

Fiduciary Income Tax Update: Unbundling Delayed For 2008

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The Internal Revenue Service has extended the delay of the unbundling requirements under proposed regulations for all returns for years prior to 2009. IRS Notice 2008-116 (December 11, 2008).

Background

Section 67(a) of the Internal Revenue Code reduces the deduction for miscellaneous itemized expenses by 2% ("the 2-percent floor"). The Internal Revenue Service and Treasury proposed regulations to implement the application of the 2-percent floor to nongrantor trusts and estates on July 27, 2007. Those proposed regulations have not been finalized, but, as written, would require the unbundling of so called "bundled fees." A "bundled fee" is a fee "for costs incurred in-house by a fiduciary, some of which are subject to the 2-percent floor and some of which are fully deductible without regard to the 2-percent floor." In IRS Notice 2008-32, 2008-11 IRB 593, the IRS advised that the unbundling requirement would not apply to any year prior to 2008.

Notice 2008-116

Notice 2008-116 holds that "Taxpayers will not be required to determine the portion of a Bundled Fiduciary Fee that is subject to the 2-percent floor under § 67 for any taxable year beginning before January 1, 2009. Instead, for each such taxable year, taxpayers may deduct the full amount of the Bundled Fiduciary Fee without regard to the 2-percent floor." The Notice warns, however, that "[p]ayments by the fiduciary to third parties for expenses subject to the 2-percent floor are readily identifiable and must be treated separately from the otherwise Bundled Fiduciary Fee."

United States Supreme Court

The Supreme Court of the United States had decided *Knight v. Commissioner*, 552 U.S. ___, 128 S. Ct. 782, 101 AFTR 2d 2008-544 (2008) on January 16, 2008 holding that costs paid to an investment advisor by a nongrantor trust or estate generally are subject to the 2-percent floor for miscellaneous itemized deductions under § 67(a).