

## Internal Revenue Service

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Department of the Treasury  
Washington, DC 20224

Third Party Communication: None  
Date of Communication: Not Applicable  
Person To Contact:  
ID No.  
Telephone Number:

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PLR-110667-10  
Date:  
August 17, 2010

### Legend:

Decedent  
Spouse  
Daughter  
Date 1  
Date 2  
Date 3  
Date 4  
Date 5  
Date 6  
Date 7  
Trust

Marital Agreement  
State Statute  
Court

Dear \_\_\_\_\_ :

This letter responds to your letter dated February 9, 2010, requesting a ruling under § 2056 of the Internal Revenue Code.

### Facts

On Date 1, Decedent established a revocable trust, Trust. Date 1 is prior to Decedent's marriage to Spouse. On Date 2, Decedent and Spouse entered into an

agreement, Marital Agreement, effective as of their date of marriage. Thereafter, on Date 3, Trust was amended and restated. Decedent died on Date 4, survived by Spouse. Decedent is also survived by a daughter, Daughter, from Decedent's previous marriage. Daughter has three children. Trust became irrevocable on Decedent's death.

Certain disputes arose in the administration of Decedent's estate. Trust and Marital Agreement have terms that are inconsistent such that both Trust and Marital Agreement cannot be administered as executed. Trust provides for certain outright distributions to Spouse and the creation of a qualified terminal interest property (QTIP) trust for Spouse. The balance of Trust's assets is to be distributed outright to Daughter. Contrary to the terms of Marital Agreement, Trust specifically provides that certain real property is to be transferred to the QTIP trust, rather than distributed outright to Spouse as provided in Marital Agreement. Further, while Decedent provided some financial benefits to Spouse in Marital Agreement, Decedent provided substantially greater financial benefits to Spouse under Trust. Spouse and Daughter also disagree on the proper construction of Trust's tax proration clause, as well as the allocation of expenses between principal and income with respect to the real property to be held in Trust.

In addition to the above, the beneficiary of an individual retirement account (IRA) owned by Decedent at the time of his death is uncertain. Decedent initially designated Trust as the beneficiary of the IRA. Thereafter, Decedent married Spouse and transferred his IRA to a different bank, without executing a new beneficiary designation. The IRA agreement with the new bank provides that, if no beneficiary designation is executed and filed with the bank, distribution of the IRA is made to the account owner's surviving spouse.

Spouse and Daughter, each represented by separate counsel, resolved the disputed issues and executed an agreement, Settlement Agreement, on Date 5. Settlement Agreement generally provides for the termination of Trust. Spouse is to receive certain property, including the real property required to be distributed to Spouse under the terms of Marital Agreement, and the IRA, outright and free of trust. Daughter will receive the remaining assets, outright and free of trust. The amounts to be distributed to Spouse and Daughter will be reduced equally by the expenses of administration of Trust incurred from the date of Decedent's death until the date of distribution. Estate taxes will be charged against and paid from the amount to be distributed to Daughter.

The Executor of Decedent's estate filed Decedent's Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return on Date 6. On Schedule M, Decedent's estate made an election to qualify the entire date of death value of the assets passing to Spouse under the terms of Settlement Agreement for the estate tax marital deduction under § 2056.

On Date 7, Court approved Settlement Agreement, effective on the date the Internal Revenue Service issues a private letter ruling confirming that assets passing to Spouse pursuant to Settlement Agreement qualify for the federal estate tax marital deduction under § 2056.

You request a ruling that Decedent's estate is entitled to a marital deduction under § 2056 for property passing to Spouse under the Settlement Agreement.

### Law and Analysis

Section 2056(a) provides that the value of the taxable estate shall be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to the surviving spouse.

Section 2056(b)(7)(A) provides that, in the case of qualified terminable interest property for purposes of the marital deduction, such property shall be treated as passing to the surviving spouse and not to any person other than the surviving spouse.

Section 2056(b)(7)(B) provides that the term "qualified terminable interest property" (QTIP) is property that passes from the decedent, in which the surviving spouse has a qualifying income interest for life, and to which an election applies. The surviving spouse has a qualifying income interest for life if the surviving spouse is entitled to all of the income payable annually or at more frequent intervals and no person has the power to appoint any part of the property to anyone other than the surviving spouse.

Section 20.2056(c)-2(d)(2) of the Estate Tax Regulations provides that, if as a result of a controversy involving the decedent's will, or involving any bequest or devise thereunder, a property interest is assigned or surrendered to the surviving spouse, the interest so acquired will be regarded as having "passed from the decedent to the surviving spouse" only if the assignment or surrender was a "bona fide recognition of enforceable rights of the surviving spouse in the decedent's estate." Such a bona fide recognition will be presumed where the assignment or surrender was pursuant to a decision of a local court upon the merits in an adversary proceeding following a genuine and active contest. However, such a decree will be accepted only to the extent that the court passed upon the facts upon which the deductibility of the property interest depends. If the assignment or surrender was pursuant to a decree rendered by consent, or pursuant to an agreement not to contest the will or not to probate the will, it will not necessarily be accepted as a bona fide evaluation of the rights of the spouse.

Rev. Rul. 66-139, 1966-1 C.B. 225, states that a valid claim by the surviving spouse to a share in the decedent's estate, made in good faith and settled as a result of arm's length negotiations without any court contest, will qualify as a bona fide claim

within the meaning of the regulations. The ruling holds that where such claim is paid by the decedent's estate, the payment qualifies for the marital deduction to the extent that the interest that would have passed to the surviving spouse as a result of the completed exercise of the spouse's right (i.e., in a court contest) would have been a deductible interest.

In Ahmanson Foundation v. United States, 674 F.2d 761 (9th Cir. 1981), the court held that property distributed to a spouse pursuant to a compromise settlement will be treated as passing from the decedent for marital deduction purposes, only if the distribution represents a good faith settlement of an enforceable claim. Relying on Commissioner v. Estate of Bosch, 387 U.S. 456 (1967), the court stated that

[E]ither a good faith settlement or a judgment of a lower state court must be based on an enforceable right under state law properly interpreted, in order to qualify as 'passing' pursuant to the estate tax marital deduction.

Ahmanson Foundation, 674 F.2d at 775.

State Statute provides that Court may terminate a trust due to changed circumstances not foreseen by the settlor of a trust. Court has the authority to terminate a trust if, due to circumstances not known and not anticipated, the continuation of the trust under its terms would defeat or substantially impair the accomplishment or the purposes of the trust.

In view of Ahmanson, property passing to a spouse pursuant to the settlement of a claim will be treated as passing from the decedent, to the extent the compromise is a bona fide settlement of a legally enforceable claim. The claim must be settled pursuant to arm's length negotiations. In this case, both Spouse and Daughter have legally enforceable rights and both are represented by separate legal counsel. Some of Trust's terms are inconsistent with the terms of Marital Agreement, while other Trust terms are ambiguous. The beneficiary of Decedent's IRA is also uncertain. Settlement Agreement is the product of arm's length negotiations and represents a good faith settlement. We recognize that, because of the uncertainty of litigation, determining a precisely correct allocation of assets in a settlement is difficult. We believe that Settlement Agreement provides an allocation of the estate's assets that is within a range of reasonable settlements. That is, the interests to be received by the parties (both as to the nature of the interests and their economic value) reflect the enforceable rights of the parties.

Based on the representations made and the information submitted, we conclude that the property passing to Spouse under Settlement Agreement passes from Decedent. Therefore, the distributions under Settlement Agreement to Spouse qualify for the federal estate tax marital deduction under § 2056.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an 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 herein, we express no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

The rulings in this letter pertaining to the federal estate and/or generation-skipping transfer tax apply only to the extent that the relevant sections of the Internal Revenue Code are in effect during the period at issue.

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,

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Leslie H. Finlow  
Acting Senior Technician Reviewer, Branch 4  
Office of the Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosure

Copy for § 6110 purposes  
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cc: