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Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20044
Via the Federal eRulemaking Portal at http://www.regulations.gov/

Re: Section 67 Limitations on Estates and Trusts; REG-128224-06; 72 Federal Register 41243 (July 27, 2007).

To Whom It May Concern:

The Pennsylvania Bankers Association ("PBA") appreciates the opportunity to comment on the Internal Revenue Service's ("IRS") proposed amendments to regulation 26 CFR 1.67.

PBA is the statewide trade association representing over 200 commercial and savings banks, savings associations, bank and trust companies, trust companies and their subsidiaries and affiliates doing business in the Commonwealth of Pennsylvania.

Many PBA members provide fiduciary and related services to individual and institutional clients including trust administration, investment management, asset, tax preparation and accounting. They must follow strict duties of loyalty, prudence, and care to the trust and its beneficiaries. These services necessarily present risks and obligations for which banks charge fees that would be subject to the proposed amendments.

PBA's members are very concerned about this proposal and its profound effect on beneficiaries and the bank trust business.

BACKGROUND

In general, when computing a taxpayer's taxable income, miscellaneous itemized deductions are allowed only to the extent that they exceed 2 percent of the adjusted gross income ("AGI"). However, Section 67(e) of the Internal Revenue Code ("Code") makes an exception for certain costs that are incurred in connection with the administration of an estate or trust, and would not have been incurred if the property were not held in an estate or trust. Under this exception, these expenses may be deducted in full from the AGI. Recently, the IRS has challenged this exception through the courts.

The courts have interpreted Section 67(e) in various ways. During this term, the Supreme Court of the United States will consider this issue in *Knight v. Commissioner of Internal Revenue.*

This IRS regulatory proposal would delineate those expenses that are "unique" to the administration of a trust or estate and those that are not and provide that only those "unique" expenses may be deducted in full; whereas, those that are not would be subject to the 2 percent floor. The regulation further would require that an estate or non-grantor trust "unbundle" any fee charged into unique and not-unique portions to facilitate the deductions allowed under the proposal.

For a number of reasons, PBA respectfully opposes this proposal and urges the IRS to delay any regulatory consideration or action until after the Supreme Court has decided on the matter. First, the proposal misinterprets the plain meaning of Section 67 and what expenses may be deducted in full. Second, the proposal ignores the significant and extensive fiduciary responsibilities imposed by state law and the governing trust instrument on trustees. Third, not only is the proposal administratively impractical and extremely costly to implement, it may indirectly harm beneficiaries.

STATE LAW BASIS FOR OUR CONCERN

In Pennsylvania, fiduciary requirements have been codified in our version of the Uniform Prudent Investor Act ("UPIA") which allows the trustee to consider the prudence of a particular investment with regard to the entire investment portfolio.[1] This modern portfolio investment standard allows trustees to consider the risk tolerance of the beneficiaries, as well as the general purpose of the trust, when deciding what investments to make.

The law now allows trustees to invest the assets for total return without having to invest separately for income beneficiaries and remaindermen. Trustees are able and expected to invest in any number of investments, from stocks and bonds to far more-sophisticated and complex alternative investments. With the alternatives now available, trustees may have a fiduciary obligation to seek the advice of outside professionals who specialize in these particular investments.

When managing an investment portfolio, professional trustees face significant fiduciary liability, including court-ordered surcharge. Individuals managing their own investments are not subject to these risks. This clear risk differential between professional trustees and individuals *requires* the first to seek outside investment advice, but not the latter. This requirement surely makes professional fiduciaries' fees "unique" to trust administration and therefore fully-deductible.

PUBLIC POLICY CONCERNS

This proposal to require bank trust departments and others to "unbundle" the fees charged to administer trust accounts would be impractical and very costly to implement.

Separating the "unique" components of trust fees is a not only a time-consuming and difficult exercise, but would lead to the inequitable treatment of trust accounts and thus cannot be supported from a fiduciary standpoint.

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[1] Before the enactment of these prudent investor rules, trustees had been governed for over a hundred years by the far more conservative investing requirements of the "prudent man rule."

The expense of complying with the proposal would be significant. Bank trust departments may have to create yet another computer system to track, calculate, and separate the fees that are deductible from those that are not.[2] Such a system would have to be tested to ensure that it properly tracks the information, as well as adjusted periodically to accommodate new services the bank offers. Furthermore, the bank must institute on-going training programs for employees. All of these expenses would add up to a significant cost for all institutions. This expense is especially burdensome for smaller institutions which often have very small trust department staffs.

Under this IRS proposal, in addition to fulfilling their tax accounting and reporting duties, these trust department employees would have to spend their time "unbundling" trust fees for the previous tax year. This complex and time-consuming activity would likely delay other necessary tax reporting activities. In the end, this requirement will not only burden beneficiaries, banks, and other trustees, it would make the tax compliance system that less efficient.

CONCLUSION

PBA appreciates the opportunity to offer its comments on this Section 67 proposal. The IRS should delay its consideration until the Supreme Court has had an opportunity to consider the matter. But regardless of how the Supreme Court decides, we strongly urge the IRS to abandon this unbundling proposal due to its burdensome nature and insensitivity to the significant fiduciary duties of trustees.

Sincerely,

[2] The most-utilized bank trust department computer systems do not have the capability to "unbundle" and track the trust fees.