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Honolulu, Hawaii

June 5, 2019

Internal Revenue Service  
CC:PA:LPD:PR (Notice 2019-30)  
Room 5203  
Post Office Box 7604  
Ben Franklin Station  
Washington, D.C. 20044

Submitted electronically at [www.regulations.gov](http://www.regulations.gov)

Re: Recommendations for 2019-2020 Priority Guidance Plan (Notice 2019-30)

Dear Ladies and Gentlemen:

The American College of Trust and Estate Counsel (ACTEC) is pleased to submit recommendations pursuant to Notice 2019-30, which invites recommendations for items that should be included on the 2019-2020 Priority Guidance Plan.

ACTEC is a professional organization of approximately 2,500 lawyers from throughout the United States. Fellows of ACTEC are elected to membership by their peers on the basis of professional reputation and ability in the fields of trusts and estates and on the basis of having made substantial contributions to those fields through lecturing, writing, teaching, and bar activities. Fellows of ACTEC have extensive experience in providing advice to taxpayers on matters of federal taxes, with a focus on estate, gift and GST tax planning, fiduciary income tax planning, and compliance. ACTEC offers technical comments about the law and its effective administration, but does not take positions on matters of policy or political objectives.

ACTEC's recommendations include items in the following categories and, when a category has multiple items, we have placed them in what we believe to be the order of their priority.

## EMPLOYEE BENEFITS

1. Guidance concerning spousal rollovers of qualified plan and IRA benefits when an estate or trust is named beneficiary of a decedent's interest.

## GIFTS AND ESTATES AND TRUSTS

1. Regulations or other guidance defining "GST Trust" under section 2632(c), particularly relating to trusts that give beneficiaries continuing withdrawal rights attributable to prior year gifts to a trust and trusts that make distributions to a non-skip

beneficiary, dependent upon both the death of a person more than ten years older and the beneficiary attaining a specified age.

2. Guidance regarding the completion of gifts and inclusion in the gross estate in the context of self-settled asset protection trusts.
3. Safe Harbor Guidance concerning the application of the Reciprocal Trust Doctrine.
4. Guidance on the tax basis of assets sold on the date of a decedent's death: when does a decedent's tax year end and the estate's tax year begin.

#### INTERNATIONAL ISSUES

1. Guidance concerning the application of the Foreign Account Tax Compliance Act ("FATCA") provisions of the Hiring Incentives to Restore Employment ("HIRE") Act (P.L. No. 111-147, 124 Stat. 71 (2010)) on reporting and withholding with respect to trusts and their beneficiaries.
2. Guidance concerning the tax consequences under Section 643(i) of the under-compensated use by a U.S. person of property owned by a foreign trust.
3. Regulation changing the due date for filing Form 3520-A from March 15 to April 15.
4. Guidance concerning the coordination of the foreign corporation anti-deferral rules and Subchapter J.

Each recommendation is described in detail in the enclosed memorandum.

If you or your staff would like to discuss the recommendations, please contact Donald D. Kozusko, Chair of the ACTEC Washington Affairs Committee, at (202) 457-7211 or [dkozusko@kozlaw.com](mailto:dkozusko@kozlaw.com), or Deborah McKinnon, ACTEC Executive Director, at (202) 684-8460 or [domckinnon@actec.org](mailto:domckinnon@actec.org).

Respectfully submitted,



John A. Terrill, II  
ACTEC President 2019-2020

Enclosures

## **EMPLOYEE BENEFITS**

1. **Guidance concerning spousal rollovers of qualified plan and IRA benefits when an estate or trust is named beneficiary of a decedent's interest.**

## **GIFTS AND ESTATES AND TRUSTS**

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2. **Guidance regarding the completion of gifts and inclusion in the gross estate in the context of self-settled asset protection trusts.**
3. **Safe Harbor Guidance concerning the application of the Reciprocal Trust Doctrine.**
2. **Guidance on the tax basis of assets sold on the date of a decedent's death: when does a decedent's tax year end and the estate's tax year begin?**

## **INTERNATIONAL ISSUES**

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2. **Guidance concerning the tax consequences under Code section 643(i) of the undercompensated use by a U.S. person of property owned by a foreign trust.**
3. **Regulation changing the due date for filing Form 3520-A from March 15 to April 15.**
4. **Guidance concerning the coordination of the foreign corporation anti-deferral rules and Subchapter J.**

## **EMPLOYEE BENEFITS**

### **1. Guidance concerning spousal rollovers of qualified plan and IRA benefits when an estate or trust is named beneficiary of a decedent's interest.**

In dozens of private letter rulings issued continuously since 1989, the Internal Revenue Service has affirmed the principle that a surviving spouse who receives from her deceased spouse's estate or trust a distribution from the deceased spouse's retirement plan is entitled to "roll over" that distribution to the surviving spouse's own retirement account even though the decedent's estate or trust was the named beneficiary of the retirement plan, as long as the surviving spouse acting alone possesses the authority to take such benefits out of the estate or trust. In thirty (30) years, the Service has never wavered or varied in its support of this principle; there is no Revenue Ruling or other Service pronouncement countering it. To date, however, the Service has not issued guidance to this effect in a form that can be relied upon by taxpayers, plan administrators, and IRA custodians as "authority" or "precedent" for a tax position. We request that the Treasury issue such guidance now.

The guidance would clearly be relevant to many taxpayers. Absent specialized tax advice during life the spouses would usually not appreciate the benefit of designating the surviving spouse as a named beneficiary when the property at death is intended to pass through or for the benefit of the surviving spouse in any event. Even some financial advisors who are well versed in their profession often demonstrate a lack of awareness of these issues and recommend death beneficiary designations of trusts and estates to their clients. The recurring nature of the problem is demonstrated by the number of requests that the Service has received for private letter rulings. Furthermore, despite dozens of private letter rulings issued on this subject, some retirement plan administrators still refuse to permit the spousal rollover unless the spouse obtains a private letter ruling. That is unnecessarily burdensome on the taxpayer and the Service. The surviving spouse is then forced to seek a private letter ruling or find an IRA provider willing to rely on the principles stated in the private letter rulings of other taxpayers. Even then, some providers may require a formal legal opinion, indemnification, or both.

These difficulties arise when the surviving spouse is already dealing with the major life upheaval caused by the death of his or her spouse, and at the same time, the surviving spouse may be dealing with a number of other issues in the "unplanned" estate, a circumstance which creates additional stress, and risk of financial loss for the surviving spouse. The difficulties already faced by a surviving spouse are needlessly compounded when he or she is compelled to search for a new IRA provider (or obtain an IRS letter ruling) to carry out a rollover that the IRS has repeatedly (though not "authoritatively") confirmed is available.

Issuing authoritative guidance would be extremely helpful to surviving spouses in this position. The guidance can be drafted in a manner that will enable taxpayers, administrators, and custodians to easily understand and apply the guidance. It will promote sound tax administration and it can be administered on a uniform basis among all taxpayers.

The guidance should address the application of the basic principle to recurring categories of facts. As indicated by the private letter rulings, the surviving spouse is entitled to roll over benefits received from a trust or estate only if the surviving spouse possesses an unrestricted right to receive those assets, without being subject to a standard (such as a health or support standard) or the discretion of another party. Qualifying categories would include, for example: (1) the surviving spouse is sole beneficiary of the estate or trust, (2) the governing instrument specifically directs that the benefits shall be paid to the surviving spouse, and (3) the surviving spouse has the right, under the governing instrument or applicable state law, as a beneficiary of the estate or trust, to elect to take the benefits as part of spouse's share of the assets. This last category would include cases where the benefits could be taken under a right to elect against the will (e.g., PLR 2005-52020, where the spouse intended to claim the IRAs as part of her elective share) as well as cases where the surviving spouse has the right, as fiduciary of the estate or trust, to pay the benefits to himself or herself as part of the spouse's share (as beneficiary) of the estate or trust (See, e.g., PLRs 2009-34046, 2009-35045, and 2009-50053).

The guidance should also address circumstances that may call for a broader application of the basic principle, such as whether the spouse has a qualifying right to the retirement benefit even if it is dependent upon a prior steps by another party and to what extent those prior steps need not be clearly mandatory. Suppose for example that the prior steps include an allocation of assets that is mandatory under a reasonable interpretation of state law (and also include a voluntary property exchange, as appeared to be involved in the favorable ruling in PLR 2011-25047). See also PLRs 8920060, 2006-15032, and 2011-25047. The language sometimes used by the private letter rulings is that "no third party can prevent" the spouse from receiving the distribution; (PLR 200632015). In one unique ruling, the trust seemed to allow the surviving spouse (who was not sole trustee) only income, annual RMDs from decedent's IRAs payable to the trust, plus principal if needed, but because the trust specified that the decedent wanted the spouse to be able to roll over the IRAs, the IRS agreed that the trustees were "forced" to distribute the IRAs to the spouse and allowed the rollover. PLR 2001-36030.

It would also be helpful if the guidance covered the proper method of tax reporting for a spousal rollover through an estate or trust.

Also, where the benefits are left to the decedent's estate, and the estate to a trust, and the benefits are payable to the surviving spouse outright under the trust terms, it should not be necessary for the parties to carry out the up to four separate transfers potentially involved (plan to estate, estate to trust, trust to spouse, spouse to IRA). The IRS has recognized that the rollover can be effected by direct transfer from the decedent's plan to the surviving spouse's IRA, skipping the intervening steps. See, e.g., PLRs 2001-36031, 2002-10066, 2009-50058, and 2012-11034. Ideally, authoritative guidance should confirm that the federal tax result is not adversely impacted by skipping the interim steps.

The guidance should address, when the participant's will or trust (or applicable state law) allows or requires debts, expenses, and/or taxes to be paid out of the estate or trust, and therefore arguably out of the retirement benefits payable to the estate or trust, does that potential liability represent a possible limit on the spouse's ability to take the benefits out of the estate or trust even

if those charges are in fact paid from other assets? Most of the PLRs do not even mention this subject, but some mention it and allow the rollover.

It would be helpful if the guidance would confirm that the spousal rollover is allowed through an estate or trust if the applicable conditions are otherwise met, even if, as in PLR 2009-40031, the amount of the surviving spouse's share is established as a pecuniary amount.

The Employee Benefits Committee of ACTEC will provide a more detailed statement on this proposed guidance in a separate letter to follow shortly.

## **GIFTS AND ESTATES AND TRUSTS**

### **1. Regulations or other guidance defining “GST Trust” under Code section 2632(c), particularly relating to trusts that give beneficiaries continuing withdrawal rights attributable to prior year gifts to a trust and trusts that make distributions to a nonskip beneficiary dependent upon both the death of a person more than ten years older and the beneficiary attaining a specified age.**

Code section 2632(c)(3)(B) defines the type of trust to which GST exemption will be automatically allocated in the absence of an election to the contrary (a “GST Trust”). The definition is in the form of a very broad general rule (“a trust that could have a generation-skipping transfer with respect to the transferor”), followed by six exceptions. The six exceptions are designed to exclude trusts to which donors are unlikely to want GST exemption to be allocated, most often because, although a generation-skipping transfer is possible under the terms of the trust, it is unlikely that a generation-skipping transfer will occur with respect to more than 75% of the trust property.<sup>1</sup> The exceptions are in turn followed by “flush language” excepting certain situations from their reach (the exception to the exception).<sup>2</sup>

In the nearly two decades since Code section 2632(c) was enacted, it has become increasingly apparent that this goal of conforming the automatic rules to a transferor's likely intent based on the terms of the trust has been frustrated in certain common types of trusts by a literal reading of two parts of the definition – the second exception to the general rule and a portion of the flush language exception to the exception. We believe that it is possible to interpret both of these provision by regulation in a manner that will cause them to be applied as necessary to better accomplish the goals of the provision. However, because many taxpayers have relied on the literal language of these provisions, any such regulations should apply prospectively and allow a period for taxpayers to elect into their retroactive allocation.

#### **a. The second exception.<sup>3</sup>**

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<sup>1</sup> According to the House Report to H.R. 8 as passed by the House on April 4, 2001, the “Committee recognizes that there are situations where a taxpayer would desire allocation of generation-skipping transfer tax exemption, yet the taxpayer had missed allocating generation-skipping transfer tax exemption to an indirect skip, *e.g.*, because the taxpayer or the taxpayer's advisor inadvertently omitted making the election on a timely-filed gift tax return or the taxpayer submitted a defective election. Thus, the Committee believes that automatic allocation is appropriate for transfers to a trust from which generation-skipping transfers are likely to occur.” House Report, p. 35.

<sup>2</sup> Code § 2632(c)(3)(B)(flush language).

<sup>3</sup> Code § 2632(c)(3)(B)(ii).

Under the second of the six exceptions, a trust is not a GST trust if the trust instrument provides that more than 25% of the trust corpus must be distributed to or may be withdrawn by one or more non-skip persons who are living on the date of death of another person identified in the instrument (by name or by class) who is more than ten years older than such individuals. For example, a trust that will terminate in favor of a child of the transferor on the death of the transferor or the transferor's spouse (if more than ten years older than the child) would fit within this exception and as a result GST exemption would not be automatically allocated to it.

Unfortunately, in the absence of a regulation to the contrary, this exception may be read to not apply to the following common types of trusts to which we believe the exception was intended to apply: (1) a trust that provides for a parent and his or her child or children until the parent's death and then holds the trust property in further trust until the child reaches a specified age, with an outright distribution of the property thereafter, or (2) an insurance trust that provides for distribution of the trust property on the last to occur of the insured's death, the insured spouse's death or when the insured's child reaches a specified age (often younger than age 46, the age specified in the first exception)<sup>4</sup> because no portion of the trust property would be distributed to the child at the death of a person unless the child had already reached the specified age. Therefore, assuming that none of the other exceptions apply,<sup>5</sup> the trusts would be GST trusts and GST exemption would be allocated automatically in the absence of an election to the contrary and except in the case of an addition to the trust after the child has attained the specified age. **However, in both types of trusts at least 25% of the trust principal is likely to pass to a non-skip person (the child) because most individuals outlive their parents and reach age 46 (if the specified age is younger than age 46).** As a result, it is likely that most transferors would not want to allocate GST exemption to the trust.

We believe regulations could and should make it clear that the second exception to the general rule applies (1) even if in addition to surviving a person who is at least 10 years older than the non-skip person, the non-skip person has to reach an age younger than age 46, the age specified in the first exception and (2) even if the non-skip person needs to survive more than one person, as long as each is at least 10 years older than the non-skip person. A narrower approach to the second suggested clarification would be to provide that for purposes of this exception a married couple is treated as a single person.

#### **b. The flush language exception to the exceptions.<sup>6</sup>**

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<sup>4</sup> Code § 2632(c)(3)(B)(i), which provides that a trust is not a GST trust if the trust instrument provides that more than 25% of the trust corpus must be distributed to or may be withdrawn by one or more non-skip persons before that individual reaches 46 years of age, on or before one or more dates specified in the trust instrument that will occur before such individual attains 46 years of age, or upon the occurrence of an event that in accordance with Treasury regulations may reasonably be expected to occur before the date that such individual attains age 46. Code § 2632(c)(3)(B)(i). That exception applies, for example, to a trust that will terminate in favor of its beneficiary when the beneficiary reaches age 45.

<sup>5</sup> Note that these type of trusts do not fit within the first exception because the death of an individual's parent or parents, in most instances, may not reasonably be expected to occur before the child reaches age 46.

<sup>6</sup> Code § 2632(c)(3)(B)(flush language).

Several of the exceptions,<sup>7</sup> without more, would apply to trusts in which one or more non-skip persons are granted a temporary right to withdraw trust property whenever property is contributed to the trust. Such lapsing withdrawal rights are often limited to the amount of the annual exclusion and lapse during or at the end of the year of the contribution, at least to the extent the lapse will not cause the power holder to be treated as having made a taxable gift by reason of the so called 5 x 5 rule of Code section 2514(e). Because many trusts that grant these powers are likely to give rise to generation-skipping transfers, an exception to this deemed allocation exception provides that the value of transferred property is not considered to be includible in the gross estate of a non-skip person or subject to a right of withdrawal by reason of such person holding a right to withdraw so much of such property as does not exceed the annual exclusion amount referred to in Code section 2503(b) with respect to any transferor. Thus, a trust with such a withdrawal right that does not fall within any of the other exceptions will be a GST trust and the deemed allocation will occur.

Unfortunately, in the absence of a clarifying regulation, this special rule for withdrawal rights tied to the annual exclusion may not always apply to trusts with powers that lapse each year only to the extent of the 5 and 5 rule. Put differently, it may not apply to transfers made at a time when the total amount that may be withdrawn (the sum of the withdrawal right arising by reason of the transfer in the current year and all prior year withdrawal rights that have not lapsed as of the date of the transfer) exceeds the current year's annual exclusion with respect to any transferor. Without this exception to the exceptions, such a trust will meet the fourth exception (and perhaps the first exception if the withdrawal amount exceeds 25% of the value of the trust property, which would not be unusual in the early years of an insurance trust) and thus will not be a GST trust for those transfers. Thus, in the first year that transfers are made to such a trust, if the amounts that could be withdrawn are within annual exclusion amount, the trust will be a GST trust and the deemed allocation will apply. In future years, the continuation of a portion of a power from one year to the next may cause the trust to no longer be a GST trust such that no deemed allocation will apply.

We believe regulations could and should rectify this confusing and complicated situation by providing that the exception to the exceptions for annual exclusion withdrawal rights applies if at the time of any transfer that gives rise to a withdrawal right, the amount subject to the withdrawal right "does not exceed the amount referred to in Code section 2503(b) with respect to any transferor" without regard to whether in future years all or a portion of the withdrawal right from a prior year remains outstanding. Put differently, we believe regulations could provide that once it is determined pursuant to the flush language that a withdrawal amount is not to be taken into account in applying the exceptions to the broad definition of a GST trust, such withdrawal amount is not to be taken into account in any year even if unlapsed.

## **2. Guidance regarding the completion of gifts and inclusion in the gross estate in the context of self-settled asset protection trusts.**

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<sup>7</sup> The fourth exception, for example, provides that a trust is not a GST trust if any portion of it would be included in the gross estate of a non-skip person (other than the transferor) if such person died immediately after the transfer. Code § 2632(c)(3)(B)(iv).

In an environment of increasing concern that wealth can attract claims and create risks, it is becoming more common for grantors to create trusts in which, for their lives, they themselves (and sometimes others too) have an interest, often in a trustee's discretion. The trust is designed to protect the trust assets from both opportunistic claims and the unwise decisions of grantors themselves. Because the amount of wealth involved in such self-settled trusts is often substantial, it is important for those grantors to know the gift and estate tax consequences – that is, whether and to what extent the transfer will be complete enough to be a taxable gift for federal gift tax purposes and whether and to what extent the value of the trust property will be included in the grantor's gross estate for federal estate tax purposes. Of those two issues, the completed gift issue is the most important, because it has immediate impact.

The principle typically applied to determine whether a transfer is a completed gift is in Treas. Reg. section 25.2511-2(b):

As to any property, or part thereof or interest therein, of which the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for his own benefit or for the benefit of another, the gift is complete. But if upon a transfer of property (whether in trust or otherwise) the donor reserves any power over its disposition, the gift may be wholly incomplete, or may be partially complete and partially incomplete, depending upon all the facts in the particular case. Accordingly, in every case of a transfer of property subject to a reserved power, the terms of the power must be examined and its scope determined.

The completed gift issue was spotlighted by the disclosure of an Office of Chief Counsel Internal Revenue Service Memorandum dated September 28, 2011 (opened to public inspection on February 24, 2012, as CCA 201208026). Quoting the above regulation, CCA 201208026 concludes that Donors had made completed gifts to a Trust (albeit not a “self-settled” trust from which the Donors themselves could receive distributions). CCA 201208026 has attracted attention among practitioners because it finds a completed gift despite the Donors' testamentary powers over the disposition of the trust property upon their deaths, powers that estate planners have frequently used specifically to prevent a transfer from being a completed gift. This in turn has raised questions about the continued application of the published guidance on which those practitioners have relied, including in the context of self-settled trusts.

As an example, Rev. Rul. 62-13, 1962 C.B. 180, ruled a transfer in trust incomplete because trustees had discretion to pay income and/or principal to the grantor and others during the grantor's life and there was therefore “no assurance that anything of value would ever pass to the remaindermen,” even though the grantor retained no power to direct the disposition of the remainder. Thus, CCA 201208026 presents the anomaly that its Donors with a power of appointment over the trust property at death were left with “no power to change [the trust property's] disposition,” while the grantor in Rev. Rul. 62-13 who retained no power had not “parted with dominion and control.” But CCA 201208026 does not cite Rev. Rul. 62-13 (or Rev. Rul. 77-378, 1977-2 C.B. 347, which “clarified” it).

As another example, CCA 201208026 rests its holding on the fact that the Donors' "limited power to appoint so much of [the trust property] as would still be in the Trust at his or her death" would be reduced or eliminated – in effect terminated – by the trustee's discretionary distributions during the Donors' lives. Treas. Reg. section 25.2511-2(f) specifically addresses the "termination" of such a power, including termination by the "receipt of income or of other enjoyment of the transferred property by the transferee or by the beneficiary (other than by the donor himself)," which "operates to free such income or other enjoyment from the power." But CCA 201208026 does not cite Treas. Reg. section 25.2511-2(f).

We appreciate that CCA 201208026 is necessarily a part of a larger file, that it is addressed to Area Counsel and thus possibly written in contemplation of litigation (or at least serious pursuit of issues in audit), and that it recites that it "may contain privileged information" (although no redaction other than identifying details, including identification of the jurisdiction, is apparent), and for all those reasons it may not tell the whole story. We also appreciate that CCA 201208026 may not be used or cited as precedent (and it so recites). Nevertheless, such documents, when made available for public inspection, are used by practitioners to guide their own best practices and assist them in advising clients. Thus, balanced (and citable) guidance that seeks to resolve questions rather than to pursue a litigation position would be desirable and would foster uniform treatment and compliance. As we have seen in other contexts (such as Rev. Rul. 81-51, 1981-1 C.B. 458, and Rev. Rul. 2004-64, 2004-2 C.B. 7), such guidance could and perhaps should address the extent to which it will be applied prospectively under Code section 7805(b)(8).

### **3. Safe Harbor Guidance concerning the application of the Reciprocal Trust Doctrine.**

Since 1940, the courts have recognized there were circumstances when trusts can be so interrelated that the economic positions of the persons who created the trusts have not changed enough to honor the separate trusts for certain tax purposes. As a result, it is possible that trusts created at about the same time may be "uncrossed" and one or more of the retained power provisions (Code sections 2036-2038) applied to cause a portion or all of the value of a trust to be included in the settlor's gross estate. This result can obtain even though the settlor was not a beneficiary of that included trust and did not retain a power with respect to that trust which would cause such inclusion absent the existence of the so-called reciprocal trust. This has come to be known as the "Reciprocal Trust Doctrine."

Even though the Doctrine was recognized and applied by the United States Supreme Court in *United States v. Grace* (395 U.S. 316 (1969)), the federal courts and the Internal Revenue Service have been required to define and apply the doctrine in a variety of settings with varying results. See, for example, *Estate of Bischoff* (69 T.C. 32 (1977)), *Estate of Herbert Levy* (T.C. Memo 1983-453 (1983)), *Estate of Green v. United States* (68 F. 3d 151 (6<sup>th</sup> Cir. 1995)), and Private Letter Rulings 199643013 and 200426008. Taxpayers and their advisors frequently are faced with a planning situation where both spouses are planning to engage in an arrangement concerning the wealth of the spouses and their family that is best structured using two trusts, which ideally might be identical in terms but for the identity of the settlors. This is most common when spouses are designing mirror image arrangements for themselves and younger family members. Skilled practitioners are able to create degrees of difference which should decrease the possibility of uncrossing such trusts. However, in the absence of a definitive set of

rules addressing this issue, taxpayers and their advisors are left to speculate, which can lead to extreme variations in plans solely to assure that one does not run afoul of the Doctrine.

While it may not be necessary to address the full range of variations that should result in trusts that need not be uncrossed, it should be possible to create greater clarity by acknowledging a set of safe harbors such as the existence of separate trustees (or co-trustees when the settlors have been named as fiduciaries) or differences in the powers granted to the spouses, both of which would make it possible to have trusts with a common purpose without requiring some of the differentiation and distortion commonly applied currently to avoid the application of the Doctrine.

**4. Guidance on the tax basis of assets sold on the date of a decedent's death: when does the decedent's tax year end and the estate's tax year begin?**

Under Code section 1014(a), the basis of property acquired from a decedent is “the fair market value of the property at the date of the decedent's death.” The introductory phrase of Code section 1014(a) references property acquired from a decedent. The subsection does not reference the treatment of property sold before the decedent's death. Presumably, such property would not be acquired from the decedent since it had been sold by the decedent. An adjustment to basis therefore would not be permitted since acquisition from the decedent is required. Only assets sold after the decedent's death would receive an adjustment to basis.

Code section 1014(a)(1) references the value of the property at the “date” of the decedent's death rather than at the “time” of the decedent's death. Presumably, section 1014(a)(1) uses the term “date” rather than “time” as a matter of administrative convenience. There is no indication that the choice of the term “date” implies that the basis adjustment applies to property sold before the decedent's death.

Thus it seems that Code section 1014(a) requires a bifurcation of all sales on the date of the decedent's death to determine which assets are sold prior to the decedent's death and those assets sold after the decedent's death. ACTEC believes that it would be helpful for the IRS to issue guidance on the treatment of assets sold on the date of the decedent's death.

The existing guidance on this issue is inconsistent. Treas. Reg. section 1.6012-3(b)(1), for example, provides: “For the decedent's taxable year which ends with the date of his death, the return shall cover the period during which he was alive.” Similar to Code section 1014(a), this Treasury Regulation seems to require a bifurcation of sales occurring on the date of the decedent's death. In contrast, IRS Publication 559, Survivors, Executors, and Administrations, sets forth the following example:

Samantha Smith died on March 21, 2017, before filing her 2016 tax return. Her personal representative must file her 2016 return by April 18, 2017. Her final return covering the period from January 1, 2017, to March 20, 2017, is due April 17, 2018.

In this example, Samantha's final tax year ends on March 20, 2017, the day before her actual date of death on March 21, 2017. Presumably, a sale on the actual date of death of March

21, 2017 would not be reflected on the final return. Thus, in contrast with the bifurcation that Code section 1014(a) and Treas. Reg. section 1.6012-3(b)(1) seem to require, the example in Pub. 559 terminates the decedent's tax year on the day before death. Further confusion arises from Treas. Reg. sections 1.443-1(a)(2) and 1.691(a)-1(b), which provide that the last day of a decedent's tax year is the date of death.

While a decedent cannot herself sell assets after the moment of death, sales do actually occur on the day of the decedent's death. For example, a taxpayer could sell assets during the business day and then die after the time of sale. Alternatively, if assets are held in a revocable trust, a trustee – unaware of a decedent's death – could sell assets on the date of death.

There are several possible resolutions of this issue.

**a. Bifurcation of Date of Death**

As discussed above, one solution would be to bifurcate the date of death. In that case, sales that took place before the time of the decedent's death would appear on the decedent's final income tax return and would not be subject to a basis adjustment, whereas sales that took place after the moment of death would be reflected on the estate's income tax return and would receive a basis adjustment under Code section 1014. Similarly, the decedent's final tax year would end at the time of the decedent's death and the tax year for the decedent's estate would begin immediately after the time of the decedent's death.

Bifurcation has the advantage that it would prevent “gaming” the system. The time listed on the death certificate could be given the presumption of accuracy. However, in reality, many taxpayers die under circumstances such that their actual time of death is unknown. For example, when a decedent dies unaccompanied at home, the time of death may be an estimate made after the body is discovered.

**b. Final Tax Year Ends Day Before Death**

IRS Publication 559 takes the position that the decedent's final tax year ends on the day before the decedent's date of death. If that were the rule, any sale on the actual date of the decedent's date of death would be reported on the estate's income tax return which begins on the actual day of the decedent's death. With this approach Code section 1014 would apply to all assets sold on the date of death. This approach does a disservice to those taxpayers who actually sell assets on the date of death but before their deaths seeking to report losses, as the basis adjustment would wipe out the losses.

**c. Final Tax Year Ends on Date of Death**

Consistent with Treas. Reg. sections 1.443-1(a)(2) and 1.691(a)-1(b), the rule would be to end the decedent's final tax year on the actual day of the decedent's death and begin the estate's tax year on the day after the decedent's date of death. Any sale on the date of death would be reported on the decedent's final tax return. Code section 1014 would not apply to sales on the date of death with this alternative. For those assets with inherent gains, this approach would require the gains to be realized and reported on the decedent's final income tax return regardless

of the fact that the sale may have occurred after the time of the decedent's death. This approach would work a disservice for those attentive fiduciaries who wish to quickly liquidate assets on the decedent's date of death.

**d. Election**

A final option would be to allow a taxpayer's executor to elect to bifurcate the day of the decedent's date of death or to treat all sales on the day of the decedent's death as being made by the decedent's estate or to treat all sales on the day of the decedent's death as being made by the taxpayer.

**e. Recommendation**

The IRS should issue guidance that is clear and consistent, addressing (1) the tax basis of assets sold on the date of a decedent's death, and (2) when a decedent's tax year ends and the estate's tax year begins. We believe that bifurcating the decedent's day of death for these purposes is the preferred and fairest approach, since it is consistent with the plain language of Code section 1014(a) and it prevents manipulation. Specifically, the decedent's tax year should end with the moment of death, the estate's tax year would begin immediately after the time of death, and section 1014(a) would only apply to those sales occurring after the moment of death.

## INTERNATIONAL ISSUES

### 1. **Additional guidance concerning the application of the Foreign Account Tax Compliance Act (“FATCA”) provisions of the Hiring Incentives to Restore Employment (“HIRE”) Act (P.L. No. 111-147, 124 Stat. 71 (2010) on reporting and withholding with respect to trusts and their beneficiaries.**

In 2014, ACTEC recommended that guidance be issued concerning the application of the Foreign Account Tax Compliance Act (“FATCA”) provisions of the Hiring Incentives to Restore Employment (“HIRE”) Act (P.L. No. 111-147, 124 Stat. 71 (2010) on reporting and withholding with respect to trusts and their beneficiaries. Since then, final regulations have been issued (See T.D. 9610, 2013-15 I.R.B. 765 (2013); T.D. 9657, 2014-13 I.R.B. 687 (2014)), and additional guidance has been forthcoming in the form of new Intergovernmental Agreements (“IGA”)s with many other countries (“FATCA Partners”). Several FATCA Partners have issued Guidance Notes to explain the provisions of the IGA. Although the final regulations and Guidance Notes have been extremely helpful, some issues remain. Some issues are (i) whether a person’s future interest in a trust is considered to be a mandatory beneficial interest for purposes of FATCA reporting; (ii) whether a private trust company and a trust managed by a private trust company are foreign financial institutions; and (iii) whether a trust managed by an individual trustee becomes a foreign financial institution if some of the trust funds are invested in one or more separate investment funds that are financial institutions (such as a mutual fund).

#### **a. Who is a “beneficiary” for purposes of FATCA?**

For purposes of FATCA, a beneficiary means a beneficiary who has a mandatory distribution right and a discretionary beneficiary if and to the extent such beneficiary actually receives a distribution. Treas. Reg. §1.1471-5(b)(3)(iii)(B). A person whose interest is wholly discretionary and who does not actually receive a distribution is not a beneficiary. Treas. Reg. §1.1471-5(b)(3)(iii)(B)(3). However, the regulations do not specifically address the treatment of a person who has a mandatory future interest in the trust, whether vested or contingent. For example, suppose the trust instrument says that income should be distributed to A for life and then to B for life and then to C if C is then living. Do the interests of B and/or C have to be reported?

Code section 6038D(a) requires U.S. taxpayers with specified foreign financial assets (including certain interests in foreign entities) to report these investments on an information return (Form 8938) when the aggregate value of the investments exceeds \$50,000. A U.S. taxpayer’s interest in a foreign trust is not considered to be a specified foreign financial asset for these purposes unless he or she knows or has reason to know (based on readily accessible information) of the interest. Treas. Reg. §§1.6038D-2(b)(4)(iv), 1.6038D-3(c). Receipt of a distribution from the foreign trust constitutes actual knowledge for this purpose. Treas. Reg. §1.6038D-3(c). The maximum value of a beneficiary’s interest in a foreign trust (*i.e.*, the value required to be reported on Form 8938) equals the sum of the amount actually received in the taxable year plus the present value of a mandatory right to receive a distribution. Treas. Reg. §1.6038D-5(f)(2). The regulations do not distinguish between reporting obligations of taxpayers who have mandatory present interests versus those who have mandatory future interests in foreign trusts.

We suggest that future interests be ignored for FATCA reporting purposes because reporting is not necessary to protect the right to collect taxes. A beneficiary of a future interest is not required to pay income tax and should not be required to file information returns.

This suggestion is consistent with the FBAR regulations, which also disregard future interests. See 31 C.F.R. §1010.350(e)(2)(iv) (defining “financial interest” to include “[a] trust in which the United States person either has a present beneficial interest in more than 50 percent of the assets or from which such person receives more than 50 percent of the current income.”)

We recommend that the FATCA regulations be amended to address future interests in the same manner that the FBAR regulations do, by adding specific language to Treas. Reg. section 1.1471-5(b)(3)(iii)(B) saying that: “A future interest is not an equity interest in a trust for these purposes.” We recommend adding specific language to Treas. Reg. section 1.6038D-3(c) saying that: “A future interest in a foreign trust is not a specified foreign financial asset of a specified person.”

- b. Private trust companies and trusts managed by private trust companies should not be treated as financial institutions for purposes of FATCA because they are not engaged in a trade or business with the general public and therefore function more like an individual trustee than an institutional trustee.**

We note that in at least one Guidance Note (for Cayman Islands) the conclusion is reached that a private trust company that is not “doing business” in the Cayman Islands is not a financial institution. Guidance Notes on the International Tax Compliance Requirements of the Intergovernmental Agreements between the Cayman Islands and the United States of America and the United Kingdom, §6.14, U.S.-Cayman Is.-U.K., Dec. 15, 2014.

We suggest that Treas. Reg. section 1.1471-5(e)(4)(i) be amended to provide that “A private trust company that is not engaged in the trade or business of providing services to the general public is not a financial institution, and trusts managed by such a private trust company are not, for that reason alone, treated as investment entities under (e)(4)(i)(B) of this section or as financial institutions under (e)(1)(iii) of this section.”

- c. Clarify whether all trusts that are FFI’s can use the “Trustee-documented trust” method of reporting if the trust is not resident in a country that has an IGA and whether a private trust company may use the Trustee-documented reporting method whether or not the private trust company is an FFI.**

The FATCA regulations do not provide for the Trustee-documented trust method of reporting. This method is provided for in both model 1 and model 2 IGA’s, Annex II, paragraph IV, which provide:

The Financial Institutions described in paragraphs A through E of this section are Non-Reporting Cayman Islands Financial Institutions that are treated as deemed-compliant FFIs for purposes of section 1471 of the U.S. Internal Revenue Code.

In addition, paragraph F of this section provides special rules applicable to an Investment Entity.

**A. Trustee-Documented Trust.** A trust established under the laws of the Cayman Islands to the extent that the trustee of the trust is a Reporting U.S. Financial Institution, Reporting Model 1 FFI, or Participating FFI and reports all information required to be reported pursuant to the Agreement with respect to all U.S. Reportable Accounts of the trust.

The classification of private trust companies as FFIs is uncertain. The Cayman Islands Guidance Notes to the IGA, indicate that not all private trust companies may be FFIs. Section 6.14 of the Cayman Islands Guidance Notes version 2.1 (July 2015) provides as follows:

A Private Trust Company (PTC) which is registered, or a similar trust company which is licensed, and conducting business in or from within the Islands, *may be considered* a Financial Institution for these purposes.

In the case of a trust of which a PTC is the trustee and the trust has all its income derived from financial assets, under the definitions of Investment Entity outlined in Section 2.9, the trust *may be* a Financial Institution. (Emphasis added)

We recommend that the trustee-documented method of reporting be permitted for all trustees, wherever located, who agree to perform the necessary reporting and for private trust companies whether or not they are classified as FFIs.

**d. Trusts managed by individual trustees are not financial institutions. Treas. Reg. §§1.1471-5(e)(4)(i)(B), 1.1471-5(e)(4)(v), Example (5). However, if a trust with an individual trustee engages a financial institution to manage investments on a discretionary basis, then the trust may be a financial institution. Treas. Reg. §§1.1471-5(e)(4)(i)(B), 1.1471-5(e)(4)(v), Example (6).**

The regulations are not clear whether a trust becomes a financial institution if the individual trustee invests some or all of the trust funds in one or more pooled investment vehicles, such as mutual funds. It is very typical for individual trustees to invest trust funds in mutual funds. It does not seem to be the intent of the regulations to make such a trust a financial institution because in this case the individual trustee remains responsible for investments, and monitoring the performance of a fund seems to be the same as monitoring the performance of individual stocks and bonds, but clarification of this point would be helpful so that the filing status of a trust could be clear.

**2. Guidance concerning the tax consequences under Section 643(i) of the undercompensated use by a U.S. person of property owned by a foreign trust.**

Code section 643(i) was amended by the Foreign Account Tax Compliance Act (“FATCA”) provisions of the Hiring Incentives to Restore Employment (“HIRE”) Act (P.L. No. 111-147, 124 Stat. 71 (2010) to provide that the use by certain U.S. persons of property owned by a foreign trust would be deemed to be a distribution by the trust equal to the fair market value

of the use of such property except to the extent adequate consideration for such use was timely paid. The amendment was effective on date of enactment, March 18, 2010. Prior to this amendment, the statute applied only to loans of cash or marketable securities and not to “loans” of other property, such as residences or works of art.

The statute applies to use by a U.S. person who is a grantor, a beneficiary or any other person who is related to a grantor or beneficiary. A person is related to a grantor or beneficiary by application of the rules in Code section 267 or Code section 707(b) applied as if family members included spouses of members of the family.<sup>8</sup> If the person using the trust property is not a grantor or beneficiary, the deemed distribution is treated as made to the grantor or beneficiary to whom such person is related rather than to the person who is or was actually using the trust property. If the person using the property is related to more than one grantor and/or beneficiary, the deemed distribution to the grantor and/or beneficiaries is to be allocated among them in accordance with regulations. No regulations or other guidance has been issued.

If compensation is paid for the use of property other than cash or marketable securities, the deemed distribution is reduced by the amount of such compensation if it is paid within a reasonable period of time of such use.

If the statute applies to deem a distribution to have been made, any subsequent transaction, such as the return of such property to the trust, shall be disregarded.

Guidance is needed concerning the following issues:

- How should the trustee and the taxpayer determine the fair market value of the use of property where there is inadequate data for determining the fair market value of the use of such property? An example would be the fair rental value of fine art. To make compliance easier, a rule of convenience would be helpful. A similar rule of convenience exists, for example, for determining fair market interest rates and the present value of life estates, annuities and remainders. A similar rule could be used for determining the fair rental value of property for which no market data is readily available.

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<sup>8</sup> Thus, related persons include members of the family (sibling, brother or sister-in-law, spouse, ancestors and their spouses, and descendants and their spouses), an individual and a corporation more than 50% owned by such individual, two corporations which are members of the same controlled group, a grantor and a fiduciary of a trust created by such grantor, fiduciaries of separate trusts created by the same grantor, a fiduciary and a beneficiary, a fiduciary and a beneficiary of another trust if the same person is the grantor of both trusts, a fiduciary of a trust and a corporation more than 50% owned by the trust or by the grantor of the trust, a person and an exempt organization if the organization is controlled by the person or a member of such person’s family, a corporation and a partnership if more than 50% of the stock or more than 50% of the capital or profits interest in the partnership interests are owned by the same persons, S corporations if the same persons own more than 50% of the stock of both, an executor of an estate and a beneficiary of an estate, a partner and a partnership if the partner owns more than 50% of the capital or profits interest and two partnerships in which the same persons own more than 50% of the capital or profits interest. In applying the related party rules, a person is treated as indirectly owning stock held through a corporation, partnership, estate or trust in which such person has an interest, and is treated as constructively owning stock owned by a family member.

- How should the trustee and the taxpayers allocate the deemed distribution where more than one person uses the property owned by the trust or the person using such property is related to more than one beneficiary and/or the grantor?
- What are the tax consequences of the receipt by the trust of compensation for the use of trust property paid by a grantor, beneficiary or related person? For example, will a beneficiary realize gross income from payments such beneficiary herself made to the trust which are distributed or required to be distributed back to her? If the rental is for the use of U.S. property, is tax withholding required? Will compensation for the use of property include expenses of use (such as utilities and condominium fees) paid by the person who uses the property and, if so, will the foreign trust be deemed to have received gross income where such person pays such expenses?
- It would be helpful to confirm that the deemed distribution carries out trust income and accumulated income but does not create income.
- It would be helpful to confirm that the statute does not apply to grantor trusts covered by Subpart E of Subchapter J.
- It would be helpful to clarify the provisions of Code section 643(i)(3) providing that subsequent transactions, such as the return of property to the trust, will be disregarded.

### **3. Guidance under Code section 6048 changing the due date for filing Form 3520-A from March 15 to April 15.**

Under Code section 6048(b), U.S. persons treated as “owners” of a foreign trust (“U.S. Owners”) must annually file a return confirming such status and must also ensure that the trust files a return providing a full and complete accounting of all trust activities and operations. The trust’s return is filed on Form 3520-A. The Form 3520-A instructions and Notice 97-34, 1997-1 C.B. 422, indicate that Form 3520-A is due by the 15th day of the third month following the close of the trust’s tax year.<sup>9</sup> Because Code section 644 provides that all trusts other than tax exempt and charitable trusts must adopt a calendar year as their taxable year for U.S. tax purposes, as a practical matter most Forms 3520-A are due on March 15<sup>th</sup>.

The Form 3520-A filing was conceived as the filing obligation of a foreign trust. However, because it is the U.S. Owner, not the trust itself, who is responsible for ensuring the form is filed, in practice the preparation and filing of the form falls to the U.S. Owner. As a result, the March 15<sup>th</sup> due date for the Form 3520-A acts as a trap for the unwary. In most cases, the U.S. Owner has an April 15<sup>th</sup> deadline for his own income tax return and therefore may not consider the filing obligations with respect to the trust until after the March 15<sup>th</sup> deadline has passed.

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<sup>9</sup> Confusingly, temporary regulations under section 6048 applicable solely to foreign grantor trusts described in section 679 specify an April 15<sup>th</sup> deadline for filing the Form 3520-A. Treas. Reg. § 401.6048-1(c)(1). These regulations pre-date the current version of section 6048.

The likely rationale for the March 15<sup>th</sup> deadline is to ensure that the U.S. Owner has time to review the Form 3520-A information and include it on his own return and Form 3520. Because the U.S. Owner is responsible for ensuring that the Form 3520-A is filed, however, in most cases the U.S. Owner's tax preparer is charged with completing the Form 3520-A, making this lead time unnecessary. Thus, we would suggest that the IRS issue guidance adopting an April 15<sup>th</sup> due date for the Form 3520-A to avoid confusion and simplify administration. In any event, the IRS should consider issuing guidance that the filing of a Form 4868 by the U.S. Owner to extend his own return is effective to extend the due date for the Form 3520-A.

#### **4. Guidance concerning the coordination of the foreign corporation anti-deferral rules and Subchapter J.**

The corporate anti-deferral rules applicable to controlled foreign corporations ("CFCs") and passive foreign investment companies ("PFICs") and the accumulation distribution rules applicable to trusts serve the same purpose – preventing the use of foreign entities to defer payment of tax or imposing an interest charge if tax payment is deferred. Proposed regulations on the corporate anti-deferral rules for passive foreign investment companies were issued on April 1, 1992, and have not been finalized. The preamble notes the need to coordinate the accumulation distribution rules of Subchapter J and the PFIC tax regime. We agree, but there has been no further published guidance on this issue in over twenty-five years. ACTEC submitted comments on this subject to representatives of the Department of the Treasury on June 23, 2010. The CFC attribution rules are an even more pressing issue in light of the changes to the CFC definition and reporting requirements in the Tax Cuts and Jobs Act of 2017.

On December 31, 2013, final, temporary and proposed regulations were issued that provide guidance on determining ownership of a PFIC.<sup>10</sup> The temporary regulations adopt the rule set forth in the proposed regulations by treating beneficiaries of nongrantor trusts and estates as owning stock in proportion to their beneficial interests, which are determined by applying a facts and circumstances test.<sup>11</sup> The temporary regulations provide that a beneficiary may be attributed ownership of PFIC stock owned by a nongrantor trust or estate whether the trust or estate is foreign or domestic. The temporary regulations also provide guidance on the annual filing requirement imposed by Code section 1298(f) on owners of PFIC stock. Under these regulations, a beneficiary of a foreign nongrantor trust or foreign estate who is considered to be the indirect owner of PFIC shares held by the foreign nongrantor trust or foreign estate is not required to report under Code section 1298(f) provided that no PFIC elections have been made for such year and no excess distribution has occurred.<sup>12</sup> This rule is significantly different from the regulations adopted under Code sections 1471-1474 and 6038D which treat a discretionary beneficiary of a foreign trust who has not received a trust distribution in a particular year as not having a beneficial interest in such trust. Treas. Reg. section 1.1298-1T(b)(iii) supports the conclusion that a beneficiary who is deemed to have received an excess distribution because he/she is treated as an indirect shareholder of a PFIC would have a reporting requirement, and a tax payment obligation, whether or not he/she received, or was entitled to receive, a distribution from the trust.

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<sup>10</sup> T.D. 9650.

<sup>11</sup> Treas. Reg. §1.1291-1T(b)(8).

<sup>12</sup> Treas. Reg. §1.1298-1T(b)(iii).

The preamble to the regulations issued in T.D. 9650 requests guidance on the determination of proportionate ownership by beneficiaries of PFIC shares owned by a nongrantor trust or estate. The preamble also states that the regulations are not providing guidance on the application of the PFIC tax rules when an estate or nongrantor trust, or a beneficiary thereof, receives or is treated as receiving an amount taxable under the PFIC rules as an excess distribution. Until further guidance is issued, the preamble states that the PFIC and Subchapter J rules must be applied in a reasonable manner to preserve or trigger the tax and interest charge rules on excess distributions under Code section 1291. The preamble also states that it would be unreasonable for the shareholders to take the position that neither the beneficiaries of an estate or trust nor the estate or trust itself is subject to the tax and interest charge on excess distributions under Code section 1291. However, it should not be unreasonable to take the position that such income was not taxable under Code section 1291 if the income was attributable to a foreign person either because the foreign person was the indirect owner of the stock or because a domestic trust or estate distributed such income to a foreign beneficiary in the year it was received.

In light of the preamble, we request that the Priority Guidance Plan include the issues of (1) attribution of ownership of PFIC and CFC shares to beneficiaries of nongrantor trusts and estates; and (2) treatment of income attributable to ownership of stock of a CFC or PFIC through a nongrantor trust or estate.

Comments previously submitted by ACTEC suggested a set of rules that would better coordinate the overlapping PFIC/CFC and subchapter J rules with the objective that tax would be owed at the time a beneficiary of a foreign nongrantor trust or estate received distributions (and not before) but the interest charge on delayed payment of tax would be preserved. Under such rules, it would not be necessary to attribute ownership through nongrantor trusts and estates. The prior comments did not address attribution of ownership through domestic trusts or estates, which we believe is not advisable.

The possible issues include:

- a. If ownership is allocated to beneficiaries, how such allocation will be made, whether it is fair and practical to impose tax on a person based on income he/she has not received and has no enforceable right to obtain, and what adjustments will be made to avoid double tax when income imputed and taxed to a beneficiary is later distributed to someone else or when the trust disposes of shares.
- b. Whether, instead of imputing income to beneficiaries, beneficiaries should be taxed only when they receive distributions (as under Subchapter J) but the interest charge under the accumulation distribution rules would be modified to treat the trust as having accrued income at the time the income accrued to the CFC or PFIC owned by the trust.
- c. Whether it is necessary or advisable to impute to beneficiaries ownership of PFICs held by domestic nongrantor trusts and domestic estates (ownership of CFCs by statute may not be imputed through U.S. entities).

Attribution from domestic nongrantor trusts and domestic estates is unnecessary to protect the PFIC tax regime, since the tax on excess distributions from a PFIC (and gains treated as excess distributions) could be collected from the U.S. taxpayer-trust and/or its U.S. beneficiaries to the extent such income is taxable to the domestic trust and/or its U.S. beneficiaries under the rules of Subchapter J. Moreover, this attribution rule is inconsistent with the attribution rule for CFCs and would interfere with the CFC and PFIC “overlap” rule in Code section 1297(d), which generally provides that where a foreign corporation is both a CFC and a PFIC, the CFC rules “trump” the PFIC rules. Attribution from domestic trusts also is inconsistent with the regulations issued under Code section 1411 addressing the tax treatment of PFIC income received by a U.S. charitable remainder trust (which is not attributed to beneficiaries of such a trust).<sup>13</sup>

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<sup>13</sup> Prop. Treas. Reg. §1.1411-3(d)(2)(ii) provides that income treated as an excess distribution within the meaning of Code section 1291 or gain treated as an excess distribution is included in the tier system applicable to distributions from charitable remainder trusts, which thus could not also be imputed to the beneficiaries of the charitable remainder trust. This is the correct result because imputing the income to beneficiaries would be inconsistent with the rules of Code section 664.