

**Internal Revenue Service**

Department of the Treasury

Index Number: 1001.02-00, 2501.01-00,  
2601.00-00

Washington, DC 20224

Number: **200021007**  
Release Date: 5/26/2000

Person to Contact:

Telephone Number:

Refer Reply To:  
CC:DOM:P&SI:7-PLR-113222-99  
Date:  
January 28, 2000

LEGEND:

Trust =

a =

Daughter =

Granddaughter 1 =

Granddaughter 2 =

Granddaughter 3 =

Grandson =

Great-Grandson 1 =

Great-Grandson 2 =

Great-Grandson 3 =

Great-Granddaughter =

b =

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c =d =

Son =

e =f =g =

Court =

h =

Trust A =

Trust B =

Trust C =

Trust D =

Trust E =

i =

Dear Sir or Madam:

In a letter, dated July 27, 1999, you requested several rulings concerning the income, gift, and generation-skipping transfer (GST) tax consequences of the partitioning of the Trust. This letter responds to your request.

The information submitted and the representations made are summarized as follows: Decedent created the Trust on a for the benefit of Daughter, Granddaughter 1,

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Granddaughter 2, Grandson, Great-Grandson 1, Great-Grandson 2, Great-Grandson 3, and Great-Granddaughter. The Trust was amended on b.

Article III, Paragraph B of the Trust provides that from and after the death of Decedent, the trustee is to pay the entire net income of the Trust estate to Daughter, so long as she shall live, on the c day of each month (the income distribution date).

Paragraph C of Article III of the Trust provides that from and after the death of the last to survive of Decedent and Daughter and continuing until the death of the last to survive of Decedent's grandchildren, Granddaughter 1, Granddaughter 2, and Grandson, and Decedent's great-grandchildren, Great-Grandson 1, Great-Grandson 2, Great-Grandson 3, and Great-Granddaughter, the trustee is to pay the entire net income on the income distribution date in equal shares to those of Granddaughter 1, Granddaughter 2, and Grandson who are living on each income distribution date, and to the lawful issue living on each income distribution date of Grandchildren who are then deceased leaving one or more lawful issue then living, the issue of a deceased Grandchild in each case to take among them, *per stirpes*, the share of the net income the Grandchild would take were she or he then living.

Paragraph D of Article III of the Trust provides that on the death of the last to survive of the Grandchildren and Great-Grandchildren named in Paragraph C of Article III, the trustee is to pay and distribute the principal of the Trust estate in equal shares *per stirpes* to the then living lawful issue, if any, of the Great-Grandchildren named in Paragraph C of Article III, of whom issue is then living.

Article III, Paragraph E of the Trust provides that if under this or any other Article of the Trust, any portion of the principal of the Trust estate becomes payable to issue of any of Decedent's above-named Grandchildren who is, at the time of the distribution, less than d years of age, that portion is to immediately vest in the issue, but distribution thereof is to be postponed by the trustee until the issue attains the age of d years and, in the meantime, the trustee is to pay the net income of that portion to the issue.

Paragraph F of Article III of the Trust provides that each and every trust, if any, still in existence on the day d years after the death of the last to survive of Decedent, and all of the beneficiaries named or described in the Trust, is to terminate forthwith and the trustee is to pay and distribute the trust or part to the then income beneficiary thereof. If there is more than one income beneficiary, the distribution is to be made to the beneficiaries in the proportions in which they are then receiving the income.

Article III, Paragraph G of the Trust provides that whenever and as often as any beneficiary under the Trust, other than Daughter, is under a legal disability or in the opinion of the trustee is unable to apply all or any part of the payments herein provided to be made to him or her, the trustee may make the payments in any one or more of the following ways: (1) directly to the beneficiary; (2) to the guardian or other legal



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2. Granddaughter 2                    e percent
3. Granddaughter 3                    e percent
4. Great-Grandson 3                  g percent
5. Great-Granddaughter              g percent

In order to facilitate the proper management of the respective shares of the Trust so that the management coincides with the investment consultant/beneficiary pursuant to Article III, Paragraph I of the Trust, a petition to partition the Trust into separate, independent shares was filed with the Court. After proper notice to all interested parties and hearing of the petition, the Court entered its order (the Order) on h. The Court ruled that based on the provisions of Article III of the Trust, it was Decedent's intent that the trust eventually would be administered and managed as separate independent shares for each net income beneficiary and his or her family. In order to carry out Decedent's intent and for each income beneficiary to effectively act as the investment consultant over his or her respective share, the Court divided the Trust by family blood lines into five separate trusts as follows:

1. Trust A as to an e percent interest;
2. Trust B as to an e percent interest;
3. Trust C as to an e percent interest;
4. Trust D as to a g percent interest; and
5. Trust E as to a g percent interest

In order to satisfy the income distribution requirements set forth in Paragraph C of Article III of the Trust, if an income beneficiary is deceased on an income distribution date, then the deceased beneficiary's then living issue shall be entitled to the net income the deceased beneficiary would have received if then living. Additionally, if an income beneficiary dies without leaving issue then living at an income distribution date, then the net income that would have been distributed to the person(s) who so die without leaving issue instead is to be distributed pro rata to the other income beneficiaries with reference to the beneficial percentage interests then held pursuant to Paragraph C of Article III of the Trust.

In order to satisfy the ultimate distribution requirements set forth in Paragraph D of Article III of the Trust, upon the ultimate distribution of the Trust estate pursuant to Paragraph D, each of the separate trusts to be created for the e percent beneficiaries is required to allocate and distribute two j percent fractional shares as follows:

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- (i) one j percent share to Trust D, and
- (ii) one j percent share to Trust E.

The trustees of Trust D and Trust E would be required to distribute these j percent shares to the remaindermen beneficiaries as part of the trust estates of the separate trusts.

It is represented that the Trust was irrevocable on September 25, 1985, and there have been no additions to it since that date.

You have requested the following rulings:

1. The partition of the Trust in accordance with the Order will not constitute a taxable disposition of the Trust assets for purposes of § 1001 of the Internal Revenue Code.

2. The partition of the Trust will not result in a transfer by any beneficiary of the Trust that is subject to the gift tax under § 2501.

3. The separate trusts resulting from the partition of the Trust will not be subject to the GST tax.

Ruling No. 1:

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

For purposes of § 1001, in an exchange of property, each party to the exchange gives up a property interest in return for a new or additional property interest.

Section 1.1001-1(a) of the Income Tax Regulations provides that the gain or loss realized from an exchange of property for other property differing materially either in kind or extent, is treated as income or as loss sustained. Such an exchange is a disposition under § 1001(a). See § 1.1001-1 of the Regulations.

An exchange of property results in the realization of gain or loss under § 1001 if the properties exchanged are materially different. Cottage Savings Association v. Commissioner, 499 U.S. 554 (1991). There is a material difference when the exchanged properties embody legal entitlements "different in kind or extent" or if they confer "different rights and powers." 499 U.S. at 565.

As ordered by Court, the partition of Trust into five shares to be administered as five separate trusts has been structured to satisfy the income distribution requirements,

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as well as the ultimate distribution requirements, of the original trust agreement. The legal entitlements, as well as the rights and powers, of the income beneficiaries and the remainder beneficiaries will remain essentially the same in kind or extent after partition of Trust. Thus, there will be no material difference in the positions of beneficiaries of Trust after the partition of Trust into five shares that are to be treated as five separate trusts.

We conclude that partitioning of the trust into five shares to be administered as separate trusts will not cause the new trusts, or their beneficiaries to realize any gain or loss from a sale or disposition under § 1001.

Ruling No. 2:

Section 2501(a) imposes a tax for each calendar year on the transfer of property by gift during the calendar year by any individual, resident or nonresident.

Section 2511(a) provides that the tax imposed by § 2501 applies 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 2512(a) provides that if the gift is made in property, the value thereof at the date of the gift is considered the amount of the gift.

Section 2512(b) provides that where property is transferred for less than an adequate and full consideration in money or money's worth, then the amount by which the value of the property exceeded the value of the consideration is deemed a gift, and is included in computing the amount of gifts made during the calendar year.

Based on the information submitted and the representations made, we conclude that the partition of the Trust will not result in a transfer by any beneficiary of the Trust that is subject to the gift tax under § 2501.

Ruling No. 3:

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

Section 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provides that the tax does not apply to any generation-skipping transfer under a trust (as defined in § 2652(b)) that was irrevocable on September 25, 1985. The rule of the preceding sentence does not apply to a *pro rata* portion of any generation-skipping transfer under an irrevocable trust if additions are made to the trust after September 25, 1985.

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Section 26.2601-1(b)(1)(ii) provides that, except as provided in § 26.2601-1(b)(1)(ii)(B) or (C), any trust in existence on September 25, 1985, is considered an irrevocable trust.

Section 2611(a) defines the term "generation-skipping transfer" as (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 26.2611-1 provides that a generation-skipping transfer is an event that is either a direct skip, a taxable distribution, or a taxable termination. The determination as to whether an event is a generation-skipping transfer is made by reference to the most recent transfer subject to the estate or gift tax.

Section 2612(c)(1) defines the term "direct skip" to mean a transfer subject to a tax imposed by chapter 11 or 12 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 that is two 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 the trust, and

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

The Trust is a generation-skipping trust because it provides for distributions to more than one generation of beneficiaries below Decedent's generation. The Trust, however, has been exempt from the GST tax pursuant to § 26.2601-1(b)(1)(i) because it was irrevocable on September 25, 1985, and there have been no additions to it since that date. You have requested a ruling that the partition of the Trust into a separate trusts will not cause the resulting sub-trusts to be subject to the GST tax.

An amendment to an exempt trust that modifies or otherwise changes the quality, value, or timing of any of the powers, or beneficial interests, rights, or

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expectancies originally provided under the terms of the trust will cause the trust to lose its exemption from the GST tax. A trust's exemption from the GST tax is not affected, however, by amendments relating to the administration of a trust.

Based on the information submitted and the representations made, the interests of the income beneficiaries under the partition of the Trust, will remain the same and the timing of the termination of the trusts will remain the same. Consequently, the value of the income or corpus interest of each income beneficiary will not change materially as a result of the partition of the Trust. Therefore, the partition of the Trust will not change the quality, value, or timing of any powers, beneficial interests, rights, or expectancies originally provided for under the terms of the Trust. Accordingly, we conclude that the partition of the Trust will not cause distributions from the resulting trusts to be subject to GST tax imposed by chapter 13, provided that no additions are made to the trusts after September 25, 1985.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) 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 yours,  
Christine E. Ellison  
Chief, Branch 7  
Office of the Assistant Chief Counsel  
(Passthroughs and Special Industries)