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Department of the Treasury
Washington, DC 20224

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Person To Contact:
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Telephone Number:

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LEGEND:

Taxpayer	=
Daughter	=
Daughter's Spouse	=
Trust 1	=
Trust 2	=
Trust 3	=
Trust 4	=
Trust 5	=
Trust 6	=
Trust 7	=
Trust 8	=
Trust 9	=
Trust 10	=
Date 1	=

Date 2	=	
Date 3	=	
Date 4	=	
Attorney	=	
State 1	=	
State 2	=	
p	=	
m	=	
n	=	
State 1 Statute 1	=	
State 1 Statute 2	=	
State 1 Statute 3	=	
Case 1	=	
Case 2	=	
Case 3	=	
Case 4	=	

Dear :

This is in response to a letter dated June 23, 2008, and other correspondence, requesting rulings regarding the federal estate and gift tax consequences of the proposed reformation of certain trusts and of the proposed correction of certain deeds.

The facts submitted are as follows. On Date 1, Taxpayer executed nine substantially identical irrevocable trusts (Trusts 1-9) for her grandchildren and great grandchildren. On Date 2, Taxpayer executed Trust 10 for the benefit of another great grandchild. Trust 10 is substantially similar to the other nine trusts except as discussed below. Attorney drafted the 10 trusts (collectively referred to as "Trusts").

Section 3 of each trust provides that each beneficiary shall have the right for 30 days following the transfer of property to the trust to withdraw all of the property. If the beneficiary fails to exercise this right within 30 days, the withdrawal right expires. The withdrawal right is not cumulative. Taxpayer, as trustor, and the trustee shall provide 10 days written notice of the beneficiary's right to withdraw property each year, and the notice shall be delivered ten (10) days before the date the property is transferred.

Section 6(a) of each trust provides that the trusts will continue until the beneficiary reaches age 40 at which time the trustee is to distribute the remaining trust property outright to the beneficiary. If the beneficiary dies prior to complete distribution of the trust estate, then the trust estate will be distributed to the deceased beneficiary's lineal descendants, or, if there are no surviving lineal descendents of the deceased beneficiary, to Taxpayer's surviving lineal descendants in equal shares.

Sections 5 and 6(b through f) include provisions that are generally included in a "supplemental needs trust." These provisions give the trustee the absolute discretion to distribute income and/or principal for the beneficiary's supplemental needs so long as such allowances do not disqualify the beneficiary from any government assistance or similar assistance from a private source. These provisions provide that the trustee's exercise of discretion in determining when and if the beneficiary needs supplemental care is conclusive; that the property held in the trust is not for the beneficiary's primary support, and that the beneficiary has no entitlement to the income or principal of the trust, except as the trustee in the trustee's complete, unfettered discretion, elects to disburse.

Section 16 of each trust provides that the trust shall be construed and administered under the laws of State 1. Section 4 of each trust provides that the trust is irrevocable.

On Dates 2, 3, and 4, Taxpayer transferred certain interests in a parcel of real estate (Property) to Trusts 1, 2, and 3. Property is located in State 2. Prior to Date 2, Taxpayer owned an undivided <u>one-third interest</u> in Property, and Taxpayer's daughter (Daughter) and Daughter's Spouse each owned an undivided one-third interest in Property. On Date 2, Deed 1 transferred Taxpayer's "partial interest equal to <u>p</u>% per Grantee" in the <u>entire</u> Property to Daughter, Daughter's Spouse, Trust 1, Trust 2, and Trust 3. Deed 1 stated that: "Each Grantee's <u>p</u>% interest is to have a dollar value of no more than and no less than $10,000." On Date 3, Deed 2 transferred Taxpayer's "partial interest equal to <u>m</u>% per Grantee" in the <u>entire</u> Property to Daughter, Daughter's Spouse, Trust 1, Trust 2, and Trust 3. Each beneficiary of Trust 1, 2, and 3 received a letter notifying each beneficiary that an interest in Property equal to no more and no less than $10,0000 was transferred to each trust and each beneficiary had the right to withdraw the transferred Property from his or her trust. On Date 4, Deed 3 transferred Taxpayer's "partial interest equal to <u>n</u>% per Grantee" in Taxpayer's <u>remaining interest</u> in Property to a revocable trust created by Daughter and Daughter's Spouse, Trust 1, Trust 2, and Trust 3. Attorney prepared all of the deeds.

Daughter is the current trustee of each trust. The beneficiaries of Trusts 1 and 2 have reached age 40. To date, the assets in Trusts 1 and 2 have not been distributed.

Taxpayer intended that the transfers to Trusts would be completed gifts that would be excluded from her estate for federal estate tax purposes and that such completed gifts would be gifts of present interests that would qualify for the federal gift tax annual exclusion. Taxpayer also intended that all of the income from each trust would be distributed to the beneficiary at least annually and that principal would only be distributed from each trust for the beneficiary's support, if resources from other sources were unavailable. Finally, Taxpayer intended to transfer an undivided <u>p</u>% interest per grantee in Taxpayer's undivided <u>one-third interest</u> in Property with Deed 1; an undivided m% interest per grantee in Taxpayer's remaining interest in Property with Deed 2, and an undivided n% interest per grantee in Taxpayer's remaining interest in Property with Deed 3.

Upon review of some of the deeds transferred to Trusts, Daughter discovered the errors Attorney made in drafting the trusts and deeds. In an affidavit (Affidavit), Attorney states that: (i) he erroneously included language in sections 5, 6(b), 6(d), and 6(f) in the trusts; (ii) he did not discuss this language with Taxpayer; (iii) this language is typically included in trusts drafted to allow an elderly trust beneficiary to continue government provided assistance; (iv) Taxpayer did not direct him to include this language; (v) the language is inconsistent with Taxpayer's intent; and (vi) none of the beneficiaries of Trusts were elderly, or receiving, or likely to receive, any state assistance for support. Further, in the Affidavit, Attorney states that a title company refused to insure the ownership of Property due to defects in Deeds 1, 2, and 3, that were prepared by him.

To correct the scrivener's errors in Trusts, pursuant to State 1 Statute 1, Taxpayer, the beneficiaries, and contingent beneficiaries of Trusts, and Daughter, as trustee of Trusts, will execute two nonjudicial agreements: Agreement 1 for Trusts 1, 2, and 3, and Agreement 2 for Trusts 4, 5, 6, 7, 8, 9, and 10. The agreements will reform Trusts, effective as of the date Taxpayer executed each trust, as follows. Each trust will provide that: (1) all of the net income shall be distributed annually; (2) each beneficiary has the right to withdraw accumulated income from his or her trust upon thirty days written notice to the trustee; (3) all accumulated income will be distributed as soon as practicable after the agreements are executed; (4) require the trustee to distribute so much principal as the trustee reasonably determines is necessary for the beneficiary's support, after taking into consideration the beneficiary's income, sources of support and resources; and (5) sections 5(b), 6(b), 6(c), 6(d), and 6(f) are deleted from each trust instrument. In addition, Agreement 1 will also provide that Trusts 1 and 2 have terminated because each respective beneficiary has reached age 40. Pursuant to State 1 Statute 2, the executed agreements will be filed in the appropriate state court.

Correction deeds will be filed in State 2. As corrected, Deed 1 transfers an undivided p% per grantee in Taxpayer's undivided one-third interest in Property, as of Date 2; Deed 2 transfers an undivided m% per grantee in Taxpayer's remaining interest in Property, as of Date 3; and Deed 3 transfers an undivided n% per grantee in Taxpayer's remaining interest in Property, as of Date 4.

Taxpayer has requested the following rulings:

1. As a result of the correction deeds due to scrivener's errors, the transfers of interests in Property to Trusts 1, 2, and 3 resulted in completed gifts on the date the original deeds were executed, in the percentages described in the correction deeds.

2. As a result of the reformation of Trusts due to scrivener's errors, pursuant to State 1 law, and Agreements 1 and 2, Taxpayer's transfers to Trusts will be treated as completed gifts of present interests that qualify for the federal gift tax annual exclusion under § 2503(b).

3. As a result of the reformation of Trusts due to scrivener's errors, pursuant to State 1 law, and Agreements 1 and 2, the assets of Trusts will not be includible in Taxpayer's gross estate under §§ 2033, 2035, 2036, 2038, or 2041.

Ruling #1

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

Under § 2511(a), the tax imposed by § 2501 applies 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 25.2511-2(b) of the Gift Tax Regulations provides that a gift is complete to the extent the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for his own benefit or for the benefit of another.

Under § 25.2511-2(c), a gift is incomplete in every instance in which a donor reserves the power to revest the beneficial title to the property in himself. A gift is also incomplete if and to the extent that a reserved power gives the donor the power to name new beneficiaries or to change the interests of the beneficiaries as between themselves.

The Supreme Court of State 2, in Case 1, stated:

> The rule is well established that where a deed is drawn with the intent to carry out a prior agreement to convey property, but by mistake of the scrivener does not fulfill such intention, equity will correct such error by reforming the instrument to conform to the intention of the parties.

In Case 2, the Court of Appeals of State 2 stated:

> The doctrine of relation back permits a party to a conveyance of real property to correct an erroneous legal description in the original deed by filing a subsequent or "correction" deed; the correction then becomes effective as of the date of the original deed.

In this case, the facts support the conclusion that the original deeds do not reflect the true intent of the parties and that the errors were due to scrivener's errors.

Accordingly, under State 2 law, Taxpayer may file correction deeds. Therefore, based upon the facts submitted and the representations made, we conclude that, as a result of the correction deeds, the transfers of Property to Trusts 1, 2, and 3 are completed gifts for federal gift tax purposes as of the date of the execution of the original deeds; and the value of the gifts will be determined by using the percentages described in the correction deeds.

Ruling # 2

Section 2503(b)(1) provides that, in the case of gifts (other than gifts of future interests in property) made to any person by the donor during the calendar year, the first $10,000 (adjusted for inflation as provided in § 2503(b)(2)) of such gifts to such person shall not be included in the total amount of gifts made during such year. This annual exclusion is only available for gifts of present interests in property. Section 25.2503-3(b) provides that a present interest in property is an unrestricted right to the immediate use, possession or enjoyment of property or the income from property (such as a life estate or term certain). See Crummey v. Commissioner, 397 F.2d 82 (9th Cir. 1968); Rev Rul. 85-24, 1985-1 C.B. 329; Rev. Rul. 73-405, 1973-2 C.B. 321.

The Supreme Court of State 1, in Case 3, stated that:

> Where there has been an agreement actually entered into which the parties have attempted to put in writing, but have failed because of a mistake either of themselves or of the scrivener, the courts having jurisdiction in matters of equitable cognizance have power to reform the instrument in such manner as to make it express the true agreement; and this in any action or proceeding where a party to the agreement seeks to take advantage of the mistake.

In Case 4, the Court of Appeals of State 1, Division 3, stated that "A scrivener's error occurs when the intention of the parties is identical at the time of the transaction but the written agreement errs in expressing that intention."

In Commissioner v. Estate of Bosch, 387 U.S. 456 (1967), the Court considered whether a state trial court's characterization of property rights conclusively binds a federal court or agency in a federal estate tax controversy. The Court concluded that the decision of a state trial court as to an underlying issue of state law should not be controlling when applied to a federal statute. Rather, the highest court of the state is the best authority on the underlying substantive rule of state law to be applied in the federal matter. If there is no decision by that court, then the federal authority must apply what it finds to be state law after giving "proper regard" to the state trial court's determination and to relevant rulings of other courts of the state. In this respect, the federal agency may be said, in effect, to be sitting as a state court.

State 1 Statute 1 provides for the nonjudicial resolution of a matter, if all necessary parties agree in a written agreement. Under State 1 Statute 2, a matter includes the determination of any question arising in the administration of a trust, and may include, without limitation, questions relating to construction of a trust. State 1 Statute 3 provides that the written agreement may be filed in court and that, upon filing the agreement, the written agreement will be deemed approved by the court and is equivalent to a final court order binding on all persons interested in the trust.

In this case, an examination of the relevant trust instruments and representations of the parties indicate that certain provisions of Trusts are contrary to the intent of Taxpayer and that those provisions are due to scrivener's errors. State 1 law allows for the reformation of trusts due to scrivener's error. See Cases 3 and 4. State 1 Statutes 1, 2, and 3 allow the parties to reform Trusts to correct the scrivener's errors by filing nonjudicial agreements with the appropriate state court. Accordingly, upon consideration of the facts and applicable case law, we conclude that the proposed reformation, based on scrivener's errors, is consistent with applicable state law. Therefore, based on the facts submitted and the representations made, we conclude that as a result of the reformation of the Trusts due to scrivener's errors, Taxpayer's transfers to Trusts will be considered completed gifts of present interests that qualify for the federal gift tax annual exclusion under § 2503(b).

<u>Ruling # 3</u>

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

Section 2033 provides that the value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of death.

Section 2035(a)(1) and (2) provide that if the decedent made a transfer (by trust or otherwise) of an interest in any property, or relinquished a power with respect to any property, during the 3-year period ending on the date of the decedent's death, and the value of such property (or any interest therein) would have been included in the decedent's gross estate under §§ 2036, 2037, 2038, or 2042 if such transferred interest or relinquished power had been retained by the decedent on the date of his death, the value of the gross estate shall include the value of any property (or interest therein) which would have been so included.

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 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 20.2036-1(b)(3) of the Estate Tax Regulations provides that the phrase "right … to designate the person or persons who shall possess or enjoy the transferred property or the income therefrom" includes a reserved power to designate the person or persons to receive the income from the transferred property, or to possess or enjoy nonincome-producing property, during the decedent's life or during any other period described in (a) of this section. With respect to such a power, it is immaterial (i) whether the power was exercisable alone or only in conjunction with another person or persons, whether or not having an adverse interest; (ii) in what capacity the power was exercisable by the decedent or by another person or persons in conjunction with the decedent; and (iii) whether the exercise of the power was subject to a contingency beyond the decedent's control which did not occur before his death (e.g., the death of another person during the decedent's lifetime). The phrase, however, does not include a power over the transferred property itself which does not affect the enjoyment of the income received or earned during the decedent's life. Nor does the phrase apply to a power held solely by a person other than the decedent. But, for example, if the decedent reserved the unrestricted power to remove or discharge a trustee at any time and appoint himself as trustee, the decedent is considered as having the powers of the trustee.

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 the case of a bona fide sale for 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 to alter, amend, revoke, or terminate the interest in the property or where the decedent relinquished such power within the three-year period ending on the date of the decedent's death.

Section 2041(a)(2) provides that the value of the gross estate shall include the value of all property to the extent of any property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under §§ 2035 to 2038, inclusive.

Section 2041(b)(1) provides that for purposes of § 2041(a), the term "general power of appointment" means a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate.

Section 2041(b)(2) provides that the lapse of a power of appointment created after October 21, 1942, during the life of the individual possessing the power shall be considered a release of such power.

In this case, the documentation submitted strongly indicates that Taxpayer intended to relinquish all control over the assets in Trusts and that Taxpayer has not retained any power of appointment over the assets in Trust. Based on the facts submitted and the representations made, we conclude that the reformation of Trusts to correct the scrivener's errors will be consistent with applicable State law. See Commissioner v. Estate of Bosch, 387 U.S. 456 (1967).

Therefore, we conclude that as the result of the reformation of Trusts: (1) Taxpayer will not have retained any interest in the property of Trusts for purposes of § 2033; (2) Taxpayer will not have released, transferred or relinquished any retained interest or power that would subject the assets in Trusts to inclusion in Taxpayer's gross estate under § 2035; (3) Taxpayer will not have retained, for Taxpayer's life, the right, either alone or in conjunction with any person, to designate who will possess or enjoy the property or income from the Trusts within the meaning of § 2036; (4) Taxpayer will not have retained any power, either alone or in conjunction with another person, to alter, amend, revoke, or terminate the reformed Trusts within the meaning of § 2038, and (5) Taxpayer will not have possessed a general power of appointment, as defined under § 2041, with respect to Trusts.

Accordingly, based on the facts submitted and the representations made and assuming that Trusts are reformed pursuant to the terms described above, we conclude that the value of the assets in Trusts, as reformed, will not be included in Taxpayer's gross estate under §§ 2033, 2035, 2036, 2038, or 2041.

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

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. Further, we express no opinion regarding the values of the interests in Property transferred or whether any of those values exceed the annual exclusion amounts for the years at issue.

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.

This 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
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure:
Copy of letter for § 6110 purposes

cc: