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PLR-127484-06

Date:
June 21, 2007

Trust =

Trustee =

Charity =

Grantors =

State =

Beneficiaries =

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a =

Dear :

This letter responds a letter dated April 26, 2006, submitted on behalf of the Trust, requesting certain rulings concerning the proposed termination of the Trust.

FACTS

The information submitted states that the Trust was formed by Grantors under the laws of State on a. The Trust is a charitable remainder unitrust the unitrust amounts of which are paid to each of the Beneficiaries (individually a "Beneficiary") for life. Upon the death of a Beneficiary, that Beneficiary's subshare terminates and the remainder is transferred to the Charity, a public charity that is a donor advised fund. Under the terms of the Trust, each Beneficiary's subshare constitutes a separate trust.

Because of reduced investment performance and administrative expenses, the Trust, its Trustee, and the Beneficiaries have agreed to terminate the Trust earlier than its terms provide. In terminating, the Trust will distribute to the Beneficiaries pro rata shares of the Trust's assets equal to the present value of the Beneficiaries' respective interests, measured on the date of termination, and will distribute the remainder to the Charity. The amounts distributed to the Beneficiaries will be determined and distributed pursuant to the valuation rules under § 7520 of the Internal Revenue Code and § 1.664-4 of the Income Tax Regulations. It is represented that the proposed termination of the Trust will be made pursuant to a court order resulting from a proceeding in which the State Attorney General is a party.

Each Beneficiary has submitted an affidavit representing that, to the best of the Beneficiary's knowledge and belief, the Beneficiary has no medical condition that is expected to result in a shorter life expectancy than that set forth in § 1.72-9, Table 1.

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RULING 1

Section 664(b) provides that the amounts distributed by a charitable remainder annuity trust or a charitable remainder unitrust shall be considered as having the following characteristics in the hands of a beneficiary to whom is paid the annuity described in § 664(d)(1)(A) or the payment described in § 664(d)(2)(A): (1) first, as amounts of income (other than gains, and amounts treated as gains, from the sale or other disposition of capital assets) includible in gross income to the extent of such income of the trust for the year and such undistributed income of the trust for prior years; (2) second, as capital gain to the extent of the capital gain of the trust for the year and the undistributed capital gain of the trust for prior years; (3) third, as other income to the extent of such income of the trust for the year and such undistributed income of the trust for prior years; and (4) fourth, as a distribution of trust corpus. For purposes of § 664, the trust shall determine the amount of its undistributed capital gain on a cumulative net basis.

Thus, § 664(b) provides rules to determine the character of the annual unitrust amounts distributed by a charitable remainder unitrust to the unitrust beneficiary. Any regular unitrust amount distributed to the Beneficiaries by the Trust prior to termination of the Trust will have the characteristics in the hands of the Beneficiaries as determined under § 664(b).

However, money and property received by the Beneficiaries upon the termination of the Trust do not represent a distribution of an annual unitrust amount; therefore, § 664 is not applicable to this amount. Rather, the Beneficiaries are disposing of their interests in the Trust in exchange for money and property in a transaction that is governed by § 1001.

Section 1001(a) provides that the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized.

Section 1001(b) provides that the amount realized from the sale or other disposition of property is the sum of any money received plus the fair market value of the property (other than money) received. Under § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under § 1001, on the sale or exchange of property shall be recognized.

Section 1001(e)(1) generally provides that in determining the gain (or loss) from the sale of a term interest in property, the portion of the adjusted basis that is

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determined under § 1014 or § 1015 shall be disregarded. Section 1001(e)(2) defines a term interest in property to include an income interest in a trust. However, § 1001(e)(3) provides that the term interest rule described in § 1001(e)(1) shall not apply to a sale or other disposition of property that is a part of a transaction in which the entire interest in property is transferred to any person or persons.

Section 1.1001-1(f)(1) provides that, for purposes of determining the gain or loss from the sale or other disposition of a term interest in property, a taxpayer shall not take into account that portion of the adjusted basis of such interest which is determined pursuant to § 1015 (relating to the basis of property acquired by gift or by a transfer in trust) to the extent that such adjusted basis is a portion of the adjusted uniform basis of the entire property (as defined in § 1.1014-5).

Section 1.1001-1(f)(3) states that the exception in § 1001(e)(3) applies when the entire interest in property is sold or otherwise disposed as part of a single transaction to a third person or persons.

Section 1223(3) provides that the term “long-term capital gain” means gain from the sale or exchange of a capital asset held for more than one year. Section 1221(a) defines the term “capital asset” as property held by the taxpayer with certain listed exceptions not applicable here.

Rev. Rul. 72-243, 1972-1 C.B. 233, provides that the proceeds received by the life tenant of a trust, in consideration for the transfer of the life tenant’s entire interest in the trust to the holder of the remainder interest, are treated as an amount realized from the sale or exchange of a capital asset under § 1222. The right to income for life from a trust estate is a right in the estate itself. See McAllister v. Commissioner, 157 F. 2d 235 (2d Cir.), cert. denied, 330 U.S. 826 (1946).

Accordingly, although the proposed transaction takes the form of a distribution of the present values of the respective interests of each Beneficiary and the Charity, it is in substance a sale of each Beneficiary’s unitrust interest to the Charity, the remainder beneficiary. Because the disposition of each Beneficiary’s interest is not part of a transaction in which the entire interest in the Trust is transferred to a third party, the adjusted basis in each Beneficiary’s interest is disregarded under § 1001(e)(1) in determining gain realized by each Beneficiary. Moreover, any gain realized by the Beneficiaries upon the early termination of the Trust will be long-term capital gain.

RULING 2

Section 4941(a)(1) imposes an excise tax on any act of self-dealing between a private foundation and any of its disqualified persons defined in § 4946.

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Section 4941(d)(1)(A) provides, in part, that an act of self dealing includes any sale or exchange between a disqualified person and a private foundation.

Section 4946(a) provides that the term “disqualified person” with respect to a private foundation includes a substantial contributor to the foundation (including the creator or the trust), a family member of a substantial contributor (including children), and a foundation manager (including a trustee).

Section 53.4946-1(a)(8) of the Foundation and Similar Excise Tax Regulations provides that for purposes of § 4941 only, the term “disqualified person” shall not include any organization which is described in § 501(c)(3) (other than an organization described in § 509(a)(4)).

Section 4947(a)(2)(A) describes split-interest trusts as those that are not exempt from federal income tax under § 501(a), not all of the unexpired interests in which are devoted to purposes in § 170(c)(2)(B), and which have amounts in trust for which a deduction was allowed under §§ 170, 545(b)(2), 556(b)(2), 642(c), 2055, 2106(a)(2), or 2522. Furthermore, split-interest trusts are subject to the rules of §§ 507, 508(e), 4941, 4943 (except (b)(3)), 4944 (except as provided in (b)(3)), and 4945.

Section 53.4947-1(c)(2)(i) provides that under § 4947(a)(2)(A), § 4941 does not apply to any amounts payable under the terms of a split-interest trust to income beneficiaries unless a deduction was allowed under §§ 170(f)(2)(B), 2055(e)(2)(B), or 2522(e)(2)(B) with respect to the income interest of such beneficiary.

Rev. Rul. 69-486, 1969-2 C.B. 159 concerns a non-pro rata distribution of trust property in kind by a trustee who had no authority to make such a distribution and did so as a result of a mutual agreement by the beneficiaries, one of which is a charitable organization. The distribution was made as a final distribution of trust property. The trust property consisted of notes that had not appreciated in value and common stock that had appreciated in value. By agreement, all of the notes were distributed to the charity and the stock to the individual beneficiary. The ruling holds that the distribution was equivalent to a pro rata distribution of the stock and notes to both followed by an exchange of the charity’s share of the common stock for the individual’s pro rata share of the notes.

The Trust is described in § 4947(a)(2) by having income beneficiaries, the Beneficiaries, and a charitable remainderman, the Charity, described in §§ 509(a)(1) and 170(b)(1)(A)(vi). By being described in § 4947(a)(2), the Trust is subject to the provisions of §§ 507, 4941, and 4945, as if it were a private foundation. The Beneficiaries are disqualified persons with respect to the Trust within the meaning of

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§ 4946(a)(1)(A). However, the Beneficiaries are not disqualified persons with respect to the charitable remainder beneficiary, the Charity, because the Charity is a donor advised fund that is a public charity described in § 509(a).

Section 4941 applies to certain transactions between private foundations and disqualified persons. By early termination, the Trust will distribute lump sums to the Beneficiaries and the Charity equal to the actuarial value of their interests in the Trust, and the distributions will also be treated as a constructive sale or exchange between the income beneficiaries, the Beneficiaries, and the charitable remainderman, the Charity, of the Trust. See Rev. Rul. 69-486.

Generally, payments to the Beneficiaries by the Trust would constitute self-dealing. However, because the distribution to each of the Beneficiaries equals the actuarial value of the respective Beneficiary's income interest, the exception to self-dealing provided by § 53.4947-1(c)(2)(i) applies and the distribution will not be an act of self-dealing. Furthermore, because the Charity is a public charity, § 4941 does not apply to the transaction between the Beneficiaries and the Charity. Therefore, based on the above law and discussion, the early termination of the Trust will not be considered an act of self-dealing under § 4941.

Except for the specific ruling above, we express or imply no opinion concerning the federal income tax consequences of the facts of this case under any other provision of the Code. Specifically, no opinion is expressed as to whether the Trust otherwise qualifies as a charitable remainder trust under § 664.

Under a power of attorney on file with this office, we are sending a copy of this letter to the Trust's authorized representative.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Sincerely,

/s/

JAMES A. QUINN
Senior Counsel, Branch 3
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure: copy of this letter for § 6110 purposes