

15 Trusts and Estates

1. Form 1041—1996 Instructions

Optional Filing Methods for Certain Grantor Type Trusts

Generally, for a trust all of which is treated as owned by one or more grantors or other persons, the trustee may use one of the following three optional methods to report instead of filing Form 1041:

Method 1. For a trust treated as owned by one grantor or by one other person, the trustee must give all payors of income during the tax year the name and taxpayer identification number (TIN) of the grantor or other person treated as the owner of the trust and the address of the trust. This method may be used only if the owner of the trust provides the trustee with a signed Form W-9, Request for Taxpayer Identification Number and Certification. In addition, unless the grantor or other person treated as owner of the trust is the trustee or a co-trustee of the trust, the trustee must give the grantor or other person treated as owner of the trust a statement that (a) shows all items of income, deduction, and credit of the trust; (b) identifies the payor of each item of income; (c) explains how the grantor or other person treated as owner of the trust takes those items into account when figuring the grantor's or other person's taxable income or tax; and (d) informs the grantor or other person treated as the owner of the trust that those items must be included when figuring taxable income and credits on his or her income tax return.

Method 2. For a trust treated as owned by one grantor or by one other person, the trustee must give all payors of income during the tax year the name, address, and TIN of the trust. The trustee also must file with the IRS the appropriate Forms 1099 to report the income or gross proceeds paid to the trust during the tax year that shows the trust as the payor and the grantor or other person treated as owner as the payee. The trustee must report each type of income in the aggregate and each item of gross proceeds separately. In addition, unless the grantor or other person treated as owner of the trust is the trustee or a co-trustee of the trust, the trustee must give the grantor or other person treated as owner of the trust a statement that (a) shows all items of income, deduction, and credit of the trust; (b) explains how the grantor or other person treated as owner of the trust takes those items into account when figuring the grantor's or other person's taxable income or tax; and (c) informs the grantor or other person treated as the owner of the trust that those items must be included when figuring taxable income and credits on his or her income tax return. This statement satisfies the requirement to give the recipient copies of the Forms 1099 filed by the trustee.

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Method 3. For a trust treated as owned by two or more grantors or other persons, the trustee must give all payors of income during the tax year the name, address, and TIN of the trust. The trustee also must file with the IRS the appropriate Forms 1099 to report the income or gross proceeds paid to the trust by all payors during the tax year attributable to the part of the trust treated as owned by each grantor or other person, showing the trust as the payor and each grantor or other person treated as owner of the trust as the payee. The trustee must report each type of income in the aggregate and each item of gross proceeds separately. In addition, the trustee must give each grantor or other person treated as owner of the trust a statement that (a) shows all items of income, deduction, and credit of the trust attributable to the part of the trust treated as owned by the grantor or other person; (b) explains how the grantor or other person treated as owner of the trust takes those items into account when figuring the grantor's or other person's taxable income or tax; and (c) informs the grantor or other person treated as the owner of the trust that those items must be included when figuring taxable income and credits on his or her income tax return. This statement satisfies the requirement to give the recipient copies of the Forms 1099 filed by the trustee.

Exceptions. The following trusts cannot report using the optional filing methods:

1. A common trust fund [as defined in §584(a)].
2. A foreign trust or a trust that has any of its assets located outside the United States.
3. A qualified subchapter S trust [as defined in §1361(d)(3)].
4. A trust all of which is treated as owned by one grantor or one other person whose tax year is other than a calendar year.
5. A trust all of which is treated as owned by one or more grantors or other persons, one of which is not a U.S. person.
6. A trust all of which is treated as owned by one or more grantors or other persons if at least one grantor or other person is an exempt recipient for information reporting purposes, unless at least one grantor or other person is not an exempt recipient and the trustee reports without treating any of the grantors or other persons as exempt recipients.

A trustee who previously had filed Form 1041 for any tax year ending before January 1, 1996 (and who previously had not filed a final Form 1041 under the simplified filing rule in effect prior to January 1, 1996), or who files a Form 1041 for any later tax year, can change to one of the optional methods by filing a final Form 1041 for the tax year that immediately precedes the first tax year for which the trustee elects to report under one of the optional methods. On the front of the final Form 1041, the trustee must write "Pursuant to section 1.671-4(g), this is the final Form 1041 for this grantor trust" and check the "Final return" box in item F. For more details on changing reporting methods, including changes from one optional method to another, see Treas. Reg. §1.671-4(g).

Backup Withholding. Generally, a grantor trust is considered a payor of reportable payments received by the trust for purposes of backup withholding. If the trust has 10 or fewer grantors, a reportable payment made to the trust is treated as a reportable payment of the same kind made to the grantors on the date the trust received the payment. If the trust has more than 10 grantors, a reportable payment made to the trust is treated as a payment of the same kind made by the trust to each grantor in an

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amount equal to the distribution made to each grantor on the date the grantor is paid or credited. The trustee must withhold 31% of reportable payments made to any grantor who is subject to backup withholding. For more information, see I.R.C. §3406 and Temp. Treas. Reg. §35a.9999-2, Q&A 20.

2. Disclaimers

Introduction

If the requirements of I.R.C. §2518 are followed, a person can "disclaim" a gift or inheritance and be treated as though he or she had never received the gift or inheritance. This method is sometimes used as a post-death estate planning device.

I.R.C. §2518

Section 2518 sets forth the requirements that must be met for a disclaimer to be treated as a qualified disclaimer for federal gift or estate tax purposes.

- Section 2518(a) provides that, if a person makes a qualified disclaimer with respect to any interest in property, **then for purposes of the estate, gift, and generation-skipping transfer taxes**, the interest will be treated as if it had never been transferred to the disclaimant.
- **Instead**, the interest will be considered as passing directly from the decedent **to the person entitled to receive the property** as a result of the disclaimer.
- Section 2518(b) defines the term "qualified disclaimer" to mean an **irrevocable and unqualified refusal by a person to accept an interest in property but only if:**
 - (1) such refusal is in **writing**;
 - (2) such writing is received by the transferor of the interest, the transferor's legal representative, or the holder of the legal title to the property to which the interest relates **not later than the date that is nine months after the date on which the transfer creating the interest in such person is made**;
 - (3) such person has **not accepted the interest or any of its benefits**; and
 - (4) as a result of such refusal, the interest passes **without any direction on the part of the person making the disclaimer to either the spouse of the decedent or to a person other than the disclaimant**.
- **Treas. Reg. §25.2518-3(a)(1), on the gift tax regulations, provides that the disclaimer of all or an undivided portion of any separate interest in property may be a qualified disclaimer even if the disclaimant has another interest in the same property.**
- A **disclaimant** shall be treated as making a qualified disclaimer of a separate interest in property if the

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disclaimer relates to severable property and the disclaimant makes a disclaimer that would be a qualified disclaimer if such property were the only property in which the disclaimant had an interest.

- Severable property is property that can be divided into separate parts, each of which, after severance, maintains a complete and independent existence.
- **Treas. Reg. §25.2518-3(a)(2)** indicates that a disclaimer of both an income interest and a remainder interest in specific property in a trust may be a qualified disclaimer, if the disclaimer results in such property being removed from the trust and the property passes, without any direction on the part of the disclaimant, to persons other than the disclaimant or to the spouse of the decedent.
- **Under §25.2518-1(b)**, if a qualified disclaimer is made, the property is treated, for federal gift, estate, and generation-skipping transfer tax purposes, as passing directly from the transferor, not from the disclaimant, to the person entitled to receive the property as a result of the disclaimer. **Thus, the disclaimant is not treated as making a gift.**
- **Under §25.2518-2(c)(1)**, the written disclaimer must be delivered no later than the date that is nine months after the date on which the transfer creating the interest in the disclaimant is made.
- **Treas. Reg. §25.2518-2(c)(3)** provides that for the purposes of the time limitation on making a qualified disclaimer, the nine (9) month period for making a disclaimer with respect to a transfer made by a decedent is determined with reference to the date of the decedent's death.
- **Treas. Reg. §25.2518-2(d)(1)** provides that a disclaimant is **not considered to have accepted an interest in property merely because under applicable local law, legal title to the property vests immediately in the disclaimant upon the death of a decedent.**

Note: Consult an attorney to determine whether to use this provision for a particular client.

Practitioner Note.

Major changes in the estate and gift tax and the trust income and expense area were made by the TRA of 1997. See [pages 390–98](#) and [426–36](#) of this book.