

# Charitable Intent



PLANNING NEWS AND IDEAS FOR THE PROFESSIONAL ADVISER

## T RUST QUALIFIES AFTER MINOR ADJUSTMENT

A decedent's will directed that the residue of the estate be held in trust for the shorter of five years or the life of the income beneficiary. The trustee was to pay the beneficiary a specified annuity each month and distribute the assets to three charities at the trust's termination. Because the annuity to be paid to the beneficiary was not at least 5% of the value of the residue, the trust was not a qualified charitable remainder trust under Code §664 and the estate was not entitled to a charitable deduction under Code §2055.

The trustee proposes to modify the trust to pay a 5% annual annuity. The beneficiary is to receive the amount specified in the will, with the charities receiving the balance of the payment. The IRS ruled that the charitable interest in the trust was reformable under Code §2055(e)(3)(C) because (1) the interest would have qualified for the estate tax charitable deduction but for the requirement that the trust be a qualified charitable remainder trust and (2) the income beneficiary's interest was a specific dollar amount, as required under Code §2055(e)(3)(C)(ii). Therefore, the value of the charitable interest is ascertainable as of the date of death and severable from the noncharitable interest.

As reformed, the actuarial value of the charitable interest will not differ by more than 5% from the original value. In addition, noted the IRS, the income beneficiary's interest will terminate at the same time and the reformation will be effective as of the donor's death. Therefore, the trust will be qualified and the estate will be entitled to a charitable deduction for the remainder interest and also the value of the charitable annuity interest.

### Letter Ruling 200726005

## S ELF-DEALING RULES AVOIDED IN REDEMPTION

A charitable remainder unitrust owns 62% of the shares of a company, with the balance owned by an employee stock ownership plan (33%) and the unitrust donor (5%). The company, which is a disqualified person in relation to the unitrust, proposes

to redeem for cash the shares of its shareholders, subject to a maximum redemption amount.

In general, any direct or indirect sale or exchange of property between a private foundation and a disqualified person is self-dealing [Code §4941(d)(1)(A)]. There is an exception, however, if the transaction is pursuant to a liquidation, merger, redemption or recapitalization, provided that all securities of the same class as that held by the foundation are subject to the same terms and the foundation receives no less than fair market value.

The value of the shares will be determined by an independent appraisal. The donor will not tender any of her shares, but the unitrust will tender as many as possible under the redemption limits. The IRS ruled that the redemption will not be self-dealing under Code §4941(d)(1).

### Letter Ruling 200720021

## S AMPLE LEAD TRUST DOCUMENTS, GUIDANCE ON VALUATION OF RETAINED INTEREST ISSUED BY IRS

Donors wishing to establish charitable lead annuity trusts will be able to rely on sample documents issued recently by the IRS. Rev. Proc. 2007-45 provides model forms for inter vivos nongrantor lead trusts and reversionary (grantor) lead trusts. Alternative provisions are included for a trust lasting for the life of an individual, the retention of a right to substitute the charitable lead beneficiary, the apportionment of the annuity amount in the discretion of the trustee, the annuity stated as a specific dollar amount and the designation of an alternative charitable beneficiary. Rev. Proc. 2007-46 provides sample language for a testamentary charitable lead annuity trust. Inter vivos trusts that are valid under local law and are substantially similar to the sample trusts or properly include one or more alternative provisions will qualify for a deduction under Code §§2522(c)(2)(B) and/or 2055(e)(2)(B). Testamentary trusts will qualify for an estate tax charitable deduction under Code §2055(e)(2)(B).

Recently issued proposed regulations (REG-119097-05) provide guidance on the portion of a

trust includible in a grantor's gross estate under Code §§2036 and 2039 if the grantor has retained the right to an annuity or unitrust payment from the trust for life. This includes charitable remainder annuity trusts and unitrusts. The rules, which follow Rev. Rul. 76-273 (1976-2 C.B. 268) and Rev. Rul. 82-105 (1982-1 C.B. 133) generally provide that the portion of the corpus of a charitable remainder trust includible in the gross estate is that portion of the trust corpus necessary to generate a return sufficient to provide the decedent's retained annuity or unitrust payment in perpetuity.

## **g** RANTOR HAS "SPECIAL INTEREST" IN TRUST ACCOUNTING

Lowell Patton and his wife created charitable remainder unitrusts for each of their three children, funding them with \$2.4 million in stock. Matthew Mack, the attorney who prepared the trusts, named himself the administrative trustee and Mark Sherwood as management trustee. In the trusts, Patton reserved the right to change a remainder beneficiary and to remove and replace the trustees. Mack was required to prepare annual accountings for Patton's review and approval.

Three years after the trusts were created, Patton filed a petition to remove Mack and Sherwood. The pair had already resigned as trustees of one unitrust, but refused to resign from the other trusts until they were released from liability and awarded fees and expenses. The trial court agreed to the removal of the two as trustees, but ruled that Patton lacked standing to object to the accounting because he was not a "beneficiary" of the trusts. Patton claimed that the trustees had charged excessive fees and breached their fiduciary duties.

The Court of Appeals of California (2d Dist., Div. 6) noted that under common law, the settlor of a trust who retains no reversionary interest in the trust property

lacks standing to enforce the trust independently of the attorney general. However, the court said that the attorney general does not have the exclusive power to enforce a trust, adding that a "person having a sufficient special interest may also bring an action." Patton reserved the power to remove and replace the trustees, to receive and object to trust accountings and to petition for court-supervised accounting. If he has standing to compel an accounting, "he has the associated right to object to the accounting," said the court, which held that the settlor of a charitable trust can object to an accounting where he has reserved the power in the trust instrument.

*Patton v. Sherwood*, 2d Civil No. B189970

## **r** ECOMMENDED GIFT ANNUITY RATES UNCHANGED

The board of the American Council on Gift Annuities has voted to maintain recommended charitable gift annuity rates, both immediate and deferred, at current levels. The rates will be in effect through June 30, 2008.

### Sample Recommended Single-Life Gift Annuity Rates

Age of Donor	Rate of Return	Age of Donor	Rate of Return
60	5.7%	76	7.2%
62	5.9%	78	7.6%
64	6.0%	80	8.0%
66	6.1%	82	8.5%
68	6.3%	84	9.2%
70	6.5%	86	9.9%
72	6.7%	88	10.6%
74	6.9%	90 or over	11.3%

### WINDOW OF OPPORTUNITY CLOSING

Clients have only a few months left to make qualified charitable distributions (QCD) from IRAs. Those age 70½ and older may give up to \$100,000 to charities through the end of 2007. Although no charitable deduction is allowed, the donor does not have to recognize the distribution in 2007 gross income. QCDs also can satisfy a client's required minimum distribution, resulting in tax savings comparable to the charitable deduction, even for donors who don't itemize deductions. Checks to charity must be written by the IRA custodian, not the donor. If you have any questions about how clients could benefit by this limited time chance to assist The Salvation Army or other favorite charities, please feel free to call our office.