TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

201432029

MAY 13 2014

Uniform Issue List: 408.03-00, 2501.00-00, 4973.00-00, 4974.00-00

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SE:T:EP:RA:T2

Legend:

Taxpayer A	=	* * *
Decedent B	=	* * *
Decedent C	=	* * *
Charity D	=	* * *
Trust	=	* * *
Financial Institution E	=	* * *
Financial Institution F	=	* * *
Financial Institution G	=	* * *
IRA H1	=	* * *
IRA H2	=	* * *
IRA I1	=	* * *
IRA I2	=	* * *

IRA J1 = * * *

IRA J2 = * * *

IRA K1 = * * *

IRA K2 = * * *

IRA L1 = * * *

IRA L2 = * * *

IRA M1 = * * *

IRA M2 = * * *

IRA M3 = * * *

IRA M4 = * * *

IRA N	=	* * *
IRA O	=	* * *
Court	=	* * *
Court Order	=	* * *
State Statute 1	=	* * *
State Statute 2	=	* * *
State Statute 3	=	* * *

Dear * * *:

This is in response to your request dated December 29, 2010, as supplemented by correspondence dated November 1, 2012, and November 5, 2013, submitted by your authorized representative on your behalf, in which you request a letter ruling under sections 408(d), 2501, 4973, and 4974 of the Internal Revenue Code (the "Code").

The following facts and representations have been submitted under penalties of perjury in support of the rulings requested.

Taxpayer A was a personal friend and business associate of Decedent B. Decedent B and Decedent C were in a long-term relationship, but were not married.

Decedent B established and owned two IRA accounts, IRA H1 (a traditional IRA under Code Section 408) and IRA H2 (a SEP IRA under Code Section 408(k)), with Financial Institution E as custodian. Decedent B named Decedent C as the beneficiary for IRAs H1 and H2, and named various charities, including Charity D, as contingent beneficiaries in the event Decedent C pre-deceased Decedent B. In addition to IRAs H1 and H2, Decedent B maintained a regular brokerage account with Financial Institution E.

Decedent B also established Trust, a revocable living trust. Trust provided that if Decedent C survived Decedent B, then Decedent C would take a life income interest in Trust and the remainder would pass to several animal welfare charity organizations, including Charity D. Decedent B was the initial trustee of Trust, and Decedent C was the first successor trustee, and Taxpayer A was the second successor trustee. A "Schedule of Trust Assets" attached to Trust listed, among other assets, Decedent B's "Financial Institution E Accounts."

Decedent B died on August 13, 2006, and had not turned 70 ½ at the time of death.

After Decedent B's death, Decedent C declined to be the trustee of Trust, and, pursuant to the Trust's terms, Taxpayer A became the trustee of Trust. In reporting the assets of Trust to the probate court after Decedent B's death, an initial filing listed IRAs H1 and H2. Taxpayer A represents that IRAs H1 and H2 were listed as assets of Trust in error and that the initial filing, which was never approved by a court, was ultimately withdrawn. A second filing that excluded IRAs H1 and H2 from the assets of Trust was made and approved by the appropriate probate court.

Pursuant to their custodial agreement, IRAs H1 and H2 were to be distributed to Decedent C by December 31 of the fifth calendar year after Decedent B's death unless Decedent C elected to receive them over a period not greater than the life expectancy of Decedent C. Decedent C did not make such an election.

Decedent C established two new IRAs for his own benefit, IRA I1 and IRA I2, with Financial Institution E as custodian. Decedent C named Taxpayer A as beneficiary of the two new IRAs. In a trustee-to-trustee transfer in November 2006, Decedent C transferred the account balances from IRA H1 to IRA I1 and from IRA H2 to IRA I2.

Decedent C died on April 5, 2007, without taking any distributions from IRA I1 and IRA I2.

After Decedent C's death, Taxpayer A established two new IRAs for her benefit as beneficiary of Decedent C, IRA J1 and IRA J2, with Financial Institution E as custodian. In a trustee-to-trustee transfer in May 2007, Taxpayer A transferred the account balances from IRA I1 to IRA J1 and from IRA I2 to IRA J2.

For customer service/economic issues, Taxpayer A then established two new IRAs for her benefit as beneficiary of Decedent C, IRA K1 and IRA K2, with Financial Institution F as custodian. In a trustee-to-trustee transfer in May 2007, Taxpayer A transferred the account balances from IRA J1 to IRA K1 and from IRA J2 to IRA K2.

In December 2007, Decedent C's estate sued Taxpayer A alleging facts that, if sustained by Court, would, pursuant to State Statute 1 and State Statute 2, preclude Taxpayer A from inheriting IRA I1 and IRA I2. In addition, if Court held that Taxpayer A violated State Statute 1, Taxpayer A would be liable for the payment of the legal fees of Decedent C's estate, pursuant to State Statute 3. Taxpayer A entered into a tentative

settlement with Decedent C's estate to divide the account balances of IRA I1 and IRA I2, which were then held in IRA K1 and IRA K2, respectively.

In anticipation of the tentative settlement being approved by Court, Taxpayer A established two new IRAs for her benefit as beneficiary of Decedent C, IRA L1 and IRA L2, with Financial Institution F as custodian. In a trustee-to-trustee transfer in September 2008, Taxpayer A transferred the portion of the account balances that was to go to Decedent C's estate under the tentative settlement from IRA K1 to IRA L1 and from IRA K2 to IRA L2. The portion of the account balances that was to remain with Taxpayer A under the tentative settlement remained in IRA K1 and IRA K2.

Before Taxpayer A and Decedent C could obtain Court's approval of their tentative settlement, Charity D, as residuary beneficiary of Trust, filed in Court a "Response and Objections of Charity D to First Account and Report of Trustee and Petition for its Settlement; Request for Disgorgement of Benefits Obtained by Breach of Trust, and for Surcharge and Other Relief" ("Objection and Request"). In its Objection and Request, Charity D sought to have Court deny the tentative settlement between Taxpayer A and Decedent C's estate on the grounds that it purported to distribute assets that were the subject of Charity D's Objection and Request.

After a further year and a half of contested litigation, Taxpayer A, Decedent C's estate, and Charity D entered into a final settlement approved by Court Order in December 2010. Court Order provides, in relevant part, that:

(1) as of Decedent C's death, a portion of IRAs I1 and I2 were and had been the property of Decedent C's estate, and the remaining portion of IRAs I1 and I2 were and had been the property of Charity D; and

(2) IRAs I1 and I2 had never been the property of Taxpayer A.

Due to ownership changes at Financial Institution F, Financial Institution G became custodian of all of the IRAs of which Financial Institution F had been custodian. As part of this change in custodianship, Financial Institution G established IRAs M1, M2, M3, and M4. In a trustee-to-trustee transfer, Financial Institution G, without the request or involvement of Taxpayer A, transferred the account balances of IRA K1 to IRA M1, from IRA K2 to IRA M2, from IRA L1 to IRA M3, and from IRA L2 to IRA M4. At this point, all of the original funds and subsequent earnings from the IRAs I1 and I2 were divided between IRAs M1, M2, M3, and M4, and there had not been any distribution from any of the IRAs.

To implement the final settlement approved by Court Order, Taxpayer A established two final IRAs, IRA N and IRA O, with Financial Institution G as custodian. IRA N was established for the benefit of Decedent C's estate, and IRA O was established for the benefit of Charity D. In a trustee-to-trustee transfer, Taxpayer A transferred the account balances from IRAs M1, M2, M3, and M4 to IRA N and IRA O based on the final

settlement proportions. Decedent C's estate received distributions totaling the entire account balance of IRA N in December of 2010 and March of 2011. Charity D received a distribution of the entire account balance of IRA O in December of 2010.

Based on the facts and representations, you request the following rulings:

(1) that entering into the final settlement agreement approved by Court Order will not be treated as a section 2501 taxable gift transfer from Taxpayer A to Decedent C's estate and/or Charity D;

(2) that Taxpayer A is not subject to income tax on the series of account balance transfers from IRA I1 and IRA I2 to IRA N and IRA O;

(3) that Taxpayer A is not subject to income tax on the final distributions of (i) IRA N to Decedent C's estate, and (ii) IRA O to Charity D; and

(4) that Taxpayer A will not be subject to Code section 4973 or section 4974 excise taxes with respect to any of the IRAs listed in this ruling request.

With respect to your first ruling request, Section 2501(a) provides that a tax is imposed for each calendar year on the transfer of property by gift during such calendar year.

Section 2511(a) provides that the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect and whether the property is real or personal, tangible or intangible.

Section 25.2511-1(c)(1) of the Gift Tax Regulations provides that any transaction in which an interest in property is gratuitously passed or conferred upon another, regardless of the means or device employed, constitutes a gift subject to tax.

Section 25.2511-1(g)(1) provides that the gift tax is not applicable to a transfer for a full and adequate consideration in money or money's worth, or to ordinary business transactions.

Section 25.2512-8 provides that a sale, exchange, or other transfer of property made in the ordinary course of business (a transaction which is bona fide, at arm's length, and free from any donative intent) will be considered as made for an adequate and full consideration in money or money's worth.

Generally, transfers pursuant to agreements in settlement of disputes between adverse parties are not subject to the gift tax. See Beveridge v. Commissioner, 10 T.C. 915 (1948); Estate of Noland v. Commissioner, T.C. Memo. 1984-209; Lampert v. Commissioner, T.C. Memo 1956-226.

In Ahmanson Found. v. United States, 674 F.2d 761 (9th Cir. 1981), the issue before the court was whether property received by the spouse pursuant to a settlement qualified for the estate tax marital deduction. Relying on Commissioner v. Estate of Bosch, 387 U.S. 456 (1967), the court held that, in order for the settlement to be recognized for transfer tax purposes, the settlement must be made in good faith, and it must be based on the spouse's underlying enforceable right under state law properly interpreted. The court limited the amount of the marital deduction to the value of the property received with respect to which the spouse had enforceable rights, notwithstanding that the spouse received a greater amount under the good faith settlement.

In this case, whether the final settlement agreement approved by Court Order results in a transfer subject to gift tax depends on whether the settlement is based on a valid enforceable claim asserted by the parties. See Ahmanson, 674 F. 2d at 774-75. Thus, state law must be examined to ascertain the legitimacy of each party's claim. If it is determined that each party has a valid claim, the Service must determine that the distribution under the settlement reflects the result that would apply under state law. If there is a difference, it is necessary to consider whether the difference may be justified because of the uncertainty of the result if the question were litigated.

The final settlement agreement approved by Court Order is a mediated settlement and is based on arm's-length negotiations among the parties after years of litigation. Under applicable State law, if Court had sustained allegations made by Decedent C's estate and Charity D, Taxpayer A would have been precluded by State Statute 1 and State Statute 2 from inheriting IRA I1 and IRA I2. Under the terms of the final settlement agreement approved by Court Order, it was agreed, in effect, that Taxpayer A did not inherit IRA I1 and IRA I2. Thus, we conclude the terms of the final settlement agreement approved by Court Order represent (i) the resolution of a bona fide controversy regarding enforceable claims of the parties; and (ii) the parties' assessments of the relative strengths of their positions. We further conclude that the final settlement agreement approved by Court Order is within the range of reasonable outcomes under the governing instruments and applicable State law.

Therefore, based on the facts submitted and representations made, we conclude that Taxpayer A did not make a taxable gift for purposes of the federal gift tax under section 2501 by entering into the final settlement agreement approved by Court Order.

With respect to your remaining ruling requests, Section 408(d)(1) of the Code provides that, except as otherwise provided in section 408(d), any amount paid or distributed out of an IRA shall be included in gross income by the payee or distributee, as the case may be, in the manner provided under section 72 of the Code.

Revenue Ruling 78-406, 1978-2 C.B. 157, ("Rev. Rul. 78-406") states that the direct transfer of funds from one IRA trustee to another does not result in a payment or distribution of the funds for purposes of section 408(d)(1) of the Code. Rev. Rul. 78-406

also says this conclusion applies regardless of whether the bank trustee initiates such a transfer or the IRA participant directs it.

Section 4973 of the Code imposes an excise tax equal to 6 percent of the amount of any excess contribution to an IRA. This 6 percent tax applies for each taxable year of the IRA owner during which such excess contributions remain in such IRA, determined as of the end of the taxable year. An excess contribution under section 4973 is defined as a contribution in excess of the maximum amount that may be contributed to an IRA.

Section 4974 of the Code provides that if the amount distributed during the taxable year of the payee under any qualified retirement plan (defined under such section to include IRAs) is less than the minimum required distribution for such taxable year, a tax equal to 50% of the amount by which such minimum required distribution exceeds the actual amount distributed during the taxable year is imposed and paid by the payee.

With respect to your second ruling request, you have represented that the account balances of IRA I1 and IRA I2 have been transferred in a series of trustee-to-trustee transfers pursuant to Rev. Rul. 78-406 to IRA N and IRA O. Therefore, we conclude that Taxpayer A did not receive a payment or distribution from and is not subject to income tax on the series of account balance transfers from IRA I1 and IRA I2 to IRA N and IRA O.

With respect to your third ruling request, you have represented that Decedent C's estate received a complete distribution of IRA N as the beneficiary of IRA N, and that Charity D received a complete distribution of IRA O as the beneficiary of IRA O. Therefore, we conclude that Taxpayer A was not the payee or distributee of IRA N or IRA O and is not subject to income tax on the final distributions of (i) IRA N to Decedent C's estate, and (ii) IRA O to Charity D.

With respect to the first part of your fourth ruling request, because we have concluded that Taxpayer A did not receive a payment or distribution from any of the above mentioned IRAs, we also conclude that Taxpayer A did not make a contribution to any IRA related to the series of account balance transfers from IRA I1 and IRA I2 to IRA N and IRA O, and is not subject to Code section 4973 excise taxes from the series of account balance transfers from IRA I1 and IRA I2 to IRA N and IRA O.

With respect to the second part of your fourth ruling request, because we have concluded that Taxpayer A did not receive a payment or distribution from the series of account balance transfers from IRA I1 and IRA I2 to IRA N and IRA O and was not the payee or distributee of IRA N or IRA O, we also conclude that Taxpayer A is not subject to Code section 4974 excise taxes with respect to any of the IRAs at issue in this ruling request.

This letter assumes that the above IRAs qualify under either section 408 of the Code or section 408A of the Code at all relevant times.

No opinion is expressed as to the tax treatment of the transaction described herein under the provisions of any other section of either the Code or regulations which may be applicable thereto.

This letter is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, a copy of this letter ruling is being sent to your authorized representative. If you wish to inquire about this ruling, please contact * * * * * * * * * * * * at (* * *) * * *-* * * *. Please address all correspondence to SE:T:EP:RA:T2.

Sincerely yours,

Jason Levine, Manager,
Employee Plans Technical Group 2

Enclosures:

Deleted copy of ruling letter

Notice of Intention to Disclose

cc: * * *