

Internal Revenue Service

Department of the Treasury

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Date:

February 29, 2000

LEGEND

Trust =

A =

Trustee =

d1 =

d2 =

d3 =

State =

x =

y =

Dear

This responds to your letter dated August 10, 1999, submitted on behalf of Trust and A, requesting rulings under §§ 664 and 170 of the Internal Revenue Code.

FACTS

According to the information submitted, A executed and funded Trust under the laws of State on d1, with Trustee as the trustee. Trust is represented to be a charitable remainder unitrust (CRUT). Under the terms of the trust a unitrust interest equal to 5 percent of the net fair market value of the trust, determined annually, is to be paid to A for A's life, then to x beneficiaries for their joint lives, and then to the survivors. On the death of the last to die of the x individuals, the corpus is to be paid to specified charities. A may, by written instrument, add or delete charitable beneficiaries, or change the portion of corpus payable to the charitable beneficiaries.

On d2, A contributed additional property to Trust. In d3, A's tax advisers discovered that the additional contribution did not comply with § 664(d)(2)(D).

Trust and Trustee petitioned a State court in d3 to sever the amount representing the additional contribution from Trust and transfer the severed amount into four separate trusts. The terms of the four new trusts will be identical to those of Trust, with the exception that each new trust has only y of the x successor unitrust beneficiaries. On the death of the last to die of the y unitrust beneficiaries for each trust, the trust will terminate, and the corpus will pass to the designated charities. Trustee and A represent that after severing and establishing new trusts, the new trusts and the original trust will comply with § 664(d)(2)(D). The court granted the petition contingent on a favorable private letter ruling from the Service. The amount severed from Trust was determined by tracing the additional assets contributed to Trust, the proceeds from the sale of those assets, and income earned prior to the severance.

LAW AND ANALYSIS

Section 664(d)(2), prior to amendment by the Taxpayer Relief Act of 1997, P.L. 105-34, (the Act) provided that a CRUT is a trust – (A) from which a fixed percentage (which is not less than 5 percent) of the net fair market value of its assets, valued annually, 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 the individual or individuals, (B) from which no amount other than the payments described in § 664(d)(2)(A) may be paid to or for the use of any person other than an organization described in § 170(c), and (C) following the termination of the payments described in § 664(d)(2)(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.

Section 1089 of the Act added, in relevant part, new §§ 664(d)(2)(D), 664(d)(4), and 2055(e)(3)(J) to the Code.

Section 664(d)(2)(D) provides an additional requirement that must be satisfied in order to qualify as a CRUT. In particular, under § 664(d)(2)(D), with respect to each contribution of property to the trust, the value (determined under § 7520) of the remainder interest in the property must be at least 10 percent of the net fair market value of the property as of the date such property is contributed to the trust. Generally, § 664(d)(2)(D) applies to transfers in trust after July 28, 1997.

Section 664(d)(4) provides that if any contribution is made to a trust which before the contribution is a CRUT, and the contribution would (but for § 664(d)(4)) result in the trust ceasing to be a CRUT by reason of § 664(d)(2)(D), the contribution shall be treated as a transfer to a separate trust under regulations prescribed by the Secretary.

Currently, there are no regulations under § 664(d)(4).

Section 2055(e)(3)(J) provides, in relevant part, that in the case of a trust that would qualify (or could be reformed to qualify pursuant to § 2055(e)(3)(B)) for the estate tax charitable deduction but for failure to satisfy the requirement of § 664(d)(2)(D), such trust may be (i) declared null and void ab initio, or (ii) changed by reformation, amendment, or otherwise to meet such requirement by reducing the payout rate or the duration (or both) of any noncharitable beneficiary's interest to the extent necessary to satisfy such requirement, pursuant to a proceeding that is commenced within the period required in § 2055(e)(3)(C)(iii). Under § 170(f)(7), the provisions of § 2055(e)(3) also apply for purposes of § 170.

The committee reports in discussing § 1089 of the Act, state, in part, as follows:

First, where a transfer is made after July 28, 1997, to a charitable remainder trust that fails the 10-percent test, the trust is treated as meeting the 10-percent requirement if the governing instrument of the trust is changed by reformation, amendment, construction, or otherwise to meet such requirement by reducing the payout rate or duration (or both) of any noncharitable beneficiary's interest to the extent necessary to satisfy such requirement so long as the reformation is commenced within the period permitted for reformations of charitable remainder trusts under section 2055(e)(3). . . .

Second, a transfer to a trust will be treated as if the transfer never had been made where a court of competent jurisdiction over the trust declares the trust void (because, e.g., the application of the 10-percent rule frustrates the purposes for which the trust was created) and judicial proceedings to revoke the trust are commenced within the period permitted for reformations of charitable remainder trusts under section 2055(e)(3). . . .

Third, where an additional contribution is made after July 28, 1997, to a charitable remainder unitrust created before July 29, 1997, and that unitrust would not meet the 10-percent requirement with respect to the additional contribution, the conference agreement provides that the additional contribution shall be treated, under regulations to be issued by the Secretary of the Treasury, as if it had been made to a new trust that does not meet the 10-percent requirement, but which does not affect the status of the original unitrust as a charitable remainder trust. . . .

H.R. Conf. Rep., No. 105-220, at 607-608 (1997).

CONCLUSIONS

After applying the applicable law to the information presented and the representations made, we conclude that an amount representing the additional contribution may be severed from Trust. The severance of the additional contribution will be treated as a transfer to a separate trust that may be reformed pursuant to § 2055(e)(3)(J)(ii) to satisfy the requirements of § 664(d)(2)(D). In this case, the severed trust will be reformed by creating four new separate trusts. Each of the four new trusts will have y successor unitrust beneficiaries; thus, reducing the duration of the noncharitable beneficiaries' interests pursuant to § 2055(e)(3)(J)(ii). In all other respects, the four separate trusts will be identical to the terms of Trust. We conclude that as a result of the severance, the additional contribution does not effect the status of Trust as a qualified CRUT under § 664(d)(2). Further, the reformation as proposed satisfies the requirements of § 2055(e)(3)(J), and therefore, the four new trusts, as reformed, will be qualified CRUTs under § 664(d)(2), effective d2. Accordingly, we conclude the additional contribution will be deductible under § 170, in the manner and to the extent provided by § 170 and the regulations thereunder.

No opinion is expressed on the federal tax consequences of the formation or operation of the trusts under any other section of the Code.

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

Under a power of attorney on file in this office, we are sending a copy of this letter to the taxpayer.

Sincerely yours,
Shannon Cohen
Acting Assistant to the Chief, Branch 3
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes