

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact: _____, ID No.

Telephone Number:

Refer Reply To:
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Date:
January 13, 2005

LEGEND:

Taxpayer =

Trust A =

Trust B =

Trustee A =

Trustee B =

Date 1 =

Date 2 =

Date 3 =

Dear _____ :

This is in response to your representative's letter dated December 15, 2003, and subsequent submissions, requesting a ruling on whether, as a result of Taxpayer's renunciation and subsequent resignation as co-trustee of Trust A and Trust B, the death benefits payable with respect to life insurance policies held by Trust A and Trust B are includible in Taxpayer's gross estate under Internal Revenue Code (Code) § 2035 or 2042.

Trust A and Trust B were not established by Taxpayer. Pursuant to the terms of each trust, Taxpayer is to receive the net income of each trust for her life. Upon her death, the principal of each trust is to be divided into equal shares for the benefit of Taxpayer's children. Taxpayer was a co-trustee of Trust A and Trust B, but on Date 1, she renounced all of her rights as co-trustee of Trust A and Trust B in connection with life insurance policies on her life. Life insurance policies on Taxpayer's life were purchased by Trusts A and B using trust corpus subsequent to Taxpayer's renunciation. Taxpayer resigned as co-trustee of Trust A and Trust B on Date 2 and Date 3, respectively. Trustee A and Trustee B are the current co-trustees of both trusts.

A ruling is requested that Taxpayer will not possess any incidents of ownership over the life insurance policies on her life held by the trustees of Trust A and Trust B and that the proceeds of the policies will not be includible in her gross estate under § 2035 or 2042(2) if she should die within three years of renouncing her rights as co-trustee in connection with the life insurance policies.

Section 2035(a) provides that if (1) the decedent made a transfer (by trust or otherwise) of an interest in any property, or relinquished a power with respect to any property, during the 3-year period ending on the date of the decedent's death, and (2) the value of such property (or an interest therein) would have been included in the decedent's gross estate under § 2036, 2037, 2038, or 2042 if such interest or relinquished power had been retained by the decedent on the date of his death, the value of the gross estate shall include the value of any property (or interest therein) which would have been so included.

Section 2042(2) provides that the value of the gross estate shall include the proceeds of all life insurance policies on the decedent's life receivable by beneficiaries other than the executor of the decedent's estate, to the extent that the decedent possessed at death any incidents of ownership exercisable either alone or in conjunction with any other person.

Section 20.2042-1(c)(2) of the Estate Tax Regulations provides that "incidents of ownership" is not limited in its meaning to ownership of a policy in the technical legal sense. Generally speaking, the term has reference to the right of the insured or his estate to the economic benefits of the policy. Thus, it includes the power to change the beneficiary, to surrender or cancel the policy, to assign the policy, to revoke an assignment, to pledge the policy for a loan, or to obtain from the insurer a loan against the surrender of the policy.

Under § 20.2042-1(c)(4), a decedent is considered to have an incident of ownership in an insurance policy on decedent's life held in trust if, under the terms of the policy, the decedent, either alone or in conjunction with another person or persons, has the power, as trustee or otherwise, to change the beneficial ownership of the policy

or its proceeds or the time or manner of enjoyment thereof, even though the decedent has no beneficial interest in the trust.

In Rev. Rul. 84-179, 1984-2 C.B. 195, the decedent purchased an insurance policy on his life and transferred all incidents of ownership to his spouse. His spouse designated their adult child as the policy beneficiary. The spouse died and her will established a residuary trust for the benefit of the child. The decedent was designated the trustee of this trust. The insurance policy on the decedent's life was transferred to the testamentary trust. As trustee, the decedent had broad discretionary powers in the management of the trust property and the power to distribute or accumulate income. Under the terms of the policy, the owner could elect to have the proceeds made payable according to various plans, use the loan value to pay the premiums, borrow on the policy, assign or pledge the policy, and elect to receive annual dividends. The will precluded the decedent from exercising these powers for the decedent's own benefit. The decedent paid the premiums on the policy out of other trust property and was still serving as trustee when he died.

Under the facts in Rev. Rul. 84-179, the decedent transferred the policy to his wife and subsequently, in an unrelated transaction, reacquired incidents of ownership over the policy in a fiduciary capacity. The ruling holds that under these circumstances, the decedent will not be considered to possess incidents of ownership in the policy for purposes of § 2042(2), provided the decedent did not furnish consideration for maintaining the policy and could not exercise the powers for the decedent's personal benefit. The ruling further provides that the result would be the same if the decedent acting as trustee purchased a policy as a trust asset. The ruling states, however, that were the decedent's powers over the policy could have been exercised for the decedent's benefit, they would constitute incidents of ownership in the policy without regard to how those powers were acquired and without consideration of whether or not the decedent was the source of the funds used to pay the premiums. See Estate of Fruehauf v. Commissioner, 427 F. 2d 80 (6th Cir. 1970).

In the present case, Taxpayer is the current income beneficiary of Trust A and Trust B. During her life, the trustees of Trust A and Trust B are to distribute all of the net income of each trust to Taxpayer. Upon Taxpayer's death, the trust is to be divided into equal shares for Taxpayer's issue. It has been represented that Taxpayer will not contribute assets to Trust A or Trust B, or maintain the life insurance policies held as assets of Trust A and Trust B with Taxpayer's personal assets.

Based on the foregoing, Taxpayer will not possess any incidents of ownership over the life insurance policies held as assets of Trust A and Trust B because Taxpayer renounced her rights as co-trustee of Trust A and Trust B in connection with the life insurance policies and ultimately resigned as co-trustee of the trusts. Therefore, we conclude that the proceeds of the life insurance policies held as assets of Trust A and Trust B will not be included in Taxpayer's gross estate under § 2042(2) or 2035,

provided the premiums for the policies are not paid from the income of Trust A or Trust B.

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

This ruling letter is directed only to the taxpayer who requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent.

In accordance with the power of attorney on file with this office, we are sending a copy of the letter to your authorized representatives.

Sincerely,

Melissa C. Liquerman

Melissa C. Liquerman
Branch Chief, Branch 9
(Passthroughs & Special Industries)

Enclosure

Copy for 6110 purposes

cc: