

an error that may prove to be misleading and is in need of clarification.

Correction of Publication

Accordingly, the publication of a notice of proposed rulemaking (REG-137125-08), which was the subject of FR Doc. 2011-15653, is corrected as follows:

On page 37036, column 2, in the preamble, under the paragraph heading “Proposed Effective/Applicability Date”, the language “These regulations under section 162(m) are proposed to apply to taxable years ending on or after the date of publication of the Treasury decision adopting these rules as final regulation in the **Federal Register**.” is removed and is replaced with the new language “These proposed regulations will be effective upon publication in the **Federal Register** of a Treasury decision adopting these rules as final regulations.”.

LaNita Van Dyke,

Chief, Publications and Regulations Branch, Legal Processing Division, Associate Chief Counsel, (Procedure and Administration) [FR Doc. 2011-22734 Filed 9-6-11; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-128224-06]

RIN 1545-BF80

Section 67 Limitations on Estates or Trusts

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Withdrawal of notice of proposed rulemaking; notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document withdraws the notice of proposed rulemaking that was published in the **Federal Register** on July 27, 2007, providing guidance on which costs incurred by estates or trusts other than grantor trusts (non-grantor trusts) are subject to the 2-percent floor for miscellaneous itemized deductions under section 67(a). This document contains proposed regulations that provide guidance on which costs incurred by estates or trusts other than grantor trusts (non-grantor trusts) are subject to the 2-percent floor for miscellaneous itemized deductions under section 67(a). The regulations affect estates and non-grantor trusts. This document also provides notice of

a public hearing on these proposed regulations.

DATES: Written and electronic comments must be received by December 6, 2011. Outlines of topics to be discussed at the public hearing scheduled for December 19, 2011 must be received by December 7, 2011.

ADDRESSES: Send submissions to CC:PA:LPD:PR (REG-128224-06), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-128224-06), Courier’s Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC, or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov/> (IRS REG-128224-06). The public hearing will be held in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Jennifer N. Keeney, (202) 622-3060; concerning submissions of comments, the hearing, or to be placed on the building access list to attend the hearing, Richard A. Hurst, (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed regulations amending 26 CFR part 1 under section 67 of the Internal Revenue Code (Code) by adding § 1.67-4 regarding which costs incurred by an estate or a non-grantor trust are subject to the 2-percent floor for miscellaneous itemized deductions under section 67(a).

Section 67(a) of the Code provides that, for an individual taxpayer, miscellaneous itemized deductions are allowed only to the extent that the aggregate of those deductions exceeds 2 percent of adjusted gross income. Section 67(b) excludes certain itemized deductions from the definition of “miscellaneous itemized deductions.” Section 67(e) provides that, for purposes of section 67, the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual. However, section 67(e)(1) provides that the deductions for costs paid or incurred in connection with the administration of the estate or trust that would not have been incurred if the property were not held in such estate or trust shall be treated as allowable in arriving at adjusted gross income. Therefore, deductions described in

section 67(e)(1) are not subject to the 2-percent floor for miscellaneous itemized deductions under section 67(a).

A notice of proposed rulemaking (REG-128224-06, 2007-36 IRB 551) was published in the **Federal Register** (72 FR 41243) on July 27, 2007. The proposed regulations provide that a cost is fully deductible to the extent that the cost is unique to an estate or trust. If a cost is not unique to an estate or trust, such that an individual could have incurred the expense, then that cost is subject to the 2-percent floor. For this purpose, the proposed regulations clarify that it is the type of product or service provided to the estate or trust in exchange for the cost, rather than the description of the cost of that product or service, that is tested to determine the uniqueness of the cost. The proposed regulations also address costs subject to the 2-percent floor that are included as part of a comprehensive commission or fee paid to the trustee or executor (“Bundled Fiduciary Fee”).

Written comments were received in response to the notice of proposed rulemaking. A public hearing was held on November 14, 2007, at which several commentators offered comments on the notice of proposed rulemaking.

On January 16, 2008, the Supreme Court of the United States issued its decision in *Michael J. Knight, Trustee of the William L. Rudkin Testamentary Trust v. Commissioner*, 552 U.S. 181, 128 S. Ct. 782 (2008), holding that fees paid to an investment advisor by a non-grantor trust or estate generally are subject to the 2-percent floor for miscellaneous itemized deductions under section 67(a). The Court reached this decision on a reading of section 67(e) that differed from that in the proposed regulations. The Court held that the proper reading of the language in section 67(e), which asks whether the expense “would not have been incurred if the property were not held in such trust or estate,” requires an inquiry into whether a hypothetical individual who held the same property outside of a trust “customarily” or “commonly” would incur such expenses. Expenses that are “customarily” or “commonly” incurred by individuals are subject to the 2-percent floor.

Following the Supreme Court’s decision in *Knight*, the Internal Revenue Service (IRS) and the Treasury Department issued Notice 2008-32 (2008-12 IRB 593) (March 24, 2008) to provide interim guidance on the treatment of Bundled Fiduciary Fees. The Notice provided that taxpayers will not be required to determine the portion of a Bundled Fiduciary Fee that is subject to the 2-percent floor under

section 67 for any taxable year beginning before January 1, 2008. In the Notice, the IRS and the Treasury Department reopened the comment period on the proposed regulations with regard to possible factors on which to base safe harbors for the allocation of a Bundled Fiduciary Fee between costs subject to the 2-percent floor and those exempt from the application of that floor. Written comments were received in response to the Notice. The IRS and the Treasury Department subsequently issued Notice 2008-116 (2008-52 IRB 1372) (December 29, 2008) extending the interim guidance provided in Notice 2008-32 to taxable years that begin before January 1, 2009, Notice 2010-32 (2010-16 IRB 594) (April 19, 2010) extending the interim guidance provided in Notice 2008-116 and Notice 2008-32 to taxable years that begin before January 1, 2010, and Notice 2011-37 (2011-20 IRB 785) (May 16, 2011) extending the existing interim guidance to taxable years that begin before the publication of final regulations in the **Federal Register**.

All comments were considered and are available for public inspection. Many of the comments recommended that the proposed regulations be withdrawn and that new proposed regulations be issued to allow the public to comment on the impact of the *Knight* decision on the regulations to be issued under section 67(e). After consideration of all of the comments received since the issuance of the proposed regulations, the proposed regulations published on July 27, 2007, are withdrawn and this document contains new proposed regulations.

Explanation of Provisions

In General

In *Knight*, the Supreme Court held that the deductibility of an expense under section 67(e)(1) depends upon whether the cost is “commonly” or “customarily” incurred when such property is held instead by an individual. In other words, section “67(e)(1) excepts from the 2-percent floor only those costs that it would be *uncommon* (or unusual, or unlikely) for such a hypothetical individual” holding the same property to incur (emphasis in original). In applying this interpretation of the statute to investment advisory fees incurred by a trust, the Court held that such fees generally are not uncommonly incurred by individual investors and thus are subject to the 2-percent floor. The Court noted, however, that it is conceivable “that a trust may have an unusual investment objective, or may require a specialized

balancing of the interests of various parties, such that a reasonable comparison with individual investors would be improper.” The Court went on to provide that, “in such a case, the incremental cost of expert advice beyond what would normally be required for the ordinary taxpayer would not be subject to the 2-percent floor.” The Court held that the investment advisory fees of the trust in *Knight* properly were subject to the 2-percent floor, and that the trustee did not assert any such unusual facts that would have brought this cost within the exception.

These proposed regulations reflect the reasoning and holding in *Knight* and provide guidance relating to the limited portion of the cost of investment advice that is not subject to the 2-percent floor. To the extent that a portion (if any) of an investment advisory fee exceeds the fee generally charged to an individual investor, and that excess is attributable to an unusual investment objective of the trust or estate or to a specialized balancing of the interests of various parties such that a reasonable comparison with individual investors would be improper, that excess is not subject to the 2-percent floor. Thus, where the costs charged to the trust do not exceed the costs charged to an individual investor, the cost attributable to taking into account the varying interests of current beneficiaries and remaindermen is included in the usual investment advisory fees and is not the type of cost that is excluded from the 2-percent floor under this narrow exception. Individual investors commonly have investment objectives that may require a balance between investing for income and investing for growth and/or a specialized approach for particular assets. Comments are requested on the types of incremental charges, as described in this paragraph, that may be incurred by trusts or estates, as well as a specific description and rationale for any such charges.

Many of the comments received in response to Notice 2008-32 highlighted the legislative intent of the provision imposing the 2-percent floor for miscellaneous itemized deductions. The commentators noted that the intent was to simplify recordkeeping, reduce taxpayer errors, ease administrative burdens for the IRS, and reduce taxpayer errors in distinguishing between nondeductible personal expenditures and deductible miscellaneous itemized deductions. The IRS and the Treasury Department recognize the administrative difficulty of determining whether every type of cost incurred by a trust or estate is the

type of cost that would be incurred commonly or customarily by individuals owning the same property. Therefore, the proposed regulations provide simplified rules for the application of section 67(e).

Several commentators questioned the authority of the IRS and the Treasury Department to require the unbundling of fiduciary commissions. However, the *Knight* decision posited just such an unbundling in the case of investment advisory costs rendered for certain services, the cost of which exceeds the costs charged to an individual investor. In determining whether a cost is subject to the 2-percent floor, the relevant cost at issue under section 67(e)(1) should be defined by reference to the products or services that were provided in exchange for that cost, rather than the label that is given to the cost. Therefore, if a fiduciary is performing services that are commonly or customarily performed by an investment advisor retained by an individual investor, then the costs attributable to those services are subject to the 2-percent floor.

Many of the comments received in response to Notice 2008-32 objected to a rule that would require any unbundling of a unitary fee due to the cost and administrative difficulty of implementing a process to track which portions of a single fee are subject to the 2-percent floor. Some commentators anticipated that such a rule would require corporate trustees to invest in expensive software to track and measure the value of the various types of services provided on a trust-by-trust and year-by-year basis.

These proposed regulations do not require the allocation described in the July 2007 proposed regulations. Instead, the proposed regulations apply section 67(e) as interpreted by the Supreme Court in *Knight*, while also addressing the Government’s and taxpayers’ interests in reducing the administrative burden of complying with the tax law. The proposed regulations limit the costs that are subject to allocations pursuant to section 67(e) and allow the use of any reasonable method to perform such allocations.

Specifically, the proposed regulations provide that the portion of a bundled fee attributable to investment advice (including any related services that would be provided to any individual investor as part of the investment advisory fee) will be subject to the 2-percent floor. In addition, the proposed regulations provide that, except for the portion so allocated to investment advice, a fiduciary fee not computed on an hourly basis is fully deductible with certain exceptions. The exceptions are

payments made to third parties out of the bundled fee that would have been subject to the 2-percent floor if they had been paid directly by the non-grantor trust or estate, and any payments for expenses separately assessed (in addition to the usual or basic fiduciary fee or commission) by the fiduciary or other service provider that are commonly or customarily incurred by an individual owner of such property. An example of such a separately assessed expense subject to the 2-percent floor might be an additional fee charged by the fiduciary for managing rental real estate owned by the non-grantor trust or estate.

The proposed regulations allow the fiduciary and/or return preparer to use any reasonable method to make these allocations. However, the amount of each payment (if any) out of the fiduciary's fee or commission to a third party for expenses subject to the 2-percent floor, and of each separately assessed expense that is commonly or customarily incurred by an individual owner of such property, is readily identifiable without any discretion on the part of the fiduciary. Therefore, the reasonable method standard does not apply to these amounts that are to be deducted from the portion of the bundled fiduciary fee that is not subject to the 2-percent floor.

Comments are requested on the types of methods for making a reasonable allocation, including possible factors on which a reasonable allocation is most likely to be based, and on the related substantiation that will be needed to satisfy the reasonable method standard proposed in these regulations. Specifically, the IRS and the Treasury Department are interested in methods for reasonably estimating the portion of a bundled fee that is attributable to investment advice. For methods based in whole or in part on time devoted to providing investment advice, the IRS and Treasury Department ask for suggestions for alternatives to contemporaneous time records for specific activities that could be used to substantiate the reasonableness of the allocation. The IRS and Treasury Department have considered comments regarding possible numerical or percentage safe harbors in response to Notice 2008-32. Commentators noted that, in many cases, fiduciaries could not rely on safe harbors because their fiduciary duties would require them to make a more accurate estimate so as to not harm the trust or their beneficiaries. In addition, safe harbors could increase complexity by requiring complicated anti-abuse rules. Therefore, comments

are requested on methods other than numerical or percentage safe harbors.

Effective/Applicability Dates

Notice 2011-37 provides that taxpayers will not be required to determine the portion of a Bundled Fiduciary Fee that is subject to the 2-percent floor under section 67 for taxable years beginning before the date that these regulations are published as final regulations in the **Federal Register**.

Availability of IRS Documents

The IRS notices cited in the preamble are published in the Cumulative Bulletin and are available at <http://www.irs.gov>.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f), the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and the Treasury Department also request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for December 19, 2011, beginning at 10 a.m. in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the Internal Revenue Building lobby more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the

FOR FURTHER INFORMATION CONTACT

section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written or electronic comments by December 6, 2011 and submit an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by December 7, 2011. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the schedule of speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Jennifer N. Keeney, Office of the Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Withdrawal of Notice of Proposed Rulemaking

Accordingly, under the authority of 26 U.S.C. 7805, the notice of proposed rulemaking amending 26 CFR parts 1 and 301 that was published in the **Federal Register** on July 27, 2007, 72 FR 41243 (REG-128224-06), is withdrawn.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.67-4 is added to read as follows:

§ 1.67-4 Costs paid or incurred by estates or non-grantor trusts.

(a) *In general.* Section 67(e) provides an exception to the 2-percent floor on miscellaneous itemized deductions for costs that are paid or incurred in connection with the administration of an estate or a trust not described in § 1.67-2T(g)(1)(i) (a non-grantor trust) and which would not have been incurred if the property were not held in such estate or trust. A cost is subject to the 2-percent floor to the extent that it is included in the definition of

miscellaneous itemized deductions under section 67(b), is incurred by an estate or non-grantor trust, and commonly or customarily would be incurred by a hypothetical individual holding the same property.

(b) *“Commonly” or “Customarily”*
Incurred—(1) *In general*. In analyzing a cost to determine whether it commonly or customarily would be incurred by a hypothetical individual owning the same property, it is the type of product or service rendered to the estate or non-grantor trust in exchange for the cost, rather than the description of the cost of that product or service, that is determinative. In addition to the types of costs described in paragraphs (b)(2), (3) and (4) of this section, costs that are incurred commonly or customarily by individuals also include expenses that do not depend upon the identity of the payor (in particular, whether the payor is an individual or instead is an estate or trust). Such commonly or customarily incurred costs include, but are not limited to, costs incurred in defense of a claim against the estate, the decedent, or the non-grantor trust that are unrelated to the existence, validity, or administration of the estate or trust.

(2) *Ownership costs*. Ownership costs are costs that are chargeable to or incurred by an owner of property simply by reason of being the owner of the property, such as condominium fees, real estate taxes, insurance premiums, maintenance and lawn services, automobile registration and insurance costs, and partnership costs deemed to be passed through to and reportable by a partner. For purposes of section 67(e), ownership costs are commonly or customarily incurred by a hypothetical individual owner of such property.

(3) *Tax preparation fees*. The application of the 2-percent floor to the cost of preparing tax returns on behalf of the estate, decedent, or non-grantor trust will depend upon the particular tax return. All estate and generation-skipping transfer tax returns, fiduciary income tax returns, and the decedent's final individual income tax returns are not subject to the 2-percent floor. The costs of preparing other individual income tax returns, gift tax returns, and tax returns for a sole proprietorship or a retirement plan, for example, are costs commonly and customarily incurred by individuals and thus are subject to the 2-percent floor.

(4) *Investment advisory fees*. Fees for investment advice (including any related services that would be provided to any individual investor as part of an investment advisory fee) are incurred commonly or customarily by a

hypothetical individual investor and therefore are subject to the 2-percent floor. However, certain incremental costs of investment advice beyond the amount that normally would be charged to an individual investor are not subject to the 2-percent floor. For this purpose, such an incremental cost is a special, additional charge added solely because the investment advice is rendered to a trust or estate instead of to an individual, that is attributable to an unusual investment objective or the need for a specialized balancing of the interests of various parties (beyond the usual balancing of the varying interests of current beneficiaries and remaindermen), in each case such that a reasonable comparison with individual investors would be improper.

(c) *Bundled fees*—(1) *In general*. If an estate or a non-grantor trust pays a single fee, commission, or other expense (such as a fiduciary's commission, attorney's fee, or accountant's fee) for both costs that are subject to the 2-percent floor and costs (in more than a de minimis amount) that are not, then the single fee, commission, or other expense (bundled fee) must be allocated, for purposes of computing the adjusted gross income of the trust or estate in compliance with section 67(e), between the costs subject to the 2-percent floor and those that are not. Out-of-pocket expenses billed to the trust or estate are treated as separate from the bundled fee.

(2) *Exception*. If a bundled fee is not computed on an hourly basis, only the portion of that fee that is attributable to investment advice is subject to the 2-percent floor; the remaining portion is not subject to that floor. In addition, payments made from the bundled fee to third parties that would have been subject to the 2-percent floor if they had been paid directly by the non-grantor trust or estate are subject to the 2-percent floor, as are any fees or expenses separately assessed by the fiduciary or other payee of the bundled fee (in addition to the usual or basic bundled fee) for services rendered to the trust or estate that are commonly or customarily incurred by an individual.

Example. A corporate trustee charges a percentage of the value of the trust income and corpus as its annual commission. In addition, the trustee bills a separate amount to the trust each year as compensation for leasing and managing the trust's rental real estate. The separate real estate management fee is subject to the 2-percent floor because it is a fee commonly or customarily incurred by an individual owner of rental real estate.

(3) *Reasonable Method*. Any reasonable method may be used to allocate a bundled fee between those

costs that are subject to the 2-percent floor and those costs that are not, including without limitation the allocation of a portion of a fiduciary commission that is a bundled fee to investment advice. The reasonable method standard does not apply to determine the portion of the bundled fee attributable to payments made to third parties for expenses subject to the 2-percent floor or to any other separately assessed expense commonly or customarily incurred by an individual, because those payments and expenses are readily identifiable without any discretion on the part of the fiduciary or return preparer.

(d) *Effective/applicability date*. These regulations apply to taxable years beginning on or after the date that these regulations are published as final regulations in the **Federal Register**.

Steven T. Miller,

Deputy Commissioner for Services and Enforcement.

[FR Doc. 2011-22732 Filed 9-6-11; 8:45 am]

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ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

[EPA-R10-OAR-2010-0917; FRL-9460-7]

Approval and Promulgation of State Implementation Plans: Alaska

AGENCY: Environmental Protection Agency (EPA).

ACTION: Proposed rule.

SUMMARY: EPA is proposing to approve revisions to Alaska's State Implementation Plan (SIP) relating to the motor vehicle inspection and maintenance program (I/M) for control of carbon monoxide (CO) in Anchorage. The State of Alaska submitted two revisions to the Alaska SIP: a November 13, 2009, submittal containing revisions to the statewide I/M program and a September 29, 2010, submittal discontinuing the I/M program in Anchorage as an active control measure in the SIP and shifting it to a contingency measure. The State's submittals include a revised CO emissions inventory and motor vehicle emissions budget. EPA is proposing to approve the 2010 submittal because it satisfies the requirements of the Clean Air Act (CAA or the Act). EPA is not taking action on the 2009 submittal because the 2010 submittal supersedes the 2009 revision.

DATES: Written comments must be received on or before October 7, 2011.