Paragraph 1. Section 20.2039-4(d)(2) is revised by inserting the phrase "be signed by the recipient and" in the third sentence after "The statement must".

This Treasury decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805). (Approved by the Office of Management and Budget under control number).

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

Approved April 23, 1984.

RONALD A. PEARLMAN,
Acting Assistant Secretary of the Treasury.

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Part IV.—Taxable Estate

Section 2053.—Expenses, Indebtedness, and Taxes

26 CFR 20.2053.1: Deductions for expenses, indebtedness, and taxes; in general.

Administration expenses; estimated future interest payments. A deduction is not allowable for the estimated amount of interest that will accrue upon funds borrowed by an executor on behalf of an estate to pay the federal estate tax if repayment of the loan can be accelerated.

Rev. Rul. 84-75

ISSUE

For purposes of section 2053 of the Internal Revenue Code, is a current deduction allowable for the estimated amount of interest that will accrue upon funds borrowed by an executor on behalf of an estate to pay the federal estate tax?

FACTS

The decedent *D*, died in 1982. *D*'s estate consisted almost entirely of stock of a closely held corporation. No election to extend the time for payment of the estate tax was made pursuant to Code section 6166. There was an insufficient amount of funds available to pay the federal estate tax, and a forced sale would have been required to convert estate assets into sufficient cash. Therefore, the executor borrowed funds, on behalf of the estate, to pay the tax obligation.

The principal amount of the loan is to be repaid over a period of six years, with ten percent interest payable annually. The loan could be fully repaid at any time at the executor's option, without penalty. If the executor fails to timely make any payment, the remaining payments can be accelerated at the lender's option.

On the federal estate tax return filed for the estate, the executor deducted 25*x* dollars as the estimated total amount of future interest to be paid during the loan term. The 25*x* dollars will be allowed as an administrative expense under applicable local law.

LAW AND ANALYSIS

Section 2053(a)(2) of the Code provides that the value of the taxable estate shall be determined by deducting from the value of the gross estate such amounts for administration expenses as are allowable by the laws of the jurisdiction under which the estate is being administered.

Section 20.2053-1(b)(3) of the Estate Tax Regulations provides that an item may be entered on the return for deduction, though its exact amount is not then known, provided it is ascertainable with reasonable certainty, and will be paid. No deduction may be taken upon the basis of a vague or uncertain estimate.

Section 20.2053-3 of the regulations provides that the amounts deductible as "administration expenses" are limited to such expenses as are actually and necessarily incurred in the administration of the decedent's estate; that is, in the collection of assets, payment of debts, and distribution of property.

Interest on a loan, obtained by an executor for an estate, is a deductible administration expense, provided the loan was reasonably and necessarily incurred in the administration of the estate. *Estate of Todd v. Commissioner*, 57 T.C. 288 (1971), *acq.* 1973-2 C.B. 4; *Hibernia Bank v. United States*, 581 F.2d 741 (9th Cir. 1978); *see Estate of Bahr v. Commissioner*, 68 T.C. 74 (1977), *acq.*, 1978-1 C.B. 1.

In this case, because the loan was obtained to avoid a forced sale of assets, the loan was reasonably and necessarily incurred in administering *D*'s estate. Therefore, interest incurred on the loan is deductible as an expense of administration under section 2053(a)(2).

In situations where the estate's obligation to make installment payments may be accelerated, the amount of future interest that will be paid is indefinite because a premature repayment will stop the accrual of interest. *See* Rev. Rul. 80-250, 1980-2 C.B. 278. Consequently, for section 2053(a)(2) deduction purposes, the possibility of prepayment renders any estimate of future interest vague and uncertain within the meaning of section 20.2053-1(b)(3). In this case, because accelerated payment could be made at the executor's option or could be required upon failure to make a timely scheduled payment, the 25*x* dollars estimated future interest expense is not allowable as a deductible administrative expense. Rather, the future interest expense will become deductible only as it accrues. See, for example, Rev. Proc. 81-27, 1981-2 C.B. 548, explaining the procedure for claiming interest deductions in situations where the estate tax liability has not been fully paid when the interest accrues. In those situations where a deduction is sought for interest that has accrued after the federal estate tax liability has been paid, a refund of tax may be requested by filing a claim for refund of tax on Form 843 within the applicable period of limitation set forth in section 6511 of the Code.

HOLDING

For purposes of section 2053 of the Code, a deduction is not allowable for the estimated amount of interest that will accrue upon funds borrowed by an executor on behalf of an estate to pay the federal estate tax if repayment of the loan could be accelerated. The interest is deductible as an administrative expense only to the extent it has accrued.

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26 CFR 20.2053-4: Deduction for claims against the estate; in general.

Whether a deduction is allowable where a donor/decedent gratuitously transfers a legally enforceable promissory note that has not been satisfied at the promisor's death. See Rev. Rul. 84-25, page 191.

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26 CFR 20.2053-7: Deduction for unpaid mortgages.
(Also Section 2036: 20.2036-1.)

Transfers; retained life estate; transferee's loan secured by mortgage on transferred property. Property in which a decedent retained a life estate is includible in the decedent's gross estate without an offset or deduction for a mortgage that was contracted for by the remainderman, even though the decedent was surety for the mortgage.

Rev. Rul. 84-42

ISSUE

What amount is includible in *D*'s gross estate under section 2036 of the Internal Revenue Code, and what amount is deductible by *D*'s estate under section 2053, if *D* is guarantor of a loan to *A* secured by a mortgage on property *D* previously transferred to *A* subject to a retained life estate?

FACTS

In 1976, *D*, a resident of State *X*, gratuitously conveyed a remainder interest in real estate to *A*, retaining a life estate.

In 1976, a bank in State *X* loaned *A* 100*x* dollars and as security received a mortgage on the property signed by both *A* and *D*. Under the law of State *X*, *D*, was a guarantor and, as such, had a right of reimbursement against *A*, the primary obligor, in the event *D* was required to pay the loan directly or if *D*'s life estate was sold in foreclosure. *A* was solvent at the time of the loan transaction, and *D* had a reasonable expectation of reimbursement from *A* in the event *D* was required to pay the loan for *A*. At and after *D*'s death, *A* remained solvent and was expected to continue paying the loan.

D died in 1981. Because *D* retained a life estate in the transferred property, the value of property was subject to inclusion in *D*'s gross estate under section 2036 of the Code. The executor of *D*'s estate sought to deduct the mortgage balance alternatively under section 2053(a)(3) or (a)(4) of the Code.

LAW AND ANALYSIS

Section 2036(a)(1) of the Code provides that the gross estate includes the value of all property to the extent of any interest therein of which the decedent has made a transfer under which the decedent retained for life the possession of, enjoyment of, or right to the income from, the property. The statute also provides an exception for bona fide sales for full and adequate consideration in money or money's worth, in which case section 2036 would not be applicable. Section 20.2036-1(a) of the Estate Tax Regulations states that if the decedent retained or reserved an interest or right with respect to all of the transferred property, the entire value of the transferred property is included in the decedent's gross estate.

Section 2053(a)(3) of the Code provides a deduction from the value of the gross estate for claims against the estate. Section 2053(a)(4) provides a deduction for unpaid mortgages on property where the value of the decedent's interest in the property is included in the gross estate.

In Rev. Rul. 76-235, 1976-1 C.B. 277, the decedent gratuitously transferred property in contemplation of death. Subsequent to the transfer and one month prior to the decedent's death, the transferee obtained a loan mortgaging the property to secure the loan. The decedent received no proceeds from the loan, and neither the decedent nor the decedent's estate was liable for the loan.

The ruling holds that the full value of the transferred property is includible in the decedent's gross estate under section 2035 of the Code as in effect prior to amendment by the Tax Reform Act of 1976, and the amount of the mortgage is not deductible from the decedent's gross estate under section 2053 of the Code.

In the present case, the decedent made a transfer described in section 2036 of the full value of the unencumbered remainder interest. The property was encumbered after the transfer, and *D* received no proceeds from the loan. Furthermore, the encumbrance of the property had no immediate effect on *D*'s continued retention of the lifetime enjoyment of the property. Other than as a guarantor, neither *D* nor his estate was liable for the loan. Therefore, in accordance with Rev. Rul. 76-235, the entire value of the property is includible in *D*'s gross estate under section 2036 of the Code, and no deduction is allowed for the mortgage under section 2053(a)(4).

Unlike the situation in Rev. Rul. 76-235, in the present case *D* participated in the loan transaction as guarantor. However, where the decedent is a guarantor, and there is a right of reimbursement, the amount deductible under section 2053(a)(3) cannot exceed the amount the estate actually pays on the debt and is further limited by any expectation of reimbursement. *See Commissioner v. Wragg*, 141 F.2d 638, 640 (lst Cir. 1944); and *Estate of DuVal v. Commissioner*, 4 T.C. 722, 726 (1945), *aff'd*, 152 F.2d 103 (9th Cir. 1945), *cert. denied* 328 U.S. 838 (1945).

If the executor of *D*'s estate is not called upon to pay the indebtedness, the amount of the indebtedness is not deductible as a claim against the estate for purposes of section 2053(a)(3) of the Code. *See* Rev. Rul. 60-247, 1960-2 C.B. 272. If the executor is called upon and pays the indebtedness, the amount of the indebtedness is not deductible for purposes of section 2053 because *A* was solvent at that time and *D*'s estate has a right of