Gift Tax Treatment of Transfers in Trust

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Section 2511(c), added by the Economic Growth and Tax Relief Reconciliation Act of 2001 and amended by the Job Creation and Worker Assistance Act of 2002, has never been closely analyzed. The plain meaning of section 2511(c) is not discernible from the statute. To date, no regulations have been issued to interpret section 2511(c). Only the Joint Committee on Taxation's technical explanation of the Job Creation and Worker Assistance Act and Notice 2010-19 offer any explanation of section 2511(c), and that is not supported by evidentiary congressional intent. At best, the IRS's guidance and clarification regarding the section is double entendre and, at worst, double speak.

The rules governing complete and incomplete transfers of property to a trust are compromised by the technical explanation and Notice 2010-19. This report provides a critical analysis of why neither the technical explanation nor Notice 2010-19 should be relied on to apply the plain meaning of section 2511(c). Among the several conclusions reached is that neither the technical explanation nor Notice 2010-19 clarifies the plain meaning of section 2511(c) — each only creates more confusion. Even if section 2511(c) is repealed for transfers of property by gift to a trust after 2010, it may continue to have a lasting effect on the IRS's scrutiny of those transfers.

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I. Introduction

Much has been written about the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), yet EGTRRA's addition of section 2511(c) has evaded serious analysis. In fact, an exhaustive search of the committee reports and *Congressional Record* does not reveal the reason or sense of Congress regarding why section 2511(c) was added to the code — it simply appeared as part of S. Amdt. 650 amending H.R. 1836, introduced by then-Senate Finance Committee Chair Chuck Grassley, R-Iowa, and then-Finance Committee ranking minority member Max Baucus, D-Mont. This seemingly innocuous section 2511(c), even if repealed, may have a lasting effect on the IRS's scrutiny of a transfer of property by gift to a trust. The Job Creation and Worker Assistance Act of 2002 (JCWAA) amended section 2511(c) with what was labeled a ''technical correction,'' presumably in an effort to clarify its meaning, but as with the creation

of the provision, no reason can be found for the amendment. Eventually, the IRS issued Notice 2010-19,[1] stating that some taxpayers may have inaccurately interpreted section 2511(c) as excluding from gift tax transfers to a trust that is treated as wholly owned by the donor or his spouse under the grantor trust rules (sections 671 through 679), even though those transfers would otherwise be taxable under chapter 12.

The plain meaning of section 2511(c) is not discernable from the statute. Only the Joint Committee on Taxation's ''Technical Explanation of the Job Creation and Worker's Assistance Act of 2002''[2] and Notice 2010-19 offer any explanation and alleged clarification. The purpose of this report is to examine the technical explanation and Notice 2010-19 and make some sense of the JCT's and IRS's positions on section 2511(c) for taxpayers and tax professionals alike. Also, an initial reading of section 2511(c) might cause one to question whether a transfer of property by gift to a charitable remainder trust (CRT) constitutes a complete gift subject to federal gift tax. Lifetime gifts to qualified charitable and religious organizations or governmental entities are generally exempt from federal gift tax.[3] If a donor transfers an interest in property for charitable purposes and retains an interest in the same property for private purposes, no federal charitable gift tax deduction is allowed for the value of the interest, unless it is a charitable remainder interest in a charitable remainder annuity trust, charitable remainder unitrust, or a pooled income fund.[4] The effect of section 2511(c) might call into question whether the entire value of property transferred in trust by gift can be deemed a complete gift subject to gift tax when in fact the gift may be wholly incomplete, or partially complete and partially incomplete. But before that examination can be made, some background information is required to better understand the significance of section 2511(c), regardless of whether it is repealed.

II. Income Taxation of Grantor Trusts

Section 2511(c) involves grantor trusts. All *inter vivos* trusts created by the grantor are divided into two categories: trusts that are treated as owned by the grantor for federal income tax purposes because the grantor has retained a present interest in or control over the trust property, and trusts that are not treated as owned by the grantor because he does not have any present interest in or control over the trust property. It is this latter category that clouds the operating definition of an irrevocable grantor trust, distinguished from a revocable grantor trust. The grantor of an irrevocable grantor trust may not have control over the property as the grantor but may have control over the property as the trustee and be taxed on the trust's income as the primary income beneficiary.

Yet the grantor may be deemed the owner of a portion of the trust, whether the grantor trust is revocable or irrevocable, because the grantor has retained an interest in the income from that portion.[5] Under section 677 the grantor is treated in any tax year as the owner of a portion of a trust whose income for that year may be distributed to the grantor or his spouse (whether or not the grantor is treated as an owner under section 674),[6] even though the grantor does not have the power to control the beneficial enjoyment of the trust estate.[7] Such a trust may be a grantor retained annuity trust (GRAT), a grantor retained unitrust (GRUT), a grantor retained income trust (GRIT), a personal residence trust (PRT), a qualified personal residence trust (QPRT), or an irrevocable life insurance trust (ILIT). Except for the ILIT, these trusts may be referred to as gift tax exemption amount leveraging trusts (GTEALTs). Because the grantor of a GTEALT receives a stream of income (either a fixed amount or a fixed percentage of the fair market value of the trust corpus valued annually), he is deemed the owner of the trust for income tax reporting purposes under sections 671 and 677, even though he does not have control of the beneficial enjoyment of the trust property. Thus, under current law, the income of a trust classified as a grantor-owned trust generally is taxed directly to the grantor to the extent that he is treated as the owner of the portion of the trust that produces the income; that is, for income tax purposes, the trust is treated as a conduit of the income from the trust directly to the grantor just as if the trust does not exist.

III. Complete and Incomplete Gifts

Understanding the effect of section 2511(c) on a transfer of property by gift to a trust requires knowledge of the terms ''complete gift'' and ''incomplete gift.'' The federal gift tax applies to all

[1]Notice 2010-19, 2010-7 IRB 404, *Doc 2010-2424, 2010 TNT 22-7*.

[2]Joint Committee on Taxation, ''Technical Explanation of the Job Creation and Worker's Assistance Act of 2002,'' JCX-12-02 (Mar. 6, 2002), at 38, *Doc 2002-5684, 2002 TNT 45-15*.

[3]Section 2522(a); reg. section 25.2522(a)-1(a).

[4]Reg. section 25.2522(c)-3(c)(1) and (2)(v). *See* section 664(d)(1), (2), and (3); reg. section 1.664-2; reg. section 1.664-3; section 642(c)(5); and reg. section 1.642(c)-5.

[5]Section 677(a); reg. section 1.677(a)-1(a)(1).

[6]Section 677(a); reg. section 1.677(a)-1(b)(2)(I) and 1.677(a)-1(g), Example 1.

[7]Reg. section 1.677(a)-1(b)(1).

transfers by gift of property and interests in property, wherever situated, by individual citizens or U.S. residents, if the value of the gift exceeds the amount of exclusions in section 2503 and the deductions under section 2521 (as in effect before its repeal by the Tax Reform Act of 1976), section 2522 (charitable and similar gifts), and section 2523 (gift to spouse).[8] Subject to the limitations in chapter 12, the gift tax imposed by section 2501 applies whether the transfer is in trust or otherwise.[9]

A. Complete Gift

For a transfer of property to be a gift, the transfer must be complete. A gift of property is complete when the donor has parted with dominion and control of the transferred property in a manner that leaves him no power to change the disposition of the gifted property, whether for his own benefit or for the benefit of another.[10] For example, the grantor of a revocable living trust who had previously conveyed to the trustee the legal title to stock made a complete gift of that stock when he relinquished his power to change the trust beneficiaries and the power to revest the beneficial ownership of the trust assets attributable to beneficial certificates in himself. (This trust arrangement had the characteristics of a pure equity trust or constitutional trust.) By relinquishing the power to change the beneficiaries and the power to revest the beneficial ownership of the trust assets attributable to the beneficial certificates in himself, the donor-grantor gave up any right he had to regain ownership of the stock or to receive income from it.[11] But if the donor-grantor reserves any power over the disposition of the property, the gift may be wholly incomplete, or partially complete and partially incomplete, depending on all the facts in the case.[12]

For example, if a donor-grantor of a revocable living trust conveys to the trustee legal title to property whose income the trustee is to pay to the donor-grantor or accumulate in the discretion of the trustee, and if the donor-grantor retains a testamentary power to appoint the remainder among his descendants, no portion of the transfer is a complete gift. However, if the donor-grantor does not retain the testamentary power of appointment but instead provides that the remainder should go to a named beneficiary or to the beneficiary's descendants, the entire value of the property transferred would be a complete gift subject to gift tax. Further, the creation of a trust whose income is to be paid annually to the donee for a period of years and whose corpus is distributable to the donee at the end of the period constitutes a complete gift if the power reserved by the donor-grantor is limited to a right to require that the income instead be accumulated and distributed with the corpus to the donee at the end of the period.[13] Also, if a donor transfers property to himself as trustee and retains no beneficial interest in the trust property and no power over the property (except fiduciary powers limited by an ascertainable standard), he has made a complete gift, and the entire value of the transferred property is subject to the gift tax.[14]

B. Incomplete Gift

As mentioned above, a gift is incomplete when the donor (for example, the grantor, trustor, or settlor of a trust) reserves the power to revest the beneficial title to the property in himself.[15] However, if the exercise of the trustee's power in favor of the donor-grantor is limited by a fixed or ascertainable standard (see reg. section 25.2511-1(g)(2)), enforceable by or on behalf of the donor-grantor, the gift is incomplete to the extent of the ascertainable value of any rights retained by the donor-grantor.[16] Except for a fiduciary power limited by an ascertainable standard, a gift is also incomplete if the donor-grantor reserves the power to name new beneficiaries or to change the beneficiaries' interests.[17] That power, coupled with the previously discussed issue of dominion and control, is the principal reason transfers of property to a revocable living trust do not constitute complete gifts for gift tax purposes.[18] However, a gift is not considered

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[8]Section 2501(a)(1); reg. section 25.2501-1(a)(1).

[9]Section 2511(a); reg. section 25.2511-1(a).

[10]*See Young v. Young*, 393 S.E.2d 398 (Va. 1990); *Brown v. Metz*, 393 S.E.2d 402 (Va. 1990); *Succession of Young*, 563 So.2d 502 (La. Ct. App. 1990); reg. section 25.2511-2(b).

[11]*Estate of Vak v. Commissioner*, 973 F.2d 1409 (8th Cir. 1992), *rev'g and remanding* T.C. Memo. 1991-503.

[12]Reg. section 25.2511-2(b); *see also* TAM 8901004, *89 TNT 7-23* (instruments conveying legal title to property conveyed to trustee in 1985 and held by grantor's agent until recorded in 1986 were completed taxable gifts in 1986); *Estate of Novetzke v. Commissioner*, T.C. Memo. 1988-268; *Estate of Cummins v. Commissioner*, T.C. Memo. 1993-518; Doug H. Moy, *A Practitioner's Guide to Estate Planning: Guidance and Planning Strategies*, section 3.01[D][1], at 3-27 (2002).

[13]Reg. section 25.2511-2(d).

[14]Reg. section 25.2511-2(g).

[15]Section 676(a); reg. section 25.2511-2(c).

[16]Reg. section 25.2511-2(b).

[17]Section 674(a); reg. section 25.2511-2(c).

[18]*Smith v. Shaughnessy*, 318 U.S. 176 (1943); reg. section 25.2511-2(a), (b), and (c); LTR 8940008, *89 TNT 206-95*. *Cf.* LTR 9230021, *92 TNT 153-32* (Trustor proposed to convey to a living trust partnership interests that were subject to liabilities that exceeded his adjusted basis in the partnership interests. The IRS ruled that the transfer of the partnership interests was not taxable to the trustor under the rationale of Rev. Rul. 85-13, 1985-1 C.B. 184, and that the adjusted basis and holding period of the property transferred to the trust is the same in the hands of the trustee as it was in the hands of the trustor before the transfer. The trustor was treated as the owner of the entire living

(Footnote continued on next page.)

incomplete merely because the donor-grantor reserves the power to change the manner or time of enjoyment of the property gifted.

If the donor-grantor directs the trustee to transfer back to him property that comprises the trust estate of a revocable living trust in the same form of ownership in which it was titled before its conveyance to the trustee, no federal gift taxable event occurs. This is because a gift is incomplete any time the donor-grantor reserves the power to revest the beneficial title to property in himself or when the donor-grantor's reserved power allows him to name new beneficiaries.[19] However, if the trustee transfers property from a revocable living trust to a beneficiary other than the donor-grantor, that transfer constitutes a complete gift subject to federal gift tax.[20]

IV. Enactment of Section 2511(c)

A. Section 511(e) of EGTRRA

Under section 2511(c), as added by EGTRRA, a transfer of property by gift in trust would have been treated as a taxable gift under section 2503, unless the trust was treated as wholly owned by the donor or his spouse under the grantor trust rules:

> Notwithstanding any other provision of this section and except as provided in regulations, a transfer in trust shall be treated as a taxable gift under section 2503, unless the trust is treated as wholly owned by the donor or the donor's spouse under sub-part E of part I of subchapter J of chapter 1.

In effect, this meant that a transfer of property to any grantor trust, other than a trust wholly owned by the donor-grantor or his spouse under the grantor trust rules, would be a taxable gift.

The phrase "taxable gift under section 2503," together with the language "unless the trust is treated as wholly owned by the donor or the donor's spouse," rightfully may have caused donors and tax professionals to believe that the value of property transferred to a CRT in excess of the donor's $1 million lifetime federal gift tax exemption would be subject to federal gift tax, thereby reducing or entirely eliminating the $1 million lifetime exemption amount to offset gift tax on other non-charitable gifts.

B. Section 411(g) of the JCWAA

Whatever the reason, a technical correction was made to section 2511(c) by section 411(g) of the JCWAA. It now provides that a transfer of property in trust is treated as a "transfer of property by gift,"[21] unless the trust is treated as wholly owned by the donor or his spouse under the grantor trust rules. Thus, the language "transfer of property by gift" was substituted for "taxable gift under section 2503."

V. Technical Explanation of Section 2511(c)

A detailed analysis of the JCT's technical explanation of section 2511(c) is warranted. Describing the technical correction to section 2511(c) under section 411(g) of the JCWAA, it reads:

> **Transfers in trust**. — The provision clarifies that the effect of section 511(e) of the Act [EGTRRA] (effective for gifts made after 2009) is to treat certain transfers in trust as transfers of property by gift. The result of the clarification is that the gift tax annual exclusion and the marital and charitable deductions may apply to such transfers. Under the provision as clarified, certain amounts transferred in trust will be treated as transfers of property by gift, despite the fact that such transfers would be regarded as incomplete gifts or would not be treated as transferred under the law applicable to gifts made prior to 2010. For example, if in 2010 an individual transfers property in trust to pay the income to one person for life, remainder to such persons and in such portions as the settlor may decide, then, the entire value of the property will be treated as being transferred by gift under the provision, even though the transfer of the remainder interest in the trust would not be treated as a completed

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trust under section 674(a). Therefore, under Rev. Rul. 85-13, he was considered the owner of all the living trust property for federal income tax purposes. Because the trustor was treated for federal income tax purposes as the owner of the partnership interests both before and after placing them in the living trust, the IRS concluded that no transfer of property occurred for purposes of section 1041(a). Therefore, that section was inapplicable. Moreover, because no transfer of property occurred, section 1041(e), which applies only when there is a transfer of property in trust, also did not apply. *See* JCT, "Explanation of Technical Corrections to the Tax Reform Act of 1984 and Other Recent Legislation" 119 (1987), which states: "These rules [section 1041(e)] are not intended to apply where any gain will be taxed to the transferor under the grantor trust rules." Because the trustor was treated as the owner of the partnership interests both before and after their transfer to the living trust, his adjusted basis in and the holding period of the partnership interests remained the same. *See also* Rev. Rul. 54-537, 1954-2 C.B. 316 and Rev. Rul. 54-538, 1954-2 C.B. 316.

[19]Reg. section 25.2511-2(c). *See also* TAM 9127008, *91 TNT 143-5*. A compromise agreement rescinding the termination of a trust after it had terminated according to its own terms during the trustor's lifetime was not effective for gift tax purposes to rescind the completed gift arising from the distribution of the trust's assets at the time of the trust's termination. A completed gift was effected when the trust terminated by its own terms.

[20]Reg. section 25.2511-2(b) and (f).

[21]Section 411(g)(1) of the JCWAA, amending section 2511(c).

gift under current Treas. Reg. Sec. 25.2511-2(c). Similarly, if in 2010 an individual transfers property in trust to pay the income to one person for life, and makes no transfer of a remainder interest, the entire value of the property will be treated as being transferred by gift under the provision.

A. 'Entire Value of the Property'

The phrase ''certain amounts'' in the technical explanation suggests that only a specific portion of the value of property transferred to a trust may be deemed wholly incomplete, or partially complete and partially incomplete. Yet, section 2511(c) clearly states:

> Notwithstanding any other provision of this section and except as provided in regulations, a *transfer in trust shall be treated as a transfer of property by gift*, unless the trust is treated as wholly owned by the donor or the donor's spouse under subpart E of part I of subchapter J of chapter 1. [Emphasis added.]

The first example in the technical explanation does not square with section 2511(c) in concluding that the donor will have made a complete gift of the *entire value of the property*, which will be treated as being transferred by gift under section 2511(c), even though the transfer of the remainder interest would not be treated as a completed gift under reg. section 25.2511-2(c). The second example describes a complete gift as it should be, regardless of section 2511(c).[22] By stating that ''under the provision as clarified, certain amounts transferred in trust will be treated as transfers of property by gift,'' the technical explanation unnecessarily implies that all transfers of property in trust will be subject to gift tax, when that is not always the case. Further, inclusion of the language ''despite the fact that such transfers would be regarded as incomplete gifts or would not be treated as transferred under the law applicable to gifts made prior to 2010'' only contributes to the confusion. In other words, the real meaning of the language is that all transfers of property in trust will be treated as transfers of property by gift, regardless of whether those gifts are complete or incomplete — not that all those transfers will be subject to gift tax. The additional language is unnecessary, since only a complete gift can be subject to gift tax, and whether the gift tax applies to a particular transfer is a factual determination.

B. 'Gift'

The confusion is furthered by the word ''gift.'' In general, when the word ''gift'' is used in any section of chapter 12, it connotes a taxable gift, inasmuch as chapter 12 is about gift tax. However, the gift tax applies only if the gift is complete. If the gift is incomplete, it does not apply. So although a transfer in trust is treated as a transfer of property by gift, that alone does not make the gift a taxable gift.

However, according to the first example in the technical explanation, if in 2010 (and perhaps beyond) a donor-grantor transfers property in trust to pay the income to one person for life with the remainder to persons in portions decided by the donor-grantor, the entire value of the property is treated as being transferred by gift, even though the transfer of the remainder interest in the trust would not be treated as a complete gift under reg. section 25.2511-2(c).[23] The language in the example is troubling because it is not included in section 2511(c). The second example in the technical explanation — that if in 2010 an individual transfers property in trust to pay the income to one person for life and makes no transfer of a remainder interest, the entire value of the property is treated as being transferred by gift subject to federal gift tax — makes sense, because that gift would have been a taxable gift if made before the enactment of section 2511(c).[24]

In the first example, the donor did not give up all dominion and control of the property transferred (that is, gifted) to the trust; the donor retained dominion and control of the remainder interest. Under reg. section 25.2511-2(c), a complete gift of the remainder interest would not have been effected; only the income interest would have been a complete gift. However, in the second example, the donor did give up all dominion and control of the property transferred (that is, gifted) to the trust. Thus, under section 2511(c), the entire value of the property transferred to the trust (the value of both the income interest and the remainder interest) is a complete gift subject to gift tax. That example supports the technical explanation that under the provision as clarified, the entire value of the property transferred in trust is treated as a transfer of property by gift, even though the transfer would have been regarded as an incomplete gift or would not be treated as transferred under the law applicable to gifts made before 2010.[25]

The technical explanation of section 2511(c) by way of the first example contradicts reg. section 25.2511-2(b) and case law decided before 2010, in

[22]JCT, *supra* note 2, at 38.

[23]*Id.*

[24]*See* reg. section 25.2511-2(g).

[25]JCT, *supra* note 2, at 38.

that the donor gave up dominion and control only of the income interest of the property transferred by gift to the trust — not dominion and control of the remainder interest. The first example illustrates a partially complete gift (the income interest) and partially incomplete gift (the remainder interest). On one hand, since the first example is found only in the technical explanation and is not part of section 2511(c), the IRS may be inclined not to follow the example.[26] On the other hand, if section 2511(c) is repealed, the IRS may choose to hang its hat on the first example. It is disturbing that the technical explanation might have the effect of legislating the taxation of an incomplete gift (the value of the remainder interest in the first example) as a complete gift when the donor in the first example did not effect a complete gift of the remainder interest in the property and would include the entire value of the property transferred to a trust as a complete gift. That result subjects the value of the remainder interest to gift tax when a complete gift of it has not legally been effected.

This would mean that the entire value of property transferred to a trust not wholly owned by the donor-grantor or his spouse under the grantor trust rules would be deemed a gift subject to gift tax, even if it is partially an incomplete gift. In this sense, the substitution of ''transfer of property by gift'' for ''taxable gift under section 2503'' in section 2511(c) has not changed the true effect of the provision. That is, the entire value of a transfer of property in trust not wholly owned by the donor-grantor or his spouse, whether or not the transfer is partially complete and partially incomplete, is a taxable gift under section 2511(c) as it was initially intended to operate under EGTRRA. In other words, the entire value of all property transferred to a trust not wholly owned by the donor-grantor or his spouse under the grantor trust rules is a complete gift subject to gift tax.

C. 'Certain Amounts Transferred in Trust'

It is troubling that the technical explanation states that ''certain amounts transferred in trust will be treated as transfers of property by gift, despite the fact that such transfers would be regarded as incomplete gifts or would not be treated as transferred under the law applicable to gifts made prior to 2010.'' The law applicable to gifts made before 2010 took into account gifts that were wholly incomplete or partially complete and partially incomplete, depending on all the facts in the particular case.[27] Again, although this language is not part of section 2511(c), the intent of section 2511(c) seems to be to treat all transfers of property to a trust not wholly owned by the donor-grantor or his spouse as complete gifts subject to gift tax as provided in sections 2501 and 2511(a). Note that the entire value of property transferred to a GTEALT is subject to gift tax, but only the actuarially determined value of the remainder interest bears the imposition of the gift tax. That is because the grantor retains the actuarially determined value of the income interest (for example, the annuity or unitrust amount), which terminates either on the grantor's death before the termination of the trust or after the term period of the trust ends,[28] thereby causing the value of the income interest not capable of transfer.[29]

D. Observations

1. Section 2511(c) reiterates section 2511(a). In both section 511(e) of EGTRRA and section 411(g) of the JCWAA, the language of section 2511(c) ''notwithstanding any other provision of section 2511'' is redundant, since section 2511(a) already provides that the gift tax imposed by section 2501 applies whether the property transferred by gift is in trust or otherwise (but interestingly, section 2511(a) does not mention whether the gift tax applies to the incomplete gift portion of the property transferred in trust). In other words, it was unnecessary to further confuse the issue with the ''notwithstanding'' language. Complete transfers of property in trust before section 2511(c) were already subject to federal gift tax. But now the so-called clarification proffered in the technical explanation, although not part of section 2511(c), supports the IRS's position in Notice 2010-19 that each transfer made in 2010 to a trust that is not treated as wholly owned by the donor or his spouse under the grantor trust rules is considered a transfer by gift of the entire interest in the property under section 2511(c)[30] — a complete gift, even if the gift is partially complete and partially incomplete. Yet, immediately following that statement, the notice provides that ''the provisions of Chapter 12 as in effect on December 31, 2009, continue to apply (both before and during 2010) to all transfers made to any other trust to determine whether the transfer is subject to gift

[26]*See* Sheldon I. Banoff, ''Dealing With the 'Authorities': Determining Valid Legal Authority in Advising Clients, Rendering Opinions, Preparing Tax Returns and Avoiding Penalties,'' in 3 *Financial and Estate Planning*, para. 26,851, at 24,336, item no. 3; LTR 8544014; Burton W. Kanter and Sheldon I. Banoff, ''Can IRS Disregard Committee Reports?'' 64 *J. Tax'n* 382 (1986).

[27]Reg. section 25.2511-2(b).

[28]Section 2702(a)(2).

[29]Both the federal gift and estate taxes are excise taxes imposed on the value of property transferred by the donor or decedent, respectively — not on any particular kind of property.

[30]Notice 2010-19.

tax.''[31] Does that seemingly contradictory statement mean that all transfers made to any other trust will be treated as wholly incomplete, or partially complete and partially incomplete, depending on all the facts in the particular case?[32] So much for clarification by both the JCT's technical explanation and the IRS's Notice 2010-19!

2. Query. If ''the result of the clarification is that the gift tax annual exclusion and the marital and charitable deductions may apply to such transfers,''[33] and since the IRS has said that ''the provisions of Chapter 12 as in effect on December 31, 2009, continue to apply (both before and during 2010) to all transfers made to any other trust to determine whether the transfer is subject to gift tax,''[34] why the need for section 2511(c) in the first place? Section 2511(a) and reg. section 25.2511-2(b) already address the gift taxation of transfers of property in trust, in effect, not wholly owned by the grantor or his spouse under the grantor trust rules.

3. Reg. section 25.2511-2. The facts in both examples in the technical explanation had in effect already been addressed in reg. section 25.2511-2; it was unnecessary to reiterate them. Moreover, the technical explanation offered no clarification or cogent reasoning for why the situation in the first example would now, under section 2511(c), be treated as a complete gift of the entire value of the property transferred in trust, when under current reg. section 25.2511-2(c), the same facts would be treated as a partially complete and partially incomplete gift.

4. Second example in technical explanation. The second example in the technical explanation makes sense, because if the donor gave up all dominion and control of the property, a complete gift was made. Nothing has changed in this regard. The code and Treasury regulations already adequately addressed this issue years ago. Why, then, the need to add subsection (c) to section 2511?

E. 'Wholly Owned'

The term ''wholly owned'' is new to chapter 12 of the code. In fact, the term appears only once in chapter 12; namely, in section 2511(c) but not in the regulations related to chapter 12. Further, ''wholly owned'' is used throughout revenue rulings and case law unrelated to the gift tax, but the term is undefined; that is, it is not described as having any particular limitations.

What does it mean that ''unless the trust is treated as wholly owned by the donor or the donor's spouse under'' the grantor trust rules? Neither the code nor Treasury regulations define the term ''wholly owned'' for federal gift tax purposes or as it relates to the grantor trust rules. The grantor trust rules govern whether the grantor of a trust or another person is to be treated as the owner of any portion of a trust for income tax reporting purposes. Since grantor trusts are the subject of section 2511(c), the relevant provisions of sections 671, 673, 674, 676, and 677 must be considered in understanding the term ''wholly owned.''

Recall that a grantor trust is a trust in which the grantor retains control over the trust property or its income to such an extent that he is taxed on the income of the trust. Interestingly, the grantor can be treated as the owner of a trust for both income tax and estate tax purposes yet not be the owner for federal estate tax purposes.[35] An example is the revocable living trust.[36]

1. Section 671. Section 671 provides:

> Where it is specified in this subpart [subpart E of part I of subchapter J of chapter 1] that the grantor or another person shall be treated as the owner of any portion of a trust, there shall then be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust which are attributable to that portion of the trust to the extent that such items would be taken into account under this chapter in computing taxable income or credits against the tax of an individual.

Thus, the grantor trust rules govern whether the grantor is treated as owner of the trust property and whether the trust or the grantor is recognized as the taxpayer for income tax reporting purposes. The grantor trust rules establish that trusts are ignored for income tax purposes and that the grantor is treated as the appropriate taxpayer whenever the grantor retains substantially unfettered powers of disposition.[37] For federal income tax purposes, an item of income, deduction, or credit included in computing the taxable income and credits of a trust's grantor under section 671 is therefore treated

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[31] *Id.*

[32] Reg. section 25.2511-2(b).

[33] JCT, *supra* note 2, at 38.

[34] Notice 2010-19.

[35] An example would be GTEALTs, all of which are subject to the provisions of section 2702 and the regulations promulgated thereunder.

[36] *Black's Law Dictionary*, 1549 (8th ed. 2004).

[37] *United States v. Smith*, 657 F. Supp. 646 (W.D. La. 1986); *United States v. Buttorf*, 761 F.2d 1056, 1061 (5th Cir. 1985); *Schultz v. Commissioner*, 686 F.2d 490, 495 (7th Cir. 1982); *Vnuk v. Commissioner*, 621 F.2d 1318 (8th Cir. 1980); Doug H. Moy, ''Revocable Living Trusts: Availability of One-Time Exclusion of Gain From Sale of Principal Residence in the Event Trustor Becomes Incompetent,'' 15 *Tax Mgmt. Est., Gifts & Trusts J.* 62, 65 (1990).

as if it had been received or paid directly by the grantor.[38] The reason for attributing items of income, deduction, and credit to the grantor under section 671 is that by exercising dominion and control over a trust (either by retaining a power over an interest in the trust or by dealing with the trust property for the grantor's benefit), the grantor has treated the trust property as if it were his own.[39]

Unfortunately, neither the code nor the regulations define owner. Generally, the word must be interpreted in context.[40] When used in a legal sense, ''owner'' means legal owner; however, it may also include any person with a beneficial interest in property.[41] Also, ownership may be an equitable interest in property.[42] In a trust, the beneficiary has an equitable interest, and the trustee holds a legal interest in the trust property.[43] Of course, the grantor of a revocable trust, as primary *inter vivos* beneficiary of the trust, possesses an equitable ownership interest in the property transferred to the trust. Thus, for purposes of sections 671 through 677, the grantor's ownership of trust assets is an equitable interest — not a legal interest.

Section 671 does not provide that in order for the grantor rather than the trust to be the taxpayer, the grantor must be both trustor and trustee. Nor does it provide that the trustor must have a legal (or fee simple) ownership interest in the trust estate.[44] In fact, sections 674 through 677 provide that the grantor will be treated as the owner of any portion of a trust for which the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.[45] Therefore, the grantor's treatment as ''owner'' under sections 671 through 677 means that he holds an equitable ownership interest in the assets composing the trust estate.[46]

2. Section 673. Section 671 is the cornerstone of the grantor trust rules, which are more specifically defined in sections 672 through 677. Also, in defining adverse party, section 672(a) says that a person having a general power of appointment over the trust property will be deemed to have a beneficial interest in the property. Section 673(a) provides:

> The grantor shall be treated as the owner of any portion of a trust in which he has a reversionary interest in either the corpus or the income therefrom, if, as of the inception of that portion of the trust, the value of such interest exceeds 5 percent of the value of such portion.

3. Section 674. Under the provisions of 674(a):

> The grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

This is true whether the power is a fiduciary power, a power of appointment, or any other power.[47]

4. Section 675. Similarly, under section 675(1), the grantor is considered the owner of the trust if he has:

> A power exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party [which] enables the grantor or any person to purchase, exchange, or otherwise deal with or dispose of the corpus or the income therefrom for less than an adequate consideration in money or money's worth.

5. Section 676. Further, under section 676(a):

> The grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under any other provision of this part [subpart E of part I of subchapter J], *where at any time the power to revest* in the grantor title to such portion *is exercisable by the grantor or a non-adverse party, or both*. [Emphasis added.]

6. Section 677. Finally, under section 677(a):

> The grantor shall be treated as the owner of a trust, whether or not he is treated as such

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[38]Reg. section 1.671-2(c); Rev. Rul. 66-159, 1966-1 C.B. 163; Moy, *supra* note 37, at 65.

[39]Rev. Rul. 85-13, 1985-1 C.B. 184, 185; reg. section 1.671-2(b); Moy, *supra* note 37, at 65.

[40]*Warren v. Borawski*, 37 A.2d 364, 365, 366 (1944); *General Realty Impt. Co. v. City of New Haven*, 50 A.2d 59, 61 (1946); Moy, *supra* note 37, at 66.

[41]*Siemer v. Schuermann Bldg. & Realty Co.*, 381 S.W.2d 821, 826 (Mo. 1964); Moy, *supra* note 37, at 66.

[42]*In re Freeman's Heirs at Law*, 128 S.E. 404, 408 (1925); Moy, *supra* note 37, at 66.

[43]American Law Institute, *Restatement (Second) of Trusts*, section 2(f) (1959); Moy, *supra* note 37, at 66.

[44]The conveyance of legal title in property to a trustee of a grantor trust does not create fee simple title in the property transferred to the trustee; rather, that title is a base fee title. Accordingly, in jurisdictions that impose a transfer fee when legal title in real property is conveyed to the trustee of a revocable trust, one can argue that a transfer fee cannot be legally imposed, since fee simple title has not been transferred.

[45]Sections 674(a), 675(1), 676(a), and 677(a); Moy, *supra* note 37, at 66.

[46]Moy, *supra* note 37, at 66.

[47]Reg. section 1.674(a)-1(a); Moy, *supra* note 37, at 67.

> owner under section 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a nonadverse party, or both, may be (1) distributed to the grantor or the grantor's spouse; (2) held or accumulated for future distribution to the grantor or the grantor's spouse.

F. 'Wholly Owned' — Term of First Impression

For purposes of section 2511(c), a grantor trust may appear to satisfy the grantor trust rules, thereby creating a first impression that the trust is wholly owned by the grantor or his spouse. However, Congress may have been thinking that what the grantor believes is a grantor trust wholly owned by him and his spouse is in fact not such a trust when other provisions of the trust demonstrate that it is not wholly owned by the grantor or his spouse.[48] Of course, the term "wholly owned" raises the question: To what extent must the trust be wholly owned by the donor or the donor's spouse? One definition of wholly is "not partially," "fully," or "completely."[49] Another definition of wholly is "to the full or entire extent" or "completely."[50]

1. Extent of 'wholly owned.' If a trust is treated as wholly owned by a donor-grantor under the grantor trust rules, must the trust satisfy all of those rules or any one of the rules as long as the trust is not regarded as a nongrantor trust? Does the definition of wholly mean that the trust must include all provisions of sections 673 through 677 for it to be deemed wholly owned by the donor-grantor or his spouse under section 2511(c)? Doesn't the word "donor" in section 2511(c) mean "grantor"? It's interesting to note that a person can be the owner of a trust but not be the grantor, and the language of section 2511(c) does not include the word "grantor," yet section 2511(c) invokes the grantor trust rules. The word "donor" can mean "settlor"; "settlor" and "grantor" are synonymous, and the word "grantor" can mean "donor."[51] Therefore, "donor" means "grantor." Thus, because section 2511(a) provides that gifts made *inter vivos* in trust are subject to gift tax imposed by section 2501, the purpose of section 2511(c) must be to clarify that only gifts made, in effect, to a grantor trust treated as wholly owned by the donor or his spouse under the grantor trust rules are not subject to gift tax.[52]

2. Observation. A person can be the owner of an *inter vivos* trust but not be the grantor.[53] Thus, the trust would not be wholly owned by the donor or his spouse, since donor means grantor. Accordingly, wouldn't the transfer of property to that trust constitute a transfer by gift subject to federal gift tax? The issue really has to do with someone other than the donor or his spouse being owner of the trust. Wouldn't the donor-grantor's transfer of property by gift to the trust for the benefit of the beneficiary who is not the donor-grantor or his spouse be considered a transfer of property by gift to a trust not wholly owned by the donor-grantor or his spouse, thereby subjecting to gift tax the entire value of the property transferred to the trust? Further, is it correct to say that a trust is not a grantor trust if someone other than the donor-grantor or his spouse is the owner of the trust under the grantor trust rules? In my opinion, the answer to both questions is yes.

3. Rev. Rul. 66-159. Is it reasonable to assume then that the term "wholly owned," as applied in the context of section 2511(c), does not mean that a grantor trust would be required to evidence all the provisions of sections 673, 674, 676, and 677 in order for a transfer of property in trust to be an incomplete gift not subject to gift tax and to be treated as wholly owned by the donor-grantor or his spouse? Rev. Rul. 66-159[54] seems to support this notion, in that:

> The conditions under which a grantor is regarded as owner of a *portion of a trust* are set forth in sections 673 through 677, inclusive, of the Code.
>
> Under the general rule provided in section 676(a) of the Code, the grantor is treated as the owner of *any portion of a trust* where at any time the power to revest in the grantor title to such portion is exercisable by the grantor or a non-adverse party, or both.

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[48] *Cf. Estate of Hurd v. Commissioner*, 160 F.2d 610 (1st Cir. 1947) (Decedent transferred property to a revocable *inter vivos* trust, naming himself and his wife as trustees, and the trust provided that the donor reserved "no right to revoke, modify or change any of the provisions of the instrument or to repossess himself of the Trust Property under any circumstances whatsoever." Nevertheless, the court found that, under other provisions of the trust, the grantor did in fact retain powers amounting to his ability to alter, amend, or revoke the trust); Moy, *supra* note 37, at 68.

[49] *Black's Law Dictionary* 1628.

[50] *Merriam-Webster's Collegiate Dictionary* 1346 (10th ed. 2001).

[51] *Black's Law Dictionary* 526, 720.

[52] *See* Rev. Rul. 81-6, 1981-1 C.B. 385 ("Section 678(a) of the Code provides that a person other than the grantor shall be treated as the owner of any portion of a trust with respect to which such person has a power exercisable solely by himself to vest the corpus or the income therefrom in himself. Section 678(b) provides that section 678(a) shall not apply if the grantor of the trust or a transferor (to whom section 679 applies) is otherwise treated as the owner under the provisions of subpart E of Part I of subchapter J, other than section 678.").

[53] *See* Rev. Rul. 81-6, 1981-1 C.B. 385.

[54] Rev. Rul. 66-159, 1966-1 C.B. 162.

> In this case [as discussed in the revenue ruling] the grantor is treated as the owner of the entire trust under section 676(a) of the Code, inasmuch as the trustee (a nonadverse party) holds a power whereby it may, in its sole discretion, pay to or apply to the use of the grantor all of the principal of the trust. [Emphasis added.]

4. Rev. Rul. 85-45. Once again, section 2511(c) provides that ''a transfer in trust shall be treated as a transfer of property by gift, unless the trust is treated as wholly owned by the donor or the donor's spouse'' under the grantor trust rules. In Rev. Rul. 85-45,[55] the IRS pointed out that:

> Section 678(a)(1) of the Code provides that a *person other than the grantor* shall be treated as the *owner of any portion of a trust* over which the person has the sole power to vest the trust corpus or income in that person.
>
> Section 671 of the Code provides that if a *grantor* or *other person* is treated as the owner of *any portion* of a trust, then those items of income, deductions, and credits against tax of the trust that are attributable to that *portion* of the trust must be included in computing the taxable income and credits of the grantor or other person [that is, the ''owner'' of the trust who is not the grantor of the trust]. [Emphasis added.]

Further, when a husband created an irrevocable *inter vivos* trust with him and his wife as co-trustees, all trust income currently distributed to their child and, at the child's death, corpus distributable to the husband and wife's grandchild, the trust was deemed a grantor trust and the husband was considered the owner of the entire trust if he expressly retained specific powers of the kind described in the grantor trust rules. The result would be the same if the trust were treated as a grantor trust by reason of powers exercisable by a party other than the grantor and ceased to be a grantor trust on the release or renunciation of those powers by that other party or on the expiration or lapse of those powers.[56]

In Rev. Rul. 85-45, the decedent husband's will provided for the establishment of a marital deduction trust for the benefit of his surviving wife. Under the terms of the trust, the wife was entitled to receive all trust income for life and any trust corpus she requested from the trustee. The trust also gave her the sole and unrestricted power to vest the entire trust corpus or trust income in any person, including herself. The IRS concluded that under section 678, the decedent's surviving wife is treated as the owner of the entire trust for federal income tax purposes and that she must, under section 671, include items of income, deductions, and credits attributable to the trust in computing her taxable income and credits. Granted, the trust involved was a testamentary trust, not a revocable *inter vivos* trust; yet the surviving spouse was treated as the owner of the entire trust under section 678 because she had the power to vest the trust corpus or income therefrom in any person, including herself. Although unmentioned, it must be assumed that the marital deduction trust was a general power of appointment marital deduction trust governed by section 2056(b)(5).

5. Observation. Quite possibly, the term ''wholly owned'' might be interpreted to mean ''exclusively.'' That is, the grantor trust is to be owned only by the donor or his spouse to the exclusion of all others.

VI. Notice 2010-19

A. Need for Additional Clarification

Eight years elapsed before the IRS issued Notice 2010-19.[57] That the Service believed there was a need to provide additional clarification further demonstrates that it must have recognized taxpayers' and tax professionals' continuing confusion about the meaning of section 2511(c) despite the JCT's technical explanation of section 411(g) of the JCWAA. It's fair to say that the IRS's guidance in Notice 2010-19 is at cross-purposes with itself. On one hand, the notice says:

> Section 2511(a) generally provides that the gift tax shall apply to transfers in trust or otherwise, whether direct or indirect. Under section 25.2511-2(b) of the Gift Tax Regulations, a gift is complete when the donor parts with sufficient dominion and control as to leave in the donor no power to change its disposition. Section 2511(c) provides that, notwithstanding any other provision of section 2511 and except as provided in regulations, a transfer in trust shall be treated as a transfer of property by gift unless the trust is treated as wholly owned by the donor or the donor's spouse under subpart E of part I of subchapter J of chapter 1. The Joint Committee on Taxation's explanation of section 2511(c) provides that certain transfers in trust are treated as transfers of property by gift even though such transfers would have been regarded as incomplete gifts, or would

[55]Rev. Rul. 85-45, 1985-1 C.B. 183.
[56]Rev. Rul. 77-402, 1977-2 C.B. 222.
[57]Notice 2010-19.

not have been treated as transfers under the gift tax provisions in effect prior to 2010.[58]

Both the JCT and the IRS interpret section 2511(c) to mean that the Service can impose gift tax on incomplete gifts of property transferred in trust, unless the trust is a grantor trust wholly owned by the donor-grantor or his spouse under the grantor trust rules.

B. Alleged Inaccurate Interpretation

The notice also says:

> Some taxpayers may have inaccurately interpreted section 2511(c) as excluding from the gift tax transfers to a trust treated as wholly owned by the donor or the donor's spouse under subpart E of part I of subchapter J of chapter 1, even though those transfers would otherwise be taxable under Chapter 12.

This is an incredible assertion in view of the language of section 2511(c), which specifically provides that "a transfer in trust shall be treated as a transfer of property by gift, unless the trust is treated as wholly owned by the donor or the donor's spouse under subpart E of part I of subchapter J of chapter 1." This assertion contradicts section 2511(c) and the technical explanation quoted in Notice 2010-19, above:

> The provisions of Chapter 12 regarding the substantive law applicable to the gift tax were not amended by EGTRRA, and those provisions continue to apply to all transfers made by donors during 2010. Section 2511(c) is an addition to those substantive law provisions and is applicable to transfers made in 2010.

By what authority and reasoning can the IRS assert that section 2511(c) is "an addition to those substantive law provisions" in effect before its enactment? The IRS has taken it on itself to decree that section 2511(c) means that the entire value of property transferred to a trust not wholly owned by the donor-grantor or his spouse under the grantor trust rules is a complete gift, even though the gift may in fact be wholly incomplete, or partially complete and partially incomplete, depending on all the facts in the case:

> Section 2511(c) broadens the types of transfers *subject to the transfer tax* under Chapter 12 *to include certain transfers to trusts that, before 2010, would have been considered incomplete and, thus, not subject to the gift tax*. [Emphasis added.]

Again, by what authority and reasoning can the IRS assert that section 2511(c) substantiates an unsubstantiated and absurd assertion?:

> Accordingly, each transfer made in 2010 to a trust that is not treated as wholly owned by the donor or the donor's spouse under subpart E of part I of subchapter J of chapter 1 is considered to be a transfer by gift of the entire interest in the property under section 2511(c). The provisions of Chapter 12 as in effect on December 31, 2009, continue to apply (both before and during 2010) to all transfers made to any other trust to determine whether the transfer is subject to gift tax.

This language in the notice contradicts itself. On the one hand, it establishes that the provisions of chapter 12, including the regulations promulgated thereunder before 2010 (reg. section 25.2511-2(b) among them), remain in effect, despite section 2511(c). On the other hand, this language contradicts the IRS's assertion that "section 2511(c) broadens the types of transfers subject to the transfer tax *under Chapter 12* to include certain transfers to trusts that, before 2010, would have been considered incomplete and, thus, not subject to the gift tax" (emphasis added). It is no wonder that some taxpayers may have allegedly inaccurately interpreted section 2511(c) as excluding from the gift tax transfers to a trust treated as wholly owned by the donor or his spouse under the grantor trust rules, even though those transfers would otherwise be taxable under chapter 12. If taxpayers are confused, it is because the IRS is confused in its interpretation of section 2511(c).

Since there is apparently no public record explaining why section 2511(c) was needed, is it reasonable to assume that it was prompted by the allegedly inaccurate interpretation by taxpayers and tax professionals alike that a transfer of property to a grantor GTEALT was not subject to gift tax, thus eliminating the need to file a gift tax return (Form 709)? Admittedly, GTEALTs are grantor trusts, inasmuch as the income of the trusts is distributed to the grantor or his spouse.[59] However, as mentioned above, these trusts are irrevocable, thereby causing the transfer of property to be a complete gift, which is therefore subject to gift tax and requires the filing of a gift tax return.

C. Queries

1. Types of gifts broadened. How does section 2511(c) broaden the types of transfers subject to the gift tax to include some transfers of property to trusts that before 2010 would have been considered

[58]JCT, *supra* note 2, at 38 (as cited in Notice 2010-19).

[59]Section 677(a)(1).

incomplete and thus not subject to the gift tax? Reg. section 25.2511-2 provides explanations of complete and incomplete gifts. Under current chapter 12 regulations, how can any transfer of property in trust that would have been considered a partially complete gift and partially incomplete gift if made before 2010 be considered a complete gift subject to gift tax if made in 2010? The IRS has offered no explanation or evidence to support its interpretation of section 2511(c). Does the IRS intend to expand the meaning of what constitutes a complete gift versus an incomplete gift? Such an effort would be interesting — if it occurs. Undoubtedly, the IRS will want to clear up any misunderstanding and misinterpretation of this entire matter.

2. Income payable to grantor. Section 677(a) provides that the grantor will be treated as the owner of a trust whose income may be distributed to the grantor or his spouse. Might taxpayers and tax professionals have ''inaccurately interpreted section 2511(c) as excluding from the gift tax'' transfers to a GRAT, GRUT, GRIT, PRT, or QPRT because they incorrectly believed those trusts to be wholly owned by the grantor, since they are grantor trusts under section 677(a)? Admittedly, those trusts are grantor trusts for income tax reporting purposes by the grantor. However, they are irrevocable grantor trusts wherein the donor-grantor absolutely and irrevocably divests himself of the title, dominion, and control of the property transferred to the trust as to leave himself no power to change its disposition, whether for his own benefit or for the benefit of another, thereby creating a complete gift, the actuarially determined remainder value of which is subject to gift tax.[60]

D. Section 2511(a) Redundancy

Even if the above misinterpretation was really that — and not just a perceived error — why the redundancy when section 2511(a) already provides that the tax imposed by section 2501 applies to a transfer of property in trust? The general rule regarding gift taxable transfers is that a tax, computed as provided in section 2502, is imposed for each calendar year on the transfer of property by gift during that calendar year by any individual resident or nonresident.[61] The term ''taxable gifts'' means the total amount of gifts made during the calendar year, less the deductions provided in sections 2522 and 2523.[62] The gift tax imposed by section 2501 applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.[63] Since the federal gift tax already applied to a transfer of property in trust when section 2511(c) was initially drafted and continued to apply even after it was enacted, why was section 2511(c) titled ''Certain treatment of transfers in trust''? If the transfer of property to a trust is a complete gift, it is subject to federal gift tax; if it is an incomplete gift, it is not subject to federal gift tax — it's just that simple.

E. Reiteration of Decades-Old Law

What is the IRS talking about? It has done nothing more than reiterate the law as it has existed for decades. Reg. section 25.2511-1 provides full explanations of what constitutes complete gifts and incomplete gifts of a transfer of property to a trust. Perhaps the unstated intended purpose of section 2511(c) is to subject to gift tax some transfers of property in trust that were previously considered incomplete gifts but have proven in case law since the enactment of section 2511[64] to be complete gifts that went unreported and untaxed. What evidence does the IRS harbor that suggests that some taxpayers and tax practitioners may have inaccurately interpreted section 2511(c) as excluding from the gift tax transfers to a trust not wholly owned by the donor or his spouse under the grantor trust rules, even though those transfers would otherwise be subject to gift tax? If in fact the IRS possesses such evidence (and assuming it can be revealed without violating taxpayer confidentiality), what is it and why hasn't the Service made it available to tax professionals? Wouldn't doing so render the IRS's assertion that some taxpayers may have inaccurately interpreted section 2511(c) more credible?

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[60]Reg. section 25.2511-2(b); section 2501(a)(1). Only the actuarial value of the remainder interest in the trust property is subject to gift tax on funding the trust. If the grantor dies during the term interest and after July 14, 2008 (reg. section 20.2036-1(c)(3)), the portion of the GRAT or GRUT corpus includable in the decedent grantor's gross estate is that portion, valued as of the grantor's date of death (or the section 2032 alternate valuation date, if applicable), necessary to yield that annual annuity, unitrust, or other payment without reducing or invading principal. (Reg. section 20.2036-1(c)(2)(i).) This portion is determined by using the section 7520 interest rate in effect on the decedent's date of death (or on the alternate valuation date, if applicable); *see* section 2033 and reg. section 25.2702-6(a)(2)(i). If the grantor dies after the term interest has terminated, the value of the property transferred to the GRAT or GRUT on the date of transfer is includable in the decedent grantor's taxable estate as an adjusted taxable gift (section 2001(b); reg. section 20.2001-1(b)).

[61]Section 2501(a)(1); reg. section 25.2501-1(a)(1).

[62]Section 2503(a).

[63]Section 2511(a); reg. section 25.2511-1(a) (''The gift tax applies to a transfer by way of gift whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible. For example, a taxable transfer may be effected by the *creation of a trust*'' (emphasis added).).

[64]Aug. 16, 1954, ch. 736.

Could it be that the IRS has compiled information suggesting that taxpayers and tax professionals erroneously believe a transfer of property to some grantor trusts (for example, GTEALTs) is not subject to gift tax because those trusts are grantor trusts of which the donor-grantor is treated as the owner for income tax purposes? If so, the IRS may have a valid reason to believe that the value of property transferred to some grantor trusts may have gone unreported and untaxed, inasmuch as the donor-grantor or his tax professional may not have understood that those transfers of property by gift are subject to gift tax. Perhaps Congress's intent in enacting section 2511(c) was to emphasize that the federal gift tax remains in effect and that additional tax revenue could be raised by placing more intense IRS scrutiny on transfers of property to trusts by eliminating the making of an incomplete gift. However, Congress may have been uncertain of section 2511(a)'s effectiveness, before the enactment of section 2511(c) under EGTRRA, to adequately address whether a transfer of property to a trust would be a complete gift or an incomplete gift subject to gift tax. Recall that the JCWAA amended section 2511(c) by striking ''taxable gift under section 2503'' and substituting ''transfer of property by gift.'' That amendment was described as a ''technical correction'' to clarify that the effect of section 511(e) of EGTRRA (effective for gifts made after 2009) was to treat some transfers of property in trust as a complete gift. It was indicated that the result of the ''clarification'' would be that the gift tax annual exclusion and the marital and charitable estate tax deductions may apply to those transfers.[65]

1. Observation. As a rule, the gift tax annual exclusion is unavailable for the value of a remainder interest in an irrevocable trust, because such a gift is a future interest — not a present interest, which is required to obtain the exclusion.[66] However, a transfer of property to an irrevocable *inter vivos* trust for the benefit of a person who has not attained age 21 on the date of the gift is considered a gift of a present interest if specified conditions are met, even though the minor is not given the unrestricted right to the immediate use, possession, or enjoyment of the property or the income from the property.[67] Under what circumstances could a ''transfer by gift of the entire interest in the property'' to a trust that, before 2010, would have been considered an incomplete gift not subject to gift tax be any different from situations perceived to be a transfer by gift of the entire interest in the property to a trust in 2010?

F. Critical Analysis of Notice 2010-19 Required

The IRS's entire explanation in the section entitled ''Interim Provision'' in Notice 2010-19 is at best double entendre and at worst doublespeak. Each sentence must be critically analyzed to better understand the meaning and effect of the notice. Again, in the opening sentence, the IRS says, ''some taxpayers may have inaccurately interpreted section 2511(c) as excluding from the gift tax transfers to a trust treated as wholly owned by the donor or the donor's spouse under [the grantor trust rules], even though those transfers would otherwise be taxable under Chapter 12.'' Perhaps taxpayers and tax professionals would have been better served if the IRS had distinguished the gift tax treatment of irrevocable grantor trusts (for example, GTEALTs) and revocable *inter vivos* trusts. The value of the remainder interest in property transferred to the former is subject to federal gift tax, but the entire value of property transferred to the latter, under the grantor trust rules, is not subject to federal gift tax. So too may some taxpayers and tax professionals have inaccurately interpreted the funding of a grantor ILIT as not being a complete gift of the value of the insurance policies transferred to the trust.

1. Opening sentence. As part of the critical analysis, one must compare the language in section 2511(c) with the language in the opening sentence of the notice's third paragraph. Recall that section 2511(c) states: ''Notwithstanding any other provision of this section and except as provided in regulations, a transfer in trust shall be treated as a transfer of property by gift, unless the trust is treated as wholly owned by the donor or the donor's spouse under'' the grantor trust rules. In the notice, the meaning of section 2511(c) is expressed through the statement: ''Some taxpayers may have inaccurately interpreted section 2511(c) as excluding from the gift tax transfers to a trust treated as wholly owned by the donor or the donor's spouse under [the grantor trust rules], even though those transfers would otherwise be taxable under Chapter 12.'' What the IRS has communicated to taxpayers and tax professionals in the notice is that the entire value of property transferred to an irrevocable grantor trust (GTEALTs, ILITs, etc.), although deemed wholly owned by the donor or his spouse only for income tax reporting purposes, is still a complete gift subject to gift tax.

2. Second and third sentences. In the second and third sentences of the third paragraph of Notice 2010-19, the IRS says:

[65]JCT, *supra* note 2, at 38.
[66]Section 2503(b)(1), flush language.
[67]Section 2503(c); Moy, *supra* note 12, section 23.05[B][3], at 23-22.

> Section 2511(c) is an addition to those substantive law provisions and is applicable to transfers made in 2010. Section 2511(c) broadens the types of transfers subject to the transfer tax under Chapter 12 to include certain transfers to trusts that, before 2010, would have been considered incomplete and, thus, not subject to the gift tax.

As discussed above, how is section 2511(c) an addition to those substantive law provisions that were in effect before 2010 for a transfer of property made to a trust in 2010? How does section 2511(c) broaden the types of transfers subject to the gift tax to include some transfers to trusts that before 2010 would have been considered incomplete and thus not subject to the gift tax? Despite the language in section 2511(c) — namely, ''a transfer in trust shall be treated as a transfer of property by gift, unless the trust is treated as wholly owned by the donor or the donor's spouse'' under the grantor trust rules — does it not contradict the IRS's assertion that section 2511(c) ''broadens the types of transfers subject to the transfer tax under Chapter 12 to include certain transfers to trusts that, before 2010, would have been considered incomplete and, thus, not subject to the gift tax''? Is it not the IRS's position, as posited in Notice 2010-19, that before 2010 a transfer of property by gift to a revocable *inter vivos* trust would have been an incomplete gift not subject to gift tax but that the transfer of property by gift to a revocable *inter vivos* trust in 2010 is a complete gift subject to gift tax? That is what the language of the third sentence in the third paragraph seems to imply.

3. Third and fourth sentences. The third and fourth sentences of the third paragraph complete the IRS's confusing, poorly reasoned explanation of section 2511(c):

> Accordingly, each transfer made in 2010 to a trust that is not treated as wholly owned by the donor or the donor's spouse under [the grantor trust rules] is considered to be a transfer by *gift of the entire interest in the property* under section 2511(c). The provisions of Chapter 12 as in effect on December 31, 2009, continue to apply (both before and during 2010) to all transfers made to any other trust to determine whether the transfer is subject to gift tax. [Emphasis added.]

4. Last sentence of the third paragraph. The IRS acknowledged in the last sentence of the third paragraph of Notice 2010-19 that ''the provisions of Chapter 12 regarding the substantive law applicable to the gift tax were not amended by EGTRRA, and those provisions continue to apply to all transfers made by donors during 2010.'' So why all the fuss? Since the law that applied before 2010 is to continue for a transfer of property to a trust in 2010, why the need for section 2511(c)?

5. Observation. The explanation of section 2511(c) that some transfers in trust are treated as transfers of property by gift simply re-plows old ground, even though those transfers would have been regarded as incomplete gifts or would not have been treated as transfers under the gift tax provisions in effect before 2010. Whether a transfer of property to a trust is a gift subject to federal gift tax depends on the extent of control the donor-grantor retains over the property transferred. Before the enactment of section 2511(c), a transfer of property to a CRT would not have been subject to federal gift tax.[68]

It seems reasonable to assume that the purpose of section 2511(c) is to subject to gift tax the *entire value* of property transferred in trust in 2010 (and perhaps beyond), which transfer would otherwise have been treated as an incomplete gift not subject to gift tax if made before 2010. Section 2511(c) makes clear that the entire value of property transferred to a trust (that is, conveyance of legal title of the property to the trustee) not wholly owned by the donor or his spouse under the grantor trust rules is subject to federal gift tax, even though the words ''entire value'' are not part of section 2511(c). As mentioned above, even though GTEALTs are irrevocable grantor trusts, the value of property comprising the remainder interest is subject to federal gift tax. So in this limited sense, the IRS's so-called ''Guidance Clarifying Treatment of Transfers in Trust,'' subtitled ''Guidance for Persons Making Transfers in Trust After December 31, 2009,'' in Notice 2010-19, is woefully misguided and incomplete. In general, a transfer of property to a revocable *inter vivos* trust is an incomplete gift. But under what circumstances would a transfer of property in trust be treated as a taxable gift in 2010 if it had not been treated as a transfer of property in trust under the gift tax provisions before 2010?

G. *Inter Vivos* Transfer of Property to a CRT

Considering the foregoing, does section 2511(c) mean that the value of an *inter vivos* transfer of property to a CRT is subject to federal gift tax since a CRT cannot be treated as wholly owned by the donor or his spouse under the grantor trust rules? Or will the value of an *inter vivos* transfer of property to a CRT not be subject to federal gift tax because the charitable gift tax deduction applies to the transferred property?

On one hand, the following would seem to imply that gift tax is imposed on a transfer of property to

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[68]Section 2522(a); reg. section 25.2522(a)-1(a); JCT, *supra* note 2, at 38; Notice 2010-19.

a CRT: ''accordingly, each transfer made in 2010 to a trust that is not treated as wholly owned by the donor or the donor's spouse under [the grantor trust rules] is considered to be a transfer by gift of the entire interest in the property under section 2511(c).'' This may be a reasonable inference, since a CRT cannot be treated as wholly owned by the donor-grantor or his spouse.[69] Recall, however, that although a transfer of property to a trust may be subject to gift tax, whether gift tax is actually imposed on the value of the property transferred is another matter for the reasons previously mentioned.

On the other hand, the following implies that the transfer of property to a CRT is exempt from federal gift tax: ''The provisions of Chapter 12 regarding the substantive law applicable to the gift tax were not amended by EGTRRA, and those provisions continue to apply to all transfers made by donors during 2010.''[70] This is true because the provisions of section 2522 regarding the charitable gift tax deduction were not amended by EGTRRA, and they continue to apply to all transfers made by donors to a CRT during 2010.[71] Thus, the value of an *inter vivos* transfer of property to a CRT is exempt from federal gift tax, despite section 2511(c).

The confusion caused by section 2511(c) regarding a transfer of property to a CRT is easily understood in view of the provision's seemingly conflicting language. It states: ''a transfer in trust shall be treated as a transfer of property by gift.'' A transfer of property to an irrevocable CRT constitutes a complete gift. Yet, the language immediately following in the same sentence reads: ''unless the trust is treated as wholly owned by the donor or the donor's spouse under'' the grantor trust rules. The former language is language of first impression in that the word ''gift'' is used, which the uninformed might interpret to mean a taxable gift. Regarding a transfer of property to a CRT, even though a CRT is not treated as a trust wholly owned by the donor-grantor or his spouse, the provisions of section 2522 cause the value of an *inter vivos* transfer of property to a CRT to be exempt from federal gift tax,[72] even in light of section 2511(c), since section 2522 was not amended by EGTRRA.[73] Reiterating, the value of an *inter vivos* transfer of property to a CRT is exempt from federal gift tax.

Without the benefit of the JCWAA's technical correction to section 2511(c), I initially believed that a transfer of property to a CRT would be a taxable gift in view of the language that ''a transfer in trust shall be treated as a taxable gift under section 2503, unless the trust is treated as wholly owned by the donor or the donor's spouse''[74] under the grantor trust rules. This was a reasonable belief, even though section 2522(a) was not amended by EGTRRA. Undoubtedly, absent the knowledge of the technical correction to section 2511(c), many tax professionals would have had to agree that the language ''taxable gift under section 2503'' was in direct conflict with section 2522(a). Hence, apparently, the technical correction.

A transfer of property to an irrevocable *inter vivos* trust constitutes a gift-taxable event, whether or not that trust is a grantor trust. As previously mentioned, GTEALTs are irrevocable grantor trusts under sections 671, 673, 675, 677, and 678, to which the transfer of property is subject to federal gift tax; that is, a transfer of property to these trusts is a federal gift-taxable event. Similarly, the transfer of property to an ILIT is a gift-taxable event, although the grantor may be deemed the owner of the trust for federal income tax purposes if the income of the trust estate may be ''applied to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse (except policies of insurance irrevocably payable for a purpose specified in section 170(c)).''[75] Hence, many ILITs are grantor trusts.

VII. Future of Section 2511(c)

A. Plain Meaning of Section 2511(c)

In effect, the plain meaning of section 2511(c) is more in keeping with the provisions of section 2511(a) and reg. section 25.2511-2(b). Section 2511(c) actually elaborates section 2511(a), and in doing so, conflicts with reg. section 25.2511-2(b), (c), and (d). These latter subsections address when a gift is incomplete. More disturbing is that the plain meaning of section 2511(c) does not explicitly provide that all transfers of property to a trust are complete gifts. The inference that section 2511(c) provides

[69]Rev. Rul. 77-285, 1977-2 C.B. 213, para. 7 (''Section 1.664-1(a)(4) of the Income Tax Regulations provides that, in order for a trust to be a charitable remainder trust, it must meet the definition of, and function exclusively as, a charitable remainder trust from the date or time of the creation of the trust. This section further provides that, solely for purposes of section 664 of the Code and the regulations thereunder, the trust will be deemed to be created at the earliest time that *neither the grantor nor any other person is treated as the owner of the entire trust* under subpart E, part 1, subchapter J, chapter 1, subtitle A [*i.e.*, the grantor trust rules]'' (emphasis added)); reg. section 1.671-1(d); sections 674(b)(4) and 2511(c).

[70]Section 2522(a); reg. section 25.2522(a)-1(a).

[71]Notice 2010-19.

[72]Section 2522; reg. section 25.2522(a)-1(a).

[73]Notice 2010-19.

[74]Section 511(e) of EGTRRA, adding subsection (c) to section 2511.

[75]Section 677(a)(3).

that all transfers of property to a trust not wholly owned by the donor or his spouse under the grantor trust rules are complete gifts is found only in the technical explanation and in Notice 2010-19 — neither of which represent the plain meaning of section 2511(c). Absent the technical explanation and Notice 2010-19, nothing in the language of section 2511(c) would lead one to infer that some transfers in trust are complete gifts ''even though such transfers would have been regarded as incomplete gifts, or would not have been treated as transfers under the gift tax provisions in effect prior to 2010.''

Would the JCT and the IRS have taxpayers and tax professionals believe that reg. section 25.2511-2(g) (defining a complete gift) applies to all transfers of property to a trust, regardless of whether the transfer of property is wholly incomplete or partially complete and partially incomplete? Likewise, are taxpayers and tax professionals to believe these authorities have the effect of law? They probably would not have the effect of law, since neither represents Congress's sense on the matter, which was not asserted before enactment of EGTRRA and the JCWAA. In this regard, it's important to comprehend the significance of reg. section 25.2511-2(b):

> As to *any property*, or part thereof or interest therein, of which the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for his own benefit or for the benefit of another, the gift is complete. But if upon a transfer of property (whether in trust or otherwise) the donor reserves any power over its disposition, the gift may be wholly incomplete, or may be partially complete and partially incomplete, depending upon all the facts in the particular case. Accordingly, in every case of a transfer of property subject to a reserved power, the terms of the power must be examined and its scope determined. For example, if a donor transfers property to another in trust to pay the income to the donor or accumulate it in the discretion of the trustee, and the donor retains a testamentary power to appoint the remainder among his descendants, no portion of the transfer is a completed gift [meaning the gift is incomplete]. On the other hand, if the donor had not retained the testamentary power of appointment, but instead provided that the remainder should go to X or his heirs, the entire transfer would be a completed gift. However, if the exercise of the trustee's power in favor of the grantor is limited by a fixed or ascertainable standard (see paragraph (g)(2) of section 25.2511-1), enforceable by or on behalf of the grantor, then the gift is incomplete to the extent of the ascertainable value of any rights thus retained by the grantor.[76]

B. Repeal of Section 2511(c)

Taxpayers and tax professionals should be concerned about section 2511(c), whether it is repealed or not. On one hand, if section 2511(c) is repealed, what weight might the IRS and the courts give to the technical explanation and to Notice 2010-19 regarding subjecting the entire value of transferred property to gift tax, even if the gift is in fact wholly incomplete or partially complete and partially incomplete? On the other hand, if section 2511(c) is not repealed, how might its questionable ''plain meaning'' be applied by the IRS and the courts in view of the technical explanation and Notice 2010-19?

In general, it is known among tax professionals that the provisions and amendments to the code effected by Title V of EGTRRA do not apply (1) to tax years, plan years, or limitation years beginning after 2010; or (2) in the case of Title V, to estates of decedents dying, gifts made, or generation-skipping transfers made after 2010.[77] Further, EGTRRA's sunset provisions provide that the code of 1986 and ERISA shall be applied and administered to years, estates, gifts, and transfers, as if the provisions and amendments made by EGTRRA in 2001 had never been enacted.[78]

This latter provision raises the question whether section 2511(c) will continue in effect after 2010. Section 411(x) of the JCWAA provides that except as provided in section 411(c) of the JCWAA, the amendments made by section 411 will take effect as if included in the EGTRRA provisions to which they relate. Thus, the provisions of section 2511(c), as amended by section 411(c) of the JCWAA, will not continue in effect after 2010 unless further amended by Congress before 2011.[79]

Section 2511(c) could be repealed if the provisions of S. Amdt. 4492 to H.R. 4213 are enacted.[80]

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[76]*See* reg. section 25.2511-2(c) and (d) for additional explanation of complete and incomplete gifts. Reg. section 301.6501(c)-1(f)(5) may also be affected by the JCT's technical explanation and the IRS's ''clarification'' of section 2511(c) in Notice 2010-19.

[77]Section 901(a) of EGTRRA.

[78]Section 901(b) of EGTRRA.

[79]Sections 901(a)(2) and (b) of EGTRRA.

[80]Section _02.(a)(2), Title X ''Responsible Estate Tax Act,'' S. Amdt. 4492 to H.R. 4213, ''American Jobs and Closing Tax Loopholes Act of 2010.'' Section _02.(a) of S. Amdt. 4492, section _02.(a) flush language provides: ''Any provision of the Internal Revenue Code of 1986 amended by such provisions are amended to read as such provisions would read if such sections had never been enacted.'' The word ''provision'' means amendments made by the provisions of EGTRRA that ''are hereby

(Footnote continued on next page.)

Even if section 2511(c) is repealed, its effect may be long lasting. The plain meaning of section 2511(c) simply reinforces section 2511(a). Nothing in section 2511(c) states unequivocally or implies that all transfers of property to a trust not wholly owned by the donor-grantor or his spouse under the grantor trust rules will be deemed complete gifts. As long as the federal gift tax is in effect, *inter vivos* transfers of property to a trust will probably invite attention by IRS examiners to the trust instruments themselves to determine to what extent the donor-grantor has made a transfer of property to the trust that is wholly incomplete, or partially complete and partially incomplete.

Yet if the IRS literally interprets the technical explanation of section 2511(c), it will probably treat all transfers of property to trusts, other than trusts wholly owned by the donor or his spouse under the grantor trust rules, as complete gifts. Certainly, if the donor-grantor transfers property to a trust wholly owned by him or his spouse under the grantor trust rules, the transfer will be a wholly incomplete gift and thus not subject to gift tax, unless of course the trust is, for example, a GTEALT under section 2702 or an ILIT. Congress's repeal of section 2511(c) would have an effect on the IRS and taxpayers similar to the effect on a jury of a judge's admonition to disregard the witness's last statement.

C. Congressional Intent

Although the JCT's technical explanation is dated March 6, 2002 — three days before the enactment of the JCWAA — it does not represent congressional intent or the sense of Congress on the need or reason for section 2511(c). The nature of section 2511(c) was not discussed in colloquies, committee reports, joint explanatory statements of managers included in conference committee reports, or floor statements made before enactment by one of the bill's managers.[81] Nor is there any evidence that the meaning of section 2511(c) as expressed in the technical explanation and Notice 2010-19 was even contemplated by Congress,[82] thereby bringing into question the credibility of the JCT staff's interpretation of its plain meaning. Moreover, most of the language in the technical explanation, Notice 2010-19, S. Amdt. 650 to H.R. 1836, EGTRRA, (successor to H.R. 8, Death Tax Elimination Act of 2001), section 411(g) of the JCWAA and, by association, section 511(e) of EGTRRA, does not appear in section 2511(c). Nor was it even mentioned in Conference Report 107-84[83] when section 2511(c) was initially enacted as part of Title V, section 511(e) of EGTRRA. The only places the language does appear is in the technical explanation, in Notice 2010-19, and in a footnote to the JCT's "General Explanation of Tax Legislation Enacted in the 107th Congress."[84]

Since the language does not express congressional intent, the technical explanation and Notice 2010-19 certainly would not constitute substantial authority under reg. section 1.6662-4(d)(3)(iii) to treat all transfers of property to a trust not wholly owned by the donor or his spouse as complete gifts subject to gift tax. It seems unlikely that the IRS or the courts would cite the technical explanation or Notice 2010-19 to buttress their argument that all transfers of property to trusts not wholly owned by the donor or his spouse are complete gifts when in fact those gifts may be wholly incomplete, or partially complete and partially incomplete.[85]

Absent evidence of congressional intent and the necessity or reason for section 2511(c), on what other evidence or understanding did the JCT staff base its interpretation of section 2511(c)? More simply stated, there is no legislative history of Congress's intent regarding section 2511(c), and that in my opinion is why the technical explanation and the IRS's interpretation of it are speculative at best. As the Third Circuit has observed, "Legislative history of a statute may not be taken as giving to it 'a meaning not fairly within its words,'[86] nor add new items to it."[87] Even if legislative history regarding the intent of section 2511(c) were found at some later date, statements made in congressional debates and hearings are not always reliable guides to legislative intent, because they have occasionally been regarded as an indication that Congress was aware of possible consequences of proposed legislation.[88] Even if a court concluded that the language

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repealed effective December 31, 2009." Arguably, since section 2511(c) was added by section 511(e) of EGTRRA but ultimately amended by the Job Creation and Worker Assistance Act of 2002 — not by EGTRRA — it may not be repealed by the aforementioned flush language.

[81]*See Antonides v. Commissioner*, 91 T.C. 686 (1988); *Schirmer v. Commissioner*, 89 T.C. 277 (1987); *Van Scoyoc v. Commissioner*, T.C. Memo. 1988-520; *Crawford v. Commissioner*, T.C. Memo. 1993-192; *Fisher v. Commissioner*, T.C. Memo. 1992-740.

[82]*See Carnation Co. v. Commissioner*, 71 T.C. 400 (1978).

[83]Conf. Rept. 107-84 (2001).

[84]JCT, "General Explanation of Tax Legislation Enacted in the 107th Congress," JCS-1-03 (Jan. 24, 2003), at 65, n.59.

[85]*See Carnation*, 71 T.C. 400.

[86]*Commissioner v. Bilder*, 289 F.2d 291 (3d Cir. 1961), citing *St. Louis, I.M. & S. Ry v. Craft*, 237 U.S. 648, 661 (1915).

[87]*Bilder*, 289 F.2d 291, citing *United States v. Shreveport Grain & El. Co.*, 287 U.S. 77, 83 (1932).

[88]*Dougherty v. Commissioner*, 60 T.C. 917 (1973), citing *O'Hara v. Luckenbach Steamship Co.*, 269 U.S. 364, 367-368 (1926); *Penn Mutual Co. v. Lederer*, 252 U.S. 523, 534 (1920).

of section 2511(c) is ambiguous despite the interpretation proffered in Notice 2010-19 and the technical explanation, it would most likely reject the argument that Congress could not have intended the meaning ascribed to section 2511(c) in Notice 2010-19.[89]

D. Tax Court Interpretation

When a statute is clear on its face, the Tax Court would require unequivocal evidence of legislative purpose before construing the statute to override the plain meaning of the words used therein.[90] The Supreme Court has stated:

> There is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes. Often these words are sufficient in and of themselves to determine the purpose of the legislation. In such cases we have followed their plain meaning. When that meaning has led to absurd or futile results, however, this Court has looked beyond the words to the purpose of the act. Frequently, however, even when the plain meaning did not produce absurd results but merely an unreasonable one ''plainly at variance with the policy of the legislation as a whole'' this Court has followed that purpose, rather than the literal words.[91]

The Supreme Court reaffirmed this ''familiar rule, that a thing may be within the letter of the statute and yet not within the statute, because not within its spirit, nor within the intention of its makers.''[92] Although the Tax Court is not free to twist the code beyond the contours of its plain and unambiguous language to comport with good policy,[93] it may go beyond the literal language of the code if reliance on that language would defeat the plain purpose of Congress.[94] Because ''words do not have an immutable meaning,'' the Tax Court has interpreted the code in a manner contrary to its literal wording when necessary to implement clearly expressed congressional intent.[95] In the absence of ''unequivocal evidence of legislative purpose,'' the court has applied the law as written by Congress.[96]

E. Silence of Statutes

Unfortunately, despite the silence of the committee reports, one cannot necessarily conclude that Congress was unaware of the effect that section 2511(c) would have on a transfer of property to a trust by gift. When the statute is silent, it may fairly be assumed that Congress did not intend to provide that all transfers of property in trust would be complete gifts.[97] Even if a court were to conclude that the language of section 2511(c) is ambiguous and not in keeping with reg. section 25.2511-2(b), it may reject the argument that Congress could not have intended the meaning ascribed to the statute by the technical explanation and the IRS's interim guidance in Notice 2010-19.[98] Still, nothing in section 2511(c) suggests or implies that all transfers of property in trust are to be treated as complete gifts subject to gift tax. Absent unequivocal evidence that Congress's intent was to treat all transfers of property in trust as complete gifts subject to gift tax, the technical explanation and the ''clarification'' proffered in Notice 2010-19 are nothing more than misconstrued interpretations of the intent of section 2511(c).

F. Congressional Directive to Issue Regulations

It's important to keep in mind that the technical explanation is dated March 6, 2002. Although undated, Notice 2010-19 applies to transfers of property made in trust after December 31, 2009. In enacting section 2511(c), Congress did not direct the secretary of the Treasury to prescribe regulations as may be appropriate to carry out the purposes of section 2511(c). When it so intends, Congress knows how to specifically delegate legislative regulatory authority for tax legislation, and nowhere in section 2511(c) is such a delegation found. Only in Notice 2010-19 is it mentioned that ''the Treasury Department and the IRS intend to issue regulations to confirm the conclusions set forth in the notice.''

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[89] *See Dougherty*, 60 T.C. at 926.

[90] *Huntsberry v. Commissioner*, 83 T.C. 742, 747-748 (1984).

[91] *United States v. American Trucking Associations*, 310 U.S. 534, 543 (1940), quoting *Ozawa v. United States*, 260 U.S. 178, 194 (1922) (footnote references omitted). *See also Zinniel v. Commissioner*, 89 T.C. 357 (1987), citing *American Trucking*, 310 U.S. at 543.

[92] *Estate of Sachs v. Commissioner*, 88 T.C. 769, 773 (1987), citing *California Federal Savings & Loan Ass'n v. Guerra*, 479 U.S. 272 (1987), quoting *Steelworkers v. Weber*, 443 U.S. 193, 201 (1979), and *Church of the Holy Trinity v. United States*, 143 U.S. 457, 459 (1892).

[93] *Estate of Sachs*, 88 T.C. at 773, citing *Badaracco v. Commissioner*, 464 U.S. 386, 398 (1984).

[94] *Estate of Sachs*, 88 T.C. at 773, citing *Bob Jones Univ. v. United States*, 461 U.S. 574, 586 (1983); *see also Church of the Holy Trinity v. United States*, 143 U.S. 457, 459 (1892); *Abdalla v. Commissioner*, 647 F.2d 487, 496 (5th Cir. 1981), and cases cited therein.

[95] *Estate of Sachs*, 88 T.C. at 773, citing *Carson v. Commissioner*, 71 T.C. 252, 262 (1978), *aff'd*, 641 F.2d 864 (10th Cir. 1979); *Focht v. Commissioner*, 68 T.C. 223 (1977); *Carasso v. Commissioner*, 34 T.C. 1139, 1142 (1960), *aff'd*, 292 F.2d 367 (2d Cir. 1961).

[96] *Estate of Sachs*, 88 T.C. at 773, citing *Huntsberry*, 83 T.C. at 747-748.

[97] *See Willamette Industries Inc. v. Commissioner*, T.C. Memo. 1991-389; *Rome I Ltd. v. Commissioner*, 96 T.C. 697, 706 (1991); *O'Brien v. Commissioner*, 79 T.C. 776, 788 (1982).

[98] *See Dougherty*, 60 T.C. 917.

Of course, any regulations would be merely interpretative, not legislative. Legislative or substantive regulations are issued by an agency under statutory authority and generally implement the statute. Interpretative rules, however, are issued by an agency to simply advise the public of the agency's construction of the statutes that it administers. The distinction between the two types of rules, although sometimes small, is important. Interpretations of legislative Treasury regulations long continued without substantial modification applying to unamended or substantially reenacted statutes are deemed to have received congressional approval and have the effect of law.[99] However, a court has the power to substitute its judgment for administrative judgment in the case of interpretive rules.[100]

No amendments to reg. section 2511-2 have been proposed to date. The language "except as provided in regulations" in section 2511(c) creates a conundrum. Does it mean Treasury regulations in effect on June 7, 2001 (the date of EGTRRA's enactment), or does it mean regulations to be issued by Treasury and the IRS to confirm the conclusions set forth in Notice 2010-19? If it means the former, a transfer of property to a grantor trust may be wholly incomplete, or may be partially complete and partially incomplete, depending on all the facts in the case as provided in reg. section 25.2511-2(b).[101]

Whether a transfer of property to a trust not wholly owned by the donor or his spouse is deemed a complete gift depends on all the facts in the particular case. "Accordingly," the regs state, "in every case of a transfer of property subject to a reserved power, the terms of the power must be examined and its scope determined."[102] Until regulations interpreting section 2511(c) are issued, reg. section 25.2511-2(b) should be cited as authority for the proposition that not all transfers of property to trusts not wholly owned by the donor or his spouse are complete gifts as provided in section 2511(c).

G. Courts Interpret Plain Meaning of Statutes

In view of this uncertainty, how might the courts decide the plain meaning of section 2511(c) relative to Treasury and the IRS's intention to issue regulations? When regulations have not been issued to deal with a current situation, a court may apply one of several approaches: (1) it may decide a particular case in favor of the taxpayer[103]; (2) it may give the IRS and Treasury additional time to issue regulations[104]; or (3) it may attempt to understand the plain meaning of an otherwise ambiguous statute like section 2511(c) in view of legislative history, if any, and render a response without the benefit of regulations.[105]

The courts consider Treasury regulations valid if they implement the congressional mandate in some reasonable manner. In determining whether a particular regulation carries out the congressional mandate in a proper manner, courts examine whether the regulation harmonizes with the statute's plain language, origin, and purpose. Harmony between statutory language and regulation is particularly

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[99]*Helvering v. Winmill*, 305 U.S. 79, 82 (1938).

[100]*Am. Med. Ass'n v. United States*, 691 F. Supp. 1170 (N.D. Ill. 1988).

[101]Reg. section 25.2511-2 was last amended on December 3, 1999 (T.D. 8845, *Doc 1999-38226*, *1999 TNT 232-6*).

[102]Reg. section 25.2511-2(b).

[103]*See Zinniel*, 89 T.C. 357 (The court acknowledged that the process for issuing Treasury regulations is often slow because of the many levels of review and the procedures for notice and comment to which regulations are usually subject. However, the court could not understand how the secretary could fail to issue any temporary or final regulations directly related to the case at hand when there was a statutory directive to issue them. The court believed that it would not have been difficult to issue temporary regulations. The failure to issue temporary or final regulations under the new statutory section frustrated the interpretation of the statute by creating a new trap for the taxpayer.).

[104]*See Am. Med. Ass'n*, 691 F. Supp. 1170 (The court decided for the taxpayer, due in part to the IRS: "By now deliberately eschewing the offered opportunity to adopt a valid Reg. (f)(4) and thus to fill the regulatory gap, the government has to be viewed as having expressly elected to treat the Reg. (f)(3)(iii) cross-reference to Reg. (f)(4) as nonexistent — as pure surplusage, to be ignored because it lacks any possible meaning. . . . 'But now Reg. (f)(4) has been invalidated, leaving a gap in the regulations: Reg. (f)(3)(iii) provides a standard, but it refers to a now-nonexistent regulation for instructions as to how to implement the standard. This Court cannot perform such major judicial surgery at AMA's request, by excising the reference to Reg. (f)(4) and reading Reg. (f)(3)(iii) as though it were intended to stand alone (as it clearly is not).'").

[105]Banoff, *supra* note 26, at 24,343; *Occidental Petroleum Corp. v. Commissioner*, 82 T.C. 819 (1984) (The court ruled in the taxpayer's favor because the secretary, although directed by Congress to prescribe regulations under which items of tax preference (of both individuals and corporations) were to be properly adjusted when the taxpayer does not derive any tax benefit from the preference, had not done so when the time arrived for the court's decision some eight years after the effective date of section 58(h): "The Secretary has not yet promulgated any such regulations. Moreover, we note further that he has not even published in the *Federal Register* any proposed regulations in this respect. However, the failure to promulgate the required regulations can hardly render the new provisions of section 58(h) inoperative. We must therefore do the best we can with these new provisions. Certainly we cannot ignore them." In justifying its position, the court said, "Congress could hardly have intended to give the Treasury the power to defeat the legislatively contemplated operative effect of such provisions merely by failing to discharge the statutorily imposed duty to promulgate the required regulations. As already indicated, we must give effect to these provisions in the absence of regulations.").

significant. When the court can measure the commissioner's interpretation against a specific provision in the code, the court owes the interpretation less deference than a legislative regulation to define a statutory term or prescribe a method of executing a statutory provision. When the commissioner acts under specific authority, the court's primary inquiry is whether the interpretation or method is within the delegation of Treasury or the commissioner's authority. Relatively less deference is owed to an interpretative regulation issued under the general grant of authority contained in section 7805(a) than one issued under a specific grant of authority; that is, a legislative regulation.[106] A rule (that is, a regulation) is interpretive rather than legislative if it is not ''issued pursuant to legislatively-delegated power to make rules having the force of law,'' or if the agency intends the rule to be no more than an expression of its construction of a statute or rule.[107] Interpretive rules are statements of what the administrative officer thinks the statute or regulation means. Those rules provide only a ''clarification of statutory language.''[108]

It's interesting to note that code sections are repealed from time to time, but conference committee reports are not. And rarely are IRS notices withdrawn. Yet conference committee reports and notices may have the effect of law, even when the code section explained or interpreted by them is repealed. The technical explanation was prepared by the JCT staff and was issued after section 2511(c) was amended. My opinion is that the technical explanation does not represent the views of legislators or an explanation available to them when acting on the technical correction to section 2511(c) and is therefore not part of the legislative history of either EGTRRA or the JCWAA. For these reasons, the portion of the technical explanation regarding ''Transfers in Trust'' noted above, standing alone, without any direct evidence of legislative intent, is not unequivocal evidence of legislative intent to require that all transfers of property in trust are to be treated as complete gifts. Based on the absence of legislative history underlying section 2511(c) and the technical explanation, it would stretch one's imagination to surmise that the Tax Court would find that Congress was attempting to require by statute that all transfers of property to a trust would be treated as complete gifts subject to gift tax and thereby preclude the secretary and the IRS from prescribing regulations contrary to the plain meaning of section 2511(c). Absent a cogently reasoned determination of the plain meaning of section 2511(c) based on the language of the statute, it is likely the Tax Court would craft its own interpretation in favor of the taxpayer and against the interpretation rendered by the technical explanation and Notice 2010-19.

Moreover, reliance on the technical explanation would be unwarranted and contrary to precedent. A staff committee's explanation of a provision is not a statement by legislators, and the explanation of section 2511(c) was not relied on by legislators when either enacting the provision under EGTRRA or making the technical correction to it under the JCWAA (H.R. 3090), inasmuch as H.R. 3090 was reported by the House Ways and Means Committee on October 17, 2001, and passed by the House on October 24, 2001.[109] Granted, H.R. 3090 was three times amended in the form of a substitute[110] and one amendment by the House to the Senate amendment. None of the amendments had anything to do with the technical correction to section 2511(c). The technical explanation cannot be considered part of the legislative history because it was authored by the staff of the JCT — not by Congress.[111] However, the technical explanation may be given some deference by the courts, especially when the views expressed are consistent with items of legislative history.[112] The technical explanation (the blue book) represents only the views of the congressional staff; it was not approved by Congress. The technical explanation of section 2511(c) was not relied on by Congress because it was not part of any of the amendments to the JCWAA. Also, the blue book should not be relied on because it is inconsistent with the plain meaning of section 2511(c), as well as reg. section 25.2511-2(b).[113]

VIII. Conclusion

The following conclusions may be made about the effect of section 2511(c):

1. The value of property transferred to an *inter vivos* revocable trust wholly owned by the

[106]*Am. Med. Ass'n*, 691 F. Supp. 1170, quoting *Rowan Cos. v. United States*, 452 U.S. 247, 252-253 (1981).

[107]*Chamber of Commerce v. OSHA*, 636 F.2d 464, 468 (D.C. Cir. 1980).

[108]*Am. Med. Ass'n*, 691 F. Supp. 1170.

[109]H.R. Rep. No. 107-251, at 1 (2001).

[110]Nov. 9, 2001; Nov. 14, 2001; Feb. 14, 2002. The House passed the bill with an amendment to the Senate amendment on March 7, 2002. The Senate agreed to the House amendment to the Senate amendment on March 8, 2002, and H.R. 3090 was signed by the president on March 9, 2002.

[111]*See Robinson v. Commissioner*, 119 T.C. 44 (2002), *Doc 2002-20462*, *2002 TNT 173-4*, citing *Estate of Hutchinson v. Commissioner*, 765 F.2d 665 (7th Cir. 1985), *aff'g* T.C. Memo. 1984-55.

[112]*Id.*

[113]*Id.*

donor or his spouse that satisfies the grantor trust rules is not a taxable gift under section 2511(a) or (c).

2. A transfer of property to a CRT is a gift under section 2511(a) and (c), but the value of the property transferred is not subject to gift tax under section 2522(a), and the donor's lifetime gift tax exemption amount is not reduced by the value of the property transferred to the CRT.

3. Absent congressional action before 2011, section 2511(c) may not be in effect after 2010, but the intent of its provisions, as interpreted by the IRS, may continue to be applied by the IRS.

4. Even if section 2511(c) is repealed, its intent may still be applied by the IRS to a transfer of property in trust not wholly owned by the donor-grantor or his spouse under the grantor trust rules in view of the effect of law made applicable by JCT conference reports and IRS notices.