

Letters to the Editor

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Follow-Up to Article on Entity Elections for Trusts

To the Editor:

In my article, "Temporary Bliss: An Entity Election for Trusts" (*Tax Notes*, Dec. 15, 2003, p. 1304) the following appears on page 1308 as part of the discussion of the time for making the election when no executor has been appointed:

However, it appears that a trust could get caught out in the cold, because the filing date extensions granted to the trust itself will control. Thus, if the [qualified revocable trust] files for extensions based on the calendar year, the election must be made before those extensions lapse, even though the trust doesn't effectively choose its tax year until it files its first return.

It has been called to my attention that this statement lacked clarity, and it has been suggested that the trustee may be able to request and obtain extensions of time to file as an estate, based on a tax year other than the calendar year. In this letter I will expand on the perceived problem raised in the article and discuss authority that permits trustees to request and obtain extensions of time to file as an estate, based on a tax year other than the calendar year.

The Problem

Reg. section 1.645-(c)(2)(i) pegs the time for making the election when there is no executor. The election must be made "for the first taxable year of the trust, taking into account the trustee's election to treat the trust as an estate under section 645 . . . If an extension is granted for filing the Form 1041 for the first taxable year of the electing trust, the election form will be timely filed if it is filed by the time prescribed for filing the Form 1041 including the extension granted with respect to the filing of the Form 1041."

Let's further examine this provision in the context of the ability of an estate to select a noncalendar tax year, together with filing extensions, but assuming that there is no executor.

Example 1

Assume that a qualified revocable trust (QRT) of a decedent who died on February 1, 2003, wishes to select a tax year ending January 31. The trust's first income tax return, not taking into account the election under section 645, is due April 15, 2004. Assuming an extension of time to file of six months is granted by the IRS, the extended due date would be October 15, 2004.

The trust's first income tax return, taking into account the election under section 645, is due May 15, 2004. Assuming a six-month extension based on this later due date, the extended due date might be November 15, 2004.

The first part of the above-quoted regulation permits the QRT to file its first return with the section 645 election as late as May 15, 2004, since that would constitute a timely filed return "for the first taxable year of the trust, taking into account the trustee's election . . ." In that case, the trustee was not required to request any extension of time to file the return.

It is clear that the trustee could request one or more extensions of time to file based on a calendar tax year, but then choose a noncalendar tax year on the first return filed. In that case, the trustee could file the first return and make a valid section 645 election as late as October 15, 2004.

The question is: Can the QRT extend the due date of the income tax return, and therefore the due date of the section 645 election, to November 15, 2004? The answer to this question lies in whether the trustee has authority to request an extension as an estate at a point in time that precedes the point in time when a valid section 645 election has been made. Although the general approach of the statute and the regulation is to "relate back" the election all the way to the date of death, it might not be the case that a trustee is in possession of the necessary authority to take any action as if it were in the shoes of an estate until after the shoes are laced up and tied.

Therefore, the IRS could take the position that the QRT is not treated as an estate for income tax purposes with authority to act as such until such time as the section 645 election is actually made, and that only after the election is made can it relate back to the date of the decedent's death. If that position is correct, then up until the point in time when the election is made on a timely filed return, the trust has no authority to act as an estate in any capacity, including requesting an extension of time to file an income tax return, based on an income tax year other than the calendar year.

This could create a trap for the unwary. The QRT might have only until October 15, 2004, to file the section 645 election and elect the January 31 year-end. Worse yet, one wonders whether, if the trustee filed the request for extension of time to file as an estate at a point in time that precedes the making of a valid 645 election, any grant of an extension might be void for lack of authority.

Example 2

Assume that a qualified revocable trust (QRT) of a decedent who died on November 1, 2003, wishes to select a tax year ending October 31. The trust's first income tax return, not taking into account the election under section 645, is based on the calendar year and is therefore due April 15, 2004. Assuming the IRS grants a six-month extension of time to file, the extended due date would be October 15, 2004.

The trust's first income tax return, taking into account the election under section 645, reflecting a tax year ending October 31, is due February 15, 2005. Assuming a six-month extension based on this later due date could be obtained, the extended due date might be August 15, 2005.

The trustee can file an election under section 645 and adopt a tax year ending October 31, if the election is filed by February 15, 2005. The first tax year begins November 1, 2003, and ends October 31, 2004.

Again, the question arises whether the trustee can file for an extension as an estate and then, at some later time, but before the extended due date, file the section 645 election.

If the trustee obtains extensions to file based on the calendar year, then the trustee has only until August 15, 2004, to file the first income tax return as an estate under the section 645 election.

But October 31, 2004, the date that was intended to be the end of the first tax year, has not yet occurred as of August 15, 2004, the extended date obtained by the trustee. However, there is no need to file the election and the first return in this manner and there is no harm in this case since, as noted above, the trustee can file as an estate and make the election as late as February 15, 2005.

Authority Permitting Fiscal Year Extension

The term "executor" as defined for purposes of regulations section 645(b)(4) applies to that regulation only, and constitutes a restriction on the definition of that term otherwise applicable for purposes of the Internal Revenue Code.

When there is no executor or administrator appointed, qualified, and acting within the United States, section 7701(a)(43) defines the term "executor" to mean "any person in actual or constructive possession of any property of the decedent." This would include the trustee of a QRT.

The grant of extensions of time to file returns is governed not by section 645 and related regulations, but by section 6081 and related regulations. Therefore, the restriction on the definition found in regulations section 645(b)(4) does not apply in that context.

The instructions to Form 2758, the form used by estates to apply for an extension of time to file income tax return, states that the extension application form may be signed by "A fiduciary, trustee, executor, administrator, or an officer representing the fiduciary or trustee filing form 1041 for an estate."

Based on the above, a trustee of a QRT should be able to apply for an extension when the trust is filing as or on behalf of an estate, based on a tax year other than the fiscal year.

Conclusion

A safe course to follow would be to file by the due date taking into account the section 645 election, but without taking into account any extensions based on a tax year other than a calendar year. Nevertheless, there appears to be ample authority for the trustee of a QRT to request and obtain an extension of time to file as an estate under sections 6081 and 7701(a)(47). Therefore, it should be permissible for the trustee to request extensions of time to file based on a tax year other than a calendar year.

Sincerely,

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Relevant Code Sections

Section 645 -- Revocable Trust Election