

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
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Date:

December 16, 1999

Re:

Legend:

- Settlor 1 =
- Settlor 2 =
- Child =
- Grandchild =
- Trust 1 =
- Trust 2 =
- Trust 3 =
- Trust 4 =
- Consolidated Trust =
- Foundation =
- State =
- Date 1 =
- Date 2 =
- Date 3 =

Dear :

This is in response to your letter of April 29, 1999, and prior correspondence submitted by your authorized representative, in which you request several rulings on the application of the generation-skipping transfer (GST) tax provisions of Chapter 13 of the Internal Revenue Code.

On Date 1, Settlor 1 created Trust 1, an irrevocable inter vivos trust, for the benefit of Child. Under the terms of Trust 1, the trustees are to pay the net income of Trust 1 to Child for life. The trustees are also authorized to pay over to Child such part or all of the trust principal as the trustees deem advisable. At Child's death, the trust terminates and the principal is to be distributed to Child's issue per stirpes. If there are no issue of Child, then living, the principal is to be distributed to Settlor 1's issue per stirpes. If there are no living issue of Settlor 1, then the proceeds are to be distributed to Foundation. If any child or grandchild of Settlor 1 living on the date of the creation of

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the trust (Date 1) becomes entitled to any part of the principal upon Trust's termination, then the trustee, in his sole discretion, may add the principal to the trusts Settlor 1 created concurrently for such child or grandchild, instead of distributing such principal outright. Child died in 1996, and the Trust 1 corpus was distributed to Trust 2 which was created concurrently with Trust 1 for the benefit of Grandchild. Under Trust 2, all trust income is to be paid to Grandchild for life, and the trustee has the discretion to distributed corpus, as deemed advisable, to Grandchild. On Grandchild's death the trust corpus is to be distributed to Grandchild's issue, per stirpes. If there are no issue of Grandchild, the principal is to be distributed to Child's issue per stirpes. If Child has no issue, then the principal is to be distributed to Settlor 1's issue per stirpes. If there are no living issue of Settlor 1, then the proceeds are to be distributed to Foundation.

Settlor 1 died on Date 2. Trust 3, a testamentary trust, was created under Article THIRD paragraphs 5 (a) and 7 of Settlor's will. A separate share was set aside for the benefit of Child to be held as a separate trust. Child is to receive the net income for life. Upon Child's death, the net assets of the trust are to be divided into separate shares for her issue, per stirpes. Under the trust terms, if the beneficiary was not living at Settlor 1's death, that beneficiary's share is to be paid outright. If the beneficiary was living at Settlor's death, then the beneficiary is to receive income for life and on the beneficiary's death the corpus is to be divided into equal shares for each surviving issue of the beneficiary. If the surviving issue was not living on the death of Settlor 1, the share is to be paid to that issue outright. However if the issue was living at the death of Settlor 1, the share is to be held in further trust for the issue. The issue is to receive income for life and at death, the corpus is to pass to the beneficiary's surviving issue, per stirpes. However, if any male issue of Child has predeceased him leaving a widow then surviving, the trustees are directed to hold that share in trust for the benefit of the widow. If no issue of Child shall survive Child but Child leaves a widow, the trustees are to hold the Child's entire share in trust for Child's widow. If Child dies leaving no issue or widow surviving, but a widow or widows of one or more deceased male issue of Child shall be surviving, the trustees are to divide Child's share into separate and equal shares for each surviving widow, or all for the survivor if the widow of only one deceased male issue shall be surviving. A widow receives the income for life. At her death, the net assets pass to Settlor 1's issue, per stirpes, provided that if any such issue is then a life beneficiary of a trust created under the will, that issue's share is to be added to the principal of that trust. With respect to all trusts created under Article THIRD, Trustee has the absolute discretion to pay or apply to the use of the life beneficiary any or all of the trust principal. If there are no issue surviving, then the net assets are to be paid to Foundation. Grandchild was the only issue living at the date of death of Child and is the current life beneficiary under the provisions of Trust 3.

Settlor 2, the wife of Settlor 1, established Trust 4, an irrevocable inter vivos trust, for the benefit of Child on Date 3. Child is to receive income for life. At Child's death, Trust 4 is to be divided into separate trusts for the surviving issue of Child, per stirpes. The issue for which the trust is established (designated the primary beneficiary)

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is to receive trust income for life. On the death of the primary beneficiary, the corpus is to be divided into equal shares, per stirpes, for the benefit of the primary beneficiary's issue (designated the secondary beneficiaries) for life. On the death of the secondary beneficiary, the principal is to be distributed to the issue of the secondary beneficiary, per stirpes. If there is in existence under any trust agreement executed by Settlor 2, a trust for the benefit of any issue of the secondary beneficiary who becomes entitled to receive trust corpus, then the corpus is to be distributed to that trust, rather than being paid outright to the beneficiary. As noted, Child died in 1996. Grandchild is currently the life beneficiary of Trust 4.

Each trust created under the terms of the Trust 4 agreement must terminate in all events 21 years after the death of the last survivor of the individual beneficiaries living at the date of the agreement. On termination, the trust property is to be distributed to the then current life beneficiary. If Child or a primary beneficiary, or a secondary beneficiary has no surviving issue, Trust 4 is to be divided into equal trust shares for the surviving issue of Settlor 2. If there are no surviving issue of Settlor 2, then the net assets are to be distributed to Foundation. The trustee has the absolute discretion to pay to or apply for the use of the life beneficiary such amounts of corpus as the trustee deems advisable.

It is represented that no issue of Settlor 1 and Settlor 2 were born between Date 1 and Date 3. All three trusts are administered under the laws of State. Under State law a trustee who is a beneficiary of the trust, cannot exercise the trustees' discretionary power to distribute trust corpus to himself or herself.

The Trustees of Trusts 2, 3, and 4 propose to merge the trusts into Consolidated Trust. Consolidated Trust will be governed by the laws of State and will contain substantially similar provisions to Trust 2, Trust 3, and Trust 4. Specifically, a fraction of the Consolidated Trust will be set aside to fund the contingent widow's interest provided under Trust 3. In addition, a separate share determined under a specified formula shall be set aside and distributed outright at the death of Grandchild to beneficiaries of Trust 2 and Trust 3 who were not living on Date 1. The Trustees also propose to authorize the trustees to designate successor trustees. Under the proposal, no more than three trustees may serve at any one time. At least one trustee must not be a descendant of Settlor 2. No trustee who is a beneficiary of Consolidated Trust may participate in any determination by the trustees as to payment of principal to himself as a beneficiary. Consolidated Trust will terminate 21 years after the death of the last survivor of such individual beneficiaries living on Date 1 (the date Trust 1 was established).

In all other respects, the terms of Consolidated Trust will be identical to the terms of Trusts 2, 3, and 4.

It is represented that Consolidated Trust will be administered under the laws of

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State.

You represent that the Trusts 2, 3, and 4 were created before September 25, 1985, and that there have been no actual or constructive additions to the trusts after that date.

You have requested the following rulings:

1. Trusts 2, 3, and 4 are exempt from the GST Tax imposed by §2601 because the trusts were irrevocable on or before September 25, 1985.
2. The proposed consolidation of Trusts 2, 3, and 4 into Consolidated Trust, will not subject Trust 2, 3 or 4 or Consolidated Trust, or any distributions from Trust 2, 3, or 4 or from the Consolidated Trust, to the GST tax.
3. Following the proposed consolidation of Trust 2, 3, and 4 into Consolidated Trust, Consolidated Trust will be exempt from the GST tax.
4. The consolidation of Trust 2, 3, and 4 into Consolidated Trust will not constitute an actual or constructive addition to any of the trusts.

Section 2601 imposes a tax on every generation-skipping transfer.

Under § 1433(b)(2)(A) of the Tax Reform Act of 1986 (the 1986 Act) and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the generation-skipping transfer tax shall not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985, but only to the extent that such transfer is not made out of corpus added to the trust after September 25, 1985 (or out of income attributable to corpus so added).

Section 26.2601-1(b)(1)(iv)(A) provides that if an addition (actual or constructive) is made after September 25, 1985, to an irrevocable trust, which is excluded from the application of Chapter 13 by § 1433(b)(2)(A) of the 1986 Act, a pro rata portion of subsequent distributions from (and terminations of interests in property held in) the trust is subject to the provisions of Chapter 13.

Section 26.2601-1(b)(1)(v)(A) provides that where any portion of a trust remains in the trust after the post-September 25, 1985, release, exercise, or lapse of a power of appointment over that portion of the trust, and the release, exercise or lapse describes "constructive" additions to trusts in certain situations involving powers of appointment and relief from liability.

A modification of a generation-skipping trust that is otherwise exempt from GST tax under § 1433 (b) (2) of the 1986 Act will generally result in a loss of its exempt or

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"grandfathered" status, if the modification changes the quality, value, or timing of any powers, beneficial interests, rights, or expectancies originally provided for under the terms of the trust.

In this case, Trusts 2, 3 and 4 were created and irrevocable before September 25, 1985. Also, it is represented that no additions (actual or constructive) have been made to the trusts since September 25, 1985. Consequently, Trusts 2, 3, and 4 are currently exempt from GST tax. As proposed, the substantive and dispositive provisions of Consolidated Trust will be identical to those of Trusts 2, 3, and 4. In addition, you represent that Consolidated Trust will be administered in accordance with the laws of State. Accordingly, we conclude that the proposed merger of Trust 2, 3 and 4 into Consolidated Trust will not change the quality, value or timing of any power, beneficial interest, right or expectancy originally provided for under the terms of Trusts 2, 3, and 4. The provision regarding the power to name a successor trustee is administrative in nature and does not effect the quality, value or timing of any beneficial interest originally provided for under the terms of Trusts 2, 3, and 4.

We conclude that the proposed transaction will not result in an actual or constructive addition and will not cause Trusts 2, 3, and 4, or the new Consolidated Trust to be subject to the provisions of Chapter 13.

In accordance with the power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

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 yours,
Assistant Chief Counsel
(Passthroughs and Special Industries)
By George Masnik, Chief, Branch 4

Enclosure
Copy for 6110 purposes