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July 23, 2007

Via United States Mail

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Re: Comments of the American College of Trust and Estate Counsel (the "College") on Proposed Regulations issued under section 2053 (REG-143316-03) on April 23, 2007

Ladies and Gentlemen:

The American College of Trust and Estate Counsel ("the College") is pleased to submit these comments on the Proposed Regulations issued under section 2053 on April 23, 2007. Drafting regulations is a difficult task and is especially so where the existing Regulations are almost 50 years old. The College appreciates the hard work of Internal Revenue Service and Treasury Department personnel and applauds the attention given an area that affects every taxable estate.

The College is a professional association of approximately 2,600 lawyers from throughout the United States. Fellows of the College are elected to membership by their peers on the basis of professional reputation and ability in the fields of trusts and estates and on the basis of having made substantial contributions to these fields through lecturing, writing, teaching and bar activities.

The College offers technical comments about the law and its effective administration. It does not take positions on matters of tax policy.

General Approach of the Proposed Regulations

The Supplementary Information states that two competing lines of cases have developed interpreting the existing Regulations under section 2053:

> One line of cases follows the decision in *Ithaca Trust v. Commissioner*, 279 U.S. 151 (1929), holding that the estate tax charitable deduction for a charitable remainder interest was to be determined as of date of death. In Federal judicial circuits where the *Ithaca Trust* date-of-death valuation approach is applied to a claim against a decedent's estate under section 2053(a)(3), courts generally hold that post-death events may not be considered when determining the amount deductible for that claim. At the opposite end of the spectrum, there is a line of cases that follows the Eighth Circuit's opinion in *Jacobs v. Commissioner*, 34 F.2d 233 (8th Cir. 1929), *cert. denied*, 280 U.S. 603 (1929), in which the court considered but rejected the date-of-death valuation approach in determining the deductible amount of a claim against the estate. The court in *Jacobs* distinguished *Ithaca Trust*, stating that, unlike charitable deductions, ". . . the claims which Congress intended to be deducted were actual claims, not theoretical ones." The court therefore held that only claims presented and determined as valid against the estate and actually paid could be deducted as claims against the estate. *Jacobs*, 34 F.2d at 235. The courts that follow *Jacobs* generally restrict the amount deductible under section 2053(a)(3) to amounts actually paid by the estate in satisfaction of the claim.

Notwithstanding this characterization of the case-law, it appears that existing law is reasonably clear that section 2053 calls for a "snapshot" approach similar to that required when valuing assets. Thus, many practitioners may disagree with the overall approach adopted by the Proposed Regulations, explained as follows in the Supplementary Information:

> One possible approach would be to value claims against a decedent's estate on the basis of the facts existing on the date of the decedent's death. The Treasury Department and the IRS believe, however, that this date-of-death valuation approach, when applied, has required an inefficient use of resources for taxpayers, the IRS, and the courts. Determining a date-of-death value requires the taxpayer and the IRS to retry the substantive issues underlying the claims against the estate in a tax controversy setting. In most cases, the tax controversy is addressed after the issue either has been settled by or has been argued by parties with adverse interests in a court of competent jurisdiction that is more familiar with the nuances of the underlying applicable law. Furthermore, this approach has proven to be expensive, both in terms of appraisal and litigation costs. In addition, this approach generally results in a deduction that is different from the amount actually paid on disputed claims. Finally, the date-of-death valuation approach often forces the taxpayer involved in actively defending against a claim to take contradictory positions on the estate tax return and in the substantive court pleadings, and may actually increase the taxpayer's potential liability.

> After carefully considering the numerous judicial decisions and the analysis and conclusion in each, the legislative history of section 2053 and its predecessors, and the various possible alternatives, and in order to further the goal of the effective and fair administration of the tax laws, the proposed regulations adopt rules based on the premise that an estate may deduct under section 2053(a)(3) only amounts actually paid in settlement of claims against the estate. If the resolution of a contested or contingent claim cannot be reached prior to the expiration of the period of limitations for claims for refund, the estate may file a protective claim for refund to preserve its right to claim a deduction under section 2053(a).

As the comments that follow will indicate, deviating from a snapshot approach is conceptually inconsistent with the approach generally taken in administering the estate tax, presents difficulties in the administration of estates and may present opportunities for unfair application on audit.

The College is particularly concerned about the concept of a protective claim that has been used rarely until now. Such a concept is contrary to the need for finality in the administration of estates, as shown by, for example, the inability to extend the estate tax statute of limitations. Furthermore, the College believes that other practitioners do not understand how such a regime would work procedurally and practically, as is discussed more fully below. The inter-relationship of protective claims and the marital/charitable deductions is of special concern.

Experience may show that the approach of the Proposed Regulations is less efficient, or at least no more efficient, than would have been a snapshot approach. While many Fellows of the College would prefer final regulations that implement a snapshot approach in a fair and reasonable manner. Nonetheless, the College believes the approach of the Proposed Regulations has merit and can likewise be implemented in a fair and reasonable manner. The College hopes the comments that follow will be helpful in that process.

Family Claims Rebuttable Presumption

Prop. Reg. §2053–4(b)(4) deals with claims by family members, related entities, or beneficiaries and creates a rebuttable presumption that such claims against an estate are invalid. This approach is directly at odds with the approach taken when valuing family entities as evidenced by Revenue Ruling 93-12. The College believes this approach is unfair and unwarranted. The Proposed Regulations throughout rely upon the concept of "bona fide and legitimate claims" (about which see comment 3 below). The College believes that that standard is sufficient to eliminate "invalid or exaggerated claims in order to reduce a decedent's taxable estate." If a claim is not bona fide it ought not to be allowed as a deduction regardless of the claimant; if a claim is bona fide, that the decedent owes a family member, beneficiary, or related entity ought not to present an automatic impediment to deduction by the estate.

The College is also concerned about the inter-relationship between a rebuttable presumption and the usual standards for the allocation of burdens of proof in the transfer tax area. The College believes that the rebuttable presumption approach is inconsistent with section 7491 and more likely than not would not be sustainable were it challenged after being included in final regulations.

The Proposed Regulations state that the concern is about collusion. That concern could be met by requiring that claims by family members and beneficiaries be subject to close scrutiny to determine if a claim is bona fide. Indeed, case law already provides for "heightened" or "close" scrutiny of claimed estate tax deductions in respect of the unpaid balance of loans owed to family members by a decedent. *See, e.g.*, Estate of Flandreau v. Commissioner, T.C. Memo. 1992-173, aff'd, 994 F.2d 91 (2d Cir. 1993); Leopold v. United States, 510 F.2d 617 (9th Cir. 1975). Further, factors could be enumerated that would indicate that a claim is bona fide, for example, if a claim were evidenced by a writing or by the statement of independent (non-family, non-beneficiary) witnesses that sets forth the circumstances creating the claim, and if the claim were adverse to the interests of other beneficiaries.

The Proposed Regulations state that "[e]vidence sufficient to rebut the presumption may include evidence that the claim arises from circumstances that would reasonably support a similar claim by unrelated persons or non-beneficiaries." The College believes this presents a contradiction. Suppose a parent is cared for in part by a child and in part by independent caregivers. If claims by the child are subject to a rebuttable presumption, must not the child present more evidence than that presented by the independent caregivers? Otherwise is not the notion of a rebuttable presumption with respect to family claims meaningless? In application and on audit, the College believes that the rebuttable presumption standard will be difficult or impossible to overcome in many bona fide and legitimate instances.

The definition of family is also problematic. To limit the collusion possibilities, the Proposed Regulations define family very broadly (for instance, the descendants of a decedent's spouse's sibling), often to include relatives who neither were close to the decedent nor to one another. At the same time, the American family is changing as an institution and in many instances even such a broad definition will not apply the rebuttable presumption to circumstances fraught with the possibility of collusion. In effect, examining agents are invited to be more preoccupied with the degree of relationship than with the merits of the claim. The merits should be based upon a facts and circumstances analysis, with closer scrutiny being appropriate if the facts indicate possible collusion. The relationship of the claimant is only one of the facts that should be considered and should not be mechanistically elevated to the most important and, in the field, likely determinative fact.

The Proposed Regulations apply the rebuttable presumption to "related entities" that are defined as follows:

> ... an entity in which the decedent, either directly or indirectly, had a beneficial ownership interest at the time of the decedent's death or at any time during the three-year period ending on the decedent's date of death. Such an entity, however, shall not include a publicly-traded entity nor shall it include a closely-held entity in which the combined beneficial interest, either direct or indirect, of the decedent and the decedent's family members, collectively, is less than thirty percent of the beneficial ownership interests (whether voting or non-voting).

The College believes that the definition is unnecessarily ambiguous as to when the determination of "related entity" is made. The apparent purpose of the definition is to include enterprises as related entities in situations where it might be economically desirable to transfer assets from a decedent's estate to the enterprise through a collusive claim because either the estate or the decedent's family own 30% or more of the enterprise. The first sentence includes as related entities all enterprises in which a decedent had a beneficial interest at the date of death or at any time during the three prior years. The second sentence carves out an exception for certain enterprises (for instance, publicly traded entities) without a time period. A determination of whether the exclusion applies should be made at the time a claim is asserted. For example, suppose the decedent owned 100% of Entity X and Entity Y at her date of death. Entity X became publicly-traded the day before the date of death and Entity Y became publicly-traded the day after the date of death. During estate administration, Entity X and Entity Y each assert a claim against the estate. Both Entity X and Entity Y should be excluded from the definition of related entities because at the time the claim was asserted each was encompassed within the exception.

<u>Administrative and Audit Issues</u>

For the convenience of the reader, in the order of the Proposed Regulations, the provisions of the Proposed Regulations are set forth followed by the comment of the College and are numbered for ease of reference.

The College believes that the issues discussed under Protective Claims (number 4) and Claims and Counter-Claims (number 8) are most challenging.

1. <u>Unsupervised Administration</u>. Prop. Reg. § 20.2053-1(b)

> (2) <u>Effect of court decree</u> -- (i) <u>In general</u>. If the court with appropriate jurisdiction over the administration of the estate reviews and approves expenditures for funeral expenses, administration expenses, claims against the estate, or unpaid mortgages as allowable estate expenditures under local law, the executor may rely on the final judicial decision in that matter to determine the amount deductible for estate tax purposes if the following conditions are satisfied: the expenditures are otherwise deductible under section 2053 and the corresponding regulations; the expenditures have been paid by the estate or meet the requirements for estimated expenses; the court reviewed the facts relating to

> the expenditures; and the court's decision is consistent with local law. See § 20.2053-2 for additional rules regarding the deductibility of funeral expenses. See § 20.2053-3 for additional rules regarding the deductibility of administration expenses. See § 20.2053-4 for additional rules regarding the deductibility of claims against the estate. See § 20.2053-7 for additional rules regarding the deductibility of unpaid mortgages. If the decision reached by the court is inconsistent with local law, the estate may not rely on the court's decree to establish the amount deductible for estate tax purposes. For example, a local court decree approving an allowance made to an executor in excess of the amount or limit prescribed by statute may not be relied upon to establish the amount deductible under section 2053. An estate will not be denied an otherwise allowable deduction under section 2053 solely because a local court decree has not been entered with respect to that amount if the amount would be allowable under local law and if no court decree is required under applicable law for payment.

In many jurisdictions a court approves the administration of an estate without specifically approving expenses and claims, absent a challenge from an interested party. The last sentence quoted above appears to cover administration in such jurisdictions. An example of when a deduction for claims and expenses would and would not be allowed in such jurisdictions would be helpful.

2. <u>Consent Decrees</u>. Prop. Reg. § 20.2053-1(b)(2)

> (ii) <u>Consent decree</u>. An executor may rely on a local court decree rendered by consent to establish the amount deductible under section 2053 for amounts paid (or meeting the requirements for estimated expenses) if the consent was a bona fide recognition of the validity of the claim and was accepted by the court as satisfactory evidence upon the merits. Consent given by all parties having interests adverse to that of the claimant will be presumed to be recognition of the claim's validity. See § 20.2053-4(b)(4) for special rules to determine the amount deductible for claims by decedent's family members, related entities, or beneficiaries of the decedent's estate or revocable trust.

The College is uncertain about the difference between a consent decree and a settlement. Often, the parties to a dispute over expenses or claims reach an agreement that is filed with the local probate court. If no one challenges that agreement, and the court is satisfied that all appropriate parties have agreed, the court is unlikely to review independently the terms of the agreement. Under such circumstances, consent will have been given by all parties having interests adverse to that of the claimant, as per the second sentence, which should be deemed to satisfy the requirements of the first sentence as well. If the first sentence contains requirements separate from that of consent of all parties having interests adverse to the claimant, then clarification of what it means for consent to be bona fide recognition of the validity of the claim would be helpful as would an understanding of what a court must do to accept an agreement as "satisfactory evidence upon the merits."

3. Settlements. Prop. Reg. § 20.2053-1(b)

> (3) Settlements. An executor may rely on a settlement to establish the amount deductible under section 2053 for amounts paid (or meeting the requirements for estimated expenses) (subject to any applicable time limitation under paragraph (a) of this section) if the following conditions are satisfied: the settlement resolves a bona fide issue in an active and genuine contest; the settlement is the product of arm's length negotiations by parties having adverse interests with respect to the claim; and the settlement is within the range of reasonable outcomes under applicable state law governing the issues resolved by the settlement. A settlement that results in a compromise between the positions of such adverse parties and reflects the parties' assessments of the relative strengths of their respective positions is a settlement that is within the range of reasonable outcomes. However, a deduction for amounts paid in settlement of a claim against the decedent's estate will not be allowed if the terms of the settlement are inconsistent with applicable local law. No deduction will be allowed for amounts paid in settlement of an unenforceable claim. See § 20.2053-4(b)(4) for special rules to determine the amount deductible for claims by decedent's family members, related entities, or beneficiaries of the decedent's estate or revocable trust. For settlements structured using recurring payments, see § 20.2053-4(b)(7).

A settlement that allows expenses to be deducted must satisfy three requirements. First, the settlement must resolve a "bona fide issue in an active and genuine contest." In Comment 2 above the Proposed Regulations used the phrase "bona fide recognition of the validity of the claim." A definition of "bona fide," not only in these contexts but with respect to any expense or claim for which a deduction is sought would be helpful. A condition for the deductibility for any expense or claim should be that it is bona fide.

Second, the settlement must be the result of arms-length negotiations by parties having adverse interests with respect to the claim. Third, a settlement must be within the range of reasonable outcomes. A compromise that reflects the parties' assessments of their relative strengths is deemed to be a settlement within the range of reasonable outcomes. Many times, the parties to litigation simply settle to avoid further expense without either party admitting to fault or wrong-doing. A clarification that such a resolution is considered the result of arms-length negotiations and within the range of reasonable outcomes would be helpful.

The third requirement is superfluous. If a settlement is inconsistent with applicable local law it will not meet the three-part test of being bona fide, the result of arms-length negotiations, and within the range of reasonable outcomes.

4. Protective Claims. Prop. Reg. § 20.2053-1(b)

> (4) Estimated amounts. A deduction will be allowed for a claim that satisfies all applicable requirements even though its exact amount is not then known, provided that the amount is ascertainable with reasonable certainty, and will be

> paid. Under this exception to the rule set forth in paragraph (b)(1) of this section, no deduction may be taken upon the basis of a vague or uncertain estimate. If a deduction is allowed in advance of payment and the payment is thereafter waived or otherwise left unpaid, it shall be the duty of the executor to notify the Commissioner and to pay the resulting tax, together with interest. To the extent that the amount of a liability otherwise deductible under section 2053 is not ascertainable with reasonable certainty at the time of examination of the return by the Commissioner, or to the extent that it is not then clear that the amount will be paid, that amount will not be allowed as a deduction by the Commissioner. If the deduction is disallowed in whole or in part on examination of the return and the amount of the liability is subsequently ascertained and paid, relief may be sought by a timely claim for refund as provided by section 6511. A protective claim for refund may be filed before the expiration of the period of limitations for claims for refund in order to preserve the estate's right to claim a refund if the amount of a liability was or will not be paid before the expiration of the period of limitations for claims for refund. Although the protective claim need not state a particular dollar amount or demand an immediate refund, the protective claim must identify the outstanding liability or claim that would have been deductible under section 2053(a) had it already been paid. The protective claim must also describe the reasons and contingencies delaying the determination of the liability or the actual payment of the claim. Action on protective claims will proceed after the executor has notified the Commissioner that the contingency has been resolved.

The first sentence provides that amounts ascertainable with reasonable certainty are deductible. The second sentence prohibits deductions on the basis of "vague and uncertain" estimates. Notwithstanding the fact that substantially identical language is found in the current Regulations, the second sentence is superfluous.

The College believes that additional information with respect to "protective claims" would be helpful. Our understanding is that these protective claims will be handled in a manner similar to those filed under other transfer tax sections (e.g. sections 2032A, 6166). Thus, "after the executor has notified the Commissioner that the contingency has been resolved" the claim will be handled not as a new claim for refund but rather as an extension of the estate tax examination through a special group currently operating from Cincinnati. Further, presumably protective claims will be filed on a new schedule (e.g. Schedule K-P). Regardless of whether our understanding is correct, an explanation of the process would be desirable.

Examples of what would be sufficient, and insufficient, information for a valid protective claim would be helpful. Often an estate may wish to limit the information provided in a protective claim to avoid potential disclosure of risk assessment or other information to opposing parties in litigation matters. Further, how much specificity is required is unclear. In the course of litigation often claims are added and dropped; and the regulations should be flexible so that pending litigation matters could be generally identified and any bona fide payments made on account of such litigation would be covered by the protective claim. The College believes that the best approach would be to allow general identification of the nature of the liability or claim. To the extent that more specific information is required, the ability to amend and expand upon a protective claim would be desirable.

The College believes strongly that guidance contemporaneous with the final regulations should be issued describing the procedures to be used when filing a protective claim and when notifying the Commissioner that the claims made in the protective claim are ready for a final determination. To be most useful, that guidance should also describe when the protective claim would be examined and approved as a valid protective claim, when a request for a final determination would be acted upon, and what remedy an estate would have if either a protective claim were denied because it did not meet the regulatory requirements or a final determination were not made within a reasonable time. Presumably, the right to a refund arising from the allowance of the claims made in a protective claim may be distributed under applicable local law to the beneficiaries of an estate, and thus the final regulations should reflect that the administrative remedies similarly become those of the beneficiaries.

The Proposed Regulations do not directly address the inter-relationship of protective claims with the marital and charitable deductions. The College believes that if the residue of an estate qualifies for either the marital or charitable deduction the estate should claim on the initial Form 706 a marital or charitable deduction for the full value of the residue without regard to any potential claim that is the subject of a protective claim. However, if this result is incorrect — so that the estate must reduce the value of the marital or charitable deduction by the amount of a protective claim — then the estate should be allowed to preserve by a protective claim the disallowed marital or charitable deduction. If the potential claim is paid by the estate and allowed as a deduction upon review of the protective claim, then the marital or charitable deduction would be reduced; but if nothing were paid on the claim, then the full marital or charitable deduction would be allowed. Examples of claims being paid from marital and charitable funds would be helpful.

A collateral effect of the approach taken by the Proposed Regulations will be to create liquidity short-falls for estates subject to claims that cannot be deducted on the Form 706 but that later become certain and payable. In some situations the need for cash to pay estate taxes may even require an estate to settle a claim prematurely, and for more than its true worth, so that it may be deducted at the time the Form 706 is filed. A further administrative complexity may be presented if the estate borrows funds to pay either the estate tax or the claims because interest will be due during estate administration and may become an additional estate tax deduction. These issues may be mitigated to some degree by a liberal policy of allowing estates with liquidity issues an extension of time to pay estate tax which would be desirable.

5. Effect of Reimbursements. Prop. Reg. § 20.2053-1(b)

> (5) Reimbursements. A deduction is not allowed to the extent that the expense or claim is or could be compensated for by insurance or otherwise reimbursed.

This provision will require the filing of substantial numbers of protective claims where an expense or claim "could be compensated for by insurance or otherwise reimbursed" if an executor is not able to demonstrate with finality that no reimbursement or insurance is available. The regulations should allow an executor to ask for a court determination that no reimbursement or insurance is available. Further, such a determination made as part of a consent decree or settlement should be accepted.

6. Attorney's Fees. Prop. Reg. § 20.2053-3

> (c) Attorney's fees. (1) The executor, in filing the estate tax return, may deduct such an amount of attorney's fees as has actually been paid, or an amount which at the time of filing may reasonably be expected to be paid. If on the examination of the return, the fees claimed have not been awarded by the proper court and paid, the deduction will, nevertheless, be allowed, if the Commissioner is reasonably satisfied that the amount claimed will be paid and that it does not exceed a reasonable remuneration for the services rendered, taking into account the size and character of the estate and the local law and practice. If the amount does not satisfy these requirements, a protective claim for refund may be filed before the expiration of the period of limitations for claims for refund in order to preserve the estate's right to claim a refund for future amounts paid as described in § 20.2053-1(b)(4). If the deduction is disallowed in whole or in part on the examination of the return and a protective claim was timely filed, the disallowance will be subject to modification once the requirements for deductibility are met.

The College believes that the second sentence should also reference the skill and expertise of the attorneys involved. This is a typical touchstone for the determination of reasonable attorney fees.

The last sentence quoted above is different from the last sentence of Prop. Reg. § 20.2053-1(b)(4), quoted above in Comment 4. Confirmation that the procedure is the same for all protective claims, regardless of the reason filed, is desirable.

7. Litigation Expenses. Prop. Reg. § 20.2053-3(d)

> (3) Expenses incurred in defending the estate against claims described in section 2053(a)(3) are deductible as provided in § 20.2053-1 if the expenses are incurred incident to the assertion of defenses to the claim available under the applicable law, even if the estate is not ultimately victorious. For purposes of this section, "expenses incurred in defending the estate against claims" include costs relating to the arbitration and mediation of contested issues, costs associated with defending the estate against claims (whether or not enforceable), and costs associated with reaching a negotiated settlement of the issues.

> Expenses incurred merely for the purpose of unreasonably extending the time for payment, or incurred other than in good faith, are not deductible.

The last sentence is troublesome. Litigation is notoriously expensive and time-consuming. Often one party believes that another is engaged in tactics that increase fees or cause delay solely to obtain advantage. Attempting to demonstrate that no expenses of litigation have been incurred "merely for the purpose of unreasonably extending the time for payment" will be difficult if not impossible in the context of the audit of an estate. If the expenses are actually incurred, in good faith, they should be deductible. Perhaps the Treasury Department is aware of cases in which litigation has been intentionally prolonged for the purpose of generating additional expenses but surely such instances are rare.

8. <u>Claims and Counter-claims</u>. Prop. Reg. § 20.2053-4

Many estates will have claims against others and claims by others against the decedent. Under the approach of the Proposed Regulations, the two types of claims are handled differently. Claims <u>by</u> an estate are valued as an asset, on the basis of a date of death snapshot approach. In contrast, under the look-back approach used by the Proposed Regulations, claims <u>against</u> an estate must actually be paid (among other requirements) in order to be deducted.

Especially in instances where the claims against the estate are inextricably related to claims by the estate, the disparate approaches taken could result in inconsistent and potentially highly inequitable results. In particular, the differing treatment of claims and counter-claims in the same litigation could lead to incongruous results. The College believes this issue deserves a very serious review.

To illustrate the potential inconsistent treatment consider the following example. Prior to death a decedent filed a multi-million dollar lawsuit against a defendant which in turn filed a multi-million dollar counter-claim against the decedent. Both the claim and counter-claim had sufficient merit to withstand a motion for summary judgment and the case advanced. The claim by the estate is valued at $1,000,000 under a date of death snapshot approach, taking into account all of the facts and circumstances related to the merits of that claim alone without regard to any consideration of the claim against the estate. Ultimately the parties agreed to settle the case by having the parties dismiss their respective claims and counter-claims. Under the Proposed Regulations, the estate would include $1,000,000 in the gross estate without an offsetting deduction under section 2053 even though the claim and counter-claim had equal value as evidenced by the terms of the arms-length settlement.

The College believes that the final regulations should allow claims and counter-claims, as in the illustration above, to be netted. For example, the estate could be allowed a section 2053 deduction to the extent that the net amount received by the estate in settlement of its claim is less than the $1,000,000 value determined under the date of death snapshot approach. Another approach would be to allow the counter-claim against the estate to be considered when valuing the claim by the estate.

9. Definition of Bona Fide. Prop. Reg. § 20.2053-4

> (a) In general. (1) For purposes of this section, liabilities imposed by law or arising out of contracts or torts are deductible if they meet the requirements set forth in § 20.2053-1 and this section. Except as provided in paragraph (b) of this section, the amounts that may be deducted as claims against a decedent's estate are limited to amounts for legitimate and bona fide claims that --
>
> (i) Represent personal obligations of the decedent existing at the time of the decedent's death;
>
> (ii) Are enforceable against the decedent's estate at the time of payment; and
>
> (iii) Are actually paid by the estate in settlement of the claim.

The phrase "legitimate and bona fide claims" should be replaced by "bona fide claims." As noted earlier, a definition of "bona fide" would be helpful. A claim that is bona fide but not also legitimate is difficult to imagine; thus the term "legitimate" appears to be superfluous.

10. Effect of Post-Mortem Events. Prop. Reg. § 20.2053-4(a)

> (2) Events occurring after the date of a decedent's death shall be considered when determining the amount deductible against a decedent's estate.

The Proposed Regulations should be expanded to make clear that the government is bound by the same analysis as an estate. That is, subsequent events, such as the payment of larger than expected claims that meet the requirements of Prop. Reg. § 20.2053-4(a)(1), will be deductible under section 2053 regardless of the status of the matter as of the date of death.

11. Contested Claims. Prop. Reg. § 20.2053-4(b)

> (2) Contested claims. No deduction may be taken on an estate tax return for a claim against the decedent's estate to the extent the estate is contesting the decedent's liability. However, see § 20.2053-1(b)(4) relating to estimated amounts.

The Proposed Regulations should provide that a protective claim may be made for such claims. As noted in Comment 4, a protective claim ought not to be required to contain information that would help an opposing party in litigation.

12. Claims Against Multiple Parties. Prop. Reg. § 20.2053-4(b)

> (3) Claims against multiple parties. If the decedent or the decedent's estate is one of two or more parties against whom the claim is being asserted, the estate may only deduct the portion of the total claim due from and paid by the estate, reduced by the total of any reimbursement received from another party, insurance, or otherwise. The estate's deductible portion will also be reduced by the amount or contribution the estate could have collected from another party or an insurer but which the estate declines or fails to attempt to collect. If, however, the estate establishes that the burden of necessary collection efforts would have outweighed the benefit from those efforts, the potential reimbursement will not reduce the estate's deductible portion of the total claim. If the estate establishes that the party from whom a potential reimbursement could be collected could only pay a portion of the potential reimbursement, then only that portion that could reasonably have been expected to be collected will reduce the estate's deductible portion of the total claim.

As noted in Comment 5, a procedure by which an executor could establish that there are no available reimbursements from other parties or insurance would be helpful. Here the need is even greater. In many instances an estate will have potential reimbursement rights against other parties but will not want to pursue those rights, sometimes due to expense but for other reasons some related to actual litigation — difficulty in proving the case — and some related to more traditional estate matters — embarrassment to the decedent's family, the need for finality, and so forth. If an estate fails to pursue a bona fide reimbursement the amount of that potential reimbursement should not be deductible, but the estate should have ample discretion in making that determination. Further, the estate should be able to obtain as part of the estate tax proceeding a determination that certain amounts are not deductible unless an action for reimbursement is pursued (in which case a protective claim would be filed).

13. Recurring Payments. Prop. Reg. § 20.2053-4(b)

> (7) Recurring payments -- (i) Non-Contingent obligations. If a decedent is obligated to make recurring payments on an enforceable and certain claim that are not subject to a contingency and if the payments will continue for a period that will likely extend beyond the final determination of the estate tax liability, the obligation may be deducted as an estimated amount using the rules in § 20.2053-1. The amount deductible is the present value of the payments on the decedent's date of death as determined under § 20.2031-7(d). See § § 20.7520-1 through 20.7520-4. If there is a reasonable likelihood that full satisfaction of the liability will not be made, then the obligation will be deemed to be subject to a contingency for purposes of this section.
>
> (ii) Contingent obligations. If a decedent has a recurring obligation to pay an enforceable and certain claim, but the decedent's obligation is subject to a contingency or is otherwise not described in paragraph (b)(7)(i) of this section,

> the estate's deduction is limited to amounts actually paid by the estate in satisfaction of the claim.
>
> (iii) Purchase of commercial annuity to satisfy recurring obligation to pay. If a decedent has a recurring obligation (whether or not contingent) to pay an enforceable and certain claim and the estate purchases a commercial annuity from an unrelated dealer in commercial annuities in an arms-length transaction to satisfy the obligation, the amount deductible by the estate is the sum of --
>
>> (A) The amount paid for the commercial annuity; and
>>
>> (B) Any amount actually paid to the claimant by the estate prior to the purchase of the commercial annuity.

Clarification of what is a recurring payment would be helpful in order to understand when a present value calculation is required. Suppose, for example, an estate settles a lawsuit against a decedent by agreeing to pay $100,000 a year for ten years to plaintiff. All other requirements for deductibility are met. May the estate deduct $1,000,000 ($100,000 X 10) or may the estate deduct only the present value of the payments? Would the result have been different if the decedent had settled the lawsuit a month before death, so that the estate had the identical obligation, namely to pay $100,000 a year for 10 years?

Conclusion

These comments were prepared by Turney P. Berry, M. Patricia Culler, Barbara Ann Dalvano, John H. Draneas, and Charles A. Redd as representatives of the Estate and Gift Tax Committee and were approved by the Executive Committee of the College. We appreciate this opportunity to comment on the Proposed Regulations and would be pleased to offer additional comments if desired.

Respectfully submitted,

Daniel H. Markstein, III
President