

Initial cash contribution by B	\$ 10,000.00
Subsequent original mortgage payments by B	0
Subsequent portion of refinanced mortgage payments made by B and attributable to the pay-off of the original mortgage	5,000.00
One-half of portion of refinanced mortgage balance outstanding and attributable to pay-off of original mortgage	
	<u>95,000-50,000</u>
	<u>2</u>
	22,500.00
Total contributions by B	\$ 37,500.00
Purchase price of property	\$100,000.00
Portion of purchase price attributable to B's contributions	
$\$37,500 \div \$100,000$.375
Value of property at date of death	\$200,000.00
Portion of value at date of death attributable to B's contributions	
$\$200,000 \times .375$	\$ 75,000.00
Amount includible in A's gross estate \$200,000, value at death, less \$75,000, B's contributions	\$125,000.00
The amount deductible from A's gross estate, under either section 2053 (a) (3) of the Code as a claim against the estate or under section 2053 (a) (4) as an unpaid mortgage on includible property is one-half of the balance due on the refinanced mortgage at the date of death, or \$47,500.00.	

Section 2043.—Transfers For Insufficient Consideration

26 CFR 20.2043-1: Transfer for insufficient consideration.

If a cash loan is made within 3 years of death in exchange for a promissory note that was less than an adequate and full consideration in money or money's worth, under section 2043(a) of the Code, is the promissory note valued as of the date of the transfer or as of the decedent's date of death (or alternate valuation date). See Rev. Rul. 81-286, page 177.

2053 of the Code as an expense of administration.

Rev. Rul. 81-256

D, a resident of State X, died on September 15, 1981. State X imposed a death tax. The executor of D's estate elected, under applicable state law, to extend payment of the state death tax liability. As a result of the extension, the state imposed an interest charge on the unpaid balance of the state death tax from the due date of the return until the date of payment.

Held, the interest expense incurred is deductible as an administration expense under section 2053(a)(2) of the Internal Revenue Code, to the extent the expense is allowable under local law. Interest expense incurred by the estate incident to a deferral, late payment, or deficiency assessment of the federal estate tax liability is an expense necessarily incurred in the administration of the estate and is deductible under section 2053(a)(2) to the extent allowable under local law. See Rev. Rul. 79-252, 1979-2 C.B. 333; Rev. Rul. 80-250, 1980-2 C.B. 278; Rev. Rul. 81-154, 1981-1 C.B. 470. For purposes

of section 2053(a)(2), no distinction should be drawn between interest expense incurred by the estate on the federal estate tax liability and interest expense incurred on the state death tax liability (regardless of whether the state tax is in the nature of an inheritance tax or an estate tax). This conclusion is applicable regardless of the reason for the interest charge.

26 CFR 20.2053-3: Deduction for expenses of administering estate.
(Also Sections 642, 6166, 6166A, 6501; 1.642(g)-1.)

Part IV.—Taxable Estate

Section 2053.—Expenses, Indebtedness, and Taxes

26 CFR 20.2053-1: Deductions for expenses, indebtedness, and taxes; in general.

Whether state gift tax owed at death, which becomes a credit against the state inheritance tax when paid, is deductible as a claim against the estate. See Rev. Rul. 81-302, page 170.

26 CFR 20.2053-3: Deduction for expenses of administering estate.

Administration expenses; interest; state death tax. Interest incurred on the deferral of state death taxes is deductible under section

Administration expenses; interest; installment payment of tax; equitable recoupment. When no waivers were filed under section 642(g) of the Code, all interest expenses actually incurred on the deferred payment of the federal estate tax are deductible under section 2053(a)(2), even though the interest expenses were claimed on the estate's income tax returns and the period of limitations on assessment of income tax has expired for those years. Under the doctrine of equitable recoup-

ment, the amount of the estate tax overpayment is offset by the deficiencies and the interest on them resulting from the deduction of interest on income tax returns for the years for which the period of limitations on assessment of income tax has expired.

Rev. Rul. 81-287

ISSUE

(1) Are interest expenses, incurred on the federal estate tax deferred under section 6166A of the Internal Revenue Code, deductible as administration expenses under section 2053(a)(2) if the interest expenses were claimed as deductions on the estate's income tax returns, no waivers were filed under section 642(g), and the period of limitations on assessment of the estate's income tax has expired?

(2) If these interest expenses are deductible, may the Service, under the doctrine of equitable recoupment, offset the resulting overpayment of estate tax by the barred income tax deficiencies and interest on them resulting from the deduction of these expenses?

FACTS

D died on December 1, 1968. The executor of D's estate filed a timely federal estate tax return on September 1, 1969, and under the predecessor of section 6166A of the Code elected to pay the portion of the estate tax liability that was attributable to a closely held business in ten equal installments. Interest incurred on the deferred payment of estate tax was deducted on the estate's income tax returns filed for the years 1970 through 1977. No waivers required by section 642(g) were filed with any of the income tax returns. On September 1, 1978, the executor paid the final installment of estate tax and interest and filed a claim for refund based on the deduction of all the interest incurred by deferring the payment of the estate tax during the preceding 10 years. The interest incurred on the deferred payment of estate tax is allowable as an administration expense by the laws of the jurisdiction in which D's estate is being administered. The amount of the overpayment of estate tax resulting

from the allowance of the deduction for the actual amount of interest incurred does not exceed the portion of the estate tax paid during the 2 years immediately preceding the filing of the claim for refund.

LAW AND ANALYSIS

Section 2053(a)(2) of the Code provides that the amount of administration expenses allowable by the laws of the jurisdiction under which the estate is being administered is deductible in determining the value of the taxable estate. Section 20.2053-3(a) of the Estate Tax Regulations states that the amount deductible as administration expenses are limited to those expenses that are actually and necessarily incurred in the administration of the decedent's estate.

Section 6166A of the Code (section 6166 prior to the Tax Reform Act of 1976, Pub. L. 94-455, 1976-3 C.B. (Vol. 1) 1) allows the executor, under certain circumstances, to pay the estate tax attributable to closely held business interests in up to ten equal annual installments.

Interest expense payable incident to the extension of the time for payment of tax under section 6166A of the Code is deductible as an expense of administration under section 2053(a)(2), if the expense is allowable under the laws of the jurisdiction in which the estate is being administered. *Estate of Bahr v. Commissioner*, 68 T.C. 74 (1977), acq., 1978-1 C.B. 1; Rev. Rul. 80-250, 1980-2 C.B. 278; Rev. Rul. 78-125, 1978-1 C.B. 292.

Section 642(g) of the Code provides that amounts allowable under section 2053 or 2054 as deductions in computing the taxable estate of a decedent are not allowed as deductions in computing the taxable income of the estate, unless the estate files a statement that the amounts have not been allowed as deductions under section 2053 or 2054 and a waiver of the right to have these amounts allowed at any time as deductions under section 2053 or 2054. Section 1.642(g)-1 of the Income Tax Regulations provides that the statement may be filed at any time before the expiration of the statutory period of limitation applicable to the taxable

year for which the deduction is sought.

Section 642(g) of the Code denies a deduction for income tax purposes if the same item is allowed as a deduction for estate tax purposes. However, there is no basis to deny a deduction for estate tax purposes if the waiver statement under section 642(g) has not been filed. See *Estate of Baldwin v. Commissioner*, T.C.M. 1959-203, involving section 162(e) of the Internal Revenue Code of 1939, which materially corresponds to section 642(g) of the 1954 Code.

In the present situation, because the period of limitations on assessment of the estate's income tax for the years 1975, 1976, and 1977 has not expired, deductions claimed on the fiduciary income tax return for interest expenses that the executor now wants to claim on the estate tax return may be disallowed and additional tax may be assessed. The period of assessment of the estate's income tax for the years from 1970 through 1974 has expired, and no statements waiving the right to claim the interest expenses as deductions on the estate tax return were filed for any of the returns. Therefore, the waiver prescribed by section 642(g) of the Code is not available to prevent the deduction under section 2053(a)(2) of the interest actually incurred during those years.

If an overpayment in one tax liability and a deficiency in another tax liability arise from the same transaction, the doctrine of equitable recoupment allows the Service to recoup the deficiency to the extent of the overpayment, even through the assessment of the deficiency is otherwise barred. See *Stone v. White*, 301 U.S. 532 (1937), Ct. D. 1232, 1937-1 C.B. 224; *Bull v. United States*, 295 U.S. 247 (1935), Ct. D. 969, XIV-1 C.B. 310; *United States v. Herring*, 240 F.2d 225 (4th Cir. 1957); Rev. Rul. 71-56, 1971-1 C.B. 404.

In the present situation, the deficiency and the overpayment result from the deduction of the same interest payments on both the fiduciary income tax return and the estate tax return. Therefore, the amount of the overpayment of estate tax attributable to each interest deduction may be re-

duced by the corresponding income tax deficiency, the assessment of which is barred by the statute of limitation. The amount of the overpayment of estate tax may also be reduced by the interest on the income tax deficiencies, the assessment of which is barred by the statute of limitations. See *Bull; E. I. DuPont DeNemours & Co. v. United States*, 147 F. Supp. 486 (Ct. Cl. 1957).

To determine the amount of the refund, computations must be made to determine the following: (1) the income tax deficiency for each period that results from disallowing the amount of interest deducted on the fiduciary income tax return, (2) the interest on these deficiencies, and (3) the amount of the overpayment of estate tax resulting from the allowance, as a deduction on the estate tax return, of the correct amount of interest incurred on the deferral of estate tax during each period. Each overpayment of the estate tax is then reduced by the income tax deficiency for each period and the interest on it.

Section 6611(a) of the Code provides that interest is allowed and will be paid on any overpayment of any internal revenue tax at an annual rate established under section 6621. Section 301.6611-1(b) of the Regulations on Procedure and Administration provides that there can be no overpayment of tax until the entire tax liability has been satisfied. Therefore, the dates of overpayment of any tax are the date of payment of the first amount that, when added to previous payments, is in excess of the tax liability and the dates of any subsequent tax payments. Section 301.6611-1(g) of the regulations provides that when an overpayment of tax is refunded, interest is allowed from the date of the overpayment to a date not more than 30 days earlier than the date of the refund check.

Therefore, interest on each overpayment of estate tax will be allowed from the determined date of overpayment to a date within 30 days preceding the date the refund is made.

HOLDING

(1) Because no waivers were filed

under section 642(g) of the Code, all interest expenses actually incurred on the deferred payment of the federal estate tax are deductible under section 2053(a)(2), even though the interest expenses were claimed on the estate's income tax returns and the period of limitations on assessment of income tax has expired for those years. (2) Under the doctrine of equitable recoupment, the amount of the estate tax overpayment is offset by the deficiencies and the interest on them resulting from the deduction of interest on income tax returns for the years for which the period of limitations on assessment of income tax has expired.

Section 6166A of the Code has been repealed by the Economic Recovery Tax Act of 1981, Pub. L. 97-34, page 256, 332, this Bulletin, section 422(d), with respect to estates of decedents dying after December 31, 1981. Nevertheless, the equitable recoupment doctrine described in this ruling will apply to similar situations under section 6166 as amended by section 422 of the Act.

26 CFR 20.2053-3: Deduction for expenses of administering estate.

Procedure to be followed by an estate that computes estate tax payable in installments under sections 6166 or 6166A because of allowable interest deduction. See Rev. Proc. 81-27, page 548.

26 CFR 20.2053-7: Deduction for unpaid mortgages.

If a decedent and spouse owned property jointly and a balance is outstanding on both a first and second mortgage at death, what amount is deductible under section 2053 of the Code with respect to the mortgages? See Rev. Rul. 81-183, page 180.

26 CFR 20.2053-7: Deduction for unpaid mortgages.

If a decedent and spouse owned property jointly and a balance is outstanding on a refinanced mortgage on the property at death, what amount is deductible under section 2053 of the Code with respect to the mortgage? See Rev. Rul. 81-184, page 181.

Section 2055.—Transfers For Public, Charitable, and Religious Uses

26 CFR 20.2055-2: Transfers not exclusively for charitable purposes.

May a farm (or family owned business) in which the decedent has transferred a life interest, in trust or otherwise, to a member of the decedent's family with the remainder interest in the property going to a charity be valued under section 2032A of the Code? See Rev. Rul. 81-220, page 175.

Subchapter B.—Estates of Nonresidents Not Citizens

Section 2102.—Credits Against Tax

Is the term "specific exemption" in the estate tax conventions between the United States and Australia, Finland, Greece, Italy, Japan, Norway and Switzerland construed to mean, with respect to the estate of a nonresident alien dying after December 31, 1976, the "unified credit" provided by section 2010 of the Code? See Rev. Rul. 81-303, page 255.

Chapter 12.—Gift Tax

Subchapter A.—Determination of Tax Liability

Section 2505.—Unified Credit Against Gift Tax

Whether the donor's available unified credit must be used to reduce the gift tax in determining the amount of the gift tax liability assumed by the donee. See Rev. Rul. 81-223, page 189.

Subchapter B.—Transfers

Section 2511.—Transfers in General

26 CFR 25.2511-1: Transfers in general.

Whether the payment of split-dollar life insurance policy annual premium and value of annual life insurance protection is a gift. See Rev. Rul. 81-198, page 188.

26 CFR 25.2511-1: Transfers in general.

Whether the value of the gift is reduced by the amount of gift tax attributable to the unified credit, when the gift is made subject to the donee's paying the donor's gift tax liability. See Rev. Rul. 81-223, page 189.

26 CFR 25.2511-2: Cessation of donor's dominion and control.

Transfers; running of statute of