Estate of Elizabeth G. Huntington, Deceased, Nancy H. Brunson, Administratrix v. Commissioner of Internal Revenue, 100 T. C. 19 (1993)

Payments made to beneficiaries in settlement of claims based on reciprocal will agreements are not deductible as claims against the estate if supported only by donative intent.

Summary

In Estate of Huntington v. Commissioner, the Tax Court ruled that payments made by an estate to settle a lawsuit based on an alleged reciprocal will agreement between the decedent and her husband were not deductible as claims against the estate. The court found that the underlying claim lacked adequate consideration under Section 2053(c), as it was based solely on the donative intent of the spouses. The decedent's estate had paid $425,000 to the decedent's stepsons to settle their claim to inherit under the alleged agreement. The court held that such payments, which were essentially testamentary in nature, could not be deducted from the estate's taxable value.

Facts

Elizabeth G. Huntington (decedent) married Dana Huntington in 1955. Dana had two sons from a prior marriage, Charles and Myles, and a daughter, Nancy, with Elizabeth. In 1978, Dana executed a will devising his estate to a trust for Elizabeth's benefit, with the remainder to be split equally among Charles, Myles, and Nancy. In 1979, Dana executed a new will leaving his entire estate to Elizabeth. After Dana's death in 1980, Charles and Myles sued Elizabeth in 1981, alleging an oral agreement between Dana and Elizabeth to execute reciprocal wills. In 1986, a settlement was reached where Elizabeth agreed to devise 40% of her estate to Charles and Myles. Elizabeth died intestate later in 1986, and her estate settled with Charles and Myles for $425,000 in 1989.

Procedural History

Charles and Myles filed a lawsuit in 1981 to impose a constructive trust on Elizabeth's property based on the alleged reciprocal will agreement. This lawsuit was settled in 1986. After Elizabeth's death, her estate paid $425,000 to Charles and Myles in 1989 to settle their claim to inherit under the settlement agreement. The estate sought to deduct this payment as a claim against the estate under Section 2053(a)(3). The IRS disallowed the deduction, leading to the estate's appeal to the U. S. Tax Court.

Issue(s)

1. Whether the $425,000 payment made by Elizabeth's estate to Charles and Myles in settlement of their claim under the alleged reciprocal will agreement is deductible as a claim against the estate under Section 2053(a)(3).

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Holding

1. No, because the payment was not supported by adequate consideration under Section 2053(c) and constituted a payment in the nature of an inheritance.

Court’s Reasoning

The court applied Section 2053(a)(3), which allows a deduction for claims against the estate if they are enforceable personal obligations of the decedent existing at death. However, Section 2053(c) requires that such claims be contracted bona fide and for adequate consideration. The court emphasized that claims based solely on the donative intent of the parties do not meet this requirement, as they serve a testamentary purpose rather than being enforceable obligations. The court cited precedent holding that payments to beneficiaries in settlement of claims based on reciprocal will agreements are not deductible if supported only by donative intent. The court found that the alleged reciprocal will agreement between Dana and Elizabeth was not supported by adequate consideration beyond their mutual intent to provide for their children. The subsequent settlement between Elizabeth and her stepsons did not change this, as it was based on the same underlying claim lacking adequate consideration.

Practical Implications

This decision clarifies that payments made to settle claims based on reciprocal will agreements are not deductible as claims against the estate if the underlying agreement lacks adequate consideration beyond the donative intent of the parties. Estate planners must ensure that any reciprocal will agreements are supported by independent consideration to qualify for estate tax deductions. The ruling reinforces the IRS’s position that such payments are essentially testamentary in nature and not deductible. Practitioners should advise clients to structure reciprocal will agreements carefully or consider alternative estate planning mechanisms to achieve their intended results while maintaining tax efficiency. Subsequent cases have followed this precedent, further solidifying the principle that donative intent alone is insufficient to support a deduction under Section 2053(a)(3).

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