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Department of the Treasury

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CC:DOM:P&SI:4/PLR 104501-99

Date: July 27, 1999

Re:

Legend:

| | |
|----------------|---|
| Decedent | = |
| Trust 1 | = |
| Date 1 | = |
| Date 2 | = |
| Date 3 | = |
| Date 4 | = |
| State X | = |
| Trust A | = |
| Trust B | = |
| W | = |
| X | = |
| Y | = |
| Z | = |
| Bank M | = |
| Brother | = |
| Beneficiary 1 | = |
| Beneficiary 2 | = |
| Beneficiary 3 | = |
| Beneficiary 4 | = |
| Beneficiary 5 | = |
| Beneficiary 6 | = |
| Beneficiary 7 | = |
| Beneficiary 8 | = |
| Beneficiary 9 | = |
| Beneficiary 10 | = |
| Beneficiary 11 | = |
| Beneficiary 12 | = |
| Beneficiary 13 | = |
| Beneficiary 14 | = |
| Beneficiary 15 | = |
| Beneficiary 16 | = |
| Beneficiary 17 | = |
| Beneficiary 18 | = |
| Beneficiary 19 | = |
| Beneficiary 20 | = |
| Beneficiary 21 | = |
| Beneficiary 22 | = |
| Beneficiary 23 | = |
| Beneficiary 24 | = |

Beneficiary 25 =
Beneficiary 26 =
Beneficiary 27 =
Beneficiary 28 =
Beneficiary 29 =
Beneficiary 30 =
Beneficiary 31 =
Beneficiary 32 =
Beneficiary 33 =

This is in response to your letter dated February 16, 1999, in which you requested rulings on the application of the generation-skipping transfer (GST) tax provisions of Chapter 13 of the Internal Revenue Code with respect to proposed trust modifications.

According to your submission, Decedent died testate on Date 1, prior to September 25, 1985, a resident of State X. Pursuant to Article Four, § 4.1, of his will, Decedent exercised his limited power of appointment over property contained in Trust A, created on Date 2, and Trust B, created on Date 3. Pursuant to the exercise of these powers, the corpus of Trust A and the corpus of Trust B were combined and held as one trust (Trust 1) and distributed under the terms of such trust.

Pursuant to Article 4, § 4.2 of Decedent's will, the trustees of Trust 1 are to pay the income from Trust 1 quarterly, on a per capita basis, to the grandchildren of Decedent's father. Upon the death of each grandchild of Decedent's father, the income is to be paid to such grandchild's issue per stirpes. The share of income allotted to any grandchild dying without issue is to be divided pro rata among the surviving grandchildren and issue of deceased grandchildren then receiving income. The income will continue to be payable to the successive issue of Decedent's father until twenty-one years after the death of the last surviving issue of Decedent's father who was living on Date 2. Upon such date, Trust 1 will terminate, and the trustees are to distribute the principal to those beneficiaries then receiving income in such proportions as represent the percentage amount of income that each beneficiary was receiving on the date Trust 1 terminated.

Pursuant to Article Seven of Decedent's will, Decedent appointed W, X, Y, and Z as executors of his estate and as trustees of any trust established under the terms of Decedent's will. W, X, Y, and Z, as executors, are given the power to

appoint any corporate fiduciary as agent, custodian, co-executor, or co-trustee.

Under Article Eight of Decedent's will, the trustees are authorized to exercise the following powers in addition to those given by law:

- (A) To invest in, accept and retain any real or personal property, including stock of a corporate fiduciary or its holding company, without restriction to legal investments;
- (B) To sell, exchange, partition or lease for any period of time any real or personal property and to give options therefor for cash or credit, with or without security;
- (C) To borrow money from any person including any fiduciary acting under the will, and to mortgage or pledge any real or personal property;
- (D) To hold shares of stock or other securities in nominee registration form;
- (E) To engage in litigation and compromise, arbitrate or abandon claims;
- (F) To make distributions in cash, or in kind at current values, or partly in each, allocating specific assets to particular distributees on a non-pro rata basis, and for such purposes to make reasonable determinations of current values;
- (G) To determine the apportionment of receipts and expenses, including extraordinary cash dividends, stock dividends, capital-gain dividends of regulated investment companies and proceeds and expenses of the sale of unproductive real estate, between income and principal, such apportionment to be made so as to balance fairly the interests of any income beneficiary and remaindermen; and
- (H) To make elections, decisions, concessions and settlements in connection with all income, estate, inheritance, gift or other tax returns and the payment of such taxes, without obligation to adjust the distributive share of income or principal of any person affected thereby.

The trustees have no power to make discretionary distributions of corpus from Trust 1 to any beneficiary. Similarly, the trustees are not authorized to prematurely terminate or accelerate any beneficial interest in the trust property. Under the laws of State X, trustees must administer trust property so as to adequately protect and preserve the

respective interests of the income beneficiaries and the remaindermen of the trust.

On Date 4, Z resigned as a trustee of Trust 1.

It is represented that no additions (constructive or otherwise) have been made to Trust 1 since September 25, 1985.

The remaining trustees propose to petition the local court to:

(1) appoint Bank M as a co-trustee of Trust 1, with all rights, powers, duties, and responsibilities granted to the original trustees;

(2) establish procedures for the appointment of successor individual trustees. Specifically, when W or X becomes unable or unwilling to continue to serve as a trustee, for any reason whatsoever, the living children of W or X, as the case may be, and if none are able or willing to act, then the living grandchildren of W or X, who are at least 21 years of age, shall, by majority vote, appoint one of the lineal descendants of W or X, as the case may be, who is at least 21 years of age as a successor trustee. In the event such successor trustee, or any successor thereto, becomes unable or unwilling to act or continue as a successor trustee, for any reason whatsoever, the preceding sentence shall be reapplied as often as necessary. In the absence of a majority vote, the trusteeship will remain vacant until such time, if any, that the individuals entitled to select a successor trustee do so by majority vote. The individuals entitled to select a successor trustee shall have no power of any nature whatsoever to remove an individual once appointed;

(3) allow the descendants of Brother (Decedent's deceased brother who predeceased him), who are beneficiaries of Trust 1, to appoint a descendant of Brother as an additional trustee of Trust 1, and the successors thereto, in accordance with the same powers granted to the descendants of W and X provided above;

(4) provide that if Y is unable or unwilling to continue as a trustee, for any reason whatsoever, such vacancy will not be filled;

(5) provide that in the event no trustee is serving, a court of competent jurisdiction will appoint a corporate fiduciary as successor trustee; and

(6) permit the individual trustees serving from time to time, by majority vote, to remove the corporate trustee. The individual trustees may appoint, at any time, by majority vote, a

successor corporate trustee. The individual trustees are not required to appoint a successor corporate trustee. Any subsequently appointed successor corporate trustee would serve with the then-serving trustees, with all rights, powers, duties, and responsibilities granted to the original trustees.

You have requested the following rulings:

(1) The proposed modifications will neither create a general power of appointment under §§ 2041 or 2514 in W, X, Y, or Beneficiaries 1 - 33, by allowing such persons to participate in the appointment of additional or successor trustees or the removal and replacement of the corporate trustee, nor will the modifications cause the corpus of Trust 1 to be included in the gross estate of W, X, Y, or Beneficiaries 1 - 33;

(2) The appointment of trustees by Beneficiaries 1 - 33 will not be deemed to be transfers for federal gift tax purposes and will not constitute taxable gifts pursuant to § 2501;

(3) The proposed modifications to Trust 1 authorizing the appointment of additional and successor individual trustees and the removal and possible replacement of the corporate trustee will not cause the trust to lose status under § 1433 of the Tax Reform Act of 1986 as exempt from application of GST tax under Chapter 13 of the Code;

(4) The proposed modifications will not be treated as additions or constructive additions to Trust 1; and

(5) All distributions from, and upon the termination of, Trust 1 will be exempt from GST tax.

Ruling Requests # 1 and 2

Section 2041(a)(2) provides that the value of the gross estate shall include the value of all property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under §§ 2035 to 2038, inclusive. Section 2041(b) provides that the term "general power of appointment" means a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate.

Section 20.2041-1(b)(1) of the Estate Tax Regulations provides that if under the terms of a trust instrument, the trustee or his successor has the power to appoint the principal

of the trust for the benefit of individuals including himself, and the decedent has the unrestricted power to remove or discharge the trustee at any time and appoint any other person including himself, the decedent is considered as having a power of appointment. A power to amend only the administrative provisions of a trust instrument, which cannot substantially affect the beneficial enjoyment of the trust property or income, is not a power of appointment. The mere power of management, investment, custody of assets, or the power to allocate receipts and disbursements as between income and principal, exercisable in a fiduciary capacity, whereby the holder has no power to enlarge or shift any of the beneficial interests therein except as an incidental consequence of the discharge of such fiduciary duties is not a power of appointment.

Section 2501 imposes a tax on the transfer of property by gift by any individual.

Section 2511 provides, in part, that the tax imposed by § 2501 shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2514(b) provides that the exercise or release of a general power of appointment created after October 21, 1942, shall be deemed a transfer of property by the individual possessing such power. The definition of a general power of appointment under § 2514(c) is the same as provided in § 2041(b). Section 25.2514-1(b)(1) of the Gift Tax Regulations contains provisions similar to § 20.2041-1(b)(1), discussed above.

In this case, the powers exercisable by the trustees do not include any discretionary powers over either income or principal, and the trustees are prohibited from prematurely terminating or accelerating any beneficial interest in the trust. In view of the terms of the trust, modifying Trust 1 to permit individuals who may also be beneficiaries of Trust 1 to appoint, and be appointed as, additional or successor trustees, or to remove and replace the corporate trustee, will not have the affect of creating a general power of appointment in any such individual for purposes of §§ 2041 or 2514. Accordingly, the modifications will not cause the corpus of Trust 1, or any portion thereof, to be included in the gross estate of W, X, Y, or Beneficiaries 1 - 33 under § 2041. Compare, Rev. Rul. 95-58, 1995-2 C.B. 191, where the trustee had broad discretionary powers over trust income and corpus. Additionally, the appointment of trustees by Beneficiaries 1 - 33 will not be deemed transfers of property for federal gift tax purposes and will not constitute taxable gifts pursuant to § 2501.

Ruling Requests # 3, 4, and 5

Section 2601 of the Code provides that a tax is imposed on every generation-skipping transfer. Section 2611 defines the term "generation-skipping transfer" to mean a taxable termination, a taxable distribution, or a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (the Act), 1986-3 (Vol. 1) C.B. 1, and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the GST tax provisions of Chapter 13 will not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985, but only to the extent that the transfer is not made out of principal added to the trust after September 25, 1985 (or out of income attributable to principal so added).

Section 26.2601-1(b)(1)(v) describes "constructive" additions to trusts in certain situations involving powers of appointment and relief from liability.

In general, modifications that change the quality, value or timing of any of the powers, beneficial interests, rights or expectancies originally provided for under the terms of the trust instrument will cause an exempt trust to lose its exempt status.

In this case, the trustees of Trust 1 have represented that there have been no additions to Trust 1 after September 25, 1985. In addition, the proposed modifications relate to the appointment and replacement of successor trustees. Under the terms of Article Four of Decedent's will, the trustees of Trust 1 have no discretionary powers to distribute income or corpus to the beneficiaries, and the trustees are prohibited from prematurely terminating or accelerating any beneficial interest in the trust property.

We conclude that, based on the facts presented and the terms of Trust 1, the proposed modifications will not result in any change in the quality, value or timing of any beneficial interest in the trust. Consequently, the modifications will not affect the exempt status of the trust with respect to the generation-skipping transfer tax. Also, the proposed modifications will not be treated as additions or constructive additions to Trust 1. Therefore, provided that no additions, constructive or otherwise, are subsequently made to Trust 1, all distributions from, and upon the termination of, Trust 1 will be exempt from GST tax.

This ruling is based on the representations noted above and the facts and applicable law in effect on the date of this letter. If there is a change in material fact or law (local or Federal) before the transactions considered in this ruling take effect, the ruling will have no force or effect. If the taxpayer is in doubt whether there has been a change in material fact or

law, a request for reconsideration of this ruling should be submitted to this office.

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

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Assistant Chief Counsel
(Passthroughs and Special
Industries)

By _____
George Masnik
Chief, Branch 4

Enclosure
Copy for section 6110 purposes