INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

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CASE MIS No.: TAM-161842-01/CC:PSI:B04

District Director:

Taxpayer's Name:

Taxpayer's Address:

Taxpayer's Identification No:

Date of Conference:

LEGEND:

Decedent	=
Spouse	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Marital Trust	=
Family Trust	=
County Court	=
State	=
State Disclaimer Statute	=
a	=
b	=
c	=
Citation 1	=
Citation 2	=

ISSUE(S):

Whether the terms of Decedent's will provide the surviving spouse (Spouse) with a qualifying income interest for life in the Marital Trust within the meaning of section 2056(b)(7)(B)(ii) of the Internal Revenue Code.

CONCLUSION:

The terms of Decedent's will do not provide Spouse with a qualifying income interest for life in the Marital Trust.

FACTS:

Decedent died on Date 2. Sections 2.01 through 2.03 of Decedent's will, executed on Date 1, provided for several specific bequests to Spouse.

Section 2.04 provides that if Spouse survives Decedent, the executor shall select an amount of cash or property, to be referred to as the "Marital Deduction Amount," to be held in Marital Trust. This bequest shall be referred to as the "Marital Deduction Bequest." Section 2.05 provides that the remainder of Decedent's estate, excluding specific bequests of $a to each of Decedent's living grandchildren, will be held in Family Trust.

Section 3.01 provides that the trustee shall pay the entire income of Marital Trust to Spouse in quarterly or more frequent installments. Section 3.02 provides that the trustee shall make supplemental distributions of principal of Marital Trust as needed to provide Spouse with a total minimum monthly payment of $b with adjustments for inflation, after taking into account Spouse's income from Marital Trust and Family Trust. To the extent the distributed income does not provide the required minimum monthly payment, the trustee shall make supplemental principal distributions. In addition, the trustee may make supplemental distributions of principal for Spouse's health, maintenance, and support in accordance with her station in life, considering all other sources of income available to Spouse.

Section 3.03 provides as follows:

> My wife, acting in her individual capacity, shall have a limited power to appoint by lifetime instrument or by Will, to appoint the income and the principal of the Marital Trust to or for the benefit of any one or more of my children or more remote descendants; provided that such power of appointment shall not extend to any life insurance policies insuring the life of my wife that constitute a part of the trust estate of the Marital Trust.
>
> This power of appointment may be exercised subject to such terms and conditions as my wife shall direct, including an appointment in trust. Any exercise of this power of appointment must be made, either in an acknowledged written instrument delivered to the Trustee, or in a duly

> probated Will, either of which to be effective must refer specifically to the power granted under this Section of my Will.

Section 3.04 provides that Marital Trust shall terminate on the date of Spouse's death. Upon termination, the trustee shall distribute to Spouse's estate an amount equal to the increased estate taxes payable by reason of inclusion of the assets of Marital Trust in Spouse's estate. After making such payments, and subject to Spouse's exercising the limited power of appointment, the remaining assets of Marital Trust shall be distributed to Decedent's children per stirpes.

Section 3.05 provides as follows:

> It is my intention that the provisions of the Marital Trust relating to the distribution, termination, investment, and administration of the Marital Trust be construed so as to permit properties passing to be eligible for the federal estate tax marital deduction if my Executor shall elect under the provisions of section 2056(b)(7) of the Code, or any successor statute, to have property passing to the Marital Trust qualify for the federal estate tax marital deduction. If my Executor makes such an election with respect to all or any portion of the trust estate of the Marital Trust, the Trustee shall have no power, express or implied, to administer the Marital Trust in a manner which would lead to the disqualification of property passing to such trust for which such election is made as "qualified terminable interest property" for federal estate tax purposes.

Section 4.01 provides that the trustee shall pay the net income of Family Trust to Spouse in quarterly or more frequent installments while Spouse is living. After the death of Spouse, the trustee shall pay at convenient intervals, at least as often as annually, all of the net income to Decedent's grandchildren, with the descendants of any deceased grandchild taking, per stirpes the share of income that the deceased grandchild would have received if living.

Section 4.02 provides that if the assets of Marital Trust have been distributed and exhausted, the trustee shall make supplemental distributions of principal of Family Trust to provide the minimum monthly payment of $b per month as provided in section 3.02. In addition, after the assets of Marital Trust have been distributed, the trustee may make supplemental distributions of principal of Family Trust for Spouse's health, maintenance, and support in accordance with her station in life, considering all other sources of income available to Spouse.

Section 11.01.A provides that the "Marital Deduction Amount" is a pecuniary amount equal to the smallest amount which, if allowed as an estate tax marital deduction under section 2056 would result in the least possible federal estate tax being payable by reason of Decedent's death.

Section 11.01.D provides that any property used in satisfying the Marital Deduction Bequest shall be property or the proceeds of property the value of which is included in Decedent's gross estate, and must be of a character which would qualify for allowance of the federal estate tax marital deduction. To the extent that the bequest cannot be satisfied with such qualifying property, this bequest shall abate.

Section 11.03 provides that the executor shall have the sole and absolute discretion to elect in whole or in part for the property passing to the Marital Trust to qualify for the federal estate tax marital deduction.

Section 11.04 provides that Spouse shall have a right to require the trustee to either make Marital Trust assets productive or to convert them into productive assets within a reasonable time.

Section 12.01 provides that if any provision of the will or any codicil thereto is held to be inoperative, invalid, or illegal, it is Decedent's intention that all remaining provisions thereof shall continue to be fully operative and effective as far as is possible and reasonable.

As noted above, Decedent died on Date 2. On Date 4, Spouse, as Decedent's executrix, filed the federal estate tax return for Decedent's estate. On Schedule M of the estate tax return, Spouse elected under section 2056(b)(7) to treat the assets totaling $c passing to the Marital Trust as qualified terminable interest property (QTIP) and claimed a marital deduction for that amount.

On Date 5, more than nine months after Date 2, Spouse executed and filed "Disclaimer" with County Court. Spouse's "Disclaimer" provided as follows:

> I, [Spouse], do hereby confirm that I, by the signing and filing of Form 706, United States Estate Tax Return, for the Estate of [Decedent], on or before [Date 3], in which I made an election to take a deduction on Schedule M thereof for the value of the assets used to fund the [Marital Trust] under Section 2056(b)(7) of the Internal Revenue Code, disclaimed and renounced any power which may have been given to me under the terms of the Will of [Decedent] which would in any way disqualify the property passing to the [Marital Trust] for the deduction taken on Schedule M of the Federal Estate Tax Return, including the power given to me under Section 3.03 of the Will to "appoint by lifetime instrument" any interest in the income and principal of the [Marital Trust].
>
> Furthermore, I do hereby again disclaim and renounce any power which I may still have under Section 3.03 of the Will to "appoint by lifetime instrument" any interest in the income and principal of the [Marital Trust].
>
> It is my intention to confirm that I have made a "qualified disclaimer" of the above described power as that term is defined by the Internal Revenue Code and the regulations promulgated thereunder and as permitted by [State Disclaimer Statute], as amended. This disclaimer is an unqualified refusal to accept the above described power and is irrevocable.

LAW AND ANALYSIS:

Section 2001(a) of the Internal Revenue Code imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2031 provides that the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated.

Section 2056(a) provides that, for purposes of the tax imposed by section 2001, the value of the taxable estate is to be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse.

Section 2056(b)(1) provides, in pertinent part, that no deduction shall be allowed under section 2056(a) where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail.

Section 2056(b)(7) provides an exception to the rule of section 2056(b)(1) in the case of qualified terminable interest property. Under section 2056(b)(7)(A), qualified terminable interest property (QTIP) is treated as passing to the surviving spouse for purposes of section 2056(a), and no part of the property is treated as passing to any person other than the surviving spouse for purposes of section 2056(b)(1).

Section 2056(b)(7)(B)(i) provides that the term “qualified terminable interest property” means property: (I) which passes from the decedent; (II) in which the surviving spouse has a qualifying income interest for life; and (III) to which an election under section 2056(b)(7)(B)(v) applies.

Under section 2056(b)(7)(B)(ii), the surviving spouse has a qualifying income interest for life in the trust property if: (I) the surviving spouse is entitled to all of the income from the property payable annually or at more frequent intervals, and (II) no person has a power to appoint any part of the property to any person other than the surviving spouse, while the surviving spouse is alive.

Section 20.2056(b)-7(d)(1) of the Estate Tax Regulations provides that for purposes of section 2056(b)(7)(B)(ii)(II), the surviving spouse is included within the prohibited class of power holders.

Section 20.2056(b)-7(d)(6) provides that an income interest in a trust will not fail to constitute a qualifying income interest for life solely because the trustee has a power to distribute principal to or for the benefit of the surviving spouse.

Section 2056(b)(7)(B)(v) provides that an election under section 2056(b)(7) with respect to any property shall be made by the executor on the return of tax imposed by section 2001. Such an election, once made, shall be irrevocable.

Section 20.2056(b)-7(h) Example 4 considers a situation where a trustee is given the power to distribute corpus to beneficiaries other than the surviving spouse. The example concludes that the property passing to the trust is not deductible under section 2056(b)(7). In addition, the example states that the trust property would not be deductible under section 2056(b)(7) if the surviving spouse, rather than the trustee, held the power to appoint. However, if the surviving spouse made a qualified disclaimer (within the meaning of section 2518) of the power to appoint, the trust could qualify for the marital deduction pursuant to section 2056(b)(7), assuming that the power is personal to the surviving spouse and surviving spouse's disclaimer terminates the power.

Section 2518(a) provides that, if a person makes a qualified disclaimer of an interest in property, the estate, gifts, and generation-skipping transfer tax provisions will apply to that interest as if it had never been transferred to such person.

Under section 2518(b), the term "qualified disclaimer" means an irrevocable and unqualified refusal by a person to accept an interest in property, provided: (1) the disclaimer is in writing; (2) the disclaimer is received by the transferor of the interest, his legal representative, or the holder of legal title to the property, not later than the date which is 9 months after the later of the date on which the transfer creating the interest is made or the date on which the person refusing the interest attains age 21; (3) the person disclaiming the interest has not accepted the interest or any of its benefits; and (4) as a result of the disclaimer, the interest passes without any direction by the person making the disclaimer and passes either to the spouse of the decedent or to a person other than the person making the disclaimer.

Section 25.2518-2(b)(1) of the Gift Tax Regulations provides that a writing must identify the interest in property disclaimed and must be signed either by the disclaimant or by the disclaimant's legal representative to be a qualified disclaimer.

State Disclaimer Statute provides that: a disclaimer must be in writing and notarized; a disclaimer must be filed in the probate court (if administration has commenced) not later than nine months after the decedent's death; copies of the disclaimer must be delivered and received by the legal representative of the transferor of the property of the property to which the disclaimer relates not later than nine months after decedent's date of death; and any disclaimer filed and served must be irrevocable.

For state law purposes, a disclaimer is effective and irrevocable only if the elements of the disclaimer statute are satisfied. See Citation 1.

The will provides Spouse with a lifetime and testamentary special power to appoint the income and principal of the Marital Trust to or for the benefit of Decedent's

descendants. The taxpayer does not dispute that Spouse was granted a lifetime power of appointment. This fact is further evidenced by the "Disclaimer" filed by Spouse in which Spouse attempts to disclaim her lifetime power of appointment in order to satisfy the requirements of section 2056(b)(7). Section 2056(b)(7)(B)(ii) requires that no person, including Spouse, have a power to appoint any part of the property to any person other than Spouse, while Spouse is alive. Because Spouse has a lifetime power of appointment, Spouse does not have a qualifying income interest for life with respect to the Marital Trust under Decedent's will. Accordingly, Decedent's estate would not be allowed a marital deduction for assets passing into the Marital Trust.

The estate makes three separate arguments in support of its position that the estate is entitled to a marital deduction for the assets passing to the Marital Trust, despite Spouse's lifetime special power of appointment.

The estate's first argument is that a marital deduction should be allowed because section 3.05 of the will contains provisions precluding the trustee from administering the Marital Trust in any manner that would disqualify the Marital Trust for the estate tax marital deduction. Generally, savings clauses of this nature, which purport to void a trustee power or direction that would disqualify the trust for marital deduction purposes are not effective for transfer tax purposes. Commissioner v. Procter, 142 F. 2d 824 (4th Cir. 1944), cert. denied, 393 U.S. 756 (1944); Rev. Rul. 65-144, 1965-1 C.B. 442. However, these provisions may be used as an aid in determining testator's intent where the instrument presents an ambiguity. For example, in Rev. Rul. 75-440, 1975-2 C.B. 372, the instrument provided for the creation of two trusts and it was not clear whether a provision authorizing the trustee to invest in life insurance applied to one or both trusts. In such a case, the savings clause is an aid in determining the testator's intent.

In this case, the provision granting Spouse a lifetime power of appointment is clearly set forth in the section of the will creating the Marital Trust. Thus, no ambiguity is presented with respect to which the savings clause could serve as an aid in construction, as was the case in Rev. Rul. 75-440. To put it another way, for transfer tax purposes, the savings clause is not effective and does not operate to create an ambiguity in the instrument. It may only be used as aid in interpreting an instrument where an ambiguity is present in another part of the instrument.

Further, the savings clause purports to invalidate only executor and trustee powers that would disqualify the Marital Trust for the marital deduction. The will does not purport to invalidate dispositive provisions that might disqualify the Marital Trust for the marital deduction. Even if we were to give the savings clause any effect in determining Decedent's intent, the savings clause would be ineffective to invalidate Spouse's lifetime power of appointment.

The mere fact that Decedent may have intended that the Marital Trust qualify for the marital deduction does not mean that it does so qualify. See United States v. First Nat'l Trust & Sav. Bank, 335 F. 2d 107, 113-14 (9th Cir. 1984); Estate of Walsh v.

Commissioner, 110 T.C. 393, 402 (1998). The courts do not have the power to change the dispositive terms of the instrument, to remake the trust, or to take property from one beneficiary and give it to another. See Bogert, The Law of Trusts and Trustees (2d Ed. Rev. 1980) § 561 at n. 29. The requirements of section 2056(b)(7) must be satisfied. Spouse's power of appointment is incompatible with the requirements of section 2056(b)(7) and only a timely disclaimer of the power of appointment would have changed this result.

The estate's second argument is that Spouse effectively disclaimed her lifetime power of appointment by timely filing a federal estate tax return which claims a marital deduction under section 2056(b)(7). The estate argues that by filing this estate tax return, Spouse effectively disclaimed any interest that would be inconsistent with the marital deduction. If Spouse effectively disclaimed her lifetime power of appointment, the Marital Trust should qualify for the estate tax marital deduction, as in Example 4 of section 20.2056(b)-7(h).

In order to satisfy the requirements of section 2518(b), a disclaimer must be valid under applicable local law. Estate of Darcy v. Commissioner, 872 F. 2d 84 (4th Cir. 1989). That is, because state law determines whether a property interest passes from one to another, the disclaimer must constitute an effective disclaimer under state law. Estate of Bennett v. Commissioner, 100 T.C. 67 (1993). In this case, the return and the subsequently filed "Disclaimer" do not satisfy the requirements of state law or section 2518(b).

Under state law and section 2518(b), the disclaimer must be a written irrevocable and unqualified refusal by a person to accept an interest in property. Nowhere on the return is there any statement by Spouse that she irrevocably and unqualifiedly refuses to accept the lifetime power of appointment. Nor was the return filed with County Court. Therefore, the return is not a disclaimer for purposes of section 2518(b).

The "Disclaimer," which Spouse filed and executed on Date 5, was not executed or filed within nine months from the date of Decedent's death (the date on which the transfer creating the interest in Spouse was made). Therefore, for purposes of state law and section 2518(b), Spouse has not disclaimed the lifetime power of appointment.

The estate's third argument is that if the Marital Trust does not qualify for the marital deduction, then under section 11.01.D the bequest abates and becomes part of the Family Trust pursuant to section 2.05 of the will. The estate further argues that because the Family Trust provides Spouse with an income interest for life, the assets in the Family Trust could qualify as QTIP.

The interpretation of a will is a matter of state law. In Commissioner v. Estate of Bosch, 387 U.S. 456 (1967), the Court concluded that the decision of a state trial court as to an underlying issue of state law should not be controlling when applied to a federal statute. Rather, the highest court of the state is the best authority on the underlying substantive rule of state law to be applied in the federal matter. If there is no

decision by that court, then the federal authority must apply what it finds to be state law after giving "proper regard" to the state trial court's determination and to relevant rulings of other courts of the state. In this respect, the federal agency may be said, in effect, to be sitting as a state court.

In construing a will, the court's focus is on the testator's intent. This intent must be ascertained from the language found within the four corners of the will. The court should focus not on what the testator intended to write, but the meaning of the words he actually used. In this light, courts must not redraft wills to vary or add provisions under the guise of construction of the language of the will to reach a presumed intent. See Citation 2.

The abatement clause in section 11.01.D of Decedent's will applies only if the property passing to the Marital Trust is of a character which would not qualify for the federal estate tax marital deduction. The "character" of the property would include such considerations as whether the property is income producing and whether it is property that would cease to provide income following a term certain to expire prior to Spouse's death. We do not interpret the clause to extend to powers granted to Spouse under the will. Rather, the clause provides a direction to the trustee regarding what property may be used to fund the Marital Trust. Therefore, the bequest to the Marital Trust would not abate under this provision.

For the above reasons, we conclude that the terms of Decedent's will do not provide Spouse with a qualifying income interest for life in the Marital Trust. Therefore, the Marital Trust would not qualify for the marital deduction under section 2056(b)(7).

CAVEAT:

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(k)(3) provides that it may not be used or cited as precedent.