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Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4/PLR-140636-02

Date:

FEBRUARY 04, 2003

In Re:

Legend:

Decedent	-
Spouse	-
Child 1	-
Child 2	-
Date 1	-
Date 2	-
Date 3	-
Date 4	-
Date 5	-
First Will	-
Second Will	-
Third Will	-
Revocable Trust	-

Dear :

This is in reference to your letter dated July 22, 2002, requesting rulings regarding the effect of the proposed judicial reformation of the trust instrument for federal estate tax purposes.

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Background

The facts submitted are as follows:

Decedent was married to Spouse and had two children, Child 1 and Child 2. On Date 1, Decedent executed First Will, his last will and testament.

Article FOURTH of First Will, as amended by Codicil, provides, in part, for the creation of a marital trust for Spouse's benefit, as follows:

(a) If my wife, [Spouse], survives me, SEVENTY PERCENT of my residuary estate shall be held in separate trust by my Trustees to pay the income therefrom in quarterly or more frequent instalments to my wife during her life.

The trustees are authorized to distribute principal to Spouse in such amounts as the trustees, in their absolute discretion, deem that she needs for "her support or by reason of illness, accident or other emergency, after giving due consideration to her other resources." On Spouse's death, the remaining balance of the trust is to be held in further trust for the benefit of Child 1, Child 2, and their descendants.

On Date 2, Decedent revoked First Will in its entirety and executed Second Will. As in the First Will, Article FOURTH of the Second Will provides, in part, for the creation of a marital trust, as follows :

(a) If my wife, [Spouse] survives me, SEVENTY PERCENT of my residuary estate shall be held in separate trust by my Trustees to pay the income therefrom in quarterly or more frequent instalments to my wife during her life.

This will also authorized the trustees to invade corpus for the benefit of Spouse under the same terms as in First Will. On Spouse's death, the remaining corpus was to be distributed in a manner similar to that provided under First Will. Finally, under Second Will, the balance of the estate was to be distributed in a manner similar to that provided under First Will.

On Date 3, Decedent, whose health was failing, revoked Second Will in its entirety and executed Third Will. At the same time, Decedent executed Revocable Trust. Article FOURTH of Third Will provided for the distribution of all the rest, residue and remainder of Decedent's estate to the Revocable Trust. Other than minor stylistic changes and the removal of certain pre-residuary beneficiaries, the dispositive provisions governing the disposition of the Revocable Trust after Decedent's death, except as discussed below, were identical to the dispositive provisions of Second Will.

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Article 3 of Revocable Trust provides for the payment of debts, funeral and administration expenses, and taxes and distribution of the trust principal upon Decedent's death. Article 3(d) provides, in pertinent part, for the disposition of the balance of the trust corpus as follows:

(d) The balance of said aggregate principal (the "Balance") shall be disposed of as follows:

(1) If the Settlor's wife, [Spouse], survives the Settlor, THIRTY PERCENT of the Balance shall be held in separate trust by the Trustees to pay the income therefrom in quarterly or more frequent instalments to the Settlor's wife during her life.

The trustees are authorized and empowered, from time to time, to pay to the Settlor's wife, such sums out of principal of her trust as the trustees, in their absolute discretion, deem that she needs for her support or by reason of illness, accident or other emergency, after giving due consideration to her other resources.

* * *

(2) SEVENTY PERCENT of the Balance (or all thereof, if the Settlor's wife predeceases the Settlor) shall be disposed of [for the benefit of Child 1, Child 2 and their descendants].

Decedent died on Date 4, shortly after executing Third Will and the Revocable Trust, survived by Spouse, Child 1 and Child 2. The current trustees of the Revocable Trust are Spouse, Child 1 and an unrelated third party. Upon submitting the Third Will and the Revocable Trust to probate proceedings, Decedent's executor discovered that, under the terms of Article 3(d)(1) of the Revocable Trust, only 30 percent of the trust residue was to be distributed in trust for the benefit of Spouse and, under Article 3(d)(2), 70 percent of the residue was to pass for the benefit of Child 1, Child 2 and their descendants. In contrast, under the terms of First Will and Second Will, Spouse's residuary trust was to receive 70 percent of the residuary estate and the balance (30 percent) was to pass for the benefit of Child 1, Child 2 and their descendants. Decedent's estate contends that, as a result of scrivener's error, the percentage figures in Article 3(d)(1) and (2) of the Revocable Trust were inadvertently transposed.

Decedent's estate filed a petition in the probate court on Date 5 to reform the Revocable Trust. Pursuant to petition, the court issued an Order of Reformation of Declaration of Trust. Pursuant to the Order, Article 3(d)(1) of the Revocable Trust was reformed to provide that "SEVENTY PERCENT" of the balance of the trust is to pass to the marital trust for the benefit of Spouse. Article 3(d)(2) was reformed to provide that

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“THIRTY PERCENT” of the balance of the trust is to pass to and for the benefit of Child 1 and Child 2 and their descendants.

Rulings Requested

You have requested the following rulings:

1. The Order of Reformation of Declaration of Trust, as issued by the probate court, is applicable as of Decedent's date of death and that, for federal estate tax purposes, seventy percent of the trust balance is the amount that passes under Article 3(d)(1) of the Revocable Trust to the trust for the benefit of Spouse.

2. The amount that passes to the marital trust under Article 3(d)(1) is eligible for treatment as qualified terminable interest property as described in § 2056(b)(7) of the Internal Revenue Code.

Law and Analysis

Section 2001(a) of the Internal Revenue Code imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2056(a) provides that, for purposes of the tax imposed by § 2001, the value of the taxable estate is to be 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.

Section 2056(b)(1) provides the general rule that no deduction is allowed under § 2056(a) 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 will terminate or fail.

Section 2056(b)(7)(A) provides that, in the case of qualified terminable interest property, the entire property is treated as passing to the surviving spouse for purposes of § 2056(a) and no part of the property is treated as passing to any person other than the surviving spouse for purposes of § 2056(b)(1)(A).

Section 2056(b)(7)(B)(i) defines “qualified terminable interest property” as property: (1) that 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)(v) provides that an election under § 2056(b)(7) with

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respect to any property shall be made by the executor on the return of tax imposed by § 2001. Such an election, once made, is irrevocable.

Section 2044(a) and (b) provides generally that the value of the gross estate includes the value of any property in which the decedent had a qualifying income interest for life and with respect to which a deduction was allowed for the transfer of the property to the decedent under § 2056(b)(7).

Section 737.201 of the Florida Estates and Trusts Code addresses the jurisdiction of the courts over trusts and provides, in part, that:

(1) The proceedings that may be maintained under this section are those concerning the administration and distribution of trusts, the declaration of rights, and the determination of any other matters involving trustees and beneficiaries. These include, but are not limited to, proceedings to:

* * *

(c) Ascertain beneficiaries; determine any question arising in the administration or distribution of any trust, including questions of construction of trust instruments; instruct trustees; and determine the existence or nonexistence of any immunity, power, privilege, duty, or right.

Fla. Stat. Ann § 737.201 (West 2002).

Further, Fla. Stat. Ann § 737.4031 (West 2002), in addressing judicial modification of trusts, provides, in part:

(3) In exercising its discretion to order a modification of a trust under this section, the court shall consider the terms and purposes of the trust, the facts and circumstances surrounding the creation of the trust, and extrinsic evidence relevant to the proposed modification.

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Florida courts have held that a trust with testamentary aspects may be reformed after the death of the settlor to correct a unilateral drafting mistake so long as the reformation is not contrary to the interest of the settlor. In re Estate of Robinson, 720 So. 2d 540, 543 (Fla. App. 4 Dist. 1998). See also, Schroeder v. Gebhart, 825 So. 2d 442, 446 (Fla. App. 5 Dist. 2002), which stated that the purpose of reformation for a mistake is to assure that the intent of the trustor is carried out and that “the mistake must be material and the party seeking reformation must establish that the trust as written does not reflect the trustor’s intent or that the trustor would have used different terms but for the mistake.”

In this case, First Will and the Second Will both provided that the marital residuary trust established for the benefit of Spouse was to be funded with 70 percent of the residuary estate and the trust established for the benefit of Decedent’s children and their descendants was to be funded with 30 percent of the residuary estate. The attorneys who drafted the Revocable Trust have stated, in affidavits, that Decedent directed that the dispositive provisions of the Revocable Trust, with respect to the disposition of the residue, were to follow the terms of the Second Will. The drafters state that the transposition of the percentages in Articles 3(d)(1) and 3(d)(2) of the trust was a mistake on their part in drafting the instrument. These assertions are supported by the fact that, but for the transposed percentages, the terms of the marital residuary trust and the residuary trust for the benefit of Child 1, Child 2 and their descendants in the Revocable Trust are virtually identical to those provided under Second Will and First Will.

Consequently, in view of the above, including Florida case law considering this issue, we conclude that the reformation by the court based on scrivener’s error is consistent with applicable Florida law that would be applied by the highest court of that state.

Therefore, seventy (70) percent of the trust residue is treated as passing to the marital residuary trust created under Article 3(d)(1) of the Revocable Trust.

In addition, the marital residuary trust created for Spouse under Article 3(d)(1) of the Revocable Trust, satisfies the requirements for the marital deduction under § 2056(b)(7) and Decedent’s estate made the election under § 2056(b)(7)(B)(v). We conclude that property interests passing to the trust created under Article 3(d)(1) will be treated as qualified terminable interest property under section 2056(b)(7)(i).

A copy of this letter should be attached to any income, gift, estate, or generation-skipping transfer tax returns that you may file relating to these matters.

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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 the 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. Except as specifically ruled above, no opinion is expressed as to the federal tax consequences of the facts described above under the cited provisions or any other provisions of the Code or regulations.

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.

Sincerely yours,

George Masnik
Chief, Branch 4
Associate Chief Counsel
(Passthroughs and Special
Industries)

Enclosure
Copy for section 6110 purposes