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**Department of the Treasury**

Washington, DC 20224

**Person To Contact:**

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**Date:**

January 27, 2004

**LEGEND**

Leasco =

Corp 2 =

Parent =

Holding =

Business Trust =

State 1 =

State 2 =

f =

g =

h =

i =

m =

o =

p =

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Dear \_\_\_\_\_ :

This responds to a letter dated September 15, 2003, submitted on behalf of Parent and Leasco, requesting rulings under § 7701(h) of the Internal Revenue Code.

According to the facts submitted and representations made, Parent is a closely held State 1 corporation that is the common parent of an affiliated group of corporations filing a consolidated Federal income tax return. Leasco, the principal operating subsidiary of Parent, is engaged in the motor vehicle fleet leasing business and has a motor vehicle fleet in excess of n vehicles. Leasco's customers lease from o to more than p vehicles. The vast majority of Leasco's customers have high-quality credit. Historically, rental defaults by Leasco's customers have been extremely low. For each customer there is a Master Lease Agreement and a Lease Order for each new vehicle added to the master lease.

Leasco provides the following services to its customers: 1) vehicle acquisitions services and maintenance and collision services; 2) license, title and tax administration services; 3) remarketing services; 4) data processing services; 5) truck engineering and coordination services; 6) gasoline credit card administration; 7) rental replacement vehicles; and 8) administration of factory incentives.

In h, Leasco formed Corp 2, a State 2 limited liability company, of which Leasco owned 100 percent. Prior to j, Leasco or Corp 2 borrowed from banks to finance the purchase of motor vehicle fleets. The debt was secured by a lien on the vehicles and a pledge of rents from the vehicle leases. In j, Leasco restructured its financing by forming Holding, another State 2 limited liability company of which Leasco owned 100 percent. Holding is capitalized with \$f and Corp 2 is capitalized with \$g. These amounts are minimum capital, which will exist at the inception of every new borrowing.

Holding formed Business Trust, a State 1 statutory trust, of which Holding owns 100 percent. Holding borrows funds from Leasco and contributes the funds to the Business Trust. Holding pledges its undivided interest in the Business Trust evidenced by an undivided Business Trust interest certificate (the "UTI Certificate") to Leasco as security for the payment of its borrowing from Leasco. Subsequently, Holding causes Business Trust to create a sub-trust comprised of identified vehicles and leases, which is allocated to a special unit of beneficial interest (the "SUBI"), evidenced by a certificate (the "SUBI Certificate"). Holding sells the SUBI Certificate to Leasco pursuant to a SUBI Certificate Transfer Agreement. To purchase the SUBI Certificate from Holding, Leasco borrows funds from a consortium of lenders on a full recourse basis and secured by the SUBI Certificate.

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Leasco proposes to reallocate certain vehicles and leases allocated to the Leasco SUBI back to Holding as UTI Beneficiary in exchange for a payment by Holding to Leasco. Business Trust will issue a new SUBI Certificate and sell that SUBI Certificate to SPV. SPV will borrow funds for the purchase from banks or other financial institutions on a full recourse basis with the SUBI Certificate as security.

Leasco, as agent for Business Trust, collects all amounts payable under a lease and all net disposition proceeds. Such rentals and disposition proceeds are distributed to the holder of the UTI or a SUBI to which the vehicles and leases are allocated. If disposition proceeds are such that the lessee is entitled to receive a payment at the termination of the lease under the terminal rental adjustment clause (a "TRAC payment"), the obligation to make the TRAC payment will be satisfied out of funds held by Business Trust or contributed to Business Trust by Holding or the holder of the SUBI to which the lease is allocated. Assuming rental defaults are consistent with historical experience, amounts received by Business trust should be sufficient for Holding, Leasco, or Corp 2 to satisfy obligations to lenders and make a profit.

Holding's liability to Leasco is a full recourse obligation. Therefore, Leasco is able to look to all of Holding's assets, subject to the ordinary debtor-creditor priority rules. Similarly, Leasco's and Corp 2's liability to the lenders is a full recourse obligation. Therefore, the lenders are able to look to all of Leasco's or Corp 2's assets, subject to the ordinary debtor-creditor priority rules.

Parent, Leasco, and Holding request rulings that 1) the Master Lease Agreement (and the Lease Order) pursuant to which the Business Trust is the lessor is a qualified motor vehicle operating agreement under § 7701(h)(2); 2) qualification of the Master Lease Agreement (and the Lease Order) as a lease, for federal income tax purposes, in the hands of the trust will be determined without regard to the TRAC provision of the Master Lease Agreement; 3) no gain, loss, or income will be realized by Leasco or Holding as a result of the transfer of money from Leasco to Holding or the transfer of the SUBI Certificate by Holding to Leasco; 4) no gain, loss, or income will be realized by Leasco or Holding as a result of the transfer of the property from Holding to Business Trust or by the Business Trust to Holding or Leasco; 5) all income, deductions and credits of Business Trust will be treated as income, deductions and credits of Leasco; and 6) no gain, loss, or income will be realized by Leasco, Holding, SPV or Business Trust as a result of the payment by Holding to Leasco in connection with the reallocation of the vehicles and leases allocated to the Leasco SUBI to the UTI, the allocation of such vehicles and leases to a new SUBI evidenced by a new SUBI Certificate and the sale of the new SUBI Certificate by Holding to SPV.

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### Rulings 1 and 2

Section 7701(h)(1) provides that in the case of a qualified motor vehicle operating agreement that contains a terminal rental adjustment clause, the agreement is treated as a lease if (but for such terminal rental adjustment clause) the agreement would be treated as a lease for federal income tax purposes, and the lessee is not treated as the owner of the property subject to the agreement during the period the agreement is in effect.

Section 7701(h)(2) defines a qualified motor vehicle operating agreement as any agreement with respect to a motor vehicle (including a trailer) that meets the following requirements. First, under the agreement, the sum of the amount the lessor is personally liable to repay, and the net fair market value of the lessor's interest in any property pledged as security for property subject to the agreement, must equal or exceed all amounts borrowed to finance the acquisition of property subject to the agreement. Any property pledged that is property subject to the agreement or property directly or indirectly financed by indebtedness secured by property subject to the agreement is not taken into account. Second, the agreement must contain a separate written statement signed by the lessee that the lessee certifies, under penalty of perjury, that it intends that more than 50 percent of the use of the property subject to the agreement is to be in a trade or business of the lessee, and that clearly and legibly states that the lessee has been advised that it would not be treated as the owner of the property subject to the agreement for federal income tax purposes. Finally, the lessor must not know that the certification is false.

The facts and representations provided indicate that the Master Lease Agreement and Lease Order will meet the definition of a "qualified motor vehicle operating agreement" under § 7701(h)(2). Accordingly, based on the foregoing facts, representations, and law, we rule that the Master Lease Agreement (and the Lease Order) pursuant to which the Business Trust is the lessor is a qualified motor vehicle operating agreement under § 7701(h)(2)). We also rule that qualification of the Master Lease Agreement (and the Lease Order) as a lease, for federal income tax purposes, in the hands of the trust will be determined without regard to the TRAC provision of the Master Lease Agreement.

### Rulings 3, 4, 5, and 6

Section 301.7701-2(b) of the Procedure and Administration Regulations provides that the definition of a corporation includes an association as determined under § 301.7701-3.

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Section 301.7701-3(a) provides that a business entity that is not classified as a corporation under § 301.7701-2(b)(1), (3), (4), (5), (6), (7), or (8) (an "eligible entity") can elect its classification for federal tax purposes. An eligible entity with a single owner can elect to be classified as an association or to be disregarded as an entity separate from its owner.

Section 301.7701-3(b)(1)(ii) provides that a domestic eligible entity with a single owner is disregarded as an entity separate from its owner for federal tax purposes unless the entity elects to be treated as a corporation. If the entity is disregarded, its activities are treated in the same manner as those of a division of its owner, and its assets will be treated as those of the owner.

Section 301.7701-4(a) provides that in general, the term "trust" refers to an arrangement created either by a will or by an inter vivos declaration whereby trustees take title to property for the purposes of protecting or conserving it for the beneficiaries. Generally speaking, an arrangement will be treated as a trust under the Internal Revenue Code if it can be shown that the purpose of the arrangement is to vest in trustees responsibility for the protection and conservation of property for beneficiaries who cannot share in the discharge of this responsibility and, therefore, are not associates in a joint enterprise for the conduct of business for profit.

Section 301.7701-4(b) addresses "business trusts" and provides that there are other arrangements which are known as trusts because the legal title to property is conveyed to trustees for the benefit of beneficiaries, but which are not classified as trusts for purposes of the Internal Revenue Code because they are not simply arrangements to protect or conserve the property for the beneficiaries. These trusts, which are often known as business or commercial trusts, generally are created by the beneficiaries simply as a device to carry on a profit-making business which normally would have been carried on through business organizations that are classified as corporations or partnerships under the Internal Revenue Code. However, the fact that the corpus of the trust is not supplied by the beneficiaries is not sufficient reason in itself for classifying the arrangement as an ordinary trust rather than as an association or partnership. The fact that any organization is technically cast in the trust form, by conveying title to property to trustees for the benefit of persons designated as beneficiaries, will not change the real character of the organization if the organization is more properly classified as a business entity under § 301.7701-2.

Based on the foregoing facts, representations, and law, we conclude that Business Trust is a business trust as described in § 301.7701-4(b) and not a trust under § 301.7701-4(a). We further conclude that under § 301.7701-3(b)(1)(ii), Business Trust, SPV and Holding are domestic eligible entities with a single owner that are disregarded as entities separate from their owner.

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Accordingly, we rule that that 1) no gain, loss or income will be realized by Leasco or Holding as a result of the transfer of money from Leasco to Holding or the transfer of the SUBI Certificate by Holding to Leasco; 2) no gain, loss or income will be realized by Leasco or Holding as a result of the transfer of the property from Holding to the Business Trust or by the Business Trust to Holding or Leasco; 3) all income, deductions and credits of the Business Trust will be treated as income, deductions and credits of Leasco; and 4) no gain, loss, or income will be realized by Leasco, Holding, SPV, or the Business Trust as a result of the payment by Holding to Leasco in connection with the reallocation of the vehicles and leases allocated to the Leasco SUBI to the UTI, the allocation of such vehicles and leases to a new SUBI evidenced by a new SUBI Certificate and the sale of the new SUBI Certificate by Holding to SPV.

These rulings are based on the ownership structure submitted and are conditioned upon no other party obtaining an equity interest in the Business Trust, SPV, or Holding, by virtue of a security interest in the SUBI Certificate or otherwise.

Except as specifically set forth above, no opinion is expressed concerning the federal income tax consequences of the above described facts under any other provision of the Code or regulations. Specifically, no opinion is expressed concerning whether or not the Master Lease Agreement and Lease Order are true leases for federal income tax purposes.

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

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to the taxpayer and the taxpayer's second authorized representative.

Sincerely,

Walter H. Woo  
Senior Technician Reviewer, Branch 5  
Office of Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)  
Copy of this letter  
Copy for § 6110 purpose