

This letter is in response to a letter from your attorney dated Date 1, requesting several rulings under section 6166 of the Internal Revenue Code. The facts as submitted reflect that Decedent died on Date 2. At the time of death, the Trust, a revocable grantor trust, held Shares (Percentage) of the Company 1, a closely held corporation organized in State. Company 1 is currently comprised of six operating units: Operating Unit 1; the Operating Unit 2; Operating Unit 3; Operating Unit 4; Operating Unit 5; and Operating Unit 6. The operations of the business units are reported on a consolidated corporate income tax return.

Rulings requested:

1. The marketing activities of the Operating Unit 2 are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1).
2. The activities of Operating Unit 3 are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1).
3. The activities of the Operating Unit 5 are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1).
4. The activities of Operating Unit 6 are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1).

Relevant Authorities:

Under section 6166(a)(1), if the value of an interest in a closely held business that is included in determining the gross estate of a decedent exceeds 35 percent of the adjusted gross estate, the estate may elect to pay all or part of the tax imposed by section 2001 (the estate tax liability) in two or more (but not exceeding ten) equal installments. Under section 6166(a)(2), the maximum amount of tax that may be deferred is the percentage of estate tax equal to the percentage of the adjusted gross estate that is comprised of the closely held business amount. Under section 6166(a)(3), if the estate makes an election under section 6166(a)(1), the estate has up to five years from the due date prescribed by section 6151(a) to make the first installment payment.

Pursuant to IRC 6166(b)(1) an “interest in a closely held business” is defined, in relevant part, as: stock in a corporation carrying on a trade or business if 20% or more of the value of voting stock of the corporation is included in the gross estate, or the corporation has 45 or fewer shareholders.

Revenue Ruling 2006-34 contains a non-exclusive list of factors that are relevant in determining whether real property interests are interests in a closely held business for purposes of section 6166: the amount of time the corporation's employees devoted to the trade or business; whether an office was maintained from which the activities of the corporation were conducted and whether the corporation maintained regular business hours for that purpose; the extent to which the corporation's employees were actively involved in finding new tenants and negotiating and executing leases; the extent to which the corporation's employees provided services beyond the mere furnishing of leased premises; the extent to which the corporation's employees personally arranged for, performed, or supervised repairs and the maintenance of property (whether or not performed by independent contractors); and the extent to which the corporation's employees handled tenant repair requests and complaints. Although Revenue Ruling 2006-34 addresses interests in real estate, the factors in the revenue ruling are helpful in evaluating whether other interests are those of an active trade or business.

Discussion:

Ruling request 1

The Date 1, letter requests a ruling that the marketing activities of the Operating Unit 2, a division of Operating Unit 1, are sufficient to constitute the "carrying on of a trade or business" such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1). According to the facts provided, Operating Unit 2 is responsible for providing remarketing, management and support services regarding equipment owned by Operating Unit 1 and Division 1 (a division of Operating Unit 1), and equipment owned by outside lessors. Operating Unit 2 has Number 1 full-time-equivalent employees that are involved in management, support, remarketing, sale and re-lease of the equipment. Operating Unit 2 has Number 2 locations and Number 3 off-site warehouse maintained where activities are conducted. Most lessees and customers are secured through direct activities of Operating Unit 2, and the repair of equipment is either arranged for, performed by, or supervised by an employee of Operating Unit 2.

Although Revenue Ruling 2006-34 addresses interests in real estate, not in the management of personal property, the factors in the revenue ruling are helpful in evaluating whether the employees of Operating Unit 2 are engaged in a trade or business. Operating Unit 2 maintains several offices and a warehouse from which the employees conduct business. The employees of Operating Unit 2: negotiate new leases and monitor current leases; market and sell, or re-lease, used equipment; and, store and maintain equipment for sale or re-lease. Accordingly, the activities of Operating Unit 2 constitute an active trade or business for purposes of section 6166.¹

¹ This ruling does not address whether decedent's interest in Operating Unit 2 qualifies as an interest in a closely-held business for purposes of section 6166(a)(1).

Ruling request 2

The Date 2, letter requests a ruling that the activities of the Operating Unit 3 a division of the Company 1, are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1). The facts provide that employees of Operating Unit 3 are involved in day-to-day operations, management, and maintenance of commercial class properties. Operating Unit 3 has Number 4 full-time-equivalent employees that work out of company offices in City, State. The employees of Operating Unit 3: find new tenants; negotiate and execute leases; arrange for, perform, and supervise property repairs and maintenance; and, handle tenant repair and maintenance requests, and complaints. Additionally, the employees hire and supervise independent contractors for substantial repairs and capital improvements, and services such as snow removal, landscaping, security, janitorial, and cafeteria services.

Applying the factors discussed in Revenue Ruling 2006-34, Operating Unit 3 has a significant number of full-time employees that are involved in the day-to-day operations, management, and maintenance of real estate. Therefore, the activities of Operating Unit 3 constitute the carrying on of a trade or business for purposes of section 6166.²

Ruling request 3

The Date 1, letter requests a ruling that the activities of Operating Unit 5, which operates under a holding company, the sole member of which is Company 1, are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1). The facts given provide that the Operating Unit 5 has Number 5 full-time equivalent non-owner employees overseeing all facets of construction and supervising operations of Company 2, an independent property management firm.

Applying Revenue Ruling 2006-34 to this situation, it appears that Company 2 is acting as an independent contractor of Operating Unit 5. The use of independent contractors to perform work does not prevent the business activities from rising to the level of the conduct of an active trade or business provided that the third-party activities do not reduce the activities of the corporation to merely holding investment property. From the facts provided, Operating Unit 5 involves non-owner employees of Company 1 actively overseeing construction of the subject properties and actively supervising the actions of Company 2. Therefore the activities of Operating Unit 5 constitute the carrying on of a trade or business for purposes of section 6166.³

² This ruling does not address whether decedent’s interest in the Operating Unit 3 qualifies as an interest in a closely-held business for purposes of section 6166(a)(1).

³ This ruling does not address whether decedent’s interest in the Operating Unit 5 unit qualifies as an interest in a closely-held business for purposes of section 6166(a)(1).

Ruling request 4

The Date 1, letter requests a ruling that the activities of Operating Unit 6 the sole member of which is Company 1, are sufficient to constitute the “carrying on of a trade or business” such that an interest therein will qualify as an interest in a closely-held business for purposes of section 6166(a)(1).

The facts presented provide that Operating Unit 6 relies on Company 3, their hotel management company, to operate and manage the subject hotel and restaurant. Operating Unit 6 has no ownership interest in Company 3. However, the facts provide that even though Company 3 operates, maintains, services, and improves the hotel, employees of Operating Unit 6 are involved in a daily basis in all aspects of the management and food service of the hotel.

Applying Revenue Ruling 2006-34 to this situation, it appears that Company 3 is acting as an independent contractor of Operating Unit 6. The use of independent contractors to perform work does not prevent the business activities from rising to the level of the conduct of an active trade or business provided that the third-party activities do not reduce the activities of the corporation to merely holding investment property. Even though Company 3 is involved in the management of the hotel, Operating Unit 6 is not merely holding an investment property. Therefore, the activities of Operating Unit 6 constitute the carrying on of a trade or business for purposes of section 6166.⁴

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

⁴ This ruling does not address whether decedent’s interest in Operating Unit 6 qualifies as an interest in a closely-held business for purposes of section 6166(a)(1).

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.

Sincerely,

Francis M. McCormick
Senior Technician Reviewer
(Procedure & Administration)