1. Introduction

With certain limited exceptions, specific provisions of estate planning documents generally trump the Probate Code. The documents can also dictate tax results (for better or for worse). That is why it is so important for the preparers of estate, gift, generation-skipping transfer (“GST”) tax and fiduciary income tax returns to understand the terms of the Will or Trust to which the return pertains and to obtain the proper legal advice if the document is ambiguous or poorly written.

To provide a few examples, the terms of estate planning documents can:

a. Determine whether or not California real estate qualifies for an exclusion from property tax reassessment.

b. Dictate whether capital gains taxes are owed on the funding of a gift, bequest or trust.

c. Change the customary allocations of trust receipts or disbursements to income or principal (e.g., by allocating capital gains to trust accounting income or characterizing 100% of royalty receipts as income).

d. Determine whether benefits paid to a trust from a tax-deferred qualified retirement plan qualify for rollover treatment or may be paid out over the life expectancy of the designated beneficiary.

e. Cause an increase in estate or GST taxes payable.

f. Cause the assets of a “bypass” or “credit shelter” trust to be subject to estate taxes in a beneficiary’s estate (contrary to the creator’s intent).

g. Fall short of the requirements for a trust for the benefit of the surviving spouse to qualify for the estate tax marital deduction.
h. Jeopardize or cause the loss of the estate tax charitable deduction for a gift, bequest or trust benefitting charity in whole or in part.

i. Fail to qualify a gift in trust for the present interest annual exclusion from gift tax, resulting in the use of too much of the donor’s estate and gift tax exclusion or the payment of too much in gift tax.

j. Fail to qualify a trust for a grandchild’s benefit, established during the lifetime of its creator, for the annual exclusion from the GST tax, resulting in the use of more of the transferor’s GST exemption than expected or the payment of too much in GST tax.

k. Cause a loss of S Corporation status.

Sometimes, problems such as these can be rectified but only if prompt action is taken. (See Section 10 of these materials.) That is why it is important to read and come to an understanding of a client’s estate planning documents as soon as possible. Consult a lawyer having an expertise in trusts and estates if you or your client has any questions about the meaning or import of a document.

2. Requirements for a Trust to Qualify for the Marital Deduction.

One cannot assume that a trust called a “Marital Deduction Trust” or another similar name qualifies for the federal estate tax marital deduction. Very specific requirements have to be met. If the surviving spouse is a U.S. citizen, the trust must meet the requirements for a Qualified Terminable Interest Property (QTIP) Trust or a General Power of Appointment Trust. With either type of trust, the surviving spouse cannot be required to survive the decedent for more than six months in order to receive benefits from it.

a. Requirements for a Qualified Terminable Interest Property (QTIP) Trust (Internal Revenue Code Section 2056(b)(7) and the accompanying Treasury Regulations)

   i. The surviving spouse must be the only beneficiary, and must be entitled to all the income from the property, payable annually or at more frequent intervals.

   ii. The surviving spouse must have the right to demand that the trustee convert non-productive assets into income-producing assets.

   iii. No person can have a power to appoint any part of the property to anyone other than the surviving spouse during that spouse’s lifetime.

   iv. A valid QTIP election must be made on a timely filed Estate Tax Return. Once made, that election is irrevocable.
b. Requirements for a General Power of Appointment Trust (Internal Revenue Code Section 2056(b)(5) and the accompanying Treasury Regulations)

i. Like a QTIP Trust, the surviving spouse must be entitled to all income from the property, payable annually or at more frequent intervals and have the right to demand that the trustee convert non-productive assets into income-producing assets.

ii. Unlike a QTIP Trust, the surviving spouse must have the power to appoint the assets of the trust in his or her own favor or in favor of his or her own estate.

iii. No other person may hold a power to appoint any part of the property to anyone other than the surviving spouse during that spouse’s lifetime.

c. If the surviving spouse is not a United States citizen and does not become a United States citizen before the deadline for filing a federal estate tax return, then in order for gifts benefitting that surviving spouse to qualify for the marital deduction, the property must be transferred to a qualified domestic trust (or “QDOT”). The requirements of a QDOT, which can be found in Internal Revenue Code Section 2056A and the accompanying Treasury Regulations, are as follows:

i. The trust must meet all requirements for marital deduction trusts for U.S. citizens.

ii. At least one trustee must be a United States citizen or a United States corporation.

iii. If the trust contains assets that exceed $2,000,000 in value (ignoring indebtedness on the assets), either at least one trustee must be a bank, or the U.S. citizen trustee must furnish a bond or letter of credit in favor of the I.R.S. equal to 65% of the fair market value of the trust assets.

iv. There are restrictions on the holding of foreign real property if the trust assets are worth $2,000,000 or less.

v. The U.S. citizen trustee must have the right to withhold any estate tax imposed under 2056A on distributions of principal.

vi. A QDOT election must be made on the last federal estate tax return filed before the due date (including extensions). If no timely return is filed, the QDOT election must be made on the first federal estate tax return filed no
later than one year after the due date (including extensions). Once made, the election is irrevocable.

d. California Probate Code Sections 21520-21525 are helpful if a marital deduction trust is lacking an essential component. If the trust manifests an intent to qualify a gift in trust for a spouse for the marital deduction, but is missing one or more of the requirements listed above (other than the QTIP election) these California statutes serve to add the missing provisions and exclude prohibited powers so that the gift will still qualify for the deduction.


The general purpose of a bypass trust is to allow a beneficiary (such as a surviving spouse) certain benefits from a trust while preventing the inclusion of the trust assets in the beneficiary’s estate for estate tax purposes. Among other things, a beneficiary cannot be permitted to revoke or amend a bypass trust. Here are other notable mistakes made in the drafting of bypass trusts, which will sabotage the estate tax objective.

Under Internal Revenue Code Section 2041, a beneficiary’s possession of a general power of appointment will cause the inclusion of the assets of the bypass trust in the beneficiary’s estate for estate tax purposes. General powers of appointment are not always immediately apparent, and may be created by the inadvertent inclusion or omission of certain language, for example:

a. A beneficiary serving as the trustee has the power to distribute principal for purposes other than his or her own support, health, education and maintenance. Some red flags (that may cause estate tax inclusions) are the ability to make distributions for one’s own comfort, happiness, enjoyment or for any reason. The terms “in case of emergency,” “welfare” and “care” may be problematic as well.

b. The trustee has the ability to make distributions for the benefit of another that would serve to discharge the trustee’s legal obligation of support (and the trustee is not precluded from making distributions that discharge that legal obligation of support).

c. A beneficiary is given a power to appoint trust assets in favor of himself or herself, the beneficiary’s creditors, the beneficiary’s estate or creditors of the beneficiary’s estate. (For example, during the lifetime of a child of the settlor, that child is permitted to appoint the assets of his or her trust in favor of the settlor’s descendants.)

d. The beneficiary is not serving as trustee. But the trustee has a power that would constitute a general power if held by the beneficiary, and the beneficiary has the
power to remove the trustee and designate the beneficiary or a person who is related or subordinate to the beneficiary as successor trustee.

e. If a beneficiary’s death taxes or debts are directed to be paid from the assets of the bypass trust.

4. Estate Tax Charitable Deduction.

For the most part, the rules that must be met in order for an outright gift or bequest or transfers to a trust to qualify for an estate tax charitable deduction are contained in Internal Revenue Code section 2055 and the Treasury Regulations promulgated under it.

a. Among other things, the amount passing to or in trust for charity must be ascertainable as of the date of the decedent’s death.

b. A gift, bequest or trust transfer taking effect at the donor’s death must be made from property that is subject to estate tax.

c. If a gift or bequest to or in trust for charity is subject to a condition, the condition has to be so remote as to be negligible.

d. A split interest charitable trust (i.e., one benefitting both charity and individuals) must meet the requirements for a charitable remainder trust or pooled income fund under Section 664 of the Internal Revenue Code or the requirements for a charitable lead trust. Sample required provisions for a charitable remainder annuity trust and a charitable lead unitrust are attached. (See Revenue Procedures 2003-53, 2016-42 and 2008-45.)


There are several California and federal laws that determine the manner in which death taxes will be apportioned if the will or trust does not specifically address the apportionment of taxes. Generally, state law governs the apportionment of the federal estate tax. Under California law, unless a decedent directs otherwise, the estate tax burden is equitably prorated among the persons having an interest in the decedent’s taxable estate. (Probate Code §20100 et seq.) However, federal statutes confer upon a decedent’s executor a right to recover the estate tax attributable to the following type of assets from the recipients of those assets (unless the decedent provides to the contrary in his or her Will):

a. Proceeds of insurance on the decedent’s life payable to a beneficiary other than the decedent’s estate (IRC §2206).
b. Property over which the decedent held a general power of appointment (IRC §2207).

c. Property included in the decedent’s gross estate by reason of IRC §2036 (IRC §2207B).

d. Assets in a qualified terminable interest (“QTIP”) trust included in a surviving spouse’s estate under IRC §2044 (IRC §2207A). IRC §2207A provides that, unless modified or waived by the surviving spouse’s Will the surviving spouse’s estate is entitled to be reimbursed for the incremental increase in the estate tax in the surviving spouse’s estate caused by inclusion of the QTIP property in the surviving spouse’s estate.

e. The surviving spouse can direct instead that the surviving spouse’s estate and the marital deduction trust each bear a share of the estate tax (at the same average rate) in proportion to size.


6. Risks of Allocating Liability for Payment of all Tax Liability to the Residue.

To “opt out” of the apportionment statutes described above, many attorneys routinely include a provision in the will or trust directing that death taxes be paid from the residue of the probate estate or living trust. Sometimes these provisions are so broad they include not only death taxes attributable to property passing through the probate estate or the trust, but death taxes attributable to assets passing outside of the estate or trust, such as proceeds of life insurance policies, joint tenancy property, and retirement plans. The gifts passing to beneficiaries under the will or trust may be eliminated or severely diminished by the payment of taxes on those gifts from property passing outside of the will or trust (perhaps to other beneficiaries).

For all examples, assume that the Taxpayer, T, has used all of his or her estate and gift tax exclusion ($11,400,000 in 2019) and all of his or her GST tax exemption.

Example: T has one child, C, and a long-time girlfriend, G. T has a revocable trust that holds his home, worth $5,000,000, and his brokerage account, with cash and securities worth $5,000,000. T also has a life insurance policy with a face amount of $5,000,000 and an IRA worth $5,000,000. G is the primary beneficiary of both the insurance policy and the IRA, T’s revocable Trust leaves his tangible personal property to G, and the residue to C. T’s trust contains a tax clause that directs the
trustee to pay “all death taxes arising as a result of T’s death from the Trust residue.” T dies in 2019.

Result: T’s estate will owe $8,000,000 in estate taxes (40% of $20,000,000). G will receive the insurance policy and the IRA worth a combined $10,000,000. C will receive the home and the brokerage account, also worth a combined $10,000,000. However, the entire $8,000,000 tax liability will be paid from the residue of the Trust, leaving only $2,000,000 for C, while G will keep the full $10,000,000. If T intended to divide his estate equally between C and G, the estate plans falls woefully short of his objective.

7. **Payment of Death Taxes from Property Qualifying for a Marital or Charitable Deduction.** If a charitable gift or property that passes to or in trust for a surviving spouse in a manner qualifying for the marital deduction bears a share of the death tax burden, then the amount of that deduction will be reduced significantly (the tax and deduction being determined by a complicated interrelated calculation).

   **Example 1:** T’s total estate is $25 million. At her death, T makes a specific gift of $5 million to her husband, and the residue to her children under the terms of her revocable inter vivos Trust. The Trust directs that all death taxes on Trust assets be paid from the Trust residue.

   Result: T’s estate is entitled to a $5 million marital deduction and pays estate taxes of $8 million on the residue (40% of $20,000,000).

   Compare this to:

   **Example 2:** T’s total estate is $25 million. At her death, T after making specific gifts of negligible value, gives 20% of the residue to her husband and 80% of the residue to her children under the terms of her revocable inter vivos Trust. The Trust directs that all death taxes on Trust assets be paid from the Trust residue.

   Result: This subjects assets passing to the husband to estate tax which will, in turn, reduce the size of the marital deduction. That, in turn, increases the amount of estate tax on the assets passing to the husband, and so on. In the end, the estate may take a marital deduction of only $3,260,869, resulting in a total tax liability of $8,695,652.

8. **Portability**

   Be sure to check the estate planning documents to see if there are specific instructions on portability. Some documents (e.g., in blended families) may for example, contain instructions on who is to bear the cost of the preparation of an Estate Tax Return that is filed solely to port the exclusion, the surviving spouse or the deceased spouse’s estate.

9. **Source of Payment of Generation-Skipping Transfer Taxes**

   Absent a provision in an estate planning document to the contrary, federal law controls the apportionment of the generation-skipping transfer ("GST") tax. IRC §2603(b) establishes the
general rule that the GST tax is charged against “the property constituting” the GST. Many intricate rules regarding how GST taxes are charged emanate from this seemingly simple statement, as the person responsible for paying the GST tax and the manner in which the tax is calculated differ for each type of GST. The “default rules” are discussed below.

The statutory apportionment scheme of the GST tax can be overridden by the instrument creating the transfer, but only if the instrument contains a “specific reference to the [GST] tax.” IRC 2603(b). Therefore, if the testator desires a different result than that provided by IRC §2603, then the governing instrument should explicitly refer to the GST tax and the source of payment of the tax.

a. Lifetime Direct Skips.

i. Definition. A lifetime direct skip is a transfer subject to gift tax made during the transferor’s lifetime to or in trust for a skip person. IRC §2612(c).

ii. Who pays the tax? The Transferor pays the tax on a lifetime direct skip. IRC §2603(a)(3).

iii. How is the tax calculated? The tax is calculated exclusive of the dollars used to pay the tax. That is, the taxable amount is the value of the property received by the transferee, and the GST tax is not included as part of the tax base. IRC §2623. However, in addition to the transferor being liable for the payment of the GST tax attributable to a lifetime direct skip, IRC §2515 imposes a gift tax on the amount of the GST tax paid by the transferor.

Example: T gifts $1 million to GC (his grandchild). The gift tax rate is 40%. The gift tax payable on the transfer is $400,000 (40% of $1 million). The GST tax payable on the transfer is $400,000 (40% of $1 million). The gift tax on the GST tax is $160,000 (40% of $400,000). Total transfer taxes amount to $960,000, or 96% of the amount transferred to GC.

Planning Considerations. If a donor would like to limit his out-of-pocket costs in connection with a lifetime direct skip, he may wish to structure the gift as a “net gift,” by having the donee agree in writing to be responsible for the payment of any gift and GST taxes attributable to the transfer. However, Technical Advice Memorandum 9246007 (July 29, 1992) indicates that with such a net gift, in calculating the tax base, the transfer still has to be “grossed up” by the amount of GST taxes payable (even though they are not being paid by the transferor), resulting in little tax saving, if any.
b. Testamentary Direct Skips.

i. Definition. A testamentary direct skip is a transfer subject to estate tax made upon the transferor’s death to or in trust for a skip person. IRC 2612(c).

ii. Who pays the Tax? With respect to a direct skip occurring at death, other than a direct skip from a trust, the executor is liable for the tax (Treasury Regulation 26.2662-1(c)(1)(v)). The trustee of the trust pays the tax in the context of a direct skip from a trust. IRC §2603(a)(2).

iii. How is the Tax Calculated? Like a lifetime direct skip, a testamentary direct skip is exclusive of the GST taxes payable. IRC §2623. However, in the case of a direct skip at death, unless the testator directs otherwise, the GST tax is apportioned to the gift itself, thereby decreasing the amount received by the skip person.

Example: T makes a $500,000 specific bequest to GC and directs that all GST taxes be paid as provided by federal law (i.e., charged to the gift to the grandchild). The Will directs that estate taxes be paid from the residue. According to Schedule R of Form 706, the GST tax is determined by using the following formula. X stands for the GST tax.

\[ X = 0.4(500,000-X) \]
\[ X / 0.4 = 500,000 - X \]
\[ 2.5X = 500,000 - X \]
\[ 2.5X + X = 500,000 \]
\[ 3.5X = 500,000 \]
\[ X = 500,000 / 3.5 \]
\[ X = \$142,857 \]

**PROOF**

\[ 0.4(500,000 - 142,857) = 142,857 \] Grandchild is left with $357,143 ($500,000 - $142,857).

Planning Considerations Relating to Payment of the GST Tax. If in the above example, T wants GC to receive $500,000, the will or trust should provide that the GST tax will be paid from the residue. With that direction in this example, GC would receive $500,000 and the GST tax would be $200,000 (40% of $500,000), with the residuary beneficiaries receiving $200,000 less than they would if the gift to GC had borne its own GST taxes.
c. Taxable Terminations.

i. Definition. A taxable termination is a termination of an interest in property held in trust unless: (1) immediately after the termination, a non-skip person has an interest in the property, or (2) no distribution may be made at any time thereafter to a skip person. IRC 2612(a)(1)

ii. Who pays the tax? The trustee of the trust is responsible for paying the tax in the context of a taxable termination. IRC 2603(a)(2).

iii. How is the tax calculated? The GST tax on a taxable termination is computed on a tax inclusive basis. IRC 2622(a). For example, if the net amount of the trust subject to the taxable termination is $1,000,000, the GST tax is 40% of $1,000,000 ($400,000) and the trust beneficiary receives $600,000.

d. Taxable Distributions.

i. Definition. A taxable distribution is any distribution (of either income or principal) from a trust to a skip person, other than a direct skip or a taxable termination. IRC 2612(b). For example, a Trustee is permitted to make distributions to a grandchild from a child’s trust.

ii. Who pays the tax? The transferee is responsible for paying the tax on a taxable distribution. IRC 2603(a)(1).

iii. How is the tax calculated? Like a taxable termination the GST tax on a taxable distribution is computed on a tax inclusive basis. IRC §2621(a). For example, if the amount of the taxable distribution from a trust with an inclusion ratio of one is $10,000, the GST tax, which the beneficiary must pay, is 40% of $10,000 ($4,000), and the beneficiary is left with $6,000.

iv. Planning Considerations. If the trust directs that the GST tax be paid by the trust, the payment of tax constitutes an additional taxable distribution to the transferee. IRC 2621(b).

Example: In 2018, a taxable distribution of $10,000 is made from a trust with an inclusion ratio of one. The trust directs the trustee to pay the GST tax on the distribution, and the trustee pays the tax in 2019. Treasury Regulation 26.2612-1(c)(1) provides that the distribution in 2018 includes the GST tax paid by the trustee in 2019, which results in an interrelated calculation to determine the amount of the GST tax. The following formula can be used to determine the amount of the tax: [Amount distributed to skip person/(1-the applicable rate)]-Amount distributed to skip person = amount of GST tax to
be paid by the trustee. In this example, the formula yields $10,000/(1-40%)-$10,000 = $6,666.

Result: The GST tax is $6,666, calculated as though $16,666 had been distributed to the skip person and leaving the skip person with $10,000. Compare this with $4,000 GST tax owed when the distributee pays the tax, leaving him or her with only $6,000.

10. Options for Correcting an Irrevocable Trust

a. **Disclaimers of Property or Interests in Property.** To be effective (and avoid a gift from the disclaimant to the person receiving the asset in his or her place), disclaimers must be made in writing within nine months of (i) the date on which the transfer creating the interest is made or (ii) the day on which the disclaimant attains age 21, whichever is later. No extension of time is available. The disclaimer must be delivered, within that time period, to the transferor, his or her legal representative or the holder of legal title to the property. Once made, disclaimers are irrevocable, and the disclaimed property must pass according to the terms of the estate planning document or applicable law to someone other than the disclaimant or to the decedent’s spouse. The disclaimant can take no benefits from the disclaimed property and cannot direct its disposition. For example, the disclaimant may not be given a power of appointment over the disclaimed property. Internal Revenue Code Section 2518 and California Probate Code Section 295.

b. **Disclaimers of Trustee Power.** A trustee may disclaim individual powers while keeping all other trustee powers if the trust terms specifically authorize the trustee to do so. If the trust does not specify whether a trustee’s disclaimer of a power operates to divest successor trustees of the same power, the successor trustees will possess the disclaimed power, unless the trust instrument directs otherwise. If the trust does not address the disclaimer of a power by the trustee, the Court may have to approve the disclaimer, successor trustees may still possess the disclaimed power, and the disclaimer may not be effective unless the beneficiaries affected by the disclaimer consent to it.

c. **Termination of Small Trusts by Trustees.** Probate Code Section 15408 permits the Trustee to terminate an irrevocable trust having a value of less than $50,000. By the same token, distributions may be made by the Trustee in keeping with the Trust terms.

d. **Court Reformation of Charitable Trusts Sanctioned by Internal Revenue Code.** No estate tax charitable deduction is allowed for a trust that benefits both charity and individuals unless that trust is a qualified charitable remainder annuity trust or unitrust described in Internal Revenue Code section 664, or a pooled income fund
described in Internal Revenue Code section 642(c)(5) or unless charity’s interest is in the form of a guaranteed annuity or a fixed percentage, distributed yearly, of the fair market value of the property (to be determined yearly). Wholly charitable trusts (like private foundations) and charitable remainder and charitable lead trusts must meet very specific technical requirements. If a governing instrument contains a gift to or in trust for charity that does not meet these requirements, Internal Revenue Code Section 2055(e) specifically permits a Court to reform the instrument to bring it into conformity with the requirements. However, any such judicial proceeding must be commenced within 90 days after the due date (including extensions) for the federal estate tax return. If no federal estate tax return is required to be filed, the judicial proceedings must be commenced within 90 days after the due date (including extensions) for filing the trust’s first income tax return.

e. Court-Order Modification or Termination of Larger Trusts under State Law. For larger trusts, an interested party must have a ground for petitioning the Court to change the Trust terms. Common grounds (found in Sections 15404 through 15408 of the Probate Code) are that most of the beneficiaries desire a change but not all can or will consent, the circumstances have changed in a way the settlor did not anticipate or the trust has become uneconomical to manage in light of the attending costs. Although Probate Code section 15404 states that while the settlor is alive, the settlor and all beneficiaries may agree to a modification without Court approval, doing so can expose the Trustee to liability if there are minor or unborn beneficiaries (for whom the Court would normally appoint a guardian ad litem before permitting a modification). Of course, there is no guarantee that the Court will grant the relief requested, especially if a party with standing objects.

f. Internal Revenue Service’s Position on Modifications under State Law. Bear in mind that under Bosch v. Commissioner, 387 U.S. 456 (1967), in tax cases the Internal Revenue Service is only fully bound by decisions from a state’s highest court. If there is no decision by the highest court on a particular matter, the federal court must apply what it finds state law to be, giving due regard to the decisions of other State Courts. In Revenue Ruling 73-142, the issue was whether the assets of an irrevocable trust were includable in the settlor’s estate at his death due to the broad powers held by the settlor and the settlor’s power to remove the trustee and appoint himself or someone related or subordinate to the settlor as trustee. Prior to the settlor’s death, a state trial court determined that the settlor could not name himself or someone related or subordinate to him as trustee. Because the trial court handed down its decision and the time for appealing the decision had passed by the time of the event giving rise to the federal tax liability (i.e., the death of the settlor), the Revenue Ruling states that the trial court decree was binding on the IRS (in terms of who the settlor was permitted to appoint as trustee) and the decedent’s estate prevailed. However, many problems within estate planning
documents are not discovered until after the testator’s or settlor’s death (or after the event giving rise to estate tax liability).

g. Decanting. Decanting is a statutory procedure that permits the terms of an irrevocable trust to be modified either by transferring assets of an existing trust to a new trust with different terms or by simply changing the terms of the first trust within certain limitations. Oftentimes, the Court does not become involved.

i. Who may decant?

A. A trustee or other fiduciary, other than a settlor, who has the discretion to distribute or direct a trustee to distribute part or all of the principal of the first trust to one or more current beneficiaries, or a special fiduciary appointed under Probate Code Section 19509, or a special-needs fiduciary under Probate Code Section 19513.

B. A fiduciary with no discretion over distributions of principal may NOT decant.

ii. What trusts may be decanted? All California trusts, except:

A. Revocable trusts, unless the trust is revocable by the settlor only with the consent of the trustee or a person holding an adverse interest.

B. Purely charitable trusts.

C. Trusts with provisions specifically limiting or preventing decanting.

iii. What must be done to decant?

A. Notice must be given to each settlor of the first trust, each qualified beneficiary of the original trust, each holder of a presently exercisable power of appointment over any part or all of the original trust, each person that currently has the right to remove or replace the authorized fiduciary, each other fiduciary of the original trust, each fiduciary of the first and second (or modified) trust, and perhaps the Attorney General (if charity has an interest).

B. A “qualified beneficiary” is anyone to whom distributions of principal are or can be made and someone to whom distributions would be made if the interests of those current beneficiaries were to terminate. If any beneficiary is an unrepresented minor, the Trustee must petition the Court to appoint a Guardian ad litem for that
person, and the trustee must give notice to that Guardian. The same procedure may have to be followed if a beneficiary is part of a class of beneficiaries, some of whom may not yet be born or ascertained. Similar rules apply for beneficiaries the fiduciary knows (or has reason to know) are unable to manage their own personal finances or resist fraud or undue influence.

C. The authorized fiduciary and the interested parties (to whom notice is given) may apply to the court to approve or prevent the exercise of the decanting power, among other things.

D. The decanting power must be exercised in writing by an authorized fiduciary.

iv. What must the Notice contain?

A. A description of the manner in which the authorized fiduciary intends to exercise the decanting power, which includes a statement as to the authorized fiduciary’s reason for the proposed decanting and an explanation as to the differences between the first trust and the second (or modified) trust.

B. The proposed effective date for exercise of the power.

C. A copy of the first trust instrument.

D. Copies of all second trust instruments (or modifications).

E. A warning, set out in a separate paragraph in not less than 10-point bold type, or a reasonable equivalent thereof, stating the following: “If you do not bring a court action to contest the proposed trust decanting (the proposed changes to the trust) within 59 days of this notice, you will lose your right to contest the decanting.”

v. What trust provisions may a trustee change using the decanting power?

The answer depends on how much discretion to distribute the principal of the trust the trustee possesses. If a trustee’s discretion to distribute principal is limited by an “ascertainable standard” (i.e. for the health, education, maintenance, and support of the beneficiary), that Trustee has what is called “limited distributive discretion.” If a Trustee’s discretion to distribute principal is not limited by an ascertainable standard, that trustee has “expanded distributive discretion.”
vi. What may a trustee with limited distributive discretion (LDD) change using the decanting power?

A. A trustee with LDD may make NO material changes to the beneficial interests of the beneficiaries.

B. A trustee with LDD may change administrative provisions. For example:
   1. Change trustees and successor trustees.
   2. Change the jurisdiction of the trust.
   3. Change the trustee’s powers.

vii. What may a trustee with expanded distributive discretion (EDD) change using the decanting power?

A trustee with EDD may change many things in a trust as long as the trustee does not (1) add a new current beneficiary or add a new remainder beneficiary; (2) reduce or eliminate a vested interest (as specifically defined in Probate Code section 19511), (3) make any changes that would be counter to the trustees fiduciary duties, including the duty to act in accordance with the purposes of the first trust, or (4) make any change that violates any of several specific and narrow prohibitions contained in Probate Code Sections 19513-19519 (which have to do with increases in fiduciary compensation, conflicts of interest for a fiduciary and tax and special needs planning).

viii. What risks of decanting should I be aware of before choosing to decant?

A. First, despite appearing to impose a 60-day limit on bringing an action to contest a proposed decanting, the California Uniform Trust Decanting Act does not provide for any time limit on a beneficiary’s right to bring an action claiming that the decanting did not comply with the statutory rules, or was an abuse of discretion or breach of fiduciary duty.

B. Second, in Section 5.01 of the 2019-01 Internal Revenue Bulletin, the IRS lists several potential income, gift, estate and GST tax issues that arise in the context of decanting about which it will not issue private letter rulings or determinations.
11. Property Tax Issues

Certain provisions in trusts can result in a property tax reassessment and significant increase in property taxes. If a decedent leaves real property in a trust that has permissible income beneficiaries other than a surviving spouse and children, the parent/child exclusion from reassessment will be disallowed. This can occur in sprinkling trusts which permit distributions to be made for the benefit of the descendants of the settlor (which include grandchildren). To qualify for the grandparent/grandchild exclusion from reassessment, the grandchild’s parents must be deceased.

One solution to this problem is to require trusts of this kind to be split into two subtrusts, one of which holds real property and will only allow income distributions to the surviving spouse and/or children, and another trust holding all other property, from which others may benefit. Another solution is to state that no California real property, no income from California real property or the proceeds of its sale may benefit anyone other than the surviving spouse or the decedent’s children.

Some clients who live with a sibling may want to give the sibling the right to live in the home until the sibling’s death. However, there is no sibling to sibling exclusion from reassessment. In the alternative, the sibling can be given the right to occupy the residence for a term of years shorter than 35 years.

12. Recognition of Kenan Gain on the Funding of Trusts and Shares. Under Kenan v Commissioner, 114 F.2d 217 (2d Cir. 1940), in some circumstances, using assets that have appreciated between the date of death and the date of distribution to satisfy a pecuniary gift will cause the trust or estate to recognize gain as if the assets were sold and the proceeds of sale were used to fund the pecuniary gift instead.

a. Kenan gain arises when a Trust or Will directs that a specific pecuniary gift may be satisfied in kind at the value of assets on the date of distribution (or upon the funding of a trust measured by a specific dollar amount) and appreciated assets are used to satisfy the gift (or fund the trust). If the Trust or Will instead directs that assets allocated in kind be valued at their date of death (or federal estate tax) values, then no gain will be recognized on the satisfaction of the specific gift or the funding of the trust with appreciated assets.

b. In Revenue Ruling 66-207, the decedent’s estate was worth considerably less than it was at the time he signed his Will. As a result, after the payment of debts and administration expenses, there were insufficient assets to fund a specific bequest to a trust under the decedent’s Will (and the residue of the estate was wiped out). Even though the bequest could not be satisfied in full, the IRS determined that Kenan gain was recognized.
c. Given the dramatic increase in the estate tax exclusion amount in recent years, on the death of the first spouse, the decedent’s share of a married couple’s assets may be insufficient assets to fund a specific pecuniary gift to a Marital Deduction Trust or a Bypass Trust. Kenan gain can be avoided in these instances by directing that assets be allocated in satisfaction of the pecuniary amount at their date of death (or federal estate tax) values or through the use of a fractional division of the decedent’s estate between the Marital Deduction Trust and Bypass Trust.

13. Crummey Withdrawal Rights

a. Varieties. Crummey withdrawal rights (designed to qualify gifts made in trust for the gift tax present interest annual exclusion) come in a variety of forms and sizes. Here are some examples of different withdrawal rights given to beneficiaries with respect to gifts made to a particular trust each calendar year:

i. Each beneficiary can withdraw the gifts to his or her trust up to (but not exceeding) the greater of $5,000 or 5% of the value of the trust at the end of the calendar year. If the power is not exercised by the end of the year, it lapses.

ii. Each beneficiary can withdraw the gifts to his or her trust up to (but not exceeding) the gift tax annual exclusion amount for each donor. If the power is not exercised within a certain period (not shorter than 30 days from the date the beneficiary receives notice of the gift and his or her right to withdraw it), the power lapses.

iii. Each beneficiary can withdraw the gifts to his or her trust up to (but not exceeding) the gift tax annual exclusion amount for each donor. At the end of each year, the power lapses as to the greater of $5,000 or 5% of the value of the trust at the end of the calendar year. The beneficiary continues to have the right to withdraw the balance. This is commonly known as a “hanging power.”

b. Common Drafting and Administration Oversights.

i. Regarding the second example in paragraph a above: If a beneficiary is given the power to withdraw gifts in the aggregate (from all sources) which exceed the greater of $5,000 or 5% of the value of the trust at the end of the calendar year, then the beneficiary is deemed to have made a taxable gift of the excess to the remaindermen of his or her trust (absent provisions in the trust that prevent that from happening). These gifts are
gifts of future (not present) interests for which gift tax returns are required to be filed. If a beneficiary is permitted to withdraw the gift tax annual exclusion amount each time a gift is made and the power lapses as to that entire amount (if it is not exercised within a certain period of time), then in order to delay the gift until the beneficiary’s death, the beneficiary can be given a power to appoint the assets remaining in the beneficiary’s trust at his or her death (usually in favor of someone other than the beneficiary’s estate or creditors of the beneficiary or the beneficiary’s estate or in favor of a more limited class).

ii. If a client’s mother and grandmother have each established a trust for the client’s benefit and under each trust the client may withdraw the greater of $5,000 or 5% of the value of the trust at the end of the calendar year, if both powers lapse at the end of the year, the taxable gift problem described in the preceding paragraph arises (because the greater of $5,000 or 5% is a per donee limitation).

iii. Each time a gift is made to a trust, the beneficiaries should be notified of their withdrawal rights, immediately. If they are not notified, on audit the IRS may disallow the annual exclusion, thereby increasing the taxable gifts made by the donor during his or her lifetime. It is a good idea to have beneficiaries acknowledge receipt of the notification.

iv. The granting of withdrawal rights can change the person to whom trust income is taxed, in whole or in part, and cause inclusion of the assets a beneficiary is permitted to withdraw in his or her estate for estate tax purposes.

SECTION 1. PURPOSE
This revenue procedure contains an annotated sample declaration of trust and alternate provisions that meet the requirements of § 664(d)(1) of the Internal Revenue Code for an inter vivos charitable remainder annuity trust (CRAT) providing for annuity payments for one measuring life followed by the distribution of trust assets to a charitable remainderman.

SECTION 2. BACKGROUND
Previously, the Internal Revenue Service issued sample trust instruments for certain types of CRATs. The Service is updating the previously issued samples and issuing new samples for additional types of CRATs; annotations and alternate sample provisions are included as further guidance. In addition to the sample trust instrument included in this revenue procedure for an inter vivos CRAT providing for annuity payments for one measuring life, samples are provided in separate revenue procedures for:

1. an inter vivos CRAT providing for annuity payments for a term of years (see Rev. Proc. 2003-54);
2. an inter vivos CRAT providing for annuity payments payable consecutively for two measuring lives (see Rev. Proc. 2003-55, superseding section 4 of Rev. Proc. 90-32, 1990-1 C.B. 546);
3. an inter vivos CRAT providing for annuity payments payable concurrently and consecutively for two measuring lives (see Rev. Proc. 2003-56, superseding section 5 of Rev. Proc. 90-32);
4. a testamentary CRAT providing for annuity payments for one measuring life (see Rev. Proc. 2003-57, superseding section 6 of Rev. Proc. 90-32);
5. a testamentary CRAT providing for annuity payments for a term of years (see Rev. Proc. 2003-58);
6. a testamentary CRAT providing for annuity payments payable consecutively for two measuring lives (see Rev. Proc. 2003-59, superseding section 7 of Rev. Proc. 90-32); and

SECTION 3. SCOPE AND OBJECTIVE
Section 4 of this revenue procedure provides a sample declaration of trust for an inter vivos CRAT with one measuring life that is created by an individual who is a citizen or resident of the United States. Section 5 of this revenue procedure provides annotations to the provisions of the sample trust. Section 6 of this revenue procedure provides samples of alternate provisions concerning: (.01) the statement of the annuity amount as a specific dollar amount; (.02) the payment of part of the annuity to an organization described in § 170(c); (.03) a qualified contingency; (.04) the last annuity payment to the recipient; (.05) the restriction of
the charitable remainderman to a public charity; (.06) a retained right to substitute the charitable remainderman; and (.07) a power of appointment to designate the charitable remainderman.

For transfers to a qualifying CRAT, as defined in § 664(d)(1), the remainder interest will be deductible by a citizen or resident of the United States under §§ 170(f)(2)(A), 2055(e)(2)(A), and 2522(c)(2)(A) for income, estate, and gift tax purposes, respectively, if the other requirements of §§ 170(f)(2)(A), 2055(e)(2)(A), and 2522(c)(2)(A) (that is, the requirements not relating to the provisions of the governing instrument) are also met. The Service will recognize a trust as a qualified CRAT meeting all of the requirements of § 664(d)(1) if the trust operates in a manner consistent with the terms of the trust instrument, if the trust is a valid trust under applicable local law, and if the trust instrument: (i) is substantially similar to the sample in section 4 of this revenue procedure; or (ii) properly integrates one or more alternate provisions from section 6 of this revenue procedure into a document substantially similar to the sample in section 4 of this revenue procedure. A trust instrument that contains substantive provisions in addition to those provided in section 4 of this revenue procedure (other than properly integrated alternate provisions from section 6 of this revenue procedure, or provisions necessary to establish a valid trust under applicable local law that are not inconsistent with the applicable federal tax requirements), or that omits any of the provisions of section 4 of this revenue procedure (unless an alternate provision from section 6 of this revenue procedure is properly integrated), will not necessarily be disqualified, but neither will that trust be assured of qualification under the provisions of this revenue procedure. The Service generally will not issue a letter ruling on whether an inter vivos trust created by an individual and with one measuring life qualifies as a CRAT. The Service, however, generally will issue letter rulings on the effect of substantive trust provisions, other than those contained in sections 4 and 6 of this revenue procedure, on the qualification of a trust as a CRAT.

SECTION 4. SAMPLE INTER VIVOS CHARITABLE REMAINDER ANNUITY TRUST — ONE LIFE

On this day of , 20__, I, (hereinafter “the Donor”), desiring to establish a charitable remainder annuity trust, within the meaning of Rev. Proc. 2003-53 and § 664(d)(1) of the Internal Revenue Code (hereinafter “the Code”), hereby enter into this trust agreement with as the initial trustee (hereinafter “the Trustee”). This trust shall be known as the Charitable Remainder Annuity Trust.

1. Funding of Trust. The Donor hereby transfers and irrevocably assigns, on the above date, to the Trustee the property described in Schedule A, and the Trustee accepts the property and agrees to hold, manage, and distribute the property under the terms set forth in this trust instrument.

2. Payment of Annuity Amount. In each taxable year of the trust during the annuity period, the Trustee shall pay to [permissible recipient] (hereinafter “the Recipient”) an annuity amount equal to [a number no less than 5 and no more than 50] percent of the initial net fair market
value of all property transferred to the trust, valued as of the above date (that is, the date of the transfer). The first day of the annuity period shall be the date the property is transferred to the trust and the last day of the annuity period shall be the date of the Recipient’s death. The annuity amount shall be paid in equal quarterly installments at the end of each calendar quarter from income, and to the extent income is not sufficient, from principal. Any income of the trust for a taxable year in excess of the annuity amount shall be added to principal. If the initial net fair market value of the trust assets is incorrectly determined, then within a reasonable period after the value is finally determined for federal tax purposes, the Trustee shall pay to the Recipient (in the case of an undervaluation) or receive from the Recipient (in the case of an overvaluation) an amount equal to the difference between the annuity amount(s) properly payable and the annuity amount(s) actually paid.

3. Proration of Annuity Amount. The Trustee shall prorate the annuity amount on a daily basis for any short taxable year. In the taxable year of the trust during which the annuity period ends, the Trustee shall prorate the annuity amount on a daily basis for the number of days of the annuity period in that taxable year.

4. Distribution to Charity. At the termination of the annuity period, the Trustee shall distribute all of the then principal and income of the trust (other than any amount due the Recipient or the Recipient’s estate under the provisions above) to [designated remainderman] (hereinafter “the Charitable Organization”). If the Charitable Organization is not an organization described in §§ 170(c), 2055(a), and 2522(a) of the Code at the time when any principal or income of the trust is to be distributed to it, then the Trustee shall distribute the then principal and income to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) of the Code as the Trustee shall select, and in the proportions as the Trustee shall decide, in the Trustee’s sole discretion.

5. Additional Contributions. No additional contributions shall be made to the trust after the initial contribution.

6. Prohibited Transactions. The Trustee shall not engage in any act of self-dealing within the meaning of § 4941(d) of the Code, as modified by § 4947(a)(2)(A) of the Code, and shall not make any taxable expenditures within the meaning of § 4945(d) of the Code, as modified by § 4947(a)(2)(A) of the Code.

7. Taxable Year. The taxable year of the trust shall be the calendar year.

8. Governing Law. The operation of the trust shall be governed by the laws of the State of . However, the Trustee is prohibited from exercising any power or discretion granted under said laws that would be inconsistent with the qualification of the trust as a charitable remainder annuity trust under § 664(d)(1) of the Code and the corresponding regulations.

9. Limited Power of Amendment. This trust is irrevocable. However, the Trustee shall have the power, acting alone, to amend the trust from time to time in any manner required for the sole purpose of ensuring that the trust qualifies and continues to qualify as a charitable remainder annuity trust within the meaning of § 664(d)(1) of the Code.
10. **Investment of Trust Assets.** Nothing in this trust instrument shall be construed to restrict the Trustee from investing the trust assets in a manner that could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets.

**SECTION 5. ANNOTATIONS REGARDING SAMPLE INTER VIVOS CHARITABLE REMAINDER ANNUITY TRUST — ONE LIFE**

.01 Annotations for Introductory Paragraph and Paragraph 1, Funding of Trust, of the Sample Trust.

1. **Factors concerning qualification of trust.** A deduction must be allowable under § 170, § 2055, or § 2522 for property contributed to the trust. Section 1.664-1(a)(1)(iii)(a) of the Income Tax Regulations. The trust must meet the definition of and function exclusively as a charitable remainder trust from the creation of the trust. Section 1.664-1(a)(4). Solely for purposes of § 664, a trust is deemed created at the earliest time that neither the grantor nor any other person is treated as the owner of the entire trust under subpart E, part 1, subchapter J, chapter 1, subtitle A of the Code (subpart E), but in no event prior to the time property is first transferred to the trust. Neither the donor nor the donor's spouse shall be treated as the owner of the trust under subpart E merely because he or she is named as a recipient of the annuity amount. Section 1.664-1(a)(4). In addition, funding the trust with certain types of assets may disqualify it as a charitable remainder trust. See § 1.664-1(a)(7) and Rev. Rul. 73-610, 1973-2 C.B. 213.

2. **Valuation of unmarketable assets.** If the trust is funded with unmarketable assets, the initial net fair market value of the assets must be determined exclusively by an independent trustee, as defined in § 1.664-1(a)(7)(iii), or must be determined by a current “qualified appraisal” from a “qualified appraiser,” as defined in § 1.170A-13(c)(3) and (c)(5), respectively. Section 1.664-1(a)(7).

3. **Income tax deductibility limitations.** The amount of the charitable deduction for income tax purposes is affected by a number of factors, including the type of property contributed to the trust, the type of charity receiving the property, whether the remainder interest is paid outright to charity or held in further trust, and the donor’s adjusted gross income (with certain adjustments). See § 170(b) and (e); § 1.170A-8; Rev. Rul. 80-38, 1980-1 C.B. 56; and Rev. Rul. 79-368, 1979-2 C.B. 109. See section 6.05 of this revenue procedure for an alternate provision that restricts the charitable remainderman to a public charity (as defined therein).

4. **Trustee provisions.** Alternate or successor trustees may be designated in the trust instrument. In addition, the trust instrument may contain other administrative provisions relating to the trustee’s duties and powers, as long as the provisions do not conflict with the rules governing charitable remainder trusts under § 664 and the regulations thereunder.
5. **Identity of donor.** For purposes of qualification under this revenue procedure, the donor may be an individual or a husband and wife. Appropriate adjustments should be made to the introductory paragraph if a husband and wife are the donors. Terms such as “grantor” or “settlor” may be substituted for “donor.”

.02 Annotations for Paragraph 2, Payment of Annuity Amount, of the Sample Trust.

1. **Permissible recipients.** For a CRAT with an annuity period based on the life of one individual, the annuity amount must generally be paid to that individual and the individual must be living at the time of the creation of the trust. See Rev. Rul. 2002-20, 2002-1 C.B. 794, for situations in which the annuity amount may be paid to a trust for the benefit of an individual who is financially disabled. An organization described in § 170(c) may receive part, but not all, of the annuity amount. Section 664(d)(1)(A) and § 1.664-2(a)(3)(i). See section 6.02 of this revenue procedure for an alternate provision that provides for payment of part of the annuity to an organization described in § 170(c).

2. **Percentage requirements.** The sum certain annuity amount must be at least 5 percent and not more than 50 percent of the initial net fair market value of the assets placed in trust. Section 664(d)(1)(A). Even if the sum certain annuity amount is at least 5 percent and not more than 50 percent of the initial net fair market value of the assets placed in trust, no deduction will be allowable under § 2055 or § 2522 if the probability that the trust corpus will be exhausted before the death of the recipient exceeds 5 percent. Rev. Rul. 77-374, 1977-2 C.B. 329 and Rev. Rul. 70-452, 1970-2 C.B. 199. See §§ 1.7520-3(b) and 25.7520-3(b) for special rules that may be applicable in valuing interests transferred to CRATs. In addition, the value (determined under § 7520) of the charitable remainder interest must be at least 10 percent of the initial net fair market value of all property placed in the trust. Section 664(d)(1)(D).

3. **Payment of annuity amount in installments.** Paragraph 2, Payment of Annuity Amount, of the sample trust specifies that the annuity amount is to be paid in equal quarterly installments at the end of each quarter. However, the trust instrument may specify that the annuity amount is to be paid to the recipient annually or in equal or unequal installments throughout the year. See § 1.664-2(a)(1)(i). The amount of the charitable deduction will be affected by the frequency of payment, by whether the installments are equal or unequal, and by whether each installment is payable at the beginning or end of the period. See § 1.664-2(c) and § 20.2031-7(d)(2)(iv).

4. **Payment of annuity amount by close of taxable year.** Generally, the annuity amount for any taxable year must be paid before the close of the taxable year for which it is due. For circumstances under which the annuity amount may be paid within a reasonable time after the close of the taxable year, see § 1.664-2(a)(1)(i)(a).

5. **Early distributions to charity.** The trust instrument may provide that an amount other than the annuity shall be paid (or may be paid in the discretion of the trustee) to an
organization described in § 170(c). If such a distribution is made in kind, the adjusted basis of the property distributed must be fairly representative of the adjusted basis of the property available for distribution on the date of distribution. Section 1.664-2(a)(4).

.03 Annotations for Paragraph 3, Proration of Annuity Amount, of the Sample Trust.

1. _Prorating annuity amount._ To compute the annuity amount in a short taxable year and in the taxable year in which the annuity period terminates, see § 1.664-2(a)(1)(iv)(a) and (b), respectively.
2. _Determining annuity amount payable in year of recipient’s death._ Paragraph 3, Proration of Annuity Amount, of the sample trust specifies that the annuity amount shall be prorated on a daily basis. See section 6.04 of this revenue procedure for an alternate provision that provides for the termination of the annuity amount with the last regular payment preceding the recipient’s death.

.04 Annotations for Paragraph 4, Distribution to Charity, of the Sample Trust.

1. _Minimum value of remainder._ As noted in section 5.02(2) of this revenue procedure, the value (determined under § 7520) of the charitable remainder interest is required to be at least 10 percent of the initial net fair market value of all property placed in the trust. Section 664(d)(1)(D).
2. _Designated remainderman._ Any named charitable remainderman must be an organization described in § 170(c) at the time of the transfer to the charitable remainder annuity trust. See § 664(d)(1)(C). Any named charitable remainderman also must be an organization described in § 2522(a) to qualify for the gift tax charitable deduction and an organization described in § 2055(a) to qualify for the estate tax charitable deduction. See Rev. Rul. 77-385, 1977-2 C.B. 331. If it is determined a deduction under § 2055(a) will not be necessary in any event, all references to § 2055(a) in the trust instrument may be deleted. The trust instrument may restrict the charitable remainderman to an organization described in §§ 170(c), 2055(a), and 2522(a), but grant to a trustee or other person the power to designate the actual charitable remainderman. The gift of the remainder interest will be incomplete for gift tax purposes if, for example: (i) the donor retains the power to substitute the charitable remainderman; or (ii) the trust instrument provides the trustee with the power to designate the charitable remainderman and the donor is not prohibited from serving as trustee. See § 25.2511-2(c). Note, however, that an income tax charitable deduction is available even if the donor has the authority to substitute the charitable remainderman or the trustee has the authority to designate the charitable remainderman.
Rev. Rul. 68-417, 1968-2 C.B. 103; Rev. Rul. 79-368, 1979-2 C.B. 109. See section 6.06 of this revenue procedure for an alternate provision in which the donor retains the right to substitute the charitable remainderman. See section 6.07 of this revenue procedure for an alternate provision in which the recipient is granted a power of appointment to designate the charitable remainderman.

3. Multiple remaindermen. The remainder interest may pass to more than one charitable organization as long as each organization is described in §§ 170(c), 2522(a), and, if needed, § 2055(a). Section 1.664-2(a)(6)(i).

4. Alternative remaindermen. The trust instrument of a CRAT must provide a means for selecting alternative charitable remaindermen in the event the designated organization is not qualified at the time any payments are to be made to it from the trust. Section 1.664-2(a)(6)(iv).

.05 Annotations for Paragraph 6, Prohibited Transactions, of the Sample Trust.

1. Payment of the annuity amount. Payment of the annuity amount to the recipient is not considered an act of self-dealing within the meaning of § 4941(d), as modified by § 4947(a)(2)(A), or a taxable expenditure within the meaning of § 4945(d), as modified by § 4947(a)(2)(A). Section 53.4947-1(c)(2) of the Foundation and Similar Excise Taxes Regulations.

2. Prohibitions against certain investments and excess business holdings. Prohibitions against investments that jeopardize the exempt purpose of the trust for purposes of § 4944, as modified by § 4947(a)(2)(A), and against retaining any excess business holdings for purposes of § 4943, as modified by § 4947(a)(2)(A), are required if the trust provides for payment of part of an annuity amount to an organization described in § 170(c) and gift and estate tax charitable deductions are sought for this interest. See § 4947(b)(3). See section 6.02 of this revenue procedure for an alternate provision that provides for payment of part of the annuity to an organization described in § 170(c).

3. Trust to continue in existence for benefit of charity. The governing instrument requirements of § 508(e) must be included in the trust instrument if, after the termination of the annuity period: (i) the trust instrument provides that the trust shall continue in existence for the benefit of the charitable remainderman and, as a result, the trust will become subject to the provisions of § 4947(a)(1); and (ii) the trust will be treated as a private foundation within the meaning of § 509(a), as modified by § 4947(a)(1). Except as provided in paragraph 6 of the sample trust, the trust instrument may limit the application of the provisions of § 508(e) to the period after the termination of the annuity period when the trust continues in existence for the benefit of the charitable remainderman. Note that when the trust provides for the trust corpus to be retained, in whole or in part, in trust for the charitable remainderman, the higher deductibility limitations in § 170(b)(1)(A) for the income tax charitable deduction will not be available (even if the charitable remainderman
is restricted to a public charity) because the contribution of the trust corpus is made “for the use of” rather than “to” the charitable remainderman. See § 1.170A-8(b).

SECTION 6. ALTERNATE PROVISIONS FOR SAMPLE INTER VIVOS CHARITABLE REMAINDER ANNUITY TRUST — ONE LIFE

.01 Annuity Amount Stated as a Specific Dollar Amount.

1. Explanation. As an alternative to stating the annuity amount as a fraction or percentage of the initial net fair market value of the assets transferred to the trust, the annuity amount may be stated as a specific dollar amount. Section 1.664-2(a)(1)(ii) and (iii). In either case, the annuity amount must be not less than 5 percent nor more than 50 percent of the initial net fair market value of all property placed in trust. Section 664(d)(1)(A).

2. Instructions for use.

   a. Replace the first sentence of paragraph 2, Payment of Annuity Amount, of the sample trust with the following sentence:

   • In each taxable year of the trust during the annuity period, the Trustee shall pay to [permissible recipient] (hereinafter “the Recipient”) an annuity amount equal to [the stated dollar amount].

   b. Delete the last sentence of paragraph 2, Payment of Annuity Amount, of the sample trust concerning the incorrect valuation of trust assets.

.02 Payment of Part of the Annuity to an Organization Described in § 170(c).

1. Explanation. An organization described in § 170(c) may receive part, but not all, of any annuity amount. Section 664(d)(1)(A). If a gift tax charitable deduction and, if needed, an estate tax charitable deduction are sought for the present value of the annuity interest passing to a charitable organization, the trust instrument must contain additional provisions. First, the trust instrument must specify the portion of each annuity payment that is payable to the noncharitable recipient and to the charitable organization described in §§ 170(c), 2522(a), and, if needed, § 2055(a). Second, the trust instrument must contain a means for selecting an alternative qualified charitable organization if the designated organization is not a qualified organization at the time when any annuity amount is to be paid to it. Third, the trust instrument must contain prohibitions against investments that jeopardize the exempt purpose of the trust for purposes of § 4944, as modified by §
4947(a)(2)(A), and against retaining any excess business holdings for purposes of § 4943, as modified by § 4947(a)(2)(A).

2. Instructions for use.

a. Replace paragraph 2, Payment of Annuity Amount, of the sample trust with the following paragraph:

- **Payment of Annuity Amount:** The annuity amount is equal to [a number no less than 5 and no more than 50] percent of the initial net fair market value of all property transferred to the trust, valued as of the above date (that is, the date of the transfer). In each taxable year of the trust during the annuity period, the Trustee shall pay [the percentage of the annuity amount payable to the noncharitable recipient] percent of the annuity amount to [permissible recipient] (hereinafter “the Recipient”); and [the percentage of the annuity amount payable to the charitable recipient] percent of the annuity amount to [an organization described in §§ 170(c), 2055(a), and 2522(a) of the Code] (hereinafter “the Charitable Recipient”). The first day of the annuity period shall be the date the property is transferred to the trust and the last day of the annuity period shall be the date of the Recipient’s death. If the Charitable Recipient is not an organization described in §§ 170(c), 2055(a), and 2522(a) of the Code at the time when any annuity payment is to be distributed to it, then the Trustee shall distribute that annuity payment to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) of the Code as the Trustee shall select, and in the proportions as the Trustee shall decide, in the Trustee’s sole discretion. The annuity amount shall be paid in equal quarterly installments at the end of each calendar quarter from income, and to the extent income is not sufficient, from principal. Any income of the trust for a taxable year in excess of the annuity amount shall be added to principal. If the initial net fair market value of the trust assets is incorrectly determined, then within a reasonable period after the value is finally determined for federal tax purposes, the Trustee shall pay to the Recipient and the Charitable Recipient (in the case of an undervaluation) or receive from the Recipient and the Charitable Recipient (in the case of an overvaluation) an amount equal to the difference between the annuity amount(s) properly payable and the annuity amount(s) actually paid.

b. Replace the first parenthetical in paragraph 4, Distribution to Charity, of the sample trust with the following parenthetical:

- (other than any amount due the Recipient or the Recipient’s estate and the Charitable Recipient under the provisions above).

c. Add the following sentence after the first and only sentence in paragraph 6, Prohibited Transactions, of the sample trust:

- The Trustee shall not make any investments that jeopardize the exempt purpose of the trust for purposes of § 4944 of the Code, as modified by § 4947(a)(2)(A) of
the Code, or retain any excess business holdings for purposes of § 4943 of the Code, as modified by § 4947(a)(2)(A) of the Code.

3.

.03 Qualified Contingency.

1. **Explanation.** Under § 664(f), payment of the annuity amount may terminate upon the earlier of the occurrence of a qualified contingency (as defined in § 664(f)(3)) or the death of the recipient. The amount of the charitable deduction, however, will be determined without regard to a qualified contingency. See § 664(f)(2).
2. **Instruction for use.** Replace the second sentence of paragraph 2, Payment of Annuity Amount, of the sample trust with the following sentence:
   
   o The first day of the annuity period shall be the date the property is transferred to the trust and the last day of the annuity period shall be the date of the Recipient’s death or, if earlier, the date on which occurs the [qualified contingency].

.04 Last Annuity Payment to the Recipient.

1. **Explanation.** As an alternative to prorating the annuity amount in the taxable year of the recipient’s death, payment of the annuity amount may terminate with the last regular payment preceding the recipient’s death. However, the fact that the recipient may not receive the last payment shall not be taken into account for purposes of determining the present value of the remainder interest. Section 1.664-2(a)(5)(i).
2. **Instruction for use.** Replace the second sentence of paragraph 3, Proration of Annuity Amount, of the sample trust with the following sentence:
   
   o In the taxable year of the trust during which the annuity period ends, the obligation of the Trustee to pay the annuity amount shall terminate with the regular quarterly installment next preceding the death of the Recipient.

.05 Restricting the Charitable Remainderman to a Public Charity.
1. **Explanation.** The amount of the donor’s income tax charitable deduction is more limited for gifts to certain private foundations than for other charitable organizations. Specifically, charitable organizations described in § 170(c) include private foundations that are not described in § 170(b)(1)(E). See § 170(b) and Rev. Rul. 79-368, 1979-2 C.B. 109. To avoid these more restrictive limitations, a donor of an inter vivos CRAT may wish to restrict the charitable remainderman to an organization that is described in § 170(b)(1)(A) as well as §§ 170(c), 2055(a), and 2522(a) (referred to herein as a “public charity”).

2. **Instruction for use.** To restrict the charitable remainderman to a public charity, each and every time the phrase “an organization described in §§ 170(c), 2055(a), and 2522(a) of the Code” appears in the sample trust, replace it with the phrase “an organization described in §§ 170(b)(1)(A), 170(c), 2055(a), and 2522(a) of the Code.”

.06 Retaining the Right to Substitute the Charitable Remainderman.

1. **Explanation.** The donor may retain the right to substitute another charitable remainderman for the charitable remainderman named in the trust instrument. See Rev. Rul. 76-8, 1976-1 C.B. 179. Note, however, that the retention of this right will cause the gift of the remainder interest to be incomplete for gift tax purposes. See § 25.2511-2(c) and Rev. Rul. 77-275, 1977-2 C.B. 346.

2. **Instruction for use.** Insert the following sentence between the first and last sentences of paragraph 4, Distribution to Charity, of the sample trust:

   - The Donor reserves the right to designate, at any time and from time to time, in lieu of the Charitable Organization identified above, one or more organizations described in §§ 170(c), 2055(a), and 2522(a) of the Code as the charitable remainderman and shall make any such designation by giving written notice to the Trustee.

.07 Power of Appointment to Designate the Charitable Remainderman.

1. **Explanation.** The trust instrument may grant the recipient a power of appointment to designate the charitable remainderman. See Rev. Rul. 76-7, 1976-1 C.B. 179.

2. **Instruction for use.** Replace paragraph 4, Distribution to Charity, of the sample trust with the following paragraph:

   - **Distribution to Charity.** At the termination of the annuity period, the Trustee shall distribute all of the then principal and income of the trust (other than any amount due the Recipient or the Recipient’s estate under the provisions above) to one or more charitable organizations described in §§ 170(c), 2055(a), and 2522(a) of the Code as the Recipient shall appoint and direct by specific reference to this power of appointment by
inter vivos or testamentary instrument. To the extent the Recipient fails to effectively exercise the power of appointment, the principal and income not effectively appointed shall be distributed to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) of the Code as the Trustee shall select, and in the proportions as the Trustee shall decide, in the Trustee’s sole discretion. If an organization fails to qualify as an organization described in §§ 170(c), 2055(a), and 2522(a) of the Code at the time when any principal or income of the trust is to be distributed to it, then the Trustee shall distribute the then principal and income to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) of the Code as the Trustee shall select, and in the proportions as the Trustee shall decide, in the Trustee’s sole discretion.

SECTION 7. EFFECT ON OTHER REVENUE PROCEDURES

DRAFTING INFORMATION
The principal authors of this revenue procedure are Karlene M. Lesho and Stephanie N. Bland of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure, contact Karlene M. Lesho or Stephanie N. Bland at (202) 622-7830 (not a toll-free call).
SECTION 1. PURPOSE
This revenue procedure contains annotated sample declarations of trust and alternate provisions that meet the requirements for an inter vivos charitable lead unitrust (CLUT) providing for unitrust payments payable to one or more charitable beneficiaries for the unitrust period followed by the distribution of trust assets to one or more noncharitable remaindermen.

SECTION 2. BACKGROUND
The Internal Revenue Service (Service) is issuing sample forms for CLUTs; annotations and alternate sample provisions are included as further guidance. In addition to the sample trust instruments for inter vivos CLUTs that are included in this revenue procedure, a sample is provided in a separate revenue procedure for a testamentary CLUT (see Rev. Proc. 2008-46).

SECTION 3. SCOPE
A CLUT is an irrevocable split-interest trust that provides for a specified amount to be paid to one or more charitable beneficiaries during the term of the trust. The principal remaining in the trust at the end of the term is paid over to, or held in a continuing trust for, a noncharitable beneficiary or beneficiaries identified in the trust. If the terms of a CLUT created during the donor’s life satisfy the applicable statutory and regulatory requirements, a gift of the charitable lead unitrust interest will qualify for the gift tax charitable deduction under § 2522(c)(2)(B) and/or the estate tax charitable deduction under § 2055(e)(2)(B). In certain cases, the gift of the unitrust interest may also qualify for the income tax charitable deduction under § 170(a). The value of the remainder interest is a taxable gift by the donor at the time of the donor’s contribution to the trust.

There are two types of inter vivos CLUTs: a “nongrantor CLUT” and a “grantor CLUT.” The income tax consequences are different for each. A nongrantor CLUT is subject to the provisions of part I, subchapter J of chapter 1 of subtitle A of the Internal Revenue Code (Code). Under the provisions of part I of subchapter J, a nongrantor CLUT is allowed a deduction under § 642(c)(1) in determining its taxable income for any amount of gross income paid for purposes specified in § 170(c). Generally, the donor is not entitled to any income tax charitable deduction.

Section 4 of this revenue procedure provides a sample declaration of trust for a nongrantor CLUT with a term of years unitrust period that is created by an individual who is a citizen or resident of the United States. Section 5 of this revenue procedure provides annotations to the provisions of the sample trust. Section 6 of this revenue procedure provides samples of certain alternate provisions concerning: (.01) a unitrust period for the life of one individual; (.02) retention of the right to substitute the charitable lead beneficiary; (.03) apportionment of the unitrust amount in the discretion of the trustee; and (.04) designation of an alternate charitable beneficiary in the trust instrument. If a trust is substantially similar to the sample trust in section 4 of this revenue procedure or properly integrates one or more alternate
provisions from section 6 into a document substantially similar to the sample trust in section 4, is a valid trust under applicable local law, and operates in a manner consistent with the terms of the instrument, and if all other deductibility requirements are satisfied, the value of the charitable lead interest will be deductible under § 2522(c)(2)(B) and/or § 2055(e)(2)(B) and payments of the unitrust amount to the charitable lead beneficiary will be deductible from the gross income of the trust to the extent provided by § 642(c)(1). In addition, a nongrantor CLUT will qualify for the safe harbor created under this revenue procedure if the trust satisfies all of the requirements set forth in the preceding sentence, except that it defines the unitrust amount as a varying percentage amount for which the value is ascertainable at the creation of the trust and/or provides for a different disposition of trust assets upon the termination of the unitrust period.

A CLUT is a grantor CLUT if the donor, who is a citizen or resident of the United States, is treated as the owner of the entire CLUT under subpart E, part I of subchapter J, chapter 1, subtitle A. The value of the charitable lead unitrust interest in a grantor CLUT may be deductible by the donor under § 170(a) for the year in which the donor made the contribution to the trust, provided that the other requirements of § 170(f)(2)(B) and the regulations thereunder are satisfied. During the term of the grantor CLUT, all trust income and capital gains are taxed to the donor and the donor is entitled to no further charitable deduction for income tax purposes as the charitable unitrust payments are made to charitable organizations each year.

Section 7 of this revenue procedure provides a sample declaration of trust for a grantor CLUT that is created by an individual who is a citizen or resident of the United States. Section 8 of this revenue procedure provides annotations to the provisions of the sample trust. Section 9 of this revenue procedure provides samples of certain alternate provisions concerning: (.01) a unitrust period for the life of one individual; (.02) retention of the right to substitute the charitable lead beneficiary; (.03) apportionment of the unitrust amount in the discretion of the trustee; and (.04) designation of an alternate charitable beneficiary in the trust instrument. If a trust is substantially similar to the sample trust in section 7 of this revenue procedure or properly integrates one or more alternate provisions from section 9 into a document substantially similar to the sample trust in section 7, is a valid trust under applicable local law, and operates in a manner consistent with the terms of the instrument, and if all other requirements for deductibility are satisfied, the value of the charitable lead unitrust interest will be deductible under §§ 170(a), 2522(c)(2)(B) and/or 2055(e)(2)(B). In addition, a grantor CLUT will qualify for the safe harbor created under this revenue procedure if the trust satisfies all of the requirements set forth in the preceding sentence, except that it: (i) reflects the choice of a different power or provision sufficient to make the donor the owner of the entire CLUT under subpart E, part I, subchapter J, chapter 1, subtitle A, provided that the power or provision selected is consistent with the requirements of a CLUT; (ii) defines the unitrust amount as a varying percentage amount for which the value is ascertainable at the creation of the trust; and/or (iii) provides for a different disposition of trust assets upon the termination of the unitrust period.
Except as provided above, a trust that contains substantive provisions in addition to those provided in section 4 or section 7 of this revenue procedure (other than properly integrated alternate provisions from section 6 or section 9, respectively, of this revenue procedure or provisions necessary to establish a valid trust under applicable local law that are not inconsistent with the applicable federal tax requirements), or that omits any of the provisions of section 4 or section 7 of this revenue procedure (unless an alternate provision from section 6 or section 9, respectively, of this revenue procedure is properly integrated), will not necessarily be ineligible for the relevant charitable deduction(s), but neither will that trust (or contributions to it) be assured of qualification for the appropriate charitable deductions. The Service generally will not issue a letter ruling on whether an inter vivos CLUT created by an individual qualifies for income, estate, and/or gift tax charitable deductions. The Service, however, generally will issue letter rulings relating to the tax consequences of the inclusion in a CLUT of substantive trust provisions other than those contained in sections 4, 6, 7, and 9 of this revenue procedure.

SECTION 4. SAMPLE INTER VIVOS NONGRANTOR CHARITABLE LEAD UNITRUST
On this day of , 20__, (hereinafter “the Donor”), desiring to establish a charitable lead unitrust within the meaning of Rev. Proc. 2008-45, hereby enter into this trust agreement with as the initial trustee (hereinafter “the Trustee”). This trust shall be known as the Nongrantor Charitable Lead Unitrust. All references to “section” or “§” in this instrument shall refer to the Internal Revenue Code of 1986, 26 U.S.C. § 1, et seq.

1. Funding of Trust. The Donor hereby transfers and irrevocably assigns to the Trustee on the above date the property described in Schedule A, and the Trustee accepts the property and agrees to hold, manage, and distribute the property under the terms set forth in this trust instrument.

2. Payment of Unitrust Amount. For each taxable year of the trust during the unitrust period, the Trustee shall pay to [designated charitable recipient] a unitrust amount equal to [number representing the annual unitrust percentage to be paid to the designated charitable recipient] percent of the net fair market value of the assets of the trust, valued as of the first day of each taxable year of the trust (hereinafter “the valuation date”). If [designated charitable recipient] is not an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the Trustee shall instead distribute such payments to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the Trustee shall select, and in such proportions as the Trustee shall decide, from time to time, in the Trustee’s sole discretion. The term “the Charitable Organization” shall be used herein to refer collectively to the organization(s) then constituting the charitable recipient, whether named in this paragraph or subsequently selected as the substitute charitable recipient. During the trust term, no payment shall be made to any person other than the Charitable Organization. The unitrust period is a term of [number of years of unitrust period] years. The first day of the unitrust period shall be the date property is first transferred to the trust, and the last day of the unitrust period shall be the day preceding the [ordinal number corresponding to the length of the unitrust period] anniversary of that date. The unitrust amount shall be paid in
equal quarterly installments at the end of each calendar quarter from income and, to the extent income is not sufficient, from principal. Any income of the trust for a taxable year in excess of the unitrust amount shall be added to principal. If for any year the net fair market value of the trust assets is incorrectly determined, then within a reasonable period after the correct value is finally determined, the Trustee shall pay to the Charitable Organization (in the case of an undervaluation) or receive from the Charitable Organization (in the case of an overvaluation) an amount equal to the difference between the unitrust amount(s) properly payable and the unitrust amount(s) actually paid.

3. **Proration of Unitrust Amount.** For a short taxable year and for the taxable year during which the unitrust period ends, the Trustee shall prorate on a daily basis for the number of days of the unitrust period in that year, the unitrust amount described in paragraph 2, or, if an additional contribution is made to the trust, the unitrust amount described in paragraph 5.

4. **Distribution Upon Termination of Unitrust Period.** At the termination of the unitrust period, the Trustee shall distribute all of the then remaining principal and income of the trust (other than any amount due to the Charitable Organization under the provisions above) to [remainder beneficiary].

5. **Additional Contributions.** If any additional contributions are made to the trust after the initial contribution, the unitrust amount for the year in which any additional contribution is made shall be [same percentage used in paragraph 2] percent of the sum of (a) the net fair market value of the trust assets as of the valuation date (excluding the assets so added and any post-contribution income from, and appreciation on, such assets during that year) and (b) for each additional contribution during the year, the fair market value of the assets so added as of the valuation date (including any post-contribution income from, and appreciation on, such assets through the valuation date) multiplied by a fraction the numerator of which is the number of days in the period that begins with the date of contribution and ends with the earlier of the last day of the taxable year or the last day of the unitrust period and the denominator of which is the number of days in the period that begins with the first day of such taxable year and ends with the earlier of the last day in such taxable year or the last day of the unitrust period. In a taxable year in which an additional contribution is made on or after the valuation date, the assets so added shall be valued as of the date of contribution, without regard to any post-contribution income or appreciation, rather than as of the valuation date.

6. **Prohibited Transactions.** The Trustee shall not engage in any act of self-dealing within the meaning of § 4941(d), as modified by § 4947(a)(2), and shall not make any taxable expenditures within the meaning of § 4945(d), as modified by § 4947(a)(2). The Trustee shall not retain any excess business holdings that would subject the trust to tax under § 4943, as modified by §§ 4947(a)(2) and 4947(b)(3). In addition, the Trustee shall not acquire any assets that would subject the trust to tax under § 4944, as modified by §§ 4947(a)(2) and 4947(b)(3), or retain assets which, if acquired by the Trustee, would subject the Trustee to tax under § 4944, as modified by §§ 4947(a)(2) and 4947(b)(3).
7. **Taxable Year.** The taxable year of the trust shall be the calendar year.

8. **Governing Law.** The operation of the trust shall be governed by the laws of the State of . However, the Trustee is prohibited from exercising any power or discretion granted under said laws that would be inconsistent with the requirements for the charitable deductions available to a charitable lead unitrust or for contributions to a charitable lead unitrust.

9. **Limited Power of Amendment.** This trust is irrevocable. However, the Trustee shall have the power, acting alone, to amend the trust from time to time in any manner required for the sole purpose of ensuring that the unitrust interest passing to the Charitable Organization is a unitrust interest under §§ 2055(e)(2)(B) and 2522(c)(2)(B) and the regulations thereunder and that payments of the unitrust amount to the Charitable Organization will be deductible from the gross income of the trust to the extent provided by § 642(c)(1) and the regulations thereunder.

10. **Investment of Trust Assets.** Except as provided in paragraph 6 herein, nothing in this trust instrument shall be construed to restrict the Trustee from investing the trust assets in a manner that could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets.

11. **Retained Powers and Interests.** Notwithstanding any other provision of this trust instrument to the contrary, no person shall hold any power or possess any interest that would cause the Donor to be treated as the owner of any portion of the trust under the provisions of subpart E, part I, subchapter J, chapter 1, subtitle A of the Internal Revenue Code.

## SECTION 5. ANNOTATIONS REGARDING SAMPLE INTER VIVOS NONGRANTOR CHARITABLE LEAD UNITRUST

### .01 Annotations for Introductory Paragraph and Paragraph 1, Funding of Trust, of the Sample Trust in Section 4.

1. **Types of charitable lead trusts.** An inter vivos charitable lead trust may be established as either a grantor charitable lead trust or a nongrantor charitable lead trust. The sample trust in section 4 is an example of a nongrantor charitable lead trust. The sample trust in section 7 is an example of a grantor charitable lead trust.

2. **Income taxation of nongrantor charitable lead trusts.** A nongrantor CLUT is a complex trust that is taxable as a separate entity under the provisions of subchapter J of the Code. The trustee of the trust must apply for a tax identification number for the trust.

3. **Deduction under § 642(c)(1) available for amounts paid for a charitable purpose.** Under § 642(c)(1), a nongrantor CLUT is allowed a deduction in computing its taxable income for any amount of gross income, without limitation, that under the terms of the trust instrument is paid for a purpose specified in § 170(c) (determined without regard to § 170(c)(2)(A)) during the taxable year. This deduction is in lieu of the charitable deduction allowed by § 170. Section 642(c)(1) and § 1.642(c)-1(a). An amount paid to a corporation, trust, or community chest, fund, or foundation otherwise described in § 170(c)(2) shall be considered paid for a purpose described in § 170(c) even though the corporation, trust, or
community chest, fund, or foundation is not created or organized in the United States, any state, the District of Columbia, or any possession of the United States. Section 1.642(c)-1(a)(2). With regard to amounts of income paid to the charitable beneficiary after the close of the taxable year in which the income was received (but on or before the last day of the next succeeding taxable year), the trustee of a nongrantor CLUT may elect to take the charitable deduction for that payment for the year in which the income was received, rather than for the year in which the payment was made. Section 642(c)(1). The election is made by filing a statement with the income tax return for the taxable year in which the charitable contribution is treated as paid. See §1.642(c)-1(b).

4. **Charitable lead beneficiary requirements.** A deduction is allowed under §642(c)(1) for any amount of the gross income of a nongrantor CLUT that is paid for a purpose specified in §170(c). Note that the class of permissible charitable recipients for obtaining a deduction under §642(c)(1) differs from the class of permissible charitable recipients for obtaining a deduction under §170(a). Compare §170(c) and §1.642(c)-1(a)(2).

5. **Unrelated business taxable income.** Under §681, a nongrantor charitable lead trust’s deduction under §642(c)(1) is disallowed in any year to the extent that the deduction is allocable to the trust’s unrelated business taxable income, as defined in §512, for that taxable year. See §1.681(a)-2. However, a partial deduction is allowed under §512(b)(11) for amounts allocable to unrelated business taxable income. Section 512(b)(11). See §512(b)(12) and §1.681(a)-2(a).

6. **Computation of estate and gift tax charitable deductions.** In general, the estate and gift tax charitable deductions available under §§2055(e)(2)(B) and 2522(c)(2)(B) with respect to contributions to a CLUT are equal to the present value of the unitrust interest. Sections 20.2055-2(f)(1) and 25.2522(c)-3(d)(1). Section 7520 requires that a unitrust interest must be valued using tables published by the Service. The method for valuing a charitable lead unitrust interest is set forth in the regulations. See §§20.7520-2 and 25.7520-2.

7. **Trustee provisions.** The trust instrument may name alternate or successor trustees and/or may include a process for the appointment of unnamed alternate or successor trustees. In addition, the trust instrument may contain certain administrative provisions relating to the trustee’s duties and powers.

8. **Identity of donor.** For purposes of qualification under this revenue procedure, the donor may be an individual or a husband and wife. Appropriate adjustments should be made to the introductory paragraph if a husband and wife are the donors. Terms such as “grantor” or “settlor” may be substituted for “donor.”

.02 Annotations for Paragraph 2, Payment of Unitrust Amount, of the Sample Trust in Section 4.

1. **Unitrust interest.** To qualify for the applicable estate and gift tax charitable deductions, a nongrantor CLUT must provide for the payment of a unitrust amount at least annually to a qualified charitable organization for each year during the unitrust period. See §§ 2055(e)(2)(B) and 2522(c)(2)(B). A unitrust interest is the right pursuant to the
instrument of transfer to receive payment, not less often than annually, of a fixed percentage of the net fair market value, determined annually, of the property that funds the unitrust interest. Payments of a unitrust interest may be paid for a specified term or for the life or lives of certain individuals, each of whom must be living at the date of the transfer and can be ascertained as of such date. Sections 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a). See section 5.02(4) for a discussion of the permissible term of a nongrantor CLUT. An interest is a unitrust interest only if it is a unitrust interest in every respect. For example, if an interest is expressed as the right to receive an annual payment from a trust equal to the lesser of a sum certain or a fixed percentage of the net fair market value of the trust assets (determined annually), the interest is not a unitrust interest. Sections 20.2055-2(e)(2)(vii)(b) and 25.2522(c)-3(c)(2)(vii)(b). See Rev. Rul. 77-300, 1977-2 C.B. 352. In addition, an interest is not a unitrust interest if the trustee has the discretion to commute and prepay the interest prior to the termination of the unitrust period. Rev. Rul. 88-27, 1988-1 C.B. 331. If a charitable interest in the form of a unitrust interest is in trust and the present value of the charitable interest on the date of gift exceeds 60 percent of the aggregate value of all amounts in the trust, the charitable interest will not be considered a unitrust interest unless the governing instrument of the trust prohibits the acquisition and retention of assets that would give rise to a tax under § 4943 or 4944, as modified by §§ 4947(a)(2) and 4947(b)(3). Section 4947(b)(3) and § 53.4947-2(b)(1)(i). See §§ 20.2055-2(e)(2)(vii)(f) and 25.2522(c)-3(c)(2)(vii)(f). These prohibitions are contained in the sample trust in section 4. See section 5.06 for a further discussion of the 60 percent test.

2. Payment requirements. CLUTs are not subject to any minimum or maximum payout requirements. The governing instrument of a CLUT must provide for the payment to a charitable organization, not less often than annually, of a fixed percentage of the net fair market value of the assets of the trust, valued annually. Alternatively, the governing instrument of a CLUT may provide for a unitrust amount that is initially stated as a fixed percentage amount but increases or decreases during the unitrust period, provided that the value of the unitrust interest is ascertainable at the time the trust is funded. The unitrust payments may be made in cash or in kind. If the trustee distributes appreciated property in satisfaction of the required unitrust payment, the trust will realize capital gain on the assets distributed to satisfy part or all of the unitrust payment and the trust will be allowed a § 642(c)(1) deduction for the realized capital gains. Rev. Rul. 83-75, 1983-1 C.B. 114.

3. Rule against perpetuities. An interest payable for a specified term of years may qualify as a unitrust interest even if the governing instrument contains a savings clause intended to ensure compliance with a rule against perpetuities. However, any such savings clause must utilize a period of vesting of not more than 21 years after the deaths of measuring lives who are selected to maximize, rather than limit, the term of the trust. Sections 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a).

4. Permissible term. Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 provides for payment of the unitrust amount for a specified term of years. Alternatively, the trust instrument may provide for payment of the unitrust amount for the
life or lives of one or more measuring lives or for the life or lives of one or more measuring lives plus a term of years. Rev. Rul. 85-49, 1985-1 C.B. 330. Only one or more of the following individuals may be used as measuring lives: the donor, the donor’s spouse, and an individual who, with respect to all remainder beneficiaries (other than charitable organizations described in § 170, 2055, or 2522), is either a lineal ancestor or the spouse of a lineal ancestor of those beneficiaries. Each person used as a measuring life for the unitrust period must be living on the date assets are transferred to the trust. Sections 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a). See section 6.01 for an alternate provision that provides for a unitrust period based on the life of an individual.

5. **Permissible recipients.** A CLUT must have one or more charitable lead beneficiaries. The failure to designate a specific charitable beneficiary will not preclude the donor from receiving a charitable deduction if the trust instrument provides for the selection by the trustee of a charitable beneficiary described in §§ 170(c), 2055(a), and 2522(a). Rev. Rul. 78-101, 1978-1 C.B. 301. If it is determined that a deduction under § 2055(a) will not be necessary in any event, all references to § 2055(a) in the trust instrument may be deleted. Note that if the donor is serving as trustee of the trust, the trustee’s power to select the charitable beneficiaries will cause the gift of the unitrust interest to be incomplete for gift tax purposes and will cause some or all of the trust property (depending on the date of the donor’s death) to be included in the donor’s gross estate. See §§ 2035(a), 2036(a)(2), and 2038(a)(1) and § 25.2511-2(c). Further note that if the charitable beneficiary is a private foundation and the donor is an officer or director of the private foundation or possesses certain decision making authority in the private foundation, some or all of the trust property may be included in the donor’s gross estate. See § 2036(a)(2). See section 6.02 for an alternate provision that provides for a donor’s retained right to substitute the charitable beneficiary. See section 6.03 for an alternate provision that provides the trustee with the power to apportion the unitrust amount among charitable beneficiaries. See section 6.04 for an alternate provision that provides for the designation of an alternate charitable beneficiary in the trust instrument.

6. **Payment of unitrust amount in installments.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 specifies that the unitrust amount is to be paid in equal quarterly installments at the end of each calendar quarter. Alternatively, the trust instrument may specify that the unitrust amount is to be paid in annual or other equal or unequal installments throughout the year. See §§ 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a). The amount of the charitable deduction will be affected by the frequency of the payment, by whether the installments are equal or unequal, and by whether each installment is payable at the beginning or end of the period. See §§ 25.2512-5 and 20.2031-7.

7. **Excess income.** Trust income in excess of the amount required to pay the unitrust amount may be retained by the trust or distributed currently to the charitable beneficiary. The sample trust in section 4 provides for the retention of excess income by the trust. If, instead, the governing instrument of a nongrantor charitable lead trust provides for the payment of excess income to or for the use of the charitable beneficiary, no additional
estate or gift tax charitable deductions are available for the excess amounts of income distributed to the charitable beneficiary. See §§ 20.2055-2(e)(2)(vii)(d) and 25.2522(c)-3(c)(2)(vii)(d). However, the trust is entitled to a charitable income tax deduction under § 642(c)(1) for any amounts of excess income paid to the charitable beneficiary. See Situation 2 of Rev. Rul. 88-82, 1988-2 C.B. 336, for the gift tax consequences of the payment of excess income to a noncharitable beneficiary. See section 5.06 for the private foundation rules applicable to charitable lead trusts.

8. **Payment of part of unitrust for private purposes.** In general, no part of a charitable lead unitrust interest may be payable for a private purpose before the expiration of all charitable lead unitrust interests. However, there are two exceptions to this rule. The first exception arises when the amount payable for a private purpose is in the form of a unitrust interest and the trust's governing instrument does not provide for any preference or priority in the payment of the private unitrust as opposed to the charitable unitrust. The second exception arises when, under the trust's governing instrument, the amount that may be paid for a private purpose is payable only from a group of assets that is devoted exclusively to private purposes and to which § 4947(a)(2) is inapplicable by reason of § 4947(a)(2)(B). Note that an amount is not deemed to have been paid for a private purpose if it was paid for full and adequate consideration in money or money's worth. Sections 20.2055-2(e)(2)(vii)(e) and 25.2522(c)-3(c)(2)(vii)(e). See section 5.06 for the private foundation rules applicable to charitable lead trusts.

9. **Valuation date.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 specifies that the net fair market value of trust assets is to be valued as of the first day of each taxable year of the trust. However, the value of the trust assets may be determined on any one date during the taxable year of the trust, or by taking the average of valuations made on more than one date during the taxable year of the trust, so long as the same valuation date or dates and the same valuation methods are used each year. If the governing instrument does not specify the valuation date or dates, the trustee must select the date or dates and indicate the selection on the first Form 1041, *U.S. Income Tax Return for Estates and Trusts*, that the trust must file. Sections 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a). Note that if the valuation date is a date other than the first day of each taxable year of the trust, it may be necessary to modify the provisions in the sample trust regarding: (i) the timing of the payment of the unitrust amount; (ii) the proration of the unitrust amount in a short taxable year and the last taxable year of the unitrust period; and (iii) additional contributions.

10. **Ordering rules.** A provision in the governing instrument of a charitable lead trust that provides for the payment to charity to consist of different classes of income determined on a non pro rata basis will not be respected because such a provision does not have economic effect independent of the income tax consequences of the payment. See § 1.642(c)-3(b)(2) and (3).

**.03 Annotation for Paragraph 3, Proration of Unitrust Amount, of the Sample Trust in Section 4.**
1. **Prorating the unitrust amount.** Paragraph 3, Proration of Unitrust Amount, of the sample trust in section 4 provides for the proration of the unitrust amount in any short taxable year, including the last year of the unitrust period.

**.04 Annotation for Paragraph 4, Distribution Upon Termination of Unitrust Period, of the Sample Trust in Section 4.**

1. **Generation-skipping transfer tax.** The generation-skipping transfer (GST) tax may apply if a CLUT has or may have a skip person, as defined in § 2613(a), as a remainder beneficiary. Under § 2651(f)(3), a charitable organization is deemed to be in the same generation as the donor to a charitable lead trust. Therefore, the GST potential of a charitable lead trust is dependent upon whether any noncharitable beneficiary is a skip person. GST tax liability is determined by multiplying the taxable amount by the applicable rate. The applicable rate is the inclusion ratio multiplied by the maximum federal estate tax rate. Section 2641(a). Note that the rules set forth in § 2642(e) for determining the inclusion ratio of certain charitable lead trusts do not apply to CLUTs.

**.05 Annotation for Paragraph 5, Additional Contributions, of the Sample Trust in Section 4.**

1. **Identity of additional contributors.** For purposes of qualification under this revenue procedure, only a donor or a donor’s estate may make an additional contribution to the trust. See section 5.01(8) of this revenue procedure for examples of who may be a donor of a CLUT.

2. **Option to prohibit additional contributions.** Paragraph 5, Additional Contributions, of the sample trust in section 4 provides rules for determining the unitrust amount payable in a year during which an additional contribution is made to the trust. However, paragraph 5 of the trust instrument may instead be drafted to prohibit contributions to the trust after the initial contribution.

3. **Proration of additional contributions.** Paragraph 5, Additional Contributions, of the sample trust in section 4 provides a formula for determining the unitrust amount in each year that an additional contribution is made to the CLUT. The formula incorporates a proration provision for additions made in a short taxable year.

4. **Valuation date in year of additional contribution.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 specifies a January 1 valuation date for the trust. The formula contained in paragraph 5, Additional Contributions, of the sample trust may be used when January 1 or any other single date during the taxable year is selected as the valuation date for a CLUT. Note, however, that if a single date other than January 1 is selected as the valuation date for a CLUT, the formulas in both paragraphs 2 and 5 of the sample trust for computing the unitrust amount will be deficient unless the trust instrument addresses the possibility that the unitrust period may end before the valuation date, for instance, by providing that in a year in which the unitrust period ends before the valuation date, the valuation date for purposes of paragraph 2 and paragraph 5 shall be the last day of the unitrust period. In addition, if the trust instrument is drafted to provide for
the valuation of trust assets by averaging the valuations as of multiple specified dates during the trust year, the additional contributions formula must be modified.

.06 Annotation for Paragraph 6, Prohibited Transactions, of the Sample Trust in Section 4.

1. Prohibitions against certain investments and excess business holdings. Prohibitions against retaining any excess business holdings within the meaning of § 4943, as modified by §§ 4947(a)(2) and 4947(b)(3), and against investments that jeopardize the exempt purpose of the trust within the meaning of § 4944, as modified by §§ 4947(a)(2) and 4947(b)(3), are generally required. The sample trust in section 4 contains prohibitions against §§ 4943 and 4944 transactions. If the present value of the charitable interest does not exceed 60 percent of the aggregate value of all amounts in the trust, the trust instrument does not provide for the payment of any of the income interest to a noncharitable beneficiary, and the trust instrument does not provide for the payment of excess income to a noncharitable beneficiary, the references to §§ 4943 and 4944 may be removed from the trust instrument. Section 4947(b)(3) and § 53.4947-2(b)(1)(i). See §§ 20.2055-2(e)(2)(vii)(A) and 25.2522(c)-3(c)(2)(vii)(A). See section 5.02(7) for a discussion of the payment of excess trust income to a noncharitable beneficiary. See section 5.02(8) for a discussion of the payment of part of the unitrust for a private purpose.

.07 Annotation for paragraph 7, Taxable Year, of the Sample Trust in Section 4.

1. Calendar year. The taxable year of a charitable lead trust must be a calendar year. Section 644(a).

.08 Annotation for paragraph 10, Investment of Trust Assets, of the Sample Trust in Section 4.

1. Capital gains. Gains from the sale or exchange of capital assets may be allocated to the income or the principal of the trust. If the governing instrument is silent, capital gains are allocated in accordance with local law. Even if gains are allocated to principal, they will be deductible under § 642(c)(1) if they are paid to the charitable beneficiary as part of a charitable unitrust payment. Rev. Rul. 83-75, 1983-1 C.B. 114.

.09 Annotation for paragraph 11, Retained Powers and Interests, of the Sample Trust in Section 4.

1. Trust not a grantor trust. Paragraph 11, Retained Powers and Interests, of the sample trust in section 4 prohibits any person from holding any power or possessing any interest that would cause the donor to be treated as the owner of the trust under subpart E, part I, subchapter J, chapter 1, subtitle A of the Code. This prohibition should be included only in nongrantor charitable lead trusts. See section 7 for a sample grantor CLUT.
SECTION 6. ALTERNATE PROVISIONS FOR SAMPLE INTER VIVOS NONGRANTOR CHARITABLE LEAD UNITRUST

.01 Unitrust Period for the Life of One Individual.

1. *Explanation.* As an alternative to establishing a CLUT for a term of years, the trust instrument of a nongrantor CLUT may provide for payment of the unitrust amount for the life or lives of an individual or individuals. However, only one or more of the following individuals may be used as measuring lives: the donor, the donor’s spouse, and an individual who, with respect to all remainder beneficiaries (other than charitable organizations described in § 170, 2055, or 2522), is either a lineal ancestor or the spouse of a lineal ancestor of those beneficiaries. A trust will satisfy the requirement that each measuring life is a lineal ancestor (or the spouse of a lineal ancestor) of all noncharitable remainder beneficiaries if there is a less than 15 percent probability at the time of the contribution to the trust that individuals who are not lineal descendants of an individual who is a measuring life will receive any trust principal. The probability must be computed under the applicable tables in § 20.2031-7. Sections 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a).

2. *Instruction for use.* Replace the fifth and sixth sentences of paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 with the following sentences:

The unitrust period is the lifetime of [designated measuring life]. The first day of the unitrust period shall be the date property is first transferred to the trust and the last day of the unitrust period shall be the date of death of [designated measuring life].

.02 Retention of the Right to Substitute the Charitable Lead Beneficiary.

1. *Explanation.* The donor to a nongrantor CLUT may retain the right to substitute another charitable beneficiary for the charitable beneficiary named in the trust instrument. Note, however, that the retention of this right will cause the gift of the unitrust interest to be incomplete for gift tax purposes and will cause some or all of the trust property (depending upon the date of the donor’s death) to be included in the donor’s gross estate. See §§ 2035(a), 2036(a)(2), and 2038(a)(1) and § 25.2511-2(c).

2. *Instruction for use.* Replace the third sentence of paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 with the following two sentences:

Notwithstanding the preceding sentences, the Donor reserves the right to designate as the charitable recipient, at any time and from time to time, in lieu of [designated charitable recipient], one or more organizations described in §§ 170(c), 2055(a), and 2522(a) and shall make any such designation by giving written notice to the Trustee. The term “the Charitable Organization” shall be used herein to refer collectively to the organization(s) then constituting the charitable recipient, whether named in this paragraph or subsequently selected as the substitute charitable recipient.

.03 Apportionment of the Unitrust Amount in the Discretion of the Trustee.
1. **Explanation.** The donor or the trustee of a nongrantor charitable lead trust may be granted the power to apportion the unitrust payment from time to time among a class of qualifying charitable beneficiaries. See § 674(b)(4). A power to apportion the unitrust amount among a class of qualifying charitable beneficiaries that is retained by the donor or the donor’s spouse will not cause the donor to be treated as the owner of the trust for income tax purposes. Section 674(b)(4). Note, however, that a retained power of apportionment by the donor, but not the donor’s spouse, will cause the gift of the unitrust interest to be incomplete for gift tax purposes and will cause some or all of the trust property to be included in the donor’s gross estate. See §§ 2035(a), 2036(a)(2), and 2038(a)(1) and § 25.2511-2(c).

2. **Instruction for use.** Replace the first three sentences of paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 with the following two sentences:

   For each taxable year of the trust during the unitrust period, the Trustee shall pay to one or more members of a class comprised of organizations described in §§ 170(c), 2055(a), and 2522(a) (hereinafter, collectively “the Charitable Organization”) a unitrust amount equal to [number representing the annual unitrust percentage to be paid to the Charitable Organization] percent of the net fair market value of the assets of the trust, valued as of the first day of each taxable year of the trust (hereinafter “the valuation date”). The Trustee may pay the unitrust amount to one or more members of the class, in equal or unequal shares, as the Trustee, in the Trustee’s sole discretion, from time to time may deem advisable.

.04 **Designation of an Alternate Charitable Beneficiary in the Trust Instrument.**

1. **Explanation.** The sample trust in section 4 provides that, in the event the charitable beneficiary designated in the trust instrument is not an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the trustee shall distribute such payments to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the trustee shall select. As an alternative, the trust instrument may specifically designate one or more alternate charitable beneficiaries.

2. **Instruction for use.** Replace the second sentence in paragraph 2, Payment of Unitrust Amount, of the sample trust in section 4 with the following two sentences:

   If [designated charitable recipient] is not an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the Trustee shall instead distribute such payments to [designated substitute charitable recipient]. If neither [designated charitable recipient] nor [designated substitute charitable recipient] is an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the Trustee shall distribute such payments to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the Trustee
shall select, and in such proportions as the Trustee shall decide, from time to time, in the Trustee’s sole discretion.

SECTION 7. SAMPLE INTER VIVOS GRANTOR CHARITABLE LEAD UNITRUST
On this day of , 20, I, (hereinafter “the Donor”), desiring to establish a charitable lead unitrust within the meaning of Rev. Proc. 2008-45, hereby enter into this trust agreement with as the initial trustee (hereinafter “the Trustee”). This trust shall be known as the Grantor Charitable Lead Unitrust. All references to “section” or “§” in this instrument shall refer to the Internal Revenue Code of 1986, 26 U.S.C. § 1, et seq.

1. Funding of Trust. The Donor hereby transfers and irrevocably assigns to the Trustee on the above date, the property described in Schedule A, and the Trustee accepts the property and agrees to hold, manage, and distribute the property under the terms set forth in this trust instrument.

2. Payment of Unitrust Amount. For each taxable year of the trust during the unitrust period, the Trustee shall pay to [designated charitable recipient] a unitrust amount equal to [number representing the annual unitrust percentage to be paid to the designated charitable recipient] percent of the assets of the trust, valued as of the first day of each taxable year of the trust (hereinafter “the valuation date”). If [designated charitable recipient] is not an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the Trustee shall instead distribute such payments to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the Trustee shall select, and in such proportions as the Trustee shall decide, from time to time, in the Trustee’s sole discretion. The term “the Charitable Organization” shall be used herein to refer collectively to the organization(s) then constituting the charitable recipient, whether named in this paragraph or subsequently selected as the substitute charitable recipient. During the trust term, no payment shall be made to any person other than the Charitable Organization. The unitrust period is a term of [number of years of unitrust period] years. The first day of the unitrust period shall be the date property is first transferred to the trust, and the last day of the unitrust period shall be the day preceding the [ordinal number corresponding to the length of the unitrust period] anniversary of that date. The unitrust amount shall be paid in equal quarterly installments at the end of each calendar quarter from income and, to the extent income is not sufficient, from principal. Any income of the trust for a taxable year in excess of the unitrust amount shall be added to principal. If for any year the net fair market value of the trust assets is incorrectly determined, then within a reasonable period after the correct value is finally determined, the Trustee shall pay to the Charitable Organization (in the case of an undervaluation) or receive from the Charitable Organization (in the case of an overvaluation) an amount equal to the difference between the unitrust amount(s) properly payable and the unitrust amount(s) actually paid.

3. Proration of Unitrust Amount. For a short taxable year, including the taxable year during which the unitrust period ends, the Trustee shall prorate on a daily basis for the number of
days of the unitrust period in that year, the unitrust amount described in paragraph 2, or, if an additional contribution is made to the trust, the unitrust amount described in paragraph 5.

4. **Distribution Upon Termination of Unitrust Period.** At the termination of the unitrust period, the Trustee shall distribute all of the then remaining principal and income of the trust (other than any amount due to the Charitable Organization under the provisions above) to [remainder beneficiary].

5. **Additional Contributions.** If any additional contributions are made to the trust after the initial contribution, the unitrust amount for the year in which any additional contribution is made shall be [same percentage used in paragraph 2] percent of the sum of (a) the net fair market value of the trust assets as of the valuation date (excluding the assets so added and any post-contribution income from, and appreciation on, such assets during that year) and (b) for each additional contribution during the year, the fair market value of the assets so added as of the valuation date (including any post-contribution income from, and appreciation on, such assets through the valuation date) multiplied by a fraction the numerator of which is the number of days in the period that begins with the date of contribution and ends with the earlier of the last day of the taxable year or the last day of the unitrust period and the denominator of which is the number of days in the period that begins with the first day of such taxable year and ends with the earlier of the last day in such taxable year or the last day of the unitrust period. In a taxable year in which an additional contribution is made on or after the valuation date, the assets so added shall be valued as of the date of contribution, without regard to any post-contribution income or appreciation, rather than as of the valuation date.

6. **Prohibited Transactions.** The Trustee shall not engage in any act of self-dealing within the meaning of § 4941(d), as modified by § 4947(a)(2), and shall not make any taxable expenditures within the meaning of § 4945(d), as modified by § 4947(a)(2). The Trustee shall not retain any excess business holdings that would subject the trust to tax under § 4943, as modified by §§ 4947(a)(2) and 4947(b)(3). In addition, the Trustee shall not acquire any assets that would subject the trust to tax under § 4944, as modified by §§ 4947(a)(2) and 4947(b)(3), or retain assets which, if acquired by the Trustee, would subject the Trustee to tax under § 4944, as modified by §§ 4947(a)(2) and 4947(b)(3).

7. **Taxable Year.** The taxable year of the trust shall be the calendar year.

8. **Governing Law.** The operation of the trust shall be governed by the laws of the State of . However, the Trustee is prohibited from exercising any power or discretion granted under said laws that would be inconsistent with the requirements for the charitable deductions available for contributions to a charitable lead unitrust.

9. **Limited Power of Amendment.** This trust is irrevocable. However, the Trustee shall have the power, acting alone, to amend the trust from time to time in any manner required for the sole purpose of ensuring that the unitrust interest passing to the Charitable Organization is a
unitrust interest under §§ 170(f)(2)(B), 2055(e)(2)(B), and 2522(c)(2)(B) and the regulations thereunder.

10. Investment of Trust Assets. Except as provided in paragraph 6 herein, nothing in this trust instrument shall be construed to restrict the Trustee from investing the trust assets in a manner that could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets.

11. Retained Powers and Interests. During the Donor’s life, [individual other than the donor, the trustee, or a disqualified person as defined in § 4946(a)(1)] shall have the right, exercisable only in a nonfiduciary capacity and without the consent or approval of any person acting in a fiduciary capacity, to acquire any property held in the trust by substituting other property of equivalent value.

SECTION 8. ANNOTATIONS REGARDING SAMPLE INTER VIVOS GRANTOR CHARITABLE LEAD UNITRUST

.01 Annotations for Introductory Paragraph and Paragraph 1, Funding of Trust, of the Sample Trust in Section 7.

1. Types of charitable lead trusts. An inter vivos charitable lead trust may be established as either a grantor charitable lead trust or a nongrantor charitable lead trust. The sample trust in section 7 is an example of a grantor charitable lead trust. The sample trust in section 4 is an example of a nongrantor charitable lead trust. In order for the donor to a charitable lead trust to claim an income tax charitable deduction under § 170(a) for the year of the donor’s contribution to the trust, the trust must be structured as a grantor charitable lead trust. See § 170(f)(2)(B). The rules governing grantor charitable lead trusts are similar to those relating to nongrantor charitable lead trusts. The most significant difference is the income tax treatment of the trust income. A charitable lead trust is a grantor charitable lead trust if the donor to the trust is treated as the owner of the entire trust for income tax purposes. See section 8.09 for a discussion of the types of powers that may be used to create a grantor charitable lead trust.

2. Income taxation of grantor charitable lead trusts. The donor to a grantor charitable lead unitrust may claim a federal income tax charitable deduction under § 170(a) for the year in which assets are irrevocably transferred to the trust. During the charitable lead unitrust period, the donor is taxed on all income earned by the trust and does not receive any charitable deduction under § 170 for the unitrust payments to the charitable beneficiary as they are made. In addition, the trust does not receive a charitable deduction under § 642(c)(1). See § 1.671-4 for the income tax reporting requirements for a grantor charitable lead unitrust.

3. Income tax deductibility limitations. The donor to a grantor charitable lead trust may claim an income tax charitable deduction under § 170(a) equal to the present value of all future payments that are to be made to the charitable beneficiary. Section 1.170A-6(c). However, a contribution of a charitable income interest in property for which a deduction is allowable under § 170(a) is considered to be made “for the use of” rather than “to” a
charitable organization. Section 1.170A-8(a)(2). Because the charitable lead interest of a grantor charitable lead trust is considered to be made “for the use of” the charitable beneficiary, the income tax charitable deduction available to an individual taxpayer is generally limited as set forth in § 170(b)(1)(B) to 30 percent of the taxpayer’s contribution base as defined in § 170(b)(1)(G). However, if the property contributed to the CLUT is capital gain property as defined in § 170(b)(1)(C)(iv), the individual taxpayer’s income tax charitable deduction generally is limited as set forth in § 170(b)(1)(D) to 20 percent of the taxpayer’s contribution base. Section 170(b)(1)(D). See §§ 1.170A-8(c) and (d). In addition, the amount of a charitable contribution of certain types of property may be reduced under § 170(e). See § 1.170A-4.

4. **Charitable lead beneficiary requirements.** A deduction is allowed under § 170(a) for contributions to a grantor CLUT only if the charitable lead beneficiary is an organization described in § 170(c). Note that the class of permissible charitable recipients for obtaining a deduction under § 170(a) differs from the class of permissible charitable recipients for obtaining a deduction under § 642(c)(1). Compare § 170(c) and § 1.642(c)-1(a)(2).

5. **Computation of charitable deduction.** In general, the income, estate, and gift tax charitable deductions available under §§ 170(a), 2055(e)(2)(B), and 2522(c)(2)(B) with respect to contributions to a CLUT are equal to the present value of the unitrust interest. Sections 1.170A-6(c)(3)(ii), 20.2055-2(f)(1), and 25.2522(c)-3(d)(1). Section 7520 generally requires that a unitrust interest must be valued using tables published by the Service. The method for valuing a charitable lead unitrust interest is set forth in the regulations. See §§ 1.7520-2, 20.7520-2, and 25.7520-2. If, however, the circumstances surrounding the transfer to a charitable lead trust suggest that the charitable beneficiary might not receive the beneficial enjoyment of the unitrust interest, an income tax deduction will be allowed only for the minimum possible amount that the charity will receive. Section 1.170A-6(c)(3)(iii). If at any time the donor ceases to be treated as the owner of the trust under subpart E, part I, subchapter J, chapter 1, subtitle A of the Code, the donor shall be considered to have received an amount of income equal to the amount of any deduction the donor received under § 170(a) for the contribution to the trust, reduced by the discounted value (as of the date of the contribution to the trust) of all amounts of income earned by the trust and taxable to the donor before the time that the donor ceased to be treated as the owner of the trust under subpart E, part I, subchapter J, chapter 1, subtitle A of the Code. Section 170(f)(2)(B).

6. **Trustee provisions.** The trust instrument may name alternate or successor trustees and/or may include a process for the appointment of unnamed alternate or successor trustees. In addition, the trust instrument may contain certain other administrative provisions relating to the trustee’s duties and powers.

7. **Identity of donor.** For purposes of qualification under this revenue procedure, the donor to a charitable lead unitrust may be an individual or a husband and wife. Appropriate adjustments should be made to the introductory paragraph if a husband and wife are the donors. Terms such as “grantor” or “settlor” may be substituted for “donor.”
.02 Annotations for Paragraph 2, Payment of Unitrust Amount, of the Sample Trust in Section 7.

1. **Unitrust interest.** To qualify for the applicable charitable deductions, a grantor CLUT must provide for the payment of a unitrust amount at least annually to a qualified charitable organization for each year during the unitrust period. See §§ 170(c), 2055(e)(2)(B), and 2522(c)(2)(B). A unitrust interest is the right pursuant to the instrument of transfer to receive payment, not less often than annually, of a fixed percentage of the net fair market value, determined annually, of the property that funds the unitrust interest. Payments of a unitrust interest may be paid for a specified term or for the life or lives of certain individuals, each of whom must be living at the date of the transfer and can be ascertained as of such date. Sections 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a). See section 8.02(4) for a discussion of the permissible term of a grantor CLUT. An interest is a unitrust interest only if it is a unitrust interest in every respect. For example, if an interest is expressed as the right to receive an annual payment from a trust equal to the lesser of a sum certain or a fixed percentage of the net fair market value of the trust assets (determined annually), the interest is not a unitrust interest. See §§ 1.170A-6(c)(2)(ii)(B), 20.2055-2(e)(2)(vii)(A), and 25.2522(c)-3(c)(2)(vii)(A). See Rev. Rul. 77-300, 1977-2 C.B. 352. In addition, an interest is not a unitrust interest if the trustee has the discretion to commute and prepay the interest prior to the termination of the unitrust period. Rev. Rul. 88-27, 1988-1 C.B. 331. If a charitable interest in the form of a unitrust interest is in trust and the present value of the charitable interest on the date of gift exceeds 60 percent of the aggregate value of all amounts in the trust, the charitable interest will not be considered a unitrust interest unless the governing instrument of the trust prohibits the acquisition and retention of assets that would give rise to a tax under § 4943 or 4944, as modified by §§ 4947(a)(2) and 4947(b)(3). Section 4947(b)(3)(A) and § 53.4947-2(b)(1)(i). See §§ 1.170A-6(c)(2)(ii)(E), 20.2055-2(e)(2)(vii)(A), and 25.2522(c)-3(c)(2)(vii)(A). These prohibitions are contained in the sample trust in section 7. See section 8.06 for a further discussion of the 60 percent test.

2. **Payment requirements.** CLUTs are not subject to any minimum or maximum payout requirements. The governing instrument of a CLUT must provide for the payment to a charitable organization, not less often than annually, of a fixed percentage of the net fair market value of the assets of the trust, valued annually. Alternatively, the governing instrument of a CLUT may provide for a unitrust amount that is initially stated as a fixed percentage amount but increases or decreases during the unitrust period, provided that the value of the unitrust interest is ascertainable at the time the trust is funded. The unitrust payments may be made in cash or in kind. If the trustee distributes appreciated property in satisfaction of the required unitrust payment, the donor will realize capital gain on the assets distributed to satisfy part or all of the unitrust payment.

3. **Rule against perpetuities.** An interest payable for a specified term of years may qualify as a unitrust interest even if the governing instrument contains a savings clause intended to ensure compliance with a rule against perpetuities. However, any such savings clause must utilize a period of vesting of not more than 21 years after the deaths of measuring
lives who are selected to maximize, rather than limit, the term of the trust. Sections 1.170A-6(c)(2)(iii)(A), 20.2055-2(e)(2)(vii)(a), and 25.2522(c)-3(c)(2)(vii)(a).

4. **Permissible term.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 7 provides for payment of the unitrust amount for a specified term of years. Alternatively, the trust instrument may provide for payment of the unitrust amount for the life or lives of one or more measuring lives or for the life or lives of one or more measuring lives plus a term of years. Rev. Rul. 85-49, 1985-1 C.B. 330. Only one or more of the following individuals may be used as measuring lives: the donor, the donor’s spouse, and an individual who, with respect to all remainder beneficiaries (other than charitable organizations described in § 170, 2055, or 2522), is either a lineal ancestor or the spouse of a lineal ancestor of those beneficiaries. Each person used as a measuring life for the unitrust period must be living on the date assets are transferred to the trust. Sections 1.170A-6(c)(2)(iii)(A), 20.2055-2(e)(2)(vii)(a) and 25.2522(c)-3(c)(2)(vii)(a). See section 9.01 for an alternate provision that provides for a unitrust period based on the life of an individual.

5. **Permissible recipients.** A CLUT must have one or more charitable lead beneficiaries. The failure to designate a specific charitable beneficiary will not preclude the donor from receiving a charitable deduction if the trust instrument provides for the selection by the trustee of a charitable beneficiary described in §§ 170(c), 2055(a), and 2522(a). Rev. Rul. 78-101, 1978-1 C.B. 301. If it is determined that a deduction under § 2055(a) will not be necessary in any event, all references to § 2055(a) in the trust instrument may be deleted. Note that if the donor is serving as trustee of the trust, the trustee’s power to select the charitable beneficiaries will cause the gift of the unitrust interest to be incomplete for gift tax purposes and will cause some or all of the trust property (depending on the date of the donor’s death) to be included in the donor’s gross estate. See §§ 2035(a), 2036(a)(2), and 2038(a)(1), and § 25.2511-2(c). Further note that if the charitable beneficiary is a private foundation and the donor is an officer or director of the private foundation or possesses certain decision making authority in the private foundation, some or all of the trust property may be included in the donor’s gross estate. See § 2036(a)(2). See section 9.02 for an alternate provision that provides for a donor’s retained right to substitute the charitable beneficiary. See section 9.03 for an alternate provision that provides the trustee with the power to apportion the unitrust amount among charitable beneficiaries. See section 9.04 for an alternate provision that provides for the designation of an alternate charitable beneficiary in the trust instrument.

6. **Payment of unitrust amount in installments.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 7 specifies that the unitrust amount is to be paid in equal quarterly installments at the end of each calendar quarter. Alternatively, the trust instrument may specify that the unitrust amount is to be paid in annual or other equal or unequal installments throughout the year. See §§ 1.170A-6(c)(2)(iii)(A), 20.2055-2(e)(2)(vii)(a), and 25.2522(c)-3(c)(2)(vii)(a). The amount of the charitable deduction will be affected by the frequency of the payment, by whether the installments are equal or unequal, and by whether each installment is payable at the beginning or end of the period. See §§ 1.170A-6, 25.2512-5, and 20.2031-7.
7. **Excess income.** Trust income in excess of the amount required to pay the unitrust amount may be retained by the trust or distributed to the charitable beneficiary. The sample trust in section 7 provides for the retention of excess income by the trust. If, instead, the governing instrument of a grantor charitable lead trust provides for the payment of excess income to or for the use of the charitable beneficiary, the donor will receive an income tax charitable deduction each year for amounts paid to a charitable beneficiary to the extent that such amounts exceed the unitrust amount. Section 1.170A-6(d)(2)(i). However, the donor is not entitled to any additional estate or gift tax charitable deductions for the excess amounts of income distributed to the charitable beneficiary. See §§ 20.2055-2(e)(2)(viii)(d) and 25.2522(c)-3(c)(2)(vii)(d). See Situation 2 of Rev. Rul. 88-82, 1988-2 C.B. 336, for the gift tax consequences of the payment of excess income to a noncharitable beneficiary. See section 8.06 for the private foundation rules applicable to charitable lead trusts.

8. **Payment of part of unitrust for private purposes.** In general, no part of a charitable lead unitrust interest may be payable for a private purpose before the expiration of all charitable lead unitrust interests. However, there are two exceptions to this rule. The first exception arises when the amount payable for a private purpose is in the form of a unitrust interest and the trust’s governing instrument does not provide for any preference or priority in the payment of the private unitrust as opposed to the charitable unitrust. The second exception arises when, under the trust’s governing instrument, the amount that may be paid for a private purpose is payable only from a group of assets that is devoted exclusively to private purposes and to which § 4947(a)(2) is inapplicable by reason of § 4947(a)(2)(B). Note that an amount is not deemed to have been paid for a private purpose if it was paid for full and adequate consideration in money or money’s worth. Sections 1.170A-6(c)(2)(ii)(E), 20.2055-2(e)(2)(viii)(e), and 25.2522(c)-3(c)(2)(vii)(e). See section 8.06 for the private foundation rules applicable to charitable lead trusts.

9. **Valuation date.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 7 specifies that the net fair market value of trust assets is to be valued as of the first day of each taxable year of the trust. However, the value of the trust assets may be determined on any one date during the taxable year of the trust, or by taking the average of valuations made on more than one date during the taxable year of the trust, so long as the same valuation date or dates and the same valuation methods are used each year. If the governing instrument does not specify the valuation date or dates, the trustee must select the date or dates and indicate the selection on the first Form 1041, *U.S. Income Tax Return for Estates and Trusts*, that the trust must file. Sections 1.170A-6(c)(2)(ii)(A), 20.2055-2(e)(2)(vii)(a), and 25.2522(c)-3(c)(2)(vii)(a). Note that if the valuation date is a date other than the first day of each taxable year of the trust, it may be necessary to modify the provisions in the sample trust regarding: (i) the timing of the payment of the unitrust amount; (ii) the proration of the unitrust amount in a short taxable year and the last taxable year of the unitrust period; and (iii) additional contributions.

.03 Annotation for Paragraph 3, Proration of Unitrust Amount, of the Sample Trust in Section 7.
1. **Prorating the unitrust amount.** Paragraph 3, Proration of Unitrust Amount, of the sample trust in section 7 provides for the proration of the unitrust amount in any short taxable year, including the last year of the unitrust period.

**.04 Annotation for Paragraph 4, Distribution Upon Termination of Unitrust Period, of the Sample Trust in Section 7.**

1. **Generation-skipping transfer tax.** The GST tax may apply if a CLUT has or may have a skip person, as defined in §2613(a), as a remainder beneficiary. Under §2651(f)(3), a charitable organization is deemed to be in the same generation as the donor of a charitable lead trust. Therefore, the GST potential of a charitable lead trust is dependent upon whether any noncharitable beneficiary is a skip person. GST tax liability is determined by multiplying the taxable amount by the applicable rate. The applicable rate is the inclusion ratio multiplied by the maximum federal estate tax rate. Section 2641(a). Note that the rules set forth in §2642(e) for determining the inclusion ratio of certain charitable lead trusts do not apply to CLUTs.

**.05 Annotation for Paragraph 5, Additional Contributions, of the Sample Trust in Section 7.**

1. **Identity of additional contributors.** For purposes of qualification under this revenue procedure, only a donor or a donor’s estate may make an additional contribution to the trust. See section 8.01(7) of this revenue procedure for examples of who may be a donor of a CLUT.

2. **Option to prohibit additional contributions.** Paragraph 5, Additional Contributions, of the sample trust in section 7 provides rules for determining the unitrust amount payable in a year during which an additional contribution is made to the trust. However, paragraph 5 of the trust instrument may instead be drafted to prohibit contributions to the trust after the initial contribution.

3. **Proration of additional contributions.** Paragraph 5, Additional Contributions, of the sample trust in section 7 provides a formula for determining the unitrust amount in each year that an additional contribution is made to the CLUT. The formula incorporates a proration provision for additions made in a short taxable year.

4. **Valuation date in year of additional contribution.** Paragraph 2, Payment of Unitrust Amount, of the sample trust in section 7 specifies a January 1 valuation date for the trust. The formula contained in paragraph 5, Additional Contributions, of the sample trust may be used when January 1 or any other single date during the taxable year is selected as the valuation date for a CLUT. Note, however, that if a single date other than January 1 is selected as the valuation date for a CLUT, the formulas in both paragraphs 2 and 5 of the sample trust for computing the unitrust amount will be deficient unless the trust instrument addresses the possibility that the unitrust period may end before the valuation date, for instance, by providing that in a year in which the unitrust period ends before the valuation date, the valuation date for purposes of paragraph 2 and paragraph 5 shall be the last day of the unitrust period. In addition, if the trust instrument is drafted to provide for
the valuation of trust assets by averaging the valuations as of multiple specified dates during the trust year, the additional contributions formula must be modified.

.06 Annotation for Paragraph 6, Prohibited Transactions, of the Sample Trust in Section 7.

1. Prohibitions against certain investments and excess business holdings. Prohibitions against retaining any excess business holdings within the meaning of § 4943, as modified by §§ 4947(a)(2) and 4947(b)(3), and against investments that jeopardize the exempt purpose of the trust within the meaning of § 4944, as modified by §§ 4947(a)(2) and 4947(b)(3) are generally required. The sample trust in section 7 contains prohibitions against §§ 4943 and 4944 transactions. If the present value of the charitable interest does not exceed 60 percent of the aggregate value of all amounts in the trust, the trust instrument does not provide for the payment of any of the income interest to a noncharitable beneficiary, and the trust instrument does not provide for the payment of excess income to a noncharitable beneficiary, the references to §§ 4943 and 4944 may be removed from the trust instrument. Section 4947(b)(3)(A) and § 53.4947-2(b)(1)(i). See §§ 1.170A-6(c)(2)(ii)(E), 20.2055-2(e)(2)(vii)(A), and 25.2522(c)-3(c)(2)(vii)(A). See section 8.02(7) for a discussion of the payment of excess trust income to a noncharitable beneficiary. See section 8.02(8) for a discussion of the payment of part of the unitrust for a private purpose.

.07 Annotation for paragraph 7, Taxable Year, of the Sample Trust in Section 7.

1. Calendar year. The taxable year of a charitable lead trust must be a calendar year. Section 644(a).

.08 Annotation for paragraph 10, Investment of Trust Assets, of the Sample Trust in Section 7.

1. Capital gains. Gains from the sale or exchange of capital assets may be allocated to the income or the principal of the trust. If the governing instrument is silent, capital gains are allocated in accordance with local law.

.09 Annotation for Paragraph 11, Retained Powers and Interests, of the Sample Trust in Section 7.

1. Power to substitute trust assets. The donor to a CLUT may claim an income tax charitable deduction under § 170(a) if the donor is treated as the owner of the entire CLUT under the provisions of subpart E, part I, subchapter J, chapter 1, subtitle A of the Code. Paragraph 11, Retained Powers and Interests, of the sample trust in section 7 creates a grantor CLUT through the use of a power to substitute trust assets under § 675(4) that is held by a person other than the donor, the trustee, or a disqualified person as defined in § 4946(a)(1), and is exercisable only in a nonfiduciary capacity. The circumstances surrounding the administration of a CLUT will determine whether a § 675(4) substitution
power is exercised in a fiduciary or nonfiduciary capacity. This is a question of fact. Note, that the exercise of a § 675(4) power may result in an act of self-dealing under § 4941.

2. Other powers or provisions to create a grantor trust. As noted above, the sample trust in section 7 includes a § 675(4) power that is held by someone other than donor, the trustee, or a disqualified person as defined in § 4946(a)(1), and that may be exercised only in a nonfiduciary capacity. The CLUT instrument may instead incorporate a power or provision, other than the one provided in the sample trust in section 7, that will cause the donor to be treated as the owner of the entire CLUT under the provisions of subpart E, part I, subchapter J, chapter 1, subtitle A of the Code. See § 671 et seq. However, practitioners should exercise caution when choosing a particular power or provision because certain methods of creating a grantor trust may have unforeseen tax consequences.

SECTION 9. ALTERNATE PROVISIONS FOR SAMPLE INTER VIVOS GRANTOR CHARITABLE LEAD UNITRUST

.01 Unitrust Period for the Life of One Individual.

1. Explanation. As an alternative to establishing a CLUT for a term of years, the trust instrument of a grantor CLUT may provide for payment of the unitrust amount for the life or lives of an individual or individuals. However, only one or more of the following individuals may be used as measuring lives: the donor, the donor’s spouse, and an individual who, with respect to all remainder beneficiaries (other than charitable organizations described in § 170, 2055, or 2522), is either a lineal ancestor or the spouse of a lineal ancestor of those beneficiaries. A trust will satisfy the requirement that each measuring life is a lineal ancestor (or the spouse of a lineal ancestor) of all noncharitable remainder beneficiaries if there is a less than 15 percent probability at the time of the contribution to the trust that individuals who are not lineal descendants of an individual who is a measuring life will receive any trust principal. The probability must be computed under the applicable tables in § 20.2031-7. Sections 1.170A-6(c)(2)(ii)(A), 20.2055-2(e)(2)(vii)(a), and 25.2522(c)-3(c)(2)(vii)(a).

2. Instruction for use. Replace the fifth and sixth sentences of paragraph 2, Payment of Unitrust Amount, of the sample trust in section 7 with the following sentences:

The unitrust period is the lifetime of [designated measuring life]. The first day of the unitrust period shall be the date property is first transferred to the trust, and the last day of the unitrust period shall be the date of death of [designated measuring life].

.02 Retention of the Right to Substitute the Charitable Lead Beneficiary.

1. Explanation. The donor to a grantor CLUT may retain the right to substitute another charitable beneficiary for the charitable beneficiary named in the trust instrument and still claim a deduction under § 170(a) in the year of the transfer to the CLUT. Note, however, that the retention of this right will cause the gift of the unitrust interest to be incomplete for gift tax purposes and will cause some or all of the trust property (depending on the date of the donor’s death) to be included in the donor’s gross estate. See §§ 2035, 2036(a)(2),
and 2038(a)(1) and § 25.2511-2(c). See section 8.01(3) for a discussion of the income tax
deductibility limitations applicable to contributions to a grantor CLUT.

2. **Instruction for use.** Replace the third sentence of paragraph 2, Payment of Unitrust
Amount, of the sample trust in section 7 with the following two sentences:

Notwithstanding the preceding sentences, the Donor reserves the right to designate
as the charitable recipient, at any time and from time to time, in lieu of [designated
charitable recipient named above], one or more organizations described in §§
170(c), 2055(a), and 2522(a) and shall make any such designation by giving written
notice to the Trustee. The term “the Charitable Organization” shall be used herein
to refer collectively to the organization(s) then constituting the charitable recipient,
whether named in this paragraph or subsequently selected as the substitute
charitable recipient.

03 **Apportionment of the Unitrust Amount in the Discretion of the Trustee.**

1. **Explanation.** The donor or the trustee of a grantor charitable lead trust may be
granted the power to apportion the unitrust payment from time to time among a class of
qualifying charitable beneficiaries. Note that a retained power of apportionment by the
donor will cause the gift of the unitrust interest to be incomplete for gift tax purposes
and will cause some or all of the trust property to be included in the donor’s gross estate. See
§§ 2035(a), 2036(a)(2), and 2038(a)(1), and § 25.2511-2(c).

2. **Instruction for use.** Replace the first three sentences of paragraph 2, Payment of
Unitrust Amount, of the sample trust in section 7 with the following two sentences:

For each taxable year of the trust during the unitrust period, the Trustee shall pay to
one or more members of a class comprised of organizations described in §§ 170(c),
2055(a), and 2522(a) (hereinafter, collectively “the Charitable Organization”) a
unitrust amount equal to [number representing the annual unitrust percentage to be
paid to the Charitable Organization] percent of the net fair market value of the
assets of the trust, valued as of the first day of each taxable year of the trust
(hereinafter the “valuation date”). The Trustee may pay the unitrust amount to one
or more members of the class, in equal or unequal shares, as the Trustee, in the
Trustee’s sole discretion, from time to time may deem advisable.

04 **Designation of an Alternate Charitable Beneficiary in the Trust Instrument.**

1. **Explanation.** The sample trust in section 7 provides that, if the charitable beneficiary
designated in the trust instrument is not an organization described in §§ 170(c), 2055(a),
and 2522(a) at the time any payment is to be made to it, the trustee shall distribute such
payments to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the
trustee shall select. As an alternative, the trust instrument may specifically designate one
or more alternate charitable beneficiaries. See section 8.01(3) for a discussion of the income tax deductibility limitations applicable to contributions to a grantor CLUT.

2. Instruction for use. Replace the second sentence in paragraph 2, Payment of Unitrust Amount, of the sample trust in section 7 with the following two sentences:

If [designated charitable recipient] is not an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the Trustee shall instead distribute such payments to [designated substitute charitable recipient]. If neither [designated charitable recipient] nor [designated substitute charitable recipient] is an organization described in §§ 170(c), 2055(a), and 2522(a) at the time any payment is to be made to it, the Trustee shall distribute such payments to one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the Trustee shall select, and in such proportions as the Trustee shall decide, from time to time, in the Trustee’s sole discretion.

SECTION 10. DRAFTING INFORMATION
The principal author of this revenue procedure is Stephanie N. Bland of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this revenue procedure, contact Stephanie N. Bland at (202) 622-3130 or James F. Hogan at (202) 622-3090.
SECTION 1. PURPOSE

This revenue procedure contains a sample provision that may be included in the governing instrument of a charitable remainder annuity trust (CRAT) providing for annuity payments payable for one or more measuring lives followed by the distribution of trust assets to one or more charitable remaindermen. The Internal Revenue Service (IRS) will treat the sample provision as a qualified contingency within the meaning of § 664(f) of the Internal Revenue Code. Thus, inclusion of the sample provision in the trust instrument does not cause the trust to fail to qualify as a charitable remainder trust under § 664. Any CRAT containing the sample provision will not be subject to the “probability of exhaustion” test set forth in Rev. Rul. 70-452, 1970-2 C.B. 199, and applied in Rev. Rul. 77-374, 1977-2 C.B. 329. The “probability of exhaustion” test is used to determine whether a CRAT complies with the regulatory requirement applicable to all contingent charitable transfers that only a negligible chance exists that the charity will receive nothing. See § 1.170A-1(e) of the Income Tax Regulations, § 20.2055-2(b) of the Estate Tax Regulations, and § 25.2522(c)-3(b)(1) of the Gift Tax Regulations.

SECTION 2. BACKGROUND

To qualify as a charitable remainder trust under § 664, a CRAT must satisfy all of the following requirements of § 664(d)(1): (A) a sum certain (not less than 5 percent and not more than 50 percent of the initial fair market value (FMV) of all property placed in trust) is to be paid at least annually to one or more persons (at least one of which is not an organization described in § 170(c) and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not to exceed 20 years) or for the life or lives of such individual or individuals; (B) no amount other than such payments and other than qualified gratuitous transfers described in § 664(d)(1)(C) may be paid to or for the use of any person other than an organization described in § 170(c); (C) following the termination of such payments, the remainder interest in the trust is to be transferred to or for the use of an organization described in § 170(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as defined in § 664(g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (ESOP) (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined by § 664(g)); and (D) the value (determined under § 7520) of the remainder interest is at least 10 percent of the initial FMV of all trust property.

To qualify as a charitable remainder trust under § 664, a CRAT also must satisfy the requirements of § 1.664-1(a)(1)(iii)(a). Section 1.664-1(a)(1)(iii)(a) defines a charitable remainder trust as a trust with respect to which a deduction is allowable under § 170, § 2055, § 2106, or § 2522. Income or gift tax charitable deductions are not allowable under § 170 or § 2522 if the remainder interest of an inter vivos CRAT does not satisfy, inter alia, the requirements of § 1.170A-1(e) or § 25.2522(c)-3(b)(1), respectively. Similarly, an estate tax charitable deduction is not allowable under § 2055 or § 2106 if the remainder interest of a testamentary CRAT does not satisfy, inter alia, the requirements of § 1.170A-1(e) and
§ 20.2055-2(b)(1). Sections 1.170A-1(e), 20.2055-2(b)(1), and 25.2522(c)-3(b)(1) provide that if, as of the date of a gift (or the date of decedent’s death for a testamentary transfer), a transfer for charitable purposes is dependent upon the performance of some act or the happening of a precedent event in order that it might become effective, no charitable deduction is allowable unless the possibility that the charitable transfer will not become effective is so remote as to be negligible. If an estate or interest has passed to, or is vested in, a charity at the time of the transfer and the estate or interest would be defeated by the subsequent performance of some act or the happening of some event, the possibility of occurrence of which appeared at the time of the transfer to be so remote as to be negligible, the deduction is allowable.

Rev. Rul. 70-452 applies these rules to a split-interest charitable remainder trust. Rev. Rul. 70-452 holds that, if there is a greater than 5 percent probability that payment of the annuity will defeat the charity’s interest by exhausting the trust assets by the end of the trust term, then the possibility that the charitable transfer will not become effective is not so remote as to be negligible. This determination is referred to as the “probability of exhaustion test.” Rev. Rul. 77-374 applies the probability of exhaustion test to a CRAT. The probability of exhaustion is calculated first by applying the § 7520 assumed rate of return on CRAT assets (§ 7250 rate) against the amount of the annuity payment to determine when the CRAT assets will be exhausted. Then, a mortality table (Mortality Table 2000CM, found in §2031-7(d)(7)) is used to determine the probability that the income beneficiary or beneficiaries will survive exhaustion of the CRAT assets. If the probability that the life beneficiary or beneficiaries will survive exhaustion of the CRAT assets is greater than 5 percent, then the charitable remainder interest of the CRAT does not qualify for an income, gift, or estate tax charitable deduction and the CRAT is not exempt from income tax under § 664(c). If the § 7520 rate at creation of the trust is equal to or greater than the percentage used to determine the annuity payment, then exhaustion will never occur under this test.

Low interest rates in recent years have greatly limited use of a CRAT as an effective charitable-giving vehicle. For example, in May of 2016, the § 7520 rate was 1.8 percent. At this interest rate, the sole life beneficiary of a CRAT that provides for the payment of the minimum allowable annuity (equal to 5 percent of the initial FMV of the trust assets) must be at least 72 years old at the creation of the trust for the trust to satisfy the probability of exhaustion test. The § 7520 rate has not exceeded the minimum 5 percent annuity payout rate since December of 2007, which has necessitated testing for the probability of exhaustion for every CRAT created since that time.

Section 664(f)(1) provides in general that, if a trust would, but for a qualified contingency, meet the requirements of § 664(d)(1)(A) (relating to CRATs) or § 664(d)(2)(A) (relating to charitable remainder unitrusts), the trust is treated as meeting these requirements. Section 664(f)(2) provides that, for purposes of determining the amount of any charitable contribution (or the actuarial value of any interest), a qualified contingency is not taken into account. Section 664(f)(3) defines a qualified contingency for purposes of § 664(f) as any provision of a trust which provides that, upon the happening of a contingency, the payments described in § 664(d)(1)(A) or (d)(2)(A) (as the case may be) will terminate not later than these payments otherwise would terminate under the trust.

SECTION 3. SCOPE
.01 This revenue procedure applies to trusts created after the effective date of this revenue procedure that—
   (1) Meet the requirements of § 664(d)(1);
   (2) Provide for annuity payments payable for one or more measuring lives; and
   (3) Contain in their governing instrument the precise language of the sample provision in section 5 of this revenue procedure.

.02 A CRAT that contains a substantive provision similar but not identical to that provided in section 5 of this revenue procedure will not necessarily be disqualified, but neither will such a provision be assured of treatment as a qualified contingency under § 664(f).

SECTION 4. APPLICATION

.01 The IRS will treat the sample provision contained in section 5 of this revenue procedure as a qualified contingency under § 664(f). Thus, the presence of this provision will not cause the trust to fail to qualify as a charitable remainder trust under § 664.

.02 The sample provision provides an alternative to satisfying the probability of exhaustion test for those CRATs to which this revenue procedure applies. The sample provision causes the early termination of the trust, followed by an immediate distribution of the remaining trust assets to the charitable remainder beneficiary. Specifically, this provision provides for early termination of the trust (and thus the end of the ability to make any more annuity payments) on the date immediately before the date on which any annuity payment would be made, if the payment of that annuity amount would result in the value of the trust corpus, when multiplied by a specified discount factor, being less than 10 percent of the value of the initial trust corpus.

.03 The sample provision is designed to ensure that the benefit from the creation of the CRAT will be available only where there is a significant benefit to charity. See Staff of the Joint Comm. on Taxation, 105th Cong., General Explanation of Tax Legislation Enacted in the 105th Congress, JCS-23-97 at 289-290 (1997). This provision also is designed to ensure that the charitable remainder beneficiary will receive an amount that accords with the charitable deduction allowed to the donor on creation of the trust. See H.R. Rep. No. 91-413, pt. 1, at 59 (1969), 1969-3 C.B. 200, 238, and S. Rep. No. 91-552, 88 and 90 (1969), 1969-3 C.B. 423, 480-81. Finally, this provision is designed to expose the charitable remainderman to some, but not all, of the investment performance risk of the CRAT assets.

SECTION 5. SAMPLE PROVISION

.01 The following language is the sample provision designed to be used in an inter vivos CRAT for one measuring life:

“The first day of the annuity period shall be the date the property is transferred to the trust and the last day of the annuity period shall be the date of the Recipient’s death or, if earlier, the date of the contingent termination. The date of the contingent termination is the date immediately preceding the payment date of any annuity payment if, after making that payment, the value of the trust corpus, when multiplied by the specified discount factor, would be less than 10 percent of the value of the initial trust corpus. The specified discount factor is equal to \([1 / (1 + i)]^t\), where \(t\) is the time from inception of the trust to the date of the annuity payment, expressed in years and fractions of a year, and \(i\) is the interest rate determined by the Internal Revenue Service for purposes of section 7520 of the Internal Revenue Code of 1986, as amended (section 7250 rate), that was used to determine the value of the charitable remainder at the
inception of the trust. The section 7520 rate used to determine the value of the charitable remainder at the inception of the trust is the section 7520 rate in effect for [insert the month and year], which is [insert the applicable section 7520 rate].”

.02 In a testamentary CRAT, the phrase “the property is transferred to the trust” (the first underlined phrase) in this sample language must be replaced with “of my death”.

.03 If the inter vivos or testamentary CRAT is created using the sample form provided in Rev. Proc. 2003-53, 2003-2 C.B. 230, or Rev. Proc. 2003-57, 2003-2 C.B. 257, respectively, the insertion of this sample provision in place of the second sentence of paragraph 2 of that sample inter vivos form, or in place of the second sentence of paragraph 1 of the sample testamentary form, respectively, will satisfy the requirements of a qualified contingency as described in section 6.03 of each revenue procedure.


SECTION 6. EXAMPLE

On January 1, Year 1, Donor transfers property valued at $1,000,000 to Trust, an inter vivos trust providing for an annuity payment of $50,000 (5 percent of the value of the initial trust corpus) on December 31 of each year to S for S’s life followed by the distribution of trust assets to Charity. Trust includes the precise language of the sample provision in section 5 of this revenue procedure providing for an early termination contingency and specifies the § 7520 rate in effect for January, Year 1, which is 3 percent. But for the early termination provision, Trust meets all of the requirements of § 664(d)(1). In accordance with this revenue procedure, the IRS will treat the early termination contingency as a qualified contingency under § 664(f). Therefore, the early termination provision does not cause Trust to fail to qualify as a CRAT under § 664. In addition, Trust qualifies as a CRAT regardless of whether it passes the probability of exhaustion test on January 1, Year 1.

Each year, prior to payment of the annuity to S, the trustee performs the calculations required to determine if Trust will terminate early in accordance with the terms of the qualified contingency. In each year from Year 1 through Year 17, the trustee determines that the value of the trust corpus, minus the $50,000 annual payment, and then multiplied by the specified discount factor, is greater than 10 percent of the initial trust corpus. The value of the trust corpus as of December 30 in Year 18 is $210,000. Only in Year 18 does the value of the trust corpus as of December 30, when reduced by the annuity payment and multiplied by the specified discount factor, fall below 10 percent of the value of the initial trust corpus. The calculations required to determine if Trust will terminate early in Year 18 are as follows:

1. $1,000,000 x 10 percent = $100,000

2. \[(210,000 - 50,000) \times \frac{1}{(1 + .03)^{18}}\]  
   \$160,000 \times (1/1.03)^{18}  
   \$160,000 \times 0.970874^{18}
$160,000 \times 0.587397 = $93,984.

Because the value of the trust corpus ($210,000), when reduced by the annuity payment ($50,000) and then multiplied by the specified discount factor (0.587397), is less than 10 percent of the value of the initial trust corpus ($100,000), Trust terminates on December 30, Year 18, and the principal and income remaining in Trust (including the annuity payment for Year 18 that otherwise would have been payable to S) then must be distributed to Charity.

SECTION 7. EFFECT ON OTHER DOCUMENTS

Rev. Rul. 70-452 and Rev. Rul. 77-374 are modified to provide an exception for CRATs that conform to this revenue procedure.


SECTION 8. EFFECTIVE DATE

This revenue procedure is effective August 8, 2016 and applies to trusts created on or after that date.

SECTION 9. DRAFTING INFORMATION

The principal author of this revenue procedure is Donna Douglas of the Office of Associate Chief Counsel (Passthroughs & Special Industries). However, other personnel from the Treasury Department and the IRS participated in its development. For further information regarding this revenue procedure, please contact Donna Douglas at (202) 317-6859 (not a toll-free number).