T.D. 8845

DEPARTMENT OF THE TREASURY
Internal Revenue Service

26 CFR Part 20

Adequate Disclosure of Gifts

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to changes made to Internal Revenue Code sections 2001, 2504, and 6501 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. These regulations are necessary because section 6501(c)(9) now requires that a gift must be adequately disclosed on a gift tax return in order to commence the running of the period of limitations on assessment with respect to the gift. Once the period of limitations expires, the amount of that gift as reported on the return may not be adjusted for purposes of determining future gift and estate tax liability. The regulations provide guidance on what constitutes adequate disclosure for purposes of the statute.

DATES: These regulations are effective December 3, 1999.

FOR FURTHER INFORMATION CONTACT: William L. Blodgett, (202) 622-3090 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these final regulations 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 1545–1637. Responses to this collection of information are mandatory.

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

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, OP:FS:FP, Washington, DC 20224, and 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.

Books or records relating to this collection of information must be retained as long as their contents may be 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.

Background

On December 22, 1998, the IRS published in the **Federal Register** (63 FR 70701) a notice of proposed rulemaking (REG–106177–98, 1998–2 C.B. 344) under sections 2001 and 2504 relating to the value of prior gifts for purposes of computing the estate and gift tax, and under section 6501 relating to the period for assessment and collection of gift tax. Written comments responding to the notice of proposed rulemaking were received and a hearing was held on April 28, 1999, at which time oral testimony was presented. This document adopts final regulations with respect to this notice of proposed rulemaking. A summary of the principal comments received and the revisions made in response to those comments is provided below.

1. *Requirements for Adequate Disclosure*

Under section 6501(c)(9), the period of limitations on the assessment of gift tax with respect to a gift will commence to run only if the gift is adequately disclosed on the gift tax return. The proposed regulations provide a list of information required to satisfy the adequate disclosure standard.

In general, the comments objected to the quantity, detail, and nature of the information required under the proposed regulations. In some cases, information required in the proposed regulations is not required in the final regulations. However, Treasury and the IRS continue to believe that the adequate disclosure rule was intended to afford the IRS a viable means to identify the returns that should be examined, with a minimum expenditure of resources. Further, the more complete and comprehensive the information filed with the return is, the more readily the IRS will be able to identify the returns that should not be examined, thus saving taxpayers needless expenditures of time and money.

Several commentators suggested that the language in §301.6501–1(f)(2) of the proposed regulations imposed two requirements for adequate disclosure. That is, the taxpayer had to provide information adequate to apprise the IRS of the nature of the gift, etc. and in addition, the taxpayer had to provide the information listed in the regulation. In response to these comments, the final regulations clarify that the adequate disclosure requirement is satisfied if the information listed in the regulation is provided.

Some commentators argued that Congress intended that the new adequate disclosure requirements be the same as the existing disclosure requirements under prior section 6501(c)(9) for pre-August 5, 1997 gifts of property subject to the special valuation rules of sections 2701 and 2702. Therefore, the commentators suggested that the IRS adopt the disclosure requirements under §301.6501(c)–1(e)(2) for transfers of those interests. This suggestion was not adopted. The IRS and Treasury believe it is necessary to expand on those disclosure requirements to address the broader range of transfers covered by the new legislation, as well as transactions and entities that may not have been prevalent when the prior regulations were promulgated.

Under the proposed regulations, if property is transferred in trust, taxpayers are required to provide a brief description of the terms of the trust. In response to comments, the final regulations provide that taxpayers may submit a complete copy of the trust document in lieu of a description of the trust terms.

The proposed regulations require the submission of a detailed description of the method used in determining the fair market value of the property, including "any relevant financial data." Commentators contended that "any relevant financial data" is a subjective concept that lacks specificity. Rather, the regulations should specify exactly what financial data must be submitted, such as balance sheets, net earnings statements, etc. In response to these comments, the final regulations require that any financial data that was used in valuing the interest must be submitted. This ensures that the information requested is available and was deemed relevant by the person valuing the interest.

Several commentators expressed concern over the requirement in the proposed regulations that, if a less-than-100-percent interest in a non-actively traded entity is transferred, the taxpayer must submit a statement regarding the fair market value of 100 percent of the entity determined without regard to any discounts. It was contended that a less-than-100-percent interest in an operating company may not be valued based on a pro rata portion of the value of 100 percent of the entity; rather the appraiser often will determine the value based on indicia other than the value of the entire entity, such as the price/earnings ratio of stock in comparable publicly-traded entities. Because the entire entity is not valued in these situations, valuing 100 percent of the entity would not be relevant. One comment stated that this requirement would be reasonable in valuing an interest in nonactively-traded entities, such as entities holding securities or real estate, since in those cases the value of an interest in the entity would be determined based on a pro rata portion of the value of 100 percent of the entity. In response to these comments, the final regulations do not require a statement of the fair market value of 100 percent of the entity (without regard to any discounts), if the value of the interest in the entity is properly determined without using the net asset value of the entire entity. If 100 percent of the value of the entity is not disclosed, the taxpayer bears the burden of demonstrating that the fair market value of the entity is properly determined by a method other than a method based on the net value of the assets held by the entity.

The proposed regulations also require valuation information for each entity (and its assets) that is owned or controlled by the entity subject to the transfer. Comments indicated that this requirement would be difficult to satisfy, because in some cases the information would not be within the control of the taxpayer and the entity subject to the transfer would not normally be required to maintain the financial records with respect to lower-tiered entities. The comments suggested that information on the lower-tiered entities should be required only to the extent such information is essential to a reasonable appraisal of the interest transferred and is in the personal control of the taxpayer. Many commentators suggested that the regulations require the submission of only that information that a qualified and competent appraiser would use in valuing the interest. In response to these comments, the final regulations provide that the information on the lower-tiered entities must be submitted if the information is relevant and material in determining the value of the interest in the entity.

Finally, comments suggested that a properly completed appraisal would contain all the information that is material and relevant to the valuation of the transferred property and, therefore, should be sufficient to satisfy any disclosure requirement. Accordingly, under the final regulations, an appraisal satisfying specific requirements may be submitted in lieu of a detailed description of the method used to determine the fair market value and in lieu of information regarding tiered entities.

The proposed regulations require a statement of relevant facts that would apprise the IRS of the nature of any potential gift tax controversy concerning the transfer, or instead of that statement, a concise description of the legal issue presented by the facts. This requirement is similar to the disclosure required to avoid the accuracy-related penalty under section 6662. It was intended to enable the IRS to easily identify issues presented so that the IRS could evaluate whether an examination is warranted during the initial review of the gift tax return. Commentators indicated that the requirement was too subjective and open-ended, since it would be difficult for a practitioner to identify or anticipate "any" potential controversy. In response to these comments, that requirement has been eliminated from the final regulations. The proposed regulations also require that the taxpayer submit a statement describing any position taken that is contrary to any temporary or final regulations or any revenue ruling. Commentators were concerned that this requirement could be interpreted as including both regulations and revenue rulings that are published after the gift tax return is filed that interpret earlier IRS positions. In response to these comments, the final regulations limit the required statement to positions taken that are contrary to any proposed, temporary or final regulation, and any revenue ruling published at the time the transfer occurred.

Commentators also noted that, under the proposed regulations, if a taxpayer failed to provide, for example, one item of information, the adequate disclosure requirement would not be satisfied, regardless of the significance of the item. The comments suggested that "substantial compliance" with the requirements of the regulations or a good-faith effort to comply should be deemed actual compliance. This suggestion was not adopted in view of the difficulty in defining and illustrating what would constitute substantial compliance. However, it is not intended that the absence of any particular item or items would necessarily preclude satisfaction of the regulatory requirements, depending on the nature of the item omitted and the overall adequacy of the information provided.

In response to comments, a rule was added regarding the application of the adequate disclosure rules in the case of "split gifts" under section 2513. Under this rule, gifts attributed to the non-donor spouse are deemed to be adequately disclosed if the gifts are adequately disclosed on the return filed by the donor spouse.

2. *Finality with Respect to Adequately Disclosed Gifts*

Under the proposed regulations, if a transfer is adequately disclosed on the gift tax return, and the period for assessment of gift tax has expired, then the IRS is foreclosed from adjusting the value of the gift under section 2504(c) (for purposes of determining the current gift tax liability) and under section 2001(f) (for purposes of determining the estate tax liability). However, the IRS is not precluded from making adjustments involving legal issues, even if the gift was adequately disclosed. This position was based on long-standing regulations applying section 2504(c) and relevant case law.

Comments suggested that this rule is contrary to Congressional intent in enacting section 2001(f) and amending section 2504(c) to provide a greater degree of finality with respect to the gift and estate tax statutory scheme. In response to these comments, the final regulations preclude adjustments with respect to all issues related to a gift once the gift tax statute of limitations expires with respect to that gift.

3. *Non-gift Transactions*

Under the proposed regulations, a completed transfer that did not constitute a gift would be considered adequately disclosed if the taxpayer submitted the information required for adequate disclosure and an explanation describing why the transfer was not subject to the gift tax. One commentator suggested that the adequate disclosure requirement should be waived if the taxpayer reasonably, in good faith, believes the transfer is not a gift (for example, a salary payment made to a child employed in a family business). Another commentator noted that the standard for adequate disclosure is higher for a "non-gift" than it is for a gift transaction since, in the non-gift situation, the donor must provide all the information required by the regulation and a statement why the transaction is not a gift. Another comment requested more guidance for reporting non-gift business transactions. In response to the comments, the final regulations limit the information required in a non-gift situation. In addition, the final regulations provide that completed transfers to members of the transferor's family (as defined in section 2032A(e)(2)) in the ordinary course of operating a business are deemed to be adequately disclosed, even if not reported on a gift tax return, if the item is properly reported by all parties for income tax purposes. For example, in the case of a salary payment made to a child of the donor employed in the donor's business, the transaction will be treated as adequately disclosed for gift tax purposes if the salary payment is properly reported by the business and the child on their income tax returns. This exception only applies to transactions conducted in the ordinary course of operating a business. It does not apply, for example, in the case of a sale of property (including a business) by a parent to a child.

4. *Effective Date Provisions*

Several comments were received regarding clarification of the statutory effective date rules.

One comment requested clarification of the effective date of section 6501(c)(9), as amended. The Taxpayer Relief Act of 1997 provides that the amendments to section 6501(c)(9) (commencing the running of the period of limitations only if the gift is adequately disclosed) apply to gifts made in calendar years ending after August 5, 1997 (that is, all gifts made in calendar year 1997 and thereafter). However, the underlying legislative history indicates that the amendment to section 6501(c)(9) applies "to gifts made in calendar years after the date of enactment [August 5, 1997]". H.R. Conf. Rep. No. 220, 105th Cong., 1st Sess. 408 (1997). Notwithstanding this statement in the legislative history, the statutory language is clear that the section as amended applies to all gifts made during the 1997 calendar year, and thereafter. In the final regulations, the statutory effective date language is restated in a manner that makes it clear that section 6501(c)(9) as amended applies to all gifts made after December 31, 1996.

Another comment suggested clarification of the application of the adequate disclosure rules and the interaction between sections 2504(c) and 6501(c)(9) with respect to gifts made between January 1, 1997, and August 6, 1997, since section 2504(c) as amended applies only to gifts made after August 5, 1997, but section 6501(c)(9) as amended applies to all gifts made in 1997. In response to this comment, an example has been added under §25.2504–2(c) involving a situation where a gift is made prior to August 6, 1997, that is not adequately disclosed on the return filed for 1997. The example clarifies that the period for assessment with respect to the pre-August 6, 1997 gift does not commence to run because the gift is not adequately disclosed. Accordingly, a gift tax may be assessed with respect to the gift at any time, and notwithstanding the effective date for section 2504(c), that 1997 gift can be adjusted as a part of prior taxable gifts in determining subsequent gift tax liability. Further, the 1997 gift can be adjusted as part of taxable gifts under section 2001 in determining estate tax liability.

Finally, in response to another comment, an example has been added illustrating the application of the effective date rules in a similar fact pattern, where the gifts are made in a calendar year prior to 1997. The example illustrates that the IRS may not revalue the gifts, for purposes of determining prior taxable gifts for gift tax purposes, if a gift tax was paid and assessed with respect to the calendar year, and the period for assessment has expired. Since the gifts were made prior to 1997, the rules of section 2504(c) and section 6501 prior to amendment apply. However, the IRS may adjust the gifts for purposes of determining adjusted taxable gifts for estate tax purposes.

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 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, the notice of proposed rulemaking preceding these regulations was submitted to the Small Business Administration for comment on their impact on small business.

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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Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 20, 25, 301 and 602 are 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 for gifts made prior to August 6, 1997.

(b) *Adjusted taxable gifts and section 2701(d) taxable events occurring after August 5, 1997.* For purposes of determining the amount 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, or with respect to an increase in taxable gifts required under section 2701(d) and §25.2701–4 of this chapter, then the amount of the taxable gift will be the amount as finally determined for gift tax purposes under chapter 12 of the Internal Revenue Code and the amount of the taxable gift may not thereafter be adjusted. The rule of this paragraph (b) applies to adjustments involving all issues relating to the gift, including valuation issues and legal issues involving the interpretation of the gift tax law.

(c) *Finally determined.* For purposes of paragraph (b) of this section, the amount of a taxable gift as finally determined for gift tax purposes is—

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

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

(3) The amount as finally determined by a court of competent jurisdiction; or

(4) The amount as 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 amount is finally determined by a court of competent jurisdiction when the court enters a final decision, judgment, decree or other order with respect to the amount of the taxable gift 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 the amount of the taxable gift.

(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) *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 December 3, 1999. Paragraphs (b) through (e) 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 December 3, 1999.

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. In §25.2504–1, a sentence is added at the end of paragraph (d) to read as follows:

§25.2504–1 Taxable gifts for preceding calendar periods.

* * * * *

(d) * * * However, see §25.2504–2(b) regarding certain gifts made after August 5, 1997.

Par. 5. Section 25.2504–2 is revised to read as follows:

§25.2504–2 Determination of 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 §25.2504–1(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 amount of the taxable 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 amount that is finally determined for gift tax purposes (within the meaning of §20.2001–1(c) of this chapter) and such amount may not be thereafter adjusted. The rule of this paragraph (b) applies to adjustments involving all issues relating to the gift including valuation issues and legal issues involving the interpretation of the gift tax law. 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) *Examples*. The following examples illustrate the rules of paragraphs (a) and (b) of this section:

Example 1. (i) *Facts*. In 1996, A transferred closely-held stock in trust for the benefit of 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 the gift tax annual exclusion and the application of A's available unified credit. In 2001, A transferred additional closely-held stock to the trust. A's Federal gift tax return reporting the 2001 transfer was timely filed and the transfer was adequately disclosed under §301.6501(c)–1(f)(2) of this chapter. In computing the amount of taxable gifts, A claimed annual exclusions with respect to the transfers in 1996 and 2001. 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 prior gifts*. Under section 2504(c), in determining A's 2003 gift tax liability, the amount of A's 1996 gift can be adjusted for purposes of computing prior taxable gifts, since that gift was made prior to August 6, 1997, and therefore, the provisions of paragraph (a) of this section apply. Adjustments can be made with respect to the valuation of the gift and legal issues presented (for example, the availability of the annual exclusion with respect to the gift). However, A's 2001 transfer was adequately disclosed on a timely filed gift tax return and, thus, under paragraph (b) of this section, the amount of the 2001 taxable gift by A may not be adjusted (either with respect to the valuation of the gift or any legal issue) for purposes of computing prior taxable gifts in determining A's 2003 gift tax liability.

Example 2. (i) *Facts*. In 1996, A transferred closely-held stock to B, A's child. A timely filed a Federal gift tax return reporting the 1996 transfer to B and paid gift tax on the value of the gift reported on the return. On August 1, 1997, A transferred additional closely-held stock to B in exchange for a promissory note signed by B. Also, on September 10, 1997, A transferred closely-held stock to C, A's other child. On April 15, 1998, A timely filed a gift tax return for 1997 reporting the September 10, 1997, transfer to C and, under §301.6501(c)–1(f)(2) of this chapter, adequately disclosed that transfer and paid gift tax with respect to the transfer. However, A believed that the transfer to B on August 1, 1997, was for full and adequate consideration and A did not report the transfer to B on the 1997 Federal gift tax return. In 2002, 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 prior gifts*. Under section 2504(c), in determining A's 2002 gift tax liability, the value of A's 1996 gift cannot be adjusted for purposes of computing the value of prior taxable gifts, since that gift was made prior to August 6, 1997, and a timely filed Federal gift tax return was filed on which a gift tax was assessed and paid. However, A's prior taxable gifts can be adjusted to reflect the August 1, 1997, transfer because, although a gift tax return for 1997 was timely filed and gift tax was paid, under §301.6501(c)–1(f) of this chapter the period for assessing gift tax with respect to the August 1, 1997, transfer did not commence to run since that transfer was not adequately disclosed on the 1997 gift tax return. Accordingly, a gift tax may be assessed with respect to the August 1, 1997, transfer and the amount of the gift would be reflected in prior taxable gifts for purposes of computing A's gift tax liability for 2002. A's September 10, 1997, transfer to C was adequately disclosed on a timely filed gift tax return and, thus, under paragraph (b) of this section, the amount of the September 10, 1997, taxable gift by A may not be adjusted for purposes of computing prior taxable gifts in determining A's 2002 gift tax liability.

Example 3. (i) *Facts*. In 1994, A transferred closely-held stock to B and C, A's children. A timely filed a Federal gift tax return reporting the 1994 transfers to B and C and paid gift tax on the value of the gifts reported on the return. Also in 1994, A transferred closely-held stock to B in exchange for a bona fide promissory note signed by B. A believed that the transfer to B in exchange for the promissory note was for full and adequate consideration and A did not report that transfer to B on the 1994 Federal gift tax return. In 2002, 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 prior gifts*. Under section 2504(c), in determining A's 2002 gift tax liability, the value of A's 1994 gifts cannot be adjusted for purposes of computing prior taxable gifts because those gifts were made prior to August 6, 1997, and a timely filed Federal gift tax return was filed with respect to which a gift tax was assessed and paid, and the period of limitations on assessment has expired. The provisions of paragraph (a) of this section apply to the 1994 transfers. However, for purposes of determining A's adjusted taxable gifts in computing A's estate tax liability, the gifts may be adjusted. See §20.2001–1(a) of this chapter.

(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 December 3, 1999.

Par. 6. In §25.2511–2, paragraph (j) is revised to read as follows:

§25.2511–2 Cessation of donor's dominion and control.

* * * * *

(j) If the donor contends that a power is of such nature as to render the gift incomplete, and hence not subject to the tax as of the calendar period (as defined in §25.2502–1(c)(1)) of the initial transfer, see §301.6501(c)–1(f)(5) of this chapter.

PART 301—PROCEDURE AND ADMINISTRATION

Par. 7. The authority citation for part 301 continues to read in part as follows:

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

Par. 8. 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 In-*

ternal Revenue Code not adequately disclosed on the return. * * *

(f) *Gifts made after December 31, 1996, 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"), or in a statement attached to the 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)(2) if the return (or a statement attached to the return) provides the following information—

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

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

(iii) If the property is transferred in trust, the trust's tax identification number and a brief description of the terms of the trust, or in lieu of a brief description of the trust terms, a copy of the trust instrument;

(iv) Except as provided in §301.6501–1(f)(3), a detailed description of the method used to determine the fair market value of property transferred, including any financial data (for example, balance sheets, etc. with explanations of any adjustments) that were utilized in determining the value of the interest, any restrictions on the transferred property that were considered in determining the fair market value of the property, 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 a transfer of an interest that is actively traded on an established exchange, such as the New York Stock Exchange, the American Stock Exchange, the NASDAQ National Market, or a regional exchange in which quotations are published on a daily basis, including recognized foreign exchanges, recitation of the exchange where the interest is listed, the CUSIP number of the security, and the mean between the highest and lowest quoted selling prices on the applicable valuation date will satisfy all of the requirements of this paragraph (f)(2)(iv). In the case of the transfer of an interest in an entity (for example, a corporation or partnership) that is not actively traded, a description must be provided of any discount claimed in valuing the interests in the entity or any assets owned by such entity. In addition, if the value of the entity or of the interests in the entity is properly determined based on the net value of the assets held by the entity, a statement must be provided 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 100 percent of the value of the entity is not disclosed, the taxpayer bears the burden of demonstrating that the fair market value of the entity is properly determined by a method other than a method based on the net value of the assets held by the entity. 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)(iv) must be provided for each entity if the information is relevant and material in determining the value of the interest; and

(v) A statement describing any position taken that is contrary to any proposed, temporary or final Treasury regulations or revenue rulings published at the time of the transfer (see §601.601(d)(2) of this chapter).

(3) *Submission of appraisals in lieu of the information required under paragraph (f)(2)(iv) of this section.* The requirements of paragraph (f)(2)(iv) of this section will be satisfied if the donor submits an appraisal of the transferred property that meets the following requirements—

(i) The appraisal is prepared by an appraiser who satisfies all of the following requirements:

(A) The appraiser is an individual who holds himself or herself out to the public as an appraiser or performs appraisals on a regular basis.

(B) Because of the appraiser's qualifications, as described in the appraisal that details the appraiser's background, experience, education, and membership, if any, in professional appraisal associations, the appraiser is qualified to make appraisals of the type of property being valued.

(C) The appraiser is not the donor or the donee of the property or a member of the family of the donor or donee, as defined in section 2032A(e)(2), or any person employed by the donor, the donee, or a member of the family of either; and

(ii) The appraisal contains all of the following:

(A) The date of the transfer, the date on which the transferred property was appraised, and the purpose of the appraisal.

(B) A description of the property.

(C) A description of the appraisal process employed.

(D) A description of the assumptions, hypothetical conditions, and any limiting conditions and restrictions on the transferred property that affect the analyses, opinions, and conclusions.

(E) The information considered in determining the appraised value, including in the case of an ownership interest in a business, all financial data that was used in determining the value of the interest that is sufficiently detailed so that another person can replicate the process and arrive at the appraised value.

(F) The appraisal procedures followed, and the reasoning that supports the analyses, opinions, and conclusions.

(G) The valuation method utilized, the rationale for the valuation method, and the procedure used in determining the fair market value of the asset transferred.

(H) The specific basis for the valuation, such as specific comparable sales or transactions, sales of similar interests, asset-based approaches, merger-acquisition transactions, etc.

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

Completed transfers to members of the transferor's family, as defined in section 2032A(e)(2), that are made in the ordinary course of operating a business are deemed to be adequately disclosed under paragraph (f)(2) of this section, even if the transfer is not reported on a gift tax return, provided the transfer is properly reported by all parties for income tax purposes. For example, in the case of salary paid to a family member employed in a family owned business, the transfer will be treated as adequately disclosed for gift tax purposes if the item is properly reported by the business and the family member on their income tax returns. For purposes of this paragraph (f)(4), any other completed transfer that is reported, in its entirety, as not constituting a transfer by gift will be considered adequately disclosed under paragraph (f)(2) of this section only if the following information is provided on, or attached to, the return—

(i) The information required for adequate disclosure under paragraphs (f)(2)(i), (ii), (iii) and (v) 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.

(5) *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 period 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 to run when the return is filed, as determined under section 6501(b). Further, once the period of assessment for gift tax expires, the transfer will not be subject to inclusion in the donor's gross estate for estate tax purposes. On the other hand, if the transfer is reported as an incomplete gift whether or not 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 with adequate disclosure.

(6) *Treatment of split gifts*. If a husband and wife elect under section 2513 to treat a gift made to a third party as made one-half by each spouse, the requirements of this paragraph (f) will be satisfied with respect to the gift deemed made by the consenting spouse if the return filed by the donor spouse (the spouse that transferred the property) satisfies the requirements of this paragraph (f) with respect to that gift.

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

Example 1. (i) *Facts*. In 2001, 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 2001 calendar year, A reports the gift to A's child of 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, identifies the stock exchange on which the stock is traded, lists the stock's CUSIP number, and lists the mean between the highest and lowest quoted selling prices for the date of transfer.

(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, 2001, A transfers closely-held stock to B, A's child. A determined that the value of the transferred stock, on December 30, 2001, was $9,000. A made no other transfers to B, or any other donee, during 2001. On A's Federal gift tax return, Form 709, for the 2001 calendar year, A provides the information required under paragraph (f)(2) of this section 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 is 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 redetermining the amount of the gift for purposes of assessing gift tax or for purposes of determining the estate tax liability. Therefore, the amount of the gift as reported on A's 2001 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 2001, 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. Based on generally applicable valuation principles, the value of X would be determined based on the net value of the assets owned by X. 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. On A's Federal gift tax return, Form 709, for the 2001 calendar year, A provides the information required under paragraph (f)(2) of this section including 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 and, based on generally applicable valuation principles, the value of each entity would be determined based on the net value of the assets owned by each entity. In 2001, A transfers a 25 percent limited partnership interest in PS to B, A's child. On the Federal gift tax return, Form 709, for the 2001 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*. The information on the lower tiered entities is relevant and material in determining the value of the transferred interest in PS. Accordingly, because A has failed to comply with requirements of paragraph (f)(2)(iv) 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.

Example 5. The facts are the same as in *Example 4* except that A submits, with the Federal tax return, an appraisal of the 25 percent limited partnership interest in PS that satisfies the requirements of paragraph (f)(3) of this section in lieu of the information required in paragraph (f)(2)(iv) of this section. Assuming the other requirements of paragraph (f)(2) of this section are satisfied, the transfer is considered adequately disclosed and the period for assessment for the transfer under section 6501 will run from the time the return is filed (as determined under section 6501(b) of this chapter).

Example 6. A owns 100 percent of the stock of X Corporation, a company actively engaged in a manufacturing business. B, A's child, is an employee of X and receives an annual salary paid in the ordinary course of operating X Corporation. B reports the annual salary as income on B's income tax returns. In 2001, A transfers property to family members and files a Federal gift tax return reporting the transfers. However, A does not disclose the 2001 salary payments made to B. Because the salary payments were reported as income on B's income tax return, the salary payments are deemed to be adequately disclosed. The transfer of property to family members, other than the salary payments to B, reported on the gift tax return must satisfy the adequate disclosure requirements under paragraph (f)(2) of this section in order for the period of assessment under section 6501 to commence to run with respect to those transfers.

(8) *Effective date.* This paragraph (f) is applicable to gifts made after December 31, 1996, for which the gift tax return for such calendar year is filed after December 3, 1999.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 9. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 10. In §602.101, paragraph (b) is amended in the table by revising the entry for 301.6501(c)–1 to read as follows:

§602.101 OMB Control numbers.

(b) * * *

CFR part or section where identified and described	Current OMB control No.
* * * * *	
301.6501(c)–1	1545–1241 1545–1637
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Robert E. Wenzel,
Deputy Commissioner of Internal Revenue.

Approved November 18, 1999

Jonathan Talisman,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on December 2, 1999, 8:45 a.m., and published in the issue of the Federal Register for December 3, 1999, 64 F.R. 67767)