

Fiduciary Income Tax Returns and Decedent's Final Income Tax Returns

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Income Tax Returns Required:

- Form 1040, U.S. Individual Income Tax *
- Form PA-40, PA Individual Income Tax *
- * Due April 15

- Form 1041, U.S. Estate & Trust Income Tax**
- Form PA-41, PA Fiduciary Income Tax**
- ** Due 15th Day of 4th Month After End of Fiscal Year

2010 Federal Income Tax Rates for Married Individuals Filing Jointly or as Surviving Spouse

Taxable Income	Tax Rate
– \$0 to \$16,750	- 10%
– \$16,750- \$68,000	- 15%
– \$68,000 to \$137,300	- 25%
– \$137,300 to \$209,250	- 28%
– \$209,250 to \$373,650	- 33%
– \$373,650 and up	- 35%

2010 Federal Income Tax Rates for Trusts and Estates

Taxable Income	Tax Rate
– \$0 to \$2,300	- 15%
– \$2,300 to \$5,350	- 25%
– \$5,350 to \$8,200	- 28%
– \$8,200 to \$11,200	- 33%
– \$11,200 and up	- 35%

Fiduciary Income Tax

Filing Exemptions (Standard Deductions)

- \$600 for Estate (None in Final Year)
- \$300 for Simple Trust (Reqd. to Dist. All Income Annually)
- \$100 for Complex Trust

Initial Income Tax Responsibilities of Executors/Counsel

- Obtain Estate EIN
- File Form 56
- Select Fiscal Year for Estate

Some Additional Income Tax Tasks

- Extend Form 1040 (6 month extension to October 15)
- Review Spouse's Quarterly Form 1040-ES
- Extend Form 709
- Liquidate Tax-Exempt Bonds (if advisable)

Decedent's Final Income Tax

- Death Ends Decedent's Tax Year
- Medical Expenses can be Deducted on Final Form 1040 or on Form 706
- Accrue U.S. Savings Bond Interest

Decedent's Final Income Tax

- No Estimated Taxes Required Post-Mortem for Decedent (contra for surviving spouse)
- Pro-Rate Income Between Decedent and Estate
- Consider Filing Separate Returns to Create Debt of Decedent

Decedent's Final Income Tax

- Before Filing Joint Return With Spouse
Consider Risks/Benefits

- Decedent's Final Income Tax Liability Can Be
Deducted on Both Form 706 and PA Inheritance
Tax Return as a Debts of Decedent

Grantor Trusts

- Grantor retains power to revoke trust or to significantly control its assets/beneficiaries
- A Grantor Trust is ignored for income tax purposes; Income/gain is reported directly on grantor's Form 1040
- Form 1041 may not be required

Section 1014 Basis Rules

Income Tax Basis of Inherited Property

- Date of Death Value Becomes New Basis
- Appreciated Assets are “Stepped-Up”
- Asset Must Be Included in Decedent’s Gross Estate
- Decedent’s Unrealized Losses Disappear

Section 1014 Basis Rules

Income Tax Basis of Inherited Property

- Alternate Valuation Applies (if used)
- All Gain/Loss is Long Term for Assets Received From a Decedent
- No Basis Increase for IRD Items

Fiduciary Income Tax Concepts

- Conduit Theory
- DNI – Distributable Net Income
- Income Flows Out to Beneficiaries on Last Day of Estate's Fiscal Year per Sch K-1
- Gains Can Be Taxed Either to Estate or Benefs.

Fiduciary Income Tax Rules

- Choice of Fiscal year- Estates Only
- 65 Day Rule for Both Estates and Trusts
- Estimated Tax Payments Req'd. After 2 Years
- Income Tax Deductions are Narrower than Form 706 Deductions

More Fiduciary Income Tax Rules

- Election to File Combined Form 1041 for Estate and Decedent's Revocable Trust (Form 8855)
- Tax-Exempt Income Reduces Income Tax Deductions
- Taxable Income May Differ From Fiduciary Accounting Income (Trapping Distribution)

Some Additional Fiduciary Income Tax Concepts

- IRD is Always Taxed to the Recipient
- Charitable Deduction/ Set-Aside
- Separate Share Election
- “Throwback” Rules

Deduction of Administration Expenses

- Deductible on Form 706 or Form 1041, but Not Both
- Also Deductible on PA Inheritance Tax Return
- Avoid Creating Losses Except in Final Year
- 2% AGI Reduction for Certain Investment-Advisory and Similar Expenses (Rudkin)

Tax Issues When Satisfying Legacies/Distributions

- Pre-Residuary Legacies, Specific Bequests and Devises Usually Do Not Trigger DNI
- No Gain/Loss Recognized on In-Kind Distributions from Residue
- Gain/Loss Recognized on In-Kind Satisfaction/Distribution for Pecuniary Bequests

Tax Issues Upon Termination of Estate/Trust

- Excess Deductions on Termination Pass to Residuary Beneficiaries, Pro-Rata
- Capital Gains are Taxable Either to Estate/ Trust or Residuary Beneficiaries
- Capital Losses Pass to Residuary Beneficiaries Upon Termination (Indefinite Loss Carry Forward)

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