

# “Don’t Undermine Your 709”

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# Beth Shapiro Kaufman

Beth Shapiro Kaufman is a Member in Caplin & Drysdale's Washington, D.C., office. She was President of the Firm from 2015 to 2018 and continues as an active member of the firm's Board of Directors.

## Awards & Rankings

- *Chambers High Net Worth Guide*, Private Wealth Law, D.C. and USA: Eastern Region, 2016-Present
- *Chambers USA*, 2010-2016
- *Best Lawyers in America*, Women in the Law, 2016; D.C. Trusts and Estates Lawyer of the Year, 2016 and 2018; Listed 2003-Present
- *Expert Guides' World's Leading Women in Business Law*, Leading Practitioner, 2014; Listed, 2013-Present
- *The Legal 500*, Recommended, 2014, 2015, 2020
- *Super Lawyers*, Washington, D.C., 2008-Present
- *Northern Virginia Magazine*, Top Lawyer, 2016
- *Fortune Magazine*, Women Leaders in the Law, 2014
- *The Washingtonian*, Top Money Advisers, 2014; Top Wealth Advisers, 2016; Best Financial Advisers, 2019; Top Lawyers, 2007-Present
- *The Washington Post*, Among the Top Attorneys in D.C., 2014
- *Martindale-Hubbell*® AV® Preeminent™

# Agenda:

- Who Needs to File
- Annual Exclusion Gifts
- Special Rules for 529 Plan Contributions
- Special Rules for Gift Splitting
- Making QTIP Election
- Claiming Valuation Discounts
- Adequate Disclosure
- Whether to Disclose Non-Gifts
- Reporting Gifts When a Defined Value Clause is Used
- Properly Completing Schedule A
- Keeping Track of Prior Gifts and Use of GST Exemption
- Gifts By Non-Resident Non-Citizens
- Q&A



# 1. Who Needs to File – Code Section 6019

Any individual who in any calendar year makes any transfer by gift other than—

**(1)** a transfer which under subsection (b) or (e) of section 2503 is not to be included in the total amount of gifts for such year,

**(2)** a transfer of an interest with respect to which a deduction is allowed under section 2523, or

**(3)** a transfer with respect to which a deduction is allowed under section 2522 but only if—

**(A)(i)** such transfer is of the donor's entire interest in the property transferred, and

**(ii)** no other interest in such property is or has been transferred (for less than adequate and full consideration in money or money's worth) from the donor to a person, or for a use, not described in subsection (a) or (b) of section 2522, or

**(B)** such transfer is described in section 2522(d),

shall make a return for such year with respect to the gift tax imposed by subtitle B.

# What needs to be reported

Once filing obligation exists, **ALL** gifts must be reported

- Includes annual exclusion gifts
- Includes marital gifts
- Includes charitable gifts



# Other Reasons to File

- Gift-splitting election
- QTIP election
- QDOT election
- Election with respect to 529 Plan contribution
- GST: allocate exemption, opt into or out of automatic allocation
- To make required disclosures (e.g. disclosure of a non-gift transaction)
- To get the statute of limitations running



## 2. Annual Exclusion Gifts

- Count each donee once and only once
- Trusts don't get an annual exclusion, only people do
- Include all annual exclusion gifts on the return

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### Part 4—Taxable Gift Reconciliation

1	Total value of gifts of donor. Add totals from column H of Parts 1, 2, and 3 . . . . .	1	
2	Total annual exclusions for gifts listed on line 1 (see instructions) . . . . .	2	
3	Total included amount of gifts. Subtract line 2 from line 1 . . . . .	3	

# The GST “Annual Exclusion” Is Different (Code section 2642(c))

- Direct skips that are nontaxable gifts (i.e. fall under the gift tax annual exclusion, or the exception for direct payment of tuition or medical expenses) get a zero inclusion ratio
- This rule does not apply to transfers in trust unless:
  - during the life of such individual, no portion of the corpus or income of the trust may be distributed to (or for the benefit of) any person other than such individual, and
  - if the trust does not terminate before the individual dies, the assets of such trust will be includible in the gross estate of such individual.



### 3. Special Rules for 529 Plan Contributions

Code section 529(c)(2)(B): “If the aggregate amount of contributions described in subparagraph (A) during the calendar year by a donor exceeds the limitation for such year under section 2503(b), such aggregate amount shall, at the election of the donor, be taken into account for purposes of such section ratably over the 5-year period beginning with such calendar year.”

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**SCHEDULE A** Computation of Taxable Gifts (Including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If “Yes,” attach explanation . . . . . Yes  No

B  ◀ Check here if you elect under section 529(c)(2)(B) to treat any transfers made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

## 4. Special Rules for Gift Splitting

- Who can split:
  - Both spouses must be U.S. citizens or residents
  - Must be married at the time of the gift
    - Cannot be married to anyone else during the remainder of the calendar year
- Election on gift tax return required
- Consent once given applies to all gifts during the taxable year (other than gifts to the consenting spouse), even those not disclosed on the return



- Gift Splitting election made by checking box on line 12
- Consenting spouse must sign (executor may sign if spouse deceased)

<b>12 Gifts by husband or wife to third parties.</b> Do you consent to have the gifts (including generation-skipping transfers) made by you and by your spouse to third parties during the calendar year considered as made one-half by each of you? (See instructions.) (If the answer is "Yes," the following information must be furnished and your spouse must sign the consent shown below. <b>If the answer is "No," skip lines 13-18.</b> ) . . . . .			
<b>13</b> Name of consenting spouse	<b>14</b> SSN		
<b>15</b> Were you married to one another during the entire calendar year? See instructions . . . . .			
<b>16</b> If line 15 is "No," check whether <input type="checkbox"/> married <input type="checkbox"/> divorced or <input type="checkbox"/> widowed/deceased, and give date. See instructions ▶			
<b>17</b> Will a gift tax return for this year be filed by your spouse? If "Yes," mail both returns in the same envelope . . . . .			
<b>18 Consent of Spouse.</b> I consent to have the gifts (and generation-skipping transfers) made by me and by my spouse to third parties during the calendar year considered as made one-half by each of us. We are both aware of the joint and several liability for tax created by the execution of this consent.			
Consenting spouse's signature ▶		Date ▶	

- Election can be made on a late gift tax return, but only if that is the first gift tax return filed for the year
- Election becomes irrevocable on the due date of the return

# Gift Splitting Mechanics

# Gift Splitting When Spouse Is a Beneficiary

- If a gift is made to the donor's spouse, that gift is not split (even if an election is made)
- If a gift is in part to the spouse and in part to third parties, gift splitting is effective with respect to the interest transferred to third parties only insofar as such interest is "ascertainable" at the time of the gift and hence "severable" from the interest transferred to the spouse. Treas. Reg. §25.2513-1(b)(4).



# GST Gift-Splitting Rule is NOT the Same

- In general, a gift-splitting election is respected for GST purposes. Code section 2652(a)(2).
  - The consenting spouse is the “transferor” of one-half for GST purposes
- BUT GST rule differs if part of the gift is not split because the spouse is a recipient.
  - Under regulations, if the gift is split at all, it is split 50/50 for GST purposes. Treas. Reg. §26.2652-1(a)(4).
- Practice tip: Add an explanatory page if the gift splitting is complicated

# 5. Making the QTIP Election

## Part 4—Taxable Gift Reconciliation

<b>1</b>	Total value of gifts of donor. Add totals from column H of Parts 1, 2, and 3 . . . . .	<b>1</b>	
<b>2</b>	Total annual exclusions for gifts listed on line 1 (see instructions) . . . . .	<b>2</b>	
<b>3</b>	Total included amount of gifts. Subtract line 2 from line 1 . . . . .	<b>3</b>	
<b>Deductions</b> (see instructions)			
<b>4</b>	Gifts of interests to spouse for which a marital deduction will be claimed, based on item numbers _____ of Schedule A . . . . .	<b>4</b>	
<b>5</b>	Exclusions attributable to gifts on line 4 . . . . .	<b>5</b>	
<b>6</b>	Marital deduction. Subtract line 5 from line 4 . . . . .	<b>6</b>	
<b>7</b>	Charitable deduction, based on item numbers _____ less exclusions . . . . .	<b>7</b>	
<b>8</b>	Total deductions. Add lines 6 and 7 . . . . .	<b>8</b>	
<b>9</b>	Subtract line 8 from line 3 . . . . .	<b>9</b>	
<b>10</b>	Generation-skipping transfer taxes payable with this Form 709 (from Schedule D, Part 3, col. G, total) . . . . .	<b>10</b>	
<b>11</b>	<b>Taxable gifts.</b> Add lines 9 and 10. Enter here and on page 1, Part 2—Tax Computation, line 1 . . . . .	<b>11</b>	

### Terminable Interest (QTIP) Marital Deduction. (See instructions for Schedule A, Part 4, line 4.)

If a trust (or other property) meets the requirements of qualified terminable interest property under section 2523(f), and:

- a. The trust (or other property) is listed on Schedule A; and
- b. The value of the trust (or other property) is entered in whole or in part as a deduction on Schedule A, Part 4, line 4, then the donor shall be deemed to have made an election to have such trust (or other property) treated as qualified terminable interest property under section 2523(f).

If less than the entire value of the trust (or other property) that the donor has included in Parts 1 and 3 of Schedule A is entered as a deduction on line 4, the donor shall be considered to have made an election only as to a fraction of the trust (or other property). The numerator of this fraction is equal to the amount of the trust (or other property) deducted on Schedule A, Part 4, line 6. The denominator is equal to the total value of the trust (or other property) listed in Parts 1 and 3 of Schedule A.

If you make the QTIP election, the terminable interest property involved will be included in your spouse's gross estate upon his or her death (section 2044). See instructions for line 4 of Schedule A. If your spouse disposes (by gift or otherwise) of all or part of the qualifying life income interest, he or she will be considered to have made a transfer of the entire property that is subject to the gift tax. See *Transfer of Certain Life Estates Received From Spouse* in the instructions.

# 6. Claiming Valuation Discounts

- Checkbox at the top of page 2 asks about valuation discounts
- No statutory or regulatory authority for this question
- Explanation will be necessary for adequate disclosure anyway

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**SCHEDULE A** Computation of Taxable Gifts (Including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If "Yes," attach explanation . . . . . Yes  No

B  ◀ Check here if you elect under section 529(c)(2)(B) to treat any transfers made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

# 7. Adequate Disclosure

- Since 1997, SOL runs on a gift by gift basis.
- In order to start the SOL, a gift must be “adequately disclosed” on the return
- Code section 6501(c)(9): If a gift is not “shown on [a] return, any tax imposed by chapter 12 on such gift may be assessed . . . at any time.” Does “not apply to any item which is disclosed in such return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature of such item.”

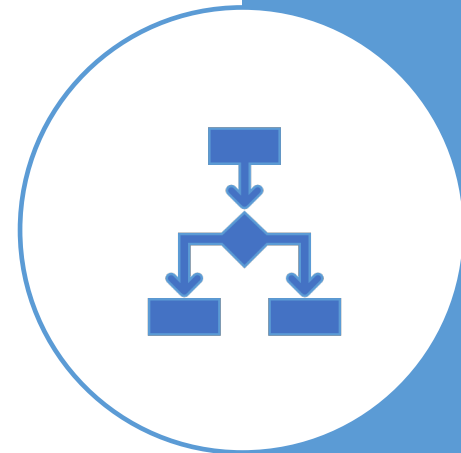


# Adequate Disclosure Regulations

- Adequate disclosure regulations give a safe harbor
- Required reading!
- Practice tip: Use regulation as a checklist
- In lieu of detailed information, can provide full appraisal that satisfies requirements in regulations
- IRS exploits foot faults to assess gift tax after three years

## 8. Whether to Disclose Non-Gifts

- Regulations allow for disclosure of non-gifts to trigger commencement of period of limitations
- But should you?
- Practitioners disagree
  - Risk of audit vs chance at certainty
  - Low audit rate of gift tax returns (under 1% of returns filed in each of the last 10 years)
  - Most will report full transaction if filing to report “seed money”



## 9. Reporting Gifts When a Defined Value Clause is Used

- Use of defined value clauses is popular
- Key to report consistent with your clause
- If gift of FLLC interests with a value of \$1,000,000 don't report that as 100 units just because your appraisal values them at \$1,000,000!
- If needed, attached explanation
- Make adequate disclosure “to apprise the Secretary of the nature of such item”



# 10. Properly Completing Schedule A

- Schedule A is divided into three parts
  - Part 1: Gifts Subject Only to Gift Tax
  - Part 2: Direct Skips
  - Part 3: Indirect skips and Other Transfers in Trust
- Form sets up different GST elections for the different categories
  - 2632(b) election out for direct skips
  - 2632(c) elections for indirect skips
- Proper categorization will reduce errors

# What Goes Where: Examples

- Part 1: Gifts subject only to gift tax – cannot possibly be subject to GST
  - Outright gift to child
  - Gift to GPOA trust for child
  - Gift to charity
- Part 2: Direct skips – the GST definition
  - Outright gift to grandchild
  - Gift to a trust that is itself a skip person
- Part 3: Indirect skips and other transfers in trust
  - Includes every transfer in trust that is not a direct skip or subject only to gift tax (doesn't say anything about whether or not it gets automatic allocation of GST)



# GST Elections Sow Confusion

- Direct skips get automatic allocation
  - Unless taxpayer elects out under 2632(b)
- Indirect skips have multiple possible elections under 2632(c) for the taxpayer
  - Elect out of automatic allocation to a “GST trust” for the transfer reported on the return
  - Elect out of automatic allocation to any or all future transfers to a particular GST trust
  - Elect to treat any trust as a GST trust with respect to any or all transfers whether or not trust falls within the statutory definition

# 2632(c) Elections

- Every 2632(c) election requires an attachment. “Attach a statement to Form 709 that describes the election you are making and clearly identifies the trusts and/or transfers to which the election applies.”
- If you err by not making an election, 9100 relief is available (but costly)
- If you err in making an election, you are out of luck.

# 11. Keeping Track of Prior Gifts and Use of GST Exemption

**SCHEDULE B** Gifts From Prior Periods

If you answered "Yes" on line 11a of page 1, Part 1, see the instructions for completing Schedule B. If you answered "No," skip to the Tax Computation on page 1 (or Schedule C or D, if applicable). Complete Schedule A before beginning Schedule B. See instructions for recalculation of the column C amounts. Attach calculations.

A Calendar year or calendar quarter (see instructions)	B Internal Revenue office where prior return was filed	C Amount of applicable credit (unified credit) against gift tax for periods after December 31, 1976	D Amount of specific exemption for prior periods ending before January 1, 1977	E Amount of taxable gifts
<b>1</b> Totals for prior periods . . . . .		<b>1</b>		
<b>2</b> Amount, if any, by which total specific exemption, line 1, column D, is more than \$30,000 . . . . .			<b>2</b>	
<b>3</b> Total amount of taxable gifts for prior periods. Add amount on line 1, column E, and amount, if any, on line 2. Enter here and on page 1, Part 2—Tax Computation, line 2 . . . . .			<b>3</b>	

*(If more space is needed, attach additional statements.)* Form **709** (2019)



# Using DSUE

- A surviving spouse uses DSUE before using her own lifetime exemption (see question 19)
- Schedule C is where the amount of remaining DSUE is tracked

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**SCHEDULE C Deceased Spousal Unused Exclusion (DSUE) Amount and Restored Exclusion**

Provide the following information to determine the DSUE amount and applicable credit received from prior spouses. Complete Schedule A before beginning Schedule C.

A Name of deceased spouse (dates of death after December 31, 2010, only)	B Date of death	C Portability election made?		D If "Yes," DSUE amount received from spouse	E DSUE amount applied by donor to lifetime gifts (list current and prior gifts)	F Date of gift(s) (enter as mm/dd/yy for Part 1 and as yyyy for Part 2)	
		Yes	No				
<b>Part 1—DSUE RECEIVED FROM LAST DECEASED SPOUSE</b>							
<b>Part 2—DSUE RECEIVED FROM PREDECEASED SPOUSE(S)</b>							
<b>TOTAL (for all DSUE amounts applied from column E for Part 1 and Part 2)</b>							
<b>1</b>	Donor's basic exclusion amount (see instructions)					<b>1</b>	
<b>2</b>	Total from column E, Parts 1 and 2					<b>2</b>	
<b>3</b>	Restored Exclusion Amount (see instructions)					<b>3</b>	
<b>4</b>	Add lines 1, 2, and 3					<b>4</b>	
<b>5</b>	Applicable credit on amount in line 4 (see <i>Table for Computing Gift Tax</i> in the instructions). Enter here and on line 7, Part 2—Tax Computation					<b>5</b>	

# GST Reconciliation

## Part 2—GST Exemption Reconciliation (Section 2631) and Section 2652(a)(3) Election

Check here  if you are making a section 2652(a)(3) (special QTIP) election. See instructions.

Enter the item numbers from Schedule A of the gifts for which you are making this election  \_\_\_\_\_

1	Maximum allowable exemption (see instructions)	1
2	Total exemption used for periods before filing this return	2
3	Exemption available for this return. Subtract line 2 from line 1	3
4	Exemption claimed on this return from Part 3, column C, total below	4
5	Automatic allocation of exemption to transfers reported on Schedule A, Part 3. To opt out of the automatic allocation rules, you must attach an "Election Out" statement. See instructions	5
6	Exemption allocated to transfers not shown on line 4 or line 5 above. <b>You must attach a "Notice of Allocation."</b> See instructions	6
7	Add lines 4, 5, and 6	7
8	Exemption available for future transfers. Subtract line 7 from line 3	8

## 12. Gifts By Non-Resident Non-Citizens

- No Form 709-NA
- NRNC fills out Form 709
- Includes only gifts of U.S. situs property subject to gift tax
  - U.S. situs real property
  - Tangible property with a U.S. situs
- Note categories of assets subject to estate tax are broader, so gifts are preferred



# Conclusion

When in doubt:

- Read the Code!
- Read the Regulations!
- Read the Instructions!



## Q&A

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