

POPPR .....	Fix .....	(Lat. 33°50'34" N., long. 118°17'18" W.)
Santa Monica (SMO) .....	VOR/DME .....	(Lat. 34°00'37" N., long. 118°27'24" W.)
CANOG .....	Fix .....	(Lat. 34°13'24" N., long. 118°35'39" W.)

**T-249 Van Nuys, CA (VNY) to Seal Beach, CA [New]**

Van Nuys (VNY) .....	VOR/DME .....	(Lat. 34°13'24" N., long. 118°29'30" W.)
Santa Monica (SMO) .....	VOR/DME .....	(Lat. 34°00'37" N., long. 118°27'24" W.)
POPPR .....	Fix .....	(Lat. 33°50'34" N., long. 118°17'18" W.)
Seal Beach (SLI) .....	VORTAC .....	(Lat. 33°47'00" N., long. 118°03'17" W.)

Issued in Washington, DC, on April 13, 2007.

**Edith V. Parish,**

*Manager, Airspace and Rules Group.*

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**DEPARTMENT OF THE TREASURY**

**Internal Revenue Service**

**26 CFR Part 20**

[REG-143316-03]

RIN 1545-BC56

**Guidance Under Section 2053 Regarding Post-Death Events**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Notice of proposed rulemaking and notice of public hearing.

**SUMMARY:** This document contains proposed amendments to the regulations relating to the amount deductible from a decedent's gross estate for claims against the estate under section 2053(a)(3) of the Internal Revenue Code (Code). In addition, the proposed regulations update the provisions relating to the deduction for certain state death taxes to reflect the statutory amendments made in 2001 under sections 2053(d) and 2058. The proposed regulations will affect estates of decedents against whom there are claims outstanding at the time of the decedent's death. This document also provides notice of a public hearing on these proposed regulations.

**DATES:** Written or electronic comments must be received by July 23, 2007. Outlines of topics to be discussed at the public hearing scheduled for August 6, 2007, at 10 a.m., must be received by July 30, 2007.

**ADDRESSES:** Send submissions to: CC:PA:LPD:PR (REG-143316-03), Room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m.

to CC:PA:LPD:PR (REG-143316-03), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC; or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-143316-03). The public hearing will be held in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

**FOR FURTHER INFORMATION CONTACT:** Concerning the proposed regulations, DeAnn K. Malone, at (202) 622-3112; concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Richard Hurst, at (202) 622-2949 (TDD telephone) (not toll-free numbers) or e-mail at [Richard.A.Hurst@ircounsel.treas.gov](mailto:Richard.A.Hurst@ircounsel.treas.gov).

**SUPPLEMENTARY INFORMATION:**

**Background**

Section 2001 of the Code imposes a tax on the transfer of the taxable estate, determined as provided in section 2051, of every decedent, citizen, or resident of the United States. Section 2031(a) generally provides that the value of the decedent's gross estate shall include the value at the time of decedent's death of all property, real or personal, tangible or intangible, wherever situated. Section 2051 provides that the value of the taxable estate is determined by deducting from the value of the gross estate the deductions provided for in sections 2051 through 2058. Pursuant to section 2053(a), "the value of the taxable estate shall be determined by deducting from the value of the gross estate such amounts—(1) for funeral expenses, (2) for administration expenses, (3) for claims against the estate, and (4) for unpaid mortgages on, or any indebtedness in respect of, property where the value of the decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate, as are allowable by the laws of the jurisdiction, whether within or without the United States, under which the estate is being administered."

The deductions allowable under sections 2051 through 2058 operate to eliminate from estate taxation those portions of the gross estate that are necessarily expended in paying certain claims and expenses of the estate. The rationale for those deductions is that those expended portions of the gross estate are not transferred to the decedent's legatees, beneficiaries, or heirs and, therefore, are not subject to the transfer tax.

The amount an estate may deduct for claims against the estate has been a highly litigious issue. Unlike section 2031, section 2053(a) does not contain a specific directive to value a deductible claim at its date of death value. Section 2053, in fact, specifically contemplates expenses such as funeral and administration expenses, which are only determinable after the decedent's date of death. Although numerous courts have addressed section 2053(a)(3), there is little or no consistency among the conclusions of those courts with regard to the extent (if any) to which post-death events are to be considered in valuing such claims. 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.

Even in the circuits where the date-of-death valuation approach has been applied in determining the amount that may be deducted for a claim against the decedent's estate, courts have recognized exceptions that necessitate taking into account events that occur after the decedent's death. For example, courts have deviated from the date-of-death valuation approach in favor of the actual payment approach when a claim is contested, contingent, unenforceable, becomes unenforceable after the decedent's death, or is not in fact presented for payment. The application and extent of these exceptions are inconsistent from circuit to circuit, however, and cannot be reconciled to form a conclusive rule applicable to all estates.

The result of this lack of consistency in the case law is that similarly situated estates are being treated differently for Federal estate tax purposes, depending only upon the jurisdiction in which the executor resides. The Treasury Department and the IRS believe that similarly situated estates should be treated consistently by having section 2053(a)(3) construed and applied in the same way in all jurisdictions.

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).

#### Explanation of Provisions

The proposed regulations will amend the regulations under section 2053 to clarify that events occurring after a decedent's death are to be considered when determining the amount deductible under all provisions of section 2053 and that deductions under section 2053 are limited to amounts actually paid by the estate in satisfaction of deductible expenses and claims. Final court decisions as to the amount and enforceability of the claim or expense are accepted in determining the amount deductible if the court passes upon the facts upon which deductibility depends. Settlements are accepted if they are reached in bona fide negotiations between adverse parties with valid claims recognizable under applicable law, and if they are not inconsistent with the applicable law. 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 will not be ascertainable by the time of the expiration of the period of limitations for claims of refund. A deduction is not allowed to the extent the expense or claim is compensated for by insurance or is otherwise reimbursed.

The proposed regulations further provide that no deduction may be taken on an estate tax return for a claim that is potential, unmatured, or contested at the time the return is filed. 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 by reason of the deduction of a

claim against the estate to the extent that claim is ultimately paid by the estate.

Additional provisions in the proposed regulations provide guidance for other particular circumstances. When a claim against an estate lists multiple defendants, the estate may only deduct the decedent's portion of the liability. Claims by family members or beneficiaries of a decedent's estate will be strictly scrutinized to ensure that they are legitimate claims. If a claim becomes unenforceable after the decedent's death, the estate may not take a section 2053(a)(3) deduction with respect to the claim. If a claim represents a decedent's obligation to make recurring payments that will likely continue for a period extending beyond the final determination of the estate tax liability, a deduction is allowed only as each payment is made, provided the period of limitations for claims for refund has not expired or the estate has properly preserved the claim for refund. Alternatively, a deduction is allowed for the cost of a commercial annuity purchased by the estate from an unrelated dealer in commercial annuities in satisfaction of that obligation.

Finally, the proposed regulations reflect changes made to section 2053(d) and the enactment of section 2058 in 2001 and clarify that the rules in section 20.2053-9 apply only to the estates of decedents dying on or before December 31, 2004.

#### Proposed Effective Date

The regulations, as proposed, apply to the estate of any decedent dying on or after the date final regulations are published in the **Federal Register**.

#### Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

## Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and the Treasury Department also request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for August 6, 2007, at 10 a.m. in the IRS Auditorium, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the **FOR FURTHER INFORMATION CONTACT** section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit electronic or written comments by July 16, 2007, and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by July 30, 2007. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

## Drafting Information

The principal author of these proposed regulations is DeAnn K. Malone, Office of the Chief Counsel, IRS.

## List of Subjects in 26 CFR Part 20

Estate taxes, Reporting and recordkeeping requirements.

## Proposed Amendments to the Regulations

Accordingly, 26 CFR part 20 is proposed to be amended as follows:

## PART 20—ESTATE TAX; ESTATES OF DECEDENTS DYING AFTER AUGUST 16, 1954

**Paragraph 1.** The authority citation for part 20 continues to read in part as follows:

**Authority:** 26 U.S.C. 7805. \* \* \*

**Par. 2.** Section 20.2051-1 is revised to read as follows:

### § 20.2051-1 Definition of taxable estate.

(a) The taxable estate of a decedent who was a citizen or resident (see § 20.0-1(b)(1)(i)) of the United States at death is determined by subtracting the total amount of the deductions authorized by sections 2052 through 2058 from the total amount which must be included in the gross estate under sections 2031 through 2044. These deductions are in general as follows:

(1) An exemption of \$60,000 (section 2052) (applicable only to the estates of decedents dying on or before December 31, 1976).

(2) Funeral and administration expenses and claims against the estate (including certain taxes and charitable pledges) (section 2053).

(3) Losses from casualty or theft during the administration of the estate (section 2054).

(4) Charitable transfers (section 2055).

(5) The marital deduction (section 2056).

(6) Qualified domestic trusts (section 2056A).

(7) Family-owned business interests (section 2057) (applicable only to the estates of decedents dying on or before December 31, 2003).

(8) State death taxes (section 2058) (applicable only to the estates of decedents dying after December 31, 2004).

(b) See section 2106 and these regulations for the computation of the taxable estate of a decedent who was not a citizen or resident of the United States. See also § 1.642(g)-1 of this chapter concerning the disallowance for income tax purposes of certain deductions allowed for estate tax purposes.

(c) *Effective date.* The rules of this section apply to the estates of decedents dying on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Par. 3.** Section 20.2053-1 is amended by:

1. Revising the introductory text of paragraph (a).

2. Adding two new sentences at the end of paragraph (b)(1).

3. Revising paragraph (b)(2).

4. Redesignating paragraph (b)(3) as (b)(4) and revising the newly-designated paragraph (b)(4).

5. Adding new paragraphs (b)(3), (b)(5), (b)(6), and (e).

The revisions and additions read as follows:

### § 20.2053-1 Deductions for expenses, indebtedness, and taxes; in general.

(a) *General rule.* In determining the taxable estate of a decedent who was a citizen or resident of the United States at death, there are allowed as deductions under section 2053(a) and (b) amounts falling within the following two categories (subject to the limitations contained in this section and in §§ 20.2053-2 through 20.2053-10):

\* \* \* \* \*

(b) \* \* \* (1) \* \* \* In order to properly take into account events occurring after the date of a decedent's death when determining the amount deductible against a decedent's estate, the deduction for any item described in paragraph (a) of this section is limited to the total amount actually paid (subject to any time requirement under paragraph (a) of this section) in settlement or satisfaction of that item. (See however, § 20.2053-1(b)(4) for a special rule for deducting certain estimated amounts.)

(2) *Effect of court decree—(i) In general.* 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.

(ii) *Consent decree.* 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.

(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).

(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.

(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.

(6) *Examples.* The following examples illustrate the application of this section. Assume that the amounts are payable out of property subject to claims and are allowable by the law of the jurisdiction governing the administration of the estate, whether the applicable

jurisdiction is within or without the United States.

*Example 1. Estimated amounts, deduction not ascertainable.* Decedent's (D's) estate was probated in state. State law provides that the personal representative shall receive compensation equal to 2.5 percent of the value of the probate estate. The executor (E) may claim a deduction for estimated fees equal to 2.5 percent of D's probate estate on the estate tax return filed for D's estate as an estimated amount, provided the amount will be paid to E after the estate tax return is filed. To the extent that, at the time of the examination of the return, the amount has not been paid and E cannot satisfy the conditions listed in paragraph (b)(4) of this section and § 20.2053-3(b)(1), the deduction will be disallowed, but the executor may file a timely protective claim for refund to protect the estate's right to a refund once the amount has been paid or satisfies the applicable conditions. If the 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.

*Example 2. Estimated amounts, deduction not ascertainable.* Prior to death, Decedent (D) is sued by Claimant (C) for \$100× in a tort proceeding and responds asserting affirmative defenses available to D under applicable local law. C and D are unrelated. D subsequently dies and D's Form 706 is due before a final judgment is entered in the case. The executor (E) of D's estate may not take a deduction for \$100× on D's estate tax return as an estimated amount because the deductible amount cannot be ascertained with reasonable certainty in accordance with § 20.2053-4(b)(2). If the amount of the actual liability will not be paid or cannot be ascertained with reasonable certainty before the expiration of the period of limitations for claims for refund, E may file a protective claim before that date in order to preserve the estate's right subsequently to claim a refund.

\* \* \* \* \*

(e) *Effective date.* The rules of this section apply to the estates of decedents dying on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Par. 4.** Section 20.2053-3 is amended by:

1. Redesignating paragraphs (b)(2) and (b)(3) as paragraphs (b)(4) and (b)(5), respectively.

2. Designating the undesignated text following paragraph (b)(1) as new paragraph (b)(3).

3. Revising paragraphs (b)(1) and (c)(1).

4. Adding new paragraphs (b)(2), (d)(3) and (e).

The revisions and additions read as follows:

**§ 20.2053-3 Deductions for expenses of administering estate.**

\* \* \* \* \*

(b) *Executor's commissions.* (1) The executor, in filing the estate tax return, may deduct executor's commissions in such an amount as has actually been paid, or in an amount which at the time of filing the estate tax return may reasonably be expected to be paid, but no deduction may be taken if no commissions are to be collected. If the amount of the commissions has not been fixed by decree of the proper court, the deduction will be allowed on the examination of the return, to the extent that all three of the following conditions are satisfied:

(i) The Commissioner is reasonably satisfied that the commissions claimed will be paid.

(ii) The amount claimed as a deduction is within the amount allowable by the laws of the jurisdiction in which the estate is being administered.

(iii) It is in accordance with the usually accepted practice in the jurisdiction to allow such an amount in estates of similar size and character.

(2) If the conditions described in paragraph (b)(1) of this section are not met, 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).

(3) 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. If the deduction is allowed in advance of payment and 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.

\* \* \* \* \*

(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.

\* \* \* \* \*

(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.

(e) *Effective date.* The rules of this section apply to the estates of decedents dying on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Par. 5.** Section 20.2053-4 is revised to read as follows:

**§ 20.2053-4 Deduction for claims against the estate.**

(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.

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

(b) *Special rules—(1) Potential and unmatured claims.* Claims that are unmatured on the date of the decedent's

death and that later mature and are paid are deductible by the estate. However, no deduction may be taken on an estate tax return for a potential or unmatured claim. If the claim matures and is paid prior to the expiration of the period of limitations for filing a claim for refund, the estate may file a 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 once the claim against the decedent's estate is matured and is paid or may be estimated as provided in § 20.2053-1(b)(4). 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, and must describe the reasons and contingencies delaying actual payment of the liability or claim. Action on protective claims will proceed after the executor has notified the Commissioner that the contingency has been resolved.

(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.

(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.

(4) *Claims by family members, related entities, or beneficiaries.* Relationships with and among a decedent and the

decedent's family members, related entities, and beneficiaries may create the potential for collusion in asserting invalid or exaggerated claims in order to reduce the decedent's taxable estate.

Thus, notwithstanding § 20.2053-1 and paragraph (a) of this section, there will be a rebuttable presumption that claims by a family member of the decedent, a related entity, or a beneficiary of the decedent's estate or revocable trust are not legitimate and bona fide and therefore are not deductible. Evidence 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. Similarly, a settlement between a decedent's estate or revocable trust and a family member, a related entity, or a beneficiary of the decedent's estate or revocable trust will be presumed to not be deductible absent evidence of the legitimacy and bona fide nature of the claim. For purposes of this section, family members include the spouse of the decedent; the grandparents, parents, siblings, and lineal descendants of the decedent or of the decedent's spouse; and the spouse and lineal descendants of any such grandparent, parent, and sibling. Family members include adopted individuals. For purposes of this section, a related entity is 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).

(5) *Unenforceable claims.* Claims that are unenforceable prior to or at the decedent's death are not deductible, even if they are actually paid. Claims that become unenforceable during the administration of the estate are not deductible to the extent that they are paid after they become unenforceable. To the extent that enforceability of a claim is at issue, see paragraph (b)(2) of this section relating to contested claims.

(6) *Claims founded upon a promise.* Except with regard to pledges or subscriptions, (see § 20.2053-5), section 2053(c)(1)(A) provides that the deduction for a claim founded upon a promise or agreement is limited to the extent that the promise or agreement was bona fide and in exchange for adequate and full consideration in

money or money's worth. For this purpose, bona fide and for adequate and full consideration in money or money's worth requires that the promise or agreement must have been made in good faith, and that the price must have been an adequate and full equivalent reducible to a money value.

(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.

(c) *Interest on claims.* The interest on a deductible claim is itself deductible as a claim under section 2053, but only to the extent of the amount of interest accrued at the date of the decedent's death and actually paid, even if the executor elects the alternate valuation method under section 2032. (Post-death accrued interest may be deductible in appropriate circumstances either as an estate tax administration expense under section 2053 or as an income tax deduction.)

(d) *Examples.* The following examples illustrate the application of paragraphs (a) through (c) of this section. Except as is otherwise provided in the examples,

assume that the claimant (C) is not a family member, related entity or beneficiary of the decedent (D) and is not the executor (E). Assume that a claim represents a personal obligation of D existing at the time of D's death and is enforceable against D's estate. Assume that the payment of the claim, where applicable, is made out of property subject to claims (as defined in section 2053(c)(2) and § 20.2053-1(c)(2)) and is allowable by the law of the jurisdiction under which the decedent's estate is being administered, or is paid prior to the filing of the estate tax return (including any extension granted under section 6081) from property not subject to claims. Assume that any court decree is based upon the facts upon which deductibility depends and is consistent with applicable local law. Assume that any settlement is reached in bona fide negotiations between or among parties having adverse interests with respect to the claim and that the terms of the settlement are not inconsistent with applicable local law.

*Example 1. Contested claim, single defendant, no decision.* D is sued by C for \$100x in a tort proceeding and responds asserting affirmative defenses available to D under applicable local law. D dies and E is substituted as defendant in the suit. D's estate tax return is due before a judgment is reached in the case. D's gross estate includes only property subject to claims and exceeds \$100x. E may not take a deduction on the return for the claim under section 2053(a)(3). A deduction may be claimed on the return, however, for expenses incurred prior to the filing of the estate tax return in defending the estate against the claim if the expenses have been paid in accordance with § 20.2053-3(c) or (d)(3) or as an estimate under § 20.2053-1(b)(4). E may file a protective claim for refund before the expiration of the period of limitations for claims for refund of the estate tax in order to preserve the estate's right to claim a refund if the amount of the liability will not be paid or cannot be ascertained with reasonable certainty by the expiration of that period of limitations. If payment is subsequently made pursuant to a court decision or a settlement, a deduction for the payment, as well as expenses incurred incident to the claim and not previously deducted, may be taken and relief may be sought by supplementing a previously filed protective claim or by filing a claim for refund as provided by section 6511.

*Example 2. Contested claim, single defendant, final court decree and payment.* The facts are the same as in *Example 1* except that, before the return is timely filed, the court enters a decision in favor of C, no timely appeal is filed, and payment is made. A deduction is allowed for the amount paid in satisfaction of the claim pursuant to the final decision of the local court, including any interest accrued prior to D's death, under section 2053(a)(3). In addition, a deduction may be available under § 20.2053-3(d)(3) for expenses incurred prior to the filing of the

estate tax return in defending the estate against the claim and in processing payment of the claim.

*Example 3. Contested claim, single defendant, settlement and payment.* The facts are the same as in *Example 1* except that, before the return is timely filed, a settlement is reached between D's estate and C for \$80x and payment is made. A deduction is allowed for the amount of the settlement paid to C (\$80x) under section 2053(a)(3). In addition, a deduction may be available under § 20.2053-3(d)(3) for expenses incurred prior to the filing of the estate tax return in defending the estate, reaching a settlement, and processing payment of the claim.

*Example 4. Contested claim, multiple defendants.* The facts are the same as in *Example 1* except that the suit filed by C lists D and K, an unrelated third-party, as defendants. If the claim is not resolved prior to the time the estate tax return is filed, E may not take a deduction for the claim under section 2053(a)(3) on the return. If payment is subsequently made of D's share of the claim pursuant to a court decision or a settlement holding D liable for 40 percent of the amount due and K liable for 60 percent of the amount due, then the estate may take a deduction for the amount paid in satisfaction of the claim representing D's share of the liability as assigned by the court decree (\$40x), plus any interest on that share accrued prior to D's death, under section 2053(a)(3). If the court decision finds D and K jointly and severally liable for the entire \$100x and D's estate pays the entire \$100x but could have reasonably collected \$50x from K in reimbursement, the estate may take a deduction under section 2053(a)(3) and paragraph (b)(3) of this section for only \$50x and the interest on \$50x accrued prior to D's death. In both instances, a deduction may also be available under § 20.2053-3(d)(3) for expenses incurred and not previously deducted in defending the estate against the claim and processing payment of the amount due from D.

*Example 5. Contested claim, multiple defendants, settlement and payment.* The facts are the same as in *Example 1* except that the suit filed by C lists D and K, an unrelated third-party, as defendants. D's estate settles with C for \$10x and payment is made before the return is timely filed. E may take a deduction for the amount paid to C in satisfaction of the claim. In addition, a deduction may be available under § 20.2053-3(d)(3) for expenses incurred prior to the filing of the estate tax return in defending the estate, reaching a settlement, and processing payment of the claim.

*Example 6. Mixed claims.* During life, D contracts with C to perform specific work on D's home for \$75x. Under the contract, additional work must be approved in advance by D. C performs additional work and sues D for \$100x for work completed including the \$75x agreed to in the contract. D dies and D's estate tax return is due before a judgment is reached in the case. E contests liability for \$25x. E may take a deduction on the return for \$75x if it has been paid or if it meets the requirements of an estimated amount. In addition, a deduction may be

claimed on the return for expenses incurred in defending the estate against the claim if they have been paid under § 20.2053-3(c) or (d)(3) or as an estimate under § 20.2053-1(b)(4). E may file a protective claim for refund before the expiration of the period of limitations on claims for refund of the estate tax in order to preserve the estate's right to claim a refund if payment on any amount in excess of \$75x is subsequently made in resolution of a claim that would qualify for a deduction under section 2053. To the extent that the expenses incurred in defending the estate against the claim are not deducted as an estimate, they may be included in the protective claim for refund.

*Example 7. Unenforceable claims.* D is sued by C for \$100x in a tort proceeding but the claim is barred by the applicable period of limitations and there is no other recourse available to C. A deduction is not allowed for the claim under section 2053(a)(3) whether or not the estate actually pays money in satisfaction of the claim. A deduction may be available, however, under § 20.2053-3(d)(3) for expenses incurred in defending the estate against the claim.

*Example 8. Non-contingent and recurring obligation to pay, binding on estate.* D's property settlement agreement incident to D's divorce, signed three years prior to D's death, obligates D or D's estate to pay to S, D's former spouse, \$20x per year for 10 years. The payments are not conditioned on whether or not S remarries. If S dies prior to the last payment, the terms of the agreement state that the remaining payments are to be made to S's estate or as S may appoint in S's will. Prior to filing D's estate tax return, D's estate pays the first of the 7 payments remaining as of D's death. The estate may take a deduction for the present value of these payments. See §§ 20.7520-1 through 20.7520-4.

*Example 9. Contingent recurring obligation to pay, binding on estate.* D's property settlement agreement incident to D's divorce, signed three years prior to D's death, obligates D or D's estate to pay to S, D's former spouse, \$20x per year for 10 years. The obligation to make the annual payments ceases upon S's remarriage or S's death prior to the due date of the last payment. Prior to filing D's estate tax return, D's estate pays the first of the 7 payments remaining as of D's death. E may take as a deduction on the return the amount of the 1 payment made prior to the filing of D's estate tax return. Additional payments become deductible as they are paid. E may file a protective claim for refund before the expiration of the period of limitations for claims for refund of the estate tax in order to preserve the estate's right to claim a refund if the amount of the liability will not be paid or is not ascertainable with reasonable certainty by the expiration of the applicable period of limitations. If the total amount to be paid in satisfaction of the liability is not ascertainable with reasonable certainty at the time of examination of the return, relief may be sought by a claim for refund (either actual or protective) as provided by section 6511.

*Example 10. Recurring obligation to pay, estate purchases a commercial annuity in satisfaction.* D's property settlement

agreement incident to D's divorce, signed three years prior to D's death, obligates D or D's estate to pay to S, D's former spouse, \$20x per year for 10 years. D's estate purchases a commercial annuity from an unrelated dealer in commercial annuities, XYZ, in a bona fide sale to satisfy the obligation to S. E may deduct the entire amount paid to XYZ to obtain the annuity, regardless of whether or not the obligation to S was contingent.

(e) *Effective date.* The rules of this section apply to the estates of decedents dying on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Par. 6.** Section 20.2053-6 is amended by revising paragraphs (a) and (c) and adding new paragraphs (g) and (h) to read as follows:

**§ 20.2053-6 Deduction for taxes.**

(a) *In general.* Taxes are deductible in computing a decedent's gross estate only as claims against the estate (except to the extent that excise taxes may be allowable as administration expenses), and only to the extent not disallowed by section 2053(c)(1)(B) (see the remaining paragraphs of this section). However, see §§ 20.2053-9 and 20.2053-10 with respect to the deduction allowed for certain state and foreign death taxes.

\* \* \* \* \*

(c) *Death taxes.* (1) For the estates of decedents dying on or before December 31, 2004, no estate, succession, legacy or inheritance tax payable by reason of the decedent's death is deductible, except as provided in § 20.2053-9 and § 20.2053-10 with respect to certain state and foreign death taxes on transfers for charitable, etc., uses. However, see sections 2011 and 2014 and these regulations with respect to credits for death taxes.

(2) For the estates of decedents dying after December 31, 2004, see section 2058 to determine the deductibility of state death taxes.

\* \* \* \* \*

(g) *Post-death adjustments of deductible tax liability.* Post-death adjustments increasing a tax liability accrued prior to the decedent's death, including increases of taxes deducted under this section, will increase the amount of the deduction taken under section 2053(a)(3) for that tax liability. Similarly, any refund subsequently determined to be due to and received by the estate with respect to taxes deducted by the estate under this section reduces the amount of the deduction taken for that tax liability under section 2053(a)(3). Expenses associated with defending the estate against the increase in tax liability or with obtaining the

refund may be deductible under § 20.2053-3(d)(3). A protective claim for refund of estate taxes 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 deductible tax liability may be affected by such an adjustment or refund. The application of this section may be illustrated by the following examples:

*Example 1. Increase in tax due.* After the decedent's death, the Internal Revenue Service examines the gift tax return filed by the decedent in the year before the decedent's death and asserts a deficiency of \$100x. The estate spends \$30x in a non-frivolous defense against the increased deficiency. The final determination of the deficiency, in the amount of \$90x, is paid by the estate. The estate may deduct \$90x under section 2053(a)(3) and \$30x under § 20.2053-3(c)(2) or (d)(3).

*Example 2. Refund of taxes paid.* Decedent's estate timely files D's individual income tax return for the year in which the decedent died. The estate timely pays the entire amount of the tax due, \$50x, as shown on that return. The entire \$50x was attributable to income received prior to the decedent's death. Decedent's estate subsequently discovers an error on the income tax return and files a timely claim for refund. Decedent's estate receives a refund of \$10x. The estate is only allowed a deduction of \$40x under section 2053(a)(3) for the income tax liability accrued prior to the decedent's death. If a deduction for \$50x was allowed on the estate tax return prior to the receipt of the refund, it shall be the duty of the executor to notify the Commissioner of the change and to pay the resulting tax, with interest.

(h) *Effective date.* The rules of this section apply to the estates of decedents dying on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Par. 7.** Section 20.2053-9 is amended as follows:

1. Revising the heading for paragraph (a) and adding a sentence at the end of paragraph (a).
2. Revising the first and last sentences of paragraph (c).
3. Adding new paragraph (f).

The revisions and addition read as follows:

**§ 20.2053-9 Deduction for certain state death taxes.**

(a) *General rules for the estates of decedents dying on or before December 31, 2004.* \* \* \* For the estates of decedents dying after December 31, 2004, see section 2058 to determine the deductibility of state death taxes.

\* \* \* \* \*

(c) *Exercise of election.* The election to take a deduction for a state death tax

imposed upon a transfer for charitable, etc., uses shall be exercised by the executor by the filing of a written notification to that effect with the Commissioner. \* \* \* The election may be revoked by the executor by the filing of a written notification to that effect with the Commissioner at any time before the expiration of such period.

\* \* \* \* \*

(f) *Effective date.* The rules of this section apply to the estates of decedents dying on or before December 31, 2004.

**Par. 8.** Section 20.2053-10 is amended by revising paragraph (c) and adding a new paragraph (e) to read as follows:

**§ 20.2053-10 Deduction for certain foreign death taxes.**

\* \* \* \* \*

(c) *Exercise of election.* The election to take a deduction for a foreign death tax imposed upon a transfer for charitable, etc., uses shall be exercised by the executor by the filing of a written notification to that effect with the Commissioner. An election to take the deduction for foreign death taxes is deemed to be a waiver of the right to claim a credit under a treaty with any foreign country for any tax or portion thereof claimed as a deduction under this section. The notification shall be filed before the expiration of the period of limitations for assessment provided in section 6501 (usually 3 years from the last day for filing the return). The election may be revoked by the executor by the filing of a written notification to that effect with the Commissioner at any time before the expiration of such period.

\* \* \* \* \*

(e) *Effective date.* The rules of this section apply to the estates of decedents dying on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Kevin M. Brown,**

*Deputy Commissioner for Services and Enforcement.*

[FR Doc. E7-7601 Filed 4-20-07; 8:45 am]

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**DEPARTMENT OF HOMELAND SECURITY**

**Coast Guard**

**33 CFR Part 165**

[CGD13-07-009]

RIN 1625-AA00

**Safety Zones: Fireworks Displays in the Captain of the Port Portland Zone**

**AGENCY:** Coast Guard, DHS.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Coast Guard is proposing to amend its regulations to establish additional safety zones on the waters of the Columbia River located in the Area of Responsibility (AOR) of the Captain of the Port, Portland, Oregon during annual fireworks displays. The Captain of the Port, Portland Oregon is taking this action to safeguard watercraft and their occupants from safety hazards associated with these displays. Entry into these zones is prohibited unless authorized by the Captain of the Port.

**DATES:** Comments and related material must reach the Coast Guard on or before May 23, 2007.

**ADDRESSES:** You may mail comments and related material to Petty Officer Michelle Duty at Sector Portland 6767 N. Basin Ave., Portland, OR 97217. Sector Portland maintains the public docket for this rulemaking. Comments and material received from the public, as well as documents indicated in this preamble as being available in the docket, will become part of this docket and will be available for inspection or copying at Sector Portland between 8 a.m. and 4 p.m., Monday through Friday, except Federal holidays.

**FOR FURTHER INFORMATION CONTACT:** Petty Officer Michelle Duty, c/o Captain of the Port, Portland 6767 N. Basin Avenue, Portland, Oregon 97217, 503-240-2590.

**SUPPLEMENTARY INFORMATION:**

**Request for Comments**

We encourage you to participate in this rulemaking by submitting comments and related material. If you do so, please include your name and address, identify the docket number for this rulemaking (CGD13-07-009), indicate the specific section of this document to which each comment applies, and give the reason for each comment. Please submit all comments and related material in an unbound format, no larger than 8½ by 11 inches, suitable for copying. If you would like to know they reached us, please enclose a stamped, self-addressed postcard or