YourOnlineProfessor.net

The Preparation of Form 8939: Allocation of Increase in Basis for Property Acquired from a Decedent

By
Edward L. Perkins, JD, LLM, CPA

FIELD OF STUDY - Taxation
PROGRAM LEVEL - Basic
PREREQUISITE - None
ADVANCE PREPARATION REQUIRED – None

YourOnlineProfessor.net
Keep Growing & Learning

The Preparation of Form 8939

Allocation of Increase in Basis for Property Acquired from a Decedent

PART I – Background and Rules of Increase in Basis Allocation

I. Purpose of Form

Form 8939 is an information return used by the executor (defined below) of a decedent who died in 2010:

1. To make the Section 1022 Election;[1]

2. To report information about property acquired from a decedent; and

3. To allocate the Basis Increase allowable under Section 1022, to certain property acquired from a decedent.

II. The Section 1022 Election

A. General

The executor of an estate of a decedent who died in 2010 can elect to apply modified carryover basis treatment to property acquired from the decedent under section 301(c) of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "Tax Relief Act").

B. Effect of Election

If the election is made, the estate will not be subject to federal estate tax and does not need to file a Form 706 even if the value of the estate is $5,000,000 or more. As a result, section 1014 generally does not apply to determine the recipient's basis in property acquired from the decedent[2]. Instead, section 1022 applies to determine the recipient's basis in most (but not all) property acquired from the decedent. This election is referred to as the "Section 1022 Election".

C. How to Make the Section 1022 Election

---

[1] Hereinafter, all code sections refer to the I.R.C. and corresponding Treasury Regulations unless indicated otherwise.

[2] § 1014 generally provides for a "step up" in basis to fair market value at the date of death for assets acquired from a decedent at the time of their death.

The Section 1022 Election is made by timely filing a Form 8939.[3] The IRS has now announced the due date on January 17, 2012. If prior filings have been made purporting to make the Section 1022 Election, that filing must be replaced with a timely filed Form 8939. If there is an executor appointed, qualified, and acting within the United States, the IRS generally will accept Form 8939 only if filed by that executor.[4]

D. Section 1022 Election Irrevocable

A Section 1022 Election cannot be revoked after the due date. Generally, once the executor has made the Section 1022 Election, the election is irrevocable. However, the executor can revoke a prior Section 1022 Election on a subsequent Form 8939 filed before the due date. To revoke the Section 1022 Election, the executor must check the box at the top of Form 8939 designated for revocation. If the executor files an amended Form 8939 that revokes a Section 1022 Election, the executor should write "Section 1022 Election Revoked" at the top of the updated statement and send a copy to each affected recipient.

E. Statute of Limitations

The IRS may contest the basis of a particular property (including the amount of basis increase allocated to the property) with respect to any tax return reporting a value dependent on the property's basis (such as depreciation, or gain of loss recognition on a sale or disposition of the asset).

F. Safe Harbor Rules

The IRS has issued Rev. Proc. 2011-41 which provides safe harbor guidance under Section 1022. If the executor makes the Section 1022 Election and follows the provisions of section 4 of Revenue Procedure 2011-41, and takes no return position contrary to any provisions of section 4, the IRS will not challenge the taxpayer's ability to rely on the provisions of section 4 on either Form 8939 or any other return of tax.[5]

III. Required Disclosure

A. Returns by Executors

---

[3] See Section V.A. below as to When to File.

[4] See Section XV.A. below for a discussion of who is the "Executor" of the estate.

[5] This is an interesting statement since the only actual "safe harbor" referenced in the Rev. Proc is that a revocable trust and trust estates that would be includible in the gross estate under Secs. 2036, 2037, and 2039, qualify for the special rule that gain recognition which can result from the funding of a pecuniary gift only results from post- death appreciation. Rev. Proc. 2011-41, is attached hereto as Appendix A.

Generally, if the executor of the estate makes the Section 1022 Election, the executor *must* report all the information required by Form 8939 and its instructions about:

1. All property acquired from the decedent (other than cash or Income in Respect to a Decedent);[6]

2. Gifts to the decedent within the last three years (other than gifts from the decedent's spouse unless the spouse also had acquired the property by gift within that three year period);

3. For nonresident aliens, any property "acquired from the decedent" that passes to a US person, as well as tangible property located in the US that passes to others.[7]

B. Returns by Trustees and Beneficiaries

If the executor is unable to make a complete return as to any property acquired from the decedent, the executor must include a description of such property and the name of every person holding a legal or beneficial interest in the property. Upon notice from the IRS, such person must file Form 8939 as to such property.

IV. Statement to Recipients

A. Initial Statement

The executor filing Form 8939 must also furnish to each person whose name is required to be set forth in such return (other than the executor filing the return) a written statement showing the information required by section 6018(e) with respect to property acquired from the decedent to the person required to receive the statement. The information specified in that section with respect to any property acquired from the decedent is:

1. The name and TIN of the recipient of such property,
2. An accurate description of such property,

---

[6] This includes non-probate assets.

[7] However, for the executor of a decedent who is a nonresident, nor a citizen of the United States, the executor must report certain information about the property if there is an executor appointed, qualified, and acting within the United States, the IRS generally will accept Form 8939 only if filed by that executor

3. The adjusted basis of such property in the hands of the decedent and its fair market value at the time of death,

4. The decedent's holding period for such property,

5. Sufficient information to determine whether any gain on the sale of the property would be treated as ordinary income,

6. The amount of basis increase allocated to the property under subsection (b) or (c) of section 1022; and

7. Such other information as the Secretary may require.

The executor must furnish this statement not later than 30 days after the date Form 8939 is filed. The statement must include information about all property acquired from the decedent by the recipient of the statement, whether or not the executor allocates any Basis Increase to that property.

Schedule A of Form 8939 is used to provide this information to each recipient of property acquired from the decedent, including the following persons: (i) the decedent's surviving spouse; (ii) the trustee of a qualified terminable interest property (QTIP) trust; (iii) any charitable remainder trust the sole non-charitable beneficiary of which is the decedent's surviving spouse; and, (iv) any other person (other than the executor filing the return) who acquires property from the decedent.

B. Updated Statements.

1. Requirement

The executor must furnish an updated statement in the following circumstances: (i) the executor files an amended or supplemental Form 8939; and, (ii) the IRS makes an adjustment to any tax return that affects the amounts properly reportable on Form 8939.

2. Timing

The executor must furnish updated statements to each affected recipient of property no later than 30 days after the executor's filing of the amended or supplemental Form 8939 or receiving notice of the adjustment from the IRS, whichever is applicable. If the property is subject to multiple interests (life estate and remainder interest), the life tenant and all holders of remainder interests are affected recipients of the property.

V. Filing Rules

A. When to File

1. Due Date

The due date for filing Form 8939 is January 17, 2012. Generally, the IRS will not grant extensions of time to file a Form 8939 and will not accept a Form 8939 or an amended Form 8939 filed after the due date. An executor is not permitted to file both an estate tax return (Form 706 or Form 706-NA) and a conditional Form 8939 that would take effect only if an estate tax audit results in an increase in the gross estate above the applicable exclusion amount in Section 2010(c).

2. Prior Filing

A Form 8939 filed prior to January 17, 2012, may be amended or revoked, but only by a subsequent Form 8939 filed on or before that date. The Form 8939 that is timely filed by an executor is the last Form 8939 filed by that executor on or before January 17, 2012. No executor's Form 8939 will have any effect on any Form 8939 filed by a different executor.

3. Extensions of Time to File

The IRS will generally not grant extensions of time to file a Form 8939 and will not accept a Form 8939 or an amended Form 8939 filed after the due date.[8]

4. Limited Extensions Allowed

For individuals serving in the Armed Forces of the United States the deadline for filing Form 8939, can be extended under Section 7508. Pursuant to Section 7508, military personnel serving in designated combat zones are entitled to an extended deadline for payment, filing, and other tax matters. Under Section 7508A, the deadline to file Form 8939 can also be postponed for a taxpayer affected by a Presidentially declared disaster, terroristic, or military action. Any executor filing a Form 8939 after January 17, 2012, pursuant to section 7508 or 7508A should write "Filed Pursuant to Section 7508" or "Filed Pursuant to Section 7508A", as applicable, on the top of the form. The failure to write these notations at the top of the Form 8939, however, will not adversely impact the extension granted under section 7508 or 7508A.

5. Private Delivery Services.

[8] But see Section VI (regarding relief provisions), and Section XV.B. below (regarding multiple filings).

The executor may use certain private delivery services designated by the IRS to meet the "timely mailing as timely filing" rule for tax returns. These private delivery services include only the following: (i) DHL Express (DHL): DHL Same Day Service; (ii) Federal Express (FedEx): FedEx Priority Overnight, FedEx Standard Overnight, FedEx 2Day, FedEx International Priority, FedEx International First; and, (iii) United Parcel Service (UPS): UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, UPS 2nd Day Air A.M., UPS Worldwide Express Plus, and UPS Worldwide Express. The private delivery service can tell you how to get written proof of the mailing date.

B. Who Must Sign

The executor who files the return must, in every case, sign the declaration on page 1 of Form 8939 under penalties of perjury.

C. No Protective Elections

Notice 2011-66 provides that a taxpayer may not file an estate tax return as well as a conditional Form 8939 that would take effect only if the estate tax audit results in an increase in the gross estate above the applicable exclusion amount.

D. Where to File

The Form should be filed at the following address: Internal Revenue Service Estate & Gift Stop 824G, 201 W. Rivercenter Blvd., Covington, KY 41011. The Form 8939 should not be filed with the decedent's final income tax return.

E. Miscellaneous

1. Rounding Off to Whole Dollars

In preparing the Form 8939, the Instructions advise that money items on the return and accompanying schedules should be shown as whole-dollar amounts. In rounding, the Instructions provide further that any amount less than 50 cents should be dropped, and any amount from 50 cents through 99 cents should be increased to the next higher dollar.

2. Required Attachments

The Instructions to Form 8939 require that following items be attached to the return: (i) the decedent's death certificate; (ii) if the decedent died testate, a certified copy of the will[9]; (iii) copies of trust

[9] If a certified copy of the will cannot be obtained, attach a copy of the will and an explanation of why it is not certified.

instruments for any trust that is shown on the return as a recipient of property acquired from the decedent; (iv) if the executor is appointed, a certified copy of the letters testamentary, letters of administration, or other similar evidence of the executor's authority to act; and, (v) appraisals used to value certain property "required under section 2031".[10]

VI. Relief Provisions

A. Limited Amendment Circumstances

There are only a few limited circumstances pursuant to which the IRS will accept an amended Form 8939.[11]

1. Allocating Spousal Property Basis Increase

First, an amended Form 8939 may be filed after the due date for the sole purpose of allocating the "Spousal Property Basis Increase"[12] among the property eligible to receive an allocation of that basis increase, provided that each of the following two requirements are satisfied: (i) the Form 8939 must have been timely filed and was complete when filed except for the allocation of the full amount of the Spousal Property Basis Increase to the eligible property reported on that Form 8939; and (ii) the amended Form 8939 must be filed no more than 90 days after the date of the distribution of the qualified spousal property to which Spousal Property Basis Increase is allocated on that amended Form 8939.

2. Section 301.9100-2(b)

Second, an amended Form 8939 may be filed, provided an executor timely filed a Form 8939, and the executor may file an amended Form 8939 under the provisions of Section 301.9100-2(b) on or before May 15, 2012, for any purpose except to make or revoke a Section 1022 Election. The executor must write "Filed Pursuant to Section 301.9100-2" on the top of the amended Form 8939.

---

[10] Sec. 2031 does not require appraisals be obtained to value property reported on Form 706. The instructions to Form 706 do not require appraisals but do require they be attached that are used to value property reported on the return. It is generally a good idea to obtain appraisals of assets with significant value which are not readily traded in an established market, e.g., real estate, interest in closely held businesses, and collectibles.

[11] See IRS Notice 2011-66 attached.

[12] See Section XIV, below, for a discussion of the Spousal Property Basis Increase.

Generally, Section 301.9100-2, provides an automatic extension of 12 months from the due date for making a regulatory election provided the taxpayer takes "corrective action", as defined below, within that 12-month extension period. If Section 301.9100-2 applies, the due date for making a regulatory election is, either (i) the extended due date of the return if the due date of the election is the due date of the return, or, (ii) the due date of the return including extensions and the taxpayer has obtained an extension of time to file the return. This extension is available regardless of whether the taxpayer timely filed its return for the year the election should have been made.

In the case of the Form 8939, the extension is only until May 15, 2012, and the section 1022 Election, "corrective action," would include filing an original or an amended Form 8939 attaching the appropriate form or statement for making the election.

3. Section 301.9100-3 Relief

a. General Rule

As a general rule, section 301.9100-3 of the Regulations provides that requests for extensions of time for regulatory elections that are not otherwise considered filed on a timely basis may be granted when the taxpayer provides evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Government.

In general, a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer: (i) requests relief under section 301.9100-3 before the failure to make the regulatory election is discovered by the IRS; (ii) failed to make the election because of intervening events beyond the taxpayer's control; (iii) failed to make the election because, after exercising reasonable diligence (taking into account the taxpayer's experience and the complexity of the return or issue), the taxpayer was unaware of the necessity for the election; (iv) reasonably relied on the written advice of the IRS; or (v) reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

b. Supplementing a Filed Form 8939

Next, an executor may apply for relief in order *to supplement a timely filed Form 8939* under § 301.9100-3. A request for relief to supplement a timely filed Form 8939 is limited to an extension of time to allocate any Basis Increase that has not previously been validly allocated, and such relief, if appropriate, will be granted only if: (i) after filing the Form 8939, the executor discovers additional property to which remaining Basis Increase could be allocated; and/or (ii) the fair market value of property reported on the Form 8939 is adjusted as the result of an IRS examination or inquiry. Relief will not be granted to reduce an allocation of Basis Increase made on a timely filed Form 8939.

c. Extension of Time in Which to File Form 8939

Finally, an executor may apply for relief under section 301.9100-3 *in the form of an extension of the time* in which to file the Form 8939 (thus, making the Section 1022 Election and the allocation of Basis Increase), which relief may be granted if the requirements of section 301.9100-3 are satisfied.

In this context, the amount of time that has elapsed since the decedent's death may constitute a lack of reasonableness and good faith and/or prejudice to the interests of the government (for example, the use of hindsight to achieve a more favorable tax result and/or the lack of records available to establish what property was or was not owned by the decedent at death), which would prevent the grant of the requested relief.

VII. Penalties

Section 6716 provides penalties for failing to file the Form 8939 on time and for failing to provide the information required unless there is reasonable cause for the failure. Generally, the penalty is $10,000 for each such failure to file on a timely basis. The penalty for failure to provide the information required by Section 6018(b)(2) is $500 for each failure. The penalty for failure to provide recipients of property acquired from the decedent the information required by Section 6018(e) is $50 for each such failure. If any failure is due to intentional disregard of the requirements of Section 6018, the penalty is 5 percent of the FMV (as of the date of death) of the property about which the information is required.

VIII. Reporting Requirements

A. Property to be Reported

If the executor makes the Section 1022 Election, the executor must report and value on Form 8939 all property (excluding cash and property that constitutes the right to receive an item of income in respect of a decedent under Section 691 ("IRD") acquired from the decedent.

B. Appreciated Property Acquired From the Decedent

In addition, the executor also must report all appreciated property acquired from the decedent, valued as of the decedent's date of death, that was required to be included on the donor's Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return, if such property was acquired by the decedent by gift or by inter vivos transfer for less than adequate and full consideration in money or money's worth during the 3-year period ending on the date of the decedent's death. This does not include property transferred to the decedent by the decedent's spouse, who had not acquired the property in whole or in part by gift or by inter vivos transfer for less than adequate and full consideration in money or money's worth during that same 3-year period.[13]

C. Non Resident Alien Property Limited

In the case of a deceased nonresident who is not a citizen of the United States, the property to be reported is limited to tangible property situated in the United States that is acquired from the decedent and any other property acquired from the decedent by a United States person.

X. Property Eligible for Increase to Basis

A. In General

Generally, the executor can allocate additional basis under Section 1022, up to the fair market value of the property to property that was both: (i) owned by the decedent at the time of death; and, (ii) acquired from the decedent. Property, the basis of which can be increased, is termed "eligible property".

B. Property Owned by the Decedent at the Time of Death

The basis of property acquired from the decedent can be increased by an allocation of Basis Increase (defined in Section XII.D., Basis Increase, later) only if and to the extent the property was owned by the decedent at the time of death.

[13] See Section XI.B., for a discussion of this rule.

Not all property acquired from the decedent is considered owned by decedent at the time of death. The following rules apply in determining whether property was owned by the decedent at the time of death.

1. Jointly held Property.

If property was owned by the decedent and one or more other persons (either as joint tenants with right of survivorship or tenants by the entirety), the following rules apply:

a. if the only other person with whom the decedent owned the property is the decedent's surviving spouse, the decedent is treated as owning 50% of the property;

b. if any other person with whom the decedent owned the property is not the decedent's surviving spouse and if the decedent furnished consideration for the acquisition of the property, the decedent is treated as the owner to the extent of the portion of the property that is proportionate to the consideration furnished by the decedent; and

c. if any other person with whom the decedent owned the property is not the decedent's surviving spouse and if the property was acquired by gift, bequest, devise or inheritance by the decedent and the other person as joint tenants with right of survivorship and their interests are not otherwise specified or fixed by law, the decedent is treated as owning a fractional part of the property. The fractional part of the property that the decedent is treated as owning is determined by dividing the value of the property by the number of joint tenants with right of survivorship.

2. Revocable Trusts.

a. General Rule

The decedent is treated as the owner of any property that the decedent transferred to a "qualified revocable trust" ("QRT") during his or her lifetime. A QRT is any trust (or part of a trust) that, on the day the decedent died, was treated as owned by the decedent under section 676 by reason of a power to revoke that was exercisable by

the decedent (determined without regard to Section 672(e)).[14] For this purpose, a QRT includes a trust that was treated as owned by the decedent under Section 676 by reason of a power to revoke that was exercisable by the decedent with the consent or approval of a non adverse party or the decedent's spouse. However, a QRT does not include a trust that was treated as owned by the decedent under Section 676 by reason of a power to revoke that was exercisable solely by a nonadverse party or the decedent's spouse and not by the decedent.[15]

Restated in terms of federal estate tax inclusion: property held by a trust which includable in the decedent's estate by reason of sec. 2036(a)(2), or sec. 2038, is considered property acquired from the decedent and eligible for basis increase under Sec. 1022, however trust property which is which includable in the decedent's estate by reason of sec. 2036(a)(1), is not.

Sec. 2036(a)(2) requires inclusion in the decedent's taxable estate when property is subject *to "the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom."* Sec. 2038, requires inclusion if the decedent held the power to *"alter, amend, revoke, or terminate, or where any such power is relinquished during the 3-year period ending on the date of the decedent's death."* Sec. 2036(a)(1), on the other hand, requires inclusion if the decedent held *"possession or enjoyment of, or the right to the income from, the property."*

The distinction seems to lie in the under sec. 2036(a)(2), and sec. 2038, there is an element of control over the property, which results in the assumption that such property is in a sense "acquired

[14] § 672(e) provides that a grantor shall be treated as holding any power or interest held by--
"(A) any individual who was the spouse of the grantor at the time of the creation of such power or interest, or (B) any individual who became the spouse of the grantor after the creation of such power or interest, but only with respect to periods after such individual became the spouse of the grantor."

[15] For more information, see §§ 645(b) and 676, and the instructions for Form 8885, Election To Treat a Qualified Revocable Trust as Part of an Estate. No election is required for a trust to be a QRT.

form the decedent", whereas the retention of the *"possession or enjoyment of, or the right to the income from, the property" does not.*

However if the property includible in the gross estate 2036(a)(1), also provides for a reversionary interest to the decedent's estate it will be considered owned by the decedent at the time of death.

b. Examples

Example 1 - On August 1, 2006, decedent (D) created a qualified personal residence trust (QPRT) pursuant to Section 25.2702-5(c). The term of the QPRT expires on July 31, 2011. The QPRT instrument provided that, if D dies prior to July 31, 2011, the property in the QPRT is to be distributed to D's child (C). D died in 2010, and D's executor made the Section 1022 Election. In this case, the property in the trust had been transferred to the trust by D during D's lifetime. The QPRT is not a qualified revocable trust as defined in Section 645(b)(1) nor is it a trust over which the decedent reserved the right to make any change in the enjoyment thereof through the exercise of a power to alter, amend, or terminate the trust. The property that passes to C under the QPRT instrument by reason of D's death is not considered to have been acquired from D and thus, section 1022 is not applicable to determine C's basis in the property held in the QPRT. Instead, C's basis in this property is determined under other applicable sections of the Code.

Example 2 - Assume the same facts as in Example 1, except that the QPRT instrument provided that, if D dies prior to July 31, 2011, the QPRT terminates and the property in the QPRT is to be distributed to D's estate. Because the trust property becomes the property of D's estate at D's death, the trust property is considered to have been acquired from D under Section 1022(e)(1). For the same reason, the property is also considered owned by D and, therefore, Basis Increase may be allocated to this trust property.

3. Powers of Appointment.

The decedent is not treated as the owner of any property by virtue of holding a power of appointment with respect to such property.

4. Community Property

Property that represents the decedent's surviving spouse's one-half share of the community property held by the decedent and his or her surviving spouse will be treated as owned by (and acquired from) the decedent if at least one-half of the whole of the community interest in such property is treated as owned by (and acquired from) the decedent under

the community property laws of the state (or possession of the United States or any foreign country) that apply to the decedent.

C. Property Acquired from the Decedent

1. General Rule

In order to be considered eligible property, the property must be "acquired from the decedent." Generally, property acquired from the decedent includes the following: (i) property acquired by bequest, devise, or inheritance, or by the decedent's estate from the decedent; (ii) property transferred by the decedent during the decedent's lifetime to (A) a qualified revocable trust (as defined in section 645(b)(1)),[16] or (B) any other trust with respect to which the decedent reserved the right to make any change in the enjoyment thereof through the exercise of a power to alter, amend, or terminate the trust; or (iii) any other property passing from the decedent by reason of death to the extent that such property passed without consideration. **2. Other Property**

In addition, the term includes any other property that passes from the decedent by reason of death to the extent that such property passes without consideration, such as: (i) any property transferred at the decedent's death by reason of the decedent's holding and/or exercising a general power of appointment (as defined in Section 2041) with respect to such property if that power was not created by the decedent; (ii) property held by the decedent and another person as joint tenants with right of survivorship or as tenants by the entirety; and, (iii) the surviving spouse's one-half interest in community property.[17]

XI. Property Not Eligible for Increase to Basis

A. General Rule

Only property owned by and acquired from the decedent is eligible for allocation of Basis Increase.[18] Certain other property as discussed in the following subsections is considered ineligible property. For these types of assets*. "the recipient's basis in property that is not subject to section 1022 is determined under*

[16] § 645 allows the executor of an estate and the trustee of certain revocable trusts to be treated as part of the estate.

[17] As discussed in section X.B.4., above. See also Rev. Proc. 2011-41.

[18] See Sec. X.B.

other applicable sections of the Code."[19] As a result the basis would be carryover basis, i.e., the basis of the asset would be retained without step up or step down.

B. Cash and Acquired Property

The executor cannot allocate Basis Increase to: (i) cash, whether acquired from the decedent, in exchange for property acquired from the decedent, or otherwise; or (ii) to property or proceeds acquired after the decedent's death in exchange for property acquired from the decedent. The basis of this property is determined under other applicable rules for determining basis.

C. Property Acquired by the Decedent by Gift Within 3 Years of Death

Generally, property that the decedent acquired by gift or lifetime transfer for less than adequate and full consideration in money or money's worth during the 3-year period ending on the date of the decedent's death is not eligible for a basis increase. However, property acquired by the decedent from the decedent's spouse during such 3-year period will generally be eligible for a basis increase, unless, during the 3-year period, the decedent's spouse acquired the property in whole or in part by gift or lifetime transfer for less than adequate and full consideration in money or money's worth.

D. Stock or Securities of Certain Entities

The decedent's interest in the following types of property is not eligible for an increase in basis: (i) stock or securities of a foreign personal holding company; (ii) stock of a domestic international sales corporation (DISC) or former DISC; (iii) Stock of a foreign investment company; or (iv) Stock of a passive foreign investment company unless such company is a qualified electing fund (as defined in section 1295) with respect to the decedent.

E. Income in Respect of a Decedent

1. General Rule

Section 1022 does not apply to property that constitutes a right to receive an item of income in respect of a decedent ("IRD") under Section 691. The executor is not required to list property that constitutes a right to receive an item of IRD on Form 8939. Generally, IRD is income that the decedent would have received had death not occurred and that was not properly includible on the decedent's final income tax return.

[19] See Rev. Proc. 2011-41, section 4.01(2).

2. Definition

IRD includes the following: (i) an installment obligation, reportable by the decedent on the installment method, that remains uncollected by the decedent: (ii) accrued but unpaid interest on a note, certificate of deposit, or other obligation; and, (iii) dividends declared on a share of stock before the decedent's death but payable to shareholders of record on a date after the decedent's death.

3. Treatment of IRD

The right to receive an amount of IRD must be treated in the hands of the estate, or by the person entitled to receive that amount by bequest, devise, or inheritance from the decedent, or by reason of the decedent's death, as if it had been acquired in the same transaction as the decedent acquired that right, and must be considered as having the same character it would have had if the decedent had lived and received that amount.[20]

Example: Installment Obligation. Decedent Tammy died in 2010 and her executor, Vince, timely makes the Section 1022 Election. Whitney, an heir of Tammy's estate, is entitled to collect an installment obligation, reported by Tammy on the installment method, that has a face value of $100, FMV of $80, and a basis in Tammy's hands on the date of her death of $60. Section 1022 does not apply to the installment obligation and does not determine the estate's basis or Whitney's basis in the installment obligation.

F. QTIP Property

Property held in QTIP trust for the benefit of the decedent which is constructively included in the decedent's estate by reason of Sec. 2041, is not considered property "acquired from the decedent." As a result Section 1022 does not apply to a decedent's interest in a QTIP trust or similar arrangement funded for the benefit of the decedent by the decedent's predeceased spouse, and a recipient's basis in this property will not be determined under section 1022.

XII. Amount of Increase to Basis

A. Allocation Rules

1. FMV Limitation

[20] For more information, see Regulations § 1.691(a)-3.

The executor can allocate General Basis Increase[21] and/or Spousal Property Basis Increase[22] to eligible property[23] but not in excess of the amount needed to increase the decedent's adjusted basis to the property's FMV as of the date of the decedent's death. The result is that, for each property, the sum of the decedent's adjusted basis in that property and the Basis Increase allocated to that property cannot exceed the FMV of that property on the decedent's date of death.

2. Asset Allocation

The executor can allocate Basis Increase[24] to property owned by and acquired from the decedent on a property-by-property basis. For example, the executor can allocate Basis Increase to one or more shares of stock or to a particular block of stock rather than to the decedent's entire holding of that stock. Basis Increase may not be allocated separately to a life estate and remainder interest in the same property.

B. Decedent's Adjusted Basis

1. General Rule

Generally, the adjusted basis of the property in the hands of the decedent as of the date of the decedent's death is the decedent's cost or other basis, adjusted as provided for under applicable provisions of Internal Revenue Code.

2. Property Acquired by Gift

If the decedent acquired property by gift, the decedent's adjusted basis at death is the decedent's basis determined under Section 1015, adjusted as required under applicable provisions of Internal Revenue laws. The decedent's original basis under Section 1015 is the same as it would be in the hands of the donor or the last preceding owner by whom it was not acquired by gift, except that if such basis (adjusted for the period before the date of the gift as provided in Section 1016) is greater than the FMV of the property at the time of the gift, then for the purpose of determining loss the basis shall be such FMV.

C. Fair Market Value ("FMV")

---

[21] Defined in Section XIII, General Basis Increase, infra.
[22] Defined in Section XIV, Spousal Property Basis Increase, infra.
[23] Defined in Section X.A. supra.
[24] Defined in Section XII.D., Basis Increase, infra.

Generally, for purposes of Section 1022, the "fair market value" of the property is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts.

D. Basis Increase

The aggregate "Basis Increase" is the sum of the "General Basis Increase" and the "Spousal Property Basis Increase".

XIII. The General Basis Increase

A. Overview

The "General Basis Increase" is the sum of the "Aggregate Basis Increase" and the "Carryovers/Unrealized Losses Increase". However, for a decedent who was neither a resident nor citizen of the United States, the General Basis Increase is limited to the Aggregate Basis Increase (limited as described below).

B. Aggregate Basis Increase

The Aggregate Basis Increase is $1,300,000. However, for a decedent who was neither a resident nor citizen of the United States, the Aggregate Basis Increase is $60,000.

C. Carryovers/Unrealized Losses Increase

The Carryovers/Unrealized Losses Increase is the sum of the following three items:

1. The amount of any capital loss carryovers under section 1212(b) that would (but for the decedent's death) be carried from the decedent's last taxable year to a later tax year;

2. The amount of any net operating loss ("NOL") carryovers under section 172 that would, but for the decedent's death, be carried from the decedent's last taxable year to a later tax year; and,

3. The amount of any losses that would be allowable under section 165 if the property acquired from the decedent had been sold at FMV immediately before the decedent's death ("unrealized losses").

Note. The amount of any losses that would be allowable under section 165 is determined based on a hypothetical sale and does not require an actual sale of property. For any decedent who was neither a citizen nor resident of the United States the amount of the Carryovers/Unrealized Losses Increase is zero.

D. Capital Loss

The capital loss carryforward included in the Carryovers/Unrealized Losses Increase is the amount of any capital loss carryforward that would, but for the decedent's death, be carried to a tax year of the decedent after the decedent's last tax year. Generally, you can figure the decedent's capital loss carryforward using the Capital Loss Carryover Worksheet in the Instructions to Schedule D (Form 1040). Existing income tax rules will apply to determine the decedent's share of a capital loss carryforward under Section 1212(b) if the decedent's final Form 1040 is filed jointly with the decedent's surviving spouse.[25]

E. Net Operating Loss (NOL).

The Net Operating Loss (the "NOL") carryovers under Section 172 included in Carryovers/Unrealized Losses Increase are the losses that would (but for the decedent's death) carry forward to tax years after the decedent's last tax year. An NOL arising in the decedent's final tax year must be carried back and used in the applicable 2-year, 3-year, 5-year, or 10-year carryback period unless the carryback period is waived on the decedent's final income tax return by attaching a statement showing that the carryback period is waived. Existing income tax rules will apply to determine the decedent's share of the NOL carryovers under Section 172 if the decedent's final Form 1040 is filed jointly with the decedent's surviving spouse.[26]

F. Unrealized Losses

1. The Amount of the Unrealized Losses

The amount of unrealized losses included in the Carryovers/Unrealized Losses Increase is the amount that would have been allowable as a deduction under Section 165 if the property acquired from the decedent had been sold at FMV immediately before the death of the decedent. The amount of losses that would have been allowable as a deduction under Section 165 is limited to losses incurred in a trade or business and losses incurred in any transaction entered into for profit, though not connected with a trade or business.

2. Certain Limitations

[25] For rules about a capital loss carry forward arising from community property, see sections 4.05 and 4.06(4) of Rev. Proc. 2011-41.

[26] For rules about NOL carryovers arising from community property, see sections 4.05 and 4.06(4) of Rev. Proc. 2011-41.

Certain limitations on the allowance of losses may apply. For example, no deduction is allowable for a loss sustained on any registration-required obligation not in registered form.[27] Figure the unrealized losses that can be included in the General Basis Increase without regard to the limitation in Section 165(f) on the allowance of losses from the sale or exchange of capital assets. The amount of any loss that would have been allowable under Section 165 if the property acquired from the decedent had been sold at FMV immediately before the decedent's death is determined without the dollar limitations on capital losses under Section 1211. [28]

Example: D owned 100 shares of stock that D held for profit within the meaning of section 165(c)(2). The stock is a capital asset, and any gain or loss from the sale of the stock would be long-term capital gain or loss under sections 1221 and 1222(3). D died in 2010, still owning the stock. As of D's date of death, D's adjusted basis in the stock pursuant to section 1011 was $5,000, and the stock's FMV on D's date of death was $1,000. D did not sell the stock during life, and thus did not incur a loss under section 165(c)(2) reportable on D's final Form 1040. The stock is considered to be property owned by and acquired from D. D's executor made the Section 1022 Election. If D had sold the stock immediately prior to D's death, D would have had a net long-term capital loss of $4,000. Based on D's 2010 taxable income, D would have been able to deduct $3,000 of the loss and $1,000 would have been carried over to future years. Section 1211(b). For purposes of section 1022, however, the full unrealized net long-term capital loss of $4,000, that would have been available to D if D had sold the stock before death, is available as a Carryovers/Unrealized Losses Basis Increase.

XIV. Spousal Property Basis Increase

A. Overview

The Spousal Property Basis Increase is $3,000,000. Generally, the executor can allocate Spousal Property Basis Increase only to "qualified spousal property" that was both acquired from and owned by the decedent.

B. Qualified Spousal Property.

Qualified spousal property means: (i) outright transfer property; and (ii) Qualified terminable interest property.

C. Outright Transfer Property.

[27] For more information, see § 165(j) and regulations § 1.165-12.

[28] For rules about unrealized losses arising from community property, see sections 4.05 and 4.06(4) of Rev. Proc. 2011-41.

1. Definition

For purposes of the Spousal Property Basis Increase, "outright transfer property" means any interest in property acquired from the decedent by the decedent's surviving spouse.

2. Terminable Interest Rule

Outright transfer property does not include an interest passing to the surviving spouse that:

a. On the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, will terminate or fail:

b. If both: (i) an interest in such property passes or has passed (for less than adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and (ii) by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse; or

c. If such interest is to be acquired for the surviving spouse, pursuant to directions of the decedent, by his executor or by the trustee of a trust.

For purposes of the exception described in the preceding sentence, an interest shall not be considered as an interest which will terminate or fail merely because it is the ownership of a bond, note, or similar contractual obligation, the discharge of which would not have the effect of an annuity for life or for a term.

For purposes of whether property is outright transfer property, an interest passing to the surviving spouse shall not be considered as an interest which will terminate or fail on the death of such spouse if both of the following two conditions are met:

a. The spouse's death will cause a termination or failure of such interest only if it occurs within a period not exceeding 6 months after the decedent's death, or only if it occurs as a result of a common disaster resulting in the death of the decedent and the surviving spouse, or only if it occurs in the case of either such event.

b. Such termination or failure does not in fact occur.

D. Qualified Terminable Interest Property ("QTIP").

For purposes of the Spousal Property Basis Increase, QTIP is property that passes from the decedent and in which the surviving spouse has a qualifying income interest for life. The surviving spouse has a qualifying income interest for life if both of the two following conditions are met: (i) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, or has a usufruct interest for life in the property; and, (ii) no person has a power to appoint any part of the property to any person other than the surviving spouse.[29] To the extent provided in regulations, an annuity shall be treated in a manner similar to an income interest in property (regardless of whether the property from which the annuity is payable can be separately identified).

E. Property Held by a CRT

1. Basic Rule

For purposes of the Spousal Property Basis Increase, the following rules apply: (i) the term "property" includes an interest in property; and, (ii) a specific portion of property is treated as separate property. For this purpose, "specific portion" only includes a portion determined on a fractional or percentage basis.

2. Allocation to Property Held by a CRT

The executor also can allocate Spousal Property Basis Increase to the property held by a testamentary charitable remainder trust (CRT) as defined in Section 664 (subject to the limitation of Section 1022(d)), if (i) the surviving spouse is the sole non-charitable beneficiary of the CRT and the CRT would have qualified for the marital deduction under Section 2056(b)(8) if the decedent's executor had not made the Section 1022 Election or (ii) the property is sold before being distributed.

However, this allocation can be made only to the extent that the executor: (i) certifies on Form 8939 that the net proceeds from the sale of that property will be distributed to or for the benefit of the decedent's surviving spouse in a manner that would qualify property as qualified

[29] Item 2, above, shall not apply to a power exercisable only at or after the death of the surviving spouse.

spousal property; and (ii) attaches to Form 8939 each document providing a bequest or devise to the surviving spouse.[30]

XV. Collateral Issues

A. Who is the Executor?

The "executor" of the estate is responsible for the allocation of the Basis Increase, on the timely filed Form 8939. The identification of the "executor' is made with Section 2203 as if that section was applicable. Section 2203 defines the "executor" as the executor or administrator of the decedent, or, if there is no executor or administrator appointed, qualified, and acting within the United States, then any person in actual or constructive possession of any property of the decedent. Accordingly, if an executor has been appointed, is qualified, and is acting for a decedent's estate within the United States, the IRS generally will only accept Forms 8939 filed by such executor. If an executor has not been appointed, any person in actual or constructive possession of property acquired from the decedent may file a Form 8939 for the property he or she actually or constructively possesses.

B. What if Multiple Forms 8939 Are Filed?

1. IRS Letter

If the IRS receives multiple Forms 8939 that collectively purport to allocate Basis Increase in an amount greater than the amount of Basis Increase available to the estate, the IRS will issue a letter to each person who filed such a form. The letter will include the name and address of each other person who filed a Form 8939 with respect to the decedent, and will explain that each of those persons must collectively sign and file a single, restated Form 8939 allocating available Basis Increase in order to make the Section 1022 Election.

2. Restated 8939

The restated Form 8939 must be filed on or before 90 days from the date the IRS mails such letters. If no restated Form 8939, signed by each such person who previously submitted a Form 8939, is filed within that 90-

[30] For more information, see Rev. Proc. 2011-41, section 4.02(3). For detailed information on how to report the property described in item 2, see the specific instructions for Schedule A, line 4, column (e)(i) and (e)(ii).

day period, the IRS will allocate the available Basis Increase as the IRS, in its discretion, may determine. In making this determination and exercising its discretion, the IRS will consider all relevant facts and circumstances disclosed to the IRS. That allocation might be made on a pro-rata basis, based on the amount of unrecognized appreciation in the property owned by the decedent at death, within the meaning of Section 1022(d), (hereinafter, "owned by the decedent") and acquired from the decedent that was reported on the timely filed Forms 8939, or in any other manner deemed appropriate for the particular decedent's estate by the IRS in the exercise of its discretion.

The recipient's basis in a particular property (including the amount of Basis Increase allocated to that property) is subject to adjustment upon the examination by the IRS of any tax return reporting a value dependent upon the property's basis (for example, the property's depreciation, sale, or other disposition that triggers gain or loss on the property, or otherwise).

C. What is the Holding Period of Inherited Property?

To the extent the recipient's basis in property acquired from the decedent is determined under Section 1022, the recipient's holding period of that property shall include the period during which the decedent held the property, whether or not the executor allocates any Basis Increase to that property. In computing the applicable percentage under Section 1250 for purposes of determining the amount of ordinary gain on the sale of Section 1250 property, Section 1250(e) applies to determine the period of time the recipient is deemed to have held section 1250 property acquired by gift or on the death of a decedent. Therefore, to the extent a recipient's basis in property is determined under Section 1022, the recipient's holding period of such property under Section 1250(e)(2) includes the period during which the property was held by the decedent, regardless of whether the executor allocates any Basis Increase to that property.

D. What is the Tax Character of Inherited Property?

1. General Rule

The tax character of property acquired from the decedent by a recipient is determined in the same way as the holding period. Thus, to the extent a recipient's basis in property is determined under Section 1022, the tax character of the property is the same as it would have been in the hands of the decedent. Consequently, for property described in Section 1221

(capital assets) or Section 1231 (property used in a trade or business and involuntary conversions), and for property subject to Section 1245 (depreciation recapture upon disposition of certain depreciable property) or Section 1250 (depreciation recapture upon disposition of certain depreciable real property), the tax character of the property described in these sections (the basis of which is determined under Section 1022) in the hands of the recipient is the same as it would have been in the hands of the decedent. However, the tax character of the property may be affected by a subsequent change in the recipient's use of the property.

2. Example

The provisions of this section are illustrated by the following example:

Example - D owned tangible personal property (section 1245 property) and claimed on D's income tax return a depreciation deduction under section 168 that would have been subject to recapture under Section 1245 if D had sold the property prior to D's death. D died in 2010 and D's executor made the Section 1022 Election. D bequeathed all of D's tangible personal property to D's child (C). Because C's basis is determined under section 1022, the property is Section 1245 property in the hands of C and therefore will be subject to recapture under Section 1245 when sold by C, regardless of whether the property is depreciable property in the hands of C or whether the executor allocates any Basis Increase to that property.[31]

E. How do I Calculate Depreciation of Property Acquired from the Decedent?

1. Basic Rule

If Section 1022 applies to property acquired from the decedent that is depreciable property in the hands of the recipient, regardless of whether the executor allocates any Basis Increase to the property, the recipient is treated for depreciation purposes as the decedent for the portion of the recipient's basis in the property that equals the decedent's adjusted basis in that property. Consequently, the recipient determines any allowable depreciation deductions for this carryover basis by using the decedent's depreciation method, recovery period, and convention applicable to the property. If the property is depreciable property in the hands of both the decedent and the recipient during 2010, the allowable depreciation

[31] See § 1.1245-3(a)(3).

deduction for 2010 for the decedent's adjusted basis in the property is computed by using the decedent's depreciation method, recovery period, and convention applicable to the property, and is allocated between the decedent and the recipient on a monthly basis.

2. Rules of Regulation 1.168(d)-1(b)(7)(ii)

This allocation is made in accordance with the rules in Regulation section 1.168(d)-1(b)(7)(ii) for allocating the depreciation deduction between the transferor and the transferee. The portion of the recipient's basis in the property that exceeds the decedent's adjusted basis in the property as of the decedent's date of death (for example, the Basis increase allocated to the property by the executor) is treated for depreciation purposes as applying to a separate asset that the recipient placed in service on the day after the date of the decedent's death. Accordingly, the recipient determines any allowable depreciation deductions for this excess basis by using the depreciation method, recovery period, and convention applicable to the property on its placed-in-service date or, if not held on that date as depreciable property by the recipient, on the date of the property's conversion to depreciable property.

F. What if I Can't Determine the Decedent's Basis

Generally the burden is on the taxpayer to establish the level of the basis of the transferor. The regulations relating to carryover basis for assets received by gift provide the following guidance if that basis cannot be readily determined:

> *"(3) If the facts necessary to determine the basis of property in the hands of the donor or the last preceding owner by whom it was not acquired by gift are unknown to the donee, the district director shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. If the district director finds it impossible to obtain such facts, the basis in the hands of such donor or last preceding owner shall be the fair market value of such property as found by the district director as of the date or approximate date at which, according to the best information the district director is able to obtain, such property was acquired by such donor or last preceding owner. See paragraph (e) of this section for rules relating to fair market value."*[32]

G. Is an Estate Allowed a Spousal Step Up in Basis if Property is Sold by the Estate?

1. In General

[32] See Reg. § 1.1015-1(a)(3)

Rev. Proc. 2011-41 addresses the question of what happens if an asset is sold by the estate prior to distribution, and allows the allocation to be made to those assets as long as the Executor certifies that the net proceeds of the sale will be distributed to the surviving spouse. A similar logic would seem to apply to assets actually passing to the surviving spouse.

Under Section 1022(c)(2), the Spousal Step Up in Basis may be allocated to any or all property owned by and acquired from the decedent that also satisfies the definition of qualified spousal property in Section 1022(c)(3). Qualified spousal property is defined as property that either is transferred outright to the decedent's surviving spouse or is QTIP, whether or not held in trust. Under Rev. Proc. 2011-41 the executor may allocate the Spousal Property Basis Increase to qualified spousal property that has already been distributed. Further Notice 2011-66, provides relief for allocating Spousal Property Basis Increase to such property distributed after the due date of the Form 8939.

2. Requirements for the Allocation

As referenced above, Rev. Proc. 2011- 41, allows a Spousal Property Basis Increase to be allocated to property that has been sold (regardless of whether the allocation of Spousal Property Basis Increase is made before or after such sale prior to its distribution, i.e., during the period of the estate administration); provided that the executor, (i) certifies on the Form 8939 that the net proceeds from the sale of that property will be distributed to or for the benefit of the decedent's surviving spouse in a manner that would qualify property as qualified spousal property, and, (ii) attaches to Form 8939 each document providing a bequest or devise to the surviving spouse.

3. Examples

The allocation of Spousal Property Basis Increase to property not distributed in kind is illustrated by the following examples. Assume that the decedent's Aggregate Basis Increase and Carryovers/Unrealized Losses Increase have been fully allocated to other assets.

Example 1 - D died in 2010 owning 20,000 shares of Corporation X stock. D's executor made the Section 1022 Election. D's adjusted basis in the stock is $600,000 ($30 per share), and the FMV on D's date of death is $2,000,000 ($100 per share). Under the terms of D's will, D's Spouse (S) is to receive 50 percent of D's estate, outright. Four months after D's death, the FMV of the stock declines to $1,800,000 ($90 per share). D's executor sells all 20,000 shares of the stock and receives $1,770,000 in proceeds net of sales commissions (thus, $88.50 per share). D's executor intends to distribute all of the proceeds from the sale of the stock to S, in partial satisfaction of S's

residuary bequest; there are no known outstanding liabilities that would reduce this distribution. D's executor may allocate up to $1,400,000 of Spousal Property Basis Increase ($70 to each of the 20,000 shares of stock) if the required certification and supporting documentation is included on a timely filed Form 8939. (Note that, to the extent that more than $58.50 per share is allocated to the stock, the sale will generate a loss.)

Example 2 - The facts are the same as in the preceding Example 1 except that D's executor applies $165,000 of the net proceeds from the sale of the stock to pay administrative expenses of D's estate. D's executor intends to distribute the remaining $1,605,000 of net proceeds from the sale of the stock to S. Spousal Property Basis Increase may be allocated to no more than 18,135 shares. This number of shares is determined either by dividing the net proceeds to be distributed to S by the net per-share proceeds ($1,605,000 / $88.50 = 18,135.6 shares, limited for this purpose to 18,135 whole shares), or by calculating the ratio of the net proceeds payable to S to the total net proceeds (20,000 shares x $1,605,000 / $1,770,000 = 18,135.6 shares, thus limited to 18,135 whole shares).

As in Example 1, D's executor may allocate up to $70 of Spousal Property Basis Increase to each of these 18,135 shares of the stock (for a total of $1,269,450), all of the net proceeds of which will be distributed to S, provided a certification and supporting documentation are included on a timely filed Form 8939.

Example 3 - D died in 2010 owning personal property with an adjusted basis of $200,000 and a FMV on D's date of death of $500,000. D's executor made the Section 1022 Election. Under the terms of D's will, D's spouse (S) is to receive 50 percent of D's estate, outright. Four months after D's death, D's executor sells the personal property for $600,000. D's executor applies $150,000 of the net proceeds from the sale of the personal property to pay administrative expenses of D's estate and intends to distribute the remaining $450,000 of net proceeds from the sale of the personal property to S. D's executor may allocate no more than $225,000 of Spousal Property Basis Increase to the personal property. This maximum allocation is determined by multiplying the unrealized appreciation at death ($300,000) by the ratio of net proceeds to be distributed to S over the total net proceeds of the sale. Thus, D's executor may allocate up to $225,000 ($300,000 X ($450,000 / $600,000)) of Spousal Property Basis Increase to the personal property, provided a certification and supporting documentation are included on a timely filed Form 8939. Spousal Property Basis Increase also may be allocated to property held by a testamentary charitable remainder trust (CRT) as defined in section 664 (subject to the limit of section 1022(d)(2)), if the surviving spouse is the sole non-charitable beneficiary of the CRT and the CRT would have qualified for the marital deduction under section2056(b)(8) if the executor of the decedent's estate had not made the Section 1022 Election.

XVI. GST Tax in 2010 - With Respect to Decedents Who Died in 2010

A. In General

The Generation Skipping Transfer Tax (the "GST" tax) was retroactively reinstated by Tax Relief Act and applies to the estates of all decedents who died

after December 31, 2009, regardless of whether a Section 1022 Election is made. The GST tax is computed by multiplying the taxable amount by the applicable rate.[33] Section 2641(a) defines the applicable rate for this purpose as the maximum federal estate tax rate applicable to the estate of a decedent dying at the time of the transfer, multiplied by the inclusion ratio with respect to that transfer. Section 302(c) of Tax Relief Act provides that, for each GST occurring during 2010, the applicable rate under section 2641(a) is zero. This provision is interpreted to mean that the maximum federal estate tax rate for purposes of computing the GST tax on such a transfer is deemed to be zero which, when multiplied by any inclusion ratio, will result in an applicable rate of zero. As under the law applicable to GSTs occurring prior to 2010, the only way to achieve a zero inclusion ratio for the transfer is to make a timely allocation of GST exemption to the transfer.

B. Allocation of the GST Exemption

1. Schedule R of Form 8939

If the executor of a decedent who died in 2010 makes the Section 1022 Election, the executor allocates that decedent's available GST exemption by attaching the Schedule R of Form 8939 to the Form 8939 for that decedent's estate. If the Form 8939 is timely filed, this allocation will be considered a timely allocation of the decedent's GST exemption under section 2632.

2. Inter Vivos Direct Skips

In the case of inter vivos direct skips that occurred in 2010, if the donor wishes to pay GST tax at the rate of zero percent and therefore does not wish to have any GST exemption allocated to that transfer, the donor may elect out of the automatic allocation of GST exemption to that direct skip in either of two ways. First, the donor affirmatively may elect out of the automatic allocation by describing, on a timely filed Form 709, both the transfer and the extent to which the automatic allocation is not to apply. [34]

---

[33] Section 2602.

[34] See Section 26.2632-1(b)(1)(i).

Alternatively, that same regulation also provides that, *". . . a timely filed Form 709 accompanied by payment of the GST tax (as shown on the return with respect to the direct skip) is sufficient to prevent an automatic allocation of GST exemption with respect to the transferred property."* Because it is clear that a 2010 transfer not in trust to a skip person is a direct skip to which the donor would never want to allocate GST exemption, the IRS will interpret the reporting of an inter vivos direct skip not in trust occurring in 2010 on a timely filed Form 709 as constituting the payment of tax (at the rate of zero percent) and therefore as an election out of the automatic allocation of GST exemption to that direct skip.

This interpretation also applies to a direct skip not in trust occurring at the close of an estate tax inclusion period ("ETIP") in 2010 other than by reason of the donor's death. However, a donor may or may not want to allocate GST exemption to a 2010 direct skip made to a trust. Therefore, this interpretation will not apply to any transfer in trust that is a direct skip or that occurs at the end of an ETIP. In addition, because this interpretation only applies to inter vivos direct skips, it will also not apply to any direct skip, or to the close of an ETIP, by reason of the donor's death. Section 26.2632-1(c)(4). The rules regarding the automatic allocation of GST exemption will apply to transfers described in the preceding sentence unless the transferor affirmatively elects to have those rules not apply.

C. Filing Deadlines

1. Election Rule

Section 2611(a) defines a GST transfer as a direct skip, a taxable distribution, or a taxable termination. An indirect skip, as defined in section 2632(c)(3), is not a GST transfer. Section 2631 provides that each individual is allowed a GST exemption amount which may be allocated to any property with respect to which such individual is the transferor. Under § 26.2632-1(b)(3) and (4), an election to treat a trust as a GST trust or to allocate GST exemption to any inter vivos transfer other than a direct skip, is made on a timely filed Form 709. Section 2632(b)(1) and (c)(1) provide that, if any individual makes a direct or indirect skip during life, any unused portion of such individual's GST exemption shall be allocated to the property transferred to the extent necessary to make the inclusion ratio for such property zero. Sections 2632(b)(3) and (c)(5) and § 26.2632-1(b)(1)(i) and

(b)(2)(ii) provide that an individual may prevent the automatic allocation of GST exemption by so providing on a timely filed Form 709.

2. Extended Deadline

Section 301(d)(2) of TRUIRJCA extends the time for filing any return required under section 2662 (including any election required to be made on such return) to report a GST transfer made after December 31, 2009, and before December 17, 2010, to September 17, 2011. Accordingly, the due date for filing a return reporting a direct skip, a taxable distribution, or a taxable termination (including any election required to be made on such return) that occurred on or after January 1, 2010, through December 16, 2010, is September 19, 2011, including extensions (because September 17, 2011, falls on a Saturday), *except in the case of a Schedule R attached to Form 8939, which is due on or before January 17, 2011.*

3. Gift Tax and GST Returns for 2010

However, the language of Section 301(d)(2) of TRUIRJCA does not extend the due date of all gift and GST returns for 2010. Specifically, to the extent a return relates to an indirect skip, or to a post-December 16, 2010, direct skip, the due date of the return is not extended. Thus, the due date for filing a Form 709 that does not report a GST transfer or that reports a GST transfer (or any election pertaining to such transfer) that occurs on or after December 17, 2010, through December 31, 2010, was April 18, 2011, including extensions.

4. Possible Sec. 301.9100-2 Relief

In addition, the due date for filing a Form 709 to elect to treat a trust as a GST trust or to allocate GST exemption to a transfer occurring during 2010 under § 26.2632-1(b)(3) or (4) was April 18, 2011, including extensions. However, if a donor timely filed Form 709 for the taxable year ending December 31, 2010, but failed to allocate GST exemption to a transfer occurring during such year, see § 301.9100-2 for possible relief.