

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:4-PLR-158890-02
Date:
August 25, 2003

Re:

Legend:

Donor =

Trust =

Corporation =

Trust Company =

Foundation =

Cash =

Date 1 =

Date 2 =

Year =

State =

Dear :

This is in response to a letter dated October 21, 2002, and subsequent correspondence, in which you requested a ruling concerning the federal estate tax consequences of a proposed distribution from Trust to Foundation, as described below.

Facts

The facts are submitted and represented to be as follows: On Date 1, Donor established an inter vivos, irrevocable trust, Trust. On this same date, Donor funded Trust with shares of Corporation nonvoting common stock. Trust is governed by the laws of State and is an electing small business trust with respect to Corporation, an S corporation. The trustees of Trust are Trust Company and Donor's sibling. Under Trust, Donor has no power to remove or replace the trustees. Further, no more than half of the trustees of Trust possessing the power of discretionary distributions shall be a related or subordinate party, within the meaning of § 672(c) of the Internal Revenue Code, with respect to Donor. The trustees of Trust have the power to make discretionary distributions of income or principal to Donor's issue, if any, and if Donor has no issue, to the issue of Donor's siblings. In addition, the trustees of Trust have the power to make discretionary distributions of income or principal to charitable beneficiaries that consist only of corporations, associations and institutions that are described in §§ 170(c) and 501(c)(3).

Foundation was incorporated under the nonprofit corporation laws of State in Year. On Date 2, the Internal Revenue Service issued a determination letter that Foundation is a private foundation within the meaning of § 501(c)(3). Currently, the members of Foundation are Donor, Donor's sibling, and Trust Company. The members elect the directors of Foundation and may remove them at any time, with or without cause, by the affirmative vote of a majority of the members. Currently, Donor is the only director of Foundation.

The trustees of Trust propose to exercise their discretionary power to make a Cash distribution (the Gift) to Foundation. In conjunction with the distribution, Donor and Foundation will execute a gift instrument, subject to the following terms and conditions, which terms and conditions shall terminate upon the death of Donor.

1. The Foundation will create a special restricted fund (the Fund) within the Foundation to hold the Gift and any income thereafter earned thereon. Amounts in the Fund may be commingled for investment with other Foundation assets, provided income, gains, expenses, and losses are allocated properly to the sources of the investment and accounted for separately.
2. The Foundation will amend its Bylaws to provide and will continue to provide in the Bylaws and any subsequent restatement thereof that neither [Donor] nor any

related or subordinate party to Donor shall have a vote on decisions concerning whether and when to distribute amounts in the Fund, the amounts and recipients of such distributions, and the terms and conditions of such distributions. One or more other directors shall have sole power to make such determinations. [Donor] and related or subordinate parties to Donor who are directors may have the power to vote on matters relating to the management and investment of amounts in the Fund. For purposes of this paragraph, "related or subordinate parties" shall mean persons having any of the following relationships to Donor: Donor's spouse if spouse is living with Donor; Donor's father, mother, issue, brother or sister; an employee of Donor; a corporation or any employee of a corporation in which the stock holdings of Donor and Foundation are significant from the viewpoint of voting control; or a subordinate employee of a corporation in which Donor is an executive, with such relationships to be determined in a manner consistent with § 672(c).

3. [Donor], agrees, for the benefit of the Trust, to abstain from exercising any power she otherwise may have as a director to vote on any decision concerning whether and when to distribute amounts in the Fund, the amounts and recipients of such distributions, and the terms and conditions of such distributions. She does not, however, surrender any right or duty she may have as a director of the Foundation to petition a court of competent jurisdiction or an appropriate agency of the State to protest, or attempt to enjoin, a breach of trust by those who have the power to vote on distributions from the Fund.

Section 4.01 of Article IV of the proposed amendments to the Bylaws provides that all gifts, grants, or contributions received by Foundation from Trust, and all income earned thereon, are to be held in the Fund separately accounted for on the books of the Foundation. Amounts in the Fund may be commingled for investment with other assets of the Foundation, provided income, gains, expenses, and losses are properly allocated between the respective sources. All decisions concerning whether and when to distribute amounts in the Fund, the amounts and recipients of such distributions, and the terms and conditions of such distributions, are to be made by a special distribution committee (Special Distribution Committee) consisting of directors other than Donor and related or subordinate parties to Donor who shall be disqualified from voting on such questions. The Special Distribution Committee is to have at least two members. Donor and related or subordinate parties will be eligible to vote on matters, other than distributions, concerning the management and investment of the Fund, provided that they are not to be eligible to vote against the liquidation of investments in the event such liquidation is necessary to provide funds for a distribution. In the event that there are less than two directors serving on the Special Distribution Committee, the members promptly are to elect directors to fill such vacancy. For purposes of this Article, "related or subordinate parties" shall mean persons having any of the following relationships to Donor: Donor's spouse if spouse is living with Donor; Donor's father, mother, issue,

brother or sister; an employee of Donor; a corporation or any employee of a corporation in which the stock holdings of Donor and Foundation are significant from the viewpoint of voting control; or a subordinate employee of a corporation in which Donor is an executive, with such relationships to be determined in a manner consistent with § 672(c).

Trust and Donor request a ruling that the proposed Cash distribution from Trust to Foundation will not cause the corpus of Trust or of the amount so distributed or income on either to be included in the gross estate of Donor for federal estate tax purposes.

Discussion

Section 2033 provides for the inclusion in the gross estate of the value of any property in which the decedent had an interest at the time of decedent's death.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death, (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 2038(a)(1) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished during the 3-year period ending on the date of the decedent's death.

Rev. Rul. 72-552, 1972-2 C.B. 525, considers a situation where, at the decedent's death, 90% of a charitable corporation's assets had been transferred to the corporation by the decedent. The decedent was one of the organizing members of the corporation, one of its original directors, and its president. The corporation's bylaws authorized the decedent, as president, and in conjunction with the vice-president, to

direct the disposition of the corporation's funds for charitable purposes. Therefore, the revenue ruling concludes that the decedent, in his capacity as president, retained the right in conjunction with others, to designate the persons who shall possess or enjoy the property transferred to the corporation. Accordingly, the value of the property decedent transferred to the corporation is includible in the decedent's gross estate under § 2036.

The trustees of Trust propose to exercise their discretionary powers to make a Cash distribution (the Gift) to Foundation pursuant to a gift instrument that is conditioned on the Foundation's agreement to create a Fund to hold the Gift and any income earned on the Gift. To implement compliance with these conditions Foundation will amend its Bylaws to (a) provide that Donor and related or subordinate parties to Donor, as defined above, are disqualified from voting on decisions concerning distributions from the Fund, (b) establish a committee with the sole power to make decisions on the distributions from the Fund, (c) provide that the members of the committee shall be the directors other than Donor and related or subordinate parties to Donor, as defined above, and (d) provide that if the committee does not have at least two eligible members, the vacancy shall be filled promptly. Further, under the instrument, Donor will agree to abstain from exercising any power she may have as a director to vote on decisions concerning distributions from the Fund. Thus, Donor retains no interest or reversion in Trust and no right to alter, amend, or revoke Trust.

Accordingly, based on the facts submitted and the representations made, the proposed distribution from Trust to Foundation will not cause the corpus of Trust or of the amount so distributed or income on either to be included in the gross estate of Donor for federal estate tax purposes.

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 the ruling, it is subject to verification on examination.

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

The 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.

Sincerely yours,

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special
Industries)

Enclosure

Copy for section 6110 purposes

cc: