

Rev. Rul. 79-363

Citations: Rev. Rul. 79-363; 1979-2 C.B. 345

Rev. Rul. 79-363

ISSUE

If a donor, A, creates a trust for the benefit of the donor's spouse, B, and their adult child, C, in a divorce settlement transaction to which section 2516 of the Internal Revenue Code is applicable, is any portion of the transfer of the trust interest to the child made for consideration in money or money's worth by virtue of the release of the support rights of the donor's spouse as part of the settlement agreement?

FACTS

In July 1977 A and B entered into a written agreement in contemplation of their obtaining a divorce. The agreement required A to create an inter vivos trust upon issuance of a divorce decree and to promptly transfer property worth no less than \$600,000 to the trust. The terms of the trust provide for a life annuity to B, with the remainder payable at B's death to C. In exchange for the creation of the trust by A, B agreed to release all rights and claims that B might have against A as a result of the marriage or against any property in which A had an interest. B's right to receive support from A was specifically enumerated as one of the rights released by B.

On July 14, 1978, A and B were divorced by the final decree of a court in State X. Under the law of State X, the divorce court has no power to alter a settlement agreement between spouses; the court decree in the present case did not incorporate any agreement between A and B. On the same day, A transferred \$600,000 to the trust. As of the date of transfer, the value of B's right to support was \$200,000, and the value of B's other marital rights was \$400,000. At that time the present value of B's right to receive a life annuity from the trust was \$300,000, and the present value of C's remainder interest was also \$300,000.

On November 15, 1978, A filed a federal gift tax return reporting the transaction as being exempt from gift tax. A concluded that B released all rights, worth a total of \$600,000, in exchange for A's transfers of the life annuity, worth \$300,000, to B and of the remainder interest, also worth \$300,000, to C. A states that the parties to the divorce settlement arrived at their agreement by bargaining simultaneously with respect to all of the rights and obligations involved. Because neither of A's transfers (to B and to C) can be attributed specifically to B's release of any particular right, A states that the value of the support rights (\$200,000) and the value of the marital rights (\$400,000) should be apportioned equally between the equal transfers to B and to C. A states that, as a result, the \$300,000 transfer to C was met by consideration in the form of support rights released by B, one half (\$100,000) of which is attributable thereto, and by B's release of marital rights, one half (\$200,000) of which is attributable to the transfer to C. A thus concludes that A's transfer to C was made in exchange for full and adequate consideration and that A's transfer to B is deemed to have been made for full and adequate consideration under section 2516 of the Code.

LAW AND ANALYSIS

Section 2511 of the Code states that the federal gift tax is applicable whether a gift is in trust or otherwise, whether direct or indirect, and whether the transferred property is real or personal, tangible or intangible.

Section 2512(b) of the Code provides that if property is transferred for less than an adequate and full consideration in money or money's worth, then the amount of the gift is the amount by which the value of the transferred property exceeds the value of the consideration received.

Section 2043(b) of the Code, an estate tax provision, requires that a relinquishment of dower or curtesy, or of a statutory estate created in lieu thereof, or "of other marital rights" in the decedent's estate, shall not be considered to any extent a consideration in money or money's worth. This provision was held applicable to the definition of "consideration in money or money's worth" for gift tax purposes, as well as for estate tax purposes, by the Supreme Court in *Merrill v Fahs*, 324 U.S. 308 (1945), Ct. D. 1635, 1945 C.B. 418. See also section 25.2512-8 of the Gift Tax Regulations.

Therefore, the release by a spouse of marital property rights cannot serve as consideration in money or money's worth for gift tax purposes. However, the release of the right to support may serve as consideration. See [Rev. Rul. 68-379](#), 1968-2 C.B. 414.

Section 2516 of the Code provides that if a married couple executes a written agreement with respect to their "marital and property rights" and if a divorce is obtained within 2 years thereafter, all transfers made under the agreement either (1) to the donor's spouse in settlement of the spouse's marital or property rights, or (2) for the support of the issue of the marriage during minority, shall be deemed to be made for full and adequate consideration in money or money's worth. Transfers to adult children and transfers that cannot be clearly defined as having been made to the divorcing spouse or to the minor issue of the marriage are not exempt, under section 2516, from the gift tax. See [Rev. Rul. 75-73](#), 1975-1 C.B. 313.

In the present case, the transfer of a life annuity interest to B qualifies under section 2516 and is thus deemed to have been made for full and adequate consideration in money or money's worth. A properly excluded the value of the transfer to B from A's taxable gifts.

The transfer of the remainder interest to C is not, however, subject to section 2516 of the Code, because C was not a minor at the time of the divorce settlement. Therefore, the full value of the remainder interest is the amount of A's gift subject to federal gift tax, unless it was made in exchange for consideration in money or money's worth.

The \$400,000 worth of marital rights released by B, of which \$200,000 was claimed by A to have been released in exchange for the transfer to C, cannot serve as consideration in money or money's worth for federal gift tax purposes. See the above discussion of section 2043(b) of the Code and its application to the federal gift tax.

The value of support rights released by B may, on the other hand, serve as consideration in money or money's worth under [Rev. Rul. 68-379](#), cited above. To be acceptable as consideration for the transfer to C, the taxpayer must show that the support rights were specifically and deliberately released by B, and their release was accepted by A, in order to induce A to make the transfer to C. See [Rev. Rul. 77-314](#), 1977-2 C.B. 349, especially situation 2, in which the spouse had actively bargained for, and agreed to receive a less

valuable transfer in exchange for, the transfer to the third party. Therefore, the donor received consideration for the transfer to the third party in the amount of the excess of the value of support rights released by the spouse, over the trust interest received by the spouse. The spouse had made a taxable gift to the third party in the amount of that excess.

In the present case, A has failed to show that B actively bargained for, and specifically released support rights for, A's transfer of the trust remainder to C. A has, instead, assumed that one half of the value of B's support rights was released in exchange for the transfer to C, because all of B's rights were released through a process of simultaneous bargaining in which no particular right was released as inducement for any particular transfer by A.

A's assumption with respect to the consideration received is not, however, a sufficient factual description of B's efforts, if any, to induce A's transfer to C by releasing support rights. It is equally reasonable, in the absence of specific facts, to assume that B released all of the support rights and \$100,000 worth of B's marital rights in exchange for what B received, the life annuity interest worth \$300,000.

HOLDING The entire amount of A's transfer of the \$300,000 remainder interest to C is a gift for federal gift tax purposes, as no consideration in money or moneys' worth was shown to have been received by A in exchange for A's transfer to C.

If A could have shown that B actively bargained for, and relinquished support rights in exchange for, A's transfer to C, the amount of A's gift to C would have been the amount of the transfer to C reduced by the amount of support rights relinquished by B. In this latter situation, B would have made a taxable gift to C in the amount relinquished.