

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:B04-PLR-120747-01
Date:

January 07, 2002

In Re:

LEGEND:

Decedent =

A =

B =

Date 1 =

Partnership =

State =

Corporation =

Partnership Agreement =

X =

Y =

Z =

Dear :

This is in reply to your letter of April 5, 2001, requesting a ruling on the estate tax treatment of the proceeds of an insurance policy held by a general partnership on the life of Decedent, a one-third partner.

FACTS

Decedent died on Date 1. At the time of his death, Decedent was a one-third partner in Partnership, a general partnership formed under the laws of State. A, Decedent's brother, and B, an individual unrelated to Decedent, were also one-third partners. Decedent was also a majority shareholder in Corporation, a closely held corporation involved in retail sales. At the time of Decedent's death, Corporation's ESOP and A were the other shareholders of Corporation. Partnership owned the premises where Corporation's retail stores were located, and leased the premises to

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Corporation.

Section 16 of the partnership agreement (“Partnership Agreement”) governing the operation of Partnership contained provisions applicable in the event of the death of a partner. Under section 16B, upon a partner’s death, Partnership was required to buy, and the deceased partner’s estate was required to sell, the decedent’s interest in Partnership. The amount to be paid for a deceased partner’s interest was to be determined periodically by mutual agreement of the partners. The Partnership Agreement specifies that the initial purchase price for a partner’s interest is \$X.

Under section 16B of the Partnership Agreement, Partnership is required to maintain life insurance policies on all the partners, in order to fund the purchase of a deceased partner’s interest. Partnership is required to be designated as beneficiary of the policies and to pay all the premiums. Further, Partnership is prohibited from modifying or impairing any of the rights or values under the policies. Partnership has the right to take out additional insurance on the life of any partner as may be required to carry out its obligations under the Partnership Agreement. Upon withdrawal from the Partnership, a withdrawing partner has the option to purchase the policy for its surrender value.

In accordance with the Partnership Agreement, Partnership maintained two policies insuring Decedent’s life, one in the amount of \$X, and one in the amount of \$Y.

On Decedent’s death, the insurance proceeds were paid to Partnership and Section 16 of the Partnership Agreement became operative. Although, pursuant to the Partnership Agreement, the partners were to determine the purchase price of each partner’s interest periodically, the initial \$X purchase price specified in the Partnership Agreement was never adjusted. After Decedent’s death, in the same negotiated settlement, Decedent’s estate sold Decedent’s Partnership interest to Partnership and Decedent’s interest in Corporation to Corporation for a total of \$Z. The Assignment and Release agreements covering both sales did not allocate any specific value between the sale price of the Partnership interest and the sale price of the Corporation stock. The estate represents that the amount paid for Decedent’s Partnership interest equated with the amount of Decedent’s capital account as of the preceding year and Decedent’s share of Partnership income from the beginning of that year until the date of his death and that the capital account (and the amount received) did not reflect any portion of the life insurance proceeds paid to Partnership.

LAW AND ANALYSIS

Under section 2042(1) of the Internal Revenue Code, the gross estate includes that value of the proceeds of any life insurance policy insuring the life of the decedent to the extent the proceeds are receivable by decedent’s executor. Under section 2042(2), the gross estate includes the value of the proceeds of any life insurance policy insuring the life of the decedent that are payable to a beneficiary other than the decedent’s executor, provided the decedent possessed at death any of the “incidents of

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ownership” with respect to the policy exercisable either alone or in conjunction with any other person. Section 20.2042-1(c)(2) provides that the term “incidents of ownership” is not limited to ownership of a policy in a technical sense, but includes generally the right of the insured to control the economic benefits of the policy, such as the power to change the beneficiary or cancel the policy.

The question of whether incidents of ownership held by a partnership with respect to a policy insuring a partner’s life should be attributed to the insured partner is considered in Rev. Rul. 83-147, 1983-2 C.B. 158. In that ruling, a general partnership owned a life insurance policy on the life of the decedent, a one-third partner, and made the premium payments in partial satisfaction of the decedent’s distributive share of partnership income. The decedent’s son was designated the sole beneficiary of the policy. The revenue ruling holds that for purposes of section 2042(2) of the Code, when a partnership owns a life insurance policy on a partner’s life and the proceeds are payable other than to or for the benefit of the partnership, the insured partner possesses incidents of ownership in the policy exercisable in conjunction with the other partners, such that the value of the proceeds is includible in the insured partner’s gross estate.

In this case, the assets of Partnership consisted primarily of real estate that was leased to Corporation and used in Corporation’s active retail business. The life insurance policies were maintained by Partnership and the proceeds were paid to Partnership as required under the terms of the Partnership Agreement. The policies facilitated the satisfaction of Partnership’s obligation to purchase the interest of a deceased partner, while avoiding liquidation of the real property that was essential to the operation of Corporation’s retail business. The other partners in the Partnership were Decedent’s brother and an unrelated third party. We conclude that, under the facts presented, the proceeds of the life insurance policies held by Partnership on Decedent’s life were payable to or for the benefit of the Partnership. Accordingly, under Rev. Rul. 83-147, the proceeds of the life insurance policies held by Partnership on Decedent’s life that were receivable by Partnership are not includible in Decedent’s gross estate under section 2042.

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.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. The rulings contained in this letter are 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 rulings, it is subject to verification on examination.

A copy of this letter must be attached to any income tax return to which it is relevant. In accordance with the Power of Attorney on file with this office, a copy of this

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letter is being sent to the taxpayer.

Sincerely,
George L. Masnik
Chief, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure

Copy for 6110 purposes