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Department of the Treasury
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Person To Contact:
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CC:ITA:B01
PLR-111449-12

Date:
September 07, 2012

In re: Letter Ruling Request Regarding Charitable Contribution

Legend

Donor =
Trust =
Charity =
Spouse =
State =
D1 =
D2 =
x =
y =

Dear :

This responds to your letter dated October 19, 2011, requesting rulings on behalf of yourself and Trust (Taxpayers). Taxpayers request rulings on the income and gift tax consequences under §§ 170 2522 and 664 of the Internal Revenue Code of a contribution to a charitable remainder beneficiary of Trust of an undivided x interest in Donor's right to unitrust payments.

RULINGS REQUESTED

- (1) Donor will be entitled to a charitable contribution deduction for income tax purposes under § 170(a)(1) for the contribution of an undivided interest in a unitrust payment transferred to Charity.

- (2) The amount of Donor's charitable contribution deduction will be equal to the present value of the right to receive annual payments equal to y percent of the net fair market value of x of the Trust assets, determined annually, for a term starting on the date of the contribution to Charity and ending on the date of death of Donor.
- (3) Donor will be entitled to a gift tax charitable contribution deduction under § 2522 for the fair market value of his gift (for gift tax purposes) of x of the corpus of Trust, not in trust.
- (4) The transfer of the undivided x interest in the unitrust payment will not cause the trust to cease to be a trust described in § 664(d)(2)
- (5) To the extent that in prior years the Trust realized capital gain income, and that income was not included in the income of Donor, such capital gain shall not be included in the income of Donor solely because of his transfer of the undivided interest in the unitrust payment to Charity.

FACTS

On D1, Donor and Spouse, as settlors, created Trust, a charitable remainder unitrust pursuant to § 664(d)(2). Trust is governed by the law of State, and all property placed into Trust at the outset was community property.

Trust provides for an annual payment to Donor and Spouse of a unitrust amount equal to y percent of the net fair market value of the assets of Trust, valued as of the first day of each taxable year of Trust (Unitrust Payment). Upon the death of either Donor or Spouse, the survivor is entitled to the entire Unitrust Payment. Neither Donor nor Spouse retained a right to revoke the respective survivorship interest transferred at the time the trust was created.

Trust also provides that on the death of the last to die of Donor and Spouse, the trustee of Trust is to distribute all of the principal and income of Trust (the Remainder) to Charity, an organization that meets the requirements of § 170(c) and § 2522(a). However, Donor and Spouse retained the right to add or delete, by inter vivos or testamentary written instrument, qualified exempt charities to receive the Remainder.

On D2, Spouse died, leaving Donor as the sole trustee of Trust and the sole beneficiary of the Unitrust Payment. As the surviving settlor of Trust, Donor has the right to add or delete, by inter vivos or testamentary written instrument, qualified exempt charities to receive the Remainder.

Donor's Proposed Transaction:

Donor proposes to contribute an undivided x interest in the Unitrust Payment to Charity and to irrevocably designate Charity as the beneficiary of an undivided x interest in the

Remainder. Donor will not receive any consideration from Charity for the contribution and designation. Donor and Charity will then consent to a partial termination of Trust in their respective capacities as settlor and beneficiary. Thereafter, Donor, as trustee, will distribute to Charity $\frac{x}{y}$ of Trust's corpus, not in trust, and continue to hold the balance of Trust's corpus in accordance with the terms of Trust.

Donor represents that (1) the $\frac{x}{y}$ interest in the Unitrust Payment and the $\frac{x}{y}$ interest in the Remainder that Charity receives will merge pursuant to State law, leaving Charity with an undivided $\frac{x}{y}$ interest in the corpus of Trust; and (2) the basis of the assets distributed to Charity in the partial liquidation of Trust will be fairly representative of the adjusted basis of the property available for payment on the date of payment.

LAW AND ANALYSIS

Ruling Request 1:

Section 170(a)(1) provides that there shall be allowed as a deduction any charitable contribution (as defined in § 170(c)) payment of which is made within the taxable year.

Section 170(f)(3)(A) provides that a contribution (not made by a transfer in trust) of less than the taxpayer's entire interest in property is not allowed as a charitable contribution deduction except to the extent such contribution would have been allowed as a deduction had it been transferred in trust.

Section 170(f)(3)(B)(ii) provides that § 170(f)(3)(A) does not apply to a contribution of an undivided portion of the taxpayer's entire interest in property.

Sections 1.170A-6(a)(2) and 1.170A-7(a)(2)(i) of the Income Tax Regulations provide that a deduction is allowed for a contribution of a partial interest in property if such interest is the taxpayer's entire interest in the property, such as an income interest or a remainder interest. If, however, the property in which such partial interest exists was divided in order to create such interest and thus to avoid § 170(f)(3)(A) the deduction will not be allowed.

Section 1.170A-7(b)(1) provides that an undivided portion of a taxpayer's entire interest in property must consist of a fraction or percentage of each and every substantial interest or right owned by the taxpayer in the property and must extend over the entire term of the taxpayer's interest in the property.

In Rev. Rul. 86-60 1986-1 C.B. 302, the Service considered whether donations of an annuity interest in a charitable remainder annuity trust (CRAT) to the remainder beneficiary of the CRAT qualify for charitable contribution deductions under §§ 170 and 2522. In Situation 1 of that ruling, Grantor A created a CRAT described in § 664(d)(1), and retained the annuity interest for life. The remainder beneficiary was a charitable organization described in §§ 170(c) and 2522. Four years later, A transferred the

annuity interest in the CRAT to the remainder beneficiary. Rev. Rul. 86-60 concludes, *inter alia*, based partly on § 1.170A-7(a)(2)(i) that the gift to the charity of A's annuity interest in the CRAT qualifies for a charitable contribution deduction under § 170.

The present case is analogous to the situation in Rev. Rul. 86-60. Donor and Spouse retained an income interest in Trust. Donor, the surviving settlor of Trust, proposes to transfer a portion of his interest in the Unitrust Payment to Charity, the remainder beneficiary of Trust. Based solely on the facts submitted and representations made, including the representation that under State law Donor's undivided x interest in the Unitrust Payment transferred to Charity merges with x of Charity's remainder interest, we conclude that Donor's transfer of an undivided portion of the unitrust interest will qualify for a charitable contribution deduction under § 170.

Ruling Request 2:

Section 1.170A-7(c) provides, in part, that the amount of the deduction under § 170 in the case of a charitable contribution (not in trust) of a partial interest in property to which § 1.170A-7(b) applies is the fair market value of the partial interest at the time of the contribution. See § 1.170A-1(c). Section 1.170A-7(b)(1) pertains to a gift of an undivided portion of a donor's entire interest. Section 1.170A-7(c) further provides that the fair market value of such a partial interest must be determined in accordance with § 20.2031-7 of the Estate Tax Regulations. The valuation methodology set forth under § 20.2031-7(d) is the same methodology described under § 664 for valuing unitrust interests for income tax purposes.

Accordingly, the amount of Donor's charitable contribution deduction will be equal to the present value of the right to receive annual payments equal to y percent of the net fair market value of x of the assets of Trust.

In order to compute the actuarial factor necessary to determine the value of Donor's contribution of an x undivided unitrust interest, IRS Publication 1458, *Actuarial Values Version 3B*, is required. The y percent payout factor is calculated for a single life using the age of Donor and the remainder factor contained in Table U(2). The actuarial factor so obtained, multiplied by x of the value of the unitrust corpus at the time of the transfer, will equal the value of the contribution for purposes of § 170.

Ruling Request 3:

Section 2501(a) imposes a tax for each calendar year on the transfer of property by gift during such calendar year by an individual.

Section 2511(a) provides that the gift tax applies to a transfer by gift 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 25.2511-2(b) of the Gift Tax Regulations provides that as to any property of which the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for his own benefit or for the benefit of another, the gift is complete.

Section 25.2511-2(c) provides that a gift is incomplete if and to the extent that a reserved power gives the donor the power to name new beneficiaries or to change the interests of the beneficiaries as between themselves unless the power is a fiduciary power limited by a fixed or ascertainable standard.

Section 2522(a) provides that, in computing taxable gifts for the calendar year, there is allowed as a deduction the amount of all gifts made during such year to or for the use of organizations described in § 2522(a)

Section 2522(c)(2) provides that where a donor transfers an interest in property (other than an interest described in § 170(f)(3)(B) i.e., a remainder interest in a farm or residence, or an undivided portion of the donor's entire interest) to or for a charity and an interest in the same property is retained by the donor, or is transferred or has been transferred (for less than adequate and full consideration in money or money's worth) from the donor to a person, or for a use, not described in § 2522(a) or (b), no deduction shall be allowed under § 2522 for the interest which is transferred unless, in the case of any interest other than a remainder interest, the interest is in the form of a guaranteed annuity or a fixed percentage distributed yearly of the annual fair market value of the property to be determined yearly (a unitrust interest).

Section 25.2522(c)-3(c)(1)(i) provides that if a donor transfers an interest in property for charitable purposes and an interest in the same property is retained by the donor, or is transferred or has been transferred (for less than adequate and full consideration in money's or money's worth) for private purposes, no deduction is allowed under § 2522 unless the charitable interest is a deductible interest as described in § 25.2522(c)-3(c)(2).

Section 25.2522(c)-3(c)(2) provides, in relevant part, that a deductible interest for purposes of § 25.2522(c)-3(c)(2)(i) includes a charitable interest in property where the charitable interest is an undivided portion, not in trust, of the donor's entire interest in property.

In this case, on D1, Donor and Spouse created Trust and contributed to it certain property that became the corpus of Trust. Under the terms of Trust, Donor and Spouse retained the right to add or delete the charitable remainder beneficiaries. Accordingly, Donor and Spouse did not make a completed gift of a remainder interest in the corpus of Trust for gift tax purposes. See § 25.2511-2(c). On the date of Spouse's death, Donor became the sole owner of the corpus of Trust for gift tax purposes.

Donor proposes to terminate Trust as to $\frac{x}{x}$ of its corpus and to contribute $\frac{x}{x}$ of the corpus of Trust, not in trust, to Charity. To accomplish this, Donor will transfer an undivided $\frac{x}{x}$ interest in the Unitrust Payment to Charity. In addition, Donor will irrevocably designate Charity as the sole beneficiary of an undivided $\frac{x}{x}$ interest in Remainder. Thereafter, Donor, as Trustee, will transfer $\frac{x}{x}$ of the corpus of Trust, not in trust, to Charity.

Based solely on the facts submitted and representations made, and specifically because Charity will own a fee interest in $\frac{x}{x}$ of the corpus of Trust, not in trust, after Donor's transfers, we conclude that for gift tax purposes, Donor will make a gift of $\frac{x}{x}$ of the corpus of Trust, not in trust, and will be entitled to a gift tax charitable contribution deduction under § 2522(a) for the fair market value of its gift.

Ruling Request 4:

Section 1.664-3(a)(4) provides that the governing instrument may provide that an amount other than the unitrust amount shall be paid (or may be paid in the discretion of the trustee) to an organization described in § 170(c) provided that, in the case of distributions in kind, the adjusted basis of the property distributed is fairly representative of the adjusted basis of the property available for the payment on the date of the payment.

The regulations thus authorized the current distribution of unitrust assets to a charitable organization. In this case, it is represented that under local law, upon Donor's transfer of an undivided $\frac{x}{x}$ portion of his Unitrust Payment to Charity and Donor's irrevocable designation of $\frac{x}{x}$ of the Remainder to Charity, the Charity's interest in the Unitrust Payment and the Remainder will merge. Although a partial termination of Trust will occur, Trust will continue to be in the form of, and will function as, a CRUT within the meaning of § 664(d)(2).

Accordingly, based solely on the facts submitted and representations made, we conclude that the transfer of the undivided $\frac{x}{x}$ interest in the Unitrust Payment will not cause Trust to cease to be a trust described in § 664(d)(2).

Ruling Request 5:

We conclude based solely on the facts and representations submitted that to the extent Trust realized capital gain income in prior years, which income was not included in the Unitrust Payments paid to Donor and thereby included in the income of Donor, that capital gain will not be currently included in Donor's income by reason of his transfer of a portion of his Unitrust Payments to Charity.

CONCLUSIONS

- (1) Donor will be entitled to a charitable contribution deduction for income tax purposes under § 170(a)(1) for the contribution of the undivided interest in a unitrust payment transferred to Charity.
- (2) The amount of Donor's charitable contribution deduction will be equal to the present value of the right to receive annual payments equal to y percent of the net fair market value of x of the Trust assets, determined annually, for a term starting on the date of the contribution to Charity and ending on the date of death of Donor.
- (3) Donor will be entitled to a gift tax charitable contribution deduction under § 2522 for the fair market value of its gift (for gift tax purposes) of x of the corpus of Trust, not in trust.
- (4) The transfer of the undivided x interest in the unitrust payment will not cause the trust to cease to be a trust described in § 664(d)(2).
- (5) To the extent that in prior years the Trust realized capital gain income, and that income was not included in the income of Donor, such capital gain shall not be included in the income of Donor solely because of his transfer of the undivided interest in the unitrust payment to Charity.

The rulings contained in this letter are based upon information and representations submitted by Taxpayers 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 expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter, including whether Trust qualifies as a CRUT and whether requirements for merger will be satisfied under local law.

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

A copy of this ruling should be attached to Donor's federal income and gift tax returns for the tax years affected. Alternatively, taxpayers filing returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of this ruling.

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,

Karin Goldsmith Gross
Acting Branch Chief, Branch 1
(Income Tax & Accounting)