Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
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Date:
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LEGEND:

a	=
Grantor	=
Spouse	=
b	=
c	=
Corporation	=
A	=
d	=
e	=
f	=
Children	=
State	=

Dear Sir:

In a letter, dated , you requested rulings under §§ 2207A, 2519, and 2702 of the Internal Revenue Code. This letter responds to your request.

The information submitted and the representations made are summarized as follows: On a, Grantor executed an Amended and Restated Trust (the Trust). Article II(B) of the Trust provides that at all times during Grantor's life, whether or not the trustee is exercising investment responsibilities, the trustee, at least quarterly, is to pay to Grantor or apply for Grantor's benefit so much of the net income and principal of the Trust property as Grantor requests at any time and, in the absence of such request, so much as the trustee in its sole discretion may decide to pay or apply. In the event of Grantor's incapacity or unavailability, as determined by the trustee in its sole discretion,

the trustee may from time to time pay to or apply for the benefit of Grantor or Spouse or any one or more of Grantor's issue so much of the income and principal as the trustee in its sole discretion deems advisable. The trustee, in its sole discretion, may also make gifts of Trust principal outright or in trust in order to continue any gift program previously commenced by Grantor or make use of available federal gift tax annual exclusions. Any income not expended under the terms of this Article is to be accumulated and added to principal annually.

Article IV(B) of the Trust provides that on Grantor's death, the trustee is to divide the balance of the Trust property (after payment of taxes, funeral expenses, and expenses of administration), as of the date of Grantor's death and according to the fair market value of the assets constituting the balance of the Trust property at the time or times of allocation, into two separate trusts, one named the Marital Election Trust, and one named the Non-Exempt Marital Trust. The trustee is to allocate to the Marital Election Trust a fraction equal to the smaller of: (a) one-half of the remaining Trust property or (b) a fraction, the numerator of which is to be an amount equal to the generation-skipping transfer (GST) tax exemption allowed to Grantor at the time of Grantor's death under § 2631 of the Internal Revenue Code of 1986 after taking into account any other transfers during Grantor's lifetime or occurring at Grantor's death, which will result in a portion of Grantor's GST tax exemption being allocated to those other transfers, and the denominator of which is to be an amount equal to the value of the balance of the Trust property, as finally determined for federal estate tax purposes. The remainder of the Trust property is to be allocated to the Non-Exempt Marital Trust. The trustee is to hold, manage, invest, and distribute the Non-Exempt Marital Trust as provided in Paragraph C of Article IV.

Article IV(C)(1) of the Trust provides that the trustee is to pay to or apply for the benefit of Spouse, during Spouse's lifetime, the entire net income from the Non-Exempt Marital Trust, in installments at least quarter-annually, and may in its discretion pay to Spouse or apply for Spouse's benefit amounts of the principal of the Non-Exempt Marital Trust; provided, however, that if only a portion of the Non-Exempt Marital Trust has qualified for the marital deduction in the federal estate tax proceeding relating to Grantor's estate, principal distributions are to be made first from that portion of the Non-Exempt Marital Trust.

Article IV(C)(2) of the Trust provides that if at any time Spouse is taxed with all or any part of the income of the Non-Exempt Marital Trust, whether or not Spouse actually receives the income, the trustee may on Spouse's written request, distribute to Spouse principal in an amount sufficient, in the trustee's discretion, to pay any federal or state income taxes directly attributable to the income.

Article IV(C)(3) of the Trust provides that in addition to the income and discretionary payments of principal from the Non-Exempt Marital Trust, the trustee is to pay to Spouse during Spouse's lifetime from the principal of the Non-Exempt Marital Trust, on Spouse's written request during the last month of each fiscal year of the Non-

Exempt Marital Trust, an amount not to exceed during the fiscal year the greater of b or c percent of the total value of the principal of the Non-Exempt Marital Trust on the last day of the fiscal year without reduction for the principal payment for the fiscal year. This right to withdrawal is noncumulative, so if Spouse does not withdraw, during the fiscal year, the full amount to which Spouse is entitled, Spouse's right to withdraw the amount not withdrawn is to lapse at the end of that fiscal year.

Article IV(C)(4) of the Trust provides that on the death of Spouse, the trustee is to pay, on the request of Spouse's personal representative, the amount of any incremental death taxes attributable to the inclusion of any of the marital trusts in Spouse's taxable estate, and is to pay over, convey, and distribute the entire remaining principal of the Non-Exempt Marital Trust to or in trust for the appointee or appointees from among Grantor's issue and the spouses of Grantor's issue, in the manner and in the proportions as Spouse may appoint in and by the Last Will of Spouse, making specific reference to this power of appointment. In default of the exercise of the power of appointment by spouse, or insofar as any part of the Non-Exempt Marital Trust is not effectively appointed, then on Spouse's death (or at the death of Grantor if Spouse does not survive Grantor), the trustee is to divide the balance of each trust into a sufficient number of equal shares to create one equal share for each child of Grantor who is then living and one equal share for the then living issue of each child of Grantor who is then deceased. In determining the shares, the trustee may allocate cash or other assets to the shares in such manner as it deems appropriate, but in allocating assets other than cash, it is to use values determined as of the date of the allocation or distribution. All shares of Corporation are to be allocated to the share created for A, if A is then living, up to the full amount of the share. Each share is to be distributed by the trustee as follows: (a) A share of the Non-Exempt Marital Trust created for a child of Grantor is to be distributed to that child, absolutely and free of trusts; (b) A share created for the issue of a deceased child of Grantor is to be paid over to the then living issue of the deceased child *per stirpes*, subject to the provisions made for trusts for persons under age d.

Grantor died on e. On Grantor's estate tax return, Grantor's estate elected to treat the Non-Exempt Marital Trust as qualified terminable interest property (QTIP) as provided in § 2056(b)(7).

The trustee of the Trust proposes to sever the Non-Exempt Marital Trust into two separate trusts: (1) Trust A, and (2) Trust B. Trust A will contain sufficient assets to make gross gifts in the aggregate amount of f to Children, and pay all of the gift taxes attributable to those gifts. Trust B would contain the remaining balance of the assets in the Non-Exempt Marital Trust.

Each of Trust A and Trust B will contain a strictly proportional amount of each asset contained in the Non-Exempt Marital Trust. Both Trust A and Trust B will be held under the same terms and conditions as the Non-Exempt Marital Trust.

It is represented that the severance is authorized under the laws of State. Under State law, a separate trust created by severance must be treated as a separate identical trust for all purposes from the effective date of the severance.

After the severance, Spouse will make a nonqualified disclaimer of all of Spouse's interest in Trust A.

You have requested the following rulings:

(1) If Spouse renounces Spouse's interest in the property in Trust A, Spouse will not be deemed to have made a gift of property in Trust B under § 2519.

(2) If Spouse renounces Spouse's interest in the property in Trust A, the value of Spouse's income interest in Trust B will not be valued at zero under § 2702.

(3) If Spouse renounces Spouse's interest in the property in Trust A and the renunciation is conditioned on Spouse's children paying all gift taxes attributable to the transfer, the amount of the gift will be reduced by the gift taxes paid by the children.

Section 2501(a) imposes a tax, computed as provided in § 2502, for each calendar year on the transfer of property by gift during the calendar year by an individual, resident or nonresident.

Section 2502(c) provides that the tax imposed by § 2501 shall be paid by the donor.

Section 2511(a) provides that the tax imposed by § 2501 shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2512(b) provides that, where property is transferred for less than adequate and full consideration in money or money's worth, the amount by which the value of the property exceeded the value of the consideration is deemed a gift, and shall be included in computing the amount of gifts made during the calendar year.

Section 2519(a) provides that any disposition of all or part of a qualifying income interest for life in any property to which this section applies shall be treated as a transfer of all interests in the property other than the qualifying income interest.

Section 2519(b) provides that § 2519(a) applies to any property if a deduction was allowed with respect to the transfer of such property to the donor—

(1) under § 2056 by reason of subsection (b)(7) thereof, or

(2) under § 2523 by reason of subsection (f) thereof.

For gift tax purposes, § 2207A(b) provides that, if for any calendar year tax is paid under chapter 12 with respect to any person by reason of property treated as transferred by such person under § 2519, such person shall be entitled to recover from the person receiving the property the amount by which—

(1) the total tax for such year under chapter 12 exceeds

(2) the total tax which would have been payable under such chapter for such year if the value of such property had not been taken into account for purposes of chapter 12.

Section 2702 provides special valuation rules in the case of transfers of interests in trusts to (or for the benefit of) a member of the transferor's family .

Section 2702(a)(1) provides that solely for purposes of determining whether a transfer of an interest in trust to (or for the benefit of) a member of the transferor's family is a gift (and the value of such transfer), the value of any interest in such trust retained by the transferor or any applicable family member shall be determined as provided in § 2702(a)(2).

Section 2702(a)(2) provides that the value of any retained interest that is not a qualified interest shall be treated as being zero. The value of any retained interest that is a qualified interest is determined under § 7520.

Section 25.2519-1(a) of the Gift Tax Regulations provides that if a donee spouse makes a disposition of all or part of a qualifying income interest for life in any property for which a deduction was allowed under § 2056(b)(7) or § 2523(f) for the transfer creating the qualifying interest, the donee spouse is treated for purposes of chapters 11 and 12 of subtitle B of the Internal Revenue Code as transferring all interests in property other than the qualifying income interest. For example, if the donee spouse makes a disposition of part of a qualifying income interest for life in trust corpus, the spouse is treated under § 2519 as making a transfer subject to chapters 11 and 12 of the entire trust other than the qualifying income interest for life. Therefore, the donee spouse is treated as making a gift under § 2519 of the entire trust less the qualifying income interest, and is treated for purposes of § 2036 as having transferred the entire trust corpus, including that portion of the trust corpus from which the retained income interest is payable. A transfer of all or a portion of the income interest of the spouse is a transfer by the spouse under § 2511.

Section 25.2519-1(c) provides that the amount treated as a transfer under § 2519 upon a disposition of all or part of a qualifying income interest for life in QTIP property is equal to the fair market value of the entire property subject to the qualifying income interest, determined on the date of the disposition (including any accumulated income and not reduced by any amount excluded from total gifts under

§ 2503(b) with respect to the transfer creating the interest), less the value of the qualifying income interest in the property on the date of the disposition. The gift tax consequences of the disposition of the qualifying income interest are determined separately under § 25.2511-2.

Section 25.2511-2(a) provides that the gift tax is not imposed upon the receipt of the property by the donee, nor is it necessarily determined by the measure of enrichment resulting to the donee from the transferor, nor is it conditioned upon the ability to identify the donee at the time of the transfer. On the contrary, the tax is a primary and personal liability of the donor, is an excise upon the donor's act of making the transfer, is measured by the value of the property passing from the donor, and attaches regardless of the fact that the identity of the donee may not then be known or ascertainable.

Rev. Rul. 75-72, 1975-1 C.B. 310, holds that gift tax imposed on a transfer that is paid by the donee may be deducted from the value of the transferred property in determining the amount of the gift, if it is established that the payment of the tax by the donee or from the property itself is a condition of the transfer. If, at the time of the transfer, the gift is made subject to a condition that the gift tax is to be paid by the donee or out of the transferred property, then the donor receives consideration for the transfer in the amount of the gift tax to be paid by the donee. Thus, under § 2512(b), the value of the gift is measured by the fair market value of the property passing from the donor minus the amount of the gift tax to be paid by the donee.

Rev. Rul. 81-223, 1981-2 C.B. 189, holds that, in determining the amount of the gift, the tax liability assumed by the donee may be deducted from the value of the transferred property, if the payment of the tax by the donee is a condition of the transfer.

Although § 2502(c) provides that the tax on the gift is the liability of the donor, in Rev. Rul. 75-72 and Rev. Rul. 81-223 the burden of the tax was shifted to the donees by agreement. The amount of the gift on which the gift tax was computed was reduced by the amount of gift tax paid by the donee.

As discussed above, with respect to the gift tax imposed as a result of a transfer under § 2519, § 2207A(b) statutorily shifts the burden, but not the liability, for paying the gift tax to the donee. In reimbursing the donor for the gift tax paid pursuant to the statute, the donee provides consideration for the gift. The donee's payment inures to the benefit of the donor because it reimburses the donor for gift tax that the donor was liable for and would otherwise be required to pay out of the donor's own funds. See Rev. Rul. 75-72. Accordingly, net gift treatment of a transfer under § 2519 is implicit under § 2207A (b).

Based on the information submitted and the representations made, we conclude that if Spouse renounces Spouse's interest in Trust A (after the Non-Exempt Marital Trust is severed into Trust A and Trust B), then

(1) Spouse will not be deemed to have made a gift of the property in Trust B under § 2519;

(2) The value of Spouse's income interest in Trust B will not be valued at zero under § 2702; and

(3) Provided that Spouse's renunciation is conditioned upon spouse's children paying all gift taxes attributable to the transfer, the amount of Spouse's gift with respect to the renunciation of Spouse's interest in Trust A will be reduced by the amount of such gift taxes paid by the children.

Except as specifically ruled above, we express or imply no opinion concerning the federal tax consequences of this transaction under the cited provisions or any other provision of the Code.

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

Sincerely yours,
Frances D. Schafer
Counsel to the Associate Chief Counsel
(Passthroughs and Special Industries)