

# Department of Finance and Administration

## Legislative Impact Statement

**Bill: HB1911**

**Bill Subtitle: TO AMEND THE INCOME TAX ACT OF 1929 CONCERNING WHO SHALL BE TREATED AS THE OWNER OF A PORTION OF A TRUST.**

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### **Basic Change :**

**Sponsor: Rep. M. Gray**

HB1911 amends § 26-51-201 by adopting federal law, 26 U.S.C. §§ 671-679 as in effect on January 1, 2018. The federal income tax laws are adopted for purposes of determining whether the grantor or another person shall be treated as the owner of a portion of a trust. These changes will clarify that Arkansas taxpayers will have the same rules for both federal and state income tax purposes. The bill is effective for tax years beginning on or after January 1, 2019.

### **Revenue Impact :**

None.

### **Taxpayer Impact :**

No taxpayer impact is expected.

### **Resources Required :**

None.

### **Time Required :**

None.

### **Procedural Changes :**

None.

### **Other Comments :**

None.

### **Legal Analysis :**

Arkansas law provides for an income tax on the entire income of every resident, individual, trust, or estate. Gross income includes gains or profits and income derived from any source whatever. In 1997, the Arkansas Department of Finance and Administration (DFA) promulgated Rule 4.26-51-102 of its Comprehensive Individual Income Tax Regulations for determining who should be deemed the owner of a trust or a portion of a trust, and thus responsible for the gains realized by the trust's property. Rule 4.26-51-102 uses the same analysis as Internal Revenue Code § 671 et seq.

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When property is owned subject to a trust agreement, questions arise with regard to who is liable for the taxes that derive from the trust property. Internal Revenue Code § 671 et seq. addresses the specific question of under what circumstances is the creator (or grantor) of the trust, instead of the trustee of the trust, liable for the taxes that derive from the trust property. The general factor to be considered in the analysis is the degree of control that the grantor retains over the trust property. An example can be found at I.R.C. § 674: "The grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the [trust property] is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party." For purposes of the rule, "adverse party" means "any person having a substantial beneficial interest in the trust that would be adversely affected by the exercise or nonexercise of the power which he possesses respecting the trust."

HB1911 would expressly adopt in statute the standards administratively used by the Department for the previous 20 years and allow the DFA to continue using the same standard it currently uses for determining whether who is liable for taxes due on gains arising out of trust property. An increase in the use of trusts for tax planning purposes warrants the General Assembly's action to confirm the existing standards into the Arkansas Code rather than just the Comprehensive Income Tax Rules.