

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:B04-PLR-154774-01

Date:

February 04, 2002

In Re:

**LEGEND:**

Taxpayer =

Trustee =

Trust =

Restated Trust =

Date 1 =

Date 2 =

Termination Date =

Dear :

This letter is in reply to your letter of October 3, 2001, requesting two rulings. You first requested a ruling that the charitable lead interests in two charitable trusts created under the Restated Trust will constitute unitrust interests within the meaning of section 2055(e)(2)(B) of the Internal Revenue Code and section 20.2055-2(e)(2)(vii) of the Estate Tax Regulations, the value of which, determined under section 20.2055-2(f)(2)(v), will be deductible under section 2055. We declined to rule on the second request.

**FACTS:**

On Date 1, Taxpayer established a revocable inter vivos trust ("Trust") which provides for her during her lifetime. On Date 2, Taxpayer completely restated the trust ("Restated Trust"). Article I, Paragraph A of the Restated Trust provides that during Taxpayer's life, the Trustee or successor trustees shall pay to Taxpayer or apply for her benefit, the entire net income of the trust estate in annual or more frequent installments. At the written request of Taxpayer, the Trustee or successor trustees shall pay to Taxpayer so much of the principal of the trust estate as Taxpayer shall request in writing. Article I, Paragraph B provides that in the event that Taxpayer becomes incapacitated or disabled, the successor trustees shall distribute to her or for her benefit, from income or principal, such sums as the successor trustees, taking into consideration the other resources of Taxpayer, deem reasonably necessary for the support, care, comfort and maintenance of Taxpayer in the standard of living to which

PLR-154774-01

she is accustomed. On Taxpayer's death, the Trust becomes irrevocable.

Article I, Paragraph C provides that, upon the death of Taxpayer, the successor trustees may pay from principal of the trust estate the last illness, funeral and burial expenses of Taxpayer, and any and all debts of Taxpayer owing at Taxpayer's death. Paragraph C further provides that in the event there are insufficient assets in the Taxpayer's probate estate to satisfy specific, demonstrative or pecuniary bequests provided for in Taxpayer's will admitted to probate, the successor trustees shall satisfy the gifts from the assets of the trust estate.

Article I, Paragraphs E and F provide that upon Taxpayer's death, and after various disbursements have been made under Article I, Paragraphs C and D, the successor trustees are to divide the balance of the trust estate into two shares, and distribute one share to Charitable Trust 1, a charitable lead trust, and one share to Charitable Trust 2, also a charitable lead trust. Article I, Paragraph G provides that the term of Charitable Trust 1 will begin upon the death of Taxpayer and terminate on the Termination Date. Article I, Paragraph H provides that the term of Charitable Trust 2 will begin upon the death of Taxpayer and terminate on the Termination Date or on the seventh year anniversary of Taxpayer's death, whichever occurs first.

Article I, Paragraphs G and H provide that during the term of each charitable trust, the successor trustees shall pay the Unitrust Amount each year in equal shares to seven named charitable organizations that qualify under sections 170(c)(2) and 2055(a). Paragraphs G and H of Article I further provide that the Unitrust Amount for each tax year is equal to five percent of the net fair market value of the trust assets determined as of the first business day of the year ("Unitrust Amount").

Article I, Paragraph I provides that payments of the Unitrust Amount for each tax year shall be made annually at the end of each taxable year of Charitable Trust 1 and Charitable Trust 2. The payments shall be made first from the ordinary taxable income of the trust (including short-term capital gains) which is not unrelated business income and, to the extent not so satisfied, from fifty percent of the unrelated business income, the long-term capital gains of the trust, the balance of the unrelated business income, the tax-exempt income, any accumulated income, and finally the principal of the trust, in that order. Any net income for a taxable year in excess of the Unitrust Amount shall be added to principal.

Article I, Paragraph I further provides that for a short taxable year and for the taxable year in which payments of the Unitrust Amount terminate, the successor trustees shall prorate the Unitrust Amount on a daily basis in accordance with section 1.664-3(a)(1)(v) of the Income Tax Regulations. In the event that the net fair market value of the trust assets as of the first business day of any taxable year has been incorrectly determined and as a result a payment to charitable beneficiaries exceeds or is less than the payment required to be made, Article I, Paragraph I provides that within a reasonable period after the final determination of the correct net fair market value the successor trustees shall pay to charitable beneficiaries (in the case of an

PLR-154774-01

undervaluation) or shall be repaid by charitable beneficiaries (in the case of an overvaluation) an amount equal to the difference between the amount which the successor trustees should have paid if the correct valuation had been used and the amount which successor trustees actually paid.

Paragraph I of Article I authorizes the successor trustees to accept, from the successor trustees or any other person, additional contributions to the trust following the initial contribution. For any taxable year in which an additional contribution is received, the Unitrust Amount shall (subject to proration as provided above, if required) be five percent of the sum of (1) the net fair market value of the trust assets as of the first business day of such taxable year and (2) that proportion of the net fair market value of the additional contribution as of the date of its transfer to the successor trustees which the number of days in the period beginning with the date of such transfer and ending with the earlier of the last day of the taxable year or the Termination Date bears to the number of days in the period beginning with the first day of the taxable year and ending with the earlier of the last day of the taxable year or the Termination Date.

Paragraph I of Article I further provides that should an addition to either charitable trust be made as a result of the death of an individual, the obligation to make the payment with respect to such addition shall commence with the date of the death of such individual, but the successor trustees may defer or may estimate the amount of payments due charitable beneficiaries on account of such addition for the period from the date of death until the end of the taxable year of the trust in which occurs the earlier of the end of a reasonable period of administration or settlement of the estate of such individual or complete funding of such addition. Additionally, Paragraph I provides that in case the successor trustees defer or estimate the amount of payments due charitable beneficiaries as the result of such addition, the amount which is payable to charitable beneficiaries on account of such addition for the period described above shall be retroactively determined within a reasonable period of time after the end of such period, and the successor trustees shall pay to charitable beneficiaries (in the case of an underpayment) or shall be repaid by charitable beneficiaries (in the case of an overpayment) the amount of any difference between the amount properly payable and the amount paid. For this purpose, the Unitrust Amount on account of such addition shall be determined in accordance with the special method provided in section 1.644-1(a)(5) (or the corresponding section of any subsequent U.S. Treasury Regulations). Interest computed at the rate required by the said regulations shall be added to any such difference.

Article I, Paragraph I also provides that if one or more of the charitable beneficiaries is not an organization described in sections 170(b)(1)(A), 170(c), 2055(a) and 2522(a), at the time any payment is to be made to the charitable beneficiaries under Article I, Paragraphs G and H, the successor trustees shall instead distribute such payments to the other named charitable beneficiaries which are such organizations, or if none, to one or more organizations described in said sections in such proportions as the successor trustees shall select in the successor trustees' sole

PLR-154774-01

discretion.

Paragraph I of Article I provides that the successor trustees shall make distributions at such time and in such manner as not to subject either charitable lead unitrust to tax under section 4942. The successor trustees shall not engage in any act of self-dealing as defined in section 4941(d) and shall not make any taxable expenditures as defined in section 4945(d). The successor trustees shall not acquire any assets or retain assets which would, if acquired by the successor trustees, subject the trusts to tax under section 4944, or retain any excess business holdings within the meaning of section 4943(c) which would subject the trusts to tax under section 4943.

Upon Taxpayer's death, the trusts become irrevocable. However, Article II provides that the successor trustees may amend the Restated Trust at any time for the sole purpose of enabling the charitable trusts to continue to qualify as charitable lead unitrusts under section 2055(e)(2)(B).

Article I, Paragraphs G and H provide that upon the termination of each charitable trusts, the remaining trust assets are to be distributed to the individual beneficiaries named if then living, or if not, to the then living lawful issue of such individual beneficiary on the principle of representation, or if not, in equal shares to those individual beneficiaries who are then living.

#### LAW AND ANALYSIS:

Section 2055(a)(2) 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 or transfers to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private stockholder or individual.

Under section 20.2055-2(a), the amount passing to charity must be ascertainable and determinable as of the date of death. Similarly, under section 20.2055-2(b)(1), if the trustee is empowered to divert the property or fund, in whole or in part, to a noncharitable purpose, the deduction is limited to that portion, if any, of the property which is exempt from an exercise of the power.

Under section 2055(e)(2), the estate tax charitable deduction is not allowable where an interest in property (other than an interest described in section 170(f)(3)(B)) passes or has passed from the decedent to a person, or for a use, described in section 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 section 2055(a), unless--

(A) in the case of a remainder interest, such interest is in a trust which is a

PLR-154774-01

charitable remainder annuity trust or a charitable remainder unitrust (described in section 664) or a pooled income fund (described in section 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).

Under section 20.2055-2(e)(1)(i), in the case of decedents dying after December 31, 1969, where an interest in property passes from the decedent for charitable purposes and an interest in the same property passes from the decedent for private purposes, no deduction is allowed under section 2055(a) for the value of the interest passing for charitable purposes unless the interest is a "deductible interest".

Under section 20.2055-2(e)(2)(vii)(a), the term "deductible interest" includes a unitrust interest. A "unitrust interest" is a right to receive 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. The unitrust interest may be paid for a specified term, or for the life or lives of named individuals, each of whom must be living at the creation of the trust.

Under section 20.2055-2(e)(2)(vii)(b), a charitable interest is a unitrust interest only if it is a unitrust interest in every respect. Under section 20.2055-2(e)(2)(vii)(d), where a unitrust interest is in trust, the instrument may provide that income of the trust in excess of the amount required to pay the unitrust interest shall be paid to or for the use of a charity. Nevertheless, the amount of the deduction under section 2055 is limited to the fair market value of the unitrust interest. Under section 20.2055-2(f)(2)(v), the present value of a unitrust interest is 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.

In this case, the amount of the unitrust interest payable with respect to Charitable Trust 1 and Charitable Trust 2 will be equal to five percent of the net fair market value of the trust assets, determined as of the first business day of the year, and must be paid annually over the term of each trust. The Unitrust Amount will be ascertainable and determinable, effective as of the date of Taxpayer's death. The successor trustees are prohibited by the terms of Restated Trust from making any unitrust payments to an organization that is not described in section 2055(a). The successor trustees may not engage in any self-dealing, nor make any taxable expenditures. Accordingly, based on the facts submitted and the representations made, we conclude that the charitable interests in Charitable Trust 1 and Charitable Trust 2 will constitute unitrust interests within the meaning of section 2055(e)(2)(B) and section 20.2055-2(e)(2)(vii). Therefore, a deduction under section 2055(a) will be allowed for the value of the unitrust interest, determined in accordance with section 20.2055-2(f)(2)(v) as of the date of Taxpayer's death.

Except as expressly provided herein, no opinion is expressed or implied

PLR-154774-01

concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant. In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer.

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.

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

Enclosure (1)