

Internal Revenue Service

Number: **200608001**
Release Date: 2/24/2006
Index Number: 2601.03-01

Department of the Treasury
Washington, DC 20224

[Third Party Communication:
Date of Communication: Month DD, YYYY]

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:4
PLR-100932-05
Date: NOVEMBER 14, 2005

DO:

Re:

Legend:

- Decedent =
- Trust =

- County =
- State =
- Son =
- Daughter 1 =
- Daughter 2 =
- Wife =
- Trustee =
- Date 1 =
- Date 2 =
- Date 3 =
- Date 4 =
- X% =
- \$Y =
- Z =

Dear :

This is in response to your authorized representative's submission dated December 31, 2004, concerning the generation-skipping transfer (GST) tax consequences of a judicial modification of Trust.

According to the facts submitted, Trust was created under the terms of Decedent's Last Will and Testament (Will) that was executed on Date 1. Decedent died on Date 2, a date before September 25, 1985.

On Date 3, Decedent's Will was filed with the Probate Court of County, State.

Item Four of Decedent's Will, provides for the bequest of X% of Decedent's estate, real and personal, that is remaining after the payment of the estate's indebtedness, taxes, expenses of administration and legacies, to Trustee, for the benefit of his heirs.

Trustee is to hold, manage, invest, and reinvest the property, comprising the trust estate, for and on behalf of the beneficiaries named, and to collect, pay, and dispose of the income from the trust estate, and to pay and dispose of the principal or corpus thereof, to the beneficiaries, in the manner provided.

Trustee is to apply the net income from the trust estate, or so much thereof as from time to time in its discretion appears necessary and proper, to the support, maintenance and education of Son, until Son attains the age of twenty-one (21) years. Any income from the trust estate which, during the minority of Son is not expended for Son's support, education, maintenance or other benefit may, in the discretion of the Trustee, be added to the principal of the trust and reinvested, or retained by Trustee and thereafter at any time disbursed by it as income. Upon Son attaining age 21, Trustee, at convenient intervals, is to pay Son the entire net income from Trust, so long as Son shall live.

Upon the death of Son, after Decedent's death and while Trust for Son's benefit is in force and effect, the trust shall terminate.

In the event that Son dies leaving issue or descendants of issue surviving, Trustee, upon the death of Son, is to pay the principal of Trust, in fee simple and absolutely, to the issue and descendants of the issue of Son, per stirpes.

In the event that Son shall die without surviving issue or descendants of issue, the principal of the estate held for Son is to inure to the benefit of Daughter 1 and Daughter 2, or to their respective issue and descendants of issue if either be then deceased, in specified ratios. Any shares so inuring to either Daughter 1 or Daughter 2 are to be held by Trustee in the respective trusts provided for them under Item Two and Item Three, respectively, of Decedent's Will.

If Son should predecease Decedent leaving issue surviving, Son's Trust is not to take effect; but the X% which would have been the share of Son's trust is to pass in fee simple and absolutely to the issue of Son, per stirpes.

If Son predeceases Decedent leaving no issue surviving, Son's Trust is not to take effect, but the X% of the residue is to be added to the remainder of the residuary

estate, and is to be taken by Trustee in trust in the same proportion that exists under the original division of Decedent's residuary estate for the benefit of Daughter 1 and Daughter 2.

Trustee is granted the power and authority to encroach upon the principal of Trust, at any time during the life of Trust, for the proper support, maintenance and education of Son.

Any income from Trust which may accrue to or become payable to Son, during his minority, and any part or portion of the Trust which Trustee may from time to time disburse for the support, education, maintenance or other benefit of Son, may in the discretion of Trustee be paid by it direct to any person or persons for the support, maintenance, education or other benefit of Son, without the necessity of interposition of a Guardian; and the receipts of such persons for such payments for the support, maintenance, education or other benefit of Son is to be full acquittance of Trustee for all said income or principal so disbursed.

Item Four Trust also provides that in the event Decedent's wife, (Wife) dissents from the terms of Will, and declines to accept the same, or shall elect to demand and take any portion of Decedent's estate as Wife may be entitled to by the laws of State or any other state, Item Four Trust for the benefit of Son will be void and of no effect, and all provisions of other Items of Will for the benefit of Son, will be void and Son is to receive, out of the residue of Decedent's estate and in lieu of all other benefits under Will, the sum of \$Y.

At the present time, Son is alive and has Z children, one of which is a minor. Decedent's Will contains no provision concerning the rule against perpetuities nor does the Will contain a perpetuities savings clause. It is represented that as of the date of execution of Decedent's Will, rule against perpetuities savings clauses were not recognized under State law, and that testamentary trusts were deemed to be required to terminate upon the death of a life in being as of the execution of the trust in order to avoid a potential violation of the rule against perpetuities.

As a result, absent modification, the Item Four Trust provides for termination of Trust upon the death of Son. At that time, the principal of Trust will be paid "in fee simple and absolutely" to the issue and descendants of issue of Son, per stirpes.

It is represented that Decedent would have preferred to retain the Item Four Trust property under trust management for as long as prudently possible. It is also represented that there have been no additions to Trust and that Trust has not been amended or modified, except for the purpose of changing the trustee.

On Date 4, Trustee and Son filed a Petition with the Probate Court of County, State, seeking an order approving the modification of the terms of Trust. The proposed modification provides that upon the death of Son, any assets that would otherwise be

distributed outright to Son's children will instead be divided into equal shares, one equal share for each child of Son then living, and one equal share for each group of then living issue of a deceased child of Son, as described below.

(1) With respect to a share for a child then living of Son, who has attained age thirty-five (35) the trustee is to pay the child's separate trust to the child outright.

(2) With respect to a share for a child who has not attained the age of thirty-five (35), the trustee is to invest the trust property, collect the income from the property and, until the child attains the age of thirty-five, pay or apply for the child's benefit all or any portion of the net income or principal of the separate trust as determined to be necessary and proper in the discretion of the trustee. After such child has attained the age of thirty-five years, the remaining principal and undistributed income is to be paid to the child.

(3) If a child dies after a separate trust has been set aside for the child, but before the entire principal and undistributed income has been distributed to the child, the trust property is to pass pursuant to the child's general power of appointment. In default of appointment, the trustee is to hold the trust property in further trust for the then living issue of the deceased child. If there are no issue then living, the trustee is to divide the trust principal and undistributed income into equal shares, one share for each child of Son then living, and one equal share for each group then living of issue of each deceased child of Son.

(4) With respect to any share held for each group of then living issue of a deceased child of Son, the trustee is to further divide the share into equal shares, one share for each of the then living issue of a then deceased child of Son, per stirpes (each such living issue of a then deceased child of Son is referred to as an "Issue Beneficiary"). The trustee is to hold and administer each share as a separate trust until such time as the separate trust may be terminated as follows:

(a) With respect to each separate trust for an Issue Beneficiary who has attained the age of thirty-five (35) years, the trustee is to pay over and deliver the Issue Beneficiary's separate trust to such person in fee.

(b) With respect to each separate trust for an Issue Beneficiary who has not attained the age of thirty-five (35) years, the trustee is to continue to hold such share in a separate trust as follows:

(A) Until such Issue Beneficiary has attained the age of thirty-five (35) years, the trustee is to pay or apply for the Issue Beneficiary's benefit all or a portion of the net income or principal of the separate trust at such times and in such manner as the trustee in its discretion determines to be necessary and proper. Any income not paid is to be added to principal.

(B) After the Issue Beneficiary has attained the age of thirty-five (35) years, the trustee is to distribute the entire remaining principal and undistributed income to the Issue Beneficiary in fee.

(C) If an Issue Beneficiary dies after a separate trust has been set apart for his or her benefit and before the entire principal and undistributed income has been distributed to him or her, the trustee is to distribute the principal and income as the Issue Beneficiary may appoint by his or her will. In default of appointment, the trustee is to distribute the trust property, per stirpes, to the then living issue of the deceased Issue Beneficiary, or if there is no such issue then living, the trustee is to divide the trust property into equal shares, one equal share for each child of Son then living, and one equal share for each group of the then living issue of each deceased child of Son, the share of any person or group for whom a trust already exists to be added to such trust, otherwise to be paid outright to such child, or per stirpes to such then living issue. Upon completion of such distribution, the separate trust for such beneficiary is to terminate.

(5) Any trust that is established under Item Four is to terminate, if not previously terminated, twenty-one (21) years after the death of the later to die of Spouse and any beneficiary of Decedent living on the date of Decedent's death, and the then remaining principal and undistributed income is to be paid to the current income beneficiaries who are then entitled to receive the income from Trust in such proportions as they are or would have been entitled to such income, and if the proportions are not specified, in equal shares to the beneficiaries, per stirpes, absolute and free of trust.

The following rulings are requested.

- 1) Trust qualifies under §1433(b)(2)(A) of the Tax Reform Act of 1986 (the Act) and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer (GST) Regulations as exempt from GST tax as a trust that was irrevocable on September 25, 1985.
- 2) The modification of Trust as proposed does not shift a beneficial interest in Trust to any beneficiary who occupies a lower generation as defined in section 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 in the original trust and, therefore, the modification of the trust will not be treated as an actual or constructive addition to the trust for purposes of the effective date rules under § 26.2601-1(b)(1)(i) and will not cause the trust to lose its exempt status under section 2601.
- 3) The separate trusts to be funded upon the death of Son, for the benefit of Son's issue will be treated as trusts which were irrevocable on September 25, 1985, for purposes of § 1433(b)(2)(A) of the Act and which exempt from the generation-skipping transfer tax.

Section 2601 imposes a tax on every generation-skipping transfer (GST), which is defined under section 2611 as a taxable distribution, a taxable termination, 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 section 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 was 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)(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 section 26.2601-1(b)(4)(i)(A), (B), or (C) of this section) 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 section 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.

In the present case, the proposed modification to Trust provides that upon Son's death, the remaining assets of Trust will be divided into separate equal trusts, one trust for each then living issue of Son and one trust for each of the then living issue of a deceased child of Son (an Issue Beneficiary). In addition, each child of Son and each Issue Beneficiary will have a testamentary general power of appointment under section 2041(a)(2) over their respective trust. Accordingly, each child of Son and each Issue Beneficiary will be treated as the transferor of the trust corpus for GST tax purposes under section 2652(a)(1).

Under these circumstances and based on the facts submitted and the representations made, we conclude:

1. Trust qualifies under §1433(b)(2)(A) of the Act and § 26.2601-1(b)(1)(i) as exempt from GST tax as a trust that was irrevocable on September 25, 1985.
2. The modification of Trust pursuant to Court Order will not shift a beneficial interest in Trust to any beneficiary who occupies a lower generation as defined in section 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 in the original trust and, therefore, the modification of the trust will not be treated as an actual or constructive addition to the trust for purposes of the effective date rules under

§ 26.2601-1(b)(1)(i) and will not cause the trust to lose its exempt status under section 2601.

3. The separate trusts to be funded upon the death of Son, for the benefit of Son's issue will be treated as trusts which were irrevocable on September 25, 1985, for purposes of § 1433(b)(2)(A) of the Act and which are exempt from the generation-skipping transfer tax.

The rulings contained in this letter are based upon information and representations submitted by the taxpayers 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 rulings, it is subject to verification on examination.

Except as specifically ruled herein, we express or imply no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

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

Sincerely,

Lorraine E. Gardner
Senior Counsel
(Office of Passthroughs and Special Industries)

Enclosure (1)
Copy of letter for section 6110 purposes

cc: