

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:DOM:IT&A:1-PLR-112803-99

Date:

November 12, 1999

Legend:

Taxpayer =

Decedent =

Trust =

Corporation =

State =

Date 1 =

Date 2 =

Date 3 =

Dear .:

This letter responds to your submission of July 22, 1999, and supplemental correspondence, dated November 3, 1999, in which you requested a ruling on behalf of Taxpayer. Specifically, you have requested a ruling that Decedent's interests in certain stock and real estate assets qualify as interests in a closely held business for purposes of section 6166 of the Internal Revenue Code (Code). For the reasons below, we conclude that these assets are interests in a single closely held business for purposes of section 6166 of the Code.

FACTS

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At the time of his death, Decedent (a United States citizen and a resident of State) indirectly owned through Trust 100% of stock in Corporation and 100% of certain real estate assets, which was comprised of land and a building. Decedent is the sole beneficiary of Trust, a grantor trust for federal tax purposes.

On Date 1, Decedent purchased land. Shortly thereafter, Decedent constructed a building on the land. On Date 2, Decedent formed Corporation, a wholesale supplier of automotive parts and related supplies, in State. Corporation used the building owned by Decedent to house the Corporation's automotive parts and supplies, and it used the remaining land for parking. On Date 3, Decedent transferred the land and building, as well as 100% of all the stock in Corporation, to Trust.

Decedent was the President and Chief Operating Officer of Corporation until the time of his death and was actively involved in the day-to-day operations of Corporation. Decedent made all decisions regarding the business, including expansion of customer base, marketing and inventory. Corporation employed a General Manager, a Warehouse Manager, and eight other employees. Decedent supervised all employees of Corporation and directed all of their activities.

The land, building, and stock of Corporation are includable in Decedent's adjusted gross estate. Decedent's interest in Corporation, together with his interest in the real estate assets, exceeds 35% of his adjusted gross estate.

LAW

Section 6166(a)(1) of the Code provides in part that if the value of an interest in a closely held business, which is included in determining the gross estate of a decedent who was (at the date of his death) a citizen or resident of the United States, exceeds 35 percent of the adjusted gross estate, the executor may elect to pay part or all of the tax imposed by section 2001 in two or more (but not exceeding ten) equal installments. If such an election is made, the first installment shall be paid on or before the date selected by the executor which is not more than five years after the date prescribed by section 6151(a) for payment of the tax.

Section 6166(b)(1) of the Code defines the term "interest in a closely held business" to include:

- (A) an interest as a proprietor in a trade or business carried on as a proprietorship
- (B) an interest as a partner in a partnership carrying on a trade or business, if
 - (i) 20 percent or more of the total capital interest in such partnership is included in determining the gross estate of the decedent, or
 - (ii) such a partnership had 15 or fewer partners; or

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- (C) stock in a corporation carrying on a trade or business if (i) 20 percent of more in value of the voting stock of such corporation is included in determining the gross estate of the decedent, or (ii) such corporation had 15 or fewer shareholders.

Section 6166(b)(2)(A) of the Code provides that the determination under section 6166(b)(1) shall be made as of the time immediately before the decedent's death.

Section 6166(b)(2)(C) of the Code provides, in part, that property owned directly or indirectly, by or for a trust, shall be considered as being owned proportionately by or for its beneficiaries. For purposes of this section, a person shall be treated as a beneficiary of a trust only if such person has a present interest in the trust.

Section 6166(b)(9) of the Code provides, in part, that for the purposes of section 6166(a)(1) and in determining the closely held business amount (but not for the purpose of section 6166(g)), the value of any interest in a closely held business shall not include the value of that portion of such interest which is attributable to passive assets held by the business. In general, the term "passive asset" means any asset other than an asset used in carrying on a trade or business.

Section 20.6166A-2(c)(2) of the Estate Tax Regulations provides that, in the case of a trade or business carried on as a proprietorship, the interest in the closely held business includes only those assets of the decedent that were actually utilized by him in the trade or business. Whether an asset is used in the trade or business will depend on the facts and circumstances of the particular case.

Rev. Rul. 75-366, 1975-2 C.B. 472, holds that where a decedent paid 40 percent of the expenses, received 40 percent of the crops, and actively participated in the important management decisions of a tenant farm included in the decedent's estate, the farm constitutes an interest in a closely held business under section 6166. Under these facts, the decedent made almost daily visits to inspect and discuss operations and occasionally delivered supplies to the tenants.

Rev. Rul. 75-367, 1975-2 C.B. 472, holds that land owned by a decedent that was held for the purpose of building homes, decedent's ownership of stock in a corporation that built homes on such land, and a business office and warehouse owned by the decedent and used by both the corporation and decedent, qualify as an interest in a closely held business under section 6166. However, eight homes built by the decedent's corporation that were sold and later repurchased by the decedent, who collected the rents, made the mortgage payments and made the necessary repairs and maintenance to the homes in order to maintain the condition and appearance of the rental homes, were not an interest in a closely held business because the decedent's relationship to the properties was merely that of an owner managing investment assets to obtain the rents ordinarily expected from them.

ANALYSIS

According to Rev. Ruls. 75-366 and 75-367, the determination of what constitutes a “trade or business” within the meaning of section 6166 should not be made merely by reference to a broad definition of the term for purposes of some other section of the Code, but should reflect the intent of Congress in enacting section 6166. Section 6166 was enacted to permit the deferral of the payment of federal estate tax when, in order to pay the tax in one payment, it would be necessary to sell assets used in an ongoing business and, thereby, disrupt or destroy the business. This section was intended to allow tax payments to be deferred on income earned from an active business rather than income earned solely from the passive ownership of property. Section 6166 was intended to apply only to a business such as a manufacturing, mercantile, or service enterprise, as distinguished from management of investment assets.

Corporation

Corporation is engaged in the business of selling wholesale automotive parts and related supplies. In addition to Decedent, Corporation employed eight full-time employees. Because 100% of Corporation’s stock is included in determining Decedent’s gross estate, Decedent’s interest in Corporation is an interest in a closely held business under section 6166.

Real Estate Assets

In order for the land and building to qualify for the tax treatment available under section 6166 of the Code, the property must be (1) owned by the Decedent, and (2) actually used in a trade or business in which the Decedent is an active participant. The facts show that the Decedent owned the land and building up to the time of his death. Additionally, the land and building were clearly essential to Decedent’s automotive supply business because they were used by Decedent in the operation of his business. The land and building represented approximately 44% of the value of the automotive parts business. The fact that the land and building were owned by the Decedent and not the Corporation does not diminish the real estate’s essentialness to the overall operation of the automotive supply business.

In this case, the land and the building were held for the benefit of the overall operation and management of Decedent’s wholesale automotive supply business. The Decedent operated his business through Corporation and as a sole proprietor. Although the core of the business was the Corporation, the individually owned land and building constituted a fundamental part of the overall operation of the wholesale automotive supply business. Thus, the Decedent was carrying on his wholesale automotive supply business as a corporation and as a proprietor in a proprietorship.

CONCLUSION

Based on the information provided and the representations made, we conclude that Decedent's interests in Corporation and in the real estate assets are interests in a single closely held business for purposes of section 6166 of the Code. Accordingly, provided the other requirements of section 6166 of the Code are met, the federal estate tax attributable to Decedent's interest in the closely held business may be paid in installments under section 6166.

Except as specifically ruled above, no opinion is expressed as to the federal tax treatment of any issue addressed in this ruling under other provisions of the Internal Revenue Code and Regulations that may be applicable.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to Taxpayer. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant.

Pursuant to the power of attorney on file in this office, the original of this letter is being sent to the Taxpayer's authorized representative.

Sincerely,
PAMELA W. FULLER
Assistant to the Branch Chief, Branch 1
Office of Assistant Chief Counsel
(Income Tax and Accounting)

Enclosures (2):

Copy of this letter
Copy for section 6110 purposes