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# Life After Death? The Role of Postmortem Events in Valuing Deductions for Claims Against Estates

Benjamin Clark Brown*

*Table of Contents*



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* Candidate for Juris Doctor, Washington and Lee University School of Law, May 2003. I dedicate this Note to the memory of my grandfather, Robert James Thrift, Jr., '29, '31L. I want to thank Professor Robert Danforth for his invaluable assistance throughout the writing process. I would also like to thank my family for their love and support. Finally, and most importantly, I want to thank Lizzy and Vail for making each day even better than the last.

## *I. Introduction*

Section 2053(a) of the Internal Revenue Code (IRC) provides for the deduction of certain expenses, indebtedness, and taxes from an estate's gross value for the purpose of determining the net taxable value of an estate.[1] Specifically, that section provides, "For purposes of the tax imposed by section 2001, the value of the taxable estate shall be determined by deducting from the value of gross estate such amounts . . . for claims against the estate."[2] The practical impact of this provision is that an estate, in computing net taxable value, may deduct from its gross value the amount of any legally enforceable claims of third parties, thereby reducing the estate's tax liability.

Section 2053(a) does not, however, specifically address the issue of whether an estate should value such claims as of the date of death irrespective of subsequent events, or whether postmortem events can affect this valuation. Several complex problems arise due to the vagueness of the statute.[3] Because the code is silent as to the issue of the timing of such valuations, executors lack a definite rule governing the computation of the value of such deductions and face the prospect that the Internal Revenue Service (IRS) will issue a

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1. *See* I.R.C. § 2053(a) (2000) (permitting deductions for claims against estate in determining estate's gross value). This section states in full:

> General rule–For purposes of the tax imposed by section 2001, the value of the taxable estate shall be determined by deducting from the value of the gross estate such amounts–(1) for funeral expenses, (2) for administration expenses, (3) for claims against the estate, and (4) for unpaid mortgages on, or any indebtedness in respect of, property where the value of the decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate, as are allowable by the laws of the jurisdiction, whether within or without the United States, under which the estate is being administered.

*Id.*

2. *Id.*

3. *See generally* Anna Meresidis, Note, *The I.R.C. § 2053(a)(3) Controversy: Should Events After Death Affect the Value of Estate Tax Deductions for Claims Against the Estate?*, 70 FORDHAM L. REV. 2705 (2002) (analyzing problems presented by vagueness of § 2053(a)(3) with respect to various types of claims typically asserted against estates and arguing in favor of date-of-death valuation rule). Ms. Meresidis's note commences with a discussion of five separate types of claims typically asserted against estates, *id.* at 2710–13, and then focuses on application of the statute to definite claims, disputed claims, and contingent claims, *id.* at 2718–43. Although this Note briefly treats definite, disputed, and contingent claims in subpart III.B, *infra*, it expands on Ms. Meresidis's note by providing a comprehensive analysis of the differing treatment of the issue by the circuit courts, *infra* Part II, discussing the differences between deduction valuation and claim validity, *infra* subpart III.A, contrasting deductions for claims with other estate deductions, *infra* subpart III.C, and engaging in a comparative analysis of the role of postmortem events in valuing the assets of an estate, *infra* Part IV.

notice of deficiency should postmortem events alter the value of claims that existed as of the date of death.

The following illustration demonstrates the potential problems that arise as a result of the code's failure to address this issue.[4] In 2002, Jane Doe makes a gift of stock in the family business to her son, John Doe. Jane determines that the value of the stock is $2,000,000 at the time of the gift, and she pays gift taxes in the amount of $435,000.[5] Three years later, in 2005, Jane dies and her estate is worth $3,000,000. Shortly after her death, the IRS initiates an investigation into the valuation of the gift she made to her son. The IRS determines that the stock she gifted was in fact worth $3,000,000 and, as a result, that her tax liability on the 2002 gift was actually $930,000.[6] Assume for the purposes of this illustration that the IRS cannot issue a notice of deficiency against Jane's estate because the statute of limitations has run. Instead, the IRS asserts liability against John Doe for the $495,000 shortfall[7] pursuant to § 6324 of the tax code, which shifts liability for unpaid gift taxes to the donee when the liability becomes unenforceable as against the donor by reason of lapse of time.[8] In response, John Doe promptly files an action in probate court asserting a claim against Jane's estate for the $495,000 deficiency. Jane's estate consequently deducts $495,000 from the gross value of the estate pursuant to John's claim, resulting in an estate tax liability of $1,037,500.[9]

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4. The author derived the factual basis for this illustration from a leading Eleventh Circuit case. *See* Estate of O'Neal v. United States, 258 F.3d 1265, 1273 (11th Cir. 2001) (upholding estate's deduction based on date-of-death valuation of claim irrespective of postmortem events that altered this valuation).

5. Pursuant to § 2001(c), the tentative tax on a gift of $2,000,000 made in 2002 is $780,800. I.R.C. § 2001(c) (West Supp. 2002). Pursuant to § 2010(c), this amount is reduced by a credit equal to the tentative tax on $1,000,000. *Id.* § 2010(c). The tentative tax on $1,000,000 is $345,800. *Id.* § 2001(c). Subtracting $345,800 from $780,800 results in a gift tax liability of $435,000.

6. Pursuant to § 2001(c), the tentative tax on a gift of $3,000,000 made in 2002 is $1,275,800. *Id.* § 2001(c). Pursuant to § 2010(c), this amount is reduced by a credit equal to the tentative tax on $1,000,000. *Id.* § 2010(c). The tentative tax on $1,000,000 is $345,800. *Id.* § 2001(c). Subtracting $345,800 from $1,275,800 results in a gift tax liability of $930,000.

7. The shortfall is the difference between the $435,000 gift tax Jane paid (based on Jane's gift valuation of $2,000,000) and the $930,000 actually due (based on the IRS gift valuation of $3,000,000).

8. *See* I.R.C. § 6324(a)(2) (2000) (imposing gift tax liability on transferees).

9. Determining Jane's estate tax liability involves a four-step process. The first step is to compute the value of Jane's taxable estate. Her taxable estate is determined by subtracting $495,000 (the value of John's claim) from $3,000,000 (her gross estate at death). *Id.* § 2053(a)(3). This results in a taxable estate of $2,505,000. The second step is to add the value of the taxable estate to the value of adjusted taxable gifts. Pursuant to § 2001(b)(1), Jane's

One year later, John and the IRS reach a settlement valuing the gifted stock at $2,500,000. This valuation would have resulted in a gift tax liability of $680,000.[10] Thus the value of John's claim after the settlement decreases to $245,000.[11] Herein lies the problem. If Jane's estate may rely on the date-of-death valuation of the claim, the $495,000 deduction remains intact, and the estate's tax liability of $1,037,500 does not change. However, if postmortem events, like John's settlement with the IRS, can affect the value of deductions for claims, then Jane's estate must amend the value of the deduction from $495,000 to $245,000, and as a result the estate's tax liability will increase to $1,163,300.[12] This represents a $125,800 increase in tax liability for Jane's estate.[13]

The previous illustration underscores the need for legislative or judicial guidance in determining the timing of valuation of deductions for claims against estates. When a postmortem event reduces the value of a claim for which an estate initially took a deduction, the executor will argue that the date-of-death valuation should govern. Conversely, when a postmortem event increases the value of such a claim, the executor will seek to increase the

executor must add the value of Jane's taxable estate at her death, $2,505,000, to the value of adjusted taxable gifts, $2,000,000, resulting in an amount of $4,505,000, which is subject to tax. *Id.* § 2001(b)(1). The third step is to calculate the tentative tax on $4,505,000, which, pursuant to § 2001(c), is $2,028,300. *Id.* § 2001(c). This tentative tax is reduced by the aggregate amount of gift tax Jane already paid. *Id.* § 2001(b)(2). Subtracting the $435,000 Jane already paid results in a tentative tax of $1,593,300. The fourth step is to apply the unified credit allowable under § 2010 to this tentative tax. The applicable credit for an estate of a decedent dying in 2005 is the tentative tax on $1,500,000. *Id.* § 2010(c). The tentative tax on $1,500,000 is $555,800. *Id.* § 2001(c). Subtracting the $555,000 credit from the tentative tax of $1,593,300 results in a tax liability for Jane's estate in the amount of $1,037,500.

10. Pursuant to § 2001(c), the tentative tax on a gift of $2,500,000 made in 2002 is $1,025,800. *Id.* § 2001(c). Pursuant to § 2010(c), this amount is reduced by a credit equal to the tentative tax on $1,000,000. *Id.* § 2010(c). The tentative tax on $1,000,000 is $345,800. *Id.* § 2001(c). Subtracting $345,800 from $1,025,800 results in a gift tax liability of $680,000.

11. The $245,000 claim value represents the difference between the $435,000 gift tax Jane paid (based on Jane's gift valuation of $2,000,000) and the $680,000 actually due (based on the $2,500,000 settlement valuation).

12. Deducting $245,000 (the amended value of the allowable § 2053(a)(3) deduction) from $3,000,000 (Jane's gross estate), and then adding to this amount the value of Jane's adjusted taxable gifts ($2,000,000), yields an amount of $4,755,000, which is subject to tax. *See supra* note 9 (explaining calculation of taxable estate). The tentative tax on $4,755,000 is $2,153,300. I.R.C. § 2001(c) (West Supp. 2002). This tax is reduced by the $435,000 gift tax Jane already paid, resulting in a tentative tax of $1,718,300. *Id.* § 2001(b)(2). Applying the $555,800 unified credit to the tentative tax of $1,718,300 results in a tax liability for Jane's estate in the amount of $1,163,300. *Id.* § 2010(c).

13. The $125,800 of tax liability represents the difference between the initial tax liability of $1,037,500 and the revised tax liability of $1,163,300.

amount of the estate's deduction for this claim. Without a hard and fast rule governing the proper role of postmortem events in valuing deductions for claims, the potential for litigation of the issue is limitless.

As one commentator eloquently observed, this issue "lies at the intersection of the two inevitables, death and taxes."[14] Executors lack guidance as to whether they may rely on deductions for claims valued as of the date of death, or whether postmortem events can play a role in altering the valuation of these deductions.[15] Furthermore, this lack of guidance continues to result in litigation that drains precious IRS resources that are already severely strained.[16]

Unfortunately, neither the courts nor Congress have succeeded in clearing these muddy waters. In the courts, a distinct circuit split has evolved as to which rule applies, with four circuits holding that estates should value deductions for claims as of the date of death irrespective of postmortem events[17] and with two circuits holding that postmortem events can alter the valuation of such deductions.[18] The statutes and administrative regulations provide even less guidance as to which rule to apply. The language of § 2053(a) is completely devoid of reference to the proper date on which to value claims deductions.[19] Furthermore, the only relevant treasury regulations concerning valuation of deductions for claims are arguably contradictory.[20]

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14. Gary Young, *Death, Taxes, and Oliver Wendell Holmes*, NAT. L.J., Aug. 20, 2001, at B6.

15. *See* Robert E. Madden & Lisa H.R. Hayes, *Subsequent Litigation Cannot Alter Amount of Claim Deducted*, 28 EST. PLAN. 548, 550 (2001) (observing that "issue of when and how to value a claim for estate tax purposes is obviously not settled" and cautioning tax practitioners to "be ready to defend their position if challenged").

16. *See* Albert B. Crenshaw, *IRS Lacks Resources It Needs, Departing Commissioner Says*, WASH. POST, Oct. 11, 2002, at E1 (noting that tight budgets and a mandate to improve technology and customer service have curtailed hiring of "revenue agents or other professionals who have the training and experience necessary to find unreported income and overstated deductions").

17. *See, e.g.*, Estate of O'Neal v. United States, 258 F.3d 1265, 1276–77 (11th Cir. 2001) (refusing to consider postmortem events in valuing deductions for claims against estates); Estate of McMorris v. Comm'r, 243 F.3d 1254, 1263 (10th Cir. 2001) (same); Estate of Smith v. Comm'r, 198 F.3d 515, 526 (5th Cir. 1999) (same); Estate of Van Horne v. Comm'r, 720 F.2d 1114, 1117 (9th Cir. 1983) (same); Propstra v. United States, 680 F.2d 1248, 1257 (9th Cir. 1982) (same).

18. *See, e.g.*, Estate of Sachs v. Comm'r, 856 F.2d 1158, 1163 (8th Cir. 1988) (ruling that postmortem events do play role in valuation of deductions for claims against estates); Comm'r v. Estate of Shively, 276 F.2d 372, 375 (2d Cir. 1960) (same); Jacobs v. Comm'r, 34 F.2d 233, 236 (8th Cir. 1929) (same).

19. *See* I.R.C. § 2053(a)(3) (2000) (lacking any reference to timing of valuation of deductions for claims).

20. *See* Estate of Smith v. Comm'r, 198 F.3d 515, 521 (5th Cir. 1999) (noting ambiguity

Seeming to support a rule in favor of consideration of postmortem events, Treasury Regulation § 20.2053-1(b)(3) permits a deduction for a claim "though its exact amount is not then known, provided it is ascertainable with reasonable certainty, and will be paid."[21] This regulation arguably requires courts to consider postmortem events when the exact value of a claim is not ascertainable upon death.[22] Conversely, Treasury Regulation § 20.2053-4 permits a deduction for "personal obligations of the decedent existing at the time of his death."[23] This temporal reference to "time of [] death" arguably favors a firm date-of-death valuation rule.[24]

It is probable that the Supreme Court will eventually grant certiorari to provide guidance as to which rule applies.[25] With the circuit courts divided over which rule to apply, nothing short of a legislative amendment or a decree from the Supreme Court will put an end to the doctrinal disarray of the law as it exists in its present form. There are two distinct policy concerns that mandate decisive resolution of this issue. First, there is a strong public policy

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of regulations).

21. *See* Treas. Reg. § 20.2053-1(b)(3) (as amended in 1972) (governing use of estimated values). This section reads as follows:

> Estimated amounts. An item may be entered on the return for deduction though its exact amount is not then known, provided it is ascertainable with reasonable certainty, and will be paid. No deduction may be taken upon the basis of a vague or uncertain estimate. If the amount of a liability was not ascertainable at the time of final audit of the return by the district director and, as a consequence, it was not allowed as a deduction in the audit, and subsequently the amount of the liability is ascertained, relief may be sought by a petition to the Tax Court or a claim for refund as provided by sections 6213(a) and 6511, respectively.

*Id.*

22. *See Smith*, 198 F.3d at 521 (explaining argument that favors consideration of postmortem events unless estate can prove that claim is "reasonably certain" and "will be paid").

23. Treas. Reg. § 20.2053-4 (1958). This section states in relevant part:

> The amounts that may be deducted as claims against a decedent's estate are such only as represent personal obligations of the decedent existing at the time of his death, whether or not then matured, and interest thereon which had accrued at the time of death. Only interest accrued at the date of the decedent's death is allowable even though the executor elects the alternate valuation method under section 2032. Only claims enforceable against the decedent's estate may be deducted.

*Id.*

24. *See Smith*, 198 F.3d at 521 (explaining argument that regulation's temporal reference to time of death calls for date-of-death valuation standard).

25. *See* Jerry A. Kasner, *Postdeath Events and Supreme Court Review*, 93 TAX NOTES 958, 960 (2001) ("It appears the Supreme Court may finally decide this issue one day."). ***But see infra*** note 283 (discussing repeal of estate tax, and noting that the Supreme Court will likely postpone treatment of the issue until Congress determines whether to make the repeal permanent).

concern for a rule that avoids uncertainty and delay in estate administration.[26] Second, there is a need to divine Congress's intent in drafting § 2053(a) so as to avoid windfall awards to estates, while at the same time preserving the federal government's interest in encouraging certain deductions.[27]

This Note attempts to shed light on these policy concerns by analyzing the evolution of the doctrinal disarray of the law as it exists today and by discussing several discrete components of the debate that should factor into a determination of whether postmortem events should play a role in valuing deductions for claims against estates. Part II of this Note traces the historical evolution of the split between the circuits and evaluates the recent entry of the U.S. Courts of Appeals for the Tenth and Eleventh Circuits into the debate. Part III of this Note discusses three components of the debate that should weigh heavily on the courts' resolution of this issue. These components include: 1) the distinction between valuation and validity of claims; 2) the distinction between certain claims and those that are contested or contingent; and 3) the distinction between deductions for claims and deductions for other estate expenses, such as funeral and administrative expenses. Part IV of this Note provides a comparative analysis of statutory and judicial treatment of using hindsight in valuing assets for purposes of determining the value of the gross estate. This analysis focuses on the following: 1) the express language of the code and treasury regulations relating to the timing of such valuation, 2) the problems inherent in using hindsight to determine fair market value, and 3) the congressional carve-out of an alternate valuation date under § 2032. In conclusion, Part V reiterates the need for resolution of the debate in light of the public policy concerns involved.

## *II. Evolution of the Circuit Split*

Crucial to an understanding of the policy concerns underlying the need for resolution of this issue is an understanding of the evolution of the debate itself. Justice Holmes laid the foundation for the debate in 1929 by refusing to consider postmortem events in valuing a charitable deduction.[28] Later that same year the U.S. Court of Appeals for the Eighth Circuit declined the opportunity to extend Holmes's reasoning to the valuation of a deduction for

26. *See* Estate of McMorris v. Comm'r, 243 F.3d 1254, 1261–62 (10th Cir. 2001) (suggesting that date-of-death valuation rule "alleviates the uncertainty and delay in estate administration which may result if events occurring months or even years after a decedent's death could be considered in valuing a claim against the estate").

27. *See infra* note 185 and accompanying text (suggesting that date-of-death valuation results in windfalls to estates).

28. *See* Ithaca Trust Co. v. United States, 279 U.S. 151, 154–55 (1929) (refusing to consider postmortem events in valuing deduction for charitable contribution).

a claim against an estate.[29] From these two divergent decisions two camps emerged: one favoring the consideration of postmortem events in valuing deductions for claims against estates and another favoring a date-of-death valuation rule. At present, the courts seem to be leaning in favor of a date-of-death valuation rule, with four circuits favoring such an interpretation and only two opposing it.[30]

The remainder of Part II analyzes the evolution of this circuit split. This analysis commences with a discussion of the Holmes opinion that gave rise to the debate. The analysis continues by discussing the resulting divergence in the circuits regarding the role of postmortem events in valuing deductions for claims. The analysis concludes with a discussion of the recent entry of the Tenth and Eleventh Circuits into the debate in 2001.

### *A. Holmes Sets the Stage*

In *Ithaca Trust Co. v. United States*,[31] Justice Holmes set the stage for the current debate over the timing of the valuation of deductions of claims against estates.[32] In *Ithaca Trust*, the testator left a will creating a trust with his widow and the petitioner as trustees.[33] The will created an estate for life in the testator's widow such that she had "authority to use from the principal any sum 'that may be necessary to suitably maintain her in as much comfort as she now enjoys.'"[34] Furthermore, the will stipulated that upon the widow's death the remainder should go to several charities.[35] Six months after the testator's death, the widow died.[36]

The executor of the decedent's estate deducted the value of the charitable bequests pursuant to Section 403(a)(3) of the Revenue Act of 1919.[37] The

29. *See* Jacobs v. Comm'r, 34 F.2d 233, 236 (8th Cir. 1929) (declining opportunity to extend *Ithaca Trust* rule to deductions for claims against estates).

30. *See* Young, *supra* note 14, at B6 (noting that Fifth, Ninth, Tenth, and Eleventh Circuits favor date-of-death valuation rule, while Second and Eighth Circuits oppose this rule).

31. Ithaca Trust Co. v. United States, 279 U.S. 151 (1929).

32. *See id.* at 154–55 (holding that estate may deduct value of charitable remainder from life estate based on estimated value of this remainder computed as of date of death).

33. *Id.* at 154.

34. *Id.*

35. *Id.*

36. *Id.*

37. Section 403(a)(3) of the Revenue Act of 1919 is a predecessor of I.R.C. § 2055(a)(2), which provides for a deduction for bequests to charitable organizations. *See* Revenue Act of 1919, ch. 18, § 403(a)(3), 40 Stat. 1057, 1098 (current version at I.R.C. § 2055(a)(2) (2000)) (providing for deduction of "all bequests, legacies, devises, or gifts, to or for the use of . . . any corporation organized and operated exclusively for religious, charitable, scientific, literary, or

Government argued that the value of the deduction for the charitable bequests should be the actuarially determined value of those bequests as of the date of the testator's death.[38] The petitioner argued that because the widow died before the estate filed the return, the actual value of the bequests was known, and therefore the actual value of the bequests should determine the allowable deduction.[39] Justice Holmes agreed with the Government and held that the actuarially determined value of the bequests as of the testator's date of death should dictate the allowable deduction for the bequests irrespective of events occurring subsequent to the testator's death.[40]

At the core of Holmes's reasoning was the principle that facts ascertained after the occurrence of a taxable event play no role in influencing the taxable value of that event.[41] He stated, "The first impression is that it is absurd to resort to statistical probabilities when you know the fact. But this is due to inaccurate thinking. The estate so far as may be is settled as of the date of the testator's death."[42] He further stated, "Tempting as it is to correct uncertain probabilities by the now certain fact, we are of opinion that it cannot be done."[43] One commentator argued that the driving force behind Holmes's reasoning was that the alternative of requiring absolute certainty in computing the valuation of charitable deductions would completely undermine and discourage such deductions:

> A call for absolute certainty would doom the charitable deduction in all cases, for there is no such thing. Even if the estate is left outright to charity, it is always possible that something might happen to defeat charity's interest—at worst, the estate might be lost through investment reverses. The only question in *Ithaca Trust* was the degree of uncertainty that the system could reasonably tolerate.[44]

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educational purposes"). Sections 664 and 2055(e) now control the *valuation* of charitable remainder gifts. *See* I.R.C. § 664 (2000) (governing charitable remainder trusts); *id.* § 2055(e) (limiting deduction of charitable remainder gifts in certain circumstances).

38. *See Ithaca Trust*, 279 U.S. at 152 ("The findings of fact as to the . . . [actuarial value of the widow's life estate] took the amount of the residuary bequest out of the field of mere speculation and afforded a reasonable basis for determining its value and amount.").

39. *Id.* Because the widow died only six months after the testator, the actual value of the bequests was greater than their actuarially determined present value as of the date of death. The estate sought to use the actual value of the bequests because it would produce a more favorable deduction. *Id.*

40. *Id.* at 155.

41. *See id.* (holding that "the value of the thing to be taxed must be estimated as of the time when the act is done" even though subsequent events might alter the original valuation).

42. *Id.*

43. *Id.*

44. Leo L. Schmolka, *Income Taxation of Charitable Remainder Trusts and Decedents'*

Evidently, Holmes felt that the system could reasonably tolerate a substantial degree of uncertainty in the interest of encouraging charitable deductions.[45]

Justice Holmes rationalized his decision by painting the degree of uncertainty of the future value of the charitable bequests in a favorable light. He asserted:

> The principal that could be used was only so much as might be necessary to continue the comfort then enjoyed [by the widow]. The standard was fixed in fact and capable of being stated in definite terms of money. It was not left to the widow's discretion. The income of the estate at the death of the testator, and even after debts and specific legacies had been paid, was more than sufficient to maintain the widow as required. There was no uncertainty appreciably greater than the general uncertainty that attends human affairs.[46]

The facility with which Holmes found that it is possible to determine the present value of a deduction based on uncertain future events exemplifies how strongly he favored a firm date-of-death valuation rule. The accepted philosophy underlying use of a date-of-death valuation of charitable deductions for estate tax purposes is that "a decedent's philanthropy (and the estate's deduction) should be measured at the time of the decedent's death and not be affected by valuation changes that result from either a mere lapse of time or postmortem contingencies."[47] Any departure from a date-of-death valuation rule with regard to charitable deductions would necessarily result in fluctuating valuations that do not truly reflect the philanthropic intent of the decedent and might ultimately discourage such contributions.[48]

Although Justice Holmes closed the door on the potential of postmortem events affecting the valuation of deductions for charitable contributions, he did not expressly extend his reasoning in the *Ithaca Trust* case to any other deductions from the taxable estate.[49] By narrowly applying the date-of-death valuation rule, he left unanswered the question of whether his reasoning should apply to deductions for claims against estates. Those courts that apply the

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*Estates: Sixty-Six Years of Astigmatism*, 40 TAX L. REV. 1, 21–22 (1984).

45. *See Ithaca Trust*, 279 U.S. at 155 (finding it unnecessary to "correct uncertain possibilities by the now certain fact").

46. *Id.* at 154.

47. RICHARD B. STEPHENS ET AL., FEDERAL ESTATE AND GIFT TAXATION ¶ 5.05[3][b] (7th ed. 1997).

48. *See supra* text accompanying note 44 (commenting that certainty in valuation would discourage charitable deductions).

49. *See Ithaca Trust*, 279 U.S. at 154–55 (holding that postmortem events do not play a role in valuation of charitable deductions, but failing to address whether this rule applies to other estate deductions).

*Ithaca Trust* rule to claims do so under the premise that there is a logical relationship between deductions for claims and deductions for charitable contributions; those that reject the *Ithaca Trust* rule with respect to claims dismiss this premise and refuse to extend Holmes's opinion beyond the realm of deductions for charitable contributions.[50]

### *B. Circuit Courts Diverge*

The debate over the applicability of Holmes's rule beyond charitable deductions began only three months after *Ithaca Trust* when the U.S. Court of Appeals for the Eighth Circuit decided *Jacobs v. Commissioner*.[51] In *Jacobs*, a husband and wife executed an antenuptial contract under which the wife was to receive $75,000 from the husband's estate upon his death.[52] However, the husband included in his will a provision granting the wife the option of foregoing the $75,000 payment in favor of net income for life from $250,000 of her husband's estate.[53] The widow exercised this income option after her husband's death.[54] Nevertheless, the executor of the decedent's estate deducted $75,000 from the gross value of the estate.[55]

The estate asserted that the $75,000 deduction represented the value of a valid and enforceable claim by the widow against the estate as of the decedent's date of death, despite the widow's subsequent choice to exercise the income option.[56] The estate argued that pursuant to *Ithaca Trust* the value of the claim as it existed on the date of death should dictate the allowable deduction without regard to events occurring subsequent to death that alter this valuation.[57] The Government argued that because the widow exercised the income option, she effectively cancelled her claim to the $75,000 payment.[58]

The Eighth Circuit agreed with the Government and upheld the Commissioner's disallowance of this deduction.[59] In response to the estate's argument

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50. *See* John Zimmerman, *Claims Against the Estate: A Continuing Controversy*, 10 TAX MGMT. EST., GIFTS, & TR. J. 65, 66 (1985) (noting that courts rejecting date-of-death valuation distinguish *Ithaca Trust* because it involved deduction for charitable contribution).

51. *See* Jacobs v. Comm'r, 34 F.2d 233, 236 (8th Cir. 1929) (ruling that postdeath events can play role in valuing deductions for claims).

52. *Id.* at 233.

53. *Id.*

54. *Id.*

55. *Id.*

56. *Id.* at 234.

57. *Id.* at 236.

58. *See id.* at 234 (stating that "when the widow elected to accept the provision made for her in the will, her election 'canceled . . . the claim arising out of the antenuptial contract'").

59. *Id.* at 236.

that *Ithaca Trust* called for a date-of-death valuation for all allowable estate deductions, the *Jacobs* court refused to extend application of Holmes's opinion beyond the realm of charitable deductions.[60] The court noted that *Ithaca Trust* involved a dispute over a charitable deduction pursuant to § 403(a)(3) of the Revenue Act of 1919,[61] while the dispute in *Jacobs* involved a deduction pursuant to § 403(a)(1) of the Revenue Act of 1921,[62] relating to claims against an estate.[63] Thus, the court foreclosed the use of *Ithaca Trust*, at least in the Eighth Circuit, as a viable argument supporting a date-of-death valuation for claims against estates.[64]

The *Jacobs* court's refusal to apply *Ithaca Trust* beyond the realm of charitable deductions laid the foundation for the circuit split that remains today. The U.S. Courts of Appeals for the Second and Eighth Circuits subscribe to the *Jacobs* reasoning and consider postmortem events in determining valuation of deductions for claims.[65] The U.S. Courts of Appeals for the Fifth and Ninth Circuits are loyal to Holmes's reasoning in *Ithaca Trust* and refuse to consider postmortem events in determining the value of deductions for claims.[66] In 2001, the U.S. Courts of Appeals for the Tenth and Eleventh Circuits sided with the Fifth and the Ninth Circuits in refusing to consider

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60. *Id.*

61. Section 403(a)(3) of the Revenue Act of 1919 is a predecessor of I.R.C. § 2055(a)(2), which provides for a deduction for bequests to charitable organizations. *See* Revenue Act of 1919, ch. 18, § 403(a)(3), 40 Stat. 1057, 1098 (current version at I.R.C. § 2055(a)(2) (2000)) (providing for deduction of "all bequests, legacies, devises, or gifts, to or for the use of . . . any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes").

62. Section 403(a)(1) of the Revenue Act of 1921 is a predecessor of I.R.C. § 2053(a)(1)–(4), which provides for a deduction for funeral and administration expenses, claims, and unpaid mortgages. *See* Revenue Act of 1921, ch.136, § 403(a)(1), 42 Stat. 227, 279 (current version at I.R.C. § 2053(a)(1)–(4) (2000)) (providing for deduction of "such amounts for funeral expenses, administration expenses, claims against the estate, unpaid mortgages . . . [and] losses incurred during the settlement of the estate arising from . . . casualty, or from theft").

63. Jacobs v. Comm'r, 34 F.2d 233, 236 (8th Cir. 1929).

64. *See* Estate of Sachs v. Comm'r, 856 F.2d 1158, 1160 (8th Cir. 1988) (reaffirming Eight Circuit's support of rule announced in *Jacobs*, stating "[i]n this Circuit, however, the date-of-death principle of valuation does not apply to claims against the estate deducted under § 2053(a)(3)").

65. *See id.* (rejecting date-of-death valuation outside the realm of charitable bequests); Comm'r v. Estate of Shively, 276 F.2d 372, 375 (2d Cir. 1960) (same).

66. *See* Estate of Smith v. Comm'r, 198 F.3d 515, 526 (5th Cir. 1999) (supporting date-of-death valuation); Estate of Van Horne v. Comm'r, 720 F.2d 1114, 1117 (9th Cir. 1983) (same); Propstra v. United States, 680 F.2d 1248, 1257 (9th Cir. 1982) (same).

postmortem events.[67] A brief discussion of the leading cases from each circuit follows.

The leading Eighth Circuit case, following the directives of the *Jacobs* court in refusing to apply *Ithaca Trust*, is *Estate of Sachs v. Commissioner.*[68] In *Sachs*, the decedent gifted stock prior to his death to three trusts benefitting his grandchildren subject to a condition that the donees pay the gift tax.[69] After the death of the decedent, the appellee filed an estate tax return including the net value of the gifts in the gross value of the estate pursuant to § 2035(a), which requires inclusion in the estate's gross value of any gifts made by the decedent within three years prior to death.[70] Shortly after the appellee filed the return, however, another Eighth Circuit case held that estates must also include in their gross value the full amount of any gift tax, whether paid by the donor or by the donee.[71] As a result, the appellee paid the additional income tax arising from the payment of the gift tax by the donees and deducted this amount as a claim against the estate pursuant to § 2053(a)(3).[72] Two years later, a provision in the Tax Reform Act of 1984 resulted in forgiveness of the additional tax liability.[73]

The appellee argued that pursuant to *Ithaca Trust*, the value of the claim as of the date of death should control for purposes of valuing the estate's deduction even though this claim ceased to exist by reason of statutory amendment after the death of the decedent.[74] The Government argued that because the statutory amendment relieved the estate of the obligation to satisfy the claim, the deduction for the claim was invalid.[75] The court agreed with the Government and held invalid the appellee's initial § 2053(a)(3) deduction, reasoning that when an estate's tax liability ceases to exist, so too does its right to take a deduction for this liability.[76]

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67. *See* Estate of O'Neal v. United States, 258 F.3d 1265, 1276–77 (11th Cir. 2001) (supporting date-of-death valuation); Estate of McMorris v. Comm'r, 243 F.3d 1254, 1263 (10th Cir. 2001) (same).

68. *See Sachs*, 856 F.2d at 1163 (ruling that postdeath events play role in valuation).

69. *Id.* at 1159.

70. *Id.*

71. *See* Diedrich v. Comm'r, 643 F.2d 499, 505 (8th Cir. 1981) (holding that payment of gift tax by donees produces taxable income for donor).

72. *Sachs*, 856 F.2d at 1159.

73. *Id.*; *see* Tax Reform Act of 1984, Pub. L. No. 98-369, § 1026(a), 98 Stat. 494, 1031 (excluding from donor's gross income amounts attributable to donee's payment of gift tax).

74. *Sachs*, 856 F.2d at 1160.

75. *Id.* at 1159–60.

76. *Id.* at 1160.

The *Sachs* court relied heavily on the principles established in *Jacobs*, reaffirming that "[t]he date-of-death valuation principle adopted in *Ithaca Trust* is not universally applicable to other tax contexts."[77] The court found even more support for considering the postmortem event in this case than in *Jacobs* because the event was an act of Congress that retroactively extinguished the tax liability and therefore the claim.[78] Thus, *Sachs* established that the Eighth Circuit would remain firmly entrenched in its rejection of *Ithaca Trust* and in its support for the consideration of postmortem events in valuing deductions for claims against estates, except in cases of charitable bequests.

In *Commissioner v. Estate of Shively*,[79] the U.S. Court of Appeals for the Second Circuit joined the *Jacobs* bandwagon and rejected date-of-death valuation principles.[80] In *Shively*, a husband and wife entered into a separation agreement pursuant to which the husband (and his estate upon his death) would pay the wife $40 per week after their son turned twenty-one and until her remarriage.[81] The husband died in June of 1952, and the estate made payments until July of 1953, when the decedent's widow remarried.[82] The estate tax return filed by the respondent, also in July of 1953, included a deduction of $27,058.30, the actuarial present value as of the date of death of future payments due to the widow.[83] The actual value of payments made by the estate to the widow prior to her remarriage was only $2,079.96.[84]

The respondent argued that pursuant to *Ithaca Trust*, the actuarially determined present value of the payments to the widow as of the date of death should dictate the allowable deduction.[85] The Government argued that because the widow remarried prior to the filing of the estate return, the actual value of the payments due to the widow was known, and therefore the actual value of the payments should determine the allowable deduction.[86] The court agreed with the Government, holding that the respondent could deduct no

77. *Id.* at 1162.

78. *Id.* at 1162–63.

79. Comm'r v. Estate of Shively, 276 F.2d 372, 375 (2d Cir. 1960).

80. *See id.* (ruling that postmortem events do play role in valuation of deductions for claims against estates).

81. *Id.* at 373.

82. *Id.*

83. *Id.* at 374.

84. *Id.*

85. *Id.*

86. *Id.*

more than the actual amount paid to the widow while the estate was in probate and prior to her remarriage.[87]

However, the court's reasoning hinged not on an interpretation of *Ithaca Trust*, but rather on the language of § 812(b)(3), a predecessor to § 2053(a)(3), which permitted deductions for claims against an estate only to the extent that such claims are allowable by the laws of the jurisdiction under which the administration of the estate takes place.[88] Pursuant to Connecticut law, had the decedent's widow sought to enforce a claim for delinquent alimony payments, she would have been limited to the actual sum of alimony payments due and could not have sought to recover the actuarially determined present value of such payments as of the date of death.[89] As a result, the court held that if the actual amount of the claim is determinable pursuant to state law prior to the filing of the tax return by the estate, then the "estate may obtain under Section 812(b)(3) no greater deduction than the established sum, irrespective of whether this amount is established through events occurring before or after the decedent's death."[90] Thus, although the holding hinged on state law, *Shively* firmly established the Second Circuit's stance in favor of consideration of postmortem events in determining estate valuation.

However, in sharp contrast to the position of the Second and Eighth Circuits, is the strong support for a date-of-death valuation rule in the U.S. Court of Appeals for the Ninth Circuit. The two leading cases, *Propstra v. United States*[91] and *Estate of Van Horne v. Commissioner*, [92] manifest this circuit's refusal to consider postmortem events in determining deduction valuations.[93]

In *Propstra*, pursuant to § 2053(a)(3), the executrix of the decedent's estate deducted $202,423.05—the amount of liens outstanding as of the date

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87. *Id.* at 375.

88. *Id.* at 374; *see* Revenue Act of 1939, ch. 3, § 812(b), 53 Stat. 1, 123 (current version at I.R.C. § 2053(a) (2000)) (permitting deductions for claims against estates only "as are allowed by the laws of the jurisdiction, whether within or without the United States, under which the estate is being administered"). Section 2053(a)(3) contains identical language. I.R.C. § 2053(a)(3) (2000).

89. *See Shively*, 276 F.2d at 374 (observing that pursuant to "Connecticut law if she had received no support payments for the period subsequent to Shively's death and had been forced to prove her claim against the estate she would have been limited at the time the estate tax return was filed to payments due her prior to her remarriage").

90. *Id.* at 375.

91. Propstra v. United States, 680 F.2d 1248 (9th Cir. 1981).

92. Estate of Van Horne v. Comm'r, 720 F.2d 1114 (9th Cir. 1983).

93. *See id.* at 1117 (refusing to consider postmortem events in valuing deductions for claims against estates); *Propstra*, 680 F.2d at 1257 (same).

of death against the decedent's one-half ownership share of real property.[94] Almost two years later, the estate settled the claims with the lienholder in the amount of $134,826.23.[95] Shortly thereafter, the Commissioner assessed a deficiency against the estate, arguing that the estate could only deduct the amount actually paid to discharge the liens.[96] The appellee argued that the value of the claim as of the date of death should dictate the allowable deduction despite the postdeath settlement.[97]

The Ninth Circuit agreed with the appellee and held valid the date-of-death valuation of the deduction for the lien claims, even though the amount actually paid by the estate in settlement of the claims was less than the amount of the deduction.[98] Relying on *Ithaca Trust* and legislative history, the court held that postmortem events are irrelevant in determining the value of deductions for claims that are certain and enforceable at death.[99] The court determined that the lien claims were certain and enforceable as of the date of death and, therefore, held that the date-of-death valuation of the deductions for these claims controlled.[100] However, the court also suggested that postmortem events do play a role in valuation when such claims are contested or contingent.[101]

In *Van Horne*, a husband and wife entered into a divorce agreement stipulating that the wife or her estate would make monthly spousal support payments of $5,000 to the husband for life.[102] The wife's estate deducted $596,386.58 from gross value, which represented the actuarial present value of future payments to the surviving ex-husband.[103] The decedent's ex-husband died seven months after the decedent, having received only $35,000 in support payments.[104]

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94. *Propstra*, 680 F.2d at 1250.

95. *Id.*

96. *Id.*

97. *Id.* at 1249.

98. *Id.* at 1257.

99. *Id.* at 1254–56.

100. *Id.* at 1254.

101. *See id.* at 1253 ("The law is clear that post-death events are relevant when computing the deduction to be taken for disputed or contingent claims."). In arriving at this conclusion, the court referred to an earlier, identical version of Treas. Reg. § 20.2053-1(b)(3) that stated, "No deduction may be taken on the basis of a vague or uncertain estimate." Treas. Reg. § 20.2053-1(b)(3) (as amended in 1972); *see infra* subpart III.B (discussing differing treatment by courts of certain, contingent, and contested claims).

102. Estate of Van Horne v. Comm'r, 720 F.2d 1114, 1115 (9th Cir. 1983).

103. *Id.*

104. *Id.*

The Government argued that the allowable deduction should be only the actual value of payments made by the estate.[105] The petitioner argued that the actuarially determined date-of-death valuation of the claim should dictate the allowable deduction irrespective of the actual amount of payments received by the surviving spouse.[106] The Ninth Circuit agreed with the petitioner and ruled that the estate properly deducted the actuarial present value of the future payments.[107]

The court based its decision on a finding that the actuarial present value of the future payments constituted a certain and enforceable claim as of the date of death and that, consequently, postmortem events do not influence the valuation of the deduction.[108] Relying on *Propstra*, the court decreed that a "claim that is actuarily [sic] valued is not uncertain for estate tax purposes."[109] Because the court found the claim to be certain and enforceable as of the date of death, it upheld the petitioner's original valuation of the deduction.[110] Thus, *Propstra* and *Van Horne* establish that the Ninth Circuit supports a date-of-death valuation for deductions of claims that are certain and enforceable at death, but likely will consider postmortem events when valuation is contested or contingent.[111]

More recently, the U.S. Court of Appeals for the Fifth Circuit joined the Ninth Circuit in its support of a date-of-death valuation for estate claims deductions. In *Smith v. Commissioner*,[112] the court upheld the date-of-death valuation of a deduction for claims of alleged overpayment of royalties for oil and gas leases by Exxon to the decedent during her lifetime.[113] In *Smith*, the decedent, prior to her death, was a defendant in litigation initiated by Exxon.[114] Exxon overpaid the decedent royalties from oil and gas leases and initiated litigation in an attempt to recover this overpayment.[115] Subsequent

105. *Id.*

106. *Id.*

107. *Id.* at 1117.

108. *Id.* at 1116.

109. *Id.*

110. *Id.*

111. *See id.* (adopting reasoning announced in *Propstra*); Propstra v. United States, 680 F.2d 1248, 1253, 1257 (9th Cir. 1981) (finding that postmortem events do affect value of contingent or contested claims, but applying date-of-death standard to certain, enforceable claims).

112. Smith v. Comm'r, 198 F.3d 515 (5th Cir. 1999).

113. *See id.* at 526 (refusing to consider postmortem events in valuing deductions for claims against estates).

114. *Id.* at 517.

115. *Id.*

to the decedent's death, this litigation resulted in a judgment favorable to Exxon against the decedent in the amount of $2,482,719, and the petitioner-estate deducted this amount from the gross value of the estate.[116] The petitioner-estate later reached a settlement with Exxon in the amount of $681,840.[117]

The Government contended that because Exxon's claims were disputed as of the date of death, only the actual amount paid to settle the claim should dictate the value of the allowable deduction.[118] The petitioner argued that Exxon's claims were "enforceable contractual rights" as of the date of death and that, therefore, the date-of-death valuation of these claims should dictate the value of the allowable deduction, despite the subsequent settlement agreement.[119]

The Fifth Circuit agreed with the petitioner and remanded the case with instructions to recalculate the allowable deduction disregarding events occurring subsequent to death.[120] The court reasoned that although it is impossible to determine the precise value of a disputed claim prior to settlement or judgment, it is possible to determine an approximate value.[121] In support of this proposition, the court noted that "the Commissioner has considered himself capable of determining the value of a pending lawsuit in exact dollars and cents, even when the claim has not been reduced to judgment."[122] The court did not find the Ninth Circuit's distinction between certain, enforceable claims and contingent or contested claims to be controlling.[123] The court suggested that the difference between certain, enforceable claims, on the one hand, and contingent or contested claims, on the other, is one of semantics and that it is possible to arrive at a just valuation of a claim that is not certain and enforceable as of the date of death.[124]

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116. *Id.* at 519 n.7.

117. *Id.*

118. *Id.* at 521.

119. *Id.*

120. *Id.* at 526.

121. *Id.* at 525.

122. *Id.*

123. *Id.*; *see* Estate of Van Horne v. Comm'r, 720 F.2d 1114, 1116 (9th Cir. 1983) (adopting reasoning announced in *Propstra*); Propstra v. United States, 680 F.2d 1248, 1253, 1257 (9th Cir. 1981) (finding that postmortem events do affect value of contingent or contested claims, but applying date-of-death standard to certain, enforceable claims).

124. *See Smith*, 198 F.3d at 525 ("There is only a semantic difference between a claim that may prove to be invalid and a valid claim that may prove to have a value of zero."); *infra* subpart III.B (analyzing different treatment by courts of certain, contested, and contingent claims).

### *C. The Tenth and Eleventh Circuits Enter the Fray*

In two cases of first impression, the Courts of Appeals for the Tenth and Eleventh Circuits took up this issue in 2001, joining the Fifth and Ninth Circuits in their support of the *Ithaca Trust* rule. These recent opinions suggest that date-of-death valuation is gaining support and may be indicative of the future path of the law concerning deductions for claims.

In *Estate of McMorris v. Commissioner*,[125] the Tenth Circuit subscribed to the Fifth Circuit's refusal to treat certain, enforceable claims differently from those that are contested or contingent.[126] In *McMorris*, the petitioner-estate deducted $3,960,525 from its gross value, representing the decedent's income tax liability on the redemption of securities prior to death.[127] Subsequently, the petitioner challenged the Commissioner's valuation of the underlying securities and eventually reached a settlement with the IRS increasing the basis of the securities, thus eliminating the petitioner's tax liability altogether.[128] The petitioner sought a refund of the tax paid to satisfy the liability existing as of the date of death, and the Government sought disallowance of the petitioner's § 2053(a)(3) deduction.[129]

The petitioner argued that because the tax liability on the redemption of the securities was certain and enforceable, the date-of-death valuation of this liability should dictate the valuation of the allowable deduction.[130] The tax court, however, had ruled that the liability was no longer certain and enforceable once the petitioner challenged the Commissioner's valuation of the securities and that the subsequent settlement should control the valuation of the deduction.[131] The Tenth Circuit agreed with the petitioner and remanded the case with instructions to recalculate the allowable deduction disregarding events occurring subsequent to death.[132] Citing the policy concern of avoiding uncertainty and delay and noting that a date-of-death valuation rule has the potential to benefit either the government or taxpayers, the court rejected the

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125. Estate of McMorris v. Comm'r, 243 F.3d 1254 (10th Cir. 2001).

126. *See id.* at 1263 (refusing to consider postmortem events in valuing deductions for claims against estates).

127. *Id.* at 1256.

128. *Id.*

129. *Id.* at 1257.

130. *Id.*

131. *See id.* at 1262 ("The tax court reasoned that once the estate challenged Evelyn's tax liabilities, they were 'no longer a valid and enforceable claim against the estate.'" (quoting Estate of McMorris v. Comm'r, 77 T.C.M. (CCH) 1552, 1555 (1999))).

132. *Id.* at 1263.

Commissioner's argument that postmortem events should play a role in the valuation of deductions for claims against estates.[133]

Likewise, in *Estate of O'Neal v. Commissioner*,[134] the U.S. Court of Appeals for the Eleventh Circuit determined that the petitioner's date-of-death valuation should control despite a subsequent settlement with the IRS that reduced the amount of the claim outstanding against the estate.[135] In *O'Neal*, the decedent gifted two classes of stock in a family business to her children during her lifetime, determining the per share value to be $54 and $61.[136] Pursuant to an audit after the death of the decedent, the IRS determined the per share value to be $375 and $415, respectively.[137] Because the statute of limitations had expired, the Government was unable to assert a deficiency against the estate and thus asserted transferee gift tax liability against the donee children pursuant to § 6324.[138] The donees asserted claims against the estate for the full amount of the transferee gift tax liability, and the appellant deducted the amount of those claims from the gross value of the estate.[139] Subsequently, the donees reached a settlement with the IRS, arriving at per share values of $77 and $82, respectively.[140]

The Government contended that the value of the subsequent settlement should dictate the value of the allowable deduction because it "represents the actual amount of taxes ultimately paid."[141] The appellant argued that value of the Government's original claim, and not the value of the postdeath settlement, should dictate the value of the deduction.[142] The Eleventh Circuit agreed with the appellant and remanded the case with instructions to recalculate the allowable deduction disregarding events occurring subsequent to eath.[143] Following the lead of the Fifth and Tenth Circuits, the court sub-

133. *Id.* at 1261–62.

134. Estate of O'Neal v. Comm'r, 258 F.3d 1265 (11th Cir. 2001).

135. *See id.* at 1276–77 (refusing to consider postmortem events in valuing deductions for claims against estates).

136. *Id.* at 1267.

137. *Id.*

138. *Id.*

139. *Id.* at 1268.

140. *Id.*

141. *Id.* at 1271.

142. *Id.*

143. *Id.* at 1275. On remand, the District Court for the Northern District of Alabama determined that § 2053(c)(2) limits the allowable value of claims deductions to the value of the estate's assets as of the date of the decedent's death. Estate of O'Neal v. United States, 228 F. Supp. 2d 1290, 1305 (N.D. Ala. 2002); *see* I.R.C. § 2053(c)(2) (2000) (referring to § 2053(a) and (b) and providing that "there shall be disallowed the amount by which the deductions

scribed to the date-of-death rule announced in *Ithaca Trust*, but noted that the valuation of deductions for claims is not necessarily determined by the claimant's alleged deficiency existing as of the date of death.[144] Rather, the court suggested that lower courts should exercise "informed judgment, reasonableness and common sense, weighing all relevant facts and evaluating their aggregate significance" so as to arrive at a proper valuation for such deductions.[145] This suggests that the Eleventh Circuit contemplates a greater degree of judicial discretion in determining the proper valuation of deductions for claims.

In conclusion, the split in the circuits as to the propriety of considering postmortem events in valuing § 2053(a)(3) deductions for claims against estates reflects the doctrinal disarray of the law. Resolution of this issue, be it judicial or statutory, is clearly necessary to address the underlying policy concerns that are at stake. The following Part explores the discrete components of the debate in an attempt to identify those issues that are critical to the ultimate resolution of this problem by the courts or by Congress.

## *III. Components of the Debate*

In response to the debate over the valuation of deductions for claims, the courts have chosen to employ a bright-line rule either favoring consideration of postmortem events or foreclosing consideration of such events altogether.[146] Eventually some resolution favoring one rule or the other must be reached so that courts and executors alike will no longer have to grapple with the uncertainty and jurisdictional inconsistency of the law as it presently exists. Three primary components of this debate should factor into any resolution of this issue. The first component involves an analysis of the distinction between the valuation of deductions for claims versus the validity of such deductions, and the proper role of postmortem events as applied to these distinct issues.[147] The second component involves the disparate judicial treatment of claims that are certain and enforceable at death as compared to claims that are contested or

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specified therein exceed the value, at the time of the decedent's death, of property subject to claims"). Because this deduction reduced the value of the decedent's taxable estate to zero, the court ordered a refund of all estate taxes and interest paid by the estate. *O'Neal*, 228 F. Supp. 2d at 1305.

144. Estate of O'Neal v. Comm'r, 258 F.3d 1265, 1275 (11th Cir. 2001).

145. *Id.*

146. *See supra* Part II (discussing distinct circuit split, with one faction applying bright-line rule supporting date-of-death valuation and other faction supporting consideration of postmortem events).

147. *See infra* subpart III.A (analyzing distinction between valuation of deductions and validity of claims).

contingent.[148] The third component involves a comparative analysis of the role that postmortem events play in other estate deductions.[149]

### A. Deduction Valuation vs. Claim Validity

The first step in any judicial analysis of whether to consider postmortem events is an understanding of the distinction between the valuation of deductions and the validity of claims. Before any court can arrive at a reasonable determination of how to value deductions for claims against an estate, that court necessarily must determine whether the claim underlying that deduction is valid in the first place.[150] If the court finds the claim to be invalid, there is no reason to visit the question of valuation.[151] Thus, it is imperative that courts decide whether postmortem events should play a role in assessing the validity of a claim as well as in determining the proper valuation of deductions for such claims.

While some courts and scholars support the position that postmortem events dictate both the validity of claims and the valuation of deductions for claims, others favor the competing position that determinations of valuation and validity warrant separate consideration.[152] The first judicial treatment of this distinction arose in *Jacobs*.[153] The basis for the court's disallowance of the deduction in that case was a finding that no claim existed at the date of death or at any subsequent time because the appellant never affirmatively asserted a claim for the $75,000 payment.[154] The court noted, "The claims which Congress intended to be deducted were actual claims, not theoretical ones. Indeed, a claim without a claimant is a sort of legal figment, which has the tendency to produce intellectual dizziness . . . ."[155] The *Jacobs* court interpreted the statute[156] to mean that the allowance of a deduction for a claim

148. *See infra* subpart III.B (contrasting certain, enforceable claims with contested and contingent claims).

149. *See infra* subpart III.C (discussing valuation of other estate deductions).

150. *See* Treas. Reg. § 20.2053-4 (1958) ("Only claims enforceable against the decedent's estate may be deducted.").

151. If the court determines that the claim is not enforceable against the decedent's estate, there is no need to proceed any further with valuation analysis because Treas. Reg. § 20.2053-4 expressly disallows such claims. *Id.*

152. *See supra* note 17 (noting leading cases from circuits favoring date-of-death valuation rule); *supra* note 18 (noting leading cases from circuits rejecting date-of-death valuation rule).

153. *See* Jacobs v. Comm'r, 34 F.2d 233, 236 (8th Cir. 1929) (ruling that postdeath events should play role in valuing deductions for claims).

154. *Id.* at 235.

155. *Id.*

156. *See* Revenue Act of 1921, ch. 136, § 403(a)(1), 42 Stat. 227, 279 (current version at

against an estate hinges on the existence of a valid and enforceable claim as of the date of death and on the assertion of a right to that claim by an actual claimant.[157] The court considered postmortem events, specifically the widow's failure to assert a claim subsequent to the decedent's death, and determined that the initial deduction was invalid.[158] The court then applied the same reasoning in holding invalid the date-of-death valuation of the deduction for this claim.[159] Thus, *Jacobs* established the principle that courts should consider postmortem events in determining not only the valuation of deductions for claims, but also in determining the validity of such deductions.

The Treasury Department also subscribes to this logic, prohibiting deductions when the claimant waives payment, fails to file a claim within prescribed time limits, fails to follow proper filing procedures, or otherwise does not pursue a claim.[160] Under this reasoning, even if a court finds that a valid claim existed as of the date of death, a deduction for such a claim would be invalid absent an affirmative attempt to assert the claim.[161] This rule necessarily requires that executors and courts look to postmortem events in determining not only the valuation of deductions for claims, but also the validity of such claims.

However, opposition exists to this interpretation of the legislative intent underlying § 2053(a)(3).[162] Although the *Jacobs* opinion mandated the consideration of postmortem events in determining both the valuation and the validity of deductions for claims, there is support for considering the effect of postmortem events on valuation and validity separately.[163] Several courts

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I.R.C. § 2053(a) (2000)) (providing for deduction of "such amounts for funeral expenses, administration expenses, claims against the estate, unpaid mortgages . . . [and] losses incurred during the settlement of the estate arising from . . . casualty, or from theft").

157. *See Jacobs*, 34 F.2d at 235 ("It was, in our opinion, claims presented and allowed or otherwise determined as valid against the estate and actually paid or to be paid that Congress had in mind, when it provided for the deduction from the gross estate of 'claims against the estate' . . . .").

158. *Id.*

159. *Id.*

160. *See* Rev. Rul. 60-247, 1960-2 C.B. 272, 273 ("It is the position of the Internal Revenue Service that no deduction will be allowed for claims against the estate which have not been paid or will not be paid because the creditor waives payment, fails to file his claim . . . or otherwise fails to enforce payment.").

161. *Id.*

162. *See* STEPHENS ET AL., *supra* note 47, ¶ 5.03[5][b], at 5-25 n.121 (criticizing Treasury's interpretation in Revenue Ruling 60-247 and suggesting that "claims can exist at death and be perfectly bona fide and allowable even though the creditor never presses for, or even if the creditor expressly waives the right to, payment").

163. *See* JOHN A. BOGDANSKI, FEDERAL TAX VALUATION ¶ 2.01[3][c][iv], at 2-74 n.282

have expressed skepticism toward the current trend of aggregating the analysis of valuation and validity issues.[164] These courts separate valuation and validity issues into two discrete categories of cases, supporting the position that while postmortem events should play a role in determining the validity of a claim, they should not play a role in determining the valuation of a deduction.[165] When the validity of the claim is not at issue, these courts subscribe to the *Ithaca Trust* rule and refuse to consider postmortem events in determining the proper valuation of a deduction for a claim.[166] However, when the validity of the claim is at issue, these courts consider postmortem events in determining the validity of the claim, but not in determining the valuation of a deduction for that claim.[167]

Furthermore, although they hold the minority view, these courts support a facts-and-circumstances analysis on a case-by-case basis to determine which rule to apply. Remarking on the difficulty of reconciling these issues with a hard and fast rule, the Tax Court noted, "While we share the yearning for certainty in this area, we are not persuaded that a legislative solution is

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(6th ed. 1996) ("It has been suggested that postdeath events might be more worthy of consideration concerning the validity of a claim rather than its valuation.").

164. *See* Estate of Kyle v. Comm'r, 94 T.C. 829, 850–51 (1990) (espousing position that court should consider postdeath events in determining validity of claim, but not in determining valuation); Estate of Cafaro v. Comm'r, 57 T.C.M. (CCH) 1002, 1005–06 (1989) (separating valuation and enforceability issues into two separate categories of cases); Estate of Van Horne v. Comm'r, 78 T.C. 728, 737 (1982) (suggesting that while *Ithaca Trust* rule might not apply to validity of deductions, it does apply to valuation of deductions).

165. *See Cafaro*, 57 T.C.M. (CCH) at 1005–06 (identifying two separate standards for analyzing valuation and validity issues). The court stated:

> In sorting out the cases and seeking a unifying thread, we have found two broad categories of cases: (1) valuation cases where value is to be determined as of the date-of-death . . . and (2) enforceability cases where claims against the estate are only potential, unmatured, contingent, or contested at date-of-death so that of necessity courts must look to post-death evidence.

*Id.*; *see also Van Horne*, 78 T.C. at 737 ("It is one thing to distinguish *Ithaca Trust* in cases involving enforceability of a claimed debt, but to distinguish it here [as applied to valuation] would be to distinguish it to the point of extinction.").

166. *See Kyle*, 94 T.C. at 850 (noting that in *Van Horne*, the Tax Court held that "the general principle announced in *Ithaca Trust* is applicable in cases involving the valuation of claims against the estate"); *Cafaro*, 57 T.C.M. (CCH) at 1006 (declaring that "[f]or valuation issues, post-death events . . . are simply not relevant").

167. *See Kyle*, 94 T.C. at 851 ("The dispute in this case involves enforceability or validity of [a] claim, not just valuation of a valid claim. Thus we look to post-death events to determine whether the . . . claim was a valid claim against decedent's estate."); *Cafaro*, 57 T.C.M. (CCH) at 1006 (finding that because "the present case does not involve either a sum certain or a claim that was legally enforceable at the date of the decedent's death . . . evidence of post-death events is relevant here").

possible or desirable. We see the problem as an issue of relevance which trial judges must wrestle with depending upon the context and the facts of the particular case."[168]

However, some commentators argue that applying different rules in determining valuation and validity issues is untenable. One suggests that "in determining the fair market value of a claim for inclusion purposes, its apparent validity is certainly a relevant factor; thus, the distinction between enforceability and valuation seems strained."[169] At least two courts have also expressly rejected a two-pronged analysis.[170] Most notably, the Fifth Circuit remarked,

> Although this dichotomy, which distinguishes between enforceability on the one hand and valuation on the other, has superficial appeal, closer examination reveals that it is not a sound basis for distinguishing claims in this context. There is only a semantic difference between a claim that may prove to be invalid and a valid claim that may prove to have a value of zero.[171]

This seems to be the more reasoned analysis. Any court faced with determining the proper valuation of a deduction for a claim must first determine the validity of the underlying claim.[172] For two reasons, it seems counterintuitive to mandate consideration of postdeath events with regard to the validity of a claim and then to ignore such events in determining the proper valuation of a deduction for the same claim. First, in almost all situations, the same factors weigh on issues of both valuation and validity.[173] There is no effective mechanism to ensure that courts will not subconsciously apply these factors to one determination and not to the other. Second, for reasons of practicality

168. *Cafaro*, 57 T.C.M. (CCH) at 1006 n.6.

169. BOGDANSKI, *supra* note 163, ¶ 2.01[3][c][iv], at 2-74 n.282.

170. *See* Estate of McMorris v. Comm'r, 243 F.3d 1254, 1263 (10th Cir. 2001) (criticizing Tax Court's reliance on distinction between enforceability of claim on one hand and valuation of claim on the other); Estate of Smith v. Comm'r, 198 F.3d 515, 525 (5th Cir. 1999) (rejecting application of one rule for validity and application of another rule for valuation).

171. *Smith*, 198 F.3d at 525.

172. *See supra* notes 150–51 and accompanying text (noting that Treas. Reg. § 20.2053-4 expressly disallows deductions for unenforceable claims, thus obviating need for valuation analysis if court finds claim unenforceable).

173. Examples of the factors that influence judicial decisions include the following: 1) whether or not it is possible to determine the amount of the claim with precision, 2) whether determination of the amount of the claim requires the use of actuarial tables, 3) whether a claim that was enforceable as of the decedent's date of death becomes unenforceable after the decedent's death, 4) whether the claim is disputed, and 5) whether the claim is contingent. *See* Meresidis, *supra* note 3, at 2718–34 (examining factors courts face in addressing deductions for claims).

and consistency, arming courts with a hard and fast rule applicable to both valuation and validity determinations seems to be the more efficient solution.[174] For these reasons, whether the ultimate resolution of this issue results in a bright-line rule favoring consideration of postmortem events or one that prohibits consideration of such events, this rule should apply equally to determinations of the validity of claims and to determinations of the proper valuation of deductions for such claims.

### *B. Certain vs. Contingent or Contested Claims*

Closely related to this debate over validity and valuation is the distinction between certain, enforceable claims and those that are contingent or contested.[175] The courts have not been successful in establishing a uniformly applicable rule that differentiates between these claims, and unfortunately neither the code nor the treasury regulations provide much guidance on the issue. Treasury Regulation § 20.2053-4 prescribes, "The amounts that may be deducted as claims against a decedent's estate are such only as represent personal obligations of the decedent existing at the time of his death, whether or not then matured, and interest thereon which had accrued at the time of death."[176] Thus, claims that have not yet matured at the date of death are eligible for a deduction pursuant to the regulation.[177] Furthermore, Treasury Regulation § 20.2053-1(b)(3) provides, "An item may be entered on the return for deduction though its exact amount is not then known, provided it is ascertainable with reasonable certainty, and will be paid. No deduction may be taken upon the basis of a vague or uncertain estimate."[178] This regulation permits the deduction of a claim even if it is impossible to assign an exact value to the claim so long as the estate can reasonably estimate its value.[179] Neither regulation expressly prohibits deductions for contested or contingent

174. *See McMorris*, 243 F.3d at 1261–62 (observing that bright-line rules bring "more certainty to estate administration, an ideal which has long been promoted by judge and commentator alike"); Comm'r v. Estate of Shively, 276 F.2d 372, 376 (2d Cir. 1960) (Moore, J., dissenting) ("In the field of estate tax law it is particularly important that there be as much certainty as possible."); Robert Clive Jones, *Estate and Income Tax: Claims Against the Estate and Events Subsequent to Date-of-Death*, 22 UCLA L. REV. 654, 681 (1975) (arguing that "the current approach to timing the valuation of claims must be made more certain and consistent").

175. *See* Meresidis, *supra* note 3, at 2718–22 (discussing certain, enforceable claims); *id.* at 2725–28 (discussing disputed claims); *id.* at 2732–34 (discussing contingent claims).

176. Treas. Reg. § 20.2053-4 (1958).

177. *See* Kasner, *supra* note 25, at 960 (noting potentially conflicting interpretations of regulations regarding contingent and contested claims).

178. Treas. Reg. § 20.2053-1(b)(3) (as amended in 1972).

179. *See* Kasner, *supra* note 25, at 958 (noting that Treasury Regulation 20.2053-1(b)(3) "requires only that [the claim] can be valued with reasonable certainty and will be paid").

claims,[180] and no regulation speaks to the propriety of considering postmortem events in valuing such claims. Therefore, central to the debate over consideration of postmortem events is the proper treatment of certain, contingent, and contested claims.

Paralleling the circuit split is the debate over the propriety of considering postmortem events with respect to claims that are certain and enforceable at death.[181] Problems arise in two distinct scenarios. First, there is disagreement as to the validity of a deduction when the creditor fails to pursue the claim[182] or cannot pursue the claim for procedural reasons.[183] Second, there is disagreement as to the validity of a deduction when a postdeath event alters the value of the claim.[184]

Mandating consideration of postmortem events under the first scenario certainly seems plausible. When a certain and enforceable claim exists at death and the creditor never asserts a right to that claim or cannot assert such a right for procedural reasons, it is arguable that permitting a deduction for the claim would result in a windfall to the estate.[185] This is decidedly the view of

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180. *See id.* ("Under the regulations, it is clearly not a requirement that the claim in question be 'matured' at the date of death; it is also not clearly necessary to determine whether the claim is subject to contingencies or disputes.").

181. *Compare* Estate of Van Horne v. Comm'r, 720 F.2d 1114, 1116 (9th Cir. 1983) (holding actuarially determined value of claim to be certain, and thus refusing to consider postdeath events that alter value), *and* Propstra v. United States, 680 F.2d 1248, 1254 (9th Cir. 1982) (holding that "as a matter of law, when claims are for sums certain and are legally enforceable as of the date-of-death, post-death events are not relevant in computing the permissible deduction"), *with* Estate of Sachs v. Comm'r, 856 F.2d 1158, 1159 (8th Cir. 1988) (holding invalid deduction for tax liability that was certain and enforceable on death, but subsequently relieved by amendment to tax laws), *and* Jacobs v. Comm'r, 34 F.2d 233, 235 (8th Cir. 1929) (refusing to uphold deduction that was certain and enforceable on death, but never enforced).

182. A creditor may choose not to pursue a claim because another party is primarily (or jointly) liable or because other property secures the claim. 5 BORIS I. BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS ¶ 131.4.2, at 131-22 n.20 (2d ed. 1993). For an example, see Schiffman v. United States, 51 F. Supp. 728, 732 (Ct. Cl. 1943) (denying deduction for claim after creditor restructured loan with other guarantors).

183. An example of a procedural default is the failure of a creditor to present a claim within the temporal parameters of the statute of limitations. 5 BITTKER & LOKKEN, *supra* note 182, ¶ 131.4.2.

184. *Compare* Estate of O'Neal v. United States, 258 F.3d 1265, 1266, 1268 (11th Cir. 2001) (ruling that deduction based on date-of-death valuation was valid although parties settled claim for lesser amount subsequent to death) *with* Comm'r v. Estate of Shively, 276 F.2d 372, 373–75 (2d Cir. 1960) (ruling that deduction based on date-of-death valuation was not valid because estate's ultimate liability was less than 10% of the value of the deduction).

185. *See* William L. Raby & Burgess J.W. Raby, *Post-Death Events and Claims Against Estates*, 91 TAX NOTES 105, 106 (2001) (observing that permitting estates to deduct claims that

those circuits that favor consideration of postmortem events in determining the proper valuation of deductions for claims.[186] Nonetheless, those circuits holding the opposing view allow a deduction based on a date-of-death valuation even if it results in a windfall to the estate.[187] As an example of one means of rationalizing this view, the U.S. Court of Appeals for the Ninth Circuit pointed to the language of Treasury Regulation § 20.2053-4, which states in part, "Only claims enforceable against the decedent's estate may be deducted."[188] The Ninth Circuit noted that this regulation "speaks of 'enforceable' rather than 'enforced' claims" as a basis for allowing deductions for claims never pursued by the creditor.[189] Thus, in spite of the potential for windfalls to estates, disagreement as to the appropriate treatment of unenforced claims that are certain and enforceable still exists.

Mandating consideration of postmortem events under the second scenario[190] presents equally challenging problems. When a postmortem event alters the value of a claim that was certain and enforceable at death, the potential for a windfall to an estate also exists.[191] Those circuits favoring consideration of postmortem events in valuing deductions for claims refuse to enable this potentiality absent a clear mandate from Congress.[192] Yet there is also support for a rule that addresses the public policy issue of reducing uncertainty and delay in estate administration.[193] The bright-line rule favoring consider-

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will not be paid constitutes windfall in certain cases). For a discussion of whether a deduction for a claim that is never paid constitutes income to the estate, see generally 1 BITTKER & LOKKEN, *supra* note 182, ¶ 5.7.

186. *See Jacobs*, 34 F.2d at 235 ("It was, in our opinion, claims presented and allowed . . . and actually paid or to be paid that Congress had in mind, when it provided for the deduction . . . .").

187. *See* Propstra v. United States, 680 F.2d 1248, 1254–56 (9th Cir. 1982) (adhering to strict interpretation of statute, and relying on interpretation of legislative intent to validate date-of-death rule, even when claim is never enforced).

188. *Id.* at 1255 (citing Treas. Reg. § 20.2053-4 (1958)).

189. *Id.*

190. *See supra* note 184 and accompanying text (noting disagreement over validity of claim when postdeath events alter value of claim).

191. If, for example, a creditor holds a certain, enforceable claim for an unpaid debt against an estate as of the date of the decedent's death and the executor settles this claim subsequent to the decedent's death for a lesser amount, the estate realizes a windfall under a date-of-death valuation rule. *See* Meresidis, *supra* note 3, at 2705 (providing hypothetical illustration of how date-of-death rule results in windfalls to estates).

192. *See* Estate of Sachs v. Comm'r, 856 F.2d 1158, 1163 (8th Cir. 1988) (invalidating deduction for tax liability relieved by amendment to tax laws, and suggesting that "Congress may grant windfalls to taxpayers if it wishes, but it would take a much clearer expression than what we have here to convince us that it intended to do so").

193. *See supra* note 174 (providing examples of courts and commentators critical of

ation of postmortem events does not establish any basis for determining temporal limitations when applying the rule. An estate that takes a deduction for a certain and enforceable claim existing as of the date of death might subsequently face the prospect of disallowance of that deduction long after the completion of estate administration.[194] Such a result might work a severe hardship on individual executors, and furthermore, it undermines the strong public policy concern for efficient and timely administration of estates.[195] If the courts ultimately choose to consider postmortem events in valuing deductions for claims, they would best serve public policy by encouraging the legislature to define a reasonable period of limitation restricting such considerations after a certain length of time.[196]

The law is in even greater disarray with regard to contingent or contested claims. Those favoring consideration of postdeath events with regard to contingent or contested claims base their argument on the proposition that it is impossible, without looking to postdeath events, to value a claim that is contingent upon a postdeath event or that is contested as of the date of death.[197] The opposing position favors the consideration of the contingencies or disputes involved to determine a reasonable deduction valuation, but does not mandate resolution of the contingency or dispute as a prerequisite to sustaining that valuation.[198]

Perhaps most illustrative of the contentious nature of this debate is the IRS response to the decision of the U.S. Court of Appeals for the Fifth Circuit in *Estate of Smith v. Commissioner*.[199] The deduction at issue in *Smith* involved a claim by Exxon for royalties from oil and gas leases.[200] As of the date of the decedent's death, the parties were litigating the claim, and, therefore, the value of the claim was contingent upon the ultimate outcome of the litigation.[201]

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uncertainty, delay, and inconsistency in estate administration).

194. *See Sachs*, 856 F.2d at 1159 (invalidating deduction two years after filing of estate return); Comm'r v. Estate of Shively, 276 F.2d 372, 373–74 (2d Cir. 1960) (invalidating deduction eight full years after decedent's death and seven years after estate filed return).

195. *Cf.* Madden & Hayes, *supra* note 15, at 550 ("We believe that creating an arbitrary rule for claims that prohibits consideration of post-death events does not speed up the preparation or processing of an estate tax return, or make the system significantly fairer.").

196. Legislating a suitable statute of limitations would prove challenging. Opponents would attack as arbitrary any proposed temporal cut-off for consideration of postdeath events.

197. *See* Kasner, *supra* note 25, at 958 (discussing competing arguments regarding contingent and contested claims).

198. *See id.* (same).

199. Estate of Smith v. Comm'r, 198 F.3d 515 (5th Cir. 1999), *nonacq.*, 2000-1 C.B. xvi.

200. *Id.* at 518–20.

201. *Id.* at 519.

Reversing a Tax Court decision[202] that limited the deduction to the amount actually paid to settle the claim, the Fifth Circuit relied on Ninth Circuit precedent in ruling that the date-of-death valuation should stand.[203]

The IRS later announced its nonacquiescence to the *Smith* decision.[204] In an Action on Decision explaining its nonacquiescence, the IRS pointed out that the Ninth Circuit cases upon which the *Smith* court relied involved certain, enforceable claims and not contingent or contested claims.[205] This distinction finds support in the case law. The Ninth Circuit itself expressly supported consideration of postdeath events with respect to contingent or contested claims.[206] This dispute suggests that, at least in the Ninth Circuit, there are two separate rules: first, a rule that prohibits consideration of postdeath events when the deduction is for a certain, enforceable claim and, second, a rule that permits consideration of postdeath events when the deduction is for a contested or contingent claim. In its Action on Decision, the IRS noted, "Every court, except the Fifth Circuit, that has addressed the . . . issue where the claim is contested, contingent, or unenforceable on the date-of-death, has considered postdeath events in determining the allowable deduction."[207]

This dispute between the Fifth Circuit and the IRS suggests a potentially viable resolution to the issue. When an estate deducts the value of a claim that is certain and enforceable on death, courts should not look to postdeath events in determining the propriety of that valuation. However, when the deduction is for a contingent or contested claim, courts should consider postmortem events. Unfortunately, this solution does not account for the potential of

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202. *See* Estate of Smith v. Comm'r, 108 T.C. 412, 419 (1997) ("Where a claim is disputed, contingent, or uncertain as of the date of the decedent's death, the estate is not entitled to a deduction until the claim is resolved and it is determined what amount, if any, will be paid."), *rev'd*, 198 F.3d 515 (5th Cir. 1999).

203. The court cited *Propstra v. United States*, 680 F.2d 1248 (9th Cir. 1982), and *Estate of Van Horne v. Commissioner*, 720 F.2d 1114 (9th Cir. 1983), for the proposition that a date-of-death valuation should apply to deductions for claims that are certain and enforceable at death. *Smith*, 198 F.3d at 522–23.

204. 2000-1 C.B. xvi.

205. *See* I.R.S. Action on Decision 2000-04 (May 9, 2000), 2000 AOD LEXIS 4, at *5 (noting that Ninth Circuit cases relied on by court "involved claims that were certain and enforceable at death, and in both cases, the Ninth Circuit limited its holding to 'certain and enforceable' claims").

206. *See Van Horne*, 720 F.2d at 1116–17 (adopting rule announced in *Propstra*); *Propstra*, 680 F.2d at 1253 ("The law is clear that post-death events are relevant when computing the deduction to be taken for disputed or contingent claims.").

207. 2000 AOD LEXIS 4, at *5. The IRS cited as support *Gowetz v. Commissioner*, 320 F.2d 874 (1st Cir. 1963), *Estate of Jacobs v. Commissioner*, 34 F.2d 233 (8th Cir. 1929), *Estate of Cafaro v. Commissioner*, 57 T.C.M. (CCH) 1002 (1989), *Estate of Courtney v. Commissioner*, 62 T.C. 317 (1974), and *Taylor v. Commissioner*, 39 T.C. 371 (1962). 2000 AOD LEXIS 4, at *5–6.

windfalls to estates when the value of certain and enforceable claims decreases as a result of postdeath events, but it does address the policy interest of avoiding uncertainty and delay in estate administration.[208]

One commentator proposes a more complex rule that would also distinguish between contingent and contested claims. Jerry Kasner suggests:

> If the claim is contingent, then it should be valued on the basis of facts known at the date of death, and the unresolved contingency would be a factor in that value. If the claim is contested, then the validity of any deduction, and certainly the amount, may depend on postdeath events. Even in this case, the law does not assume the final payment determines the actual amount of the deductible claim, although it is strong evidence of its value at the date of death.[209]

While this argument has superficial appeal, it is susceptible to attack on two fronts. First, it assumes that there is a reliable way for courts to derive a date-of-death valuation.[210] Second, precise differentiation of "contested" and "contingent" claims may prove challenging in many circumstances.[211] For practical reasons, it seems more reasonable to have a single rule that applies to both contingent and contested claims.[212]

The dispute between the IRS and the Fifth Circuit suggests that the ultimate resolution of this issue will include a rule that permits consideration of postmortem events in valuing deductions for contingent or contested claims, but prohibits consideration of such events in valuing deductions for certain, enforceable claims.[213] This is probably the most reasonable and equitable solution, but it is vital that the courts fashion the rule in such a way as to minimize windfalls to estates.

### *C. Deductions for Claims vs. Other Estate Deductions*

Another controversial aspect of the debate over considering postmortem events is the fact that other deductions permitted pursuant to § 2053(a) neces-

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208. *See supra* note 174 (providing examples of courts and commentators critical of uncertainty, delay, and inconsistency in estate administration).

209. Kasner, *supra* note 25, at 960.

210. *See* Meresidis, *supra* note 3, at 2712 (observing that it is often very difficult to ascertain the value of a contingent claim, such as a tort claim, with any precision).

211. *See* Estate of Smith v. Comm'r, 198 F.3d 515, 525 (5th Cir. 1999) (dismissing as unsound the basis used by the Tax Court in drawing distinction between certain, enforceable claims and disputed or contingent claims).

212. *See id.* (criticizing use of different standards for different types of claims).

213. *See supra* notes 204-08 and accompanying text (discussing IRS response to *Smith*, and noting possibility that hybrid rule will emerge favoring date-of-death valuation for certain, enforceable claims, but not for contested or contingent claims).

sarily require analysis of events occurring subsequent to death. Specifically, that section permits the estate to deduct the value of funeral expenses and estate administration expenses.[214] The estate cannot definitively value these expenses as of the date of death. Proponents of a rule authorizing consideration of postmortem events with respect to claims proffer an interesting argument. They argue that because Congress included the provision governing claims deductions in the same code section as the provisions governing funeral and administration expenses, which necessarily mandate consideration of postdeath events, Congress intended that postdeath events also be a factor in valuing deductions for claims.[215] Proponents of a date-of-death valuation rule argue that the legislative history does not support such an interpretation and note that § 2053(a) also contains a provision for the deduction of unpaid mortgages,[216] a value that is readily ascertainable in most circumstances without regard to postdeath events.[217]

One pair of commentators aptly refers to this argument as "the 'guilt by association' approach to discerning congressional intent."[218] Under this approach, opponents of a date-of-death valuation assert that although legislative intent is not clear with regard to claims, it is clear with regard to funeral and administration expenses, and, consequently, courts should infer that postmortem events play a role in valuing all deductions permitted under § 2053(a). The Eighth Circuit, in *Jacobs*, was the first court to lend credence to the "guilt by association" argument.[219] The *Jacobs* court, in support of its belief that valuation of claims should not rely on facts only existing at the date of death, boldly asserted that the Supreme Court "has not said that the deductions authorized by paragraph (1) of section 403 must be determined solely by the facts and conditions existing on the day of the death, and we are confident

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214. *See* I.R.C. § 2053(a)(1)–(2) (2000) ("[T]he value of the taxable estate shall be determined by deducting from the value of the gross estate such amounts—(1) for funeral expenses, [and] (2) for administration expenses . . . .").

215. *See* Raby & Raby, *supra* note 185, at 106 (discussing "guilt by association" argument that if Congress supported date-of-death valuation, it would not have included provision for claims deductions in § 2053(a)).

216. *See* I.R.C. § 2053(a)(4) (2000) (permitting deduction "for unpaid mortgages on, or any indebtedness in respect of, property where the value of the decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate").

217. *See* Estate of McMorris v. Comm'r, 243 F.3d 1254, 1261 (10th Cir. 2001) (commenting that "we find it insignificant that Congress placed funeral and estate administration expenses, which are calculated after death, with claims against the estate in section 2053(a), because that section also contains a deduction for unpaid mortgages, which may be calculated without reference to post-death events").

218. Raby & Raby, *supra* note 185, at 106.

219. *See* Jacobs v. Comm'r, 34 F.2d 233, 236 (8th Cir. 1929) (analyzing legislative intent with regard to claims, funeral expenses, and estate administration expenses).

that [C]ourt will never say so."[220] The *Jacobs* court went on to note that "[a]ll these, funeral expenses, administration expenses, and claims against the estate, under this paragraph, were intended by Congress to be determined in the course of an orderly administration of the estate in and by state courts."[221] In support of its interpretation of the legislature's intention that postmortem events should play a role in valuation, the court noted that Section 405 of the Revenue Act of 1921 directs the government to prepare the estate return when an estate fails to file a return or if an estate return misrepresents a material fact.[222] Without providing any statutory or judicial support, the court summarily interpreted this to mean that the government should look to postmortem events when preparing a return pursuant to Section 405.[223] The logic of the court's reasoning is flawed. Section 405 of the Revenue Act of 1921 only speaks to the fact that Congress authorized preparation of returns by the collector in certain circumstances.[224] The statute contains no language indicating a preference for considering postmortem events in determining the valuation of deductions in the course of such preparation of returns.[225] Without more concrete support, the court's decision to read into the statute a requirement of considering postmortem events seems untenable. Furthermore, there is no indication of a preference for considering postmortem events in the code's current counterpart to Section 405, even though Congress has had more than eighty years to amend the language of that section to indicate such intent.[226] For these reasons, the

220. *Id.* The *Jacobs* court was referring to Section 403 of the Revenue Act of 1921. *See* Revenue Act of 1921, ch. 136, § 403(a)(1), 42 Stat. 227, 279 (current version at I.R.C. § 2053(a) (2000)) (permitting deductions for funeral expenses, administration expenses, claims, unpaid mortgages, and casualty losses incurred during settlement of estate). History has shown that this statement was not so bold. The Supreme Court has not ruled on the issue in the seventy-four years that have lapsed since the *Jacobs* opinion.

221. *Jacobs*, 34 F.2d at 236.

222. *Id.*; *see* Revenue Act of 1921, § 405 (current version at I.R.C. § 6020(b)(1) (2000)) (directing government to prepare return in certain circumstances). This provision states in relevant part:

> [I]f no administration is granted upon the estate of a decedent, or if no return is filed as provided in section 404, or if a return contains a false or incorrect statement of a material fact, the collector or deputy collector shall make a return and the Commissioner shall assess the tax thereon.

*Id.*

223. *Jacobs*, 34 F.2d at 236.

224. Revenue Act of 1921, § 405(a)(1) (current version at I.R.C. § 6020(b)(1) (2000)).

225. *Id.*

226. *See* I.R.C. § 6020(b)(1) (2000) ("If any person fails to make any return required by any internal revenue law or regulation made thereunder at the time prescribed therefore, or makes, willfully or otherwise, a false or fraudulent return, the Secretary shall make such return from his own knowledge and from such information as he can obtain through testimony or

language of Section 405 has no bearing whatsoever on the role of postmortem events in valuing deductions for claims, and as a result, the *Jacobs* court's reliance on this section was misplaced.

Those opposing the "guilt by association" approach attack not only their opponents' attenuated interpretation of legislative intent, but also offer three other persuasive arguments. First, they point out that § 2053(a) also contains a provision for the deduction of unpaid mortgages, the value of which is determinable without consideration of postmortem events.[227] Second, they assert that consideration of postmortem events in valuing deductions is contrary to the estate tax's underlying purpose: taxation of the estate as it exists at the moment of death.[228] One commentator even goes so far as to claim that decisions rejecting a date-of-death valuation "fly in the face of early precedent and are inconsistent with the obvious purpose of the estate tax to measure the taxable estate at death, except where Congress clearly elects to recognize post-death events."[229] Third, they point to other parts of the code as evidence that when Congress intends the consideration of postmortem events, it manifests this intention clearly and unequivocally.[230]

The argument against the "guilt by association" approach to congressional intent seems to be the more reasonable interpretation. An attempt to draw inferences about legislative intent based on the provisions contained within the same code section as the rule at issue is unpersuasive. In other parts of the code, if it is not obvious that postdeath events should play a role, Congress has been clear in expressing its intentions as to whether consideration of such events is appropriate.[231] Of course, it is plausible that omission of any direc-

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otherwise.").

227. *See* Estate of McMorris v. Comm'r, 243 F.3d 1254, 1261 (10th Cir. 2001) (arguing that Congress would not have included deduction for unpaid mortgages in § 2053(a) if it intended consideration of postmortem events for all deductions in that section).

228. *See* STEPHENS ET AL., *supra* note 47, ¶ 5.03[5][b] (rejecting consideration of postmortem events in valuing deductions as contrary to policy underlying estate tax generally).

229. *Id.*

230. *See* Propstra v. United States, 680 F.2d 1248, 1256 (9th Cir. 1982) ("Moreover, except with regard to matters like funeral and administrative expenses, which by their very nature require valuation after a decedent's death, Congress has been explicit in providing for consideration of post-death events."). The *Propstra* court offered as examples § 2013, § 2032, and § 2054 of the tax code, all of which contain valuation schemes that require consideration of postmortem events. *Id.*; *see* I.R.C. § 2013 (2000) (requiring consideration of postdeath events in computation of credit for tax on prior transfers); *id.* § 2032 (requiring consideration of postdeath events for estates electing alternate valuation of assets); *id.* § 2054 (requiring consideration of postmortem events in computing deductions for casualty losses occurring during estate administration).

231. *See supra* note 230 (discussing examples of other code sections in which Congress has clearly manifested its intent that postdeath events play role in valuation).

tion as to consideration of postdeath events in valuing deductions for claims against estates was simply an oversight. However, in the seventy-four years since Holmes's decision in *Ithaca Trust*, Congress has done nothing to correct this oversight.[232] It is more likely that Congress simply views this issue as a hot potato more appropriate for judicial determination.

## *IV. Postmortem Events and Asset Valuation*

Unfortunately, the issue of valuation of § 2053(a)(3) deductions is indeed a hot potato thus far beyond the reach of judicial resolution. From what quarter, then, will come relief from the uncertainty and delay in estate administration caused by the current disarray of the law? One component of the debate largely ignored thus far by the courts and scholars alike in determining the proper timing for valuing deductions for claims is a comparative analysis of the role that postmortem events play in the valuation of assets for estate tax purposes. Similar policy concerns underlie both issues, and the principles governing the role of postmortem events in determining asset valuation should factor into the debate over the role of such events in the valuation of deductions for claims.[233]

As a general proposition, postmortem events do not play a role in asset valuation for purposes of determining the value of the gross estate. First, the language of the statutes and the regulations governing computation of the gross estate contain express language mandating a date-of-death valuation.[234] Second, the accepted practice of determining the fair market value of assets involves determining the consideration a willing buyer would pay a willing seller for that asset on a particular date.[235] Because the theoretical buyer and seller do not have the benefit of hindsight in determining the proper valuation of an asset, courts typically refuse to consider postmortem events in valuing assets.[236] Third, the code provides for an alternate valuation date for assets in limited circumstances.[237] The existence of this provision lends credence to an

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232. *Supra* note 220.

233. *See* Burgess J.W. Raby & William L. Raby, *Seize the Day—Valuation and Post-Death Events*, 1999 TAX NOTES TODAY 249-21, ¶ 18 ("Every tax practitioner knows that estates are taxable on the value of the assets the decedent owned . . . . That value is determined as of the date of death or the alternate valuation date, if elected. Claims against the estate should logically be treated in the same manner.").

234. *See infra* subpart IV.A (discussing express language of code and treasury regulations mandating date-of-death valuation).

235. *See infra* subpart IV.B (discussing "fair market value" doctrine).

236. *See infra* subpart IV.B (explaining courts' refusal to consider "hindsight" when valuing estate assets).

237. *See infra* subpart IV.C (discussing alternate valuation date provision of § 2032).

interpretation that postmortem events should play a role in valuing assets only if expressly permitted by Congress.

### *A. Express Language of the Statutes and Regulations*

As a practical matter, the most persuasive argument against considering postmortem events when valuing assets is the plain language of the statutes and regulations governing computation of the gross estate. With the exception of the alternate valuation election in § 2032, virtually every code section and treasury regulation that relates to the gross estate contains language expressly prescribing the date of death as the time for valuation.[238] Such express language weighs heavily against the argument that postmortem events should play a role in valuing assets and determining the value of the gross estate.

Section 2031 of the code provides a definition of "gross estate."[239] That section states in part that "[t]he value of the gross estate of the decedent shall be determined by including to the extent provided for in this part, the value *at the time of his death* of all property, real or personal, tangible or intangible, wherever situated."[240] The treasury regulations accompanying § 2031 further provide, "The value of every item of property includible in a decedent's gross estate . . . is its fair market value *at the time of the decedent's death*, except that if the executor elects the alternate valuation method under section 2032, it is the fair market value" as of the alternate valuation date prescribed by that section.[241]

Section 2033 of the code governs the inclusion of the decedent's property interests in the gross estate. This section states, "The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent *at the time of his death*."[242] The treasury regulations accompanying § 2033 further provide:

> The gross estate of a decedent who was a citizen or resident of the United States *at the time of his death* includes under section 2033 the value of all property, whether real or personal, tangible or intangible, and wherever situated, beneficially owned by the decedent *at the time of his death*.[243]

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238. *See* I.R.C. §§ 2031–46 (2000) (governing valuation of gross estate). The only tax code provision other than § 2032 that expressly provides for a valuation adjustment based on postmortem events is § 2031(c)(9), which provides for the allowance of a deduction for qualified conservation easements granted to the estate after decedent's death, but before the estate return due date. *Id.* § 2031(c)(9).

239. *See id.* § 2031 (defining "gross estate").

240. *Id.* § 2031(a) (emphasis added).

241. Treas. Reg. § 20.2031-1(b) (as amended in 1965) (emphasis added).

242. I.R.C. § 2033 (2000) (emphasis added).

243. Treas. Reg. § 20.2033-1(a) (as amended in 1963) (emphases added).

Similar language prescribing the date of death as the measure for valuation appears in other sections of the code relating to computation of the gross estate.[244]

Facially, the code and the treasury regulations establish a presumptive date-of-death valuation rule for purposes of determining the gross estate.[245] The express language of the statutory scheme leaves little doubt as to the legislative intent regarding the timing of valuation of the gross estate's assets. It is the glaring omission of such express language in § 2053(a)(3) that has spawned a seventy-four-year debate over the role of postmortem events in valuing deductions for claims against estates.[246]

*B. Fair Market Value and Hindsight*

Underlying the express statutory language of the code with respect to valuing assets is the doctrine of fair market value. As previously noted, Treasury Regulation § 20.2031-1(b) prescribes that for purposes of the gross estate, the value of an asset is its fair market value at the date of death.[247] It is in determining what actually constitutes fair market value that the question of using hindsight becomes important.

The generally accepted definition of fair market value for purposes of the estate tax is "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts."[248] This definition presumes that the buyer and seller have knowledge of the relevant facts that exist as of the date of valuation, but that it is impossible for them to have knowledge of events that occur after the date of valuation.[249] Therefore, subsequent events that alter this valuation do not truly reflect the fair market value of assets based on the knowledge of the buyer and seller on the date of valuation, and courts generally refuse to consider subsequent events.[250]

244. *See* I.R.C. § 2034 (2000) (including dower and curtesy interests existing "at the time of the decedent's death" in gross estate); *id.* § 2035 (including in gross estate value of gifts made by decedent "during the 3-year period ending on the date of the decedent's death").

245. *See* STEPHENS ET AL., *supra* note 47, ¶ 4.02 ("Section 2031 also expresses the presumptive date-of-death rule for the time of valuation.").

246. *See supra* text accompanying notes 231–32 (suggesting that omission of any direction in § 2053(a)(3) as to consideration of postdeath events was not legislative oversight).

247. Treas. Reg. § 20.2031-1(b) (as amended in 1965). This section also requires the use of fair market value in determining the value of assets under the alternate valuation date of § 2032. *Id.*

248. *Id.*

249. *See* BOGDANSKI, *supra* note 163, ¶ 2.01[3][c][i] (discussing role of hindsight in determining fair market value of assets).

250. *See id.* ("This attitude flows from the perception that the willing buyer and willing

The proposition that the proper value of assets for estate tax purposes is the fair market value of those assets at the moment of death also finds support in the courts. In *United States v. Land*,[251] the U.S. Court of Appeals for the Fifth Circuit established the presumptive date-of-death rule for valuation of assets.[252] Judge Wisdom announced, "Brief as is the instant of death, the court must pinpoint its valuation at this instant—the moment of truth, when the ownership of the decedent ends and the ownership of the successors begins."[253] The court's support of a strict date-of-death valuation rule hinged on an analysis of the "willing buyer/willing seller" concept of fair market value.[254] Although *Land* involved a claim that the value of an asset *prior* to death should control, other courts have adopted the rationale of that decision

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seller cannot be expected to know on the valuation date events that have not yet occurred. Thus, subsequent events are said not to be relevant as direct proof . . . of value on the all-important valuation date.").

251. United States v. Land, 303 F.2d 170 (5th Cir. 1962). *Land* involved a dispute over the valuation of the partnership interests of two decedents. *Id.* at 171. The partnership agreement stipulated that if any partner withdrew from the partnership during his lifetime, the partnership had the option of purchasing that interest at two-thirds value. *Id.* The agreement further stipulated that upon the death of a partner, the partnership had the option to purchase the decedent's interest at full value. *Id.* The respondent estates reported the value of the decedents' interests at two-thirds value, asserting that the value of the interests prior to death controlled for estate tax purposes. *Id.* The court rejected this theory, ruling that the date-of-death value of the property controls for estate tax purposes, not the value prior or subsequent to death. *Id.* at 172. The court based its ruling on the theory of fair market value, which mandates analysis of the knowledge of the willing buyer and seller at the moment of valuation, not at any time prior or subsequent to that valuation. *Id.* at 173.

252. *See id.* at 175 (ruling that date-of-death value of partnership interest controls for estate tax purposes).

253. *Id.* at 172.

254. *See id.* at 173 (discussing conception of fair market value from viewpoint of "potential buyer"). The court stated:

> To find the fair market value of a property interest at the decedent's death we put ourselves in the position of a potential purchaser of the interest at that time. Such a person would not be influenced in his calculations by past risks that had failed to materialize or by restrictions that had ended. Death tolls the bell for risks, contingencies, or restrictions which exist only during the life of the decedent. A potential buyer focuses on the value the property has in the present or will have in the future. He attributes full value to any right that vests or matures at death, and he reduces his valuation to account for any risk or deprivation that death brings into effect, such as the effect of the death on the brains of a small, close corporation. These are factors that would affect his enjoyment of the property should he purchase it, and on which he bases his valuation. The sense of the situation suggests that we follow suit.

*Id.*

in foreclosing the consideration of events occurring *subsequent* to death in determining asset valuation.[255]

The fact that the courts and the legislature frown on the use of hindsight in valuing assets for estate tax purposes seems logical in the context of the fair-market-value doctrine. Unlike assets, however, courts do not value claims based on a hypothetical arm's-length-bargaining transaction between a willing buyer and a willing seller; the doctrine of fair market value is not applicable in valuing a claim under § 2053(a)(3) of the code.[256] This distinction lends credence to the argument that subsequent events should play a role in valuing deductions for claims against estates.[257] Because the value of a claim does not depend on the knowledge of the claimant and the estate at a particular point in time, it is not unreasonable to use hindsight in determining the value of deductions for such claims.

### *C. Section 2032—Alternate Valuation Date*

The foregoing analysis exemplifies the strong policy arguments against the use of hindsight in valuing assets, as well as the legislature's express statutory mandate that the date of death governs timing for the computation of asset values. Interestingly, however, Congress has carved out a limited exception to this hard and fast rule, providing in § 2032 of the code for the election of an alternate asset valuation date—six months after the date of death—for purposes of computing the estate's tax liability.[258]

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255. *See* Morris v. Comm'r, 761 F.2d 1195, 1201–02 (6th Cir. 1985) (refusing to admit evidence concerning lack of development of decedent's property eight years after date-of-death valuation). Other courts have refused to consider events occurring subsequent to *transfer* in determining asset valuation. *See* Lebowitz v. Comm'r, 917 F.2d 1314, 1318 (2d Cir. 1990) (refusing to consider events subsequent to purchase in determining whether nonrecourse debt sufficiently reflected underlying property's fair market value); Ebben v. Comm'r, 783 F.2d 906, 909–10 (9th Cir. 1986) (upholding valuation as of date of transfer and refusing to consider property appraisal based primarily on events occurring subsequent to transfer). For a comprehensive list of decisions rejecting the use of hindsight in determining asset valuation for estate tax purposes, see BOGDANSKI, *supra* note 163, ¶ 2.01[3][c][i], at 2-60 n.231.

256. *See* I.R.C. § 2053(a) (2000) (containing no reference to fair market value with regard to the valuation of estate deductions).

257. *But see* Meresidis, *supra* note 3, at 2717 ("The difference in treatment for claims and assets seems to be a contradictory policy, since both are a part of the estate that is transferred at death.").

258. *See* I.R.C. § 2032(a) (2000) (providing for election of alternate valuation date for assets). This section states in full:

> The value of the gross estate may be determined, if the executor so elects, by valuing all the property included in the gross estate as follows: (1) In the case of property distributed, sold, exchanged, or otherwise disposed of, within 6 months

The fact that Congress provides for an alternate postdeath valuation date for assets (and a corresponding alternate determination of the value of marital and charitable deductions) is of great relevance to the issue of valuing deductions for claims against estates. First, the fact that Congress carved out this exception to the date-of-death valuation rule lends credence to the proposition that postmortem events should play a role in valuation only if expressly authorized by statute.[259] This interpretation supports the argument that because § 2053(a)(3) does not contain a similar express statutory exception, postmortem events should not play a role in valuing deductions for claims against estates.[260] Second, it is arguable that a similar statutory scheme providing for an alternative valuation date for deductions for claims against estates might be an effective means of addressing the current conflict among the circuits.[261] Presently, there is no indication that the courts will reconcile their differences of opinion in the near future.[262] Therefore, a statutory compromise in a vein similar to § 2032 might ultimately be a more reasonable solution to this debate.

The first step in assessing the benefits of fashioning a statutory solution to the debate over the valuation of § 2053(a)(3) deductions is to analyze the public policy interests served by § 2032. The underlying purpose of § 2032(a) is to shield the estate from tax liability on estate assets whose values decline sharply as a result of market forces beyond the control of the estate during administration.[263] However, an executor can only elect an alternate valuation when the decline in value of the estate assets is not the result of a voluntary act

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> after the decedent's death such property shall be valued as of the date of distribution, sale, exchange, or other disposition. (2) In the case of property not distributed, sold, exchanged, or otherwise disposed of, within 6 months after the decedent's death such property shall be valued as of the date 6 months after the decedent's death. (3) Any interest or estate which is affected by mere lapse of time shall be included at its value as of the time of death (instead of the later date) with adjustment for any difference in its value as of the later date not due to mere lapse of time.

*Id.*

259. *See supra* note 230 and accompanying text (arguing that if Congress intends consideration of postmortem events in valuation, it conveys this intent expressly by statute).

260. *See supra* note 230 and accompanying text (same).

261. *See* Raby & Raby, *supra* note 233, at 249-21, ¶ 18 (arguing that alternate valuation election should apply to valuation of claims deductions as well as to valuation of assets).

262. *See supra* Part II (detailing circuit split); *infra* note 283 (discussing repeal of estate tax, and observing that until Congress determines whether to make repeal permanent, resolution of this issue may be elusive).

263. *See* 2 J. MARTIN BURKE ET AL., MODERN ESTATE PLANNING § 19.02 (2d ed. 2002) ("The alternate valuation election is provided solely to mitigate the hardship on an estate due to declining market values."). Congress enacted § 2032 in 1935 in response to the dramatic and rapid decline in property values during the Great Depression. Jones, *supra* note 174, at 677.

on the part of the executor or other interested party.[264] Thus, this provision acts as an equitable protection against the unsavory prospect that an estate will have to pay taxes on a high asset value determined on the date of death, even though uncontrollable market forces have reduced the value of those assets drastically in the months following death. Furthermore, § 2032(b) provides for a corresponding alternate determination of the value of marital and charitable deductions that result from circumstances other than mere lapse of time or the occurrence or nonoccurrence of a contingency.[265] The code provides for an alternate determination of the value of these deductions either as of the alternate valuation date or as of the date of disposition of the underlying property, whichever occurs first.[266]

The following illustration demonstrates the effect of a § 2032 election on a charitable gift. John Doe devises to a charity real property valued at $300,000 as of the date of his death. The executor of his estate elects the alternate valuation date. A month after John's death, the executor transfers the property to the charity, but the value of the property at the time of the transfer is $400,000 as a result of market conditions. Six months after John's death (the alternate valuation date), the value of the property has increased even further, to $500,000. Because the increase in the value was not due to a mere lapse of time or the occurrence or nonoccurrence of a contingency, the estate may properly deduct $400,000.[267] However, if the estate transferred the property to the charity seven months after John's death, the proper deduction would have been $500,000, the value of the property as of the alternate valuation date.[268]

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264. *See* 2 BURKE ET AL., *supra* note 263, § 19.02 ("A voluntary postmortem act of a surviving spouse, trustee or executor that results in a reduction of value is not to be considered in determining the alternative value of the property.").

265. *See* I.R.C. § 2032(b) (2000) (governing treatment of charitable and marital deductions under alternate valuation date election). This section states in part:

> In case of an election made by the executor under this section, then—(1) for purposes of the charitable deduction under section 2055 or 2106(a)(2), any bequest, legacy, devise, or transfer enumerated therein, and (2) for the purpose of the marital deduction under section 2056, any interest in property passing to the surviving spouse, shall be valued as of the date of the decedent's death with adjustment for any difference in value (not due to mere lapse of time or the occurrence or nonoccurrence of a contingency) of the property as of the date 6 months after the decedent's death (substituting, in the case of property distributed by the executor or trustee, or sold, exchanged, or otherwise disposed of, during such 6-month period, the date thereof).

*Id.*

266. *Id.*

267. *See id.* (providing for alternate valuation only if difference in value is "not due to mere lapse of time or the occurrence or nonoccurrence of a contingency").

268. *See* 2 BURKE ET AL., *supra* note 263, § 19.02 (offering similar illustration in which

This illustration shows that pursuant to § 2032, postmortem events can affect the valuation of deductions in limited circumstances. Although the statute does not extend to deductions for claims, it does show that Congress is willing to draft a rule recognizing the consideration of postmortem events in particular situations.

Section 2032 is a reasonable and effective means of protecting the taxpayer from the hardship of tax liabilities that do not truly reflect the value of the assets underlying those liabilities, but at the same time it also serves the government's interests. First, the statute does not apply to property burdened with contingencies because contingencies decrease the value of the assets and result in a lower valuation base for tax purposes.[269] Second, the statute does not apply in cases in which the value of the underlying property decreases by reason of a mere lapse of time.[270] In such cases, it is certain that the value of the assets will decline after the date of death, and permitting an alternate valuation election with regard to such property would undermine the estate tax's underlying purpose: taxation of the estate as it exists at the moment of death.[271] Third, the statute does not apply in cases in which the change in value of the underlying property is the result of a voluntary act on the part of the executor, surviving spouse, or other interested party.[272] This protects the government from unmeritorious manipulation of the value of the estate's assets after death as a means of reducing the value of the taxable estate under the rule.

Congress seems to have fashioned a reasonable compromise between government and taxpayer interests in § 2032. The statute does not rely on a bright-line date-of-death valuation principle, but neither does it extend post-

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value of property increases after death).

269. *See* Jerry A. Kasner, *IRS Makes a Close Call on the Alternate Valuation Date*, 62 TAX NOTES 1313, 1314 (1994) ("The government has successfully contended that the property should be valued free of the contingencies, since that produces a higher valuation.").

270. Examples of assets that decrease in value due to a mere lapse of time are patents, annuities, reversions, and real property, when the decline is a result of depreciation. 2 BURKE ET AL., *supra* note 263, § 19.04. In such cases, the date-of-death valuation, not the alternate valuation, applies in computing the value of the assets. *Id.*

271. *See* Edwards v. Slocum, 264 U.S. 61, 62-63 (1924) ("[The estate tax] is a tax upon a transfer of his net estate by a decedent.... It comes into existence before and is independent of the receipt of the property by the legatee. It taxes... 'not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death.'"); Propstra v. United States, 680 F.2d 1248, 1250 (9th Cir. 1981) ("Because the estate tax is a tax on the privilege of transferring property upon one's death, the property to be valued for estate tax purposes is that which the decedent actually transfers at his death rather than the interest held by the decedent before death or that held by the legatee after death.").

272. *See* 2 BURKE ET AL., *supra* note 263, § 19.02 ("A voluntary postmortem act of a surviving spouse, trustee or executor that results in a reduction of value is not to be considered in determining the alternative value of the property.").

mortem valuation indefinitely into the future.[273] Furthermore, the statute recognizes the potential inequities involved in estate asset valuation by providing for postmortem review within reasonable temporal limitations.[274]

The statutory compromise reached in § 2032 serves important policy interests, and a similar statutory solution governing § 2053(a)(3) might ameliorate the present disarray of the law with respect to deductions for claims.[275] However, there is an inherent problem in establishing a temporal limitations period for the consideration of subsequent events in valuing deductions for claims. Even if the legislature established a mandatory alternate valuation date for valuing deductions for claims, there is potential for taxpayer abuse.[276] Taxpayers who are fairly certain of settling a claim for less than its date-of-death value could simply prolong settlement negotiations beyond the statutorily mandated alternate valuation date.[277] Thus, the deduction for the claim would not reflect the true amount paid to satisfy the claim, but rather, the fictitious date-of-death value.

Nevertheless, some form of statutorily imposed temporal limitations period on valuing deductions for claims would at the very least address the underlying policy concern of avoiding uncertainty and delay in estate administration.[278] Although fashioning a suitable statutory remedy to the dispute over valuing deductions for claims is beyond the scope of this Note, consideration of the legislature's establishment of an alternate valuation date under § 2032 with respect to the valuation of assets for estate tax purposes is arguably relevant to the debate over the timing of valuation of deductions for claims against estates, and should factor into the ultimate resolution of this issue.

## *V. Conclusion*

The dispute over the role of postmortem events in valuing deductions for claims against estates is ripe for ultimate resolution, be it judicial or statutory.

273. *See* I.R.C. § 2032(a) (2000) (limiting alternate valuation date to six months after decedent's death).

274. *See* 2 BURKE ET AL., *supra* note 263, § 19.02 (observing that purpose of alternate valuation election is to mitigate hardships resulting from uncontrollable declines in market value within a short period after decedent's death).

275. *See* Raby & Raby, *supra* note 233, at 249-21, ¶ 18 (arguing that alternate valuation election should apply to valuation of claims deductions as well as to valuation of assets).

276. *See* Meresidis, *supra* note 3, at 2743 ("Even if there is a 'statute-of-limitations' period during which claims may be valued up to a certain point after death, there will still arise the danger of the estate purposefully settling a claim just beyond that period to avoid higher estate tax duties.").

277. *Id.*

278. *See supra* note 174 (providing examples of courts and commentators critical of uncertainty, delay, and inconsistency in estate administration).

Two competing policy concerns underlie this debate. First, there is a strong need for a solution that mitigates the uncertainty and delay in estate administration that is the product of the lack of statutory guidance as to the role of postmortem events in valuing deductions for claims.[279] Second, there is also a need for a solution that will protect against windfall awards to estates, but that at the same time will preserve the interest of the legislature in encouraging certain deductions.[280]

Fashioning a suitable remedy to this debate has thus far proved to be difficult, at best, and with good reason. Issues of valuation are not fixed and concrete, but rather are subjective and in constant flux.[281] As Learned Hand noted, "In the end value is no more than the opinions of those who have, and those who have not, when they coincide."[282]

The resolution of this issue necessarily must be the product of a reasoned balancing of the public policy issues involved. If the concern for avoiding uncertainty and delay in estate administration is the more pressing issue, then a date-of-death valuation should prevail. However, if the overarching concern is protecting against windfall awards to estates, then arguably postmortem events should play a role in valuation. Thus far, the courts have not been able to decide which policy concern should prevail, and Congress has chosen not to intervene. Until the Supreme Court or the legislature weighs in on this issue, the doctrinal disarray of the law in its present state will continue to confound executors and the IRS alike and will continue to invite costly litigation over the role of postmortem events in valuing deductions for claims against estates.[283]

279. *See supra* note 174 (providing examples of courts and commentators critical of uncertainty, delay, and inconsistency in estate administration).

280. *See supra* note 185 and accompanying text (suggesting that date-of-death valuation results in windfalls to estates).

281. *See* Ithaca Trust Co. v. United States, 279 U.S. 151, 155 (1929) (noting that valuation "depends upon the relative intensity of the social desire for it at that time"); John G. Steinkamp, *Fair Market Value, Blockage, and the Valuation of Art*, 71 DENV. U. L. REV. 335, 340 (1994) ("The value of property is not static; it changes with time as economic conditions shift and perceptions about the future change.").

282. Rice v. Eisner, 16 F.2d 358, 361 (2d Cir. 1926).

283. It is important to note that Congress passed legislation in 2001 that provides for a total repeal of the federal estate tax in 2010. *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 501(a), 115 Stat. 38, 69 (eliminating estate tax in 2010). The Act gradually phases out the tax through 2009, *id.* § 511(a), 115 Stat. at 70–71, but unless Congress extends the repeal beyond 2010, the estate tax will reemerge in its present form in 2011, *see id.* § 901, 115 Stat. at 150 (prescribing "sunset" provisions for estate tax repeal). As a result of this repeal, it is not likely that the Supreme Court or Congress will take up the issue of valuing deductions for claims until such time as the future of the estate tax is more certain.