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IRS Issues Guidance on Charitable Remainder Annuity Trusts

The IRS has issued Rev. Proc. 2016-42; 2016-34 IRB 1 (see <https://www.irs.gov/pub/irs-drop/rp-16-42.pdf>), containing 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 IRS will treat the sample provision as a qualified contingency within the meaning of Section 664(f) (section references are to the Internal Revenue Code of 1986, as amended). 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 Section 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. To qualify as a charitable remainder trust under Section 664, a CRAT must meet certain requirements described in Section 664(d)(1) and Treasury Regulations Section 1.664-1(a)(1)(iii)(a). Rev. Proc. 2016-42 applies to trusts created after Aug. 8 (the effective date of the revenue procedure) that (1) meet the requirements of Section 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 the revenue procedure.

With certain modifications depending on the type of CRAT, the following 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 7520 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].

A CRAT that contains a substantive provision similar but not identical to that provided above will not necessarily be disqualified, but neither will such a provision

be ensured treatment as a qualified contingency under Section 664(f). The IRS will treat the sample provision as a qualified contingency under Section 664(f). Thus, the presence of this provision will not cause the trust to fail to qualify as a charitable remainder trust under Section 664.

ISDA Requests Delay in Dividend Equivalent Regulations

The International Swaps and Derivatives Association Inc. (ISDA) submitted a letter (see <http://www.stradley.com/~media/Files/Publications/2016/ISDASection871mEffectiveDateLetterFINAL.pdf>) in support of the comments submitted by the Securities Industry and Financial Markets Association (SIFMA) seeking a delay of the implementation date for the final and temporary regulations under Section 871(m). ISDA also noted that a number of concerns expressed by SIFMA with respect to the qualified derivatives dealer rules remain unaddressed.

Treasury Publishes List of Boycott Countries

Treasury has published a current list (<https://www.gpo.gov/fdsys/pkg/FR-2016-08-05/pdf/2016-18619.pdf>) of countries that may require participation in, or cooperation with, an international boycott for purposes of Section 999(b)(3).

2016 Cambodia-U.S. FATCA IGA Arrangement Available

The Cambodian and U.S. competent authorities have signed an arrangement (see <https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Cambodia-9-14-2015.pdf>) under the two jurisdictions' 2015 intergovernmental agreement to implement the information reporting and withholding tax provisions of FATCA.

IRS Updates FATCA Systems FAQs

The IRS has updated its list of frequently asked questions (see <https://www.irs.gov/businesses/corporations/fatca-ides-technical-faqs>) on the systems used for FATCA data, updating



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several questions and adding questions on (1) FATCA reports filed by a direct-reporting nonfinancial foreign entity, (2) the procedure for reporting accounts with nil payments and (3) how the IRS will handle updates to the XML schema.

Comments Submitted on Proposed Regulations on Deemed Distributions of Stock

Several groups have submitted comments on the proposed regulation on deemed distributions of stock (see our prior coverage at <http://www.stradley.com/insights/publications/2016/tax-insights-2016/tax-insights-april-20-2016>):

- The Investment Company Institute (see <https://www.ici.org/pdf/30067.pdf>)
- The Investment Industry Association of Canada (see <http://www.stradley.com/~media/Files/Publications/2016/Investment-Industry-Association-Canada-Comments.pdf>)
- The Managed Funds Association (see <https://www.managedfunds.org/issues-policy/mfa-comment-letters/mfa-comment-letter-proposed-rules-section-305c-tax-code/>)

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