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FEDERAL ESTATE INCOME TAX MATTERS

The most overlooked part of your job as a fiduciary is that the U.S. Government has a “general tax lien” on all estate and/or trust property owned by the decedent at his/her death. To address this lien you must collect all estate and/or trust assets and liabilities so that they can be accounted for. In addition, Section §6012(b) of the IRS Code holds a Fiduciary responsible for filing the decedent's final income and estate tax returns. Once the assets and liabilities are accumulated you, as the fiduciary for the estate/trust, should obtain copies of all Federal Income and Gift Tax Returns filed by the decedent over the past seven (7) years). Analysis of this information will make you aware of potential prior year income and/or gift tax issues that require immediate attention. Once you have gathered all of the financial information (assets, liabilities and tax returns) we can discuss how to proceed forward.

Step 1:

In order to address this potential issue and work with the IRS we will need to file a “Notice Concerning Fiduciary Relationship” (IRS Form 56). This notifies the IRS of the fact that you are serving as the representative for the estate/trust. We can then file IRS Form 4506, Request for Copy or Transcript of Tax Form, with the IRS. The response received from the IRS will you, as the Fiduciary, as to which, if any, tax returns (income, gift, etc.) were filed by the decedent prior to his or her death. The request will need to include the Letters of Administration, if applicable, and a Power of Attorney (IRS Form 2848).

Step 2:

Once we have received the requested tax information, the next step will be to file IRS Form 4810, Request for Prompt Assessment. This document requests a prompt assessment and review of all tax returns filed by the decedent with the IRS. The Form 4810 must detail the following: (i) type of tax; (ii) tax periods covered; (iii) name, social security or EIN on each return; (iv) date the returns were filed; and (v) letters of administration or comparable authority to act on behalf of the estate or trust. Filing Form 4810 will shorten the statute of limitations period for the tax return from three years from the date of filing or due date of the return to eighteen (18) months from the date of its filing with the IRS. It is important to note that the shortened statute of limitations period will not apply to: (i) fraudulent tax returns; (ii) unfiled tax returns (*IRC §6501(c)*); (iii) any tax return with “substantial omissions” (*IRC §6501(e)*); or (iv) any tax assessment described in *IRC §6501(c)*.

Step 3:

Once the decedent’s federal income tax return(s) has been filed with the IRS you, as the Fiduciary, may file a written application requesting release from personal liability for income and gift

taxes. The IRS will then be limited to nine (9) months (the “notification period”) to notify you of any tax due. Under IRC §6905, upon expiration of the notification period, you will be discharged from personal liability for any tax deficiency thereafter found to be due and owing. The application should be filed with the IRS officer with whom the estate tax return was filed (or, if no estate tax return was required, to the IRS office where the decedent’s final income tax return was filed).

LIABILITY:

If the above steps are not utilized, it is IMPORTANT to understand that under IRC §3713, you, as the Fiduciary, will be held personally liable for a federal tax liability under the following conditions: (i) the U.S. Government must have a claim for taxes; (ii) the Fiduciary must have: (a) knowledge of the government’s claim or be placed on inquiry notice of the claim, and (b) paid a “debt” of the decedent or distributed assets to a beneficiary; (iii) the “debt” or distribution must have been paid at a time when the estate or trust was insolvent or the distribution created the insolvency; and (iv) the IRS must have filed a timely assessment against the fiduciary personally. “The knowledge requirement ... may be satisfied by either actual knowledge of the liability or notice of such facts as would put a reasonably prudent person on inquiry as to the existence of the unpaid claim of the United States.”

A Fiduciary who fails to abide by this requirement will subject themselves to personally liability for the amount of the unpaid tax deficiency (*31 U.S.C. §3713(b)*). When there are insufficient estate or trust assets to pay a federal tax obligation, as a result of the Fiduciary’s actions, the IRS may collect the tax obligation directly from the Fiduciary without regard to transferee liability.

OTHER ISSUES - INSUFFICIENT ESTATE ASSETS:

On occasion a Fiduciary may be placed into a position where assets passing outside the probate estate (life insurance, jointly held property, retirement accounts, and pension plans) or trust, over which they have no control, constitute a substantial portion of the assets (real property, stocks, cash, etc.) subject to estate taxation. Without the ability to direct or assume control of the assets you, as the Fiduciary, may have both a liquidity problem and lack of means to satisfy the estates tax (income or estate) obligation. For this reason alone, a Fiduciary should be very reluctant to distribute any funds to a beneficiary before all statute of limitation periods expire for the Internal Revenue Service (“IRS”) to assess a tax deficiency.

FLORIDA PROBATE LAW

Under Florida law, a claim for federal taxes (income, estate or gift) will not be subject to F.S. §733.702, §733.710 or the requirement that a creditor claim be filed in probate proceedings. The federal tax obligation will then receive preference over all other claims against and obligations (state inheritance taxes, and other expenses) of an estate. As a result, even if the IRS fails to file a claim against an estate, the Fiduciary must actively assert the U.S. Government’s priority under IRC §3713.

Florida Statutes:

Florida Statutes §733.801 and §733.802 may be utilized to protect a Fiduciary by limiting the circumstances under which they will be required to either pay or deliver a devise or distributive share to a beneficiary. The limitations include: (i) not earlier than five (5) months after the granting of letters of administration; and (ii) compelled, prior to final distribution, to pay a devise in money, deliver specific personal property, unless the personal property is exempt personal property. Even then, unless the beneficiary establishes that the assets will not be required for the payment of estate and inheritance tax, a claim (debts, elective share, expenses of administration, etc.), provide funds for contribution, or to enforce equalization in case of advancements. If the administration of the estate is not completed before the entry of an order of partial distribution (devise, family allowance, or elective share) a court may require the beneficiary to post a bond with sureties and require them to make contribution, plus interest, if it is later determined that there are insufficient assets.

Homestead Property:

Federal tax law, except as provided under IRC §6334, Property Exempt from Levy, will preempt Florida's exempt property statutes and constitutional homestead protection laws. The preemption will allow the IRS to impose a federal tax lien or levy on personal assets of an estate or trust for collection.