Steinberg v. Commissioner, 141 T. C. 258 (2013) (United States Tax Court, 2013)

In Steinberg v. Commissioner, the U. S. Tax Court rejected the IRS's motion for summary judgment, holding that a donee's assumption of potential estate tax liability under Section 2035(b) could be considered as part of the consideration for a gift. This decision impacts how gift tax liability may be calculated in net gift agreements, allowing for potential discounts based on the donee's assumption of estate tax risks.

Parties

Jean Steinberg, as the donor and petitioner, filed against the Commissioner of Internal Revenue as the respondent. Steinberg was the petitioner throughout the proceedings in the U. S. Tax Court.

Facts

Jean Steinberg, aged 89, entered into a binding gift agreement on April 17, 2007, with her four adult daughters (the donees). Under the agreement, Steinberg transferred cash and securities to her daughters. In exchange, the daughters agreed to assume and pay any resulting federal gift tax liability and any potential federal or state estate tax liability under Section 2035(b) if Steinberg died within three years of the gift. An appraiser calculated the fair market value of the "net gift" by reducing the value of the transferred assets by the gift tax the daughters paid and the actuarial value of their assumption of potential Section 2035(b) estate tax liability. Steinberg reported taxable gifts of $71,598,056 on her Form 709 for 2007, which included a discount of $5,838,540 for the daughters' assumption of the potential estate tax liability. The IRS issued a notice of deficiency, increasing the value of the gifts and disallowing this discount.

Procedural History

After receiving the notice of deficiency on July 25, 2011, Steinberg timely filed a petition with the U. S. Tax Court. The Commissioner moved for summary judgment on the issue of whether the donees' assumption of potential Section 2035(b) estate tax liability constituted consideration in money or money's worth under Section 2512(b). The Tax Court reviewed the motion, with several judges agreeing with the Court's opinion, others concurring in the result only, and one judge dissenting.

Issue(s)

Whether a donee's promise to pay any Federal or State estate tax liability that may arise under Section 2035(b) if the donor dies within three years of the gift may constitute consideration in money or money's worth within the meaning of Section 2512(b)?

Rule(s) of Law

The amount of a gift is the value of the property transferred minus any consideration received in money or money's worth. Section 2512(b) states that the amount of a gift is determined by the value of the property transferred minus the value of any consideration received. Section 2035(b) provides that the gross estate shall be increased by the amount of gift taxes paid on any gift made by the decedent during the three-year period preceding the decedent's death. The IRS regulation at Section 25. 2512-8, Gift Tax Regs. , specifies that consideration in money or money's worth must be reducible to a value in money or money's worth.

Holding

The U. S. Tax Court held that the donees' assumption of potential Section 2035(b) estate tax liability could constitute consideration in money or money's worth under Section 2512(b). Therefore, the fair market value of Steinberg's taxable gift may be determined with reference to the daughters' assumption of the potential Section 2035(b) estate tax liability.

Reasoning

The Tax Court rejected the IRS's arguments based on its prior decision in McCord v. Commissioner, which had held that such an assumption was too speculative to be valued for gift tax purposes. The Court distinguished McCord, noting that the contingency in this case (the donor's survival for three years) was simpler and more ascertainable than the complex contingency in McCord. The Court also rejected the IRS's argument that the donees' assumption of potential estate tax did not replenish Steinberg's estate, citing the estate depletion theory. The Court reasoned that the donees' assumption of the potential estate tax liability could have a tangible monetary value that benefits the donor's estate. Furthermore, the Court found that the donees' assumption was not necessarily a gift between family members, as it was a bona fide agreement negotiated at arm's length with separate counsel. The Court also noted that potential tax liabilities, such as capital gains tax, are considered in valuations despite their speculative nature, suggesting a similar treatment for potential estate tax liabilities.

Disposition

The Tax Court denied the Commissioner's motion for summary judgment and declined to follow McCord v. Commissioner to the extent it held otherwise regarding the consideration of potential Section 2035(b) estate tax liability in net gift agreements.

Significance/Impact

The Steinberg decision is significant for its departure from McCord, allowing taxpayers to potentially reduce the value of a gift by the actuarial value of a donee's assumption of potential Section 2035(b) estate tax liability. This ruling impacts the calculation of gift tax in net gift agreements and may encourage such arrangements. It reflects a broader judicial trend towards considering potential tax liabilities in valuation exercises, which could influence future tax planning and litigation. The decision also underscores the importance of factual determinations in assessing whether a contingency is too speculative to be valued, which may lead to more detailed evidentiary presentations in similar cases.