2026 NATIONAL INCOME TAX WORKBOOK

Chapter 2: Gift Tax

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LEARNING OBJECTIVES

Recognize	Recognize when a taxpayer has made a gift
Understand	Understand when the annual exclusion from gift tax applies
Know	Know when direct gifts for education or medical expenses are excluded from gifts
Recognize	Recognize when spouses can split gifts
Know	Know the gift tax treatment of a gift to a spouse

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LEARNING OBJECTIVES

Understand	Understand how the deceased spousal unused exclusion ordering rules are applied
Understand	Understand the valuation of a gift for gift tax purposes
Know	Know how to adequately disclose a gift on a gift tax return
Recognize	Recognize when to file Form 709
Know	Know how to complete Form 709

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ISSUE 1: DEFINITION OF A GIFT

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DEFINITION OF A GIFT P 49

I.R.C. § 2501(a)(1) imposes a tax on transfers of property made **without full and adequate consideration**

A direct or indirect transfer of cash, property, or income without receiving something of at least equal value in return (the full and adequate consideration)

- ***Examples***: *Cash; Digital Assets (Crypto); forgiven debts; powers of appointment; divorce-related property settlements; and below-market or interest-free loans*

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FULL AND ADEQUATE CONSIDERATION

A transfer is **not** a gift if full and adequate consideration is received in return (think business transactions)

Example 2.2: A $75,000 truck given in return for domestic and emotional support is a **taxable gift**, as non-monetary considerations are disregarded in determining the value of the gift

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PRACTITIONER NOTE: ENCUMBERED PROPERTY

The gift value of encumbered property = FMV – debt assumed

The liability assumed by the donee is treated as consideration paid to the donor

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COMPLETED GIFT P 50

- To make a gift, donor must transfer beneficial interest and title
- If donor transfers less than full interest in property, then donor has made a gift of only the partial interest transferred
- **Example 2.3**: If $75,000 truck from Example 2.2 is purchased and titled in both donor and donee's name, gift value = ½ of $75,000

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RETAINED INTERESTS

Completed v. Incomplete Gifts:

- *A gift is complete when the donor relinquishes all control and dominion; retained powers over disposition may cause the gift to be partially or fully incomplete*

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INCOMPLETE GIFT & RETAINED INTEREST P 50

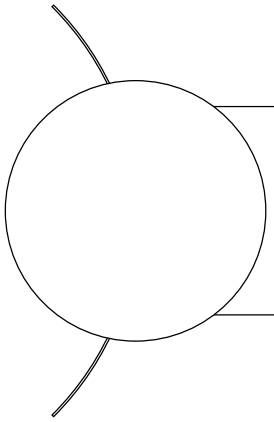
A gift may be incomplete if the donor retains powers to:

- *Reclaim the property*
- *Change beneficiaries (absent some fixed or ascertainable standard)*
- *Reallocate beneficiary interests (absent some fixed or ascertainable standard)*

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EXAMPLE 2.4: RETAINED INTERESTS



Transfer to a trust is not a completed gift when the donor retains a testamentary power to control remainder distribution, preserving control over the property

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PRACTITIONER NOTE: ASCERTAINABLE STANDARD

Measurable standard under which the holder of a power is legally accountable

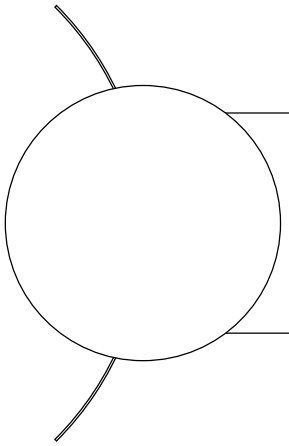
Health, education, maintenance, support → *ascertainable*

Pleasure, desire, happiness → ***NOT*** *ascertainable*

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COMPLETED GIFT WITH LIMITED CONTROL



A donor may retain limited control over timing or conditions of distributions (e.g., income accumulation rules) and still make a completed gift if ultimate ownership is not retained

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COMPLETED GIFT WITH LIMITED CONTROL

Example 2.5: Mother's transfer to an irrevocable trust for daughter is a completed gift even though mother retained limited authority to adjust income timing based on conditions like education or employment

Example 2.6: Creating a joint account is not a completed gift until the other party withdraws funds for their own benefit, at which point the amount withdrawn is treated as the gift

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DONOR AS TRUSTEE

If a donor transfers property to self as trustee and retains no beneficial interest in the property and no power over it except fiduciary powers to change beneficiaries → **completed gift**

Trustee's powers must be limited by a fixed or ascertainable standard

Example 2.8: Trustee's powers limited to an ascertainable standard → completed gift

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INDIRECT GIFTS

Transfers Subject to Gift Tax: include sales, exchanges, and other disposition of property **if the consideration received is less than FMV**

Bargain Sales: Treated as a partial gift

Use of Personal Property: Allowing use of personal property for less than FMV may also be a gift

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PART SALE PART GIFT

Below Market Transfers: Property transferred for less than FMV triggers gift tax

The difference between the FMV and the consideration received = gift amount

Example 2.9: Dad sold son a car for $24,000 under FMV. That $24,000 is a gift to son.

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USE OF PROPERTY

Support to Adult Children: Providing financial support to adult children may trigger gift tax rules if there is no legally enforceable obligation to support the child

Example 2.10: Mom allowing son to rent vacation home while in school for a price well under FMV = gift to son

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ESTATE TAX AND BASIS ADJUSTMENTS

Different Tax Treatments: A transfer can be a completed gift for gift tax but incomplete for estate tax or basis purposes

Contemplation of Death: Gifts made in contemplation of death are included in the gross estate of donor (not treated as a completed gift for estate tax)

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GIFTS IN CONTEMPLATION OF DEATH

1-Year Basis Rule: Certain gifts made to decedent within 1 year of death do not receive step-up in basis, instead receive a carryover basis

A gift in contemplation of death is an **incomplete gift for estate tax** purposes

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GIFTS IN CONTEMPLATION OF DEATH

A gift is made in contemplation of death if:

- *Transfer or relinquishment of property happens within 3 years of death;* ***and***
- *Property would have been included in decedent's estate under I.R.C. §§ 2036-2038 if retained*

Gift Tax Add Back: Gift taxes paid on transfers within the 3-year period are included in the estate of decedent

- **Exception**: Does not apply to bona fide sales for full and adequate consideration

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PRACTITIONER NOTE: STATE LAW – GIFTS IN CONTEMPLATION OF DEATH

Gifts made in contemplation of death may be revocable under state law.

If donor can reacquire property after the threat of death has passed, the gift is an incomplete gift for gift tax purposes

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QUALIFIED DISCLAIMERS

Disclaimer: A donee's refusal to accept gift or inheritance

No Gift by Disclaimer: The person disclaiming is not making a gift to the ultimate recipient

Timing:

- *Generally, 9-month period is determined separately for each taxable transfer*
- ***Gift Context**: For gifts, the period begins when the transfer is complete for gift tax purposes*

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QUALIFIED DISCLAIMERS

Qualified Disclaimer Requirements:

- *Must be in writing;*
- *Must be made within 9 months of transfer (after reaching age 21);*
- *Disclaimant must not have accepted any interest or benefits from the property;*
- *Property must pass without direction from the disclaimant; and*
- *The refusal must be irrevocable and unqualified*

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GIFT TAX EXCLUSION

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AMOUNT OF THE ANNUAL EXCLUSION

2026 Exclusion: $19,000 per recipient excluded from taxable gifts

Broad Applicability: Annual exclusion applies to gifts to all donees regardless of relationship to donor

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PRACTITIONER NOTE: GIFTS TO NON-U.S. SPOUSE

For 2026

- *$194,000 of gifts to a spouse who is **not a U.S. citizen** are not included in total amount of taxable gifts*

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GIFTS & PRESENT INTEREST

Future Interests Not Eligible: Annual exclusion does not apply to future interests (e.g., remainders, reversions)

Future Interest Defined: Right to use, possess, or enjoy property at a later date

Present Interest Defined: Immediate use, possession, or enjoyment of property (or income from property)

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TRANSFERS FOR THE BENEFIT OF MINORS

Donor wishes to give minor child a present interest in a gift

Donor can use a Crummey Trust or I.R.C. § 2503(c) trust qualify for the annual exclusion even if the beneficiary does not have present use or enjoyment of the trust income or principal

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PRACTITIONER NOTE: CUSTODIAL ACCOUNT IS PRESENT INTEREST

The Uniform Transfers to Minors Act and Uniform Gifts to Minors Act allows a transfer of assets to a custodian for the benefit of a minor child

A gift to a custodial account is a gift of a present interest that qualifies for annual exclusion

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USE OF A CRUMMEY TRUST

- Allows donor to make a gift of a present interest that qualifies for annual exclusion
- ***Crummey v. Commissioner***:
  - *Parents created a trust for 4 children that required trustee to accumulate income and add it to the trust principal until each child was 21*
  - *From ages 21-35, trust required distributions of income*
  - *After age 35, trustee had discretion to distribute income and principal*
  - *Trust also gave each child right to demand $4,000 of the additional contributions (at the time annual exclusion = $3,000)*

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CRUMMEY TRUST

Crummey v. Commissioner:

- **Court Holding**: Withdrawal rights of children created a present interest, and the court upheld the annual exclusion for the additional gifts to the trust because beneficiaries had unrestricted present right to demand distribution above the annual exclusion amount

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EDUCATIONAL AND MEDICAL EXCLUSIONS

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EDUCATIONAL AND MEDICAL EXCLUSIONS

Payment of another's education or medical care made directly to the provider are not treated as gifts to the person who received the education or medical assistance

This is an exclusion **in addition** to annual gift tax exclusion

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EXCLUSION OF EDUCATION PAYMENTS

Direct Tuition Requirement: Payments must be made directly to a qualified educational organization

Qualifying Institution: Organization that normally maintains regular faculty, curriculum, and enrolled student body

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EXCLUSION OF EDUCATION PAYMENTS

Limited to Tuition Only: Exclusion does not apply to amounts paid for books, supplies, room and board, and other non-tuition costs

Applies Broadly: Covers full-time or part-time students

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I.R.C. § 529 QUALIFIED TUITION PLAN (QTP)

- *529 contributions are subject to gift tax rules*
- *If contributions exceed annual exclusion amount, donor can elect to account contributions ratably over a 5-year period*
- ***Form 709**: Donor must file Form 709 to make election and report one-fifth of the gift amount on the return*

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EXCLUSION OF MEDICAL PAYMENTS

Direct Payment Requirement: Medical expenses must be paid directly to the healthcare provider

Qualified Medical Expenses: Includes costs for:

- *Diagnosis, cure, mitigation, treatment, or prevention of disease;*
- *For the purpose of affecting any structure or function of the body;*
- *For transportation primarily for and essential to medical care*
- *Medical insurance paid on behalf of the individual*

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GIFT SPLITTING

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GIFT SPLITTING

One spouse's gift to a third party can be treated as if the gift was made 50/50 by both spouses

Eligibility: Both spouses must be U.S. citizens or residents

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GIFT SPLITTING

Marital Status: Spouses must be married at the time of the gift and cannot marry anyone else during the remainder of the year

Liability: *Consenting* spouses are **jointly and severally liable** for any gift tax due

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PRACTITIONER NOTE: SPOUSAL CONSENT TO SPLIT GIFTS

Consenting spouse no longer required to sign Form 709, but must sign Notice of Consent to be attached to donor's return (*See Figure 2.3 on P. 61*)

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MAKING THE ELECTION TO SPLIT GIFTS

- To elect to split gifts, donor spouse must file Form 709 and attach Notice of Consent signed and dated by the consenting spouse
- If only one spouse required to file gift tax return → only one Notice of Consent required
- If both spouses required to file gift tax return → each spouse should execute a Notice of Consent and attach to return

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THE ELECTION TO SPLIT GIFTS: TIMING OF CONSENT

Generally, Notice of Consent may be signed at any time after the end of the calendar year

Exceptions:

- **April 15 Deadline**: Notice of Consent must be signed by April 15 of the following year.
- If neither spouse filed a gift tax return for year on or before that date, then the consent must be made on the first gift tax return filed by either spouse
- **Deficiency Limitation**: Consent may not be obtained after a notice of deficiency for the gift tax

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WHEN CONSENTING SPOUSE MUST FILE GIFT TAX RETURN

Separate Returns Required: Spouses who elect gift splitting must each file their own gift tax return (No joint returns allowed)

Exceptions: Only one spouse required to file if:

Only one spouse made any gifts, total value to each third-party did not exceed $38,000, and all gifts were of present interests; ***or***	*Donor spouse made gifts of more than $19,000 but less than $38,000 to third-party; Consenting spouse made only gifts of less than $19,000 to* ***different*** *third-parties, and all gifts (by both spouses) were of present interests*

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GIFTS TO A SPOUSE



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GIFTS TO A SPOUSE

General Rule: Taxpayers have an unlimited deduction for gifts to a spouse

- *Applies to gifts to a* ***U.S. citizen spouse***
- Gifts to non-U.S. citizen spouses limited (2026: $194,000)
- *Deduction for* ***gifts of a terminable interest are limited***

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TRANSFERS INCIDENT TO DIVORCE

I.R.C. § 2516 – Divorce Property Settlements & Gift Tax

- *Provides a special rule for property settlements between divorcing spouses*
- *Applies when spouses enter into a written agreement regarding marital or property rights*
- *Divorce must occur within 2 years of the agreement*
- *Transfers pursuant to the agreement are treated as made for "full and adequate consideration"*
- ***Gift tax does not apply***

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CROSS REFERENCE: TRANSFERS INCIDENT TO DIVORCE

Cross Reference: Gain or Loss on Transfer (I.R.C. § 1041) – no gain or loss is recognized on transfers between spouses; no gain or loss recognized on transfers incident to divorce

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TERMINABLE INTERESTS – EXCEPTIONS

Exceptions allow the marital deduction for:

- Gifts of a power of appointment
- Qualified Terminable Interest Property (QTIP)
- Certain joint interests
- Qualified charitable remainder trusts

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DEFINITION OF TERMINABLE INTEREST

A **terminable interest** is an interest that ends due to:

- *The passage of time, or*
- *The occurrence (or nonoccurrence) of an event or contingency*

Examples of Terminable Interests:

- *Life Estates*
- *Terms for years*
- *Annuities*
- *Patents*
- *Copyrights*

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LIFE ESTATE WITH POWER OF APPOINTMENT

A gifted life estate qualifies for the marital deduction if all of the following apply:

- *The donee spouse is entitled to all income from the property for life (or from a specific portion);*
- *The income is paid at least annually;*
- *Donee spouse has the power to appoint the property to self or estate;*
- *The power of appointment must be exercisable solely by the donee spouse and in all events;*
- *No part of the interest can be appointed to any other person during donee's lifetime*

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QUALIFIED TERMINABLE INTEREST PROPERTY (QTIP)

Eligible for marital deduction

Three Requirements:

Donor spouse transfers the property	*Donee spouse holds a* ***qualifying income interest*** *for life*	*Donor makes a qualifying election*

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PRACTITIONER NOTE: DONOR SPOUSE MAKES THE QTIP ELECTION

Donor spouse makes the QTIP election by:

Listing the QTIP property on Schedule A of Form 709	*Deducting its value on Schedule A, Part 4, Line 4*

Election is **presumed** for all qualified property listed

Election **cannot** be made on a **late-filed** Form 709

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PRACTITIONER NOTE: EARLY TERMINATION QTIP TRUST

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QTIP assets are **included** in surviving spouse's gross estate

- *Surviving spouse and remainder beneficiaries may wish to terminate the trust*

McDougall v. Commissioner: Early termination and distribution of trust assets to surviving spouse = **taxable gift** from remainder beneficiaries to surviving spouse

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CHARITABLE REMAINDER TRUST

When Donor & Spouse are the ONLY Noncharitable Beneficiaries:

Terminable interest rules ***do not apply***	*Spouse's annuity or unitrust interest qualifies for the* ***marital deduction***	*Remainder interest qualifies for the* ***charitable deduction***

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USE OF THE DECEASED SPOUSAL UNUSED EXCLUSION (DSUE) FOR GIFTS

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DSUE FOR GIFTS

- OBBBA increased the **basic exclusion amount (BEA)** to $15,000,000 for gifts for 2026
- The **deceased spousal unused exclusion (DSUE)** is the unused portion of a deceased spouse's estate and gift tax exclusion
- **Applicable Exclusion Amount** = BEA + DSUE

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DSUE FOR GIFTS

- DSUE remains available to surviving spouse even after remarriage
- **To Elect Portability of DSUE**: Estate representative must file Form 706

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PRACTITIONER NOTE: ELECTING DSUE PORTABILITY

Electing portability may seem unnecessary when combined marital assets fall below BEA

Why Practitioner Should Still Consider the Election:

- *Gross estate values and the BEA **may change** in the future*
- *Surviving spouse may lock in the higher exclusion amount*

Best Practice:

- ***Discuss** portability election with clients – even when it appears unnecessary*
- ***Document** any decision made not to elect portability*

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DECEASED & DIVORCED SPOUSE

General Rule: DSUE based on the **last deceased spouse's** unused exclusion amount

Remarriage & the DSUE: If surviving spouse remarries and second spouse dies, the second spouse's DSUE replaces the first spouse's DSUE

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DECEASED & DIVORCED SPOUSE

If surviving spouse's subsequent marriage ends in divorce/annulment, the divorced spouse's later death **does not** replace prior deceased spouse's DSUE

- *Divorced spouse cannot be "last deceased spouse" because they were not married at the time of death*

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EXAMPLE 2.29: DSUE IS USED FIRST

- **2025**: Carole dies with no taxable gifts or estate; full $13.9 million DSUE (2025 BEA) elected and transferred to Carole's husband Wylie
- Wylie did not remarry
- **2026**: Wylie made $16 million in taxable gifts
- No gift tax due because of the DSUE and a portion of Wylie's BEA → Wylie still has some exclusion amount to apply to future gifts

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EXAMPLE 2.30: DSUE OF FIRST AND SECOND SPOUSE

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- **2021:** Hunter died; executor elected portability of $11.7 million DSUE to Whitney
- **2023**: Whitney gifted $2 million to children, applying Hunter's DSUE – **no gift tax due**
- **2025**: Whitney married Miguel
- **2026**: Miguel died; estate of $12,340,000 passed to children; executor elected portability of Miguel's remaining $2,660,000 DSUE
- Miguel's DSUE replaces Hunter's remaining DSUE

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VALUATION OF A GIFT

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VALUATION OF A GIFT

Why Valuation Matters:

- *Ensures accurate reporting on gift tax return*
- *Avoids penalties*
- *Determines the taxpayer's* ***remaining exclusion*** *for estate tax purposes*

Valuation Standard:

- *Gifts of property are valued at FMV on the date of the gift*

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VALUATION OF A GIFT

Relevant Factors to Determine Gift's Value:

- *Cost or selling price of the item*
- *Sales of comparable properties*
- *Replacement cost*
- *Professional appraisals*

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VALUATION OF A GIFT

Additional Considerations:

- *Desirability, use, condition, scarcity, and market demand*
- *Other characteristics may also be relevant depending on type of property*
- *See IRS Publication 561, Determining the Value of Donated Property, for considerations in determining FMV of stocks/bonds, business interests, real estate, and various other property*

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PRACTITIONER NOTE: ACCURACY-RELATED PENALTIES

Substantial Valuation Understatement:

- *Applies when claimed value is **65% or less** of correct value*
- *Penalty: **20%** of underpayment*
- *Penalty **does not apply** if underpayment is **$5,000 or less***

Gross Valuation Misstatement:

- *Applies when claimed value is **40% or less** of correct value*
- *Penalty increases to **40%** of underpayment*

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VALUATION OF STOCKS/BONDS WHEN PRICES UNAVAILABLE

Bond Valuation Factors:

- *Soundness of the security*
- *Interest yield and maturity date*
- *Other relevant factors*

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VALUATION OF STOCKS/BONDS WHEN PRICES UNAVAILABLE

Stock Valuation Factors:

- *Company's net worth*
- *Company's prospective earning power and dividend-paying capacity*
- *Goodwill of the business*
- *Economic outlook of the industry*
- *Company's position in the industry and its management*
- *Degree of control represented by the block of stock to be valued*
- *Values of comparable publicly traded securities in the same industry*

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VALUATION OF A GIFT: BUSINESS INTERESTS

General Rule:

- FMV = net amount a willing buyer would pay a willing seller (with neither being compelled to act and having knowledge of relevant facts)

Key Valuation Factors:

- *Fair appraisal of all assets (tangible, intangible, and goodwill)*
- *Demonstrated earning capacity of the business*
- *Other relevant corporate stock valuation factors, where applicable*

Required Documentation:

- *Complete financial data*
- *Examination and reports by accountants, engineers, or other technical experts*

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CROSS REFERENCE: BUSINESS VALUATION

Key Resource:

- *IRS "Valuation of Non-Controlling Interests in Business Entities Electing to be Treated as S Corporations – A Job Aid for IRS Valuation Analysts"*

Purpose:

- *Provides guidance on applying Rev. Rul. 59-60 1959-1 C.B. 237, to determine the FMV of interests in a closely held or non-publicly traded entity*

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VALUATION OF A GIFT: REAL ESTATE

Appraisal Requirements:

- *Be performed by a professional real estate appraiser*
- *Appraiser's report must include:*
  - Complete property description
  - Physical features, condition, and dimensions
  - Current use, zoning, permitted uses, and potential **higher and better use**

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VALUATION OF A GIFT: REAL ESTATE

Three Main Valuation Approaches:

- ***Comparable Sales*** *– based on prices of similar properties*
- ***Income Capitalization*** *– based on income-producing potential*
- ***Replacement Cost*** *– based on cost to replace the property*

An appraisal may require the combined use of two or three methods rather than only one.

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VALUATION OF REAL ESTATE: COMPARABLE SALES

General Approach: Compares subject property to similar properties recently sold.

Appraiser Considerations: *Relative correlation and reliability of value indicators*

Unimproved Real Property – Additional Factors:

- *Location, size, and zoning or use restrictions*
- *Accessibility, road frontage, utilities, and water rights*

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INCOME CAPITALIZATION

General Approach:

- *Capitalizes net income from the property at a rate reflecting a fair return given the investment's risks*
- *Two key elements:* ***income to be capitalized*** *and the* ***capitalization rate***

Income Stream Projection Based On:

- Historical financial income and expense statements
- Vacancy rates and rent rolls
- Terms and length of existing leases
- Current market conditions

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INCOME CAPITALIZATION

Valuation Process:

- *Convert net income and cash flow projections to present value (using capitalization techniques reflective of typical investors for the property type)*
- *Appraisers must justify and support all income and expense projections*
- *Make adjustments to reflect income streams consistent with the selected valuation method*

Capitalization & Discount Rates Must be Supported by:

- Reliable market data
- Industry surveys
- Market-supported technical methodology and computations

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REPLACEMENT COST

Replacement Cost Method:

- *Typically supports values determined by other appraisal methods*
- ***Improved Realty**: Land and improvements are valued separately*
- *Best suited for **specialty properties** where other approaches lack sufficient data and where land value and depreciation amounts are reasonably determinable*

Replacement Cost of a Building:

- Based on the materials, quality of workmanship, and square/cubic footage
- Includes total cost of labor, materials, overhead, and profit

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REPLACEMENT COST

Appraiser must also consider:

- ***Physical Deterioration**: Wear and tear on the building itself*
- ***Functional Obsolescence**: Inadequate lighting, plumbing, or heating*
- ***Economic Obsolescence**: External forces making the surrounding area less desirable*

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ADEQUATE DISCLOSURE ON GIFT TAX RETURNS



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ADEQUATE DISCLOSURE ON GIFT TAX RETURNS

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Adequate disclosure of a gift on Form 709 commences the statute of limitations on assessment

Adequate Disclosure Standard:

- *Transfer must be reported in a manner that informs IRS of the nature of the gift and the basis for the reported value*

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ADEQUATE DISCLOSURE ON GIFT TAX RETURNS

Gift Tax Statute of Limitations:

- *Generally, **3 years** (with some exceptions)*
- ***6 years** if a gift tax return omits one or more gifts with a value exceeding 25% of total gift value*
- ***No limitation** if taxpayer fails to file a gift tax return **or** if value of gift is not adequately disclosed*

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ADEQUATE DISCLOSURE ON GIFT TAX RETURNS

Description of transferred property and any consideration received

Identity and relationship of transferor and each transferee

For property transferred in trust:

- *The trust's tax ID number and description of trust terms (or a copy of the trust instrument)*

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ADEQUATE DISCLOSURE ON GIFT TAX RETURNS

*A conforming appraisal **or** a detailed description of the method used to determine FMV*

Statement of any position taken contrary to proposed, temporary, or final Treasury regulations or revenue rulings

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PRACTITIONER NOTE: ESTATE TAX CALCULATION

When the statute of limitations expires on an adequately disclosed gift:

- *The reported gift value is **finally determined** for estate tax purposes*
- *The IRS **cannot adjust** the gift value for purposes of:*
  - Determining **prior taxable gifts** and current tax liability *(§ 2504(c))*
  - Determining **adjusted taxable gifts** and estate tax liability *(§ 2001(f))*

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NO DESCRIPTION OF AMOUNT OR CLASS OF INTEREST TRANSFERRED

Adequate Disclosure – LLC Interest Case
C.C.A. 2002-21-010 (February 12, 2002)

- **IRS Chief Counsel Conclusion**:
  - *The description of a gift of an LLC interest should include:*
    - Number of units transferred
    - Class type of the units
    - Percentage of ownership interest represented
- **Result**:
  - *Statute of limitations remained* ***open***

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NO DESCRIPTION OF HOW VALUATION DISCOUNTS WERE CALCULATED

Adequate Disclosure – Partnership Interest Case
G.C.M. 2015-22-01F (March 13, 2015)

- **IRS Conclusion**:
  - *Gift tax return* ***failed to adequately disclose*** *transfer of partnership interests because:*
    - Appraisal covered the **wrong asset** (land vs. partnership interest)
    - No explanation of **discount methodology**
    - No description of **FMV valuation method**
- **Result**:
  - *Statute of limitations remained open – IRS could assess gift tax at any time*

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ADEQUATE DISCLOSURE ON OTHER DOCUMENTS

Adequate Disclosure – OVDP Case
Schlapfer v. Commissioner, T.C. Memo. 2023-65

- **Court Findings**:
  - *Treas. Reg. § 301.6501(c)-1(f)(2) requirements are* ***guidance, not mandatory***
  - *Court may consider* ***all relevant documents*** *(including attachments and informational documents referenced in the return)*
  - *The full OVDP packet provided sufficient information to satisfy adequate disclosure requirements → initiated statute of limitations*
- **Key Takeaway**: Adequate disclosure can be satisfied through supporting documents beyond the gift tax return itself

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ADEQUATE DISCLOSURE ON AN AMENDED RETURN

Curing Adequate Disclosure – Amended Form 709

- **When Prior Disclosure Was Inadequate**:
  - *Practitioner may assist taxpayer in filing an* ***amended Form 709***
  - *Statute of limitations* ***begins*** *to run upon adequate disclosure on the amended return*

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WHEN TO FILE FORM 709



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WHEN TO FILE FORM 709

- *Gifts to any person (other than spouse)* ***exceed the annual exclusion***
- *Gifts of a* ***future interest*** *are made – even if under the annual exclusion*
- *Spouses* ***split gifts****, regardless of the amount*
- *Gift to a spouse is a* ***terminable interest*** *not qualifying for the marital deduction*
- *Gift to a spouse qualifies for the* ***QTIP election***

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WHEN FORM 709 IS NOT REQUIRED:

- *Transfers to **political organizations***
- *Transfers of an entire interest to certain **tax-exempt organizations** (§§ 501(c)(4), (5), (6))*
- *Payments qualifying for the **educational exclusion***
- *Payments qualifying for the **medical exclusion***
- ** Even if a taxpayer is not required to file Form 709, it may be advisable to file anyway to start the statute of limitations*

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PRACTITIONER NOTE: INDIVIDUAL RETURNS REQUIRED

Each spouse must file their own Form 709

Only **individuals** are required to file gift tax returns

If a **trust, estate, partnership, or corporation** makes a gift:

- *The individual beneficiaries, partners, or stockholders are considered the donors*
- *Those individuals may be liable for gift and generation-skipping transfer taxes*

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PRACTITIONER NOTE: NONRESIDENT DONORS

Nonresident noncitizens are subject to gift tax of **tangible property located in the U.S.**

Must File Form 709 When:

- *Gifts of **future interests** are made*
- *Gifts of present interests to a donee (other than a spouse) **exceed annual exclusion***
- *Outright gifts to a **non-U.S. citizen spouse** exceed $194,000*

** If a donee receives a gift (or bequest) from a non-U.S. person in excess of $100,000 → Must file Form 3520*

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EXAMPLE 2.33: REPORTING AN ANNUAL EXCLUSION GIFT

2026: Worthy gifted her grandson a 1% interest in a privately held family company

Estimated company FMV: $1.5 million

Value of 1% interest: $15,000 – below the $19,000 annual exclusion

Form 709 Analysis:

- *Required to file? No – gift is below annual exclusion*
- *Recommended to file? Yes – start the clock! (IRS may later challenge FMV of company and/or 1% interest)*

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FORM 709 FILING DEADLINES

General Rule: Form 709 due by April 15 of the year following the gift

When the Donor Dies During the Year: The executor must file Form 709 by the **earlier of**:

- *The due date (with extensions) for the **donor's estate tax return**, or*
- *The **April 15 due date** for Form 709 (or extended due date)*

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EXTENSIONS OF TIME TO FILE

Two Extension Methods for Form 709:

- *Income Tax Return Extension*
- *Form 8892*

No Extension of time to pay gift tax

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FORM 8892: APPLICATION OF TIME TO FILE

Key Limitation:

- *DOES NOT extend time to pay gift tax owed*

Dual Purpose of 8892:

- *6-month extension of time to file*
- *Serves as a payment voucher (Form 8892-V) for any gift tax due*

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EXTENSION OF TIME TO PAY

General Rule:

- *Extension to **pay** must be requested separately from extension to **file***
- *Maximum extension**: 6 months** (longer if taxpayer is abroad)*

How to Request – Form 1127:

- *Form 1127 is used to request an extension of time to pay*
- *Must be received by the IRS **on or before** the Form 709 due date (not including extensions)*

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PENALTIES

Failure to File Penalty:

- *5% of tax due for each month or partial month the return is late*
- *Maximum penalty: 25% of tax due*

Failure to Pay Penalty:

- *0.5% per month on the unpaid balance*
- *Maximum penalty: 25% of the amount due*

When both penalties apply in the same month:

- Reduce the failure-to-file penalty (5%) by the failure-to-pay penalty (0.5%)

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REASONABLE CAUSE DETERMINATIONS

How to Avoid Penalties:

- *Establish that the failure to file (or pay) was due to* ***reasonable cause*** *and not* ***willful neglect***

Reasonable Cause Standard:

- *Taxpayer exercised* ***ordinary business care and prudence*** *but was unable to comply*
- *An event* ***outside the taxpayer's control****,* OR *an* ***undue hardship***

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TAX PREPARER PENALTIES

Unreasonable Position

- *Penalty = greater of $1,000 or 50% of income earned for preparation of return*

Willful or Reckless Conduct

- *Penalty = greater of $5,000 or 75% of income earned for preparation of the return*

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COMPLETING FORM 709

Land Grant University
Tax Education Foundation

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COMPLETING FORM 709 – OVERVIEW

Step-by-Step:

- Complete ***Part I – General Information*** (Lines 1-21)
- Complete ***Part III – Spouse's Consent on Gifts to Third Parties*** (Lines 1-7), if applicable
- List each gift on the appropriate part of ***Schedule A***

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COMPLETING FORM 709 – OVERVIEW

Step-by-Step (cont'd):

- Complete ***Schedule B*** – Gifts From Prior Periods, if applicable
- Complete ***Schedule C*** – DSUE Amount and Restored Exclusion, if applicable
- Complete ***Schedule D*** – Computation of Generation-Skipping Transfer Tax, if gifts were listed on Schedule A, Parts 2 or 3

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COMPLETING FORM 709 – OVERVIEW

Step-by-Step (cont'd):

- Complete ***Schedule A, Part 4*** – Taxable Gift Reconciliation
- Complete ***Part II – Tax Computation***
- ***Sign and date*** the return

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FORM 709 SCHEDULE A

Schedule A is organized into **four parts**:

- *Part 1 – Gifts Subject Only to Gift Tax*
- *Part 2 – Direct Skips*
- *Part 3 – Indirect Skips*
- *Part 4 – Taxable Gift Reconciliation*

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SCHEDULE A, PART 1: GIFTS SUBJECT ONLY TO GIFT TAX

Required Information for Each Gift:

- *Donee's name and address*
- *Relationship to donor (if any)*
- *Description of the gift*
- *Donor's **adjusted basis** in the gift*
- *Date of the gift*
- *FMV on the date of the gift*
- *Spouse's gifts, if electing to split gifts*

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PRACTITIONER NOTE: TRANSCRIPT REQUEST

Requesting a Gift Tax Transcript – Form 4506-T

- *Line 6: Enter "Form 709"*
- *Only available transcript type for gift tax: **Account Transcript** (Line 6, Box B)*
- *Line 9: Enter the tax period (MMDDYYYY)*

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FORM 709 SCHEDULE C: DSUE

Part 1 – DSUE From Last Deceased Spouse

- *Identifies the **last deceased spouse** and applicable DSUE amount*
- *Last deceased spouse = most recently deceased person married to the surviving spouse at **the time of death***
- *Determined on the **date a taxable gift is made***
- *Remarriage does not affect the designation of last deceased spouse*

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FORM 709 SCHEDULE C

Part 2 – DSUE From Predeceased Spouse(s):

- *Part 2 identifies deceased spouses to whom the taxpayer was married prior to the last deceased spouse and any DSUE received from those spouses*

Key Rules:

- *Remaining DSUE from a predeceased spouse **cannot** be applied to current gifts if that spouse **is not** the most recently deceased spouse – even if the last deceased spouse had no DSUE or made no portability election*
- *DSUE from last deceased spouse is **always applied before** surviving spouse's basic exclusion amount*

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EXAMPLE 2.34: REPORTING THE DSUE

- **2021: Hunter died; executor elected portability of $11.7 million DSUE to Whitney**
- **2023**: Whitney applied $2 million of Hunter's DSUE to taxable gifts
- **2025**: Whitney remarried Miguel
- **2026**: Miguel died; executor elected portability of $2,660,000
- **2027**: Whitney made a $1 million taxable gift

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EXAMPLE 2.34: REPORTING THE DSUE

Applicable Credit Calculation

Component	**Amount**
Whitney's 2027 BEA (estimated)	$15,190,000
Hunter's DSUE (applied to prior gifts)	$2,000,000
Miguel's DSUE (applied to current gift)	$1,000,000
Total Exclusion Base	**$18,190,000**
Less: 2027 Taxable Gift	($1,000,000)
Net Amount	$17,190,000
Applicable Credit (($15,190,000 + $3,000,000 - $1,000,000)x40%) + $345,800	**$7,221,800**

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FORM 709 PART 2 P 82

Form 709 Part 2 is where a taxpayer calculates the gift tax

Step 1 – Calculate the Gift Tax:

Calculate tax on **current and prior-year taxable gifts**	Use the **Unified Rate Schedule** (Figure 2.4)

Step 2 – Calculate Applicable Credit:

No DSUE: Credit based on BEA only (Figure 2.6)	**DSUE Available**: Credit calculated on Schedule C (BEA + DSUE)

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QUESTIONS?

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