Internal Revenue Service

Number: **200109041**
Release Date: 3/2/2001
Index No.: 2511.18-00

Department of the Treasury

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Person to Contact:

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Refer Reply To:
CC:PSI:4 - PLR-110703-00
Date: December 04, 2000

Re:

Legend

Decedent =

Date 1 =

Spouse =

Daughter =

Decedent's Will =

Date 2 =

Daughter's Will =

Date 3 =

Taxpayer =

Son =

Court =

Date 4 =

State =

Date 5 =

Y =

Dear :

This is in response to a letter dated March 15, 2000, and subsequent correspondence, requesting a ruling regarding the federal gift tax consequences of a proposed disclaimer.

Facts

The facts submitted and representations made are as follows:

Decedent died testate on Date 1, survived by Daughter. Decedent's Spouse predeceased Decedent. Taxpayer is Decedent's nephew.

Under paragraph 5 of Decedent's Will, the residuary estate passed to a trust. The net income of the trust was to be paid at least semi-annually to Spouse for life, then to Daughter for life, and then to Daughter's children until the youngest reached age 21, at which time the trust would terminate. Paragraph 5(e) provides that, if Daughter predeceases Spouse without surviving children, the trust assets will be distributed as Daughter appoints in her will pursuant to a general power of appointment or, in default of that appointment, to Daughter's heirs at law. If Daughter predeceases Spouse with surviving children, then the trust assets will be divided among those children when the youngest reaches age 21. The will contains no direction regarding disposition of the residuary trust on Daughter's death, if Daughter dies after Spouse.

Daughter died on Date 2 without surviving children. Item IV of Daughter's Will states that Daughter exercises the power of appointment given her under Decedent's Will to appoint the trust established under Decedent's Will. Item IV provides for the payment from those trust assets of specified sums to specified individuals and charities, including $100,000 to Taxpayer. Item V of Daughter's Will provides that, to the extent there are insufficient funds to fund the gifts under Item IV, those gifts will be paid out of Daughter's residuary estate. The balance of the residuary estate is to pass to an inter vivos trust established by Daughter prior to her death for the benefit of several charities.

On Date 3, the attorney for the administrator of Daughter's estate notified Taxpayer by letter that under Item IV of Daughter's Will, Daughter exercised the power of appointment given her in paragraph 5 of Decedent's Will and appointed $100,000 to Taxpayer. However, the letter noted that there is a question whether Daughter possessed the power of appointment because Daughter did not predecease either of her parents and she died without issue. Before receiving this letter, taxpayer was unaware of the provisions of either Decedent's or Daughter's testamentary instruments.

Shortly after receiving this letter, Taxpayer engaged an attorney to advise him regarding his interests. Taxpayer's attorney takes a position that the trust property passes by intestacy. Specifically, Daughter died after Spouse without surviving children. Thus, the circumstances of Daughter's death did not meet the requirements of paragraph 5(e) of Decedent's Will providing for creation of the power, or of any other provision under paragraph 5 providing for the disposition of the remainder of the trust. Therefore, the remainder passes by intestacy, and under applicable state law, the

identity of Decedent's intestate heirs must be determined at Daughter's death. Thus, Taxpayer is entitled to one-third of the trust corpus, as an intestate heir of Decedent.

The charities and other parties with interests under Daughter's Will take the position that Decedent's will should be construed in a manner that would make Daughter's exercise of the power valid. Alternatively, they take the position that, if Daughter did not possess the power at death and the trust passes by intestacy, the intestate heirs should be determined as of Decedent's death. Thus, under state law, Daughter is Decedent's only intestate heir and, as such, the remainder of the trust became part of Daughter's estate and passes under Item V of Daughter's will.

The parties executed a settlement agreement pursuant to which a portion of the trust will be divided among Decedent's intestate heirs, determined as of Daughter's date of death. As an intestate heir, Taxpayer will receive one-third of this portion of the trust. The remaining portion of the trust will be distributed based on Daughter's exercise of the general power of appointment. Taxpayer will receive no funds from this portion of the trust. The agreement was approved by Court on Date 4.

On Date 5, Taxpayer disclaimed, under the law of State, a fractional portion of his intestate interest in the trust created under Decedent's Will. Taxpayer 's disclaimer reads, in part, as follows:

> Whereas, it is the intention of [Taxpayer] to disclaim an undivided portion of the property passing to him as an intestate heir of [Decedent]. The disclaimed portion is [Y%] of all interests in the property to which [Taxpayer] would be otherwise entitled as his intestate share of the trust under the Will of [Decedent].
>
> Now therefore, I, [Taxpayer], an intestate heir of the testamentary trust under the Will of [Decedent], hereby disclaim all of my interest to [Y%] of the property to which I am otherwise entitled.

We have been requested to rule that Taxpayer's disclaimer of all of his interest in Y% of the intestate share Taxpayer is entitled to receive from the trust created under Decedent's Will will not result in a taxable transfer for federal gift tax purposes.

Law

Federal Law

Section 2501(a)(1) imposes a tax, for each calendar year, on the transfer of property by gift by any individual, resident or nonresident.

Section 2511 provides that the tax imposed by section 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 25.2511-1(c)(1) provides that the gift tax also applies to gifts indirectly made. Thus, any transaction in which an interest in property is gratuitously passed or conferred upon another, regardless of the means or device employed, constitutes a gift subject to tax.

Section 25.2511-1(c)(2) provides that in the case of taxable transfers creating an interest in the person disclaiming made before January 1, 1977, where the law governing the administration of the decedent's estate gives a beneficiary, heir, or next-of-kin a right completely and unqualifiedly to refuse to accept ownership of property transferred from a decedent, a refusal to accept ownership does not constitute the making of a gift if the refusal is made within a reasonable time after knowledge of the existence of the transfer. The refusal must be unequivocal and effective under the local law. There can be no refusal of ownership of property after its acceptance. In the absence of facts to the contrary, if a person fails to refuse to accept a transfer to him of ownership of a decedent's property within a reasonable time after learning of the existence of the transfer, he will be presumed to have accepted the property. In any case where a refusal is purported to relate to only a part of the property, the determination of whether or not there has been a complete and unqualified refusal to accept ownership will depend on all of the facts and circumstances in each particular case, taking into account the recognition and effectiveness of such a purported refusal under local law.

Thus, for a disclaimer to be recognized for federal gift tax purposes, with respect to a property interest created in a pre-1977 transfer, it must be (1) recognized under local law, (2) made within a "reasonable time" after knowledge of the existence of the transfer, (3) made before the acceptance of the property transferred, and (4) unequivocal.

In Jewett v. Commissioner, 455 U.S. 305 (1982), the Supreme Court recognized that, under this regulation, an interest must be disclaimed within a reasonable time after obtaining knowledge of the transfer creating the interest to be disclaimed, rather than a reasonable time after the distribution or vesting of the interest. The requirement in the regulations that the disclaimer must be made within a "reasonable time" is a matter of federal, rather than local law. Id. at 316. Whether a period of time is reasonable under the regulations is dependent on the facts and circumstances presented. See, Jewett v. Commissioner, 70 T.C. 430, 438 (1978), aff'd., 455 U.S. 305 (1982).

With respect to property interests created after December 31, 1976, § 2518 and the regulations thereunder set forth the requirements that must be met for a disclaimer to be effective for federal estate and gift tax purposes. In order to constitute a qualified disclaimer, the disclaimant cannot accept the interest to be disclaimed or any of its benefits prior to the disclaimer.

Under § 25.2518-2(d)(1), acceptance is manifested by an affirmative act which is consistent with ownership of the interest in property. Acts indicative of acceptance include using the property or the interest in property; accepting income from the property; and directing others to act with respect to the property or interest in property. Merely taking delivery of an instrument of title, without more, does not constitute

acceptance. Further, a disclaimant is not considered to have accepted property merely because under applicable local law title to the property vests immediately in the disclaimant upon the death of a decedent.

Section 25.2518-3(b) provides that a disclaimer of an undivided portion of a separate interest in property which meets the other requirements of a qualified disclaimer under § 2518(b) and the corresponding regulations is a qualified disclaimer. An undivided portion of a disclaimant's separate interest in property must consist of a fraction or percentage of each and every substantial interest or right owned by the disclaimant in such property and must extend over the entire term of the disclaimant's interest in such property and in other property into which such property is converted.

Rev. Rul. 90-45, 1990-1 C.B. 175, addresses the application of § 2518 in two situations in which a surviving spouse, B, elects within 9 months of a decedent's death to take a statutory share of the decedent's estate and subsequently disclaims an undivided portion of the elected statutory share. The ruling states that the transfer creating B's elected statutory share occurred on the decedent's date of death, even though B was not entitled to the interest until B exercised the right of election. Accordingly, in order to constitute a qualified disclaimer, the disclaimer had to be made within 9 months after the decedent's death. Further, the ruling concludes that B's statutory share election merely perfected B's right to receive a portion of the estate. Therefore, although B's election to take a statutory share constitutes an affirmative act that vests title to the elective share in B, it is not an acceptance of the property or its benefits, for purposes of § 2518(a)(3).

State Law

Applicable State law provides that:

> A person to whom an interest in property would have devolved by whatever means, including a beneficiary under a will, an appointee under the exercise of a power of appointment, a person entitled to take by intestacy, a joint tenant with right of survivorship, a donee of an inter vivos transfer, a donee under a third-party beneficiary contract (including beneficiaries of life insurance and annuity policies and pension, profit-sharing and other employee benefit plans), and a person entitled to a disclaimed interest, may disclaim it in whole or in part by a written disclaimer which shall: (1) describe the interest disclaimed; (2) declare the disclaimer and extent thereof; and (3) be signed by the disclaimant. The right to disclaim shall exist notwithstanding any limitation on the interest in the nature of a spendthrift provision or similar restriction.

Under State law the disclaimer relates back for all purposes to the date of the death of the decedent. Further, unless the testator or donor has provided for another disposition, the disclaimer, for purposes of determining the rights of other parties, is

equivalent to the disclaimant's having died before the decedent in the case of a devolution by will or intestacy.

Finally, state law provides, as follows:

> A disclaimer may be made at any time before acceptance. An acceptance may be express or may be inferred from actions of the person entitled to receive an interest in property such as the following: (1) The taking of possession or accepting delivery of the property or interest. (2) A written waiver of the right to disclaim. (3) An assignment, conveyance, encumbrance, pledge or other transfer of the interest or a contract to do so. (4) A representation that the interest has been or will be accepted to a person who relies thereon to his detriment. (5) A sale of the interest under a judicial sale. To constitute a bar to a disclaimer, a prior acceptance must be affirmatively proved. The mere lapse of time, with or without knowledge of the interest on the part of the disclaimant, shall not constitute an acceptance.

Analysis

We believe that the interests to be received by the parties (both as to the nature of the interests and their economic value) under the settlement agreement are consistent with the relative merit of the claims asserted by the parties.

Further, we conclude that, consistent with the characterization in the settlement agreement, the interest in the trust assets is passing to Taxpayer in recognition of Taxpayer's rights as an intestate heir of Decedent. Taxpayer could only be entitled to such a large portion of the trust assets as an intestate heir of Decedent. On the other hand, if the trust assets passed under Daughter's will either pursuant to her exercise of the testamentary general power of appointment over the trust assets or because Daughter was deemed to be Decedent's intestate heir, Taxpayer would be entitled to receive only $100,000 of the trust assets. Accordingly, under these circumstances, the transfer creating Taxpayer's interest in the trust occurred on Decedent's death on Date 1. Accordingly, the effectiveness of Taxpayer's disclaimer is determined under the rules of § 25.2511-1(c)(2).

Further, as is the case in Rev. Rul. 90-45, Taxpayer's actions to establish his interest in a portion of the trust do not constitute an acceptance of his interest in the trust assets. In addition, Taxpayer's disclaimer meets the requirements of § 25.2518-3(b) for disclaimers of an undivided portion of a separate interest in property. Thus, in view of the form of the disclaimer, we believe that Taxpayer has not accepted any of the benefits of the disclaimed property in executing the disclaimer.

Finally, based on the facts presented and representations made, Taxpayer had no knowledge of his interest in the trust until Date 3. Therefore, based on the facts

presented, we conclude that Taxpayer's disclaimer was made within a reasonable time after Taxpayer obtained knowledge of the transfer creating the interest to be disclaimed, for purposes of § 25.2511-1(c)(2).

Accordingly, based on the facts submitted and representations made, we rule that, assuming Taxpayer's disclaimer is effective under local law, Taxpayer's disclaimer of all of his interest in Y% of the intestate share Taxpayer is entitled to receive from the trust created under Decedent's Will did not result in a taxable transfer for federal gift tax purposes.

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.

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

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

Enclosure
Copy for section 6110 purposes