

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B09

PLR-115574-04

Date:

September 30, 2004

In Re:

Legend:

Taxpayer =

Year 1 =

Year 2 =

Spouse =

Child 1 =

Child 2 =

Child 3 =

Child 4 =

Child 5 =

Property 1 =

State =

Child 6 =

Date 1 =

Agreement =

Date 2 =

Date 3 =

Addendum =

Property 2 =

Dear :

This is in response to your letter dated October 14, 2003, and subsequent correspondence, submitted on behalf of Taxpayer, requesting a ruling regarding the applicability of § 2702 of the Internal Revenue Code.

The information submitted and representations made are summarized as follows: In Year 1 and Year 2 (dates prior to October 8, 1990), Taxpayer, Spouse, and five of their six children (Child 1, Child 2, Child 3, Child 4, and Child 5) purchased Property 1 located in State for fair market value from an unrelated party. Taxpayer acquired a life

interest, Spouse acquired a life interest that would become effective upon the death of Taxpayer, Child 1 acquired a one-third common undivided interest in the remainder, and Children 2 through 5 each acquired a one-sixth common undivided interest in the remainder. It is represented that Taxpayer, Spouse, and their five children each paid the actuarial value of their respective interest from their own resources and that none of the five children used any funds acquired from their parents to acquire their interests. Child 6 did not participate in the initial acquisition of Property 1 because he was a minor.

On Date 1, Taxpayer, Spouse, and Children 1 through 5 executed an Agreement in connection with the Property 1 acquisition. The Agreement provides, generally, for the parties' respective rights, duties, and obligations in the acquisition, ownership, and disposition of Property 1.

Article 1 of the Agreement provides that Taxpayer (the primary life tenant) and Spouse (the secondary life tenant) shall pay toward the purchase of Property 1 (including associated closing costs) an amount equal to the actuarial value of their respective rights to the use of and the income from Property 1. Taxpayer shall have a legal life estate for her natural life, and upon her death, unless Spouse predeceases her, Spouse shall have a legal life estate for his natural life.

Article 2 of the Agreement provides that Children 1 through 5 (the remaindermen) shall contribute to the purchase of Property 1 (including associated closing costs) the actuarially determined value of their respective remainder interests in such property.

Article 4 of the Agreement provides that the parties to the Agreement intend that no gift be made and agree that they shall take whatever actions are necessary to insure that no gift is in fact made. It is the express intent of the parties that they shall pay fair market value for their respective interests in Property 1. If it is at any time determined by a court of law that the actuarial interest or value used herein represents less than fair and adequate consideration with respect to each such interest, then a re-computation shall be made and the parties which have not paid fair value shall re-contribute to the other parties the difference, with interest thereon at the rate of 11 percent per annum.

Article 5 of the Agreement provides, in part, that if Property 1 should be disposed of prior to the expiration of the respective life tenancies, the proceeds into which the property is converted shall be impressed with a trust, and the life tenants (or the survivor) shall be the trustees. After the payment of income taxes, the remaining proceeds shall be held by the trustees, invested and reinvested, and the trustees shall pay to the life tenants, at least annually, all income (but not principal) earned by the trust assets. Upon the death of both life tenants, the trust shall terminate and the trust assets shall be immediately paid to the remaindermen in accordance with their respective interests.

Article 6 of the Agreement provides, in part, that the sale of Property 1 shall require the consent of the life tenants and the remaindermen.

Article 8 of the Agreement provides that the parties agree that Child 1 may transfer to Child 6 (upon his attainment of age 18) a one-sixth interest in the remainder estate, being one-half of Child 1's interest, without the consent of any party to this agreement, provided that such transferee agrees to be bound by the terms of the Agreement.

On Date 2, Child 6 attained the age of majority and received his one-sixth interest by conveyance from Child 1. On Date 3, Taxpayer, Spouse, and Children 1 through 6 executed an Addendum to the Agreement. Taxpayer, Spouse, and Children 1 through 6 are collectively referred to as the "Family Members."

The Addendum modifies the Agreement by adding a new Article 10 which provides that in the event the parties agree to collectively acquire any subsequent real property as life tenants and remaindermen, the newly acquired property shall be subject to the same terms and conditions as between the life tenants and remaindermen as set forth in the Agreement.

The Addendum also adds a new Article 11 which provides that in the event substantial improvements are made to any of the properties that are the subject of the Agreement, the life tenants and the remaindermen shall contribute toward the cost thereof the actuarial interest that they shall have therein. Notwithstanding the foregoing, by agreement of the parties, any such improvements may be made by Taxpayer, or by Spouse upon the death of Taxpayer in which event such improvements shall belong to the party who paid for such improvements and may be thereafter severed and removed from the real property.

The Addendum also provides that Child 6 is added as a one-sixth remainderman upon such transfer by his sister, Child 1, and that Child 6 agrees to be bound by all of the terms and conditions of the Agreement, as amended.

The Agreement and Addendum are collectively referred to as the "Current Agreement."

Subsequent to the initial acquisition of Property 1, the Family Members acquired additional property located in State in the same manner of holding title as they employed for Property 1. All of the properties so acquired, other than Property 1, are referred to as Property 2.

The parties represent that they have not acquired any property as life tenants and remaindermen after October 8, 1990, and that the Current Agreement has not been modified or amended after October 8, 1990.

Subject to the receipt of a favorable ruling from the Service, the Family Members propose to sell Property 1 for fair market value to an unrelated party. The

Family Members intend to continue to own Property 2, however, a decision to sell Property 2 could be made in the future. Upon any disposition of Property 1, the proceeds would be placed in trust pursuant to the provisions of the Current Agreement.

Taxpayer has requested the following rulings:

(1) The proceeds of a sale or other conveyance of Property 1 and the principal proceeds of any investments or reinvestments thereof, that are held in trust pursuant to the provisions of the Current Agreement, will continue to be treated as a transfer occurring prior to October 8, 1990, for purposes of applying the provisions of Chapter 14 of the Code, and, therefore, Chapter 14 will not apply thereto;

(2) The proceeds of a sale or other conveyance of all or a portion of Property 2 and the principal proceeds of any investments or reinvestments thereof, that are held in trust pursuant to the provisions of the Current Agreement, will continue to be treated as a transfer occurring prior to October 8, 1990, for purposes of applying the provisions of Chapter 14 of the Code, and, therefore, Chapter 14 will not apply thereto; and

(3) After the sale of Property 1, Property 2 will continue to be treated as property acquired pursuant to a transfer occurring prior to October 8, 1990.

The provisions of Chapter 14 of the Code were added by the Revenue Reconciliation Act of 1990 and are effective for transfers occurring after October 8, 1990.

Section 2702(a)(1) provides, generally, 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 such trust retained by the transferor or any applicable family member shall be determined as provided in § 2702(a)(2).

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

In this case, Property 1 and Property 2 were both acquired prior to October 8, 1990. The Agreement and Addendum relating to the acquisition of Property 1 and Property 2 were also executed prior to October 8, 1990. Neither the sale or other disposition of Property 1 or Property 2, nor the deposit of the proceeds of such sale or disposition in trust pursuant to the Current Agreement will involve any transfer of value among the Family Members. In addition, the Family Members will have substantially identical interests both before and after the proposed transaction.

Based on the facts submitted and representations made, we conclude that the proceeds of a sale or other conveyance of Property 1 and/or all or a portion of

Property 2, and the principal proceeds of any investments or reinvestments that are held in trust pursuant to the provisions of the Current Agreement will be treated as a transfer or transfers occurring prior to October 8, 1990, for purposes of applying the provisions of Chapter 14 of the Code, and, therefore, Chapter 14 will not apply thereto. Further, after the sale of Property 1, Property 2 will continue to be treated as property acquired pursuant to a transfer occurring prior to October 8, 1990.

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. If there is a change in material fact or law (local or federal) before the transactions considered in this ruling take effect, the ruling will have no force or effect. 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. Specifically, no opinion is expressed or implied with respect to the income, estate, or gift tax consequences of any aspect of any transaction discussed in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to Taxpayer.

Sincerely,

Stephanie N. Bland
Acting Senior Technician Reviewer, Branch 4
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure:

Copy for § 6110 purposes