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Person To Contact:
, ID No.

Telephone Number:

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Date:
June 01, 2007

LEGEND

Husband =
Trust =

Date 1 =
State =
Wife =
Foundation =
Date 2 =
Trust A =
Trust B =
State Statute =

Dear :

This is in response to your authorized representative's letter dated August 3, 2006, in which you requested rulings regarding a proposed division of a charitable remainder unitrust.

The information presented and representations made are as follows: Husband created Trust, a charitable remainder unitrust within the meaning of § 664(d)(2) of the Internal Revenue Code, on Date 1. Trust is irrevocable and governed by the laws of State.

Article II of Trust provides generally that in each taxable year of the trust, the trustee shall pay a unitrust amount to Husband during his lifetime, and after his death to Wife for such time as she survives. Upon the death of the survivor of Husband and Wife, the trustee shall distribute all of the then remaining principal and income of Trust to Foundation, an organization described in §§ 170(c), 2055(a), and 2522(a). Husband reserves the right to at any time designate or appoint one or more organizations described in §§ 170(c), 2055(a), and 2522(a) as the charitable remainderman in lieu of Foundation.

Article II, Section 2.01(B) provides that for each taxable year that begins on or before the sale of unmarketable trust property, the unitrust amount shall be the lesser of the trust income for the taxable year, and nine percent of the initial net fair market value of the trust assets, valued as of the valuation date. For each taxable year that begins after the sale of unmarketable trust property, the unitrust amount shall be equal to nine percent of the net fair market value of the trust assets, valued as of the valuation date.

Husband and Wife are legally separated and in the process of obtaining a divorce. On Date 2, Husband and Wife entered into a marriage separation agreement (the "MSA") to settle their marital and property rights. The MSA provides that Trust shall be divided into two separate and equal trusts, known as Trust A and Trust B. Each trust is intended to qualify as a charitable remainder unitrust under § 664(d)(2). As proposed, the assets of Trust will be divided equally in kind between Trust A and Trust B.

Trust A and Trust B will be identical to Trust except that (i) Husband will be the unitrust beneficiary of Trust A and Wife will be the unitrust beneficiary of Trust B; (ii) each spouse will retain a survivorship interest in the other's unitrust amount; (iii) Husband will have the right to designate the charitable remainder beneficiaries of Trust A and Wife will have the right to designate the charitable remainder beneficiaries of Trust B; (iv) the surviving spouse will not be permitted to appoint or change the charitable remainder beneficiaries of the other spouse's new trust; (v) Husband will be the trustee of Trust A and Wife will be the trustee of Trust B; (vi) the subsections of Article II, Section 2.01 of Trust relating to the definition of the unitrust amount prior to the sale of unmarketable trust property will be deleted because Trust has sold such property and those provisions are no longer applicable; (vii) Trust A will provide that no one other than Husband may make additional contributions to Trust A; and (viii) Trust B will provide that no one other than Wife may make additional contributions to Trust B.

Pursuant to State Statute, the trustee of Trust has tentatively approved the division of Trust into Trust A and Trust B. However, the final dissolution of Trust and its division into Trust A and Trust B is contingent upon a favorable private letter ruling.

Based on the foregoing, the trustee requests the following rulings:

1. The division of Trust into Trust A and Trust B will not cause Trust, Trust A or Trust B to fail to qualify as a charitable remainder unitrust under § 664(d)(2);

2. No gain or loss will be recognized by Husband or Wife on the transfer by Husband of his one-half unitrust interest in Trust to Wife, and Wife will receive that interest with a carryover basis from Husband;

3. No gain or loss will be recognized by Trust, Trust A or Trust B on the division of Trust into Trust A and Trust B;

4. Trust A and Trust B will determine their basis in the assets by reference to the basis of the assets in the hands of Trust under § 1015(a) or (b), and the holding periods of the assets held by Trust A and Trust B will include the period that assets were held by Trust;

5. To the extent the division of Trust into Trust A and Trust B results in transfers of property between Husband and Wife, the transfers will not be subject to gift tax by application of the provisions of § 2516;

6. The proposed transfers of Trust's assets will not terminate Trust's status as a private foundation or result in the imposition of taxes under § 507;

7. The proposed transfers of Trust's assets will not result in an act of self dealing under § 4941; and

8. The proposed transfers of Trust's assets will not be a taxable expenditure under § 4945.

RULING 1

Section 664(d)(2) provides that a charitable remainder unitrust is a trust (A) from which a fixed percentage (which is not less than 5 percent nor more than 50 percent) of the net fair market value of its assets, valued annually, is to be paid, not less often than annually, to one or more persons (at least one of which is not an organization described in § 170(c) and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals, (B) from which no amount other than the payments described in § 664(d)(2)(A) and other than qualified gratuitous transfers described in § 664(d)(2)(C) may be paid to or for the use of any person other than an organization described in § 170(c), (C) following the termination of the payments described in § 664(d)(2)(A), the remainder interest in the trust is to be transferred to, or for the use of, an organization described in § 170(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as

defined in § 664(g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (as defined in § 4975(e)(7)) in a qualified gratuitous transfer (as defined by § 664(g)), and (D) with respect to each contribution of property to the trust, the value (determined under § 7520) of such remainder interest in such property is at least 10 percent of the net fair market value of such property as of the date such property is contributed to the trust.

Section 1.664-1(a)(4) of the Income Tax Regulations provides, in part, that in order for a trust to be a charitable remainder trust, it must meet the definition of and function exclusively as a charitable remainder trust from the creation of the trust.

Based on the information provided and the representations made, the division of Trust into two separate trusts will not cause Trust, Trust A or Trust B to fail to qualify as a charitable remainder unitrust under § 664.

RULINGS 2 and 3

Under § 61(a)(3), gross income includes gains derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property is the excess of the amount realized over the adjusted basis provided in § 1011 for determining gain, and the loss is the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized. Under § 1001(c), the entire amount of gain or loss must be recognized, except as otherwise provided.

Section 1.1001-1(a) provides that except as otherwise provided in subtitle A of the Code, the gain or loss realized from the exchange of property for other property differing materially either in kind or in extent, is treated as income or as loss sustained.

An exchange of property results in the realization of gain or loss under § 1001 if the properties exchanged are materially different. Cottage Savings Ass'n v. Commissioner, 499 U.S. 554 (1991). Properties exchanged are materially different if the properties embody legal entitlements "different in kind or extent" or if the properties confer "different rights and powers." Id. at 565. In Cottage Savings, 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. Id. at 566. 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. Id. at 564-65.

Section 1041 provides that no gain or loss will be recognized on a transfer of property from an individual to (or in trust for the benefit of) a spouse, or former spouse if the transfer is incident to the divorce. Under § 1041(b), for purposes of subtitle A, the

transferee is treated as having acquired the property by gift from the transferor with a carryover basis from the transferor. Pursuant to § 1041(c) a transfer of property is incident to the divorce if the transfer occurs within one year after the date on which the marriage ceases, or is related to the cessation of the marriage.

Section 1.1041-1T(b), Q&A-7 of the Temporary Income Tax Regulations provides that a transfer of property is "related to the cessation of the marriage" if the transfer is pursuant to a divorce or separation instrument, as defined by § 71(b)(2), and the transfer occurs not more than six years after the date on which the marriage ceases. A divorce or separation instrument includes a modification or amendment to such decree or instrument.

Section 1041 was added to the Code by § 421 of the Tax Reform Act of 1984 (1984 Act), Pub. L. No. 98-369. The House Report accompanying the 1984 Act expresses the intent of Congress behind § 1041:

> The bill provides that the transfer of property to a spouse incident to a divorce will be treated, for income tax purposes, in the same manner as a gift. Gain (including recapture income) or loss will not be recognized to the transferor, and the transferee will receive the property at the transferor's basis … Thus, uniform Federal income tax consequences will apply to these transfers notwithstanding that the property may be subject to differing state property laws.

H.R. Rep. No. 432, 98th Cong., 2d Sess., Part 2, at 1491-92 (1984) (House Report)

Concerning transfers of annuities between spouses and beneficial interests in trusts, the above legislative history specifically states: "Where an annuity is transferred, or a beneficial interest in a trust is transferred or created, incident to a divorce or separation, the transferee will be entitled to the usual annuity treatment, including recovery of the transferor's investment in the contract (under § 72), or the usual treatment as the beneficiary of a trust (by reason of § 682)…" Id.

We note that for purposes of subtitle A, § 1041(a) provides a broad rule of nonrecognition of gain or loss for any transfer of property between present spouses and between divorcing spouses if the transfer is incident to divorce. In our view, a broad application of § 1041 is consistent with the language and the above statement of Congressional intent.

In this case, Husband currently receives annual trust payments equal to a nine percent unitrust amount. Wife has no present interest in either the income or corpus of Trust. Trust will be divided into two equal charitable remainder unitrusts, Trust A and Trust B, each of which will hold fifty percent of the corpus of Trust. Husband and Wife

will each receive payments equal to a nine percent unitrust amount determined only from the fifty percent of the assets held in his or her respective trust. Wife's interest becomes immediate and possessory in the unitrust amount from Trust B. As a result of the partition of Trust, Husband's interest declines significantly and Wife's interest is significantly increased. Husband in essence is transferring half of his interest in Trust to Wife.

For purposes of § 1001 and § 1.1001-1(a), the legal rights and entitlements enjoyed by Husband and Wife in Trust before divorce are materially different in kind and extent from the legal rights and entitlement enjoyed by each of them after divorce and the division of Trust. However, even though their respective rights and legal entitlements in trust become materially different in kind or extent under the Cottage Savings test and thus would otherwise constitute a taxable event under § 1001 to the spouses, because the MSA is a divorce or separation instrument within the meaning of § 71(b)(2), the division of Trust pursuant to the MSA results in a property transfer between spouses or former spouses incident to divorce. Consequently, § 1041 applies at the spousal level. We therefore conclude that no gain or loss will be recognized by Husband or Wife on the transfer of one-half of Husband's interest in Trust to Wife, and Wife receives that interest with a carryover basis from Husband under § 1041(b).

As stated above, recognized gains or losses are included in gross income under §§ 61(a)(3) and 1001. At the trust level, to the extent the division of Trust into Trust A and Trust B results in a transfer of property from one trust to the other, such transfer of property is not between spouses or former spouses. Therefore, § 1041 would not be applicable at the trust level. However, pursuant to § 664(c) a charitable remainder unitrust is exempt from federal income tax. Because the division of Trust into Trust A and Trust B will not cause Trust, Trust A or Trust B to fail to qualify as a charitable remainder unitrust under § 664(d)(2), then the tax-exempt status of Trust, Trust A and Trust B will preclude any of the trusts from recognizing any gain or loss in this case.

RULING 4

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 the property was held by any other person, if under Chapter 1 of the Code such property has, for the purposes of determining gain or loss from a sale or exchange, the same basis in whole or in part in the taxpayer's hands as it would have in the hands of such other person.

Section 1015 provides that the basis in property acquired by a transfer in trust is the same as it would be in the hands of the grantor, with adjustments for gain and loss recognized.

Based on the foregoing, we conclude that the basis and holding period of the assets in Trust A and Trust B will be the same as they were immediately before the division of Trust into Trust A and Trust B.

RULING 5

Section 2501(a) imposes a gift tax for each calendar year on the transfer of property by gift during the calendar year.

Section 2511 provides that the gift tax shall apply 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 2512(b) provides that where property is transferred for less than an adequate and full consideration in money or money's worth, the amount by which the value of the property exceeded the value of the consideration shall be deemed a gift.

Section 2516 provides that where a husband and wife enter into a written agreement relative to their marital and property rights and divorce occurs within the three year period beginning on the date one year before such agreement is entered into (whether or not such agreement is approved by the divorce decree), any transfers of property interests in property made pursuant to such agreement (1) to either spouse in settlement of his or her marital or property rights, or (2) to provide a reasonable allowance for the support of issue of the marriage during minority, shall be deemed to be transfers made for a full and adequate consideration in money or money's worth.

In this case, Husband and Wife entered into the MSA on Date 2. Provided that Husband and Wife's divorce becomes final within the three year period beginning on the date one year before Date 2, the division of Trust into Trust A and Trust B and the transfer of property interests in Trust to Trust A and Trust B made pursuant to the MSA will be deemed to be transfers made for full and adequate consideration in money or money's worth and, therefore, will not be subject to gift tax.

RULINGS 6, 7 and 8

Section 507(a) provides that, except as provided in § 507(b), a private foundation may terminate its private foundation status only under the specific rules set forth in § 507(a).

Section 507(b)(2) provides that in the case of a transfer of assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization, the transferee foundation shall not be treated as a newly created organization.

Section 507(c) imposes an excise tax on any private foundation that voluntarily terminates its private foundation status under § 507(a)(1).

Section 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute a termination of the transferor's private foundation status under § 507(a)(1).

Section 1.507-3(c)(1) provides, in pertinent part, that as used in § 507(b)(2) the term "other adjustment, organization or reorganization" shall include any partial liquidation or any other "significant disposition of assets" to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income.

Section 1.507-3(c)(2)(ii) provides that the term "significant disposition of assets" means the transfer of 25 percent or more of the net assets of the foundation at the beginning of the year, which disposition may be made in a single year or in a series of related dispositions over more than one year.

Section 1.507-3(a)(3) provides, in general, that in the event of a transfer of assets described in § 507(b)(2), any person who is a substantial contributor (within the meaning of § 507(d)(2)) with respect to the transferor foundation shall be treated as a substantial contributor with respect to the transferee foundation.

Section 1.507-3(b)(6) provides that if a private foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2), such transferor foundation will not have terminated its private foundation status under §507(a)(1).

Section 1.507-3(a)(1) and (2)(i) provides in substance that in the transfer of assets from one private foundation to one or more private foundations in a § 507(b)(2) transfer, each transferee private foundation shall not be treated as a newly created organization, but shall succeed to the transferor's aggregate tax benefit within the meaning of § 507(d) in proportion to the assets transferred to each.

Section 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations that are effectively controlled, directly or indirectly, by the same person or persons that effectively controlled the transferor foundation, such transferee private foundation shall be treated as if it were the transferor private foundation for purposes of §§ 4940 through 4948 and §§ 507 through 509.

Section 1.507-3(b) provides, in pertinent part, that a transfer of assets pursuant to any liquidations, merger, redemption, recapitalization, or other adjustment,

organization or reorganization to an organization that is described in § 4947 is not a taxable expenditure under § 4945(d).

Section 4941(a) imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation.

Section 4941(d)(1)(E) provides that the term "self dealing" means any direct or indirect transfer to, or for the use by or for the benefit of, a disqualified person of the income or assets of a private foundation.

Section 4945 imposes an excise tax on a private foundation's making of any taxable expenditure under § 4945(d).

Section 53.4945-6(b)(2) of the Foundation and Similar Excise Taxes Regulations provides that expenditures for unreasonable administrative expenses, including compensation, consultant fees, and other fees for services rendered, will ordinarily be taxable expenditures under § 4945(d)(5) unless the foundation can demonstrate that such expenses were paid in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence.

Section 4946(a) provides the term "disqualified person" with respect to a private foundation includes a substantial contributor to the foundation (including the creator of a trust), the foundation manager (including a trustee) and the members of the family of those individuals.

Section 53.4947-1(c)(1)(ii) provides that a split-interest trust is subject to the provisions of §§ 507 (except as provided in § 53.4947-1(e)), 508(e) to the extent applicable to a split-interest trust), 4941, 4943 (except as provided in § 4947(b)(3)), 4944 (except as provided in § 4947(b)(3)), and 4945 in the same manner as if such trust were a private foundation.

Section 53.4947-1(c)(2)(i) provides, in general, that under § 4947(a)(2)(A), section 4941 does not apply to any amounts payable under the terms of a split interest trust to income beneficiaries unless a deduction was allowed under §§ 170(f)(2)(B), 2055(e)(2)(B) or 2522(e)(2)(B) with respect to the income interest of any such beneficiary.

As a split interest trust, Trust is created as if it were a private foundation. Thus, except as provided in § 53.4947-1(c)(2)(i), it is subject to §§ 507, 4941, and 4945.

The proposed transfers of all of Trust’s assets to Trust A and Trust B will constitute a significant disposition of Trust’s assets. The proposed transfers will not be

for full and adequate consideration and will not be distributions out of current income. Thus, the proposed transfers will be § 507(b)(2) transfers.

A transfer of assets described in § 507(b)(2) does not constitute a termination of the transferor's private foundation status under § 507(a)(1) unless the transferor voluntarily gives notice pursuant to § 507(a)(1). Since Trust has not given notice of its intent to terminate, it will retain its private foundation status and the tax imposed by § 507(c) will not apply.

Since Trust A and Trust B will be treated as if they were Trust for purposes of § 4941, transfers between Trust and Trust A and Trust B will not be acts of self-dealing.

Assuming no deduction was allowed, payments to the unitrust beneficiaries named will not be acts of self-dealing under § 4941. See § 53.4947-1(c)(2)(i).

A transfer of assets pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, reorganization to an organization that is described in § 4947 is not a taxable expenditure under § 4945(d). Accordingly, Trust's proposed transfer of all of its assets to Trust A and Trust B will not be a taxable expenditure.

Section 53.4945-6(b)(2) provides that expenditures for unreasonable administrative expenses, including compensation, consultant fees, and other fees for services rendered will ordinarily be taxable expenditures under § 4945(d)(5) unless the foundation can demonstrate that such expenses were paid or incurred in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence. Trust represents that the fees related to the proposed transfer of assets will be reasonable and will be consistent with ordinary business care and prudence.

Based solely on the representations made and the information submitted, we conclude that the proposed transfers of assets will not terminate Trust's status as a private foundation or result in the imposition of taxes under § 507. We further conclude that the proposed transfers of Trust's assets will not result in an act of self-dealing under § 4941 and will not be a taxable expenditure under § 4945.

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. Specifically, the Service is not ruling on the consequences under chapter 11 to Husband and Wife upon their respective deaths. In addition, we express no opinion as to whether Trust, Trust A, or Trust B qualify as charitable remainder trusts under § 664.

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, a copy of this letter is being sent to your authorized representatives.

Sincerely,

James F. Hogan
Senior Technician Reviewer, Branch 4
(Passthroughs & Special Industries)

Enclosure
Copy of letter for 6110 purposes