

## Internal Revenue Service

## Department of the Treasury

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Person to Contact:

Telephone Number:

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Date:

March 30, 1999

### Legend

Taxpayer =

Decedent =

Trust =

Year =

Date =

Amount =

State =

Statute =

We received your letter dated March 2, 1999, and prior correspondence, requesting rulings under §§ 2207A, 2519 and 2702 of the Internal Revenue Code regarding the proposed severance of Trust. This letter responds to that request.

Decedent died testate in Year. Trust was established pursuant to the terms of Article V of Decedent's Last Will and Testament dated Date. Under the terms of Trust,

Taxpayer is to receive all of the net income from Trust during her lifetime. In addition, the trustees have the discretion to pay principal for Taxpayer's health or support. On the death of Taxpayer, the remaining assets of Trust are to be distributed in equal shares to the children of Taxpayer and Decedent. On Decedent's estate tax return, Decedent's estate elected to treat Trust as qualified terminable interest property ("QTIP") as provided in § 2056(b)(7).

Under the proposed transaction, Trust is to be severed into two separate trusts. One trust, Trust A, will contain sufficient assets to make gifts of Amount to each of Taxpayer's and Decedent's children, as well as pay all of the gift taxes attributable to those gifts. The remaining balance of the assets in Trust would be known as Trust B. Trust A and Trust B will each contain a strictly proportional amount of each asset contained in Trust. Both Trust A and Trust B will be held under the same terms and conditions as Trust. The severance of Trust is authorized under the laws of State. Under State Statute, a separate trust created by severance must be treated as a separate trust for all purposes from the effective date of the severance. After the severance, Taxpayer will renounce (*i.e.*, make a non-qualified disclaimer) Taxpayer's interest in Trust A.

The following rulings have been requested:

1. If Taxpayer renounces Taxpayer's interest in the property in Trust A, Taxpayer will not be deemed to have made a gift of the property in Trust B under § 2519.
2. If Taxpayer renounces Taxpayer's interest in the property in Trust A, the value of Taxpayer's income interest in Trust B will not be valued at zero under § 2702.
3. If Taxpayer renounces Taxpayer's interest in the property in Trust A, and such renunciation is conditioned on Taxpayer's children paying all gift taxes attributable to the transfer, the amount of the gift will be reduced by the gift taxes paid by the children.

Section 2501 imposes a tax on the transfer of property by gift by an individual. Section 2502(c) provides that the payment of the gift tax is the liability of the donor. Section 2511 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 2512(b) provides that, where property is transferred for less than 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 this section applies is treated as a transfer of all

interests in the property other than the qualifying income interest. Section 2519(b) provides that paragraph (a) applies to any property if a deduction was allowed with respect to the transfer of such property to the donor under § 2056(b)(7).

For gift tax purposes § 2207A(b) provides that, if for any calendar year tax is paid under chapter 12 with respect to any person by reason of property treated as transferred by such person under § 2519, such person shall be entitled to recover from the person receiving the property the amount by which (1) the total tax for such year under chapter 12 exceeds (2) the total tax which would have been payable under such chapter for such year if the value of such property had not been taken into account for purposes of chapter 12.

Section 2702 provides special valuation rules in the case of transfers of interests in trusts. Under § 2702(a), whether a transfer of an interest in trust to (or for the benefit of) a member of the transferor's family is a gift (and the value of such transfer), the value of any interest in such trust retained by the transferor or any applicable family member shall be determined as provided in paragraph (a)(2). Paragraph (a)(2) provides that the value of any retained interest that is not a qualified interest shall be treated as being zero. The value of any retained interest that is a qualified interest is determined under § 7520.

Section 25.2519-1(a) of the Gift Tax Regulations provides that a transfer of all or a portion of the income interest of the spouse in QTIP property is a transfer by the spouse under § 2511. Section 25.2519-1(c) 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 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 gift tax consequences of the disposition of the qualifying income interest are determined separately under § 25.2511-2.

Section 25.2511-2(a) provides that the gift tax is a primary and personal liability of the donor, is an excise upon the donor's 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.

Rev. Rul. 75-72, 1975-1 C.B. 310, holds that gift tax imposed on a transfer that is paid by the donee may be deducted from the value of the transferred property in determining the amount of the gift, if it is established that the payment of the tax by the donee or from the property itself is a condition of the transfer. If, at the time of the transfer, the 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 measured by the fair market value of the property passing from the donor minus the amount of the gift tax to be paid by the donee.

Rev. Rul. 81-223, 1981-2 C.B. 189, holds that, in determining the amount of the gift, the tax liability assumed by the donee may be deducted from the value of the transferred property, if the payment of the tax by the donee is a condition of the transfer.

Although § 2502(c) provides that the tax on the gift is the liability of the donor, in Rev. Rul. 75-72 and Rev. Rul. 81-223 the burden of the tax was shifted to the donees by agreement. The amount of the gift on which the gift tax was computed was reduced by the amount of gift tax paid by the donee.

As discussed above, with respect to the gift tax imposed as a result of a transfer under § 2519, § 2207A(b) statutorily shifts the burden, but not the liability, for paying the gift tax to the donee. In reimbursing the donor for the gift tax paid pursuant to the statute, the donee provides consideration for the gift. The donee's payment inures to the benefit of the donor because it reimburses the donor for gift tax that the donor was liable for and would otherwise be required to pay out of the donor's own funds. See Rev. Rul. 75-72. Accordingly, net gift treatment of a transfer under § 2519 is implicit under § 2207A(b).

Based on the above, we conclude that if Taxpayer renounces Taxpayer's interest in Trust A (i.e., makes a non-qualified disclaimer), then:

1. Taxpayer will not be deemed to have made a gift of the property in Trust B under § 2519,
2. The value of Taxpayer's income interest in Trust B will not be valued at zero under § 2702, and
3. If such renunciation is conditioned on Taxpayer's children paying all gift taxes attributable to the transfer, the amount of the gift will be reduced by the gift taxes paid by the children.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under the cited provisions or any other provisions of the Code.

This ruling 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.

Sincerely,

Assistant Chief Counsel  
(Passthroughs and Special  
Industries)

By \_\_\_\_\_  
Katherine A. Mellody  
Assistant to the Branch Chief  
Branch 4

Enclosure  
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