

**INTERNAL REVENUE SERVICE**  
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

November 19, 2001

Number: **200210009**  
Release Date: 3/8/2002  
Index (UIL) No.: 2036.23-00, 2039.02-00  
CASE MIS No.: TAM-130863-01/CC:PSI:B04

Taxpayer's Name:

Taxpayer's Identification No:      SSN:  
Date of Death:  
Date of Conference:

**LEGEND:**

Decedent	-
Wife	-
Daughter	-
GRAT	-
Date 1	-
Date 2	-
Date 3	-
Date 4	-
\$A	-
\$B	-
\$C	-

**ISSUE:**

To what extent is the corpus of GRAT, a grantor retained annuity trust established by Decedent, includible in Decedent's gross estate under §§ 2036 or 2039 of the Internal Revenue Code?

**CONCLUSION:**

Under § 2036, the fair market value of the GRAT corpus is includible in Decedent's gross estate as determined under Rev. Rul. 82-105, 1982-1 C.B. 133. Under § 2039, the entire value of the GRAT on the date of Decedent's death is includible in the Decedent's gross estate.

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FACTS:

On Date 1, Decedent established GRAT, a grantor retained annuity trust intended to meet the requirements of § 2702 of the Internal Revenue Code. The trustees of GRAT were Decedent and his daughter (Daughter). Under the terms of GRAT, the trustees were to manage the corpus and pay annually to the Decedent for a period of 10 years, an annuity amount equal to 15 percent of the fair market value of the initial trust corpus. If the Decedent died before the expiration of the 10-year term, the annuity was to be paid to the executor of Decedent's estate for the remaining balance of the 10-year term. At the expiration of the 10 year term, GRAT is to terminate and its assets are to be distributed to Daughter, if she is living at that time. If Daughter does not survive the term of GRAT, the assets are to be distributed to Wife. If neither Daughter nor Wife survive the 10-year term, the assets of GRAT are to be distributed to the issue of Decedent and Wife, per stirpes, or if none, to Decedent's sons in equal shares, or if one son survives Decedent, all to the survivor. If neither son survives Decedent, the assets are to pass to the sons' issue, per stirpes.

Decedent died on Date 2, during the sixth year of the 10-year term of GRAT. Since Date 2, the annual annuity payments (\$A) have been paid to Decedent's estate pursuant to the terms of GRAT. The 10-year term of GRAT will terminate on Date 4, at which time the payments to the estate will terminate and the trust corpus will be distributed in accordance with the trust instrument.

As of Date 2, the fair market value of the corpus of GRAT was \$B. Decedent's estate timely filed Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return on Date 3. On the return, the estate reported that \$C was includible in the gross estate with respect to GRAT, which amount represented a fraction of the fair market value of the GRAT on the date of death.

LAW AND ANALYSIS:

Section 2001 imposes a tax on the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2033 provides that the value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of the decedent's death.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death, (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy

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the property or the income from the property.

In Rev. Rul. 82-105, 1982-1 C.B. 133, the decedent, prior to his death, created a charitable remainder annuity trust, pursuant to which the decedent retained the right to receive an annuity of 12x dollars for life. The ruling concludes that the decedent's retained annuity represents the retained right to receive all of the income from all or a specific portion of the trust for purposes of section 2036. Under Rev. Rul. 82-105, the amount of the corpus with respect to which the decedent retained the income is that amount of corpus that would be sufficient to yield the annual annuity based on the assumed rate of return prescribed by the regulations as of the applicable valuation date. The revenue ruling prescribes the following formula for this determination:

$$(\text{Annual Annuity}) / (\text{Assumed Rate of Return}) = \text{Amount Includible}$$

That portion of the trust corpus with respect to which the decedent retained a right to receive all of the income, as determined under the formula, is includible in the decedent's gross estate under section 2036(a)(1). The ruling states that the holding applies only to the portion of the value of a charitable remainder annuity trust that is includible in the gross estate under § 2036. The ruling expressly does not consider the amount, if any, that may be includible in the gross estate under any other provisions of the Internal Revenue Code.

Section 2039(a) provides, in pertinent part, that the gross estate shall include the value of an annuity or other payment receivable by any beneficiary by reason of surviving the decedent under any form of contract or agreement entered into after March 3, 1931, if, under the contract or agreement, an annuity or other payment was payable to the decedent, or the decedent possessed the right to receive such annuity or payment, either alone or in conjunction with another, for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death.

Section 2039(b) provides, in pertinent part, that the amount includible under section 2039(a) is the part of the value of the annuity or other payment receivable under the contract or agreement as is proportionate to the part of the purchase price contributed by the decedent.

Section 20.2039-1(b)(1) of the Estate Tax Regulations provides, in part, that the term "annuity or other payment" as used with respect to both the decedent and the survivor beneficiary has reference to a payment or payments that may be equal or unequal, conditional or unconditional, periodic or sporadic. Section 20.2039-1(b)(1) further provides that the term "contract or agreement" includes understandings, arrangements and plans.

#### Section 2036

Under the trust agreement in the instant case, Decedent transferred property to

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the GRAT, but retained the right to receive an annuity payment for a term of 10 years or until his prior death. Decedent died during the sixth year of the term, and at the time of his death was receiving annual payments from the GRAT. Thus, Decedent had retained for a period which did not in fact end before his death, the right to receive the annuity payments from the GRAT. Accordingly, under § 2036, a portion of the GRAT is includible in Decedent's gross estate. In accordance with Rev. Rul. 82-105, the portion of the value of the GRAT includible under § 2036 is the amount of corpus necessary to yield \$A a year (the amount of Decedent's retained annuity), based upon an assumed rate of return equal to the § 7520 rate on the date of Decedent's death.

### Section 2039

We also believe that, under § 2039(a), 100 percent of the value of the GRAT corpus on Decedent's date of death is includible in the gross estate. In this case, the annuity payable to the Decedent, and the payments to be made after Decedent's death, are all payable under the terms of a trust instrument, which constitutes a contract or agreement, as required under § 2039(a). Further, the annuity was paid to Decedent for a period that did not in fact end before his death. Finally, under the terms of the GRAT, the annuity and other payments receivable by the estate (and, thus, the estate beneficiaries) and the remainder beneficiaries of the GRAT, are receivable by reason of surviving the Decedent.

Decedent's estate contends that this final requirement is not satisfied in this case because, under the terms of the GRAT, Daughter, or any successor alternative remainder beneficiary, must survive the term of the GRAT in order to receive the remainder interest. Thus, the remainder interest is not receivable by any person by reason of surviving the Decedent. Rather, because an annuity is first payable to the estate for the balance of the GRAT term, the remainder interest will be receivable by Daughter (or the alternative successor beneficiaries) only by reason of surviving the 10 year term of the GRAT.

However, we disagree that §2039(a) is not applicable to the entire GRAT corpus in this case merely because the annuity or other payment is first payable to the Decedent's estate for a term of years and then to the remainder beneficiaries, if they are then living. For example, assume payments are to be made to a decedent for 10 years or his prior death, and on the earlier of the decedent's death or the expiration of the 10 year period, the payments are to be made to the decedent's child (or the child's issue if the child is not then living) for 15 years. It seems clear that if the decedent died within the initial 10 year term and the payments continued to the child, the survivor payments would be subject to inclusion under § 2039(a). The payments to the child (or the child's issue) are receivable because of the decedent's death, and because the child (or issue) survived the decedent. See, C. Lowndes, R. Kramer, J. McCord, Federal Estate and Gift Taxes, §10.6 (3<sup>rd</sup> ed. 1974). The result should be the same if the payments commencing after the decedent's death are first payable to the decedent's estate (and through the estate to the estate beneficiaries) for a term of years and then to the child. The annuity and other payments, whether payable initially

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to the estate beneficiaries and then to the child, or initially to the child, commence by reason of the decedent's death and will be received by the ultimate beneficiaries because they survived the decedent. The fact that the total benefit payable after the decedent's death is divided between several beneficiaries on a temporal basis should have no effect on the application of § 2039(a). See also, Rev. Rul. 76-404, 1976-2 C.B. 294, in which a nonqualified pension plan provides for a payment to the surviving spouse until death or remarriage. If the spouse dies or remarries, the annuity is payable to the decedent's child under age 21 until they attain age 21. The primary focus of the revenue ruling is whether the spouse's interest qualifies for the estate tax marital deduction. However, the ruling states that the value of the annuity payments receivable by the spouse and the child are includible under § 2039(a). Thus, the child's annuity is viewed as receivable by reason of surviving the decedent, even though additional conditions were imposed on the child's receipt of the annuity; that is, the child could only receive the annuity if the spouse died or remarried before the child attained age 21.

We believe this position is consistent with Congressional intent in enacting §§ 2039(a) and (b). Prior to the enactment of § 2039, courts had repeatedly concluded that a commercial survivor annuity payable after the death of the primary annuitant/purchaser was includible in the primary annuitant/purchaser's gross estate under the predecessor statutes to § 2036. See, e.g., Commissioner v. Clise, 122 F.2d 998 (9<sup>th</sup> Cir. 1941). See also, Rev. Rul. 55-302, 1955-1 C.B. 446. Section 2039 was added to the Internal Revenue Code by the Revenue Act of 1954 to codify this result and to provide rules for the estate taxation of survivor annuities payable under employee pension plans. S. Rep. No. 1622, 83<sup>rd</sup> Cong. 2d Sess. 123 (June 18, 1954).

In enacting §§ 2039(a) and (b), Congress borrowed many aspects of § 2036 and its predecessors, which had previously been held applicable to survivor annuities. For example, § 2036 applies if the decedent retained an interest in transferred property for life or for a period not ascertainable without reference to death or for a period that did not in fact end before death. Section 2039(a) applies if the decedent received payments under a contract or agreement for these same periods. Section 2036 does not apply to transfers prior to March 4, 1931. Similarly, § 2039(a) contains the identical effective date. Thus, it is clear that, in enacting §§ 2039(a) and (b), Congress incorporated the operating rules for § 2036. Clearly, § 2036 applies where the decedent's retained interest in property, in fact, terminates at death and the benefit of the property passes to others. Section 2039 applies under the same circumstances; that is, where the decedent's annuity, in fact, terminates at death and the benefits payable under the contract or agreement pass on to the survivors. As is the case under § 2036, it should make no difference that, after the decedent's death, the benefits are first payable to the decedent's estate for a term of years and then to specified designated beneficiaries if they are then living.

In the instant case, commencing on Decedent's death, assets of GRAT will be distributed first to the estate (and through the estate to the beneficiaries) for a 4 year period, and then to Daughter if she is living, and if not then living, to designated

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contingent beneficiaries. As discussed above, the payments commenced by reason of the Decedent's death and each beneficiary must, in fact, survive the Decedent in order to receive any payments from the GRAT. Accordingly, all post-death payments from the GRAT are receivable by reason of surviving the Decedent under section 2039(a).<sup>1</sup> Consequently, the entire value of the GRAT on the date of Decedent's death is includible in Decedent's gross estate under § 2039(a).

CAVEAT:

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(k)(3) provides that it may not be used or cited as precedent.

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<sup>1</sup>An annuity payable to the estate would be includible under §2039(a), as well as §2033. See Rev. Rul. 77-157, 1977-1 C.B. 279.