Philadelphia Estate Planning Council
Tax Updates – October 2016
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GUIDANCE FROM THE IRS:

***Rev Rul 2016-25, 2016-41 IRB* - October 2016 Rates:**

- Section 7520 Rate: 1.6%
- Annual Short Term AFR (0-3 years): .66%
- Annual Mid Term AFR (3-9 years): 1.29%
- Annual Long Term AFR (over 9 years): 1.95%

Form 8971 Amended instructions. The IRS has issued amended instructions to Form 8971. Of note the prohibition on attachments has been relaxed:

> "Listing of bulk assets may be attached to Schedule A in lieu of a detailed description of each item that has been acquired (or is expected to be acquired) by a beneficiary. The listing should consist of a (sic) related property (for example, stocks held in a single brokerage account) and only include information relevant to basis reporting such as name/description of the property, value, and valuation date. Do not attach property appraisals to Schedule A."

The full instructions may be obtained at the link below:
https://www.irs.gov/pub/irs-pdf/i8971.pdf?_ga=1.188496936.1053688344.1470948058

T.D. 9785, 08/31/2016, Reg. § 1.7701-1 , Reg. § 20.7701-2, Reg. § 25.7701-2, Reg. § 26.7701-2 , Reg. § 31.7701-2, Reg. § 301.7701-18 – Marriage Definitions Post Windsor and Obergefell. The IRS has issued final regulations redefining the Internal Revenue Code's marriage related terms in light of the *Windsor* and *Obergefell* decisions.

For federal tax purposes, the terms "spouse," "husband," and "wife" shall mean an individual lawfully married to another individual; and the term "husband and wife" means two individuals lawfully married to each other.

The IRS rejected certain changes suggested by commentators, stating that it believes these definitions apply equally to same-sex couples and opposite-sex couples, and that no clarification is needed. The IRS suggests the language is specifically gender neutral, which reflects the holdings in *Windsor* and *Obergefell* and is consistent with Rev Rul 2013-17.

The terms "spouse," "husband," and "wife" do not include individuals who have entered into a registered domestic partnership, civil union, or other similar relationship which is not denominated as a marriage under the state law. The term "husband and wife" does not include couples who have entered into such a relationship, and the term "marriage" does not include such relationships.

The IRS notes that even though some same sex couples did not have the opportunity to enter into a marriage at the time they entered into an alternative legal relationship, they now have such right and treating an alternative legal relationship as marriage for tax purposes may have unintended consequences. For example, the filing status of a couple treated as married for federal tax purposes is strictly limited to filing jointly or filing as married filing separately, which often results in a higher tax liability than filing as single or head of household and if alternative legal relationships were treated as marriage for tax purposes, domestic partners, for example, would be brought into the marriage tax landscape without actually making the choice to enter marriage.

Since alternative legal arrangements do not fall under the definition of marriage for tax purposes, participants in such relationships cannot rely on the certainty of tax treatment associated with provisions under the Code such as Code Sec. 71 (the income exclusion for alimony and separate maintenance), Code Sec. 215 (the deduction for alimony or separate maintenance payments), Code Sec. 414(p) (defining qualified domestic relations orders), Code Sec. 1041 (transfers of

property between spouses incident to divorce), Code Sec. 2056 (the estate tax marital deduction), and Code Sec. 2523 (gifts to spouses).

Rev Proc 2016-49, 2016-42 IRB – Disregarding Unnecessary QTIP Elections.

The IRS has provided procedures to disregard and treat as null for transfer tax purposes, a QTIP election where such election wasn't necessary to reduce the estate tax liability to zero.

As a result of the serious tax consequences of QTIP elections, Rev. Proc. 2001-38 was previously put in place to avoid unnecessary QTIP election stating such election would be null and void. Such earlier Rev. Proc was premised on the belief that an executor would never purposefully elect QTIP treatment for property if the election was not necessary to reduce the decedent's estate tax liability.

However, the earlier rule was developed before the enactment of the portability rules. The possibility of the portability election means that estates may want to make QTIP elections to increase the amount of the DSUE credit available to the surviving spouse to offset the surviving spouse's gift or estate tax liability.

Under this new Rev Proc, QTIP elections made in cases where all of the following requirements are satisfied are treated as void:

(1) The estate's federal estate tax liability was zero, regardless of the QTIP election, based on values as finally determined for federal estate tax purposes, thus making the QTIP election unnecessary to reduce the federal estate tax liability;

(2) The executor of the estate neither made, nor was considered to have made, the portability election as provided in Code Sec. 2010(c)(5)(A) and its regs; and

(3) The procedural requirements of Rev Proc 2016-49, Sec. 4.02, are satisfied. (Rev Proc 2016-49, Sec. 3.01)

For a QTIP election within the scope of Rev Proc 2016-49, IRS will disregard the QTIP election and treat it as null and void as follows:

(1) The property will not be includible in the gross estate of the surviving spouse under Code Sec. 2044,

(2) The spouse will not be treated as making a gift under Code Sec. 2519 if the spouse disposes of part or all of the income interest with respect to the property; and

(3) The surviving spouse will not be treated as the transferor of the property for generation-skipping transfer tax purposes under Code Sec. 2652(a).

But a QTIP Election will not be null and void if:

(1) A partial QTIP election was required with respect to a trust to reduce the estate tax liability, and the executor made the election with respect to more trust property than was necessary to reduce the estate tax liability to zero;

(2) A QTIP election was stated in terms of a formula designed to reduce the estate tax to zero (e.g., see Reg. § 20.2056(b)-7(h), Ex. 7 and 8);

(3) The QTIP election was a protective election under Reg. § 20.2056(b)-7(c);

(4) The executor of the estate made a portability election in accordance with Code Sec. 2010(c)(5)(A) and its regs, even if the decedent's DSUE amount was zero based on values as finally determined for federal estate tax purposes; or

(5) The requirements of Rev Proc 2016-49, Sec. 4.02, are not satisfied. (Rev Proc 2016-49, Sec. 3.02)