Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

[Third Party Communication:
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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B09
PLR-155335-05

Date:
March 15, 2006

In Re:

Legend

Decedent	=
Spouse	=
Child	=
Possession	=
State	=
Date 1	=

Dear Executors:

This is in response to your letter dated October 26, 2005, and subsequent correspondence, requesting a ruling regarding the credit under § 2014 of the Internal Revenue Code for Decedent's estate.

Decedent was a United States citizen domiciled in State, who owned assets in Possession. Decedent died on Date 1, survived by Spouse and children. Article Second of Decedent's will provides that Spouse is to receive Decedent's articles of tangible personal property.

Article Fourth provides that the residuary of Decedent's estate is to be held in trust for the benefit of Spouse and Child. During Spouse's lifetime, Spouse is to receive all of the net income of the trust at least quarterly. Income accrued but not distributed at Spouse's death is to be paid to Spouse's estate. The trustees have the discretion to invade trust principal for Spouse's benefit. Finally, Spouse has an annual power to withdrawal from trust principal the greater of 5 percent of the value of the trust calculated annually or $ 5,000. Upon Spouse's death, the remainder of the trust is to be held in further trust for Child.

On the Schedule M of the Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, filed for Decedent's estate, a marital deduction was claimed for assets passing to Spouse under Articles Second and Fourth of Decedent's will.

The executors have requested a ruling as to the method to be used to calculate the credit under § 2014(b)(2) for Decedent's estate.

Law and Analysis:

Section 2014(a) provides that, in general, the tax imposed by § 2001 shall be credited with the amount of any estate, inheritance, legacy, or succession taxes actually paid to any foreign country in respect of any property situated within such foreign country and included in the gross estate (not including any such taxes paid with respect to the estate of a person other than the decedent). The determination of the country within which property is situated shall be made in accordance with the rules applicable under subchapter B (§ 2101 and following) in determining whether property is situated within or without the United States.

Section 2014(b) provides that the credit provided in this section with respect to such taxes paid to any foreign country--(1) shall not, with respect to any such tax, exceed an amount which bears the same ratio to the amount of such tax actually paid to such foreign country as the value of property which is--(A) situated within such foreign country, (B) subjected to such tax, and (C) included in the gross estate bears to the value of all property subjected to such tax; and (2) shall not, with respect to all such taxes, exceed an amount which bears the same ratio to the tax imposed by § 2001 (after deducting from such tax the credits provided by §§ 2010, 2011, and 2012) as the value of property which is--(A) situated within such foreign country, (B) subjected to the taxes of such foreign country, and (C) included in the gross estate bears to the value of the entire gross estate reduced by the aggregate amount of the deductions allowed under §§ 2055 and 2056.

Section 2014(c)(1) provides that the values referred to in the ratio stated in subsection (b)(1) are the values determined for purposes of the tax imposed by such foreign country.

Section 2014(c)(2) provides that the values referred to in the ratio stated in subsection (b)(2) are the values determined under this chapter; but, in applying such ratio, the value of any property described in subparagraphs (A), (B), and (C) thereof shall be reduced by such amount as will properly reflect, in accordance with regulations prescribed by the Secretary, the deductions allowed in respect of such property under §§ 2055 and 2056 (relating to charitable and marital deductions).

Section 2014(g) provides that for purposes of the credits authorized by this section, each possession of the United States shall be deemed to be a foreign country.

Section 20.2014-1(a)(1) provides, in part, that a credit is allowed under § 2014 against the Federal estate tax for any estate, inheritance, legacy, or succession taxes actually paid to any foreign country (hereinafter referred to as "foreign death taxes"). The credit is allowed only for foreign death taxes paid (i) with respect to property situated within the country to which the tax is paid, (ii) with respect to property included in the decedent's gross estate, and (iii) with respect to the decedent's estate. The credit is allowable to the estate of a decedent who was a citizen of the United States at the time of his death. The credit is allowable not only for death taxes paid to foreign countries which are states in the international sense, but also for death taxes paid to possessions or political subdivisions of foreign states. With respect to the estate of a decedent dying after September 2, 1958, the term "foreign country", as used in this section and §§ 20.2014-2 to 20.2014-6, includes a possession of the United States. No credit is allowable for interest or penalties paid in connection with foreign death taxes.

Section 20.2014-1(a)(3) provides, in part, whether or not particular property of a decedent is situated in the foreign country imposing the tax is determined in accordance with the same principles that would be applied in determining whether or not similar property of a nonresident decedent not a citizen of the United States is situated within the United States for Federal estate tax purposes. See §§ 20.2104-1 and 20.2105-1.

Section 20.2014-1(b) provides that the credit for foreign death taxes is limited to the smaller of the following amounts: (1) The amount of a particular foreign death tax attributable to property situated in the country imposing the tax and included in the decedent's gross estate for Federal estate tax purposes, computed as set forth in § 20.2014-2; or (2) The amount of the Federal estate tax attributable to particular property situated in a foreign country, subjected to foreign death tax in that country, and included in the decedent's gross estate for Federal estate tax purposes, computed as set forth in § 20.2014-3.

Section 20.2014-2(a) provides that the amount of a particular foreign death tax attributable to property situated in the country imposing the tax and included in the decedent's gross estate for Federal estate tax purposes is the "first limitation." Thus, the credit for any foreign death tax is limited to an amount, A, which bears the same ratio to B (the amount of the foreign death tax without allowance of credit, if any, for Federal estate tax), as C (the value of the property situated in the country imposing the foreign death tax, subjected to the foreign death tax, included in the gross estate and for which a deduction is not allowed under § 2053(d)) bears to D (the value of all property subjected to the foreign death tax).

Stated algebraically, the "first limitation" A equals $B \times \frac{C}{D}$,

where : B = Amount of foreign death tax;
C = Value of property in foreign country subjected to death tax, included in gross estate, and for which a deduction is not allowed under § 2053(d); and
D = Value of all property subjected to foreign death tax.

The values used in this proportion are the values determined for the purpose of the foreign death tax. The amount of the foreign death tax for which credit is allowable must be converted into United States money.

Section 20.2014-3(a) provides that the amount of the Federal estate tax attributable to particular property situated in a foreign country, subjected to foreign death tax in that country, and included in the decedent's gross estate for Federal estate tax purposes is the "second limitation." Thus, the credit is limited to an amount, E, which bears the same ratio to F (the gross Federal estate tax, reduced by any credit for State death taxes under § 2011 and by any credit for gift tax under § 2012) as G (the "adjusted value of the property situated in the foreign country, subjected to foreign death tax, and included in the gross estate", computed as described in paragraph (b) of this section) bears to H (the value of the entire gross estate, reduced by the total amount of the deductions allowed under § 2055 (charitable deduction) and § 2056 (marital deduction)).

Stated algebraically, the "second limitation," E, equals $F \times \frac{G}{H}$,

where: F = Gross Federal estate tax, less credits for state death taxes and gift tax
G = Adjusted value of the property situated in the foreign country; subjected to foreign death taxes, and included in the gross estate; and
H = Value of entire gross estate, less charitable and marital deductions.

The values used in this proportion are the values determined for the purpose of the Federal estate tax.

Section 20.2014-3(b) provides that adjustment is required to factor "G" of the ratio stated in paragraph (a) of this section if a deduction for foreign death taxes under § 2053(d), a charitable deduction under § 2055, or a marital deduction under § 2056 is allowed with respect to the foreign property. If a deduction for foreign death taxes is allowed, the value of the property situated in the foreign country, subjected to foreign death tax, and included in the gross estate does not include the value of any property in respect of which the deduction for foreign death taxes is allowed. See § 20.2014-7. If a charitable deduction or a marital deduction is allowed, the value of such foreign property (after exclusion of the value of any property in respect of which the deduction for foreign death taxes is allowed) is reduced as follows:

(1) If a charitable deduction or a marital deduction is allowed to a decedent's estate with respect to any part of the foreign property, except foreign property in respect of which a deduction for foreign death taxes is allowed, specifically bequeathed, devised, or otherwise specifically passing to a charitable organization or to the decedent's spouse, the value of the foreign property is reduced by the amount of the charitable deduction or marital deduction allowed with respect to such specific transfer. See example (1) of paragraph (c) of this section.

(2) If a charitable deduction or a marital deduction is allowed to a decedent's estate with respect to a bequest, devise or other transfer of an interest in a group of assets including both the foreign property and other property, the value of the foreign property is reduced by an amount, I, which bears the same ratio to J (the amount of the charitable deduction or marital deduction allowed with respect to such transfer of an interest in a group of assets) as K (the value of the foreign property, except foreign property in respect of which a deduction for foreign death taxes is allowed, included in the group of assets) bears to L (the value of the entire group of assets). As used in this subparagraph, the term "group of assets" has reference to those assets which, under applicable law, are chargeable with the charitable or marital transfer. See example (2) of paragraph (c) of this section.

Stated algebraically, the reduction to the value of the foreign property is equal to I below:

$$I = J \times \frac{K}{L},$$

where: J = Amount of the charitable deduction or marital deduction allowed with respect to such transfer of an interest in a group of assets;

K = Value of the foreign property, except foreign property in respect of which a deduction for foreign death taxes is allowed, included in the group of assets; and

L = Value of the entire group of assets.

Any reduction described in §§ 20.2014-3(b)(1) or (b)(2) on account of the marital deduction must proportionately take into account, if applicable, the limitation on the aggregate amount of the marital deduction contained in § 20.2056(a)-1(c). See § 20.2014-3(c), Example 3.

Section 20.2014-3(c), Example (1) provides as follows. (i) Decedent, a citizen and resident of the United States at the time of his death on February 1, 1967, left a gross estate of $ 1,000,000 which includes the following: shares of stock issued by a domestic corporation, valued at $ 750,000; bonds issued in 1960 by the United States and physically located in foreign Country X, valued at $ 50,000; and shares of stock issued

by a Country X corporation, valued at $ 200,000, with respect to which death taxes were paid to Country X. Expenses, indebtedness, etc., amounted to $ 60,000. Decedent specifically bequeathed $ 40,000 of the stock issued by the Country X corporation to a U.S. charity and left the residue of his estate, in equal shares, to his son and daughter. The gross Federal estate tax is $ 266,500, and the credit for state death taxes is $ 27,600. Under the situs rules referred to in paragraph (a)(3) of § 20.2014-1**,** the shares of stock issued by the Country X corporation comprise the only property deemed to be situated in Country X. (The bonds also would be deemed to have their situs in Country X if the decedent had died before November 14, 1966.)

(ii) For the "second limitation" E on the credit for foreign death taxes,

E = second limitation;
F = $ 266,500 - $ 27,600 = $ 238,900;
G = $ 200,000 - $ 40,000 = $ 160,000; and
H = $ 1,000,000 - $ 40,000 = $ 960,000; therefore

$$E = \$\ 238{,}900 \times \frac{\$\ 160{,}000}{\$\ 960{,}000} = \$\ 39{,}816.67.$$

The lesser of this amount and the amount of the "first limitation" (computed under § 20.2014-2) is the credit for foreign death taxes.

Section 20.2014-3(c), Example (2) provides as follows: (i) Decedent, a citizen and resident of the United States at the time of his death, left a gross estate of $ 1,000,000 which includes: shares of stock issued by a United States corporation, valued at $ 650,000; shares of stock issued by a Country X corporation, valued at $ 200,000; and life insurance, in the amount of $ 150,000, payable to a son. Expenses, indebtedness, etc., amounted to $ 40,000. The decedent made a specific bequest of $ 25,000 of the Country X corporation stock to Charity A and a general bequest of $ 100,000 to Charity B. The residue of his estate was left to his daughter. The gross Federal estate tax is $ 242,450 and the credit for state death taxes is $ 24,480. Under these facts and applicable law, neither the stock of the Country X corporation specifically bequeathed to Charity A nor the insurance payable to the son could be charged with satisfying the bequest to Charity B. Therefore, the "group of assets" which could be so charged is limited to stock of the Country X corporation valued at $ 175,000 and stock of the United States corporation valued at $ 650,000.

(ii) Factor "G" of the ratio which is used in determining the "second limitation" is computed as follows:

Value of property situated in Country X	$ 200,000
Less:	

Reduction described in § 20.2014-3(b)(1) $ 25,000
Reduction I described in § 20.2014-3(b)(2)

I = reduction amount;
J = $ 100,000;
K = $ 175,000; and
L = $ 175,000 + $ 650,000 = $ 825,000; therefore

$$I = \$\ 100{,}000 \times \frac{\$\ 175{,}000}{\$\ 175{,}000 + \$\ 650{,}000} = \$\ 21{,}212.12$$

$ 46,212.12

Factor “G” of the ratio is $153,787.88

(iii) In this case, the "second limitation" on the credit for foreign death taxes is computed as follows:

E = second limitation;
F = $ 242,450 - $ 24,480 = $ 217,970;
G = $ 153,787.88; and
H = $ $ 1,000,000 - $ 125,000 = $ 875,000; therefore

$$E = \$\ 217{,}970 \times \frac{\$\ 153{,}787.88}{\$\ 875{,}000.00} = \$\ 38{,}309.88.$$

Section 20.2014-3(c), Example (3) provides as follows. (i) Decedent, a citizen and resident of the United States at the time of his death, left a gross estate of $ 850,000 which includes: shares of stock issued by United States corporations, valued at $ 440,000; real estate located in the United States, valued at $ 110,000; and shares of stock issued by Country X corporations, valued at $ 300,000. Expenses, indebtedness, etc., amounted to $ 50,000. Decedent devised $ 40,000 in real estate to a United States charity. In addition, he bequeathed to his wife $ 200,000 in United States stocks and $ 300,000 in Country X stocks. The residue of his estate passed to his children. The gross Federal estate tax is $ 81,700 and the credit for State death taxes is $ 5,520.

(ii) Decedent's adjusted gross estate is $ 800,000 (i.e., the $ 850,000, gross estate less $ 50,000, expenses, indebtedness, etc.). Assume that the limitation imposed by § 2056(c), as in effect before 1982, is applicable so that the aggregate allowable marital deduction is limited to one-half the adjusted gross estate, or $ 400,000 (which is 50 percent of $ 800,000). Factor "G" of the ratio which is used in determining the "second limitation" is computed as follows:

Value of property situated in Country X		$ 300,000
Less: Reduction described in § 20.2014-3 (b)(1) Determined as follows (see also end of § 20.2014-3(b)) –		
Total amount of bequests which qualify for the marital deduction:		
Specific bequest of Country X stock	$ 300,000	
Specific bequest of United States stock	$ 200,000	
	$ 500,000	
Limitation on aggregate marital deduction under § 2056(c)	$ 400,000	
Part of specific bequest of Country X stock with respect to which the marital deduction is allowed: ($ 400,000 x $ 300,000 / $ 500,000)		$ 240,000
Factor "G" of the ratio		$ 60,000

(iii) Thus, the "second limitation" on the credit for foreign death taxes is computed as follows:

E = second limitation;
F = $ 81,700 - $ 5,520 = $ 76,180;
G = $ 60,000;
H = $ 850,000 - $ 40,000 - $ 400,000 = $ 410,000; and so

$$E = \$\,76{,}180 \times \frac{\$\,60{,}000}{\$\,410{,}000} = \$\,11{,}148.29.$$

In this case, the available credit under § 2014 is the lesser of the “first limitation” calculated under § 20.2014-2(a) and the “second limitation” calculated under § 20.2014-3(a). Assets that pass to Spouse under the provisions of Article Second of Decedent’s will are specifically bequeathed to Spouse. Therefore, to the extent that the situs of assets passing to Spouse under Article Second for purposes of § 20.2014-1(a)(3) are in Possession, the adjustment set forth in § 20.2014-3(b)(1) is applicable in determining the available credit under § 2014. Assets that pass to Spouse under the provisions of Article Fourth of Decedent’s will constitute a general bequest to Spouse. Therefore, to the extent that the situs of assets passing to Spouse under Article Fourth for purposes of § 20.2014-1(a)(3) are in Possession, the adjustment set forth in § 20.2014-3(b)(2) is applicable in determining the available credit under § 2014.

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) 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.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Melissa Liquerman

Melissa Liquerman
Branch Chief, Branch 9
(Passthroughs & Special Industries)

Enclosures: Copy for § 6110 purposes