

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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RE:

Legend

- Date 1 =
- Decedent =
- Child 1 =
- Child 2 =
- Date 2 =
- Date 3 =
- Grandchild 1 =
- Grandchild 2 =
- Greatgrandchild 1 =
- Greatgrandchild 2 =
- State =
- Statute 1 =
- Statute 2 =

Dear _____ :

This responds to your authorized representative’s letter dated November 5, 2009 requesting rulings regarding the generation-skipping transfer (GST) tax consequences of the proposed division of two trusts.

The facts submitted and representations made are as follows:

On Date 1, Decedent died testate survived by Child 1, Child 2, Grandchild 1, and Grandchild 2. Under Decedent’s will, an irrevocable trust (“Decedent’s Trust”), was created to hold the residuary estate for the benefit of Child 1. It is represented that no additions, actual or constructive, have been made to Decedent’s Trust after September 25, 1985. Pursuant to the terms of Decedent’s Trust, during Child 1’s lifetime, the trustees may pay the net income of Decedent’s Trust to or for the benefit of

Child 1. The trustees may also pay as much of the principal of Decedent's Trust to or for the benefit of Child 1 as the trustees determine in their discretion for her support and welfare, after considering Child 1's other resources.

Upon Child 1's death, the remaining principal of Decedent's Trust is to be divided into two equal shares for the benefit of each of Decedent's children and respective issue (individually, "Continuing Trust" or "Child 1 Continuing Trust" and "Child 2 Continuing Trust", or collectively, "Continuing Trusts"). The terms of each Continuing Trust are identical but for the identity of the primary beneficiaries. The income from a Continuing Trust is to be paid to the respective child and issue of Child 1 and Child 2, per stirpes. Moreover, discretionary distributions of principal may be made to the respective issue of Child 1 and Child 2 for support, welfare, and education. If, prior to the termination of a Continuing Trust, there is no one living to receive the income from a Continuing Trust, the income is to be paid over to the other Continuing Trust. Each Continuing Trust will terminate at the expiration of twenty-one years after the death of the last survivor of Decedent, Child 1, Child 2, the children and issue of Child 1, and the children and issue of Child 2, living at the time of Decedent's death ("Perpetuities Period"). Upon termination of a Continuing Trust, the remaining principal will be paid over, per stirpes, to the issue then living of Child 1 or Child 2, as the case may be.

Child 1 died on Date 2 leaving no issue. Child 2 died on Date 3 survived by Grandchild 1, Grandchild 2, Greatgrandchild 1, and Greatgrandchild 2. Accordingly, pursuant to the terms of Decedent's Trust, the current income beneficiaries of Child 1 Continuing Trust and Child 2 Continuing Trust are Grandchild 1 and Grandchild 2. Grandchild 1, Grandchild 2, Greatgrandchild 1, and Greatgrandchild 2 may also receive discretionary distributions of principal from Child 2 Continuing Trust. However, no distributions of principal are permitted under Child 1 Continuing Trust.

It is represented that no additions, actual or constructive, have been made to Decedent's Trust after September 25, 1985.

In order to invest the assets of the Continuing Trusts for each of Child 1's issue independently of each other, the trustees and beneficiaries of the Continuing Trusts have entered into a nonjudicial settlement agreement ("Settlement Agreement") to divide each of the Continuing Trusts into two equal successor trusts, with each successor trust to be held for the benefit of Child 1's children and issue (individually, "Successor Trust" or "Grandchild 1 Successor Trust A", "Grandchild 1 Successor Trust B", "Grandchild 2 Successor Trust A", and "Grandchild 2 Successor Trust B", or collectively, "Successor Trusts"). The proposed division is conditioned upon the receipt of a favorable ruling on the GST tax ruling requests from the Internal Revenue Service.

Under the proposed division, Child 2 Continuing Trust will be divided into Grandchild 1 Successor Trust B and Grandchild 2 Successor Trust B. The income of a Successor Trust B will be distributed to Grandchild 1 or Grandchild 2, respectively, and upon a

grandchild's death, to his surviving issue, per stirpes. The principal of a Successor Trust B will be distributed among any one or more of the respective grandchild and such grandchild's issue as the trustees determine in their discretion for the individual's support, welfare, and education, after considering his, or her, or their resources. Each Successor Trust B will terminate upon the expiration of the Perpetuities Period. Upon termination, the remaining principal will be distributed to the respective grandchild's living issue, per stirpes, or if none, to the living issue of the other grandchild, per stirpes. If a grandchild and all of such grandchild's issue die prior to the termination of such grandchild's respective Successor Trust B, then the remaining principal will continue to be held in the Successor Trust B and the income and principal of such trust will be distributed to the other grandchild and such other grandchild's issue in accordance with the terms of the other grandchild's Successor Trust B.

Child 1 Continuing Trust will be divided into Grandchild 1 Successor Trust A and Grandchild 2 Successor Trust A. The income of a Successor Trust A will be distributed to Grandchild 1 or Grandchild 2, respectively, and upon a grandchild's death, to his surviving issue, per stirpes. The principal of a Successor Trust A will be held in trust until the termination of each Successor Trust A. Each Successor Trust A will terminate upon the expiration of the Perpetuities Period. Upon termination the remaining principal will be distributed to the respective grandchild's living issue, per stirpes, or if none, to the living issue of the other grandchild, per stirpes. If a grandchild and all of such grandchild's issue die prior to the termination of such grandchild's respective Successor Trust A, then the remaining principal will continue to be held in the Successor Trust A and the income and principal of such trust will be distributed to the other grandchild and such other grandchild's issue in accordance with the terms of the other grandchild's Successor Trust A.

State Statute 1 provides, in part, that the beneficiaries and trustees of a trust may enter into a binding nonjudicial settlement agreement with respect to any matter involving the trust so long as the agreement does not violate a material purpose of the trust and could properly be approved by the appropriate State court. State Statute 2 provides that an appropriate State court could properly authorize the division of a trust into two separate trusts upon such terms and conditions as the court directs. State Statute 2 also provides that a trustee may, without court approval, divide a trust into separate trusts, and the beneficiaries of the separate trusts may be different so long as their rights are not impaired.

The trustees request rulings that the proposed division of each of the Continuing Trusts into two equal Successor Trusts pursuant to the Settlement Agreement:

- 1) will not cause the generation-skipping transfer tax imposed under chapter 13 to apply to the Continuing Trusts or the Successor Trusts;

- 2) will not subject future distributions from the Successor Trusts to the generation-skipping transfer tax imposed under chapter 13;
- 3) will not result in a taxable termination under chapter 13 upon the termination of any interest in the property held in the Continuing Trusts or the Successor Trusts; and
- 4) will not subject the termination of the Continuing Trusts and the Successor Trusts to the generation-skipping transfer tax imposed under chapter 13 of the Code.

LAW AND ANALYSIS

Section 2601 of the Internal Revenue Code imposes a tax on every generation-skipping transfer, which is defined under § 2611 as a taxable distribution, a taxable termination, or a direct skip.

Under § 1433 of the Tax Reform Act of 1986 (the Act), GST tax is generally applicable to generation-skipping transfers made after October 22, 1986. However, under § 1433(b)(2)(A) of the Act and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the tax does not apply to a transfer under a trust that was irrevocable on September 25, 1985, except to the extent the transfer is made out of corpus added to the trust by an actual or constructive addition after September 25, 1985.

Section 26.2601-1(b)(4)(i) 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) will not cause the trust to lose its exempt status. These rules are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. 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) 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 § 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.

In the instant case, it is represented that Decedent's Trust is exempt from GST tax because the trust was irrevocable on September 25, 1985, and no additions, actual or constructive, were made to Decedent's Trust after that date.

Based on the facts presented and the representations made, the proposed division of Child 1 Continuing Trust into Grandchild 1 Successor Trust A and Grandchild 2 Successor Trust A, and the proposed division of Child 2 Continuing Trust into Grandchild 1 Successor Trust B and Grandchild 2 Successor Trust B, as described above, will not result in a shift of any beneficial interest in Decedent's Trust to any beneficiary who occupies a generation lower than the persons holding the beneficial interests prior to the division. Further, the proposed division will not extend the time for vesting of any beneficial interest in the new trusts beyond the period provided for under the original Trust.

Accordingly, we conclude that the proposed division of each of the Continuing Trusts into two equal Successor Trusts pursuant to the Settlement Agreement will not cause the generation-skipping transfer tax to apply to the Continuing Trusts or the Successor Trusts and will not subject future distributions from the Successor Trusts to the generation-skipping transfer tax. Further, we conclude that the proposed division will not result in a taxable termination under chapter 13 upon the termination of any interest in the property held in the Continuing Trusts or the Successor Trusts, and will not subject the termination of the Continuing Trusts and the Successor Trusts to the generation-skipping transfer tax.

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. The ruling(s) in this letter pertaining to the federal estate and/or generation-skipping transfer tax apply only to the extent that the relevant sections of the Internal Revenue Code are in effect during the period at issue.

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.

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. 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.

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,

Lorraine E. Gardner
Senior Counsel, Branch 4
(Passthroughs & Special Industries)

Enclosures (2)
Copy of § 6110 purposes

cc: