Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

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Number: **199903015**
Release Date: 1/22/1999

Date:
October 23, 1998

Re:

Legend

Decedent:
Date 1:
Date 2:
X:
Y:
Charitable Trust:
Foundation:

Dear :

We received your letter dated requesting rulings concerning the application of § 2055(e)(3) of the Internal Revenue Code to the proposed reformation of Article THIRD of Decedent's will. Specifically, you requested the following:

1) The charitable remainder interests provided for under Article THIRD of Decedent's will before reformation are "reformable interests" as described in § 2055(e)(3)(C)(ii);

2) The proposed reformation of Article THIRD of Decedent's Will will constitute a "qualified reformation" within the meaning of § 2055(e)(3);

3) The proposed charitable remainder unitrusts created under the will, as reformed, will constitute charitable remainder unitrusts under § 664 provided the trusts operate in a manner consistent with the terms of the Will, as reformed, and are valid trusts under local law; and,

4) Decedent's estate will be entitled to a federal estate tax charitable deduction under § 2055 for the value of the remainder interests in the various unitrusts

passing to the Charitable Trust and the Foundation.

The facts as represented are as follows. Decedent died on Date 1. Decedent's Will established X split-interest trusts intended to constitute charitable remainder unitrusts. One beneficiary predeceased Decedent, so only Y trusts will be created.

Under the terms of the trusts created under Decedent's will, each beneficiary will receive a unitrust amount of six percent of the net fair market value of the assets comprising their respective trusts. These income interests are payable to individual beneficiaries for their lifetimes, with the exception of one of the trusts, which is payable jointly to two individuals, and the survivor thereof upon the death of either, (concurrently and consecutively).

Article THIRD further provides that upon the death of each respective income beneficiary, the remainder interests are to be distributed to Charitable Trust and/or Foundation. You represent that the trustees under Decedent's will are applying for a determination letter recognizing Charitable Trust as exempt from taxation under § 501(c)(3), and that, at a later time, the trustees intend to apply for a similar determination letter with respect to Foundation.

The trusts created under Article THIRD of the will do not contain all of the technical requirements set forth in § 2055(e) and § 664. Consequently, the co-executors filed a petition to reform the trusts in accordance with § 2055(e)(3). On Date 2, the court issued a "Decree of Construction and Reformation to Conform Will to Federal Tax Law." Taxpayers represent that the split-interest trusts, as reformed, are substantially similar to the actual language of Sections 6 and 8 of Rev. Proc. 90-30, 1990-1 C.B. 534.

Trusts, as reformed, provide that the trustees will pay to each beneficiary, in each taxable year of their lives, a unitrust amount equal to six percent of the net fair market value of the assets constituting the applicable charitable remainder unitrust valued as of the first day of each taxable year. The unitrust amounts are to be paid in equal quarterly amounts from income, or to the extent that income is insufficient, from principal. Any net income in excess of the unitrust amount will be added to principal.

If for any year the net fair market value of the trust assets are incorrectly determined, then within a reasonable period after the value is finally determined for federal tax purposes, the trustees shall pay to the applicable recipients (in the case of an undervaluation) or receive from the applicable recipients (in the case of an overvaluation) an amount equal to the difference between the unitrust amount properly payable and the unitrust amount actually paid. Notwithstanding the foregoing, in the case of the trust for two beneficiaries, upon the death of the first recipient to die, the surviving recipient shall be entitled to receive the entire unitrust amount.

The obligation to pay the unitrust amount shall commence as of the date of Decedent's death, but payment of the unitrust amount may be deferred until the end of the taxable year of the applicable unitrust in which occurs the complete funding of the applicable reformed trust. If the unitrust payments are deferred, interest compounded annually must be paid for the deferral period.

Upon the death of the applicable trust beneficiary, the applicable trust will terminate, and reformed trust assets will be distributed to Charitable Trust. If Charitable Trust is not an organization described in §§ 170(c) and 2055(a) at the time when any principal or income of any unitrust is to be distributed to it, then the trustees shall distribute such principal or income to such one or more organizations described in §§ 170(c) and 2055(a) as the trustees shall select in their sole discretion.

Section 2055(a) provides that the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, and transfers to or for a corporation or certain other organizations organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes.

Section 2055(e)(2)(A) provides that where an interest in property passes or has passed from the decedent to a person, or for a use, described in § 2055(a), and an interest (other than an interest that is extinguished upon the decedent's death) in the same property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to a person, or for a use, described in § 2055(a), no deduction shall be allowed under this section for the interest which passes or has passed to the person, or for the use, described in subsection (a) unless in the case of a remainder interest, the interest is in a charitable remainder annuity trust or a charitable remainder unitrust (described in § 664) or a pooled income fund (described in § 642(c)(5)).

Section 2055(e)(3)(A) provides that a deduction is allowed under § 2055(a) for any qualified reformation.

Section 2055(e)(3)(B) defines the term "qualified reformation" to mean a change of a governing instrument by reformation, amendment, construction, or otherwise that changes a reformable interest into a qualified interest, but only if–

(i) any difference between (I) the actuarial value (determined as of the date of the decedent's death) of the qualified interest, and (II) the actuarial value (as so determined) of the reformable interest does not exceed 5 percent of the actuarial value (as so determined) of the reformable interest,

(ii) in the case of (I) a charitable remainder interest, the nonremainder interest (before and after the qualified reformation) terminated at the same time, or, (II) any

other interest, the reformable interest and the qualified interest are for the same period, and

(iii) the change is effective as of the date of the decedent's death.

Section 2055(e)(3)(C)(i) defines the term "reformable interest" to mean any interest for which the deduction would be allowable under § 2055(a) at the time of the decedent's death but for § 2055(e)(2).

Section 2055(e)(3)(C)(ii) provides that generally the term "reformable interest" does not include any interest unless, before the remainder vests in possession, all payments to persons other than an organization described in § 2055(a) are expressed either in specified dollar amounts or a fixed percentage of the fair market value of the property.

Section 2055(e)(3)(C)(iii) provides, in part, that § 2055(e)(3)(C)(ii) does not apply to any interest if not later than 90 days after the last date (including extensions) for filing an estate tax return, if an estate tax return is required to be filed, a judicial proceeding is commenced to change the interest into a qualified interest.

Section 2055(e)(3)(D) defines the term "qualified interest" to mean an interest for which a deduction is allowable under § 2055(a).

Rev. Proc. 90-30, 1990-1 C.B. 534, provides that trusts containing language that substantially follows one of the sample forms of trust contained in that Revenue Procedure will be recognized by the Service as meeting all of the requirements of a charitable remainder unitrust, provided that the trust operates in a manner consistent with the terms of the instrument creating the trust and provided it is a valid trust under local law.

Based on the information submitted and the representations made, we conclude that the interests passing to Charitable Trust under the trusts created under Article THIRD of Decedent's will are reformable interests within the meaning of § 2055(e)(3)(C)(i) because an estate tax deduction for the value of the remainder interest would have been allowable under § 2055(a) but for the provisions of § 2055(e).

The reformation of the trusts will be effective as of the date of the Decedent's death, and the nonremainder interests will terminate at the same time before and after the reformation. The actuarial value of the charitable remainder interest in the trusts before and after the reformation did not change. Thus, the difference between the actuarial value of the qualified interest and the actuarial value of the reformable interest does not exceed 5 percent of the actuarial value of the reformable interest.

Reformed trusts contain the provisions set forth in Rev. Rul. 72-395, 1972-2 C.B.

340, as modified by Rev. Rul. 80-123, 1980-1 C.B. 205, and Rev. Rul. 82-128, 1982-2 C.B. 71, and clarified by Rev. Rul. 82-165, 1982-2 C.B. 117. The reformed trusts also follow the sample language in Rev. Proc. 90-30, 1990-1 C.B. 534. We conclude that the reformation of the trusts is a qualified reformation for purposes of § 2055(e)(3), and the reformed trusts meet the requirements of a charitable remainder unitrust as described in § 664(d)(2). Accordingly, the present value of the remainder interest in the reformed trusts will be allowed as an estate tax deduction under § 2055(a).

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

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,

Christine E. Ellison, Chief
Branch 7
Office of the Assistant Chief Counsel
(Passthroughs & Special Industries)

cc: § 6110 purposes