CRTs in Midlife Crisis:

Terminating, Accelerating and Fixing Charitable Remainder Trusts

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A charitable remainder trust (CRT) may make perfect sense to all parties concerned at the time it is established. But these irrevocable trusts can last for decades. Since things change over time, including a donor's income requirements and philanthropic objectives, it may be desirable to explore ways to change the arrangement to fit changed circumstances (or simply to correct mistakes). Summarized below are planning alternatives, and technical issues that must be considered, in some common situations.

I. Life Goes On – But the Trust Remains the Same

The majority of CRTs are established for life, and therefore the term of these irrevocable trusts can extend for decades. Because they are irrevocable, CRT governing instruments typically provide very little flexibility to account for changing circumstances of the income and remainder beneficiaries. But over time, things change:

A. Donor or other income beneficiary may no longer have the same income requirement

1. Income beneficiary may need access to principal

2. Donor may wish to the increase size of the original charitable gift, or simply accelerate it

3. The charitable remainder beneficiary may have a current need for funds, such as a building program.

II. Division of CRT in Divorce – "We both need the income"

A. A number of Private Letter Rulings have addressed the situation in which a married couple has established a CRT with either joint or successive income interests for the spouses, who are now divorcing. As part of the division of their assets incident to the divorce, the soon-to-be ex-spouses want to divide the CRT into two separate trusts, one for each. Before turning to tax considerations, the planner must first determine that the trust is divisible under state law, which should usually be the case. The Uniform Trust Code provides that a trust may be divided if the result will not impair rights of any beneficiary or adversely affect achievement of the purpose of the trust.[1] But of course the state law governing the trust in question needs to be consulted

[1] Uniform Trust Code § 417

B. In Private Letter Ruling 9851007, the Service ruled that division of the CRT will not cause either the original trust or the two new trusts to not qualify as CRTs.

C. Case Study #1

Husband established a CRT in which he gave Wife a successive income interest and retained the right to designate the charitable remainder beneficiaries. The divorce property settlement provides for equal division of the CRT into two new trusts, giving each spouse a current income interest in one of the trusts and a successive income interest in the other trust and allowing each spouse to designate the charity to receive the remainder in the trust for which he or she is the primary income beneficiary. In this situation, the IRS ruled[2]:

(1) Division will not cause the original or the two new trusts to fail to qualify.

(2) The basis and holding periods of CRT assets will carry over to the new trusts

(3) There are no gift taxes, citing Section 2516

(4) Husband will not recognize gain on the transfer of this interest in the trust to Wife, citing Section 1041. (Note that the Service has ruled elsewhere the *CRTs* also will not have taxable gain or loss under Section 1041.[3] Wife will have a carryover basis in her CRT income interest under Section 1041(b).)

D. Divorcing spouses have received similar favorable rulings allowing the division of CRTs incident to a property settlement, in a variety of fact patterns. [4]

III. Gift of Income Interest in CRT – "I don't need the income"

An income beneficiary of a CRT may determine that she no longer needs the income from the trust. In this case, she might simply transfer her income interest in the CRT to the charity that is its remainder beneficiary.

A. Allowed under state law?

The threshold question is whether an assignment by the income beneficiary of his annuity interest to charity is permissible under state law governing the trust. The starting place is to see if there is a spendthrift clause in the trust document. If

[2] PLR 200120016

[3] PLR 200221042

[4] E.g. PLRs 9851006; 200035014; 200045038;200143028; 200221042; 200333013; 200301020; and 200340022

there is no spendthrift clause, then there is no prohibition against the beneficiary making the assignment. If there is a spendthrift clause, the next inquiry is to see whether the beneficiary was also the settlor of the CRT. If the beneficiary is the settlor, the spendthrift clause may be unenforceable under state law.

The next issue under state law is figuring out how to terminate the CRT so that the assets in the CRT can be distributed to the charity. If the charity is the trustee of the CRT, then the issue is simple, since the charity would be both the sole trustee and the sole beneficiary of the CRT. Under the common law doctrine of merger, a trust is deemed to be terminated where the sole trustee and the sole beneficiary is the same person.[5] If the charity is not the trustee, it might be possible for the existing trustee to resign and the Charity to be appointed as successor trustee, thereby making the doctrine of merger applicable.

B. Charitable income tax deduction

1. Is a deduction allowed?

Where the Income beneficiary gives his annuity interest to the charity, the beneficiary is entitled to a charitable deduction in an amount equal to the fair market value of the donated interest pursuant to Revenue Ruling 86-60[6]. That ruling involved two factual situations. In the first situation the donor created a CRAT where he was the income beneficiary for life with the remainder going to a specified charity. In the second situation, the donor created a CRAT where he was the first income beneficiary for life, then another person was a secondary income beneficiary for life, and then the remainder went to charity. In the first situation, the IRS ruled that when the donor transferred his income interest to the charitable remainderman, he received a charitable deduction equal to the market value of his income interest. In the second situation both the primary and secondary income beneficiaries received charitable deductions for the market value of their respective income interests.

2. Partial interest rule

Sections 170(f)(2) and 170(f)(3)[7] set forth certain limitations on the deduction of charitable contributions of partial interests in property. However, the Regulations make it clear that this limitation is inapplicable to a contribution of a partial interest in property if that interest represents the taxpayer's entire interest in the property, such as an income interest.[8] However the Regulation goes on to state that if the property in which such

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[5] Restatement (3rd) of Trusts, Section 69; Estate of Washburn, 11 Cal.App. 735 (1909).

[6] 1986-1 CB 302.

[7] Unless otherwise stated, all section references in this Article are to the Internal Revenue Code.

[8] Reg. §1.170A-7(a)(2)(i).

partial interest exists was previously divided so as to avoid the partial interest rule, then the charitable deduction will not be allowed.

In Rev. Rul. 86-80 this problem was eliminated by a statement in the recitation of facts that no property interests were created for the purpose of avoiding the partial interest rule. It is difficult to see how formation of a CRT could ever be viewed as an attempt to circumvent the partial interest rule. However, the IRS apparently views this as at least a possibility. In issuing private letter rulings, the IRS has required a favorable factual representation on this issue as a requirement of obtaining the ruling.[9] Thus, there is at least a theoretical possibility that in some case the IRS will attempt to argue that a charitable deduction should be disallowed in this situation.

3. Capital asset

In every case in which property is given to charity it is necessary to determine whether or not a hypothetical sale of that property would give rise to long-term capital gain. Under Section 170(e)(1)(A) where the contribution is of ordinary income property or short-term capital gain property, the deduction is limited to the taxpayer's basis. Accordingly, it must be determined whether the income interest given to charity by the beneficiary qualifies as long-term capital gain property.

On the issue of whether the income interest is a capital asset, the leading case is the 1946 decision of the Second Circuit in *McAlister v. Commissioner.*[10] This case held that the proceeds received by a life tenant of a testamentary trust in consideration of a transfer of her interest in the trust to the remainderman are treated as gain from the sale of a capital asset. The IRS had argued that the amount received was a substitute for future ordinary income, and accordingly the gain on the sale of the life estate should be taxed as ordinary income based on assignment of income principles. This argument was rejected by the Second Circuit. In Rev. Rul. 72-243[11] the IRS stated that it would follow the *McAlister* decision. Subsequent to Rev. Rul. 72-243 there have been no cases or published rulings on this issue. However, there have been private letter rulings which have held that an income interest in a CRT is a capital asset, citing *McAlister* and Rev. Rul. 72-243.[12] In addition to the income interest being considered a capital asset, it is necessary for the beneficiary to have more

[9] PLR 9550026; PLR 200152018

[10] 157 F.2d 235 (2nd Cir. 1946).

[11] 1972-1CB 233.

[12] For example, PLR 200152018 and 8613046.

than a 12 month holding period for the income interest so that the capital gain is long-term.

4. Taxation of undistributed CRT gain

If the transfer of the income beneficiary's income interest in a CRT to the charity would cause the income beneficiary to be taxed on any capital gains previously realized by the CRT, the gift would be a tax disaster. Somewhat surprisingly there is very little authority on this issue. In a 1995 private letter ruling, the IRS ruled favorably on this issue.[13] The ruling cited the case of Palmer v. Commissioner[14] for the proposition that a donor does not normally recognize gain on the contribution of appreciated property to a charity.

C. Case study #2

Donor created a CRAT that distributes $70,000 to him for a fixed term of years. When the CRAT assets are valued at $1 million of principal, and has a remaining term of ten years, the Donor decides to make a contribution of his remaining income interest to the charity named as the charitable remainder beneficiary in the CRAT document. Assume that the Section 7520 rate in effect at the time of the gift (not the Section 7520 rate at the time the CRAT was originally established) is 2.6%. The value of the right to receive a $70,000 annuity for 10 years using a 2.6% interest rate is $615,400. Accordingly, the Donor will be entitled to a charitable deduction of this amount. Since it is a gift of a capital asset with a zero basis (see below), his deduction will be limited to 30% of AGI.

IV. Gift of *Partial* Income Interest – "I don't need all the income"

A. Partial interest rule

The general rule of Section 170 (f)(3) that denies a deduction for a charitable contribution of a partial interest in property does not apply to an undivided portion of the donor's entire interest in the property.[15]

B. Case study #3

The donor, a dentist, and his wife funded a CRT several years ago naming themselves as income beneficiaries and the university dental school he attended as the remainder beneficiary. The assets of the trust have a current value of $10 million. The university is planning a new building for the dental school and asks the donor to consider a gift of $2 million. The donor explains that even though he

[13] PLR 9550026; see also PLR 200152018.

[14] 62 TC 684 (1974), affirmed on another issue. 523 F2d 1308 (8th Cir. 1975)

[15] Section 170(f)(3)(B)(ii)

and his wife don't need all the income they receive from the CRT, most of their financial assets are held in the trust. The university planned giving officer suggests that the donor his wife transfer 20% of their income interest in the CRT to the university. Since the university is already the remainder beneficiary as well as the trustee of the trust, this will result in a partial termination of the trust as to this 20%, resulting in an immediate distribution of $2 million from the trust to the university. Assuming a CRT factor of 40%, based on the CRT payout percentage and the ages of the husband and wife, they will be entitled to claim a charitable deduction of $800,000, which may be used up to 30% of AGI.[16] The remaining assets, valued at $8 million, will remain in the CRT to produce income distributions to husband and wife during their lives, with the remainder to the university.

V. Termination of CRT – "I need my share in a lump sum"

Suppose that the income beneficiary wishes to terminate a CRT, but does not plan for the value of her income interest to end up with the charity. Instead, her objectives, and/or perhaps those of the charity, would be best served by terminating the trust now, and dividing the trust assets actuarially between the income and remainder beneficiaries, with the result that each would receive the current value of their respective interests in the trust now, rather than over time (in the case of the income beneficiary) or at some point in the perhaps distant future (in the case of the charity).

A. Mechanics under state law

As always, we need to remember that even though CRTs are creatures of the Internal Revenue Code, they are still trusts that are governed by state trust law. The planner must address the same issues mentioned above:

1. Can an interest in the trust be conveyed?

2. Can the trust be terminated by agreement of the settlor and all beneficiaries?

3. Is a court petition required?

B. Gain recognition

The IRS regards the termination, with the income beneficiary receiving her share of trust assets, as a sale by the income beneficiary to the remainder beneficiary of her interest in the trust, with the amount realized in the sale transaction being the assets received by the beneficiary from the trust

1. Capital Asset

[16] PLR 9550026; PLR 200152018

As noted above, an income interest in a trust is a capital asset.

2. Holding period.

The holding period of the beneficiary's interest in the trust is determined by when the beneficiary acquired her interest. If the trust was established more than 12 months ago, the beneficiary will have a long-term holding period.

3. Basis

The critical question is what is the income beneficiary's basis in her interest in the trust, since this basis will determine the amount, if any, of long term capital gain recognized. As we shall see, the answer is a good clear "it depends."

C. Life expectancy of income beneficiary

In some of the IRS rulings approving the termination of a CRT, with the income beneficiary receiving the actuarial value of her interest in the trust based on her life expectancy, the IRS has required as a condition of the ruling a statement that the income beneficiary has no medical condition that was expected to result in a shorter-than average longevity. The government's concern here is that an income beneficiary with a health condition that gives her a life expectancy shorter than normal might receive a larger share of the CRT assets on termination calculated based on normal life expectancies. These statements are given under penalty of perjury, and have been required of the income beneficiary and her physician,[17] and in other cases only from the income beneficiary.[18] If the plan is to terminate the CRT without seeking a ruling, it would be prudent to obtain a physician statement to be kept in the file in case it is needed for a future IRS inquiry.

D. Case study #4

A CRAT owns a piece of unencumbered rental real property having a current value of $1,000,000 and a basis of $600,000. The beneficiary has the right to receive $70,000 a year from the trust for an additional 10 years. The current AFR is 2.6%, so that the actuarial value of the beneficiary's interest in the CRAT is $615,400 while the value of the charity's interest is $384,600.

Assume a third party Buyer is willing to purchase the property for $1,000,000 and for purposes of simplicity assume there are no closing costs. Both the charity and the income beneficiary desire that the CRT assets be converted into cash, that the CRT be terminated, and that the $1,000,000 be divided between them. Assume

[17] PLR 200208039; PLR 200324035

[18] PLR 200314021; PLR 200304025

the beneficiary and the charity agree that the money will be divided $615,400 to the beneficiary and $384,600 to the charity.[19]

1. Alternative No. 1 – CRT Sells real property and terminates

The simplest structure is for the CRT to sell the real property to the Buyer for $1,000,000. The CRT would then terminate and, by agreement between the Charity and the beneficiary, would distribute $615,400 to the beneficiary and $384,600 to the Charity. The beneficiary will recognize $615,400 of taxable long term capital gain on this transaction.

In this alternative, the entire $615,400 is subject to tax without regard to any tax basis which the CRT has in the real property or any basis which the beneficiary has in his income interest. This result follows from Section 1001(e) which provides that in determining gain from the sale of an income interest in a trust, any basis that would otherwise exist is disregarded. There is an exception contained in Section 1001(e)(3) where the income interest is disposed of in a transaction in which the entire trust interest is transferred to any person. However, the IRS has ruled that this exception is inapplicable in the context of a termination of a CRT, but rather would only be applicable where the income interest and the remainder interest in the CRT are both sold to a third party.[20] Under the IRS analysis the transaction is treated as though the beneficiary sold his CRT income interest to the charity, and the exception is inapplicable since there is no third party involved.

This result may come as a surprise to the beneficiary. For example, assume that the beneficiary is also the settlor of the CRT, and the CRT was initially funded with cash. In this situation the beneficiary will be recognizing taxable gain, although from his standpoint he is simply getting a portion of his own money back.

2. Alternative No. 2 – beneficiary and charity sell CRT interests to buyer

While Alternative No. 1 meets the test of being "simplest", it does not create the best tax result for the income beneficiary. Accordingly, let us consider an alternative technique in which the beneficiary sells his income interest in the CRT to the Buyer for $615,400, and simultaneously

[19] Nothing mandates that the split be based on the current Section 7520 rates, and the income beneficiary and the charity are free to negotiate any other split that is agreeable to them. If the amount received by the income beneficiary is less than the value of the annuity interest, the income beneficiary is entitled to a charitable deduction. For example, in PLR 200152018 the income beneficiary transferred his income interest in a CRT to the charity in exchange for a private annuity; the IRS ruled that a charitable deduction was allowed for the excess of the value of the income interest over the value of the private annuity.

[20] PLR 200314021

the charity sells its remainder interest in the CRT to the Buyer for $384,600.

Under this Alternative No. 2, the exception in Section 1001(e)(3) should be applicable since the annuity interest is being disposed of in a transaction in which the entire interest in the trust is being transferred to a third person. Thus, the beneficiary may not have to include the entire $615,400 received by him in income but can offset part of the amount received with his share of the CRT's $600,000 basis in the real property.

Accordingly, it becomes necessary to determine how much of the $600,000 basis is allocable to the beneficiary. The Regulations contain "uniform basis" rules.[21] Under these rules the uniform basis of the property remains fixed (subject to adjustments for such items as depreciation and capital improvements), but the portion of this basis allocated to the income beneficiary and the remainderman is adjusted to reflect the relative values of such interests resulting from the lapse of time. In some instances the calculations required by these Regulations can be complex, but in the hypothetical example the result is simple – 61.5% of the basis would be allocated to the income beneficiary and 38.5% to the charity. Thus, of the $615,400 received by the income beneficiary, $369,000 (i.e., 61.5% of $600,000) is a recovery of basis, so the amount of taxable gain realized is only $246,000.

3. <u>Alternative No. 3 – CRT sells real property and beneficiary and charity sell CRT interests to buyer</u>

In Alternative No. 1, the beneficiary recognized $615,400 of taxable gain. In Alternative No. 2, that gain was reduced to only $246,000. Can we improve on that result if the CRT sells the property for $1,000,000 cash, followed by a sale by the beneficiaries and charity of their interests to the buyer in order to invoke the exception in Section 1001(e)(3)?

Under Alternative 3, the CRT would sell the real property for $1,000,000 for cash. The cash, of course, has a tax basis of $1,000,000 which would seem to suggest that under the uniform basis rule 61.5% of this amount, or $615,000, would be the basis of the beneficiary's income interest. If the charity and beneficiary join together to sell their respective interests to a third party for $1,000,000, the beneficiary should realize little or no taxable gain.

However, the Regulations prevent this result. Section 1.1014-5(c) provides that in the case of the sale of the income interest in a CRT, the income beneficiary's pro rata share of the uniform basis is reduced by the beneficiary's pro rata share of the CRT's undistributed capital gains. In

[21] Reg. §1.1015-1(b); Reg. §1.1014-5.

our example, the beneficiary's basis in the income interest would be reduced to the same figure as her share of the uniform basis when the CRT still held the real property, in Alternative 2, with the result that the capital gain recognized by the beneficiary, when the charity and beneficiary sell their CRT interests in the same transaction to the same third party purchaser, will be the same in Alternatives 2 and 3.

E. Case Study #5

The income beneficiary of a CRT desires to terminate the trust with the trust assets to be actuarially divided between the income beneficiary and the charitable remainder beneficiary, which is a private foundation, and seeks an IRS ruling in line with previous rulings approving this type of termination. The IRS grants the favorable ruling. [22] So far, so good. But then something unexpected happens – the IRS revokes its earlier ruling, saying that the early termination constitutes a prohibited act of self dealing under Section 4941.[23] This is consistent with the way in which the IRS characterizes the termination of a CRT, that is as a *sale* by the income beneficiary of his interest in the trust to the charitable remainder beneficiary in exchange for sales proceeds equal to the actuarial value of the income interest. Of course, if the remainder beneficiary is a private foundation, a purchase of assets from a disqualified person would be squarely within the definition of an act of self dealing.[24] If the income beneficiary was the original creator of the CRT, or a family member of that person, the beneficiary would be with the category of disqualified persons as a substantial contributor to the private foundation.[25] This one CRT resulted in a third ruling when the income beneficiary, using a power that had been reserved to him in the trust document, substituted a public charity for the private foundation, so that the public charity would receive the distribution of the actuarial value of the remainder interest, and the deemed sale would not be with a private foundation. With this change, the IRS blessed the termination and issued a favorable ruling.[26]

VI. Transforming the Income Stream – "I need more income"

A. The CRT Rollover

1. A large number of CRUTs, especially those originating in the financial planning context, contain a net-income limitation. For whatever reason the situation arises, it is increasingly common for the income beneficiary

[22] PLR 200525014

[23] PLR 200614032

[24] Section 4941(d)(1)(A)

[25] Section 4946(a)(1)(A)

[26] PLR 200616035

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of a NICRUT or NIMCRUT to conclude that the trust simply distributes too little income as a result of the income limitation.

2. One possibility is for the income beneficiary to transfer her interest in the NICRUT to a standard CRUT, followed by the termination of the NICRUT and distribution of its assets to the two beneficiaries – the charitable remainderman and the new standard CRUT. Following these steps, the individual will be the income beneficiary of a standard CRUT funded with the actuarial equivalent of his income interest in the NICRUT.

   a) Of course, the planner will need to inquire whether the transfer of the NICRUT income interest is allowable under state law. E.g., does the trust agreement contain a spendthrift clause? Is it enforceable?

   b) Case study #6

      The husband and wife income beneficiaries, both age 65, established an 11% NICRUT several years ago. The value of its assets is $1 million, but it only generates income of 2.5% (current yield of interest and dividends), or $25,000 per year. They need twice that to live on. The planner determines that the current actuarial value of their income interest in the NICRUT is $900,000. The plan is to transfer their income interest to a standard 6% CRUT that will initially distribute $54,000 per year, and will maintain or grow that income level if the trust assets can be invested for an 6% or greater total return. The new trust will be funded with a capital asset with a value of $900,000, resulting in a charitable deduction of $247,860.[27] But the new SCRUT can only invest and distribute if the old NICRUT is terminated. Here, the charitable remainderman has an incentive to agree to the termination, since it not only will receive the immediate terminating distribution from the NICRUT of $100,000, it will also continue to hold a remainder interest in the SCRUT with a value of $247,860.

      Query #1 from Inquiring Minds: How can it possibly be that the "donors" are able to double their income from an irrevocable trust and be entitled to a charitable deduction in the process? It is because the method dictated by Code section 664(e), as amended in 2015 by the PATH Act does not take the income limitation into account so an 11% unitrust interest in which only 2.5% current

[27] Of course, a qualified appraisal is required to substantiate the charitable deduction (Section 170(f)(11)).

yield is distributed is valued the same as an 11% unitrust interest in which the full unitrust amount is actually distributed.[28]

Query #2 from Inquiring Minds: The charity in this case jumped at the opportunity to "roll over" the old NICRUT into the new SCRUT, since it received the immediate terminating distribution from the NICRUT of $100,000 (when it otherwise might have waited another 25 years to receive anything from this trust), plus it is still holds the remainder interest with a greater present value. But is the charity really better off? If everything remained the same (always a dangerous assumption), the value of the remainder in the NICRUT was growing by total return in excess of the 2.5% current income of dividends and interest. Now, however, its remainder will grow only by any total return in excess of the 6% total return – a much higher threshold to clear.

B. Gift Annuity Funded with CRT Income Interest

1. Perhaps the charity can assist the donor in accomplishing the same objective by issuing a charitable gift annuity in exchange for the income interest in the trust

2. Case Study #7

Same facts as the previous case study, except the planner asks the charity to consider issuing a CGA at its standard ACGA rates to the husband and wife, in exchange for the contribution of their income interest in the NICRUT. The couple will use their power under the trust agreement to name the charity as the successor trustee to that the trust may immediately terminate under the doctrine of merger. The charity informs the planner that its standard ACGA rate for a 2 life annuity for annuitants both age 65 is 4.2%, resulting in an annuity for their joint lives, based on the $900,000 actuarial value of the NICRUT income interest, of $37,800 or a 50+% improvement over the current income stream from the NICRUT. These donors would be able to claim a deduction of about $263,835.[29]

C. Solutions Under the Principal and Income Trust Accounting Rules

1. The low current yield of the NICRUT in the previous case study may be augmented by realized capital gains of the trust – the total return may be higher when these gains, normally allocated to income and not to principal, are taken into account. The distributable income might be increased if the trustee has a power to allocate trust receipts between the income and principal accounts to better balance the respective interests of

[28] *Caveat:* see Note 27 above

[29] Same *caveat* regarding the true fair market value of the income interest. See note 27 above.

the income and remainder beneficiaries, as the trustee would have under the Revised Uniform Principal and Income Act.[30] However, that power may typically not be exercised by the trustee if the trustee is also a beneficiary of the trust.[31]

2. Another solution is suggested by another provision of the Revised Uniform Principal and Income Act that contains the general rule that if a trust holds an interest in an entity such as a corporation or partnership, it will have income from that entity when and to the extent it receives a distribution from the entity.[32]

3. Case Study #8

Same facts as the previous case study. The planner suggests that the income beneficiaries form a partnership with the NICRUT, with husband and wife holding a 1% interest in the partnership and the NICRUT holding a 99% interest. The trust contributes $1 million to the partnership and the husband and wife contribute 1/99 of this amount, $10,101. The plan for the partnership is to invest for total return and each year distribute 6% of the value of the partnership portfolio at the beginning of the year. Since each distribution from the partnership to the NICRUT will be income under RUPIA, the entire amount will be distributable to the husband and wife. Their income from the NICRUT will increase to $60,000 in the first year.

a) The IRS is not unaware of this planning technique for controlling the income of a NICRUT. On its annual list of areas in which it refuses to issue a ruling, it includes whether a NIMCRUT qualifies as a charitable remainder trust if certain individuals can control the timing of the trust's receipt of income from a partnership of a deferred annuity contract.[33]

VII. Rescission of CRT -- "This just isn't working for me"

A. The gift plan may have been a mistake from the beginning, for a variety of reasons. However, for the trustors to be able to completely undo the trust and recover all trust assets, with nothing going to the charitable remainder beneficiary, they must first satisfy state law requirements for rescission of a trust. The

[30] RUPIA § 104

[31] RUPIA § 104

[32] RUPIA § 401(b)

[33] Rev Proc 2017-3. I.R.B. 2017-1

standard grounds are that the trust was created on the basis of fraud, duress, undue influence or mistake (with mistake being by far the most common in IRS rulings)

B. Examples

1. Donors obtained rescission from the court based on a claimed "substantial mistake of law and fact in the execution of" a CRT, due to mistaken advice from the charity regarding the tax consequences of the gift (Donors created an SCRUT when a NICRUT or NIMCRUT was apparently intended).[34]

2. If a trust does not satisfy the 10% requirement for the minimum value for the charitable interest, it may well be "null and void *ab initio*"[35]

C. Income Tax Consequences

1. If rescission occurs in the same year the trust is created, there are no consequences – there is no charitable deduction for funding the trust and the trustor is treated as continuing to own the property that was transferred to the trust.[36]

2. If rescission occurs in a later year, Rev Rul 80-58 suggests that the charitable deduction should be allowed for the year the trust is created, but then recaptured as income in the year of rescission.[37]

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[34] PLR 200219012

[35] Sections 2055(e)(3)(J) and 170(f)(7)

[36] Rev Rul 80-58, 1980-1C.B. 181

[37] See also *Rosen* 611 F. 2d 942 (1st Cir 1980)