

---

Folks:

**Quick-Take:** The use of multiple Trusts might be a good way for a donor to make lifetime gifts. However, the use of multiple Trusts might not work if the donor's goal is to avoid high federal income taxes if several Trusts are treated as one.

**Background:** As more individual begin to seriously think about the scheduled *sunset* date of their large applicable exemption amount, it is understandable that over the next 18 months that they will begin to look closely at making lifetime gifts to take advantage of their large applicable exemption amount while it is still available to be used. Those donors might also consider making gifts to irrevocable Trusts to protect the gifted assets from the beneficiary's creditor claims. Then again, when those donors are advised that an irrevocable Trust attains the highest marginal federal income tax bracket when the Trust's accumulated income is more than \$15,200 a year, they may be tempted to consider making gifts to several Trusts, for the same beneficiaries, just to avoid that high (37%) marginal federal income tax rate faced by the Trust. It is at this point that those donors need to be reminded of IRC 643(f).

**IRC 643(f):** This Tax Code section was added as part of the 2017 Tax Act. In part, it was added to avoid anticipated abuses of the newly added IRC 199A, which was the new additional federal income tax deduction that was created for closely held pass-through entities. [While IRC 199A is set to *sunset* in 2026, that is not the case with IRC 643(f)- it's a permanent change.] In essence, IRC 643(f) provides that two or more non-grantor Trusts will be treated by the IRS as a single Trust, but only if two conditions are met.

**IRC 643(f)(1):** The first condition provides that two or more Trusts will be treated as one Trust if such Trusts have substantially the same grantor or grantors and substantially the same primary beneficiaries; **and**

**IRC 643(f)(2):** The second condition is that the principal purpose of such Trusts is the avoidance of taxes that are imposed on the Trusts.

**Presumption:** If these two conditions are met, then there is a statutory, albeit rebuttable, presumption that the Trusts were created to avoid income taxes. [Regulation 1.643(f)-1(c).] The settlor bears the burden of proof to rebut this statutory presumption.

**Spouses:** For purposes of these conditions and the presumption, a **husband and wife will be treated as one person.**

**Principal Purpose:** The Regulations under IRC 643(f) define a *principal purpose* as: *A principal purpose for establishing or funding a trust is presumed if it results in a significant income tax benefit unless the significant non-tax (or non-income tax) purpose that could not be achieved without the creation of these separate trusts.* [Regulation 1.643(f)-1(b).]

**Observation:** While multiple Trusts might be created and funded to take advantage of the donor's currently large applicable exemption amount, the use of multiple Trusts as the donees of such lifetime gifts might not be sufficient to avoid the high 37% marginal federal income tax bracket if those multiple Trusts are treated by the IRS as a single Trust.

**Planning:** If lifetime gifts to Trusts are contemplated by a donor, then it will be important to not have substantially the same trust beneficiaries for each Trust. A Trust for each of the donor's children would suffice to overcome the statutory presumption. It would be even better if the multiple Trusts had different distribution provisions, e.g., withdrawal rights in one, but not the other; a lifetime limited power of appointment held by the current beneficiary of one Trust, but not the other; different independent trustees of each Trust with different distribution provisions for each Trust. It would also be helpful if the settlor expressly identified in each Trust, its non-tax purpose, such as: *"I intend that this Trust is to protect its assets from my child's creditors"*, or *"I*

*intend that this Trust is to hold for an extended period the closely-held business interests of our family that are transferred to it.”*

**Conclusion:** As lifetime gifts take ‘front stage center’ over the next 18 months for many wealthy individuals who have been watching what Congress does with the tax laws, it will be important to remind them of the provisions of IRC 643(f) and its presumption of tax avoidance, which is intended to expose the Trust(s) to the highest marginal federal income tax bracket. Mirror image Trusts is something to be avoided if IRC 643(f) is to be avoided.