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RE: Purpose Trusts

Dear Ms. Fields and Mr. Alinsky:

On behalf of the American Institute of CPAs (AICPA), we are writing to suggest the Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) consider suggestions regarding the tax classification of purpose trusts, and functionally similar structures, for federal income tax purposes. Our recommendations will simplify filing for taxpayers and practitioners and will reduce the administrative burden on the IRS as well.

In the below comments, we recommend that Treasury and IRS provide guidance regarding purpose trusts, including:

1. Amend regulations to provide a purpose trust generally is classified for federal income tax purposes as an ordinary trust.
2. Amend regulations to clarify distributions in furtherance of the purpose of a purpose trust that are not treated as distributions to a beneficiary are not deductible as distributions under section¹ 661 and not taxable to recipients under section 662.
3. Issue guidance on the application to purpose trusts of the grantor trust rules, transfers to foreign nongrantor trusts, and information reporting requirements.
4. Issue guidance for federal income tax purposes regarding the classification of structures organized as foundations that are functioning like purpose trusts as trusts, and entities organized as nonstock corporations that are functioning like purpose trusts as corporations. Allow purpose trusts and foundations functioning like purpose trusts to elect (such as on Form 8832, *Entity Classification Election*,) to be classified as associations taxable as corporations, and entities organized as nonstock corporations to elect to be classified as ordinary trusts.

¹ Unless otherwise indicated, references to a “section” are to a section of the Internal Revenue Code of 1986, as amended (the “Code”), and references to a “Treas. Reg. §” are to the Treasury regulations promulgated under the Code.

5. Provide guidance on section 4947 to clarify that it applies not only to wholly charitable nonexempt trusts, but also to wholly charitable nonexempt foundations, wholly charitable nonexempt nonstock corporations, and wholly charitable nonexempt trusts that elect to be taxable as associations taxable as corporations but in each case only if a deduction for the structure was allowed under sections 170, 545(b)(2), 642(c), 2055, 2106(a)(2) or 2522 (or corresponding provisions of prior law).

Specific Comments

Background

Treasury Regulation § 301.7701-4(a) defines an ordinary trust as an arrangement whereby trustees hold title to property for the purpose of protecting or conserving it for the benefit of beneficiaries. This definition seems to require that there be “beneficiaries” in order for an arrangement to be taxable as an ordinary trust.

A purpose trust has no ascertainable beneficiaries. As a result, at common law,² purpose trusts often were held to be invalid. If there are no ascertainable beneficiaries, the validity of the trust may depend on whether another person has the ability to enforce the trust.³

A charitable trust may be enforced by state attorneys general. All states recognize charitable purpose trusts, some by statute. Those states that recognize noncharitable purpose trusts require that a person, such as an “enforcer” or “protector” or the court, have the ability to enforce the trustee’s obligation to carry out the purposes of the trust. However, nothing in the Code or regulations defines either a charitable trust or a noncharitable purpose trust as a trust for federal income tax purposes. In fact, Treas. Reg. § 301.7701-4(a) seems to treat an arrangement as a trust only if its purpose is to vest in trustees responsibility for the protection and conservation of property for beneficiaries.

This definition is out of date because under the laws of many states, a trust created for any lawful purpose is valid even if it has no ascertainable beneficiaries. See, for example, Section 409 of the [Uniform Trust Code](#) (“UTC”):

SECTION 409. NONCHARITABLE TRUST WITHOUT ASCERTAINABLE

BENEFICIARY. Except as otherwise provided in Section 408 [dealing with trusts for the care of animals, a subset of noncharitable purpose trusts] or by another statute [some states have statutes governing other types of purpose trusts such a cemetery trusts or stewardship trusts], the following rules apply:

² For a history of noncharitable purpose trusts see, Richard Ausness, “[Non-Charitable Purpose Trusts – Past, Present and Future.](#)”

³ Scott and Ascher on Trusts – Scott, Ascher and Fratcher, 6th edition, 2023 Cum. Supp. §12.10. In the case of a noncharitable purpose trust whose purpose was sufficiently clear and not unlawful or frivolous, sometimes courts would recognize the noncharitable purpose trust as an honorary trust – one in which the trustee had the right but not the duty to carry out the purposes of the trust. However, because the estate of the settlor had a reversion, in practical effect, there was a beneficiary who could enforce the reversionary interest.

- (1) A trust may be created for a noncharitable purpose without a definite or definitely ascertainable beneficiary or for a noncharitable but otherwise valid purpose to be selected by the trustee. The trust may not be enforced for more than [21] years.
- (2) A trust authorized by this section may be enforced by a person appointed in the terms of the trust or, if no person is so appointed, by a person appointed by the court.
- (3) Property of a trust authorized by this section may be applied only to its intended use, except to the extent the court determines that the value of the trust property exceeds the amount required for the intended use. Except as otherwise provided in the terms of the trust, property not required for the intended use must be distributed to the settlor, if then living, otherwise to the settlor's successors in interest.

Although Treas. Reg. § 301.7701-4(a) seems to require that there be beneficiaries in order for an arrangement to be taxable as a trust, there are at least three authorities indicating that this may not be the view of the IRS: [Rev. Rul. 58-190](#), 1958-1 C.B. 15 (cemetery trust), [Rev. Rul. 76-486](#), 1976-2 C.B. 192 (pet trust), and [INFO 2015-0039](#) (gun trust).

In INFO 2015-0039, the IRS stated:

The fact that a person is not identified in the trust agreement as a beneficiary does not necessarily mean that a person is not a beneficiary for either property law or federal tax purposes. *** Even if we did not consider the...Trust as having beneficiaries within the meaning of § 643, we would likely still classify it as a trust under § 301.7701-4 under the principles applied in the two revenue rulings. In each of Rev. Rul. 58-190, 1958-1 C.B. 15 and Rev. Rul. 76-486, 1976-1 C.B. 192, the Service considered the income tax consequences of nongrantor purpose trust without beneficiaries. *** The rulings hold that, even though the trusts lacked beneficiaries, if the trusts were valid under state law, they would still be recognized as trusts for federal tax purposes and thus taxable under § 641.

If this is the position of the IRS, Treasury and IRS should amend the regulation to provide clearer guidance regarding the proper classification of purpose trusts.

In addition, because the purposes of a purpose trust might be carried out through alternative structures, such as foundations (authorized in New Hampshire and Wyoming⁴ as well as under foreign law) or nonstock corporations (e.g. 8 Del. C. 1953 § 101 et. seq.), guidance is needed regarding the tax classification of these alternative structures. In [IRS Chief Counsel Attorney Memo AM2009-012](#), the IRS stated that a foreign civil law foundation will be treated and taxed as a trust unless, based on the facts and circumstances, it is more properly classified as a business entity due to its commercial activities. See also, [Rost v. Commissioner](#), 44 F.4th 294 (5th Cir. 2022) and [Estate of Swan](#), [24 T.C. 829 \(1955\)](#) [247 F.2d 144 \(2nd Cir. 1957\)](#) both of which treated foreign foundations as trusts.

⁴ [Wyoming Revised Statute 17-30-101](#) et. seq., [New Hampshire RSA 564-F \(2017\)](#).

Below are some examples of purposes served by noncharitable purpose trusts:

- Stewardship of a business to avoid sale, protect interests of “stakeholders” – employees, customers, suppliers and the community,
- Ownership of a family office to provide continuity,
- Preservation of a family vacation property,
- Maintenance of a collection such as automobiles, guns, manuscripts or memorabilia,
- Promotion of a cause that may not be within the definition of “charitable” such as promoting investigative journalism, promotion of sports or games, maintain a community park, continue festivals, maintain genealogy records,
- Maintenance of gravesites,
- Publication of manuscripts that were unpublished at the author’s death,
- Preservation of wealth for persons using cryogenics, or
- Ownership of assets off-balance sheet of a business enterprise in order to maintain independence from management or avoid ownership restrictions on the business enterprise.

The use of noncharitable purpose trusts has received increased attention due to perceived growth in their use. For example, in 2022 a purpose trust acquired all of the voting stock, representing 2% of the equity, of Patagonia,⁵ a \$3 billion company. Meta recently set up a purpose trust to oversee its media content oversight board.⁶ Organically Grown Company is one example of a U.S. business now owned by a purpose trust.⁷ Although the use of purpose trusts to own companies is a relatively recent phenomenon in the United States, there are over 100 large European companies that use similar structures,⁸ including well-known companies, such as Bosch⁹ and Ikea.¹⁰ The Purpose Foundation has been organized to promote the use of “purpose” structures to own businesses.¹¹ It is timely that tax authorities provide clear guidance regarding the tax implications of this new development.

In addition, we note that section 4947 extends the private foundation rules to certain wholly charitable nonexempt trusts. Section 4947 clearly should have no application to noncharitable purpose trusts. However, currently, section 4947 treatment and guidance may not be applicable to wholly charitable entities organized as foundations or nonstock corporations that have not filed for recognition of tax-exempt status as charities.

⁵ <https://www.patagoniaworks.com/press/2022/9/14/patagonias-next-chapter-earth-is-now-our-only-shareholder>

⁶ https://about.fb.com/wp-content/uploads/2019/09/oversight_board_charter.pdf and <https://www.oversightboard.com/governance/>

⁷ <https://www.organicgrown.com>

⁸ <https://purpose-economy.org/en/whats-steward-ownership/>

⁹ <https://www.bosch.us/our-company/bosch-group-worldwide/>

¹⁰ <https://www.ingka.com/this-is-ingka-group/how-we-are-organised/>

¹¹ <https://www.purpose-us.com>

Recommendations

Treasury and IRS should provide guidance regarding purpose trusts, including:

1. Amend regulations to provide a purpose trust generally is classified for federal income tax purposes as an ordinary trust.

We recommend that Treasury and IRS amend regulations to provide that a purpose trust that is not described in Treas. Reg. § 301.7701-4(b)-(e) or whose tax classification is not otherwise controlled by statute is classified for federal income tax purposes as an ordinary trust.

2. Amend regulations to clarify distributions in furtherance of the purpose of a purpose trust that are not treated as distributions to a beneficiary are not deductible as distributions under section 661 and not taxable to recipients under section 662.

We recommend clarification of the application of sections 661 and 662 to payments in furtherance of a trust's purpose (as distinguished from payments to a beneficiary of a purpose trust). Consistent with IRS [Rev. Rul. 76-486](#), (holding that a pet trust is a valid trust even though it has no "beneficiaries" and no deduction is allowed for distributions for the care of the pet because a pet is not a person), we recommend that Treasury and IRS amend regulations under section 661 to clarify that distributions in furtherance of the purpose of a purpose trust that are not properly treated as distributions to a beneficiary are not deductible as distributions under section 661 (although they may be deductible under section 642(c) if made for charitable purposes) and not taxable to the recipients under section 662.

3. Issue guidance on the application to purpose trusts of the grantor trust rules, transfers to foreign nongrantor trusts, and information reporting requirements.

Further, we recommend that Treasury and IRS issue guidance for federal income tax purposes concerning the application to purpose trusts of Subpart E of Subchapter J (the grantor trust rules, and particularly section 679), section 684 (transfers to foreign nongrantor trusts), and section 6048 and other information reporting requirements. Treasury and IRS should also provide clarification that the grantor trust rules apply.

4. Issue guidance for federal income tax purposes regarding the classification of structures organized as foundations that are functioning like purpose trusts as trusts, and entities organized as nonstock corporations that are functioning like purpose trusts as corporations. Allow purpose trusts and foundations functioning like purpose trusts to elect (such as on Form 8832) to be classified as associations taxable as corporations, and entities organized as nonstock corporations to elect to be classified as ordinary trusts.

Specifically, we recommend that Treasury and IRS issue guidance classifying for federal income tax purposes:

- (A) Structures organized as foundations that are functioning like purpose trusts as trusts; and
- (B) Entities organized as nonstock corporations that are functioning like purpose trusts as corporations.

We also recommend that Treasury and IRS issue guidance allowing for federal income tax purposes:

- (A) Purpose trusts and foundations that are functioning like purpose trusts to elect to be classified as associations taxable as corporations (and the grantor trust rules would not apply); and
- (B) Entities organized as nonstock corporations that are functioning like purpose trusts to elect to be classified as ordinary trusts.

Treasury and IRS should adopt this recommendation and amend Treas. Reg. § 301.7701-4(a) to provide that structures that are validly organized as purpose trusts under applicable property law are taxable as “ordinary trusts” under Treas. Reg. § 307.7701-4(a), unless the trust is a business trust as defined in Treas. Reg. § 301.7701-4(b), a fixed investment trust as defined in Treas. Reg. § 301.7701-4(c), a liquidating trust as defined in Treas. Reg. § 301.7701-4(d), or an environmental remediation trust defined in Treas. Reg. § 301.7701-4(e). A “purpose trust” is a trust organized for a purpose – which may be charitable or noncharitable and may or may not be economic – that does not have at least one ascertainable beneficiary who has standing to enforce the fiduciary obligations of the trustee.

Similarly, we also recommend that a structure organized as a foundation under applicable property law that is functioning in the same manner as a purpose trust also should be classified and taxed as an ordinary trust.

However, structures created for similar purposes and organized as nonstock corporations should be taxable as corporations in accordance with Treas. Reg. § 301.7701-2(b)(1).

While we recommend that the default treatment (unless there is an election otherwise), a purpose trust and a functionally similar foundation should be classified as a trust and a nonstock corporation should be taxable as a corporation, we suggest Treasury and IRS allow taxpayers to elect whether a trust, or a foundation, or corporation functioning as a purpose trust will be taxed as a trust or as an association taxable as a corporation.

- 5. Provide guidance on section 4947 to clarify that it applies not only to wholly charitable nonexempt trusts, but also to wholly charitable nonexempt foundations, wholly charitable nonexempt nonstock corporations, and wholly charitable nonexempt trusts that elect to be taxable as associations taxable as corporations but in each case only if a deduction for the structure was allowed under sections 170, 545(b)(2), 642(c), 2055, 2106(a)(2) or 2522 (or corresponding provisions of prior law).**

Treasury and IRS should provide guidance regarding section 4947 to clarify that in addition to applying to wholly charitable nonexempt trusts, it also applies to alternative structures, such as

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wholly charitable nonexempt foundations and wholly charitable nonexempt nonstock corporations, as well as to nonexempt charitable trusts that elect to be taxable as associations taxable as corporations.

Analysis

The absence of guidance on the tax classification of purpose trusts makes compliance difficult. Taxpayers and their advisors need clarification of the fundamental question as to what rules apply and what forms are required to be filed.

The growth in the use of noncharitable purpose trusts makes this issue important. If a purpose trust is not treated as a trust, the existing regulations offer no guidance as to how it should be classified. Under Treas. Reg. § 301.7701-3, it would be treated as an eligible entity with the right to elect to be classified as an association taxable as a corporation, or as a partnership, and if it has only one member, as a disregarded entity. Since a purpose trust has no members, if it were classified as a disregarded entity or as a partnership there would be no members or partners to pay the tax on the trust's income.

Treating purpose trusts as trusts appears to be consistent with prior IRS guidance on this issue. Similarly, treating foundations functioning like trusts as trusts is consistent with prior IRS guidance.

Treasury Regulation § 301.7701-2(b)(1) states that all corporations organized under state or federal corporation laws or under a statute of a federally recognized Indian tribe are classified as corporations for tax purposes. Nothing in the regulation creates an exception for nonstock corporations.

Although the election in our recommendations would expand the definition of "business entities" that are eligible to make tax classification elections under Treas. Reg. § 301.7701-3(a) to include trusts, (because currently trusts are not included as "business entities" under Treas. Reg. § 301.7701-2), in practical effect, it is not a meaningful expansion of election rights because an entity can effectively elect its tax classification by choice of the law under which it is organized. We think allowing a purpose trust, or an alternative structure functioning as a purpose trust, to elect its tax classification is a reasonable expansion of the election allowed in Treas. Reg. § 301.7701-3 for business entities because a de facto election is possible by appropriately choosing to organize as a trust, foundation, or corporation under state law.

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individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

We appreciate your consideration of our recommendations and welcome the opportunity to discuss our comments. If you have any questions, please contact Irene Estrada, Chair, AICPA Trust, Estate, and Gift Tax Technical Resource Panel, at (703) 628-5243 or Irene.C.Estrada@pwc.com; Eileen Sherr, AICPA Director – Tax Policy & Advocacy, at (202) 434-9256 or Eileen.Sherr@aicpa-cima.com; or me at (830) 372-9692 or bvickers@alamo-group.com.

Sincerely,



Blake Vickers, CPA
Chair, AICPA Tax Executive Committee

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