RECENT DEVELOPMENTS IN FIDUCIARY INCOME TAX

ABA SECTION OF TAXATION
2019 MIDYEAR MEETING
FIDUCIARY INCOME TAX COMMITTEE

NEW ORLEANS, LA
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Anna Katherine Moody
Emily A. Plocki
Venable LLP
600 Massachusetts Avenue NW
Washington, DC 20001
(202) 344-4000
akmoody@venable.com
eaplocki@venable.com
1. LEGISLATIVE & TREASURY UPDATE


.01 Tax Rate Tables. For taxable years beginning in 2019, the tax rate tables under § 1 are as follows:

<table>
<thead>
<tr>
<th>If Taxable Income Is:</th>
<th>The Tax Is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not over $2,600</td>
<td>10% of the taxable income</td>
</tr>
<tr>
<td>Over $2,600 but not over $9,300</td>
<td>$260 plus 24% of the excess over $2,600</td>
</tr>
<tr>
<td>Over $9,300 but not over $12,750</td>
<td>$1,868 plus 35% of the excess over $9,300</td>
</tr>
<tr>
<td>Over $12,750</td>
<td>$3,075.50 plus 37% of the excess over $12,750</td>
</tr>
</tbody>
</table>

.41 Unified Credit Against Estate Tax. For an estate of any decedent dying in calendar year 2019, the basic exclusion amount is $11,400,000 for determining the amount of the unified credit against estate tax under § 2010.

b. IRS Section 20.2010-1(c) Proposed Regulations on Estate and Gift Taxes; Difference in the Basic Exclusion Amount (November 23, 2018)

In computing the amount of Federal gift tax to be paid on a gift or the amount of Federal estate tax to be paid at death, the gift and estate tax provisions of the Internal Revenue Code (Code) apply a unified rate schedule to the taxpayer's cumulative taxable gifts and taxable estate on death to arrive at a net tentative tax. Prior to January 1, 2018, for estates of decedents dying and gifts made beginning in 2011, section 2010(c)(3) provided a basic exclusion amount ("BEA") of $5 million, indexed for inflation after 2011. The credit is applied first against the gift tax, on a cumulative basis, as taxable gifts are made. To the extent that any credit remains at death, it is applied against the estate tax.

Section 11061 of the TCJA amended section 2010(c)(3) to provide that, for decedents dying and gifts made after December 31, 2017, and before January 1, 2026, the BEA is increased by $5 million to $10 million as adjusted for inflation (increased BEA). On January 1, 2026, the BEA will revert to $5 million. Thus, an individual or the individual's estate may utilize the increased BEA to shelter from gift and estate taxes an additional $5 million of transfers made
during the eight-year period beginning on January 1, 2018, and ending on December 31, 2025 (increased BEA period).

In addition, section 11002 of the TCJA amended section 1(f)(3) of the Code to base the determination of annual cost-of-living adjustments, including those for gift and estate tax purposes, on the Chained Consumer Price Index for All Urban Consumers for all taxable years beginning after December 31, 2017. Section 11002 of the TCJA also made conforming changes in sections 2010(c)(3)(B)(ii), 2032A(a)(3)(B), and 2503(b)(2)(B).

The Preamble to the Proposed Regulations clarifies that, for gift tax purposes, the increased BEA available during the increased BEA period is not reduced by pre-2018 gifts on which gift tax actually was paid. Further, for estate tax purposes, the increased BEA available during the increased BEA period is not reduced by pre-2018 gifts on which gift tax actually was paid. Further, the Preamble clarifies that, in the instance of a post-2025 gift, the full amount of the gift tax liability on the increased BEA period gifts is removed from the gift tax computation, regardless of whether that liability was sheltered from gift tax by the BEA or was satisfied by a gift tax payment.

The Proposed Regulations provide that, for estate tax purposes, a gift made during the increased BEA period that was sheltered from gift tax by the increased BEA will not inflate post-2025 estate tax liability.


Part 1: Implementation of Tax Cuts and Jobs Act

- Final regulations on computational, definitional, and anti-avoidance rules under new §199A and §643(f). Proposed regulations on computational, definitional, and anti-avoidance guidance under new §199A and §643(f) published on August 16, 2018 in FR as REG-107892-18 (NPRM) (Released on August 8, 2018).
- Guidance implementing changes made to §529 by sections 11025 and 11032 of the TCJA and section 302 of the Protecting Americans from Tax Hikes (PATH) Act of 2015.
  - PUBLISHED 08/13/18 in IRB 2018-33 as NOT. 2018-58 (RELEASED 07/30/18).
- Notice on the increased contribution limit to §529A ABLE accounts, as added by section 11024 of the TCJA.
  - PUBLISHED 08/20/18 in IRB 2018-34 as NOT. 2018-62 (RELEASED 08/03/18)
- Guidance implementing changes to §1361 regarding electing small business trusts.
- Regulations under §2010 addressing the computation of the estate tax in the event of a difference between the basic exclusion amount applicable to gifts and that applicable at the donor’s date of death.
- Regulations under §170 providing rules governing the availability of the charitable contribution deduction when a taxpayer receives or expects to receive a state or local tax credit.
  - PUBLISHED 08/27/18 in FR as REG-112176-18 (NPRM).
Part 3: Burden Reduction

- Final regulations under §§1014(f) and 6035 regarding basis consistency between estate and person acquiring property from decedent. Proposed and temporary regulations were published on March 4, 2016.
- Guidance under §170(e)(3) regarding charitable contributions of inventory.
- Final regulations under §2642(g) describing the circumstances and procedures under which an extension of time will be granted to allocate GST exemption.
- Final regulations streamlining the §754 election statement. Proposed regulations were published on October 12, 2017.
- Guidance under §1362(f) regarding the validity or continuation of an S corporation election in certain situations involving disproportionate distributions, inconsistent tax return filings, or omissions on Form 2553, Election by a Small Business Corporation.

Part 5: General Guidance; Gifts and Estates and Trusts

- Guidance on basis of grantor trust assets at death under §1014.
- Final regulations under §2032(a) regarding imposition of restrictions on estate assets during the six month alternate valuation period. Proposed regulations were published on November 18, 2011.
- Regulations under §2053 regarding personal guarantees and the application of present value concepts in determining the deductible amount of expenses and claims against the estate.
- Regulations under §7520 regarding the use of actuarial tables in valuing annuities, interests for life or terms of years, and remainder or reversionary interests.

**d. IRS Section 1400Z-2 Proposed Regulations on Investing in Qualified Opportunity Funds (October 29, 2018)**

Section 1400Z-2, in conjunction with section 1400Z-1, seeks to encourage economic growth and investment in designated distressed communities (qualified opportunity zones) by providing Federal income tax benefits to taxpayers who invest in businesses located within these zones. Section 1400Z-2 provides two main tax incentives to encourage investment in qualified opportunity zones. First, it allows for the deferral of inclusion in gross income for certain gains to the extent that corresponding amounts are reinvested in a qualified opportunity fund (“QOF”). Second, it excludes from gross income the post-acquisition gains on investments in QOFs that are held for at least 10 years.

The proposed regulations provide rules that permit a partnership to elect deferral under section 1400Z-2 and, to the extent that the partnership does not elect deferral, provide rules that allow a partner to do so. These rules both clarify the circumstances under which each can elect and clarify when the applicable 180-day period begins. The proposed regulations state that rules analogous to the rules provided for partnerships and partners apply to other pass-through entities (including S corporations, decedents’ estates, and trusts) and to their shareholders and beneficiaries.
The American College of Trust and Estate Counsel (ACTEC) submitted comments regarding Section 1400Z-2 Proposed Regulations on December 27, 2018 requesting clarification on the following issues:

- The income tax consequences resulting from the death of a taxpayer who has deferred gain through a timely reinvestment of gain in a QOF, and to provide relief for successors-in-interest. Section 1400Z-2(e)(3) provides that, “[i]n the case of a decedent, amounts recognized under this section shall, if not properly includible in the gross income of the decedent, be includible in gross income as provided by section 691.” This statutory provision raises questions concerning the appropriate treatment of the deferred gain where a person who has rolled over gain through a timely investment in a QOF dies prior to December 31, 2026 without having previously disposed of the QOF investment.
- The income tax consequences resulting from the gift of an interest in a QOF where the donor has deferred gain through a timely reinvestment of gain in a QOF.
- Clarification concerning grantor trusts, including confirmation that a transaction with a grantor trust that is disregarded for income tax purposes pursuant to Rev. Rul. 85-13 should not be considered a sale or exchange of an interest in a QOF.
- A request that relief be provided to extend the 180-day period for rollover of gain to a QOF should be granted to partners, S corporation shareholders and beneficiaries of estates and trusts because they may not receive a Schedule K-1 indicating capital gains until more than 180 days after the end of the taxable year.

**e. Comments to Proposed Regulations under Section 199A and 643(f)**

The American College of Trust and Estate Counsel (ACTEC) submitted comments regarding Section 199A and 643(f) Proposed Regulations on September 27, 2018 on the following issues:

- The Treasury and the IRS’s request for comments on providing a special rule for a relevant passthrough entity (“RPE”) with no owners having taxable income above the threshold amount that would exempt the RPE from determining and reporting W-2 wages, unadjusted basis immediately after acquisition (“UBIA”) of qualified property, and whether the trade or business is a specified service trade or business (“SSTB”). ACTEC believes that having this special rule would avoid unnecessary compliance costs for RPEs, would reduce potential confusion on the part of owners who do not need this additional information, and would reduce the amount of unnecessary information provided to the IRS.
- As the Preamble states, section 199A(c)(4) provides that qualified business income (“QBI”) does not include reasonable compensation paid to a taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business, any guaranteed payment described in section 707(c) paid to a partner for services rendered with respect to the trade or business, and to the extent provided in regulations, any payment described in section 707(a) to a partner for services rendered with respect to the trade or business. Although the legislative history for section 199A does not explain why these items were excluded, ACTEC suggests that the intent was to prevent a taxpayer who provides services to a single trade or business from having QBI with respect to payments it receives for those services. ACTEC does not believe that this exclusion was intended to apply to payments described in section 707(a) or (c) earned by a taxpayer that conducts its
own trade or business, so long as that trade or business is not focused primarily on providing services to only one qualified trade or business. Therefore, ACTEC recommends proposed section 1.199A-3(b)(2)(ii)(I) and (J) provide an exception when payments are made to a service provider conducting its own trade or business.

- Commenting on the aggregation rules of proposed section 1.199A-4, ACTEC suggests that the rules be expanded to include attribution used in other areas of the proposed regulations and the tax laws, such as expanding the persons included as a family member and providing for an alternative ownership test focused on voting rights. ACTEC would also appreciate clarification regarding the manner in which beneficial interests in trusts are considered for purposes of aggregation.

- ACTEC has concerns regarding the threshold amount generally and also how it applies to electing small business trusts (ESBTs).
  - Proposed section 1.199A-6(d)(3)(iii) would require trusts and estates to determine their taxable income before any income distribution deduction in order to determine whether taxable income exceeds the threshold amount, thereby counting twice (at the trust level and at the beneficiary level) any taxable income reported to a beneficiary on a Schedule K-1. ACTEC believes this violates section 199A(e)(1), which takes into account all taxable income, modified by disregarding only the section 199A deduction.
  - ACTEC also requested confirmation that the taxable income threshold would apply separately for the S portion and the non-S portion. ACTEC believes that proposed section 1.199A-6(d)(3)(v), “Anti-abuse rule for creation of multiple trusts to avoid exceeding the threshold amount.” is overbroad and should focus on what would be considered abusive and describe appropriate consequences.
  - ACTEC is concerned with section 1.199A-6(d)(3)(vi), Example (1), which seems to overlook section 167(d).

- Section 643(f) contains at least one undefined term, “primary beneficiary,” and the legislative history does not clarify its definition but rather injects uncertainty. Proposed section 1.643(f)-1 seems to redefine “principal purpose.” ACTEC requested clarification of the terms “primary beneficiary” and “principal purpose” and guidance on when “primary beneficiaries” and “grantors” are each considered to be substantially the same.

- ACTEC requested clarification be made to the definitions of “unadjusted basis immediately after acquisition” (“UBIA”) of “qualified property” of a taxpayer, and the “depreciable period” with respect to such qualified property, under section 199A(b)(6)(B). The comments include the effect of a taxpayer’s death or the contribution of property to partnerships by partners and to S corporations by shareholders.

- Section 199A does not specifically address the proper treatment of the deduction by charitable remainder trusts (“CRTs”).
  - Although CRTs are trusts for tax purposes, they are governed by section 664, rather than the rules that apply to taxable trusts. Further complicating the application of section 199A to CRTs is the fact that CRTs are hybrids because a CRT is not subject to income tax unless it has unrelated business taxable income (“UBTI”), but beneficiaries of CRTs are taxed on CRT distributions under a “worst in-first out” tier system designed to tax the most highly taxed types of income first, whether earned in the current year or earned and accumulated in any prior year.
ACTEC notes at the outset that this is not an issue that often arises. Since UBTI is subject to a 100% excise tax under section 664(c), well-advised trustees will avoid holding any assets that may generate UBTI. The only types of income that would qualify as QBI but not be UBTI would be real estate rentals, REIT dividends, royalty income, and possibly a few other narrow categories of income.

ACTEC also notes that QBI cannot be a separate tier in the section 664 tier classification system. The tiers described in section 664 are separated by a difference in tax rate. The section 199A deduction is a deduction, not a rate difference.

Because a CRT does not have taxable income, its section 199A items would be treated as an RPE in the same manner as a trust to the extent of the beneficiaries’ share of distributable net income. However, given a CRT’s tier level, ACTEC believes that QBI should be at the bottom of tier 1 (meaning that it is the last income item from tier 1 to be distributed), and the section 199A items would be reported to a beneficiary on a Schedule K-1 when the associated QBI is considered to have been distributed.

2. CASE LAW

a. Kaestner & Fielding


FACTS:

The taxpayer acquired a tract of land near Birmingham, Alabama, and conveyed to a qualified land trust, in 2005, 2006, and 2007, easements covering relatively small portions of that property. Each easement defined a conservation area that was to be restricted in perpetuity from commercial and residential development, with a carve-out in the 2005 and 2006 easements for 16 reserved “building areas,” within each of which P could construct a single-family residence. The 2006 easement did not specify the location of the building areas, and the 2005 easement permitted the taxpayer (with the qualified land trust’s consent) to move the building areas from their initially designated locations to any other location within the conservation area. The 2005 easement also reserved to the taxpayer the rights to construct, within the conservation area, other facilities appurtenant to residential development, such as barns, riding stables, scenic overlooks, and boat storage buildings, some of which could include additional living quarters.
The taxpayer claimed charitable contribution deductions for the easements on its 2005, 2006, and 2007 tax returns. The Service contends that the easements were not “qualified real property interest[s]” under I.R.C. sec. 170(h)(1)(A); that the easements were not made “exclusively for conservation purposes” under I.R.C. sec. 170(h)(1)(C); and that the taxpayer overstated the fair market values of the easements.

**HOLDINGS:**

1. The 2005 and 2006 easements did not restrict a specific, identifiable piece of real property because they allowed supposedly conserved land to be taken back and used for residential development. Because neither easement constituted “a restriction (granted in perpetuity) on the use which may be made of the real property,” I.R.C. sec. 170(h)(2)(C), neither easement constituted a “qualified real property interest” that could give rise to a charitable contribution deduction under I.R.C. sec. 170(h)(1)(A). Belk v. Commissioner, 774 F.3d 221 (4th Cir. 2014), aff’d 140 T.C. 1 (2013), followed.

2. The 2007 easement covered a specific, identifiable piece of real property and was “granted in perpetuity” under I.R.C. sec. 170(h)(2)(C). The 2007 easement was made “exclusively for conservation purposes” under I.R.C. sec. 170(h)(1)(C). Further, the inclusion in the 2007 easement of a provision allowing amendments, provided that they were “not inconsistent with the conservation purposes of the donation,” did not prevent that easement from satisfying the granted-in-perpetuity requirement of I.R.C. sec. 170(h)(2)(C).

**ANALYSIS:**

Section 170(a)(1) allows a deduction for any charitable contribution made within the taxable year. If the taxpayer makes a charitable contribution of property other than money, the amount of the contribution is generally equal to the fair market value of the property at the time the gift is made. See sec. 1.170A-1(c)(1), Income Tax Regs. The Code generally restricts a taxpayer’s charitable contribution deduction for the donation of “an interest in property which consists of less than the taxpayer’s entire interest in such property.” Sec. 170(f)(3)(A). But there is an exception to this rule for a “qualified conservation contribution.” Sec. 170(f)(3)(B)(iii). This exception applies where: (1) the taxpayer makes a contribution of a “qualified real property interest,” (2) the donee is a “qualified organization,” and (3) the contribution is “exclusively for conservation purposes.” Sec. 170(h)(1). “Any rights reserved by the donor in the donation of a perpetual conservation restriction must conform to the requirements” of section 170(h) and the regulations thereunder. Sec. 1.170A14(b)(2), Income Tax Regs.

Regarding the 2005 and 2006 easements, the IRS contends that the easements do not constitute “qualified real property interest[s]” because the restrictions on the use that could be made of the conserved land were not “granted in perpetuity.” Sec. 170(h)(2)(C). That is so, in the IRS’ view, because the “Reserved Rights” enumerated in the easements enable the developer to take back supposedly conserved land and dedicate it to residential development. That development could consist of up to 16 single-family residences, as well as boathouses, riding stables, scenic overlook outbuildings, and other structures intended for the homeowners’ recreation and enjoyment.
The 2006 easement permits the taxpayer to establish within the 2006 Conservation Area six Building Areas, each as large as one acre. Each Building Area may include a single-family dwelling plus “a shed, garage, gazebo, and pool,” and the owner of each Building Area may construct a 5,000-square-foot barn within 1,000 feet of its perimeter. However, the 2006 easement does not specify, either in the deed itself or in an attached plat, the locations of the six Building Areas, and it places no limitations on where within the 2006 Conservation Area such Building Areas may be located, except to say that these locations must be “approved in advance” by the North American Land Trust (“NALT”). The Court found that the 2006 easement does not embody “a restriction (granted in perpetuity) on the use which may be made of the real property.” See sec. 170(h)(2)(C). Although the restriction placed by the easement is perpetual, “the restriction on ‘the real property’ is not.” Belk v. Commissioner (“Belk III”), 774 F.3d 221, at 226 (quoting section 170(h)(2)(C)). Pine Mountain remained free to build a six-acre residential development within the 2006 Conservation Area, thus converting to commercial use land that was supposed to be protected in perpetuity from development. NALT had to approve the precise location of the six residences within the 2006 Conservation Area. By so doing, NALT might minimize the derogation of conservation values that the subdivision caused and perhaps ensure that “the conservation purpose [wa]s protected in perpetuity.” Sec. 170(h)(5)(A). But this does not change the fact that the easement, when granted, did not create a perpetual use restriction on a defined parcel of land, as required by section 170(h)(2)(C). Because the 2006 easement does not constitute a “qualified real property interest,” Pine Mountain could not claim for the donation of this interest a charitable contribution deduction under section 170(f)(3)(B)(iii) and (h)(1).

Most of the 2005 Conservation Area consists of ridgelines and higher elevation land and the balance consists of lower lying land around a man-made lake. Overall the easement covers about 47% of the acreage of Parcel 2. It reserves to Pine Mountain or individual homeowners the rights to construct one single-family dwelling and appurtenant structures within each of ten “Building Areas” inside the 2005 Conservation Area. Although the deed itself does not limit the size or location of these ten Building Areas, a plat shows each Building Area as a one-acre lot situated around the man-made lake. The easement, however, provides that the “boundaries of the Building Areas may be modified by mutual agreement” of the taxpayer and NALT. Such modification is subject to the proviso that “the areas of a Building Area shall not be increased” and that the boundary modifications shall not, in NALT’s “reasonable judgment,” adversely affect conservation purposes. The easement thus permits the Building Areas to be relocated (with NALT’s consent) to higher elevation zones or to other locations within the 2005 Conservation Area. The court concluded that the rights reserved to the taxpayer, considered in their entirety, prevent the 2005 easement from constituting a “qualified real property interest.” See sec. 170(h)(2).

Unlike the other two easements, the 2007 easement designates no “Building Areas” and permits no residential construction anywhere within the 2007 Conservation Area. It likewise reserves to Pine Mountain no rights to construct scenic overlooks, barns, riding stables, boat storage buildings, piers, or other structures appurtenant to residential development. Apart from hunting blinds, the only structure permitted within the 2007 Conservation Area is a water tower to which may be attached underground pipes to provide water service to other parts of the Pine Mountain property. Although the water tower, if poorly placed, could conceivably affect whether
“the conservation purpose is protected in perpetuity” under section 170(h)(5)(A), the court concluded that it has no effect on whether the use restriction attaches in perpetuity “to a defined parcel of real property” as required by section 170(h)(2)(C).

c. **Chrem v. Commissioner, T.C. Memo. 2018-164**

**FACTS:**

Petitioners (along with eight other individuals or couples) owned 100% of the stock of Comtrad Trading, Ltd. (“Comtrad”), a closely held Hong Kong corporation. A related company proposed to purchase 100% of Comtrad’s stock for $4,500 per share. After Comtrad’s shareholders agreed to tender about 87% of their shares, Petitioners donated the balance of their stock to a charitable organization, the Jewish Communal Fund (“JCF”). The acquiring company, SDI Technologies, Inc. (“SDI”), whose shares were owned by an ESOP, then completed the acquisition, purchasing the donated stock for $4,500 per share.

On their 2012 Federal income tax returns, Petitioners claimed charitable contribution deductions for their gifts, valuing the donated stock at $4,500 per share. In timely notices of deficiency the Internal Revenue Service (“IRS” or “Respondent”) determined that petitioners were liable for tax under the assignment of income doctrine on their transfers of stock to the charity. The IRS also determined that Petitioners had failed to obtain and (where applicable) attach to their returns “qualified appraisals” of the donated property. See sec. 170(f)(11)(C) and (D). The Petitioners filed a motion for summary judgment as to the assignment of income issue and both parties filed cross-motions for summary judgment as to the appraisal issue. The Court denied all motions.

**ASSIGNMENT OF INCOME ISSUE:**

Petitioners seek summary judgment on Respondent’s application of the assignment of income doctrine to their donations of stock. A longstanding principle of tax law is that income is taxed to the person who earns it. United States v. Basye, 410 U.S. 441, 450 (1973) (“[H]e who earns income may not avoid taxation through anticipatory arrangements no matter how clever or subtle[.]”). Thus, a person anticipating receipt of income “cannot avoid taxation by entering into a contractual arrangement whereby that income is diverted to some other person.” Id. at 449 (citing Lucas v. Earl, 281 U.S. 111, 115 (1930)).

The Court had previously considered the assignment of income doctrine as applied to charitable contributions. In the typical scenario, the taxpayer donates to a charity stock that is about to be acquired by the issuing corporation via redemption, or by another corporation via merger or acquisition. In determining whether the taxpayer has assigned income in these circumstances, one relevant question is whether the prospective acquisition is a mere expectation or a virtual certainty. “More than expectation or anticipation of income is required before the assignment of income doctrine applies.” Greene v. United States, 13 F.3d 577, 582 (2d Cir. 1994). Another relevant question is whether the charity is obligated, or can be compelled by one of the parties to the transaction, to surrender the donated shares to the acquirer. Rev. Rul. 78-197, 1978-1 C.B. 83 (1978); see Rauenhorst v. Commissioner, 119 T.C. 157, 166 (2002) (finding “the donee’s
control to be *** an important factor"). The Court concluded that there existed genuine disputes of material fact that prevented the Court from resolving the assignment of income issue summarily, and, therefore, denied summary judgment.

**QUALIFIED APPRAISAL ISSUE:**

Section 170(a)(1) allows as a deduction for any charitable contribution made within the taxable year. If the taxpayer makes a charitable contribution of property other than money, the amount of the contribution is generally equal to the FMV of the property when contributed. See sec. 1.170A-1(c)(1), Income Tax Regs. “A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary.” Sec. 170(a)(1). When a taxpayer makes a charitable contribution of property (other than publicly traded securities) valued in excess of $5,000, he is required to secure a “qualified appraisal.” Sec. 170(f)(11)(C). If he claims a value in excess of $500,000 for such property, he is required to attach a copy of the appraisal to his return. Sec. 170(f)(11)(D).

The regulations prescribed by the Secretary require that a “qualified appraisal” include (among other things) the following: (1) “[a] description of the property in sufficient detail for a person who is not generally familiar with the type of property to ascertain that the property that was appraised is the property that was (or will be) contributed,” (2) a “statement that the appraisal was prepared for income tax purposes,” (3) “[t]he date (or expected date) of contribution to the donee,” (4) “[t]he date (or dates) on which the property was appraised,” and (5) “[t]he appraised fair market value * * * of the property.” Sec. 1.170A-13(c)(3)(ii), Income Tax Regs. None of Petitioners secured for their contributions, or attached to their returns, an appraisal that was addressed to them.

However, each of Petitioners’ returns included an “appraisal summary” on Form 8283, Noncash Charitable Contributions. In Part I of these forms, captioned “Information on Donated Property,” Petitioners noted the number of Comtrad shares that each had donated. They stated that they had acquired those shares by purchase and supplied their respective cost bases for the donated shares. Gregory Sullivan, the managing director of Empire who had signed the fairness opinion issued to the ESOP trustee, signed the “Declaration of Appraiser” on each Form 8283. Saul Wadowski, an officer of JCF, signed the “Donee Acknowledgment” on each form, which listed December 5, 2012, as the date on which JCF had received the donated stock.

Even if Petitioners did not strictly or substantially comply with the regulatory reporting requirements, they all sought haven in section 170(f)(11)(A)(ii)(II). That provision excuses failure to satisfy the reporting requirements discussed above if it is shown that such failure “is due to reasonable cause and not to willful neglect.” Petitioners alleged that their 2012 returns were prepared by an experienced certified public accountant (“CPA”), that they supplied her with the Empire report and all relevant information about the Comtrad stock acquisition, and that she did not direct any of the Petitioners to include a copy of the Empire report with their returns. The record as it stands was silent concerning the advice (if any) that the CPA provided the Petitioners regarding the Empire report and whether they relied in good faith on whatever advice she may have supplied. For these reasons, the Court concluded that Petitioners’ ability to rely on the
“reasonable cause” defense of section 170(f)(11)(A)(ii)(II) presents genuine disputes of material fact that are not susceptible to resolution by summary judgment.

3. OTHER GUIDANCE

a. PLR 201850004 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners

See also:
- PLR 201850006 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners
- PLR 201850001 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners
- PLR 201850003 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners
- PLR 201850002 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners
- PLR 201850005 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners
- PLR 201848002 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners
- PLR 201848009 - Section 671 - Trust income, deductions, and credits attributable to grantors and others as substantial owners

FACTS:

On Date, Grantor and Spouse (collectively Grantors) created Trust, an irrevocable trust, for the benefit of Grantors, Grantors’ issue, and Friend 1 and Friend 2 (collectively the “Beneficiaries”). A corporate trustee is Trustee of Trust. The situs of Trust is State 1.

Grantors are married and reside in State 2, a community property state. Trust provides that all property transferred to Trust is community property. Moreover, any and all property transferred to Trust prior to the death of the first spouse to die (Predeceased Grantor) is and shall retain its character as community property.

During Grantors’ lifetimes, Trustee must distribute such amounts of net income and/or principal to each Grantor and the Beneficiaries as directed by the Power of Appointment Committee and/or Grantors, as follows:

(1) Trustee, pursuant to a writing executed by either of the Grantors and by a majority of the other members of the Power of Appointment Committee, shall distribute to the Beneficiaries and/or Grantors such amounts of income or principal (including the whole thereof) as the Power of Appointment Committee appoints. (Grantor’s Consent Power);
(2) Trustee, pursuant to a writing executed by all then serving members of the Power of Appointment Committee other than Grantors, shall distribute to or for the benefit of the Beneficiaries and/or Grantors such amounts of income or principal (including the whole thereof) as the Power of Appointment Committee appoints. (Unanimous Member Power); and

(3) Each Grantor has the power, in a nonfiduciary capacity, at any time and from time to time, to appoint to any one or more of the Beneficiaries, such amounts of the principal (including the whole thereof) as such Grantor deems advisable to provide for the health, education, maintenance, or support of the Beneficiaries. (Grantor’s Sole Power).

The Power of Appointment Committee may appoint income or principal equally or unequally and to or for the benefit of either or both of Grantors, or any one or more of the Beneficiaries of Trust to the exclusion of others. Any net income not distributed by Trustee will be accumulated and added to principal.

The Power of Appointment Committee is composed of Grantors, Child 1, Guardian acting on behalf of Child 2, Friend 1 and Friend 2. Daughter, while a minor, is considered a member of the Power of Appointment Committee acting through her Guardian. If at any time the Power of Appointment Committee includes three or more members, other than the Grantors, then all the members of the Power of Appointment Committee including the Grantors may by unanimous vote, at any time and from time to time, add one or more members of the Power of Appointment Committee provided that such members are Beneficiaries and, provided further that, if any one or more of them is a minor, the members of the Power of Appointment Committee shall by unanimous vote have designated an individual to serve as Guardian for such minor. The members of the Power of Appointment Committee in their capacities as such shall not serve or act in a fiduciary capacity. The Power of Appointment Committee ceases to exist upon the first to occur of the death of the Survivor of the Predeceased Grantor, or the date the Power of Appointment Committee is reduced to one member, other than Grantors.

If the Power of Appointment Committee ceases to exist prior to the Distribution Date the Trustee may, pursuant to a written instrument, at any time distribute to the Beneficiaries and/or Grantors such amounts of the net income or principal of Trust (including the whole thereof) as the Trustee determines.

Any distribution from Trust to either Grantor prior to the death of the Predeceased Grantor will be a distribution of community property. Any distribution of income or principal from Trust to a beneficiary prior to the death of the Predeceased Spouse, whether made by the Power of Appointment Committee, the Trustee, or a Grantor’s exercise of the powers retained by Grantors will be a distribution of community property.

With respect to the lifetime powers of appointment retained by Grantors, prior to the death of the Predeceased Grantor, any such appointment by Grantor of the principal of Trust will be funded equally from each Grantor’s share of community property. Each Grantor consents to all distributions by the other Grantor.
With respect to the testamentary power of appointment retained by the Predeceased Spouse, any appointment by the Predeceased Spouse shall be funded solely from the Predeceased Spouse’s one-half interest in the property held Trust.

Upon the death of the Predeceased Grantor, Trustee shall distribute the Predeceased Grantor’s entire interest in the trust property to or for the benefit of any person or entity or entities, other than the Predeceased Grantor’s estate, the Predeceased Grantor’s creditors, or the creditors of the Predeceased Grantor’s estate, as Predeceased Grantor appoints by will (Predeceased Grantor’s Testamentary Power).

Upon the death of the Predeceased Grantor, any remaining property held in Trust in the Predeceased Grantor’s one-half interest that has not been effectively appointed by will, shall be distributed five percent (5%) to each serving member of the Power of Appointment Committee other than the Grantor’s issue, and any remaining balance shall be distributed, per stirpes, to the Grantor’s issue who are then living subject to restrictions in the trust for beneficiaries article. If none, such remaining balance shall be disposed of under an alternate disposition article which provides for distributions according to applicable state law.

Upon the death of the Surviving Grantor, Trustee shall distribute the balance of Trust to or for the benefit of any person or entity or entities, other than the Surviving Grantor’s estate, the Surviving Grantor’s creditors, or the creditors of the Surviving Grantor’s estate, as Surviving Grantor appoints by will (Surviving Grantor’s Testamentary Power).

Upon the death of the Surviving Grantor, any remaining property held in Trust that has not been effectively appointed by will shall be distributed, five percent (5%) to each serving member of the Power of Appointment Committee other than the Grantor’s issue, and any remaining balance shall be distributed, per stirpes to the Grantor’s issue who are then living subject to restrictions in the trust for beneficiaries article. If none, such remaining balance shall be disposed of under an alternate disposition article which provides for distributions according to applicable state law.

No distribution by the Trustee to a beneficiary, and no distribution to a beneficiary pursuant to the exercise of a power of appointment granted hereunder, shall discharge any individual’s legal obligation to support the beneficiary.

RULINGS REQUESTED:

1. As long as the Power of Appointment Committee is serving, no portion of the items of income, deductions, and credits against tax of Trust shall be included in computing under § 671 the taxable income, deductions, and credits of Grantors or any member of the Power of Appointment Committee.

2. The contribution of property to Trust by Grantors will not be a completed gift subject to federal gift tax.
3. Any distribution of property by the Power of Appointment Committee from Trust to either Grantor will not be a completed gift, subject to federal gift tax, by any member of the Power of Appointment Committee.

4. Any distribution of property by the Power of Appointment Committee from Trust to any beneficiary of Trust, other than to either Grantor, will not be a completed gift subject to federal gift tax, by any member of the Power of Appointment Committee.

5. No member of the Power of Appointment Committee upon his or her death will include in his or her estate any property held in Trust because such member is deemed to have a general power of appointment within the meaning of § 2041 over property held in Trust.

6. The basis of all community property in Trust on the date of the death of the Predeceased Grantor will receive an adjustment in basis to the fair market value of such property at the date of death of the Predeceased Grantor.

RULING 1

Section 671 provides that where it is specified in subpart E of part I of subchapter J that the grantor or another person shall be treated as the owner of any portion of a trust, there shall then be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust which are attributable to that portion of the trust to the extent that such items would be taken into account under chapter 1 in computing taxable income or credits against the tax of an individual.

Section 672(a) provides, for purposes of subpart E, that the term “adverse party” means any person having a substantial beneficial interest in the trust which would be adversely affected by the exercise or nonexercise of the power which he possesses respecting the trust.

Sections 673 through 677 specify the circumstances under which the grantor is treated as the owner of a portion of a trust.

Section 673(a) provides that the grantor shall be treated as the owner of any portion of a trust in which the grantor has a reversionary interest in either the corpus or the income therefrom, if, as of the inception of that portion of the trust, the value of such interest exceeds five percent of the value of such portion.

Section 674(a) provides, in general, that the grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

Section 674(b) provides that § 674(a) shall not apply to the power in § 674(b)(5) regardless of by whom held.
Section 674(b)(3) provides that § 674(a) shall not apply to a power exercisable only by will, other than a power in the grantor to appoint by will the income of the trust where the income is accumulated for such disposition by the grantor or may be so accumulated in the discretion of the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

Section 674(b)(5) provides that § 674(a) shall not apply to a power to distribute corpus to or for a beneficiary, provided that the power is limited by a reasonably definite standard.

Section 674(c) provides that § 674(a) shall not apply to a power exercisable (without the approval or consent of any other person) by a trustee or trustees, none of whom is the grantor, and no more than half of whom are related or subordinate parties who are subservient to the wishes of the grantor (1) to distribute, apportion, or accumulate income to or for a beneficiary or beneficiaries, or to, for, or within a class of beneficiaries, or (2) to pay out corpus to or for a beneficiary or beneficiaries or to a class of beneficiaries (whether or not income beneficiaries).

Under § 675 and applicable regulations, the grantor is treated as the owner of any portion of a trust if, under the terms of the trust agreement or circumstances attendant to its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiary of the trust.

Section 676(a) provides that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under any other provision of part I, subchapter J, chapter 1, where at any time the power to revest in the grantor title to such portion is exercisable by the grantor or a nonadverse party, or both.

Section 677(a) provides, in general, that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under § 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a nonadverse party, or both, may be (1) distributed to the grantor or the grantor’s spouse; (2) held or accumulated for future distribution to the grantor or the grantor’s spouse; or (3) applied to the payment of premiums on policies of insurance on the life of the grantor or the grantor’s spouse.

Section 678(a) provides that a person other than the grantor shall be treated as the owner of any portion of a trust with respect to which: (1) such person has a power exercisable solely by himself to vest the corpus or the income therefrom in himself, or (2) such person has previously partially released or otherwise modified such a power and after the release or modification retains such control as would, within the principles of §§ 671-677, inclusive, subject a grantor of a trust to treatment as the owner thereof.

Section 679(a) provides that a United States person who directly or indirectly transfers property to a foreign trust shall be treated as the owner for his taxable year of the portion of such trust attributable to such property if for such year there is a United States beneficiary of any portion of the trust.

Based solely on the facts submitted and representations made, we conclude that an examination of Trust reveals none of the circumstances that would cause either Grantor to be
treated as the owner of any portion of Trust under §§ 673, 674, 676, or 677 as long as the Power of Appointment Committee remains in existence and is serving because none of the Power of Appointment Committee members has a power exercisable solely by himself, to vest Trust income or corpus in himself, none shall be treated as the owner of any portion of the Trust under § 678(a).

We further conclude that an examination of Trust reveals none of the circumstances that would cause administrative controls to be considered exercisable primarily for the benefit of either Grantor under § 675. Thus, the circumstances attendant to the operation of Trust will determine whether either Grantor will be treated as the owner of any portion of Trust under § 675. This is a question of fact, the determination of which must be deferred until the federal income tax returns of the parties involved have been examined by the office with responsibility for such examination.

RULINGS 2 AND 3 [ANALYSIS OMITTED]

Accordingly, based on the facts submitted and the representations made, we conclude that the contribution of property to Trust by Grantors is not a completed gift subject to federal gift tax. Any distribution from Trust to either Grantor prior to the death of the Predeceased Grantor is a distribution of community property. Any distribution from Trust to either Grantor is merely a return of each Grantor’s property. Therefore, we conclude that any distribution of property from Trust by the Power of Appointment Committee to either Grantor will not be a completed gift subject to federal gift tax, by any member of the Power of Appointment Committee. Further, upon the Predeceased Spouse's death, the fair market value of the Predeceased Spouse's interest in Trust is includible in the Predeceased Grantor's gross estate for federal estate tax purposes. Moreover, upon the Surviving Grantor's death, the fair market value of the balance in Trust is includible in the Surviving Grantor's gross estate for federal estate tax purposes.

RULINGS 4 AND 5 [ANALYSIS OMITTED]

Based upon the facts submitted and representations made, we conclude that any distribution of property by the Power of Appointment Committee from Trust to any beneficiary of Trust, other than the Grantors, will not be a completed gift subject to federal gift tax, by any member of the Power of Appointment Committee. Further, we conclude that any distribution of property from Trust to a beneficiary other than Grantors will be a completed gift by the Grantors. Trust provides that all distributions of the net income or principal prior to the death of the Predeceased Spouse, whether made by the Power of Appointment Committee, the Disinterested Trustee or a Grantor's exercise of the powers retained by such Grantor, to a beneficiary is and shall be a distribution out of community property. Accordingly, distributions to beneficiaries, other than Grantors, will be gifts made one-half by each Grantor. Finally, we conclude that the powers held by the Power of Appointment Committee members are not general powers of appointment for purposes of § 2041(a)(2) and, accordingly, the possession of these powers by the Power of Appointment Committee members will not cause Trust property to be includible in any Committee member's gross estate under § 2041(a)(2).

RULING 6
Section 1014(a) provides, in part, that, except as otherwise provided in this section, the basis of property in the hands of a person acquiring the property from a decedent or to whom the property passed from a decedent will, if not sold, exchanged, or otherwise disposed of before the decedent's death by such person, be the fair market value of the property at the date of the decedent's death.

Section 1014(b)(6) provides that, in the case of decedents dying after December 31, 1947, property which represents the surviving spouse's one-half share of community property held by the decedent and the surviving spouse under the community property laws of any State, is considered, for purposes of § 1014(a), to have been acquired from or to have passed from the decedent if at least one-half of the whole of the community interest in such property was includible in determining the value of the decedent's gross estate.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 2038(a)(1) provides that the value of the decedent's gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished during the three-year period on the date of the decedent's death.

Grantors are married and reside in State 2, a community property state. Trust provides that all transferred property to Trust is community property. Moreover, any and all property transferred to Trust prior to the death of the Predeceased Grantor is and shall retain its character as community property. As concluded above, upon the death of each of Grantor, his or her respective interest in Trust as either the Predeceased Grantor or the Surviving Grantor will be includible in his or her respective gross estate for federal estate tax purposes.

Accordingly, based upon the facts submitted and representations made, we conclude that the basis of all community property in Trust on the date of death of the Predeceased Grantor will receive an adjustment in basis to the fair market value of such property at the date of death of the Predeceased Grantor.
b. PLR 201846002 - Section 1362 - Election; revocation; termination

See also:
- PLR 201840004 - Section 1362 - Election; revocation; termination
- PLR 201848001 - Section 1362 - Election; revocation; termination
- PLR 201845005 - Section 1362 - Election; revocation; termination
- PLR 201845004 - Section 1362 - Election; revocation; termination
- PLR 201845003 - Section 1362 - Election; revocation; termination

FACTS:

X was formed under the laws of State on D1 and elected to be an S corporation effective D2. On D3, Trust purchased X stock. X represents that Trust was eligible to be an electing small business trust (ESBT) within the meaning of § 1361(e) on D3, but the trustee did not timely file an ESBT election. Therefore, because Trust was not a permitted shareholder, X’s S corporation election terminated on D3.

X represents that the termination of its S corporation election was not motivated by tax avoidance or retroactive tax planning. X further represents that X and its shareholders have filed consistently with the treatment of X as an S corporation since D2. X and its shareholders have agreed to make any adjustments that the Commissioner may require, consistent with the treatment of X as an S corporation.

LAW AND ANALYSIS:

Section 1362(a)(1) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

Section 1361(a)(1) provides that the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) provides that the term “small business corporation” means a domestic corporation which is not an ineligible corporation and which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1361(c)(2)(A)(v) provides that for purposes of § 1361(b)(1)(B) an ESBT may be a shareholder.

Section 1361(e)(1)(A) provides that, except as provided in § 1361(e)(1)(B), an ESBT means any trust if (i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, (III) an organization described in 170(c)(2)(3), (4), or (5) or (IV) an organization described in § 170(c)(1) which holds a contingent interest in such trust and is not a
potential current beneficiary, (ii) no interest in such trust was acquired by purchase, and (iii) an election under § 1361(e) applies to such trust.

Section 1361(e)(3) provides that an election under § 1361(e) shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent years of the trust unless revoked with the consent of the Secretary.

Section 1.1361-1(m)(2)(i) of the Income Tax Regulations provides that the trustee of an ESBT must make the ESBT election by signing and filing, with the service center where the S corporation files its income tax return, a statement that meets the requirements of § 1.1361-1(m)(2)(ii).

Section 1362(d)(2)(A) provides that an election under § 1362(a) will be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation. Section 1362(d)(2)(B) provides that any termination under § 1362(d) is effective on and after the date of cessation.

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in the termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in the termination, steps were taken so that the corporation for which the termination occurred is a small business corporation, and (4) the corporation for which the termination occurred, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in the termination, the corporation will be treated as an S corporation during the period specified by the Secretary.

CONCLUSION:

Based solely on the facts submitted and the representations made, we conclude that X’s S corporation election terminated on D3. We also conclude that the circumstances resulting in the termination were inadvertent within the meaning of § 1362(f). Accordingly, under § 1362(f), X will be treated as an S corporation from D3 and thereafter, provided X’s S corporation election was otherwise valid and has not otherwise terminated under § 1362(d).

This ruling is conditioned on the trustee of the Trust filing an ESBT election effective D2, with the appropriate service center within 120 days of the date of this letter. A copy of this letter should be attached to the ESBT election. X and its shareholders must file any original and amended returns for all open years consistent with the relief granted in this letter. If these conditions are not met, then this ruling is null and void.
c. **PLR 201846001 - Section 1361 - S corporation defined**

**FACTS:**

According to the information submitted, X was incorporated on Date 1, under the laws of State. Effective Date 2, X elected to be taxed as an S corporation.

On Date 3, A transferred shares in X from Trust 1 to Trust 2. Trust 1 was a grantor trust as to A, an eligible shareholder of X under § 1361(c)(2)(A)(i). On Date 4, A transferred shares in X from Trust 1 to Trust 3. The beneficiaries of Trust 1 and Trust 3 failed to make timely qualified subchapter S trust (QSST) elections. Thus, X’s S corporation election terminated on Date 5.

X represents that Trust 2 and Trust 3 qualified as QSSTs under § 1361(d) as of Date 5 and thereafter. X further represents that the circumstances resulting in the failure to file a QSST election for Trust 2 and Trust 3 were inadvertent and was not motivated by tax avoidance or retroactive tax planning. X and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as may be required by the Secretary.

**LAW AND ANALYSIS:**

Section 1361(a)(1) of the Code provides that the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) defines a “small business corporation” as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1361(c)(2)(A)(i) provides that for purposes of § 1361(b)(1)(B), a trust all of which is treated (under subpart E) as owned by an individual who is a citizen or resident of the United States may be a shareholder.

Section 1361(d)(1) provides that a QSST whose beneficiary makes an election under § 1362(d)(2) will be treated as a trust described in § 1361(c)(2)(A)(i), and the QSST’s beneficiary will be treated as the owner (for purposes of § 678(a)) of that portion of the QSST’s S corporation stock to which the election under § 1361(d)(2) applies. Under § 1361(d)(2)(A), a beneficiary of a QSST may elect to have § 1361(d) apply. Under § 1361(d)(2)(D), this election will be effective up to 15 days and two months before the date of the election.

Section 1361(d)(3) provides that for purposes of § 1361(d), the term “qualified subchapter S trust” means a trust (A) the terms of which require that – (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust; (ii) any corpus distributed during the life of the current beneficiary may be distributed only to such beneficiary; (iii) the income interest of the current income beneficiary in the trust shall terminate on the earlier of such...
beneficiary’s death or the termination of the trust; and (iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to that beneficiary; and (B) all of the income (within the meaning of § 643(b)) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1st day of the 1st taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b); (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken so that the corporation for which the termination occurred is a small business corporation; and (4) the corporation for which the termination occurred, and each person who was a shareholder in such corporation at any time during the period specified pursuant to § 1362(f), agrees to make the adjustments (consistent with the treatment of such corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

CONCLUSION:

Based solely on the facts submitted and the representations made, we conclude that X’s S corporation election terminated on Date 5 as a result of the failure to make a timely QSST election for Trust 2 and Trust 3. We further conclude that the termination of X’s S election on Date 5 was inadvertent within the meaning of § 1362(f). Pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation as of Date 2 and thereafter, provided that the beneficiaries of Trust 2 and Trust 3 file QSST elections for Trust 2 and Trust 3 with an effective date of Date 3 and Date 4, respectively, with the appropriate service center within 120 days from the date of this letter, and X’s S corporation election is not otherwise terminated under § 1362(d). A copy of this letter must be attached to the QSST election.

Accordingly, X’s shareholders, in determining their respective income tax liabilities, must include their pro rata share of the separately and non-separately computed items of X as provided in § 1366, make any adjustments to stock basis as provided in § 1367, and take into account distributions made by X as of provided by § 1368.
d. PLR 201845014 - Section 664 - Charitable remainder trusts

FACTS:

The information submitted states that X intends to form two CRUTs, CRUT #1 and CRUT #2, and fund CRUT #1 and CRUT #2 with property worth approximately $a each. CRUT #1 and CRUT #2 are intended to qualify as valid CRUTs under § 664(d)(2) and the corresponding regulations.

CRUT #1

Article 2.01(b) provides that the unitrust amount for each taxable year shall be an amount equal to b% of the net fair market value of the trust property determined as of the first business day of that taxable year.

Article 2.01 provides that until the date of X’s death (the “term ending date”), the trustee shall administer the trust property as described in Article 2. Article 2.01(a)(1) provides that in each taxable year including the year in which the term ending date occurs, the trustee shall distribute to X (A) c% of the unitrust amount and (B) such additional portion of the unitrust amount, if any, as the independent trustee determines is necessary to ensure the total portion of the unitrust amount distributed to X in each taxable year shall not be de minimis under the facts and circumstances.

Article 2.01(a)(2) provides that after providing for distribution of the minimum amount (the aggregate of amounts described in Article 2.01(a)(1)(A) and (B)) the trustee shall distribute the balance of the unitrust amount (the “net unitrust amount”) to such one or more of X and one or more charitable organizations (as are described in §§ 170(c), 2055(a) and 2522(a) of the Code) included in the charitable class as the independent trustee selects in the independent trustee’s sole discretion without the approval or consent of any other person, and in such equal or unequal portions as the independent trustee determines in the independent trustee’s sole discretion without the approval or consent of any other person. The independent trustee shall designate by signed irrevocable written instrument delivered to X on or before the date that is thirty (30) days before the payment date, if X is then living, the portion of the net unitrust amount to be paid to the charitable class for the taxable year. Under Article 6.07, the term “payment date” means the last day of each calendar year and the term ending date.

Under, Article 2.01(a)(3) the charitable class means (A) such one or more charitable organizations that X, as an individual and not in any fiduciary capacity, designates as potential recipients of the charitable portion by signed written instrument delivered to the independent trustee, which shall remain revocable until the payment date such that X retains the power to designate the charitable class until such power lapses on the payment date, or if X does not provide such designation on or before the payment date, (B) such one or more charitable organizations as the independent trustee, in the independent trustee’s sole discretion, shall determine.

Article 2.02 provides that as of the term ending date, the trustee shall distribute the trust property remaining after providing for the payment of all unitrust amounts under the preceding provisions of Article 2 to one or more charitable organizations in such proportion among them as
X may appoint by will, or to the extent X does not exercise the power of appointment, to Y, if it is a charitable organization on the term ending date, or if not, to such one or more charitable organizations and in such equal or unequal proportions among them as the trustee, in the trustee’s sole discretion, decides.

Article 3.02 provides that at all times at least one independent trustee must be acting. “Independent trustee” means a trustee other than X, X’s spouse, or a subordinate party as to either X or X’s spouse. The authority of the independent trustee shall be solely limited to the actions described in Articles 2.01(a)(1), 2.01(a)(2), 2.01(a)(3) and 3.02.

Article 3.04 provides, in part, that whenever the identity of the appointer is to be determined, the appointer shall be X or if X fails to act, X’s wife. A person named as appointer shall not be deemed to have failed to act unless (a) the vacancy in any office is required to be filled and that person has not appointed a successor within 30 days after that person has been notified of the vacancy, or (b) that person declines to act as appointer to fill that vacancy or any vacancy by signed instrument delivered to the individuals or entities named to act as appointer if that person fails to act and to the trustee.

Article 3.05 provides, in part, that at any time or times the remover may remove an independent trustee. X is the initial remover, and when X ceases to act, X’s wife is the remover.

CRUT #2

Except as identified below, the provisions of CRUT #2 are identical to the provisions of CRUT #1. While CRUT #1 proposes an inter vivos CRUT with one measuring life, X, CRUT #2 proposes an inter vivos CRUT with consecutive interests with two measuring lives, X and X’s spouse, subject to X’s right to revoke the survivor unitrust interest.

Article 2.01 provides that until the date of the survivor of X’s wife and X’s death (the "term ending date"), the trustee shall administer the trust property as described in Article 2.

Article 2.01(b) provides that X may revoke the survivor unitrust interest by will specifically referring to this right of revocation. The term “survivor unitrust interest” means the right to receive the unitrust amounts, if any, payable on payment dates following X’s death.

Your authorized representatives have requested the following rulings with respect to CRUT #1 and CRUT #2:

1. The independent trustee’s power to allocate a portion of the unitrust amount of CRUT #1 between noncharitable and charitable beneficiaries will not prevent CRUT #1 from qualifying as a qualified CRUT under § 664.

2. The independent trustee’s power to allocate a portion of the unitrust amount of CRUT #2 between noncharitable and charitable beneficiaries will not prevent CRUT #2 from qualifying as a qualified CRUT under § 664.
3. X and X’s wife’s powers to replace the independent trustee will not prevent CRUT #1 from qualifying as a qualified CRUT under § 664.

4. X and X’s wife’s powers to replace the independent trustee will not prevent CRUT #2 from qualifying as a qualified CRUT under § 664.

5. X’s power to designate the charitable class of CRUT #1 will not prevent CRUT #1 from qualifying as a qualified CRUT under § 664.

6. X’s power to designate the charitable class of CRUT #2 will not prevent CRUT #2 from qualifying as a qualified CRUT under § 664.

7. X’s testamentary power to revoke by a provision in his will all interests in the survivor unitrust will not prevent CRUT #2 from qualifying as a qualified CRUT under § 664.

8. Regarding CRUT #1, X’s power to designate the charitable class will prevent completion of the gift of the net unitrust amount (defined in Article 2.01(a)(2) of CRUT #1) during X’s lifetime until such power lapses. Upon the annual lapse of X’s power to designate the charitable class during X’s lifetime and to the extent each year the net unitrust amount is distributed to one or more charitable organizations (defined in Article 6.07(a)), the distributions will be completed gifts and will qualify for the gift tax charitable deduction under § 2522(a).

9. Regarding CRUT #2, X’s power to designate the charitable class will prevent completion of the gift of the net unitrust amount (defined in Article 2.01(a)(2) of CRUT #2) during X’s lifetime until such power lapses. Upon the annual lapse of X’s power to designate the charitable class during X’s lifetime and to the extent each year the net unitrust amount is distributed to one or more charitable organizations (defined in Article 6.07(a)), the distributions will be completed gifts and will qualify for the gift tax charitable deduction under § 2522(a).

10. Regarding CRUT #2, X’s testamentary power to revoke by a provision in his will all interests in the survivor unitrust interest will cause X’s gift of the survivor unitrust interest to remain incomplete until X’s death.

11. Regarding CRUT #2, if X’s spouse survives X and if X does not revoke the survivor unitrust interest at X’s death, the entire value of the assets of CRUT #2 included in X’s estate will be deductible because of the combined charitable and marital estate tax deductions available under §§ 2055(a) and 2056(a).

**LAW AND ANALYSIS:**

**CRUT Issues**

Section 664(d)(2) provides that for purposes of § 664, a charitable remainder unitrust is a trust (A) from which a fixed percentage (which is not less than 5 percent nor more than 50 percent) of the net fair market value of its assets, valued annually, is to be paid, not less often than annually, to one or more persons (at least one of which is not an organization described in § 170(c) and, in
the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals, (B) from which no amount other than the payments described in § 664(d)(2)(A) and other than qualified gratuitous transfers described in § 664(d)(2)(C) may be paid to or for the use of any person other than an organization described in 170(c)(C) following the termination of the payments described in § 664(d)(2)(A), the remainder interest is to be transferred to, or for the use of, an organization described in § 170(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as defined in § 664(g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined by § 664(g)), and) with respect to each contribution of property to the trust, the value (as determined under § 7520) of such remainder interest in such property is at least 10 percent of the net fair market value of such property as of the date such property is contributed to the trust.

Section 1.664-1(a)(i) of the Income Tax Regulations provides that, generally, a charitable remainder trust is a trust which provides for a specified distribution, at least annually, to one or more beneficiaries, at least one of which is not a charity, for life or for a term of years, with an irrevocable remainder interest to be held for the benefit of, or paid over to, charity. In the case of a charitable remainder unitrust, the specified distribution to be paid at least annually must be a fixed percentage which is not less than 5 percent of the net fair market value of the trust assets, valued annually.

Section 1.664-1(a)(4) provides that in order for a trust to be a charitable remainder trust, it must meet the definition of and function exclusively as a charitable remainder trust from the creation of the trust. Solely for the purposes of § 664 and the regulations thereunder, the trust will be deemed to be created at the earliest time that neither the grantor nor any other person is treated as the owner of the entire trust under subpart E, part 1, subchapter J, chapter 1, subtitle A of the Code (relating to grantors and other treated as substantial owners), but in no event prior to the time property is first transferred to the trust. For purposes of the preceding sentence, neither the grantor nor his spouse shall be treated as the owner of the trust under such subpart E merely because the grantor or his spouse is named as a recipient.

Section 1.664-3(a)(1)(i) requires that the governing instrument provides that the trust will pay not less often than annually a fixed percentage of the net fair market value of the trust assets determined annually to a person or persons described in § 1.664-3(a)(3) for each taxable year of the period specified in § 1.664-3(a)(5).

Section 1.664-3(a)(3)(i) provides that the amount described in § 1.664-3(a)(1) must be payable to or for the use of a named person or persons, at least one of which is not an organization described in § 170(c). If the amount described in § 1.664-3(a)(1) is to be paid to an individual or individuals, all such individuals must be living at the time of creation of the trust. A named person or persons may include members of a named class except in the case of a class which includes an individual, all such individuals must be alive and ascertainable at the time of the creation of the trust unless the period for which the unitrust amount is to be paid to such class consists solely of a term of years.
Section 1.664-3(a)(3)(ii) provides that a trust is not a charitable remainder unitrust if any person has the power to alter the amount to be paid to any named person other than an organization described in § 170(c) if such power would cause any person to be treated as the owner of the trust, or any portion thereof, if subpart E, part 1, subchapter J, chapter 1, subtitle A of the Code were applicable to such trust. The governing instrument may not grant the trustee the power to allocate the fixed percentage among members of a class unless such power falls within one of the exceptions to § 674(a).

Section 674(a) provides the general rule that the grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of an adverse party.

Section 674(b)(3) provides § 674(a) shall not apply to a power exercisable only by will, other than a power in the grantor to appoint by will the income of the trust where the income is accumulated for such disposition by the grantor or may be so accumulated in the discretion of the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

Section 674(b)(4) provides that § 674(a) shall not apply to a power to determine the beneficial enjoyment of the corpus or the income therefrom if the corpus or income is irrevocably payable for a purpose specified in § 170(c) (relating to the definition of charitable contributions) or to an employee stock ownership plan (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined in § 664(g)(1)).

Section 1.674(b)-1(b)(4) provides that under § 674(b)(4) a power in any person to determine the beneficial enjoyment of corpus or income which is irrevocably payable for purposes specified in § 170(c) (relating to the definition of charitable contributions) will not cause the grantor to be treated as an owner under § 674(a). For example, if a grantor creates a trust, the income of which is irrevocably payable solely to educational or other organizations that qualify under § 170(c), he is not treated as an owner under § 674 although he retains the power to allocate the income among such organizations.

Section 674(c) provides that § 674(a) shall not apply to a power solely exercisable (without the approval or consent of any other person) by a trustee or trustees, none of whom is the grantor, and no more than half of whom are related or subordinate parties who are subservient to the wishes of the grantor (1) to distribute, apportion, or accumulate income to or for a beneficiary or beneficiaries, or to, for, or within a class of beneficiaries; or (2) to pay out corpus to or for a beneficiary, or beneficiaries or to or for a class of beneficiaries (whether or not income beneficiaries).

Section 1.674(c)-1 provides that the powers to which § 674(c) applies are powers (a) to distribute, apportion, or accumulate income to or for a beneficiary or beneficiaries, or to, for, or within a class of beneficiaries, or (b) to pay out corpus to or for a beneficiary or beneficiaries or to or for a class of beneficiaries (whether or not income beneficiaries). In order for such a power to fall within the exception of § 674(c) it must be exercisable solely (without the approval or consent
of any other person) by a trustee or trustees none of whom is the grantor and no more than half of whom are related or subordinate parties who are subservient to the wishes of the grantor.

Section 1.674(d)-2(a) provides that a power in the grantor to remove, substitute, or add trustees may prevent a trust from qualifying under § 674(c) or (d). On the other hand, if the grantor’s power to remove, substitute, or add trustees is limited so that its exercise could not alter the trust in a manner that would disqualify it under § 674(c) or (d), as the case may be, the power itself does not disqualify the trust. Thus, for example, a power in the grantor to remove or discharge an independent trustee on the condition that he substitute another independent trustee will not prevent the trust from qualifying under § 674(c).

Ruling #1 and Ruling #2

In the present case, with respect to CRUT #1 and CRUT #2, Article 2.01(a)(2) provides that after providing for distribution of the minimum amount (the aggregate of amounts described in Article 2.01(a)(1)(A) and (B)) the trustee shall distribute the balance of the unitrust amount to such one or more of X and one or more charitable organizations (organization described in §§ 170(c), 2055(a) and 2522(a)) included in the charitable class as the independent trustee selects in the independent trustee’s sole discretion without the approval or consent of any other person, and in such equal or unequal portions as the independent trustee determines in the independent trustee’s sole discretion without the approval or consent of any other person.

As noted above, § 674(c) provides an exception to the general rule of § 674(a) with regard to certain powers to apportion trust income or principal among classes of beneficiaries. Thus, a provision that gives an independent trustee the power to allocate the unitrust amount among the charitable and noncharitable beneficiaries on an annual basis is not inconsistent with the provisions of the Code and regulations governing charitable remainder trusts, provided that the governing instrument requires that a portion of the unitrust amount must be allocated and paid to the noncharitable beneficiaries each year and provided that the portion of the unitrust amount so paid is not de minimis under the facts and circumstances for each year.

Based on the foregoing, and based solely on the information submitted and representations made, we conclude that the provisions in CRUT #1 and CRUT #2 that give the independent trustee the power to allocate a portion of the unitrust amount between noncharitable and charitable beneficiaries will not prevent CRUT #1 or CRUT #2 from qualifying as a CRUT under § 664(d)(2).

Ruling #3 and Ruling #4

With respect to both CRUT #1 and CRUT #2, Article 3.02 provides that at all times at least one independent trustee must be acting. “Independent trustee” means a trustee other than X, X’s spouse, or a subordinate party as to either X or X’s spouse. If at any time a vacancy occurs in the office of independent trustee, the appointer shall fill the vacancy by appointing an independent trustee.
Article 3.04 provides, in part, that the appointer shall be X or if X fails to act, X’s wife. Article 3.05 provides, in part, that at any time or times the remover may remove an independent trustee. X is the initial remover, and when X ceases to act, X’s wife is the remover.

Based solely on the information submitted and representations made, with respect to CRUT #1 and CRUT #2, we conclude that X and X’s wife have not retained a power to remove the independent trustee that would allow either of them to substitute any person, including themselves, as independent trustee, or that would subordinate the independent trustee to X or X’s wife. Article 3.02 and Article 3.04 of CRUT #1 and CRUT #2 provide that the independent trustee can be replaced only by the persons named in the trust agreements and in the order they are named. In no event will the independent trustee be a person or entity related to or subordinate to X or X’s wife. For these reasons, we conclude that X and X’s wife’s powers to replace the independent trustee will not prevent CRUT #1 or CRUT #2 from qualifying as a CRUT under § 664(d)(2).

Ruling #5 and Ruling #6

Article 2.01(a)(3) of both CRUT #1 and CRUT #2 defines the charitable class as one or more charitable organizations that X designates or, if X does not designate a charitable class before the payment date, one or more charitable organizations as the independent trustee in the independent trustee’s sole discretion shall determine.

Article 2.01(a)(2) of both CRUT #1 and CRUT #2 provides, in part, that the independent trustee shall designate by signed irrevocable written instrument delivered to X on or before the date that is thirty (30) days before the payment date, if X is then living, the portion of the net unitrust amount to be paid to the charitable class for the taxable year. Under Article 6.07, the term “payment date” means the last day of each calendar year and the term ending date.

Section 674(b)(4) provides that § 674(a) shall not apply to a power to determine the beneficial enjoyment of the corpus or the income therefrom if the corpus or income is irrevocably payable for a purpose specified in § 170(c) (relating to the definition of charitable contributions) or to an employee stock ownership plan (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined in § 664(g)(1)).

Based solely on the information submitted and representations made, we conclude that X’s power to designate the charitable class of CRUT #1 and CRUT #2 will not prevent CRUT #1 or CRUT #2 from qualifying as a CRUT under § 664(d)(2).

Ruling #7

Article 2.01(b) of CRUT #2 provides that X may revoke the survivor unitrust interest by will specifically referring to this right of revocation. “Survivor unitrust interest” means the right to receive the unitrust amounts, if any, payable on dates following X’s death.

As mentioned above, § 674(b)(3) provides an exception to the application of § 674(a) where a power is exercisable only by will, other than a power in the grantor to appoint by will the income of the trust where the income is accumulated for such disposition by the grantor or may be
so accumulated in the discretion of the grantor or a nonadverse party, or both, without the approval or consent of the adverse party. Section 1.664-3(a)(4) provides, in part, that the trust may not be subject to a power to invade, alter, amend, or revoke for the beneficial use of a person other than an organization described in § 170(c). Notwithstanding the preceding sentence, the grantor may retain the power exercisable only by will to revoke or terminate the interest of any recipient other than an organization described in § 170(c).

For these reasons, and based solely on the information submitted and representations made, we conclude that X’s testamentary power to revoke by a provision in X’s will all interests in the survivor unitrust in CRUT #2 will not prevent CRUT #2 from qualifying as a CRUT under § 664(d)(2).

Gift and Estate Tax Issues Rulings #8 - #10 [ANALYSIS OMITTED.]

Accordingly, based on the facts submitted and the representations made, we conclude that X’s power to designate the charitable class will prevent completion of the gift of the net unitrust amount of CRUT #1 and the net unitrust amount of CRUT #2 during X’s lifetime until such power lapses. Furthermore, upon the annual lapse of X’s power to designate the charitable class during X’s lifetime and to the extent each year the net unitrust amount is distributed to one or more charitable organizations within the meaning of Article 6.07(a) of each of CRUT #1 and CRUT #2, the distributions will be completed gifts and will qualify for the gift tax charitable deduction under § 2522(a).

With regard to X’s testamentary power to revoke by a provision in his will all interests in the survivor unitrust interest of CRUT #2 (to include both the minimum unitrust amount and the net unitrust amount), retention of this power will cause X’s gift of the survivor unitrust interest to remain incomplete until his death. See § 25.2511-2.

Ruling #11 [ANALYSIS OMITTED.]

In light of the legislative history noted above, we conclude that under these facts, where X’s spouse is the only noncharitable beneficiary of the survivor unitrust interest, the estate tax marital deduction under § 2056(a) will completely offset the value of the assets of CRUT #2 included in the gross estate of X after deducting the value of the remainder interest of CRUT #2 qualifying for a charitable deduction under § 2055(a).

e. PLR 201850012 - Section 4941 - Taxes on self-dealing

FACTS:

Taxpayer is a non-profit organization recognized as described in § 501(c)(3) of the Internal Revenue Code and exempt from federal income tax under § 501(a). Taxpayer is a private foundation described in § 509(a).
H and W, husband and wife, respectively, created Taxpayer, whose mission includes educational, religious, scientific, and charitable purposes. H and W have been the only contributors to Taxpayer.

H’s revocable trust (“Trust”) provides that upon H’s death, Taxpayer shall receive H’s Shares in Corporation (“H’s Shares”). H’s total contributions and bequests to Taxpayer exceed $5,000 and 2% of the total contributions and bequests that Taxpayer has received.

Corporation was incorporated by H under State’s laws and is an S corporation for federal tax purposes. H owned a% of Corporation’s non-voting shares (which constitutes a majority of Corporation’s non-voting shares) and b% of its voting shares (which constitutes less than a majority of Corporation’s voting shares). W owned voting and non-voting shares of Corporation. Prior to W’s death, H and W’s daughter, D, owned b% of Corporation’s voting shares, as well as c% of Corporation’s non-voting shares. Following W’s death, D received all of W’s voting shares, resulting in D’s owning a majority of Corporation’s voting shares. D also is the CEO of Corporation.

After W’s death, D terminated H’s employment with Corporation. H, after his termination, together with Trust and Trust’s trustee, filed a lawsuit against Corporation and D under State’s laws (the “Litigation”) on Date 1. H alleged shareholder oppression and breach of fiduciary duties. H asked the Litigation court to enter an order requiring D and/or Corporation to buy H’s Shares, or an order requiring H to purchase D’s shares, among other relief possibilities.

Within three months after H initiated the Litigation, Corporation and D, pursuant to State’s laws, filed a notice (the “Election”) under the Litigation to purchase H’s Shares. H filed a motion to nullify the Election. The court denied H’s nullification motion, granted Corporation’s motion for summary judgment, and ruled that the Election was valid.

H died on Date 2, and Trust became irrevocable. Trust’s administration is ongoing. Pursuant to Trust’s terms, the trustee under pertinent laws and authority shall have the power and authority to enter into a sale or exercise of any stock rights. Because of the Litigation, Taxpayer has not received H’s Shares from Trust, and during the Litigation, Trust cannot sell H’s Shares to anyone other than Corporation.

The court in the Litigation, which is set for trial on Date 4, is required by state law to determine the “fair value” of H’s Shares as of Date 1 or such other date the Litigation court deems appropriate. The court may determine the fair value of H’s Shares to be less than the fair market value of H’s Shares after marketability and control discounts are applied.

A State district court (the “Probate Court”), not the Litigation court, is overseeing administration of Trust. The Probate Court has the responsibility to ensure that Taxpayer receives the full value of H’s Shares and is required to approve H’s Shares valuation and their sale to Corporation (the “Proposed Transaction”). If the Probate Court approves the Proposed Transaction, the Litigation court will honor the Probate Court’s approval.
Trust is required to file on H’s behalf a Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, which is due on Date 3. To enable the Litigation court to resolve the Litigation before the Form 706 is filed, Trust expects to request an extension of time within which to file the Form 706.

Taxpayer represents that before the sale of H’s Shares by Trust takes place, distributions required to be made from the Trust to any beneficiary other than the Taxpayer will have been made, and Taxpayer will be the sole remaining beneficiary of the Trust.

Taxpayer represents that because of the active and on-going status of the Litigation, Trust’s trustees are, and will be, unable to complete the ordinary duties of administration necessary for the settlement of the Trust prior to the date of the sale of H’s Shares, and Trust should not be considered terminated for Federal income tax purposes pursuant to § 4947 and Treas. Reg. §§ 53.4947-1(b)(2)(v) prior to the date of the sale of H’s Shares.

Taxpayer represents that it understands and acknowledges that the Treas. Reg. § 53.4941(d)-1(b)(3) exception to indirect self-dealing is inapplicable to the Proposed Transaction if the Probate Court (or another court having jurisdiction over Trust or over Taxpayer) does not approve the Proposed Transaction.

Taxpayer represents that it understands and acknowledges that the Treas. Reg. § 53.4941(d)-1(b)(3) exception to indirect self-dealing is inapplicable to the Proposed Transaction if the Trust does not receive an amount that equals or exceeds the fair market value of H’s Shares at the time of the Proposed Transaction.

Taxpayer represents that it understands and acknowledges that regarding the Proposed Transaction, this ruling does not address what the fair market value of H’s Shares is, and does not address whether any amount set by any court or paid for H’s Shares will constitute at least fair market value of H’s Shares at the time of transaction.

RULING REQUESTED:

Taxpayer requests a ruling that Corporation’s purchase of H’s Shares of Corporation held by the Trust will satisfy the indirect self-dealing exception under Treas. Reg. § 53- 4941(d)-1(b)(3).

LAW:

Section 4941(a)(1) imposes a tax on acts of self-dealing between a disqualified person as defined in § 4946(a)(1) and a private foundation.

Section 4941(d)(1)(A) provides, in part, that the term "self-dealing" includes any direct or indirect sale or exchange, or leasing, of property between a private foundation and a disqualified person.
Treas. Reg. § 53.4941(d)-1(a) provides that for purposes of § 4941, the term "self-dealing" means any direct or indirect transaction described in Treas. Reg. § 53.4941(d)-2. For purposes of this section, it is immaterial whether the transaction results in a benefit or a detriment to the private foundation.

Treas. Reg. § 53.4941(d)-1(b)(3) provides, in part, that the term "indirect self-dealing" shall not include a transaction with respect to a private foundation's interest or expectancy in property (whether or not encumbered) held by a revocable trust, including a trust which has become irrevocable on a grantor's death, regardless of when title to the property vests under local law, if:

(i) The trustee of the revocable trust either:

(a) Possesses a power of sale with respect to the property,
(b) Has the power to reallocate the property to another beneficiary, or
(c) Is required to sell the property under the terms of any option subject to which the property was acquired by the revocable trust;

(ii) Such transaction is approved by a court having jurisdiction over the trust or over the private foundation;

(iii) Such transaction occurs, in the case of a revocable trust, before it is considered subject to § 4947;

(iv) The trust receives an amount which equals or exceeds the fair market value of the foundation's interest or expectancy in such property at the time of the transaction, taking into account the terms of any option subject to which the property was acquired by the trust; and

(v) With respect to transactions occurring after April 16, 1973, the transaction either:

(a) Results in the foundation receiving an interest or expectancy at least as liquid as the one it gave up,
(b) Results in the foundation receiving an asset related to the active carrying out of its exempt purposes, or
(c) Is required under the terms of any option, which is binding on the trust.

Section 4946(a)(1) provides that the term "disqualified person" means, in part, with respect to a private foundation, a person who is:

(A) a substantial contributor to the foundation,
(B) a foundation manager (within the meaning of subsection (b)(1)),
(C) an owner of more than 20 percent of:

(i) the total combined voting power of a corporation,
(ii) the profits interest of a partnership, or
(iii) the beneficial interest of a trust or unincorporated enterprise, which is a substantial contributor to the foundation

(D) a member of the family (as defined in § 4946(d)) of any individual described in subparagraph (A), (B), or (C), or

(E) a corporation of which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the total combined voting power.

Section 4946(d) provides that the term “members of family” with respect to any person who is a disqualified person includes the individual’s spouse, ancestors, children, grandchildren, great grandchildren, and the spouses of children, grandchildren, and great grandchildren.

Treas. Reg. § 53.4947-1(b)(2)(v) provides, in part, that as to certain revocable trusts that wind up, a revocable trust that becomes irrevocable upon the death of the decedent-grantor, from which the trustee is required to distribute all of the net assets in trust for or free of trust to charitable beneficiaries, is not considered a charitable trust under section 4947(a)(1) for a reasonable period of settlement (within the meaning of Treas. Reg. § 53.4947-1(b)(2)(iv)) after becoming irrevocable. After that period, the trust is considered a charitable trust under section 4947(a)(1).

Treas. Reg. § 53.4947-1(b)(2)(iv) provides, in part, that the term "reasonable period of settlement" means that period reasonably required (or if shorter, actually required) by the trustee to perform the ordinary duties of administration necessary for the settlement of the trust. These duties include, for example, the collection of assets, the payment of debts, taxes, and distributions, and the determination of the rights of the subsequent beneficiaries.

Rev. Proc. 2018-3, section 3.01(80) provides that rulings will not be issued as to whether the period of administration or settlement of a trust is reasonable or unduly prolonged.

ANALYSIS:

H’s contributions and bequests to Taxpayer totaled more than $5,000 and were more than 2% of Taxpayer’s total bequests and contributions at close of the taxable years in which Taxpayer received the bequests and contributions from H. Therefore, H was a disqualified person as described under § 4946(a)(1)(A).

H’s children are disqualified persons as to Taxpayer because their father, H, is a substantial contributor to Taxpayer. See § 4946(a)(1)(D). Corporation also is a disqualified person as to Taxpayer because H’s daughter, D, owns more than 35% of Corporation’s voting shares. See § 4946(a)(1)(E).

Since Corporation is a disqualified person as to Taxpayer, because of Taxpayer’s expectancy of H’s Shares from Trust, the proposed sale of H’s Shares by Trust to Corporation pursuant to the Litigation Court’s order (Proposed Transaction) could be indirect self-dealing under § 4941. See § 4941(d)(1) and Treas. Reg. § 53.4941(d)-1(a).
However, Treas. Reg. § 53.4941(d)-1(b)(3) provides that the term “indirect self-dealing” shall not include a transaction with respect to a private foundation’s interest or expectancy in property (whether or not encumbered) held by a trust that has become irrevocable on a grantor’s death, regardless of when title to the property vests under local law, if specific requirements are satisfied.

First, under Treas. Reg. § 53.4941(d)-1(b)(3), a trust administrator must have the power to sell the trust’s property. See Treas. Reg. § 53.4941(d)-1(b)(3)(i). Pursuant to the trust agreement that created Trust, Trust’s administrator or trustee has the power to sell any Trust assets, which includes H’s Shares. Thus, the Proposed Transaction will meet the first requirement of Treas. Reg. § 53.4941(d)-1(b)(3).

Second, a court with jurisdiction over the trust must approve the transaction. See Treas. Reg. § 53.4941(d)-1(b)(3)(ii). Taxpayer will seek and obtain the approval of the Proposed Transaction from the Probate Court that has jurisdiction and is overseeing administration of Trust. Thus, the Proposed Transaction will meet the second requirement of Treas. Reg. § 53.4941(d)-1(b)(3) upon the Trust’s receipt of the Probate Court’s approval of the proposed sale.

Third, the Proposed Transaction must occur before the trust is considered subject to section 4947. Taxpayer represents that because of the active and on-going status of the Litigation, Trust’s trustees are, and will be, unable to complete the ordinary duties of administration necessary for the settlement of Trust prior to the date of the sale of H’s Shares, and Trust should not be considered subject to section 4947 pursuant to Treas. Reg. § 53.4947-1(b)(2)(iv) and (v) prior to the date of the sale of H’s Shares. Before the sale of H’s Shares by Trust takes place, Trust will have made distributions required to be made from the Trust to any beneficiary other than Taxpayer, and Taxpayer will be the sole remaining beneficiary of the Trust. Under Rev. Proc. 2018-3, section 3.01(80) provides that rulings will not be issued as to whether the period of administration or settlement of a trust is reasonable or unduly prolonged. Thus, if Trust is not considered terminated for Federal income tax purposes prior to the Proposed Transaction, the Proposed Transaction will meet the third requirement of Treas. Reg. § 53.4941(d)-1(b)(3).

Fourth, the trust must receive an amount that equals or exceeds the fair market value of the private foundation’s interest or expectancy in such property at the time of the transaction. See Treas. Reg. § 53.4941(d)-1(b)(3)(iv). The Litigation court is tasked with valuing H’s Shares. Taxpayer will endeavor to ensure that the Litigation court orders sale of H’s Shares to Corporation at a price that is not less than the fair market value at the time of the Proposed Transaction. Thus, the Proposed Transaction will meet the fourth requirement of Treas. Reg. § 53.4941(d)-1(b)(3) if H’s Shares are sold to Corporation at no less than their fair market value at the time of the transaction.

Fifth, the sale of the private foundation’s interest or expectancy must result in the private foundation’s receiving an interest as liquid as the one that was given up. See Treas. Reg. § 53.4941(d)-1(b)(3)(v). Pursuant to the trust agreement, Taxpayer currently has the expectancy of receiving H’s Shares, which are illiquid. Upon the completion of the Proposed Transaction, Taxpayer will receive the money that Corporation pays Trust for H’s Shares. Thus, the Proposed
Transaction will meet the fifth requirement of Treas. Reg. § 53.4941(d)-1(b)(3) if Taxpayer receives the money proceeds from the Proposed Transaction.

RULING:

Based solely on the facts and representations submitted by Taxpayer, as described above, we rule that Corporation’s purchase of the shares of Corporation held by Trust, as described in the request for ruling, exhibits, and subsequent submissions, will satisfy the exception from indirect self-dealing under Treas. Reg. § 53-4941(d)-1(b)(3), contingent on the following:

1. The Probate Court (or another court having jurisdiction over Trust or over Taxpayer) approves the Proposed Transaction;

2. Trust is not considered subject to section 4947 pursuant Treas. Reg. § 53.4947-1(b)(2)(v) prior to the date of the sale of H’s Shares by Trust;

3. Trust receives from the sale of H’s Shares to Corporation an amount of cash or its equivalent that equals or exceeds the fair market value of H’s Shares at the time of the transaction.

This ruling does not address what the fair market value of H’s Shares is and does not address whether any amount paid for H’s Shares will constitute at least fair market value.

f. PLR 201840003 - Section 754 - Manner of electing optional adjustment to basis of partnership property

FACTS:

The information submitted states that X was formed on Date 1 under the laws of State as a limited partnership classified as a partnership for federal tax purposes. X intended to file an election under § 754 to adjust the basis of partnership property with its return for its taxable year ending in Year. However, X inadvertently failed to file a properly executed § 754 election.

X represents that it has filed returns for its taxable year ended in Year and subsequent years consistent with the election having been made, and that all affected partners have also filed their returns consistent with the election having been made.

Further, X represents that it has acted reasonably and in good faith, that granting relief will not prejudice the interests of the government, and that it is not using hindsight in making the election.

LAW AND ANALYSIS:

Section 754 provides that a partnership may elect to adjust the basis of partnership property when there is a distribution of property or a transfer of a partnership interest.
An election under § 754 applies with respect to all distributions of property by the partnership and to all transfers of interests in the partnership during the taxable year with respect to which the election was filed and all subsequent taxable years.

Section 1.754-1(b) of the Income Tax Regulations provides that an election under § 754 to adjust the basis of partnership property under §§ 734(b) and 743(b), with respect to a distribution of property to a partner or a transfer of an interest in a partnership, must be made in a written statement filed with the partnership return for the taxable year during which the distribution or transfer occurs.

For the election to be valid, the statement must (i) set forth the name and address of the partnership making the election, (ii) be signed by any one of the partners, and (iii) contain a declaration that the partnership elects under § 754 to apply the provisions of §§ 734(b) and 743(b).

Under § 301.9100-1(c), the Commissioner may grant a reasonable extension of time to make a regulatory election, or a statutory election (but no more than six months except in the case of a taxpayer who is abroad), under all subtitles of the Code, except subtitles E, G, H, and I. Section 301.9100-1(b) defines the term “regulatory election” as including an election whose due date is prescribed by a regulation published in the Federal Register, or a revenue ruling, revenue procedure, announcement, or notice published in the Internal Revenue Bulletin.

Sections 301.9100-1 through 301.9100-3 provide the standards that the Commissioner will use to determine whether to grant an extension of time to make an election. Section 301.9100-2 provides automatic extensions of time for making certain elections. Section 301.9100-3 provides rules for requesting extensions of time for regulatory elections that do not meet the requirements of § 301.9100-2. Requests for relief under § 301.9100-3 will be granted when the taxpayer provides evidence to establish that the taxpayer acted reasonably and in good faith, and that granting relief will not prejudice the interests of the government.

CONCLUSION:

Based solely upon the facts submitted and the representations made, we conclude that the requirements of §§ 301.9100-1 and 301.9100-3 have been satisfied. As a result, X is granted an extension of time of 120 days from the date of this letter to make a § 754 election for its taxable year ended in Year. The election should be made in a written statement filed with the appropriate service center. A copy of this letter should be attached to the § 754 election. A copy is enclosed for that purpose.