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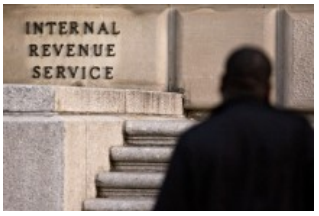
IRS mulls rules for estates and trusts after tax law

By **Michael Cohn**
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The Internal Revenue Service is showing signs that it's planning to issue regulations on the deductibility of expenses for estates and trusts in the wake of the Tax Cuts and Jobs Act.



Earlier this month, the IRS and the Treasury Department issued a notice saying they intend to issue regulations around estates and non-grantor trusts in the context of last December's Tax Code overhaul (see IRS plans regulations on non-grantor trusts and new tax law).

In Notice 2018-61, the IRS and the Treasury said they plan to release regulations to provide clarification on the effect of Section 67(g) of the Tax Code overhaul on the deductibility of certain expenses described in Section 67(b) and that are incurred by estates and non-grantor trusts. They plan to clarify that estates and non-grantor trusts may continue to deduct each expense that is described in Section 67(e)(1) or is allowable under Section 642(b), 651 or 661, in determining adjusted gross income for all taxable years, even while the application of Section 67(a) is suspended pursuant to Section 67(g).

Amanda DiChello, a trusts and estates litigator at the law firm Cozen O'Connor, believes the upcoming regulations could provide some much-needed clarity on deductions for trusts and estates for practitioners.

"The big concern was that everybody thought that these miscellaneous itemized deductions were no longer deductible, and that the change in the Tax Code was going to prevent the deductibility of those for individuals," she said.

The notice seems to indicate that some of the same expenses that used to be deductible before the passage of the Tax Cuts and Jobs Act would still be deductible for trusts and estates, although the regulations themselves have yet to be issued.

"A trust files an income tax return just like an individual does, and on that tax return are certain deductions — above the line, or below the line — deductions that are taken on the return against gross income," said DiChello. "The concern was whether things like administration expenses and counsel fees would still be deductible with the changes in the current Tax Code on itemized deductions. It looks like they're saying yes to the extent that those deductions pertain to the fact that this is a trust and that trust has these ongoing obligations by reason of it being a trust and not an obligation that it would otherwise have if it was an individual, that they are deductible as above-the-line expenses. I think that was good news to see that the IRS is taking the position that they're still deductible, but it remains to be seen entirely what the regs are going to say on this."

She is unsure whether the regulations will deal with the use of non-grantor trusts as a way to get around the limits in the TCJA on deductibility of state and local taxes such as property taxes. The IRS has already indicated it will take a dim view on the use of state-run charitable funds as a way to get around the limits on state tax deductions. But the IRS may be more willing to allow trusts and estates to keep their traditional tax benefits.

"It would appear that they're still keeping the door open to the deductibility of a lot of these expenses that are trust-related costs, but they definitely differentiate," said DiChello. "For instance, investment advisory fees have long been an issue for deductibility of non-grantor trusts because the argument is that they're expenses that an individual would incur on their own. They're not special trust expenses."

She pointed to the 2008 Supreme Court decision in the case Knight v. Commissioner, which centered on the deductibility of investment expenses. The court ruled on the applicability of the 2 percent adjusted gross income limit to the deductibility of investment fees by trusts.

"You can have a full deduction only for those costs that could not have been incurred by an individual property owner, and the result is that investment advisory fees were at the time subject to the 2 percent floor on itemized deductions against AGI," said DiChello. "Now that 2 percent floor is gone and we're dealing with [whether] any expenses the trust incurred are specific to the trust being a trust, and not expenses that an individual would incur. Because of that, I think the same policy is going to apply to investment advisory fees. Investment advisory fees weren't deductible before, and I think they're going to remain not deductible. I don't think much is going to change on the above-the-line deductions, not for fiduciary income tax returns."

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She sees a bigger issue in the matter of carryforward losses for the final year of the tax return for a trust or an estate. "Those could be distributed out to the beneficiary, and what we're looking at as practitioners is whether or not the ability to distribute those out in the final year of the trust or estate's income tax return, whether that's going to be curbed because of the new Tax Code and what the regs are going to say on that," said DiChello. "I think the notice suggests that they're going to come to a conclusion or provide clarification on that issue. That's a really big issue because when we do administration, in the final year it's always an added benefit to be able to carry forward the losses and to be able to distribute them out, so that could be an impactful result depending on what position they take on that. In that notice they weren't clear. They were more clear on their position as to the deductibility of itemized deduction issues for trusts and estates than they were on that issue of the carryforward losses and the distribution of them."

She noted that the IRS is looking for comments from practitioners on the notice, and the answer could ultimately depend on the feedback it receives.

"The notice suggested they're looking for practitioners to weigh in, and I think that some of what they do is going to depend on what they're getting," said DiChello. "I would think that there's going to be a lot of weighing in on the latter issue because it could have a big impact on estates and trusts. I don't think it's the intended result of the change under Section 67, so I think if the IRS is going to take the position that the deductions could still be made with respect to estates and trusts on their taxes, it would seem to be inconsistent to me that they should suggest that they can't carry forward the loss in the final year and distribute it out."

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Michael Cohn, editor-in-chief of AccountingToday.com, has been covering business and technology for a variety of publications since 1985.

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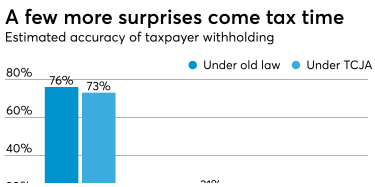
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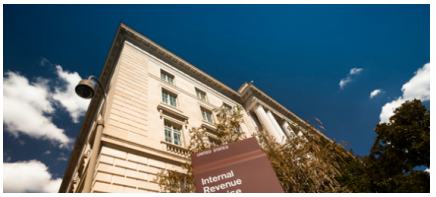
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