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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B04
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Date:
October 07, 2022

In Re:

Legend

Date 1	=
Date 2	=
Date 3	=
Decedent	=
Spouse	=
Child 1	=
Child 2	=
x	=
Trust	=
Marital Trust	=
Non-Marital Trust	=
State Statute	=

Dear :

This letter responds to your authorized representative's letter dated March 28, 2022, requesting rulings concerning the federal income, gift, and estate tax treatment of Spouse's renunciation of her interests in Marital Trust and Non-Marital Trust and a net gift agreement between Spouse and the remainder beneficiaries of Non-Marital Trust.

FACTS

The facts submitted and the representations made are summarized as follows:
On Date 1, Decedent established Trust, a revocable trust. Trust was amended and restated several times prior to Decedent's death on Date 2, at which time Trust became irrevocable. Decedent was survived by Spouse, Child 1, and Child 2.

On Date 3, the executor of Decedent's estate timely filed Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. On Schedule M of Decedent's Form 706, the executor of Decedent's estate elected to treat Marital Trust as qualified terminable interest property (QTIP) pursuant to § 2056(b)(7) of the Internal Revenue Code.

The trust agreement of Trust ("Trust Agreement") provides that upon Decedent's death, the trustee is to divide the trust estate into two separate trusts, Marital Trust and Non-Marital Trust. Trust Agreement provides that Marital Trust is to be funded with property equal in value to that fractional share of Decedent's gross estate, the numerator of which is the marital deduction amount and the denominator of which is the value of Decedent's gross estate at its federal estate tax value after paying expenses and taxes. The marital deduction amount is defined as that amount which equals the lowest marital deduction which results in no federal estate tax being owed by reason of Decedent's death. Pursuant to Trust Agreement, the remaining portion of the trust estate was to fund Non-Marital Trust. Because Decedent had exhausted the entirety of his Basic Exclusion Amount before his death, Non-Marital Trust was not funded, and the entirety of the trust estate passed to Marital Trust.

Trust Agreement requires the trustee to pay Spouse all the net income of Marital Trust for her lifetime. In addition, Trust Agreement provides that the trustee may distribute to Spouse as much principal as the trustee, in its sole discretion, deems necessary or advisable for Spouse's comfort, support, or welfare. Upon Spouse's death, the remaining principal and income of Marital Trust passes to Non-Marital Trust after payment of any taxes attributable to Marital Trust's inclusion in Spouse's estate.

Trust Agreement provides that trustee must distribute all income of Non-Marital Trust between Spouse, Child 1, and Child 2. Trust Agreement further provides that trustee may distribute as much principal of Non-Marital Trust to Spouse, Child 1, or Child 2 as the trustee in its sole discretion deems necessary for their education, support, maintenance, and health. Trust Agreement provides that upon Spouse's death, Non-Marital Trust will split into separate shares for Child 1 and Child 2. The assets of each child's separate share will be distributed outright to him or her at age x. Child 1 and Child 2 have both attained the age of x.

Trust Agreement provides that Spouse may disclaim her right to receive income and principal from part or all of Marital Trust as Spouse specifies in a writing deposited with the trustee during Spouse's life. Trust Agreement further provides that assets disclaimed by Spouse are to be added to Non-Marital Trust.

Spouse proposes to renounce her interests in Marital Trust and, in accordance with State Statute, her interest in Non-Marital Trust. After the renunciations, because both Child 1 and Child 2 have attained age x, the property of Non-Marital Trust will be distributed to Child 1 and Child 2 under the express provisions of Trust Agreement, in accordance with State Statute. Additionally, as a condition of such renunciation, Spouse, Child 1 and Child 2 intend to enter into a net gift agreement ("Net Gift Agreement") providing that gift tax imposed on Spouse's gift of her qualifying income interest under § 2511 will be paid by Child 1 and Child 2. Finally, Spouse intends to exercise her right under § 2207A to recover from Child 1 and Child 2 the gift tax attributable to Spouse's deemed gift of the remainder of Marital Trust under § 2519.

You have requested the following rulings:

1. Spouse's renunciation of her interest in Marital Trust will be treated as a gift of Spouse's qualifying income interest in Marital Trust under § 2511 and a gift of the remaining portion of Marital Trust under § 2519.

2. Spouse's renunciation of her interest in Non-Marital Trust will be timely under § 2518(b)(2), and thus, will be a qualified disclaimer under § 2518 for federal tax purposes.

3. The amount of Spouse's gift of her qualified income interest in Marital Trust resulting from the renunciation of her interest in Marital Trust under § 2511 will be reduced by the gift taxes paid by Child 1 and Child 2 as a result of the Net Gift Agreement.

4. The amount of Spouse's gift of the remaining portion of Marital Trust under § 2519 resulting from the renunciation of her interest in Marital Trust will be reduced by her right under § 2207A to recover from Child 1 and Child 2 the gift tax attributable to the portion of such gift.

5. After Spouse's renunciation of her interest in Marital Trust and Non-Marital Trust, no portion of Marital Trust or Non-Marital Trust will be included in Spouse's gross estate.

6. All gift tax imposed on Spouse's gift of the interests in Marital Trust under §§ 2511 and 2519 will be included in Spouse's gross estate under § 2035(b) if Spouse dies within three years of having made the gift.

7. Spouse will recognize gain in the amount of the gift tax paid or reimbursed by Child 1 and Child 2 attributable to Spouse's gift of her income interest in Marital Trust under § 2511 in accordance with the Net Gift Agreement.

LAW AND ANALYSIS

Rulings 1-4

Section 2501 imposes a tax on the transfer of property by gift by an individual. Under § 2502(c), the gift tax imposed under § 2501 is the liability of the donor.

Section 2511(a) provides that the tax imposed by § 2501 shall apply 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 the gift tax applies to gifts indirectly made. Thus, 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 25.2511-2(a) provides that the gift tax is a primary and personal liability of the donor, is an excise upon his act of making the transfer, is measured by the value of the property passing from the donor, and attaches regardless of the fact that the identity of the donee may not then be known or ascertainable.

Section 2518(a) provides that, if a person makes a qualified disclaimer with respect to any interest in property, the disclaimed interest is treated as if it had never been transferred to the person making the qualified disclaimer for purposes of the federal estate, gift, and generation-skipping tax provisions.

Under § 2518(b), the term “qualified disclaimer” means an irrevocable and unqualified refusal by a person to accept an interest in property, provided (1) the refusal is in writing, (2) the disclaimer is received by the transferor of the interest, his legal representative, or the holder of legal title to the property to which the interest relates within nine months from the later of the date on which the transfer creating the interest in such person is made, or the date on which the person refusing the interest attains age 21, (3) the person refusing the interest has not accepted the interest or any of its benefits, and (4) as a result of the refusal, the interest passes without any direction on the part of the person making the disclaimer and passes either to the spouse of the decedent or to a person other than the person making the disclaimer.

Section 25.2518-2(c)(3) provides that the 9-month period for making a disclaimer generally is to be determined with reference to the transfer creating the interest in the disclaimant. With respect to inter vivos transfers, a transfer creating an interest occurs when there is a completed gift for Federal gift tax purposes regardless of whether a gift tax is imposed on the completed gift. With respect to transfers made by a decedent at death or transfers that become irrevocable at death, the transfer creating the interest occurs on the date of the decedent's death, even if an estate tax is not imposed on the transfer.

Section 2519(a) provides that any disposition of all or part of a qualifying income interest for life in any property to which § 2519 applies is treated as a transfer of all interests in the property other than the qualifying income interest. Section 2519(b) provides that § 2519 applies to any property if a deduction was allowed with respect to the transfer of such property to the donor under § 2056(b)(7).

Section 25.2519-1(a) provides that if a donee spouse makes a disposition of all or part of a qualifying income interest for life in any property for which a deduction was allowed under § 2056(b)(7), the donee spouse is treated for purposes of chapters 11 and 12 as transferring all interests in property other than the qualifying income interest. A transfer of all or a portion of the income interest of the spouse is a transfer by the spouse under § 2511.

Section 25.2519-1(c)(1) provides that the amount treated as a transfer under § 2519 upon a disposition of all or part of a qualifying income interest for life in QTIP is equal to the fair market value of the entire property subject to the qualifying income interest, determined on the date of the disposition (including any accumulated income and not reduced by any amount excluded from total gifts under § 2503(b) with respect to the transfer creating the interest), less the value of the qualifying income interest in the property on the date of the disposition. The gift tax consequences of the disposition of the qualifying income interest are determined separately under § 25.2511-2. Section 25.2519-1(c)(4) provides that the amount treated as a transfer under § 25.2519-1(c)(1) is further reduced by the amount the donee spouse is entitled to recover under § 2207A(b). If the donee spouse is entitled to recover gift tax under § 2207A(b), the amount of the gift tax recoverable and the value of the remainder interest treated as transferred under § 2519 are determined by using the same interrelated computation applicable for other transfers in which the transferee assumes the gift tax liability. The gift tax consequences of failing to exercise the right of recovery are determined separately under § 25.2207A-1(b).

Under § 2207A(b) and § 25.2207A-1(a), if an individual is treated as transferring an interest in property by reason of § 2519, the individual is entitled to recover from the "person receiving the property" (as defined in § 25.2207A-1(e)) the amount of gift tax attributable to that property. Under § 25.2207A-1(e), if the property is in trust at the time of the transfer, the "person receiving the property" is the trustee, and any person who has received a distribution of the property prior to the expiration of the right of recovery if the property does not remain in trust. Under § 25.2207A-1(b), the failure of a person to exercise a right of recovery provided by § 2207A(b) is treated as a transfer for federal gift tax purposes of the unrecovered amounts to the persons from whom the recovery could have been obtained.

Rev. Rul. 75-72, 1975-1 C.B. 310, holds that if, at the time of the transfer, a gift is made subject to a condition that the gift tax is to be paid by the donee or out of the transferred property, then the donor receives consideration for the transfer in the amount of the gift

tax to be paid by the donee. Thus, under § 2512(b), the value of the gift is the fair market value of the property passing from the donor less the amount of the gift tax to be paid by the donee or from the property itself.

Rev. Rul. 81-223, 1981-2 C.B. 189, holds that, in determining the amount of the gift tax liability that is to be subtracted from the value of the transferred property, the donor's available unified credit must be used to reduce the gift tax liability that the donee has assumed to the extent unified credit is available.

State Statute provides, in part, that a person may disclaim, in whole or in part, conditionally or unconditionally, any interest in or over property. Under State Statute, a disclaimer becomes irrevocable when any conditions to which the disclaimant has made the disclaimer are satisfied and when the disclaimer is delivered and filed in accordance with State law. Further, State Statute provides that if a donative instrument expressly provides for the distribution of property if there is a disclaimer, the property shall be distributed in accordance with the donative instrument. However, in the absence of express provisions to the contrary in the donative instrument, the property or interest in property disclaimed, and any future interest that is to take effect in possession or enjoyment at or after the termination of the interest disclaimed, shall be distributed as if the disclaimant had predeceased the decedent.

In this case, Spouse's renunciation of her interest in Marital Trust will not constitute a qualified disclaimer under § 2518 and the applicable regulations because it was not made within nine months of the creation of the interest (which in this case is Decedent's death) and Spouse has already accepted benefits from the Marital Trust. Based upon the facts submitted and the representations made, the renunciation of Spouse's interest in Marital Trust is a disposition of Spouse's qualifying income interest for life in property for which a marital deduction was allowed under § 2056(b)(7). Spouse will make a completed gift of her qualifying income interest in Marital Trust under § 2511 and will be deemed to have made a completed gift of all of the other property and other interests in property then owned by Marital Trust, other than Spouse's qualifying income interest in Marital Trust, under § 2519.

Because Spouse's renunciation of her interest in Marital Trust will result in a completed transfer to Non-Marital trust, Spouse will be considered to make an inter vivos transfer to Non-Marital Trust. Consequently, under § 2518 and the applicable regulations, the Non-Marital Trust beneficiaries' interests with respect to the property transferred from Marital Trust will be created as of the date of Spouse's renunciation of her interest in Marital Trust. Accordingly, the beneficiaries of Non-Marital Trust may disclaim their interests in the property transferred by Spouse to Non-Marital Trust within nine months of Spouse's renunciation of her interests in Marital Trust. Therefore, based on the facts submitted and the representations made, Spouse's renunciation of her interest in the property transferred to Non-Marital Trust will constitute a qualified disclaimer under § 2518 and the applicable regulations.

As a condition of the gift resulting from Spouse's renunciations of her interest in Marital Trust and Non-Marital Trust, Spouse, Child 1, and Child 2 intend to enter into Net Gift Agreement providing that gift tax imposed on Spouse's qualifying income interest under § 2511 will be paid by Child 1 and Child 2. Thus, based on the facts submitted and the representations made, after the renunciations, the amount of the gift will be reduced by the gift taxes paid by or recovered from Child 1 and Child 2.

Furthermore, based on the facts submitted and the representations made, Spouse's gift under § 2519 will be reduced by Spouse's right under § 2207A to recover from Child 1 and Child 2 the gift tax attributable to such gift.

Ruling 5

Section 2044(a) provides that the value of the gross estate shall include the value of any property in which the decedent had a qualifying income interest for life. Section 2044(b) provides that § 2044(a) applies to any property if—(1) a deduction was allowed with respect to the transfer of such property to the decedent under § 2056(b)(7), and (2) section 2519 did not apply with respect to a disposition by the decedent of part or all of such property.

Section 2518(a) provides that, if a person makes a qualified disclaimer with respect to any interest in property, the disclaimed interest is treated as if it had never been transferred to the person making the qualified disclaimer for purposes of the federal estate, gift, and generation-skipping tax provisions.

When Spouse renounces her entire interest in Marital Trust, Spouse will have made a gift of her qualifying income interest in Marital Trust under § 2511 and a gift of all of the other property and other interests in property then owned by Marital Trust, other than Spouse's qualifying income interest in Marital Trust, under § 2519. Accordingly, based on the facts submitted and the representations made, none of Marital Trust will be includible in Spouse's gross estate under § 2044(a) because of the application of § 2044(b)(2).

Because Spouse's disclaimer of her interest in Non-Marital Trust qualified under § 2518, Spouse is treated as never having received an interest in Non-Marital Trust for estate tax purposes. Accordingly, based on the facts submitted and the representations made, none of Non-Marital Trust will be includible in Spouse's gross estate.

Ruling 6

Section 2035(b) provides that the amount of the gross estate shall be increased by the amount of any tax paid under chapter 12 by the decedent or his estate on any gift made by the decedent or his spouse during the 3-year period ending on the date of the decedent's death.

In *Estate of Sachs v. Commissioner*, 856 F.2d 1158 (8th Cir. 1988), donor made a gift to trust, and, pursuant to a net gift agreement, the trustee paid the gift tax associated with the gift. When donor died within three years of making the gift, the court held that the gift tax paid was included in donor's estate even though it was actually paid by the donees. The court stated "[j]ust as the donee's tax payment must be included in the donor's taxable income, a donee's tax payment (on a gift made within three years of the donor's death) is an includable part of the donor's gross estate under [§ 2035(b)]. The fact that the Internal Revenue Service received the payment for the decedent's gift-tax liability *via* the donee does not make it any less a 'tax paid…by the decedent or his estate' within the meaning of [§ 2035(b)]." *Id.* at 1164.

In *Estate of Morgens v. Commissioner*, 133 T.C. 402 (2009), ***aff'd***, 678 F.3d 769 (9th Cir. 2012), decedent transferred her income interest in a QTIP trust to the remainder beneficiaries and died within three years of making the gift. As a condition of the gift, the remainder beneficiaries agreed to pay the gift tax liability arising under § 2519. The court held that neither the donees' agreement to pay the gift tax nor the decedent's right of recovery under § 2207A(b) prevented the gift tax paid from being included in the decedent's estate under § 2035(b).

The legislative history to § 2035(b) provides that "the gift tax paid on transfers made within 3 years of death should in all cases be included in the decedent's gross estate." H.R. Rep. No. 94-1380 at 3366.

Based on the facts submitted and the representations made, all gift tax imposed on Spouse's gift of the interests in Marital Trust under §§ 2511 and 2519 will be included in Spouse's gross estate under § 2035(b) if she dies within three years of having made the gift.

Ruling 7

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain. Section 1001(b) provides that the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Section 1001(c) provides that, except as otherwise provided in subtitle A, the entire amount of gain determined under § 1001 on the sale or exchange of property shall be recognized.

Section 1001(e)(1) provides that in determining gain or loss from the sale or other disposition of a term interest in property, that portion of the adjusted basis of such interest which is determined pursuant to § 1014, § 1015, or § 1041 (to the extent that such adjusted basis is a portion of the entire adjusted basis of the property) shall be

disregarded. Section 1001(e)(2)(C) provides that the term "term interest in property" means an income interest in a trust.

The character of the gain will depend on the nature of the asset sold. Section 1222 provides that long-term capital gain is gain from the sale or exchange of a capital asset held for more than one year. Section 1221 provides that the term "capital asset" means property held by the taxpayer, excluding certain types of property not apparently at issue in this case.

Rev. Rul. 72-243, 1972-1 C.B. 233, holds that the proceeds received by the life tenant of a testamentary trust, in consideration for the transfer of her entire interest in the trust to the remainderman, are to be treated as an amount realized from the sale or exchange of a capital asset under § 1222 and that the life tenant's basis attributable to his life interest at the time of the sale is considered to be zero, pursuant to § 1001(e). See §§ 1.1001-1(f) and 1014-5(b) and (c) of the Income Tax Regulations.

In *Diedrich v. Commissioner*, 457 U.S. 191 (1982), the Court held that, if a donor makes a gift transfer of appreciated property that is conditioned upon the transferee's payment of the resulting gift tax, the donor realizes gross income to the extent that the gift tax paid by the donee exceeds the donor's adjusted basis in the transferred property. The Court reasoned that, when a donor makes a gift to a donee, a debt to the United States for the amount of the gift tax is incurred by the donor. When the donee agrees to discharge an indebtedness in consideration of the gift, the person relieved of the tax liability realizes an economic benefit.

Based on the facts submitted and the representations made, the amount realized by Spouse, under § 1001(b), will be the amount of gift tax paid or reimbursed by Child 1 and Child 2 attributable to Spouse's gift of her income interest under § 2511 pursuant to the Net Gift Agreement. Gift tax paid or reimbursed by Child 1 and Child 2 attributable to Spouse's gift under § 2519 of the remainder of Marital Trust is not part of the amount realized by Spouse under § 1001(b).

Because Spouse's adjusted basis in the property she is transferring is considered to be zero under § 1001(e), the gain from Spouse's disposition of the property will be equal to the amount realized. Accordingly, under § 1001(c), the entire amount of gain will be recognized.

Under Rev. Rul. 72-243 and *Diedrich*, Spouse's gain from the transfer of her entire interest in Marital Trust will be treated as an amount realized from the sale or exchange of a capital asset under § 1222.

Accordingly, based on the facts submitted and the representations made, the current federal income tax imposed on Spouse as a result of the proposed transaction will be calculated by treating the amount of gift tax paid or reimbursed by Child 1 and Child 2 attributable to Spouse's gift of her income interest under § 2511 pursuant to the Net Gift

Agreement as gain from the sale of a capital asset.

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.

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 authorized representative.

Sincerely,

Karlene M. Lesho
Senior Technician Reviewer, Branch 4
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures:
Copy for §6110 purposes

cc: