Internal Revenue bulletin

Bulletin No. 2009-44
November 2, 2009

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 2009–35, page 568.

Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate. For purposes of sections 382, 642, 1274, 1288, and other sections of the Code, tables set forth the rates for November 2009.

Notice 2009–83, page 588.

Credit for carbon dioxide sequestration under section 45Q. This notice sets forth interim guidance, pending the issuance of regulations, relating to the credit for carbon dioxide sequestration under section 45Q of the Code. Specifically, the notice provides guidance on determining eligibility for the credit and the amount of the credit, as well as rules regarding adequate security measures for secure geological storage of carbon dioxide. The notice also sets forth a separate reporting requirement.

EXEMPT ORGANIZATIONS

Announcement 2009–78, page 594.

The IRS has revoked its determination that Concerned Residents of Southeast, Inc., of Brewster, NY, qualifies as an organization described in sections 501(c)(3) and 170(c)(2) of the Code.

ESTATE TAX

T.D. 9468, page 570.

Final regulations under section 2053 of the Code relate to the amount deductible from a decedent's gross estate for claims against the estate. In addition, the regulations update the provisions relating to the deduction for certain state death taxes to reflect the statutory amendments made in 2001 to sections 2053(d) and 2058.

Notice 2009–84, page 592.

This notice provides a limited administrative exception to the ability of the Service to examine a Form 706, *United States Estate (and Generation-Skipping Transfer) Tax Return*, in connection with certain Code section 2053 protective claims for refund filed within the time prescribed in section 6511(a).

GIFT TAX

T.D. 9460, page 584.

Final regulations under section 7477 of the Code provide guidance for determining whether a donor may petition the Tax Court for a declaratory judgment with respect to the value of a taxable gift, where the gift does not generate any current gift tax liability.

(Continued on the next page)

Finding Lists begin on page ii.

Department of the Treasury
Internal Revenue Service

ADMINISTRATIVE

T.D. 9460, page 584.

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The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents are compiled semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 42.—Low-Income Housing Credit

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 382.—Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

The adjusted applicable federal long-term rate is set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 412.—Minimum Funding Standards

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 467.—Certain Payments for the Use of Property or Services

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 482.—Allocation of Income and Deductions Among Taxpayers

Federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 483.—Interest on Certain Deferred Payments

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 642.—Special Rules for Credits and Deductions

Federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 807.—Rules for Certain Reserves

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 846.—Discounted Unpaid Losses Defined

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 42, 280G, 382, 412, 467, 468, 482, 483, 642, 807, 846, 1288, 7520, 7872.)

Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate. For purposes of sections 382, 642, 1274, 1288, and other sections of the Code, tables set forth the rates for November 2009.

Rev. Rul. 2009–35

This revenue ruling provides various prescribed rates for federal income tax purposes for November 2009 (the current month). Table 1 contains the short-term, mid-term, and long-term applicable federal rates (AFR) for the current month for purposes of section 1274(d) of the Internal Revenue Code. Table 2 contains the short-term, mid-term, and long-term adjusted applicable federal rates (adjusted AFR) for the current month for purposes of section 1288(b). Table 3 sets forth the adjusted federal long-term rate and the long-term tax-exempt rate described in section 382(f). Table 4 contains the appropriate percentages for determining the low-income housing credit described in section 42(b)(1) for buildings placed in service during the current month. However, under section 42(b)(2), the applicable percentage for non-federally subsidized new buildings placed in service after July 30, 2008, and before December 31, 2013, shall not be less than 9%. Finally, Table 5 contains the federal rate for determining the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest for purposes of section 7520.

REV. RUL. 2009–35 TABLE 1

Applicable Federal Rates (AFR) for November 2009

Period for Compounding

	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-term				
AFR	.71%	.71%	.71%	.71%
110% AFR	.78%	.78%	.78%	.78%
120% AFR	.85%	.85%	.85%	.85%
130% AFR	.92%	.92%	.92%	.92%
Mid-term				
AFR	2.59%	2.57%	2.56%	2.56%
110% AFR	2.85%	2.83%	2.82%	2.81%
120% AFR	3.10%	3.08%	3.07%	3.06%
130% AFR	3.37%	3.34%	3.33%	3.32%
150% AFR	3.90%	3.86%	3.84%	3.83%
175% AFR	4.55%	4.50%	4.47%	4.46%
Long-term				
AFR	4.01%	3.97%	3.95%	3.94%
110% AFR	4.42%	4.37%	4.35%	4.33%
120% AFR	4.82%	4.76%	4.73%	4.71%
130% AFR	5.23%	5.16%	5.13%	5.11%

REV. RUL. 2009–35 TABLE 2

Adjusted AFR for November 2009

Period for Compounding

	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-term adjusted AFR	.80%	.80%	.80%	.80%
Mid-term adjusted AFR	1.89%	1.88%	1.88%	1.87%
Long-term adjusted AFR	3.92%	3.88%	3.86%	3.85%

REV. RUL. 2009–35 TABLE 3

Rates Under Section 382 for November 2009

Adjusted federal long-term rate for the current month	3.92%
Long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months.)	4.33%

REV. RUL. 2009–35 TABLE 4

Appropriate Percentages Under Section 42(b)(1) for November 2009

Note: Under Section 42(b)(2), the applicable percentage for non-federally subsidized new buildings placed in service after July 30, 2008, and before December 31, 2013, shall not be less than 9%.

Appropriate percentage for the 70% present value low-income housing credit	7.76%
Appropriate percentage for the 30% present value low-income housing credit	3.33%

REV. RUL. 2009–35 TABLE 5	
Rate Under Section 7520 for November 2009	
Applicable federal rate for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest	3.2%

Section 1288.—Treatment of Original Issue Discount on Tax-Exempt Obligations

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 2053.—Expenses, Indebtedness, and Taxes

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

This notice provides a limited administrative exception to the ability of the Internal Revenue Service to examine a Form 706 (*United States Estate (and Generation-Skipping Transfer) Tax Return*) in connection with certain protective claims for refund that are based on a deduction under section 2053 of the Internal Revenue Code and are filed within the time prescribed in section 6511(a) of the Code. See Notice 2009-84, page 592.

T.D. 9468

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 20

Guidance Under Section 2053 Regarding Post-Death Events

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final 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 regulations update the provisions relating to the deduction for certain state death taxes to reflect the statutory amendments made in 2001 to sections 2053(d) and 2058. The regulations primarily will affect estates of decedents against which there are claims outstanding at the time of the decedent's death.

DATES: *Effective Date:* The regulations are effective on October 20, 2009.

Applicability Dates: For dates of applicability, see §§20.2051–1(c), 20.2053–1(f), 20.2053–3(e), 20.2053–4(f), 20.2053–6(h), 20.2053–9(f), and 20.2053–10(e).

FOR FURTHER INFORMATION CONTACT: Karlene M. Lesho, (202) 622–3090 (not a toll-free number).

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 amount an estate may deduct for claims against the estate has been a highly litigious issue. See the Background in the notice of proposed rulemaking published in the **Federal Register** on April 23, 2007 (REG–143316–03, 2007–1 C.B. 1292 [72 FR 20080]). Unlike section 2031, section 2053(a) does not contain a specific directive to value a deductible claim at its value at the time of the decedent's death. Section 2053 specifically contemplates expenses such as funeral and administration expenses, which are only determinable after the decedent's death.

The lack of consistency in the case law has resulted in different estate tax treatment of estates that are similarly situated, 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.

Accordingly, in an effort to further the goal of effective and fair administration of the tax laws, the Treasury Department and the IRS published proposed regulations in the **Federal Register** on April 23, 2007. In formulating the proposed rule, the Treasury Department and the IRS carefully considered: the statutory framework and legislative history of section 2053 and its predecessors; the existing regulatory provisions under section 2053, particularly those that are generally applicable to all amounts deductible under section 2053; the numerous judicial decisions involving an issue under section 2053(a)(3) and the analysis and conclusion in each; and, the practical consequences of various possible alternatives for determining the amount deductible under section 2053(a)(3).

The proposed regulations proposed amendments to 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 generally are limited to amounts actually paid by the estate in satisfaction of deductible expenses and claims. The proposed regulations also proposed amendments to address more specifically issues involving final court decisions, settlements, protective claims, reimbursed amounts, claims that are potential, unmatured, or contested, claims involving multiple defendants, claims by a family member or beneficiary of a decedent's estate, unenforceable claims, recurring payments, and the changes made to section 2053(d) in 2001.

Written comments were received on the proposed regulations and a public hearing was held on August 6, 2007. After careful consideration of the written and oral comments, the proposed regulations are adopted as revised by this Treasury decision. In addition, the Treasury Department and the IRS plan to issue additional guidance, including additional proposed regulations, in order to respond to certain comments and emerging issues that the Treasury Department and the IRS believe merit further consideration, as indicated in the Summary.

The comments and revisions to the proposed regulations are discussed in this preamble.

Summary of Comments and Explanation of Revisions

1. *Comments Relating to Prop. Reg. §20.2051–1*

One commentator suggested that the sentence relating to the computation of the taxable estate of a decedent who was not a citizen or resident of the United States should continue to reference the regulations under section 2106, and not the regulations under section 2051. The final regulations restore the reference to the regulations under section 2106.

2. *Comments Relating to the Standard for Deductibility Set Forth in the Proposed Regulation*

The proposed regulations generally provide that only claims actually paid by the estate may be deducted under section 2053(a)(3). Many commentators disagreed with this approach and suggested that claims against a decedent's estate be valued on the basis of what was reasonably known on the date of the decedent's death. These commentators cited the line of cases following the decision in *Ithaca Trust v. Commissioner*, 279 U.S. 151 (1929), to support the same valuation rule for both claims against the estate and claims for inclusion purposes under section 2031. Commentators were concerned that the approach of the proposed regulations could lengthen the process of estate administration (on account of the anticipated increase in the need for protective claims), cause tax motivations to factor into litigation strategy, and produce liquidity shortfalls in estates with both claims by and claims against a decedent. The divergence of court opinions on this issue is evidence that the proper way to deduct claims against an estate is a very difficult issue. After giving serious consideration to the comments submitted on this issue, the Treasury Department and the IRS continue to believe that a deduction for claims under section 2053(a)(3) only for amounts actually paid by the estate most closely aligns with the legislative intent behind section 2053 and its predecessors and best furthers the goal of effective and fair administration of the tax laws. Accordingly, the final regulations generally maintain the approach of the proposed regulations.

Notwithstanding the adherence to the general approach of the proposed regulations, however, the Treasury Department and the IRS acknowledge that, as was pointed out in many of the comments, there are practical difficulties associated with each of the alternatives, including the approach taken in the proposed regulations. In order to make the practical application of the approach more administrable, the final regulations include several exceptions to the approach of the proposed regulations. The final regulations include an exception for claims against the estate with respect to which there is an asset or claim includible in the gross estate that is substantially related to the claim against the estate. See paragraph 10 of this "Summary of Comments and Explanation of Revisions" and §20.2053–4(b). The final regulations also include an exception for claims against the estate that, collectively, do not exceed $500,000 (not including those deductible as ascertainable amounts). See paragraph 5 of this "Summary of Comments and Explanation of Revisions" and §20.2053–4(c). Although both exceptions provide an opportunity to claim a deduction at the time of filing the *United States Estate (and Generation-Skipping Transfer) Tax Return* (Form 706), in each case, the amount of the deduction is subject to adjustment to reflect post-death events, consistent with the general approach of the regulations.

3. *Comments Relating to the Effect of a Court Decree in Prop. Reg. §20.2053–1(b)(2)*

The proposed regulations changed the language regarding a court decree from "the court passes upon the facts upon which deductibility depends" to "the court reviewed the facts relating to the expenditures." A commentator suggested that such a change in language may give the unintended impression that this constitutes a substantive change. Thus, these final regulations remove the language of the proposed regulations and reinstate the original language.

A commentator also requested that an example be added to clarify that the last sentence of Prop. Reg. §20.2053–1(b)(2)(i) would apply to jurisdictions in which a court approves the administration of an estate without specifically approving expenses and claims, absent a challenge from an interested party. The final regulations include such an example.

Some commentators recommended the removal of the requirement that a settlement be within the range of reasonable outcomes under applicable state law in order for a settlement amount to be deductible because the requirement places the Commissioner or a court in the position of having to evaluate the legal merits of a claim adjudicated in another court proceeding. The commentators also maintained that the requirement is superfluous in light of the existing requirements that the settlement resolve a bona fide issue in an active and genuine contest and that adverse parties negotiate at arm's length. The final regulations eliminate the separate requirement that the settlement be within the range of reasonable outcomes under applicable state law.

Some commentators claimed that the rules relating to settlements did not recognize that, in some instances, the cost of defending a claim and the delay associated with litigating the claim will factor into the decision to settle a claim. The final regulations clarify that a deduction will not be denied for a settlement amount otherwise deductible under section 2053 if an estate can establish that the cost of defending the claim or contesting the expense, the delay associated with litigating such claim or expense, or another significant factor will impose a higher burden on the estate relative to the amount paid to settle the claim or the contested expense.

4. *Comments Relating to the Rule for Estimated Amounts in Prop. Reg. §20.2053–1(b)(4)*

The rule provided in Prop. Reg. §20.2053–1(b)(4) involving estimated amounts is now provided in §20.2053–1(d)(4) of these final regulations and the paragraph heading is changed from "[e]stimated amounts" to "[e]xception for certain ascertainable amounts." The final regulations use a consistent description of the rule contained in §20.2053–1(d)(4) where applicable in the remainder of the regulation. No substantive change is intended; rather, the modified paragraph heading in the final regulations is intended to describe the substance of the rule more accurately.

A commentator noted that use of the language "will be paid" in Prop. Reg. §20.2053–1(b)(4) may be inconsistent with the language in Prop. Reg. §20.2053–3(b)(1) ("may reasonably be expected to be paid") and in Prop. Reg. §20.2053–4(b)(7)(i) (claims cannot be estimated if there is "reasonable likelihood that full satisfaction of the liability will not be made"). The commentator suggested modification of the language in Prop. Reg. §20.2053–1(b)(4) to incorporate the reasonableness standard found in the other sections and requested conforming changes throughout the regulation for consistency purposes. The final regulations do not add a reasonableness component to the standard for meeting the "will be paid" requirement, although the final regulations clarify that a deduction is allowed under the rule for deducting certain ascertainable amounts to the extent that the Commissioner is reasonably satisfied that the amount to be paid is ascertainable with reasonable certainty and will be paid. The final regulations use consistent language where applicable in describing the standard for meeting the "will be paid" requirement in each reference to the rule for deducting certain ascertainable amounts.

In addition, some commentators requested clarification on whether the rule previously provided in Prop. Reg. §20.2053–1(b)(4) applies not only to claims but to administration expenses as well. The final regulations make the requested clarification and §20.2053–1(d)(4) provides that the rule for deducting certain ascertainable amounts applies to both a claim and an expense.

A commentator suggested that the statement in Prop. Reg. §20.2053–1(b)(4) prohibiting a deduction for "a vague or uncertain estimate" be omitted because it puts forth a subjective standard open to a wide range of interpretations. The Treasury Department and the IRS believe that the rule previously provided in Prop. Reg. §20.2053–1(b)(4), now provided in §20.2053–1(d)(4) of these final regulations, sets forth clear requirements for determining the amount allowable as a deduction under section 2053. Because the statement in Prop. Reg. §20.2053–1(b)(4) merely clarifies this rule, the statement has been retained in the final regulations.

A commentator suggested that the language in Prop. Reg. §20.2053–1(b)(4), indicating that a deduction in advance of payment will be disallowed if the payment is thereafter waived or otherwise left unpaid, negates the purpose of allowing a deduction for an estimated amount and should be deleted. However, the Treasury Department and the IRS believe that there is an important difference. The rule for deducting certain ascertainable amounts previously provided in Prop. Reg. §20.2053–1(b)(4), and now provided in §20.2053–1(d)(4) of these final regulations, provides an estate with the opportunity to claim a deduction at the time of filing Form 706, even though the amount ultimately allowable as a deduction under this rule will take into account events occurring after the date of a decedent's death. The ability to deduct an ascertainable amount does not change the general rule that the amount of the deduction is to reflect post-death events.

Some commentators questioned whether the proposed regulations impose a duty on the executor to report amounts that were claimed as deductions on the estate tax return, but were subsequently not paid or not paid in full, and whether such a duty could be enforced after the period of limitations on assessment has expired. The Treasury Department and the IRS did not intend for the proposed regulations to impose a duty on the executor that could be enforced after the expiration of the period of limitations on assessment. As a result, the final regulations eliminate this provision. The final regulations also include a provision clarifying the period during which post-death events will be considered.

5. *Comments Relating to Protective Claims*

A commentator expressed concern that the protective claim procedures in the proposed regulations would result in increased administrative costs and a delay in the administration of the estate because filing a protective claim effectively would keep the period of limitations open to the extent of the amount of the claim for refund. The Treasury Department and the IRS believe that protective claims for refund are an appropriate and necessary component of these regulations, as they provide a mechanism to ensure that the deductibility rule provided for in these regulations is implemented in a fair and equitable manner. Nevertheless, the Treasury Department and the IRS acknowledge that the commentator's concern is valid. In an effort to make the regulation more administrable for both taxpayers and the Commissioner, the final regulations in §20.2053–4(c) include an exception for claims against the estate that do not exceed, in the aggregate, $500,000. Because the purpose of this provision is to provide certain relief from the need to file a protective claim, a claim is not eligible for this provision unless the entire amount of the claim may be covered within this cap. This rule allows an estate a deduction on Form 706 for claims against the estate. However, consistent with the general approach of the final regulations, the amount of the deduction is subject to adjustment to reflect post-death events. To address the commentator's concern regarding the effect of a protective claim for refund on the applicable period of limitations, the Treasury Department and the IRS are issuing, concurrent with this regulation, a notice announcing the IRS's decision to limit the review of a return, in certain circumstances, when a timely-filed claim for refund of estate taxes that is based on a deduction under section 2053 ripens after the expiration of the limitations period on assessment.

Some commentators requested more detailed guidance on the procedures for filing a protective claim for refund. In response to this comment, the final regulations include a provision under §20.2053–1(d)(5) to explain the protective claim for refund process. The Treasury Department and the IRS also intend to provide, by publication in the Internal Revenue Bulletin, further procedural guidance on protective claims for refund due to section 2053 claims or expenses. In addition, a commentator suggested that Form 706 be revised to incorporate a protective claim for refund so that a separate form need not be filed. The Treasury Department and the IRS believe this suggestion will make the final regulations more administrable and are contemplating amending Form 706 to implement this suggestion.

Another commentator suggested that the IRS be lenient in granting extensions of time to pay the estate tax under section 6161 when an estate is confronting a liquidity issue arising from the inability to deduct a claim that is the subject of a protective claim for refund. Although in many cases the illiquidity resulting from a not-yet-deductible claim may be reasonable cause for granting an extension of time to pay the estate tax for purposes of section 6161, the Treasury Department and the IRS believe that any regulatory provision implementing this suggestion would be outside the scope of this regulation.

6. *Comments Relating to the Effect on the Marital and Charitable Deductions*

Some commentators requested clarification of the impact of the approach taken in the proposed regulations on the marital and charitable deductions in estates where a claim or expense is payable in whole or in part from a bequest that qualifies for the marital or charitable deduction. Commentators requested that the final regulations include a rule confirming that, if a claim or expense is the subject of a protective claim for refund under section 2053 and is payable out of a fund that meets the requirements for a charitable or marital deduction under section 2055 or 2056, respectively, the charitable or marital deduction will not be reduced by the amount of the claim or expense until the amount is actually paid. In the interest of enhancing the administrability of these regulations, such a rule is included in §20.2053–1(d)(5)(ii). The Treasury Department and the IRS view this rule as similar to the rules in the regulations under sections 2055 and 2056 that provide, respectively, for the reduction of the value of the charitable or marital share by the amount of estate transmission expenses paid from the charitable or marital share. For purposes of the estate tax charitable deduction under section 2055, a claim or expense that is the subject of a protective claim for refund under section 2053 will not render the charitable deduction, to the extent of the amount of that claim or expense, contingent and thus nondeductible under section 2055.

7. *Comments Relating to Reimbursements, Prop. Reg. §20.2053–1(b)(3)*

The proposed regulations provide that a deduction is not allowed to the extent that the expense or claim is or could be compensated for by insurance or is or could be otherwise reimbursed. A commentator recommended that the final regulations explain the method by which an executor may establish that there is no available reimbursement either from another party or insurance. In response to this comment, the final regulations provide that an executor may certify on Form 706 that no reimbursement is available for a claim or expense if the executor neither knows nor reasonably should have known of the availability of any such reimbursement.

Additionally, some commentators recommended that the final regulations reflect the possibility that the cost of obtaining the reimbursement might outweigh the benefit of reimbursement. In response, the final regulations provide that an executor need not reduce the amount of a claim or expense deductible under section 2053 by the amount of a potential reimbursement if the executor provides a reasonable explanation on Form 706 for his or her reasonable determination that the burden of necessary collection efforts would outweigh the anticipated benefits from those efforts.

8. *Comments Relating to Deduction for Expenses of Administering Estate under Prop. Reg. §20.2053–3*

A commentator recommended removing from Prop. Reg. §20.2053–3(b) and (c) any language restating the general requirements for deductibility set forth in Prop. Reg. §20.2053–1 and the general rules regarding protective claims. The commentator suggested that duplicating the language in Prop. Reg. §20.2053–3(b) and (c) was unnecessary and perhaps confusing. In response, the final regulations remove the language that merely restates the general rules set forth in Prop. Reg. §20.2053–1.

Some commentators recommended omitting the sentence in Prop. Reg. §20.2053–3(d)(3) that prohibits a deduction for expenses incurred merely for the purpose of unreasonably extending the time for payment, or incurred other than in good faith. The commentators stated that a situation where litigation has been intentionally prolonged other than in good faith is rare and unlikely to occur. Furthermore, the commentators expressed concern that the rule may subject the estate's legal strategy to IRS inquiry. Finally, the commentators maintained that it would be extremely difficult to prove that litigation expenses have not been incurred to unreasonably extend the time for payment or other than in good faith. The Treasury Department and the IRS find these comments persuasive and additionally believe that including this sentence in the final regulations is not necessary because expenses incurred merely for the purpose of unreasonably extending the time for payment or other than in good faith will not be considered actually and necessarily incurred in the administration of the decedent's estate and, therefore, are not deductible for that reason.

9. *Comments Relating to Claims Against the Estate, Prop. Reg. §20.2053–4(a)*

The proposed regulations provide that deductible claims against a decedent's estate are limited to legitimate and bona fide claims. A commentator stated that the terms "legitimate" and "bona fide" in Prop.

Reg. §20.2053–4(a)(1) are redundant. The final regulations remove the term "legitimate" and provide that deductible claims against a decedent's estate are limited to bona fide claims.

A commentator requested clarification that the Commissioner shall be bound in the same manner as the estate to consider events occurring after the date of a decedent's death when determining the amount deductible by the decedent's estate. The Treasury Department and the IRS believe that the rule of Prop. Reg. §20.2053–4(a)(2) sets forth a general principle that governs the determination of the amount deductible against a decedent's estate, and that therefore is binding on both estates and the Commissioner. Accordingly, no change is believed to be necessary.

10. *Comments Relating to Claims and Counterclaims*

Some commentators, citing fairness and liquidity concerns, suggested allowing a deduction for a claim against the estate on the initial filing of Form 706 if the value of the gross estate includes a claim in the same or a substantially-related matter or includes an asset integrally related or subject to the claim against the estate. The Treasury Department and the IRS find this suggestion persuasive when a decedent's substantially-related claim against a third party or a decedent's integrally-related asset constitutes a significant percentage of the gross estate. The final regulations under §20.2053–4(b) provide that the current value of a claim against the estate with respect to which there is one or more substantially-related claims or integrally-related assets that are included in a decedent's gross estate may be deducted on Form 706, provided that the related claim or asset of the estate constitutes at least 10 percent of the decedent's gross estate, the value of each such claim against the estate is determined from a "qualified appraisal" performed by a "qualified appraiser" (within the meaning of section 170 of the Code and the corresponding regulations), and the value of each such claim against the estate is subject to adjustment to reflect post-death events. The deductible amount of each such claim is limited to the value of the related asset or claim included in the gross estate. The amount of the claim against the estate in excess of this limitation may be the subject of a protective claim for refund.

11. *Comments Relating to Prop. Reg. §20.2053–4(b)(4), Claims by Family Members, Related Entities, or Beneficiaries*

The proposed regulations include a rebuttable presumption that claims by a family member of the decedent, a related entity, or a beneficiary of the decedent's estate or a revocable trust are not legitimate and bona fide. Many commentators requested that the rebuttable presumption be removed from the regulation. A commentator suggested that the presumption be replaced by a provision requiring close scrutiny of claims by family members, related entities, or beneficiaries. Although such claims are in fact closely scrutinized during the examination of a return, the Treasury Department and the IRS believe that a regulatory provision prescribing the level of scrutiny to be given a particular item is not appropriate for this regulation.

Other commentators stated that the presumption is inconsistent with the burden of proof provision of section 7491 and that such a presumption should apply only when the facts indicate possible collusion. After careful consideration, the Treasury Department and the IRS have concluded that the rebuttable presumption in the proposed regulations does not conflict with section 7491.

Some commentators maintained that the presumption is unfair and unwarranted because the proposed regulations and the burden of proof provisions adequately deter the manipulation of claims by family members, related entities or beneficiaries. The Treasury Department and the IRS carefully considered these comments and, in response to the enumerated concerns with the creation of a rebuttable presumption, have removed the presumption from the final regulations. Instead, the final regulations continue to include the generally applicable requirement that any claim or expense deductible under section 2053 must be bona fide in nature, but also include a paragraph that (as suggested by a commentator) provides a nonexclusive list of factors indicative of the bona fide nature of a claim or expense involving a family member, related entity, or beneficiary of the estate of a decedent.

12. *Comments Relating to Payments in Prop. Reg. §20.2053–4(b)(5)*

A commentator suggested removing the rule in Prop. Reg. §20.2053–4(b)(5) providing that claims that are unenforceable prior to or at the decedent's death are not deductible even if paid. The Treasury Department and the IRS believe that this rule is mandated by the statutory requirement that only amounts allowable by the laws of the jurisdiction under which the estate is being administered may be deducted from the value of the gross estate. Therefore, this suggestion has not been adopted.

13. *Comments Relating to Recurring Payments in Prop. Reg. §20.2053–4(b)(7)*

The proposed regulations provide that certain recurring, noncontingent obligations may be deducted as estimated amounts. Some commentators suggested that not allowing an estate to deduct the value of a contingent obligation is inefficient and inequitable because it forces the estate to remain open unless the estate purchases a commercial annuity. The Treasury Department and the IRS acknowledge that a contingent obligation may extend the period of estate administration unless the estate purchases a commercial annuity to satisfy the obligation or makes distributions that are encumbered by the contingent obligation. However, the Treasury Department and the IRS believe that allowing a deduction for a noncontingent recurring payment as an ascertainable amount (deductible under §20.2053–1(d)(4) of the final regulations), but not allowing a deduction for a contingent recurring payment until paid is a necessary component of the rules of deductibility provided for in these regulations. Nevertheless, the Treasury Department and the IRS believe that the purchase of a commercial annuity (with a cost determined by the market and based on the particular contingency) to fund a contingent obligation should be deemed to be substantially equivalent to a reasonably ascertainable (and thus deductible) noncontingent obligation for purposes of section 2053 and these regulations.

Some commentators requested clarification on whether death or remarriage is considered a contingency with respect to decedent's obligation to make a recurring payment. The final regulations clarify that, for purposes of section 2053, an obligation subject to death or remarriage is treated as a noncontingent obligation under §20.2053–4(d)(6)(i).

Some commentators suggested that the disparate treatment afforded noncontingent obligations (deduction for present value of obligations) versus contingent obligations (dollar-for-dollar deduction as paid) is inequitable and produces an inconsistent result without meaningful justification. These commentators requested that the final regulations allow an estate to choose between deducting the present value of a noncontingent recurring payment on the estate tax return, or instead deducting the amounts paid in the same manner as provided for a contingent obligation (after filing an appropriate protective claim for refund). The Treasury Department and the IRS find the arguments against the disparate treatment of noncontingent and contingent obligations to be persuasive. The final regulations eliminate the disparate treatment by removing the present value limitation applicable only to noncontingent recurring payments. The Treasury Department and the IRS believe that the issue of the appropriate use of present value in determining the amount of the deduction allowable under section 2053 merits further consideration. The final regulations reserve §20.2053–1(d)(6) to provide future guidance on this issue.

A commentator requested clarification on whether the rule in Prop. Reg. §20.2053–4(b)(7) will or will not apply to mortgages and other indebtedness under a note. The final regulations clarify that the rules applicable to recurring payments do not apply to payments made in connection with a mortgage or other indebtedness described in §20.2053–7.

Finally, a commentator requested further guidance on the commercial annuity provision; specifically, whether the executor must transfer ownership of the purchased annuity to the creditor or to a third party who will use the annuity to make payments to the creditor, or whether granting the creditor a security interest in the annuity is sufficient in order for the amount paid for the annuity to be deductible under section 2053. For income tax purposes, the transfer of the annuity is likely to cause immediate gain recognition of the entire amount to the transferee unless the annuity meets several specific requirements. In light of the purpose and intent of these regulations, the Treasury Department and the IRS believe that the purchase of a commercial annuity, and the nonrefundable and generally significant costs involved in that purchase, should be sufficient to permit a deduction of the cost of the annuity for purposes of section 2053. For these reasons, the final regulations clarify that the estate may be permitted to own the annuity.

Special Analyses

It has been determined that this Treasury decision 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 regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Karlene M. Lesho, Office of the Associate Chief Counsel (Passthroughs and Special Industries). Other personnel from the IRS and the Treasury Department participated in their development.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 20 is 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) *General rule*. The taxable estate of a decedent who was a citizen or resident (see §20.0–1(b)(1)) of the United States at death is determined by subtracting the total amount of the deductions authorized by sections 2053 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) Funeral and administration expenses and claims against the estate (including certain taxes and charitable pledges) (section 2053).

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

(3) Charitable transfers (section 2055).

(4) The marital deduction (section 2056).

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

(6) Family-owned business interests (section 2057) to the extent applicable to estates of decedents.

(7) State death taxes (section 2058) to the extent applicable to estates of decedents.

(b) *Special rules*. See section 2106 and the corresponding regulations for special rules regarding 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/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

Par. 3. Section 20.2053–1 is amended by:

1. Revising paragraphs (a), (b)(2), (b)(3), and adding paragraph (b)(4).

2. Redesignating paragraph (d) as paragraph (e).

3. Adding paragraphs (d) and (f).

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) * * *

(2) *Bona fide requirement*—(i) *In general*. Amounts allowed as deductions under section 2053(a) and (b) must be expenses and claims that are bona fide in nature. No deduction is permissible to the extent it is founded on a transfer that is essentially donative in character (a mere cloak for a gift or bequest) except to the extent the deduction is for a claim that would be allowable as a deduction under section 2055 as a charitable bequest.

(ii) *Claims and expenses involving family members*. Factors indicative (but not necessarily determinative) of the bona fide nature of a claim or expense involving a family member of a decedent, a related entity, or a beneficiary of a decedent's estate or revocable trust, in relevant instances, may include, but are not limited to, the following—

(A) The transaction underlying the claim or expense occurs in the ordinary course of business, is negotiated at arm's length, and is free from donative intent.

(B) The nature of the claim or expense is not related to an expectation or claim of inheritance.

(C) The claim or expense originates pursuant to an agreement between the decedent and the family member, related entity, or beneficiary, and the agreement is substantiated with contemporaneous evidence.

(D) Performance by the claimant is pursuant to the terms of an agreement between the decedent and the family member, related entity, or beneficiary and the performance and the agreement can be substantiated.

(E) All amounts paid in satisfaction or settlement of a claim or expense are reported by each party for Federal income and employment tax purposes, to the extent appropriate, in a manner that is consistent with the reported nature of the claim or expense.

(iii) *Definitions*. The following definitions apply for purposes of this paragraph (b)(2):

(A) *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.

(B) 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 30 percent of the beneficial ownership interests (whether voting or non-voting and whether an interest in stock, capital and/or profits), as determined at the time a claim described in this section is being asserted. Notwithstanding the foregoing, an entity in which the decedent, directly or indirectly, had any managing interest (for example, as a general partner of a partnership or as a managing member of a limited liability company) at the time of the decedent's death shall be considered a related entity.

(C) *Beneficiaries* of a decedent's estate include beneficiaries of a trust of the decedent.

(3) *Court decrees and settlements*—(i) *Court decree*. If a court of competent jurisdiction over the administration of an estate reviews and approves expenditures for funeral expenses, administration expenses, claims against the estate, or unpaid mortgages (referred to in this section as a "claim or expense"), a final judicial decision in that matter may be relied upon to establish the amount of a claim or expense that is otherwise deductible under section 2053 and these regulations provided that the court actually passes upon the facts on which deductibility depends. If the court does not pass upon those facts, its decree may not be relied upon to establish the amount of the claim or expense that is otherwise deductible under section 2053. It must appear that the court actually passed upon the merits of the claim. This will be presumed in all cases of an active and genuine contest. If the result reached appears to be unreasonable, this is some evidence that there was not such a contest, but it may be rebutted by proof to the contrary. Any amount meeting the requirements of this paragraph (b)(3)(i) is deductible to the extent it actually has been paid or will be paid, subject to any applicable limitations in this section.

(ii) *Claims and expenses where court approval not required under local law*. A deduction for the amount of a claim or expense that is otherwise deductible under section 2053 and these regulations will not be denied under section 2053 solely because a local court decree has not been entered with respect to such amount, provided that no court decree is required under applicable law to determine the amount or allowability of the claim or expense.

(iii) *Consent decree*. A local court decree rendered by consent may be relied on to establish the amount of a claim or expense that is otherwise deductible under section 2053 and these regulations provided that the consent resolves a bona fide issue in a genuine contest. Consent given by all parties having interests adverse to that of the claimant will be presumed to resolve a bona fide issue in a genuine contest. Any amount meeting the requirements of this paragraph (b)(3)(iii) is deductible to the extent it actually has been paid or will be paid, subject to any applicable limitations in this section.

(iv) *Settlements*. A settlement may be relied on to establish the amount of a claim or expense (whether contingent or noncontingent) that is otherwise deductible under section 2053 and these regulations, provided that the settlement resolves a bona fide issue in a genuine contest and is the product of arm's-length negotiations by parties having adverse interests with respect to the claim or expense. A deduction will not be denied for a settlement amount paid by an estate if the estate can establish that the cost of defending or contesting the claim or expense, or the delay associated with litigating the claim or expense, would impose a higher burden on the estate than the payment of the amount paid to settle the claim or expense. Nevertheless, no deduction will be allowed for amounts paid in settlement of an unenforceable claim.

For this purpose, to the extent a claim exceeds an applicable limit under local law, the claim is deemed to be unenforceable. However, as long as the enforceability of the claim is at issue in a bona fide dispute, the claim will not be deemed to be unenforceable for this purpose. Any amount meeting the requirements of this paragraph (b)(3)(iv) is deductible to the extent it actually has been paid or will be paid, subject to any applicable limitations in this section.

(v) *Additional rules*. Notwithstanding paragraph (b)(3)(i) through (iv) of this section, additional rules may apply to the deductibility of certain claims and expenses. 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.

(4) *Examples*. Unless otherwise provided, assume that the amount of any claim or expense is paid out of property subject to claims and is paid within the time prescribed for filing the *United States Estate (and Generation-Skipping Transfer) Tax Return,* Form 706. The following examples illustrate the application of this paragraph (b):

Example 1. Consent decree at variance with the law of the State. Decedent's (D's) estate is probated in State. D's probate estate is valued at $100x. State law provides that the executor's commission shall not exceed 3 percent of the probate estate. A consent decree is entered allowing the executor's commission in the amount of $5x. The estate pays the executor's commission in the amount of $5x. For purposes of section 2053, the executor may deduct only $3x of the $5x expense paid for the executor's commission because the amount approved by the consent decree in excess of $3x is in excess of the applicable limit for executor's commissions under local law. Therefore, for purposes of section 2053, the consent decree may not be relied upon to establish the amount of the expense for the executor's commission.

Example 2. Decedent's (D's) estate is probated in State. State law grants authority to an executor to administer an estate without court approval, so long as notice of and a right to object to a proposed action is provided to interested persons. The executor of D's estate (E) proposes to sell property of the estate in order to pay the debts of D. E gives requisite notice to all interested parties and no interested person objects. E sells the real estate and pays a real estate commission of $20x to a professional real estate agent. The amount of the real estate commission paid does not exceed the applicable limit under State law. Provided that the sale of the property was necessary to pay D's debts, expenses of administration, or taxes, to preserve the estate, or to effect distribution, the executor may deduct the $20x expense for the real estate commission under section 2053 even though no court decree was entered approving the expense.

Example 3. Claim by family member. For a period of three years prior to D's death, D's niece (N) provides accounting and bookkeeping services on D's behalf. N is a CPA and provides similar accounting and bookkeeping services to unrelated clients. At the end of each month, N presents an itemized bill to D for services rendered. The fees charged by N conform to the prevailing market rate for the services rendered and are comparable to the fees N charges other clients for similar services. The amount due is timely paid each month by D and is properly reported for Federal income and employment tax purposes by N. In the six months prior to D's death, D's poor health prevents D from making payments to N for the amount due. After D's death, N asserts a claim against the estate for $25x, an amount representing the amount due for the six-month period prior to D's death. D's estate pays $25x to N in satisfaction of the claim before the return is timely filed and N properly reports the $25x received by E for income tax purposes. Barring any other relevant facts or circumstances, E may rely on the following factors to establish that the claim is bona fide: (1) N's claim for services rendered arose in the ordinary course of business, as N is a CPA performing similar services for other clients; (2) the fees charged were deemed to be negotiated at arm's length, as the fees were consistent with the fees N charged for similar services to unrelated clients; (3) the billing records and the records of D's timely payments to N constitute contemporaneous evidence of an agreement between D and N for N's bookkeeping services; and (4) the amount of the payments to N is properly reported by N for Federal income and employment tax purposes. E may deduct the amount paid to N in satisfaction of the claim.

* * * * *

(d) *Amount deductible*—(1) *General rule*. To take into account properly events occurring after the date of a decedent's death in determining the amount deductible under section 2053 and these regulations, the deduction for any claim or expense described in paragraph (a) of this section is limited to the total amount actually paid in settlement or satisfaction of that item (subject to any applicable limitations in this section). However, see paragraph (d)(4) of this section for the rules for deducting certain ascertainable amounts; see §20.2053–4(b) and (c) for the rules regarding the deductibility of certain claims against the estate; and see §20.2053–7 for the rules regarding the deductibility of unpaid mortgages and other indebtedness.

(2) *Application of post-death events*. In determining whether and to what extent a deduction under section 2053 is allowable, events occurring after the date of a decedent's death will be taken into consideration—

(i) Until the expiration of the applicable period of limitations on assessment prescribed in section 6501 (including without limitation at all times during which the running of the period of limitations is suspended); and

(ii) During subsequent periods, in determining the amount (if any) of an overpayment of estate tax due in connection with a claim for refund filed within the time prescribed in section 6511(a).

(3) *Reimbursements*. A deduction is not allowed to the extent that a claim or expense described in paragraph (a) of this section is or could be compensated for by insurance or otherwise could be reimbursed. If the executor is able to establish that only a partial reimbursement could be collected, then only that portion of the potential reimbursement that reasonably could have been expected to be collected will reduce the estate's deductible portion of the total claim or expense. An executor may certify that the executor neither knows nor reasonably should have known of any available reimbursement for a claim or expense described in section 2053(a) or (b) on the estate's *United States Estate (and Generation-Skipping Transfer) Tax Return* (Form 706), in accordance with the instructions for that form. A potential reimbursement will not reduce the deductible amount of a claim or expense to the extent that the executor, on Form 706 and in accordance with the instructions for that form, provides a reasonable explanation for his or her reasonable determination that the burden of necessary collection efforts in pursuit of a right of reimbursement would outweigh the anticipated benefit from those efforts. Nevertheless, even if a reasonable explanation is provided, subsequent events (including without limitation an actual reimbursement) occurring within the period described in §20.2053–1(d)(2) will be considered in determining the amount (if any) of a reduction under this paragraph (d)(3) in the deductible amount of a claim or expense.

(4) *Exception for certain ascertainable amounts*—(i) *General rule*. A deduction will be allowed for a claim or expense that satisfies all applicable requirements even though it is not yet paid, provided that the amount to be paid is ascertainable with rea-

sonable certainty and will be paid. For example, executors' commissions and attorneys' fees that are not yet paid, and that meet the requirements for deductibility under §20.2053–3(b) and (c), respectively, are deemed to be ascertainable with reasonable certainty and may be deducted if such expenses will be paid. However, no deduction may be taken upon the basis of a vague or uncertain estimate. To the extent a claim or expense is contested or contingent, such a claim or expense cannot be ascertained with reasonable certainty.

(ii) *Effect of post-death events*. A deduction under this paragraph (d)(4) will be allowed to the extent the Commissioner is reasonably satisfied that the amount to be paid is ascertainable with reasonable certainty and will be paid. In making this determination, the Commissioner will take into account events occurring after the date of a decedent's death. To the extent the amount for which a deduction was claimed does not satisfy the requirements of this paragraph (d)(4), and is not otherwise deductible, the deduction will be disallowed by the Commissioner. If a deduction is claimed on Form 706 for an amount that is not yet paid and the deduction is disallowed in whole or in part (or if no deduction is claimed on Form 706), then if the claim or expense subsequently satisfies the requirements of this paragraph (d)(4) or is paid, relief may be sought by filing a claim for refund. To preserve the estate's right to claim a refund for amounts becoming deductible after the expiration of the period of limitation for the filing of a claim for refund, a protective claim for refund may be filed in accordance with paragraph (d)(5) of this section.

(5) *Protective claim for refund*—(i) *In general*. A protective claim for refund under this section may be filed at any time before the expiration of the period of limitation prescribed in section 6511(a) for the filing of a claim for refund to preserve the estate's right to claim a refund by reason of claims or expenses that are not paid or do not otherwise meet the requirements of deductibility under section 2053 and these regulations until after the expiration of the period of limitation for filing a claim for refund. Such a protective claim shall be made in accordance with guidance that may be provided from time to time by publication in the Internal Revenue Bulletin (see §601.601(d)(2)(ii)(*b*)). Although the protective claim need not state a particular dollar amount or demand an immediate refund, a protective claim must identify each outstanding claim or expense that would have been deductible under section 2053(a) or (b) if such item already had been paid and must describe the reasons and contingencies delaying the actual payment of the claim or expense. Action on protective claims will proceed after the executor has notified the Commissioner within a reasonable period that the contingency has been resolved and that the amount deductible under §20.2053–1 has been established.

(ii) *Effect on marital and charitable deduction*. To the extent that a protective claim for refund is filed with respect to a claim or expense that would have been deductible under section 2053(a) or (b) if such item already had been paid and that is payable out of a share that meets the requirements for a charitable deduction under section 2055 or a marital deduction under section 2056 or section 2056A, or from a combination thereof, neither the charitable deduction nor the marital deduction shall be reduced by the amount of such claim or expense until the amount is actually paid or meets the requirements of paragraph (d)(4) of this section for deducting certain ascertainable amounts or the requirements of §20.2053–4(b) or (c) for deducting certain claims against the estate.

(6) [Reserved].

(7) *Examples*. Assume that the amounts described in section 2053(a) 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 outside of the United States. Assume that the claims against the estate are not deductible under §20.2053–4(b) or (c). Also assume, unless otherwise provided, that none of the limitations on the amount of the deduction described in this section apply to the deduction claimed under section 2053. The following examples illustrate the application of this paragraph (d):

Example 1. Amount of expense 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 Form 706 filed for D's estate under the rule for deducting certain ascertainable amounts set forth in paragraph (d)(4) of this section, provided that the estimated amount will be paid. However, the Commissioner will disallow the deduction upon examination of the estate's Form 706 to the extent that the amount for which a deduction was claimed no longer satisfies the requirements of paragraph (d)(4) of this section. If this occurs, E may file a protective claim for refund in accordance with paragraph (d)(5) of this section in order to preserve the estate's right to claim a refund for the amount of the fee that is subsequently paid or that subsequently meets the requirements of paragraph (d)(4) of this section for deducting certain ascertainable amounts.

Example 2. Amount of claim not ascertainable. Prior to death, Decedent (D) is sued by Claimant (C) for $100x 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 of D's estate (E) may not claim a deduction with respect to C's claim on D's Form 706 under the special rule contained in paragraph (d)(4) of this section because the deductible amount cannot be ascertained with reasonable certainty. However, E may file a timely protective claim for refund in accordance with paragraph (d)(5) of this section in order to preserve the estate's right to subsequently claim a refund at the time a final judgment is entered in the case and the claim is either paid or meets the requirements of paragraph (d)(4) of this section for deducting certain ascertainable amounts.

Example 3. Amount of claim payable out of property qualifying for marital deduction. The facts are the same as in *Example 2* except that the applicable credit amount, under section 2010, against the estate tax was fully consumed by D's lifetime gifts, D is survived by Spouse (S), and D's estate passes entirely to S in a bequest that qualifies for the marital deduction under section 2056. Even though any amount D's estate ultimately pays with respect to C's claim will be paid from the assets qualifying for the marital deduction, in filing Form 706, E need not reduce the amount of the marital deduction claimed on D's Form 706. Instead, pursuant to the protective claim for refund filed by E, the marital deduction will be reduced by the claim once a final judgment is entered in the case. At that time, a deduction will be allowed for the amount that is either paid or meets the requirements of paragraph (d)(4) of this section for deducting certain ascertainable amounts.

* * * * *

(f) *Effective/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

Par. 4. Section 20.2053–3 is amended by:

1. Revising paragraph (b)(1) and the second sentence of paragraph (b)(2).

2. Revising paragraph (c)(1) and the second sentence of paragraph (c)(2).

3. Revising the second sentence of paragraph (d)(1) and the first sentence of paragraph (d)(2).

4. Adding paragraphs (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) Executors' commissions are deductible to the extent permitted by §20.2053–1 and this section, but no deduction may be taken if no commissions are to be paid. In addition, the amount of the commissions claimed as a deduction must be in accordance with the usually accepted standards and practice of allowing such an amount in estates of similar size and character in the jurisdiction in which the estate is being administered, or any deviation from the usually accepted standards or range of amounts (permissible under applicable local law) must be justified to the satisfaction of the Commissioner.

(2) * * * If, however, the terms of the will set forth the compensation payable to the executor for services to be rendered in the administration of the estate, a deduction may be taken to the extent that the amount so fixed does not exceed the compensation allowable by the local law or practice and to the extent permitted by §20.2053–1.

* * * * *

(c) *Attorney's fees*—(1) Attorney's fees are deductible to the extent permitted by §20.2053–1 and this section. Further, the amount of the fees claimed as a deduction may not exceed a reasonable remuneration for the services rendered, taking into account the size and character of the estate, the law and practice in the jurisdiction in which the estate is being administered, and the skill and expertise of the attorneys.

(2) * * * A deduction for reasonable attorney's fees actually incurred in contesting an asserted deficiency or in prosecuting a claim for refund will be allowed to the extent permitted by §20.2053–1 even though the deduction, as such, was not claimed on the estate tax return or in the claim for refund. * * *

* * * * *

(d) * * *

(1) * * * Expenses necessarily incurred in preserving and distributing the estate, including the cost of storing or maintaining property of the estate if it is impossible to effect immediate distribution to the beneficiaries, are deductible to the extent permitted by §20.2053–1. * * *

(2) Expenses for selling property of the estate are deductible to the extent permitted by §20.2053–1 if the sale is necessary in order to pay the decedent's debts, expenses of administration, or taxes, to preserve the estate, or to effect distribution. * * *

(3) Expenses incurred in defending the estate against claims described in section 2053(a)(3) are deductible to the extent permitted by §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 ultimately does not prevail. For purposes of this paragraph (d)(3), "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.

(e) *Effective/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

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) *General rule*. For purposes of this section, liabilities imposed by law or arising out of contracts or torts are deductible if they meet the applicable requirements set forth in §20.2053–1 and this section. To be deductible, a claim against a decedent's estate must represent a personal obligation of the decedent existing at the time of the decedent's death. Except as otherwise provided in paragraphs (b) and (c) of this section and to the extent permitted by §20.2053–1, the amounts that may be deducted as claims against a decedent's estate are limited to the amounts of bona fide claims that are enforceable against the decedent's estate (and are not unenforceable when paid) and claims that—

(i) Are actually paid by the estate in satisfaction of the claim; or

(ii) Meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

(2) *Effect of post-death events*. Events occurring after the date of a decedent's death shall be considered in determining whether and to what extent a deduction is allowable under section 2053. See §20.2053–1(d)(2).

(b) *Exception for claims and counterclaims in related matter*—(1) *General rule*. If a decedent's gross estate includes one or more claims or causes of action and there are one or more claims against the decedent's estate in the same or a substantially-related matter, or, if a decedent's gross estate includes a particular asset and there are one or more claims against the decedent's estate integrally related to that particular asset, the executor may deduct on the estate's *United States Estate (and Generation-Skipping Transfer) Tax Return* (Form 706) the current value of the claim or claims against the estate, even though payment has not been made, provided that—

(i) Each such claim against the estate otherwise satisfies the applicable requirements set forth in §20.2053–1;

(ii) Each such claim against the estate represents a personal obligation of the decedent existing at the time of the decedent's death;

(iii) Each such claim is enforceable against the decedent's estate (and is not unenforceable when paid);

(iv) The value of each such claim against the estate is determined from a "qualified appraisal" performed by a "qualified appraiser" within the meaning of section 170 of the Internal Revenue Code and the corresponding regulations;

(v) The value of each such claim against the estate is subject to adjustment for post-death events; and

(vi) The aggregate value of the related claims or assets included in the decedent's gross estate exceeds 10 percent of the decedent's gross estate.

(2) *Limitation on deduction*. The deduction under this paragraph (b) is limited to the value of the related claims or particular assets included in decedent's gross estate.

(3) *Effect of post-death events*. If, under this paragraph (b), a deduction is claimed on Form 706 for a claim against the estate and, during the period described in §20.2053–1(d)(2), the claim is paid or meets the requirements of §20.2053–1(d)(4) for deducting certain

ascertainable amounts, the claimed deduction is subject to adjustment to reflect, and may not exceed, the amount paid on the claim or the amount meeting the requirements of §20.2053–1(d)(4). If, under this paragraph (b), a deduction is claimed on Form 706 for a claim against the estate and, during the period described in §20.2053–1(d)(2), the claim remains unpaid (and does not meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts), the claimed deduction is subject to adjustment to reflect, and may not exceed, the current valuation of the claim. A valuation of the claim will be considered current if it reflects events occurring after the decedent's death. With regard to any amount in excess of the amount deductible under this paragraph (b), an estate may preserve the estate's right to claim a refund for claims that are paid or that meet the requirements of §20.2053–(1)(d)(4) after the expiration of the period of limitation for filing a claim for refund by filing a protective claim for refund in accordance with the rules in §20.2053–1(d)(5).

(c) *Exception for claims totaling not more than $500,000*—(1) *General rule*. An executor may deduct on Form 706 the current value of one or more claims against the estate even though payment has not been made on the claim or claims to the extent that—

(i) Each such claim against the estate otherwise satisfies the applicable requirements for deductibility set forth in §20.2053–1;

(ii) Each such claim against the estate represents a personal obligation of the decedent existing at the time of the decedent's death;

(iii) Each such claim is enforceable against the decedent's estate (and is not unenforceable when paid);

(iv) The value of each such claim against the estate is determined from a "qualified appraisal" performed by a "qualified appraiser" within the meaning of section 170 of the Internal Revenue Code and the corresponding regulations;

(v) The total amount deducted by the estate under this paragraph (c) does not exceed $500,000;

(vi) The full value of each claim, rather than just a portion of that amount, must be deductible under this paragraph (c) and, for this purpose, the full value of each such claim is deemed to be the unpaid amount of that claim that is not deductible after the application of §§20.2053–1 and 20.2053–4(b); and

(vii) The value of each claim deducted under this paragraph (c) is subject to adjustment for post-death events.

(2) *Effect of post-death events*. If, under this paragraph (c), a deduction is claimed for a claim against the estate and, during the period described in §20.2053–1(d)(2), the claim is paid or meets the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts, the amount of the allowable deduction for that claim is subject to adjustment to reflect, and may not exceed, the amount paid on the claim or the amount meeting the requirements of §20.2053–1(d)(4). If, under this paragraph (c), a deduction is claimed for a claim against the estate and, during the period described in §20.2053–1(d)(2), the claim remains unpaid (and does not meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts), the amount of the allowable deduction for that claim is subject to adjustment to reflect, and may not exceed, the current value of the claim. The value of the claim will be considered current if it reflects events occurring after the decedent's death. To claim a deduction for amounts in excess of the amount deductible under this paragraph (c), the estate may preserve the estate's right to claim a refund for claims that are not paid or that do not meet the requirements of §20.2053–1(d)(4) until after the expiration of the period of limitation for the filing of a claim for refund by filing a protective claim for refund in accordance with the rules in §20.2053–1(d)(5).

(3) *Examples*. The following examples illustrate the application of this paragraph (c). Assume that the value of each claim is determined from a "qualified appraisal" performed by a "qualified appraiser" and reflects events occurring after the death of the decedent (D). Also assume that each claim represents a personal obligation of D that existed at D's death, that each claim is enforceable against the decedent's estate (and is not unenforceable when paid), and that each claim otherwise satisfies the requirements for deductibility of §20.2053–1.

Example 1. There are three claims against the estate of the decedent (D) that are not paid and are not deductible under §20.2053–1(d)(4) or paragraph (b) of this section: $25,000 of Claimant A, $35,000 of Claimant B, and $1,000,000 of Claimant C. The executor of D's estate (E) may not claim a deduction under this paragraph with respect to any portion of the claim of Claimant C because the value of that claim exceeds $500,000. E may claim a deduction under this paragraph for the total amount of the claims filed by Claimant A and Claimant B ($60,000) because the aggregate value of the full amount of those claims does not exceed $500,000.

Example 2. There are three claims against the estate of the decedent (D) that are not paid and are not deductible under §20.2053–1(d)(4) or paragraph (b) of this section; specifically, a separate $200,000 claim of each of three claimants, A, B and C. The executor of D's estate (E) may claim a deduction under this paragraph for any two of these three claims because the aggregate value of the full amount of any two of the claims does not exceed $500,000. E may not deduct any part of the value of the remaining claim under this paragraph because the aggregate value of the full amount of all three claims would exceed $500,000.

Example 3. As a result of an automobile accident involving the decedent (D) and A, D's gross estate includes a claim against A that is valued at $750,000. In the same matter, A files a counterclaim against D's estate that is valued at $1,000,000. A's claim against D's estate is not paid and is not deductible under §20.2053–1(d)(4). All other section 2053 claims and expenses of D's estate have been paid and are deductible. The executor of D's estate (E) deducts $750,000 of A's claim against the estate under §20.2053–4(b). E may claim a deduction under this paragraph (c) for the total value of A's claim not deducted under §20.2053–4(b), or $250,000. If, instead, the value of A's claim against D's estate is $1,500,000, so that the amount not deductible under §20.2053–4(b) exceeds $500,000, no deduction is available under this paragraph (c).

(d) *Special rules*—(1) *Potential and unmatured claims*. Except as provided in §20.2053–1(d)(4) and in paragraphs (b) and (c) of this section, no estate tax deduction may be taken for a claim against the decedent's estate while it remains a potential or unmatured claim. Claims that later mature may be deducted (to the extent permitted by §20.2053–1) in connection with a timely claim for refund. To preserve the estate's right to claim a refund for claims that mature and become deductible after the expiration of the period of limitation for filing a claim for refund, a protective claim for refund may be filed in accordance with §20.2053–1(d)(5). See §20.2053–1(b)(3) for rules relating to the treatment of court decrees and settlements.

(2) *Contested claims*. Except as provided in paragraphs (b) and (c) of this section, no estate tax deduction may be taken for a claim against the decedent's estate to the extent the estate is contesting the decedent's liability. Contested claims that

later mature may be deducted (to the extent permitted by §20.2053–1) in connection with a claim for refund filed within the time prescribed in section 6511(a). To preserve the estate's right to claim a refund for claims that mature and become deductible after the expiration of the period of limitation for the filing a claim for refund, a protective claim for refund may be filed in accordance with §20.2053–1(d)(5). See §20.2053–1(b)(3) for rules relating to the treatment of court decrees and settlements.

(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 deduct only 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 also will be reduced by the contribution or other amount the estate could have collected from another party or an insurer but which the estate declines or fails to attempt to collect. See further §20.2053–1(d)(3).

(4) *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 (or will be paid) after they become unenforceable. However, see §20.2053–1(b)(3)(iv) regarding a claim whose enforceability is at issue.

(5) *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; that is, the promise or agreement must have been bargained for at arm's length and the price must have been an adequate and full equivalent reducible to a money value.

(6) *Recurring payments*—(i) *Noncontingent obligations*. If a decedent is obligated to make recurring payments on an enforceable and certain claim that satisfies the requirements for deductibility under this section and the payments are not subject to a contingency, the amount of the claim will be deemed ascertainable with reasonable certainty for purposes of the rule for deducting certain ascertainable amounts set forth in §20.2053–1(d)(4). If the recurring payments will be paid, a deduction will be allowed under the rule for deducting certain ascertainable amounts set forth in §20.2053–1(d)(4) (subject to any applicable limitations in §20.2053–1). Recurring payments for purposes of this section exclude those payments made in connection with a mortgage or indebtedness described in and governed by §20.2053–7. If a decedent's obligation to make a recurring payment is contingent on the death or remarriage of the claimant and otherwise satisfies the requirements of this paragraph (d)(6)(i), the amount of the claim (measured according to actuarial principles, using factors set forth in the transfer tax regulations or otherwise provided by the IRS) will be deemed ascertainable with reasonable certainty for purposes of the rule for deducting certain ascertainable amounts set forth in §20.2053–1(d)(4).

(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 not otherwise described in paragraph (d)(6)(i) of this section, the amount of the claim is not ascertainable with reasonable certainty for purposes of the rule for deducting certain ascertainable amounts set forth in §20.2053–1(d)(4). Accordingly, the amount deductible is limited to amounts actually paid by the estate in satisfaction of the claim in accordance with §20.2053–1(d)(1) (subject to any applicable limitations in §20.2053–1).

(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 arm's-length transaction to satisfy the obligation, the amount deductible by the estate (subject to any applicable limitations in §20.2053–1) is the sum of—

(A) The amount paid for the commercial annuity, to the extent that the amount paid is not refunded, or expected to be refunded, to the estate;

(B) Any amount actually paid to the claimant by the estate prior to the purchase of the commercial annuity; and

(C) Any amount actually paid to the claimant by the estate in excess of the annuity amount as is necessary to satisfy the recurring obligation.

(7) *Examples*. The following examples illustrate the application of paragraph (d) of this section. Except as is otherwise provided in the examples, assume—

(i) A claim satisfies the applicable requirements set forth in §20.2053–1 and paragraph (a) of this section, is payable from property subject to claims, and the amount of the claim is not subject to any other applicable limitations in §20.2053–1;

(ii) A claim is not deductible under paragraphs (b) or (c) of this section as an exception to the general rule contained in paragraph (a) of this section; and

(iii) The claimant (C) is not a family member, related entity or beneficiary of the estate of decedent (D) and is not the executor (E).

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 Form 706 is due before a judgment is reached in the case. D's gross estate exceeds $100x. E may not take a deduction on Form 706 for the claim against the estate. However, E may claim a deduction under §20.2053–3(c) or §20.2053–3(d)(3) for expenses incurred in defending the estate against the claim if the expenses have been paid in accordance with §20.2053–1(d)(1) or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts. E may file a protective claim for refund before the expiration of the period of limitation prescribed in section 6511(a) in order to preserve the estate's right to claim a refund, if the amount of the claim will not be paid or cannot be ascertained with reasonable certainty by the expiration of this limitation period. If payment is subsequently made pursuant to a court decision or a settlement, the payment, as well as expenses incurred incident to the claim and not previously deducted, may be deducted and relief may be sought in connection with a timely-filed claim for refund.

Example 2. Contested claim, single defendant, final court decree and payment. The facts are the same as in *Example 1* except that, before the Form 706 is timely filed, the court enters a decision in favor of C, no timely appeal is filed, and payment is made. E may claim a deduction on Form 706 for the amount paid in satisfaction of the claim against the estate pursuant to the final decision of the local court, including any interest accrued prior to D's death. In addition, E may claim a deduction under §20.2053–3(c) or §20.2053–3(d)(3) for expenses incurred in defending the estate against the claim and in processing payment of the claim if the expenses have been paid in accordance with §20.2053–1(d)(1) or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

Example 3. Contested claim, single defendant, settlement and payment. The facts are the same as in *Example 1* except that a settlement is reached between E and C for $80x and payment is made before Form 706 is timely filed. E may claim a deduction on Form 706 for the amount paid to C ($80x) in satisfaction of the claim against the estate. In addition, E may claim a deduction under §20.2053–3(c) or §20.2053–3(d)(3) for expenses incurred in defending the estate, reaching a settlement, and processing payment of the claim if the expenses have been paid in accordance with §20.2053–1(d)(1) or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

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 an unrelated third-party (K) as defendants. If the claim against the estate is not resolved prior to the time the Form 706 is filed, E may not take a deduction for the claim on Form 706. If payment is subsequently made of D's share of the claim pursuant to a court decision holding D liable for 40 percent of the amount due and K liable for 60 percent of the amount due, then E may claim a deduction for the amount paid in satisfaction of the claim against the estate 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. 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, E may claim a deduction of $50x together with the interest on $50x accrued prior to D's death. In both instances, E also may claim a deduction under §20.2053–3(c) or §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 if the expenses have been paid in accordance with §20.2053–1(d)(1) or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

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 an unrelated third-party (K) as defendants. D's estate settles with C for $10x and payment is made before Form 706 is timely filed. E may take a deduction on Form 706 for the amount paid to C ($10x) in satisfaction of the claim against the estate. In addition, E may claim a deduction under §20.2053–3(c) or §20.2053–3(d)(3) for expenses incurred in defending the estate, reaching a settlement, and processing payment of the claim if the expenses have been paid in accordance with §20.2053–1(d)(1) or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

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 Form 706 is due before a judgment is reached in the case. E accepts liability of $75x but contests liability of $25x. E may take a deduction of $75x on Form 706 if the amount has been paid or meets the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts. In addition, E may claim a deduction under §20.2053–3(c) or §20.2053–3(d)(3) for expenses incurred in defending the estate against the claim if the expenses have been paid or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts. E may file a protective claim for refund before the expiration of the period of limitation prescribed in section 6511(a) in order to preserve the estate's right to claim a refund for any amount in excess of $75x that is subsequently paid to resolve the claim against the estate. To the extent that any unpaid expenses incurred in defending the estate against the claim are not deducted as an ascertainable amount pursuant to §20.2053–1(d)(4), they may be included in the protective claim for refund.

Example 7. Claim having issue of enforceability. D is sued by C for $100x in a tort proceeding in which there is an issue as to whether the claim is barred by the applicable period of limitations. After D's death but prior to the decision of the court, a settlement meeting the requirements of §20.2053–1(b)(3)(iv) is reached between E and C in the amount of $50x. E pays C this amount before the Form 706 is timely filed. E may take a deduction on Form 706 for the amount paid to C ($50x) in satisfaction of the claim. If, subsequent to E's payment to C, facts develop to indicate that the claim was, in fact, unenforceable, the deduction will not be denied provided the enforceability of the claim was at issue in a bona dispute at the time of the payment. See §20.2053–1(b)(3)(iv). A deduction may be available under §20.2053–3(d)(3) for expenses incurred in defending the estate, reaching a settlement, and processing payment of the claim if the expenses have been paid in accordance with §20.2053–1(d)(1) or if the expenses meet the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

Example 8. Noncontingent 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 until S's death or remarriage. Prior to D's death, D made payments in accordance with the agreement and, after D's death, E continues to make the payments in accordance with the agreement. D's obligation to pay S under the property settlement agreement is deemed to be a claim against the estate that is ascertainable with reasonable certainty for purposes of §20.2053–1(d)(4). To the extent the obligation to make the recurring payment is a claim that will be paid, E may deduct the amount of the claim (measured according to actuarial principles, using factors set forth in the transfer tax regulations or otherwise provided by the IRS) under the rule for deducting certain ascertainable amounts set forth in §20.2053–1(d)(4).

Example 9. Recurring obligation to pay, estate purchases a commercial annuity in satisfaction. D's settlement agreement with T, the claimant in a suit against D, signed three years prior to D's death, obligates D or D's estate to pay to T $20x per year for 10 years, provided that T does not reveal the details of the claim or of the settlement during that period. D dies in Year 1. In Year 2, D's estate purchases a commercial annuity from an unrelated issuer of commercial annuities, XYZ, to fund the obligation to T. E may deduct the entire amount paid to XYZ to obtain the annuity, even though the obligation to T was contingent.

(e) *Interest on claim*—(1) Subject to any applicable limitations in §20.2053–1, the interest on a deductible claim is itself deductible as a claim under section 2053 to the extent of the amount of interest accrued at the decedent's death (even if the executor elects the alternate valuation method under section 2032), but only to the extent of the amount of interest actually paid or meeting the requirements of §20.2053–1(d)(4) for deducting certain ascertainable amounts.

(2) 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.

(f) *Effective/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

Par. 6. Section 20.2053–5 is amended by:

1. Redesignating paragraphs (a) and (b) as (a)(1) and (a)(2).

2. Redesignating the introductory text as paragraph (a).

3. Revising newly redesignated paragraph (a).

4. Adding a new paragraph (b).

The revision and addition read as follows:

§20.2035–5 Deductions for charitable, etc., pledges or subscriptions.

(a) A pledge or a subscription, evidenced by a promissory note or otherwise, even though enforceable against the estate, is deductible (subject to any applicable limitations in §20.2053–1) only to the extent that—

* * * * *

(b) *Effective/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

Par. 7. Section 20.2053–6 is amended by:

1. Revising paragraphs (a) and (c).

2. Adding paragraphs (g) and (h).

The revisions and additions read as follows:

§20.2053–6 Deduction for taxes.

(a) *In general*—(1) Taxes are deductible in computing a decedent's gross estate—

(i) Only as claims against the estate (except to the extent that excise taxes may be allowable as administration expenses);

(ii) Only to the extent not disallowed by section 2053(c)(1)(B) and this section; and

(iii) Subject to any applicable limitations in §20.2053–1.

(2) 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 the corresponding 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 available under section 2053(a)(3) for that tax liability. Similarly, any refund subsequently determined to be due to and received by the estate or its successor in interest with respect to taxes deducted by the estate under this section reduce 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 limitation for filing a claim 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 pays attorney's fees of $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 prior to the expiration of the limitation period for filing a claim for refund. The estate may deduct $90x under section 2053(a)(3) and $30x under §20.2053–3(c)(2) or (d)(3) in connection with a timely claim for refund.

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 timely files a claim for refund of income tax. Decedent's estate receives a refund of $10x. The estate is allowed a deduction of only $40x under section 2053(a)(3) for the income tax liability accrued prior to the decedent's death. If D's estate had claimed a deduction of $50x on D's *United States Estate (and Generation-Skipping Transfer) Tax Return* (Form 706), the deduction claimed under section 2053(a)(3) will be allowed only to the extent of $40x upon examination by the Commissioner.

(h) *Effective/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

Par. 8. Section 20.2053–9 is amended by:

1. Adding a sentence at the end of paragraph (a).

2. Revising the first and last sentences of paragraph (c).

3. Adding paragraph (f).

The revisions and addition read as follows:

§20.2053–9 Deduction for certain State death taxes.

(a) * * * However, see section 2058 to determine the deductibility of state death taxes by estates to which section 2058 is applicable.

* * * * *

(c) * * * 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/applicability date*—(1) The last sentence of paragraph (a) of this section applies to the estates of decedents dying on or after October 20, 2009, to which section 2058 is applicable.

(2) The other provisions of this section apply to the estates of decedents dying on or after October 20, 2009, to which section 2058 is not applicable.

Par. 9. Section 20.2053–10 is amended by removing the language "district director" and adding the language "Commissioner" in its place in paragraph (c) and by adding a new paragraph (e) to read as follows:

§20.2053–10 Deduction for certain foreign death taxes.

* * * * *

(e) *Effective/applicability date*. This section applies to the estates of decedents dying on or after October 20, 2009.

Linda E. Stiff,
Deputy Commissioner for Services and Enforcement.

Approved October 14, 2009.

Michael F. Mundaca,
Acting Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on October 16, 2009, 11:15 a.m., and published in the issue of the Federal Register for October 20, 2009, F.R. 53652)

Section 6402.—Authority to Make Credits or Refunds

26 CFR 301.6402–1: Authority to make credits or refunds.

This notice provides a limited administrative exception to the ability of the Internal Revenue Service to examine a Form 706 (*United States Estate (and Generation-Skipping Transfer) Tax Return*) in connection with certain protective claims for refund that are based on a deduction under section 2053 of the Internal Revenue Code and are filed within the time prescribed in section 6511(a) of the Code. See Notice 2009-84, page 592.

Section 6501.—Limitations on Assessment and Collection

26 CFR 301.6501(a)–1: Period of limitations upon assessment and collection.

This notice provides a limited administrative exception to the ability of the Internal Revenue Service to examine a Form 706 (*United States Estate (and*

Generation-Skipping Transfer) Tax Return) in connection with certain protective claims for refund that are based on a deduction under section 2053 of the Internal Revenue Code and are filed within the time prescribed in section 6511(a) of the Code. See Notice 2009-84, page 592.

Section 6511.—Limitations on Credit or Refund

26 CFR 301.6511(a)–1: Period of limitation on filing claim.

This notice provides a limited administrative exception to the ability of the Internal Revenue Service to examine a Form 706 (*United States Estate (and Generation-Skipping Transfer) Tax Return*) in connection with certain protective claims for refund that are based on a deduction under section 2053 of the Internal Revenue Code and are filed within the time prescribed in section 6511(a) of the Code. See Notice 2009-84, page 592.

Section 6514.—Credits or Refunds after Period of Limitation

26 CFR 301.6514(a)–1: Credits or refunds after period of limitation.

This notice provides a limited administrative exception to the ability of the Internal Revenue Service to examine a Form 706 (*United States Estate (and Generation-Skipping Transfer) Tax Return*) in connection with certain protective claims for refund that are based on a deduction under section 2053 of the Internal Revenue Code and are filed within the time prescribed in section 6511(a) of the Code. See Notice 2009-84, page 592.

Section 7477.—Declaratory Judgments Relating to Value of Certain Gifts

26 CFR 301.7477–1: Declaratory judgments relating to the value of certain gifts for gift tax purposes.

T.D. 9460

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 301

Declaratory Judgments — Gift Tax Determinations

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations under section 7477 of the Internal Revenue Code (Code) regarding petitions filed with the United States Tax Court for declaratory judgments with respect to the valuation of gifts. Changes to the applicable law were made by section 506(c)(1) of the Taxpayer Relief Act of 1997. These final regulations primarily affect individuals who are donors of gifts. The final regulations provide rules for determining whether a donor may petition the Tax Court for a determination regarding the value of a gift, including guidance regarding the definition of "exhaustion of administrative remedies."

DATES: *Effective date:* These regulations are effective September 9, 2009.

Applicability date: For the date of applicability, see §301.7477–1(f).

FOR FURTHER INFORMATION CONTACT: Juli Ro Kim or George Masnik (202) 622–3090 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

Section 7477, enacted in conjunction with other provisions as part of the Taxpayer Relief Act of 1997 (TRA) (Public Law 105–34, 111 Stat. 855), provides a declaratory judgment procedure pursuant to which taxpayers may contest in the United States Tax Court an IRS determination regarding the value of a gift. Prior law did not provide a judicial remedy in situations where the proposed IRS adjustment would not result in a gift tax deficiency or a tax overpayment. The new procedure applies, for example, where an increase in gift tax determined under section 2502 is offset by the taxpayer's applicable credit amount under section 2505(a), so that no additional tax is assessed as a result of a valuation increase. Because there is no tax deficiency, in the absence of section 7477, the taxpayer would be unable to challenge the IRS determination, even though, upon the expiration of the statute of limitations, that determination would become binding for purposes of calculating the cumulative gift tax on all future gifts of that taxpayer, as well as the taxpayer's estate tax liability. See H. R. CONF. REP. NO. 105–220, at 407–408 (1997).

On June 9, 2008, proposed regulations under section 7477 were published in the **Federal Register** (REG–143716–04, 2008–1 C.B. 1170 [73 FR 32503]). The IRS received no written or oral comments responding to the notice of proposed rulemaking. No public hearing was requested or held.

The final regulations include a few clarifications. In particular, under section 7477, in order to be eligible for the declaratory judgment procedure, the Tax Court must determine that the donor exhausted all administrative remedies. In general, the proposed regulations provide that the IRS will consider a donor to have exhausted all administrative remedies if an Appeals conference is requested timely and the donor (or an authorized representative) "participates fully" in the Appeals process. The final regulations contain a separate subsection specifying that full participation requires timely submission of requested information and disclosure of all relevant information regarding the controversy. In addition, a provision has been added specifying that, if Appeals does not grant the donor's request for a conference, the donor will be treated as having exhausted all administrative remedies if, after filing a Tax Court petition for a declaratory judgment, the donor (or authorized representative) participates fully in the Appeals office consideration when offered by the IRS while the case is in docketed status.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has 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 on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding this regulation was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal authors of these final regulations are George Masnik and Juli Ro Kim, Office of the Associate Chief Counsel (Passthroughs and Special Industries), IRS. Other personnel from the IRS and the Treasury Department participated in their development.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

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

Par. 2. Section 301.7477–1 is revised to read as follows:

§301.7477–1 Declaratory judgments relating to the value of certain gifts for gift tax purposes.

(a) *In general.* If the adjustment(s) proposed by the Internal Revenue Service (IRS) will not result in any deficiency in or refund of the donor's gift tax liability for the calendar year, and if the requirements contained in paragraph (d) of this section are satisfied, then the declaratory judgment procedure under section 7477 is available to the donor for determining the amount of one or more of the donor's gifts during that calendar year for Federal gift tax purposes.

(b) *Declaratory judgment procedure*—(1) *In general.* If a donor does not resolve a dispute with the IRS concerning the value of a transfer for gift tax purposes at the Examination level, the donor will be sent a notice of preliminary determination of value (Letter 950-G or such other document as may be utilized by the IRS for this purpose from time to time, but referred to in this section as Letter 950-G), inviting the donor to file a formal protest and to request consideration by the appropriate IRS Appeals office. See §§601.105 and 601.106 of this chapter. Subsequently, the donor will be sent a notice of determination of value (Letter 3569, or such other document as may be utilized from time to time by the IRS for this purpose in cases where no deficiency or refund would result, but referred to in this section as Letter 3569) if—

(i) The donor requests Appeals consideration in writing within 30 calendar days after the mailing date of the Letter 950-G, or by such later date as determined pursuant to IRS procedures, and the matter is not resolved by Appeals;

(ii) The donor does not request Appeals consideration within the time provided in paragraph (b)(1)(i) of this section; or

(iii) The IRS does not issue a Letter 950-G in circumstances described in paragraph (d)(4)(iv) of this section.

(2) *Notice of determination of value.* The Letter 3569 will notify the donor of the adjustment(s) proposed by the IRS, and will advise the donor that the donor may contest the determination made by the IRS by filing a petition with the Tax Court before the 91st day after the date on which the Letter 3569 was mailed to the donor by the IRS.

(3) *Tax Court petition.* If the donor does not file a timely petition with the Tax Court, the IRS determination as set forth in the Letter 3569 will be considered the final determination of value, as defined in sections 2504(c) and 2001(f). If the donor files a timely petition with the Tax Court, the Tax Court will determine whether the donor has exhausted available administrative remedies. Under section 7477, the Tax Court is not authorized to issue a declaratory judgment unless the Tax Court finds that the donor has exhausted all administrative remedies within the IRS. See paragraph (d)(4) of this section regarding the exhaustion of administrative remedies.

(c) *Adjustments subject to declaratory judgment procedure.* The declaratory judgment procedures set forth in this section apply to adjustments involving all issues relating to the transfer, including without limitation valuation issues and legal issues involving the interpretation and application of the gift tax law.

(d) *Requirements for declaratory judgment procedure*—(1) *In general.* The declaratory judgment procedure provided in this section is available to a donor with respect to a transfer only if all the requirements of paragraphs (d)(2) through (5) of this section with regard to that transfer are satisfied.

(2) *Reporting.* The transfer is shown or disclosed on the return of tax imposed by chapter 12 for the calendar year during which the transfer was made or on a statement attached to such return. For purposes of this paragraph (d)(2), the term *return of tax imposed by chapter 12* means the last gift tax return (Form 709, "*United States Gift (and Generation-Skipping Transfer) Tax Return*" or such other form as may be utilized for this purpose from time to time by the IRS) for the calendar year filed on or before the due date of the return, including extensions granted if any, or, if a timely return is not filed, the first gift tax return for that calendar year filed after the due date. For purposes of satisfying this requirement, the transfer need not be reported in a manner that constitutes adequate disclosure within the meaning of §301.6501(c)–1(e) or (f) (and thus for which, under §§20.2001–1(b) and 25.2504–2(b) of this chapter, the period during which the IRS may adjust the value of the gift will not expire). The issuance of a Letter 3569 with regard to a transfer disclosed on a return does not constitute a determination by the IRS that the transfer was adequately disclosed, or otherwise cause the period of limitations on assessment to commence to run with respect to that transfer. In addition, in the case of a transfer that is shown on the return, the IRS may in its discretion defer until a later time making a determination with regard to such transfer. If the IRS exercises its discretion to defer such determination in that case, the transfer will not be addressed in the Letter 3569 (if any) sent to the donor currently, and the donor is not yet eligible for a declaratory judgment with regard to that transfer under section 7477.

(3) *IRS determination and actual controversy.* The IRS makes a determination regarding the gift tax treatment of the transfer that results in an actual controversy. The IRS makes a determination that results in an actual controversy with respect to a transfer by mailing a Letter 3569 to the donor, thereby notifying the donor of the adjustment(s) proposed by the IRS with regard to that transfer and of the donor's rights under section 7477.

(4) *Exhaustion of administrative remedies*—(i) *In general.* The Tax Court determines whether the donor has exhausted all administrative remedies available within the IRS for resolving the controversy.

(ii) *Appeals office consideration*. For purposes of this section, the IRS will consider a donor to have exhausted all administrative remedies if, prior to filing a petition in Tax Court (except as provided in paragraphs (d)(4)(iii) and (iv) of this section), the donor, or a qualified representative of the donor described in §601.502 of this chapter, timely requests consideration by Appeals and participates fully (within the meaning of paragraph (d)(4)(vi) of this section) in the Appeals consideration process. A timely request for consideration by Appeals is a written request from the donor for Appeals consideration made within 30 days after the mailing date of the Letter 950-G, or by such later date for responding to the Letter 950-G as is agreed to between the donor and the IRS.

(iii) *Request for Appeals office consideration not granted*. If the donor, or a qualified representative of the donor described in §601.502 of this chapter, timely requests consideration by Appeals and Appeals does not grant that request, the IRS nevertheless will consider the donor to have exhausted all administrative remedies within the IRS for purposes of section 7477 upon the issuance of the Letter 3569, provided that the donor, or a qualified representative of the donor described in §601.502 of this chapter, after the filing of a petition in Tax Court for a declaratory judgment pursuant to section 7477, participates fully (within the meaning of paragraph (d)(4)(vi) of this section) in the Appeals office consideration if offered by the IRS while the case is in docketed status.

(iv) *No Letter 950-G issued*. If the IRS does not issue a Letter 950-G to the donor prior to the issuance of Letter 3569, the IRS nevertheless will consider the donor to have exhausted all administrative remedies within the IRS for purposes of section 7477 upon the issuance of the Letter 3569, provided that—

(A) The IRS decision not to issue the Letter 950-G was not due to actions or inactions of the donor (such as a failure to supply requested information or a current mailing address to the Area Director having jurisdiction over the tax matter); and

(B) The donor, or a qualified representative of the donor described in §601.502 of this chapter, after the filing of a petition in Tax Court for a declaratory judgment pursuant to section 7477, participates fully (within the meaning of paragraph (d)(4)(vi) of this section) in the Appeals office consideration if offered by the IRS while the case is in docketed status.

(v) *Failure to agree to extension of time for assessment*. For purposes of section 7477, the donor's refusal to agree to an extension of the time under section 6501 within which gift tax with respect to the transfer at issue (if any) may be assessed will not be considered by the IRS to constitute a failure by the donor to exhaust all administrative remedies available to the donor within the IRS.

(vi) *Participation in Appeals consideration process*. For purposes of this section, the donor or a qualified representative of the donor described in §601.502 of this chapter participates fully in the Appeals consideration process if the donor or the qualified representative timely submits all information related to the transfer that is requested by the IRS in connection with the Appeals consideration and discloses to the Appeals office all relevant information regarding the controversy to the extent such information and its relevance is known or should be known by the donor or the qualified representative during the time the issue is under consideration by Appeals.

(5) *Timely petition in Tax Court*. The donor files a pleading with the Tax Court requesting a declaratory judgment under section 7477. This pleading must be filed with the Tax Court before the 91st day after the date of mailing of the Letter 3569 by the IRS to the donor. The pleading must be in the form of a petition subject to Tax Court Rule 211(d).

(e) *Examples*. The following examples illustrate the provisions of this section, and assume that in each case the Tax Court petition is filed on or after September 9, 2009.

These examples, however, do not address any other situations that might affect the Tax Court's jurisdiction over the proceeding:

Example 1. Exhaustion of administrative remedies. The donor (D) timely files a Form 709, "*United States Gift (and Generation-Skipping Transfer) Tax Return*," on which D reports D's completed gift of closely held stock. After conducting an examination, the IRS concludes that the value of the stock on the date of the gift is greater than the value reported on the return. Because the amount of D's available applicable credit amount under section 2505 is sufficient to cover any resulting tax liability, no gift tax deficiency will result from the adjustment. D is unable to resolve the matter with the IRS examiner. The IRS sends a Letter 950-G to D informing D of the proposed adjustment. D, within 30 calendar days after the mailing date of the letter, submits a written request for Appeals consideration. During the Appeals process, D provides to the Appeals office all additional information (if any) requested by Appeals relevant to the determination of the value of the stock in a timely fashion. The Appeals office and D are unable to reach an agreement regarding the value of the stock as of the date of the gift. The Appeals office sends D a notice of determination of value (Letter 3569). For purposes of section 7477, the IRS will consider D to have exhausted all available administrative remedies within the IRS, and thus will not contest the allegation in D's petition that D has exhausted all such administrative remedies.

Example 2. Exhaustion of administrative remedies. Assume the same facts as in *Example 1*, except that D does not timely request consideration by Appeals after receiving the Letter 950-G. A Letter 3569 is mailed to D more than 30 days after the mailing of the Letter 950-G and prior to the expiration of the period of limitations for assessment of gift tax. D timely files a petition in Tax Court pursuant to section 7477. After the case is docketed, D requests Appeals consideration. In this situation, because D did not respond timely to the Letter 950-G with a written request for Appeals consideration, the IRS will not consider D to have exhausted all administrative remedies available within the IRS for purposes of section 7477 prior to filing the petition in Tax Court, and thus may contest any allegation in D's petition that D has exhausted all such administrative remedies.

Example 3. Exhaustion of administrative remedies. D timely files a Form 709 on which D reports D's completed gifts of interests in a family limited partnership. After conducting an examination, the IRS proposes to adjust the value of the gifts as reported on the return. No gift tax deficiency will result from the adjustments, however, because D has a sufficient amount of available applicable credit amount under section 2505. D declines to consent to extend the time for the assessment of gift tax with respect to the gifts at issue. Because of the pending expiration of the period of limitation on assessment within which a gift tax, if any, could be assessed, the IRS determines that there is not adequate time for Appeals consideration. Accordingly, the IRS mails to D a Letter 3569, even though a Letter 950-G had not first been issued to D. D timely files a petition in Tax Court pursuant to section 7477. After the case is docketed in Tax Court, D is offered the opportunity for Appeals to consider any dispute regarding the determination and participates fully in the Appeals consideration process. However, the Appeals office and D are unable to resolve the issue. The IRS will consider D to have exhausted all administrative remedies available within the IRS, and thus will not assert that D has not exhausted all such administrative remedies.

Example 4. Legal issue. D transfers nonvested stock options to a trust for the benefit of D's child. D timely files a Form 709 reporting the transfer as a completed gift for Federal gift tax purposes and complies with the adequate disclosure requirements for purposes of triggering the commencement of the applicable statute of limitations. Pursuant to

§301.6501(c)–1(f)(5), adequate disclosure of a transfer that is reported as a completed gift on the Form 709 will commence the running of the period of limitations for assessment of gift tax on D, even if the transfer is ultimately determined to be an incomplete gift for purposes of §25.2511–2 of this chapter. After conducting an examination, the IRS concurs with the reported valuation of the stock options, but concludes that the reported transfer is not a completed gift for Federal gift tax purposes. D is unable to resolve the matter with the IRS examiner. The IRS sends a Letter 950-G to D, who timely mails a written request for Appeals consideration. Assuming that the IRS mails to D a Letter 3569 with regard to this transfer, and that D complies with the administrative procedures set forth in this section, including the exhaustion of all administrative remedies available within the IRS, then D may file a petition for declaratory judgment with the Tax Court pursuant to section 7477.

Example 5. *Transfers in controversy*. On April 16, 2007, D timely files a Form 709 on which D reports gifts made in 2006 of fractional interests in certain real property and of interests in a family limited partnership (FLP). However, although the gifts are disclosed on the return, the return does not contain information sufficient to constitute adequate disclosure under §301.6501(c)–1(e) or (f) for purposes of the application of the statute of limitations on assessment of gift tax with respect to the reported gifts. The IRS conducts an examination and concludes that the value of both the interests in the real property and the FLP interests on the date(s) of the transfers are greater than the values reported on the return. No gift tax deficiency will result from the adjustments because D has a sufficient amount of remaining applicable credit amount under section 2505. However, D does not agree with the adjustments. The IRS sends a Letter 950-G to D informing D of the proposed adjustments in the value of the reported gifts. D, within 30 calendar days after the mailing date of the letter, submits a written request for Appeals consideration. The Appeals office and D are unable to reach an agreement regarding the value of any of the gifts. In the exercise of its discretion, the IRS decides to resolve currently only the value of the real property interests, and to defer the resolution of the value of the FLP interests. On May 28, 2009, the Appeals office sends D a Letter 3569 addressing only the value of the gifts of interests in the real property. Because none of the gifts reported on the return filed on April 16, 2007, were adequately disclosed for purposes of §301.6501(c)–1(e) or (f), the period of limitations during which the IRS may adjust the value of those gifts has not begun to run. Accordingly, the Letter 3569 is timely mailed. If D timely files a petition in Tax Court pursuant to section 7477 with regard to the value of the interests in the real property, then, assuming the other requirements of section 7477 are satisfied with regard to those interests, the Tax Court's declaratory judgment, once it becomes final, will determine the value of the gifts of the interests in the real property. Because the IRS has not yet put the gift tax value of the interests in the FLP into controversy, the procedure under section 7477 is not yet available with regard to those gifts.

(f) *Effective/applicability date*. This section applies to civil proceedings described in section 7477 filed in the United States Tax Court on or after September 9, 2009.

Linda E. Stiff,
Deputy Commissioner for Services and Enforcement.

Approved August 26, 2009.

Michael Mundaca,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on September 8, 2009, 8:45 a.m., and published in the issue of the Federal Register for September 9, 2009, F.R. 46347)

Section 7520.—Valuation Tables

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Section 7872.—Treatment of Loans With Below-Market Interest Rates

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2009. See Rev. Rul. 2009-35, page 568.

Part III. Administrative, Procedural, and Miscellaneous

Credit for Carbon Dioxide Sequestration Under Section 45Q

Notice 2009–83

SECTION 1. PURPOSE

This notice sets forth interim guidance, pending the issuance of regulations, relating to the credit for carbon dioxide (CO_2) sequestration under section 45Q of the Internal Revenue Code. Specifically, this notice provides guidance on determining eligibility for the credit and the amount of the credit, as well as rules regarding adequate security measures for secure geological storage of CO_2. This notice also sets forth a separate reporting requirement. The Internal Revenue Service (Service) and Treasury Department (Treasury) expect that the regulations will incorporate the rules set forth in this notice.

SECTION 2. BACKGROUND

.01 Section 45Q was enacted by § 115 of the Energy Improvement and Extension Act of 2008, Pub. L. No. 110–343, 122 Stat. 3829 (October 3, 2008), as amended by § 1131 of the American Recovery and Reinvestment Tax Act of 2009, Division B of Pub. L. 111–5, 123 Stat 115 (Feb. 17, 2009). Section 45Q(a) provides that a credit for CO_2 sequestration (§ 45Q credit) is generally available to a taxpayer that captures qualified CO_2 at a qualified facility and disposes of the CO_2 in secure geological storage within the United States, effective for CO_2 captured after October 3, 2008. As originally enacted, § 45Q(a)(1) provides for a credit of $20 per metric ton of qualified CO_2 that is captured and disposed of in secure geological storage, and § 45Q(a)(2) provides for a credit of $10 per metric ton of qualified CO_2 that is captured and used as a tertiary injectant in a qualified enhanced oil or natural gas recovery project (EOR project). Section 45Q(a), as amended, provides additional requirements effective after February 17, 2009, that, for purposes of the $20 per metric ton credit under § 45Q(a)(1), the qualified CO_2 must not be used as a tertiary injectant; and, for purposes of the $10 per metric ton credit under § 45Q(a)(2), the qualified CO_2 used as a tertiary injectant must be disposed of in secure geological storage.

.02 Section 45Q(d)(2) as amended provides that the Secretary of Treasury or his or her delegate (the Secretary), in consultation with the Administrator of the Environmental Protection Agency (EPA), the Secretary of Energy (DOE), and the Secretary of the Interior (DOI), shall establish regulations for determining adequate security measures for the geological storage of CO_2 such that the CO_2 does not escape into the atmosphere.

.03 Section 45Q(d)(5) provides that the § 45Q credit is attributable to the person that captures and physically or contractually ensures the disposal of or the use as a tertiary injectant of the qualified CO_2, except to the extent provided in regulations prescribed by the Secretary.

.04 Section 45Q(d)(6) provides for a recapture of the benefit of any credit allowable under § 45Q(a) with respect to any qualified CO_2 that ceases to be captured, disposed of, or used as a tertiary injectant in a manner consistent with the requirements of § 45Q.

.05 Section 45Q(d)(7) provides that, for taxable years beginning in a calendar year after 2009, the dollar amount contained in § 45Q(a) will be substituted for an amount equal to the product of such dollar amount multiplied by the inflation adjustment factor for such calendar year determined under § 43(b)(3)(B), determined by substituting "2008" for "1990."

.06 Section 45Q(e) as amended provides that the § 45Q credit will apply with respect to qualified CO_2 before the end of the calendar year in which the Secretary, in consultation with EPA, certifies that 75,000,000 metric tons of qualified CO_2 have been taken into account in accordance with § 45Q(a).

SECTION 3. TERMS AND DEFINITIONS

.01 *Terms*. For purposes of this notice,

(a) The terms disposal, storage, and sequestration are used interchangeably,

(b) The term credit refers to a tax credit and shall not be interpreted or construed as a CO_2 allowance, permit, or any other CO_2 emissions property right, and

(c) The term leakage refers to CO_2 that ceases to be sequestered via escape or release from the subsurface to the atmosphere or ocean.

.02 *Industrial Facility*.

(a) Industrial facility refers to a facility that produces a CO_2 stream from a fuel combustion source, a manufacturing process, or a fugitive CO_2 emission source that, absent capture and disposal, would otherwise be released into the atmosphere as industrial emission of greenhouse gas.

(b) An industrial facility does not include a facility that produces CO_2 from CO_2 production wells at natural CO_2-bearing formations.

.03 *Qualified Carbon Dioxide*. Qualified carbon dioxide means CO_2 that is:

(a) Captured from an industrial source that would otherwise be released into the atmosphere as industrial emission of greenhouse gas (GHG),

(b) Measured at the source of capture, and

(c) Verified at the point of disposal or injection.

Qualified CO_2 includes the initial deposit of captured CO_2 used as a tertiary injectant but does not include CO_2 that is re-captured, recycled, or otherwise re-injected as part of the enhanced oil and natural gas recovery process.

.04 *Qualified Enhanced Oil or Natural Gas Recovery Project*. Qualified enhanced oil or natural gas recovery project has the same meaning given the term "qualified enhanced oil recovery project" under § 43(c)(2) by substituting "crude oil or natural gas" for "crude oil" in § 43(c)(2)(A)(i).

.05 *Qualified Facility*. Qualified facility means an industrial facility that is owned by the taxpayer where carbon capture equipment is placed in service and where at least 500,000 metric tons of qualified CO_2 is captured during the taxable year.

SECTION 4. APPLICATION OF SECTION 45Q CREDIT

.01 *In General*. Taxpayers who capture qualified CO_2 from a qualified facility in a taxable year beginning after October 3, 2008, and meet all of the other requirements of § 45Q are eligible to claim the credit.

.02 *Section 45Q Credit Amount*. (a) The amount of the § 45Q credit is equal to the sum of:

(i) $20 per metric ton of qualified CO_2 if the qualified CO_2 is not used as a tertiary injectant in an EOR project; and

(ii) $10 per metric ton of qualified CO_2 if the qualified CO_2 is used as a tertiary injectant in an EOR project.

Pursuant to § 45Q(d)(5), a taxpayer that captures and physically or contractually ensures the disposal of or the use as a tertiary injectant of qualified CO_2 is eligible to claim the § 45Q credit.

(b) *Inflation Adjustment*. The § 45Q credit amount will be adjusted for inflation for any taxable year beginning in a calendar year after 2009. The Service will announce in later guidance the applicable inflation adjustment for the amount of § 45Q credit for a given taxable year.

.03 *Carbon Dioxide Measured by Weight*. (a) In order to claim a § 45Q credit, the amount of CO_2 must be measured at the source of capture and verified either at the point of disposal in secure geological storage or at the point of injection as a tertiary injectant in an EOR project. The amount of qualified CO_2 for purposes of the § 45Q credit is presumed to be the lesser of the amount measured at capture and the amount verified at disposal or injection, unless the taxpayer can establish to the satisfaction of the Secretary that the greater amount is the correct amount.

(b) For the purpose of calculating the § 45Q credit, a metric ton of CO_2 includes only the contained weight of the CO_2. The weight of any other substances, such as water or impurities, is not included in the calculation. For example, if a metric ton of a substance that is bought and sold as "CO_2" is 95 percent pure CO_2 by weight, for purposes of the § 45Q credit, 1.0526 tons (equivalent to 1 divided by 0.95) of the 95 percent pure substance is considered to be one metric ton of CO_2.

.04 *Captured and Disposed of or Used within the United States*. Section 45Q credit applies only to qualified CO_2 that is captured and disposed of or used as a tertiary injectant within the United States (as defined in § 638(1)) or a possession of the United States (as defined in § 638(2)).

.05 *Taxpayers Eligible to Claim the § 45Q Credit*. (a) To be eligible to claim the § 45Q credit, a person must (i) own an industrial facility at which carbon capture equipment is placed in service, (ii) capture not less than 500,000 metric tons of qualified CO_2 during the taxable year at such industrial facility, and (iii) physically or contractually ensure that the qualified CO_2 is securely stored in a geologic formation, including where such CO_2 is captured and transported for use in an EOR project. In the case of qualified CO_2 that is used as a tertiary injectant in an EOR project, requirement (iii) above applies only to CO_2 captured after February 17, 2009.

Each industrial facility for which the § 45Q credit is claimed must be equipped with carbon capture equipment and must capture not less than 500,000 metric tons of qualified CO_2 during the taxable year. Additionally, a person that buys the captured CO_2 at the point of transit or disposal but does not own the industrial facility at which the CO_2 is captured does not meet the qualified facility requirement of § 45Q(c) and is therefore ineligible to claim the § 45Q credit.

(b) *Example*. (i) X, a calendar year taxpayer, owns a manufacturing facility in the United States and releases CO_2 into the atmosphere as a by-product of the facility's operations. On November 1, 2009, X leases carbon capture equipment and places it in service at the manufacturing facility. On February 1, 2010, Y, an oil company, enters into a contract with X to purchase the CO_2 for use as a tertiary injectant in an EOR project. Pursuant to the terms of the contract, X captures the CO_2 and delivers it to Y at the manufacturing facility. Y transports the CO_2 in a pipeline to Y's oil fields located in the United States. Pursuant to its contract with X, Y uses the CO_2 as a tertiary injectant in an EOR project and thereafter disposes of the CO_2 in secure geological storage in the United States in 2010 and later years. During the taxable year beginning on January 1, 2010, 700,000 metric tons of CO_2 is captured at X's facility and injected as a tertiary injectant under the terms of the agreement. X measures the amount of CO_2 at the source of capture and Y verifies the amount of CO_2 at the point of injection during taxable year 2010.

(ii) CO_2 captured from X's facility is qualified CO_2 under § 45Q(b) because the CO_2 was captured from an industrial source from which it would otherwise have been released into the atmosphere and is measured at the source of capture and verified at the point of injection in the United States. The CO_2 was captured at a qualified facility within the meaning of section 3.05 of this notice because it is an industrial facility, within the meaning of section 3.02 of this notice, that is owned by X, at which carbon capture equipment is placed in service, and the facility captures not less than 500,000 metric tons of CO_2 during the taxable year. Therefore, X is eligible to claim the § 45Q credit in 2010 for the qualified CO_2 captured and used as a tertiary injectant in an EOR project in 2010. The amount of qualified CO_2 for purposes of the § 45Q credit is presumed to be the lesser of the amount measured at capture and the amount verified at injection, unless X can establish to the satisfaction of the Secretary that the greater amount is the correct amount.

.06 *Allocation of § 45Q Credit Among Qualified Facility Owners*. Eligibility for the § 45Q credit is based on the total amount of CO_2 captured and disposed of in secure geological storage during a taxable year subject to the following:

(a) If the qualified facility is owned by a partnership that has not made a valid election under § 761(a), the partnership will be considered the taxpayer for purposes of this notice. In such cases, the § 45Q credit must be allocated in accordance with § 1.704–1(b)(4)(ii).

(b) If the qualified facility is owned by a partnership that has made a valid § 761(a) election, then each partner in the partnership will be considered the taxpayer for purposes of this notice. In such case, the taxpayer may claim the § 45Q credit in accordance with its portion of the total amount of qualified CO_2 that is commensurate with its undivided ownership of the qualified facility.

.07 *Applicability of Credit for Projects under §§ 48A and 48B of the Code*. Qualified CO_2 for purposes of the § 45Q credit does not include CO_2 that is captured and sequestered in a project to the extent required under an agreement executed with the Service under the qualifying advanced coal project program of § 48A or the qualifying gasification project program of § 48B.

.08 *Credit Recapture*. Taxpayers must physically or contractually ensure that all qualified CO_2 disposed of in secure geological storage remains stored and is not released into the atmosphere. Taxpayers must recapture the benefit of any credit allowable under § 45Q(a) with respect to any qualified CO_2 that ceases to be captured, disposed of, or used as a tertiary injectant in a manner consistent with the requirements of § 45Q. Procedures regarding § 45Q credit recapture will be provided in future guidance.

.09 *Credit Termination*. Pursuant to § 45Q(e), at such time as the Service certifies, in consultation with the EPA, that 75,000,000 metric tons of qualified CO_2 have been taken into account for purposes of § 45Q credit, the Service will publicly announce that the § 45Q credit will cease to be available for the calendar year following such announcement.

SECTION 5. SECURE GEOLOGICAL STORAGE

.01 *In General*. In order to qualify for the § 45Q credit, a taxpayer must either physically or contractually dispose of captured CO_2 in secure geological storage using adequate security measures as provided by the Secretary in regulations. The term "secure geological storage" includes storage at deep saline formations, oil and gas reservoirs, and unminable coal seams under such conditions as the Secretary may determine under regulations. There are not yet regulations setting forth the requirements for secure geological storage. This section of the notice provides interim procedures for a taxpayer to determine adequate security measures for the secure geological storage of CO_2 until such regulations are promulgated. In the event that a taxpayer disposes of the qualified CO_2 contractually, the taxpayer must ensure that the contracting party complies with the requirements of this section of the notice at all times, and the taxpayer must be able to provide documentation of such compliance as required under section 7 of this notice. In order to demonstrate secure geological storage for purposes of the § 45Q credit, a taxpayer must meet the requirements of section 5.02 of this notice.

.02 *Requirements of Secure Geological Storage*.

(a) *Measurement of CO_2 at the Source of Capture: Final Mandatory GHG Reporting Rule*. On September 22, 2009, EPA issued the Final Mandatory GHG Reporting Rule (Reporting Rule) (to be codified at 40 C.F.R pt. 98), to require reporting of greenhouse gas emissions from all sectors of the economy. The Reporting Rule applies to fossil fuel suppliers and industrial gas suppliers, including CO_2 suppliers, as well as to direct greenhouse gas emitters. The Reporting Rule does not require control of greenhouse gases: rather, it requires only that certain sources monitor and report emissions. A taxpayer claiming the § 45Q credit must use the methodology, inputs, and equations in the Reporting Rule (or any successor rule) to calculate the amount of CO_2 measured at the source of capture. The amount reported under the Reporting Rule (or any successor rule) must be consistent with the amount of qualified CO_2 taken into account for purposes of the § 45Q credit.

(b) *Sequestration Site Rules*.

(i) *IPCC Guidelines*. In order for geological storage to be considered adequately secure for purposes of the § 45Q credit such that the injected CO_2 does not escape into the atmosphere, a taxpayer must conduct at the frequency appropriate for the site conditions, except as otherwise provided under paragraph (c), the following procedures outlined in the 2006 Intergovernmental Panel on Climate Change Guidelines for National Greenhouse Gas Inventories (IPCC Guidelines):

(A) Conduct a site characterization by evaluating the geology of the storage site and surrounding strata and identifying the local and regional hydrogeology and leakage pathways such as deep wells, faults, and fractures.

(B) Conduct an assessment of the risks of CO_2 leakage, or escape of CO_2 from the subsurface to the atmosphere, by evaluating the potential for leakage through a combination of site characterization and realistic models that predict movement of CO_2 over time and locations where emissions might occur. A range of modeling tools is available, including reservoir simulators that are widely used in the oil and gas industry and have proved effective in predicting movement of gases and liquids, including CO_2, through geological formations. Reservoir simulation can be used to predict the likely location, timing, and flux of emissions. Additional numerical modeling techniques may need to be used to analyze aspects of the geology, such as multi-phase reaction transport models and geomechanical models.

(C) Monitor potential leakage pathways, measure leakage at those pathways as necessary, monitor the current and future behavior of the CO_2 and of the storage system, and use the results of the monitoring plan to validate and/or update models as appropriate. Monitoring should be conducted according to a suitable plan. This should take into account the expectations from the modeling on where leakage might occur, as well as measurements made over the entire zone in which CO_2 is likely to be present.

(ii) *UIC Program: Proposed Rules for Geologic Storage*. The Underground Injection Control (UIC) program was established under the authority of Part C of the Safe Drinking Water Act (42 U.S.C. 300h *et seq.*) (SDWA), which regulates underground injection wells. The SDWA is designed to protect the quality of drinking water sources in the United States. The SDWA gives the EPA authority to issue regulations for state programs that contain "minimum requirements for effective programs to prevent underground injection which endangers drinking water sources." Under the UIC program, the EPA promulgated a series of regulations (40 C.F.R. parts 144 through 148) to employ a multiple barrier approach that includes requirements for the proper geologic siting, construction, operation, testing, and closure of injection wells to ensure that injected fluids remain isolated from underground sources of drinking water (USDWs) and the environment.

On July 25, 2008, the EPA proposed rules relating to federal requirements under the UIC Program for CO_2 Geologic Sequestration Wells (73 Fed. Register No. 144, 40 C.F.R. parts 144–146). The EPA proposes to create a new category of injection well (Class VI) under its existing UIC Program with new federal requirements to permit the injection of CO_2 for the purpose of geologic sequestration (*i.e.*, the long-term containment of a gaseous, liquid, or supercritical CO_2 stream in subsurface geologic formations). The EPA proposes to tailor existing UIC program components to create standards appropriate for injecting large amounts of CO_2 into a variety of geologic formations to ensure that USDWs are not endangered.

The proposed UIC program rules have not been finalized as of the date of this notice. Once the UIC program rules are finalized, any taxpayer claiming the § 45Q credit who is covered by the new program rules must follow the modeling, monitoring, well construction, and other requirements of the relevant permit as required under the rules. The requirements in the final UIC program rules (or any successor rules) will apply in lieu of the requirements of the IPCC Guidelines under paragraph (i). However, any taxpayer that is not covered by the final UIC program rules must continue to follow the procedures outlined in the IPCC Guidelines pursuant to paragraph (i).

(iii) *Proposed Geologic Sequestration Rules*. Subpart PP of the Final Mandatory GHG Reporting Rule announces EPA's plans to propose new rules to require reporting of the amount of CO_2 that is geologically sequestered. EPA will seek comments on monitoring, reporting, and verification methodologies that can be used to determine the amount of CO_2 emitted and geologically sequestered at active EOR facilities and geologic sequestration sites where CO_2 is injected (for long-term storage) into saline aquifers, oil and gas reservoirs, or other geologic formations. When the proposed geologic sequestration rules are finalized, such rules (or any successor rules) will apply in addition to the final UIC program rules (to the extent applicable), and the requirements of the IPCC Guidelines under paragraph (i) will no longer apply.

(c) *Compliance with Additional Regulatory Requirements*. EPA may impose additional or different requirements for secure geological storage, including additional methodology, inputs, and equations to calculate the amount of CO_2 measured and verified at the source of injection and/or the amount of CO_2 emitted from secure geological storage. Furthermore, various aspects of geologic sequestration, including well construction, operation, well plugging, and post-injection site closure may be subject to other existing or future requirements from government bodies, including EPA's regional or state UIC programs. Any taxpayer claiming the § 45Q credit must follow such additional requirements together with the Reporting Rule and the IPCC Guidelines (or, in lieu of the IPCC guidelines, the UIC program rule as applicable and the geologic sequestration rule, once they are finalized) in order to demonstrate secure geological storage for purposes of the § 45Q credit.

SECTION 6. REPORTING REQUIREMENTS

.01 *Annual Reports*. A taxpayer that has claimed the § 45Q credit on a tax return must submit an annual report to the Service containing the following information:

(a) The name, address, and taxpayer identification number of the reporting taxpayer, and all parties with which the taxpayer contractually ensures the secure geological storage of the CO_2;

(b) The name and location of the qualified facilities at which the CO_2 was captured;

(c) The amounts (in metric tons) of qualified CO_2 for the taxable year that has been taken into account for purposes of claiming the § 45Q credit;

(d) Any changes in the information included in prior annual reports submitted under section 6.01 of this notice, including adjustments to the amount (in metric tons) of qualified CO_2 taken into account for purposes of the § 45Q credit in prior taxable years; and

(e) A declaration, applicable to the report and any accompanying documents, signed by a person currently authorized to bind the taxpayer in these matters, in the following form:

"Under penalties of perjury, I declare that I have examined this report, including accompanying documents, and to the best of my knowledge and belief, the facts presented in support of this report are true, correct, and complete."

.02 *Time for Filing Reports*. The annual report described in section 6.01 of this notice must be filed with the Service at the following address not later than the last day of the second calendar month following the month during which the tax return on which the § 45Q credit is claimed was due (including extensions):

Internal Revenue Service
Attn: CC:PSI:6, Room 5116
P.O. Box 14095
Benjamin Franklin Station
Washington, D.C. 20044

SECTION 7. RECORDKEEPING REQUIREMENT

.01 *In General*. A taxpayer is not required to attach documentation to the return on which the credit is claimed. However, § 6001 of the Code provides that every person liable for any tax imposed by the Code, or for the collection thereof, must keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. See Treas. Reg. § 1.6001–1(e).

.02 *Information Must Be Available for Inspection*. The taxpayer must retain in its records documentation establishing that the taxpayer qualifies for the § 45Q credit. The taxpayer must, upon request, make such documentation available for inspection by the Service regardless of whether the taxpayer physically or contractually ensures injection or disposal in secure geological storage. Such necessary documentation includes, but is not limited to, the following:

(a) Methodology, inputs, and equations used to measure the amount of CO_2 at the source of capture and verify the amount at the point of disposal or injection. Qualified CO_2 for purposes of the § 45Q credit does not include the amount of CO_2 recycled or re-injected as part of EOR operations.

(b) Evidence of disposal of captured CO_2 in secure geological storage, as specified in section 5 of this notice. As future Federal and state regulations are promulgated, such evidence may also include any certificates issued or determinations made by a Federal or state government that the geological storage meets the necessary requirements to ensure secure storage.

(c) Methodology, inputs, and equations used to calculate the amount of CO_2 emitted from secure geological storage.

(d) All contracts entered into by the taxpayer and any contracting party that ensures the use of the CO_2 as a tertiary injectant or the disposal of the CO_2 in secure geological storage.

SECTION 8. PAPERWORK REDUCTION ACT

The collection of information contained in this notice has been reviewed and approved by the Office of Management and

Budget in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545–2153.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collection of information is in section 6 of this notice. This information is required to allow the Secretary to determine when 75,000,000 metric tons of qualified CO_2 have been taken into account for purposes of the § 45Q credit. The § 45Q credit will cease to be available after the end of the calendar year in which the Secretary, in consultation with the EPA, certifies that 75,000,000 metric tons of qualified CO_2 have been taken into account. This collection of information is required to obtain a benefit. The likely respondents are businesses or other for-profit institutions.

The estimated total annual reporting burden is 180 hours.

The estimated annual burden per respondent varies from 2 to 10 hours, depending on individual circumstances, with an estimated average of 6 hours. The estimated number of respondents is 30.

The estimated annual frequency of responses is annually.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. § 6103.

SECTION 9. DRAFTING INFORMATION

The principal author of this notice is Jennifer C. Bernardini of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this notice, contact Jennifer C. Bernardini at (202) 622–3110 (not a toll-free call).

Limited Reexamination of Estate Tax Return Applicable to Certain Section 2053 Claims for Refund

Notice 2009–84

PURPOSE

This notice provides a limited administrative exception to the ability of the Internal Revenue Service (Service) to examine a Form 706 (*United States Estate (and Generation-Skipping Transfer) Tax Return*) in connection with certain protective claims for refund filed within the time prescribed in section 6511(a) of the Internal Revenue Code (Code). Specifically, in processing a timely-filed protective claim for refund of tax based on a deduction under section 2053 of the Code, if the claim for refund ripens and becomes ready for consideration after the expiration of the period of limitations on assessment prescribed in section 6501, the Service will limit its review of the Form 706 to the evidence relating to the deduction under section 2053 that was the subject of the protective claim.

BACKGROUND

Concurrently with the issuance of this notice, the Treasury Department and the Service are issuing final regulations under section 2053 of the Code (T.D. 9468) to provide guidance in determining the deductible amount of a claim against a decedent's estate under section 2053. Section 20.2053–1(d)(1) of the final regulations provides the general rule that a deduction for any claim or expense described in section 2053 and the final regulations is limited, with several exceptions, to the amount actually paid in settlement or satisfaction of the claim or expense.

Under the final regulations, if a claim or expense that would have been deductible under section 2053 had it already been paid is not fully deductible within the period of limitation prescribed in section 6511(a), the estate may file a protective claim for refund to preserve the estate's right to claim a refund of tax attributable to the deduction of such claim or expense in the event that it becomes deductible in whole or in part after the expiration of the period of limitation prescribed in section 6511(a). Section 20.2053–1(d)(5). A protective claim for refund may be filed at any time before the expiration of the period of limitation prescribed in section 6511(a) for the filing of a claim for credit or refund. See section 6514. Once the claim or expense has been paid or otherwise has become deductible under section 2053, the executor may notify the Service that the decedent's estate is ready to pursue the claim for refund.

In considering a claim for refund, the Service must determine if there is an overpayment of tax for purposes of section 6402. An overpayment exists to the extent the amount of tax paid exceeds the correct tax liability. To determine the correct tax liability, the Service has the authority to examine each item on the return regardless of whether the period of limitations on assessment has expired. See *Lewis v. Reynolds, 284 U.S. 281, 283 (1932)*. Even if the Service is barred from assessing any additional amount of tax by reason of the expiration of the period of limitations on assessment under section 6501, the Service may reject the claim for refund to the extent the Service determines there is no overpayment of tax.

DISCUSSION

Commentators responding to the proposed regulations (published in the Federal Register on April 23, 2007 (REG–143316–03, 2007–1 C.B. 1292 [72 FR 20080])) expressed concerns that the protective claim procedures effectively would keep the period of limitations on assessment open to the extent of the amount of the claim for refund and, therefore, would impede the goal of achieving finality in the administration of a decedent's estate. In cases in which the Service accepts the Form 706 as filed or in which any disputes between the estate and the Service are resolved without a judicial determination, the executor generally relies on the estate tax closing letter (Letter 627) that is issued by the Service to advise the estate that the Form 706 has been accepted, either as filed or after an adjustment to which the estate has agreed. Practitioners are concerned that, if an estate must file a protective claim for refund in order to claim a deduction for a claim or expense under section 2053 of the Code, executors will be unable to rely on the estate tax closing letter because the Service has the ability to examine the entire Form 706 when a timely-filed claim for refund is ready for consideration by the Service.

The final regulations under section 2053, issued concurrently with this notice, provide several exceptions to the general rule that a deduction for a claim or expense is limited to the amount paid in settlement or satisfaction of that claim or expense. As a result of these exceptions, the Treasury Department and the Service anticipate that the number of protective refund claims filed to preserve a deduction under section 2053 will be significantly smaller than was anticipated by commentators to the proposed regulations. The Treasury Department and the Service, nevertheless, acknowledge the value in achieving finality in the administration of estates and in making the regulations under section 2053 more administrable.

Accordingly, if the period of limitations on assessment has expired and the Service is notified that a timely-filed protective claim for refund of tax based on a deduction under section 2053 has ripened and is ready for consideration, the Service generally will refrain from exercising its authority to examine each item on the Form 706 to determine if there is an overpayment of tax for purposes of section 6402. Instead, when such a timely-filed claim for refund ripens after the expiration of the period of limitations on assessment, the Service will limit its examination of the Form 706 to the evidence relating to the deduction under section 2053 that was the subject of the protective claim.

To the extent that the Service determines the deduction under section 2053 is allowable, the Service will recompute the estate tax liability of the estate (and the marital and charitable deductions, and all other amounts determined as part of that process) by allowing that deduction.

SCOPE

The Service's decision to limit its examination of the Form 706 to the evidence relating to the deduction under section 2053 of the Code applies only to estates in which a timely protective refund claim was filed to preserve an estate's ability to claim a deduction under section 2053 for a claim or expense that subsequently is paid or otherwise meets the requirements for deductibility under the final regulations. This administrative exception does not apply, however, when the Service is considering a protective claim for refund based on a deduction under section 2053 and, in the same estate, is considering a claim for refund not based on a protective claim regarding a deduction under section 2053. In addition, the Service's decision to limit its examination of the Form 706 applies only if the protective claim for refund ripens after the expiration of the period of limitations on assessment and does not apply if there is evidence of fraud, malfeasance, collusion, concealment, or misrepresentation of a material fact.

EFFECTIVE DATE

This notice is applicable with respect to protective claims for refund filed on behalf of estates of decedents dying on or after October 20, 2009.

DRAFTING INFORMATION

The principal author of this notice is Karlene Lesho of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, contact Karlene Lesho at (202) 622–3090 (not a toll-free call).

Part IV. Items of General Interest

Deletions From Cumulative List of Organizations Contributions to Which are Deductible Under Section 170 of the Code

Announcement 2009–78

The Internal Revenue Service has revoked its determination that the organizations listed below qualify as organizations described in sections 501(c)(3) and 170(c)(2) of the Internal Revenue Code of 1986 effective January 1, 2006.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

Concerned Residents of Southeast, Inc.
Brewster, NY

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in laws or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in a new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D. —Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z —Corporation.

Numerical Finding List[1]

Bulletins 2009–27 through 2009–44

Announcements:

2009-56, 2009-28 I.R.B. *145*
2009-57, 2009-29 I.R.B. *158*
2009-58, 2009-29 I.R.B. *158*
2009-59, 2009-29 I.R.B. *158*
2009-60, 2009-30 I.R.B. *166*
2009-61, 2009-33 I.R.B. *246*
2009-62, 2009-33 I.R.B. *247*
2009-63, 2009-33 I.R.B. *248*
2009-64, 2009-36 I.R.B. *319*
2009-65, 2009-36 I.R.B. *319*
2009-66, 2009-37 I.R.B. *364*
2009-67, 2009-38 I.R.B. *388*
2009-68, 2009-38 I.R.B. *388*
2009-69, 2009-40 I.R.B. *475*
2009-70, 2009-41 I.R.B. *499*
2009-71, 2009-40 I.R.B. *475*
2009-72, 2009-41 I.R.B. *500*
2009-73, 2009-41 I.R.B. *500*
2009-74, 2009-42 I.R.B. *537*
2009-75, 2009-42 I.R.B. *537*
2009-77, 2009-43 I.R.B. *567*
2009-78, 2009-44 I.R.B. *594*

Notices:

2009-51, 2009-28 I.R.B. *128*
2009-55, 2009-31 I.R.B. *170*
2009-57, 2009-29 I.R.B. *147*
2009-58, 2009-30 I.R.B. *163*
2009-59, 2009-31 I.R.B. *170*
2009-60, 2009-32 I.R.B. *181*
2009-61, 2009-32 I.R.B. *181*
2009-62, 2009-35 I.R.B. *260*
2009-63, 2009-34 I.R.B. *252*
2009-64, 2009-36 I.R.B. *307*
2009-65, 2009-39 I.R.B. *413*
2009-66, 2009-39 I.R.B. *418*
2009-67, 2009-39 I.R.B. *420*
2009-68, 2009-39 I.R.B. *423*
2009-69, 2009-35 I.R.B. *261*
2009-70, 2009-34 I.R.B. *255*
2009-71, 2009-35 I.R.B. *262*
2009-72, 2009-37 I.R.B. *325*
2009-73, 2009-38 I.R.B. *369*
2009-74, 2009-38 I.R.B. *370*
2009-75, 2009-39 I.R.B. *436*
2009-76, 2009-43 I.R.B. *554*
2009-77, 2009-40 I.R.B. *449*
2009-78, 2009-40 I.R.B. *452*
2009-79, 2009-40 I.R.B. *454*
2009-81, 2009-40 I.R.B. *455*
2009-82, 2009-41 I.R.B. *491*

Notices— Continued:

2009-83, 2009-44 I.R.B. *588*
2009-84, 2009-44 I.R.B. *592*

Proposed Regulations:

REG-140492-02, 2009-43 I.R.B. *559*
REG-152166-05, 2009-32 I.R.B. *183*
REG-112994-06, 2009-28 I.R.B. *144*
REG-127270-06, 2009-42 I.R.B. *534*
REG-136563-07, 2009-41 I.R.B. *497*
REG-108045-08, 2009-43 I.R.B. *557*
REG-113289-08, 2009-33 I.R.B. *244*
REG-116614-08, 2009-42 I.R.B. *536*
REG-130200-08, 2009-31 I.R.B. *174*
REG-139068-08, 2009-43 I.R.B. *558*

Revenue Procedures:

2009-30, 2009-27 I.R.B. *27*
2009-31, 2009-27 I.R.B. *107*
2009-32, 2009-28 I.R.B. *142*
2009-33, 2009-29 I.R.B. *150*
2009-34, 2009-34 I.R.B. *258*
2009-35, 2009-35 I.R.B. *265*
2009-36, 2009-35 I.R.B. *304*
2009-37, 2009-36 I.R.B. *309*
2009-38, 2009-37 I.R.B. *362*
2009-39, 2009-38 I.R.B. *371*
2009-40, 2009-39 I.R.B. *438*
2009-41, 2009-39 I.R.B. *439*
2009-42, 2009-40 I.R.B. *459*
2009-43, 2009-40 I.R.B. *460*
2009-44, 2009-40 I.R.B. *462*
2009-45, 2009-40 I.R.B. *471*
2009-46, 2009-42 I.R.B. *507*
2009-47, 2009-42 I.R.B. *524*

Revenue Rulings:

2009-18, 2009-27 I.R.B. *1*
2009-19, 2009-28 I.R.B. *111*
2009-20, 2009-28 I.R.B. *112*
2009-21, 2009-30 I.R.B. *162*
2009-22, 2009-31 I.R.B. *167*
2009-23, 2009-32 I.R.B. *177*
2009-24, 2009-36 I.R.B. *306*
2009-25, 2009-38 I.R.B. *365*
2009-26, 2009-38 I.R.B. *366*
2009-27, 2009-39 I.R.B. *404*
2009-28, 2009-39 I.R.B. *391*
2009-29, 2009-37 I.R.B. *322*
2009-30, 2009-39 I.R.B. *391*
2009-31, 2009-39 I.R.B. *395*
2009-32, 2009-39 I.R.B. *399*
2009-33, 2009-40 I.R.B. *447*
2009-34, 2009-42 I.R.B. *502*
2009-35, 2009-44 I.R.B. *568*

Treasury Decisions:

9452, 2009-27 I.R.B. *1*
9453, 2009-28 I.R.B. *114*
9454, 2009-32 I.R.B. *178*
9455, 2009-33 I.R.B. *239*
9456, 2009-33 I.R.B. *188*
9457, 2009-41 I.R.B. *482*
9458, 2009-43 I.R.B. *547*
9459, 2009-41 I.R.B. *480*
9460, 2009-44 I.R.B. *584*
9461, 2009-41 I.R.B. *488*
9462, 2009-42 I.R.B. *504*
9463, 2009-40 I.R.B. *442*
9465, 2009-43 I.R.B. *542*
9466, 2009-43 I.R.B. *551*
9468, 2009-44 I.R.B. *570*

[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2009–1 through 2009–26 is in Internal Revenue Bulletin 2009–26, dated June 29, 2009.

Finding List of Current Actions on Previously Published Items[1]

Bulletins 2009–27 through 2009–44

Announcements:

2006-93
Superseded by
Ann. 2009-62, 2009-33 I.R.B. *247*

Notices:

2002-3
Modified and superseded by
Notice 2009-68, 2009-39 I.R.B. *423*

2004-67
Supplemented and superseded by
Notice 2009-59, 2009-31 I.R.B. *170*

2006-70
Obsoleted by
T.D. 9453, 2009-28 I.R.B. *114*

2006-109
Superseded in part by
Rev. Proc. 2009-32, 2009-28 I.R.B. *142*

2007-7
Modified by
Notice 2009-82, 2009-41 I.R.B. *491*

2008-30
Amplified and clarified by
Notice 2009-75, 2009-39 I.R.B. *436*

2008-43
Obsoleted by
REG-113289-08, 2009-33 I.R.B. *244*

2009-28
Clarified by
Notice 2009-69, 2009-35 I.R.B. *261*

2009-31
Amplified by
Rev. Proc. 2009-43, 2009-40 I.R.B. *460*

2009-42
Amplified by
Rev. Proc. 2009-43, 2009-40 I.R.B. *460*

Revenue Procedures:

97-27
Clarified and modified by
Rev. Proc. 2009-39, 2009-38 I.R.B. *371*

97-49
Modified and superseded by
Rev. Proc. 2009-31, 2009-27 I.R.B. *107*

2002-44
Superseded by
Rev. Proc. 2009-44, 2009-40 I.R.B. *462*

Revenue Procedures— Continued:

2002-59
Superseded by
Rev. Proc. 2009-41, 2009-39 I.R.B. *439*

2005-63
Modified by
Rev. Proc. 2009-39, 2009-38 I.R.B. *371*

2007-44
Modified by
Rev. Proc. 2009-36, 2009-35 I.R.B. *304*

2007-65
Modified by
Ann. 2009-69, 2009-40 I.R.B. *475*

2008-34
Superseded by
Rev. Proc. 2009-46, 2009-42 I.R.B. *507*

2008-38
Superseded by
Rev. Proc. 2009-30, 2009-27 I.R.B. *27*

2008-44
Superseded by
Rev. Proc. 2009-35, 2009-35 I.R.B. *265*

2008-52
Amplified, clarified, and modified by
Rev. Proc. 2009-39, 2009-38 I.R.B. *371*

2008-59
Superseded by
Rev. Proc. 2009-47, 2009-42 I.R.B. *524*

2008-65
Modified by
Rev. Proc. 2009-33, 2009-29 I.R.B. *150*

2009-16
Modified by
Rev. Proc. 2009-33, 2009-29 I.R.B. *150*

2009-39
Modified by
Ann. 2009-67, 2009-38 I.R.B. *388*

Revenue Rulings:

74-346
Superseded by
Rev. Rul. 2009-34, 2009-42 I.R.B. *502*

75-190
Superseded by
Rev. Rul. 2009-34, 2009-42 I.R.B. *502*

75-398
Superseded by
Rev. Rul. 2009-34, 2009-42 I.R.B. *502*

75-526
Superseded by
Rev. Rul. 2009-34, 2009-42 I.R.B. *502*

Revenue Rulings— Continued:

2009-22
Corrected by
Ann. 2009-74, 2009-42 I.R.B. *537*

2009-29
Corrected by
Ann. 2009-74, 2009-42 I.R.B. *537*

Treasury Decisions:

9456
Corrected by
Ann. 2009-73, 2009-41 I.R.B. *500*

[1] A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2009–1 through 2009–26 is in Internal Revenue Bulletin 2009–26, dated June 29, 2009.

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