

to denote the body of property comprehended within the community property system; the expression "separate property" includes any noncommunity property, whether held in joint tenancy, tenancy by the entirety, tenancy in common, or otherwise; and the term "conversion" includes any transaction or agreement which transforms property from a community status into a noncommunity status.

(3) The separate property which section 2523(f) classifies as community property is not limited to that which was in existence at the time of the conversion. The following are illustrative of the scope of section 2523(f):

(i) A partition of community property between husband and wife, whereby a portion of the property became the separate property of each, is a conversion of community property.

(ii) A transfer of community property into some other form of coownership, such as a joint tenancy, is a conversion of the property.

(iii) An agreement (whether made before or after marriage) that future earnings and gains which would otherwise be community property shall be shared by the spouses as separate property effects a conversion of such earnings and gains.

(iv) A change in the form of ownership of property which causes future rentals, which would otherwise have been acquired as community property, to be acquired as separate property effects a conversion of the rentals.

(4) The rules of section 2523(f) are applicable, however, only if the conversion took place after December 31, 1941, and only to the extent stated in this section.

(5) If the value of the separate property acquired by the donor as a result of a conversion did not exceed the value of the separate property thus acquired by the donee spouse, the entire separate property thus acquired by the donor is to be considered, for the purposes of this section, as held by him and the donee spouse as community property. If the value (at the time of conversion) of the separate property so acquired by the donor exceeded the value (at that time) of the separate property so acquired by the donee spouse, only a part of the separate

property so acquired by the donor (and only the same fractional part of property acquired by him in exchange for such separate property) is to be considered, for purposes of this section, as held by him and the donee spouse as community property. The part of such separate property (or property acquired in exchange for it) which is considered as so held is the same proportion of it which the value (at the time of the conversion) of the separate property so acquired by the donee spouse is of the value (at that time) of the separate property so acquired by the donor. The following example illustrates the application of the provisions of this paragraph:

Example. During 1942 the donor and his spouse partitioned certain real property held by them under community property laws. The real property then had a value of \$224,000. A portion of the property, then having a value of \$160,000, was converted into the donor's separate property, and the remaining portion, then having a value of \$64,000, was converted into his spouse's separate property. In 1955 the donor made a gift to his spouse of the property acquired by him as a result of the partition, which property then had a value of \$200,000. The portion of the property transferred by gift which is considered as community property is

\$64,000 (value of property acquired by donee spouse) ÷ \$160,000 (value of property acquired by donor spouse) × \$200,000 = \$80,000.

The marital deduction with respect to the gift is, therefore, limited to one-half of \$120,000 (the difference between \$200,000, the value of the gift, and \$80,000, the portion of the gift considered to have been of "community property"). The marital deduction with respect to the gift is, therefore, \$60,000.

[T.D. 6334, 23 FR 8904, Nov. 15, 1958; 25 FR 14021, Dec. 31, 1960. Redesignated and amended by T.D. 8522, 59 FR 9660, Mar. 1, 1994]

SPECIAL VALUATION RULES

§ 25.2701-0 Table of contents.

This section lists the major paragraphs contained in §§ 25.2701-1 through 25.2701-8.

§ 25.2701-1 *Special valuation rules in the case of transfers of certain interests in corporations and partnerships.*

(a) In general.

(1) Scope of section 2701.

(2) Effect of section 2701.

(3) Example.

- (b) Transfers and other triggering events.
 - (1) Completed transfers.
 - (2) Transactions treated as transfers.
 - (3) Excluded transactions.
 - (c) Circumstances in which section 2701 does not apply.
 - (1) Marketable transferred interests.
 - (2) Marketable retained interests.
 - (3) Interests of the same class.
 - (4) Proportionate transfers.
 - (d) Family definitions.
 - (1) Member of the family.
 - (2) Applicable family member.
 - (3) Relationship by adoption.
 - (e) Examples.
 - § 25.2701-2 *Special valuation rules for applicable retained interests.*
 - (a) In general.
 - (1) Valuing an extraordinary payment right.
 - (2) Valuing a distribution right.
 - (3) Special rule for valuing a qualified payment right held in conjunction with an extraordinary payment right.
 - (4) Valuing other rights.
 - (5) Example.
 - (b) Definitions.
 - (1) Applicable retained interest.
 - (2) Extraordinary payment right.
 - (3) Distribution right.
 - (4) Rights that are not extraordinary payment rights or distribution rights.
 - (5) Controlled entity.
 - (6) Qualified payment right.
 - (c) Qualified payment elections.
 - (1) Election to treat a qualified payment right as other than a qualified payment right.
 - (2) Election to treat other distribution rights as qualified payment rights.
 - (3) Elections irrevocable.
 - (4) Treatment of certain payments to applicable family members.
 - (5) Time and manner of elections.
 - (d) Examples.
 - § 25.2701-3 *Determination of amount of gift.*
 - (a) Overview.
 - (1) In general.
 - (2) Definitions.
 - (b) Valuation methodology.
 - (1) Step 1—Valuation of family-held interests.
 - (2) Step 2—Subtract the value of senior equity interests.
 - (3) Step 3—Allocate the remaining value among the transferred interests and other family-held subordinate equity interests.
 - (4) Step 4—Determine the amount of the gift.
 - (5) Adjustment in Step 2.
 - (c) Minimum value rule.
 - (1) In general.
 - (2) Junior equity interest.
 - (3) Indebtedness.
 - (d) Examples.
 - § 25.2701-4 *Accumulated qualified payments.*
 - (a) In general.
 - (b) Taxable event.
 - (1) In general.
 - (2) Exception.
 - (3) Individual treated as interest holder.
 - (c) Amount of increase.
 - (1) In general.
 - (2) Due date of qualified payments.
 - (3) Appropriate discount rate.
 - (4) Application of payments.
 - (5) Payment.
 - (6) Limitation.
 - (d) Taxpayer election.
 - (1) In general.
 - (2) Limitation not applicable.
 - (3) Time and manner of election.
 - (4) Example.
 - § 25.2701-5 *Adjustments to mitigate double taxation.*
 - (a) Reduction of transfer tax base.
 - (1) In general.
 - (2) Federal gift tax modification.
 - (3) Federal estate tax modification.
 - (4) Section 2701 interest.
 - (b) Amount of reduction.
 - (c) Duplicated amount.
 - (1) In general.
 - (2) Transfer tax value—in general.
 - (3) Special transfer tax value rules.
 - (d) Examples.
 - (e) Computation of reduction if initial transfer is split under section 2513.
 - (1) In general.
 - (2) Transfers during joint lives.
 - (3) Transfers at or after death of either spouse.
 - (f) Examples.
 - (g) Double taxation otherwise avoided.
 - (h) Effective date.
 - § 25.2701-6 *Indirect holding of interests.*
 - (a) In general.
 - (1) Attribution to individuals.
 - (2) Corporations.
 - (3) Partnerships.
 - (4) Estates, trusts, and other entities.
 - (5) Multiple attribution.
 - (b) Examples.
 - § 25.2701-7 *Separate interests.*
 - § 25.2701-8 *Effective dates.*
- [T.D. 8395, 57 FR 4255, Feb. 4, 1992, as amended by T.D. 8536, 59 FR 23154, May 5, 1994]
- § 25.2701-1 Special valuation rules in the case of transfers of certain interests in corporations and partnerships.**
- (a) *In general*—(1) *Scope of section 2701.* Section 2701 provides special valuation rules to determine the amount of the gift when an individual transfers an equity interest in a corporation or partnership to a member of the individual's family. For section 2701 to apply, the transferor or an applicable family member (as defined in paragraph (d)(2) of this section) must, immediately