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Department of the Treasury

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Person To Contact:

Telephone Number:

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Date:

April 16, 2019

Legend

Trustee

Trust

Grantor

Date 1

Date 2

Date 3

Date 4

Charity A

Charity B

Charity C

Termination Date

a

b

c

d

Dear _____ :

This letter responds to your authorized representative's letter dated November 6, 2018, and subsequent correspondence, requesting rulings under §§ 7520 and 507(c) of the Internal Revenue Code with regard to Trust.

The facts and representations submitted are summarized as follows:

Grantor died on Date 1. Pursuant to Grantor's will, Grantor's interests in several specified grantor retained annuity trusts were distributed to Trustee to hold, administer, and distribute in accordance with the terms of Trust.

Trust was established as a charitable lead annuity trust, and Charity C was granted an interest in Trust in the form of a guaranteed annuity interest under § 2055(e)(2)(B). Article II of Trust provides, in relevant part, that the initial annuity amount was equal to a percent of the initial value of the trust property. The annuity amount is increased on each anniversary of the trust by b percent (the ramp rate) of the prior year's annuity amount. The annuity amount is to be paid in equal quarterly installments from income, and to the extent that income is not sufficient, from principal. Any trust accounting income of the trust for a taxable year in excess of the annuity amount is to be distributed to Charity C and devoted solely to the purposes set forth in § 170(c)(2)(B). In determining the annuity amount the trustee is to prorate the same, on a daily basis, for a short taxable year. No additional contributions are to be made to Trust after the initial contribution.

Trust is to have a term, computed with respect to the date of Grantor's death, just sufficient to make the income interest in the trust for which a deduction would be allowed under § 2055 have an aggregate value of c percent of the aggregate fair market value of all amounts in the trust at its commencement. Upon the expiration of this term, the trustee is to distribute all trust principal to Grantor's children, the remainder beneficiaries.

On Date 2, Charity C was divided into two separate foundations by court order, Charity A and Charity B. Charity A and Charity B each receive one-half of Charity C's guaranteed annuity interest in Trust.

The Trustee represents that, before any distribution to the remainder beneficiaries, all annuity payments, including interest, will be made to Charity A and Charity B in accordance with the terms of Grantor's will and the trust instrument and consistent with the schedule of amounts attached to the ruling request.

You have requested the following rulings:

- 1) Under the terms of the will and the regulations, Trust will terminate on Termination Date.
- 2) The termination of Trust on Termination Date will not result in the imposition of a termination tax under § 507(c).

LAW AND ANALYSIS

Ruling 1

Section 2055(a) allows a deduction from the value of a decedent's gross estate for the amount of bequests to or for the use of any organization organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes.

Under § 2055(e)(2), the estate tax charitable deduction is not allowable 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 which 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), unless (A) in the case of a remainder interest, such interest is in a trust which is 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 any other interest, 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 20.2055-2(e)(1) of the Estate Tax Regulations provides that in the case of a decedent dying after December 31, 1969, where an interest in property passes or has passed from the decedent for charitable purposes and an interest in the same property passes or has passed from the decedent for private purposes after October 9, 1969, no deduction is allowed under § 2055 for the value of the interest which passes or has passed for charitable purposes unless the interest in property is a deductible interest described in § 20.2055-2(e)(2).

Under § 20.2055-2(e)(2)(vi)(a), the term “deductible interest” includes a guaranteed annuity interest. A “guaranteed annuity interest” is a right to receive a guaranteed annuity. A guaranteed annuity is an arrangement under which a determinable amount is paid periodically, but not less often than annually, for a specified term or for the life or lives of an individual or individuals, each of whom must be living at the date of death of the decedent and can be ascertained at such date. An amount is determinable if the exact amount which must be paid under the conditions specified in the instrument of transfer can be ascertained as of the appropriate valuation date.

Under § 20.2055-2(e)(2)(vi)(b), a charitable interest is a guaranteed annuity interest only if it is a guaranteed annuity interest in every respect. Under § 20.2055-2(e)(2)(vi)(d), where a guaranteed annuity interest is in trust, the instrument may provide that income of the trust in excess of the amount required to pay the guaranteed annuity interest shall be paid to or for the use of a charity. Nevertheless,

the amount of the deduction is limited to the fair market value of the guaranteed annuity interest.

Section 20.2055-2(f)(1) provides that the amount of the deduction in the case of a contribution of a partial interest in property is the fair market value of the partial interest at the appropriate valuation date, as defined in § 20.2055-2(e)(2)(vi)(h). The fair market value of an annuity, life estate, term for years, remainder, reversion, or unitrust interest is its present value.

Section 20.2055-2(f)(2)(iv) provides that the present value of a guaranteed annuity interest described in § 20.2055-2(e)(2)(vi) is to be determined under § 20.2031-7. A deduction will be allowed under § 2055 only for the minimum amount it is evident the charity will receive. Thus, if the date of death value of the guaranteed annuity interest exceeds the date of death value of the trust assets, the allowable deduction is limited to the date of death value of the trust assets.

Section 7520(a)(1) provides, in part, that if an income, estate, or gift tax charitable contribution is allowable for any part of the property transferred, the taxpayer may elect to use the federal midterm rate for either of the two months preceding the month in which the valuation date falls.

Section 20.7520-1 provides, in relevant part, that in the case of estates of decedents with valuation dates after April 30, 1989, the fair market value of annuities, interests for life or for a term of years (including unitrust interests), remainders, and reversions is their present value determined under this section. See § 20.2031-7(d) for the computation of the value of annuities, unitrust interests, life estates, terms for years, remainders, and reversions.

Section 20.7520-2 provides, in relevant part, that the fair market value of annuities, interests for life or for a term of years, remainders, and reversions for which an estate tax charitable deduction is allowable is the present value of such interests determined under § 20.7520-1.

Trust's Closing Agreement with the IRS, which is attached to the ruling request, recognizes that the Charities' interest in the Trust was in the form of a guaranteed annuity interest, as required by § 2055(e)(2)(B), and that Trust is a testamentary charitable lead annuity trust. Accordingly, the Closing Agreement allowed an estate tax deduction of c percent of the estate's Initial Value.

To determine whether the Trust will properly terminate under the terms of the Grantor's will, a termination date must be calculated under § 7520 so that the present value of the Charities' guaranteed annuity interest equals c percent of Trust's initial value. We performed calculations based upon our understanding of the trust mechanics as set forth above and basic actuarial and financial principles associated

with the time value of money and the theory of interest. Our goal was to determine a termination date that would render the total present value of the charitable annuity to equal c percent of the initial trust value. In order to effect this, the final payment may need to be a partial payment that occurs between two otherwise scheduled payment dates.

We determined that the theoretical partial quarterly payment would need to occur between the payment scheduled for Date 3 and the payment scheduled for Date 4. We further identified that a partial payment d days into the quarter, discounted back to the date of death will render the total present value of the charitable annuity to equal c percent of the initial trust value as required. D days after Date 3 is Termination Date. Thus, based on the facts submitted and representations made we conclude that Trust will terminate on Termination Date.

Ruling 2

Section 4947(a)(2) (relating to split-interest trusts) provides that, in the case of a trust not exempt from tax under § 501(a), not all of the unexpired interests in which are devoted to a purpose described in § 170(c)(2)(B), and which has amounts in trust for which a deduction was allowed under, *inter alia*, § 2055, § 507 (relating to termination of private foundation status) shall apply as if that trust were a private foundation. Trust is described in § 4947(a)(2).

Section 507 imposes a “termination tax” on any private foundation that notifies the Secretary of its intention to terminate or the status of which is terminated by the Secretary as a result of willful or flagrant violations of the private foundation provisions. The amount of the tax is the lower of the “aggregate tax benefit” resulting from the tax-exempt status of the private foundation or the fair market value of its assets.

Generally, § 507 does not apply to split-interest trusts. Section 53.4947-1(e)(1) of the Foundation and Similar Excise Taxes Regulations provides that § 507(a) shall not apply to a trust described in § 4947(a)(2) by reason of any payment to a beneficiary that is directed by the terms of the governing instrument of the trust and is not discretionary with the trustee or, in the case of a discretionary payment, by reason of, or following, the expiration of the last remaining charitable interest in the trust.

The examples in § 53.4947-1(e)(2) illustrate the application of § 53.4947-1(e). In *Example (2)*, H creates a trust under which X, an organization described in § 501(c)(3), receives \$20,000 per year for a period of 20 years, remainder to S, H's son. H is allowed a deduction under § 2522 for the present value of X's interest. When the final payment to X has been made at the end of the 20-year period in accordance with the terms of the trust, the provisions of § 4947(a)(2) will cease to apply to the trust because the trust no longer retains any amounts for which the deduction under § 2522 was

allowed. The final payment to X is not considered a termination of the trust's private foundation status within the meaning of § 507(a).

In this case, Trust is terminating by reason of a payment to a beneficiary that is directed by the terms of the governing instrument of the trust and is not discretionary with the trustee. Similar to § 53.4947-1(e)(2), *Example (2)*, when Trust terminates on Termination Date, the provisions of § 4947(a)(2) will cease to apply because Trust no longer retains any amounts for which the deduction under § 2055 was allowed. Thus, the final payment to the remainder beneficiaries will not be considered a termination of the trust's private foundation status within the meaning of § 507(a). Without a termination under § 507(a), no termination tax under § 507(c) applies to Trust.

Accordingly, based on the facts submitted and representations made we conclude that the termination of Trust on Termination Date will not result in the imposition of the § 507(c) termination tax.

In accordance with the Power of Attorney on file with this office, we have sent a copy of this letter to your authorized representatives.

Except as expressly provided herein, we neither express nor imply any opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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. 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.

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

Sincerely,

Lorraine E. Gardner

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures

Copy for § 6110 purposes
Copy of this letter