

if investment adjustments made to the basis of shares of S1 stock affect the investment adjustments made to the basis of shares of S stock. The” is corrected to read “bases of shares of S2 stock under § 1.1502–32 affect the investment adjustments made to the bases of shares of S1 stock. A subsidiary (S1) (and its shares of stock) is lower tier with respect to another subsidiary (S) (and its shares of stock) if investment adjustments made to the bases of shares of S1 stock affect the investment adjustments made to the bases of shares of S stock. The”.

86. On page 3019, column 1, § 1.1502–36(g)(2) *Example 3.(ii)*, line 4 of the paragraph, the language “there is no disparity in the basis of the” is corrected to read “there is no disparity in the bases of the”.

87. On page 3019, column 1, § 1.1502–36(g)(2) *Example 4.(i)*, lines 5 through 6 from the bottom of the paragraph, the language “equal basis that exceeds value. S owns Asset 1 with a basis that exceeds value and cash.” is corrected to read “equal basis that exceeds value. S owns Cash and Asset 1 with a basis that exceeds value.”.

88. On page 3019, column 1, § 1.1502–36(g)(2) *Example 4.(ii)*, line 4 of the paragraph, the language “there is no disparity in the basis of the” is corrected to read “there is no disparity in the bases of the”.

**LaNita Van Dyke,**

*Chief, Publications and Regulations Branch, Legal Processing Division, Associate Chief Counsel (Procedure and Administration).*

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**DEPARTMENT OF THE TREASURY**

**Internal Revenue Service**

**26 CFR Part 20**

[REG–119097–05]

RIN 1545–BE52

**Grantor Retained Interest Trusts—  
Application of Sections 2036 and 2039**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Notice of proposed rulemaking and notice of public hearing.

**SUMMARY:** This document contains proposed regulations providing guidance on the portion of a trust properly includible in a grantor’s gross estate under Internal Revenue Code (Code) sections 2036 and 2039 if the grantor has retained the use of property in a trust or the right to an annuity,

unitrust, or other income payment from such trust for life, for any period not ascertainable without reference to the grantor’s death, or for a period that does not in fact end before the grantor’s death. This document also provides notice of a public hearing on these proposed regulations.

**DATES:** Written or electronic comments must be received by September 5, 2007. Outlines of topics to be discussed at the public hearing scheduled for September 26, 2007, must be received by September 5, 2007.

**ADDRESSES:** Send submissions to: CC:PA:LPD:PR (REG–119097–05), Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered to the Courier’s Desk, Internal Revenue Service, Attn: CC:PA:LPD:PR (REG–119097–05), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington DC 20044. Alternatively, submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–119097–05), Courier’s Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington DC, or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG–119097–05). The public hearing will be held in the auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

**FOR FURTHER INFORMATION CONTACT:** Concerning the proposed regulations, Theresa M. Melchiorre, (202) 622–7830; concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Richard Hurst, (202) 622–7180 (not toll-free numbers) or e-mail at [Richard.A.Hurst@irs.counsel.treas.gov](mailto:Richard.A.Hurst@irs.counsel.treas.gov).

**SUPPLEMENTARY INFORMATION:**

**Background**

The proposed regulations provide guidance on what portion of a trust is includible in the deceased grantor’s gross estate under section 2036 if the grantor retained the right to use property in the trust or the right to receive from that trust an annuity, unitrust, or other income payment for the grantor’s life, for any period not ascertainable without reference to the grantor’s death, or for any period that does not in fact end before the grantor’s death. In addition, the proposed regulations provide guidance on the possible application of section 2039 to trusts in which the decedent has retained the use of property held in the trust or has retained an annuity,

unitrust, or other income interest that is includible in the decedent’s gross estate under section 2036. These trusts include without limitation certain charitable trusts (collectively CRTs) such as charitable remainder annuity trusts (CRATs) within the meaning of section 664(d)(1), charitable remainder unitrusts (CRUTs) within the meaning of section 664(d)(2) or (d)(3), and charitable remainder trusts that do not qualify under section 664, as well as other trusts established by a grantor (collectively GRTs) such as grantor retained annuity trusts (GRATs), grantor retained unitrusts (GRUTs), and various forms of grantor retained income trusts (GRITs), such as qualified personal residence trusts (QPRTs) and personal residence trusts (PRTs). A CRT is within the scope of these proposed regulations whether or not the CRT meets the qualifications of sections 664(d)(1), (2), or (3) and a GRT is within the scope of these proposed regulations whether or not the grantor’s retained interest is a “qualified interest” as defined in section 2702(b). This guidance does not apply to trusts or other contractual arrangements arising by reason of a decedent’s employment and generally does not apply to annuities purchased by the decedent, as these types of interests fall within the ambit of section 2039.

Under section 2036(a), a decedent’s gross estate includes the value of any interest in property transferred by the decedent in which the decedent retained for the decedent’s life, for any period not ascertainable without reference to the decedent’s death, or for any period that does not in fact end before the decedent’s death, either the possession or enjoyment of the property or a right to the income from the property, or the right (either alone or with another) to designate the persons who may possess or enjoy the property or its income. Section 20.2036–1(a) provides generally that, if the decedent retained or reserved an interest with respect to all of the property transferred by the decedent, the amount to be included in the gross estate under section 2036 is the value of the entire property on the date of death. If the decedent retained a right with respect to only part of the property transferred, the amount to be included in the decedent’s gross estate under section 2036 is the corresponding proportionate amount of the corpus. Rev. Rul. 76–273, 1976–2 CB 268, and Rev. Rul. 82–105, 1982–1 CB 133 (See § 601.601(d)(2)), generally provide that the portion of the corpus of a CRUT and CRAT includible in the decedent’s gross estate under section

2036 is that portion of the trust corpus necessary to generate a return sufficient to provide the decedent's retained annuity or unitrust payment.

Rev. Rul. 76-273 considers a situation where the decedent created an *intervivos* trust that provided for a stated unitrust percentage of 6 percent to be paid each year to the decedent during life. At the decedent's death, the remainder is to be paid to a charitable organization. The revenue ruling concludes that, for purposes of section 2036(a), the portion of the value of the trust corpus includible in the decedent's gross estate is the portion necessary to yield (at the then current interest rate specified under the applicable regulations) the amount of the annual unitrust payment in perpetuity. Based upon the valuation rules and interest rate assumptions specified in § 20.2031-10 (the regulations applicable at the time the ruling was issued), the revenue ruling provides the following formula to be used to determine this includible portion of the trust corpus: Equivalent income interest rate divided by the interest rate mandated by the applicable regulations at the date of death, where the equivalent income interest rate = adjusted payout rate/1 minus adjusted payout rate. The result, however, is limited to 100 percent of the trust corpus. (Since the issuance of this revenue ruling, the regulations (§ 20.2031-7(d)(1)) have been changed to instead require the use of the section 7520 interest rate in lieu of the rate specified in § 20.2031-10.) The revenue ruling concludes that, because the equivalent income interest of the unitrust payment exceeds the equivalent income interest required to produce that unitrust payment, the grantor retained an interest in the entire corpus of the trust, and thus the entire trust corpus is includible in the deceased grantor's gross estate under section 2036.

Rev. Rul. 82-105 considers a situation where the decedent created an *intervivos* CRAT, pursuant to which the decedent retained the right to receive a fixed annuity for life. The ruling confirms that the decedent's retained annuity represents the retained right to receive all of the income from all or a specific portion of the trust for purposes of section 2036. That portion of the trust corpus with respect to which the decedent retained a right to receive all of the income is properly includible in the decedent's gross estate under section 2036(a)(1). Under the ruling, the amount of the corpus with respect to which the decedent retained the income is that amount of corpus that would be sufficient to yield the annual annuity based on the assumed rate of return

prescribed by the regulations as of the applicable valuation date. The ruling prescribes the following formula for this determination: (Annual Annuity) / (Assumed Rate of Return) = Amount Includible. Assuming a rate of return of 6 percent, as specified under § 20.2031-10 (the regulation applicable at the time the ruling was issued), the ruling concludes that only a portion of the trust's corpus is includible in the deceased grantor's gross estate. (Since the issuance of this revenue ruling, the regulations (§ 20.2031-7(d)(1)) have been changed to instead require the use of the section 7520 interest rate in place of the rate specified in § 20.2031-10.) Rev. Rul. 82-105 expressly qualifies this conclusion by stating that the ruling does not consider the amount, if any, that may be includible in the gross estate under any other provisions of the Code.

Section 2039(a) provides that a decedent's gross estate includes the value of an annuity or other payment under any form of contract or agreement (other than an insurance policy on the decedent's life) receivable by any beneficiary by reason of surviving the decedent if, under the contract or agreement, an annuity or other payment was payable to the decedent, or the decedent possessed the right to receive such annuity or other payment, for the decedent's life or for any period not ascertainable without reference to the decedent's death, or for any period that does not in fact end before the decedent's death.

Section 2039(b) provides, in part, that the amount includible in the decedent's gross estate is limited to that portion of the value of the annuity or other payment receivable under the contract or agreement as is proportionate to the portion of the purchase price of the contract or agreement that was contributed by the decedent. Section 20.2039-1(b)(1) provides, in part, that the term "annuity or other payment," as used with respect to both the payment receivable by the decedent and by the beneficiary, has reference to one or more payments extending over any period of time, whether the payments are equal or unequal, conditional or unconditional, periodic or sporadic. The term "contract or agreement" includes any arrangement, understanding, or plan, or any combination of them, arising by reason of the decedent's employment. Section 20.2039-1(b)(1).

As is acknowledged in Rev. Rul. 82-105, section 2036 as well as other sections of the Code might apply to the same interest or trust for purposes of the Federal estate tax. Although either section 2036 or section 2039 may be

applied to include at least some portion of a trust in the decedent's gross estate if the decedent transfers property during life to a trust and retains the right to use the trust's property or the right to an annuity, unitrust, or other payment from the trust, the amount includible may differ depending upon which section is applied for this purpose.

#### Explanation of Provisions

The proposed regulations amend § 20.2036-1 to incorporate the guidance provided in Rev. Rul. 76-273 and Rev. Rul. 82-105. The proposed regulations provide that, if a decedent transfers property during life to a trust and retains the right to an annuity, unitrust, or other income payment from, or retains the use of an asset in, the trust for the decedent's life, for a period that does not in fact end before the decedent's death, or for a period not ascertainable without reference to the decedent's death, the decedent has retained the right to income from all or a specific portion of the property transferred as described in section 2036. The portion of the trust corpus includible in the decedent's gross estate is that portion of the trust corpus, valued as of the decedent's death (or the alternate valuation date, if applicable) necessary to yield that annual payment (or use) using the appropriate section 7520 interest rate. In this regard, because the specific portion of corpus includible in the gross estate is properly determined as of the decedent's death, the appropriate section 7520 rate is the rate in effect on the decedent's date of death (or on the alternate valuation date, if applicable). The proposed regulations provide both rules and examples for calculating the amount of trust corpus to be included in a deceased grantor's gross estate under section 2036 in such a case.

The IRS and Treasury Department believe that in many cases both section 2036 and section 2039 may be applicable to these annuity and unitrust interests and to such other payments retained by a deceased grantor. Although the language of section 2039 is broad enough to include all or a portion of a trust's corpus if the grantor retains an annuity or unitrust interest in, or other payments from, a trust, the IRS and Treasury Department believe that, in the interest of ensuring similar tax treatment for similarly situated taxpayers, it is appropriate in this circumstance to provide regulatory rules under which only one of these two potentially applicable Code sections (section 2036 and section 2039) will be applied in the future. For the reasons mentioned below, the IRS and Treasury

Department have concluded that section 2036 (and therefore, when applicable, section 2035), rather than section 2039, will be applied in the future to these interests. First, section 2039 appears to have been intended to address annuities purchased by or on behalf of the decedent and annuities provided by the decedent's employer. Second, the interests retained by grantors in the types of trusts described in this guidance are more similar in most relevant respects to the interests addressed under section 2036 than those most clearly addressed under section 2039. Accordingly, the proposed regulations also amend § 20.2039-1(b)(1) by providing that section 2039 shall not be applied to an annuity, unitrust, or other payment retained by a deceased grantor in a CRT or GRT.

Although these proposed regulations provide guidance as to which section of the Code (specifically, section 2036 or section 2039) is to be used in certain circumstances when each of those sections applies to the same CRT or GRT, these proposed regulations should not be construed to imply that only one section of the Code may apply to a particular situation or interest. These proposed regulations are not intended to foreclose the possibility that any applicable section of the Code (sections 2035 through 2039, or any other section) properly may be applied in the future by the IRS in appropriate circumstances beyond those described in these proposed regulations. (For example, although section 2039 generally will apply to govern the includability of annuities purchased by or on behalf of the decedent and annuities provided by the decedent's employer in the decedent's gross estate, section 2036 may instead be applied if the facts and circumstances indicate that the annuity constituted a retained interest in the property exchanged for that annuity.)

#### Proposed Effective Date

The first, second, and fourth sentences in § 20.2039-1(a) and the provisions in § 20.2036-1(a)(1), (a)(2), and (c)(1)(i) are applicable to the estates of decedents dying after August 16, 1954. The fifth sentence of § 20.2039-1(a) is applicable to the estates of decedents dying on or after October 27, 1972, and to the estates of decedents for which the period for filing a claim for credit or refund of an estate tax overpayment ends on or after October 27, 1972. The provisions of § 20.2036-1(c)(1)(ii) and (2), § 20.2039-1(e), and the third, sixth, and seventh sentences of § 20.2039-1(a) apply to the estates of decedents for which the valuation date of the gross estate is on or after the date

of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

#### Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

#### Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department also request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for September 26, 2007 in the auditorium Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must use the main building entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For more information about having your name placed on the list to attend the hearing, see the **FOR FURTHER INFORMATION CONTACT** section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written (a signed original and eight (8) copies) or electronic comments by September 5, 2007 and an outline of the topics to be discussed and the time to be devoted to each topic by September 5, 2007. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for

receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

#### Drafting Information

The principal author of these regulations is Theresa M. Melchiorre, Office of Chief Counsel, IRS.

#### List of Subjects in 26 CFR Part 20

Estate taxes, Reporting and recordkeeping requirements.

#### Proposed Amendments to the Regulations

Accordingly, 26 CFR part 20 is proposed to be amended as follows:

#### PART 20—ESTATE TAX; ESTATES OF DECEDENTS DYING AFTER AUGUST 16, 1954

**Paragraph 1.** The authority citation for part 20 continues to read in part as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

**Par. 2.** Section 20.2036-1 is amended by:

1. Redesignating paragraphs (a)(i) and (a)(ii) as paragraphs (a)(1) and (a)(2), respectively.

2. Designating the undesignated text following newly-designated paragraph (a)(2) as paragraph (c)(1)(i) and adding new paragraph headings.

3. Adding paragraphs (c)(1)(ii), (c)(2), and (c)(3).

The additions read as follows:

#### § 20.2036-1 Transfers with retained life estate.

\* \* \* \* \*

(c) *Retained or reserved interest*—(1) *Amount included in gross estate*—(i) *In general.* \* \* \*

(ii) *Example.* The application of paragraph (c)(1)(i) of this section is illustrated in the following example:

*Example.* In 2001, Decedent (D) creates an irrevocable inter vivos trust. The terms of the trust provide that all of the trust's income is to be paid to D and E, D's spouse who is a U.S. citizen, in equal shares during their joint lives and, on the death of either of them, all of the income is to be paid to the survivor of them. On the death of the survivor of D and E, the remainder is to be paid to another individual, F. In 2006, D dies with E still surviving. A portion of the trust's corpus is includible in D's gross estate because D retained the right to receive a portion of the income from the trust for a period that does not in fact end before D's death. The portion of the trust's corpus includible in D's gross estate bears the same ratio to the entire corpus as D's income interest in the trust bears to the entire income interest in the trust. Therefore, in this case, because D and E share equally in the trust's income, 50 percent of the trust's corpus is includible in D's gross estate under section 2036. If instead

E had predeceased D, D would have died while entitled to all of the income from the trust, so that the entire trust corpus would have been includible in D's gross estate under section 2036.

(2) *Retained annuity and unitrust interests in trusts*—(i) *In general.* This paragraph (c)(2) applies to a grantor's retained use of an asset held in trust or a retained annuity, unitrust, or other income interest in any trust (other than a trust constituting an employee benefit) including without limitation the following (collectively referred to in this paragraph (c)(2) as "trusts"): Certain charitable trusts (collectively CRTs) such as a charitable remainder annuity trust (CRAT) within the meaning of section 664(d)(1), a charitable remainder unitrust (CRUT) within the meaning of section 664(d)(2) or (d)(3), and any charitable remainder trust that does not qualify under section 664(d), as well as other trusts established by a grantor (collectively GRTs) such as a grantor retained annuity trust (GRAT), a grantor retained unitrust (GRUT), and various other forms of grantor retained income trusts (GRITs), whether or not the grantor's retained interest is a qualified interest as defined in section 2702(b), including without limitation qualified personal residence trusts (QPRTs) and personal residence trusts (PRTs). If a decedent transferred property into such a trust, and retained or reserved the right to use such property or the right to an annuity, unitrust, other income interest in such trust with respect to the property so transferred by the decedent, or to determine the persons who may possess or enjoy the property or its income, for the decedent's life, for any period not ascertainable without reference to the decedent's death, or for a period that does not in fact end before the decedent's death, then the decedent's right to use the property or retained annuity, unitrust, or other income interest (or to designate the beneficiaries of the property) represents the retained right to receive all of the income from all or a specific portion of the trust for purposes of section 2036. The portion of the trust's corpus includible in the decedent's gross estate for Federal estate tax purposes is that portion of the trust corpus necessary to yield the decedent's retained use or retained annuity, unitrust, other income payment as determined in accordance with § 20.2031-7 (or § 20.2031-7A, if applicable).

(ii) *Examples.* The application of paragraph (c)(2)(i) of this section is illustrated in the following examples:

*Example 1.* (i) In 2000, Decedent (D) transferred \$100,000 to a trust that qualifies as a CRAT under section 664(d)(1). The trust

agreement provides for an annuity of \$12,000 to be paid each year to D for D's life, then to D's child (C) for C's life, with the remainder to be distributed upon the survivor's death to N, a charitable organization described in sections 170(c), 2055(a), and 2522(a). The annuity is payable to D or C, as the case may be, annually on each December 31st. D died in 2006, survived by C who was then age 40. On D's death, the value of the trust assets was \$300,000 and the section 7520 interest rate was 6 percent. D's executor did not elect to use the alternate valuation date.

(ii) The amount of corpus with respect to which D retained the right to the income, and thus the amount includible in D's gross estate under section 2036, is that amount of corpus necessary to yield the annual annuity payment to D. In this case, the formula for determining the amount of corpus necessary to yield the annual annuity payment to D is: annual annuity/section 7520 interest rate = amount includible under section 2036. The amount of corpus necessary to yield the annual annuity is  $\$12,000 / .06 = \$200,000$ . Therefore, \$200,000 is includible in D's gross estate under section 2036(a)(1). (The result would be the same if D had irrevocably relinquished D's annuity interest no more than 3 years prior to D's death because of the application of section 2035.) D's estate is entitled to a charitable deduction under section 2055 for the present value of N's remainder interest in the CRAT. The applicable annuity factor (based on C's age on D's death and the section 7520 rate applicable on that date) is 14.1646. Therefore, the present value of the annuity is  $\$169,975.20$  ( $14.1646 \times \$12,000$ ). As a result, the allowable charitable deduction for D's estate is  $\$30,024.80$  ( $\$200,000 - \$169,975.20$ ). Under the facts presented, the Internal Revenue Service (IRS) will not seek (and the estate will not be permitted) to include under section 2039 any amount in D's gross estate by reason of this retained annuity. See § 20.2039-1(e).

*Example 2.* (i) D transferred \$100,000 to a GRAT in which D's annuity is a qualified interest described in section 2702(b). The trust agreement provides for an annuity of \$12,000 per year to be paid to D for a term of ten years or until D's earlier death. The annuity amount is payable at the end of each month in twelve equal installments. At the expiration of the term of years or on D's earlier death, the remainder is to be distributed to C, D's child. No additional contributions were made to the trust after D's transfer at the creation of the trust. D dies prior to the expiration of the ten-year term. On the date of D's death, the value of the trust assets was \$300,000 and the section 7520 interest rate was 6 percent. D's executor did not elect to use the alternate valuation date.

(ii) The amount of corpus with respect to which D retained the right to the income, and thus the amount includible in D's gross estate under section 2036, is that amount of corpus necessary to yield the annual annuity payment to D. In this case, the formula for determining the amount of corpus necessary to yield the annual annuity payment to D is: annual annuity (adjusted for monthly

payments)/section 7520 interest rate = amount includible under section 2036. The Table K adjustment factor for monthly annuity payments in this case is 1.0272. Thus, the amount of corpus necessary to yield the annual annuity is  $(\$12,000 \times 1.0272) / .06 = \$205,440$ . Therefore, \$205,440 is includible in D's gross estate under section 2036(a)(1). Under the facts presented, the IRS will not seek (and the estate will not be permitted) to include under section 2039 any amount in D's gross estate by reason of this retained annuity. See § 20.2039-1(e).

*Example 3.* (i) In 2000, D created a CRUT within the meaning of section 664(d)(2). The trust instrument directs the trustee to hold, invest, and reinvest the corpus of the trust and to pay to D for D's life, and then to D's child (C) for C's life, in equal quarterly installments payable at the end of each calendar quarter, an amount equal to 6 percent of the fair market value of the trust as valued on December 15 of the prior taxable year of the trust. At the termination of the trust, the then corpus, together with any and all the accrued income, is to be distributed to N, a charitable organization described in sections 170(c), 2055(a), and 2522(a). D died in 2006, survived by C, who was then age 55. The value of the trust assets on D's death was \$300,000 and D's executor did not elect to use the alternate valuation date.

(ii) The amount of the corpus with respect to which D retained the right to the income, and thus the amount includible in D's gross estate under section 2036, is that amount of corpus necessary to yield the unitrust payments. In this case, such amount of corpus is determined by dividing the trust's equivalent income interest rate by the section 7520 rate (which was 6 percent at the time of D's death). The equivalent income interest rate is determined by dividing the trust's adjusted payout rate by the excess of 1 over the adjusted payout rate. Based on § 1.664-4(e)(3) of the Income Tax Regulations, the appropriate adjusted payout rate for the trust at D's death is 5.786 percent (6 percent  $\times$  .964365). Thus, the equivalent income interest rate is 6.141 percent (5.786 percent / (1—5.786 percent)). The ratio of the equivalent interest rate to the assumed interest rate under section 7520 is 102.35 percent (6.141 percent / 6 percent). Because this exceeds 100 percent, D's retained payout interest exceeds a full income interest in the trust, and D effectively retained the income from all the assets transferred to the trust. Accordingly, because D retained for life an interest at least equal to the right to the income from all the property transferred by D to the CRUT, the entire value of the corpus of the CRUT is includible in D's gross estate under section 2036(a)(1). D's estate is entitled to a charitable deduction under section 2055 for the present value of N's remainder interest in the CRAT. The remainder factor (based on C's age at D's death, the section 7520 rate in effect on D's death, and the timing and frequency of the payments) is 0.28253. Therefore, the charitable deduction allowable to D's estate is  $\$84,759$  ( $\$300,000 \times 0.28253$ ). Under the facts presented, the IRS will not seek (and the estate will not be permitted) to include under section 2039 any amount in D's gross estate by reason of D's retained unitrust interest. See § 20.2039-1(e).

(iii) If instead D had retained the right to a unitrust amount having an adjusted payout for which the corresponding equivalent interest rate would be less than the 6 percent assumed interest rate of section 7520, then a correspondingly reduced proportion of the trust corpus would be includible in D's gross estate under section 2036(a)(1). Alternatively, if the interest retained by D was instead only one-half of the 6 percent unitrust interest, the computation of the portion of the trust includable in D's gross estate (set forth in *Example 3* (ii)) would be reduced by one-half. In each case, the amount of the estate's charitable deduction for the remainder interest in the trust also would be reduced. All of the results in this *Example 3* (except those relating to the charitable deduction) would be the same if the trust was a GRUT instead of a CRUT.

*Example 4.* During D's life, D established a 15-year GRIT for the benefit of individuals who are not members of D's family within the meaning of section 2704(c)(2). D retained the right to receive all of the net income from the GRIT, payable annually, during the GRIT's term. D died during the third year of the GRIT term. D's executor did not elect to use the alternate valuation date. In this case, the GRIT's corpus is includible in D's gross estate under section 2036 because D retained the right to receive all of the income from the GRIT for a period that did not in fact end before D's death. If instead, D had retained the right to receive 60 percent of the GRIT's net income, then 60 percent of the GRIT's corpus would have been includible in D's gross estate under section 2036.

*Example 5.* D transferred D's personal residence to a trust that met the requirements of a qualified personal residence trust (QPRT) as set forth in § 25.2702-5(c) of this chapter. Pursuant to the terms of the QPRT, D retained the right to use the residence for 10 years or until D's prior death. D died before the end of the term. D's executor did not elect to use the alternate valuation date. In this case, the fair market value of the QPRT's assets on the date of D's death are includible in D's gross estate under section 2036 because D retained the right to use the residence for a period that did not in fact end before D's death.

(3) *Effective dates.* Paragraphs (a)(1), (a)(2), and (c)(1)(i) of this section are applicable to the estates of decedents dying after August 16, 1954. Paragraphs (c)(1)(ii) and (c)(2) of this section apply to the estates of decedents for which the valuation date of the gross estate is on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

**Par. 3.** Section 20.2039-1 is amended by:

1. Revising paragraph (a).
2. Adding a new paragraph (e).

The revision and addition reads as follows:

**§ 20.2039-1 Annuities.**

(a) *In general.* A decedent's gross estate includes under section 2039(a)

and (b) the value of an annuity or other payment receivable by any beneficiary by reason of surviving the decedent under certain agreements or plans to the extent that the value of the annuity or other payment is attributable to contributions made by the decedent or his employer. Section 2039(a) and (b), however, has no application to an amount which constitutes the proceeds of insurance under a policy on the decedent's life. Paragraph (b) of this section describes the agreements or plans to which section 2039(a) and (b) applies; paragraph (c) of this section provides rules for determining the amount includible in the decedent's gross estate; paragraph (d) of this section distinguishes proceeds of life insurance; and paragraph (e) of this section distinguishes annuity, unitrust, and other income interests retained by a decedent in certain trusts. The fact that an annuity or other payment is not includible in a decedent's gross estate under section 2039(a) and (b) does not mean that it is not includible under some other section of part III of subchapter A of chapter 11. However, see section 2039(c) and (d) and § 20.2039-2 for rules relating to the exclusion from a decedent's gross estate of annuities and other payments under certain "qualified plans." Further, the fact that an annuity or other payment may be includible under section 2039(a) will not preclude the application of another section of chapter 11 with regard to that interest. For annuity interests in trust, see paragraph (e)(1) of this section.

\* \* \* \* \*

(e)(1) *No application to certain trusts.* Section 2039 shall not be applied to include in a decedent's gross estate all or any portion of a trust (other than a trust constituting an employee benefit, but including those described in the following sentence) if the decedent retained a right to use property of the trust or retained an annuity, unitrust, or other income interest in the trust, in either case as described in section 2036. Such trusts include without limitation the following (collectively referred to in this paragraph (e)(1) as "trusts"): certain charitable trusts (collectively CRTs) such as a charitable remainder annuity trust (CRAT) within the meaning of section 664(d)(1), a charitable remainder unitrust (CRUT) within the meaning of section 664(d)(2) or (d)(3), and any other charitable remainder trust that does not qualify under section 664(d), as well as other trusts established by a grantor (collectively GRTs) such as a grantor retained annuity trust (GRAT), a grantor retained unitrust (GRUT), and various

forms of grantor retained income trusts (GRITs), whether or not the grantor's retained interest is a qualified interest as defined in section 2702(b), including without limitation qualified personal residence trusts (QPRTs) and personal residence trusts (PRTs). For purposes of determining the extent to which a retained interest causes all or a portion of a trust to be included in a decedent's gross estate, see § 20.2036-1(c)(1), (2), and (3).

(2) *Effective date.* The first, second, and fourth sentences in paragraph (a) of this section are applicable to the estates of decedents dying after August 16, 1954. The fifth sentence of paragraph (a) of this section is applicable to the estates of decedents dying on or after October 27, 1972, and to the estates of decedents for which the period for filing a claim for credit or refund of an estate tax overpayment ends on or after October 27, 1972. The third, sixth, and seventh sentences of paragraph (a) of this section and this paragraph (e) are applicable to the estates of decedents for which the valuation date of the gross estate is on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

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**Kevin M. Brown,**

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**ENVIRONMENTAL PROTECTION AGENCY**

**40 CFR Parts 51 and 52**

[EPA-HQ-OAR-2005-0163; FRL-8321-9]

RIN-2060-AN28

**Supplemental Notice of Proposed Rulemaking for Prevention of Significant Deterioration (PSD) and Nonattainment New Source Review (NSR): Emission Increases for Electric Generating Units**

**AGENCY:** Environmental Protection Agency (EPA).

**ACTION:** Notice of public hearing.

**SUMMARY:** The EPA is announcing a public hearing to be held on June 29, 2007 for the supplemental proposed rule on "Prevention of Significant Deterioration (PSD) and Nonattainment New Source Review (NSR): Emission Increases for Electric Generating Units." This rulemaking action was published in the **Federal Register** on May 8, 2007