

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200715005**

Release Date: 4/13/2007

Index Number: 671.00-00, 2501.00-00,
2501.01-00

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B02
PLR-135533-06

Date:
January 03, 2007

Legend

A =

B =

C =

Trust =

State =
1 =

State
2

Dear :

This letter responds to your letter dated July 15, 2006, and subsequent correspondence, submitted on behalf of Trust, requesting rulings under §§ 671 and 2501 of the Internal Revenue Code.

The information submitted states that A, a resident of State 1, proposes to execute Trust, which will be governed by the laws of State 2 and will have a State 2 corporate trustee. B is a sibling of A, and C is a child of A.

Article Second (A) of Trust, provides that during A's lifetime, the Trustee may distribute all or any part of the net income and principal to such one or more of A, B, and A's descendants, whenever born, and in such shares or proportions as the Distribution Committee shall determine, or may reimburse (or provide advances to) any person with whom any beneficiary resides for any expenses (including, without limitation, housing, housekeeping, child care, educational and health-related expenses) incurred in connection with caring for such beneficiary; provided, however, that such distributions shall be made only at such time or times as (1) the Distribution Committee shall by unanimous agreement direct the Trustee or (2) either member of the Distribution Committee, acting alone, shall so direct the Trustee upon obtaining A's prior written consent to each distribution.

Article Second (B) of Trust provides that the Trustee shall make no distribution other than as directed by the Distribution Committee in accordance with the provisions of Article Second (A).

Article Second (D) of Trust provides that the Trustee shall add all undistributed net income to principal at least annually.

Article Second (E)(1) of Trust provides that upon the death of A, the principal and all income of Trust shall be distributed to such one or more persons, and in such estates, interests and proportions (other than A, A's creditors, A's estate or to pay any obligations owed to A's creditors or the creditors of A's estate), as A directs by a provision of A's last will and testament duly admitted to probate (or by a provision of a revocable inter vivos trust, which shall, by its terms, become irrevocable upon A's death and the assets of which will be includable in A's gross estate for federal estate tax purposes) and expressly referring to the power of appointment granted to A by Article Second (E)(1). It is further provided that A may at any time, by a written, acknowledged instrument delivered to the Trustee, release such power of appointment with respect to any or all of the property subject to such power or may further limit the persons or entities in whose favor or the extent to which this power may be exercised.

Any property that A does not effectively appoint through the exercise of the power of appointment granted by Article Second (E)(1) will be divided into separate and equal shares for A's then living descendants, per stirpes. Each share so set apart for a child of A shall be administered in accordance with the provisions of Article Third, and each share so set apart for a grandchild of A shall be administered in accordance with the provisions of Article Fourth.

Article Third of Trust provides that any property set apart for a child of A will be held in further trust for the child's life. The Trustee may distribute all or any part of the net income and principal to A's child at any time. At the child's death, the property will be distributed to his or her children and will be held in further trust accordance with the

provisions of Article Fourth.

Article Fourth of Trust provides that any property set apart for a descendant (other than a child) of A will be held in further trust for the descendant's life. The Trustee may distribute all or any part of the net income and principal to A's descendant at any time. At the descendant's death, the property will be distributed to his or her children and will be held in further trust until the maximum period permitted by law, at which time it will be distributed outright and free of trust to the then income beneficiary of the trust.

Article Fifth provides that if, at A's death or the termination of any trust created after A's death, none of A's descendants are then living, the trust property shall be divided into two equal shares. One share shall be further divided into equal subparts for each then living descendant of B per stirpes, and one share shall be further divided into equal subparts for each then living descendant of A's sister per stirpes. Each subpart will be held in further trust for A's niece or nephew for who such subpart was so set apart. Upon the death of A's said niece or nephew, the trust property will be distributed to the descendants of A's niece or nephew.

Article Ninth (A) of Trust provides that the Distribution Committee shall initially consist of A's brother, B, and child, C.

Article Ninth (B) of Trust provides that at all times during A's lifetime, the Distribution Committee will be composed of two beneficiaries of the Trust, other than A, or any spouse of A. In the event that B or C are unable to act, A's son will be the first beneficiary to fill the vacant position on the Distribution Committee. Thereafter, the then eldest beneficiary of the Trust shall fill any vacant position on the Distribution Committee. If at any time, there are less than two adult beneficiaries, the parent or guardian of the next eldest beneficiary shall fill any vacant position on the Distribution Committee. If all of A's descendants predecease A, the Distribution Committee powers will vest in the Trustee.

You have requested the following rulings:

1. So long as the Distribution Committee is serving, no portion of the items of income, deductions, and credits against tax of Trust shall be included in computing the taxable income, deductions, and credits of A or any other person under § 671.
2. The contribution of property to Trust by A will not be a completed gift subject to federal gift tax.
3. Any distribution of property from Trust to A by the Distribution Committee will not be a completed gift subject to federal gift tax.

RULING 1

Section 671 provides that where it is specified in subpart E of part I of subchapter J that the grantor or another person shall be treated as the owner of any portion of a trust, there shall then be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust which are attributable to that portion of the trust to the extent that such items would be taken into account under chapter 1 in computing taxable income or credits against the tax of an individual.

Section 672(a) provides, for purposes of subpart E, the term "adverse party" means any person having a substantial beneficial interest in the trust which would be adversely affected by the exercise or nonexercise of the power which he possesses respecting the trust.

Sections 673 through 677 specify the circumstances under which the grantor is treated as the owner of a portion of a trust.

Section 673(a) provides that the grantor shall be treated as the owner of any portion of a trust in which the grantor has a reversionary interest in either the corpus or the income therefrom, if, as of the inception of that portion of the trust, the value of such interest exceeds 5 percent of the value of such portion.

Section 674(a) provides, in general, that the grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

Section 674(b)(3) provides that § 674(a) shall not apply to a power exercisable only by will, other than a power in the grantor to appoint by will the income of the trust where the income is accumulated for such disposition by the grantor or may be so accumulated in the discretion of the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

Under § 675 and applicable regulations, the grantor is treated as the owner of any portion of a trust if, under the terms of the trust agreement or circumstances attendant on its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiary of the trust.

Section 676(a) provides that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under any other provision of part I, subchapter J, chapter 1, where at any time the power to revest in the grantor title to such portion is exercisable by the grantor or a nonadverse party, or both.

Section 677(a) provides, in general, that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under § 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a nonadverse party, or both, may be (1) distributed to the grantor or the grantor's spouse; (2) held or accumulated for future distribution to the grantor or the grantor's spouse; or (3) applied to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse.

Section 678(a)(1) provides a general rule that a person other than a grantor shall be treated as the owner of any portion of a trust with respect to which such person has a power exercisable solely by himself to vest the corpus or the income therefrom in himself.

Based solely on the facts and representations submitted, we conclude an examination of Trust reveals none of the circumstances that would cause A or any other person to be treated as the owner of any portion of Trust under § § 673, 674, 676, 677, or 678.

We further conclude that an examination of Trust reveals none of the circumstances that would cause administrative controls to be considered exercisable primarily for the benefit of A or any other person under § 675. Thus, the circumstances attendant on the operation of Trust will determine whether A or any other person will be treated as the owner of any portion of Trust under § 675. This is a question of fact, the determination of which must be deferred until the federal income tax returns of the parties involved have been examined by the office with responsibility for such examination.

RULINGS 2 AND 3

Section 2501(a)(1) provides for the imposition of a gift tax on the transfer of property by gift. Section 2511(a) provides that the gift tax applies to a transfer by way of gift 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 25.2511-2(b) of the Gift Tax Regulations provides that a gift is complete as to any property with respect to which the donor has so parted with dominion and control as to leave the donor with no power to change the disposition of the property, whether for the donor's own benefit, or for the benefit of another. But if upon a transfer of property (whether in trust or otherwise) the donor reserves any power over its disposition, the gift may be wholly incomplete, or may be partially complete and partially incomplete, depending upon all the facts in the particular case. Accordingly, in every case of a transfer of property subject to a reserved power, the terms of the power must be examined and its scope determined.

Section 25.2511-2(b) provides an example, where the donor transfers property in trust to pay the income to the donor, or accumulate it in the discretion of the trustee, and the donor retains a testamentary power to appoint the remainder among the donor's descendants. The regulation concludes that no portion of the transfer is a completed gift. However, if the donor had not retained a testamentary power of appointment, but had instead provided that the remainder should go to X or his heirs, the entire transfer would be a completed gift.

Section 25.2511-2(c) provides that a gift is incomplete in every instance in which a donor reserves the power to revest the beneficial title in himself or herself. A gift is also incomplete if and to the extent that a reserved power gives the donor the power to name new beneficiaries or to change the interests of the beneficiaries as between themselves unless the power is a fiduciary power limited by a fixed or ascertainable standard. Under § 25.2511-2(e), a donor is considered as possessing a power if it is exercisable by the donor in conjunction with any person not having a substantial adverse interest in the disposition of the transferred property.

Section 25.2511-2(f) provides that the relinquishment or termination of a power to change the beneficiaries of transferred property, occurring otherwise than by death of the donor, is regarded as the event which completes the gift and causes the gift tax to apply. See also, Estate of Sanford v. Commissioner, 308 U.S. 39 (1939).

Section 2514(b) provides that, in the case of a power of appointment created after October 21, 1942, the exercise or release of a general power of appointment shall be deemed a transfer of property by the individual possessing such power.

Section 2514(c) provides that the term "general power of appointment" means a power exercisable in favor of the individual possessing the power, the individual's estate, the individual's creditors, or the creditors of the individual's estate.

Section 25.2514-1(c)(1) provides that a power of appointment is not a general power if by its terms it is exercisable only in favor of one or more designated persons or classes other than the possessor or his creditors, or the possessor's estate or the creditors of the estate.

Section 2514(c)(3)(B) provides, that in the case of a power of appointment created after October 21, 1942, that is exercisable by the possessor only in conjunction with another person, if the power is not exercisable by the possessor except in conjunction with a person having a substantial interest in the property subject to the power, which is adverse to the exercise of the power in favor of the possessor, then the power is not a general power of appointment. For purposes of § 2514(c)(3)(B), a person who, after the death of the possessor, may be possessed of a power of appointment (with respect to the property subject to the possessor's power) which he may exercise in his own favor shall be deemed as having an interest in the property and such interest shall be

deemed adverse to such exercise of the possessor's power.

Section 25.2514-3(b)(2) provides, in part, that a co-holder of a power of appointment has no adverse interest merely because of his joint possession of the power nor merely because he is a permissible appointee under a power. However, a co-holder of a power is considered as having an adverse interest where he may possess the power after the possessor's death and may exercise it at that time in favor of himself, his estate, his creditors, or the creditors of his estate. Thus, for example, if X, Y, and Z held a power jointly to appoint among a group of persons which includes themselves and if on the death of X the power will pass to Y and Z jointly, then Y and Z are considered to have interests adverse to the exercise of the power in favor of X. Similarly, if on Y's death the power will pass to Z, Z is considered to have an interest adverse to the exercise of the power in favor of Y.

Section 25.2514-1(b)(2) provides that the term "power of appointment" does not include the powers reserved by a donor to himself or herself. However, no provision of § 2514 or the applicable regulations is to be construed as limiting the application of any other Code section or provision of the regulations.

In this case, A retains a limited testamentary power to appoint the Trust corpus and accumulated income to any persons (other than A, A's creditors, A's estate or the creditors of A's estate). In view of this retained power, A's transfer of property to Trust will not be a completed gift subject to federal gift tax. See, § 25.2511-2(b). However, A will be treated as making a taxable gift at such time as Trust corpus or income is distributed to a beneficiary other than A, or if, during A's lifetime, A releases the testamentary power to appoint the Trust property. See, § 25.2511-2(f).

In addition, B and C as members of the Distribution Committee, have the power to distribute Trust income and corpus to themselves. However, B's power can only be exercised with the consent of A or C, and C's power can only be exercised with the consent of A or B. Further, on the death of either B or C, the deceased's power will devolve to the survivor and A's son jointly. Therefore, B and C will not have a general power of appointment by reason of the joint distribution power. See, § 25.2514-3(b)(2). Accordingly, during the period the Distribution Committee consists of B and C, neither B nor C will be treated as making a taxable gift if Trust corpus or income is distributed to A under the terms of Trust.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code.

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

In accordance with the power of attorney on file with this office, copies of this letter are being sent to the taxpayer's authorized representatives.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)