

Internal Revenue Service

Department of the Treasury

Number: **200121015**
Release Date: 5/25/2001
Index Number: 2702-00.00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:4-PLR-115276-00
Date:

February 14, 2001

Re:

Legend

Settlor A =
Settlor B =
Property =

State =
X =

Dear :

This is in response to your letter dated October 17, 2000, and prior correspondence, requesting several rulings concerning the application of § 2702 of the Internal Revenue Code.

The facts and representations submitted are summarized as follows. Settlor A and Settlor B, husband and wife, own Property as tenants in common. Property is located in State. Property consists of one parcel on the local tax map and is assessed as one parcel for property tax purposes. Property consists of X acres and is improved by a residence, a small shed, and a small caretaker's facility. Property is similar in size to nearby properties used for residential purposes. It is represented that Property and the residence situated on Property qualifies as a residence of Settlor A and Settlor B under § 280A(d)(1), without regard to § 280A(d)(2). Each Settlor proposes to convey his or her one-half interest in Property to a separate qualified personal residence trust (QPRT). Trust A will hold Settlor A's one-half interest in Property, and Trust B will hold Settlor B's one-half interest.

During the term of Trust A and Trust B, the respective Settlor will be entitled to the exclusive use, possession and enjoyment of the interest in property held by the trustee and all the trust income must be distributed to the Settlor annually. Each trust document prohibits distribution of corpus to anyone other than the Settlor.

Other than Property, each trust will hold no assets other than amounts permitted under § 25.2702-5(c)(5) of the Gift Tax Regulations. The trusts provide that the Settlor's interest in the trust may not be commuted. In addition, the trustee of each trust

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is prohibited from selling or otherwise transferring any interest in Property held in the trust directly or indirectly to the Settlor, the Settlor's spouse or any entity controlled by the Settlor or the Settlor's spouse, in any transaction that would result in disqualification of the trust as a qualified personal residence trust under § 25.2702-5(c) of the Gift Tax Regulations.

Each trust will terminate at the earliest of the expiration of 20 years from the date it is established or the date of the respective Settlor's death, or the date the trust ceases to be a QPRT.

If a trust terminates at the end of the 20-year term, the trustee shall distribute the trust property equally to the respective living children of the Settlor. If the Settlor dies before the 20-year term expires, the assets of the trust are to be paid to the Settlor's estate. If the trust ceases to be a QPRT with respect to any assets held in trust, the trustee must hold those assets as a qualified annuity interest payable to the Settlor. The trust as converted must function as a qualified annuity trust from the conversion date until the termination of trust as specified in § 25.2702- 5(c)(8)(ii) of the Gift Tax Regulations.

You represent that Settlor A and Settlor B each previously established a separate QPRT to which each transferred his or her interest in their principal residence.

You have requested the following rulings:

1. Property, to be transferred to Trust A and Trust B, is a personal residence within the meaning of § 25.2702-5(c)(2).
2. Trust A and Trust B will constitute qualified personal residence trusts within the meaning of § 25.2702-5(c).

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 such trust retained by the transferor or any applicable family member (as defined in § 2701(e)(2)) shall be 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 2702(a)(3)(A)(ii) provides that § 2702(a) shall not apply to any transfer of an interest in trust all the property in which consists of a residence to be used as a personal residence by persons holding term interests in such trust.

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Section 25.2702-5(a)(1) provides, in part, that § 2702 does not apply to a transfer in trust meeting the requirements of that section. A transfer in trust meets the requirements of the section only if the trust is a personal residence trust as defined in § 25.2702-5(b). Section 25.2702-5(b)(1) provides that a personal residence trust is a trust the governing instrument of which prohibits the trust from holding any asset other than one residence to be used as the personal residence of the term holder. A trust meeting the requirements of a “qualified personal residence trust” as defined in § 25.2702-5(c) is treated as a personal residence trust. A trust of which the term holder is the grantor that otherwise meets the requirements of a personal residence trust or a qualified personal residence trust is not a personal residence trust or a qualified personal residence trust if, at the time of the transfer the term holder already holds term interests in two trusts that are personal residence trusts or qualified personal residence trusts of which the term holder was the grantor.

Section 25.2702-5(c)(1) provides that for purposes of § 2702(a)(3)(A)(ii), a qualified personal residence trust is a trust meeting all the requirements of the section. These requirements must be met by provisions in the governing instrument, and these governing instrument provisions must by their terms continue in effect during the existence of any term interest in the trust.

Section 25.2702-5(c)(2)(i) provides that a personal residence of a term holder is either the principal residence of the term holder (within the meaning of § 1034), one other residence of the term holder (within the meaning of § 280A(d)(1) but without regard to § 280A(d)(2)), or an undivided fractional interest in either.

Section 25.2702-5(c)(2)(ii) provides that a personal residence may include appurtenant structures used by the term holder for residential purposes and adjacent land not in excess of that which is reasonably appropriate for residential purposes (taking into account the residence's size and location). The fact that a residence is subject to a mortgage does not affect its status as a personal residence. The term personal residence does not include any personal property (e.g., household furnishings).

Section 25.2702-5(c)(2)(iii) provides that the principal residence of the term holder will not fail to meet this requirement merely because a portion of the residence is used in an activity meeting the requirements of § 280A(c)(1) or (4), (relating to the deductibility of expenses related to certain uses in a trade or business of the taxpayer), provided that such use is secondary to use of the residence as a residence. A residence is not used primarily as a residence if it is used to provide transient lodging and substantial services in connection with the provision of lodging (e.g., a hotel or a bed and breakfast).

In this case, Property is comparable in size to other adjoining and nearby residential properties. Based on the facts submitted and the representations made, we conclude that Property is not in excess of that which is reasonably appropriate for

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residential purposes within the meaning of § 20.2702-5(c)(2)(ii) and that Property, including improvements, is a personal residence within the meaning of § 25.2702-5(c)(2). We further conclude that Trust A and Trust B satisfy the requirements of § 25.2702-5(c) and constitute qualified personal residence trusts.

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 based on the facts and applicable law in effect on the date of this letter. If there is a change in material fact or law (local or Federal) before the transactions considered in the ruling take effect, the ruling will have no force or effect. If the taxpayer is in doubt whether there has been a change in material fact or law, a request for reconsideration of this ruling should be submitted to this office.

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

Sincerely yours,
Associate Chief Counsel
(Passthroughs and Special Industries)
By: George Masnik
Chief, Branch 4

Enclosure
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