
Notice of Proposed Rulemaking and Notice of Public Hearing

Adequate Disclosure of Gifts

REG-106177-98

AGENCY: Internal Revenue Service (IRS), Treasury.

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

SUMMARY: This document contains proposed regulations relating to changes made by the Taxpayer Relief Act of 1997 and the Internal Revenue Service Restructuring and Reform Act of 1998 regarding the valuation of prior gifts in determining estate and gift tax liability, and the period of limitations for assessing and collecting gift tax. The proposed regulations affect individual donors and the estates of those donors. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written and electronic comments must be received by March 22, 1999. Outlines of topics to be discussed at the public hearing scheduled for Wednesday, April 28, 1999, must be received by Wednesday, April 7, 1999.

ADDRESSES: Send submissions to CC:DOM:CORP:R [REG-106177-98] room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington DC 20044. Submissions may also be hand delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R [REG-106177-98], Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may submit comments electronically via

the internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS internet site at http://www.irs.ustreas.gov/prod/tax_regs/comments.html. The public hearing will be held in room 2615, at 10 a.m., Internal Revenue Building, 1111 Constitution Avenue, NW, Washington DC.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, William L. Blodgett, (202) 622-3090; concerning submissions and the hearing, and/or to be placed on the building access list to attend the hearing, LaNita Van Dyke, (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Introduction

This document proposes to amend the Estate and Gift Tax Regulations (26 CFR parts 20 and 25) under sections 2001 and 2504 relating to the value of prior gifts for purposes of computing the estate and gift tax. This document also proposes to amend the Procedure and Administration Regulations relating to the period for assessment and collection of gift tax under section 6501.

Paperwork Reduction Act

The collection of information contained in this notice of proposed rulemaking has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, OP:FS:FP, Washington, DC 20224. Comments on the collection of information should be received by February 22, 1999. Comments are specifically requested concerning:

Whether the proposed collection of information is necessary for the proper performance of the functions of the Internal Revenue Service, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collection of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of service to provide information.

The collection of information in this proposed regulation is proposed §301.6501(c)–1(f) of the Procedure and Administration Regulations. This information is required by statute in order to commence the period of limitations on assessment. This information will be used to identify gift tax issues relating to the reported transfers. The collection of information is mandatory. The likely respondents are individuals.

The reporting burden contained in §301.6501–1(f) is reflected in the burden of Form 709, U.S. Gift (and Generation-Skipping Transfer) Tax Return.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

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 information are confidential, as required by 26 U.S.C. 6103.

Background

Under the unified estate and gift tax system, a single rate schedule is applied to an individual's cumulative gifts and bequests. Gift tax is computed by determining a tax on the total of the gifts made by the donor in the current calendar year plus the gifts made in prior years (prior taxable gifts). The tax computed is then reduced by the tax that would have been payable on the prior taxable gifts. The result (after taking into account the applicable credit amount under section 2505) is the gift tax on the current gifts. Similarly, the

estate tax is computed by determining a tax on the value of the decedent's taxable estate plus the value of lifetime gifts (adjusted taxable gifts) made by the decedent. The tax computed is then reduced by the gift tax that would have been payable on the adjusted taxable gifts. The result (after allowing for various credits) is the estate tax on the taxable estate.

The Statute of Limitations for Assessment of Gift Tax Under Section 6501(c)(9) of the Internal Revenue Code

Prior to the Taxpayer Relief Act of 1997 (the 1997 Act) and the Internal Revenue Service Restructuring and Reform Act of 1998 (the 1998 Act), the period for assessment of gift tax for a calendar period generally expired three years from the date a gift tax return for that period was deemed to be filed. The statute of limitation protection extended to all gifts made in a calendar period for which a return was filed, including gifts not reported on the gift tax return for the period. An exception to this general rule applied for gifts subject to the special valuation rules of sections 2701 and 2702. For gifts subject to these rules, section 6501(c)(9) extends the period of assessment indefinitely unless the gifts were disclosed on the gift tax return in a manner adequate to apprise the IRS of the nature of the transfer.

Under the 1997 and 1998 Acts, this adequate disclosure requirement was extended to all gifts, whether or not subject to section 2701 or 2702. Consequently, the period of assessment will not close for any gift made in a calendar year ending after August 5, 1997, or with respect to any increase in gift tax required under section 2701(d), that is not adequately disclosed on a gift tax return.

The proposed regulations provide a list of information that, if applicable to a transaction, must be reported on a gift tax return, or a statement attached thereto, in order for the transaction to be considered adequately disclosed to cause the period for assessment to commence. The required information must completely and accurately describe the transaction and include: the nature of the transferred property; the parties involved; the value of the transferred property; and how the value was determined, including any discounts or adjustments used in valuing the transferred property.

Specific rules are provided in the case of transfers of entities that are not actively traded that own interests in other non-actively traded entities. Comments are requested on how these rules should be applied when the required information is not available to the donor.

In addition, the return must disclose the facts affecting the gift tax treatment of the transaction in a manner that reasonably may be expected to apprise the IRS of the nature of any potential controversy regarding the gift tax treatment of the transfer. In lieu of this statement, the taxpayer may provide a statement of any legal issue presented by the facts. Finally, the taxpayer must also provide a statement of any position taken by the taxpayer that is contrary to any temporary or final Treasury regulation or any revenue ruling. These standards are based on those currently employed under §6662 in determining whether an item is adequately disclosed under that section, such that accuracy-related penalties will not be imposed.

The proposed regulations contain examples that illustrate adequate disclosure under these standards.

Under the proposed regulations, adequate disclosure of a transfer that is reported as a completed gift on the gift tax return will commence the running of the statute of limitations under section 6501(c)(9) even if the transfer is ultimately determined to be an incomplete gift. Thus, if the donor reports a transfer on the gift tax return as a completed gift for gift tax purposes, the period for assessing a gift tax with respect to the transfer will commence. If the IRS does not examine the transaction reported on the gift tax return prior to the expiration of the running of the statute of limitations, the transaction will be treated as a completed gift as reported on the gift tax return. If the IRS, upon examination, disagrees with the donor's characterization of the transaction, and the issue remains unresolved through the administrative process, the donor will be sent a final notice of determination and the donor will be able to seek a declaratory judgment on the matter pursuant to section 7477.

On the other hand, if a donor initially reports a transfer as an incomplete gift, even if adequately disclosed, the statute of limitations does not commence to run

until the donor reports the transfer as a completed gift. The IRS would have three years from the date of filing of the subsequent gift tax return disclosing the completed gift to make any assessment with respect to the gift.

As discussed below, the 1997 and 1998 Act amendments to sections 2001 and 2504 curtail the IRS' ability to redetermine the value of a gift in computing the estate or gift tax, after the statute of limitations expires. However, the adequate disclosure requirement contained in section 6501(c)(9) is intended to afford the IRS the reasonable opportunity to identify in a timely manner and with a minimum expenditure of resources returns that present issues that merit further examination. Accordingly, the information required is intended to enable the IRS to identify issues, if any, without imposing an undue burden on taxpayers.

The proposed regulations conform the regulations to the new statutory rules for gifts made in calendar years ending after August 5, 1997, if such gift tax return is filed after the regulations are published as final regulations. In the interim period, the statutory provisions apply.

Valuation of Prior Gifts for Gift Tax Purposes

Prior to the 1997 and 1998 Acts, section 2504(c) provided that if a gift tax had been paid or assessed with respect to the calendar period in which the gift occurred and the statute of limitations on assessment for the prior gift had expired, then the value of any gift made in such calendar period could not be adjusted for purposes of determining the total amount of prior taxable gifts that the individual had made. This prohibition on adjustments applied even if a particular gift was not disclosed on the gift tax return. This rule continues to apply for gifts made prior to August 6, 1997.

Under section 2504(c) as amended by the 1997 and 1998 Acts, if a gift was adequately disclosed such that the time has expired for assessing gift tax for a preceding calendar period under section 6501, then the value of such gift made in the prior calendar period cannot be adjusted (regardless of whether or not a gift tax has been assessed or paid for a prior calendar period). Rather, the value of the gift is the value as finally determined for gift tax

purposes, as defined in section 2001(f). A similar rule applies with respect to any increase in taxable gifts required under section 2701(d) (pertaining to the transfer of applicable retained interests under section 2701).

Section 2504(c) applies only to adjustments involving issues of valuation. Thus, even after the 1997 and 1998 amendments to section 2504(c), adjustments to prior taxable gifts may be made if the adjustment is not related to the valuation of the gift; e.g., the erroneous inclusion or exclusion of property for gift tax purposes. See Rev. Rul. 76-451 (1976-2 C.B. 304). This result is consistent with the legislative history to the 1997 Act which emphasizes that the statutory change imposes a prohibition on revaluing certain gifts. The House Committee report states that a gift for which the limitations period has passed cannot be revalued for purposes of determining the applicable estate tax bracket and available unified credit. H.R. Rep. No. 148, 105th Cong., 1st Sess. 359 (1997).

The proposed regulations conform the regulations to the new statutory rules for gift tax returns filed after the regulations are published as final regulations. In the interim period, the statutory provisions apply.

Valuation of Prior Gifts for Estate Tax Purposes

Prior to the enactment of the 1997 and 1998 Acts, there was no estate tax provision corresponding to section 2504(c). Therefore, even where the period of assessment expired for a calendar period, and gift tax was paid or assessed for that period, the value of any gifts made in that period could be adjusted for purposes of determining the estate tax liability. The statutory change and these proposed regulations preserve that treatment for gifts made prior to August 6, 1997.

Section 2001(f) was added by the 1997 Act and amended by the 1998 Act. Under section 2001(f) as amended, if the time has expired for assessing gift tax for a preceding calendar period under section 6501, then the value of the gift, for purposes of computing the estate tax liability, is the value of the gift as finally determined for gift tax purposes. A similar rule applies for any increase in taxable gifts required under section 2701(d).

Under the statute, the value of a gift is finally determined if: the value is shown on a gift tax return and the IRS does not contest the value before the period for assessing gift tax expires; or, before the period for assessing gift tax expires, the value is specified by the IRS and the taxpayer does not contest the specified value; or, the value is determined by a court or pursuant to a settlement agreement between the taxpayer and the IRS.

As discussed above, the provision only limits the IRS' ability to make adjustments related to the value of a gift. Thus, the IRS is not precluded from making adjustments that are not related to value, such as the erroneous inclusion or exclusion of property for gift tax purposes.

The proposed regulations conform the current regulations to the statutory change for gift tax returns filed after the regulations are published as final regulations. In the interim period, the statutory provisions apply.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 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 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 Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Small Business Administration for comment on their impact on small business.

Comment and Public Hearing

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

A public hearing has been scheduled for Wednesday, April 28, 1999, at 10 a.m. in Room 2615 of the Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC. Due to building security procedures, visitors must enter at the 10th Street entrance, located between Constitution and Pennsylvania Avenues, NW. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 15 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written comments and an outline of the topics to be discussed and the time to be devoted to each topic (a signed original and eight (8) copies) by Wednesday, April 7, 1999.

A period of 10 minutes will be allocated to each person for making comments.

An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is William L. Blodgett, Office of Assistant Chief Counsel (Passthroughs and Special Industries), IRS. However, other personnel from the IRS and Treasury Department participated in their development.

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Proposed Amendments to the Regulations

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

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

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

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

Par. 2. Section 20.2001-1 is revised to read as follows:

§20.2001-1 Valuation of adjusted taxable gifts and section 2701(d) taxable events.

(a) *Adjusted taxable gifts made prior to August 6, 1997.* For purposes of determining the value of adjusted taxable gifts as defined in section 2001(b), if the gift was made prior to August 6, 1997, the value of the gift may be adjusted at any time, even if the time within which a gift tax may be assessed has expired under section 6501. This paragraph (a) also applies to adjustments involving issues other than valuation.

(b) *Adjusted taxable gifts and section 2701(d) taxable events occurring after August 5, 1997.* For purposes of determining the value of adjusted taxable gifts as defined in section 2001(b), if, under section 6501, the time has expired within which a gift tax may be assessed under chapter 12 of the Internal Revenue Code (or under corresponding provisions of prior laws) with respect to a gift made after August 5, 1997, and during a preceding calendar period (as defined in §25.2502-1(c)(2) of this chapter), or with respect to an increase in taxable gifts required under section 2701(d) and §25.2701-4 of this chapter, then the value of the gift will be the value as finally determined for gift tax purposes under chapter 12 of the Internal Revenue Code. This paragraph (b) does not apply to adjustments involving issues other than valuation. See §25.2504-1(d) of this chapter.

(c) *Finally determined.* For purposes of paragraph (a) of this section, the value of a gift is finally determined for gift tax purposes if—

(1) The value is shown on a gift tax return, or on a statement attached to the return, and the Internal Revenue Service does not contest the value before the time has expired under section 6501 within which gift taxes may be assessed;

(2) The value is specified by the Internal Revenue Service before the time has expired under section 6501 within which gift taxes may be assessed on the gift and such specified value is not timely contested by the taxpayer;

(3) The value is finally determined by a court of competent jurisdiction; or

(4) The value is determined pursuant to a settlement agreement entered into between the taxpayer and the Internal Revenue Service.

(d) *Definitions.* For purposes of paragraph (b) of this section, the value is finally determined by a court of competent jurisdiction when the court enters a final decision, judgment, decree or other order passing on the valuation that is not subject to appeal. See, for example, section 7481 regarding the finality of a decision by the U.S. Tax Court. Also, for purposes of paragraph (b) of this section, a settlement agreement means any agreement entered into by the Internal Revenue Service and the taxpayer that is binding on both. The term includes a closing agreement under section 7121, a compromise under section 7122, and an agreement entered into in settlement of litigation involving a valuation issue.

(e) *Expiration of period of assessment.* For purposes of determining if the time has expired within which a tax may be assessed under chapter 12 of the Internal Revenue Code, see §301.6501(c)-1(e) and (f) of this chapter.

(f) *Examples.* The following examples illustrate the rules of this section:

Example 1. (i) *Facts.* A owns Blackacre and B, A's child, owns Whiteacre. In 1999, A and B exchange ownership of these properties. On A's federal gift tax return, Form 709, for the 1999 calendar year, the transfer of Blackacre to B is adequately disclosed under §301.6501(c)-1(f)(2) of this chapter. A reports the transfer as nontaxable, representing that the fair market values of Whiteacre and Blackacre, at the time of the transfer, were equal. A dies after the period of assessment for the transfer has expired.

(ii) *Application of the rule limiting adjustments to valuation issues.* The fair market values of Blackacre and Whiteacre at the time of the transfer are valuation issues. Because A filed the return adequately disclosing the transfer, the period of assessment with respect to A's transfer has expired, notwithstanding the fact that no gift tax return was required to be filed. Therefore, the Internal Revenue Service is precluded from revaluing Blackacre and Whiteacre in determining the amount of A's adjusted taxable gifts in computing A's estate tax liability.

Example 2. (i) *Facts.* In 1999, A transfers stock in a closely-held corporation to an irrevocable trust. Under the terms of the trust, the trustee has the discretion to accumulate trust net income or distribute it among A's children. At A's death, the trust is to terminate and the trust corpus is to be paid to A's surviving issue. On A's federal gift tax return, Form 709, filed for the 1999 calendar year, the transfer is adequately disclosed under §301.6501(c)-1(f)(2) of this chapter. A claims an annual exclusion under

section 2503(b) for the transfer. A dies after the period of assessment for the transfer has expired.

(ii) *Application of the rule limiting adjustments to valuation issues*. Because the period of assessment has closed on the transfer due to adequate disclosure, the Internal Revenue Service is precluded from revaluing the transferred stock for purposes of assessing gift tax. Therefore, the value of the transfer as reported on A's 1999 Federal gift tax return may not be redetermined for purposes of determining A's adjusted taxable gifts. However, the applicability of the annual exclusion to the transfer is a question of law and not of valuation. Accordingly, although the Internal Revenue Service may not assess or collect additional gift tax on the 1999 transfer (because the period of assessment has closed), the Internal Revenue Service is not precluded from challenging the annual exclusion claimed by A for purposes of determining A's adjusted taxable gifts in computing the estate tax liability.

(g) *Effective dates*. Paragraph (a) of this section applies to transfers of property by gift made prior to August 6, 1997, if the estate tax return for the donor/decedent's estate is filed after this document is published as a final regulation in the **Federal Register**. Paragraphs (b) through (f) of this section apply to transfers of property by gift made after August 5, 1997, if the gift tax return for the calendar period in which the gift is made is filed after this document is published as a final regulation in the **Federal Register**.

PART 25—GIFT TAX; GIFTS MADE AFTER DECEMBER 31, 1954

Par. 3. The authority citation for part 25 continues to read in part as follows:

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

Par. 4. Section 25.2504-2 is revised to read as follows:

§25.2504-2 Valuation of certain gifts for preceding calendar periods.

(a) *Gifts made before August 6, 1997*. If the time has expired within which a tax may be assessed under chapter 12 of the Internal Revenue Code (or under corresponding provisions of prior laws) on the transfer of property by gift made during a preceding calendar period, as defined in §25.2502-1(c)(2), the gift was made prior to August 6, 1997, and a tax has been assessed or paid for such prior calendar period, the value of the gift, for purposes of arriving at the correct amount of the taxable gifts for the preceding calendar periods (as defined under §25.2504-1(a)), is the value used in computing the tax for the last preceding calendar period for

which a tax was assessed or paid under chapter 12 of the Internal Revenue Code or the corresponding provisions of prior laws. However, this rule does not apply where no tax was paid or assessed for the prior calendar period. Furthermore, this rule does not apply to adjustments involving issues other than valuation. See §25.2504-(d).

(b) *Gifts made or section 2701(d) taxable events occurring after August 5, 1997*. If the time has expired under section 6501 within which a gift tax may be assessed under chapter 12 of the Internal Revenue Code (or under corresponding provisions of prior laws) on the transfer of property by gift made during a preceding calendar period, as defined in §25.2502-1(c)(2), or with respect to an increase in taxable gifts required under section 2701(d) and §25.2701-4, and the gift was made, or the section 2701(d) taxable event occurred, after August 5, 1997, the value of the gift or the amount of the increase in taxable gifts, for purposes of determining the correct amount of taxable gifts for the preceding calendar periods (as defined in §25.2504-1(a)), is the value that is finally determined for gift tax purposes (within the meaning of §20.2001-1(c) of this chapter). This rule does not apply to adjustments involving issues other than valuation. See §25.2504-1(d). For an illustration of this rule, see the examples under §20.2001-1(f) of this chapter. For purposes of determining if the time has expired within which a gift tax may be assessed, see §301.6501(c)-1(e) and (f) of this chapter.

(c) *Example*. The following example illustrates the rules of paragraphs (a) and (b) of this section:

Example. (i) *Facts*. In 1996, A transfers closely-held stock to B, A's child. A timely filed a federal gift tax return reporting the 1996 transfer to B. No gift tax was assessed or paid as a result of application of A's available unified credit. In 1999, A transfers additional closely-held stock to B. A's federal gift tax return reporting the 1999 transfer is timely filed and the transfer is adequately disclosed under §301.6501(c)-1(f)(2) of this chapter. In 2003, A transfers additional property to B and timely files a federal gift tax return reporting the gift.

(ii) *Application of the rule limiting adjustments to valuation of prior gifts*. Under section 2504(c), in determining A's 2003 gift tax liability, the value of A's 1996 gift can be adjusted for purposes of computing the value of prior taxable gifts, since that gift was made prior to August 6, 1997, and therefore, the provisions of paragraph (a) of this section apply.

However, A's 1999 transfer was adequately disclosed on a timely filed gift tax return and, thus, under §25.2504-1(b), the value of the 1999 gift by A may not be adjusted for purposes of computing the value of prior taxable gifts in determining A's 2003 gift tax liability.

(d) *Effective dates*. Paragraph (a) of this section applies to transfers of property by gift made prior to August 6, 1997. Paragraphs (b) and (c) of this section apply to transfers of property by gift made after August 5, 1997, if the gift tax return for the calendar period in which the transfer is reported is filed after this document is published as a final regulation in the Federal Register.

PART 301—PROCEDURE AND ADMINISTRATION

Par. 5. The authority citation for part 301 continues to read in part as follows:

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

Par. 6. Section 301.6501(c)-1 is amended by:

1. Revising the heading to paragraph (e).
2. Adding paragraph (f).

The revision and addition reads as follows:

§301.6501(c)-1 Exceptions to general period of limitations on assessment and collection.

* * * * *

(e) *Gifts subject to chapter 14 of the Internal Revenue Code not adequately disclosed on the return—*

* * * * *

(f) *Gifts made after August 5, 1997, not adequately disclosed on the return—(1) In general*. If a transfer of property, other than a transfer described in paragraph (e) of this section, is not adequately disclosed on a gift tax return (Form 709 United States Gift (and Generation-Skipping Transfer) Tax Return) filed for the calendar period in which the transfer occurs, then any gift tax imposed by chapter 12 of subtitle B of the Internal Revenue Code on the transfer may be assessed, or a proceeding in court for the collection of the appropriate tax may be begun without assessment, at any time.

(2) *Adequate disclosure of transfers of property reported as gifts*. A transfer will be adequately disclosed on the return only

if it is reported in a manner adequate to apprise the Internal Revenue Service of the nature of the gift and the basis for the value so reported. Transfers reported on the gift tax return as transfers of property by gift will be considered adequately disclosed under this paragraph (f) only if the return provides a complete and accurate description of the transaction including—

(i) A description of the transferred property and any consideration received by the transferor;

(ii) The identity of, and relationship between, the transferor and the transferee;

(iii) A detailed description of the method used to determine the fair market value of property transferred, including any relevant financial data and a description of any discounts, such as discounts for blockage, minority or fractional interests, and lack of marketability, claimed in valuing the property. In the case of the transfer of an interest in an entity (e.g., a corporation or partnership) that is not actively traded, a description of any discount claimed in valuing the entity or any assets owned by such entity, including a statement regarding the fair market value of 100 percent of the entity (determined without regard to any discounts in valuing the entity or any assets owned by the entity), the pro rata portion of the entity subject to the transfer, and the fair market value of the transferred interest as reported on the return. If the entity that is the subject of the transfer owns an interest in another non-actively traded entity (either directly or through ownership of an entity), the information required in this paragraph (f)(2)(iii) must be provided for each entity and the assets owned by each entity;

(iv) If the property is transferred in trust, the trust's tax identification number and a brief description of the terms of the trust;

(v) Any restrictions on the transferred property that were considered in determining the fair market value of the property; and

(vi) A statement of the relevant facts affecting the gift tax treatment of the transfer that reasonably may be expected to apprise the Internal Revenue Service of the nature of any potential controversy concerning the gift tax treatment of the transfer, or in lieu of this statement, a concise description of the legal issue pre-

sented by the facts. In addition, a statement describing any position taken that is contrary to any temporary or final Treasury regulations or revenue rulings.

(3) Adequate disclosure of non-gift completed transfers or transactions.

Completed transfers, all or a portion of which are reported as not constituting a transfer by gift (for example, a transaction in the ordinary course of business), will be considered adequately disclosed under this paragraph (f) only if the following information is provided on or attached to the return—

(i) The information required for adequate disclosure under paragraph (f)(2) of this section; and

(ii) An explanation as to why the transfer is not a transfer by gift under chapter 12 of the Internal Revenue Code.

(4) Adequate disclosure of incomplete transfers. Adequate disclosure of a transfer that is reported as a completed gift on the gift tax return will commence the running of the statute of limitations for assessment of gift tax on the transfer, even if the transfer is ultimately determined to be an incomplete gift for purposes of §25.2511-2 of this chapter. For example, if an incomplete gift is reported as a completed gift on the gift tax return and is adequately disclosed, the period for assessment of the gift tax will begin running when the return is filed, as determined under section 6501(b). On the other hand, if the transfer is reported as an incomplete gift and adequately disclosed, the period for assessing a gift tax with respect to the transfer will not commence to run even if the transfer is ultimately determined to be a completed gift. In that situation, the gift tax with respect to the transfer may be assessed at any time, up until three years after the donor files a return reporting the transfer as a completed gift.

(5) Examples. The following examples illustrate the rules of this paragraph (f):

Example 1. (i) Facts. In 1999, A transfers 100 shares of common stock of XYZ Corporation to A's child. The common stock of XYZ Corporation is actively traded on a major stock exchange. For gift tax purposes, the fair market value of one share of XYZ common stock on the date of the transfer, determined in accordance with §25.2512-2(b) of this chapter (based on the mean between the highest and lowest quoted selling prices), is \$150.00. On A's federal gift tax return, Form 709, for the 1999 calendar year, A reports the gift as 100 shares of common stock of XYZ Corporation with a value for gift tax

purposes of \$15,000. A specifies the date of the transfer, recites that the stock is publicly traded, and identifies the stock exchange on which the stock is traded.

(ii) *Application of the adequate disclosure standard.* A has adequately disclosed the transfer. Therefore, the period of assessment for the transfer under section 6501 will run from the time the return is filed (as determined under section 6501(b)).

Example 2. (i) Facts. On December 30, 1999, A transferred closely-held stock to B, A's child. A determined that the value of the transferred stock, on December 30, 1999, was \$9,000. A made no other transfers to B, or any other donee, during 1999. On A's federal gift tax return, Form 709, filed for the 1999 calendar year, A provides the information required under paragraph (f)(2) of this section (including the method used to determine the fair market value of the stock and a description of discounts claimed) such that the transfer is adequately disclosed. A claims an annual exclusion under section 2503(b) for the transfer.

(ii) *Application of the adequate disclosure standard.* Because the transfer was adequately disclosed under paragraph (f)(2) of this section, the period of assessment for the transfer will expire as prescribed by section 6501(b), notwithstanding that if A's valuation of the closely-held stock was correct, A was not required to file a gift tax return reporting the transfer under section 6019. After the period of assessment has expired on the transfer, the Internal Revenue Service is precluded from revaluing the transferred stock for purposes of assessing gift tax or for purposes of determining the estate tax liability. Therefore, the value of the transfer as reported on A's 1999 federal gift tax return may not be redetermined for purposes of determining A's prior taxable gifts (for gift tax purposes) or A's adjusted taxable gifts (for estate tax purposes).

Example 3. (i) Facts. A owns 100 percent of the common stock of X, a closely-held corporation. X does not hold an interest in any other entity that is not actively traded. In 1999, A transfers 20 percent of the X stock to B and C, A's children, in a transfer that is not subject to the special valuation rules of section 2701. The transfer is made outright with no restrictions on ownership rights, including voting rights and the right to transfer the stock. The reported value of the transferred stock incorporates the use of minority discounts and lack of marketability discounts. No other discounts were used in arriving at the fair market value of the transferred stock or any assets owned by X. A reports the transfer on a federal gift tax return, Form 709, for the 1999 calendar year. On the return, A provides a statement reporting the fair market value of 100 percent of X (before taking into account any discounts), the pro rata portion of X subject to the transfer, and the reported value of the transfer. A also attaches a statement regarding the determination of value that includes a discussion of the discounts claimed and how the discounts were determined.

(ii) *Application of the adequate disclosure standard.* A has provided sufficient information such that the transfer will be considered adequately disclosed and the period of assessment for the transfer under section 6501 will run from the time the return is filed (as determined under section 6501(b)).

Example 4. (i) Facts. A owns a 70 percent limited partnership interest in PS. PS owns 40 percent

of the stock in X, a closely-held corporation. The assets of X include a 50 percent general partnership interest in PB. PB owns an interest in commercial real property. None of the entities (PS, X, or PB) is actively traded. In 1999, A transfers a 25 percent limited partnership interest in PS to B, A's child. On the federal gift tax return, Form 709, filed for the 1999 calendar year, A reports the transfer of the 25 percent limited partnership interest in PS and that the fair market value of 100 percent of PS is \$y and that the value of 25 percent of PS is \$z, reflecting marketability and minority discounts with respect to the 25 percent interest. However, A does not disclose that PS owns 40 percent of X, and that X owns 50 percent of PB and that, in arriving at the \$y fair market value of 100 percent of PS, discounts were claimed in valuing PS's interest in X, X's interest in PB, and PB's interest in the commercial real property.

(ii) *Application of the adequate disclosure standard.* Because A has failed to comply with requirements of paragraph (f)(2) of this section regarding PS's interest in X, X's interest in PB, and PB's interest in the commercial real property, the transfer will not be considered adequately disclosed and the period of assessment for the transfer under section 6501 will remain open indefinitely.

(6) *Effective date.* This paragraph (f) is applicable to gifts made in calendar years ending after August 5, 1997, if the gift tax return for such calendar year is filed after this document is published as a final regulation in the Federal Register.

Robert E. Wenzel,
*Deputy Commissioner of
Internal Revenue.*

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