

Internal Revenue Service

Department of the Treasury

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June 14, 1999

Re :

Legend

Decedent =

Spouse =

Trust =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Child A =

Child B =

Child C =

This is in response to your letter dated May 14, 1999, and prior correspondence, in which you request a ruling concerning the application of §§ 2511 and 2519 of the Internal Revenue Code to a proposed transaction.

Under Decedent's will, executed on Date 1, Decedent bequeathed the residue of his estate to a revocable trust that Decedent and Spouse had created on Date 2. On Date 3, prior to Decedent's death, the revocable trust, was amended, restated, and renamed (Trust).

Under the terms of Trust, if Decedent predeceases Spouse, then the trustee is to divide the trust estate into a Marital Trust, Decedent's Trust, and a Survivor's Trust. After funding the Survivor's Trust and Decedent's Trust, the residue of the Trust property is to be allocated to the Marital Trust. The Marital Trust provides that the trust income is to be paid to Spouse for life. Upon the death of Spouse, the Marital Trust property is divided into equal shares to be held in separate trusts, one share to be held for each living child of the settlor and one share to be held for the surviving issue of a deceased

child. Under the terms of each trust, after the child attains age 21, the trustee shall pay to the child the net income of the trust. If the income is not sufficient for the child's reasonable support, health, maintenance and education, in accordance with the child's accustomed standard of living, the trustee is to pay the child as much of the principal as is necessary for such purpose. When the child attains age 30, the trustee is to distribute $\frac{1}{6}$ of the principal to the child. When the child attains age 35, the trustee is to distribute $\frac{1}{5}$ of the remaining principal to the child. When the child attains age 40, $\frac{1}{2}$ of the balance is to be distributed to the child. If the child has attained age 30, 35, or 40 when the Spouse dies and the trust is divided into shares, the trustee is to distribute to the child $\frac{1}{6}$, $\frac{1}{3}$, or $\frac{1}{2}$ of the trust share, as the case may be.

On the death of a child, the balance of the child's share is to be divided into a number of trusts equal to the number of child's surviving issue (grandchildren) and deceased issue with living issue. If a grandchild has attained age 40, the grandchild's trust is to be distributed outright to the grandchild. If a grandchild has not attained age 21, then the trustee is to distribute as much of the net income and principal as the trustee considers necessary for the grandchild's proper support, health, maintenance and education. After the grandchild attains age 21, the trustee is to distribute all the net income to the grandchild. The trustee also has discretion to distribute corpus to the grandchild. When a grandchild attains age 30 the trustee is to distribute $\frac{1}{3}$ of the corpus to the grandchild; at age 35, $\frac{1}{2}$ of the balance is to be distributed; and at age 40, the balance is to be distributed. If a grandchild predeceases a child, but is survived by issue, the trustee is to pay as much of the net income and principal as the trustee considers necessary for the issues' proper support, health, maintenance and education. When the youngest issue attains age 25, the trustee is to distribute the trust corpus to the grandchild's issue, by right of representation.

Decedent died on Date 4. On a timely filed estate tax return, Decedent's executor elected to treat the assets passing to the Marital Trust as qualified terminable interest property (QTIP) under § 2056(b)(7).

Decedent is survived by Spouse (age 59), Child A (age 43), Child B (age 42), and Child C (age 31). Child A has two children (ages 17 and 21) and Child B has one child (age 2).

Spouse proposes to purchase the remainder interest in the Marital Trust. A guardian ad litem will be appointed to represent any minor and unborn issue. Spouse will transfer cash

equal to the present value of the right to receive the trust corpus on the Spouse's death. Under the terms of the transaction, Spouse will be reimbursed for the gift tax imposed on the transaction. The trustee of the Marital Trust will then distribute all the trust assets to Spouse.

You have requested a ruling that if Spouse purchases the remainder interest in the Marital Trust, as proposed, then Spouse will make a gift for gift tax purposes equal to the greater of (i) (under § 2519) the present value of the remainder interest, or (ii) (under §§ 2511 and 2512) the amount transferred by Spouse in exchange for the remainder interest.

Section 2044(a) provides that the value of the gross estate includes the value of any property described in s 2044(b) in which the decedent had a qualifying income interest for life. Section 2044(b) provides that § 2044 applies to any property if a deduction was allowed with respect to the transfer of the property to the decedent under § 2056(b)(7).

Section 2056(a) provides that the value of the taxable estate is, except as limited by § 2056(b), determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse.

Under § 2056(b)(1), if an interest passing to the surviving spouse will terminate, no deduction is allowed with respect to such interest if, after termination of the spouse's interest, an interest in the property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than the surviving spouse (or the estate of such spouse).

Section 2056(b)(7)(A) provides that qualified terminable interest property (QTIP), for purposes of § 2056(a), is treated as passing to the surviving spouse, and no part of such property is treated as passing to any person other than the surviving spouse. In general, qualified terminable interest property is property in which the spouse receives a qualifying income interest for life, and with respect to which the executor makes an election to treat the property as QTIP.

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 2512(b) provides that where property is transferred for less than an adequate and full consideration in money or money's worth, the amount by which the value of the property exceeds the value of the consideration is deemed a gift.

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

Under § 2519, if a surviving spouse disposes of any part of the qualifying income interest, the spouse is treated as making a gift of the remainder interest in the underlying property (i.e., all interests in the property other than the income interest). Correspondingly, under § 2511, the disposition of the income interest by the spouse is treated as a gift, to the extent the income interest is transferred to another for less than adequate consideration.

Under § 25.2519-1(c)(1), the amount treated as a transfer upon disposition of all or part of a qualifying income interest for life in qualified terminable interest property 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 term "disposition," as used in § 2519, applies broadly to circumstances in which the surviving spouse's right to receive the income is relinquished or otherwise terminated, by whatever means. H. Rep. No. 201, 97th Cong., 1st Sess. 161 (1981).

In Rev. Rul. 98-8, 1998-7 I.R.B. 24, the surviving spouse acquired the remainder interest in a QTIP trust by transferring to the remainderman a promissory note equal to the actuarial value of the remainder interest. Subsequently, the trustee distributed the trust assets to the spouse and the spouse paid the balance due on the note with trust assets. The revenue ruling concludes that the transaction constitutes a disposition of the spouse's income interest for purposes of § 2519, resulting in a gift of the present value of the remainder interest, or in the alternative, a transfer of the promissory note for less than adequate consideration, resulting in a gift equal to the value of

the promissory note. Accordingly, the revenue ruling concludes that the spouse made a gift equal to the greater of (i) the present value of the remainder interest (pursuant to § 2519), or (ii) the value of the property or cash transferred in exchange for the remainder interest (pursuant to §§ 2511 and 2512). The ruling notes that the result would be the same if the Spouse transferred cash in exchange for the remainder interest, rather than issuing a note.

In the present case, the proposed transaction is similar to the one considered in Rev. Rul. 98-8. Therefore, Spouse will be regarded as making a gift equal to the greater of (i) the present value of the remainder interest (i.e., the amount of the transfer under § 2519 and § 25.2519-1(c)(1)), or (ii) the amount transferred by Spouse in exchange for the remainder interest (pursuant to §§ 2511 and 2512). However, the amount subject to gift tax must be adjusted to reflect any reimbursement Spouse receives under the terms of the transaction for the gift tax imposed on the transfer.

Except as we have specifically ruled herein, we express no opinion under the cited provisions or under any other provision of the Code.

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

Sincerely yours,

Assistant Chief Counsel
(Passthroughs and Special
Industries)

By _____
George L. Masnik
Chief Branch 4

Enclosure
Copy for 6110 purposes