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September 26, 2007

Internal Revenue Service
Attn: CC:PA:LPD:PR (CC:PSI:4)
Room 5203, POB 7604
Ben Franklin Station
Washington, DC 20044

Re: IR-2007-127 (dated July 9, 2007)

Dear Madams and Sirs:

The attached comments are in response to the above referenced Internal Revenue Service ("IRS") News Release asking for comments about whether certain private letter rulings (the "PLRs"), such as PLRs 200715005, 200647001, 200637025, 200612002 and 200502014, issued by the IRS are consistent with certain prior revenue rulings, namely Rev. Rul. 76-503, 1976-2 CB 275 and Rev. Rul. 77-158, 1977-1 CB 285, with respect to the conclusion contained in each PLR that no member of the so-called "Distribution Committee" of the trust holds a general power of appointment under section 2514.

The comments are being submitted on behalf of the American Bar Association Section of Real Property, Trust and Estate Law. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and should not be construed as representing the position of the American Bar Association.

The comments were prepared by members of the Estate and Gift Tax Committee of the Trust and Estate Division of the ABA's Section of Real Property, Trust and Estate Law. Although the members of the Section who prepared these comments have clients who would be affected by the Federal tax principles addressed, or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a submission with respect to, or otherwise influence the development or the outcome of, the specific subject matter of these comments.

If you have any questions, please do not hesitate to contact James V. Roberts, Co-Vice Chair of the Estate and Gift Tax Committee, at Glast, Phillips & Murray, P.C., 2200 One Galleria Tower, 13355 Noel Road LB48, Dallas, Texas 75240, (214) 528-2822, jim@jamesvroberts.com

Very truly yours,

Kathleen M. Martin
Section Chair

cc: Armando Lasa-Ferrer, ABA Secretary
Denise Cardman, ABA Governmental Affairs
Steve R. Akers, Vice-Chair, Section of Real Property, Probate and Trust Law

ABA SECTION OF REAL PROPERTY | TRUST & ESTATE LAW

COMMENTS OF THE
AMERICAN BAR ASSOCIATION
REAL PROPERTY, TRUST AND ESTATE LAW SECTION

INCOMPLETE GIFT RESPONSE

Internal Revenue Service
Attn: CC:PA:LPD:PR (CC:PSI:4)
Room 5203, POB 7604
Ben Franklin Station
Washington, DC 20044

Re: IR-2007-127 (dated July 9, 2007)

Dear Madams and Sirs:

Introduction

The following comments are submitted on behalf of the Real Property, Trust and Estate Law Section (formerly the Real Property, Probate and Trust Law Section) of the American Bar Association (the "Section"). The views expressed herein have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, accordingly, should not be construed as representing the position of the American Bar Association.

The comments were prepared by members of the Estate and Gift Tax Committee of the Trust and Estate Division of the Section. James V. Roberts, Co-Vice Chair of the Estate & Gift Tax Committee of the Section, supervised the preparation of these comments and participated in their preparation with Jonathan Blattmachr, Todd Flubachr, Professor Mitchell Gans, Edward M. Manigault, Carlyn S. McCaffrey, Richard W. Nenno, Stephen E. Parker, Laura M. Twomey and Diana S.C. Zeydel. These comments were reviewed by Steven B. Gorin on behalf of the Section's Committee on Governmental Submissions.

Although the members of the Section who prepared these comments have clients who would be affected by the Federal tax principles addressed, or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a submission with respect to, or otherwise influence the development or the outcome of, the specific subject matter of these comments.

These comments are in response to the request contained in the above-referenced Internal Revenue Service ("IRS") News Release asking for comments about whether certain private letter rulings (the "PLRs"), such as PLRs 200715005, 200647001, 200637025, 200612002 and 200502014, issued by the IRS are consistent with certain prior revenue rulings, namely Rev. Rul. 76-503, 1976-2 CB 275 and Rev. Rul. 77-158, 1977-1 CB 285, with respect to the conclusion

contained in each PLR that no member of the so-called "Distribution Committee" of the trust holds a general power of appointment under section 2514.[1]

For the reasons set forth below, we conclude that no member of the Distribution Committee has such a power.

Scope of this Letter

In this letter, we take the liberty of not just addressing whether the foregoing conclusion contained in the PLRs is consistent with the two revenue rulings cited above, but also discuss an aspect of the revenue rulings themselves that we think may be appropriate to clarify and to discuss certain related matters. We conclude that the PLRs are not inconsistent with the revenue rulings, which involve circumstances that are different from the PLRs, and that the conclusion in the PLRs that no member of the Distribution Committee holds a general power of appoint is correct, for a number of reasons.

To minimize the length of this letter, we do not recite all the facts of the PLRs or discuss their reasoning or conclusions with respect to any other issue.

In each of the PLRs, A creates a discretionary trust for the benefit of A and others ("permissible beneficiaries"). A corporate trustee is appointed as sole trustee of the trust. A committee (the "Distribution Committee") consisting of two of the permissible beneficiaries has the power, by unanimous consent, to direct the trustee to pay or apply net income and principal of the trust to or among any one or more of the permissible beneficiaries. In addition, A and one member of the Distribution Committee may by agreement direct the trustee to make such distributions. If any member of the Distribution Committee ceases to serve for any reason, a permissible beneficiary (other than A or A's spouse) is appointed as the successor member. A retains a testamentary power to appoint the trust to any person or persons other than A's estate or creditors or the creditors of A's estate.

Background about General Powers of Appointment

Under section 2514, a "general power of appointment"" means a power that is exercisable in favor of the individual possessing the power, his or her estate or creditors, or the creditors of his or her estate. The exercise or release of a general power of appointment, subject to limitations and special rules, is treated as a transfer for Federal gift tax purposes.

Under section 2514(c)(3)(A), a person is not treated as holding a general power of appointment if the power is exercisable only with the consent of the person who created this power. We think this provision forecloses treating either member of the Distribution Committee as holding a general power of appointment with respect to the ability of a Distribution Committee member to exercise the power of appointment together with the grantor of the trust creating the power. Under the PLRs, however, the members of the Distribution Committee may

[1] Each reference to "section" is to a section of the Internal Revenue Code of 1986, as amended.

also exercise the power with the consent of each other and without, in that case, the consent of the grantor.

Under section 2514(c)(3)(B), a person is not treated as holding a general power of appointment if the power is not exercisable except in conjunction with a person having a substantial interest, in the property subject to the power, which interest is adverse to exercise of the power in favor of the person who holds the power. For the purposes of section 2514(c)(3)(B), a person who, after the death of the possessor of the power, may be possessed of a power of appointment which that person may exercise in his or her own favor is deemed as having an interest that is adverse to such exercise of the possessor's power. The rule contained in section 2514(c)(3)(B) is sometimes referred to as the joint power rule.

Treas. Reg. § 25.2514-3(b)(2) spells out part of the scope of the joint power rule by providing, in part, that

> a coholder of a power is considered as having an adverse interest where he may possess the power after the possessor's death and may exercise it at that time in favor of himself, his estate, his creditors, or the creditors of his estate. Thus, for example, if X, Y, and Z held a power jointly to appoint among a group of persons which includes themselves and if on the death of X the power will pass to Y and Z jointly, then Y and Z are considered to have interests adverse to the exercise of the power in favor of X. Similarly, if on Y's death the power will pass to Z, Z is considered to have an interest adverse to the exercise of the power in favor of Y.

However, Treas. Reg. § 25.2514-3(b)(3) indicates that, if a power is exercisable only with another or others in whose favor it may also be exercised, it will be treated as a general power as to an aliquot (proportionate) share of the property over which the power extends if the other power holders do not alone succeed to the power.

Nowhere in Treas. Reg. § 25.2514-3(b)(2) is succession to power on the death of a coholder required for adversity. Had the regulation contemplated that a coholder could only be adverse by succeeding to power on the death of a fellow coholder, the regulation would have simply stated this as a requirement. Rather, the regulation provides a way out for those who are "merely" coholders by nonetheless "considering" them adverse where such coholder succeeds to power upon the death of a fellow coholder. The succession to power essentially provides a coholder whose only interest would otherwise be as a mere coholder and as a mere potential appointee with an additional economic interest in the trust to cause him to be adverse.

When read as a whole, Treas. Reg. § 25.2514-3(b)(2) requires that a coholder must possess some additional economic interest in the trust to be considered adverse; however, this additional economic interest need not be in the form of succession to power on the death of a fellow coholder. The succession to power illustrated in the "XYZ" example quoted above is simply an illustration of one way to achieve adversity. Had the regulation contemplated that a coholder could only be adverse by succeeding to power on the death of a fellow coholder, the regulation would have simply stated this as a requirement. Rather, the regulation provides a way out for those who are "merely" coholders by nonetheless "considering" them adverse where such

coholder succeeds to power upon the death of a fellow coholder. The succession to power essentially provides a coholder whose only interest would otherwise be as a mere coholder and as a mere potential appointee with an additional economic interest in the trust to cause him to be adverse.

The numbered Examples (1) and (2) of the regulation, clearly demonstrate that coholders can be adverse even where there is no succession to power due to other economic interests that they possess in the trust. In Example (1) of the Regulation, where T and R are the trustees of a trust under which income is paid to T for life, then to M for life, remainder to R, and the trustees have the power to distribute principal to T, R is adverse because the exercise of his power to distribute principal to T would adversely affect his remainder interest in the trust. Likewise, if M were a trustee with T, M would be adverse because the exercise of his power in favor of T would adversely affect M's succeeding life interest in the trust. Thus, R as remainderman, and M as successor life beneficiary, are not merely coholders, but each has an additional economic interest in the trust that make them adverse. Example (2) of the regulation, where T and L are the trustees of a trust under which income is paid to L for life, then to M for life, remainder to T, and the trustees have the power to distribute principal to T, L is adverse because his life interest in the trust would be adversely affected by appointing principal to T. Similarly, if M were a trustee with T, M would likewise be adverse because the exercise of his power in favor of T would adversely affect M's succeeding life interest in the trust. Thus, it is L's economic interest as an income beneficiary of the trust that makes him adverse and, if M were a trustee, M's succeeding life interest in the trust that would make him adverse.

Because of their other economic interests in the trust, the coholders in these examples do not need to succeed to power to be considered adverse; rather these other economic interests in the trust by themselves make the coholders adverse. This is further underscored in Example (3) of the regulation, where there is no adversity because the coholder's interest in the trust is not affected by the exercise of the power. Here, where T and L are the trustees of a trust under which income is paid to L for life, remainder to A or T as the trustees determine, L is not an adverse party because L's interest in the trust is not affected by his and T's power to appoint the remainder among T or A at L's death.

In these examples, the coholders have an additional interest in the trust which would be negatively impacted by agreeing to a distribution of any amount to the other party. In Example (1), R has incentive to deny T's request for principal distributions. If R agrees to make a principal distribution to T, there is less principal for R to receive at the end of the day. Similarly, the Distribution Committee members in the PLRs have an additional interest in the trust that would be negatively impacted by agreeing to any distributions to their coholders. They have incentive to vote against distributions because any distributions, even a distribution which splits the trust among them equally, adversely affects their ability to obtain more than half, even all, of the trust principal, by exercising their solo power with the consent of the grantor.

Description of Rev. Rul. 76-503 and Rev. Rul. 77-158

In Rev. Rul. 76-503 and Rev. Rul. 77-158, three siblings established a trust for the benefit of their descendants. The trust was funded with a family business with the intended purpose of

keeping the family enterprise intact. The trust, therefore, was a dynasty type trust that would continue until twenty years after the death of the last surviving descendant of any of the siblings living on the date of creation of the trust. Each of the siblings designated one of his or her children as an initial trustee. The three trustees held a joint power to appoint the trust property to whomever they selected including themselves. Each trustee was privileged to designate one of the trustee's relatives to serve as a successor trustee in the event of the trustee's death or resignation. In the absence of such a designation, the oldest adult living descendant of the deceased or resigned trustee who was willing to serve as the new trustee would occupy the vacant trustee position. The rulings conclude that in the event of the death of any trustee, the trustee would be treated as holding a general power of appointment (within the meaning of section 2041(a)) over one-third of the trust causing one-third of the trust to be included in the trustee's gross estate for United States estate tax purposes.

We construe the revenue rulings as providing that, in the case of a dynasty type trust, if a trustee with the unanimous consent of the other trustees (Rev. Rul. 76-503) or with the consent of a majority of the other trustees (in Rev. Rul. 77-158), has a power to distribute property in his or her favor, and also has the power to designate a family member as successor trustee or, in the absence of such a designation, a successor trustee who is a family member will be appointed, then the trustee will be deemed to possess a general power of appointment over a proportionate share of the trust. It appears to us relevant that the trust in the rulings was a dynasty type trust so that the only real potential for beneficial enjoyment of the trust property by the trustee would be as a result of current distributions. In addition, the trustee's ability to appoint a relative as successor trustee or, in default of such appointment, the trustee's oldest living adult descendant would be appointed leaves little opportunity for any trustee to gain economic advantage by holding out on distributions in favor of another trustee. Moreover, the rulings do not appear to take into account that no successor trustee might be appointed, for example if the resigning or deceased trustee fails to designate a successor and has no adult descendants, in which case the remaining trustees alone would possess the power. In such a situation, and especially considering that being adverse is more than just looking at the succession of power of appointment, we think the example contained in Treas. Reg. § 25.2514-3(b)(2) involving X, Y and Z, quoted above, would mean that the deceased trustee would not be treated as holding a general power of appointment at death. We believe that it may be appropriate for the IRS to issue further guidance discussing the foregoing issues.

Subject to the foregoing, however, we think on their particular facts the revenue rulings are consistent with the Treasury Regulations.

We also think it appropriate to discuss Rev. Rul. 79-63, 1979-1 CB 102. In that ruling, the decedent's spouse created a testamentary trust under the terms of which the trust income was payable to the decedent for life, and the remainder was payable equally to the decedent's children or to any one of such children as the decedent might direct by will. In addition, the trust terms provided that at any time during the decedent's lifetime the decedent, with the consent of one of the decedent's children, could direct the trustees to distribute all or any part of the trust property to anyone, including the decedent.

Rev. Rul. 79-63 concludes that the decedent held a general power of appointment at death because the child was only a default taker of the trust property to the extent the decedent did not exercise the testamentary special power of appointment over the trust. Although under Treas. Reg. § 25.2514-3(b)(2) (fourth sentence) a taker in default of appointment under a power has an interest that is adverse to an exercise of the power, the ruling apparently concludes, without explicitly so stating, that the child's position as a default taker was insufficient to make the child an adverse party because the interest could by eliminated by the exercise of the decedent's special testamentary power of appointment.

We are not certain that that conclusion is correct. We find nothing in the regulations that compels such a result. The ruling relies, in part, on *Estate of Towle v. Commissioner*, 54 T.C. 368 (1970). In that case, the Tax Court states, in part:

> We think that the phrase "substantial interest in the property, subject to the power, which is adverse to exercise of the power in favor of the decedent," as used in section 2041(b)(1)(C)(ii) was intended at the very least to require that the third person have a *present or future chance* to obtain a personal benefit from the property itself.

(Footnote omitted; emphasis added.)

We think that the child acting as trustee in Rev. Rul. 79-63 who could consent to allow the decedent to withdraw the property from the trust certainly had "a present or future chance to obtain a personal benefit from the property itself."

Analyzing the facts of the PLRs against those of the three rulings discussed above, we think the members of the Distribution Committee are in a substantially different position than the position of the trustees in the rulings. A surviving member of the Distribution Committee stands to succeed to an interest in the trust property that is materially greater than the interest the surviving member has in the existing trust. The trust in the PLRs is not a dynasty type trust intended to continue as a single trust for the benefit of the entire family for essentially the period permitted under the applicable rule against perpetuities. The members of the Distribution Committee also do not have discretion to appoint relatives as successor trustees who could act as their "alter egos" for purposes of making current distributions in their favor. Moreover, unlike the children who were trustees in Rev. Rul. 76-503 and Rev. Rul. 77-158, each surviving member of the Distribution Committee would also hold the power to appoint property to himself or herself with the consent of the grantor and not just with the consent of other beneficiaries. The surviving member of the Distribution Committee with respect to the exercise of the power of appointment is also different than the position of the child in Rev. Rul. 79-63. Unlike the child in the revenue ruling, the surviving member of the Distribution Committee not only is a default taker of a testamentary power of appointment but would hold, after the death of the other member of the Distribution Committee, the power to appoint the property, either with the consent of the successor member of the committee or with the grantor, to himself or herself. We think that these differences are sufficient to distinguish the situation of a member of the Distribution Committee in the PLRs from the circumstances described in the three foregoing revenue rulings and sufficient to permit the IRS to conclude that each such member is adverse

with the respect to the power held by another member so that no member holds a general power of appointment.

Moreover, the plain language of Treas. Reg. § 25.2514-3(b)(2) supports the conclusion that the Distribution Committee members are adverse. The regulation provides that a coholder of a power is not adverse *merely* because he is a coholder nor *merely* because he is a permissible appointee. These two interests alone do not establish adversity. The regulation then goes on to state,"[*h*]*owever,* a coholder *is considered as having* an adverse interest" when he will succeed to power on the death of a coholder. In other words, a coholder will be *deemed* adverse even where his only interest in a trust is as a coholder of a power, if he may eventually inherit this power on the death of a fellow coholder.

Referring back to the last paragraph under "Background about General Powers of Appointment" (above) and the examples cited therein, we would submit that in sharp contrast, the coholders of the power in the above described revenue rulings are mere potential appointees and do not have an additional interest in the trust. Their best bet is to agree with their coholder to split the trust principal. Thus, they have no incentive to vote against distributions, as doing so will not impact their interest in the trust. It makes sense that the XYZ example in the regulation requires a succession to power where the coholders are mere potential appointees, because the possibility of inheriting the whole distribution power is the only incentive not to exercise their power to split the trust. Clearly, the Distribution Committee members in the PLRs are very different from the coholders in the above described revenue rulings and from the XYZ example of the regulation. Rather, the Distribution Committee members in the PLRs are analogous to Examples (1) and (2) and are adverse.

While, as explained above, we do not believe that a succession to power is necessary for a finding of adversity in the general power of appointment context, it is clearly not necessary for income tax purposes under the grantor trust rules. The grantor trust rules clearly define adversity and, in fact, the IRS has correctly interpreted that coholders are adverse for purposes of the grantor trust rules even where there is a successor trustee designated and the coholders will not succeed to power. *See* PLR 9016079 (where a trustee who is beneficiary of a trust is found to be adverse for purposes of the grantor trust rules when a successor trustee will take his place at his failure to act).

In Any Case, the Conclusion Reached in the PLRs Is Correct Because a Taxpayer Cannot Hold a General Power Over Property the Transfer of Which Is Incomplete

For an alternate reason, we think the conclusion reached in the PLRs that no member of the Distribution Committee holds a general power of appoint is correct.

None of Rev. Rul. 76-503, 77-158 and 79-63 involves a circumstance where the power of appointment was over property the transfer of which was incomplete for estate and gift tax purposes. We think the conclusion in the PLRs that the gift by the grantor is incomplete to the trust is correct. And, as we discuss below, we think that forecloses any member of the Distribution Committee being treated as holding a general power of appointment. There are, in our view, two aspects of that conclusion.

First, the two members of the Distribution Committee, either acting together, or either one of them with the consent of the grantor, may distribute trust property back to the grantor. We think that an exercise in favor of the grantor by either or both members of the Distribution Committee should not be treated as a gift by either of them. We believe this conclusion is supported by Treas. Reg. § 25.2511-2(f) which specifies that no completed gift occurs with respect to property subject to the taxpayer's power of amendment unless it is distributed to a person "other than the donor."[2] We do not believe Rev. Rul. 67-370, discussed below, forecloses such a construction of Treas. Reg. § 25.2511-2(f) because in that revenue ruling, and unlike the situations in the PLRs, the grantor was not a permissible recipient of the property involved, a circumstance required by the regulation to avoid a completed gift.

We recognize that the regulation quoted in the paragraph immediately above may be read as determining only whether the grantor would be deemed to make a gift if the property were distributed to the grantor. But, in our view, it suggests that no one would be deemed to have made a gift by the distribution to the grantor of property with respect to which the grantor's gift was incomplete. We also believe that the regulation implies that, because the grantor/donor would be treated as making a competed gift upon the distribution of trust property to someone other than the grantor, no one else could be treated as making a completed gift by virtue of such a distribution.

We think the conclusion reached in the PLRs that no member of the Distribution Committee holds a general power of appoint also is correct because we think that no one may be deemed to have a general power until the transfer of the property subject to the power is complete for gift or estate tax purposes. We think this is a fundamental precept of gift and estate taxation. Nevertheless, we acknowledge that one item of published guidance (Rev. Rul. 67-370), one case (*Johnstone*) and four private letters rulings (PLRs 200101012, 200210051, 200403094, 200604028) might be viewed as inconsistent with our view. But correctly analyzed, they are not, in our judgment, inconsistent.

Rev. Rul. 67-370 Does Not Apply

In Rev. Rul. 67-370, 1967-1 CB 324, the value of a defeasible remainder interest in trust that was subject to termination at the will of another was held to be included under section 2033 in the gross estate of the remainder beneficiary who died before the defeasance ceased. The reasoning of the revenue ruling limits the application of the gross estate inclusion. It seems to be limited to a circumstance where the remainder is "clearly 'descendible, devisable, and alienable' as a matter of [governing] law, for example, and would undoubtedly have resulted in the receipt of substantial assets by decedent's estate if the settlor had not proceeded to revoke the same. In re: Hornblower's Estate, 180 N.Y. Misc. 517, 40 N.Y.S.2d 712 (1943)." In the circumstance involved in the PLRs, no part of the Distribution Committee member's power of appointment or other interest in the trust is descendible, devisable or alienable. Accordingly, we think Rev. Rul.

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[2] The regulation provides in part, "The receipt of income or of other enjoyment of the transferred property by the transferee or by the beneficiary *(other than by the donor himself)* during the interim between the making of the initial transfer and the relinquishment or termination of the power operates to free such income or other enjoyment from the power, and constitutes a gift of such income or of such other enjoyment…." (Emphasis added.)

67-370 is inapplicable to the issue of whether the Distribution Committee members should be treated as holding a general power of appointment.

Rev. Rul. 67-370 is distinguishable on another grounds as well. If the members of the Distribution Committee made a distribution to a beneficiary other than themselves including the grantor, the gift by the grantor would be complete. Treas. Reg. § 25.2511-2(f). If, however, the members of the Distribution Committee were deemed to hold a general power of appointment under section 2514, the distribution to a beneficiary also would *simultaneously* be deemed to be a gift by the members of the Distribution Committee. Although property certainly can be taxed consecutively for estate and gift tax purposes (as presumably it was in Rev. Rul. 67-370), we know of no instance where it is taxed simultaneously under the same tax, here gift tax.

Indeed, the generation-skipping transfer tax provisions envision that only one person may be treated as being the transferor of property for gift or estate tax purposes at any one time. See section 2652(a). In fact, Treas. Reg. § 26.2652-1 states, in part, "the individual with respect to whom property was *most recently* subject to Federal estate or gift tax is the transferor of that property for purposes of chapter 13." (Emphasis added.) For example, suppose the grantor's sibling were a member of the Distribution Committee and the grantor and the sibling decided to distribute trust property to a grandchild of the grantor (who would be a skip-person with respect to both the grantor and the grantor's sibling). It appears certain to us that only one of the grantor and the sibling may be treated as the transferor of the direct skip made to the grandchild. It seems to us that the grantor should be treated as the transferor and that the sibling should not be treated as the transferor.[3] Hence, no member of the Distribution Committee should be treated as holding a general power of appointment while the grantor's transfer is incomplete for Federal estate and gift tax purposes.

Johnstone Is Distinguishable.

In this connection, we think *Johnstone v. Commissioner,* 76 F.2d 55 (9th Cir. 1935), also should be discussed. In that case, the decedent's mother had created a trust for her son over which he was granted a testamentary general power of appointment. The mother retained the power to amend (but not revoke) the trust before her son's death. It seems her power of amendment could include eliminating the son's power of appointment prior to, but not upon or after, his death. The United States Court of Appeals for the Ninth Circuit held that the property over which the son held the power of appointment was included in his gross estate for Federal estate tax purposes. First, although the Court of Appeals discusses that the power of appointment became irrevocable when the son died, it does not seem that the son's estate argued that he did not have the power of appointment at his death. It seems that the taxpayer, the IRS and the court assumed that, at the moment of the son's death, he alone could exercise the power. Under section 2514(c)(2) and (3)(A) and section 2041(b)(a)(B) and (C)(i), a person is not treated a holding a power of appointment if it is exercisable only with the consent of the person who has

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[3] Such a result is consistent with the view of the IRS with respect to determining who is the grantor of a trust that would be a grantor trust with respect to the actual grantor and a beneficiary who holds a power to withdraw under section 678. *See, e.g.,* PLRs 9309023, 9141027 and 8929040. We appreciate that, under section 6110(k)(3), neither a private letter ruling nor a national office technical advice memorandum may be cited or used as precedent but thought it appropriate to mention the forgoing and certain other private letter rulings in this letter.

created it. It seems that the parties and the court assumed that the son's death meant he no longer needed his mother's consent to exercise because, in essence, as of his death, he could exercise it alone. Second, and in any event, the case does not stand for the proposition that one act may produce transfer tax events with respect to two different people. When the son died in 1928, there was no Federal gift tax, so the mother could not be treated as making a taxable gift by reason of her son's death which eliminated her power of amendment which might have prevented the gift from being complete for Federal gift tax purposes, as there was no gift tax when she created the trust nor when her son died and her power to amend apparently ended. Third, and, perhaps, most important, the circumstances involving the PLRs are different from *Johnstone:* in *Johnstone,* the mother's power to amend the trust was expunged at the son's death; in the PLRs, the grantor's ability to change the disposition of the trust by exercise of the grantor's testamentary special power of appointment over the trust would continue after the death of any member of the Distribution Committee.

We think one other point about *Johnstone* should be discussed. We do not believe that a decedent's gross estate would ever include any interest the decedent might have under the Will of a living person. For example, the Will of a child's living parent bequeaths property to the child or, if the child does not survive the parent, to the child's estate. If the child dies before the parent, we believe that law would not require that anything be included in the child's gross estate on account of this expectancy under the surviving parent's Will. We believe that the result should be the same with respect to an expectancy under a trust that is revocable by its grantor. And we think that the meaning of revocability means incompleteness for gift tax purposes. Otherwise, an unwise and unreasonable "mismatch" would exist in the law between expectancies under a Will of a living person and a trust that is revocable by its grantor for tax purposes, meaning that it is modifiable by a living grantor in such a manner that no completed transfer has yet taken place for transfer tax purposes.

Other Private Letter Rulings Are Distinguishable.

We also think it appropriate to mention four private letter rulings involving the grant in a revocable trust of a general power of appointment to a deceased spouse from the surviving spouse.[4] In these rulings, the IRS held that upon the death of the first spouse to die, the surviving spouse makes a completed gift qualifying for the gift tax marital deduction to the deceased spouse at the moment of the latter's death by the grant to the deceased spouse of a general power of appointment and the property subject to the power is included under section 2041 in the gross estate of the deceased spouse. These rulings seem to conclude that the gift to the deceased spouse occurs the moment *before* his or her death (as a gift may qualify for the marital deduction only if both spouses are alive at the time of the transfer[5]) and that the deceased spouse, therefore, holds the general power of appointment *at death.* The conclusion that the gift qualifies for the marital deduction may be based upon an analogy to the "common disaster" provisions of section 2056(b)(3)(A). Again, these four private letter rulings are distinguishable from the PLRs in that the gift by the grantor in the PLRs would remain incomplete when a member of the Distribution Committee dies.

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4 PLRs 200101012, 200210051, 200403094, 200604028.

5 *See, e.g., Estate of Bagley v. U.S.*, 443 F.2d 1266 (5th Cir 1971). Although the common disaster provision is limited to the estate tax, it may be that it was used analogous in the four private letter rulings' conclusion.

Special Effective Date Rules for Pre-1942 and Post-1942 Powers Support the Conclusion that There Can Be No General Power Until the Transfer of the Property Over Which the Power Applies Is Complete

One additional point, we feel, needs to be addressed and we think it supports our conclusion that a person cannot be treated as holding a general power over appointment over property the transfer of which is incomplete for estate and gift tax purposes.

Treas. Reg. § 25.2514-1(e) provides, in part, that a power of appointment created by lifetime instrument is considered created on the date the instrument "takes effect" and the power is not considered created at some future time merely because it is revocable, is not exercisable on the date the instrument takes effect or because the identity of its holders is not ascertainable until after the instrument takes effect. We believe that this rule is merely part of the special effective date rules relating to the amendments to the Code with respect to general powers of appointment that became effective October 21, 1942. It seems simply to be an expansion of what is now section 2514(f) which provides, "For purposes of this section a power of appointment created by a will executed on or before October 21, 1942, shall be considered a power created on or before such date if the person executing such will dies before July 1, 1949, without having republished such will, by codicil or otherwise, after October 21, 1942." In fact, the entire regulatory section provides:

> A power of appointment created by will is, in general, considered as created on the date of the testator's death. However, section 2514(f) provides that a power of appointment created by a will executed on or before October 21, 1942, is considered a power created on or before that date if the testator dies before July 1, 1949, without having republished the will, by codicil or otherwise, after October 21, 1942. A power of appointment created by an inter vivos instrument is considered as created on the date the instrument takes effect. Such a power is not considered as created at some future date merely because it is not exercisable on the date the instrument takes effect, or because it is revocable, or because the identity of its holders is not ascertainable until after the date the instrument takes effect. However, if the holder of a power exercises it by creating a second power, the second power is considered as created at the time of the exercise of the first.

An identical provision is contained in Treas. Reg. § 20.2041-1(e). These regulatory provisions under sections 2514 and 2041 certainly are *special* effective date rules. In our judgment, these special effective date rules which provide, in part, that a power of appointment is deemed created before the effective date of legislation even if the power is revocable supports the conclusion that in all other cases a power of appointment is not deemed created while it is revocable. Were the result otherwise, the effective date rules would be unnecessary to protect property from a new tax regime for general powers of appointment which was enacted effective October 21, 1942 with respect to general powers of appointment.

The foregoing effective date regulation is somewhat similar to other effective date rules. *See., e.g.,* Treas. Reg. § 26.2601-1(b)(2), dealing with the effective date provisions of the generation-skipping transfer tax. These effective date rules "grandparent" certain transfers from

the generation-skipping transfer tax imposed by section 2601. Revocable trusts, *except for limited transitional rules* contained in that regulation, created before the effective date of the generation-skipping transfer tax, are not grandparented and any generation-skipping transfers with respect to such trusts, after the effective date of the generation-skipping transfer tax, are subject to that tax (unless falling under another exception or exemption).

Indeed, we have reviewed the analysis submitted to you by Professor Mitchell M. Gans of Hofstra Law School and believe his analysis further supports our conclusion that an individual cannot be treated as holding a general power over property with respect to which no completed gift has occurred. As Professor Gans discusses in detail, *United States v. Turner*, 287 F.2d 821 (8th Cir. 1961) held that a general power of appointment was created prior to 1942 even though the court held that the power would not have triggered section 2041 in the power holder's estate as long as the person granting the power had the right to revoke it. See *id.* at 827. *United States. v. Merchants Nat. Bank of Mobile*, 261 F.2d 570 (5th Cir. 1958) used an identical analysis and reached the same conclusion.

Both *Turner* and *Merchants National Bank of Mobile* made a critical distinction between (1) the time when a power is deemed created and (2) the time when it becomes subject to inclusion under section 2041 in the gross estate of the power holder: treating a power of appointment that is subject to a power of revocation as immediately created for purposes of determining whether it is a pre- or post-1942 power, but not imposing estate tax (or gift tax) in the power holder's gross estate until the revocation or amendment authority over the power of appointment is terminated. These cases fully support the notion that the donee is not treated as holding a power of appointment for purposes of sections 2041 and 2514 while the power is over property with respect to which no completed transfer has occurred for estate and gift tax purposes.

Disclaimer Rules Support Notion That No General Power Arises While Gift is Incomplete

As a policy matter, given section 2518, it makes no sense to treat a person as having a general power of appointment where the initial gift remains incomplete. Consider, for example, the case where a grantor creates a revocable trust under which A is given a general power. If A should die without having exercised the power or otherwise accepted it, her executor should be permitted to disclaim it even if death should occur more than nine months after the grantor executed the revocable trust. See Treas. Reg. § 25.2518-2(c)(3) (indicating that where a general power is granted under an incomplete-gift instrument, the donee of the power can disclaim within nine months of the time the gift becomes complete). In effect, as long as the grantor retains a revocation power and A has not accepted the power (by exercising it or otherwise), it can be disclaimed at any time. Indeed, it is even arguable that A’s executor would have a duty to disclaim in order to avoid inclusion of the property subject to the power in A’s estate. Since, in the case of an incomplete gift, a disclaimer made at any time can avoid inclusion in the estate of the donee of the power, such inclusion should not result merely because A or A’s executor fails to make the disclaimer. Instead, the IRS should take the position that, whenever a power of appointment is created under an incomplete-gift instrument, the donee does not have a general power.

Additional Comments

We respectfully offer four additional comments or requests.

First, if the IRS concludes that it cannot rule that no member of the Distribution Committee holds a general power of appointment under the facts in the PLRs, we respectfully request that the IRS issue published guidance involving facts identical to the ones in the PLRs except that there would be three initial members of the Distribution Committee who could not be replaced upon the death of a Distribution Committee member and who cannot appoint their own successor. We believe that the published guidance should conclude, pursuant to the X, Y and Z example contained in Treas. Reg. § 25.2514-3(b)(2) and discussed above, that neither of the first two members of the Distribution Committee to die would be treated as holding a general power of appointment.

Second, if the IRS concludes that it cannot rule that no member of the Distribution Committee holds a general power of appointment under the facts in the PLRs, we respectfully request that the IRS also issue published guidance involving facts identical to the ones in the PLRs except that the grantor, if he or she exercises the testamentary power of appointment, would be required to exercise it, in part, in favor of each Distribution Committee member who survives the grantor thereby reaching the conclusion that no member of the Distribution Committee would be deemed to hold a general power of appointment.

Third, if the IRS concludes that it cannot rule that no member of the Distribution Committee holds a general power of appointment under the facts in the PLRs, we respectfully request that the IRS also issue published guidance involving facts identical to the ones in the PLRs but conclude that, to the extent that the property in the trust is distributed to the grantor, no member of the Distribution Committee would be deemed to have made a gift by the exercise of a general power of appointment.

Fourth, we respectfully request that if the IRS concludes that each member of the Distribution Committee does holds a general power of appointment under the facts in the PLRs, you apply that conclusion prospectively only pursuant to section 7805(b).

Conclusion

Accordingly, the Section believes that the PLRs are correct in their conclusions that no member of the Distribution Committee holds a general power of appointment.

We hope that our remarks are helpful. We appreciate the opportunity to submit these written comments and would welcome the opportunity to offer any additional assistance that may be desired.