

WHY BUY AN IRREVOCABLE TRUST TO HOLD DINARS BEFORE REVALUATION?

You purchased the IQD in hopes of it revaluing and you becoming wealthy. It is more than having money to be wealthy. The wealthy do not pay taxes they don't have to pay and if there is a way of legally reducing that burden, they are going to take it. Isn't it time you started thinking like the wealthy?

Today, the holders of these and other under-valued currencies are eagerly awaiting the announcement of revaluations which would make them immensely wealthy. That is a wonderful anticipation to have, but is that the end of the story? Not if you are a resident of the United States of America. In the USA we have something called the Internal Revenue Code ("IRC"), which provides for taxes on various types of activities that generate something called 'income', not to mention on other activities and events such as duties on the importation of or bringing property into the country, tariffs, passing estates, tobacco and alcohol sales and manufacture and many others.

If something is considered "income" it is subject to the income tax and must be paid. "Income" is defined in Section 61 of the IRC. It is money that you earn by your physical and/or mental labor (wages, salary, commissions and professional fees). It is also profit from the operation of a business. This is pretty straight forward and is what most people think of as income. It is payable by "taxable entities". What are taxable entities? **You** are a taxable entity as are corporations and some LLCs. Irrevocable Trusts are taxable entities, but living trusts are not. Interest on debt obligations is "income" as are dividends from stock which is nothing more than a proportionate share of profit distributed to the owners of a corporation. Rent paid by tenants to the owner of the premises they occupy is income to the owner.

The profit people obtain for something they purchased and sold for more than they paid is under certain circumstances, "income." This kind of income is known as capital gain, and as such is subject to various rules, which ultimately determine if a tax is due, and if so; the rate of the tax. The rules for this kind of income are dependent on a number of factors, including, the "taxable entity" and the type of property it is. Most people consider capital gains as coming from the sale of stock or mutual funds at a profit. Profit from the sale of real estate is gain, and if it is for the sale of your principal residence it is subject to another set of rules which determine whether or not it is subject to tax, and if so, the rate. As you can see not all money is taxed the same way, in fact, if you borrow money, that money is not considered income at all, although the interest you pay on the loan to the lender is considered income to it. Which brings us to the point of this article.

Foreign currency trading is a growing source of income in today's world economy and there are many people who trade currency regularly and generate millions in profits. Because of this there are special sections in the IRC devoted to the taxation of foreign currency; Secs.

985-988 are the primary ones for the purpose of this discussion. If you are like most people who own IQD, you don't trade in futures, or pools, or straddles, you own the dinars and have them in your own possession. IRC Sec. 988(e) pertains to you, it provides:

Application to individuals

(1) In general. The preceding provisions of this section shall not apply to any section 988 transaction entered into by an individual which is a personal transaction.

(2) Exclusion for certain personal transactions. If nonfunctional currency is disposed of by an individual in any transaction, and such transaction is a personal transaction, no gain shall be recognized for purposes of this subtitle by reason of changes in exchange rates after such currency was acquired by such individual and before such disposition. The preceding sentence shall not apply if the gain which would otherwise be recognized on the transaction exceeds \$200.

(3) Personal transactions. For purposes of this subsection, the term "personal transaction" means any transaction entered into by an individual, except that such term shall not include any transaction to the extent that expenses properly allocable to such transaction meet the requirements of

(A) section 162 (other than traveling expenses described in subsection (a)(2) thereof), or,

(B) section 212 (other than that part of section 212 dealing with expenses incurred in connection with taxes).

In effect, if you own IQD or any other under-valued foreign currency in hopes that it will revalue, you will be taxed on the profit if it is over \$200.00. The owners of IQD will generate much more than \$200.00 if the IQD revalues at any significant amount as is hoped by the owners thereof.

A previous memorandum that was authored by Trusts Unlimited's counsel addresses the consequences resulting from waiting until after revaluation to create an irrevocable trust; going so far as to suggest that the mere creation of an irrevocable trust and transferring unexchanged IQD to the trust could trigger a tax on the mere transfer of the IQD even though no cash was actually received: a tax the grantor (**you** if you wait) would have to pay. This memorandum is available on the Trusts Unlimited web site and will not be repeated here. Suffice it to say, that is enough to justify the creation of an irrevocable trust pre-revaluation.

Other sections of the IRC may very well apply and they are Secs. 641¹, 643(3)² and 1221³. These sections deal with the taxation of irrevocable complex trusts which is what Trusts

ENDNOTES

Section 641 Imposition of Tax (Subchapter J, Part I, Subpart A—General Rules for Taxation of Estates and Trusts)

a) Application of tax The tax imposed by section 1 (e)[tax on taxable income of estates and trusts] shall apply to the taxable income of estates or of any kind of property held in trust, including

- (1) income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;
- (2) income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;
- (3) income received by estates of deceased persons during the period of administration or settlement of the estate; and
- (4) income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

² Section 643

(a) Distributable Net Income—For purposes of this part, the term “distributable net income” means, with respect to any taxable year, the taxable income of the estate or trust computed with the following modifications---

(3) Capital gains and losses

Gains from the sale or exchange of *capital assets* shall be excluded to the extent that such gains are allocated to corpus and are not

- (A) paid, credited, or required to be distributed to any beneficiary during the taxable year, or
 - (B) paid, permanently set aside, or to be used for the purposes specified in section 642 (c).
- Losses from the sale or exchange of capital assets shall be excluded, except to the extent such losses are taken into account in determining the amount of gains from the sale or exchange of capital assets which are paid, credited, or required to be distributed to any beneficiary during the taxable year. The exclusion under section 1202 shall not be taken into account.

³ Section 1221 Capital Asset Defined

(a) In general

For purposes of this subtitle, the term “capital asset” means property held by the taxpayer (whether or not connected with his trade or business), but does *not* include—

- (1) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;
- (2) property, used in his trade or business, of a character which is subject to the allowance for depreciation provided in section 167, or real property used in his trade or business;
- (3) a copyright, a literary, musical, or artistic composition, a letter or memorandum, or similar property, held by—
 - (A) a taxpayer whose personal efforts created such property,
 - (B) in the case of a letter, memorandum, or similar property, a taxpayer for whom such property was prepared or produced, or
 - (C) a taxpayer in whose hands the basis of such property is determined, for purposes of determining gain from a sale or exchange, in whole or part by reference to the basis of such property in the hands of a taxpayer described in subparagraph (A) or (B);
- (4) accounts or notes receivable acquired in the ordinary course of trade or business for services rendered or from the sale of property described in paragraph (1);
- (5) a publication of the United States Government (including the Congressional Record) which is received from the United States Government or any agency thereof, other than by purchase at the price at which it is offered for sale to the public, and which is held by—
 - (A) a taxpayer who so received such publication, or
 - (B) a taxpayer in whose hands the basis of such publication is determined, for purposes of determining gain from a sale or exchange, in whole or in part by reference to the basis of such publication in the hands of a taxpayer described in subparagraph (A);
- (6) any commodities derivative financial instrument held by a commodities derivatives dealer, unless—

Unlimited's Trusts are, how "capital assets" are defined and when read in conjunction with one another might enable those who own their IQD in irrevocable trusts to defer their gain when exchanged.

Trusts Unlimited is unaware of any cases, regulations, private letter rulings (PLR) or regulation rulings (Reg. Rul) which might affect treatment of profit from the exchange of highly appreciated foreign currency, either pro or con, so this article does not undertake to promote it as such. However, it should be remembered that the IRC places a great deal of emphasis on the meanings and usage of words. In Sec. 988(e) it refers to the profit derived from the exchange of appreciated foreign currency as **gain**. It is significant to note that while Sec. 988(a-f) treats profit related to foreign currency as **ordinary income**, the very first sentence in 988 reads: "***The preceding provisions of this section shall not apply to any section 988 transaction entered into by an individual which is a personal transaction***". Since IQD held as assets of an irrevocable,

(A) it is established to the satisfaction of the Secretary that such instrument has no connection to the activities of such dealer as a dealer, and

(B) such instrument is clearly identified in such dealer's records as being described in subparagraph (A) before the close of the day on which it was acquired, originated, or entered into (or such other time as the Secretary may by regulations prescribe);

(7) any hedging transaction which is clearly identified as such before the close of the day on which it was acquired, originated, or entered into (or such other time as the Secretary may by regulations prescribe); or

(8) supplies of a type regularly used or consumed by the taxpayer in the ordinary course of a trade or business of the taxpayer.

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complex trust could be considered a capital asset, it is arguable that Secs. 641 and 643 could operate to defer any gain resulting from the revaluation and exchange of IQD or any other undervalued currency for that matter until it is distributed to the beneficiaries of the trust. Probably the best course of action might be to treat the profit as ordinary income, pay the tax and then seek a refund either directly from the IRS, or through action in the U.S. District Court. In this way, if the Service or the Court agrees, you could get a refund, and if it disagrees, you will not be penalized for failing to pay. The thing to keep in mind is that without a funded irrevocable, complex trust in effect before a revaluation, you will not be able to take advantage of any of these sections, and would have to pay the tax yourself without any deferral whether it is considered capital gain or ordinary income, not to mention the possibility of a personal audit.