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Department of the Treasury

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Refer Reply To:
CC:DOM:P&SI:4 - PLR-109360-98
Date: February 8, 1999

Re:

LEGEND:

Decedent =
Spouse =
Trust =
Bank =
Country =
City =
\$x =
State =
County =
Date =

This is in response to your letter dated April 6, 1998, in which you requested a ruling concerning the application of § 2056A of the Internal Revenue Code.

Decedent died testate on Date. Decedent was a naturalized United States citizen. Decedent was married to Spouse, a citizen of Country.

Decedent's will was executed under the laws of Country in 1983. Under the terms of Decedent's will, all of Decedent's property passed outright to Spouse. At the time of his death, Decedent owned a commercial building (Building) located in City in Country. Building currently has two commercial tenants.

Because Spouse is not a United States citizen, in order for Decedent's estate to qualify for the estate tax marital

deduction, property passing from Decedent to Spouse must be placed in a qualified domestic trust (QDOT).

It is represented that the law of Country does not recognize a common law trust, such as a QDOT, as the owner of real property. As a result, Spouse proposes to transfer Building to a corporation (Corporation) formed under the applicable laws of Country. In exchange for the transfer of Building to Corporation, Spouse will receive one share of stock representing 100 percent ownership in Corporation. Upon receipt of the share, Spouse proposes to transfer 94.9 percent of her interest in Corporation to a QDOT (Trust) that Spouse will establish with Bank, as the United States Trustee.

Upon making the transfer of the 94.9 percent interest in Corporation to Trust, Spouse intends to appoint herself as co-trustee of Trust, along with Bank. As co-trustee, Spouse and Bank will be authorized to make decisions regarding the administration of Trust.

The pertinent terms of the QDOT that Spouse proposes to establish are as follows:

Article Two, Section 3, provides that at least one of the trustees of the Trust acting at any time when all or a portion of the Trust is being treated as a qualified domestic trust, within the meaning of section 2056A, must be a U.S. Trustee as defined in § 20.2056A-2(c). If at any time there is no U.S. Trustee of the Trust, Spouse shall by written instrument appoint as a trustee an individual or a corporation that qualifies as a U.S. Trustee under § 20.2056A-2(c).

Under Article Two, Section 5(a) and (b), the trustee shall comply with all regulations promulgated under section 2056A including the security arrangements set forth in § 20.2056A-2(d)(1)(i) with respect to QDOTs in excess of \$2 million on the date of the decedent's death (determined without reduction for any indebtedness) and § 20.2056A-2(d)(1)(ii) with respect to QDOTs having a fair market value at the date of the decedent's death of \$2 million or less (determined without reduction for any indebtedness).

Under Article Two, Section 5(e), the trustee is directed to file any annual statements required under § 20.2056A-2(d)(3).

Article Two, Section 6 provides that the Trust is intended to be a qualified domestic trust under section 2056A. The U.S. Trustee shall have the power and is directed to modify any provision of the Trust Agreement in order that the Trust shall be a qualified domestic trust under section 2056A and in order that

transfers to the Trust will qualify for the federal estate tax marital deduction.

Article Two, Section 7 provides that in the case of any taxable event as defined in section 2056A(b)(9), the U.S. Trustee shall have a right to withhold, pay, or make provision for the payment from each distribution, allocation, or payment from the Trust (other than distributions, allocations, or payments from income) including without limitation distributions, allocations, or payments during the lifetime of Spouse or upon the death of Spouse. The U.S. Trustee shall also have the discretionary right to sell trust assets, or take other actions, to ensure the payment of federal estate tax imposed under section 2056A.

Article Three, Section 1 provides that, to the extent that the trustee holds any income-producing property, the trustee is to pay Spouse the net income of the Trust in convenient installments, at least quarterly, during her lifetime.

Article Three, Section 2 provides that the trustee is to distribute to Spouse such amounts of principal from the Trust as Spouse directs in writing. Section 3 provides that any distribution of principal or income may be made only after taking steps to set aside sufficient cash or properties to satisfy the federal estate tax imposed by section 2056A.

Under Article Four, upon the death of Spouse, after payment of the Trust's share of the federal estate tax imposed by section 2056A by reason of the death of Spouse, the balance of the Trust estate is to pass in separate shares of equal value to charities to be designated by Spouse, providing that each such charity is an organization described in section 2055(a).

Article Five, Section 1 provides that decisions concerning the management, administration, investment, or distribution of the Trust Estate are to be made by a majority vote of the trustees if there is more than one Trustee then acting. Any provision of the Trust notwithstanding, no decision of the trustees may abrogate or curtail the rights granted to, or the duties imposed upon, the U.S. Trustee under Article Two.

Under Article Six, the trustee is to maintain the records of Trust activities and carry out its duties required under Trust and by applicable law within the geographical boundaries of County in State. The internal laws of State are to govern the administration of Trust and the validity and interpretation of the provisions of Trust. Any action to enforce or construe the provisions of Trust or to determine any issue regarding the administration of Trust is to be brought in the Circuit Court of County, State or, in the event jurisdiction and venue lie

therein, in the United States District Court for the Northern District of State.

Under Article Seven, Section 1, subject to the provisions of Article Two, Spouse, unilaterally, as grantor and beneficiary, but not as fiduciary has the following powers: (1) to appoint one or more persons to serve as trustee of Trust; (2) to remove a trustee, provided that at all times there is at least one U.S. Trustee; (3) to amend or revoke the Trust in part or in whole; provided that no amendment or revocation shall affect the right and duty of the U.S. Trustee to pay or make provisions for the payment of any U.S. federal estate tax imposed under § 2056A.

Under Article Seven, Section 2, subject to the provisions of Article Two, Spouse as grantor and beneficiary but not as fiduciary, may veto any one or more of the following decisions: (1) to alter or change any investment of Trust comprising more than ten percent of the value of the Trust property; (2) to compromise, arbitrate, or abandon claims of the Trust; and (3) to sue on behalf of the Trust or defend suits against the Trust, except that Spouse may not veto a decision to defend a suit that is brought by Spouse or her legal representatives.

The rulings requested are as follows:

1. The Trust will qualify as a QDOT defined in § 2056A(a), provided Spouse makes a timely election under § 2056A(a)(3).

2. For purposes of § 20.2056A-4(b)(3), the interest in Corporation received by Spouse in exchange for her transfer of Building to Corporation will constitute proceeds from the exchange of property passing from Decedent to Spouse.

3. Provided the QDOT election is made, Decedent's estate will be entitled to a marital deduction equal to the fair market value of the 94.9 percent interest in Corporation transferred to Trust determined based on the fair market value of the Building as of the date of Decedent's death.

4. Classification of Trust as a foreign trust within the meaning of § 7701(a)(31)(B) will not affect the qualification of Trust as a QDOT under § 2056A.

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

Under § 2056(a), for purposes of the tax imposed by § 2001, the value of the taxable estate is determined, except as limited by § 2056(b), by deducting from the value of the gross estate an amount equal to the value of any interest in property which

passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Under § 2056(d)(1) and (d)(2)(A), if the surviving spouse of a decedent is not a United States citizen, the marital deduction is disallowed unless property passes to the surviving spouse in a qualified domestic trust (QDOT).

Under § 2056A(a) a QDOT is a trust if (1) the trust instrument- (A) requires that at least one trustee of the trust be an individual citizen of the United States or a domestic corporation, and (B) provides that no distribution (other than a distribution of income) may be made from the trust unless a trustee who is an individual citizen of the United States or domestic corporation has the right to withhold from such distribution the tax imposed under § 2056A(b) on the distribution, (2) such trust meets such requirements as the Secretary may by regulations prescribe to ensure the collection of any tax imposed by § 2056A(b), and (3) an election under § 2056A is made with respect to the trust.

Under § 2056(d)(2)(B) and § 20.2056A-4(b)(1) of the Estate Tax Regulations, if an interest in property passes outright from a decedent to a noncitizen surviving spouse either by testamentary bequest or devise, and such property interest otherwise qualifies for a marital deduction except that it does not pass in a QDOT, solely for purposes of § 2056(d)(2)(A), the property is treated as passing to the surviving spouse in a QDOT if the property interest is either actually transferred to a QDOT before the date the estate tax return is filed and on or before the last date prescribed by law that the QDOT election may be made, or is assigned to a QDOT under an enforceable and irrevocable written assignment made on or before the last date prescribed by law that the QDOT election may be made.

Under § 20.2056A-4(b)(3), if a transfer or assignment is of a specific asset or group of assets, only assets included in the decedent's gross estate and passing from the decedent to the spouse (or the proceeds from the sale, exchange or conversion of such assets) may be transferred or assigned to the QDOT.

Section 7701(a)(31)(B) provides that the term "foreign trust" means any trust other than a trust described in § 7701(a)(30)(E). Section 7701(a)(30)(E) describes a trust with the following attributes: (i) a court within the United States is able to exercise primary supervision over the administration of the trust; and (ii) one or more United States persons have the authority to control all substantial decisions of the trust.

Ruling #1. Trust incorporates the sample paragraphs provided in Rev. Proc. 96-54, 1996-2 C.B. 386, that may be used to satisfy the governing instrument requirements of §§ 20.2056A-2(d)(1)(i) and (d)(1)(ii) of the Estate Tax Regulations for a qualified domestic trust described in § 2056A(a). We conclude that Trust will qualify as a QDOT defined in § 2056A(a), provided a timely election is made under § 2056A(a)(3) and § 2056(d).

Ruling #2. Spouse proposes to transfer Building to Corporation, formed under the applicable laws of Country. In exchange for the transfer of Building to Corporation, Spouse will receive one share of stock representing 100 percent ownership in Corporation. Upon receipt of the share, Spouse proposes to transfer 94.9 percent of her interest in Corporation to Trust. Under § 20.2056A-4(b)(3), a spouse may transfer or assign to a QDOT only assets that are included in the decedent's gross estate that pass from the decedent to the spouse; or the proceeds from the sale, exchange or conversion of such assets. We conclude that the interest in Corporation that Spouse will receive in exchange for her transfer of Building to Corporation will constitute proceeds from the exchange of property passing from Decedent to Spouse within the meaning of § 20.2056A-4(b)(3), such that the interest in Corporation may be transferred or assigned to Trust for purposes of § 2056A.

Ruling #3. Upon transfer of 94.9 percent of Spouse's 100 percent stock ownership interest in Corporation, provided the QDOT election is timely made under § 2056A(a)(3) and § 2056(d), Decedent's estate will be entitled to a marital deduction equal to the fair market value of the 94.9 percent interest in Corporation transferred to Trust. The fair market value of the 94.9 percent interest in Corporation is to be determined based on the fair market value of Building on the date of Decedent's death. For this purpose, any additional assets spouse transfers to Corporation that were not includible in Decedent's gross estate and did not pass from Decedent to Spouse, will not be taken into account.

Ruling # 4. If Trust is classified as a foreign trust within the meaning of § 7701(a)(31)(B), such classification will not cause Trust to fail to qualify as a QDOT under § 2056A(a), § 20.2055A-2, or Rev. Proc. 96-54, 1996- C.B. 386.

Except as we have specifically ruled herein, we express no opinion as to the consequences of this transaction under the cited provisions or under any other provisions of the Code.

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

A copy of this letter should be attached to the Decedent's estate tax return when it is filed. A copy is enclosed for that purpose.

Sincerely yours,

Assistant Chief Counsel
(Passthroughs and Special
Industries)

By _____
George Masnik
Chief, Branch 4

Enclosures

Copy for section 6110 purpose
Copy of letter

Initiator

Reviewer

Reviewer

Reviewer