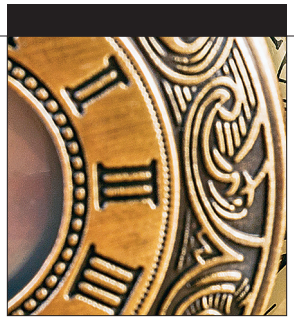

Managing Multiple Businesses With a Section 6166 Election

Estates seeking to defer the payment of estate tax under Section 6166 need to count their business holdings and dispositions of those holdings carefully.

MICHAEL KOSNITZKY AND REBECCA M.G. ZUKS

Since its inception in 1916, with the exclusion of the year 2010, Congress has imposed a federal tax on the transfer of certain property interests at death.[1] Generally, this federal estate tax is due nine months from the decedent's death.[2]

At historic marginal rates reaching as high as 77%,[3] the federal estate tax can cause devastating consequences to illiquid privately held businesses.[4] For estates that primarily consist of closely held businesses, Section 6166 may be the only way to avoid a forced sale to pay the tax.[5]

Section 6166 was enacted during a growing trend where small businesses and farms were forced to sell their assets to have sufficient liquidity to pay the estate tax.[6] As originally enacted in 1958, Congress intended Section 6166 to spread out estate tax payments so that estates with closely held businesses could pay the tax out of earnings or otherwise have time to obtain the funds to pay the estate tax "without upsetting the operation of the business."[7] Section 6166 allows business owners to make "a planned, orderly transfer" of a closely held business.[8]

Since 1958, Section 6166 has become progressively more liberalized and taxpayer friendly. The original version of the statute provided for a nine-year deferral of the estate tax if the business interests were more than 35% of the decedent's gross estate or 50% of the decedent's taxable estate and provided for a below-market interest rate on the deferred tax.[9] In 1976, Congress enacted a new Section 6166A, expanding relief by providing for four years of interest payments followed by ten equal payments of the estate tax if the decedent's adjusted gross estate consisted of more than 65% of business interests. The interest rate charged on a portion of the deferred tax was fixed at a below-market 4% interest rate.[10]

By 1981, Congress further expanded relief when it repealed Section 6166A and enacted a new Section 6166.[11] The 1981 revisions combined the most taxpayer-favorable provisions of the 1958 and 1976 statutes.[12] The 1981 version of Section 6166 reduced the business interest percentage from 65% to 35% of the adjusted gross estate.[13] In 1997, Congress then amended Section 6601(j). This legislative change:

1. Reduced the interest rate from 4% to 2% on a portion of the deferred tax.
2. Increased the deferred tax subject to the fixed interest rate of 2%.
3. Added a discounted floating interest rate for the portion of

MICHAEL KOSNITZKY is a partner of Pillsbury Winthrop Shaw Pittman LLP, resident in the law firm's Miami and New York offices. Rebecca M.G. Zuks is an associate in the firm's New York office.

the deferred tax not subject to the 2% rate.[14]

In 2002, Section 6166 was expanded to permit certain investment or rental activities to qualify for a more limited estate tax deferral if they are "qualifying lending and finance businesses."[15]

Requirements for election

Under current law, to qualify for estate tax deferral under Section 6166, certain requirements must be met, namely:

1. The decedent must have been a U.S. citizen or resident with a closely held business at the time of his or her death.
2. The value of the decedent's interest in a closely held business exceeds 35% of the decedent's adjusted gross estate.
3. The estate's personal representative must make an election on a timely filed estate tax return.[16]

Defining a closely held business. Meeting the definition of a "closely held business" for purposes of Section 6166 is a fairly high standard. The business or businesses must be "active" and must meet certain threshold percentage tests. What exactly constitutes an active business has been the subject of much debate, but the IRS generally takes the position that the business must have been engaged in an active trade or business as of the decedent's death.[17] The mere management of investment assets generally is not an active trade or business. This frequently arises in the context of decedents who are involved in the rental of real property.[18]

Section 6166(b)(1) defines an interest in a closely held business as an interest in any of the following:

1. A proprietorship engaged in a trade or business.
2. A partnership if at least 20% of the total capital interest in the partnership is included in the decedent's estate or with no more than 45 partners.
3. A corporation in which the decedent must own at least 20% of the value of voting stock or the corporation must not have more than 45 shareholders.

Since Section 6166 was enacted, Congress increased the number of partners and shareholders a business may have under Sections 6166(b)(1)(B) and 6166(b)(1)(C) to be considered closely held from ten to 15 before reaching this current level of 45, making it easier for these types of businesses to qualify.

The 35% threshold. To make a Section 6166 election, the aggregate value of the interests in one or more closely held business must exceed 35% of the value of the adjusted gross estate. The "adjusted gross estate" is the excess of the value of the gross estate after the deductions permitted under Section 2053 for administration and funeral expenses, claims, and mortgages and Section 2054 for casualty losses.[19]

For the purposes of determining the value of the closely held business in the estate, any portion of the

1 See Sections 2001 and 2010; Preminger, Thomas, Frunzi, and Kilker, *Trusts and Estates Practice in New York* (Thomson Reuters), § 9:1.

2 See Section 6151 (unless otherwise provided, taxpayers should pay the tax at the time and place fixed for filing the tax return); Section 6075 (the estate tax return should be filed within nine months after the decedent's death).

3 In 2002, the maximum estate tax rate was 50% on estates exceeding $1 million. "Federal Estate and Gift Tax Rates, Exemptions, and Exclusions, 1916-2017," www.TaxFoundation.org (last visited 7/12/2017). In 2017, the maximum estate tax rate is 40% and is imposed on estates in excess of $5.49 million.

4 See Section 2001(c); Belcher and Sanderson, "Estate Planning for the Closely Held Business," 56 Ann. Tax Conf. cxxxviii (2010); Miller, "Dividing a Family Business May Prevent Estate Tax Deferral," 51 Tax'n Acc'tants 18 (July 1993).

5 See Miller, *supra* note 4.

6 See Sheffield, "Liquidity Problems of Owners of Closely Held Corporations: Relief Provided by Sections 303 and 6166," 38 U. Fla. L. Rev. 787, 795 (1986).

7 H.R. Rep't. No. 2198, 85th Cong., 1st Sess. (1958), reprinted in 1959-2 CB 713.

8 See Saltzman and Saltzman, *IRS Procedural Forms and Analysis* (Thomson Reuters), § 3.14[1].

9 See Belcher and Sanderson, *supra* note 4; Mezzulo, "Estate Planning for Owners of Closely Held Business Interests," 309-4th Tax Mgmt. (BNA) Estates, Gifts and Trusts at III.C.2. The original 1958 statute provided for a 4% interest rate on the deferred tax. In 1975, Public Law 93-625 altered this interest rate by linking it to a fluctuating rate, designed to be approximately 90% of the prime rate. See Campbell and Carrol, "Section 6166: Preserving the Family Business or Farm Through Estate Tax Deferral," 25 Drake L. Rev. 521, 536 at n. 2 (1976).

10 See Belcher and Sanderson, *supra* note 4, at 53-54.

11 See *id* at 54.

12 See Beckerman, "Estate Tax Payments and Liabilities: Sections 6161 and 6166," 832-2nd Tax Mgmt. (BNA) Estates, Gifts and Trusts at [I][B].

13 See Belcher and Sanderson, *supra* note 4, at 54.

14 See Pub.L. 105-206, Title III, § 3301(b); Belcher, *supra* note 4, at 54.

15 See 6166(b)(10); 5-74 *Federal Income, Gift and Estate Taxation* § 74.01[5][b][i].

16 See Sections 6166(a)(1) and 6166(d).

17 See Belcher and Sanderson, *supra* note 4, at 57; *U.S. Master Estate and Gift Tax Guide* (Matthew Bender) ¶ 1672.

18 Private letter rulings on this topic include Ltr. Ruls. 8020101, 8144012, 8601005, 8332025, 8314003, and 8240054.

19 See Section 6166(b)(6). This amount is determined based on the facts and circumstances as they exist on the date for filing the estate tax return. These are all deductions allowable, not necessarily all deductions taken.

20 Section 6166(b)(9).

21 Section 6166(b)(9)(iii).

22 Bitker and Lokken, *Federal Taxation of Income, Estates & Gifts* (Thomson Reuters) ¶ 137.5.2.

23 See Section 6166(b)(2).

24 See Section 6166(b)(7); see Belcher and Sanderson, *supra* note 4, at 6.

25 1979-2 CB 539.

26 See Rico, "Borrowing for Postmortem Liquidity, Part 2—A Primer on IRC § 6166," 25 Prob. & Prop. 47, 49 (January/February 2011).

27 See Section 6166(h); Reg. 20.6166-1(c).

28 See Reg. 20.6166-1(d).

29 See Section 6324(a)(1).

30 See Notice 2007-90, 2006-46 IRB 1003.

31 See Sections 6165 and 6324A.

32 See Sections 6324(a)(2) and 2204 (general fiduciary discharge). Posting the bond or granting the lien will not eliminate transferee liability under Section 6324(b), per Section 6324(c). However, provided the IRS's interest is adequately secured using the bond and lien, the possibility of the IRS imposing transferee liability is mitigated.

interest that is attributable to passive assets (i.e., assets other than those used in carrying on a trade or business) cannot qualify.[20] One exception occurs where (1) a corporation owns 20% or more in value of the voting stock of another corporation or such other corporation has 45 or fewer shareholders, and (2) 80% or more of the value of the assets of each such corporation is attributable to assets used in carrying on a trade or business.[21] If this test is met, the corporations are combined and are treated as a single closely held business.

Section 6166(c) also provides a special rule for estates that hold an interest in two or more closely held businesses. In that situation, for each business in which the decedent's gross estate holds 20% or more of the total value of each business, the interests "shall be treated as an interest in a single closely held business." Adding further flexibility, if the decedent's surviving spouse owned an interest in the one or more of the businesses as community property or as joint tenants, tenants by the entirety, or tenants in common with the decedent, Section 6166(c) includes their collective interest, inclusive of the spouse's share, as part of the gross estate for the purposes of meeting this 20% requirement.

Although the 35% threshold is said to be an "all-or-nothing requirement, with potentially drastic consequences at the margin," Section 6166 also has several "attribution" rules to make it easier for estates to qualify.[22] These rules include:

- Property owned directly, indirectly, by or for a corporation, partnership, estate, or trust is treated as being owned proportionately by or for its shareholders, partners, or beneficiaries.
- Certain interests held as husband and wife.
- Stock and partnership interests held by certain members of the decedent's family.[23]

Section 6166(b)(7) further permits the interests of certain related persons in non-readily tradable stock to be included in determining the value of the decedent's gross estate so that an estate may qualify for a more limited version of Section 6166 relief.[24]

Thus, Section 6166 contains many flexible attribution and affiliation rules that are intended to permit multiple businesses to be treated as a single closely held business for purposes of applying the statutory relief.

Making the election. Reg. 20.6166-1(b) and Rev. Proc. 79-55[25] set out the procedure for making and processing a Section 6166 election.[26] The personal representative of an estate makes a Section 6166 election as an attachment to a timely filed estate tax return. Even if that election is not made, the personal representative may make a Section 6166 election within 60 days of receiving a notice and demand for the payment of an estate tax deficiency.[27] However, that election extends only to the deficiency amount. Section 6166 also permits the filing of a protective election with the estate tax return.[28] This permits estates that do not appear to qualify for the Section 6166 election to qualify if it is later determined that the estate does qualify.

Once the Section 6166 election has been made, special Code provisions provide the IRS with security for the amount of the deferred tax in order to protect the interest of the Government for the actual payment of the tax. Under Section 6324(a), a general federal estate tax lien arises upon the decedent's date of death and attaches for ten years to all assets of the gross estate.[29] This lien secures the Government's interest for a maximum of ten years from the decedent's date of death.[30] Because the Section 6166 election can extend an estate's time to pay the tax to 14 years from the date the estate tax is due—leaving the IRS's interest unsecured for the final four years and nine months—the IRS can require a special lien on the Section 6166 property or the estate to furnish a bond in an amount not to exceed double the tax for which the extension was granted.[31] The personal representative may also post the bond to be discharged from personal liability for unpaid estate tax.[32]

In 2002, the IRS implemented a policy requiring either the lien or

the bond as a prerequisite of the Section 6166 election.[33] The Tax Court subsequently held that the IRS could not make this a universal requirement.[34] Currently, the Internal Revenue Manual refers to Notice 2007-90[35] for the factors for determining whether the lien or bond will be required as security for the deferred tax.[36] The IRS will examine the facts and circumstances of the situation, including but not limited to:

1. The nature of the closely held businesses, the business's assets, and market factors that may affect the business.
2. The expected manner, ability, and likelihood of making annual tax and interest payments.
3. The business' history with federal tax compliance.

Boundaries of Section 6166

Section 6166 is considered taxpayer friendly in that it permits personal representatives to operate their estate businesses with great cash-management flexibility to generate the liquidity necessary to pay the deferred estate tax. This flexibility is not, however, unlimited. Personal representatives must operate within specified statutory limits or risk the acceleration of the deferred estate tax. To ensure that Section 6166 is used for its intended purpose of not forcing estates to liquidate businesses, three triggers cause the estate to lose the benefit of the Section 6166 election:

1. Failure to make a required payment.
2. Excessive dispositions and withdrawals from the closely held business.
3. Undistributed net income of the closely held business.[37]

Provided the personal representative operates within the boundaries of the Internal Revenue Code, the personal representative is permitted to run the combined businesses as he or she sees fit.

Failure to pay installments. If the personal representative fails to make an installment payment of principal or interest when due, the unpaid balance becomes payable upon notice and demand, unless payment is made within six months of the due date.[38] Although the installment privilege is restored, a penalty of 5% multiplied by the number of months of the delinquency is imposed.[39]

50% disposition and withdrawal limit. One of the more complex aspects of Section 6166 is the acceleration of tax triggered by major dispositions of stock and withdrawals from the business. When an aggregate of 50% of the business is withdrawn or disposed of through distribution, sale, exchange, or otherwise, all unpaid installments of tax become due.[40] This is because the sale or liquidation of the closely held business defeats the need to defer the payment of the estate tax.[41]

The 50% threshold is triggered when the decedent's interest in the qualifying business is disposed of, or money or property attributable to the interest is withdrawn from the business and the aggregate of such dispositions and withdrawals, equals or exceeds 50% of the value of the entire interest, measured at the value reported on the estate tax return or as otherwise adjusted by the Code or the IRS.

The IRS has concluded that where a corporation distributed all of its earnings accumulated both before and after the decedent's death, a withdrawal occurred to the extent of the earnings accumulated before the date of death.[42] This conclusion indicates that dividends made from earnings *after* the decedent's death should not be considered a withdrawal for purposes of

33 See Notice 2007-90, 2006-46 IRB 1003.

34 See *id.*; Estate of Roski, 128 TC 113 (2007); Rico, *supra* note 26, at 50.

35 Note 33, *supra.*

36 See IRM 5.17.2.9.1(9) (12/12/2014).

37 See Section 6166(g); Sheffield, *supra* note 6, at 801.

38 See Section 6166(g)(3).

39 See Section 6166(g)(3)(B)(iii).

40 See Section 6166(g)(1).

41 See Kahn, "Closely Held Stocks—Deferral and Financing of Estate Tax Costs Through Sections 303 and 6166," 35 Tax Law. 639, 658 (1982).

42 See Rev. Rul. 75-401, 1975-2 CB 473.

43 See Beckerman, *supra* note 12, at [H].

44 See Reg. 20.6166A-3(d)(3), Example 3; Reg. 20.6166A-3(e)(6), Example 2; Kasner, Strauss, and Strauss, *Post Mortem Tax Planning* (Thomson Reuters) ¶ 9.03[20][r].

45 See Reg. 20.6166A-3(d)(3), Example 3; Reg. 20.6166A-3(e)(6), Example 2. To illustrate using a simplified version of Example 3, the decedent's estate has two businesses worth $400,000 and $300,000 respectively. The executor withdraws $270,000 from the business worth $300,000. Although this well exceeds the 50% limit at 90% of the value of the business, because only $270,000 of the total $700,000 closely held business was withdrawn (approximately 39%) the acceleration provision is not triggered.

46 See Section 6166(g)(1)(B); Belcher and Sanderson, *supra* note 4, at 91.

47 See Section 6166(g)(1)(D); Reg. 20.6166A-3(d); 5-74 *Federal Income, Gift and Estate Taxation* (Matthew Bender) § 74.01[5][b][v].

48 See Section 6166(g)(1)(C); Rev. Rul. 66-62, 1966-1 CB 272.

49 See Section 6166(g)(2).

50 See Sections 6166(g)(2) and 661.

51 See Reg. 20.6166A-2(b).

52 See Reg. 20.6166A-3(f)(1). The regulations require the personal representative to notify the "district director" within 30 days of learning of the above-described transactions. The position of district director no longer exists within the IRS. Section 6166 elections are now handled by the Cincinnati Campus Estate and Gift Tax Operations (the E&G Campus) of the IRS. Each year the E&G Campus updates an internal form, Form 4349, to calculate the interest on the entire deferred estate tax balance due and then prepares and issues to the personal representative a Letter 249C, which includes the interest and principal installment payment. This Letter 249C is sent approximately 30 days prior to the anniversary payment date. IRM 4.25.2.1.13.

53 Again, this disclosure is to be made to the "district director" under the Reg. 20.6166A-3(f)(2). Now it is made to the E&G Campus.

54 See Reg. 20.6166A-3(f)(1).

55 See Reg. 20.6166A-3(f)(3).

56 See Sheffield, *supra* note 6, at 788.

Section 6166(g), particularly if the value of the decedent's interest in the business is not diminished.[43]

Regulations under Section 6166 make clear that for purposes of estates with multiple closely held businesses, the 50% withdrawal and distribution limits apply to the businesses covered by the election in the aggregate.[44] The regulations provide two examples that show, among other things, the value of amounts that are withdrawn or distributed by a closely held business will be aggregated with the value of all closely held businesses qualifying for the Section 6166 election under Section 6166(c) for purposes of the 50% rule.[45]

Even with this generous distribution limit, there are several exempted transactions that will not trigger acceleration, all involving the business continuing to run as a business. Redemptions of stock pursuant to Section 303 (permitting a redemption of stock owned by a deceased shareholder made by a corporation to be treated as an exchange in full value rather than as a dividend to the extent it is used for payment of federal estate taxes and other specific expenses) are exempt, provided the tax paid is equal to the value of property and cash withdrawn from the corporation.[46] Transfers within the family by reason of death are generally protected.[47] Exchanges of stock pursuant to a tax-free reorganization plan are similarly excluded, as are changes from corporate to noncorporate forms of business where the nature of the business and the estate's interest therein are not altered.[48]

Undistributed net income. Any "undistributed net income" in an estate for any tax year beginning with the year of the first installment payment of deferred tax must be paid toward the unpaid tax.[49] Undistributed net income consists of distributable net income exceeding the sum of the following:

1. Amounts required to be distributed currently or amounts properly paid or credited or required to be distributed.
2. Tax imposed for the tax year on the estate.
3. Any estate taxes owed in that tax year.[50]

This payment is allocated equally among the subsequent installment payments.[51]

Reporting obligations of the personal representative and the estate. Once a Section 6166 election has been made, the personal representative has ongoing reporting obligations to the IRS. Each time a withdrawal or disposition of the type described above is made, the personal representative is to notify the E&G Campus of the IRS in writing within 30 days of acquiring knowledge of such withdrawals or dispositions.[52]

Also, each year on the date fixed for payment of an installment of tax, the personal representative must furnish a disclosure in writing to the E&G Campus of the IRS.[53] This disclosure is to be a complete disclosure of all withdrawals or dispositions not previously reported and whether, to the personal representative's knowledge, the 50% test discussed above is satisfied.[54] The IRS may require the personal representative to submit any additional information it deems necessary to establish the estate's right to continue the payment of the tax in installments.[55]

Benefits of the election

Succinctly stated, Section 6166 is a taxpayer-friendly provision because it permits deferral of the estate tax and permits closely held businesses to keep their doors open.[56]

The deferral of taxation, or the ability to pay tax in the future, is a cornerstone of all tax planning and one of its most fundamental principles. This principle permeates virtually all forms of taxation because of the importance of the "time value of money," which articulates the idea that a dollar received today is more valuable than a dollar received in the future. In the context of tax planning, each dollar in tax paid today costs a taxpayer more than that same dollar paid in the future. Moreover, it is generally understood that deferred payment of tax confers a benefit to the estate. The personal representative is always acting in furtherance of and to benefit an estate if he or she can defer taxes to a later date.

Rules that allow taxpayers to defer the payment of tax are rare, and these rules are often narrowly construed. However, in the context of Section 6166, the opposite is the case. Rather than being restricted to cover fewer situations, Section 6166 has been expanded—making it more available, not less available, to personal representatives.

Under Section 6166, the maximum tax deferred is the amount bearing the same ratio to the total federal estate taxes imposed as the value of the interest in the closely held business bears to the value of the adjusted gross estate.[57] Personal representatives are permitted to pay the tax in a minimum of two and a maximum of ten, equal, annual installments.[58]

For most closely held businesses, during the first four years after the decedent's death, only interest is paid annually, beginning one year from the original due date for the estate tax payment.[59] The first installment payment must be made not more than five years from the original due date for the estate tax payment. The subsequent nine payments consist of annual payments of interest together with the annual installment payment.[60] There thus is a total deferral period of 14 years.

As mentioned above, Section 6166 further provides a below-market interest rate on the deferred tax. Interest on the tax attributable to the first $1 million (adjusted for inflation) of value of the closely held business receives a special rate of only 2%.[61] For amounts above that first $1 million, the interest rate is 45% of the IRS underpayment rate.[62] With the current underpayment rate of 4%, the balance of the deferred tax is subject just to a 1.8% interest rate. Given these favorable interest rates, the Section 6166 election will clearly outweigh borrowing from other sources to pay the estate tax.[63]

While the above-referenced tax deferral is a substantial benefit to estates, Congress's primary intention was to maintain the existence and viability of closely held businesses by an estate. For estates that qualify for the Section 6166 election, the favorable deferral terms help to avoid forced liquidation at reduced prices. Often, when an estate is forced to sell assets to raise cash, the estate will receive a lower price than if it had the opportunity to sell at a more advantageous time.[64]

For the purposes of determining the value of the closely held business in the estate, any portion of the interest that is attributable to passive assets cannot qualify.

Additionally, while a Section 6166 election defers the payment of the tax, it creates a "freeze" on the tax amount owed in a manner that is not achieved by using the unlimited marital deduction, one of the most common estate planning tools. Currently, married persons are permitted an unlimited transfer of assets to their spouses without paying a transfer tax. However, this requires the business to be transferred between spouses. When the second spouse dies or disposes of the business, there is a risk that the assets will have appreciated in value and that there will be increased tax rates.

Unlike the unlimited marital deduction which defers both assessment and payment of the tax, Section 6166 defers only the payment. This means that, aside from interest owed on the deferred tax, the amount of tax owed will not be affected by appreciation of the assets or potential estate tax increases. Moreover, the business can be passed on to the next generation now, rather than after the surviving spouse's death.

Multiple businesses operated as one

A personal representative operating multiple business entities in an estate as one integrated business enterprise is consistent with the policy behind Section 6166. As stated above, Section 6166(c) provides that where 20% or more of the total value of each of two or more businesses is included in determining the value of a decedent's estate, the decedent's interests in those closely held businesses are treated as an interest in a single closely held business.

In Rev. Rul. 75-367,[65] the decedent's business interests in several entities were found to be an interest in a single closely held business for purposes of the Section 6166 election. The decedent was a builder who:

1. Did home construction through a wholly owned small business corporation and through a sole proprietorship.
2. Conducted a real estate development and sales operation.
3. Owned a business office and warehouse, both of which were used by the corporation and the development and sales operation.
4. Owned and rented out several houses that he had built.

The IRS ruled that, while the rental activity consisted of mere investment assets and did not represent a business for Section 6166 purposes, the other three activities met the requisite threshold for business status. Therefore, because the decedent owned more than a 50% interest in each activity (as the statute then required), the IRS ruled that all three business activities should be

aggregated and treated as an interest in a single closely held business.

Furthermore, Section 6166(g)(1) specifically imposes a prohibition against distributions and withdrawals of money and other property from an interest in a qualifying closely held business *but only* if said distribution or withdrawal equals or exceeds 50% of the value of that interest. If the withdrawal is of less than 50%, or particularly, if the withdrawal is of current earnings accumulated after the inclusion of the estate, as explained in Ltr. Rul. 201403012, the distribution is allowed because it is completely outside the purview of Section 6166(g)(1) to begin with. If on the other hand the 50% threshold is exceeded, then the Section 6166(a) extension of time for the payment of tax ceases to apply and the tax due is accelerated.

Again, this 50% threshold analyzes the businesses held by the estate in the aggregate.[66] Thus, the statute specifically contemplates the aggregation of businesses and withdrawing funds from these businesses. Moreover, the statute does not mention and there is no negative inference associated with contributing distributed or withdrawn funds into other businesses.

As previously explained, in general, if an estate fails to pay principal or interest under Section 6166 on or before the date fixed for its payment (including any extension of time), the balance of the estate tax payable in installments is required to be paid upon notice and demand from the IRS under Section 6166(g)(3)(A). However, Section 6166(g)(3)(B) provides a reprieve if the unpaid principal or interest is paid within six months of the date fixed for its payment. In that case, the general rule of Section 6166(g)(3)(A) does not apply; the Section 6601(j) provision for determination of interest on the payment does not apply; instead there is imposed a penalty in an amount equal to the product of (1) 5% of the unpaid payment and (2) the number of months or fractions of months after the payment date and before payment is actually made. Thus, it is in the best interest of the estate and the personal representative that the estate is managed in such a manner as to produce sufficient funds so that installment tax obligations are paid timely and that no penalties are assessed.

There is an additional overarching reason for a personal representative to distribute and contribute money to another estate business, and thus, enhance the value of the entire estate. As described above, Sections 6166(k)(1) and 6165 permit the IRS to require a surety bond (not exceeding double the amount with respect to which the extension is granted) from an estate to ensure payment of the deferred estate tax. In lieu of the requirement to post a surety bond, the personal representative may elect to grant the IRS a special extended estate tax lien (in the amount of the deferred amount plus any interest, additional amount, addition to tax, assessable penalty, and costs attributable to the deferred amount) to secure the Government's interest.[67] This special lien does not expire until the earlier of the date the estate tax is paid in full or the tax becomes uncollectible.[68]

Pursuant to Notice 2007-90, two of the key factors that the IRS considers in requiring a bond or a special lien is the stability of the business and the ability to timely pay the deferred tax installments. A special IRS lien could inhibit the ability of an operating business to borrow funds from third-party lenders and potentially expose the underlying business to violation of partnership and lending covenants. Furthermore, a surety bond for a large sum could be very difficult to obtain. As a fiduciary of the estate, the personal representative has a duty to mitigate to the extent possible the imposition of the special lien or the posting of the bond. Commingling assets and contributing funds to other estate businesses is a valid strategy to mitigate the possibility of either a surety bond or a special lien.

Conclusion

While Section 6166 is very complex, over time Congress has enhanced the benefits of this Section for estates as it liberalized the rules, making it easier for estates to qualify and maintain the tax-deferral privilege. Today, this provision facilitates a personal representative's oversight of cash-management for multiple businesses in a flexible manner. The statutory scheme makes it easier to manage multiple businesses within an estate because when certain requirements are met, businesses with subsidiaries and brother-sister businesses owned individually are all treated as a single, closely held business under Section 6166. This liberal treatment permits personal representatives to easily deploy funds from one entity to another because under these tax rules, all of the entities are treated as a single, closely held business owned by the estate. ■

57 See Section 6166(a)(2).

58 See Section 6166(a)(1).

59 See Section 6166(f)(1).

60 See Sections 6166(a)(3) and 6166(f).

61 See Section 6601(j). For example, for estates of decedents dying in 2002, the interest rate on the unpaid tax is 2% on the tax attributable to the first $1.1 million of value of closely held business interests. The 2% interest rate applies to the first $484,000 of deferred tax.

62 See Section 6601(j)(1)(B). The current interest rate for underpayments is 4%. IR-2017-53, 3/7/2017.

63 See 1-7 *Planning for Large Estates* (Matthew Bender) § 7.07[6].

64 See *Id.* at § 7.07[3].

65 1975-2 CB 472.

66 See Reg. 20.6166A-3(d)(3), Example 3; Reg. 20.6166A-3(e)(6), Example 2.

67 Sections 6166(k)(2) and 6324A.

68 Sections 6324A(d)(2), 6052, and 6503(d).