfers) made by you and by your spouse to third parties during the calendar year considered as made one-half by each of you? (See instructions.) (If the answer is "Yes," the following information must be furnished and your spouse must sign the consent shown below. **If the answer is "No," skip lines 13–18 and go to Schedule A.**)		
13	Name of consenting spouse — 14 SSN		
15	Were you married to one another during the entire calendar year? (see instructions)		
16	If the answer to 15 is "No," check whether ☐ married ☐ divorced or ☐ widowed, and give date (see instructions) ▶		
17	Will a gift tax return for this calendar year be filed by your spouse?		
18	**Consent of Spouse**—I consent to have the gifts (and generation-skipping transfers) made by me and by my spouse to third parties during the calendar year considered as made one-half by each of us. We are both aware of the joint and several liability for tax created by the execution of this consent.		

Consenting spouse's signature ▶ **Date** ▶

Part 2—Tax Computation

1	Enter the amount from Schedule A, Part 3, line 15	1		
2	Enter the amount from Schedule B, line 3	2		
3	Total taxable gifts (add lines 1 and 2)	3		
4	Tax computed on amount on line 3 (see Table for Computing Tax in separate instructions). . .	4		
5	Tax computed on amount on line 2 (see Table for Computing Tax in separate instructions). . .	5		
6	Balance (subtract line 5 from line 4)	6		
7	Maximum unified credit (nonresident aliens, see instructions)	7	211,300	00
8	Enter the unified credit against tax allowable for all prior periods (from Sch. B, line 1, col. C) . .	8		
9	Balance (subtract line 8 from line 7)	9		
10	Enter 20% (.20) of the amount allowed as a specific exemption for gifts made after September 8, 1976, and before January 1, 1977 (see instructions)	10		
11	Balance (subtract line 10 from line 9)	11		
12	Unified credit (enter the smaller of line 6 or line 11)	12		
13	Credit for foreign gift taxes (see instructions)	13		
14	Total credits (add lines 12 and 13)	14		
15	Balance (subtract line 14 from line 6) (do not enter less than zero)	15		
16	Generation-skipping transfer taxes (from Schedule C, Part 3, col. H, Total)	16		
17	Total tax (add lines 15 and 16)	17		
18	Gift and generation-skipping transfer taxes prepaid with extension of time to file	18		
19	If line 18 is less than line 17, enter BALANCE DUE (see instructions)	19		
20	If line 18 is greater than line 17, enter AMOUNT TO BE REFUNDED	20		

Attach check or money order here.

Under penalties of perjury, I declare that I have examined this return, including any accompanying schedules and statements, and to the best of my knowledge and belief it is true, correct, and complete. Declaration of preparer (other than donor) is based on all information of which preparer has any knowledge.

Donor's signature ▶ Date ▶

Preparer's signature (other than donor) ▶ Date ▶

Preparer's address (other than donor) ▶

For Paperwork Reduction Act Notice, see page 8 of the separate instructions for this form. Cat. No. 16783M Form **709** (1999)

Form 709 (1999) Page **2**

SCHEDULE A **Computation of Taxable Gifts** (Including Transfers in Trust)

A Does the value of any item listed on Schedule A reflect any valuation discount? If the answer is "Yes," see instructions . . Yes ☐ No ☐

B ☐ ◄ Check here if you elect under section 529(c)(2)(B) to treat any transfers made this year to a qualified state tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

Part 1—Gifts Subject Only to Gift Tax. *Gifts less political organization, medical, and educational exclusions—see instructions*

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was made by means of a trust, enter trust's identifying number and attach a copy of the trust instrument • If the gift was of securities, give CUSIP number	C Donor's adjusted basis of gift	D Date of gift	E Value at date of gift
1				

Total of Part 1 (add amounts from Part 1, column E) . . . . ►

Part 2—Gifts That are Direct Skips and are Subject to Both Gift Tax and Generation-Skipping Transfer Tax. You must list the gifts in chronological order. *Gifts less political organization, medical, and educational exclusions—see instructions. (Also list here direct skips that are subject only to the GST tax at this time as the result of the termination of an "estate tax inclusion period." See instructions.)*

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was made by means of a trust, enter trust's identifying number and attach a copy of the trust instrument • If the gift was of securities, give CUSIP number	C Donor's adjusted basis of gift	D Date of gift	E Value at date of gift
1				

Total of Part 2 (add amounts from Part 2, column E) . . . . ►

Part 3—Taxable Gift Reconciliation

1	Total value of gifts of donor (add totals from column E of Parts 1 and 2)	1	
2	One-half of items .... attributable to spouse (see instructions)	2	
3	Balance (subtract line 2 from line 1)	3	
4	Gifts of spouse to be included (from Schedule A, Part 3, line 2 of spouse's return—see instructions) . .	4	
	If any of the gifts included on this line are also subject to the generation-skipping transfer tax, check here ► ☐ and enter those gifts also on Schedule C, Part 1.		
5	Total gifts (add lines 3 and 4)	5	
6	Total annual exclusions for gifts listed on Schedule A (including line 4, above) (see instructions) . . .	6	
7	Total included amount of gifts (subtract line 6 from line 5)	7	

Deductions (see instructions)

8	Gifts of interests to spouse for which a marital deduction will be claimed, based on items .... of Schedule A	8			
9	Exclusions attributable to gifts on line 8	9			
10	Marital deduction—subtract line 9 from line 8	10			
11	Charitable deduction, based on items ....less exclusions . .	11			
12	Total deductions—add lines 10 and 11			12	
13	Subtract line 12 from line 7			13	
14	Generation-skipping transfer taxes payable with this Form 709 (from Schedule C, Part 3, col. H, Total) .			14	
15	Taxable gifts (add lines 13 and 14). Enter here and on line 1 of the Tax Computation on page 1 . . .			15	

(If more space is needed, attach additional sheets of same size.) Form **709** (1999)

Form 709 (1999) Page 3

SCHEDULE A Computation of Taxable Gifts *(continued)*

16 Terminable Interest (QTIP) Marital Deduction. (See instructions for line 8 of Schedule A.)

If a trust (or other property) meets the requirements of qualified terminable interest property under section 2523(f), and

a. The trust (or other property) is listed on Schedule A, and

b. The value of the trust (or other property) is entered in whole or in part as a deduction on line 8, Part 3 of Schedule A,

then the donor shall be deemed to have made an election to have such trust (or other property) treated as qualified terminable interest property under section 2523(f).

If less than the entire value of the trust (or other property) that the donor has included in Part 1 of Schedule A is entered as a deduction on line 8, the donor shall be considered to have made an election only as to a fraction of the trust (or other property). The numerator of this fraction is equal to the amount of the trust (or other property) deducted on line 10 of Part 3, Schedule A. The denominator is equal to the total value of the trust (or other property) listed in Part 1 of Schedule A.

If you make the QTIP election (see instructions for line 8 of Schedule A), the terminable interest property involved will be included in your spouse's gross estate upon his or her death (section 2044). If your spouse disposes (by gift or otherwise) of all or part of the qualifying life income interest, he or she will be considered to have made a transfer of the entire property that is subject to the gift tax (see Transfer of Certain Life Estates on page 3 of the instructions).

17 Election Out of QTIP Treatment of Annuities

☐ ◄ Check here if you elect under section 2523(f)(6) **NOT** to treat as qualified terminable interest property any joint and survivor annuities that are reported on Schedule A and would otherwise be treated as qualified terminable interest property under section 2523(f). (See instructions.)
Enter the item numbers (from Schedule A) for the annuities for which you are making this election ►

SCHEDULE B Gifts From Prior Periods

If you answered "Yes" on line 11a of page 1, Part 1, see the instructions for completing Schedule B. If you answered "No," skip to the Tax Computation on page 1 (or Schedule C, if applicable).

A Calendar year or calendar quarter (see instructions)	B Internal Revenue office where prior return was filed	C Amount of unified credit against gift tax for periods after December 31, 1976	D Amount of specific exemption for prior periods ending before January 1, 1977	E Amount of taxable gifts
1 Totals for prior periods (without adjustment for reduced specific exemption)	1			
2 Amount, if any, by which total specific exemption, line 1, column D, is more than $30,000			2	
3 Total amount of taxable gifts for prior periods (add amount, column E, line 1, and amount, if any, on line 2). (Enter here and on line 2 of the Tax Computation on page 1.)			3	

(If more space is needed, attach additional sheets of same size.)

Form **709** (1999)

Form 709 (1999) Page 4

SCHEDULE C Computation of Generation-Skipping Transfer Tax

Note: *Inter vivos direct skips that are completely excluded by the GST exemption must still be fully reported (including value and exemptions claimed) on Schedule C.*

Part 1—Generation-Skipping Transfers

A Item No. (from Schedule A, Part 2, col. A)	B Value (from Schedule A, Part 2, col. E)	C Split Gifts (enter ½ of col. B) (see instructions)	D Subtract col. C from col. B	E Nontaxable portion of transfer	F Net Transfer (subtract col. E from col. D)
1					
2					
3					
4					
5					
6					

If you elected gift splitting and your spouse was required to file a separate Form 709 (see the instructions for "Split Gifts"), you must enter all of the gifts shown on Schedule A, Part 2, of your spouse's Form 709 here. In column C, enter the item number of each gift in the order it appears in column A of your spouse's Schedule A, Part 2. We have preprinted the prefix "S-" to distinguish your spouse's item numbers from your own when you complete column A of Schedule C, Part 3. In column D, for each gift, enter the amount reported in column C, Schedule C, Part 1, of your spouse's Form 709.	Split gifts from spouse's Form 709 (enter item number)	Value included from spouse's Form 709	Nontaxable portion of transfer	Net transfer (subtract col. E from col. D)
	S-			
	S-			
	S-			
	S-			
	S-			
	S-			
	S-			
	S-			

Part 2—GST Exemption Reconciliation (Section 2631) and Section 2652(a)(3) Election

Check box ▶ ☐ if you are making a section 2652(a)(3) (special QTIP) election (see instructions)

Enter the item numbers (from Schedule A) of the gifts for which you are making this election ▶ ....

1	Maximum allowable exemption (see instructions)	1	
2	Total exemption used for periods before filing this return	2	
3	Exemption available for this return (subtract line 2 from line 1)	3	
4	Exemption claimed on this return (from Part 3, col. C total, below)	4	
5	Exemption allocated to transfers not shown on Part 3, below. **You must attach a Notice of Allocation.** (See instructions.)	5	
6	Add lines 4 and 5	6	
7	Exemption available for future transfers (subtract line 6 from line 3)	7	

Part 3—Tax Computation

A Item No. (from Schedule C, Part 1)	B Net transfer (from Schedule C, Part 1, col. F)	C GST Exemption Allocated	D Divide col. C by col. B	E Inclusion Ratio (subtract col. D from 1.000)	F Maximum Estate Tax Rate	G Applicable Rate (multiply col. E by col. F)	H Generation-Skipping Transfer Tax (multiply col. B by col. G)
1					55% (.55)		
2					55% (.55)		
3					55% (.55)		
4					55% (.55)		
5					55% (.55)		
6					55% (.55)		
					55% (.55)		
					55% (.55)		
					55% (.55)		
					55% (.55)		
Total exemption claimed. Enter here and on line 4, Part 2, above. May not exceed line 3, Part 2, above			**Total generation-skipping transfer tax.** Enter here, on line 14 of Schedule A, Part 3, and on line 16 of the Tax Computation on page 1				

(If more space is needed, attach additional sheets of same size.) Form **709** (1999)

Form **709-A**
(Rev. November 1999)
Department of the Treasury
Internal Revenue Service

United States Short Form Gift Tax Return

(For "Privacy Act" notice, see the Form 1040 instructions)

Calendar year ....

OMB No. 1545-0021

1 Donor's first name and middle initial	2 Donor's last name	3 **Donor's social security number**
4 Address (number, street, and apartment number)		5 Legal residence (domicile)
6 City, state, and ZIP code		7 Citizenship

8 Did you file any gift tax returns for prior periods? . . . . ☐ **Yes** ☐ **No**

If "Yes," state when and where earlier returns were filed ▶

9 Name of consenting spouse	10 **Consenting spouse's social security number**

Note: *Do not use this form to report gifts of closely held stock, partnership interests, fractional interests in real estate, or gifts for which the value has been reduced to reflect a valuation discount. Instead, use Form 709.*

List of Gifts

(a) Donee's name and address and description of gift	(b) Donor's adjusted basis of gift	(c) Date of gift	(d) Value at date of gift

Consent

I consent to have the gifts made by my spouse to third parties during the calendar year considered as made one-half by each of us.

Consenting spouse's signature ▶ **Date** ▶

Under penalties of perjury, I declare that I have examined this return, and to the best of my knowledge and belief it is true, correct, and complete. Declaration of preparer (other than donor) is based on all information of which preparer has any knowledge.

Donor's signature ▶ .... **Date** ▶ ....

Preparer's signature (other than donor's) ▶ .... **Date** ▶ ....

Preparer's address (other than donor's) ▶

For Paperwork Reduction Act Notice, see the instructions on the reverse side of this form. Cat. No. 10171G Form **709-A** (Rev. 11-99)

Form 709-A (Rev. 11-99) Page **2**

General Instructions

For Privacy Act notice, see the Form 1040 instructions.

Form 709-A is an annual short form gift tax return that certain married couples may use instead of **Form 709,** United States Gift (and Generation-Skipping Transfer) Tax Return, to report nontaxable gifts that they consent to split.

Who May File

Gifts to your spouse. For gifts to your spouse who is a U.S. citizen, you must only file a gift tax return to report certain gifts of terminable interests. For details on this and for filing rules for gifts to a spouse who is not a U.S. citizen, see the Instructions for Form 709.

Gifts to donee other than your spouse. You must file a gift tax return if you gave either of the following gifts to someone other than your spouse:

1. Gifts of future interests of any amount; or

2. Gifts of present interests of more than $10,000 (annual exclusion) to any one donee. The amount of the annual exclusion is indexed for inflation and is announced annually in a revenue procedure published by the IRS.

Exceptions. You do not have to file a gift tax return for any year in which the only gifts you made were for any of the following:

1. Gifts that were paid on behalf of an individual as tuition to an educational organization;

2. Gifts that were paid on behalf of an individual as payment for medical care to a provider of medical care; or

3. Gifts to charity if:

- The gifts were of your entire interest in the property,
- The entire transfer qualifies for the gift tax charitable deduction, and
- You have never previously transferred another interest in the property other than as a gift that qualified for the gift tax charitable deduction.

However, if you are required to file a return to report noncharitable gifts and you made gifts to charities, you must include all of your gifts to charities on the return.

You may use Form 709-A if you meet all of the following requirements:

1. You are a citizen or resident of the United States, and were married during the entire calendar year to one individual who is also a citizen or resident of the United States. Both you and your spouse were alive at the end of the calendar year.

2. Your only gifts (other than qualifying gifts for tuition or medical care) to a third party consisted entirely of present interests in tangible personal property, cash, U.S. Savings Bonds, or stocks and bonds listed on a stock exchange. A "third-party donee" is any donee other than your spouse.

3. Your gifts to any one third-party donee (other than qualifying gifts for tuition or medical care) during the calendar year did not total more than $20,000. If the donee is a charity, no part of that gift may be given to a noncharitable donee.

4. During the calendar year, you did not make any gifts of terminable interests to your spouse.

5. During the calendar year, your spouse did not make any gifts to any of the donees listed on this form, did not make gifts of terminable interests to you, did not make gifts (other than qualifying gifts for tuition or medical care) of over $10,000 to any other donee, and did not make any gifts of future interests to any other donee.

6. You and your spouse agree to split all of the gifts either of you made during the calendar year.

7. You did not file a Form 709 for this calendar year.

If you meet all seven requirements above, you may also use Form 709-A to report gifts made under the Uniform Gifts to Minors Act.

Note: *Gifts include transfers of property when no money changes hands and also transfers when some payment was made, but the payment made was less than the value of the item transferred.*

When To File

Form 709-A is a calendar-year return to be filed on or after January 1 but not later than April 15 of the year following the year when the nontaxable split gifts were made.

If the due date falls on a Saturday, Sunday, or legal holiday, file on the next business day.

Any extension of time granted to file your calendar year income tax return will also extend the time to file Form 709-A. Income tax extensions are made using Forms 4868, 2688, or 2350. See Form 4868 to get an automatic 4-month extension by phone. If you received an extension, attach a copy of it to Form 709-A.

You may not file Form 709-A later than April 15 (or the extension due date). Instead, you must file Form 709.

Where To File

File Form 709-A with the Internal Revenue Service Center where you would file your Federal income tax return. See the Form 1040 instructions for a list of filing locations.

Additional Help

The Instructions for Form 709 contain further information on the gift tax, including information about the following matters:

1. Annual exclusion.

2. Present and future interest.

3. Fair market value.

4. Adjusted basis. See **Pub. 551,** Basis of Assets, and the instructions for Schedule D (Form 1040).

5. Extension of time to file.

6. Terminable interest.

7. Gifts for tuition or medical care.

Specific Instructions

Column (a). List the names and addresses of all third party donees to whom you made gifts (other than qualifying gifts for tuition or medical care) totaling more than $10,000 during the calendar year. Do not list the names of donees to whom you gave only qualifying gifts for tuition, medical care, or to whom you gave gifts of present interests of $10,000 or less.

Describe the gifts in enough detail so they may be easily identified.

If you list **bonds,** include in your description:

- The number of bonds transferred;
- The principal amount of the bonds;
- The name of the obligor;
- The date of maturity of the bonds;
- The rate of interest;
- The date or dates on which interest is payable;
- The series number (if there is more than one issue);
- The exchange where the bond is listed; and
- The CUSIP number. The CUSIP number is a nine-digit number assigned by the American Banking Association to traded securities.

If you list **stocks,** you should include:

- The number of shares transferred;
- Whether the stocks are common or preferred. (If the stocks are preferred, list the issue and par value.);
- Exact name of corporation;
- Principal exchange where the stocks are sold; and
- The CUSIP number (see "bonds" above).

If you list **tangible personal property** (such as a car), describe the property in enough detail so that its fair market value (FMV) can be accurately figured.

Column (b). Show the basis you would use for income tax purposes if you sold or exchanged the property.

Column (d). If you make the gift in property other than money, determine the FMV as of the date the gift was made.

Consent

Your spouse must consent to split all gifts made by either of you. Your spouse gives this consent by signing in the space provided. You give your consent by signing in the space for the donor's signature. The guardian of a legally incompetent spouse may sign the consent. The executor for a deceased spouse may sign the consent if the spouse died after the close of the calendar year. Although a properly filed Form 709-A will not result in any gift tax liability, you should know that if you and your spouse consent to split gifts, either or both of you will be liable in the event any gift tax is later determined to be due.

Signature

You, as a donor, must sign the return. If you pay another person, firm, or corporation to prepare your return, that person must also sign the return as preparer unless he or she is your regular, full-time employee.

Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

Recordkeeping	13 min.
Learning about the law or the form	11 min.
Preparing the form	14 min.
Copying, assembling, and sending the form to the IRS	20 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **DO NOT** send the tax form to this office. Instead, see **Where To File** on this page.

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