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Department of the Treasury

Washington, D.C. 20224

Person to Contact:

Telephone Number:

Refer Reply to:
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LEGEND:

Trust	=
Fund A	=
Fund B	=
Limited Partnership	=
Company A	=
Company B	=
State X	=
State Y	=
Date 1	=
Date 2	=
Date 3	=
a	=
b	=

Dear :

This is in response to a March 30, 2000, letter and subsequent correspondence submitted on behalf of Fund A and Fund B (each a "Fund" or collectively "the Funds") and Trust. The four rulings requested in the letter are as follows:

Ruling 1: Trust will not be a publicly traded partnership taxed as a corporation under § 7704 of the Internal Revenue Code (the "Code").

Ruling 2: Each of the Funds will be deemed to own a proportionate share of each of the assets of Trust and will be deemed to be entitled to the income of Trust attributable to such share for purposes of determining whether the Fund satisfies the requirements of §§ 851(b)(2), 851(b)(3), 852(b)(5), 853(a), and 854.

Ruling 3: Under § 721, no gain or loss will be recognized by Trust or the Funds upon a contribution of property to Trust by a Fund in exchange for shares of beneficial interest in Trust.

Ruling 4: The method to be employed by Trust for making forward and reverse § 704(c) allocations among the Funds, including aggregating qualified financial assets, is a reasonable method within the meaning of §§ 1.704-3(a)(1) and 1.704-3(e)(3) of the Income Tax Regulations and is permitted by the Commissioner under § 1.704-3(e)(4)(iii).

FACTS

The Funds were organized as State X corporations on Date 1 under the sponsorship of Limited Partnership. The Funds intend to qualify for and elect status as regulated investment companies ("RICs") under §§ 851-855 of the Code. The Funds have elected to have a fiscal year ending on February 28.

Limited Partnership is a limited partnership, the partners of which are Company A and Company B. Limited Partnership is in the business of providing investment management and related services and is registered with the Securities and Exchange Commission as an investment adviser under the Investment Advisers Act of 1940. It is anticipated that Limited Partnership will be the principal investment adviser of each Fund.

Limited Partnership established Trust as a State Y business trust by filing a Certificate of Trust and by conveying assets to the trustees for the Trust. A Declaration of Trust (Declaration) dated on Date 2 sets out the terms of the Trust. Trust is registered as an open-end management company under the Investment Company Act of 1940 ("the 1940 Act"). Trust has a taxable year identical to that of the Funds. On Date 3, Limited Partnership transferred $a to each of the Funds. On the same date, the Funds then transferred the $a each received from Limited Partnership to Trust in exchange for general partnership interests in Trust. Also, Company B transferred $b to Trust in exchange for a general partnership interest in Trust. Trust is registered as an open-end management company under the Investment Company Act of 1940. Trust will be involved in the investment of the funds of its investors. The investment objective of Trust will be identical to that of the Funds. All of the assets contributed to Trust will be managed at the Trust level.

Interests in Trust will be offered and sold only to RICs, insurance company separate accounts, common or commingled trust funds, group trusts and similar entities that qualify as accredited investors within the meaning of Regulation D under the Securities Act of 1933. Such entities are referred to as "Institutional Investors." Any entity with an interest in Trust is referred to as a "Holder" and will be limited to Institutional Investors. Trust will not issue interests to any individual, S corporation, partnership, or grantor trust, a grantor of which includes an individual, S corporation, or partnership.

Taxpayer represents that Trust will be classified as a partnership for federal tax purposes. Trust will establish a capital account for each Holder upon such Holder’s contribution of capital (cash or securities) to Trust. A Holder’s interest in Trust will be determined by reference to its capital account therein. The initial value of any Holder’s capital account will be the fair market value of the assets contributed on the date of contribution. Trust will adjust each Holder’s capital account, and, therefore, its interest in the Trust, daily, pursuant to § 1.704-1(b)(2)(iv)(f) of the regulations. Trust will also adjust each Holder’s capital account for each Holder’s ratable share of unrealized gain or loss. Allocations of book income of Trust will be in accordance with the Holder’s interest in each class of interests in Trust determined by reference to its capital account.

Trust represents that it is a management company within the meaning of § 1.704-3(e)(3)(iii)(B) and will hold as assets only qualified financial assets, within the meaning of § 1.704-3(e)(3)(ii), and cash. Trust will aggregate gains and losses from its financial assets as provided in § 1.704-3(e)(3) by using the full netting approach set forth in § 1.704-3(e)(3)(v).

REPRESENTATIONS

The following representations are made on the behalf of Trust, Fund A, and Fund B:

<u>Ruling 1</u>:

Trust will not have a Holder that is a flow-through entity with a principal purpose of permitting the Trust to satisfy the 100-partner limitation under § 7704 of the Code.

The number of Holders owning interests in Trust will be less than 100 and none of the Holders will be a partnership, grantor trust, or an S corporation that is beneficially owned by more than one individual.

No interests in Trust have been traded on an established securities market or issued in a transaction registered under the Securities Act of 1933.

Ruling 2:

For purposes of determining the required distribution under § 4982(a)(1) of the Code, Fund A and Fund B will each account for its share of partnership items of income, gain, loss, and deduction as they are taken into account by Trust.

Except as required by § 704(c) and § 1.704-1(b)(4) of the regulations, Fund A's and Fund B's allocable share of Trust's income, gain, loss, deduction, and credit will be comprised of a proportionate share of each item of income includible in Trust's gross income.

The organization of Trust was done in a manner to enable it to be classified as a partnership and was not done to enable a partner that is a RIC to make distributions that would be prohibited under Rev. Rul. 89-81, 1989-21 C.B. 226, had the RIC invested directly in Trust's assets.

Ruling 3:

Fund A and Fund B have contributed or will contribute solely cash and/or a diversified portfolio of stock and securities to Trust.

Any other transferor who has contributed or will contribute assets to Trust has contributed or will contribute solely cash and/or a diversified portfolio of stock and securities to Trust.

For purposes of these representations, a portfolio of stocks and securities is diversified if it satisfies the 25 and 50 percent tests of § 368(a)(2)(F)(ii) of the Code, applying the relevant provisions of § 368(a)(2)(F), except that in applying § 368(a)(2)(F)(iv), government securities are included in determining total assets unless the government securities are acquired to meet the requirements of § 368(a)(2)(F)(ii).

Ruling 4:

Trust is a management company within the meaning of § 1.704-3(e)(3)(iii)(B) of the regulations and will hold as assets only qualified financial assets, within the meaning of § 1.704-3(e)(3)(ii), and cash.

Trust will comply in all respects with the capital account maintenance rules set forth in § 1.704-1(b)(2)(iv).

Revaluations and the corresponding allocations of tax items by Trust are not and will not be made with a view to shifting the tax consequences of built-in-gain or loss among its partners in a manner that substantially reduces the present value of the partners' aggregate tax liability.

The Funds intend to qualify for and elect status as regulated investment companies ("RICs") under §§ 851-855.

Future partners in Trust will satisfy the following conditions: (1) the partner is registered under the Investment Company Act of 1940, 15 U.S.C. 80a-1 et seq., and would be considered a "publicly offered regulated investment company" as defined in § 67(c)(2)(B) and § 1.67-2T(g)(3)(ii); (2) the partner's contribution is made and accepted for valid business purposes (and not made primarily for tax motivated reasons (other than the fact that the contribution to Trust is tax-free)); and (3) to the extent Trust relies on this ruling for the contribution, Trust will document any such contribution on its tax return filed subsequent to the contribution.

LAW AND ANALYSIS

Ruling 1:

Section 7704(a) of the Code provides that a publicly traded partnership is treated as a corporation. Section 7704(b) and § 1.7704-1(a) of the regulations provide that, under § 7704, the term "publicly traded partnership" means any partnership if interests in the partnership are (i) traded on an established securities market, or (ii) readily tradable on a secondary market or the substantial equivalent thereof.

Section 1.7704-1(c)(1) provides that interests in a partnership are readily tradable on a secondary market or the substantial equivalent thereof if, taking into account all of the facts and circumstances, the partners are readily able to buy, sell, or exchange their partnership interests in a manner that is comparable economically to trading on an established securities market.

Section 1.7704-1(h)(1) provides that interests in a partnership are not treated as readily tradable on a secondary market or the substantial equivalent thereof within the meaning of § 7704(b) if (i) all interests in the partnership were issued in a transaction (or transactions) that was not registered under the 1933 Act; and (ii) the partnership does not have more than 100 partners at any time during the taxable year.

Section 1.7704-1(h)(3) provides that, for § 1.7704-1(h)(1) a person who owns an interest in a partnership, grantor trust, or S corporation (flow-through entities) that owns, directly or through other flow-through entities, an interest in the partnership is treated as a partner in the partnership only if (i) substantially all of the value of the beneficial owner’s interest in the flow-through entity is attributable to the flow-through entity’s interest (direct or indirect) in the partnership; and (ii) a principal purpose of the use of the tiered arrangement is to permit the partnership to satisfy the 100-partner limitation of § 1.7704-1(h)(1)(ii).

Ruling 2:

Section 851(a) of the Code defines a RIC, in part, as a domestic corporation registered under the 1940 Act as a management company.

Section 851(b) limits the definition of a RIC to a corporation meeting certain election, gross income, and diversification requirements.

Section 851(b)(2) provides that, to qualify as a RIC, 90 percent of a corporation's gross income must be derived from dividends, interest, payments with respect to securities loans (as defined in § 512(a)(5)), gains from the sale or other disposition of stocks, securities, foreign currencies, or other income derived with respect to the business of investing in such stocks, securities, or currencies.

Section 851(b)(3)(A) requires that, to qualify as a RIC, at the close of each quarter of the taxable year, at least 50 percent of the value of a corporation's total assets must be represented by cash and cash items (including receivables), Government securities, securities of other RICs, and other securities generally limited in respect of one issuer to an amount not greater in value than 5 percent of the value of the total assets of the corporation and to not more than 10 percent of the outstanding voting securities of such issuer.

Section 851(b)(3)(B) provides that, to qualify as a RIC, not more than 25 percent of the corporation's total assets may be invested in the securities (other than Government securities and securities of other RICs) of any one issuer, or of two or more issuers that the corporation controls and which are determined, under regulations, to be engaged in the same or similar trades or businesses or related trades or businesses.

Section 852(b)(5) provides that a RIC at least 50 percent of the value (as defined in § 851(c)(4)) of whose total assets at the close of each calendar quarter consists of obligations described in § 103(a) is eligible to pay exempt-interest dividends, which are treated by the RIC’s shareholders as interest excludable from gross income pursuant to § 103(a).

Section 853(a) provides that a RIC more than 50 percent of the value (as defined in § 851(c)(4)) of whose total assets at the close of the taxable year consists of stock or securities in foreign corporations and which meets the requirements of § 852(a) for the taxable year may elect to treat its shareholders as if they had paid certain foreign taxes incurred by the RIC for purposes of determining a shareholder’s foreign tax credit under § 901.

Section 854(b)(1)(A) provides that a dividend, other than a capital gain dividend, received from a RIC qualifies for the dividends received deduction under § 243(a) to the extent so designated by the RIC provided that the RIC meets the requirements of § 852(a) for the taxable year during which it paid the dividend.

Section 854(b)(1)(B) provides that the aggregate amount that may be designated as dividends under § 854(b)(1)(A) shall not exceed the aggregate dividends received by the RIC for the taxable year.

Section 854(b)(3)(A) provides that the term "aggregate dividends received" includes only dividends received from domestic corporations.

Section 854(b)(4) provides, in part, that for purposes of determining an amount to be treated as a dividend eligible for the dividends received deduction under § 243 of the Code a payment to a RIC shall not be treated as a dividend unless, had it not been a RIC, it would have been allowed a dividends received deduction under § 243 with respect to the payment.

Section 702(b) provides that the character of items stated in § 702(a) that are included in a partner's distributive share shall be determined as if such items were realized directly from the source from which realized by the partnership, or incurred in the same manner as incurred by the partnership. Section 702(c) provides that where it is necessary to determine the amount or character of the gross income of a partner, such amount shall include his distributive share of the gross income of the partnership.

Section 1006(n)(1) of the Technical and Miscellaneous Revenue Act of 1988 added a sentence to the flush language of § 851(b) of the Code that states that income derived from a partnership or trust shall be treated as satisfying the 90 percent test of § 851(b)(2) only to the extent that such income is attributable to items of income of the partnership or trust which would be described in § 851(b)(2) if earned directly by the RIC. The legislative history of that sentence indicates that it was intended to clarify the general rule used to characterize items of income, gain, loss, deduction, or credit includible in a partner's distributive share, as applied to RICs that are partners. It therefore explains the relationship of § 702 to the 90 percent test under § 851(b)(2). See S. Rep. No. 445, 100th Cong., 2d Sess. 78 (1988).

Under subchapter K of the Code, a partnership is considered to be either an aggregate of its members or a separate entity. Under the aggregate approach, each partner is treated as an owner of an undivided interest in partnership assets and operations. The entity theory provides that the partnership is a separate entity in which partners have no direct interest in partnership assets and operations. See S. Rep. No. 1622, 83d Cong., 2d Sess. 89 (1954) and H.R. Rep. No. 2543, 83d Cong., 2d Sess. 59 (1954).

In order for the Funds to qualify as RICs under the diversification tests of § 851, the aggregate approach will have to be applied to each Fund’s partnership interest in Trust. As an aggregate, each Fund will be able to take into account its share of the individual items of income and assets of Trust.

Rev. Rul. 75-62, 1975-1 C.B. 188, concerns a life insurance company that contributed cash to a partnership in exchange for a 50 percent interest in the partnership. The partnership held real estate as its principal asset. For the taxable year in question, § 805(b) required life insurance companies to value their assets each taxable year. For this purpose, § 805(b)(4) required that shares of stock and real estate be valued at their fair market values, and that other assets be valued at their adjusted basis. The issue presented in the ruling is whether, for purposes of § 805(b)(4), the life insurance company's interest in the partnership is considered to be an investment in the real estate held by the partnership (an aggregate approach), or an investment in other property (an entity approach).

Rev. Rul. 75-62, holds that the partnership interest held by the life insurance company must be accounted for as other property for purposes of § 805(b)(4). The ruling cites §§ 705 and 741 of the Code, both of which generally treat an interest in a partnership as an interest in an entity, as evidence of an intent in subchapter K to take the entity approach in questions concerning the nature of an interest in a partnership. The ruling states that the legislative history of § 805(b)(4) does not indicate that application of the entity approach to the facts of the ruling is inappropriate and that there is no compelling reason to take the aggregate approach.

The flush language of § 851(b)(3) of the Code (formerly § 851(b)(4) for taxable years of a RIC that began before August 5, 1997) and its legislative history indicate that here, unlike the situation described in Rev. Rul. 75-62, Congress intended that an aggregate approach be taken in determining the nature of the partnership interests held by the Funds. The flush language of § 851(b) mandates an aggregate approach in applying the 90 percent gross income test of § 851(b)(2) to RICs that hold partnership interests. It would be anomalous to suggest that Congress intended that a RIC's interest in a partnership be viewed as a direct investment in the partnership's assets for purposes of the § 851(b)(2) test but not be viewed as a direct investment in those assets for purposes of the tests set out in, _inter alia_, § 851(b)(3).

The tax treatment accorded real estate investment trusts (REITs) lends further support to applying the aggregate approach to the present case. REITs were created to provide an investment vehicle similar to the RIC for small investors to invest in real estate and real estate mortgages. _See_ H.R. Rep. No. 2020, 86th Cong., 2d Sess. 3-4, (1960). Like RICs, REITs are subject to restrictions on the type of assets they can hold if they want to retain the benefits accorded them under subchapter M. For example, under § 856(c)(3) of the Code, at least 75 percent of the gross income of a REIT must be derived from any or all of nine sources, including rents from real property, interest on obligations secured by mortgages, gain from the sale or disposition of real property, and income and gain derived from foreclosure property. REITs and RICs also have similar distribution and holding period requirements.

Section 1.856-3(g) of the regulations provides that:

> In the case of a real estate investment trust which is a partner in a partnership, as defined in § 7701(a)(2) and the regulations thereunder, the trust will be deemed to own its proportionate share of each of the assets of the partnership and will be deemed to be entitled to the income of the partnership attributable to such share. For purposes of § 856, the interest of a partner in a partnership's assets shall be determined in accordance with his capital interest in the partnership. The character of the various assets in the hands of the partnership and items of gross income of

> the partnership shall retain the same character in the hands of the partners for all purposes of § 856. Thus, for example, if a trust owns a 30 percent capital interest in a partnership which owns a piece of rental property, the trust will be treated as owning 30 percent of such property being entitled to 30 percent of the rent derived from the property by the partnership. Similarly, if the partnership holds any property primarily for sale to customers in the ordinary course of its trade or business, the trust will be treated as holding its proportionate share of such property primarily for such purpose. Also, for example, where a partnership sells real property or a trust sells its interest in a partnership which owns real property, any gross income realized from such sale, to the extent that it is attributable to the real property, shall be deemed gross income from the sale or disposition of real property held for either the period that the partnership has held the real property or the period that the trust was a member of the partnership, whichever is shorter.

Thus, the regulations adopt the language of the aggregate "look-through" approach in determining how a REIT should account for its partnership interests for purposes of all of the income and asset qualification tests under § 856 of the Code.

The legislative purpose underlying the creation of both RICs and REITs was to provide small investors a means of pooling their resources to invest in a particular type of assets without the imposition of the corporate income tax. The qualification tests are similar for each. Therefore, although the RIC regulations do not specifically address the issue herein, it is appropriate to adopt an approach for RICs that parallels that set forth for REITs.

Ruling 3:

Section 721(a) of the Code provides that no gain or loss is recognized to a partnership or any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership.

Section 721(b) provides, however, that § 721(a) does not apply to gain realized on a transfer of property to a partnership that would be treated as an investment company (within the meaning of § 351) if the partnership were incorporated.

Section 351 states that no gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock in such corporation and immediately after the exchange such person or persons are in control (as defined in § 368(c)) of the corporation. Section 351 does not apply to a transfer of property to an investment company. Section 351(e)(1).

Section 1.351-1(c)(1) of the regulations states that a transfer to an investment company will occur when (i) the transfer results, directly or indirectly, in diversification of the transferors' interests and (ii) the transferee is a RIC, REIT, or a corporation more than 80-percent of the value of whose assets (excluding cash and non-convertible debt obligations from consideration) are held for investment and are readily marketable stocks or securities, or interests in RICs or REITs.

Section 1002 of the Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 (1997) (the "Act"), amends § 351(e) for transfers after June 8, 1997, in taxable years ending after such date, subject to certain transitional relief provisions. Section 1002 of the Act is intended to expand the types of assets considered in determining whether a transfer is to a transferee described in § 1.351-1(c)(1)(ii)(c) to include certain assets in addition to "readily marketable stocks or securities" and interests in RICs and REITs. However, the Act is not intended to alter the requirement of § 1.351-1(c)(1)(i) that a transfer of property will be considered to be a transfer to an investment company under § 351(e) only if the transfer results, directly or indirectly, in diversification of the transferors' interests. *See* S. Rep. 105-33, 105th Cong., 1st Sess. 131 (1997); H. R. Rep. 105-148, 105th Cong., 1st Sess. 447 (1997); H. R. Rep. 105-220, 105th Cong., 1st Sess. 516-17 (1997).

Section 1.351-1(c)(5) provides that a transfer ordinarily results in diversification of the transferors' interests if two or more persons transfer nonidentical assets to a corporation in the exchange. It further provides that, if a transfer is part of a plan to achieve diversification without recognition of gain, such as a plan which contemplates a subsequent transfer, however delayed, of the corporate assets (or of the stock or securities received in the earlier exchange) to an investment company in a transaction purporting to qualify for nonrecognition treatment, the original transfer will be treated as resulting in diversification. Section 1.351-1(c)(6)(i) provides that (i) a transfer of stocks and securities will not be treated as resulting in a diversification of the transferors' interests if each transferor transfers a diversified portfolio of stocks and securities and (ii) a portfolio of stocks and securities is considered to be diversified if it satisfies the 25 and 50-percent tests of § 368(a)(2)(F)(ii), applying the relevant provisions of § 368(a)(2)(F), except that government securities are included in total assets for purposes of the denominator of the 25 and 50-percent tests (unless acquired to meet the 25 and 50-percent tests), but are not treated as securities of an issuer for purposes of the numerator of the 25 and 50-percent tests.

A corporation is diversified within the meaning of § 368(a)(2)(F)(ii) if not more than 25 percent of the value of its total assets is invested in the stock and securities of any one issuer and not more than 50 percent of the value of its total assets is invested in the stock and securities of 5 or fewer issuers.

Ruling 4:

Section 704(c)(1)(A) of the Code provides that under regulations prescribed by the Secretary income, gain, loss, and deduction with respect to property contributed to the partnership by a partner shall be shared among the partners so as to take account of the variation between the basis of the property to the partnership and its fair market value at the time of contribution.

Section 1.704-3(a)(1) of the regulations provides that the purpose of § 704(c) is to prevent the shifting of tax consequences among partners with respect to pre-contribution gain or loss. Under § 704(c), a partnership must allocate income, gain, loss, and deductions with respect to property contributed by a partner to the partnership so as to take into account any variation between the adjusted tax basis of the property and its fair market value at the time of contribution. Notwithstanding any other provision of § 1.704-3, the allocations must be made using a reasonable method that is consistent with the purpose of § 704(c).

Section 1.704-3(a)(6) of the regulations provides that the principles of § 1.704-3 apply to allocations with respect to property for which differences between book value and adjusted tax basis are created when a partnership revalues partnership property pursuant to § 1.704-1(b)(2)(iv)(f) (reverse § 704(c) allocations). A partnership that makes allocations with respect to revalued property must use a reasonable method that is consistent with the purposes of § 704(b) and (c).

Section 704(c) generally applies on a property-by-property basis. Section 1.704-3(a)(2). Therefore, in determining whether there is a disparity between adjusted tax basis and fair market value, the built-in gains and built-in losses on items of contributed or revalued property generally cannot be aggregated.

Section 1.704-3(e)(3) sets forth a special rule allowing certain securities partnerships to make reverse § 704(c) allocations on an aggregate basis. Specifically, § 1.704-3(e)(3)(i) provides that, for purposes of making reverse § 704(c) allocations, a securities partnership may aggregate gains and losses from qualified financial assets using any reasonable approach that is consistent with the purpose of § 704(c). Once a partnership adopts an aggregate approach, the partnership must apply the same aggregate approach to all of its qualified financial assets for all taxable years in which the partnership qualifies as a securities partnership.

Section 1.704-3(e)(3)(iii)(A) of the regulations provides that a partnership is a securities partnership if the partnership is either a management company or an investment partnership, and the partnership makes all of its book allocations in proportion to the partners' relative book capital accounts (except for reasonable special allocations to a partner that provides management services or investment advisory services to the partnership). Under § 1.704-3(e)(3)(iii)(B)(1), a partnership is a management company if it is registered as a management company under the 1940 Act.

Section 1.704-3(e)(3)(ii) provides that a qualified financial asset is any personal property (including stock) that is actively traded as defined in § 1.1092(d)-1. For a management company, qualified financial assets also include the following, even if not actively traded: shares of stock in a corporation; notes, bonds, debentures, or other evidences of indebtedness; interest rate, currency, or equity notional principal contracts; evidences of an interest in, or derivative financial instruments in, any security, currency, or commodity, including any option, forward or futures contract, or short position; or any similar financial instrument.

Section 1.704-3(e)(3) only applies to reverse § 704(c) allocations; thus, a securities partnership using an aggregate approach must generally account for any built-in gain or loss from contributed property separately. The preamble to § 1.704-3(e)(3) explains that the final regulations do not authorize aggregation of built-in gains and losses from contributed property with built-in gains and losses from revaluations because this type of aggregation can lead to substantial distortions in the character and timing of income and loss recognized by contributing partners. T.D. 8585, 1995-1 C.B. 120, 123. However, the preamble also recognizes that there may be instances in which the likelihood of character and timing distortions is minimal and the burden of making § 704(c) allocations is great. *Id*. Consequently, § 1.704-3(e)(4)(iii) authorizes the Commissioner to permit, by published guidance or by letter ruling, aggregation of qualified financial assets for purposes of making § 704(c) allocations in the same manner as that described in § 1.704-3(e)(3).

In this case, Trust's burden of making § 704(c) allocations separate from reverse § 704(c) allocations is substantial. While the assets of Trust will be purchased and sold in conformity with its investment objectives and policies, it is impossible to predict which particular assets will be purchased or sold or when such a purchase or sale will occur, since Trust will be managed in response to changing market conditions. The recognition and/or allocation of built-in gain or loss on contributed property cannot be predicted. Further, due to the large volume of securities held and the related transactions, tracking the contributed built-in gains and losses on an asset-by-asset basis and on a partner-by-partner basis would be a significant cost burden and would largely nullify the economic benefits otherwise anticipated in a master/feeder structure.

HOLDINGS

Based upon the facts presented and the representations made by the taxpayer, we rule as follows:

1. Trust will not be a publicly traded partnership under § 7704 of the Code.

2. In accordance with the relationships detailed above, Fund A and Fund B, as partners in Trust, will be deemed to own a proportionate share of the assets of Trust and will be deemed to be entitled to the income of Trust attributable to that share for purposes of determining whether Fund A and Fund B each satisfies the requirements of §§ 851(b)(2), 851(b)(3), 852(b)(5), 853(a), and 854 of the Code. For purposes of these sections, the interest of Fund A and Fund B in Trust shall be determined in accordance with Fund A’s and Fund B’s capital interest in Trust

3. Provided Trust is treated as a partnership for purposes of § 721:

   The transfers by Fund A, Fund B, and Company B to Trust are not transfers of property to a partnership that would be treated as an investment company (within the meaning of § 351) if Trust were incorporated, provided that these are the only transfers to Trust (except for transfers solely of cash and/or a diversified portfolio of stocks and securities, within the meaning of § 1.351-1(c)(6)(i) of the regulations).

   Contributions solely of cash and/or a diversified portfolio of stocks and securities (within the meaning of § 1.351-1(c)(6)(i)) to Trust by new funds, will not cause the initial transfers by the Funds or Company B to be treated as a transfer of property to a partnership (*i.e.*, Trust) that would be treated as an investment company within the meaning of § 351 if the partnership were incorporated.

4. Trust may aggregate built-in gains and losses from qualified financial assets contributed to it by the Funds with built-in gains and losses from revaluations of qualified financial assets held by Trust for purposes of making § 704(c)(1)(A) and reverse § 704(c) allocations. Trust’s method of making § 704(c)(1)(A) and reverse § 704(c) allocations is reasonable within the meaning of § 1.704-3(e)(3), and is a method which is permitted by the Commissioner under § 1.704-3(e)(4)(iii).

   We further conclude that Trust may aggregate built-in gains and losses from qualified financial assets contributed by future partners with built-in gains and losses from revaluations of qualified financial assets held by Trust for purposes of making § 704(c)(1)(A) and reverse § 704(c) allocations, and that Trust’s method of making these allocations is reasonable within the meaning of § 1.704-3(e)(3), and is a method which is permitted by the Commissioner under § 1.704-3(e)(4)(iii), to the extent that the future partners are "qualified contributors." A qualified contributor is a partner for which the following conditions are satisfied: (1) the partner is registered under the Investment Company Act of 1940, as amended, and would be considered a "publicly offered regulated investment company" as defined in § 67(c)(2)(B) and § 1.67-2T(2)(g)(3)(ii); the contribution is made and accepted for valid business purposes and not made primarily for tax-motivated reasons (other than the fact that the contribution to Trust is tax-free); and (3) to the extent Trust relies on this ruling for the contribution, it will document any such contribution on its tax return filed subsequent to the contribution.

This ruling is limited to Fund A, Fund B, and Trust. No opinion is expressed with respect to the federal income tax consequences of this transaction other than as concluded above. Specifically, no opinion is expressed as to whether Fund A or Fund B qualifies as a RIC that is taxable under subchapter M, part I of the Code. Moreover, we express no opinion on the propriety of any of the rulings herein with respect to the contribution and subsequent admission of additional partners in Trust which are not specifically included in any representation given by the taxpayer. Additionally, we express no opinion as to whether the transaction involving the transfers from the Funds and Company B is part of a plan to achieve diversification without recognition of gain under § 1.351-1(c)(5). Furthermore, we express no opinion as to the consequences of other transfers to Trust, either as to whether such other transfers would be "transfers to an investment company" or whether such other transfers would, when taken together with the transfers by the Funds and Company B, cause those transfers to be considered "transfers to an investment company," except for transfers solely of cash and/or a diversified portfolio of stocks and securities.

Temporary or final regulations pertaining to one or more of the issues addressed in this ruling letter have not yet been adopted. Therefore, this ruling will be modified or revoked if adopted temporary or final regulations are inconsistent with any conclusions in the ruling. *See* § 12.04 of Rev. Proc. 2000-1, 2000-1 I.R.B. 4, 46 (January 3, 2000). However, when the criteria in § 12.05 of Rev. Proc. 2000-1 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

In accordance with the provisions of a Power of Attorney currently on file, we are sending a copy of this ruling letter to your authorized representative.

A copy of this letter should be attached to the federal income tax return for Fund A and Fund B for every taxable year in which it participates in the arrangement described in this letter.

Sincerely yours,
Acting Associate Chief Counsel
(Financial Institutions and Products)

By: ______________________
Alice M. Bennett
Chief, Branch 3

Enclosures:
Copy of this letter
Copy for section 6110 purposes