

Internal Revenue Service

Department of the Treasury

Number: **200119023**
Release Date: 5/11/2001
Index Number: 2601.03-01

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:9-PLR-120670-00
Date:
February 6, 2001

Re:

Legend:

- Decedent =
- Spouse =
- Residuary Trust =
- Co-Trustees =
- Alternative Successor Trustees =
- Secondary Successor Trustee =
- New Successor Trustee =
- Children =
- Date =
- State =

Dear _____ :

This is in response to the letter submitted by your authorized representative, dated October 10, 2000, requesting a ruling concerning the generation-skipping transfer tax ("GSTT") consequences of the modification of a trust.

The facts as they have been represented are as follows: Decedent died testate

PLR-120670-00

on Date, several years prior to September 25, 1985, survived by Spouse and Children. Decedent's last will and testament established a marital trust for the benefit of Spouse and a residuary trust ("Residuary Trust"). The beneficiaries of Residuary Trust are Spouse, Children, the spouses of Children, and the issue of Children (collectively, "Beneficiaries").

Distributions from Residuary Trust are governed by Article Fourth of Decedent's will, which provides that the net income of Residuary Trust may, in the discretion of Co-Trustees, be distributed quarterly or more frequently to or among the beneficiaries in proportions and amounts determined by Co-Trustees, without regard to equality. Any income not distributed is to be added to principal. Co-Trustees may distribute the principal of Residuary Trust at any time, and in such amounts as they deem fit, to any beneficiary. Principal distributions are applied against the share of principal, if any, ultimately to be distributed to the relevant beneficiary.

Decedent's will further provides that, upon the death of Spouse, Residuary Trust is to terminate and separate and equal shares of the assets of Residuary Trust are to be distributed into separate trusts ("Issue Trusts"), one Issue Trust to be established for the benefit of each Child and such Child's descendants. Co-Trustees of Residuary Trust are to be the trustees of each Issue Trust. Co-Trustees are authorized to distribute the income and principal of the Issue Trusts to the relevant beneficiary or beneficiaries in the same manner that income and principal may be distributed under Residuary Trust. Upon the death of a Child, the relevant Issue Trust will terminate and the principal of such Issue Trust will be distributed per stirpes to the surviving issue of that Child or, if none, per stirpes to the surviving issue of Decedent.

The trustees of Residuary Trust (and of the eventual Issue Trusts) are designated and empowered under Article Thirteenth of Decedent's will, as follows:

I nominate, constitute and appoint [Co-Trustees], or the survivor of them, executors and trustees under this my last will and testament. I further direct that in the event that either executor and trustee shall fail to survive me or should fail, for any reason whatsoever, to serve as such executor and trustee, or, having begun to serve, shall cease to serve as such executor and trustee, then the survivor of such executors and trustees shall have the power and right to appoint, as co-executor and co-trustee under this, my last will and testament any of the [Alternative Successor Trustees]. I further direct that in the event that any two of the persons just named by me in this Article shall fail to survive me or fail, for any reason whatsoever, to serve as such executor and trustee, or having begun to serve, shall cease to serve as such executor and trustee, the survivor of such executors and trustees shall have the power and right to appoint, as co-executor and co-trustee, under this, my last will and testament, any one of the persons heretofore named.

PLR-120670-00

If there ever shall come a time thereafter when there is only one (1) surviving, qualified and acting executor and trustee, and every other person heretofore named in this Article is either dead or shall fail, for any reason whatsoever, to serve as such executor and trustee, or having begun to serve, shall cease to serve as such executor and trustee, then I nominate, constitute and appoint [Secondary Successor Trustee] co-executor and co-trustee under this my last will and testament. [Secondary Successor Trustee] may act as sole executor or trustee under this my last will and testament after the death or retirement of all other persons named in this Article.

State law provides that a trustee who has the absolute discretion under the terms of a testamentary instrument to invade the principal of a trust for the benefit of the income beneficiaries of the trust may exercise such discretion by appointing any amount or all of the principal of the trust in favor of a trustee of a trust under an instrument other than that under which the power to invade is created or under the same instrument with the consent of all persons interested in the trust and without prior court approval. Such an exercise of discretion may not reduce any fixed income interest of any income beneficiary and must be in favor of the beneficiaries of the trust. State law further provides, however, that except in the case of a trust that is revocable by such person during life, the trustee of a trust who is also, or becomes also, a beneficiary of the trust may not exercise any distribution or allocation powers to his or her own benefit.

Co-Trustees and Beneficiaries propose that Co-Trustees appoint all of the assets of Residuary Trust to a new trust ("New Trust"). New Trust will be governed by a trust document containing provisions identical to the provisions now governing Residuary Trust, including a provision terminating New Trust and creating Issue Trusts upon the death of Spouse, except that the successor trustee provision currently found in Article Thirteenth of Decedent's will would be modified in the following manner:

[Co-Trustees] shall serve as Trustees of all trusts held under this Declaration of Trust. Each Trustee is authorized, hereafter, at any time and from time to time, by an instrument in writing, signed and acknowledged, to appoint his/her successor and the successor's successors. In the event that [either of the Co-Trustees] ceases to serve as Trustee and has failed to exercise the power to appoint his/her own successor, or having appointed one or more successor Trustees all of such successors have either failed to qualify or ceased to serve as successor Trustee, the surviving Trustee shall appoint a Trustee to fill the vacancy in the office of the Trustee so occurring.

At all times there shall be two Trustees in office. In the event that there is at any time a vacancy in the office of Trustee (after applying the provisions of the previous paragraph), [New Successor Trustee] shall

PLR-120670-00

become a Trustee of this Trust. If at any time [New Successor Trustee] is serving as sole Trustee, [New Successor Trustee] is authorized by an instrument in writing, signed and acknowledged, to appoint a co-Trustee.

If at any time no Trustee is serving as such of a trust held hereunder and none has been designated in accordance with the foregoing provisions of this Article, a majority of the beneficiaries of such trust not under a legal disability (or if none, a majority of the natural or legal guardians of any beneficiary under a legal disability) shall appoint a successor Trustee to act.

Successor Trustees and co-Trustees shall assume all the responsibilities and have all the powers and authority of the original Trustees, including but not limited to the power to appoint successor Trustees, except that in the event of a conflict in the selection of a successor, the choices of earlier serving Trustees shall have precedence over the choices of later serving Trustees in the appointment of successors.

Any instrument appointing a successor Trustee shall be revocable by the appointing Trustee at any time prior to the designated successor having commenced serving as Trustee. In the event that the appointing Trustee shall have executed more than one instrument appointing a successor Trustee, then the instrument which shall bear the most recent date and shall be unrevoked shall govern.

Any Trustee, at any time in office, may resign by an instrument in writing, signed and acknowledged, delivered to his/her co-Trustee then in office.

Any Trustee may, at any time and from time to time, by an instrument in writing, delegate any or all of his/her rights, powers, duties, authority and privileges whether or not discretionary, to his/her co-Trustee, for such period or periods of time as may be specified in such written instrument, provided, however, that any Trustee who is granted any discretionary power hereunder may not delegate such discretionary power to any co-Trustee who is not granted such discretionary power.

It is represented that no additions to Residuary Trust, actual or constructive, have been made since the original funding of Residuary Trust at the time of Decedent's death.

The following rulings have been requested:

1. The proposed appointment of the assets of Residuary Trust to New Trust, with governing provisions identical to those governing Residuary Trust except for modification of the successor trustee provision, will not cause New Trust to be subject

PLR-120670-00

to the GSTT.

2. Issue Trusts, as established either under the provisions governing Residuary Trust or under the provisions to govern proposed New Trust, will not be subject to the GSTT.

Law and analysis:

Section 2601 of the Internal Revenue Code imposes a tax on every generation-skipping transfer.

Section 2611(a) defines a “generation-skipping transfer” as: (1) a taxable distribution; (2) a taxable termination; and (3) a direct skip.

Section 2612(a) defines a “taxable termination” generally as the termination (by death, lapse of time, release of power, or otherwise) of an interest in property held in a trust unless –

(A) immediately after such termination, a non-skip person has an interest in such property, or

(B) at no time after such termination may a distribution (including distributions on termination) be made from such trust to a skip person.

Section 2612(b) defines a “taxable distribution” as any distribution from a trust to a skip person (other than a taxable termination or a direct skip).

Section 2612(c)(1) defines the term “direct skip” to mean a transfer subject to a tax imposed by chapter 11 or 12 (estate or gift tax) of an interest in property to a skip person.

Section 2613(a) defines the term “skip person” to mean –

(1) a natural person assigned to a generation which is 2 or more generations below the generation assignment of the transferor, or

(2) a trust –

(A) if all interests in such trust are held by skip persons, or

(B) if –

(i) there is no person holding an interest in such trust, and

PLR-120670-00

(ii) at no time after such transfer may a distribution (including distributions on termination) be made from such trust to a non-skip person.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 and section 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the GSTT does not apply to any generation-skipping transfer under a trust (as defined in section 2652(b)) that was irrevocable on September 25, 1985.

Section 26.2601-1(b)(1)(ii)(A) provides, in general, that unless otherwise provided in section 26.2601-1(b)(1)(ii)(B) or (C), any trust in existence on September 25, 1985, is considered an irrevocable trust.

Section 26.2601-1(b)(1)(iv) provides that if an addition is made after September 25, 1985, to an irrevocable trust which is excluded from the generation-skipping transfer tax by reason of section 26.2601-1(b)(1), a pro rata portion of subsequent distributions from (and terminations of interests in property held in) the trust is subject to the generation-skipping transfer tax.

Section 26.2601-1(b)(4), T.D. 8912, ____ C.B. ____ (Dec. 19, 2000) (effective Dec. 20, 2000), in general, provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the generation-skipping transfer tax under section 26.2601-1(b)(1), (2), or (3) (hereinafter referred to as an exempt trust) will not cause the trust to lose its exempt status for generation-skipping transfer tax purposes.

Section 26.2601-1(b)(4)(i)(A) provides that the distribution of trust principal from an exempt trust to a new trust or retention of trust principal in a continuing trust will not cause the new or continuing trust to be subject to the generation-skipping transfer tax if –

(1) Either --

(i) The terms of the governing instrument of the exempt trust authorize distributions to the new trust or the retention of trust principal in a continuing trust, without the consent or approval of any beneficiary or court; or

(ii) at the time the exempt trust became irrevocable, state law authorized distributions to the new trust or retention of principal in the continuing trust, without the consent or approval of any beneficiary or court; and

(2) The terms of the governing instrument of the new or

PLR-120670-00

continuing trust do not extend the time for vesting of any beneficial interest in the trust in a manner that may postpone or suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date the original trust became irrevocable, extending beyond any life in being at the date the original trust became irrevocable plus a period of 21 years, plus if necessary, a reasonable period of gestation.

Section 26.2601-1(b)(4)(i)(D)(1) provides that a modification of the governing instrument of an exempt trust (including a trustee distribution, settlement, or construction that does not satisfy paragraph (b)(4)(i)(A), (B), or (C) of section 26.2601-1) by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust.

Section 26.2601-1(b)(4)(i)(E), Example 10, illustrates the application of paragraph (b)(4) as follows:

Administrative change to terms of a trust. In 1980, Grantor executed an irrevocable trust for the benefit of Grantor's issue, naming a bank and five other individuals as trustees. In 2002, the appropriate local court approves a modification of the trust that decreases the number of trustees which results in lower administrative costs. The modification pertains to the administration of the trust and does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the modification. In addition, the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. Therefore, the trust will not be subject to the provisions of chapter 13 of the Internal Revenue code.

Residuary Trust is a generation-skipping trust because it provides for distributions to beneficiaries who are more than one generation below Decedent's generation. Residuary Trust was in existence on September 25, 1985 and, pursuant to section 26.2601-1(b)(1)(ii)(A), is considered an irrevocable trust. It is represented that there have been no additions, actual or constructive, to the trust since that date. Accordingly, Residuary Trust has been exempt from the GSTT pursuant to section 26.2601-1(b)(1)(i).

Based on the facts submitted and representations made, the interests of the

PLR-120670-00

beneficiaries of Residuary Trust will remain the same under New Trust. The modification of Residuary Trust through transfer of its assets to New Trust effectuates an administrative change to the successor trustee provisions, and does not shift a beneficial interest in Residuary Trust to any beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the modification. The modification does not extend the time for vesting of any beneficial interest beyond the period provided for such vesting in the original trust. The timing of the termination of New Trust and of the creation of Issue Trusts under New Trust will remain the same as such timing under Residuary Trust.

Therefore, pursuant to section 26.2601-1(b)(4)(i)(D)(1), we conclude that the appointment of assets of Residuary Trust to New Trust, with the proposed modification of the governing successor trustee provision, will not cause distributions from New Trust or from any Issue Trust created under the governing provisions of New Trust to be subject to the GSTT. See also section 26.2601-1(b)(4)(i)(E), Example 10. This result does not, however, apply to any additions that might be made to New Trust or Issue Trusts (except for the original funding from Residuary Trust and New Trust, respectively) after September 25, 1985.

Except as specifically ruled herein, we express no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for the ruling, it is subject to verification on examination.

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 representative.

Sincerely,
Lorraine E. Gardner
Assistant Branch Chief
Branch 9
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure:

Copy for section 6110 purposes