Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:04
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Date: SEPTEMBER 30, 2005

Legend:

Decedent =
Spouse =
Spouse's Trust =

Family Trust =
Marital Trust =
Descendants Trust =
X =
Company =
Year 1 =
Date 1 =
Date 2 =
Date 3 =
State =
State Court =
State Law 1 =
State Law 2 =

Dear :

This letter is in response to a letter dated March 10, 2005 and subsequent correspondence from your authorized representative requesting a ruling concerning the gift tax treatment of a proposed non-qualified disclaimer of the entire interest in a qualified terminable interest property (QTIP) trust.

The facts and representations submitted are summarized as follows:

Decedent and Spouse, residents of State, created Family Trust, a revocable inter vivos trust, in Year 1, and funded the trust with community property.

Decedent died on Date 1 survived by Spouse and eight children. Spouse and children are still living. Under the provisions of Family Trust, upon the death of Decedent, the trust is to be divided into two separate shares, the Decedent's Share and the Survivor's Share.

Under Section A of Article VI of Family Trust, one-half of all community property comprising part of the trust or added to the trust by reason of Decedent's death is to be allocated to each share. Decedent's interest in any property which was the Decedent's separate property passing to the trust by reason of Decedent's death is to be allocated to Decedent's Share. Survivor's Share is to be distributed to Spouse's Trust and administered in accordance with its provisions.

Section D-2(d) of Article VI of Family Trust provides that the residue of Decedent's Share is to be distributed to Marital Trust. Under Article VIII, the trustee is to pay the entire net income of Marital Trust to Spouse during Spouse's lifetime in quarterly or more frequent installments. The trustee is to pay Spouse the principal of Marital Trust if Spouse is in need of additional money for reasonable support. Spouse also has the right to occupy, without rental or accounting to the trustee, any home, apartment, or condominium in which Marital Trust has any interest and the right to direct the trustee to sell trust assets that produce little or no income and reinvest the proceeds in income-producing assets selected by the trustee.

Under Section D of Article VIII of Family Trust, after Spouse's death, the trustee is to pay any undistributed income of Marital Trust to Spouse's estate, and the balance of Marital Trust, after payment of taxes and a distribution of $X to Company, is to be distributed to Descendants Trust for the benefit of descendants of Decedent.

Decedent's United States Estate (and Generation-Skipping Transfer) Tax Return, Form 706, was filed on or before Date 3. The executors of Decedent's estate elected to treat Marital Trust as a qualified terminable interest property trust pursuant to § 2056(b)(7) of the Internal Revenue Code.

Spouse proposes to execute an irrevocable disclaimer of Spouse's entire interest in Marital Trust. The disclaimer will not be a qualified disclaimer under § 2518 and, thus, will be subject to federal gift tax.

State law provides that a beneficiary may disclaim an interest in a trust, and if the disclaimer is a valid disclaimer under State law, the trust will be distributed as if the disclaimant predeceased the person creating the trust. State Law 1. Under State law, a disclaimer made within nine months of the decedent's death is presumed to be a timely disclaimer and if the disclaimer is made more than nine months from the date of the decedent's death, the burden is on the disclaimant to demonstrate that the disclaimer was made within a reasonable time after the disclaimant acquired knowledge of the interest being disclaimed. State Law 2.

On Date 2, State Court issued an order that Spouse's disclaimer made within 30 days following the issuance of a favorable private letter ruling from the Internal Revenue Service will be a timely disclaimer under State law. The order also provides that pursuant to State law and Family Trust, as a result of such disclaimer, the assets of Marital Trust will pass to Spouse's issue by right of representation as provided in Marital Trust.

Spouse and Decedent's children have executed an agreement that, in the event Spouse executes the disclaimer and receives a private letter ruling from the Internal Revenue Service that the disclaimer will result in certain tax consequences, Decedent's children agree to pay all gift tax attributable to Spouse's transfer.

Spouse requests a ruling that Spouse's non-qualified disclaimer of his entire interest in Marital Trust will be treated as a disposition of Spouse's qualifying income interest for life under § 2519 of the fair market value of the entire property of Marital Trust less the amount of federal gift tax paid by the persons receiving the property.

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

Section 2056(a) provides that, for purposes of the tax imposed by § 2001, the value of the taxable estate is to be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes from the decedent to the surviving spouse.

Section 2056(b)(1) provides, in pertinent part, that no deduction shall be allowed under § 2056(a) 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, and on such termination, the property passes to a person other than the surviving spouse or the spouse's estate.

Section 2056(b)(7) provides an exception to the rule of § 2056(b)(1) in the case of qualified terminable interest property. Under § 2056(b)(7)(A), qualified terminable interest property is treated as passing to the surviving spouse for purposes of § 2056(a) and no part of the property is treated as passing to any person other than the surviving spouse for purposes of § 2056(b)(1).

Under § 2056(b)(7)(B)(i), the term "qualified terminable interest property" means property which 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)(B)(v) applies. Section 2056(b)(7)(B)(ii) provides that the surviving spouse has a qualifying income interest for life if the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, and no person has a power to appoint any part of the property to any person other than the surviving spouse during

the surviving spouse's life.

Section 2044(a) provides that the value of the gross estate shall include the value of any property in which the decedent had a qualifying income interest for life. Section 2044(b)(2) provides that § 2044(a) applies to any property if § 2519 did not apply with respect to a disposition by the decedent of part or all of such property.

Section 2501 imposes a tax for each calendar year on the transfer of property by gift by an individual, and § 2502(c) provides that the payment of the gift tax is the liability of the donor. Section 2511 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 exceeds the value of the consideration is deemed a gift.

Section 2518(a) provides, in part, that if a person makes a qualified disclaimer with respect to any interest in property, then subtitle B of the Code shall apply with respect to such interest as if the interest had never been transferred to such person. Section 2518(b)(2) provides, in part, that a disclaimer will not be treated as a qualified disclaimer unless it is made within nine months after the date on which the transfer creating the interest in such property is made.

Section 2519 provides that any disposition of all or a part of a qualifying income interest for life in property for which an election has been made under § 2056(b)(7), is treated as the transfer of all interests in the property other than the qualifying income interest.

Section 2207A(b) provides that if a gift tax is paid with respect to any person because of a transfer made by that person under § 2519, then that person shall be entitled to recover the tax attributable to the transfer from the person receiving the property.

Under § 25.2207A-1(a) of the Gift Tax Regulations, if an individual is treated as transferring an interest in property by reason of § 2519, the individual is entitled to recover from the "person receiving the property" (as defined in § 25.2207A-1(e)) the amount of gift tax attributable to that property. Under § 25.2207A-1(e), if the property is in trust at the time of the transfer, the "person receiving the property" is the trustee, and any person who has received a distribution of the property prior to the expiration of the right of recovery if the property does not remain in trust.

Section 25.2519-1(c)(1) 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 qualified terminable interest 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 25.2519-1(c)(4) provides that the amount treated as a transfer under § 25.2519-1(c)(1) is further reduced by the amount the donee spouse is entitled to recover under § 2207A(b) (relating to the right to recover gift tax attributable to the remainder interest). The gift tax consequences of failing to exercise the right of recovery are determined separately under § 25.2207A-1(b).

Section 25.2511-2(a) provides that the gift tax is a primary and personal liability of the donor, is an excise upon his 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 or from the property itself.

Rev. Rul. 81-223, 1981-2 C.B. 189, holds that, in determining the amount of the gift, the gift 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. The donor's available unified credit must be used to reduce the tax liability that the donee has assumed to the extent the unified credit is available.

Rev. Rul. 80-111, 1980-1 C.B. 209, considers a situation where a state gift tax that was paid by the donee was, under state law, a liability of the donee to the extent of one-half of the tax. The ruling holds that the donee's payment of the one-half of the state gift tax that the donee was liable for did not constitute consideration for the transfer. The payment satisfied the donee's liability and did not in any way benefit the donor. Only the one-half of the gift tax that the donor was liable for but that was paid by the donee was consideration for the transfer and could be deducted from the value of the gift in determining the amount of the gift.

Although § 2502(c) provides that the tax on a 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 donees.

In the present case, Spouse's disclaimer is not a qualified disclaimer under § 2518. Accordingly, Spouse's disclaimer of his entire interest in Marital Trust is a disposition of his qualifying income interest in Marital Trust for purposes of § 2519. The amount of the gift made by Spouse under § 2519 is equal to the fair market value of the entire property subject to the qualifying income interest, determined at the date of the disposition, less the value of the qualifying income interest in the property on the date of the disposition, less the amount Spouse is entitled to recover under § 2207A(b). In addition, Spouse is treated as making a gift of the fair market value of his income interest in Marital Trust under § 2511. Under § 2512(b), the amount of the gift made by Spouse is equal to the fair market value of the income interest minus the amount of gift tax paid by the donees.

A copy of this letter should be attached to any gift, estate, or generation-skipping transfer tax returns that you may file relating to these matters.

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. In addition, we express or imply no opinion regarding the value of the property in Marital Trust.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer 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 ruling, it is subject to verification on examination.

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

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

Sincerely,

Lorraine E. Gardner
Senior Counsel, Branch 4
(Passthroughs & Special Industries)

Enclosures
Copy for section 6110 purposes
Copy of this letter

cc:

cc: