

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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Nov 3 2003

LEGEND

Debtors =

Trust =

D1 =

D2 =

D3 =

Dear \_\_\_\_\_ :

This is in reply to a letter dated May 20, 2003 submitted on behalf of Trust, requesting rulings regarding the classification of Trust as a liquidating trust under § 301.7701-4(d) of the Procedure and Administration Regulations and that Trust will be a grantor trust and the Beneficiaries of Trust will be treated as owners of Trust under §§ 671 and 677.

FACTS

Debtor filed a voluntary petition under Chapter 11 of the Bankruptcy Code in the Bankruptcy Court on D1. On D2, the Bankruptcy Court confirmed the Modified Second Amended Plan of Reorganization under Chapter 11 of the Bankruptcy Code, as amended by the Order Technically Amending the Plan of Reorganization (the "Plan").

Pursuant to the Plan, Trust was created to prosecute litigation claims and provide a mechanism for the liquidation and distribution of the assets of Debtor. Under the Trust Agreement (the "Agreement") the liquidating trustee is authorized and directed to take all reasonable and necessary action to hold, conserve, and protect Trust's assets and to collect on, sell, or otherwise liquidate or dispose of Trust's assets, and to distribute the net proceeds of such disposition to the Trust beneficiaries as provided in the Plan in as prompt, efficient and orderly a fashion as possible.

The Agreement generally provides that Trust will terminate no later than ten years after its formation. Trust represents that its time frame for termination is required because the litigation against Trust cannot be resolved until after litigation undertaken by Trust against a third party is resolved. Among Trust's assets is an intangible asset, the value of which the trustee believes can be maximized by licensing it. Trust represents that it has no employees and will not engage in any support or development functions with regard to the asset. If the asset has not been permanently sold by D3, Trust will abandon it.

Trust shall not receive or retain cash in excess of a reasonable amount to meet claims and contingent liabilities (including disputed claims) or to maintain the value of the assets during liquidation. Cash not available for distribution and cash pending distribution will be held in demand and time deposits, such as short-term certificates of deposit, in banks or other savings institutions, or other temporary, liquid investments such as Treasury bills. Trust is required, under the terms of the Agreement, to distribute to the Beneficiaries, at least annually its net income and all net proceeds from the sale of Trust's assets, or licensing of the intangible asset, except that Trust may retain an amount of net proceeds or net income reasonably necessary to maintain the value of the property or to meet claims or contingent liabilities.

The Agreement provides that the Beneficiaries will be treated as the grantors and deemed owners of Trust. It further provides that the parties agree to value all assets transferred to Trust consistently and to use such values for all federal income tax purposes.

The Agreement provides that the trustee shall file returns as a grantor trust pursuant to section 1.671-4(a) of the Income Tax Regulations.

The Agreement, consistent with the requirements set out in Rev. Proc. 94-45, 1994-2 C.B. 684, provides that the transfer of the liquidating trust assets to the liquidating trust will be treated for all federal tax purposes (e.g., sections 61(a)(12), 483, 1001, 1012, and 1274) as a transfer from the bankruptcy estate to the Beneficiaries followed by a deemed transfer by the Beneficiaries to the liquidating trust.

## LAW AND ANALYSIS

Section 671 of the Code provides that where it is specified in subpart E that the grantor or another person shall be treated as the owner of any portion of a trust, there then shall be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust that are attributable to that portion of the trust to the extent that such items would be taken into account under chapter 1 of the Code in computing taxable income or credits against the tax of an individual.

Section 1.671-4(a) of the Income Tax Regulations provides that except as provided in section 1.671-4(b)(1) and (2), items of income, deduction, and credit attributable to any portion of a trust which, under the provisions of subpart E (section 671 and following), part I, subchapter J, chapter 1 of the Code, are treated as owned by the grantor or another person should not be reported by the trust on Form 1041, but should be shown on a separate statement attached to that form.

Section 677(a) of the Code provides, in part, that the grantor shall be treated as the owner of any portion of a trust, whether or not the grantor is treated as such owner under section 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a non-adverse party, or both, may be (1) distributed to the grantor or the grantor's spouse; or (2) held or accumulated for future distribution to the grantor or the grantor's spouse.

Section 301.7701-4(d) of the regulations provides that certain organizations which are commonly known as liquidating trusts are treated as trusts for purposes of the Internal Revenue Code. An organization will be considered a liquidating trust if it is organized for the primary purpose of liquidating and distributing the assets transferred to it, and if its activities are all reasonably necessary to, and consistent with, the accomplishment of that purpose. A liquidating trust is treated as a trust for purposes of the Code because it is formed with the objective of liquidating particular assets and not as an organization having as its purpose the carrying on of a profit-making business which normally would be conducted through business organizations classified as corporations or partnerships. However, if the liquidation is unreasonably prolonged or if the liquidation purpose becomes so obscured by business activities that the declared purpose of liquidation can be said to be lost or abandoned, the status of the organization will no longer be that of a liquidating trust.

Rev. Proc. 94-45 provides the conditions under which the Service will consider issuing advance rulings classifying certain trusts as liquidating trusts under § 301.7701-4(d).

## CONCLUSIONS

Rev. Proc. 94-45, states that the Service will issue a ruling classifying an entity created pursuant to a bankruptcy plan under Chapter 11 of the Bankruptcy Code, 11 U.S.C. section 1101, et. seq. (1988), as a liquidating trust under section 301.7701-4(d) of the regulations if certain specified conditions are met. Based on the information submitted and the representations made, we conclude that the conditions of Rev. Proc. 94-45 have been satisfied.

Accordingly, based on the representations made and the information submitted, we rule as follows:

Trust will be classified for federal income tax purposes as a liquidating trust under section 301.7701-4(d) of the regulations.

Trust will be a grantor trust and the Beneficiaries of Trust will be treated as the owners of Trust under sections 671 and 677.

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.

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.

Sincerely,

/s/ David R. Haglund

David R. Haglund  
Senior Technician Reviewer  
Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosure (2):  
Copy of this letter  
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