**Office of Chief Counsel**
**Internal Revenue Service**
# memorandum
CC:ITA:B01:LAAyres

date: 5/2/2008

to: Singleton Michael K, Program Advisor
Office of the National Public Liaison, Stakeholder Relationship Mgmt

from: TaJuana Nelson Hyde, Assistant Chief Branch 1:ITA

---

subject: Exchange Traded Funds Invested in Metal (Wall Street Journal Article)
PRENO-105240-08
(External Stakeholder Issue)

We have been asked to respond to the question of whether the sale of an interest in an exchange traded fund (ETF) that directly invests in metal ("physically backed metal ETF") is treated as the sale of a "collectible" such that any gain from the sale of the interest is subject to the maximum capital gain rate of 28%.

An ETF is sometimes structured as an investment trust that is intended to be treated as a trust for federal tax purposes. For an ETF to be treated as a trust for federal tax purposes, the ETF must fall within the description of an investment trust that will be treated as a trust under § 301.7701-4(c). In general, § 301.7701-4(c) provides that an investment trust with a single class of ownership interests, representing undivided beneficial interests in the assets of the trust, will be classified as a trust if there is no power under the trust agreement to vary the investment of the certificate holders. The existence of a power to vary the investment of the certificate holders will depend on the particular language of a given trust indenture or trust agreement and must be determined on a case by case basis.

If an ETF is treated as a trust under § 301.7701-4(c), investors in the ETF are considered to have undivided beneficial interests in the assets held by the trust. Hence, investors in a "physically backed metal ETF" are considered to own undivided beneficial interests in the underlying physical metal. If a trustee of a "physically backed metal ETF" treated as a trust sells some of the metal held by the trust, the investors are treated as having sold the metal. Additionally, if an investor in a "physically backed metal ETF" treated as a trust sells or redeems an interest in that ETF, the sale or redemption is treated as a sale of the investor's proportionate share of the metal held by the "physically backed metal ETF." See Rev. Rul. 90-7, 1990-1 C.B. 153; Rev. Rul. 85-13, 1985-1 C.B. 184; and Rev. Rul. 84-10, 1984-1 C.B 155.

Although § 1(h)(5)(B) and § 1.1(h)-1 provide rules regarding collectible gain and loss with respect to partnerships, S corporations and trusts, these sections do not apply to investment trusts treated as trusts under §§ 301.7701-4(c) because the investors' interests in these trusts represent undivided beneficial interests in the trust assets. Investors in a "physically backed metal ETF" are treated as having undivided interests in the metal held by the trust and thus, the investors' collectible gain or loss on either the sale of the trust interest or the sale of metal by the trust is determined under § 1(h)(5)(A). Further, an investor in a "physically backed metal ETF" that is treated as a trust under § 301.7701-4(c) meets the requirement under §1(h)(5)(A) that the investor hold the metal for more than one year if the investor has owned an interest in the trust for more than one year and the trust has owned the metal for more than one year.

Thus, in the case of a "physically backed metal ETF" which is treated as a trust under § 301.7701-4(c), the investor is treated as owning an undivided beneficial interest in the collectible held by the trust. If the investor sells his interest in the ETF or the trust sells a portion of the collectible, the investor is treated as having sold all or a portion of his share of the collectible held by the trust and any gain from the sale of the trust interest or sale of the collectible by the trust is treated as collectible gain and subject to the maximum capital gain rate of 28%.

We note that "physically backed metal ETFs" are sometimes structured as trusts for federal tax purposes and that if a "physically backed metal ETF" is not structured as a trust or if the ETF does not directly invest in the metal, the above analysis does not apply. The structure of each "physically backed metal ETF" should be considered to determine the tax consequences of an investment in that ETF.

Finally, taxpayers seeking information regarding specific taxable transactions are encouraged to request a private letter ruling.

If you have any questions, please contact Leta Ayres or me at (202) 622-5020.