IRS MEMO AM 2023-006:
How It Fails the Accounting Community

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The Internal Revenue Service's issuance of Memorandum AM 2023-006 has reignited debate over the proper taxation of non-grantor, irrevocable, complex, discretionary, spendthrift trusts (NGICDS trusts). While presented as a measure to curb perceived abuses, the memorandum rests on a mischaracterization of both statutory law and constitutional limits and fails to account for decades of established fiduciary principles and judicial precedent. Its conclusions—particularly those that suggest all gross receipts in such trusts must eventually be taxed—are in fundamental tension with the foundational doctrines of trust law, the Internal Revenue Code, and the U.S. Constitution.

At the center of this controversy is the attempt to blur the line between income and corpus, an act which if allowed to stand, would undermine the integrity of estate and trust planning across the nation. NGICDS trusts are sophisticated legal instruments created to achieve lawful tax deferral, protect wealth, and administer intergenerational estate plans. Their core structure allows trustees to allocate passive income—such as dividends, royalties, capital gains, rents, and interest—to corpus when supported by the governing instrument and applicable state law. This allocation is not a loophole or evasion mechanism; it is an express feature of both Subchapter J of the Internal Revenue Code and the fiduciary frameworks recognized under state law and reinforced by Treasury regulations.

Internal Revenue Code §643(b) and Treasury Regulation §1.643(a)-3 provide trustees with the authority to classify extraordinary dividends and similar receipts as principal. When done in good faith, in compliance with the trust instrument and relevant fiduciary duties, such classification places the income outside the scope of Distributable Net Income (DNI). As DNI serves as the conduit through which trust income is passed to beneficiaries and subsequently taxed, any receipt not included in DNI is excluded from current income taxation. The trustee's lawful discretion in this regard is essential to the integrity of trust administration.

The IRS memorandum sidesteps this reality by assuming that gross income received by the trust must be taxed at some point, regardless of whether it has been lawfully allocated to corpus and retained. This presumption ignores the design of NGICDS trusts, which do not create DNI and do not make distributions that carry out taxable income. Instead, they accumulate corpus for long-term strategic objectives, deferring taxation until, and only if, distributions are made that carry out income. In structures where no distributions of DNI occur and only principal is disbursed, the income is never taxed to either the trust or its beneficiaries.

The constitutional underpinnings of this framework cannot be ignored. The Sixteenth Amendment empowers Congress to tax "incomes, from whatever source derived," but this power is not without limitation. In Eisner v. Macomber (1920), the Supreme Court made clear that income requires a realization event. Mere changes in the form or ownership of capital within a trust do not constitute taxable income. This realization principle was further reinforced in

Commissioner v. Glenshaw Glass Co. (1955), where the Court articulated that income must reflect an undeniable accession to wealth, clearly realized, and over which the taxpayer has complete dominion. Corpus distributions—particularly those arising from principal allocations made under fiduciary authority—fail this test.

Judicial precedent also resists the IRS's expansive interpretation. In Estate of German v. United States (1985), the court upheld the trustee's decision to allocate extraordinary dividends to corpus and ruled that such allocations, when made in accordance with the trust instrument and applicable state law, do not generate DNI and therefore do not create taxable events upon distribution. This principle was reaffirmed in Helvering v. Stuart (1942), which emphasized the importance of trustee discretion and fidelity to the governing instrument in determining the character of trust receipts.

Even earlier, in Nichols v. Eaton (1875), the Supreme Court upheld the validity of spendthrift provisions and recognized the inviolability of trust structures designed to preserve capital from external claims and premature taxation. These decisions collectively form a consistent judicial message: where trustees act within their lawful authority to allocate receipts to corpus, and where those receipts are never converted into distributions of income, there is no trigger for taxation.

The IRS's attempt to dismiss these foundational elements by using vague terminology such as "self-styled trusts" only adds confusion. If the memorandum addresses self-settled or grantor trusts, its conclusions are irrelevant to truly independent, third-party-created NGICDS trusts. If it attempts to apply its conclusions to all non-grantor complex trusts, then it mistakenly collapses two fundamentally distinct legal categories and spreads undue fear across the estate planning community.

This ambiguity is compounded by the memorandum's neglect of the Uniform Principal and Income Act (UPIA), a core component of fiduciary law adopted in many jurisdictions. UPIA grants trustees the authority and responsibility to balance the interests of income and remainder beneficiaries by allocating receipts in accordance with fairness and the trust's intent. The IRS cannot override this statutory mandate with administrative fiat. In Freuler v. Helvering (1934), the Supreme Court explicitly held that the IRS must respect fiduciary accounting choices made in good faith and pursuant to local law.

Equally troubling is the IRS's historical inconsistency. For years, its own training materials have acknowledged that Trust Accounting Income (TAI) is not determined by the IRS but by the trustee under local law and the trust document. This tacit admission was included in internal IRS presentations—specifically, a PowerPoint that was once publicly available on the IRS website, which stated that the IRS does not define or control TAI. Notably, the IRS deleted this PowerPoint presentation approximately one month after the release of AM 2023-006. This act raises significant questions about the timing and intent of its removal. Was the IRS attempting to erase a contradictory position in light of its new memorandum? At minimum, it reveals an internal inconsistency that undermines the IRS's credibility and highlights a lack of transparency.

The trustee's discretion, rooted in statutory authority and case law, allows for income to be classified as extraordinary and lawfully allocated to principal. When a trust earns passive income and the trustee, using fiduciary judgment and proper documentation, allocates that income to corpus, there is no realization of income and no DNI. If such corpus is later distributed, it is not income, it is capital. This simple truth aligns with the text of the Internal Revenue Code, Supreme Court doctrine, and the original understanding of the Sixteenth Amendment.

Trusts that operate within these legal boundaries do not issue K-1s, do not deduct distributions, and do not pass income through to beneficiaries. Their design is based not on avoidance, but on compliance—compliance with the Constitution, with Subchapter J, and with fiduciary law. Any IRS attempt to override this framework by administrative memorandum, particularly one lacking clarity, statutory support, and constitutional grounding, should be viewed with skepticism.

Professionals working with NGICDS trusts should continue to rely on rigorous documentation, well-drafted governing instruments, and a clear understanding of both federal tax principles and state fiduciary laws. The courts have repeatedly supported their discretion. The statutes affirm their authority. The Constitution limits the power of the IRS to tax beyond the boundaries of income. All three branches of government have provided the tools to resist the encroachment implied by AM 2023-006.

Furthermore, estate planners, fiduciaries, and tax professionals must remain vigilant against fear-based interpretations that threaten well-established practices. The overwhelming weight of judicial precedent supports the legitimacy of properly administered NGICDS trusts. Cases like Markosian v. Commissioner (1979) demonstrate that courts will honor the substance of fiduciary behavior and the intent of trust provisions when those are executed faithfully. Courts consistently favor genuine adherence to fiduciary law over form-driven allegations of abuse.

When fiduciaries allocate extraordinary dividends—large, irregular, or non-recurring payments stemming from corporate liquidations, stock redemptions, or restructuring events—to corpus, they are not evading tax, but preserving capital in accordance with centuries of trust doctrine. The trust's governing instrument, often drafted with considerable precision and professional counsel, typically provides explicit authority to make such allocations. Moreover, courts have emphasized that capital distributions do not become income merely by passing through a fiduciary entity.

The IRS's neglect of this deep legal context threatens to create an environment in which legitimate trust planning is chilled or discouraged. The memo's failure to provide clear guidance—relying instead on broad generalizations and undefined terminology—leaves fiduciaries without practical direction and places undue risk on those seeking to operate within the bounds of the law.

Additionally, the absence of any meaningful statutory remedy within AM 2023-006 only compounds the problem. The memorandum purports to identify improper tax behavior but offers no path forward, no clarification, and no distinction between compliant and noncompliant practices. This void of constructive guidance reflects a broader failure: the IRS's inability to acknowledge its own historical acceptance of corpus allocation and its current unwillingness to separate legitimate trusts from abusive arrangements.

Education and transparency must become the cornerstones of response to AM 2023-006. Tax professionals should advocate for proper interpretation of Subchapter J, for respect of fiduciary discretion under UPIA, and for the preservation of constitutionally protected principles such as realization and capital classification. The wealth management industry must not permit ambiguous administrative positions to erode long-standing doctrines that preserve the integrity of fiduciary relationships.

In the end, the IRS memorandum is not law. It is a position. And like all administrative interpretations that fail to align with statutory text, constitutional doctrine, and judicial precedent, it must be met with well-grounded resistance. If unchecked, AM 2023-006 risks becoming a tool of intimidation rather than guidance. Its misuse of language and omission of nuance have already confused both professionals and the public. The path forward is to reaffirm the central tenets of trust law—discretion, documentation, separation of corpus and income, and the requirement of realization before taxation. Only by doing so can fiduciaries continue to fulfill their duties and uphold the legal structures that have served American families for generations.