



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Uniform Issue List: 401.06-02

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MAR - 4 2010

LEGEND:

Taxpayer A:

Taxpayer B:

Taxpayer C:

Taxpayer D:

Individual E:

Individual F:

Company AA:

Date 1:

Date 2:

Date 3:

Date 4

Date 5:

Date 6:

Date 7:

Date 8:

Date 9:

Designated Age A:

Trust T:

Amount 1:

Fund F:

Court V:

County B:

State S:

IRA X:

Dear:

This is in response to the January 12, 2009, letter submitted on your behalf by your authorized representative, as supplemented by correspondence dated September 9, 2009, in which you request several letter rulings under section 401(a)(9) of the Internal Revenue Code ("Code").

The following facts and representations have been submitted under penalty of perjury in support of the ruling requested:

Taxpayer A and Taxpayer B created Trust T, a revocable trust, on Date 1. Trust T was restated (Restated Trust) in its entirety on Date 2.

Article 8 of the Restated Trust provides for the creation of various trusts upon either the death of Taxpayer A or Taxpayer B, whomever is the first deceased.

Article 8.2 of the Restated Trust provides for the creation of a Survivor's Trust.

Article 8.3 of the Restated Trust provides for the creation of a Bypass Trust (named beneficiary of IRA X). The Bypass Trust is disposed of under the provisions of section 9.2 of the Restated Trust.

Article 8.4 of the Restated Trust provides for the creation of a Marital Deduction Trust.

Article 8.5 of the Restated Trust provides for a Disclaimed Property Trust.

Article 9 of the Restated Trust provides for the administration and distribution of the trusts created under Article 8.

Article 9.1 explains, in relevant part, that the beneficiary (Surviving Trust Creator) of the Survivor's Trust shall receive income from the trust as long as he/she is competent. If incompetent, the Trustee shall distribute such amounts as the Trustee determines appropriate for the health care, maintenance, support and welfare of the beneficiary of the trust.

Article 9.2 provides, in relevant part, that the Trustee shall distribute income from the Bypass Trust in installments, at least quarterly, for the health care,

maintenance, support and welfare of the beneficiary of the trust but only if other resources are clearly inadequate or not reasonably available to meet the needs of the beneficiary. The beneficiary of the Bypass Trust shall retain the power to allocate principal from the trust to Secondary Beneficiaries of the Bypass Trust and their descendants as long as the grantor beneficiary is competent and exercises the power in writing. To the extent that the beneficiary of the Bypass Trust does not effectively exercise this power of appointment, the balance of the Bypass Trust shall be disposed of under Article X.

Article X of the Restated Trust applies when both of the creators of Trust T (subsequently the Restated Trust) are deceased.

Article 10.1.1 of the Restated Trust provides for specific bequests set forth on Schedules E and F thereof.

Article 10.1.2 of the Restated Trust allocates a formula amount to Fund F ("Amount 1"). On or about Date 9, 2008, Amount 1 was paid to Fund F. Fund F was then immediately terminated, and Amount 1 was divided equally between Individuals E and F, the grandchildren of Taxpayers A and B.

Articles 10.2 and 10.3 of the Restated Trust create and provide for the administration of two Separate Protective Trusts (further described below). Article 10.2 further describes Taxpayers C and D as the "Secondary Beneficiaries").

Article 10.3.1 of the Restated Trust provides, in relevant part, that the Trustee is to distribute appropriate amounts of income and principal for the health care, maintenance, support, and education of the beneficiary of a Protective Trust, and, if a Special Independent Trustee is appointed by the beneficiary, to the descendants of the beneficiary.

Article 10.3.2 of the Restated Trust gives each of the beneficiaries of the Protective Trusts who has attained Designated Age A a lifetime power of appointment over the assets of his/her Protective Trust which power extends to charities.

Article 10.3.3 of the Restated Trust provides, in relevant part, that a beneficiary of a Protective Trust who dies after attaining Designated Age A may appoint, in writing, including by will, any Protective Trust assets to persons and entities, including charities, with certain exceptions specifically referenced therein.

Article XI of the Restated Trust provides that any trust assets not disposed of under Article X shall be disposed of as provided therein.

Article 11.1 of the Restated Trust provides for specific bequests to persons named or described in Schedule H attached thereto.

Article 11.2 of the Restated Trust provides that the residue shall be divided among the persons named or described in Schedule I attached thereto. Article 11.2 provides that a charity or other non-natural person was eligible to be a contingent beneficiary. Schedule I, however, does not reference any charity.

On Date 3, Taxpayer A and Taxpayer B amended the Restated Trust. The First Amendment inserted a new section, Section 13.3, that provides, in relevant part, that:

With respect to any IRA, 401K or other retirement plan payable to the trust on the death of either Trust Creator, it is the Trust Creators' desire that the Trustee utilize the minimum distribution rules described in the Internal Revenue Code ("IRC") and applicable regulations when making withdrawals from said retirement account...In particular, the trustee should be guided by the following: (a) The Trustee should first determine whether the custodian allows for long-term deferral of income taxes by the Trustee;...(c) the Trustee should determine what requirements exist, if any, in order to elect the longest tax-deferral period; (d) Having made the appropriate election in order to elect the longest tax-deferral period of time, the Trustee should withdraw funds from the retirement plan in the minimum amounts required under IRC and applicable regulations without penalty; additional amounts should be withdrawn only if the Trustee determines that a need exists;...(f)...The provisions of this instrument are intended to inform the Trustee of the Trust Creators' desire that the rules commonly known as the "stretch IRA" rules should be applied to all retirement plans. It is the Trust Creators' hope that the Trustee will use his or her best efforts to minimize income taxes on these assets for the maximum duration permitted by law...For purposes of qualifying as a Designated Beneficiary under IRC and applicable regulations, each Beneficiary may amend the terms of the trust which govern the distribution of his or her trust at death in the absence of a complete and effective exercise of any applicable power of appointment;...

Taxpayer A died on Date 4, 2003. Upon the death of Taxpayer A, several trusts were created under the terms of the Restated Trust (as stated above).

Taxpayer A was survived by her husband, Taxpayer B, and two children, Taxpayer C and Taxpayer D. Taxpayer B became the sole Trustee of the trusts administered under the terms of the Restated Trust upon the death of Taxpayer A.

Taxpayer B exercised his power as sole Trustee to appoint his daughters, Taxpayer C and Taxpayer D, as Co-Trustees of the above-referenced Bypass Trust.

Taxpayer B maintained an individual retirement account (IRA), IRA X, with Company AA. IRA X was intended to satisfy the requirements described in section 408 of the Code. During his life, Taxpayer B named the Trustee of the Bypass Trust as the beneficiary of his IRA X.

Taxpayer B died on Date 5, 2008. Date 5, 2008 was after Taxpayer B's required beginning date as that term is defined in section 401(a)(9)(C) of the Internal Revenue Code. When Taxpayer B died, the Restated Trust and all the trusts administered under it became irrevocable.

As of Date 4, 2003 and Date 5, 2008, both Taxpayer C and Taxpayer D had attained Designated Age A.

After the death of Taxpayer B, pursuant to Article X of the Restated Trust document, all the trusts administered under the Restated Trust instrument were consolidated and equally divided into the above described two Protective Trusts created for the benefit of Taxpayer C and Taxpayer D. One protective trust was created for the benefit of Taxpayer C and one for Taxpayer D. Taxpayer C and Taxpayer D was each individually appointed as Trustee of his/her respective Protective Trust.

On Date 6, 2008 Taxpayer C and Taxpayer D, acting as Trustees of the Bypass Trust, filed for a Declaratory Judgment in Court V, which is located in County B of State S. Taxpayer C and Taxpayer D asked Court V to modify the Restated Trust to comply with certain requirements under section 1.401(a)(9) of the Income Tax Regulations (Regulations).

On Date 7, 2008 Court V issued an order modifying the Restated Trust retroactively to Taxpayer B's death as requested.

The court order which modified the Restated Trust provided, in relevant part, as follows:

- (1) all amounts received from the custodian of IRA X are to be distributed to the beneficiaries of the Protective Trusts;
- (2) the Trustee is authorized to arrange direct distributions from the IRA to the beneficiary;
- (3) if a Special Independent Trustee is selected, distributions to descendents of beneficiaries born before 1955 are prohibited;
- (4) descendents of beneficiaries born before 1955, Contingent Beneficiaries and charities are removed as potential appointees of a beneficiary's lifetime power of appointment;
- (5) any individual born before 1955 is removed as a potential appointee of a beneficiary's testamentary power of appointment;
- (6) Taxpayer C (the oldest lineal descendant of Taxpayer B) is named as the designated beneficiary under section 1.401(a)(9)-4, Q&A-4, and the trust is to be administered so that all beneficiaries following

- Taxpayer C and Taxpayer D are "successor beneficiaries," as defined in section 1.401(a)(9)-5, A-7(c)(1); and
- (7) the Trustee is directed to use IRA proceeds to pay debts, administration expenses or taxes of Taxpayer B's estate only after other assets are exhausted, and is prohibited from using any IRA proceeds to make such payments after Date 8, 2009.

Based on the above, you through your authorized representative request the following letter rulings:

- (1) That IRA X be distributed as though the beneficiaries of the Bypass Trust administered under the Restated Trust, as amended by the First Amendment and Judgment Entry, were named beneficiaries of IRA X thereby satisfying the guidance set forth in section 1.401(a)(9)-4, Questions & Answers-4 and 5 of the Income Tax Regulations;
- (2) That Taxpayer C is the "designated beneficiary," as that term is used in section 401(a)(9)(A)(ii) of the Code, of IRA X based on the judicial modification of the Restated Trust retroactively to Taxpayer B's death, which modification is valid under State S's Revised Code;
- (3) Alternatively, that Taxpayer C is the "designated beneficiary," as used in section 401(a)(9)(A)(ii) of the Code, of IRA X as a result of removing certain discretionary distributees and potential objects of powers of appointment before Date 8, 2009 through the judicial modification of the Restated Trust under State S's Revised Code; and
- (4) That the applicable distribution period as used in section 1.401(a)(9)-5, A-5(c)(1) of the Regulations, for the applicable calendar year (2009) is 30.5 years (reduced yearly), which is Taxpayer C's life expectancy based upon her current year (2009) birthday.

With respect to your ruling requests, Code section 401(a)(9)(A) provides, in general, that a trust will not be considered qualified unless the plan provides that the entire interest of each employee --

(i) will be distributed to such employee not later than the required beginning date, or

(ii) will be distributed, beginning not later than the required beginning date, over the life of such employee or over the lives of such employee and a designated beneficiary or over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and a designated beneficiary. Section 401(a)(9)(C) of the Code provides, in relevant part, that, for purposes of this paragraph, the term "required beginning date" means April 1 of the calendar year following the calendar year in which the IRA holder attains age 70 1/2.

Section 401(a)(9)(B) of the Code provides that when an employee dies before their entire interest has been distributed but after distributions have begun under subparagraph of (A)(ii), the remaining portion of such interest will be distributed

at least as rapidly as under the method being used under subparagraph (A)(ii) as of the date of death.

Section 401(a)(9)(E) of the Code provides that for the purpose of section 401, the term designated beneficiary means any individual designated as a beneficiary by the employee.

Section 1.401(a)(9)-4 of the Income Tax Regulations, Question and Answer A-1, provides, in relevant part, that a designated beneficiary is an individual who is designated as a beneficiary under the plan. An individual may be designated as a beneficiary under the plan either by the terms of the plan or, if the plan so provides, by an affirmative election by the employee (or the employee's surviving spouse) specifying the beneficiary. Under these Regulations, a designated beneficiary need not be specified in the name of the plan in order to be a designated beneficiary so long as the individual who is to be the beneficiary is identifiable under the plan. The member of a class of beneficiaries capable of contraction or expansion will be treated as being identifiable if it is possible to identify the class member with the shortest life expectancy. Further, the passing of an employee's interest to an individual under a will or otherwise under applicable state law will not make that individual a designated beneficiary under section 1.401(a)(9)(E) unless that individual is designated as a beneficiary under the plan.

Section 1.401(a)(9)-4 of the Regulations, Q&A-3, provides that only individuals may be designated beneficiaries for purposes of section 401(a)(9). A person who is not an individual, such as the employee's estate or a charitable organization, may not be a designated beneficiary. If a person other than an individual is designated as a beneficiary of an employee's benefit, the employee will be treated as having no beneficiary for purposes of section 401(a)(9), even if there are also individuals designated as beneficiaries.

Section 1.401(a)(9)-4 of the Regulations, Q&A-5, provides that beneficiaries of a trust with respect to the trust's interest in an employee's benefit may be treated as designated beneficiaries if the following requirements are met:

- (1) the trust is valid under state law or would be but for the fact there is no corpus.
- (2) the trust is irrevocable or will, by its terms, become irrevocable upon the death of the employee.
- (3) the beneficiaries of the trust who are beneficiaries with respect to the trust's interest in the employee's benefit are identifiable within the meaning of A-1 of this section from the trust instrument.
- (4) relevant documentation has been timely provided to the plan administrator.

Section 1.401(a)(9)-4 of the Regulations, Q&A-4, provides in relevant part, that in order to be a designated beneficiary, an individual must be a beneficiary as of the date of the employee's death. Generally, an employee's designated beneficiary will be determined based on the beneficiaries designated as of the date of death who remain beneficiaries as of September 30 of the calendar year following the calendar year of the date of death.

Section 1.401(a)(9)-5 of the Regulations, Q&A-7(b), provides, in short, that except as provided in paragraph (c)(1) of this A-7, if a beneficiary's entitled to an employee's benefit after the employee's death is a contingent right, such contingent beneficiary is nevertheless considered to be a beneficiary for purposes of determining who, if anyone, is the employee's designated beneficiary.

Section 1.401(a)(9)-5 of the Regulations, Q&A- 5(a)(2) provides, in summary, that if an employee dies on or after his required beginning date without having designated a beneficiary, then post-death distributions must be made over the remaining life expectancy of the employee determined in accordance with paragraph (c)(3) of A-5.

Section 1.401(a)(9)-5 of the regulations, Q&A- 5(c)(1) provides, in general, that, with respect to a non-spouse designated beneficiary of a plan or IRA, the applicable distribution period measured by the beneficiary's remaining life expectancy is determined using the beneficiary's age as of the beneficiary's birthday in the calendar year immediately following the calendar year of the employee's death reduced by one for each subsequent calendar year.

Section 1.401(a)(9)-5 of the regulations, Q&A- 5(c)(3) provides, in general, that, with respect to an employee who does not have a designated beneficiary, the applicable distribution period measured by the employee's remaining life expectancy is the life expectancy of the employee using the age of the employee as of the employee's birthday in the calendar year of the employee's death. In subsequent calendar years, the applicable distribution period is reduced by one for each calendar year that has elapsed after the calendar year of the employee's death.

Section 1.401(a)(9)-5 of the regulations, Q&A- 7(b) provides, in general, that "contingent" beneficiaries must be considered in determining who, if anyone, is the "designated" beneficiary of a plan or IRA. A "successor" beneficiary, defined in Q&A-7(c) of the regulations as one who merely takes as the successor of a prior beneficiary after the death of said prior beneficiary, is not a "contingent" beneficiary.

Generally, the reformation of a trust instrument is not effective to change the tax consequences of a completed transaction. For example, in *Estate of La Meres v. Commissioner*, 98 T.C. 294 (1992), the trustees retroactively reformed a governing instrument solely for the purposes of qualifying the bequest for the

estate tax charitable deduction. The Tax Court held that the retroactive reformation, undertaken solely for tax considerations, was not effective for federal tax purposes. In *Estate of La Meres*, the Tax Court stated:

This and other courts have generally disregarded the retroactive effect of State court decrees for Federal tax purposes. See *Van Den Wymelenberg v. United States*, 397 F.2d 443, 445 (7th Cir. 1968); *Straight Trust v. Commissioner*, 245 F.2d 327, 329-330 (8th Cir. 1957), affg. 24 T.C. 69 (1955); *Estate of Nicholson v. Commissioner*, 94 T.C. 666, 673 (1990); *Fono v. Commissioner*, 79 T.C. 680, 695 (1982), affd. without published opinion 749 F.2d 37 (9th Cir. 1984); *American Nurseryman Publishing Co. v. Commissioner*, 75 T.C. 271, 275 (1980), affd. without published opinion 673 F.2d 1333 (7th Cir. 1981).

While we will look to local law in order to determine the nature of the interests provided under a trust document, we are not bound to give effect to a local court order which modifies the dispositive provisions of the document after respondent has acquired rights to tax revenues under its terms. As the Court of Appeals explained in *Van Den Wymelenberg v. United States*, supra at 445:

Were the law otherwise there would exist considerable opportunity for "collusive" state court actions having the sole purpose of reducing federal tax liabilities. Furthermore, federal tax liabilities would remain unsettled for years after their assessment if state courts and private persons were empowered to retroactively affect the tax consequences of completed transactions and completed tax years.

Estate of La Meres v. Commissioner, 98 T.C. at 311-312.

Generally, the Service will treat a state court order as controlling with respect to a reformation if the reformation is specifically authorized by the Internal Revenue Code, such as under section 2055(e)(3), which allows the parties to reform a split-interest charitable trust in order that the charitable interest will qualify for the charitable deduction as authorized under that statute. There is no applicable federal statute which authorizes Taxpayer C's or Taxpayer D's retroactive reformation of Trust T (or the later Restated Trust). Accordingly, absent specific authority in the Code or Regulations, the modification of the Restated Trust will not be recognized for federal tax purposes.

In this instance, the efforts undertaken to modify the terms of the Restated Trust will not be given retroactive effect for federal tax purposes and the designated beneficiary of IRA X must be determined under the terms of the Restated Trust as it existed at the time of Taxpayer B's death.

The Bypass Trust created under the terms of the Restated Trust was named as the beneficiary of Taxpayer B's IRA X. Provided said trust meets the requirements set forth in section 1.401(a)(9)-4 of the Regulations, Q&A-5, it is permissible to "look

through" the trust in order to determine who, if anyone, is the designated beneficiary.

In the situation described above, there was no identifiable designated beneficiary of IRA X at the time of Taxpayer B's death. The relevant terms of the Restated Trust, specifically the terms of the Bypass and related trusts, do not require or authorize either Taxpayer C or Taxpayer D to receive all amounts that are distributed from IRA X. The terms of the Restated Trust authorize only income and principal subject to a standard to be paid to or for the benefit of either Taxpayer C or Taxpayer D. The relevant Restated Trust terms also do not require that amounts distributed from IRA X, based on the life expectancy of Taxpayer C, be paid either to Taxpayer C, Taxpayer D, or any other natural person (human being). Relevant Restated Trust terms permit either Taxpayer C or Taxpayer D to appoint income or principal to descendants or charities. Because the terms of the Restated Trust allow for the accumulation of amounts distributed from IRA X, the remainder beneficiaries must be considered beneficiaries of IRA X for purposes of determining who, if anyone, was/is the designated beneficiary of IRA X. Charitable organizations are clearly authorized to be potential/contingent beneficiaries under relevant provisions of the Restated Trust instrument. However, only individuals may be designated beneficiaries for purposes of satisfying the requirements of Code section 401(a)(9) and related Income Tax Regulations. As a result, Taxpayer B is treated as having designated no beneficiary of his IRA X for purposes of section 401(a)(9) of the Code.

Potential beneficiaries may be eliminated after the date of death of a taxpayer and prior to September 30 of the calendar year following the calendar year of death of a taxpayer for purposes of determining who is the designated beneficiary of a plan/IRA for purposes of Code section 401(a)(9). However, beneficiaries may not be added during this same period. Furthermore, a "designated beneficiary" must be in existence as of an IRA holder's date of death. A designated beneficiary cannot be created after the date of death by means of a State Court Order even if said order is valid under State law.

In this case, due to the language of relevant terms of the controlling Restated Trust document there is no designated beneficiary for purposes of a section 401(a)(9) analysis. Subsequent efforts to obtain a post-mortem judicial modification had the effect of creating a designated beneficiary after the death of the taxpayer. Said efforts will not be given effect for purposes of Code section 401(a)(9).

Thus, with respect to your ruling requests, we conclude as follows:

- (1) IRA X is to be distributed as if Taxpayer B's IRA X had no designated beneficiary. In short, because entities ineligible to be treated as "designated beneficiaries" were eligible to receive amounts from Taxpayer B's IRA X, said entities (charities) constituted contingent beneficiaries as that term is used in the Income Tax Regulations promulgated under Code section 401(a)(9). Thus, Taxpayer B is treated

- as having designated no beneficiary within the meaning of Code section 401(a)(9) and the relevant Regulations with respect to his IRA X.
- (2) The requested response to this second ruling request cannot be provided as a result of our response to your first requested ruling.
 - (3) Taxpayer C cannot be treated as the "designated beneficiary" of Taxpayer B's IRA X based on the above-referenced State S Court Order since said order created a "designated beneficiary" of IRA X where none existed prior to the entry of the Court order. As described above, said creation of a designated beneficiary after the death of the IRA X owner (Taxpayer B) does not comply with the requirements of Code section 401(a)(9).
 - (4) Since Taxpayer B had attained his Code section 401(a)(9) required beginning date prior to his death, the applicable required distribution period with respect to his IRA X is the remaining life expectancy of Taxpayer B in accordance with paragraph (c)(3) of section 1.401(a)(9)-5, Q&A-5 of the Regulations.

No opinion is expressed as to the tax treatment of the transaction described herein under the provisions of any other section of either the Code or regulations which may be applicable thereto.

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

Pursuant to the power of attorney on file with this office, you are receiving the original of this letter ruling and your representative is receiving a copy of the letter ruling.

If you wish to inquire about this ruling, please address all correspondence to SE:T:EP:RA:T3.

Sincerely,


Frances V. Sloan, Manager,
Employee Plans Technical Group 3