Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200927013**
Release Date: 7/2/2009

Index Number: 2055.12-00, 2055.12-10

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B04
PLR-140919-08
Date:
March 18, 2009

Re:

Legend
Decedent =
Trust =

Trust 1 =

Trust 2 =

Institution =
Corporate Fiduciary =
Court =

A =
B =
C =
D =
E =
$x =
$y =
Date 1 =
Date 2 =
Date 3 =
Date 4 =
Date 5 =

Date 6 =
Date 7 =
State Laws 1 and 2 =

Dear :

This letter responds to a letter from your authorized representative, dated August 1, 2008, and other correspondence requesting a ruling on the application of § 2055(e)(3) of the Internal Revenue Code to the judicial reformation of Trust.

Decedent created Trust as a revocable trust on Date 1 and designated himself as the trustee. He amended Trust on Date 2, Date 3, and Date 4. Decedent transferred all of his property to Trust. He died on Date 5, and Trust became irrevocable.

Under Article Sixth (B) and (C) of Trust, certain real property is to be distributed to A and B, and Decedent's personal property is to be distributed to C. Under Article Sixth (D), all the rest, residue and remainder of the Trust corpus is to be divided into two Trusts, Trust 1 and Trust 2.

Article Sixth (D)(1) provides that Trust 1 is to consist of Trust assets of a value of $x to be held for the life of C. In each taxable year, C is to receive an annuity amount equal to six percent of the initial net fair market value of the Trust 1 assets. The annuity is to be paid from annual net trust income and, if income is insufficient, then from principal. Any net income not distributed to C is to be accumulated and added to principal.

Article Sixth (D)(2) provides that Trust 2 is to consist of the remaining Trust assets. In each taxable year, an annuity equal to five percent of the initial net fair market value of the Trust 2 assets is to be distributed between D and E during their joint lives and to the survivor of them for life. The annuity is to be paid from annual net trust income and, if income is insufficient, then from principal. Any net income not distributed is to be accumulated and added to principal.

Article Sixth (D)(3) provides that on C's death, the remaining assets of Trust 1 are to be distributed to Institution. When the survivor of D and E has died, the remaining assets of Trust 2 are, likewise, to be distributed to Institution. Institution is an organization described in §§ 170(c), 2055(a), and 2522(a).

Under Article Sixth (D)(4), all federal estate taxes imposed on Decedent's gross estate are to be paid out of Trust and charged to the residuary of Trust so that neither the specific property being given to specific beneficiaries nor the trust beneficiaries are to be charged with the taxes.

Article Seventh provides that, on Decedent's death, Institution is to be the trustee

having the power to designate a co-trustee. The current trustees are Institution and Corporate Fiduciary.

Although Trust 1 and Trust 2, as drafted, provided for lifetime annuity amounts for individuals followed by a remainder distributable to Institution, the trusts did not include certain provisions required by §§ 1.664-1 (for all charitable remainder trusts) and 1.664-2 (for charitable remainder annuity trusts). Therefore, the remainder interests passing to Institution did not did not qualify for the deduction allowed under § 2055(a) for charitable transfers.

On Date 6, prior to the date for filing the estate tax return for Decedent's estate, the trustees filed a petition in Court to reform Trust 1 and Trust 2 under State Laws 1 and 2 in order to qualify the trusts as charitable remainder annuity trusts described in § 664(d). On Date 7, Court issued an order approving the reformation of Trust 1 and Trust 2. The order is effective upon the trustees' receipt of a private letter ruling from the Internal Revenue Service holding that that Trust 1 and Trust 2 qualify as charitable remainder trusts eligible for the federal estate tax deduction under § 2055(a).

Under the reformation, Trust 1 and Trust 2 are deemed created on the date of Decedent's death, and the trustees' obligation to pay the annuity commences as of that date. However, the trustees may defer payment until the end of the taxable year in which the respective trust is completely funded.

In the case of a short taxable year, other than the final year, the annuity amount otherwise payable is to be based on the actual number of days in the short taxable year. In the last taxable year, the annuity amount is to equal the product of (1) the annuity amount, and (2) a fraction, the numerator of which is the number of days between the first day of the last taxable year of the trust and the last day of the trust, and the denominator of which is 365 (or 366, as the case may be), except that the trustee is to terminate payments with the payment next preceding the death of the beneficiary.

If the trustee determines incorrectly the initial net fair market value of the trust estate, the trustee is to pay to the beneficiary (in the case of an undervaluation) or be repaid by the beneficiary (in the case of an overvaluation) the amount equal to the difference between the amount properly payable to the beneficiary if the trustee used the correct value and the amount actually paid to the beneficiary.

No additional contributions may be made. The trustees may not engage in any act of self-dealing, as defined in § 4941(d); make any taxable expenditures, as defined in § 4945(d); pay any amount other than the annuity amount for less than full and adequate consideration to or for the use of any person other than an organization described in §§ 170(b), 170(c), 2055(a), and 2522(a); retain any excess business holdings as defined in § 4943(c); nor make any investments which would subject a trust to tax under § 4944.

In addition, all federal and state estate taxes are to be paid from the Trust corpus, not including the Trust 1 corpus. The estate's representative confirms that this does not change the original tax allocation provided for by Decedent. That is, as before, the taxes are to be paid from the Trust residue before any distribution may be made to either Trust 1 or Trust 2. The value of the Trust residue after payment of debts, administration expenses and taxes is approximately $y. Of that amount, $x will be distributed to Trust 1, and the remaining amount will be distributed to Trust 2.

You have requested the following rulings:

(1) The judicial reformation of Trust 1 and Trust 2 is a qualified reformation for purposes of § 2055(e)(3).

(2) A deduction is allowable under § 2055(a) for the present value of the remainder interests in Trust 1 and Trust 2 passing to Institution.

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 § 2055(a), and an interest (other than an interest that is extinguished upon the decedent's death) in the same property passes or has passed (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 § 2055(a), no deduction is allowed under § 2055(a) for the interest that passes or has passed to the person, or for a use, described in § 2055(a), unless in the case of a remainder interest, the interest is in a charitable remainder annuity trust or a charitable remainder unitrust (described in § 664) or a pooled income fund (described in § 642(c)(5)). In the case of an interest other than a remainder interest, the interest must be in the form of a guaranteed annuity, or a fixed percentage distributed annually of the net fair market value of the trust assets, determined annually.

Section 2055(e)(3)(A) provides that a deduction shall be allowed under § 2055(a) with respect to 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) the 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 generally 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, in part, that § 2055(a)(e)(3)(C)(ii) does not apply to any interest if a judicial proceeding is commenced to change the interest into a qualified interest not later than 90 days after the last date (including extensions) for filing an estate tax return, if an estate tax return is required to be filed.

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

In this case, the charitable remainder interests in Trust 1 and Trust 2 are reformable interests under § 2055(e)(3)(C). As originally drafted, the trusts provided for charitable remainder interests that were presently ascertainable and severable from the noncharitable interests. See § 20.2055-2(a) and (b). Accordingly, the remainder interests passing to Institution would have qualified for an estate tax charitable deduction under § 2055(a), but for the requirements of §§ 2055(e)(2) and 664. In addition, the reformation proceeding was commenced within the time prescribed in § 2055(a)(e)(3)C()(iii).

Further, the reformation will constitute a qualified reformation under § 2055(e)(3)(B). The actuarial value of the respective charitable remainder interests in Trust 1 and Trust 2 will not differ by more than 5 percent from the actuarial value of those interests provided for prior to reformation, determined under § 7520. Therefore, the proposed reformation satisfies the requirements of § 2055(a)(e)(3)(B)(i). In addition, under the terms of Trust 1 and Trust 2, the interests of A, B, and C will terminate at the same time as those interests would have terminated under the terms of the original trusts. Therefore, the proposed reformation satisfies the requirements of § 2055(e)(3)(B)(ii)(II).

The reformation will be effective as of the date of Decedent's death. Therefore, the requirement of § 2055(e)(3)(B)(iii) is satisfied. Finally, Trust 1 and Trust 2 qualify as charitable remainder annuity trusts, as described in § 664(d)(1).

Accordingly, based on the information submitted and representations made, we conclude that the reformation of Trust 1 and Trust 2, as described above, is a qualified reformation within the meaning of § 2055(e)(3), provided the reformation is effective under local law. Therefore, an estate tax charitable deduction is allowable under § 2055(a) for the present value of the charitable remainder interests, determined under § 20.2055-2(f)(2)(i**).**

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 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,

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures
Copy for § 6110 purposes