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Refer Reply To:  
CC:PSI:B04  
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Date:  
April 22, 2019

Re:

Legend

- Grantor =
- Revocable Trust =
- Marital Trust =
- CLAT =
- Date 1 =
- Date 2 =
- Charity =
- x =

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

This letter responds to your authorized representative's letter dated October 30, 2018, requesting rulings under § 2055 of the Internal Revenue Code.

The facts and representations are as follows:

On Date 1, Grantor established Revocable Trust, a revocable trust. Revocable Trust was amended and restated on Date 2. Grantor is the trustee of Revocable Trust.

Article I, Paragraph D of Revocable Trust sets forth the dispositive provisions applicable upon Grantor's death. Specifically, after (i) the payment of debts, taxes, and expenses pursuant to Paragraph C of Article I; (ii) the distribution of Grantor's personal property and the making of specific bequests to certain individuals; and (iii) the distribution of amounts to establish a generation-skipping tax exempt trust and a trust equal to the allowable credit under § 2011, the remainder of Revocable Trust will be distributed to either a marital trust, Marital Trust, to benefit Grantor's spouse, Spouse, if Spouse survives Grantor, or to a charitable lead annuity trust (CLAT), if Grantor survives Spouse.

Paragraph C(7) of Article I provides that if Grantor survives Spouse, upon the death of Grantor, any taxes owed shall be charged against, and reduce the amount passing to the CLAT.

Article II, Paragraph A sets forth the provisions governing Marital Trust. Specifically, Spouse is entitled to all the income from the trust and the trustee has the discretion to distribute principal to Spouse as necessary to provide for the health, education, maintenance, and/or support of Spouse. Marital Trust grants Spouse a testamentary power of appointment to appoint the assets of Marital Trust to various individuals and charities. To the extent Spouse fails to exercise this power or is otherwise in default of such exercise, the assets of Marital Trust will be distributed to the CLAT. If Revocable Trust is not revoked or amended, Marital Trust, as drafted, is intended to qualify for the marital deduction under § 2056.

If Spouse does not survive Grantor, upon the death of Grantor, the residue of Revocable Trust will be distributed to the CLAT. Article II, Paragraph B sets forth the terms of the CLAT. Specifically, commencing with the date of death of the survivor of Grantor and Spouse, and in each taxable year of the CLAT prior to the Termination Date, the trustee shall pay the Annuity Amount to the Annuity Beneficiary.

The Annuity Amount is an amount equal to five percent (5%) of the fair market value of the initial trust estate (as finally determined for federal estate tax purposes in the estate of the survivor of the Grantor and Spouse). The Annuity Amount will be prorated, on a daily basis, by the trustee for (i) a short taxable year, and (ii) the taxable year in which the Termination Date occurs. The Annuity Amount will be paid annually on the last day of the taxable year of the CLAT. The first taxable year of the CLAT begins with the date of the death of the survivor of Grantor and Spouse and ends on the last day of such calendar year. Thereafter, the CLAT will be on a calendar year.

The Annuity Beneficiary is Charity. However, if the Annuity Beneficiary is not an exempt organization described in §§ 170(c), 2522(a) or (b), and 2055(a), the Annuity Amount will be paid to such one or more exempt organizations, as the trustee shall select.

The term of years and Termination Date of the CLAT is established by formula under Paragraph B(4) of Article II, as follows. Payment of the Annuity Amount terminates at the end of that number of years, rounded up to the nearest whole year, starting on the date of death of the survivor of Grantor and Spouse which, taking into account (i) the lowest federal mid-term rate which may be elected under § 7520; (ii) the frequency of the payment of the Annuity Amount; (iii) the Annuity Amount; and (iv) such valuation methods, tables, factors, and applicable rates prescribed by the appropriate provisions of the Code, results in a charitable deduction for federal estate tax purposes in the estate of the survivor of Grantor and Spouse equal to (or as close as possible to) one hundred percent (100%) of the fair market value of the property transferred to the CLAT

as finally determined for federal estate tax purposes in the estate of the survivor of Grantor and Spouse. Specifically, the trustee:

- (i) shall determine or obtain from the personal representative of the estate of the survivor of the Grantor and Spouse, the fair market value (Initial FMV) of the property transferred to the CLAT as finally determined for federal estate tax purposes in the estate of the survivor of the Grantor and Spouse;
- (ii) shall determine the Annuity Amount by multiplying the Initial FMV of the CLAT by the annual percentage payout rate of five percent (5%);
- (iii) shall then divide the Initial FMV of the CLAT by the Annuity Amount;
- (iv) shall determine the two term-of-years annuity factors between which fall the result determined in (iii) above, using the factors based on the applicable Treasury regulations or publications issued by the Internal Revenue Service using the applicable assumed rate of return prescribed by § 7520.
- (v) The number of whole years for which the CLAT must be in effect in order to produce a charitable deduction in an amount that will be equal to or as close as possible to the fair market value of the property transferred to the CLAT as finally determined for federal estate tax purposes in the estate of the survivor of Grantor and Spouse, will be that number of years which corresponds to the greater of the two annuity factors determined in (iv) above. If the values used by the trustee in determining the Termination Date are incorrectly determined or if the Termination Date as determined is not correctly determined initially, then, within a reasonable time after the correct determination is made, the trustee shall lengthen or shorten the term of the CLAT to the correct duration.

If the trustee does not obtain a favorable private letter ruling from the Service, the term of years will be  $\underline{x}$  years starting on the date of death of the survivor of Grantor and Spouse.

Upon the Termination Date, the remaining principal of the CLAT, together with all accumulated and undistributed income, will be added to other family trusts.

Paragraph B(5) of Article II provides that no additional contributions may be made to the CLAT after the initial contribution.

Paragraph B(7) of Article II provides that notwithstanding any other provisions of Revocable Trust, the CLAT is subject to the following provisions: (i) the trustee shall not engage in any act of self-dealing as defined in § 4941(d), nor make any taxable expenditures as defined in § 4945(d); and (ii) except to the extent provided in § 4947(b)(3), the trustee shall not retain any excess business holdings (as defined in § 4943(c)), which would subject the CLAT to tax under § 4943, nor shall the trustee acquire any assets which would subject the CLAT to tax under § 4944 or retain any assets which would, if acquired by the trustee, subject the CLAT to tax under § 4944.

You have requested the following rulings:

1. The use of the formula set forth in Article II, Paragraph B(4) of Revocable Trust satisfies the requirement that a guaranteed annuity must be paid for a specified term of years under § 2055(e)(2)(B).
2. The estate of the survivor of Grantor and Spouse will be entitled to a federal estate tax deduction under § 2055(a) for the present value of the annuity interest payable to Charity, as determined in accordance with § 20.2055-2(f)(2)(iv).

### Rulings 1 and 2

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

Section 2055(a) provides, in part, that for purposes of the federal estate tax, the value of the taxable estate is determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, or transfers to or for the use of certain charitable organizations.

Section 2055(b) provides that property includible in the decedent's gross estate under § 2041 (relating to powers of appointment) received by a donee described in this section shall, for purposes of this section, be considered a bequest of such decedent.

Section 2055(c) provides that if the tax imposed by § 2001, or any estate, succession, legacy, or inheritance taxes, are, either by the terms of the will, by the law of the jurisdiction under which the estate is administered, or by the law of the jurisdiction imposing the particular tax, payable in whole or in part out of the bequests, legacies, or devises otherwise deductible under this section, then the amount deductible under this section shall be the amount of such bequests, legacies, or devises reduced by the amount of such taxes.

Section 2055(d) provides that the amount of the charitable deduction under this section for any transfer shall not exceed the value of the transferred property required to be included in the gross estate.

Section 2055(e)(1) provides that no deduction is allowed under § 2055(a) for a transfer to or for the use of an organization or trust described in § 508(d) or § 4948(c)(4) subject to the conditions specified in such section.

Section 2055(e)(2)(B) disallows the deduction under § 2055(a) where the lead interest in property passes to a charitable or other organization described in § 2055(a) and the remainder interest in the same property passes to a noncharitable beneficiary, unless the lead interest is in the form of a guaranteed annuity or is a fixed percentage of the fair market value of all the property (to be determined yearly) and distributed annually.

Section 20.2055-2(a) of the Estate Tax Regulations provides that if a trust is created or property is transferred for both a charitable and a private purpose, a deduction may be taken for the value of the charitable beneficial interest only insofar as that interest is presently ascertainable, and hence severable from the noncharitable interest.

Section 20.2055-2(e)(1) provides, in part, that in the case of decedents dying after December 31, 1969, where an interest in property passes or has passed from the decedent for charitable purposes and an interest (other than an interest which is extinguished upon the decedent's death) in the same property passes or has passed from the decedent for private purposes (for less than an adequate and full consideration in money or money's worth) after October 9, 1969, no deduction is allowed under § 2055 for the value of the interest which passes or has passed for charitable purposes unless the interest in property is a deductible interest described in subparagraph (2) of § 20.2055-2(e).

Subparagraph (2)(vi) of § 20.2055-2(e) provides, in relevant part, that a "deductible interest" for purposes of subparagraph (1) includes a charitable interest in property where the charitable interest is a guaranteed annuity interest, whether or not such interest is in trust. For this purpose, the term "guaranteed annuity interest" means the right pursuant to the instrument of transfer to receive a guaranteed annuity. A guaranteed annuity is an arrangement under which a determinable amount is paid periodically, but not less often than annually, for a specified term of years or for the life or lives of certain individuals, each of whom must be living at the date of death of the decedent and can be ascertained at such date. An interest payable for a specified term of years can qualify as a guaranteed annuity interest even if the governing instrument contains a savings clause intended to ensure compliance with a rule against perpetuities. The savings clause must utilize a period for vesting of 21 years after the deaths of the measuring lives who are selected to maximize, rather than limit, the term of the trust. An amount is determinable if the exact amount which must be paid under the conditions specified in the instrument of transfer can be ascertained as of the

appropriate valuation date. For example, the amount to be paid may be a stated sum for a term of years.

Section 20.2055-2(e)(2)(vi)(e) provides that where a charitable interest in the form of a guaranteed annuity interest is in trust and the present value, on the appropriate valuation date, of all the income interests for a charitable purpose exceeds 60 percent of the aggregate fair market value of all amounts in such trust (after the payment of estate taxes and all other liabilities), the charitable interest will not be considered a guaranteed annuity interest unless the governing instrument of the trust prohibits both the acquisition and the retention of assets which would give rise to a tax under § 4944 if the trustee had acquired such assets.

Section 2056(a) provides that the value of the taxable estate will, except as limited by § 2056(b), 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 his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Section 2056(b)(1) provides that where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction will be allowed with respect to the interest if the decedent transfers to any person other than the surviving spouse an interest in the property, and if by reason of the transfer the other person may possess or enjoy any part of the property after the termination or failure of the interest transferred to the surviving spouse.

Section 2056(b)(7)(A) provides that, in the case of qualified terminable interest property, for purposes of § 2056(b)(1), no part of the property will be considered as transferred to any person other than the surviving spouse.

Section 2056(b)(7)(B) provides that the term “qualified terminable interest property” (QTIP) means property that passes from the decedent, in which the surviving spouse has a qualifying income interest for life, and to which an election under § 2056(b)(7) applies. The surviving spouse has a qualifying income interest for life if: (i) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, or has a usufruct interest for life in the property, and (ii) no person has a power to appoint any part of the property to any person other than the surviving spouse. A specific portion of property will be treated as separate property. An election under paragraph (b)(7) with respect to any property will be made by the executor on the return of tax imposed by § 2001. The election, once made, is irrevocable.

Section 2044(a) and (b) provide that, for purposes of the federal estate tax, the gross estate of a decedent will include the value of property with respect to which a deduction

was allowed for the transfer of the property to the decedent under § 2056(b)(7). Section 2044(c) treats this property as passing from the decedent.

### Analysis

In this case, the Annuity Amount is an amount equal to five percent (5%) of the fair market value of the initial trust estate (as finally determined for federal estate tax purposes in the estate of the survivor of the Grantor and Spouse). Accordingly, the amount of the annual annuity payment will be a determinable amount, ascertainable as of the date of death of the survivor of Grantor and Spouse. However, a formula set forth in Article II, Paragraph B(4) of the CLAT is used to determine the specific term of years for which the annuity payments will be made. The computation of the term is based in part on the initial net fair market value of assets passing to the CLAT as finally determined for federal estate tax purposes. Thus, the provision for determining the term of years of the CLAT is permissible because the term, although not expressly stated in the instrument, is determinable as of the date of death of the survivor of Grantor and Spouse, based on the formula in the instrument. Because the term of the CLAT is ascertainable as of the date of death of the survivor of Grantor and Spouse, under the terms of the instrument, we conclude that the CLAT satisfies the “specified term” requirement of § 20.2055-2(e)(2)(vi). Based upon the facts submitted and the representations made, we conclude that the use of the formula set forth in Article II, Paragraph B(4) of Revocable Trust satisfies the requirement that a guaranteed annuity must be paid for a specified term of years under § 2055(e)(2)(B).

In addition, based upon the facts submitted and the representations made and provided that the CLAT is established and administered under the provisions of Article II of Revocable Trust, as submitted, and further provided that the CLAT is a valid trust under state law, we conclude that if Grantor survives Spouse, and dies without modifying or revoking Revocable Trust, Grantor’s estate will be entitled to a deduction under § 2055(a) for the present value of the annuity from the CLAT provided the recipient of the annuity from the CLAT is a charitable organization described in §§ 170(c), 2055(a), and 501(c)(3). Further, we conclude that if Spouse survives Grantor, and Grantor dies without modifying or revoking Revocable Trust, Spouse’s estate will be entitled to a deduction under § 2055(a) for the present value of the annuity from the CLAT provided: (i) the recipient of the annuity from the CLAT is a charitable organization described in §§ 170(c), 2055(a), and 501(c)(3); (ii) the terms of Marital Trust satisfy the requirements of § 2056(b)(7); (iii) the election under § 2056(b)(7) is properly made for the assets of Marital Trust; and (iv) Spouse does not exercise her testamentary power of appointment such that the assets of Marital Trust actually pass to the CLAT.

To the extent any estate, succession, legacy, or inheritance taxes are paid from the residue prior to funding the CLAT pursuant to the terms of Revocable Trust or by the law of the jurisdiction under which the estate is administered, the amount of the

charitable deduction in either estate is determined using the actual amount passing to the CLAT after payment of such taxes. Section 2055(c).

This ruling is based on the facts and applicable law in effect on the date of this letter. If there is a change in material fact or law (local or federal) before the transactions considered in the ruling take effect, the ruling will have no force or effect.

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. In particular, we express no opinion as to whether or not the charitable beneficiary designated in Revocable Trust is described in §§ 170(b)(1)(A), 2055(a), and 2522(a).

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

*Leslie H. Finlow*

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

cc: