Steve Leimberg's Estate Planning Email Newsletter - Archive Message #3211
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From: Steve Leimberg's Estate Planning Newsletter
Subject: Marc Soss on Estate of Spizzirri v. Commissioner: Are Estate Payments Made Pursuant to Stepchildren Under a Premarital Agreement a Deductible Claim Against the Estate?

"It is not common for a pre-marital or post-marital agreement to include a provision requiring the disposition of assets, upon a wealthier spouse's death, to the other spouse's children. However, the distributions to the children will not constitute tax deductible payments, as 'claims against the estate' under 26 U.S.C. § 2053(a)(3) for tax purposes."

Marc Soss provides members with his analysis of Estate of Spizzirri v. Commissioner of Internal Revenue, No. 23-14049 (11th Cir. 2025)

Marc Soss' practice focuses on estate planning, probate and trust administration, and corporate law in Southwest Florida. Marc is a frequent contributor to LISI and has published articles in the Florida Bar, Rhode Island Bar, North Carolina Bar, Association of the United States Navy and Military.Com. Marc is a retired United States Navy Supply Corps Officer.

Here is his commentary:

EXECUTIVE SUMMARY:

Richard Spizzirri ("Richard") and his fourth wife, Holly Lueders ("Holly"), entered into a prenuptial agreement that required the Richard's estate to transfer $6 million to his wife, Holly, and $3 million to Holly's children upon his death. After his death, his estate distributed the funds to Holly's children and claimed a deduction under 26 U.S.C. § 2053(a)(3) as "claims against the estate" for tax purposes. The Commissioner of Internal Revenue, the U.S. Tax Court and ultimately the United States Court of Appeals denied these deductions on the basis they were neither "contracted bona fide" nor "for an adequate and full consideration in money or money's worth."

COMMENT:

In 1997, prior to their marriage, Richard and Holly entered into a prenuptial agreement. At the time the agreement was entered into, Richard had a significant net worth and four children from a prior marriage, while Holly had a net worth of around $1 million and three children from a prior marriage. Over the course of their 18-year marriage, the prenuptial agreement was modified five (5) times.

The third modification was executed on November 3, 2005, and amended the pre-marital provisions pertaining to what Holly would receive after Richard's death. Specifically, Holly waived her right to a marital trust and residency rights under his Last Will and Tstament to receive instead a $9 million bequest upon his death ($6 million to Holly and $3 million to her adult children). Later modifications reaffirmed the promise to pay $1 million to each of Holly's children.

Notwithstanding the modifications made to the pre-marital agreement and several codicils, Robert did not update his 1979 Last Will and Testament to incorporate the agreed upon bequest to Holly or her children. Robert ultimately passed away in May 2015. After his death, Holly's children filed claims against the estate seeking their $1 million dollar payments. The estate then paid the claims and penalties for late payment, filed a Form 1099-MISC and deducted the payments as "claims against the estate".

Estate Tax:

The Internal Revenue Code taxes "the transmission of wealth at death" through an estate tax based upon each individuals unified credit at date of death. United States v. Stapf, 375 U.S. 118, 134 (1963); 26 U.S.C. § 2001. In contrast, a taxpayer may use any allowable deductions to decrease the value of the decedent's gross estate. 26 U.S.C. §§ 2051, 2053(a). Increased deductions equate to a reduced gross estate subject to the estate tax. Gregory v. Helvering, 293 U.S. 465, 469 (1935). To qualify as a deductible "claim against the estate," a claim must be "contracted bona fide and for an adequate and full consideration in money or money's worth." 26 U.S.C.§ 2053(c)(1)(A).

Tax Law:

26 U.S.C. § 2053(c)(1)(A) requires that, for a claim against the estate to be deductible, it must be "contracted bona fide and for an adequate and full consideration in money or money's worth". This requirement is designed to prevent gifts and testamentary transfers from being "transformed into deductible claims through collaboration and creative contracting".

26 U.S.C § 7491(a) addresses the required burden of proof for a taxpayer to shift the burden if they introduce "credible evidence" and follow substantiation and record-keeping requirements.

Treas. Reg. § 20.2053-1(b) provides five factors to guide the evaluation of whether an intrafamily transfer was contracted bona fide: (i) The transaction occurs in the ordinary course of business, is negotiated at arm's length, and is free from donative intent; (ii) The claim is not related to an expectation or claim of inheritance; (iii) The claim originates pursuant to an agreement between the decedent and the family member; (iv) Performance by the claimant stems from an agreement between the decedent and the family member; and (v) All amounts paid are reported by each party for Federal income and employment tax purposes consistently with the claim's nature.

Court Proceedings:

The Commissioner of Internal Revenue issued a notice of deficiency disallowing the deduction for the payments made to Holly's children. The estate then appealed the matter to both the U.S. Tax Court and United States Court of Appeals for the Eleventh Circuit. At trial before the U.S. Tax Court, the estate presented witnesses who testified as to the enforceability of the agreement and the value of Lueders's waived marital rights.

Before the Eleventh Circuit, the estate argued that it had shifted the burden of proof to the Commissioner by introducing credible evidence of its entitlement to the deduction under 26 U.S.C. § 7491(a). The court noted that the determination of whether a deduction for a claim against an estate is allowed is fact-intensive and must be made on a case-by-case basis and focused its analysis on the "bona fide" requirement under Treasury Regulation § 20.2053-1(b)(2)(i) “(the bona fide requirement bars a deduction if the claim is based on a transfer that is "essentially donative in character)”. The Court emphasized that “[t]ransactions between family members are subject to "particular scrutiny" because a testator is more likely to be making a bequest.” Regarding the burden of proof, the court stated that a taxpayer can shift the burden under § 7491(a) if they introduce "credible evidence" and comply with substantiation and record-keeping requirements which it did not believe had been achieved.

Both the U.S. Tax Court and United States Court of Appeals concurred and ruled that the transfers to Holly’s children were donative in character and “not deductible as claims against the estate” because they were neither “contracted bona fide” nor “for an adequate and full consideration in money or money’s worth.” § 2053(a)(3)(c)(1)(A).

CONCLUSION:

This court ruling underscores the strict requirements for deducting claims arising from agreements between family members, particularly those tied to prenuptial agreements or testamentary arrangements. The Court found that the payments to the stepchildren to be contracted “in lieu” of Lueders’s rights as a surviving spouse, the stepchildren’s claims were “related to” Lueders’s “expectation or claim of inheritance,” and “lacked the other characteristics of a bona-fide transaction.” These conclusions were predicated upon the findings that the claims did not originate from any transaction between the stepchildren and Richard and the stepchildren had no obligations to perform under any agreement.

HOPE THIS HELPS YOU HELP OTHERS MAKE A POSITIVE DIFFERENCE!

Marc Soss