

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4-PLR-164160-01

Date:

NOVEMBER 19, 2002

Re:

Legend

Father	=
Mother	=
Son A	=
Son B	=
Date 1	=
Date 2	=
State	=

Dear :

This is in response to your letter dated November 13, 2002, and prior correspondence, requesting rulings concerning the income and gift tax consequences of the transaction described below.

The facts and representations submitted are summarized as follows. Father and Mother have two children, Son A and Son B. In 1992, Mother died from Alzheimer's disease. Father, concerned with his own medical situation and desiring a simple and orderly accounting of his affairs, deeded his personal residence, Residence, to his sons while retaining a life estate in Residence. Prior to the execution of the deed, Father requested and received an oral promise from his two sons to reconvey the property to Father in the event Father wanted the Residence returned. The deed was executed on Date 1. In early 1999, approximately 3 years later, Father desired to move to another state and requested a return of Residence in order to sell the property. Son A and B refused. Shortly thereafter, Father commenced a lawsuit in State court seeking to create a constructive trust and a reconveyance of the Residence to Father. After opposing Father's law suit, the Sons, under a stipulation of settlement dated, Date 2, and ordered by the court, deeded Residence to Father.

PLR-164160-01

You have requested rulings that: (1) the conveyance of Residence from Father to Sons A and B is not a completed gift under § 2511 of the Internal Revenue Code and will not be subject to tax under § 2501; (2) the reconveyance of the Residence from Sons A and B to Father will not be a gift under § 2511 and will not be subject to tax under § 2501; and (3) the conveyance and reconveyance of Residence will not cause Father, Son A or Son B to recognize income under § 61.

GIFT TAX RULING

Section 2501(a)(1) provides for the imposition of a gift tax on the transfer of property by gift. Section 2511(a) provides that the gift tax applies to a transfer by way of gift whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 25.2511-2(b) of the Gift Tax Regulations provides that a gift of property is complete to the extent the donor has so parted with dominion and control as to leave him no power to change its disposition, whether for his own benefit or for the benefit of another.

Section 25.2511-2(c) provides in part, that a gift is incomplete in every instance in which a donor reserves the power to revest the beneficial title to the property in himself. Similarly, in Burnet v. Guggenheim, 288 U.S. 280 (1933), the United States Supreme Court held that the Federal gift tax “is not aimed at every transfer of the legal title without consideration. Such a transfer there would be if the trustees were to hold for the use of the grantor. It is aimed at transfers of the title that have the quality of a gift, and a gift is not consummate until put beyond recall.” See also Rev. Rul. 54-537, 1954-2 C.B. 316, where the right to revest the beneficial title to property transferred in trust by the donor is an incomplete gift, and Rev. Rul. 74-365, 1974-2 C.B. 324, where the Service held a gift causa mortis was not a completed gift because the gift was revocable and the subsequent return of the property did not result in a gift.

In Farano v. Stephanelli, 183 N.Y.S. 2d 707 (N.Y.App. Div. 1959), a father deeded his house and two other properties to his three daughters with an oral agreement that if the father wanted the properties returned, the daughters would reconvey the properties to their father. The father continued to live in the house. Six months later the father requested a return of the properties and one of the daughters deeded her interest back to the father. The remaining daughters refused and father brought suit on the theory that a constructive trust was created. The trial court found there was no express promise of reconveyance. On appeal, the court cited the Restatement, Trusts, § 44, and, and other authorities that “a constructive trust will be imposed if the transfer was procured, among other things, by fraud or in an abuse of a confidential relationship.” The case was remanded for a new trial (even though the trial court found no express promise of conveyance) to determine, whether or not there was a tacit promise or understanding that the properties were to be reconveyed.

PLR-164160-01

In the present case, Father deeded Residence to his sons reserving not only a life estate but also the power to revest the property in himself. There is little doubt under the facts of this case and under State law, that Father was entitled to a return of Residence. As such, pursuant to a stipulated settlement, Sons deeded Residence to Father. Accordingly, we conclude Father's conveyance of Residence to Sons A and B is not a completed gift under § 2511 and will not be subject to tax under § 2501. See also § 25.2511-2(c) and Rev. Rul. 54-537. In addition, the reconveyance of Residence from Sons A and B to Father is not a gift by Son A and Son B under § 2511 and will not be subject to tax under § 2501.

INCOME TAX RULING

Section 61 provides that gross income means all income from whatever source derived. Section 1.61-1(a) of the Income Tax Regulations provides that income realized in any form, whether in money, property, or services is gross income. It is well-settled that "gross income" as that term is used in § 61 includes economic gains not covered by any specific statutory exclusion -- even though the same were realized without cost or consideration. Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955); Healy v. Commissioner, 345 U.S. 278 (1953); Corliss v. Bowers, 281 U.S. 376 (1930). In general, when a law-abiding taxpayer mistakenly receives income or property in one year, which receipt is assailed and found to be invalid in a subsequent year, the taxpayer must nonetheless report the amount as "gross income." United States v. Lewis, 340 U.S. 590 (1951); Healy v. Commissioner, *supra*. Mistake as to the validity of the recipient's claim to the property does not permit exception to the requirement of inclusion into the recipient's gross income. North American Oil v. Burnet, 286 U.S. 417 (1932).

However, in such cases where the court has held that a taxpayer receiving income or property either under a claim or right or through wrongful appropriations must include the value in gross income, the taxpayers has had either actual command over the property taxed or the actual benefit for which tax is paid. Corliss v. Bowers, *supra*; Zips v. Commissioner, 38 T.C. 620 (1962). During the entire period after the purported gift of Residence was made, Father continued to use the Residence and Son A and B never had either actual command or actual benefit from Residence. Son A and B realized no income in any form after they received Residence which was determined to be an invalid gift. The value of the property is not includible in the gross income of Son A and B. Moreover, in view of the foregoing conclusion, the issue of the income tax treatment upon reconveyance is moot.

Except as we have specifically ruled herein, we express no opinion under the cited provisions or under any other provision of the Code.

This ruling is based on the facts and applicable law in effect on the date of this letter. If there is a change in material fact or law (local or Federal), the ruling will have no force or effect. If the taxpayer is in doubt whether there has been a change in

PLR-164160-01

material fact or law, a request for reconsideration of this ruling should be submitted to this office.

This ruling is directed only to the taxpayers who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely yours,

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special
Industries)

Enclosure
Copy for section 6110 purposes