

Internal Revenue Service

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Person to Contact:

Telephone Number:

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CC:PSI:9 / PLR-128718-00

Date:

March 21, 2001

Legend:

A

B

C

D

E

F

G

H

I

J

K

Family 1

Family 2

Company

Foundation

State

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Series 1 Trusts

Series 2 Trusts

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Series 3 Trusts

Series 4 Trusts

Year 1

Year 2

Date 1

Dear

We received your letter requesting rulings under §§ 2036, 2038, 2041, and 2601

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of the Internal Revenue Code. This letter responds to your ruling request.

In Year 1, Family 1 created Series 1 Trusts, Series 2 Trusts, Series 3 Trusts, and Series 4 Trusts (collectively "Trusts"). A, B, C, D, and E (collectively "Grantors") created Series 1 Trusts for each of his or her children. Grantors created Series 2 Trusts for each of the grandchildren of F and G, the parents of Grantors. F and G created Series 3 Trusts and Series 4 Trusts for Grantors. Trusts were irrevocable at their creation. All the trust agreements creating Trusts are substantially identical to one another.

Article IV of the trust agreement provides in part that any trustee acting hereunder from time to time, whether individual or corporate, can be removed at any time by a majority vote of the board of directors of Foundation. Any successor trustee shall be selected by a majority vote of the board of directors of Foundation, provided that there shall be at all times at least one trustee acting hereunder which trustee is an independent trustee and is not a "related or subordinate party" as now defined in § 672(c) of the Internal Revenue Code of 1954 or as defined in any subsequent statute, rule or case law relating to the same subject as said § 672(c).

Article VI Paragraph 4 of the trust agreement provides in part that if any beneficiary child or issue of the creator [of the trust] is then living, the independent trustee may in such trustee's sole discretion pay all or part of the annual net income of the trust (after deduction of the payments provided in Article VI Paragraph 2 hereof) held for such child to or for the benefit of such child for the support, maintenance, education and general welfare of such child; provided, however, such trustee may accumulate all or part of such income. Any annual net income of a trust not so paid by the independent trustee shall become a part of the principal of such trust.

Article VI Paragraph 5 of the trust agreement provides in part that if any beneficiary child dies leaving issue, such child's trust estate shall be held for the benefit of such issue on a per stirpes basis with said trust estate being divided into separate and distinct trusts for each such child's issue. In the event any beneficiary child dies leaving no issue, that child's trust estate shall pass into and become a part of the other trusts created hereunder which are then in existence, such disposition to be in such manner as if such trust estate had belonged to the creator and the creator originally disposed of same hereunder as a part of such other trust estates.

Article VI Paragraph 6 of the trust agreement provides that on the death of the last survivor of issue of F and G in being on the date of execution of this instrument plus an additional twenty-one (21) years all of the trusts created hereunder shall terminate immediately and the assets thereof distributed, delivered and paid over to the then living issue of F and G in equal parts, per capita, whether or not they then are immediate income beneficiaries of the trusts. If there are no living issue of F and G, the

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remaining trust funds shall be delivered and paid over to Foundation.

In Year 2, Family 1 and Family 2 formed Company, a State limited banking association, for the purpose of rendering trust services. Company has two classes of shares, each of which represents 50% of the total voting power of all the Company's outstanding shares. Initially, Series 1 Trusts of Family 1 acquired all of one class of shares. Series I Trusts of Family 1 then transferred the shares to a voting trust that Family 1 previously established. The thirteen current voting trustees of the voting trust are all eleven beneficiaries of Series 1 Trusts, A, and J, an unrelated person. All of the other class of shares are held by Family 2.

Section 7.2 of the bylaws and participation agreement of Company provides in part that the number of directors of Company shall be nine. The board of directors may expand the number of director positions as long as the total number of director positions following such expansion is an odd number. The board of directors may reduce the number of director positions following the occurrence of a vacancy so long as the total number of director positions following such reduction is an odd number.

Notwithstanding the foregoing, Company shall have not less than five nor more than eleven directors.

Section 7.17 of the bylaws and participation agreement of Company provides that no officer or director of Company shall participate in a decision of Company (nor be present during any board or committee discussion of or vote on such a decision) involving:

(a) The exercise of any discretionary power, other than investment powers, with respect to any trust of which Company is a trustee if the officer, director, or spouse of such officer or director is:

(1) A grantor of or donor to such trust,

(2) A current or contingent beneficiary of such trust, or

(3) A descendant, or spouse (or former spouse) of a descendant, of either F or K, but this § 7.17(a)(3) shall apply only with respect to a trust a current or contingent beneficiary of which is a descendant, or a spouse (or former spouse) of a descendant, of either F or K; or

(b) The exercise of any incidence of ownership of any life insurance policy insuring the life of such officer or director.

A director that is subject to the restrictions of this § 7.17 with respect to a decision of Company, although absent from at least that part of the meeting, shall be deemed

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present for the purpose of determining whether a quorum is present for that part of the meeting.

The current trustees of Trusts, A, H, and I, desire to resign as trustees. The board of the trustees of Foundation desires to appoint Company as the sole trustee of Trusts.

On Date 1, the Service issued to the board of the trustees of Foundation a private letter ruling in which the Service concluded that Company was not a related or subordinate party with respect to Grantors within the meaning of § 672(c).

You represent that no additions, actual or constructive, have been made to Trusts after September 25, 1985.

You have requested the following rulings:

(1) Neither the appointment of Company as trustee of Trusts nor its exercise of the discretionary powers over income distributions to beneficiaries of Trusts will result in the inclusion of any portion of Trusts in the respective estates of Grantors under §§ 2036 or 2038 or of the beneficiaries of Trusts under § 2041.

(2) The appointment of Company as trustee of Trusts will not constitute a constructive addition to Trusts under § 2601 and will not affect the grandfathered status of Trusts for purposes of the Generation-Skipping Transfer (GST) tax.

Section 2036(a) provides 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, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his 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 therefrom.

Section 2036(b) provides in part that

(1) For purposes of § 2036(a)(1), the retention of the right to vote (directly

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or indirectly) shares of stock of a controlled corporation shall be considered to be a retention of the enjoyment of transferred property.

(2) For purposes of § 2036(b)(1), a corporation shall be treated as a controlled corporation if, at any time after the transfer of the property and during the 3-year period ending on the date of the decedent's death, the decedent owned (with the application of § 318), or had the right (either alone or in conjunction with any person) to vote, stock possessing at least 20 percent of the total combined voting power of all classes of stock.

Section 2038(a)(1) provides 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 (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished during the 3-year period ending on the date of the decedent's death.

Section 2041(a)(2) provides 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. For purposes of this paragraph (2), the power of appointment shall be considered to exist on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even though the exercise of the power takes effect only on the expiration of a stated period after its exercise, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised.

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

Section 2611(a) provides that, for purposes of the GST tax, the term "generation-skipping transfer" means –

- (1) a taxable distribution,
- (2) a taxable termination, and
- (3) a direct skip.

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Section 2612(a)(1) provides that, for purposes of the GST tax, the term “taxable termination” means the termination (by death, lapse of time, release of power, or otherwise) of an interest in property held in a trust unless –

(A) immediately after such termination, a non-skip person has an interest in such property, or

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

Section 2612(b) provides that, for purposes of the GST tax, the term “taxable distribution” means any distribution from a trust to a skip person (other than a taxable termination or a direct skip).

Section 2612(c)(1) provides that, for purposes of the GST tax, the term “direct skip” means a transfer subject to a tax imposed by chapter 11 or 12 of an interest in property to a skip person.

Section 2613(a) provides that, for purposes of the GST tax, the term “skip person” means –

(1) a natural person assigned to a generation which is 2 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 such trust, and

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

Section 2613(b) provides that, for purposes of the GST tax, the term “non-skip person” means any person who is not a skip person.

Section 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provides in part that the GST 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

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generation-skipping transfer under an irrevocable trust if additions are made to the trust after September 25, 1985.

Section 26.2601-1(b)(1)(ii)(A) provides that, except as provided in § 26.2601-1(b)(1)(ii)(B) or (C), any trust (as defined in § 2652(b)) in existence on September 25, 1985, is considered an irrevocable trust.

Section 26.2601-1(b)(1)(v) provides that

(A) except as provided in paragraph (b)(1)(v)(B) of this section, 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 is treated to any extent as a taxable transfer under chapter 11 or chapter 12, the value of the entire portion of the trust subject to the power that was released, exercised, or lapsed is treated as if that portion had been withdrawn and immediately retransferred to the trust at the time of the release, exercise, or lapse. The creator of the power will be considered the transferor of the addition except to the extent that the release, exercise, or lapse of the power is treated as a taxable transfer under chapter 11 or chapter 12.

(B) The release, exercise, or lapse of a power of appointment (other than a general power of appointment as defined in § 2041(b)) is not treated as an addition to a trust if –

(1) Such power of appointment was created in an irrevocable trust that is not subject to chapter 13 under paragraph (b)(1) of this section; and

(2) In the case of an exercise, the power of appointment is not exercised in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of the trust, extending beyond any life in being at the date of creation of the trust plus a period of 21 years plus, if necessary, a reasonable period of gestation (the perpetuities period). For purposes of this paragraph (b)(1)(v)(B)(2), the exercise of a power of appointment that validly postpones or suspends the vesting, absolute ownership or power of alienation of an interest in property for a term of years that will not exceed 90 years (measured from the date of creation of the trust) will not be considered an exercise that postpones or suspends vesting, absolute ownership or the power of alienation beyond the perpetuities period. If a power is exercised by creating another power, it is deemed to be exercised to whatever extent the second power may be

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exercised.

(C) Where a trust described in paragraph (b)(1) of this section is relieved of any liability properly payable out of the assets of such trust, the person or entity who actually satisfies the liability is considered to have made a constructive addition to the trust in an amount equal to the liability. The

constructive addition occurs when the trust is relieved of liability (e.g., when the right of recovery is no longer enforceable).

Based on the information submitted and representations made, we conclude that neither the appointment of Company as trustee of Trusts nor its exercise of the discretionary powers over income distributions to beneficiaries of Trusts will result in the inclusion of any portion of Trusts in the respective estates of Grantors under §§ 2036 or 2038 or of the beneficiaries of Trusts under § 2041. We further conclude that the appointment of Company as the sole trustee of Trusts is administrative in nature and, therefore, will not constitute a constructive addition to Trusts under § 2601 and will not affect the grandfathered status of Trusts for purposes of the GST tax.

This ruling is based on the facts presented and the 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.

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

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

Sincerely,

Christine E. Ellison
Chief, Branch 7
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure: Copy for § 6110 purposes