Basis Consistency Temporary and Proposed Regulations

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Temporary and Proposed Regulations Provide Guidance Regarding Basis Consistency and Reporting

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SYNOPSIS

Temporary and proposed regulations provide additional guidance regarding the basis consistency and information reporting requirements of new §§1014(f) and 6035. Some of the highlights and surprises include the following:

- The final value for estate tax purposes sets the *initial* basis; normal post-death basis adjustments are still applicable;
- For property subject to non-recourse debt, the basis is the gross value of the property, not just the net value reported on the estate return;
- The reporting requirement does not apply to estates that are not required to file estate tax returns but do so merely to make the portability election;
- Property that qualifies for the marital or charitable deduction is not subject to the basis consistency requirement, but is subject to the reporting requirements;
- Tangible personal property that does not have a marked artistic or intrinsic value over $3,000 is not subject to the basis consistency or reporting requirements;
- After-discovered or omitted property gets a basis of zero if the property is not reported on an estate tax return before the period of limitations on assessments has expired;
- The Form 8971 and Schedules A to beneficiaries can omit cash, IRD, tangible personal property (as described above), and property sold before the information reports are due;
- For bequests to a trust, estate or entity the Schedules A are given to the trustee, executor or entity (not the trust beneficiaries);
- For life estates, Schedules A must be sent to the life tenant and presumptive remainderman (and if the initial remainderman dies before the life tenant, the executor apparently must send supplemental reports to the IRS and to the new remainderman);
- If the executor has not determined what property will be distributed to a beneficiary when the information report is due, all property that could be used to satisfy the bequest must be included on the Schedule A to that beneficiary (and the executor does not have to send supplemental reports to the IRS and to that beneficiary after the bequest is funded);
- The executor must file a supplemental Form 8971 with the IRS and send supplemental Schedules A to beneficiaries if any previously reported information is incorrect or incomplete (such as if the final estate tax value is changed), but a supplement is not needed for inconsequential errors or omissions;
- If a recipient of an asset in the gross estate makes a subsequent gift or distribution to a "related transferee" (which, for some strange reason, includes a grantor trust but not a non-grantor trust for a related party) the recipient must file a Schedule A with the IRS and transferee reporting the change in ownership and final estate tax value of the property; and
- The Form 8971 and Schedules A to each beneficiary are due 30 days after the earlier of the due date or the date the estate tax return is actually filed (as required by the statute); the proposed regulations do not adopt the relaxation of the due date in the Instructions to Form 8971 saying that if the estate tax return is filed late, the information reports are not due until 30 days after the date the return is actually filed.

Highlights

Temporary and proposed regulations regarding the basis consistency and information reporting requirements of new §§1014(f) and 6035 were published in the Federal Register on March 4, 2016.

Highlights of some of the provisions in the temporary and proposed regulations are summarized below.

1. **Transitional Relief Regarding Initial Time for Filing**. Temporary regulations provide that persons required to file an information statement under §6035(a)(1) or (a)(2) before March 31, 2016 "need not do so" until March 31, 2016. Perhaps this is not a formal "extension" of a statutory filing deadline, but it reflects Notices 2015-57 and 2016-19, which provide relief in the time for filing reports initially to February 29, 2016, and then to March 31, 2016.

2. **Post Death Adjustments**. Section 1014(f) states that the basis of property acquired from a decedent "shall not exceed" the finally determined estate tax value of the property. Post-death adjustments to a property's basis under other Code provisions are still made—the estate tax value of property merely becomes the upper limit on the *initial* basis of the property after the decedent's death. Prop. Reg. §1.1014-10(a)(2).

   Property Encumbered by Debt. Post-death payments on debt secured by property in the gross estate do not result in an adjustment to the property's basis because "[t]he existence of recourse or non-recourse debt secured by property at the time of the decedent's death does not affect the property's basis, whether the gross value of the property and the outstanding debt are reported separately on the estate tax return or the net value of the property is reported." Prop. Reg. §§1.1014-10(a)(2), 1.1014-10(e) Ex. 4. [Treas. Reg. §20.2053-7 provides that if the decedent's estate is not liable for the debt (i.e., if it is non-recourse debt), "only the value of the equity of redemption (or the value of the property, less the mortgage or indebtedness) need be returned as part of the value of the gross estate." In light of that regulation, planners have been uncertain as to whether basis would be allowed for the full gross value of estate property that is subject to non-recourse indebtedness. The proposed regulation clarifies this issue.]

   [Schedule A will be confusing for assets subject to non-recourse debt if the net value is reported on the estate tax return. Column E on Schedule A entitled "Estate Tax Value" might suggest that the net value reported on the estate tax return should be listed (the Form 8971 Instructions say to "list the value reported on the Form 706" in this column), but the proposed regulations indicate that the beneficiary's basis will be the gross value of the asset not reduced by the non-recourse debt.]

3. **Property Subject to Consistency Requirement**. The basis consistency requirement applies to property includable in a decedent's gross estate under §§2031 and 2106 that generates federal estate tax in excess of allowable credits (other than a credit for a prepayment of the tax). Prop. Reg. §1.1014-10(b)(1).

   Marital or Charitable Deduction Property. Section 1014(f)(2) states that the basis consistency rule only applies to property whose inclusion in the gross estate increased the liability for estate tax (reduced by allowable credits). (This exception for property that does not increase the estate tax liability only applies for the basis consistency rule; this exception does not extend to the information reporting requirements.) Proposed regulations clarify that property that qualifies for an estate tax charitable or marital

deduction under §§2055, 2056, or 2056A "does not generate a tax liability under chapter 11 and therefore is excluded from the property subject to the consistency requirement." Therefore, even if the estate pays estate tax, any property passing to a surviving spouse or charity that qualifies for a marital or charitable deduction is excluded from the basis consistency requirement. Prop. Reg. §1.1014-10(b)(2).

Certain Tangible Personal Property. The proposed regulations add an exclusion (not included in the statute) for tangible personal property for which an appraisal is not required under Regulation §20.2031-6(b), which requires an appraisal for "household and personal effects articles having marked artistic or intrinsic value of a total value in excess of $3,000 (e.g., jewelry, furs, silverware, paintings, etchings, engravings, antiques, books, statuary vases, oriental rugs, coin or stamp collections)" Prop. Reg. §1.1014-10(b)(2). An example in the proposed regulations of an analogous exception under the information reporting rules hints that this exception applies for any *individual* asset that is under $3,000. Prop. Reg. §1.6035-1(b)(2)Ex.1. However, Reg. §20.2031-6(b) applies if the *"total value*" of articles "having marked artistic or intrinsic value" exceeds $3,000. The Instructions to Form 706 relax this appraisal requirement somewhat, though, by requiring an appraisal for "works of art or items with collectible value (for example, jewelry, furs, silverware, books, statuary, vases, oriental rugs, coin or stamp collections) … [i]f any item or collection of *similar items* is valued at more than $3,000." (emphasis added). This suggests, for example, that jewelry and furs would not be aggregated for purposes of the $3,000 test amount.

All Property Other Than Exceptions. If the estate must pay any estate tax, all property in the gross estate, other than marital or charitable deduction property or tangible personal property for which an appraisal is not required, is subject to the basis consistency requirement. If the estate pays no federal estate tax, none of the estate property is subject to basis consistency. Prop. Reg. §1.1014-10(b)(3).

4. **Final Value**. The proposed regulations address how the "final" estate tax value is determined. Prop. Reg. §1.1014-10(c)(1). The "final value" is the value reported on the estate tax return once the period of limitations on assessment has expired, or the amount determined by the IRS once it can no longer be contested, or the amount determined in an agreement binding on all parties, or the value determined by a court once the court's determination is final. Until the final value of property is determined, the recipient of the property may not claim a basis for that property in excess of the value reported on the information statement (i.e., the Schedule A) given to the recipient. If the final value, once it is determined, is less than the reported value, the recipient may not rely on the value listed in the initial statement and may have a deficiency and underpayment attributable to the difference. Prop. Reg. §1.1014-10(c)(2).

5. **After-Discovered or Omitted Property**. If property is discovered after the estate tax return has been filed or is otherwise omitted from that return, special rules apply. If the property is later reported on a supplemental estate tax return before the period of limitation on assessment of tax expires, the normal "final value" rules apply. Prop. Reg. §1.1014-10(c)(3)(i)(A). In an extension of the basis consistency statute, however, if the after-discovered or omitted property is not reported on a supplemental estate tax return before the limitation period expires (generally three years from the filing date, §6501(a)), the basis of such property is *zero*. Prop. Reg. §1.1014-10(c)(3)(i)(B). [Planners generally believe that no duty exists to report after-discovered property if the estate tax return was filed in good faith. *See* David Pratt & George Karibjanian, *Filing a Supplemental Estate Tax*

Return After Probate Litigation, EST. PL. (Sept. 2009). If a supplemental estate tax return is not filed reporting the additional asset, however, the recipient may not take the position that the basis is the fair market value at the date of death even though the property was acquired from a decedent (despite the language of §1014(a) which says that property "acquired from a decedent" has a basis equal to the fair market value of the property at the date of death). Accordingly, if a preparer determines that no obligation to amend a return exists to report omitted property, the failure to report the property may result in a 40% estate tax savings, but that savings may be offset by a 23.8% federal capital gains tax (plus any state capital gains tax) or an even higher income tax attributable to the inability to depreciate the property. If the recipient of the after-discovered asset is not the party responsible for paying estate tax with respect to that asset, the executor may be put in an inherent conflict situation; the party who bears estate taxes will not want the property reported but the party who receives the asset will want it reported to have a basis equal to the date of death value of the asset. [This rule means that after-discovered *cash* might have a basis of zero, which raises interesting issues regarding the effect of cash having a zero basis—is the use of the cash to buy something treated as a "sale or exchange" of the cash, thus generating capital gain?]

6. **Executor**. For purposes of knowing who must file information reports under §6035, the term "executor" is defined broadly to mean the appointed executor, or if none is appointed, any person in possession of property (incorporating §2203), or any other beneficiary required to file a return under §6018(b). Prop. Reg. §§1.1014-10(d), 1.6035-1(g)(1).

7. **Requirement to Provide Information Statement**. The "executor" (see immediately above) who is required to file an estate tax return under §6018(a) (i.e., if the size of the gross estate plus adjusted taxable gifts exceeds the basic exclusion amount), must provide information statements to the IRS (on Form 8971) and the recipients of property that was included in the gross estate (with several exceptions described below in Item 8). Prop. Reg. §1.6035-1(g)(2)-(3). The preamble says this means that Form 8971 and all Schedules A must be provided to the IRS and Schedules A must be provided to recipients.

   Portability Returns and Other Returns Filed But Not Required. The reporting requirement does not apply if the executor is not required to file an estate tax return but does so anyway (such as to make a GST exemption allocation or portability election, or to file a protective return in case an asset value is later determined to cause a return to be required). Prop. Reg. §1.6035-1(a)(2).

8. **What Property Must be Reported**? The reporting requirement generally applies to all property on the estate tax return (or property with basis determined in whole or in part with reference to property in the gross estate, such as like-kind exchange property). For a non-resident alien, this includes only property subject to the U.S. estate tax. Only the decedent's one-half of community property is subject to the reporting requirement (even though both community halves get a basis adjustment under §1014(b)(6)).

   The proposed regulations provide four exceptions: (i) csh other than coins or paper bills with a numismatic value [query, does "cash" include amounts in checking accounts, bank accounts, money market funds, or certificates of deposit?]; (ii) income in respect of a decedent assets; (iii) tangible personal property for which an appraisal is not required under Reg. §20.2031-6(b); and (iv) property in the gross estate that has been sold by the

estate (and therefore not distributed to the beneficiary) in a transaction in which capital gain or loss is recognized. Prop. Reg. §1.6035-1(b)(1). These exceptions are very important. The executor does not have to give reports to the IRS or recipients about any of those four types of assets that are distributed to estate recipients.

The executor should not assume that any amounts in IRAs or retirement plans are not reportable. Non-deductible contributions may have been made to the IRA or plan, and a portion of the IRA or plan may not be income in respect of a decedent.

No exception exists for property includable in the gross estate under the "string" statutes of §§ 2035-2042 (including assets in a funded revocable trust). The executor is required to provide information to the IRS and recipients of assets included in the gross estate under those sections even though the executor may not have any control over those assets. (If a trust holds those assets, the information would be given to the trustee.) However, adjustments to the gross estate under §2035(b) for gift tax on gifts made within three years of the date of death do not reflect assets passing to a beneficiary and therefore would not seem to be reportable to the IRS or any beneficiary.

9. **Who Are "Beneficiaries" Who Must Receive Reports With Respect to Reportable Property**? Beneficiaries generally include any person receiving reportable property, including the executor who is also a beneficiary. Prop. Reg. §1.6035-1(c)(1). (No exception applies for beneficiaries who are surviving spouses or charities to whom bequests qualify for the marital or charitable deduction. Even though they are not subject to the basis consistency limitation, as discussed above in Item 3, they must still receive the required information under the reporting requirements.)

Life Estates. A special complicating rule applies for life estates. Beneficiaries who receive reports include the life tenant and the remainderman(men) who would receive property if the life tenant were to die immediately after the decedent. If a "contingent beneficiary" changes (presumably because a presumptive remainderman dies before the life tenant), the executor must do a supplemental reporting to the IRS and new remainderman. Prop. Reg. §1.6035-1(c)(1). This could create a continuing duty of the executor to give reports years in the future. What if the estate has been closed and the executor is discharged—does the life tenant become the "executor" for reporting purposes? (The word "not" appears to have been inadvertently omitted from the proposed regulation; the regulation apparently should say the beneficiary of a contingent interest is "not" a beneficiary unless the contingency occurs before the Form 8971 is filed.)

Trusts or Estates. If the beneficiary is a trust or another estate, the executor gives the information to the trustee or executor—not to the beneficiaries of that trust or estate. Prop. Reg. §1.6035-1(c)(2). (See Item 12 below as to whether additional reporting requirements may apply when that trust or estate distributes the property.)

Undistributed Property (Undetermined Beneficiary). If the executor has not decided what property will be distributed to each beneficiary by the due date of the information statement (30 days after the estate tax return due date, as discussed below), "the executor must report on the Statement for each such beneficiary all of the property that the executor could use to satisfy that beneficiary's interest." Prop. Reg. §1.6035-1(c)(3). In effect, "mini-706s" will have to be given to each such beneficiary listing all remaining property in the gross estate, other than cash, IRD, or certain tangible personal property. The preamble acknowledges that this will result in duplicate reporting of assets on multiple Schedules A. If the executor has "determined" what property will be distributed

to a beneficiary but has simply not made the distribution when the information statement is due, this special provision would not literally apply, and presumably the executor would list the property that the executor has determined will be used to satisfy that beneficiary. *See* Prop. Reg. §1.6035-1(e)(3)(ii)Ex.1. After the executor later determines what property will be used to satisfy a particular beneficiary's interest, "the executor may, but is not required" to file a supplemental return with the IRS and a supplemental statement with the beneficiary. [Presumably the beneficiary would not need a supplemental statement because the beneficiary would know what property was actually received and can find the property listed on the initial statement.]

The Instructions to the Form 8971 provide that

> the executor must list all items of property that could be used, in whole or in part, to fund the beneficiary's distribution on that beneficiary's Schedule A. (This means that the same property may be reflected on more than one Schedule A.) A supplemental Form 8971 and corresponding Schedule(s) A should be filed once the distribution to each such beneficiary has been made.

The last sentence quoted above from the Instructions has been revised by the proposed regulations; supplemental reporting is allowed but is not required.

When the Form 8971 is filed 30 days after the Form 706 has been filed (and before most of the assets have been distributed), each beneficiary will receive a Schedule A reporting all items in the gross estate that "could be used" to fund the bequest to that beneficiary, "in whole or in part" (which presumably would be pretty well all of the assets in the gross estate that have not previously been distributed or sold).

The proposed regulations state that "all of the property that the executor could use to satisfy that beneficiary's interest" must be listed. It does not refer merely to remaining "reportable" property in the estate, but an example suggests that only reportable property must be listed. Prop. Reg. §1.6035-1(e)(3)(ii)Ex. 2 (the initial Schedule A for an unfunded bequest did not list tangible personal property for which no appraisal was required in the list of property that could be used to satisfy the bequest). Accordingly cash, IRD, tangible personal property for which an appraisal is not required, or the proceeds of liquidated assets would not have to be included in this list because those assets are not property "for which reporting is required" under Prop. Reg. §1.6035-1(b). [One way to avoid advising beneficiaries whose bequests cannot be funded prior to the reporting date about most of the assets in the gross estate would be to liquidate the estate soon after the date of death.]

[This reporting requirement for undistributed property may cause real heartburn for some estates. Executors may be reluctant to provide full information about all estate assets to beneficiaries who are only entitled to receive a general bequest that may represent a fairly small portion of the estate. Furthermore, it will be burdensome. In effect, *each* beneficiary who has not already been funded by the 30 day due date will receive a report that may be about as long as the Form 706 without attachments–including a list of all assets listed on the return that have not yet been sold or distributed and that could be distributed to the beneficiary.]

Beneficiary Cannot Be Located. If a beneficiary cannot be located by the time the report is due, the executor must still file the information report, explaining the efforts to locate

the beneficiary, and a supplemental report must be filed within 30 days of later locating the beneficiary. Prop. Reg. §1.6035-1(c)(4).

10. **Due Dates of Reports**. The information reports to the IRS and recipients of reportable property (as described above) are due the earlier of 30 days after the due date of the estate tax return or the date it is actually filed. Prop. Reg. §1.6035-1(d). This reiterates the due date as provided in §6035(a)(3)(A). The Instructions to Form 8971 revise this due date—stating the reports are due within 30 days of the *filing* date if the estate tax return is not filed until after the due date. [This makes sense because the information on the Schedules A is based on information in the estate tax return and the Schedules A could not be completed if the estate tax return has not been filed. The statute is flawed and the Instructions adopt the only reasonable approach—even though that results in an extension of the statutory due date.]

11. **Supplemental Information**. Supplemental information returns (Form 8971) and statements (Schedules A) generally must be provided if any change occurs that causes the reported information to be correct. Examples include the discovery of additional property, a change in value of property pursuant to an examination of litigation, or the executor's disposition of property in a transaction in which basis is determined in whole or in part with reference to property in the gross estate, such as a like-kind exchange. Prop. Reg. §1.6035-1(a)(1)-(2). Two exceptions apply: (1) inconsequential errors or omissions; and (2) the actual distribution of property previously reported as being available to satisfy unfunded bequests described in Item 9 above. Prop. Reg. §1.6035-1(a)(3).

    Inconsequential Error or Omission. No further guidance is in the proposed regulations as to what constitutes an "inconsequently error or omission, but the Instructions to Form 8971 give further guidance as to inconsequential errors or omissions that would qualify for the reasonable cause exception from penalties. Errors on Form 8971 "that are **never** inconsequential are those related to a TIN, a beneficiary's surname, and the value of the asset the beneficiary is receiving from the estate." (emphasis included in original). Errors on a Schedule A "that are **never** inconsequential are those related to (a) the value of the asset the beneficiary is receiving from the estate, and (b) a significant item in a beneficiary's address." (emphasis in original).

    Due Date. The due date of supplemental returns and statements is 30 days after (1) the final value is determined, (2) incorrect or incomplete information is discovered by the executor, or (3) a supplemental estate tax return is filed reporting additional assets. Prop. Reg. §1.6035-1(a)(4)(i). An exception to the due date applies for undistributed property from a probate estate or revocable trust—if one of the three events listed in the preceding sentence occurs before the property is distributed to a beneficiary from the probate estate or revocable trust, the due date of the information return and statement is 30 days after the property is distributed to the beneficiary. Prop. Reg. §1.6035-1(a)(4)(ii).

12. **Subsequent Transfers**. A surprise in the proposed regulations is the requirement for recipients of a decedent's property to provide a "supplemental Statement" with the IRS and a transferee upon making subsequent distributions or transfers to a "related transferee" in which the basis is determined, in whole or in part, by reference to the recipient/transferor's basis (for example, a gift). Prop. Reg. §1.6035-1(f). If the subsequent transfer occurs before the final value is determined, the recipient/transferor must also give the executor a copy of the information Statement that is provided to the

IRS and transferee, so that if the executor subsequently provides any information Statements, they can be given to the new transferee.

These requirements regarding subsequent transfers can impose a significant reporting burden on estate recipients for possibly many years in the future (and penalties can apply if the reports are not given). Some planners have even suggested that executors might consider liquidating many of the estate assets so that estate beneficiaries would not receive assets that were in the gross estate; the assets would not have to be reported to the initial recipient on a Schedule A, and the initial recipient would not be burdened with having to provide reports on making any future gifts of those assets to related parties.]

Purpose. The preamble to the proposed regulations gives the following reason for imposing this requirement: "The Treasury Department and the IRS are concerned, however, that opportunities may exist in some circumstances for the recipient of such reporting to circumvent the purposes of the statute (for example, by making a gift of the property to a complex trust for the benefit of the transferor's family)."

Related Transferee. The proposed regulation has an objective definition of who constitutes a "related transferee" of a subsequent transfer that will require supplemental Statements.

> For purposes of this provision, a related transferee means any member of the transferor's family as defined in section 2704(c)(2), any controlled entity (a corporation or any other entity in which the transferor and members of the transferor's family (as defined in section 2704(c)(2)), whether directly or indirectly, have control within the meaning of section 2701(b)(2)(A) or (B)), and any trust of which the transferor is a deemed owner for income tax purposes. Prop. Reg. §1.6035-1(f).

Section 2704(c)(2) defines a "member of the family" with respect to any individual as meaning (1) the individual's spouse, (2) any ancestor or descendant of such individual or such individual's spouse, (3) any sibling of the individual, and (4) any spouse of an individual described in items (2) or (3). For example, if the estate distributes an asset to the decedent's surviving wife, who later gives the asset to a daughter, the subsequent transfer would require the surviving wife to give an information Statement to the IRS and her daughter (even if that subsequent gift occurs many years later).

Subsequent Distribution From Trust Recipient. What about a transfer from a decedent's estate to a trust and later distribution from the trust to a beneficiary? The trust clearly is a recipient and is making a subsequent transfer in which the basis is determined, at least in part, by the trust's basis (assuming the distribution is not made in satisfaction of a pecuniary distribution (which is a gain recognition event) and assuming the trustee does not make the election to recognize gain under §643(e)(3)). However, it is not clear that the beneficiary who receives the distribution from the trust is a "related transferee" of the trust (which is the "recipient/transferor"). Section 2704(c)(2) describes who is a member of the family "with respect to any *individual*," and the trust is not an individual. However, if the attribution rule of §2704(c)(3) were to be applied to determine the interests held by any individual, the individuals who are beneficiaries of the trust would likely be treated as indirectly owning the trust assets, and a distribution to another beneficiary may be treated as a transfer to a "related transferee." The definition of related transferee in the proposed regulation, makes reference to §2704(c)(2), and does not specifically make reference to §2704(c)(3) (but is §2704(c)(3) necessarily applicable in applying §2704(c)(2)?).

Thus, if a trust that receives estate property (and receives a Schedule A from the executor) makes a later distribution to a beneficiary, the distribution would not appear to require the trustee (or other trust beneficiaries who might be deemed transferors under §2704(c)(3) if it applied) to file an information Statement with the IRS and trust beneficiary about the finally determined estate tax value of the property.

Subsequent Distribution From Individual Recipient to a Grantor Trust. If the recipient/transferor who is an individual who makes a transfer to a grantor trust, the individual would have to provide information Statements to the IRS and the trustee of the grantor trust. On the other hand, if the individual gives the property received from an estate to a non-grantor trust, apparently, no such information Statements are required. [This makes no sense. Indeed, giving information Statements for gifts to a non-grantor trust would make more sense because the distribution from an individual to a grantor trust is generally treated as a non-event for income tax purposes and the person would in effect be giving notice to herself. For example, if a surviving wife who receives assets from her husband's estate makes a subsequent gift of such an asset outright to her daughter or to a GRAT that is a grantor trust or to another type of grantor trust for her daughter, the gift would be reportable; if the gift is made to a non-grantor trust for her daughter, the gift would not be reportable.]

Due Date. The supplemental Statement must be given to the IRS and the transferee within 30 days of the date of the distribution or other transfer.

Information Statement. The term "Statement" is defined to be Schedule A of the Form 8971 (or any successor schedule issued by the IRS). Prop. Reg. §1.6035-1(g)(3). Therefore, information regarding subsequent transfers will be described on a Schedule A (both to the transferee and the IRS). This is different from the way that basis consistency information is given to the IRS in all other circumstances; in other situations the IRS is advised with an "information return" (which is Form 8971), but in this situation both the IRS and recipient are advised using a Schedule A.

How Will Recipient Know About Requirement To Report Subsequent Transfers? Perhaps the Notice on Schedule A should be revised by the IRS, or perhaps the transmittal letter sending a Schedule A to a beneficiary should notify the beneficiary that reporting requirements may exist with respect to certain subsequent transfers of property reported on the Schedule A.

13. **"Information Return" and "Statement"**. The proposed regulations use the terms "Information Return" and "Statement" throughout the regulations. "Information Return" is defined as Form 8971 and "Statement" is defined as Schedule A (or any successor form issued by the IRS). Prop. Reg. §1.6035-1(g))(2)-(3).

14. **No New Process for Beneficiaries to Contest Estate Tax Values**. This basis consistency limitation can lead to unfair results because the beneficiary may have had no input in the values reported on an estate tax return or in audit negotiations. In an audit, the executor may have "traded off" on the valuation of various assets. With this provision, the executor will have to consider the effect of audit negotiations on the basis of assets received by the various individual beneficiaries. Furthermore, the executor will have to consider the values that are reported on the Form 706 with respect to the impact upon beneficiaries for basis purposes.

The preamble to the proposed regulations says that one commenter asked the IRS to provide a process by which a beneficiary could challenge a value reported by the executor on an estate tax return. The IRS responded that "[t]he beneficiary's rights with regard to the estate tax valuation of property are governed by applicable state law"—meaning that the beneficiary can pursue state law remedies with the executor.

FORM 8971

The positions of the proposed regulations are reflected in the Form 8971 and its Instructions, which were previously released on January 29, 2016.

- Part I of Form 8971 lists general information about the decedent and executor.
- Part II lists information about beneficiaries (including TIN, address, and the date that Schedules A are "provided" to each beneficiary).
- A Schedule A is attached to provide information to each estate beneficiary. The Schedule A includes the Form 706 Item number and description of property that the beneficiary has acquired from the decedent. For each asset listed, the executor indicates whether the asset increases estate tax liability and provides the valuation date and value. Schedule A contains a "Notice to Beneficiaries" directing the beneficiary to retain the schedule for tax reporting purposes and informing the beneficiary that if the property increased the estate tax liability, the Code requires consistent reporting of basis. [That notice could be confusing and even extremely misleading to some beneficiaries (for example, for donors who receive property back from a decedent that was gifted within one year prior to the date of death, for which no basis adjustment is allowed under §1014(e)). The executor may want to send the Schedule A with a letter providing more information to the beneficiary about the importance of the information reported on the Schedule A and possible reporting requirements if the recipient makes certain subsequent gifts or transfers.]
- If the executor is also a beneficiary, the executor will have to send a Schedule A to himself or herself.
- The executor is directed to "[s]ubmit Form 8971 with a copy of each completed Schedule A to the IRS." The Instructions direct the executor to file the Form 8971 with all Schedules A to the IRS within 30 days after the due date (but if the return is filed late, within 30 days of the filing date) of the estate tax return. The Form 8971 and attached Schedules A are not to be filed with the Form 706, but must be filed separately. If values are adjusted, a Supplemental Form 8971 and Schedules A must be filed with the IRS within 30 days after the adjustment.
- Beneficiaries only receive Schedules A and not the Form 8971 itself. The Schedules A must be "provided" (in person or by email, U.S. mail or private delivery service) within 30 days of the due date of the estate tax return (or, according to the Instructions but not the statute or the proposed regulation, within 30 days of the filing date if the return is filed late). If adjustments are made to assets listed on the estate tax return (such as values or the inclusion of additional assets), an updated Supplemental Schedule A must be given to each affected beneficiary within 30 days of the adjustment.