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Washington, DC 20224

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August 15, 2005

Legend

Trust 1 =

Grantor 1 =
Date 1 =
Date 2 =
Taxpayer =
Trust 2 =

Grantor 2 =
Trust 3 =

Trust 4 =

Trust 5 =

Date 3 =

Dear :

This is in response to your representative's letter, dated August 12, 2004, requesting rulings regarding the income, gift, and generation-skipping transfer (GST) tax consequences of the consolidation of certain trusts.

The facts submitted and the representations made are summarized as follows: Trust 1 was created under Article VII, Section A of the Amended and Restated

Declaration of Trust of Grantor 1 dated Date 1. Trust 1 was established at Grantor 1's death on Date 2. Trust 1 is held for the benefit of Taxpayer.

Trust 2 was created under Article VII, Section A of the Amended and Restated Declaration of Trust of Grantor 2 dated Date 1. Trust 2 was established at Grantor 1's death. Trust 2 is held for the benefit of Taxpayer.

Grantor 1 and Grantor 2 created Trust 3 on Date 1. Under the terms of the trust, Trust 3 was established for the benefit of Taxpayer on the death of Grantor 1.

Under Article VII, Section B of the Amended and Restated Declaration of Trust of Grantor 1 dated Date 1, Trust 4 was established on the death of Grantor 1 for the benefit of Taxpayer.

Under Article VII, Section B of the Amended and Restated Declaration of Trust of Grantor 2 dated Date 1, Trust 5 was established on the death of Grantor 1 for the benefit of Taxpayer.

Grantor 1 and Grantor 2 were husband and wife. Grantor 2 died on Date 3. Trust 1, Trust 2, Trust 3, Trust 4, and Trust 5 have substantially similar operating provisions. The taxpayer represents that Trust 1, Trust 2, and Trust 3 each have a GST inclusion ratio of zero.

A provision in each of the trusts provides that two or more trusts created under the applicable trust instrument or under an instrument created by any other person with the same beneficiaries, trustees, and substantially the same dispositive provisions, may be consolidated for ease and efficiency of administration.

A provision in each of the trusts provides that the trustee shall distribute eighty percent of the income of each separate trust, no less frequently than annually, to the child for whom the trust was established or, unless otherwise appointed by the child, per stirpes to the issue of that deceased child. Any income not so distributed shall be accumulated and added to principal.

A provision in each of the trusts provides that the trustee shall distribute trust principal from a separate trust for the proper health, education, maintenance, and support of the child for whom the trust was established or, unless otherwise appointed by that child, for the proper health, education, maintenance, and support of the issue of that child.

Pursuant to the terms of the trusts, the individual termination date of each trust may differ.

In order to reduce the costs of administration, Taxpayer proposes to consolidate Trust 1, Trust 2, and Trust 3 into Trust A. Trust A will have the same terms as Trust 1.

Furthermore, Taxpayer proposes to consolidate Trust 4 and Trust 5 into Trust B. Trust B will have the same terms as Trust 4.

Because the existing trusts have different perpetuities provisions, the eventual termination dates may vary from trust to trust. To account for this difference, at the time of consolidation, the individual values of each trust will be established in order to determine each trust's proportionate percentage of Trust A or Trust B. Each proportionate percentage will retain its original measuring date for purposes of determining termination under the applicable perpetuities provision. The proportionate value will be utilized in the event that the resulting trust is subsequently separated either pursuant to an election by the trustees, or because part of a resulting trust terminates. In the event that it becomes necessary to separate one of the resulting trusts, the amount separated will be determined using the following formula: the value of the resulting trust upon separation will be multiplied by a fraction, the numerator of which will be the fair market value of the share of the applicable existing trust as of the date of the consolidation, and the denominator of which will be the fair market value of the shares of the resulting trusts (representing shares of two or more of the existing trusts, as the case may be) as of the date of the consolidation.

Taxpayer has requested the following rulings in conjunction with the proposed consolidation of trusts: (1) the proposed consolidation of Trust 1, Trust 2, and Trust 3 will not be considered a constructive addition for purposes of the GST tax and will not subject Trust 1, Trust 2, or Trust 3 or distributions from Trust A to the GST tax; (2) following the proposed consolidation of trusts, Trust A will have an inclusion ratio of zero for purposes of the GST tax; (3) the proposed consolidation of trusts will not cause any beneficiary of an existing trust or any beneficiary of a resulting trust to have made a taxable gift for federal gift tax purposes; (4) the proposed consolidation of trusts will not cause any existing trust or resulting trust to recognize any gain or loss from the sale or other disposition of property under §§ 61 or 1001; (5) pursuant to § 1015, the basis of the resulting trust in each asset received from a trust will be the same as the transferring trust's basis in the asset; and (6) pursuant to § 1223(2), the holding period of each consolidated trust in any asset received from a trust will include the holding period of the transferring trust in the asset.

Rulings 1 and 2

Section 2601 imposes a tax on every generation-skipping transfer.

Section 2611(a) defines the term "generation-skipping transfer" to include a taxable distribution, taxable termination, and a direct skip.

In this case, Trust 1, Trust 2, and Trust 3 are GST trusts because they provide for distributions to more than one generation of beneficiaries below the grantor's generation. Each trust was created after September 25, 1985, and Taxpayer

represents that each trust had an inclusion ratio of zero prior to the proposed consolidation into Trust A.

A modification of the governing instrument of an exempt trust by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapters 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided in the original trust. Furthermore, a modification that is administrative in nature that only indirectly increases the amount transferred (for example, by lowering administrative costs or income taxes) will not be considered a shift in a beneficial interest in a trust.

The terms of the trusts to be consolidated are identical with respect to the interests of the Taxpayer and the Taxpayer's issue except for differences in the termination date under the applicable perpetuities provisions. After the consolidation there will be no change in the dispositive provisions with respect to the property previously held in the existing trusts. However, in order to account for the differences in the termination dates of the existing trusts, at the time that one of the original trusts would have terminated, a portion of Trust A will be separated and distributed. The portion separated from Trust A will be derived based on the proportionate percentage of the existing trust to Trust A at the time of consolidation pursuant to the formula set forth above. Accordingly the proposed consolidation does not shift a beneficial interest in any trust to a beneficiary who occupies a lower generation than the person(s) who held the beneficial interest prior to the modification. In addition, the modification does not extend the time for vesting of any beneficial interest in trust beyond the period provided in the existing trusts. We therefore conclude that the proposed consolidation will not change the inclusion ratio of Trust 1, Trust 2, or Trust 3.

Ruling 3

Section 2501 imposes a tax on the transfer of property by gift by an individual. Section 2502(c) provides that the payment of the gift tax is the liability of the donor.

Section 2503(a) provides that the term "taxable gifts" means the total amount of gifts made during the calendar year, less the deductions provided in subchapter C.

Section 2503(b)(1) provides, generally, that in the case of gifts (other than gifts of future interests in property) made to any person by the donor during the calendar year, the first $10,000 (adjusted for inflation as provided in § 2503(b)(2)) of such gifts to such person shall not be included in the total amount of gifts made during the year.

Section 25.2503-3(a) of the Gift Tax Regulations provides that the term "future interest" includes reversions, remainders, and other interests or estates, whether vested

or contingent, and whether or not supported by a particular interest or estate, which are limited to commence in use, possession, or enjoyment at some future date or time. Section 25.2503-3(b) defines a present interest in property as an unrestricted right to immediate use, possession, or enjoyment of property or the income from property (such as a life estate or term certain).

Section 2511 provides that the tax imposed by § 2501 shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible. Section 2512(a) provides that, where property is transferred for less than adequate and full consideration in money or money's worth, the amount by which the value of the property exceeds the value of the consideration is deemed a gift.

Section 25.2511-2(a) provides that the gift tax is a primary and personal liability of the donor, is an excise upon his act of making the transfer, is measured by the value of the property passing from the donor, and attaches regardless of the fact that the identity of the donee may not then be known or ascertainable.

Section 25.2512-5(d)(2) provides that, in general, if the donor assigns or relinquishes an annuity, life estate, remainder, or reversion that the donor holds by virtue of a transfer previously made by the donor or another, the value of the gift is the value of the interest transferred.

In this case, the beneficiaries of the resulting trusts will have the same interests after the proposed consolidation that they had as beneficiaries under the existing trusts. Because the beneficial interests, rights, and expectancies of the beneficiaries are substantially similar, both before and after the proposed transaction, no transfer of property will be deemed to occur as a result of the consolidation. Accordingly, we conclude that the consolidation of Trust 1, Trust 2, and Trust 3 into Trust A and the consolidation of Trust 4 and Trust 5 into Trust B as proposed is not a transfer, direct or indirect, of property that will be subject to the gift tax imposed by § 2501.

Rulings 4, 5 and 6

Section 61(a)(3) provides that gross income includes gains derived from dealing in property. Under § 1001(a) the gain from the sale or other disposition of property is the excess of the amount realized therefrom over the adjusted basis (provided in § 1011), and the loss is the excess of the adjusted basis over the amount realized.

Section 1.1001-1(a) of the Income Tax Regulations treats as income or as loss sustained the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent.

In Cottage Savings Association v. Commissioner, 499 U.S. 554 (1991), the Supreme Court of the United States examined the issue of what constitutes a material

difference in exchanged properties or a disposition of property for purposes of the realization requirement implicit in § 1001(a). In Cottage a savings and loan association sold 90-percent participation interests in 252 mortgage loans to four other lenders. Simultaneously, the association purchased 90-percent participation interests in 305 mortgage loans held by these lenders. The exchanged properties were derived from loans made to different obligors, secured by different homes, and thus embodied legally distinct entitlements. The association claimed a deduction under § 165(a) for the adjusted difference between the face value of the participation interests the association had traded and the fair market value of the participation interests it had received.

The Supreme Court set forth a test for determining whether exchanged properties are materially different for purposes of § 1001: their respective possessors enjoy legal entitlements that are different in kind or extent. Cottage, at 565. Because the mortgages had different mortgagors and were secured by different properties, the loans were materially different. The Court, therefore, held that the taxpayer actually sustained a loss for purposes of § 165(a).

The assets of Trust 1, Trust 2, and Trust 3 will be consolidated into Trust A for administrative convenience. In addition, the assets of Trust 4 and Trust 5 will be consolidated into Trust B for administrative convenience. The beneficiaries will possess the same interests before and after the consolidation of the trusts. Both before and after the consolidation, each beneficiary is entitled to the same income and/or remainder interests in the assets of all the trusts. The interests of the beneficiaries in Trust 1, Trust 2, and Trust 3 will not materially differ from their interests in Trust A. Furthermore, the interests of the beneficiaries in Trust 4 and Trust 5 will not materially differ from their interests in Trust B.

Accordingly, we conclude that the consolidation of Trust 1, Trust 2, and Trust 3 into Trust A will not be considered to be a sale or other disposition of trust property and, thus, will not cause any beneficiary, trust, or consolidated trust to recognize any gain or loss from the sale or other disposition of property under §§ 61 or 1001.

Section 1015 provides that if property is acquired after December 31, 1920, by a transfer in trust (other than by a transfer in trust by a gift, bequest, or devise), the basis shall be the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized by the grantor on such transfer.

Section 1223(2) provides that in determining the period for which the taxpayer has held property however acquired, there shall be included in the period for which the property was held by any other person, if under Chapter 1 of the Internal Revenue Code such property has, for the purposes of determining gain or loss from a sale or exchange, the same basis in whole or in part in the taxpayer's hands as it would have in the hands of such other person.

Because there is no gain or loss recognized on the consolidation under § 1001, the assets transferred from the existing trusts into Trust A and Trust B will have the same basis before and after the consolidation under § 1015. Furthermore, the holding period of each resulting trust in any asset received from a trust will include, pursuant to § 1223(2), the holding period of the transferring trust in such asset.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Pursuant to the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer's representative.

Sincerely,

Melissa C. Liquerman

Melissa C. Liquerman
Branch Chief, Branch 9
(Passthroughs & Special Industries)

Enclosure
Copy for § 6110 purposes

cc: