



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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UIL No. 219.01-00, 408.00-00, 408A.00-00

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Legend:

Company X =

Investment Advisory Account A =

Investment Advisory Account B =

Investment Advisory Account C =

Dear:

This is in response to your letter dated April 14, 2008, submitted on your behalf by your authorized representative concerning the treatment of certain fees assessed in connection with investment advisory account services provided to owners of traditional individual retirement arrangements (IRAs) as described in section 408(a) and Roth IRAs as described in section 408A of the Internal Revenue Code (the "Code").

Under penalty of perjury the following facts and representations have been submitted in support of the rulings requested:

Company X is a securities broker-dealer and investment adviser, offering investment planning, advice and related financial services to its clients. Company X offers IRAs and Roth IRAs to its clients. You represent that Company X was approved as a non-bank custodian for IRAs pursuant to section 408(h) of the Code and section 1.408-2(e) of the Income Tax Regulations ("Regulations"), and that the Service has approved the original and amended versions of Company X's prototype individual retirement custodial account agreement.

Company X, the custodian of each of the IRAs, has established investment advisory account options that provide IRA account holders with investment advice and trade execution services for a quarterly fee. The fee is a percentage of assets under management and is not related to the number of trades executed in any account. This fee is referred to as a "wrap fee".

Following is a list and description of the advisory account options Company X currently offers to its IRA and Roth IRA account holders:

a. Investment Advisory Account A

Investment Advisory Account A is an investment advisory account through which clients receive discretionary and/or non-discretionary investment advice regarding the investment in eligible securities. With the exception of the discretionary services provided by separate account managers, the client is responsible for making all investment decisions in the account. Company X provides customized and professional investment advisory services through Investment Advisory Account A, which offers access to independent professional separate account managers, mutual funds and exchange traded funds. Company X assists the client in identifying investment goals, risk tolerance and investment preferences, and monitors the investment portfolio and goals. The client can choose to invest in a mutual fund portfolio, an exchange-traded fund ("ETF") portfolio, and/or through a separate account manager. If the client chooses the mutual fund portfolio, assets are allocated among an approved list of mutual funds. If the client chooses the ETF fund portfolio, assets are invested in one or more ETFs, which are a customized portfolio of underlying securities designed to capture performance of a particular index or industry sector. Clients can choose to have their mutual fund and/or ETF portfolios automatically rebalanced on annual, semi-annual or quarterly basis or can elect not to have the account automatically rebalanced. Rebalancing restores the balance of asset classes in a portfolio to its original target asset allocation. The mutual fund and ETFs are screened by an independent third party provider. If the client chooses a separate account manager, the manager provides portfolio management for a particular asset class and/or investment style on a discretionary basis. The separate account manager makes investment decisions and executes transactions on the client's behalf. The separate account manager option can be combined with the mutual fund and/or ETF portfolios. Each client receives a quarterly performance report that allows the client to monitor his or her portfolio and compare its performance against industry benchmarks. Additional services provided by Company X to accountholders include custody of securities and brokerage transaction execution. When opening Investment Advisory Account A, a client must also open a companion brokerage account with Company X. This companion account is used to effect brokerage transactions for the account.

The wrap fee for Investment Advisory Account A is an asset-based fee, based on the value of the assets held in the account. The amount of the fee varies, depending on the amount of assets under management and

type of investments in the account. Separate brokerage fees are not assessed under the companion brokerage account; the wrap fee covers brokers' commissions and fees.

b. Investment Advisory Account B

In Investment Advisory Account B, Company X provides financial planning and investment guidance, financial market and securities research, quarterly performance reporting, periodic portfolio review and brokerage transaction execution. Clients that select this account receive non-discretionary advice regarding investment in eligible securities, and the client makes all investment decisions. Clients can choose to invest their IRA assets in a wide range of eligible securities, including equity securities, bonds, mutual funds and ETFs. When opening Investment Advisory Account B, a client must also open a companion brokerage account with Company X. This companion account is used to effect brokerage transactions for the account.

The wrap fee for Investment Advisory Account B is an asset-based fee, based on the value of the assets held in the account. The wrap fee does not cover, and clients are responsible for paying, certain other expenses, including commissions charged by brokers other than Company X; interest on debit account balances; interest charges on margin loans; the entire public offering price (including underwriting commissions and discounts) on securities purchased from an underwriter or dealer involved in a distribution of securities; bid-ask spreads; odd lot differentials; exchange fees, transfer taxes and other fees required by law; transaction charges on the liquidation of assets not eligible for the account; and short-term trading charges for purchases and corresponding redemptions of certain mutual fund shares made within short periods of time as defined by the fund prospectus ("Other Expenses:"). In addition, any trade exceeding the trade caps specified in the account terms and conditions will be charged a \$55 active trader fee. Separate brokerage fees are not assessed under the companion brokerage account. Although there may be some additional expenses under the brokerage account, the wrap fee covers brokers' commissions and fees, regardless of the number of trades executed.

c. Investment Advisory Account C

Investment Advisory Account C is a non-discretionary investment advisory account. In this account option, Company X offers account holders a choice of one of five risk-based portfolios invested in mutual funds, as follows:

- Aggressive Portfolio;
- Moderate Aggressive Portfolio;

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- Moderate Portfolio;
- Moderate Conservative Portfolio; and
- Conservative Portfolio.

A Company X advisor assists the account holder in selecting an appropriate portfolio, based on his or her financial goals, time horizon to invest and risk tolerance. Each portfolio features professional risk allocation and quarterly rebalancing, including monitoring and review of the underlying funds in the account by a research specialist focused on portfolio management.

The wrap fee for Investment Advisory Account C is a quarterly asset-based fee, based on the value of the assets held in the account. Clients are also responsible for paying any other expenses assessed against the account.

Each Investment Advisory Account described above includes a securities trading service, the cost of which is included in the wrap fee. Clients who participate in these accounts are predominantly paying for investment advisory, money management, custodial and other administrative services.

Currently, the fees are invoiced to and paid from the IRA assets on a quarterly basis. Company X would like to offer clients the option of paying the wrap fee with non-IRA assets, without such payment being a "deemed" contribution to the client's IRA and/or Roth IRA.

Based on these facts and representations, the following rulings are requested:

1. Under Code section 408(a) for IRA accountholders and Code section 408A for Roth IRA accountholders who select Investment Advisory Account A, the payment of the wrap fee with funds that are not part of the clients' IRA and/or Roth IRA will not be treated as deemed contributions to such clients' IRA and/or Roth IRA.
2. Under Code section 408(a) for IRA accountholders and Code section 408A for Roth IRA accountholders who select Investment Advisory Account B, the payment of the wrap fee with funds that are not part of the clients' IRA and/or Roth IRA will not be treated as deemed contributions to such clients' IRA and/or Roth IRA.
3. Under Code section 408(a) for IRA accountholders and Code section 408A for Roth IRA accountholders who select Investment Advisory Account C, the payment of the wrap fee with funds that are not part of the clients' IRA and/or Roth IRA will not be treated as deemed contributions to such clients' IRA and/or Roth IRA.

Section 162 of the Code allows a deduction for the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

Section 212 of the Code provides that in the case of an individual, there shall be allowed as a deduction of all the ordinary and necessary expenses paid or incurred during the taxable year (1) for the production or collection of income, (2) for the management, conservation, or maintenance of property held for the production of income, or (3) in connection with the determination, collection or refund of any tax. Section 1.212-1(e) of the Regulations provides, in part, that section 212 does not allow the deduction of any expenses which are disallowed by any of the provisions of Subtitle A of the Code (relating to income taxes) even though such expenses may be paid or incurred for one of the purposes specified in section 212.

Section 219(a) of the Code provides that there shall be allowed as a deduction an amount equal to the qualified retirement contributions of the individual for the taxable year. Section 219(e)(1) provides that such contributions include amounts paid by or on behalf of an individual to an IRA.

Section 408A of the Code provides that an eligible individual may make a non-deductible contribution to a Roth IRA up to the limit specified in section 408A(c)(2).

Section 1.404(a)-3(d) of the Regulations provides that any expenses incurred by the employer in connection with a qualified employees' plan, such as trustee's and actuary's fees, which are not provided for by contributions under the plan are deductible by the employer under section 162 of the Code (relating to trade or business expenses), or section 212 (relating to expenses for the production of income), to the extent that such expenses are ordinary and necessary. Amounts that are not ordinary and necessary expenses are not deductible under section 162.

Rev. Rul. 84-146, 1984-2 C.B. 61, discusses the deductibility of trustee's fees with respect to IRAs. It holds that, consistent with the rules governing deductions in connection with qualified plans, amounts paid by the IRA owner for such fees in connection with an IRA are deductible under section 212 of the Code to the extent they satisfy the requirements of that section, but that the amounts paid that are not ordinary and necessary expenses, such as capital expenditures and disguised IRA contributions, are not deductible under section 212.

Rev. Rul. 86-142, 1986-2 C.B. 60, considered the deductibility of broker's commissions charged in connection with the purchase and sale of securities for a qualified employee's trust or an IRA. It notes that brokers' fees are not recurring administrative or overhead expenses incurred in connection with the maintenance of the trust or IRA. Rather, brokers' commissions are intrinsic to the

value of the trusts or account's assets; buying commissions are part of the cost of securities purchased and selling commissions are an offset against the sales price. Based on this analysis, IRA contributions to pay broker's commissions on transactions involving IRA assets are not deductible under section 162 or 212. Such contributions (and payments treated as IRA contributions) are deductible subject to the limits of section 219.

With respect to each Investment Advisory Account offered by Company X, the services provided to its accountholders include investment advice, performance monitoring and review, trade execution, money management and custodial services.

The wrap fees assessed by Company X for services it provides with respect to Investment Advisory Accounts A, B and C are based on a fee structure calculated as a percentage of the value of the assets held in the respective account. The fees do not vary with the frequency of the transactions performed and are distinct from the cost or volume of any assets purchased or sold. Even though the companion brokerage account with each Investment Advisory Account provides brokerage services, the fee charged is still calculated as a percentage of the total assets under management, and clients' can make an unlimited number and amount of trades without incurring additional fees. The fees assessed by Company X for its services with respect to Investment Advisory Accounts A, B and C are recurring administrative or overhead expenses incurred in connection with the maintenance of clients' respective IRAs and/or Roth IRAs.

Therefore, with respect to your ruling requests one, two and three, we conclude that the payment of wrap fees by accountholders that participate in Investment Advisory Accounts A, Investment Advisory Account B and/or Investment Advisory Account C will not be deemed contributions to such clients' traditional IRAs under section 408(a) of the Code, and/or Roth IRAs under section 408A of the Code if paid directly from funds that are not part of the accountholders' respective IRAs and/or Roth IRAs.

No opinion is expressed as to the tax treatment of the transaction described herein under the provisions of any other section of either the Code or Regulations which may be applicable thereto.


This ruling is limited to the treatment of program fees paid to Company X in the manner herein described and is not intended to apply to any additional fees that may be charged by Company X to its IRA and Roth IRA clients that participate in any of the Investment Advisory Accounts described herein.

This 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.

A copy of this ruling letter has been sent to your authorized representative in accordance with power of attorney on file in this office.

If you wish to inquire about this ruling, please contact ***, I.D. No. ***, at ***. Please address all correspondence to SE:T:EP:RA:T4.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Laura B. Warshawsky".

Laura B. Warshawsky, Manager
Employee Plans, Technical Group 4

Enclosures:

Deleted Copy of Ruling Letter
Notice of Intention to Disclose

cc: