

## Internal Revenue Service

Department of the Treasury

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Person to Contact:

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Refer Reply To:

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Date:

**August 29,2001**

### LEGEND

Child =  
Children =

County =  
Decedent =  
Estate =  
Foundation =

Grandchild =  
Initial Special Trustees =

State =

Dear :

This is in response to your letter dated May 4, 2001, in which you requested rulings under sections 2518 and 2055 of the Internal Revenue Code ("Code"). Specifically, you request rulings that:

1. The proposed disclaimer by Child will constitute a qualified disclaimer within the meaning of section 2518 of the Code.

2. That the amount passing to Foundation by reason of Child's proposed disclaimer will be treated as passing from Decedent to Foundation for purposes of section 2055(a) of the Code and thus will qualify as a federal estate tax charitable deduction for Estate.

The information submitted and the representations made are summarized as follows. Decedent died survived by three children ("Children"). Prior to his death, Decedent and his spouse formed Foundation. Children are the current trustees of Foundation. It has been represented that Foundation is a private foundation within the meaning of section 509(a) of the Code and is recognized by the Internal Revenue Service ("Service") as a federally tax-exempt organization under section 501(c)(3) of the Code.

PLR-125716-01

Article II of Foundation Agreement provides that Foundation is organized and operated solely and exclusively for religious, charitable, scientific, literary, and educational purposes within the meaning of section 501(c)(3) of the Code.

Article VII, section (1), of Foundation Agreement provides, in pertinent part, that Foundation Agreement may be amended with the approval of not less than two thirds of the trustees; but no amendment shall alter the general character of Foundation as one organized and operated exclusively for religious, charitable, scientific, literary, and educational purposes.

Article Second, Section C, of Decedent's will bequeaths \$                      to Foundation. Article Fourth of Decedent's will provides that Children receive Decedent's residuary estate. It has been represented that after Decedent's death, Children each received approximately \$                      from the residuary estate.

Article Fifth of Decedent's will provides that if, any child disclaims any portion of the residuary bequest under Article Fourth of the will, the disclaimed portion is to pass to Foundation.

One of Decedent's Children, Child proposes to disclaim from Child's share of the residuary estate, all right, title, and interest in all except that fractional amount of Child's portion of the residuary estate that produces a sum equal to \$                      , after the amount is reduced for state and federal inheritance taxes chargeable to her share of the residuary estate under Article Seventh of Decedent's will.

In connection with Child's proposed disclaimer, Children, as trustees of Foundation, propose to execute First Amendment to Foundation Agreement ("Amended Agreement") to provide for the addition of Article VIII to Foundation Agreement.

Article VIII of Amended Agreement provides that assets received by Foundation as a result of any qualified disclaimer by one or more of the Children who are trustees ("Disclaiming Trustee(s)") will be held in one or more segregated accounts ("Special Account(s)"), separate and apart from any other assets of Foundation ("Other Foundation Assets").

Article VIII, section (1), of Amended Agreement provides, in pertinent part, that the right to distribute income and/or principal of Special Account(s) and to select the recipients of such distributions is held exclusively by Special Trustee(s). All other rights and powers with respect to Special Account, including, without limitation, the power to make investments and reinvestments of the principal and accumulated income, will be held by the trustees. The trustees will have no rights or powers respecting the disposition of Special Account(s) or the appointment or removal of Special Trustee(s).

Article VIII, section (2), of Amended Agreement provides that Special Trustees have the uncontrolled discretion to distribute, from time to time, such portions, or the whole, of

PLR-125716-01

the net income and/or principal of Special Account in such manner that complies with Foundation's charitable purpose, as defined in Article II of Foundation Agreement.

Article VIII, section (4), of Amended Agreement provides, in pertinent part, for the appointment of Initial Special Trustees and provides that Special Trustees have the power to increase or decrease the number of Special Trustees; provided, however, that Grandchild has the right to become a Special Trustee when Grandchild turns thirty years old. Article VIII, section (4), further provides, in pertinent part, that Special Trustees have the power to select successor Special Trustees to fill vacancies. Should Special Trustees fail to appoint successor Special Trustee(s) within three months of the vacancy's occurrence, the Orphans' Court of County, in State may, upon application, appoint such successor Special Trustee(s). A successor or additional Special Trustee may be a corporation (other than a corporation in which a Disclaiming Trustee owns any interest or serves as an officer, director, or employee) or an individual, provided that no Disclaiming Trustee and no person under the age of thirty years who is a lineal descendent of a Disclaiming Trustee may be selected as a Special Trustee.

Article VIII, section (14), of Amended Agreement provides that, upon the death of the last surviving Disclaiming Trustee, Special Account(s) will be merged with Other Foundation Assets, and all rights powers, and duties of the Special Trustees will terminate.

Article VIII, section (15), of Amended Agreement provides that the provisions of Article VIII may not be revoked or amended in any manner that would allow a Disclaiming Trustee or any other person under the age of thirty who is a lineal descendant of a Disclaiming Trustee to possess, directly or indirectly, any rights with respect to the disposition of Special Account(s) or any right to appoint or remove Special Trustee(s).

#### LAW - ISSUE 1

Section 2046 of the Code provides that for estate tax purposes, disclaimers of property interests passing upon death are treated as provided in section 2518.

Section 2518(a) provides that, if a person makes a qualified disclaimer with respect to any interest in property, the federal estate, gift, and generation-skipping transfer tax provisions will apply to that interest as if it had never been transferred to such person.

Under section 2518(b), the term "qualified disclaimer" means an irrevocable and unqualified refusal by a person to accept an interest in property, provided: (1) such refusal is in writing; (2) the disclaimer is received by the transferor of the interest, his legal representative, or the holder of the legal title to the property to which the interest relates not later than the date which is nine months after the later of (A) the date on which the transfer creating the interest in such person is made, or (B) the day on which such person attains age twenty-one; (3) the person disclaiming the interest has not accepted the interest or any of its benefits; and (4) as a result of such refusal, the interest passes without any direction on the part of the person making the disclaimer

PLR-125716-01

and passes either (A) to the spouse of the decedent, or (B) to a person other than the person making the disclaimer.

Section 2518(c)(1) provides that a disclaimer with respect to an undivided portion of an interest which meets the requirements of section 2518(b) shall be treated as a qualified disclaimer of such portion of the interest.

Under section 25.2518-1(b) of the Gift Tax Regulations, if a qualified disclaimer is made, the property is treated, for federal gift, estate, and generation-skipping transfer tax purposes, as passing directly from the transferor, and not from the disclaimant, to the person entitled to receive the property as a result of the disclaimer. Thus, the disclaimant is not treated as making a gift.

Section 25.2518-2(d)(2) provides, in pertinent part, that if a beneficiary who disclaims an interest in property is also a fiduciary, the disclaimant cannot retain a wholly discretionary power to direct the enjoyment of the disclaimed interest. For example, a fiduciary's disclaimer of a beneficial interest does not meet the requirements of a qualified disclaimer if the fiduciary exercised or retains a discretionary power to allocate enjoyment of that interest among members of a designated class.

Under section 25.2518-2(e), in general, a disclaimer is not a qualified disclaimer unless the disclaimed interest passes without any direction on the part of the disclaimant to a person other than the disclaimant. The disclaimer will not be qualified if the disclaimant, either alone or in conjunction with another, directs the redistribution or transfer of the property or interest in property to another person (or has the power to direct the redistribution or transfer of the property or interest in property to another person) unless such power is limited by an ascertainable standard.

Section 25.2518-3(c) states that a disclaimer of a specific pecuniary amount out of a pecuniary or nonpecuniary bequest or gift which satisfies the other requirements of a qualified disclaimer under section 2518(b) and the corresponding regulations is a qualified disclaimer provided that no income or other benefit of the disclaimed amount inures to the benefit of the disclaimant, either prior to or subsequent to the disclaimer. Thus, following the disclaimer of a specific pecuniary amount from a bequest or gift, the amount disclaimed and any income attributable to such amount must be segregated from the portion of the gift that was not disclaimed. The segregation of assets making up the disclaimer of a pecuniary amount must be made on the basis of the fair market value of the assets on the date of the disclaimer or on the basis that is fairly representative of value changes that may have occurred between the date of transfer and the date of disclaimer. A pecuniary amount distributed to the disclaimant from the bequest or gift prior to the disclaimer shall be treated as a distribution of corpus the bequest or gift. However, the acceptance of a distribution from the gift or bequest shall also be considered to be an acceptance of a proportionate amount of income earned by the bequest or gift. The proportionate share of income considered to be accepted by the disclaimant shall be determined at the time of the disclaimer according to the

PLR-125716-01

following formula: the total amount of distributions received by the disclaimant out of the gift or bequest divided by the total value of the gift or bequest on the date of the transfer multiplied by the total amount of income earned by the gift or bequest between the date of transfer and the date of disclaimer.

In section 25.2518-3(d), Example (17), D bequeaths his brokerage account to E. The account consists of stocks and bonds and a cash amount earning interest. The total value of the cash and assets in the account on the date of D's death is \$100,000. Four months after D's death, E makes a withdrawal of cash from the account for personal use amounting to \$40,000. Eight months after D's death, E disclaims \$60,000 of the account without specifying any particular assets or cash. The cumulative fair market value of the stocks and bonds in the account on the date of the disclaimer is equal to the value of such stocks and bonds on the date of D's death. The income earned by the account between the date of D's death and the date of E's disclaimer was \$20,000. The amount of income earned by the account that E accepted by withdrawing \$40,000 from the account prior to the disclaimer is determined by applying the formula set forth in section 25.2518-3(c) as follows: \$40,000 divided by \$100,000 multiplied by \$20,000 equals \$8,000. E is considered to have accepted \$8,000 of the income earned by the account. If (i) the \$60,000 disclaimed by E and the \$12,000 of income earned prior to the disclaimer which is attributable to that amount are segregated from the \$8,000 of income E is considered to have accepted, (ii) E does not accept any benefits of the \$72,000 so segregated, and (iii) the other requirements of section 2518(b) are met, then E's disclaimer of \$60,000 from the account is a qualified disclaimer.

In Rev. Rul. 72-552, 1972-2 C.B. 525, the decedent, who was the president and a director of a corporation organized under section 501(c)(3), transferred property to the corporation. In his capacity as president and a director, the decedent, in conjunction with the other directors of the corporation, had the power to direct the disposition of the corporation's funds for charitable purposes. The ruling holds that, because the decedent retained the right, in conjunction with others, to designate the entities that would possess or enjoy the property transferred to the corporation, the property transferred by the decedent to the corporation was included in the decedent's gross estate at his death under section 2036.

## DISCUSSION - ISSUE 1

In the present case, any property that is disclaimed by Child will pass to Foundation pursuant to the terms of Article Fifth of Decedent's will. Pursuant to the terms of the proposed Amended Agreement, the disclaimed property will be held in a segregated Special Account in Foundation, separate and apart from the Other Foundation Assets. The power to make distributions from the income and/or principal from the Special Account and to select the recipients of such distributions will be held exclusively by the Initial and any subsequent Special Trustees. Child is precluded from becoming a Special Trustee and will have no power to appoint or remove a Special Trustee. Further, Child will have no power to revoke or amend the proposed Amended

PLR-125716-01

Agreement in any manner that would allow Child to possess, directly or indirectly, any rights with respect to the disposition of the assets held in the Special Account.

Therefore, we conclude that the disclaimer will constitute a qualified disclaimer under section 2518 provided the Amended Agreement is executed and its terms are effective under state and federal law and the other requirements of section 2518 are satisfied, including the requirements of sections 25.2518-3(c) respecting the \$ distribution to Child from Decedent's residuary estate.

## LAW - ISSUE 2

Under section 2055(a)(2), for estate tax purposes, 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, or transfers to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes. A trust that qualifies under section 501(c)(3) is one that is organized and operated exclusively for these purposes.

Section 20.2055-2(c)(1)(i) of the Estate Tax Regulations states that in the case of a bequest, devise, or transfer made by a decedent dying after December 31, 1976, the amount of a bequest, devise, or transfer for which a deduction is allowable under section 2055 includes an interest which falls into the bequest, devise, or transfer as the result of a qualified disclaimer under section 2518.

## DISCUSSION - ISSUE 2

It is represented that Foundation is a private foundation within the meaning of section 509(a) of the Code and is recognized by the Service as a federally tax-exempt organization under section 501(c)(3). Under the terms of Decedent's will, any amount disclaimed by Child will pass to Foundation. Accordingly, based on the representations noted above, the property passing to Foundation as a result of Child's disclaimer and segregated in the Special Account will qualify for an estate tax charitable deduction for Estate under section 2055, provided the proposed Amended Agreement is executed and its terms are effective under state and federal law and Child's disclaimer is a qualified disclaimer under section 2518.

The rulings contained in this letter are based upon information submitted and representations made 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.

PLR-125716-01

This ruling is directed only to the taxpayer(s) 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 the taxpayer.

By: Sincerely,  
Assistant Chief Counsel  
(Passthroughs and Special Industries)  
James Hogan  
Senior Technician Reviewer, Branch 9

Enclosure: Copy for section 6110 purposes