

Internal Revenue Service

Number: **200648025**

Release Date: 12/1/2006

Index Number: 2522.02-04, 170.00-00,
642.03-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

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CC:PSI:B09

PLR-163261-05

Date:

June 22, 2006

LEGEND

Taxpayer =
State =
Trust =

Beneficiary 1 =
Beneficiary 2 =
\$x =

Dear :

This is in response to your authorized representative's letter dated December 12, 2005, requesting gift, estate, and income tax rulings related to a proposed transaction. The facts submitted and representations made are as follows:

Taxpayer, a resident of State, proposes to establish Trust, a charitable lead annuity trust.

Article First, Paragraph (a) of the proposed trust agreement provides that in each taxable year of the trust until the termination date, the trustee shall pay the annuity amount to such one or more charitable organizations described in §§ 170(c), 2055(a), and 2522(a) of the Internal Revenue Code as the trustee shall select.

Article First, Paragraph (b) provides that on the termination date, the trust shall terminate and the remaining trust property shall be distributed in equal shares to Beneficiary 1 and Beneficiary 2. If a beneficiary is not living on the termination date, the share that would have been distributed to such deceased beneficiary shall be distributed to his estate.

Article First, Paragraph (c) provides that the annuity amount shall be \$x.

Article First, Paragraph (d) provides that the termination date of the trust shall be the seventh anniversary of the date of execution of the trust instrument.

Article Second, Paragraph (a) provides that payments for each taxable year shall be made annually on or before the end of each taxable year of the trust. Payments shall be made first from the ordinary taxable income of the trust (including short term capital gains) that is not unrelated business income, then from the capital gains of the trust other than short term capital gains, then from any unrelated business income, then from any tax exempt income, and finally from the principal of the trust, in that order. Any net income for a taxable year in excess of the annuity amount shall be added to principal.

Article Second, Paragraph (b) provides that for a short taxable year and for the taxable year in which the payment of the annuity amount terminates, the trustee shall prorate the annuity amount on a daily basis.

Article Fourth provides that the trust is intended to qualify as a charitable lead annuity trust so that the value of the interest passing to charity is deductible as a charitable guaranteed annuity interest under §§ 2055(e)(2)(B) and 2522(c)(2)(B) and so that the payments of the annuity amount to charity will be deducted from the gross income of the trust to the extent provided by § 642(c).

Article Fourth, Paragraph (a) provides that the trustee shall not engage in any act of self-dealing as defined in § 4941(d), nor make any taxable expenditures as defined in § 4945(d).

Article Fourth, Paragraph (b) provides that except to the extent provided in § 4947(b)(3), the trustee shall not retain any excess business holding as defined in § 4943(c) which would subject the trust to tax under § 4943, nor shall the trustee acquire any assets which would subject the trust to tax under § 4944 or retain any assets which, if acquired by the trustee, would subject the trustee to tax under § 4944.

Article Fourth, Paragraph (c) provides that if § 4942 is at any time applicable to the trust, the trustee shall make distributions at such time and in such manner as not to subject the trust to tax under § 4942.

Article Fourth, Paragraph (d) provides that no provisions of the trust agreement shall be construed to restrict the trustee from investing the trust assets in a manner that could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets.

Article Fourth, Paragraph (e) provides that no additional contributions shall be made to the trust after the initial contribution.

Article Sixth describes the powers exercisable by the trustee. All such powers are limited so that the value of the interest passing to the charity is deductible as a charitable guaranteed annuity interest under §§ 2055(e)(2)(B) and 2522(c)(2)(B) and so that the payments of the annuity amount to charity will be deductible under § 642(c).

Article Seventh provides that neither Taxpayer nor Taxpayer's spouse shall ever be appointed as the trustee of the trust.

Article Ninth provides that the trust shall be irrevocable and shall not be subject to alteration or amendment; provided that the trustee may amend any provision of the trust at any time to enable the trust to qualify or continue to qualify as a charitable lead annuity trust under §§ 2055(e)(2)(B) and 2522(c)(2)(B), the regulations thereunder and decisional law.

Article Tenth expresses the intent that the trust not be taxed as a "grantor trust" under § 671 and that the provisions of Article Tenth shall control any contradictory provisions.

Article Tenth, Paragraph (a) provides that Taxpayer shall have no interest in the principal or income of the trust and prohibits the trustee from making a distribution of principal or income to Taxpayer as described in § 673.

Article Tenth, Paragraph (b) provides that neither Taxpayer nor any person classified as a nonadverse party under § 672 shall have any power to determine beneficial enjoyment of the principal or income in any manner that would cause any part of the income or principal of the trust to be considered a "grantor trust" under § 674.

Article Tenth, Paragraph (c) provides that neither Taxpayer nor any other person shall have the power (i) to dispose of the income or principal of the trust for less than adequate consideration in money or money's worth, with the exception of the power granted to the trustee in paragraph (a) of Article First of the trust, (ii) to borrow principal or income of the trust, directly or indirectly, without adequate interest or security, or (iii) to borrow directly or indirectly, the principal or income of the trust. In addition, neither Taxpayer nor any other person shall have a power exercisable in a nonfiduciary capacity without the approval or consent of any person in a fiduciary capacity.

Article Tenth, Paragraph (d) provides that neither the trustee nor any other person shall have the power to revest any income or principal of the trust in Taxpayer.

Article Tenth, Paragraph (e) provides that no income of the trust may be distributed to Taxpayer or Taxpayer's spouse, held for future distribution to Taxpayer or Taxpayer's spouse or applied to the payment of premiums on a policy of insurance on the life of Taxpayer or Taxpayer's spouse.

Article Tenth, Paragraph (f) provides that no person may become vested of a power over income or principal of the trust to vest the principal or income of the trust in himself.

Article Eleventh, Paragraph (a) provides that Taxpayer shall have no interest in the income or principal of the trust, and prohibits the trustee from making a distribution of principal or income to Taxpayer.

Article Eleventh, Paragraph (b) provides that Taxpayer shall have no power to designate the persons who shall enjoy the principal or income of the trust nor shall Taxpayer have any right to income or to possess or enjoy the assets of the trust.

Article Eleventh, Paragraph (c) provides that no part of the trust estate or any of the trust may revert to Taxpayer.

Article Eleventh, Paragraph (d) provides that Taxpayer shall not have the right to alter, amend, revoke, or terminate the trust.

Article Eleventh, Paragraph (e) provides that Taxpayer shall not have the right to appoint any property transferred to the trust nor may Taxpayer be granted a power to appoint property transferred to the trust.

Article Eleventh, Paragraph (f) provides that Taxpayer may not purchase life insurance on the life of Taxpayer, Taxpayer's spouse, or both of their lives.

Taxpayer requests the following rulings:

1. The annuity amount paid from Trust will qualify under § 2522(c)(2)(B) as a guaranteed annuity. Taxpayer will be entitled to a gift tax charitable deduction under § 2522(a) for the value of the annuity amount (valued under §§ 2502 and 7520) to be paid to the charitable organization(s) during the charitable term.
2. No part of the assets transferred to Trust will be included in Taxpayer's gross estate under § 2036.
3. No part of the assets transferred to Trust will be included in Taxpayer's gross estate under § 2037.

4. No part of the assets transferred to Trust will be included in Taxpayer's gross estate under § 2038.
5. No part of the assets transferred to Trust will be included in Taxpayer's gross estate under § 2041.
6. No part of the assets transferred to Trust will be included in Taxpayer's gross estate under § 2042.
7. No part of the assets transferred to Trust will be included in Taxpayer's gross estate under § 2035.
8. No part of the income or principal transferred to Trust will be owned by Taxpayer under § 671 due to the application of § 673.
9. No part of the income or principal transferred to Trust will be owned by Taxpayer under § 671 due to the application of § 674.
10. No part of the income or principal transferred to Trust will be owned by Taxpayer under § 671 due to the application of § 675.
11. No part of the income or principal transferred to Trust will be owned by Taxpayer under § 671 due to the application of § 676.
12. No part of the income or principal transferred to Trust will be owned by Taxpayer under § 671 due to the application of § 677.
13. No part of the income or principal transferred to Trust will be owned by Taxpayer under § 671 due to the application of § 678.
14. The payments of the annuity amount from Trust to a charitable organization will be amounts that are paid for a purpose specified in § 170(c).
15. The payment of the annuity amount from Trust to a charitable organization will be allowed as an income tax charitable deduction in computing Trust's taxable income under § 642(c) to the extent paid from gross income.

RULING 1

Section 2501 provides that a tax is imposed in each calendar year on the transfer of property by gift during such calendar year by any individual.

Section 2511 provides that the gift tax 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 25.2511-2(b) of the Gift Tax Regulations provides that as to any property, or part thereof, of which the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for the donor's own benefit or for the benefit of another, the gift is complete.

Section 25.2511-2(c) provides, in part, that a gift is incomplete in every instance in which a donor reserves the power to revest the beneficial title to the property in himself. A gift is also incomplete if and to the extent that a reserved power gives the donor the power to name new beneficiaries or to change the interests of the beneficiaries as between themselves.

Section 2522(a) provides, in part, that in computing taxable gifts for the calendar year, there shall be allowed as a deduction the amount of all gifts made during the year to or for the use of the charitable purposes described therein.

Section 2522(c)(2) provides that where a donor transfers an interest in property (other than an interest described in § 170(f)(3)(B)) to a person, or for a use, described in § 2522(a) and an interest in the same property is retained by the donor, or is transferred or has been transferred (for less than adequate and full consideration in money or money's worth) from the donor to a person, or for a use, not described in § 2522(a), no deduction shall be allowed for the interest which is, or has been transferred to the person, or for the use, described in § 2522(a) unless – (A) in the case of a remainder interest, such interest is in a trust which is a charitable remainder annuity trust or a charitable remainder unitrust (described in § 664) or a pooled income fund (described in § 642(c)(5)), or (B) in the case of any other interest, the interest is in the form of a guaranteed annuity or is a fixed percentage distributed yearly of the fair market value of the property (to be determined yearly).

Section 25.2522(c)-3(c)(2)(vi)(a) provides that the term "guaranteed annuity interest" means an irrevocable right pursuant to the instrument of transfer to receive a guaranteed annuity. A guaranteed annuity is an arrangement under which a determinable amount is paid periodically, but not less often than annually, for a specified term of years or for the life or lives of certain individuals, each of whom must be living at the date of the gift and can be ascertained at such date.

Under § 25.2522-3(d)(2)(iv), the present value of a guaranteed annuity interest in trust is to be determined under § 25.2512-5.

In this case, Taxpayer's transfer of assets to Trust constitutes a completed gift under § 25.2511-2(b) because Trust is irrevocable and Taxpayer has retained no interest or reversion in Trust. In addition, the trust agreement irrevocably provides for the payment of an annual annuity of \$x from Trust to qualified charities.

Based on the forgoing, we conclude that the annuity payable under Trust satisfies the requirements of § 25.2522(c)-3(c)(2)(vi) and constitutes a guaranteed annuity for purposes of § 2522(c)(2)(B). Accordingly, Taxpayer is entitled to a gift tax deduction under § 2522(a), based on the present value of the guaranteed annuity of Trust payable to charity as determined under § 25.2512-5.

RULINGS 2, 3, 4, 5, 6 and 7

Section 2033 provides that the value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of the decedent's death.

Section 2035(a) provides that if – (1) the decedent made a transfer (by trust or otherwise) of an interest in any property, or relinquished a power with respect to any property, during the 3-year period ending on the date of the decedent's death, and (2) the value of such property (or an interest therein) would have been included in the decedent's gross estate under § 2036, § 2037, § 2038, or § 2042 if such transferred interest or relinquished power had been retained by the decedent on the date of the decedent's death, then the value of the gross estate shall include the value of any property (or interest therein) that would have been so included.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which the decedent has retained for life or for any period not ascertainable without reference to the decedent's death or for any period which does not in fact end before the decedent's death – (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 20.2036-1(a) of the Estate Tax Regulations, provides, in part, that for purposes of § 2036, an interest or right is treated as having been retained or reserved by the decedent, if at the time of the transfer there was an understanding, express or implied, that the interest or right would later be conferred.

Section 2037(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at

any time after September 7, 1916, made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, if – (1) possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent, and (2) the decedent has retained a reversionary interest in the property and the value of such reversionary interest immediately before the death of the decedent exceeds 5 percent of the value of such property.

Section 2038(a)(1) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of the decedent's death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person to alter, amend, revoke, or terminate, or where any such power is relinquished during the 3-year period ending on the date of the decedent's death.

Section 2041(a)(2) provides that the value of the gross estate shall include the value of all property to the extent of any property with respect to which the decedent has, at the time of the decedent's death, a general power of appointment or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition that is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under §§ 2035 through 2038, inclusive.

Section 2041(b)(1)(A) provides that a general power of appointment is a power that is exercisable in favor of the decedent, the decedent's estate, the decedent's creditors, or the creditors of the decedent's estate, except that a power to consume, invade or appropriate property for the benefit of the decedent which is limited by an ascertainable standard relating to the health, education, support, or maintenance of the decedent shall not be deemed a general power of appointment.

Section 2042(2) provides that the value of the gross estate shall be the value of all property to the extent of the amount receivable by all other beneficiaries as insurance under policies on the life of the decedent with respect to which the decedent possessed at death any of the incidents of ownership, exercisable either alone or in conjunction with any other person.

In the present case, Trust is irrevocable. For a seven year period, Trustee must distribute annually a fixed annuity amount of \$x to organizations described in §§ 170(c), 2055(a), and 2522(a). Upon the termination of the seven year annuity period, the remaining property in Trust will pass to Beneficiary 1 and Beneficiary 2.

Taxpayer has not retained any (i) interest or reversion in Trust, (ii) any right to alter, amend, or revoke Trust, or (iii) any right to receive an annuity or other payment from Trust during Taxpayer's lifetime. In addition, Taxpayer holds no general power of appointment over the property held in Trust.

Assuming there is no understanding, express or implied, between Taxpayer and Trustee regarding the disposition of the amounts held as part of Trust, we conclude that no portion of the assets of Trust will be included in Taxpayer's gross estate under § 2036, § 2037, § 2038, § 2041 or § 2042 for federal estate tax purposes. We further conclude that because no portion of the assets transferred by Taxpayer to Trust will be includible in Taxpayer's gross estate under § 2036, § 2037, § 2038, or § 2042, no portion of the assets transferred by Taxpayer to Trust will be includible in Taxpayer's gross estate under § 2035.

RULINGS 8, 9, 10, 11, 12 and 13

Section 671 provides that where it is specified in subpart E of Part I of subchapter J that the grantor or another person shall be treated as the owner of any portion of a trust, there shall then be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust that are attributable to that portion of the trust to the extent that such items would be taken into account under chapter 1 in computing taxable income or credits against the tax of an individual.

Sections 673 through 678 specify the circumstances under which the grantor or a person other than the grantor is treated as the owner of a portion of a trust.

Section 673 provides that the grantor shall be treated as the owner of any portion of a trust in which the grantor has a reversionary interest in either the corpus or the income therefrom, if, as of the inception of that portion of the trust, the value of such interest exceeds 5 percent of the value of such portion.

Section 674(a) provides, in general, that the grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

Section 674(b)(4) provides that § 674(a) shall not apply to a power to determine the beneficial enjoyment of the corpus or the income therefrom if the corpus or income is irrevocably payable for a purpose specified in § 170(c) (relating to the definition of charitable contributions).

Under § 675 and applicable regulations, the grantor is treated as the owner of any portion of a trust if, under the terms of the trust agreement or circumstances attendant on its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiary of the trust.

Section 676(a) provides that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under any other provision of part I, subchapter J, chapter 1, where at any time the power to revest in the grantor title to such portion is exercisable by the grantor or a nonadverse party, or both.

Section 677(a) provides, in general, that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under § 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a nonadverse party, or both, may be (1) distributed to the grantor or the grantor's spouse, (2) held or accumulated for future distribution to the grantor or the grantor's spouse, or (3) applied to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse.

Section 678(a) provides, in general, that a person other than the grantor shall be treated as the owner of any portion of a trust with respect to which (1) such person has a power exercisable solely by himself to vest the corpus or the income therefrom in himself, or (2) such person has previously partially released or otherwise modified such a power and after the release or modification retains such control as would, within the principles of §§ 671 to 677, inclusive, subject a grantor of a trust to treatment as the owner thereof.

Based solely on the facts and representations submitted, we conclude that an examination of Trust reveals none of the circumstances that would cause Taxpayer or any other person to be treated as the owner of any portion of Trust under § 673, § 674, § 676, § 677, or § 678.

We further conclude that an examination of Trust reveals none of the circumstances that would cause administrative controls to be considered exercisable primarily for the benefit of Taxpayer under § 675. Thus, the circumstances attendant on the operation of Trust will determine whether Taxpayer will be treated as the owner of any portion of Trust under § 675. This is a question of fact, the determination of which must be deferred until the federal income tax returns of the parties involved have been examined by the office with responsibility for such examination.

RULING 14

Section 170(a) provides, subject to certain limitations, a deduction for charitable contributions as defined in § 170(c), payment of which is made in the taxable year.

Section 170(c) provides, in part, that for purposes of § 170, the term “charitable contribution” means a contribution or gift to or for the use of: (1) federal or other government entities for exclusively public purposes; (2) a corporation, trust, or community chest, fund, or foundation created in the United States and organized exclusively for religious, charitable, scientific, literary, or educational purposes (with no part of the net earnings inuring to the benefit of a private shareholder or individual); or (3) certain transfers to fraternal or veterans organizations.

In this case, Trust provides that, for a specified term of seven years, the annuity amount is to be distributed to one or more organizations described in § 170(c), 2055(a), and 2522(a). The trust agreement further provides that if the receiving organization is not a qualifying organization under § 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, such payments shall instead be distributed to one or more organizations described in § 170(c), 2055(a), and 2522(a). Accordingly, the annuity amount paid by Trust will be paid for purposes specified in § 170(c).

RULING 15

Section 642(c)(1) provides that in the case of an estate or trust (other than a trust meeting the specifications of subpart B), there shall be allowed as a deduction in computing its taxable income (in lieu of the deduction allowed by § 170(a), relating to deduction for charitable, etc., contributions and gifts) any amount of the gross income, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, paid for a purpose specified in § 170(c) (determined without regard to § 170(c)(2)(A)). Section 642(c)(4) provides that the deduction allowed for a trust is subject to § 681 (relating to unrelated business income).

Section 681(a) provides that no charitable deduction is allowable to a trust under § 642(c) for any amount allocable to the trust’s “unrelated business income” for the taxable year. The term “unrelated business income” means an amount under § 512, if the trust were exempt from tax under § 501(a) by reason of § 501(c)(3), that would be computed as its unrelated business taxable income under § 512.

Except to the extent that Trust has unrelated business income under § 681(a), and except to the extent that contributions are nondeductible under § 508(d) or § 4948(c), Trust will be allowed deductions in accordance with § 642(c)(1) for amounts of gross income paid to charitable organizations during that taxable year, or the close of the following taxable year, if Trustee makes an election under § 1.642(c)-1(b). Because the deduction under § 642(c)(1) is limited to amounts of gross income, no deduction will be allowed for a distribution of principal except to the extent that the amount distributed has been included in the gross income of the trust and provided no deduction was allowed for any previous taxable year for the amount distributed.

In addition, the ordering of income distributions provided in Article Second, Paragraph (a) of the trust agreement will not be given effect for federal income tax purposes because the ordering provision has no economic effect on the distributions independent of tax consequences. The trust agreement requires that Trust pay annually a stated annuity amount to organizations described in §§ 170(c), 2055(a), and 2522(a), regardless of the amount or character of income earned by Trust. Instead, income distributed to the organizations described in §§ 170(c), 2055(a), and 2522(a) shall consist of the same proportion of each class of the items of income of Trust as the total of each class bears to the total of all classes. See § 1.642(c)-3(b)(2).

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) 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.

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,

Melissa C. Liquerman
Branch Chief, Branch 9
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure

Copy for 6110 purposes