

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:  
CC:PSI:4-PLR-129138-00

Date: September 12, 2001

Re:

Legend:

Trust =

Trustee =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Decedent =

Daughter =

Stock =

Grandchild 1 =

Grandchild 2 =

Grandchild 3 =

Great Grandchild 1 =

Great Grandchild 2 =

Great Grandchild 3 =

Court =

State =

Dear :

This is in response to a letter dated May 21, 2001 and prior correspondence submitted on your behalf by your authorized representatives, in which a ruling was requested concerning the generation-skipping transfer tax consequences of a proposed reformation of Trust.

Facts:

The facts are represented to be as follows: Decedent died testate on Date 1. Decedent's will was admitted to probate on Date 2. Under paragraph SIXTH of Decedent's will, Decedent established Trust for the benefit of Decedent's daughter (Daughter) and her descendants, to be funded with Stock, together with any rights of option or subscription, or otherwise, which may be incident to Stock. The trustees are to maintain Stock intact as a trust fund, and neither the whole nor any part of Stock is to be sold, encumbered, or in anyway disposed of so long as Daughter was alive, or so long as any child of hers living on Decedent's death was alive, and for twenty-one (21) years thereafter. On Date 3, however, due to changed circumstances, Court authorized and directed Trustee to transfer Stock in accordance with a certain purchase agreement and hold the consideration received therefrom subject to the terms of Trust.

Under the terms of paragraph SIXTH (a) of the will, for so long as Daughter is alive or so long as any child of Daughter then living survives, and for 21 years thereafter, Trust income is to be paid one-half to Daughter during her life and the other one-half to Grandchild 1, Grandchild 2, and Grandchild 3 and to their heirs of their mother's blood until the last survivor of Grandchild 1, Grandchild 2, and Grandchild 3 has died. Distributions are to be made quarterly.

Under paragraph SIXTH (b) of the will, upon the death of the last survivor of Grandchild 1, Grandchild 2, and Grandchild 3 (and after the death of Daughter), the corpus of Trust is to be divided into three equal parts and administered for twenty-one (21) years by the trustees, or their successor or successors as follows: the income from one part is to be paid quarterly to the heirs of Grandchild 1 of his mother's blood; the income from another part is to be paid quarterly to the heirs of Grandchild 2 of her mother's blood; and the income from the third part is to be paid quarterly to the heirs of Grandchild 3 of her mother's blood. Upon the expiration of twenty-one years after the death of the last survivor of Grandchild 1, Grandchild 2, and Grandchild 3, the trustees are to sell the corpus of Trust and divide the proceeds into three equal portions and pay one portion to the heirs of Grandchild 1 of his mother's blood, one portion to the heirs of Grandchild 2 of her mother's blood, and one portion to the heirs of Grandchild 3 of her mother's blood.

In the event, however, of the death of all three of Decedent's grandchildren, without leaving issue, the trustees are to administer Trust for Daughter, if she is alive, and upon her death, Trust is to be reduced to cash and paid to Decedent's heirs in accordance with the statute of descents and distribution. Likewise, in the event of the death of all three of Decedent's grandchildren, without leaving issue, if Daughter has predeceased them, Trust is to be reduced to cash and paid to Decedent's heirs in accordance with the statute of descents and distribution.

In the present case, Trust was irrevocable on September 25, 1985. It is represented that no additions or contributions have been made to Trust after that date. Daughter died survived by Grandchild 1, Grandchild 2, and Grandchild 3. Subsequently, Grandchild 2 died survived by three children, Great Grandchild 1, Great Grandchild 2, and Great Grandchild 3.

On Date 4, an order was signed by Court to reform paragraph SIXTH (a) and (b) of the will pursuant to State law. Under paragraph SIXTH (a) as reformed, Trustee is directed to pay quarterly the greater of Trust's annual net income or six percent (6%) of Trust's total value as determined on the first day of each year in equal shares to Grandchild 1, Grandchild 2, and Grandchild 3 and the heirs of a deceased grandchild of his or her mother's blood, until the death of the last to die of the survivor of Grandchild 1, Grandchild 2, and Grandchild 3. Under

Paragraph SIXTH (b) as reformed, upon the death of the last survivor of Grandchild 1, Grandchild 2, and Grandchild 3, the trust estate is to be divided into three equal parts. For a period of 21 years thereafter, Trustee is to distribute quarterly the greater of Trust's annual net income or six percent of Trust's total value as determined on the first day of each year as follows: one-third to the heirs of Grandchild 1 of his mother's blood; one-third to the heirs of Grandchild 2 of her mother's blood; one-third to the heirs of Grandchild 3 of her mother's blood.

Trustee requests a ruling that the reformation of Trust to provide for the annual distribution to Trust's income beneficiaries of the greater of Trust's annual net income or six percent of Trust's total value as determined on the first day of each year will not cause Trust to lose its exempt status for purposes of the generation-skipping transfer tax under § 2601.

#### Law and Analysis:

Section 2601 imposes a tax on each generation-skipping transfer made by a transferor to a skip person.

Under § 1433(a) of the Tax Reform Act of 1986, the generation-skipping transfer tax is generally applicable to generation-skipping transfers made after October 22, 1986. However, under § 1433(b)(2)(A) of the Tax Reform Act and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the tax does not apply to a transfer from a trust, if the trust was irrevocable on September 25, 1985, and no addition (actual or constructive) was made to the trust after that date. Under § 26.2601-1(b)(1)(ii), any trust in existence on September 25, 1985, will be considered irrevocable unless the settlor had a power that would have caused inclusion of the trust in his or her gross estate under §§ 2038 or 2042, if the settlor had died on September 25, 1985.

Section 26.2601-1(b)(4)(i) 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 will not cause the trust to lose its exempt status. The regulation provides that the rules contained in the paragraph are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. The rules do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(D)(1) and (2) provides that a modification 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 § 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. A modification will not result in the shift of a beneficial interest to a lower generation beneficiary if the modification does not result in an increase in the amount of a GST transfer or the creation of a new GST transfer.

In the present case, the proposed reformation of the method of distribution under Trust to provide for the distribution of the greater of Trust's annual net income or six percent of Trust's total value as determined on the first day of each year will not result in a shift of any beneficial interest in trust to any beneficiary who occupies a generation lower than the persons holding the beneficial interests prior to the reformation. See § 26.2601-1(b)(4)(i)(E), Example 8. Further, the proposed reformation will not extend the time for vesting of any beneficial interest

in the trust beyond the period provided for in Trust. Accordingly, based on the facts submitted and the representations made, the proposed reformation will not cause Trust to lose its exempt status for purposes of the generation-skipping transfer tax under § 2601.

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.

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. We are specifically not ruling on the gift tax and income tax consequences of the reformation.

The 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 yours,  
George L. Masnik  
Chief, Branch 4  
Office of Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosure  
Copy for section 6110 purposes