

## Internal Revenue Service

## Department of the Treasury

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Re:

### Legend

Settlor A =

Settlor B =

Trust =

Charity X =

This is in response to your letter dated June 11, 1999, and prior correspondence, in which you request several rulings concerning the application of § 2702 of the Internal Revenue Code.

Settlor A and Settlor B propose to establish an irrevocable charitable lead unitrust, Trust. Under the Trust terms, the trustee is to pay, for a term of 12 years, a specified percentage of the net fair market value of the trust corpus, determined annually, to a charitable recipient designated in the trust instrument, Charity X. If at any time the charitable recipient does not qualify as an organization described in §§ 170(b)(1)(A), 170(c), 2055(a) and 2522(a) of the Internal Revenue Code, the trustee is required to distribute the annual unitrust payment to one or more organizations that are qualified. The unitrust amount is to be paid annually at the end of each taxable year. The trust provides that the unitrust amount is to be paid first from trust income, and to the extent the income for the taxable year is insufficient, from principal. At the end of the 12-year term, any remaining income and corpus will be distributed to a trust for the benefit of Settlor's grandchildren. The Trust also provides for a daily proration of the unitrust amount for a short taxable year and the year of termination. A third party will be the trustee of Trust.

The trust provides that the trustee may not make any distribution to a charitable recipient of which Settlor A or Settlor B are officers or fiduciary, or to any organization over

which the Settlers have the power to direct the disposition of funds for charitable purposes, unless the by-laws of the organization are structured such that the gifts are segregated, administered, and distributed by a separate fund committee.

Article V of the Trust provides that: the trustee shall not engage in any act of self-dealing as defined in § 4941(d) of the Code, nor make any taxable expenditures as defined in § 4945(d) of the Code; except to the extent provided in § 4947(b)(3) of the Code, the trustee shall not retain any excess business holdings (as defined in § 4943(c) of the Code) which would subject the trust to tax under § 4944 of the Code or retain assets which would, if acquired by the trustee, subject the trust to tax under § 4944.

Settlers have requested the following rulings:

1. The Settlers will not retain an interest in the Trust within the meaning § 2702 and the regulations thereunder.
2. The value of the unitrust interest payable to charity and the remainder interest is determined under the valuation principles and methodology of §§ 7520 and 664.

Section 2501 provides that a tax, computed as provided in § 2502, is imposed for each calendar year on the transfer of property by gift during such calendar year by any individual, resident, or nonresident.

Section 2511(a) provides, in part, that subject to limitations contained in chapter 12, 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 2522(a) provides that, in computing an individual's taxable gifts for the calendar year, a deduction shall be allowed for the amount of all gifts to or for the use of certain governmental entities, certain corporations organized and operated exclusively for religious, charitable, scientific, educational purposes, and certain other fraternal organizations.

Section 2522(c)(2)(B) provides that, where a transfer is made to both a charitable and a noncharitable person or entity, no deduction shall be allowed for the charitable portion of the gift unless, in the case of interests other than charitable remainder interests, such 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)(vii)(a) states that the term "unitrust interest" means the right pursuant to the instrument of transfer to receive a payment, not less often than annually, of a fixed percentage of the net fair market value, determined annually, of the property which funds the unitrust interest. In computing the net fair market value of the property which funds the unitrust interest, all assets and liabilities shall be taken into account without regard to whether particular items are taken into account in determining the income from the property. The net fair market value of the property which funds the unitrust interest may be determined on any one date during the year or by taking the average of valuations made on more than one date during the year, provided that the same valuation date or dates and valuation methods are used each year. Payments under a unitrust interest may be paid for a specified term or for the life or lives of a named individual or individuals, each of whom must be living at the date of the gift and can be ascertained at such date.

Section 25.2522(c)-3(d)(1) provides that the amount of the deduction in the case of a contribution of a partial interest in property to which § 2522, applies is the fair market value of the partial interest on the date of gift. The fair market value of an annuity, life estate, term for years, remainder, reversion, or unitrust interest is its present value.

Section 25.2522(c)-3(d)(2)(v) provides that the present value of a unitrust interest is to be determined by subtracting the present value of all interests in the transferred property other than the unitrust interest from the fair market value of the transferred property.

Section 2702(a)(1) provides that solely for purposes of determining 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 the trust retained by the transferor or any applicable family member (as defined in § 2701(e)(2)) is determined as provided in § 2702(a)(2).

Section 2702(a)(2) provides that the value of any retained interest that is not a qualified interest is treated as being zero. The value of any retained interest that is a qualified interest is determined under § 7520.

Section 25.2702-1(c)(5), captioned "Charitable lead trust", provides that § 2702 does not apply to a transfer in trust if the only interest in trust, other than the remainder interest or a

qualified annuity or unitrust interest, is an interest that qualifies for a deduction under § 2522.

Based upon the facts submitted and the representations made, we conclude that the charitable interest in trust is a unitrust interest within the meaning of § 2522(c)(2)(B) and the regulations thereunder and qualifies for a gift tax charitable deduction under section 2522(a). Accordingly, we conclude that § 2702 does not apply to the proposed charitable lead unitrust. See § 25.2702-1(c)(5). Further, the present value of the charitable lead unitrust interest and remainder interest is to be determined using the appropriate interest rate prescribed under § 7520 and the methodology used in § 1.664-4T of the Income Tax Regulations.

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 Masnik  
Chief, Branch 4

Enclosure  
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