



## Private Letter Rulings

*“Private letter rulings” are written statements issued to a taxpayer by the department, that interpret Wisconsin tax laws based on the taxpayer’s specific set of facts. Any taxpayer may rely upon the ruling to the extent the facts are the same as those in the ruling.*

*The ruling number is interpreted as follows: The “W” is for “Wisconsin”; the first four digits are the year and week the ruling becomes available for publication (80 days after it is issued to the taxpayer); the last three digits are the number in the series of rulings issued that year. The date is the date the ruling was issued.*

*Certain information that could identify the taxpayer has been deleted. Additional information is available in Wisconsin Publication 111, “How to Get a Private Letter Ruling From the Wisconsin Department of Revenue.”*

The following private letter ruling is included:

### Fiduciary Income Tax

Trusts - situs and resident status; Trusts - taxation generally; Trusts - taxation if ESBT or QSST elections are made

W 0315002 (p. 28)

✱ W 0315002 ✱

**January 17, 2003**

**Type Tax:** Fiduciary Income Tax

**Issue:** Trusts - situs and resident status; Trusts - taxation generally; Trusts - taxation if ESBT or QSST elections are made

**Statutes:** Sections 71.04(1)(a),(b)1 and (b)2, 71.04(4), 71.125(2), and 71.25(2), Wis. Stats. (1999-00)

This letter responds to your request for a private letter ruling, regarding the resident status of certain enumerated trusts and the Wisconsin tax treatment of the trusts and the beneficiaries under qualified subchapter S trust (“QSST”) and electing small business trust (“ESBT”) elections. Appendix I provides the names and addresses of the Co-Trustees of the trusts and the beneficiaries of these trusts.

### Facts as stated in your request:

The thirteen trusts are separate testamentary trusts and were created under the will of Decedent D, a decedent from a state other than Wisconsin (the “decedent”). The will is being probated in the other state. There also is an ancillary administration in Wisconsin. A copy of the decedent’s will was attached as Appendix II.

Each trust has a single beneficiary during the trust’s term, and each of the beneficiaries is the grandchild of the decedent. Appendix I lists each trust and the sole current beneficiary of each trust. All but one of the trusts terminates 20 years after the death of the decedent and is payable outright to the grandchild/beneficiary. One trust is to exist for the entire life of the beneficiary of that trust. The beneficiary of each trust has a general testamentary power of appointment over the trust for his or her benefit.

Appendix I breaks the trusts into two categories: trusts with beneficiaries who currently are Wisconsin residents (each such trust and respective beneficiary is hereinafter referred to as “Trust A” and “Beneficiary A”); and trusts with beneficiaries who currently are not Wisconsin residents (each such trust and respective beneficiary is hereinafter referred to as “Trust B” and “Beneficiary B”).

The trusts all have the same four Co-Trustees. The Co-Trustees are individuals. Three Co-Trustees presently reside in Wisconsin, and one of the Co-trustees resides in the other state. There is no requirement that the Co-Trustees reside in Wisconsin or the other state.

The trusts are not subject to Wisconsin jurisdiction. They are not required to file any annual trust reports with the Wisconsin probate court.

The trusts are cash method taxpayers and operate on a calendar year.

The decedent owned an interest in Corporation XYZ, a Wisconsin S corporation (the “Company”). The Company has income from both Wisconsin and non-Wisconsin sources and apportions its income. Pursuant to the decedent’s will, the decedent’s interest in the Company, as well as the balance of the decedent’s residuary estate, will be distributed to the trusts.

The trusts qualify under Federal law for both a Qualified Subchapter S trust (QSST) election and an Electing Small Business Trust (ESBT) election. The Co-Trustees and the beneficiaries are deciding whether to make a QSST or ESBT election with respect to the trusts.

**Request:** The Co-Trustees request the following rulings:

1. The trusts are not Wisconsin residents.
2. As to the portion of the trusts that do not hold the Company stock, secs. 71.04(4) and 71.04(1)(b)1, Wis. Stats., shall apply.
3. If an ESBT election is made with respect to one of the trusts, then, as to the ESBT portion of that trust:
  - a. Pursuant to sec. 71.04(4), Wis. Stats., the trust only will be taxed by Wisconsin on the trust's income that is derived from business transacted and property located within Wisconsin, which in this case, would be the trust's share of Company income apportioned to Wisconsin.
  - b. Beneficiary A and Beneficiary B will have no Wisconsin income with respect to distributions from the ESBT portion of the beneficiary's respective trusts.
4. If the QSST election is made with respect to one of the trusts, then, as to the QSST portion of that trust:
  - a. The trust will be disregarded for Wisconsin income tax purposes.
  - b. The trust's share of Company income will be taxed to the beneficiary according to the beneficiary's resident status (i.e., as if the beneficiary owned directly the Company stock owned by the beneficiary's respective trust). Thus, Beneficiary A, a Wisconsin resident, would report S Corporation income from all sources, and Beneficiary B, a non-Wisconsin resident, would report S corporation income from Wisconsin sources only.

**Ruling:**

1. Yes, the trusts are not Wisconsin residents.
2. Yes, for the portion of the trusts that do not hold the Company stock, secs. 71.04(4) and 71.04(1)(b)1, Wis. Stats., shall apply.

3. Yes, if an ESBT election is made with respect to one of the trusts, then, as to the ESBT portion of that trust:
  - a. Pursuant to sec. 71.04(4), Wis. Stats., the trust only will be taxed by Wisconsin on the trust's income that is derived from business transacted and property located within Wisconsin, which in this case, would be the trust's share of Company income apportioned to Wisconsin.
  - b. Beneficiary A and Beneficiary B will have no Wisconsin income with respect to distributions from the ESBT portion of the beneficiary's respective trusts.
4. Yes, If the QSST election is made with respect to one of the trusts, then, as to the QSST portion of that trust:
  - a. The trust will be disregarded for Wisconsin income tax purposes.
  - b. The trust's share of Company income will be taxed to the beneficiary according to the beneficiary's resident status (i.e., as if the beneficiary owned directly the Company stock owned by the beneficiary's respective trust). Thus, Beneficiary A, a Wisconsin resident, would report S Corporation income from all sources, and Beneficiary B, a non-Wisconsin resident, would report S corporation income from Wisconsin sources only.

**Applicable Law:**

Section 71.04(1)(a), Wis. Stats. (1999-00), provides in pertinent part:

All income or loss of resident individuals and resident estates and trusts shall follow the residence of the individual, estate or trust.

Section 71.04(1)(b)1, Wis. Stats. (1999-00), provides:

The situs of income derived by any taxpayer as the beneficiary of the estate of a decedent or of a trust estate shall be determined as if such income had been received without the intervention of a fiduciary.

Section 71.04(1)(b)2, Wis. Stats. (1999-00), provides:

The situs of income received by a trustee, which income, under the internal revenue code, is taxable to the grantor of the trust or any person other than the

trust, shall be determined as if such income had been actually received directly by such grantor or such other person, without the intervention of the trust.

Section 71.04(4), Wis. Stats. (1999-00), provides in pertinent part:

Nonresident individuals and nonresident estates and trusts engaged in business within and without the state shall be taxed only on such income as is derived from business transacted and property located within the state.

Section 71.25(2), Wis. Stats. (1999-00), provides:

The situs of income received by a trustee, which income, under the internal revenue code, is taxable to the grantor of the trust or to any person other than the trust, shall be determined as if such income had been actually received directly by such grantor or such other person, without the intervention of the trust.

Section 71.125(2), Wis. Stats. (1999-00), provides:

Each electing small business trust, as defined in section 1361(e)(1) of the Internal Revenue Code, is subject to tax at the highest rate under s. 71.06(1), (1m), (1n) or (1p), whichever taxable year is applicable, on its income as computed under section 641 of the Internal Revenue Code, as modified by s. 71.05(6) to (12), (19) and (20).

Internal Revenue Code (“IRC”) sec. 1361(d)(1)(B) provides for purposes of sec. 678(a), the beneficiary of a QSST shall be treated as the owner of that portion of the trust which consists of stock in an S corporation with respect to which the election under paragraph (2) is made.

### **Analysis:**

#### Situs of the Trusts

The trusts are not Wisconsin trusts. Testamentary trusts are sited in the state where the decedent was domiciled at death, sec. 71.14(2), Wis. Stats. The trusts are not subject to the jurisdiction of Wisconsin courts, secs. 71.14(2) and 72.27(1), Wis. Stats. The Co-Trustees are not required to file any annual accounting with any court in Wisconsin.

The other state does not have a procedure for the transfer of the jurisdiction of a trust. Therefore, no transfer of

jurisdiction of the trusts from a court of the other state to a Wisconsin court has taken place or will take place.

The trusts should be treated as residents of the other state for income tax purposes.

#### Taxation of the Trusts Generally

The trust should only report income to Wisconsin that is attributable to Wisconsin sources. To the extent that distributable net income is carried out to the beneficiary, then the beneficiary will report such income consistent with the “beneficiary” status as a resident or non-resident of Wisconsin, secs. 71.04(4) and 71.04(1)(b)1, Wis. Stats.

#### Taxation if ESBT Elections are Made

If ESBT elections are made with respect to the trusts, the ESBT portion of each trust will be taxed by Wisconsin only on the trust’s income that is derived from business transacted and property located within Wisconsin, sec. 71.04(4), Wis. Stats. Under the facts as submitted, this would be each trust’s share of Company income apportioned to Wisconsin. This Wisconsin income would be taxed at the highest Wisconsin tax rate pursuant to sec. 71.125(2), Wis. Stats.

Each trust would owe no Wisconsin income tax on the trust’s share of the Company non-Wisconsin income, or on the trust’s other non-Wisconsin income.

Beneficiary A and Beneficiary B would have no Wisconsin income with respect to the distributions from the ESBT portion of the trust, as Wisconsin is taxing all such income at the trust level.

#### Taxation if QSST Elections are Made

If QSST elections are made with respect to a trust, the income of the QSST portion of the trust (the trust’s share of the Company income) will be treated as received directly by the beneficiary, sec. 71.25(2), Wis. Stats., and IRC secs. 1361(d), 678(a) and 671. The QSST portion of the trust will be disregarded for Wisconsin income tax purposes.

Beneficiary B (a non-resident of Wisconsin) will report to Wisconsin the Wisconsin portion of Trust B’s share of Company income. 