



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

Number: 200817039  
Release Date: 4/25/2008

Date: January 31, 2008

UIL 4941.00-00

237639

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

SE:T:EO:RA:T3

Employer Identification Number:

Legend:

A =  
B =  
C =  
D =  
E =  
F =  
G =

Dear \_\_\_\_\_ :

We have considered the ruling request dated April 17, 2006, as amended by subsequent correspondence, regarding the early termination of A under sections 507, 4941 and 1001 of the Internal Revenue Code ("the Code").

B and C established A on \_\_\_\_\_, 1998, as a charitable remainder unitrust under section 664(d)(3) of the Code. B and C serve as trustees of A and D served as Independent Special Trustee. According to the Trust Agreement, B and C funded A with \_\_\_\_\_ shares of E common stock on \_\_\_\_\_, 1988, and no subsequent additions have been made to A.

C resigned as Independent Special Trustee effective as of March 3, \_\_\_\_\_. The Trust Agreement provides, among other things, if an Independent Special Trustee resigns at a time when one is required by the Trust, the remaining Trustees are required to appoint a successor Independent Special Trustee. The Trust Agreement requires an Independent Special Trustee to be appointed for the following situations:

- (1) Whenever the Trust holds any asset that does not have an "objectively and readily

ascertainable fair market value" , the Independent Special Trustee shall take title to, have investment over for and complete all valuations with respect to such Trust assets; and

(2) Whenever the Trust acquires an annuity contract of any type, the Independent Special Trustee shall exercise any discretion provided to the Trust as the owner of such annuity contract.

If an Independent Special Trustee resigns, as did D, the Trust Agreement does not require the appointment of a successor Independent Special Trustee unless and until the two situations described above require an Independent Special Trustee to be appointed. It is represented, that at present, all Trust assets have objective and readily ascertainable fair market values and the Trust does not have any interest in any annuity contract. Accordingly, no successor Independent Special Trustee is serving in place of D and B and C serve as A's only Trustees.

The Trust Agreement provides that the "Trust Term" commenced with the date on which B and C funded the Trust and will continue for the lifetimes of B and C or for a maximum term of twenty (20) years from the date the Trust was first funded, whichever period is shorter.

The Trust Agreement further provides that during the Trust Term the Trustees are required to distribute to the "Recipients" in each taxable year of the Trust an amount (the "Distribution Amount") equal to the smallest of (i) Trust income for such year, and (ii) ten percent (10%) of the net fair market value of the assets of the Trust, generally valued as of the first business day of such year (the "Fixed Percentage Amount"). The Distribution Amount for each taxable year is to be paid in equal quarterly installments at the end of each quarter for such year. The recipients are B and C, in equal proportions during their joint lifetimes, and thereafter, the survivor of them.

The Trustees also are required to distribute to the Recipients a "Deficiency Payable" consisting of any Trust income for a taxable year in excess of the Fixed Percentage Amount for such year, to the extent the aggregate of all amounts distributed to the Recipients in the Trust's prior taxable years was less than the aggregate of the Fixed Percentage Amounts for such prior taxable years.

Upon the expiration of the Trust Term, the Trust Agreement provides that the Trustees shall distribute the principal of the Trust and any Trust income, other than income due to the Recipients, (the "Charitable Remainder") to one or more charitable remainder beneficiaries, each of which must be a "Qualified Organization" described in sections 170(c), 2055(a) and 2522(a) of the Code. However, the Trust Agreement grants B and C the right, by a "Written Instrument" delivered to the Trustees, to modify or eliminate the interests of any contingent charitable remainder beneficiary designated by the Trust Agreement or an earlier Written Instrument, and to add or substitute other Qualified Organizations as charitable remainder beneficiaries.

Subject to a limited exception set forth in the Trust Agreement, the Trust Agreement provides that the Trust is governed by the laws of the State of E, notwithstanding the residence in another jurisdiction of B and C or of any of the persons who may have an interest in the Trust.

Pursuant to a "Written Instrument Designating Sole Remainder Beneficiary" effective as of March 15, , B and C designated G as sole charitable remainder beneficiary of the Trust. G is recognized as exempt from federal income tax under section 501(c)(3) of the Code, is classified as other than a private foundation under section 509(a), and is an organization described in sections 170(c), 2055(a) and 2522(a) of the Code.

Pursuant to a written agreement effective as of March 31, , B, C, and G have agreed to an early termination of the Trust and that such early termination would be in each of their best interests. You state that the agreement authorizes the Trustees to terminate the Trust upon receipt of this ruling from the Internal Revenue Service (the Service). Upon such termination, you state the Trustees (1) will distribute to G the actuarial value of its interest in the Trust, and (2) will distribute to B and C, in equal shares, the actuarial value of their interests in the Trust. In your initial ruling request you stated that the actuarial values of the parties' interest in the Trust will be determined using the discount rate in effect on the date of the termination under section 7520 of the Code, and using the methodology under section 1.664-4 of the regulations for valuing interests in charitable remainder trusts.

B's date of birth is October 25, and C's date of birth is November 3, , and both state that they are not aware of any physical condition that would decrease their life expectancies. In a letter dated March 15, 2007, amending their ruling request, B and C submitted a statement from their respective physicians confirming that they had examined B and C and that there was no indication that B or C's life expectancies were less than would otherwise be expected for a man or woman of their ages.

Also in the letter dated March 15, 2007, B and C agree to calculate the actuarial value of their interests in A upon termination under the methodology provided by this office as follows:

The actuarial value of G, B and C's interests in the Trust upon termination will be determined using the discount rate in effect on the date of termination under section 7520 and using the methodology under Treas. Reg. section 1.664-4 for valuing interests in charitable remainder trusts in all respects, except that for purposes of the calculation of the value of B and C's unitrust interest in the Trust will be reduced from 10% as provided in the Trust Agreement, to the discount rate in effect on the date of termination under section 7520.

#### RULINGS REQUESTED

A, through its Trustees, has requested the following rulings:

- (1) Early termination of A and distribution of the Trust's assets to B, C and G will not result in a termination tax under section 507 of the Code.
- (2) Early termination of A will not constitute self-dealing under section 4941 of the Code.

LAW

Section 507(c) of the Code imposes a tax on a private foundation under certain circumstances.

Section 664 of the Code exempts from income tax charitable remainder unitrusts, which it defines as those from which a fixed percentage of the net fair market value of its assets is paid to at least one person not an organization described in section 170(c) for a term of years, after which the remainder interest is transferred to an organization described in section 170(c).

Section 4941(a)(1) of the Code imposes an excise tax on disqualified persons for each act of self-dealing between a disqualified person and a private foundation.

Section 4941(a)(2) of the Code imposes an excise tax on a foundation manager for each act of self-dealing between a foundation manager and a private foundation when the foundation manager knowingly participates in such act.

Section 4941(d)(1) of the Code defines self-dealing as including any direct or indirect:

- (A) sale or exchange, or leasing of property between a private foundation and a disqualified Person, or
- (E) transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation.

Section 4946(a)(1) of the Code provides that for purposes of this subchapter, the term "disqualified person" means, with respect to a private foundation, a person who is---

- (A) a substantial contributor to the foundation,
- (B) a foundation manager (within the meaning of section (b)(1)).

Section 4946(a)(2) of the Code provides that for purposes of paragraph (1), the term "substantial contributor" means a person who is described in section 507(d)(2).

Section 4946(b) of the Code provides that for purposes of this subchapter, the term "foundation manager" means, with respect to any private foundation:

- (1) an officer, director, or trustee of a foundation (or an individual having powers or responsibilities similar to those of officers, directors, or trustees of the foundation) and
- (2) with respect to any act (or failure to act), the employees of the foundation having authority or responsibility with respect to such act (or failure to act).

Section 4947(a)(2) of the Code provides, in pertinent part, that in the case of a trust which is not exempt from tax under section 501(a), not all of the unexpired interests of which are devoted to charitable purposes, and which has amounts in trust for which a charitable deduction was allowed, sections 507 and 4941 apply as if such trust were a private foundation.

Section 4947(a)(2)(A) of the Code provides that section 4947(a)(2) shall not apply with respect to any amounts payable under the terms of such trust to non-charitable beneficiaries. Section 53.4947-1(c)(2)(ii) of the Foundation and Similar Excise Taxes Regulations provides, in essence, that payments of income by a charitable remainder unitrust to its individual income beneficiaries do not result in any tax on self-dealing under section 4947.

Section 1.7520-3(b)(1)(ii) of the Federal Income Tax Regulations (the regulations) provides that the standard 7520 annuity, life estate, or remainder factor may not be used to value a restricted beneficial interest. However, a special factor may be used to value a restricted beneficial interest in some circumstances. Section 1.7520-3(b)(1)(i)(C) of the regulations provides that the standard factor for an ordinary remainder interest represents the present worth of the right to receive \$1.00 at the end of a defined period. Section 1.7520-3(b)(1)(i)(B) of the regulations provides that the standard factor for an ordinary life estate interest represents the right to receive the use of \$1.00 for a defined period.

#### ANALYSIS

A is a split-interest trust described in section 4947(a)(2) of the Code, and by being described in section 4947(a)(2), A is subject to the provisions of sections 507 and 4941 of the Code as if it were a private foundation. The income beneficiaries, B and C are disqualified persons with respect to A within the meaning of section 4946(a)(1)(A) by virtue of being settlors of A. In this case, the charitable remainder beneficiary is a public charity so for purposes of sections 4941 and 4946, the income beneficiaries are not disqualified persons with respect to the charitable remainder beneficiary.

Section 4941 applies to certain transactions between private foundations and disqualified persons. By early termination, A will distribute lump sums to the income beneficiaries, B and C, and charitable remainderman equal to the actuarial value of their interests in A (taking into account the net-income provisions of the trust), and the distributions are also treated as a constructive sale or exchange between B and C and the charitable remainderman. See Rev. Rul. 69-486.

Generally, payments to the income beneficiaries, B and C, from A would constitute self-dealing. However, because the distribution to the income beneficiaries equals the actuarial value of the income interest, taking into account the net-income provisions of the trust, the exception to self-dealing provided by section 53.4947-1(c)(2)(i) of the regulations applies and the distribution will not be an act of self-dealing. Furthermore, because the charitable remainderman is a public charity, section 4941 does not apply to the transaction between B and C and the charitable remainderman.

The appropriate calculation of the actuarial value of the income interest of B and C, taking into account the net-income provisions of the trust, requires the use of a reasonable method for the calculation which does not inappropriately inflate the income beneficiary's interest to the detriment of the charitable remainderman.

One reasonable method to calculate the actuarial value of the income and remainder interests is the following:

The computation of the remainder interest is found using a special factor as indicated in section 1.7520-3(b)(1)(ii) of the regulations. The special remainder factor is found by using the methodology stated in section 1.664-4 for computing the factor for a remainder interest in a unitrust, with the following modification: where section 1.664-4(a)(3) of the regulations provides an assumption that the trust's stated payout percentage is to be paid out each year, instead the assumed payout shall be that of a fixed percentage which is equal to the lesser of the trust's stated payout percentage or the section 7520 rate for the month of termination. The special factor for the non-charitable payout interest is 1 minus the special remainder factor.

Based on this methodology, the calculation of B and C's income interest in A may be demonstrated as follows:

As of February , 2008, 10 years and 10 months remain of the initial trust term of 20 years. The section 7520 rate for February 2008 is 4.2 percent. The trust's stated payout percentage is 10 percent. The lesser of these two rates is 4.2 percent. The ages (at nearest birthday) of the payout recipients in February 2008 are 48 and 52.

Based on Table 90CM, interest at 4.2 percent, an unadjusted payout rate of 4.2 percent, and quarterly payments made at the end quarter, the present value of the remainder interest in the unitrust which falls in 10 years and 10 months hence or at the earlier of the death of the last to die of 2 persons ages 48 and 52 is \$0.63652 for each \$ 1.00 of the trust estate. The present value of the payout interest in the same unitrust payable for the shorter of 10 years and 10 months or until the prior death of the last to die of two persons is \$ 1.00 minus \$0.63652 or \$0.36348 for each \$ 1.00 of the trust estate.

In this case, the income beneficiaries are not expected to receive more than they would during the full term of the trust under the above-described methodology for valuing their interest in a charitable remainder trust with a net income make-up feature. Further, state law provides for early termination under the facts presented.

In addition, B and C's personal physicians have conducted physical examinations and have stated under penalties of perjury that they find no medical conditions expected to result in a shorter-than-average longevity; and B and C have signed similar statements.

Furthermore, because the effect of the transaction is to vest the income interest and remainder interest in the remainder beneficiaries, the trust no longer will be a split-interest trust and section 4947(a)(2) will no longer apply and section 507 will not apply.

## CONCLUSIONS

Therefore, we rule that:

- (1) The proposed termination of A will not be subject to a termination tax under section 507 of the Code.
- (2) Early termination of A will not constitute self-dealing under section 4941(d) of the Code using the methodology described on the prior page for the date of termination.

We acknowledge receipt of the letter of your authorized representative withdrawing your ruling request regarding section 1001 of the Code.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Manager, Exempt Organizations  
Technical Group 3

Enclosure  
Notice 437

cc: