Nemser v. Commissioner, 66 T. C. 780 (1976)

Purchasers of interests in a testamentary trust are not considered "beneficiaries succeeding to the property of the estate or trust" under IRC § 642(h) and thus cannot claim deductions for the trust's excess expenses in its terminal year.

Summary

Alan Nemser purchased a fractional interest in a testamentary trust created by Silas J. Llewellyn. When the trust terminated, Nemser sought to deduct his pro rata share of the trust's excess expenses over income. The Tax Court held that Nemser was not a beneficiary under IRC § 642(h) because he acquired his interest by purchase, not by succession through bequest, devise, or inheritance. Therefore, he could not claim deductions for the trust's terminal year expenses, emphasizing that the statutory language and legislative intent limit such deductions to true beneficiaries.

Facts

Silas J. Llewellyn's testamentary trust was created upon his death in 1925. Mary Isabelle Llewellyn, a granddaughter and a remainder beneficiary, sold a portion of her interest in the trust to the Richard Kadish group in 1946. Alan Nemser then purchased a portion of Kadish's interest for investment purposes. In 1968, the trust terminated, and Nemser received a distribution of stocks. He claimed a deduction for his share of the trust's excess expenses over income for the terminal year, which was disallowed by the IRS.

Procedural History

Nemser filed a petition in the U. S. Tax Court challenging the IRS's disallowance of his deduction claim. The Tax Court considered the case and issued its opinion on July 27, 1976, holding in favor of the Commissioner.

Issue(s)

1. Whether a purchaser of an interest in a testamentary trust is considered a "beneficiary succeeding to the property of the estate or trust" under IRC § 642(h)(2), allowing them to deduct their pro rata share of the trust's excess expenses in its terminal year?

Holding

1. No, because the court found that the phrase "beneficiaries succeeding to the property" in IRC § 642(h) refers only to recipients by gift, bequest, devise, or inheritance, not to purchasers of interests.

Court's Reasoning

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The court analyzed the language and legislative intent of IRC § 642(h), which allows deductions for excess expenses to "beneficiaries succeeding to the property of the estate or trust. " The court noted that Nemser acquired his interest through purchase, not by succession. The court cited the legislative history indicating that § 642(h) was meant to provide relief to heirs and designated takers under a will whose inheritance is diminished by estate expenses. The court referenced its prior decision in Sletteland, where a similar claim by a purchaser of an estate interest was rejected. The court concluded that Nemser did not bear the burden of the trust's expenses as he purchased a portion of the trust's principal after expenses were accounted for, thus not qualifying as a beneficiary under § 642(h).

Practical Implications

This decision clarifies that only true beneficiaries by succession can claim deductions for a trust's terminal year expenses under IRC § 642(h). Legal practitioners advising clients on estate and trust planning must distinguish between beneficiaries and purchasers of interests. Purchasers should not expect to claim such deductions, impacting investment decisions in trust interests. The case also underscores the importance of understanding the specific statutory language and legislative intent when dealing with tax deductions. Subsequent cases, such as Sletteland, have continued to apply this principle, reinforcing its impact on tax practice in this area.

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