



Date 3 =  
 Bank =  
 Date 4 =  
 Date 5 =  
 Corporate Trustee 2 =  
 Date 6 =  
 Court =  
  
 State Statute 2 =  
 Corporation 2 =  
 Individual =  
 State Statute 3 =

Dear :

This is in response to your letter dated August 9, 2003, submitted on behalf of the trustee of the Trust, requesting rulings regarding the estate and generation-skipping transfer (GST) tax consequences of a proposed modification to a trust that is exempt from the application of the GST tax imposed under § 2601 of the Internal Revenue Code.

The information submitted and representations made are summarized as follows: Taxpayer established the Trust on Date 1, for the primary benefit of his children, Child 1, Child 2, and Child 3. Taxpayer funded the Trust with a shares of stock in Corporation 1. Article I of the Trust provides that the Trust shall be irrevocable.

Article II provides that the trustees shall divide the corpus of the Trust into three equal separate shares with one share for Child 1 (Subtrust A), one share for Child 2 (Subtrust B), and one share for Child 3 (Subtrust C). Each share shall constitute and be administered as a separate trust ("subtrust").

Article IV provides for the administration and disposition of the subtrusts. Article IV, paragraph A provides that the trustees shall distribute to or for the benefit of the beneficiary of a subtrust all of the income of her subtrust, quarter-annually or more frequently. Article IV, paragraph B provides that the trustees shall distribute to or for the benefit of the beneficiary of a subtrust so much of the corpus of her subtrust as the trustees may deem necessary or advisable for her education and maintenance in health and reasonable comfort; provided, however, that so long as the corpus of a subtrust shall consist of any stock in Corporation 1, or any successor, there shall be no corpus distribution pursuant to this paragraph B from the portion of the corpus consisting of Corporation 1 stock. The trustees shall not be required to liquidate the stock for distributions.

Article IV, paragraph E provides that a beneficiary's subtrust shall terminate upon the earlier of (i) the date when all of that subtrust shall have been distributed or (ii) the death of that beneficiary.

Article IV, paragraph F provides that if any beneficiary of a subtrust dies before complete distribution of her subtrust, then upon the death of that beneficiary, the corpus of each subtrust shall be distributed to that beneficiary's descendants, per stirpes, or if none, then per stirpes to Taxpayer's daughters who were named in Article II, or if none, then to Grandchild, if he is then living, but if not, then to Taxpayer's heirs-at-law.

Article VII, paragraph A provides that if Trustee 1 or Trustee 2 shall die or otherwise be unable or unwilling to serve, then the survivor shall serve as the sole trustee. If both Trustee 1 and Trustee 2 die or otherwise are unable or unwilling to serve, then Corporate Trustee 1 shall serve as the sole trustee. In the event that Trustee 1 and Trustee 2, or the survivor, are trustees and sell any of the stock in Corporation 1 or any successor that they own as trustees, then thereafter Bank 1 shall serve as a co-trustee along with Trustee 1, if he is then serving, with Trustee 2 ceasing to serve as a trustee, but if Trustee 1 is not then serving, then Trustee 2 shall serve with Bank 1. If at any time there is no trustee serving as a trustee of the subtrusts, then a majority of the adult beneficiaries of the subtrusts and the guardians of the property of any minor beneficiaries of the subtrusts shall appoint a corporate trustee.

Article VII, paragraph B provides that if Trustee 1 or Trustee 2 and a corporate trustee are then serving as trustees, then the corporate trustee shall have sole custody of the cash proceeds of the sale of any stock in Corporation 1 or any successor and any investments of the net proceeds.

Article VII, paragraph F provides, generally, that to the extent permitted by law, Taxpayer waives compliance by the trustees with all of the provisions of State Statute 1 and any law requiring qualification, administration or accounting to any court.

Article VII, paragraph G provides that if a corporate trustee is serving as trustee of the subtrusts, then the corporate trustee may be changed at any time by a majority of the adult beneficiaries of the subtrusts and the guardians of the property of the minor beneficiaries of the subtrusts appointing another corporate trustee, provided, however, that such change shall be effective only if: (i) the successor corporate trustee has assets under its management which are at least equal to those of its predecessor; (ii) such successor consents in writing to the appointment; and (iii) the individual trustee consents if there is one then serving as a co-trustee.

Article VIII, paragraph A provides that the powers of administration, within the meaning of § 675(4) of the Internal Revenue Code, as are granted to the trustees with respect to the entire trust or any subtrust shall never be exercised for the benefit of Taxpayer or any person other than the beneficiaries of the Trust.

Article VIII, paragraph C provides that notwithstanding the powers granted to the trustees, the Trust and any subtrust have not been established to discharge any legal obligation of support Taxpayer may have for the beneficiaries of the subtrusts or any other person. Any amounts distributed from the Trust or any subtrust to a daughter of Taxpayer or any other person are not intended to be, and shall not be made, in lieu or in discharge of any obligation Taxpayer may have for support of that daughter or person. Taxpayer shall have no right to require or demand that any income or corpus of the Trust or any subtrust be used to support or maintain any of his daughters or any person whom he is legally obligated to support.

Article VIII, paragraph D provides that no power enumerated herein shall be construed to enable the trustees to apply any part or all of the income or corpus of the Trust or any subtrust to the payment of premiums on policies of life insurance on the life of Taxpayer or his spouse.

Article VIII, paragraph E provides that Taxpayer shall have no right to exercise any voting rights with respect to any stock held by the trustees when such retention is considered to be a retention of the enjoyment of such stock under § 2036(a) of the Internal Revenue Code.

Trustee 2 resigned as co-trustee on Date 2. Trustee 1 resigned as trustee on Date 3. Corporate Trustee 1 merged into a different financial institution, Bank. Bank declined to serve as trustee on Date 4. Pursuant to Article VII, paragraph A of the Trust, on Date 5, all of the adult beneficiaries of the subtrusts (Child 1, Child 2, and Child 3) appointed Corporate Trustee 2 to serve as successor trustee. Corporate Trustee 2 accepted its appointment on Date 6.

Taxpayer and the current income beneficiaries, with the consent of the adult remainder beneficiaries, a parent of each remainder beneficiary who is a minor and the guardian ad litem for such minor beneficiaries, and the trustee of the Trust have filed a complaint in Court to modify the Trust. Since the Trust holds stock in Corporation 1, a family operated business, Taxpayer seeks to modify the trustee succession provisions of the Trust to allow Taxpayer or other family members to control the removal and appointment of trustees and to enable Taxpayer's daughters to vote and make decisions regarding the disposition of the stock of Corporation 1 owned by the Trust.

Pursuant to the proposed modification, Article VII, paragraphs A and B will be modified to provide as follows. Article VII, paragraph A.1. will provide, generally, that notwithstanding any provisions herein to the contrary, Taxpayer, during his lifetime, shall have the right to appoint one or more individual and/or qualified successor corporate trustees to serve as co-trustees with the then serving trustee upon written notice to the then serving trustee; and to remove any trustee (including but not limited to Corporate Trustee 2) then serving or designated as a successor at any time and for any reason, upon written notice to that trustee and to appoint one or more individual and/or qualified successor corporate trustee (the "Appointment and Removal Power").

Notwithstanding any other provisions of this paragraph: (i) Taxpayer shall only appoint a trustee that is not related or subordinate to Taxpayer within the meaning of § 672(c) of the Internal Revenue Code and in accordance with the provisions of Revenue Ruling 95-58; and (ii) any individual trustee appointed by Taxpayer must have attained the age of twenty-five years, must have graduated from an accredited university or college in the United States of America with at least a baccalaureate degree, and must not be disqualified from serving as a personal representative pursuant to State Statute 2. In no event may Taxpayer appoint himself as trustee or co-trustee of the Trust or of any subtrust. The power retained by Taxpayer in Article VII, paragraph A is personal to Taxpayer and shall not be exercised by a guardian of Taxpayer or by Taxpayer's attorney-in-fact acting under a durable power of attorney. Taxpayer may renounce the Appointment and Removal Power, in whole or in part, by a written instrument delivered to the then serving trustee.

Article VII, paragraph A.2. will provide that in the event of Taxpayer's death, incapacity or renunciation of the Appointment and Removal Power, the Appointment and Removal Power may be exercised with respect to each separate subtrust by a majority in number of: (i) the then living adult income or principal beneficiary, whether discretionary or mandatory, of the separate subtrust (and the guardian of the property of any living minor income or principal beneficiary, whether discretionary or mandatory, of the separate subtrust); and (ii) the adult remainder beneficiaries of such separate subtrust who would become current income and/or discretionary beneficiaries immediately upon the death of the current income or principal beneficiary if the current income or principal beneficiary died at the time of the exercise of the Appointment and Removal Power. The Appointment and Removal Power may be exercised by such beneficiaries without obtaining the consent of any other beneficiary; provided, however, that such beneficiaries (and/or guardian, as the case may be) may not remove the "Special Trustee," may only appoint a qualified successor corporate trustee that is not related or subordinate to Taxpayer (during his lifetime) or the beneficiaries within the meaning of § 672(c) of the Internal Revenue Code and in accordance with the provisions of Revenue Ruling 95-58, and may only exercise that power a total of five times during each ten-year period. Any person vested with the Appointment and Removal Power may, at any time, renounce that power by a written instrument delivered to the then serving trustee.

Article VII, paragraph A.3. will provide that the power to designate successor trustees may be exercised in such a manner so as to designate or appoint different successor trustees for each of the separate subtrusts created hereunder. Any such designation or appointment may be exercised by an instrument in writing signed by the holder of the Appointment and Removal Power and delivered to the then acting trustee and to the beneficiary of the separate subtrust for which a successor trustee is being designated, with a copy to the designated successor trustee.

Article VII, paragraph A.4. will provide that notwithstanding anything contained herein to the contrary, the power to remove and replace trustees shall only be

exercisable to the extent that the possession of such power or its exercise will not result, in and of itself, in the inclusion of the assets of the Trust or any subtrust in the gross estate of Taxpayer or any beneficiary, or adversely affect the exempt status of the Trust or any subtrust for purposes of the GST tax under § 2601 of the Internal Revenue Code.

Article VII, paragraph A.5. will provide that a qualified successor corporate trustee shall mean a bank or trust company authorized to administer trusts in State and shall have: (i) total capital funds of at least fifty million dollars; or (ii) trust or other investment assets under management of a value of at least one billion dollars.

Article VII, paragraph B will provide that during such time as the Trust or any subtrust owns shares of Corporation 2 (which is the successor corporation to Corporation 1) or any successor company to Corporation 2, or any company into which Corporation 2 may have been merged subsequent to the date of this instrument ("Company"), Taxpayer's daughters, Child 1, Child 2, and Child 3, shall serve as "Special Trustees" of the Trust and each subtrust.

Article VII, paragraph B.1. will provide that during such time as Child 1, Child 2, and Child 3 serve as Special Trustees, all action taken by the Special Trustees shall be by majority vote. Article VII, paragraph B.1.a. will provide that in the event that any one of Taxpayer's daughters shall cease to serve as Special Trustee for any reason, then all action taken by the remaining Special Trustees shall be by unanimous agreement of the Special Trustees. In the event that the remaining Special Trustees are unable to agree upon any particular decision which must be made by them in their fiduciary capacity as Special Trustees, the tie breaking vote shall be made by Individual.

Article VII, paragraph B.1.b. will provide that in the event that only one of Taxpayer's daughters is able to serve and is serving as Special Trustee, then Individual shall serve as a successor Special Trustee along with Taxpayer's daughter who is then serving as Special Trustee, and all action taken by such Special Trustees shall be by unanimous agreement of the Special Trustees. In the event that such Special Trustees are unable to agree on any particular decision which must be made by them in their fiduciary capacity as Special Trustees, the tie breaking vote shall be made by Corporate Trustee 2 (or the then serving qualified successor corporate trustee).

Article VII, paragraph B.1.c. will provide that in the event that all of Taxpayer's daughters shall cease to serve as Special Trustees for any reason, then Individual and Corporate Trustee 2 (or the qualified successor corporate trustee) shall serve as successor Special Trustees and all action taken by the Special Trustees shall be by unanimous agreement of the Special Trustees. In the event that Individual also fails or ceases to serve as Special Trustee for any reason, then Corporate Trustee 2 (or the qualified successor corporate trustee) shall serve as the sole successor Special Trustee.

Article VII, paragraph B.2. will provide that Taxpayer's daughters who are serving as Special Trustees shall have the power, acting by majority vote if all three of them are serving, and acting by unanimous agreement if only two of them are serving, to remove the tie breaker and to replace the tie breaker with another tie breaker by delivering written notice to the removed tie breaker. The tie breaker may renounce or resign the position as tie breaker at any time by written notice to all trustees then serving. In the event of the renunciation, resignation, refusal or incapacity of the tie breaker, the Special Trustees who are then serving, acting by a majority if all three of them are serving, and acting by unanimous agreement if only two of them are serving, shall appoint a successor tie breaker. The Special Trustees may exercise the power to remove the tie breaker only five times during each ten-year period.

Article VII, paragraph B.3. will provide that the Special Trustees shall have the exclusive authority to: (i) vote all shares of Company which are owned by the Trust or any subtrust created; and (ii) control the timing of the disposition of the shares of Company which are owned by the Trust or any subtrust as well as the price and other terms and conditions of sale. Article VII, paragraph B.3.a. will provide that the individual Special Trustees shall have no powers or authority with respect to the Trust or subtrusts created hereunder except as specifically set forth in Article VII, subparagraph B.3. Article VII, paragraph B.3.b. will provide that the trustees, other than the Special Trustees, from time to time in office shall have: (a) no duty and no power to question the Special Trustees' exercise of their authority, (b) no duty to make any investment review of the assets removed from the other trustees' authority, and (c) no liability for failure to implement measures over the remaining portion of the trust estate in which the other trustees do participate in making investment decisions that would counter the effects or consequences of decisions that are removed from the other trustees' authority. During such time or times as the corporate trustee is not a Special Trustee, the corporate trustee shall have no liability for any damage or liability of any nature sustained by the trust estate, any beneficiary, or any other person because of the Special Trustees' exercise or failure to exercise their authority under this subparagraph B.3.

Article VII, paragraph B.4. will provide that notwithstanding anything contained herein to the contrary, Taxpayer's daughters shall only serve as Special Trustees, and Individual shall only serve as successor Special Trustee, to the extent that the appointment of Taxpayer's daughters as Special Trustees and the appointment of Individual as successor Special Trustee, and the possession of the powers and authority of the Special Trustees or the exercise of such powers and authority will not result in the inclusion of the assets of the Trust or any subtrust in the gross estate of Taxpayer or any of Taxpayer's daughters, or adversely affect the exempt status of the Trust or any subtrust for purposes of GST tax under § 2601 of the Code.

Article VII, paragraph F will be modified to provide that the Trust and all subtrusts shall be governed by State Statute 3.

The Court has granted the parties' complaint for modification subject to the trustee receiving a favorable ruling from the Service that neither Taxpayer's nor a beneficiary's power to appoint and remove trustees, nor any other provision of the proposed modification will result in the inclusion of the assets of the Trust or any subtrust in the estate of Taxpayer or any beneficiary for federal estate tax purposes, or adversely affect the exempt status of the Trust or any subtrust from the GST tax under § 2601 of the Internal Revenue Code.

Corporate Trustee 2 requests the following rulings:

- (1) The Court's interim order that allows the Trust to be modified to provide Taxpayer with the power to appoint additional trustees and to remove and replace trustees: (i) will not cause the assets of the Trust to be included in Taxpayer's gross estate for federal estate tax purposes; and (ii) will not cause the Trust (or any subtrust) to lose its status as exempt from the GST tax.
- (2) The Court's interim order that allows the Trust to be modified to provide that in the event of Taxpayer's death, incapacity or renunciation of the power to appoint additional trustees and the power to remove and replace trustees, a majority of the current income beneficiaries and adult remainder beneficiaries of each separate subtrust shall have the power to appoint additional trustees and the power to remove and replace trustees: (i) will not result in Taxpayer or any of the current income beneficiaries or adult remainder beneficiaries of each separate subtrust having a general power of appointment over any assets of the Trust or cause any of the assets of the Trust to be included in the gross estate of Taxpayer or any of the current income beneficiaries or adult remainder beneficiaries of each separate subtrust for federal estate tax purposes; and (ii) will not cause the Trust to lose its status as exempt from the GST tax.
- (3) The Court's interim order that allows the Trust to be modified to appoint Taxpayer's daughters as "Special Trustees" with the authority to control the stock of Corporation which is owned by the Trust: (i) will not result in Taxpayer or any of Taxpayer's daughters having a general power of appointment over any assets of the Trust or cause any of the assets of the Trust to be included in the gross estate of Taxpayer or in the gross estate of any of Taxpayer's daughters; and (ii) will not cause the Trust (or any subtrust) to lose its status as exempt from the GST tax.

#### Estate Tax Rulings (Ruling Requests 1(i), 2(i), and 3(i))

Section 2001(a) imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2033 provides that the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death.

Section 2036(a) provides that the value of the decedent's gross estate includes the value of all property to the extent of any interest of which the decedent has made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which the decedent has retained for life, or for any period not ascertainable without reference to the decedent's death, or any period that does not in fact end before the decedent's death, (1) the possession or enjoyment of, or the right to the income from the property, or (2) the right either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income from the property.

Section 20.2036-1(b)(2) of the Estate Tax Regulations provides that the "use, possession, right to the income, or other enjoyment of the transferred property" is considered as having been retained by or reserved to the decedent to the extent that the use, possession, right to the income, or other enjoyment is to be applied toward the discharge of a legal obligation of the decedent, or otherwise for his pecuniary benefit. The term "legal obligation" includes a legal obligation to support a dependent during the decedent's lifetime.

Section 2038(a)(1) provides, generally, that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person to alter, amend, revoke, or terminate, or where such power is relinquished during the 3-year period ending on the date of the decedent's death.

Section 20.2038-1(a) provides, generally, that a decedent's gross estate includes under § 2038 the value of any interest in property transferred by the decedent, whether in trust or otherwise, if the enjoyment of the interest was subject at the date of the decedent's death to any change through the exercise of a power by the decedent to alter, amend, revoke, or terminate, or if the decedent relinquished such a power in contemplation of death. However, § 20.2038-1(a)(3) provides that § 2038 does not apply to a power held solely by a person other than the decedent. But, for example, if the decedent had the unrestricted power to remove or discharge a trustee at any time and appoint himself trustee, the decedent is considered as having the powers of the trustee.

Section 2041(a)(2) provides, generally, that the value of the gross estate shall include the value of all property to the extent of any 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)(1) provides, in part, 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) provides, in part, that 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 20.2041-1(c)(2) provides, in part, that a power to consume, invade, or appropriate income or corpus, or both, for the benefit of the decedent which is limited by an ascertainable standard relating to the health, education, support, or maintenance of the decedent is, by reason of § 2041(b)(1)(A), not a general power of appointment.

Under State Statute 3, a trustee who is also a beneficiary of a trust is prohibited from exercising any power: (i) to make discretionary distributions of either principal or income to or for the benefit of the trustee as a beneficiary, except to provide for that trustee's health, education, maintenance, or support as described in §§ 2041 and 2514; (ii) to make discretionary allocations of receipts or expenses as between principal and income, unless such trustee acts in a fiduciary capacity whereby such trustee has no power to enlarge or shift any beneficial interest except as an incidental consequence of the discharge of such trustee's fiduciary duties; (iii) to make discretionary distributions of either principal or income to satisfy any legal support obligations of such trustee; or (iv) to exercise any other power, including the right to remove or to replace any trustee, so as to cause the powers enumerated in (i), (ii), or (iii) to be exercised on behalf of, or for the benefit of, a beneficiary who is also a trustee. In addition, State Statute 3 provides that a person who has the right to remove or to replace a trustee does not possess nor may that person be deemed to possess, by virtue of having that right, the powers of the trustee that is subject to removal or to replacement.

In the present case, under the terms of the Trust, the Trust is irrevocable and Taxpayer has retained no right, title, interest in or power over, or privilege or incident of ownership with regard to any trust property. Taxpayer has retained no beneficial interest in the Trust and has not retained any right to alter, amend, revoke, or terminate the Trust within the meaning of § 2038, or the right to designate the persons who will possess or enjoy the property or the income within the meaning of § 2036.

Under the proposed modification, Taxpayer will retain the power to appoint additional trustees and to remove and replace trustees, however, any trustee appointed by Taxpayer must not be related or subordinate to Taxpayer within the meaning of

§ 672(c) and in no event may Taxpayer appoint himself as trustee or co-trustee of the Trust or any subtrust. In addition, the Trust provides that: (i) the trustees are prohibited from making any distributions which would discharge any support obligation of Taxpayer; and (ii) distributions of principal may only be made for the education and maintenance in health and reasonable comfort of the beneficiaries. Accordingly, Taxpayer's appointment, removal and replacement powers will not be considered the reservation of the trustee's powers for purposes of § 2038. Further, Taxpayer's power to appoint additional trustees and remove and replace trustees will not result in Taxpayer having a general power of appointment over any assets of the Trust and no interest in the Trust will be includible in Taxpayer's gross estate under § 2041.

As mentioned above, the Trust provides that distributions of principal may only be made for the education and maintenance in health and reasonable comfort of the beneficiaries. In addition, the proposed modification provides that any successor corporate trustee appointed by the beneficiaries must not be related or subordinate to Taxpayer (during his life) or the beneficiaries within the meaning of § 672(c). Thus, the proposed modification of the Trust to provide that a majority of the current income beneficiaries and adult remainder beneficiaries of each separate subtrust shall have the power to appoint additional trustees and the power to remove and replace trustees in the event of Taxpayer's death, incapacity or renunciation of the power, will not result in Taxpayer or any of the current income beneficiaries or adult remainder beneficiaries of each separate subtrust having a general power of appointment over any assets of the Trust. Thus, no interest in the Trust will be includible in the estate of Taxpayer or any of the current income beneficiaries or adult remainder beneficiaries of each separate subtrust under § 2041.

Further, under the proposed modification, Taxpayer's daughters will be appointed as Special Trustees of the Trust. The proposed modification also provides that the Special Trustees shall have no power or authority with respect to the Trust or subtrusts, except the power to control the stock of the family corporation which is owned by the Trust. Thus the appointment of Taxpayer's daughters as Special Trustees will not result in Taxpayer or any of Taxpayer's daughters having a general power of appointment over any assets of the Trust or cause any of the assets of the Trust to be included in the gross estate of Taxpayer or in the gross estate of any of Taxpayer's daughters under § 2041.

#### GST Rulings (Ruling Requests 1(ii), 2(ii), and 3(ii))

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

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

Under § 1433(b)(2)(A) of the Tax Reform Act of 1986 and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the generation-skipping transfer tax

provisions do not apply to any generation-skipping transfer under a trust (as defined in § 2652(b)) that was irrevocable on September 25, 1985. However, this exemption does not apply if additions (actual or constructive) are made to the trust after September 25, 1985.

Section 26.2601-1(b)(1)(ii)(A) of the Generation-Skipping Transfer Regulations provides that any trust in existence on September 25, 1985, will be considered an irrevocable trust except as provided in § 26.2601-1(b)(ii)(B) or (C), which relates to property includible in a grantor's gross estate under §§ 2038 and 2042. In the present case, the Trust is considered to have been irrevocable on September 25, 1985, because neither § 2038 nor § 2042 applies.

Section 26.2601-1(b)(4) 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 § 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. In general, unless specifically provided otherwise, the rules contained in § 26.2601-1(b)(4) are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. Unless specifically noted, 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) provides that a modification of the governing instrument of an exempt trust (including a trustee distribution, settlement, or construction that does not satisfy § 26.2601-1(b)(4)(i)(A), (B), or (C)) 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 § 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)(D)(2) provides that for purposes of this section, a modification of an exempt trust will result in a shift in beneficial interest to a lower generation beneficiary if the modification can result in either an increase in the amount of a GST transfer or the creation of a new GST transfer. To determine whether a modification of an irrevocable trust will shift a beneficial interest in a trust to a beneficiary who occupies a lower generation, the effect of the instrument on the date of the modification is measured against the effect of the instrument in existence immediately before the modification. If the effect of the modification cannot be immediately determined, it is deemed to shift a beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in § 2651) than the person or

persons who held the beneficial interest prior to the modification. A modification that is administrative in nature that only indirectly increases the amount transferred (for example, by lowering administrative costs or income taxes) will not be considered to shift a beneficial interest in the 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 § 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.

In the present case, the Trust was established and became irrevocable on Date 1, and it is represented that there have been no additions made to the Trust after September 25, 1985. Accordingly, the Trust is exempt from the GST tax under § 26.2601-1(b)(1).

Based on the facts submitted and the representations made, the proposed modification of the Trust as described above effectuates an administrative change and will not result in a shift of any beneficial interest in the Trust to any beneficiary who occupies a lower generation than the persons holding the beneficial interests prior to the modification. Further, the proposed modification will not extend the time for vesting of any beneficial interest beyond the period originally provided for under the terms of the Trust. As a result, the proposed modification will not cause distributions from or terminations of any interests in the Trust to be subject to the GST tax, provided there are no additions to the Trust.

Provided that the Court approves the proposed modification, the modification will not cause the Trust or any of the sub-trusts to lose their GST exempt status under § 1433(b)(2)(A) of the Tax Reform Act of 1986.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. 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. While this office has not verified any of the material

submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In addition, no opinion is expressed or implied with respect to the income tax consequences of any transaction.

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.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to Corporate Trustee 2.

Sincerely,

Melissa C. Liquerman  
Branch Chief, Branch 9  
Office of Associate Chief Counsel  
(Passthroughs & Special Industries)