

concerning the federal tax consequences of the proposed division of Trust into Trust 1 and Trust 2 and the subsequent termination of Trust 1.

The facts and representations submitted are summarized as follows. Decedent died on Date 1, survived by his wife, Taxpayer. More than nine months have elapsed since Date 1. Prior to his death, Decedent created Trust which became irrevocable on Date 1. Pursuant to the terms of Trust, upon the death of Decedent the property of Trust was held in a separate trust known as the "Marital Trust" for the benefit of Taxpayer. Pursuant to Article IV of Trust, Taxpayer is the sole income beneficiary of Trust and is to receive all the net income in quarterly or more frequent installments. Taxpayer has the unrestricted use and exclusive enjoyment during her lifetime of all real and personal tangible property held by Trust. Upon the death of Taxpayer, the remaining Trust assets are to be distributed to Foundation, free and clear of trusts, for its general charitable purposes. Taxpayer is the current successor trustee of Trust. The principal of Trust currently includes certain tracts or parcels of improved and unimproved real property of approximately x acres in Location, State 1.

Article VI of Trust provides that Taxpayer may, at any time, disclaim any interest in the trust, or may disclaim any portion of such interest. The disclaimer must be in writing and delivered to the trustees. If the disclaimer is not a "qualified interest" pursuant to section 2518, then the disclaimed interest will be disposed of, and the provisions of Trust which relate to the disclaimed interest will be administered as though Taxpayer died at the time the disclaimer was delivered to the trustee.

Prior to Decedent's death, Decedent formed Foundation, a State 2 nonprofit corporation that is classified within the meaning of sections 170(c), 501(c)(3), 2055(a)(2), and 2522(a)(2). Taxpayer is the President, chairman, and sole director of Foundation.

On Date 2, Foundation, as settlor, established Charitable Trust. Charitable Trust is a State 2 charitable trust that is described in sections 170(c), 501(c)(3), 2055(a)(2), and 2522(a)(2). Taxpayer and nine other individuals are the trustees of Charitable Trust. Pursuant to Article V, paragraph H of the Charitable Trust instrument, Taxpayer has the right to make the final decision regarding all issues relating to the administration of Charitable Trust, including, but not limited to, all issues relating to the activities, operations and programs described therein, and the making of expenditures and distributions from Charitable Trust. Pursuant to Article VIII, paragraph B, the trustees have the power to sell or otherwise dispose of any property owned by Charitable Trust. However, this power is limited with respect to certain property not relevant to this ruling.

On the United States Estate (and Generation-Skipping Transfer) Tax Return, Form 706, filed for the Decedent's estate, the executors elected under section 2056(b)(7) to treat the entire value of the property held by Trust at the Decedent's death as passing from the Decedent to the Taxpayer, for which an estate tax marital deduction was allowed under section 2056(a).

On Date 2, Foundation irrevocably assigned its remainder interest in Trust to Charitable Trust. Consequently, upon Taxpayer's death, the remaining assets of Trust will be distributed to Charitable Trust.

Taxpayer, as the income beneficiary of Trust and as the trustee of Charitable Trust, proposes to file a petition with Court to enter an order to divide Trust into two separate and distinct successor trusts, to be known as Trust 1 and Trust 2. Each trust is to be administered, governed and distributed in accordance with the terms and conditions of the original Trust. The Court order to divide Trust into Trust 1 and Trust 2 will be specifically conditioned upon a favorable tax ruling from the Internal Revenue Service (IRS).

Upon the division of Trust into Trust 1 and Trust 2, an unimproved parcel of real property, Parcel, currently owned by Trust, consisting of y acres, will be transferred to Trust 1 by conveyance and assignment. Trust 2 will continue to hold all of the other assets currently owned by Trust. After the division of Trust, Taxpayer proposes to disclaim her entire interest in Trust 1, pursuant to the terms of Article VI of Trust. Accordingly, Trust 1 will terminate as a result of Taxpayer's disclaimer of her entire interest in Trust 1, and Parcel will be transferred to Charitable Trust.

State Law provides that a court may, for cause shown, authorize the division of a trust into two or more separate trusts upon such terms and conditions and with such notice as it may direct.

You have requested the following rulings:

1) The division of Trust into two separate and distinct trusts, Trust 1 and Trust 2, will not adversely affect the availability of the estate tax marital deduction by the Decedent's estate, the election under section 2056(b)(7) with respect to Trust, nor the status of the property held by the two successor trusts as qualified terminable interest property.

2) Upon Taxpayer's disclaimer of her entire interest in Trust 1, Taxpayer will not be deemed to have made a transfer for gift tax purposes of any property of Trust 2 under sections 2511 and 2519, and therefore, there is no transfer by Taxpayer of any property in Trust 2 by gift under section 2501 as a result of Taxpayer's disclaimer of her entire interest in Trust 1.

3) Upon Taxpayer's disclaimer of her entire interest in Trust 1, any transfer for gift tax purposes of any property in Trust 1 that would otherwise result under sections 2511 and 2519 is incomplete because of Taxpayer's position as trustee of Charitable Trust and, therefore, there is no transfer of any property in Trust 1 by gift under section 2501 as a result of Taxpayer's disclaimer of her entire interest in Trust 1.

- 4) The value of the property transferred from Trust 1 to Charitable Trust as a result of Taxpayer's disclaimer of her entire interest in Trust 1 will be included in Taxpayer's gross estate under section 2036(a)(2).
- 5) Taxpayer will be entitled to a charitable estate tax deduction under section 2055(a) for the value of the property included in her gross estate under section 2036(a)(2) as a result of the disclaimer of her entire interest in Trust 1.
- 6) The value of the property in Trust 2 will be included in Taxpayer's gross estate under section 2044(a).
- 7) Taxpayer will be entitled to a charitable estate tax deduction under section 2055(a) for value of the property in Trust 2 included in her gross estate under section 2044(a).
- 8) The division of Trust into Trust 1 and Trust 2 and the funding of Trust 1 and Trust 2 on a non-pro rata basis will not cause Trust to realize gain or loss under section 1001.
- 9) Neither Taxpayer's disclaimer of her entire interest in Trust 1, the transfer of Parcel in Trust 1 to Charitable Trust, nor the ownership of the property by Charitable Trust of the property transferred from Trust 1 as a result of Taxpayer's disclaimer will result in an act of self-dealing under section 4941.

Rulings 1-7

Section 2501(a) provides that a tax is imposed on the transfer of property by gift by any individual. Section 2511(a) provides that the gift tax applies 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 and subject to the gift tax when the donor has so parted with dominion and control over the property transferred as to leave in the donor no power to change its disposition, whether for the donor's own benefit or for the benefit of another.

Section 25.2511-2(c) provides, in part, that a gift is incomplete in every instance in which a donor reserves the power to revest the beneficial title to the property in himself. 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.

Section 25.2511-2(e) provides that a donor is considered to have 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, such as a trustee.

Section 2519(a) provides that, for gift and estate tax purposes, any disposition of all or part of a qualifying income interest for life in any property to which the section applies shall be treated as a transfer of all interests in the property other than the qualifying income interest. Section 2519(b) provides that the section applies to any property if a deduction was allowed with respect to the transfer of the property to the donor under section 2056(b)(7).

Section 25.2519-1(a) provides that, if a donee spouse makes a disposition of all or part of a qualifying income interest for life in any property for which a deduction was allowed under section 2056(b)(7), the donee spouse is treated, for purposes of the estate and gift tax, as transferring all interests in property other than the qualifying income interest.

Section 2056(a) provides that the value of the taxable estate shall, except as limited by section 2056(b), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse.

Under section 2056(b)(1), if an interest passing to the surviving spouse will terminate, no deduction shall be allowed with respect to such interest if, after termination of the spouse's interest, an interest in the property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than the surviving spouse (or the estate of the spouse).

Section 2056(b)(7)(A) provides that qualified terminable interest property (QTIP), for purposes of section 2056(a), shall be treated as passing to the surviving spouse, and no part of the property shall be treated as passing to any person other than the surviving spouse. In general, under section 2056(b)(7)(B)(i), qualified terminable interest property is property that passes from the decedent in which the spouse receives a qualifying income interest for life (defined in section 2056(b)(7)(B)(ii)), and with respect to which the executor makes an election to treat the property as QTIP.

Section 2044(a) provides that the value of the gross estate includes the value of any property described in section 2044(b) in which the decedent had a qualifying income interest for life. Section 2044(b) provides that section 2044 applies to any property if a deduction was allowed with respect to the transfer of the property to the decedent under section 2056(b)(7).

Section 2036(a) provides that the value of the gross estate includes the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which the decedent has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death: (1) the

possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

In Rev. Rul. 72-552, 1972-2 C.B. 525, the decedent, who was the president and director of a corporation organized under section 501(a), transferred property to the corporation. In his capacity as president and a director, the decedent, in conjunction with the other directors of the corporation, had the power to direct the disposition of the corporation's funds for charitable purposes. The ruling held that, due to the president's right, in conjunction with others, to designate the entities that shall possess or enjoy the properties transferred to the corporation, the property transferred by the president to the corporation was included in the president's gross estate at his death under section 2036.

Section 2055(a) provides, in part, that for estate tax purposes, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, or transfers to or for the use of any corporation organized and operated exclusively for religious, charitable, educational and certain other purposes.

In this case, upon Decedent's death, the entire property held by Trust was treated as qualified terminable interest property and a marital estate tax deduction under section 2056(b)(7) was allowed by the IRS. Taxpayer is the sole income beneficiary of Trust and is to receive all the net income in quarterly or more frequent installments. Under the proposed transaction, the resultant successor trusts, Trust 1 and Trust 2, will each be administered, governed and distributed in accordance with the terms and conditions of the original Trust. Accordingly, the division of Trust into two separate and distinct trusts, Trust 1 and Trust 2, will not adversely affect the availability of the estate tax marital deduction by the Decedent's estate, the election under section 2056(b)(7) with respect to Trust, nor the status of the property held by the two successor trusts as qualified terminable interest property.

As a result of Taxpayer's disclaimer of her interest in Trust 1, Taxpayer is treated as making a transfer of her interest in Trust 1 under section 2511, and a disposition of her qualifying income interest under section 2519 such that Taxpayer is also treated as making a transfer of the remainder interest in the Trust 1 corpus, consisting of Parcel. However, in accordance with Article VI of Trust, as a result of Taxpayer's disclaimer, Parcel will pass to Charitable Trust. Taxpayer is a trustee of Charitable Trust, and under the terms of Charitable Trust, has the right to make the final decision regarding all issues relating to the administration of Charitable Trust, including the power to direct expenditures and distributions for charitable purposes. Therefore, Taxpayer's proposed disclaimer of her interest in Trust 1 constitutes an incomplete gift for purposes of section 2511. Similarly, Taxpayer's transfer under section 2519 also constitutes an incomplete gift. See Rev. Rul. 72-552. Accordingly, Taxpayer will not be treated as making a completed gift subject to gift tax under section 2501 as a result of the disclaimer.

We further conclude that, assuming Taxpayer retains her powers over the transferred property until her death, the value of the property transferred from Trust 1 to Charitable Trust as a result of Taxpayer's disclaimer will be included in Taxpayer's gross estate under section 2036(a)(2). Rev. Rul. 72-552. See also, section 25.2519-1(g), Example 4 and Example 5. Taxpayer's estate will be entitled to an estate tax charitable deduction under section 2055(a) for the value of the property included her gross estate under section 2036(a)(2) as a result of her disclaimer of her entire interest in Trust 1.

Moreover, upon Taxpayer's disclaimer of her entire interest in Trust 1, Taxpayer will not be deemed to have made a transfer for gift tax purposes of any property of Trust 2 under sections 2511 and 2519, and therefore, there is no transfer by Taxpayer of any property in Trust 2 by gift under section 2501 as a result of Taxpayer's disclaimer of her entire interest in Trust 1. Thus, upon her death the value of the property in Trust 2 will be included in Taxpayer's gross estate under section 2044(a). Taxpayer will be entitled to a charitable estate tax deduction under section 2055(a) for the value of the property in Trust 2 included in her gross estate under section 2044(a).

Ruling 8

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

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 section 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in section 1011 for determining loss over the amount realized.

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

Section 1.1001-1(a) of the Income Tax Regulations provides that the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or loss sustained.

A partition of jointly owned property is not a sale or other disposition of property where the co-owners of the joint property sever their joint interests but do not acquire a new or additional interest as a result of the transaction. Thus, neither gain nor loss is realized on a partition. See Rev. Rul. 56-437, 1956-2 C.B. 507.

Cottage Savings Ass'n v. Commissioner, 499 U.S. 554 (1991), concerns the issue of whether a sale or exchange that has taken place results in the realization of gain or loss under section 1001. In Cottage Savings, a financial institution exchanged its interests in one group of residential mortgage loans for another lender's interests in a different group of residential mortgage loans. The two groups of mortgages were considered "substantially identical" by the agency that regulated the financial institution.

The Court in Cottage Savings, concluded that section 1.1001-1 reasonably interprets section 1001(a) and stated that an exchange of property gives rise to a realization event under section 1001(a) if the properties exchanged are "materially different." In defining what constitutes a "material difference" for purposes of section 1001(a), the Court stated that properties are "different" in the sense that is "material" to the Internal Revenue Code so long as their respective possessors enjoy legal entitlements that are different in kind or extent. Cottage Savings, 499 U.S. at 564-65. The Court held that mortgage loans made to different obligors and secured by different homes did embody distinct legal entitlements, and that the taxpayer realized losses when it exchanged interests in the loans. Cottage Savings, 499 U.S. at 566.

In the present case, provided that Court approves the petition for division, it is consistent with the Supreme Court's opinion in Cottage Savings to find that the interests of the beneficiaries of Trust 1 and Trust 2 will not differ materially from their interests in Trust. In the proposed transaction, Trust will be divided but the beneficiaries' interests in the property will not change in kind or extent and no interests will be created. All of the provisions of Trust will remain unchanged. Accordingly, the proposed transaction will not result in a material difference in kind or extent of the legal entitlements enjoyed by the beneficiaries, and no gain or loss is recognized by the beneficiaries or the trusts on the partition for purposes of section 1001.

Ruling 9

Section 4941(a), in part, imposes a tax on each act of self-dealing between a private foundation and a disqualified person. The tax is imposed on the disqualified person and, in certain situations, a tax is also imposed on the foundation manager(s) participating in the act or acts.

Section 4941(d)(1)(E) includes in the definition of self-dealing any direct or indirect transfer to, or use for the benefit of, a disqualified person of the income or assets of a private foundation.

Section 4946(a)(1) states in part that the term "disqualified person" means, with respect to a private foundation, a person who is— (A) a substantial contributor to the foundation, (B) a foundation manager (within the meaning of subsection (b)(1)), (C) an owner of more than 20 percent of—(i) the total combined voting power of a corporation, (ii) the profits interest of a partnership, or (iii) the beneficial interest of a trust or unincorporated enterprise, which is a substantial contributor to the foundation, (D) a

member of the family (as defined in subsection (d)) of any individual described in subparagraph (A), (B), or (C).

Section 53.4941(d)-1 of the Foundation and Similar Excise Taxes Regulations provides, in general, that for purposes of section 4941, the term "self-dealing" means any direct or indirect transaction described in section 53.4941(d)-2. For purposes of this section it is immaterial whether the transaction results in a benefit or a detriment to the private foundation.

Section 53.4941(d)-2(f)(2) provides that an exception to the prohibited use of foundation assets applies where a disqualified person receives only an incidental or tenuous benefit from the use by a private foundation of its income or assets.

Taxpayer is a disqualified person within the meaning of sections 4946(a)(1)(B) and (D). Taxpayer will receive no consideration in connection with the proposed transaction, and will have no private use or ownership of Parcel in Trust 1 after the transfer to Charitable Trust. All of the property in Trust 1 will be used exclusively by Charitable Trust in furtherance of its charitable purposes and activities. Accordingly, neither the Taxpayer's disclaimer, nor the transfer of Parcel, nor the ownership of Parcel by Charitable Trust will result in an act of self-dealing within the meaning of section 4941.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

George L. Masnik
Branch Chief, Branch 4
(Passthroughs & Special Industries)

Enclosures

Copy for section 6110 purposes
Copy of this letter