

**Internal Revenue Service**

Department of the Treasury  
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Person To Contact:

ID No.

Telephone Number:

In Re:

Refer Reply To:  
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Date  
February 14, 2011

**Legend:**

- Settlor =
- Trust =
- Child's Trust =
- Date 1 =
- Child =
- State =
- Court =
- State Law =
- Date 2 =
- Date 3 =

Dear :

This letter responds to your authorized representative's letter of September 30, 2010, requesting a generation-skipping transfer (GST) tax ruling with respect to the proposed modification of a trust.

On Date 1, a date prior to September 25, 1985, Settlor executed an irrevocable trust, Trust. Article I, paragraph 1.A of Trust provides for the creation of Child's Trust. Article I, paragraph 2 provides that the trustees of Child's Trust have the discretion to distribute net income and corpus for the benefit of Child and Child's issue. Under the terms of Trust, there is no requirement to equalize payments between beneficiaries. Income not distributed in any year is to be retained as accumulated income.

Article I, paragraph 3 provides that the trustees have the discretion to distribute one-half of the corpus of Child's Trust to Child when Child attains age 28. Article I, paragraph 4 provides that the trustees have the discretion to distribute the remaining corpus of Child's Trust to Child when Child attains age 35. Article I, paragraph 5 provides that Child has a testamentary limited power to appoint the corpus of Child's Trust. Corpus not appointed is to be distributed to Child's then living issue, if

any, *per stirpes*, but if none, to Settlor's then living issue, *per stirpes*. Article II provides that, in the event that under the provisions of Trust there is no taker for any share or portion of a share of any trust created thereunder or any other property held hereunder, then such share, portion of a share or other property, shall be paid to such person or persons as would have been entitled to receive Settlor's estate, and in the same proportions as they would have taken, had Settlor died immediately following the time as of which there is no taker, intestate, unmarried, domiciled in State.

Pursuant to the requirements of Article I, paragraph 2, the trustees have retained undistributed income in Child's Trust as accumulated income.

In reviewing the trust agreement for purposes of estate planning for Child, the trustees realized that Child did not have a power of appointment over the accumulated income in Child's Trust and that the trust agreement did not expressly specify what was to happen to the accumulated income at Child's death. Upon reviewing the files from the law firm that drafted the trust agreement, the trustees concluded that Settlor intended that the beneficiaries of the corpus and the accumulated income be the same, that Child's power of appointment was to apply to both corpus and accumulated income, and that at Child's death, the corpus and accumulated income that was not appointed by Child's will, was to pass to Child's then living issue.

On Date 2, the trustees petitioned Court pursuant to State Law to modify the provisions of Article I, paragraph 2 to provide that income not distributed in any year is to be added to corpus instead of being retained as accumulated income. Settlor is alive and has attested that the proposed modification reflects his intent. On Date 3, Court issued an order approving the proposed modification subject to the issuance of a private letter ruling from the Internal Revenue Service that the proposed modification will not cause Child's Trust to lose its status as a trust that is exempt from the GST tax.

It has been represented that there have not been any additions (actual or constructive) to Child's Trust after September 25, 1986.

The trustees request a ruling that the proposed modification to Article 1, paragraph 2 of the trust agreement will not cause Child's Trust to lose its status as a trust that is exempt from the GST tax.

#### Law and Analysis:

Section 2601 of the Internal Revenue Code (Code) imposes a tax on every generation-skipping transfer made after October 22, 1986.

Under § 1433 of the Tax Reform Act of 1986 (Act) and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the GST tax does not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985,

except to the extent the transfer is made from 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 GST tax will not cause the trust to lose its exempt status. In general, unless specifically provided otherwise, the rules contained in this paragraph are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. Thus, 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 gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(C) provides that a judicial construction of a governing instrument to resolve an ambiguity in the terms of the instrument or to correct a scrivener's error will not cause an exempt trust to become subject to the provisions of chapter 13 if the judicial action involves a bona fide issue; and the construction is consistent with applicable state law that would be applied by the highest court of the state.

State Law provides that the court may reform the terms of a trust, even if unambiguous, to conform the terms to the settlor's intention if it is proved by clear and convincing evidence that both the settlor's intent and the terms of the trust were affected by a mistake of fact or law, whether in expression or inducement.

In this case, the trust agreement does not give Child a power of appointment over the accumulated income in Child's Trust and does not expressly specify what happens to accumulated income at Child's death. The trust agreement does contain a "no takers clause" under Article II which provides that if there is no taker for any property at the death of Child, then the property, such as the accumulated income of Child's Trust, will be distributed to Settlor's heirs, determined as if Settlor died intestate and unmarried in State.

Thus, the trust agreement could be interpreted to require that the accumulated income of Child's Trust be distributed to Settlor's heirs, which would include Child's issue and Child's then living siblings and the issue of any deceased sibling. By contrast, the corpus of Child's Trust would be distributed pursuant to Child's limited power of appointment or to Child's then living issue.

These possible constructions of the trust agreement created bona fide issues, *i.e.*, how should accumulated income be disposed of at Child's death and whether or not the accumulated income is subject to Child's limited power of appointment. The trustees petitioned Court to resolve these issues. Court applied State Law and construed the trust agreement in a manner that is consistent with State Law that would

be applied by the highest court of the state. Accordingly, based on the facts submitted and the representations made, we conclude that the proposed modification of Child's Trust will not cause Child's Trust to lose its status as a trust that is exempt from the GST tax under § 2601.

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.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(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.

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.

Sincerely,

Lorraine E. Gardner

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

Enclosures

Copy for § 6110 purposes  
Copy of this letter