

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4-PLR-113078-01

Date:

May 2, 2001

Legend

Decedent =

Trust =

Spouse =

Child 1 =

Child 2 =

Child 3 =

Brother 1 =

Brother 2 =

Niece =

Nephew 1 =

Nephew 2 =

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Ancestor =

Date 1 =

Date 2 =

State =

Court =

Property B =

Dear \_\_\_\_\_ :

This responds to your letter dated February 21, 2001, requesting rulings regarding the application of § 2518 of the Internal Revenue Code to disclaimers of interests in certain trusts and regarding the application of § 2056 to the division of the marital deduction share of a trust.

### FACTS

Decedent died testate on Date 1 survived by Spouse, Child 1, Child 2, and Child 3. All of Decedent's children are minors. Decedent was the settlor and trustee of Trust, a revocable trust created on Date 2.

Section 5.4 of the Trust Agreement provides:

If the settlor is survived by his wife and by issue, upon the death of the settlor, the trustee shall divide the trust estate remaining after the special gift described in Section 5.1 into two shares, hereafter referred to as the Marital Deduction Share and the Nonmarital Share.

(a) The Nonmarital Share shall consist of all of the settlor's interests in closely held businesses (as defined in Article 8) and in assets that do not qualify for the marital deduction.

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(b) The Nonmarital Share shall be divided into as many shares of equal market value as are necessary to create one share for each of the settlor's children then living and one share for each of the settlor's children then deceased and survived by issue. Each share created for a child of the settlor who has reached the age of thirty-five (35) years shall be distributed outright and free of trust to that child. Each share created for a child of the settlor who is under the age of thirty-five (35) years shall be held, administered, and distributed as a separate trust according to the terms of the Child's Trust as set forth in Article 6. Each share created for the issue then living of a deceased child of the settlor shall be distributed outright and free of trust to those issue in the manner provided in [State Probate Code].

(c) The Marital Deduction Share shall consist of all assets not allocated to the Nonmarital Share under Section 5.4(a).

(d) The Marital Deduction Share shall be held, administered, and distributed according to the terms of the Marital Trust as set forth in Article 6.

Article 6.1(a) indicates that the Marital Trust is intended to qualify for the Federal estate tax marital deduction as qualified terminable interest property under § 2056(b)(7).

Under Article 6.1(e) of the Trust Agreement, the Marital Trust is to terminate upon the death of the settlor's wife. At that time, Article 6.1(g) provides that the balance of the trust principal shall be distributed as follows:

(i) All of the tangible personal property in the trust shall be divided among the settlor's issue then living in the manner provided in [State Probate Code] and as they agree or, if they are unable to agree, as the trustee determines.

(ii) The remaining property in the trust shall be divided into as many shares of equal market value as are necessary to create one share for each of the settlor's children then living and one share for each of the settlor's children then deceased and survived by issue. Each share created for a child of the settlor who has reached the age of thirty-five (35) years shall be distributed outright and free of trust to that child. Each share created for a child of the settlor who is under the age of thirty-five (35) years shall be held, administered, and distributed as a separate trust according to the terms of the Child's Trust as set forth in Article 6. Each share created for the issue then living of a deceased child of the settlor shall be distributed outright and free of trust to those issue in the manner provided in [State Probate Code].

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(iii) If none of the settlor's children are living at the time that the trust property would otherwise be divided into shares pursuant to the foregoing provisions of this subsection, instead of dividing the property into shares and distributing it in the manner provided above, the trustee shall distribute all of the trust property outright to the settlor's then-living issue in the manner provided in [State Probate Code].

(iv) If the property of the trust is not completely disposed of by the preceding provisions, the trustee shall pay over and deliver the undisposed of property outright and free of trust to the issue then living of [Ancestor], the settlor's father, who are to take in the manner provided in [State Probate Code]; and if there are none, to the settlor's heirs.

Article 7.16 provides:

In order to satisfy a pecuniary gift or to distribute or divide trust assets into shares or partial shares, the trustee may distribute or divide those assets in kind, or divide undivided interests in those assets, or sell all or any part of those assets and distribute or divide the property in cash, in kind, or partly in cash and partly in kind. Property distributed to satisfy a pecuniary gift under this instrument shall be valued at its fair market value at the time of distribution. This section shall apply only to the extent that it does not conflict with the provisions in this instrument specifying allocation of assets involving the marital deduction gift.

Several disclaimers are proposed. A guardian ad litem has been appointed by Court for each of Child 1, Child 2, Child 3, and their respective unborn issue, and for Niece, Nephew 1, Nephew 2, the unborn issue of Brother 1, and the unborn issue of Brother 2.

The guardian ad litem, on behalf of Child 1, Child 2, and Child 3 will disclaim a fractional share of the respective Child's Nonmarital Share Trust determined by a fraction, the numerator of which is the amount equal to the value of the Nonmarital Share as finally determined for Federal estate tax purposes reduced by the "estate tax exempt amount," and the denominator is an amount equal to the value of the Nonmarital Share as finally determined for Federal estate tax purposes. In addition, the guardian ad litem on behalf of Child 1, Child 2, and Child 3 will disclaim all rights and interests in the Martial Trust remainder under Article 6.1(g)(i), Article 6.1(g)(ii), and as an issue of Ancestor under Article 6.1(g)(iv) of the Trust Agreement. The guardian ad litem on behalf of the unborn issue of Child 1, Child 2, and Child 3 will disclaim all rights and interests in the Martial Trust remainder under Article 6.1(g)(i), Article 6.1(g)(ii), Article 6.1(g)(iii), and as an issue of Ancestor under Article 6.1(g)(iv) of the Trust Agreement. The "estate tax exempt amount" is defined, in part, as the largest amount, if any, that can pass free of Federal estate tax based on the credit allowable against such tax under § 2010 of the Internal Revenue Code, with certain specified adjustments.

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Brother 1 and Brother 2 will disclaim their respective remainder interests in the Marital Trust as an issue of Ancestor under Article 6.1(g)(iv) of the Trust Agreement. The guardian ad litem for Niece, Nephew 1, Nephew 2, the unborn issue of Brother 1, and the unborn issue of Brother 2 will disclaim their respective remainder interests in the Marital Trust as an issue of Ancestor under Article 6.1(g)(iv) of the Trust Agreement.

The Trust Agreement is silent regarding the effect of a disclaimer by any beneficiary other than Spouse. It has been represented that all of the proposed disclaimers will be irrevocable, in writing, and delivered to the appropriate party within 9 months of Decedent's death. It has also been represented that none of the disclaimants will have accepted the disclaimed interests or any benefits therefrom.

Following the execution of the proposed disclaimers, the trustee, acting pursuant to a power granted in the Trust Agreement, will divide the Marital Deduction Share into two separate marital trusts, Marital Trust A and Marital Trust B. In all respects, the terms of the two trusts will be identical to those provided for under Article 6 regarding the Marital Trust. Property B is a "closely held business" as defined in Article 8 of the Trust Agreement. Decedent owned a minority interest in Property B. The trustee will allocate the interest in Property B passing to the Marital Deduction Share as a result of the above disclaimers to Marital Trust B. All property of the Marital Deduction Share other than the Property B interest allocated to Marital Trust B will be allocated to Marital Trust A. Pursuant to § 2056(b)(7), separate elections will be made to treat both Marital Trust A and Marital Trust B as qualified terminable interest property.

You have requested the following rulings:

1. All of the proposed disclaimers will constitute qualified disclaimers under § 2518 and the Federal estate tax value of the property passing at Decedent's death to the three Nonmarital Share Trusts will in the aggregate equal the applicable exclusion amount as described in § 2010(c).
2. If all of the proposed disclaimers are qualified disclaimers, the property allocated to Marital Trust A will be treated for Federal estate tax purposes as passing directly from Decedent to Marital Trust A and Property B allocated to Marital Trust B will be treated for Federal estate tax purposes as passing directly from Decedent to Marital Trust B.

#### RULING REQUEST NO. 1 -- DISCLAIMERS

Section 2518(a) provides that, if a person makes a qualified disclaimer with respect to any interest in property, Subtitle B (relating to the estate, gift and generation-skipping transfer taxes) shall apply with respect to such interest as if the interest had never been transferred to such person.

Section 2518(b) provides that the term "qualified disclaimer" means an irrevocable and unqualified refusal by a person to accept an interest in property but

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only if --

1. such refusal is in writing,
2. such writing is received by the transferor of the interest, the transferor's legal representative, or the holder of the legal title to the property to which the interest related not later than the date which is 9 months after the later of --
  - (A) the date on which the transfer creating the interest in such person is made, or
  - (B) the day on which such person attains age 21,
3. such person has not accepted the interest or any of its benefits, and
4. as a result of such refusal, the interest passes without any direction on the part of the person making the disclaimer and passes either --
  - (A) to the spouse of the decedent, or
  - (B) to a person other than the person making the disclaimer.

Section 25.2518-1(b) of the Gift Tax Regulations provides that, if a qualified disclaimer is made, the property is treated, for Federal gift, estate, and generation-skipping transfer tax purposes, as passing directly from the transferor, and not from the disclaimant, to the person entitled to receive the property as a result of the disclaimer.

Under section 25.2518-2(e)(1), in order to constitute a qualified disclaimer, the disclaimed interest must pass without any direction on the part of the person making the disclaimer to a person other than the disclaimant. The requirements of a qualified disclaimer under section 2518 are not satisfied if the disclaimant, either alone or in conjunction with another, directs the redistribution or transfer of the property or interest in property to another person (or has the power to direct the redistribution or transfer of the property or interest in property to another person unless such power is limited by an ascertainable standard).

Under section 25.2518-3(a)(1), the disclaimer of all or an undivided portion of any separate interest in property may be a qualified disclaimer even if the disclaimant has another interest in the same property. In general, each interest in property that is separately created by the transferor is treated as a separate interest. For example, if an income interest in securities is bequeathed to A for life, then to B for life, with the remainder interest in such securities bequeathed to A's estate, and if the remaining requirements of § 2518(b) are met, A could make a qualified disclaimer of either the income interest or the remainder, or an undivided portion of either interest. A could not, however, make a qualified disclaimer of the income interest for a certain number of years.

In § 25.2518-3(d), Example 8, under the terms of E's will, E's shares of stock in X, Y, and Z corporations are transferred to a trust. The trust instrument provides that all income is to be distributed currently to F and G in equal parts until F attains the age of 45 years. At that time the corpus of the trust is to be divided equally between F and G.

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F disclaims F's entire income interest in the trust while retaining the interest F has in corpus. The example concludes that the disclaimer is a qualified disclaimer.

Section 25.2518-3(d), Example 11, describes a situation where under the terms of a testamentary trust, W is to receive all trust income for life. The trustee has the power to invade trust corpus for the support and maintenance of D during the life of W. At W's death, the trust corpus is payable to D. D disclaims the right to receive distributions of trust corpus during W's lifetime, but retains the right to receive the remainder on W's death. The example concludes that D's disclaimer is a qualified disclaimer.

Section 25.2518-3(b) provides that a disclaimer of an "undivided portion" of a separate interest in property that meets the other requirements of § 2518(b) and the corresponding regulations is a qualified disclaimer. An undivided portion of a disclaimant's separate interest in property must consist of a fraction or percentage of each and every substantial interest or right owned by the disclaimant in such property.

In order to satisfy the requirements of § 2518(b), a disclaimer must be valid under applicable local law. Estate of Dancy v. Commissioner, 872 F.2d 84 (4<sup>th</sup> Cir. 1989). That is, because state law determines whether a property interest passes from one to another, the disclaimer must constitute an effective renunciation under state law. Estate of Bennett v. Commissioner, 100 T.C. 67 (1993).

Under State law, a disclaimer on behalf of a minor is to be made by the guardian of the estate of the minor if one has been appointed, or, if none has been appointed, by a guardian ad litem. Upon a hearing, the Court in its discretion may make an order

authorizing or requiring the guardian to execute and file the disclaimer if the court determines, taking into consideration all of the relevant circumstances, that the minor as a prudent person would disclaim the interest if he or she had the capacity to do so.

Under State law, unless the creator of the interest provides for a specific disposition of the interest in the event of a disclaimer, the interest disclaimed shall descend, go, be distributed, or continue to be held (1) as to a present interest, as if the disclaimant had predeceased the creator of the interest, or (2) as to a future interest, as if the disclaimant had died before the event determining that the taker of the interest had become finally ascertained and the taker's interest indefeasibly vested. A disclaimer relates back for all purposes to the date of the death of the creator of the disclaimed interest or the determinative event, as the case may be.

#### Disclaimers by Child 1, Child 2, and Child 3

In the present case, the guardian ad litem for Child 1, Child 2, and Child 3 will seek court approval to execute the disclaimers.

It is represented that the disclaimers will be irrevocable, in writing, delivered to

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the Executor of Decedent's estate not later than 9 months after Decedent's death, and that Child 1, Child 2, and Child 3 have not accepted any benefits from the disclaimed property. Further, each Child's disclaimer of a fractional interest in their respective Nonmarital Share will satisfy the requirements of § 25.2518-3(b). However, to be qualified disclaimers for purposes of § 2518, the disclaimers must be valid under applicable local law. In this regard, we express no opinion as to whether the disclaimers by Child 1, Child 2, and Child 3, Decedent's minor children, are valid under applicable local law. However, provided the disclaimers are valid under state law, the disclaimers will be qualified disclaimers under § 2518. See Estate of Goree v. Commissioner, T.C. Memo. 1994-331. Therefore, provided the disclaimers by Child 1, Child 2, and Child 3 are qualified disclaimers, the Federal estate tax value of the property passing at Decedent's death to the three Nonmarital Share Trusts will in the aggregate equal the applicable exclusion amount.

Disclaimers by Brother 1, Brother 2, the guardian ad litem on behalf of Niece, Nephew 1, Nephew 2, and the guardian ad litem on behalf of the unborn issue of Child 1, Child 2, Child 3, Brother 1, and Brother 2.

It is represented that the disclaimers will be irrevocable, in writing, delivered to the Executor of decedent's estate not later than 9 months after Decedent's death, and that the disclaimants have not accepted any benefits from the disclaimed property. It is further represented that the disclaimers are valid under State law. Therefore, based on the facts and representations, we conclude that the disclaimers executed by Brother 1, Brother 2, and the guardian ad litem on behalf of Niece, Nephew 1, Nephew 2, and the guardian ad litem on behalf of the unborn issue of Child 1, Child 2, Child 3, Brother 1, and Brother 2 satisfy the requirements of § 2518.

#### RULING REQUEST NO. 2 -- QUALIFIED TERMINABLE INTEREST PROPERTY

Section 2056(a) provides that the value of a decedent's taxable estate is determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Section 2056(b)(1) provides the general rule that no deduction is allowed for an interest passing to the surviving spouse if, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, the interest passing to the surviving spouse will terminate or fail.

Section 2056(b)(7) provides an exception to the terminable interest rule in the case of qualified terminable interest property. Section 2056(b)(7)(A) provides that qualified terminable interest property is treated as passing to the surviving spouse and no part of such property is treated as passing to any person other than the surviving spouse. Thus, the value of such property is deductible from the value of the gross estate under § 2056(a).



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Section 2056(b)(7)(B)(i) defines the term "qualified terminable interest property" as property: (1) which passes from the decedent, (2) in which the surviving spouse has a qualifying income interest for life, and (3) to which an election under § 2056(b)(7)(B)(v) applies. Section 2056(b)(7)(B)(ii) and the regulations thereunder provide that the surviving spouse will be considered to have a qualifying income interest for life if: (1) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, and (2) no person, including the surviving spouse, has a power to appoint any part of the property to any person other than the surviving spouse during the surviving spouse's lifetime.

Section 20.2056(b)-7(b)(2)(i) of the Estate Tax Regulations provides that the election under § 2056(b)(7)(B)(v) may relate to all or any part of property that meets the requirements of § 2056(b)(7)(B)(i), provided that any partial election must be made with respect to a fractional or percentage share of the property so that the elective portion reflects its proportionate share of the increase or decrease in value of the entire property for purposes of applying §§ 2044 or 2519. The fraction or percentage may be defined by formula.

Section 20.2056(d)-2(b) provides that if an interest in property passes from a decedent to a person other than the surviving spouse, and (1) the person other than the surviving spouse makes a qualified disclaimer with respect to such interest, and (2) the surviving spouse is entitled to such interest in property as a result of such disclaimer, the disclaimed interest is treated as passing directly from the decedent to the surviving spouse.

In the present case, after execution of the proposed disclaimers, the trustee proposes to divided the Marital Deduction Share into two separate trusts, Marital Trust A and Marital Trust B, each with terms identical to the terms of the Marital Trust as provided in Article 6 of the Trust Agreement. We conclude that, provided the disclaimers by Child 1, Child 2, and Child 3 are valid and effective under State law, and are therefore qualified disclaimers for purposes of § 2518, the property allocated to Marital Trust A will be treated for Federal estate tax purposes as passing directly from Decedent to Marital Trust A and the interest in Property B allocated to Marital Trust B will be treated for Federal estate tax purposes as passing directly from Decedent to Marital Trust B.

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. 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 who requested it. Section 6110(k)(3)

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of the Code provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, a copy of this ruling is being sent to the taxpayer and the taxpayer's other authorized representative.

Sincerely,

Associate Chief Counsel  
(Passthroughs and Special  
Industries)

By \_\_\_\_\_  
George L. Masnik  
Chief, Branch 4