

INTERNAL REVENUE SERVICE

Number: **200102017**

Release Date: 1/12/2001

Index Number: 302.05-02

CC:CORP:1-PLR-107954-00

28 September 2000

Legend

Corporation =

State X =

Shareholder A =

Spouse =

Trust A =

Trustee A =

Trustee B =

Successor Trustees =

Shareholder A's =
Foundation

Children's =
Foundations

Dear :

This letter responds to a letter dated April 3, 2000, requesting rulings concerning the federal income tax consequences of a proposed transaction. A previous private letter ruling (TR-31-2494-93) issued to you with regard to § 2055 and 2056 of the Internal Revenue Code is unaffected by the present letter. The information submitted for consideration is summarized below.

Corporation, a State X corporation, uses the accrual method of accounting and a calendar year. Corporation has outstanding voting and nonvoting common stock. Over 50 percent of each type and class of stock is held by Shareholder A or by trusts for the

benefit of Shareholder A and trusts for the benefit of Shareholder A's children and grandchildren ("Children" and "Grandchildren"). Following Shareholder A's death, a significant portion of the stock in Corporation will be held by Trust A or marital trust ("Marital Trust") for the benefit of Spouse, the wife of Shareholder A, during her lifetime.

Trust A is a revocable trust for the benefit of Shareholder A. Following Shareholder A's death, Trust A becomes an irrevocable trust for the benefit of Spouse and, eventually, for the benefit of various foundations, a medical research organization, and/or various other charities. If Spouse were to predecease Shareholder A, then, at Shareholder A's death, the foundations and/or other charities would become the immediate beneficiaries of Trust A.

At present, Trust A has three trustees: Shareholder A, Spouse, and Trustee A. Shareholder A and Trustee A have each named successor trustees ("Successor Trustees"). Trustee A and all of the Successor Trustees are officers and/or directors of Corporation. Trustee A and all of his Successor Trustees are also Trustees or Successor Trustees of the trusts for the benefit of the Children and Grandchildren. Some of the ultimate beneficiaries of Trust A have already been named. However, with regard to part of the Trust A assets, the trustees have the power ("Asset Allocation Power") to choose who will be the recipients and how the assets will be allocated among foundations, charities, and medical research organizations.

Trust A has as beneficiaries five private foundations ("the Five Foundations"). The Five Foundations include "Shareholder A's Foundation" of which Shareholder A is an officer, director, and member and four "Children's Foundations" each of which has a child of Shareholder A as one of its officers, directors, and members.

Shareholder A intends that, following his death, control of Corporation remain with his family (or family trusts). He desires that none of the Corporation stock held by Trust A pass outside the family. Accordingly, the following steps (to be undertaken shortly after Shareholder A's death) are proposed:

- (I) Any stock (and warrants, options, convertible debentures and equity interests) in Corporation held by Estate will be distributed from Estate to Trust A.
- (II) Corporation will redeem for cash and/or notes or other obligations of Corporation all of the stock (and any warrants, options, convertible debentures and equity

interests) in Corporation held by Trust A.

The following representations have been made in connection with the redemption:

- (a) Corporation and Trust A will each pay their own expenses associated with the redemption.
- (b) Throughout the 10-year period immediately following the redemption: (i) the only persons having any beneficial interest in Trust A will be Spouse, Marital Trust, and the Five Foundations; and (ii) Trust A will have no beneficial interest in any entity holding, either directly or indirectly, any stock (or warrants, options, or equity interest) in Corporation, except that Trust A may have a beneficial interest in Estate.
- (c) Throughout the 10-year period immediately following the proposed redemption, neither Trust A, nor any of the persons holding a beneficial interest in Trust A, nor any person in which Trust A holds a beneficial interest (that is, Marital Trust, Spouse, the Five Foundations, and Estate) will hold, directly or indirectly (within the meaning of § 318), any stock, warrants, options, or equity interest in Corporation. The only exceptions to the preceding sentence are the possible holding of an indirect interest in Corporation by Spouse and/or Estate. The only interest in Corporation held by Spouse would be by attribution from her children or grandchildren under § 318(a)(1). The only interest in Corporation held by Estate would be by attribution from its beneficiaries under § 318(a)(3)(A).
- (d) Trust A and Spouse will each execute and file the agreement required by § 302(c)(2)(A)(iii) with respect to the acquisition of any interest in Corporation within 10 years from the date of the redemption.
- (e) Throughout the 10-year period immediately following the redemption, neither Trust A nor Spouse will have any interest in Corporation, including an interest as an officer, director, or employee (other than an interest as a creditor as described in § 1.302-4(d) of the Income Tax Regulations, and constructive ownership under § 318(a)(1) of the Code).
- (f) Throughout the 10-year period immediately following the redemption, neither Trust A, Estate, the Marital Trust, Spouse, or any of the Five Foundations will hold an economic interest in, or influence over, Corporation (except for creditor interests).

- (g) Throughout the 10-year period immediately following the proposed redemption, Trustee A and all other persons who are directors, officers, or employees of Corporation will act with regard to Corporation independently of any position they may have with Trust A or a related entity (including a position such as trustee, executor, or employee of Trust A, Shareholder A's Estate, the Marital Trust or any of the Five Foundations).
- (h) Throughout the 10-year period immediately prior to the proposed redemption, there will have been no transfers of Corporation stock (or warrants, options, convertible debentures, or any equity interests in Corporation) to or from Estate, Trust A, Marital Trust, Spouse, or any of the Five Foundations, except for the receipt by Estate and/or Trust A of Corporation Stock from Shareholder A on his death, and/or the receipt by Trust A of Corporation Stock from Estate. Any transfer of Corporation stock (or warrants, options, convertible debentures, or any equity interests in Corporation) from Estate to Trust A will be undertaken in the normal course of settling the estate and will not be undertaken with a purpose of avoiding federal income tax.
- (i) Each of the Five Foundations was recognized as exempt from federal income tax under § 501(c)(3) and classified as a private foundation under § 509(a). The Trust A assets will be distributed solely to charitable organizations described in **SS** 2055(a).
- (j) Throughout the 10-year period immediately following the redemption, none of the Children's Foundations will at any time cease to be a "private foundation" as described in § 509(a) or its successor, unless such foundation ceases to exist in conjunction with the transfer of its assets to a § 501(c)(3) charity.
- (k) Throughout the 10-year period immediately following the redemption, no person will hold both (i) a beneficial interest in any of the Five Foundations and (ii) stock (or warrants, options, convertible debentures or any equity interest) in Corporation (directly or indirectly under the attribution rules of § 318).
- (l) Throughout the 10-year period immediately following the redemption, none of any Corporation notes (or other obligations of Corporation) held by Trust A will constitute an equity interest in Corporation.
- (m) In no event will the last payment on any Corporation notes (or any other obligations of Corporation) received by Trust A be made more than 15 years after the date of

the obligation's issuance.

- (n) None of the consideration from Corporation, including interest, will consist entirely or partly of Corporation's promise to pay an amount that is based on, or contingent on, future earnings of Corporation, an amount that is contingent on working capital being maintained at a certain level, or any similar contingency.
- (o) Any Corporation note or other obligation to be issued to Trust A will not be subordinated to the claims of general creditors of Corporation.
- (p) In the event of default on any note or other obligation, no shares of stock in Corporation or any related corporation will revert to Trust A or Spouse or any related entity, nor will Trust A or Spouse or any related entity be permitted to purchase such stock at any public or private sale.
- (q) No shareholder of Corporation has been or will be obligated to purchase any of the stock to be redeemed.
- (r) None of the stock to be redeemed will be "section 306 stock" within the meaning of § 306(c).
- (s) There will be no declared but unpaid dividends, or funds set apart for dividends, on any of the stock to be redeemed.
- (t) At the time of the redemption, the amount of cash plus the fair market value of any Corporation notes or other obligations to be received from Corporation by Trust A will approximately equal the fair market value of the Corporation stock to be surrendered by Trust A in exchange therefor. The redemption price will be reached through arms-length bargaining between Corporation and Trust A.
- (u) Any note or other obligation of Corporation received by Trust A will be a debt and not an equity interest.
- (v) The terms of any notes or other obligations of Corporation received by Trust A will provide rights that will be no greater or broader in scope than necessary for enforcement of Trust A's claim for payment of the notes or other obligations.

Based solely on the information submitted and the representations set forth above, we hold as follows:

- (1) Any Corporation stock (or other interests in Corporation) that is considered held by Estate as a result of attribution to Estate from any of Estate's beneficiaries under § 318(3)(A) will not be considered to be further attributed to Trust A under § 318(a)(2)(A). Section 318(a)(5)(C).
- (2) The transfer of Corporation stock (or other interests in Corporation) from Estate to Trust A undertaken in the normal course of settling the estate will not prevent Trust A and Spouse from using the provisions of § 302(c)(2) to cut § 318(a)(1) family attribution.
- (3) The fact that directors, officers, and employees of Corporation may also be trustees, executors, officers, or employees of Trust A (or related entities) and have Asset Allocation Power, as described above, will not prevent Trust A and Spouse from using the provisions of § 302(c)(2) to cut § 318(a)(1) family attribution.
- (4) Provided that throughout the 10-year period immediately following the redemption Children and Grandchildren are not beneficiaries of any of the Children's Foundations and hold less than 50 percent of the vote in determining the affairs of each of the Children's Foundations, the fact that the Children's Foundations have Children or Grandchildren as members, officers, or directors will not prevent Trust A and Spouse from using the provisions of § 302(c)(2) to cut § 318(a)(1) family attribution.
- (5) Provided that (i) Trust A and Spouse both file the agreement described in § 302(c)(2)(A)(iii) of the Code in accordance with § 1.302-4(a) of the Income Tax Regulations, and (ii) the conditions stated in § 302(c)(2)(A)(i) and (ii) are satisfied, § 318(a)(1) will not apply and the redemption by Corporation of its stock held by Trust A, as described above, will constitute a "complete termination" of Trust A's interest within the meaning of § 302(b)(3). The amount distributed to Trust A by Corporation in the redemption will be treated as a distribution in full payment for the stock surrendered as provided in § 302(a).
- (6) As provided by § 1001, Trust A will realize and recognize gain or loss on the redemption of the Corporation stock. For each share of stock surrendered, gain or loss will be recognized to the extent of the difference between the redemption price (the amount of cash plus the fair market value of the portion of any Corporation notes or other obligations received in exchange for such share) and

the adjusted basis of such share as determined under § 1011. Provided that § 341 (relating to collapsible corporations) is not applicable and that the Corporation stock is a capital asset in the hands of Trust A, gain or loss, if any, will be considered capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1.

- (7) No gain or loss will be recognized to Corporation on the distribution to Trust A of solely cash and its own notes or other obligations.

We express no opinion about the tax treatment of the transaction under other provisions of the Code and regulations or about the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by the above rulings. The rulings contained in this letter are based on the law and Service positions as currently in effect. For the continuing validity of the rulings contained herein see section 12 of Rev. Proc. 2000-1, 2000-1 I.R.B. 4, 46.

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

It is important that a copy of this letter be attached to the federal income tax returns of the taxpayers involved for the taxable year in which the transactions covered by this letter are consummated.

In accordance with the power of attorney on file in this office, copies of this letter are being sent to your authorized representatives.

Sincerely yours,
Associate Chief Counsel (Corporate)
By Mark S. Jennings,
Acting Branch Chief, Branch 1