Part III. Administrative, Procedural, and Miscellaneous

Transaction of Interest—Potential for Avoidance of Tax Through Sale of Charitable Remainder Trust Interests

Notice 2008–99

The Internal Revenue Service and the Treasury Department are aware of a type of transaction, described below, in which a sale or other disposition of all interests in a charitable remainder trust (subsequent to the contribution of appreciated assets to and their reinvestment by the trust), results in the grantor or other noncharitable recipient receiving the value of that person's trust interest while claiming to recognize little or no taxable gain. The IRS and Treasury Department believe this transaction has the potential for tax avoidance or evasion, but lack enough information to determine whether the transaction should be identified specifically as a tax avoidance transaction. This notice identifies this transaction and substantially similar transactions as transactions of interest for purposes of § 1.6011–4(b)(6) of the Income Tax Regulations and §§ 6111 and 6112 of the Internal Revenue Code. This notice also alerts persons involved in these transactions to certain responsibilities that may arise from their involvement.

FACTS

In one variation of the transaction, Grantor creates a charitable remainder trust (Trust) and contributes appreciated assets (Appreciated Assets) to Trust. Grantor retains an annuity or unitrust interest (term interest) in Trust and designates an organization described in §§ 170(c), 2055(a) and 2522(a) (Charity) as the remainder beneficiary. Charity may, but need not, be controlled by Grantor; Grantor may, but need not, reserve the right to change the Charity designated as the remainder beneficiary. Next, Trust sells or liquidates the Appreciated Assets and reinvests the net proceeds in other assets (New Assets) such as money market funds, marketable securities, and/or other assets, often to acquire a diversified portfolio. Because a charitable remainder trust generally is a tax-exempt entity under § 664, Trust's sale of the Appreciated Assets is exempt from income tax, and Trust's basis in the New Assets is the price Trust pays for those New Assets. Some portion of Trust's ordinary income and capital gains may become taxable to Grantor as the periodic annuity or unitrust payments are made by Trust in accordance with the rules of § 664 and the regulations thereunder. Next, Grantor and Charity, in a transaction they claim is described in § 1001(e)(3), sell or otherwise dispose of their respective interests in Trust to X, an unrelated third party, for an amount that approximates the fair market value of the assets of the trust, including the New Assets. Trust then terminates, and the assets of Trust, including the New Assets, are distributed to X.

Grantor takes the following positions regarding the tax consequences of this transaction. Grantor claims a charitable deduction for the portion of the fair market value of the Appreciated Assets as of the date of their contribution to Trust that is attributable to the remainder interest. Grantor claims to recognize no gain from the Trust's sale or liquidation of the Appreciated Assets. When Grantor and Charity sell their respective interests in Trust to X, Grantor and Charity take the position that they have sold the entire interest in Trust within the meaning of § 1001(e)(3). Because the entire interest in Trust is sold, Grantor claims that § 1001(e)(1), which disregards basis in the case of a sale of a term interest, does not apply to the transaction. Grantor also takes the position that, under § 1001(a) and related provisions, the gain on the sale of Grantor's term interest is computed by taking into account the portion of uniform basis allocable to Grantor's term interest under §1.1014–5 and § 1.1015–1(b), and that this uniform basis is derived from the basis of the New Assets rather than the basis of the Appreciated Assets.

The transaction may use trusts with circumstances that vary from the situation described in the facts of this notice. In some variations, a net income with make-up provision charitable remainder unitrust (NIMCRUT) may be used as Trust, Trust may have been in existence for some time prior to the sale of Trust interests, the Appreciated Assets already may be in Trust prior to the commencement of the transaction, the recipient and seller of the term interest may be the Grantor and/or another person, or Grantor may contribute the Appreciated Assets to a partnership or other passthrough entity and then contribute the interest in the entity to Trust.

A result of the claimed tax treatment of the transaction is that the gain on the sale of the Appreciated Assets is never taxed, even though the Grantor receives the Grantor's share of the appreciated fair market value of those assets. The IRS and Treasury Department are not concerned about the mere creation and funding of a charitable remainder trust and/or the trust's reinvestment of the contributed appreciated property, and such events alone do not constitute the transaction subject to this notice.

However, the IRS and Treasury Department are concerned about the manipulation of the uniform basis rules to avoid tax on gain from the sale or other disposition of appreciated assets. Accordingly, the type of transaction described in this notice includes a coordinated sale or other coordinated disposition of the respective interests of the Grantor or other noncharitable recipient and the Charity in a charitable remainder trust in a transaction claimed to be described in § 1001(e)(3), subsequent to the contribution of appreciated assets and the trust's reinvestment of those assets. In particular, the IRS and Treasury Department are concerned about Grantor's claim to an increased basis in the term interest coupled with the termination of the Trust in a single coordinated transaction under § 1001(e) to avoid tax on gain from the sale or other disposition of the Appreciated Assets.

TRANSACTION OF INTEREST

Effective Date

Transactions that are the same as, or substantially similar to, the transaction described in this notice are identified as transactions of interest for purposes of § 1.6011–4(b)(6) and §§ 6111 and 6112 effective October 31, 2008, the date this notice was released to the public. Persons entering into these transactions on or after November 2, 2006, must disclose the transaction as described in § 1.6011–4. Material advisors who make a tax statement on or after November 2, 2006, with respect to transactions entered into on or after November 2, 2006, have disclosure and list maintenance obligations under §§ 6111 and 6112. See § 1.6011–4(h) and §§ 301.6111–3(i) and 301.6112–1(g) of the Procedure and Administration Regulations.

Independent of their classification as transactions of interest, transactions that are the same as, or substantially similar to, the transaction described in this notice already may be subject to the requirements of §§ 6011, 6111, or 6112, or the regulations thereunder. When the IRS and Treasury Department have gathered enough information to make an informed decision as to whether this transaction is a tax avoidance type of transaction, the IRS and Treasury Department may take one or more actions, including removing the transaction from the transactions of interest category in published guidance, designating the transaction as a listed transaction, or providing a new category of reportable transaction.

Participation

Under § 1.6011–4(c)(3)(i)(E), each recipient of the term interest and Trust are participants in this transaction for each year in which their respective tax returns reflect tax consequences or a tax strategy described in this notice. Charity is not a participant if it sold or otherwise disposed of its interest in Trust on or prior to October 31, 2008. For interests sold or otherwise disposed of after October 31, 2008, under § 1.6011–4(c)(3)(i)(E), Charity is a participant for the first year for which Charity's tax return reflects or is required to reflect the sale or other disposition of Charity's interest in Trust. In general, Charity is required to report the sale or other disposition of its interest in Trust on its return for the year of the sale or other disposition. See § 6033 and § 1.6033–2(a)(ii). Therefore, in general, Charity will be a participant for the year in which charity sells or otherwise disposes of its interest in Trust.

Time for Disclosure

See §1.6011–4(e) and § 301.6111–3(e).

Material Advisor Threshold Amount

The threshold amounts in § 301.6111–3(b)(3)(i)(B) are reduced to $5,000.

Penalties

Persons required to disclose these transactions under § 1.6011–4 who fail to do so may be subject to the penalty under § 6707A. Persons required to disclose these transactions under § 6111 who fail to do so may be subject to the penalty under § 6707(a). Persons required to maintain lists of advisees under § 6112 who fail to do so (or who fail to provide such lists when requested by the IRS) may be subject to the penalty under § 6708(a). In addition, the IRS may impose other penalties on parties involved in these transactions or substantially similar transactions, including the accuracy-related penalty under § 6662 or § 6662A.

REQUESTING COMMENTS

The IRS and Treasury Department are aware of concerns expressed by commentators regarding this transaction of interest. The IRS and Treasury Department share these concerns and are requesting written comments on how the transaction might be addressed in published guidance. One approach might involve issuing regulations under the authority of § 643(a)(7) to address the uniform basis rules under §§ 1014 and 1015 and the regulations thereunder.

Comments should be submitted by January 31, 2009, to: Internal Revenue Service, CC:PA:LPD:PR (Notice 2008–99), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20224. Alternatively, comments may be hand delivered Monday through Friday between the hours of 8:00 a.m. to 4:00 p.m. to: CC:PA:LPD:PR (Notice 2008–99), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC. Comments also may be submitted electronically via the following email address: *Notice.Comments@irscounsel.treas.gov*. Please include "Notice 2008–99" in the subject line of any electronic submissions. All comments received will be open to public inspection and copying.

DRAFTING INFORMATION

The principal author of this notice is Allison Carmody of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, contact Ms. Carmody at (202) 622–3070 (not a toll-free call).

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26 CFR 601.601: Rules and regulations.
(Also Part I, §§ 582, 702, 1221.)

Rev. Proc. 2008–64

SECTION 1. PURPOSE

This revenue procedure provides guidance under section 301 of the Emergency Economic Stabilization Act of 2008, Pub. L. No. 110–343, Division A § 301, 122 Stat. 3765 (EESA[1]). EESA § 301 treats as ordinary income or loss certain gain or loss recognized by banks and certain other financial institutions on the sale or exchange of preferred stock of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). EESA § 301 also grants the Secretary of the Treasury authority to issue guidance as necessary to carry out the purposes of that section.

SECTION 2. BACKGROUND

.01 Before September 2008, many banks and bank holding companies invested in the preferred stock of Fannie Mae and Freddie Mac. Many institutions invested directly in the preferred stock. Others invested indirectly—for example, through corporate subsidiaries that are not banks or through adjustable rate preferred interests in certain trusts designed to be

[1] Only the first of the statute's three divisions is the Emergency Economic Stabilization Act of 2008. Each of the other two divisions has its own section 301, both of which are unrelated to EESA § 301.