Internal Revenue Service

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Legend

Taxpayer =
Trust =

Partnership =
Company =
Agreement =
Partnership Interest =

a =
b =
c =
d =
e =
f =
g =

Dear

This letter responds to your request, dated June 20, 2002, requesting rulings with respect to the transfer of certain property under the following circumstances.

Taxpayer is an individual aged a, who owns a real estate investment organization that provides a full range of services including acquisitions, planning, development leasing, property management and project management. Taxpayer proposes to transfer his interest in a partnership to the Trust in exchange for a private annuity that will provide fixed annual payments for his lifetime.

The Trust was established in Year 1, and the beneficiaries of the Trust are the grandchildren of Taxpayer. The Trust's assets consist of publicly traded stocks with a value of approximately b and real estate holdings with an approximate value of c. The Trust's only liability is a note payable in the amount of d.

The Partnership owns e% of the outstanding stock in the Company that owns interests in entities that own real estate. Taxpayer's Partnership Interest has a fair market value of f, and his basis in the Partnership Interest is g.

Pursuant to the Agreement, Taxpayer will irrevocably transfer his partnership interest to the Trust in exchange for the Trust's obligation to pay Taxpayer, upon 60 days demand, an annual annuity. The amount of the annuity payments will be calculated pursuant to applicable Internal Revenue Service and Tables to equal the value of the Partnership Interest on the date of the transfer. Pursuant to the terms of the Agreement, the annuity payments from the Trust to the Taxpayer shall terminate and lapse with the last payment immediately preceding the Taxpayer's death or upon the death of the Taxpayer if no payments have been made prior to the Taxpayer's death. The Trust's obligation to make the annuity payments will not be secured by any assets owned by the Trust and the Trust will not establish any security or any fixed or other specific chargeable source for the payment of the annuity to Taxpayer. However, the Trustee is authorized to invade or dispose of Trust principal in order to meet the annuity obligations.

LAW AND ANALYSIS

An annuity is a periodic amount paid at a regular interval under an annuity contract which provides a determinable amount of payments in consideration for a fixed sum or a transfer of property. See, section 1.72-2 of the Income Tax Regulations. A private annuity is generally an arrangement whereby an individual or entity promises to make periodic payments to the transferor for the remaining life of the transferor.

Section 1275(a)(1)(B), in pertinent part, provides that the term debt instrument does not include any annuity contract to which section 72 applies which depends (in whole or in substantial part) of the life expectancy of one or more individuals. Section 1.1275-1(j)(2)(i) provides that for purposes of section 1275(a)(1)(B)(i) an annuity contract depends (in whole or in substantial part) on the life expectancy of one or more individuals only if (i) the contract provides for periodic distributions made not less frequently than annually for the life (or joint lives) of an individual (or a reasonable number of individuals); and (ii) the contract does not contain any terms or provisions that can significantly reduce the probability that total distributions under the contract will increase commensurately with the longevity of the annuitant (or annuitants). Paragraphs (3) through (7) of section 1.1275-1(j) describe certain terms and conditions that can significantly reduce the probability that total distributions under the contract will increase commensurately with the longevity of the annuitant (or annuitants). Those terms and conditions are (1) the availability of a cash surrender option; (2) the availability of a loan secured by the contract; (3) a minimum payout provision; (4) a maximum payout provision; and (5) a decreasing payout provision.

In the instant case, the parties represent that at the time the Agreement becomes effective, it will be their intent that Taxpayer will receive annuity payments over his lifetime beginning on an agreed starting date within the period of the Taxpayer's life expectancy determined under the applicable Tables. On the annuity starting date, the annuity payments will be made at least annually. The Agreement does not contain any terms that will significantly reduce the probability that the total annuity payments to the Taxpayer will increase commensurately with longevity.

CONCLUSION

Based upon the facts presented, and the representations of the Taxpayer, we conclude that the private annuity obligation is excepted from the definition of debt instrument and the original issue discount provisions of section 1275.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Donald J. Drees
Senior Technician Reviewer, Branch 4

Office of Office of Associate Chief Counsel
(Financial Institutions & Products)