
When Is It Time to Lay an Estate to Rest?

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Deciding when to close out an estate can be tricky, particularly when the business of an estate and its beneficiaries are tied closely together.

Depending on your perspective, federal regulations make it either more or less tricky. Specific regulations govern when an estate ceases to exist for tax purposes. Attorneys and accountants need to be aware of the rules – and make sure that administrators abide by them; failing to do otherwise can have significant impact on how beneficiaries are taxed.

ESTATE ADMINISTRATION – WHAT IT IS

The IRS code states that the tax existence of an estate is limited to the time needed to perform bona fide estate administration duties. For most estates, these include:

- ❖ Collecting estate taxes.
- ❖ Paying debts.
- ❖ Paying legacies.
- ❖ Settling claims against the estate.

Each of these activities is considered a legitimate duty of the estate administrator. The IRS requires that estate administrators show diligence, but recognizes that, in some cases, it may take an extended period to perform estate administration duties. The IRS also recognizes that there may be justifiable reasons for a delay in commencing administration.

ESTATE ADMINISTRATION: WHAT IT ISN'T

Estate administrators are often intimately connected with estate beneficiaries. As such, it often seems that some extended

duties are part of the administrator's role. The IRS, however, does not recognize them as such and expects that they will be carried out by successors to the estate's assets. These include, but may not be limited to:

- ❖ Investing the estate's assets.
- ❖ Supervising the estate's assets.
- ❖ Participating in business judgments as to assets.

In addition, while the IRS recognizes that it may take some time to complete bona fide estate administration duties, they are pretty strict about how extended time is calculated. The code states explicitly that it cannot take extended time to close out an estate as a result of “capricious and arbitrary” action – or of no action.

SURPRISINGLY IRRELEVANT

When trying to show that an estate is still active, professionals like attorneys and CPAs typically rely on a number of activities. Interestingly enough, the IRS does not recognize all of them as being



relevant to whether an estate still exists for tax purposes. These include:

- ❖ Instructions in the will directing the executor to carry on a certain activity for a period of time.
- ❖ Ongoing state court actions.
- ❖ Filing date of the estate's final accounting.
- ❖ Date of the decree dissolving the estate.

Again, as far as the IRS is concerned, the only real test is whether there are bona fide administration duties to be performed.

EXAMPLES

How do these rules work in real life? Let's look at some brief examples:

- ❖ An estate includes **fractional interests (as tenants in common) in 50 domestic and foreign jurisdictions**. Although the executor has attempted to quitclaim them, ancillary probate proceedings are required in all jurisdictions. This could take 10 years.

The estate continues to exist until these interests are settled without future liability to the estate.

- ❖ An estate's main assets are **stock in a closely held operating company and stock in a personal holding company** (whose assets consist of stock in the operating company). It will take 10 years to resolve the matter – including negotiations and litigation.

The estate continues to exist because substantial estate taxes will be due once the issues are settled.

- ❖ An estate includes the decedent's **partnership interest**. At the time of death, he was a limited partner, but had been general partner for many years. The IRS is examining the partnership's income tax returns.

The estate continues to exist until the IRS matter is fully resolved because it may

result in a large potential liability to the estate.

- ❖ An insurance broker's estate includes the right to receive **renewal commissions** for 10 years. All liabilities and taxes are settled and there is one beneficiary.

The estate ceases to exist once liabilities are settled. The right to the renewal commissions is fixed and determined.

- ❖ An estate has two adult beneficiaries. One is away on a **multi-year trip abroad** when the informal accounting is ready and the release needs to be signed.

The estate ceases to exist once the normal administrative duties have been completed; it may not be prolonged for the mere convenience of its beneficiaries.

- ❖ An estate includes **shares in an S corporation**. The executor decides to hold the stock for the 14 year period allowable under Section 6166 in order to qualify for installment payment of estate taxes.

The estate continues to exist as long as it is in compliance with Section 6166 since one of the ordinary duties of the executor is paying estate taxes.

- ❖ An estate is **liable under a lease** that still has 10 years to run. There is no cancellation on death clause and the executor is unable to find a sublessor for the premises.

The estate continues to exist so long as the total liability of the lease (monthly rent x 12 months x 10 years) is reasonably large compared to the size of the estate.

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THE BOTTOM LINE

While at first glance it may be confusing to decide when an estate ceases to exist, the law is actually quite clear. Attorneys and accountants must be diligent in ensuring that the rules are followed appropriately.

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