Bloomberg Tax

bloombergbna.com

Reproduced with permission. Published August 10, 2018. Copyright © 2018 The Bureau of National Affairs, Inc. 800-372-1033. For further use, please visit http://www.bna.com/copyright-permission-request/

*Trusts*

# Use Trusts for Pass-Through Tax Break? Yes, You Still Can

BY ALLYSON VERSPRILLE

Taxpayers could still use multiple trusts to exploit a tax break for pass-through businesses under newly proposed IRS rules, because the rules' trust restrictions apply only if the trusts have the same beneficiary.

Multiple trusts would still work as long as there are different beneficiaries of each trust. "And that's the right answer, because they are separate in reality" for tax purposes, said Don Kozusko, a partner at Kozusko Harris Vetter Wareh Duncan LLP in Washington.

The limitation on use of multiple trusts is an anti-abuse provision that the Internal Revenue Service included in Aug. 8 proposed regulations (REG-107892-18) under tax code Section 199A implementing the new tax law's 20 percent deduction for pass-throughs. The businesses, which include sole proprietorships and S corporations among other structures, pass income through to their owners, who pay tax on it at individual rates.

The deduction is available to all pass-through owners making less than $157,500 as individuals or $315,000 as joint filers but is limited above those thresholds.

The anti-abuse measure, drafted under tax code Section 643(f), says that the government will treat multiple trusts as a single trust if they have "substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries," and if "a principal purpose for establishing such trusts or contributing additional cash or other property to such trusts is the avoidance of Federal income tax."

The provision is aimed at preventing taxpayers from using separate nongrantor trusts to split up pass-through assets and take the 20 percent deduction more than once. While it specifically targets Section 199A gaming, James F. Hogan, managing director at Andersen Tax LLC in Washington and a former IRS official, said the provision—because it creates a general rule under Section 643(f)—could potentially be applied to strategies where people divide real estate interests into multiple trusts to game the new $10,000 cap on the state and local tax deduction.

"There were practitioners that were recommending setting up a bunch of different trusts for each child in order to get additional $10,000 SALT deductions," said Jonathan S. Forster, a shareholder at Weinstock Manion in Los Angeles, noting that the same logic could have been applicable to the Section 199A deduction. The anti-abuse rules would prevent taxpayers from setting up multiple trusts for a single child, but "you should be able to set up one trust for many different children," he said in an email.

The key is the phrase "substantially the same" in Section 643(f). This means that a taxpayer can still establish multiple trusts, as long as the beneficiaries are different individuals and there is no cross-over. For example, a parent could create four trusts—one for each child—and do multi-trust planning to get more tax deductions.

**'Warning Shot'** David Kirk, a partner in private client services at Ernst & Young LLP's National Tax Department in Washington, said he believes the IRS already had the tools it needed to crack down on the perceived abuse addressed in the regulations—a grantor establishing multiple trusts for the same beneficiary—especially since the rules don't diverge much from the original statutory language in Section 643(f).

"You might not have needed a reg," he told Bloomberg Tax. He said the anti-abuse provision may be more of a "warning shot" for taxpayers.

Kirk said the strategy the government is attempting to curtail was never something he considered in his own practice "because it was just too much of a nuisance."

Even if taxpayers can use multiple trusts to get additional tax breaks, they may find it's not worth the "administrative costs and the tax compliance costs and the general hassle," Kirk said.

To contact the reporter on this story: Allyson Versprille in Washington at aversprille@bloombergtax.com

To contact the editor responsible for this story: Meg Shreve at mshreve@bloombergtax.com

COPYRIGHT © 2018 BY THE BUREAU OF NATIONAL AFFAIRS, INC.