

Part I

Section 7701—Definitions

26 CFR 301.7701-4: Trusts

Rev. Rul. 2013-14

ISSUE

Is the fideicomiso or Mexican Land Trust arrangement (“MLT”), described below, a trust under Treasury Regulation § 301.7701-4(a)?

FACTS

The Mexican Federal Constitution prohibits non-Mexican persons from directly holding title to residential real property in certain areas of Mexico (“restricted zones”). Non-Mexican persons, however, may hold residential real property located in the restricted zones through an MLT with a Mexican bank after obtaining a permit from the Mexican Ministry of Foreign Affairs.

*Situation 1*

A, a U.S. citizen, is the sole owner of X, a limited liability company organized under the laws of state Z in the United States. X is disregarded as an entity separate

from its owner under § 301.7701-2(a) (a disregarded entity). A, through X, wanted to purchase Greenacre. Greenacre is Mexican residential real property located in a restricted zone. Neither A nor X may hold title directly to Greenacre under Mexican law.

X obtained a permit from the Mexican Ministry of Foreign Affairs and signed an MLT agreement with B, a Mexican bank. X negotiated the purchase of Greenacre directly with the seller of the property and paid the seller directly. The seller had no interactions with B with respect to the sale. At settlement, legal title to Greenacre was transferred from the seller to B, subject to the MLT agreement, as of the date of sale. No property other than Greenacre is subject to the MLT agreement.

Under the terms of the MLT agreement, X has the right to sell Greenacre without permission from B. Further, B must grant a security interest in Greenacre to a third party, such as a mortgage lender, if X so requests. X is directly responsible for the payment of all liabilities relating to Greenacre. X must pay any taxes due in Mexico with respect to Greenacre directly to the Mexican taxing authority. X has the exclusive right to possess Greenacre and to make any desired modifications, limited only by the need to obtain the proper licenses and permits in Mexico. If Greenacre is occasionally leased, X directly receives the rental income and A, as the owner of X, reports the income on A's U.S. federal income tax return.

Although B is identified as a fiduciary in the MLT agreement, it disclaims all responsibility for Greenacre, including obtaining clear title. B has no duty to defend or maintain Greenacre. B collects a nominal annual fee from X. There is no other agreement or arrangement between or among A, X, B, or a third party that would cause

the overall relationship to be classified as a partnership (or any other type of entity) for U.S. federal income tax purposes.

*Situation 2*

The facts are the same as in *Situation 1* except that X is a corporation organized under the laws of State Z in the United States. X is treated as a corporation under § 301.7701-2(a). If Greenacre is occasionally leased, X directly receives the rental income and reports the income on its U.S. federal income tax return.

*Situation 3*

The facts are the same as in *Situation 1* except that A deals directly with B without interposing X or any other entity. A obtained the permit from the Mexican Ministry of Foreign Affairs, signed the MLT agreement with B, and negotiated the purchase of Greenacre. Additionally, the provisions of the MLT agreement that apply to X in *Situation 1* instead apply to A. If Greenacre is occasionally leased, A directly receives the rental income and reports the income on A's U.S. federal income tax return. B collects a nominal annual fee from A. There is no other agreement or arrangement between or among A, B, or a third party that would cause the overall relationship to be classified as a partnership (or any other type of entity) for U.S. federal income tax purposes.

LAW AND ANALYSIS

Section 301.7701-1(a)(1) provides that whether an organization is an entity separate from its owners for federal tax purposes is a matter of federal tax law and does not depend on whether the organization is recognized as an entity under local law.

Section 301.7701-2(a) defines a “business entity” as any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under § 301.7701-3) that is not properly classified as a trust under § 301.7701-4 or otherwise subject to special treatment under the Code. If a business entity with only one owner is disregarded as separate from its owner, its activities generally are treated in the same manner as a sole proprietorship, branch, or division of the owner.

Section 301.7701-4(a) provides that the term “trust” refers to an arrangement created by a will or by an inter vivos declaration whereby trustees take title to property for the purpose of protecting or conserving it for the beneficiaries. Usually the beneficiaries of such a trust do no more than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. However, the beneficiaries of a trust may be the persons who create it, and it will be recognized as a trust if it was created for the purpose of protecting and conserving the trust property for beneficiaries who stand in the same relation to the trust as they would if the trust had been created by others for them. Generally, an arrangement is treated as a trust if it can be shown that the purpose of the arrangement is to vest in trustees the responsibility for the protection and conservation of property for beneficiaries who cannot share in the discharge of this responsibility.

Rev. Rul. 92-105, 1992-2 C.B. 204, addresses the transfer of a taxpayer’s interest in an Illinois land trust under § 1031. Under the facts of the ruling, an individual taxpayer created an Illinois land trust and named a domestic corporation as trustee.

Under the deed of trust, the taxpayer transferred legal and equitable title to the real property to the trust, subject to the provisions of an accompanying land trust agreement. The land trust agreement provided that the taxpayer retained exclusive control of the management, operation, renting, and selling of the real property, together with an exclusive right to the earnings and proceeds from the real property. Under the agreement, the taxpayer was required to file all tax returns, pay all taxes, and satisfy any other liabilities with respect to the real property. Rev. Rul. 92-105 concludes that, because the trustee's only responsibility was to hold and transfer title at the direction of the taxpayer, a trust, as defined in § 301.7701-4(a), was not established. The ruling holds that, on the facts described in the ruling, the trustee was a mere agent for the holding and transfer of title to the real property, and the taxpayer retained direct ownership of the real property for federal income tax purposes.

*Situation 1*

Because B's only duties under the MLT agreement are to hold the legal title to Greenacre and transfer title at the direction of X, the MLT is not a trust. X retains the right to manage and control Greenacre. X has the right to collect any rent on Greenacre. In addition, X has the obligation to pay directly any taxes and other liabilities due with respect to Greenacre. Accordingly, because X is treated as a disregarded entity under § 301.7701-2, A is treated as the owner of Greenacre.

### *Situation 2*

The MLT is not a trust, and the analysis is the same as in *Situation 1* except that, because X is treated as a corporation under § 301.7701-2(a), X is treated as the owner of Greenacre.

### *Situation 3*

Because B's only duties under the MLT agreement are to hold the legal title to Greenacre and transfer title at the direction of A, the MLT is not a trust. A retains the right to manage and control Greenacre. A has the right to collect any rent on Greenacre. In addition, A has the obligation to pay directly any taxes and other liabilities due with respect to Greenacre. Accordingly, A is treated as the owner of Greenacre.

### HOLDING(S)

In all three situations described above, the MLT is not a trust within the meaning of § 301.7701-4(a). If, under the MLT agreement, B holds legal title to any assets other than Greenacre or is permitted or required to engage in any activity beyond holding legal title to Greenacre, the holding of this revenue ruling does not apply and the rules of §§ 301.7701-1 through 301.7701-4 will determine the federal tax classification of the MLT.

### DRAFTING INFORMATION

The principal author of this revenue ruling is Wendy L. Kribell of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this revenue ruling, contact Ms. Kribell at (202) 622-3050 (not a toll-free call).