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| **Internal Revenue Service** | Department of the Treasury<br>Washington, DC 20224 |
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| | Person To Contact:<br>, ID No.<br>Telephone Number: |
| | Refer Reply To:<br>CC:FIP:4 – PLR-158742-05<br>Date:<br>March 22, 2006 |

In Re:

Legend

Trustee =

Trust =

Insurance Company X =

Insurance Company Y =

Old Annuity =

New Annuity =

Settlor =

Beneficiary A =

Beneficiary B =

Beneficiary C =

Beneficiary D =

Month E =

Month F =

Month G =

Year 1 =

Year 3 =

Year 9 =

Year 14 =

Year 15 =

Year 16 =

Dear :

This is in reply to a letter dated October 20, 2005 submitted on behalf of a trust requesting a ruling on the subject of the taxability of annuities held by a trust on behalf of the natural person beneficiaries of the trust under § 72(u)(1) of the Internal Revenue Code. Additional information was submitted in a letter dated March 6, 2006.

In Month G of Year 1, Settlor established Trust. Trust was established as an irrevocable trust and Settlor did not retain the right to alter, amend, revoke or terminate Trust or any provision thereof. Settlor did not retain any right, title or interest in the income or the principal of Trust, and no right, title, interest power, option, incident of ownership, benefit or privilege in any property of Trust. Trust provided that neither Settlor nor her estate had any reversionary interest in Trust or in any of Trust property. Settlor funded Trust with cash with a view to invest in products sold by life insurance companies. During Settlor's lifetime, Trustee had no power to make distributions from Trust.

In Month E of Year 3, Trust purchased a deferred annuity (Old Annuity) from Insurance Company X. Old Annuity contained the usual commercial annuity terms. Trust was the owner and beneficiary of Old Annuity. Beneficiary A, the son of Settlor, was the annuitant. Beneficiaries B and C were also sons of Settlor. Beneficiary D was the daughter of Settlor. In Month F of Year 9, Old Annuity was exchanged for a new deferred annuity (New Annuity), which was issued by Insurance Company Y in a transaction represented to have been a § 1035 exchange. New Annuity had the usual terms of a commercial deferred annuity including a contingent deferred sales charge, which subtracted certain percentages for an early surrender of New Annuity. Trust remained the owner and beneficiary of New Annuity and Beneficiary A was the annuitant. Beneficiaries A, B, C and D remained the primary beneficiaries of Trust.

Upon Settlor's death, Trustee was to divide Trust property into equal shares for the children of Settlor then living (and deceased children of Settlor with issue then living). Each share set aside was to be held by Trustee in a separate trust for the benefit of such child.

Settlor died in Year 14. Each of the children (Beneficiaries A, B, C and D) had the right to, and did elect to, withdraw his (or her) share of the principal of Trust. Thus, Trust was not divided into separate trusts and there are no plans to do so now or at any time in the future. (New Annuity is the only asset that Trust presently owns.) Trust will surrender New Annuity to Insurance Company Y and distribute the proceeds to the four children (Beneficiaries A, B, C and D) after waiting a short period of time until Month F of Year 16 when Insurance Company Y's contingent deferred sales charge is zero.

Section 72(u)(1) of the Internal Revenue Code provides that if an annuity contract is held by a person who is not a natural person, then such contract shall not be treated as an annuity contract for purposes of subtitle A (other than subchapter L) and the income on the contract for any taxable year of the policyholder shall be treated as ordinary income received or accrued by the owner during such taxable year. Section 72(u)(1) further provides that if an annuity contract is held by a trust or other entity as an agent for a natural person, then § 72(u)(1) shall not apply.

The legislative history to § 72(u)(1) of the Code states that if an annuity contract is held by a person who is not a natural person (such as a corporation), then the contract is not treated as an annuity contract for Federal income tax purposes and the income on the contract for any taxable year is treated as ordinary income received or accrued by the owner of the contract during the taxable year. However, the legislative history further provides that in the case of an annuity contract the nominal owner of which is not a natural person (e.g., a corporation or a trust), but the beneficial owner of which is a natural person, the contract is treated as held by a natural person. H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. II-401-402 (1986), 1986-3 (Vol. 4) C.B. 401-402. Although Trustee has a role as the contract owner of the annuities, his ownership interest as a trustee is nominal compared to the interests of the four beneficiaries (A, B, C and D). Consequently, the beneficiaries (A, B, C and D) are considered the beneficial owners of Old Annuity and New Annuity.

The following representations were made in connection with this ruling request:

(a) Trust has not and will not receive any consideration from a beneficiary, or any other individual or entity in exchange for any distributions with respect to the annuities to a beneficiary.

(b) Each beneficiary is a natural person as that term is defined in § 72(u) of the Code.

(c) Settlor of Trust was not considered the owner of Trust for purposes of §§ 671-679 of the Code.

(d) None of the beneficiaries are employed by Trust.

(e) Any annuity contracts involved satisfy the terms of § 72(s).

(f) Under no circumstances has Trust made or will make any distributions with respect to Old Annuity and New Annuity to anyone other than a beneficiary named above (A, B, C or D).

(g) The exchange of Old Annuity for New Annuity in Year 9 was a § 1035 exchange.

Accordingly, based solely on the information submitted, the representations made, and provided Trust has or will have filed Forms 1041 (U.S. Income Tax Returns for Estates and Trusts) for Years 3 through Year 15 by yearend Year 16 and will file the Year 16 Form 1041 by that return's due date (with allowable extensions), we conclude as follows:

Old Annuity and New Annuity are considered owned by a natural person for purposes of § 72(u)(1) of the Code.

Except as specifically set forth above, no opinion is expressed as to the tax treatment of Old Annuity, New Annuity or Trust under the provisions of any other section of the Code or the Income Tax Regulations. Specifically, no opinion is expressed as to whether or not Old Annuity or New Annuity were or are in fact annuity contracts under § 72 of the Code. Furthermore, no opinion is expressed as to whether Old Annuity or New Annuity meet the requirements of § 72(s). Finally, no opinion is expressed as to whether Trust is a grantor trust. See §§ 671-679 of the Code.

This ruling letter is directed only to the taxpayer who requested it. Section 6110)(k)(3) of the Code provides that it may not be used or cited as precedent. Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling will be modified or revoked by the adoption of temporary or final regulations to the extent the regulations are inconsistent with any conclusion in the ruling.

A copy of this letter should be attached to the Federal income tax returns to which it is relevant.

In accordance with the power of attorney on file in this office, we are sending a copy of this letter to your authorized representative.

Sincerely yours,

/S/

DONALD J. DREES, JR.
Senior Technician Reviewer
Branch 4
Office of Associate Chief Counsel
(Financial Institutions & Products)