

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200746010**
Release Date: 11/16/2007

Third Party Communication: None
Date of Communication: Not Applicable

Index Number: 2055.12-07

Person To Contact: _____, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B04
PLR-128846-06

Date:
June 19, 2007

LEGEND:

- Decedent =
- Date 1 =
- Date 2 =
- A =
- B =
- C =
- \$m =
- \$y =
- \$x =
- a years =
- Charity 1 =
- Charity 2 =
- Charity 3 =
- Charity 4 =
- Charity 5 =
- Charity 6 =
- Charity 7 =
- Charity 8 =
- Charity 9 =
- Charity 10 =
- Charity 11 =
- Charity 12 =

Dear _____ :

This is in response to your authorized representative's letter of April 26, 2007, and other correspondence, requesting rulings on the application of § 2055(a) of the Internal Revenue Code to a trust.

Decedent died testate on Date 1. Under the terms of her will, the residuary estate, valued at \$x as of the date of her death, passed to a trust ("Trust"). Under Paragraph Fourth (2) of the Trust, \$m per month (or \$y per year) of Trust income is to be divided among A, B, and C, per capita, until the death of the last to survive of A, B, and C. The remaining Trust income is to be distributed among Charities 1-12, provided the organization is tax-exempt under § 501(c)(3) and charitable in nature. Under no condition is the annual distribution to be less than 5% of the initial fair market value of the Trust property. If the minimum required distribution exceeds the net income in any period, the trustees are to invade the Trust principal as necessary. On the death of the last to survive of A, B, and C, the Trust will continue and the income will be distributed exclusively to Charities 1-12.

Under the terms of Trust, the amount to be distributed to the charities until all of A, B, and C have died does not meet the requirements of a guaranteed annuity or a fixed percentage distributed yearly of the fair market value of the property, as required by § 2055(e)(2). Also, Trust does not satisfy the requirements of § 664 as required under § 2055(e)(2) in order for the charitable remainder interest to qualify for an estate tax deduction.

Moreover, based on: (i) the ages of A, B, and C, and (ii) the Trust provision for the use of principal to pay the annuities, there is a potential for the Trust principal to be fully consumed before A, B, and C have all died. That is, based on appropriate actuarial factors, the annuity period is to continue until all of A, B, and C have died or upon the expiration of a years, whichever occurs first. See § 25.7520-3(b)(2)(i); 25.7520-3(b)(2)(v) Example 5. For this reason, a deduction under § 2055(a) is not allowable for the charitable remainder interest in any event because, on the date of Decedent's death, the possibility that the remainder will fail is not so remote as to be negligible. Section 20.2055-2(b)(1) of the Estate Tax Regulations.

On Date 2, a date prior to the due date of the federal estate tax return for Decedent's estate, the executor of Decedent's estate and trustee of the Trust commenced a judicial proceeding to reform Trust under the provisions of state law and § 2055(e)(3). The proceeding is still pending at this time.

Under the proposed reformation, the Trust will distribute annually an amount equal to 5 percent of the initial net fair market value of the Trust, as follows:

- (1) An annual annuity amount of \$y (or .38% of the fair market value of the Trust assets at Decedent's date of death) is to be paid to A, B, and C or the survivor of them, until all of A, B, and C have died or upon the expiration of a

years, whichever occurs first (the "Annuity Term").

- (2) An annual annuity amount (the "Charitable Lead Annuity") equal to 4.62% of the fair market value of the Trust assets at Decedent's date of death is to be paid to Charities 1-12 for the Annuity Term.
- (3) At the end of the Annuity Term, any property remaining in the trust will be held for the exclusive benefit of Charities 1-12.

Under the terms of Trust, the trustee is precluded from engaging in any act of self dealing, failing to make distributions, retaining any excess business holdings, or making any taxable expenditures, so as to subject the trust to any tax under §§ 4941, 4942, 4943, 4944, or 4945.

It is represented that the proposed reformation of Trust will be effective as of Decedent's date of death and that Charities 1-12 are charitable organizations described in § 2055(a).

You have requested the following rulings:

1. The charitable lead annuity interest created in Article Fourth of the Trust is a "reformable interest", within the meaning of § 2055(e)(3)(C);
2. The Petition for Reformation, when granted, will result in a qualified reformation of the Trust, within the meaning of § 2055(e)(3)(B);
3. A deduction under § 2055(a) is allowable for the present value of the Charitable Lead Annuity, as reformed.

Section 2055(a) provides that the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, and transfers to or for a corporation or certain other organizations organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes.

Section 2055(e)(2) provides that where an interest in property passes or has passed from the decedent to a person or for a use described in subsection (a), and an interest in the same property passes (for less than an adequate and full consideration in money or money's worth) from the decedent to a person or for a use not described in subsection (a), no deduction shall be allowed under § 2055(a) unless: (A) in the case of a remainder interest, the interest is in a trust which is a charitable remainder annuity trust or a charitable remainder unitrust described in § 664, or a pooled income fund described in § 642(c)(5), or (B) in the case of any other interest, the interest is in the form of a guaranteed annuity or is a fixed percentage distributed yearly of the fair

market value of the property (to be determined yearly).

Section 20.2055-2(e)(1)(i) provides that where an interest in property passes or has passed from the decedent for charitable purposes and an interest in the same property passes or has passed from the decedent for private purposes (for less than an adequate and full consideration in money or money's worth) no deduction is allowed under § 2055 for the value of the interest which passes or has passed for charitable purposes unless the interest in property is a deductible interest described in § 20.2055-2(e)(2).

Under § 20.2055-2(e)(2)(vi)(a), a deductible interest includes a charitable interest in the form of a guaranteed annuity interest. The term "guaranteed annuity interest" means the right pursuant to the instrument of transfer to receive a guaranteed annuity. A guaranteed annuity is an arrangement under which a determinable amount is paid periodically, but not less often than annually, for a specified term of years or for the life or lives of certain individuals, each of whom must be living at the date of death of the decedent and can be ascertained at such date. An amount is determinable if the exact amount which must be paid under the conditions specified in the instrument of transfer can be ascertained as of the appropriate valuation date. For example, the amount to be paid may be a stated sum for a term of years, or for the life of the decedent's spouse, at the expiration of which it may be changed by a specified amount. In further illustration, the amount to be paid may be expressed in terms of a fraction or a percentage of the net fair market value, as finally determined for Federal estate tax purposes, of the residue of the estate on the appropriate valuation date.

Section 20.2055-2(e)(2)(vi)(f) provides that where a charitable interest in the form of a guaranteed annuity interest is in trust, the charitable interest generally is not a guaranteed annuity interest if any amount may be paid by the trust for a private purpose before the expiration of all the charitable annuity interests. There are two exceptions to this general rule. First, the charitable interest is a guaranteed annuity interest if the amount payable for a private purpose is in the form of a guaranteed annuity interest and the trust's governing instrument does not provide for any preference or priority in the payment of the private annuity as opposed to the charitable annuity. Second, the charitable interest is a guaranteed annuity interest if under the trust's governing instrument the amount that may be paid for a private purpose is payable only from a group of assets that are devoted exclusively to private purposes and to which § 4947(a)(2) is inapplicable by reason of § 4947(a)(2)(B). For purposes of this paragraph, an amount is not paid for a private purpose if it is paid for an adequate and full consideration in money or money's worth.

Section 2055(e)(3)(A) provides that a deduction shall be allowed under § 2055(a) in respect of any qualified reformation.

Section 2055(e)(3)(B) provides that the term "qualified reformation" means a

change of a governing instrument by reformation, amendment, construction, or otherwise that changes a reformable interest into a qualified interest but only if-- (i) any difference between- (I) the actuarial value (determined as of the date of the decedent's death) of the qualified interest, and (II) the actuarial value (as so determined) of the reformable interest, does not exceed 5 percent of the actuarial value (as so determined) of the reformable interest, (ii) in the case of- (I) a charitable remainder interest, the nonremainder interest (before and after the qualified reformation) terminated at the same time, or (II) any other interest, the reformable interest and the qualified interest are for the same period, and (iii) such change is effective as of the date of the decedent's death.

Section 2055(e)(3)(C)(i) provides that the term "reformable interest" means any interest for which a deduction would be allowable under § 2055(a) at the time of the decedent's death but for § 2055(e)(2).

Section 2055(e)(3)(C)(ii) provides that the term "reformable interest" does not include any interest unless, before the remainder vests in possession, all payments to persons other than an organization described in § 2055(a) are expressed either in specified dollar amounts or a fixed percentage of the fair market value of the property.

Section 2055(e)(3)(C)(iii) provides, however, that § 2055(e)(3)(C)(ii) shall not apply to any interest if a judicial proceeding is commenced to change such interest into a qualified interest not later than the 90th day after-- (I) if an estate tax return is required to be filed, the last date (including extensions) for filing such return, or (II) if no estate tax return is required to be filed, the last date (including extensions) for filing the income tax return for the first taxable year for which such a return is required to be filed by the trust.

Section 2055(e)(3)(D) provides that the term "qualified interest" means an interest for which a deduction is allowable under § 2055(a).

Section 2055(e)(3)(E) provides that the deduction referred to in § 2055(e)(3)(A) shall not exceed the amount of the deduction which would have been allowable for the reformable interest but for § 2055(e)(2).

Under the terms of Trust, as reformed, Trust will pay an annual annuity equal to 5% the initial fair market value of the Trust property on Decedent's date of death. Of this, the Charitable Lead Annuity amount will be equal to 4.62 % of the fair market value of the Trust assets on Decedent's date of death.

We have determined that the difference between the actuarial value (determined as of the date of decedent's death) of the qualified interest and the actuarial value (as so determined) of the reformable interest does not exceed 5 % of the actuarial value (as so determined) of the reformable interest. See § 2055(e)(3)(B). Furthermore, the term

of the Charitable Lead Annuity is for the same period both before and after the reformation. See § 2055(e)(3)(B)(ii)(II). In addition, the charitable lead interest provided under the terms of Trust prior to reformation constitutes a “reformable interest” within the meaning of § 2055(e)(3)(C). The annuity interest to be paid during the Annuity Term to the charities will constitute a guaranteed annuity within the meaning of § 2055(e)(2)(B). Accordingly, we conclude that the reformation, when judicially approved, will constitute a qualified reformation within the meaning of § 2055(e)(3)(B). Therefore, a charitable deduction will be allowable under § 2055(a) for the present value of the Charitable Lead Annuity, determined in accordance with § 20.2055-2(f)(2)(iv).

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.

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

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.

Sincerely yours,

George L. Masnik
Chief, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure
copy for 6110 purposes