

Internal Revenue Service

Department of the Treasury

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Person to Contact:

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Date:

February 16, 2000

Legend

Estate =

Executor =

Trust =

Reformed Trust =

Trustee =

Decedent =

Beneficiary 1 =

Beneficiary 2 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

\$S =

\$T =

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\$U =

\$V =

W =

Dear Sir or Madam:

We received your letter dated September 28, 1999, submitted on behalf of Estate, of which you are Executor. Rulings are sought concerning the application of § 2055(e)(3) of the Internal Revenue Code to the proposed reformation of Trust, of which you are Trustee. This letter responds to that request.

The facts and representations submitted are summarized as follows: On Date 1, Decedent created a holographic will and a testamentary trust ("Will"). Will instructed that the residue of Decedent's estate be used to fund Trust. Furthermore, Will provided for \$S a month to be paid to Beneficiary 1 and \$T a month to be paid to Beneficiary 2 for as long as each shall live. The remainder was left for the benefit of a charitable trust to be administered by Trustee. Decedent died on Date 2. Decedent's Will was admitted to probate on Date 3.

The terms of Trust, as contained in Will, do not qualify Estate for the federal estate tax charitable deduction for the amount of the charitable interest because Trust does not qualify as a charitable remainder trust under § 664. Trustee filed a petition to reform Trust with the appropriate court on Date 4. The court has instructed the Trustee to seek a private letter ruling from the Internal Revenue Service regarding the tax effects of the proposed construction and reformation of Trust prior to judicial approval of the reformation of Trust.

The Executor requested and received an extension of time to file the Estate Tax Return (the "Return"). The Return is due, including extensions, on Date 5.

Reformed Trust would be funded with the residue of Decedent's estate after the payment of all debts, expenses, and taxes of the Estate. Section 3.2 of Article III of Reformed Trust provides: (A) a level annuity for Beneficiary 1 of \$U per year, payable in monthly installments for life; (B) a level annuity for Beneficiary 2 of \$V per year, payable in monthly installments for life; and (C) an annual annuity amount to be distributed to one or more charities selected by the Trustee. While either Beneficiary 1 or Beneficiary 2 are alive, the annuity amount to be distributed to one or more charities shall be W percent of the initial value of the assets of Reformed Trust less the amount of the annuities paid to Beneficiary 1 and Beneficiary 2 during the year. At the death of Beneficiary 1, that annuity amount shall cease to be paid and shall instead be added to the amount of the annuity to be paid to one or more charities. At the death of

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Beneficiary 2, that annuity amount shall cease to be paid and shall instead be added to the amount of the annuity to be paid to one or more charities.

At the death of the last to die of Beneficiary 1 and Beneficiary 2, Reformed Trust will be a wholly charitable trust. Reformed Trust will not have a term certain, but can be terminated by the Trustee after the deaths of both Beneficiary 1 and Beneficiary 2, under the authority of Section 3.3(D) of Article III of Reformed Trust as long as the assets remaining in Reformed Trust at the time of the termination are distributed outright to one or more charities selected by the Trustee upon such termination. Section 1.7 of Article I of Reformed Trust states that all references to "charities" mean organizations which are exempt from federal income tax under § 501(c)(3) of the Code and which are described in §§ 170(c) and 2055(a) of the Code. Reformed Trust will be effective as of Date 2.

You effectively have requested the following rulings: (1) the amount of Decedent's bequest for the benefit of a charitable trust to be administered by Trustee is a reformable interest under § 2055(e)(3)(C); (2) Reformed Trust will be a qualified charitable remainder annuity trust under the provisions of § 664(d)(1); (3) The reformation of Trust will constitute a qualified reformation under the provisions of § 2055(e)(3); and (4) Decedent's bequest for the benefit of a charitable trust to be administered by Trustee is deductible despite the fact that no specific charities are named.

Section 664(d)(1) provides that a charitable remainder annuity trust is a trust:

(A) from which a sum certain (which is not less than 5 percent nor more than 50 percent of the initial net fair market value of all property placed in trust) is to be paid, not less often than annually, to one or more persons (at least one of which is not an organization described in § 170(c) and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals,

(B) from which no amount other than the payments described in subparagraph (A) and other than qualified gratuitous transfers described in subparagraph (C) may be paid to or for the use of any person other than an organization described in § 170(c),

(C) following the termination of the payments described in subparagraph (A), the remainder interest in the trust is to be transferred to, or for the use of, an organization described in § 170(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as defined in subsection (g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined by subsection (g)), and

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(D) the value (determined under § 7520) of such remainder interest is at least 10 percent of the initial net fair market value of all property placed in trust.

Section 664(d)(1)(D) was added to the Code by § 1086 of the Taxpayer Relief Act of 1997, P.L. 105-34, and generally applies to transfers in trust after July 28, 1997.

Section 2055(a) provides that, for purposes of the federal estate tax, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, and transfers to or for a corporation or certain other organizations organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes.

Section 2055(e)(2) provides that where an interest in property (other than an interest described in § 170(f)(3)(B)) passes or has passed from the decedent to a person, or for a use, described in § 2055(a), and an interest (other than an interest that is extinguished upon the decedent's death) in the same property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to a person, or for a use, not described in § 2055(a), no deduction is allowed under § 2055(a) for the interest that passes or has passed to the person, or for a use, described in § 2055(a), unless (A) in the case of a remainder interest, the interest is in 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 interests other than charitable remainder interests, such interest is in the form of a guaranteed annuity described in § 20.2055-2(e)(2)(vi) of the Estate Tax Regulations or is a fixed percentage distributed yearly of the fair market value of the property (to be determined yearly).

Section 2055(e)(3)(A) provides that a deduction is allowed under § 2055(a) for any qualified "reformation."

Section 2055(e)(3)(B) defines the term "qualified reformation" to mean a change of a governing instrument by reformation, amendment, construction, or otherwise that changes a reformable interest into a qualified interest, but only if (i) any difference between the actuarial value (determined as of the date of the decedent's death) of the qualified interest, and the actuarial value (as so determined) of the reformable interest does not exceed five percent of the actuarial value (as so determined) of the reformable interest, (ii) in the case of a charitable remainder interest, the nonremainder interest (before and after the qualified reformation) terminates at the same time, or, in the case of any other interest, the reformable interest and the qualified interest are for the same period, and (iii) the change is effective as of the date of the decedent's death.

Section 2055(e)(3)(C)(i) defines the term "reformable interest" to mean any interest for which a deduction would be allowable under § 2055(a) at the time of the decedent's death but for § 2055(e)(2).

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Section 2055(e)(3)(C)(ii) provides that the term “reformable interest” does not include any interest unless, before the remainder vests in possession, all payments to persons other than an organization described in § 2055(a) are expressed either in specified dollar amounts or a fixed percentage of the fair market value of the property.

Section 2055(e)(3)(C)(iii) provides, however, that the restriction in § 2055(e)(3)(C)(ii) does not apply if a judicial proceeding is commenced to change the charitable interest into a qualified interest not later than the 90th day after the last date (including extensions) for filing the estate tax return, if one is required to be filed.

Section 2055(e)(3)(D) defines the term “qualified interest” to mean an interest for which a deduction is allowable under § 2055(a).

Section 2055(e)(3)(E) provides that the deduction referred to in subsection (A) shall not exceed the amount of the deduction which would have been allowable for the reformable interest but for paragraph (2).

We conclude that the interest passing to charity under Reformed Trust is a reformable interest within the meaning of § 2055(e)(3)(C)(i) because an estate tax deduction for the value of the remainder interest would have been allowable under § 2055(a) but for the provisions of § 2055(e).

Beneficiary 1's and Beneficiary 2's respective nonremainder life interests terminate at the same time before and after the reformation, and the reformation will be effective as of the date of Decedent's death. The difference between the actuarial value of the qualified interest (determined as of the date of decedent's death) and the actuarial value (as so determined) of the reformable interest does not exceed 5 percent of the actuarial value of the reformable interest.

Reformed Trust will contain the provisions set forth in Rev. Rul. 72-395, 1972-2 C.B. 340, as modified by Rev. Rul. 80-123, 1980-1 C.B. 205, and Rev. Rul. 82-128, 1982-2 C.B. 71, and clarified by Rev. Rul. 82-165, 1982-2 C.B. 117. Consequently, the trust meets the requirements of a charitable remainder annuity trust under § 664. Accordingly, provided that Reformed Trust is valid under applicable local law, we conclude that the proposed reformation will be a qualified reformation within the meaning of § 2055(e)(3). Estate will be entitled to a charitable deduction under § 2055 with respect to the present value of the charitable remainder interests in Reformed Trust.

Section 1.7 of Article I of Reformed Trust defines “charities” with reference to §§ 170(c) and 2055(a). Neither § 2055(a) nor § 664(d)(1)(C) requires a specific charity to be named to qualify under the section. Therefore, we conclude that the interest passing to charity is deductible despite the fact that no specific charities are named

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because the definition of charity in Section 1.7 of Article I of Reformed Trust is sufficient to qualify under §§ 2055(a) and 664(d)(1)(C).

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,

James C. Gibbons

James C. Gibbons
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Office of the Assistant Chief Counsel
(Passthroughs & Special Industries)

Enclosure

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