

Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B02
PLR-158118-04
Date:

September 19, 2005

Legend

Trust 1:

Trust 2:

Trust 3:

Trust 4:

Settlor:

A:

W:

X:

Y:

Z:

State:

a:

b:

c:

Date 1:

Date 2:

Dear _____ :

This letter responds to a letter dated November 3, 2004, and subsequent correspondence, submitted on behalf of Trust 1, Trust 2, Trust 3 and Trust 4 (collectively, the Family Trusts) by the Family Trusts' authorized representative, requesting certain rulings under the Internal Revenue Code.

The information submitted states that the Family Trusts were established on Date 1 and Date 2 by Settlor for the benefit of the issue of A, a child of Settlor. The provisions and the beneficiaries of each of the Family Trusts are identical. Currently, the Family Trusts have the same trustee. Under the terms of each of the Family Trust agreements, the trustees have discretion to distribute income or principal to or among a class of beneficiaries consisting of the issue of A. A currently has a children and b grandchildren. All of A's children are adults and all of A's grandchildren are minors. Each of the Family Trust agreements provides that upon the death of the last surviving child of A (or upon the death of A if he survives his children), each of the Family Trusts will be divided into equal shares, one for each A's children who leave descendants then living, and each share is then further subdivided *per stirpes* into separate parts for the descendants of each of A's children. Each part for a descendant is directed to be held in further trust for such descendant, provided that any descendant may withdraw his or her trust after age 21, and any descendant has a general testamentary power to appoint his or her trust upon that descendant's death.

Each of the Family Trusts owns a 99 percent general partnership interest in a general partnership. Trust 1 holds an interest in W. Trust 2 holds an interest in X. Trust 3 holds an interest in Y. Trust 4 holds an interest in Z. A owns the remaining 1 percent general partnership interest in each of the partnerships.

Trustees propose to merge and divide the Family Trusts taking into account the separate investment objectives of A's children and their families. First, Trust 1, Trust 2, and Trust 3 will be merged with and into Trust 4 under State law. Then the assets of the merged Trust 4 will be divided pro rata into a separate trusts (New Trusts), one for each child of A. Each of the New Trusts will contain substantially the same terms and

hold equal interests in all four partnerships.

RULING 1

Section 61(a)(3) provides that gross income includes gains derived from dealings in property and, under § 61(a)(15), from an interest in a trust.

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

Section 1001(b) provides 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 § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under § 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 when a sale or exchange has taken place that results in realization of gain or loss under § 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 Supreme Court of the United States in Cottage Savings, 499 U.S. at 560-61, concluded that § 1.1001-1 reasonably interprets § 1001(a) and stated that an exchange of property gives rise to a realization event under § 1001(a) if the properties exchanged are "materially different." In defining what constitutes a "material difference" for purposes of § 1001(a), the Court stated that properties are "different" in the sense that is "material" to the 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.

It is consistent with the Supreme Court's opinion in Cottage Savings to find that the interests of the beneficiaries of the New Trusts will not differ materially from their interests in Trust 1, Trust 2, Trust 3 and Trust 4 before the merger and division. Each beneficiary will continue to hold, through his or her interest in a New Trust, the same beneficial interest in each asset of Trust 1, Trust 2, Trust 3 and Trust 4 that he or she held before the merger and division, and each interest in the divided trust will contain substantially the same terms. Accordingly, the proposed trust merger and division will not result in a material difference in kind or extent of the legal entitlements, and no gain or loss is recognized on the trust merger and division by any trust or trust beneficiary for purposes of § 1001(a).

RULINGS 2 and 3

Section 1015(b) provides that if property is acquired by a transfer in trust (other than a transfer in trust by a gift, bequest, or devise), the basis shall be the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor on such transfer.

Section 1.1015-2(a)(1) provides that in the case of property acquired after December 31, 1920, by transfer in trust (other than by transfer in trust by gift, bequest, or devise) the basis of property so acquired is the same as it would be in the hands of the grantor increased by the amount of gain or decreased in the amount of loss recognized to the grantor on the transfer under the law applicable to the year in which the transfer was made. If the taxpayer acquired the property by transfer in trust, this basis applies whether the property be in the hands of the trustee, or the beneficiary, and whether acquired prior to termination of the trust and distribution of the property, or thereafter.

Section 1223(2) provides that, in determining the period for which the taxpayer has held property however acquired, there shall be included the period for which such property was held by any other person, if under Chapter 1 of Subtitle A such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as it would have in the hands of such other person. See also § 1.1223-1(b).

Based solely on the facts and representations submitted, we conclude that because § 1001 does not apply to the proposed Family Trusts mergers, under § 1015, the tax basis that the merged Trust 4 has in the assets of the merging Family Trusts immediately after the mergers will be the same as the tax basis of the merging Family Trusts in such assets immediately before the mergers. The tax basis of the historic assets in merged Trust 4 immediately after the mergers will be the same as the tax basis that the Family Trusts had in those assets immediately before the mergers. We further conclude that each asset transferred by the Family Trusts to merged Trust 4 will have the same holding period in the hands of the merged Trust 4 immediately after the mergers that it had in the hands of the Family Trusts immediately before the mergers.

Each historic asset of the merged Trust 4 will have the same holding period immediately after the mergers that it had immediately before the mergers.

We also conclude that because § 1001 does not apply to the proposed division of merged Trust 4, under § 1015, the tax basis that the New Trusts have in the assets of the New Trusts immediately after the division will be the same as the tax basis of the merged Trust 4 in such assets immediately before the division. The tax basis of the historic assets in the New Trusts immediately after the division will be the same as the tax basis that the merged Trust 4 had in those assets immediately before the division. We further conclude that each asset transferred by the merged Trust 4 to the New Trusts will have the same holding period in the hands of the New Trusts immediately after the division that it had in the hands of the merged Trust 4 immediately before the division. Each historic asset of the New Trusts will have the same holding period immediately after the division that it had immediately before the division.

We additionally conclude that in each of the mergers of the Family Trusts into Trust 4, the merged Trust 4 will succeed to and take into account any net operating loss carry forward (NOLCF), net capital loss, and other tax attributes, including passive activity losses and credit carryforwards, of the merging Family Trusts. Each asset transferred by the merging Family Trusts to the merged Trust 4 will have the same tax attributes immediately after the merger that it had immediately before the merger. Each historic asset of the merged Trust 4 will have the same tax attributes immediately after the merger that it had immediately before the merger. All NOLCFs, net capital losses, and other tax attributes, including passive activity losses and credit carryforwards, of the merging Family Trusts immediately before the mergers will survive and remain available to the merged Trust 4 after the mergers and no limitation will be imposed as a result of the proposed mergers on the merged Trust 4's use of such tax attributes.

Finally, we conclude that on the division of the merged Trust 4 into New Trusts, each of the New Trusts will succeed to and take into account c of any net operating loss carry forward (NOLCF), net capital loss, and other tax attributes, including passive activity losses and credit carryforwards, of the divided merged Trust 4. Each asset transferred by the divided merged Trust 4 to the New Trusts will have the same tax attributes immediately after the division that it had immediately before the division. Each historic asset of the New Trusts will have the same tax attributes immediately after the division that it had immediately before the division. All NOLCFs, net capital losses, and other tax attributes, including passive activity losses and credit carryforwards, of the divided merged Trust 4 immediately before the division will survive and remain available to the divided New Trusts after the division and no limitation will be imposed as a result of the proposed division on the New Trusts' use of such tax attributes.

Except as specifically ruled above, we express no opinion concerning the federal tax consequences of the transactions described above under any other provisions of the Code.

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

Pursuant to a power of attorney on file, a copy of this letter is being sent to the Family Trusts' authorized representative.

Sincerely,

J. THOMAS HINES
Chief, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures: 2
Copy of this letter
Copy for § 6110 purposes

cc: