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May 30, 2006

Mr. Eric Solomon
Acting Deputy Assistant Secretary (Tax Policy)
Department of the Treasury
Room 3112 MT
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

The Honorable Mark W. Everson
Commissioner
Internal Revenue Service
Room 3000 IR
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Re: IRS Guidance Regarding Family-Owned Trust Companies

Dear Acting Deputy Assistant Secretary Solomon and
Commissioner Everson:

I am pleased to enclose New York State Bar Association Tax Section Report No. 1111, commenting on the guidance to be proposed regarding the tax consequences of appointing a family-owned trust company (an "FTC") to serve as trustee of a trust for the benefit of family members (an "FTC Trust"). The report addresses estate, gift and generation skipping transfer taxes (collectively, "transfer taxes"), as well as the grantor trust rules under subchapter J.

The Report describes the differences between FTCs and independent trust companies and, after a brief discussion of the existing applicable income and transfer tax law, including discussions of attribution of trustee powers under Revenue Ruling 95-58 and of the reciprocal trust doctrine, proposes that a set of rules relating to the exercise of "Tax-Sensitive Powers" be adopted. An individual's "Tax-

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Sensitive Powers” are defined to include any power over a trust that, if held directly by her, would cause trust property to be included in her gross estate, would cause a gift made by her to be incomplete for gift tax purposes or would cause her or another to be treated as the owner of the trust under the grantor trust rules of Subchapter J.

The Report proposes that the guidance require that an FTC’s by-laws establish one or more committees the purpose of which would be to isolate the Tax-Sensitive Powers and prevent the grantor and the beneficiaries from participating in decisions regarding such powers.

Specifically, we suggest that the definitions and requirements described below be incorporated into the guidance to be issued and that the guidance provide that trustee powers will not be attributed to a grantor, beneficiary or other individual who owns an interest in, is employed by or participates in the governance of a FTC if the FTC’s by laws, trust agreements or trustee appointment documents satisfy these requirements.

- The by-laws of the FTC should prohibit (1) any grantor of a trust of which the FTC is serving as trustee from participating in any decisions by any committee regarding the exercise of a power that is a Tax-Sensitive Power as to her (a “Grantor Tax-Sensitive” Power), (2) a beneficiary from participating in any decisions by any committee regarding the exercise of a Power that is a Tax-Sensitive Power as to her (a “Beneficiary Tax-Sensitive” Power), or (3) any person who is a related or subordinate party to the grantor from participating any decisions by any committee regarding the exercise of a power that is a Tax-Sensitive Power as to her (a “Related Party Tax-Sensitive Power”) unless there are an equal number of members of such committee who are not related or subordinate parties as to the grantor.
- The by-laws of the FTC should provide that, if a grantor or a beneficiary of an FTC Trust participates in the removal and replacement of a member of a committee who holds powers that are Tax-Sensitive to her, the replacement member must not be related or subordinate to the grantor or such beneficiary.
- The by-laws of the FTC should prohibit grantors and beneficiaries from participating in decisions regarding the exercise of any Tax-Sensitive Powers over any trusts as to which any other member of the committee exercising the power is the grantor or a beneficiary. The purpose of this rule is to avoid reciprocal arrangements among grantors and beneficiaries.

- The trust agreement establishing the FTC Trust should provide that the FTC will cease to serve as trustee of the FTC Trust or cease to possess any "Tax-Sensitive Powers" over the FTC Trust if the safeguards discussed are eliminated via by-law amendment. Alternatively, the instrument appointing the FTC as trustee should contain this limitation.

In addition, we suggest that consideration be given to imposing an additional requirement relating to the ownership of the FTC that must be satisfied to avoid attribution of trustee powers to individuals requiring that the ownership and control of the FTC not be concentrated in one person. The requirement could be, for example, that an ownership interest in an FTC will not result in attribution of the FTC's Tax Sensitive powers unless an individual owns directly or indirectly more than a specified percent of the voting interests of the FTC. For purposes of this test, an individual should be treated as owning a voting interest only if she actually has the power to exercise that interest's voting rights.

Our proposed guidelines are similar to the existing income and transfer tax rules that provide boundaries within which individual and institutional trustees have operated for many years. We believe that if these rules are incorporated into the proposed guidance, equal tax treatment for all grantors and beneficiaries will be available, regardless of whether an FTC, an independent trust company or an individual trustee is in control.

We appreciate your consideration of our recommendations and comments. We would be pleased to discuss these matters with you further or provide any other assistance that you would find helpful.

Respectfully submitted,



Kimberly S. Blanchard
Chair

Enclosure

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