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Person To Contact:

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Legend

Settlor
Trust

Trustee 1
Trustee 2
Trustee 3
Child
Grandchild 1
Grandchild 2
Grandchild 1 Trust

Grandchild 2 Trust

Individual

Date 1

Date 2

Date 3

Date 4

Date 5

State

X

Court 1

Court 2

State Statute 1

State Statute 2

Dear _____ :

This letter responds to your authorized representative's letter dated September 18, 2020, and subsequent correspondence, requesting income, estate, gift, and generation-skipping transfer (GST) tax rulings with respect to the proposed division of Trust.

The facts and representations submitted are summarized as follows:

Trust was created under the will of Settlor, dated Date 1. Settlor died on Date 2 (a date prior to September 25, 1985). Settlor was a resident of State. Settlor was survived by her spouse and children. Child is one of Settlor's children. Trustee 1 is currently serving as trustee of Trust.

Article V of Settlor's will provides, in relevant part, that the residue of Settlor's estate is to be held in trust.

Article V.A provides, in relevant part, that the trustee is to divide the trust estate into separate shares of equal value for each child of Settlor then living, and for each lawful descendant then living of each child then deceased leaving one or more lawful descendants. Each separate share is to be held, managed, and distributed as a separate trust.

Article V.B provides, in relevant part, that during the life of Settlor's spouse, the trustee is to pay to any member of the class composed of spouse, child, and child's descendants as much of the income of the separate share then held in trust as trustee deems necessary for support, education, and health of the class members. All of the net income for each fiscal year of such trust not distributed prior to the last day of such year is then to be added to the principal of such separate share.

Article V.C provides, in relevant part, that upon the death of Settlor's spouse, the trustee is to pay the net income of each separate share then held in trust to any member of the class composed of child, and child's descendants in the same manner and upon the same terms and conditions as provided in Article V.B. so long as child is alive or until the distribution of child's separate share to such child, whichever event shall first occur.

Article V.E provides, in relevant part, that if a separate share is provided for Child, Child is not to have, at any time, any right to request the withdrawal of any part of the principal of her separate share, it being Settlor's express intention that Child's rights and interests in such share shall be limited to the rights and interests provided in Articles V.B, V.C, and VI.A.

Article V.G provides, in relevant part, that upon the death of Child, the trustee is to pay and distribute all of the principal and the accrued, accumulated and unpaid net income of Child's separate share to her then living descendants *per stirpes*. Provided, however, that the share or portion thereof payable and distributable to each lawful descendant of Settlor for whose primary benefit the trustee is then holding a separate share or portion thereof in trust is to be added to and become part of the principal and income of such separate share or portion.

Article V.L provides, in relevant part, that anything provided to the contrary notwithstanding with respect to payments of income to any beneficiary, the trustee, in exercising its discretion, is to consider all income and other resources known to the trustee to be available to such beneficiary and limit any amount so paid to the amount that may be reasonably necessary to permit such beneficiary to maintain his or her accustomed standard of living and station in life.

Article VI.A provides, in relevant part, that if, in the sole judgment of the trustee, the aggregate of income payable hereunder and accruing from all other sources known to the trustee to any beneficiary is to be insufficient to provide for his or her suitable care, maintenance, education, and medical attention, the trustee, in the trustee's sole discretion, may pay to or apply for the benefit of such beneficiary a portion of the principal then held in trust.

Article VII.H provides, in relevant part, that in the retention, investment, management and distribution of each separate trust, the trustee is given the full power and authority to make any division or distribution in kind or partly in kind and partly in money and to determine the value of any such property so allotted, divided, or distributed.

Articles IX.A and IX.B provide, in relevant part, that Settlor's husband is to be the trustee of Trust. In the event of the death, resignation, refusal or other inability of Settlor's husband to act as trustee, Settlor nominates Trustee 1 to act as successor trustee.

Article IX.C provides, in relevant part, that in the event of the death, resignation, refusal or other inability of Trustee 1 to act as successor trustee, Settlor nominates Trustee 2 to act as successor trustee.

Article IX.E provides, in relevant part, that upon the resignation of either or both Settlor's husband and Trustee 1, the appointment of his successor is to be determined as hereinafter provided. Upon the resignation of Trustee 2, or any successor in trust thereafter, the person or persons to whom such resignation is delivered is to immediately appoint any bank or trust company wherever situated having a combined capital and surplus of not less than \$x as successor trustee.

On Date 3, in response to a petition by Trustee 1, Court 1 ordered that the provisions of Settlor's will that govern Trust to be modified. Article IX.C was modified to provide that in the event of the death, resignation, refusal, removal, or other inability of Trustee 1 to act as successor trustee, Trustee 3 is to act as successor trustee.

Article IX.E was modified by the Date 3 court order to provide, in relevant part, that upon the death, resignation, refusal, removal or other inability of all and each of Settlor's husband, Trustee 1, Trustee 3, and any successor to act as trustee or successor trustee, the adult beneficiaries of such trust who are then eligible to receive income distributions from such trust and who have capacity, one of whom must be Child, if she is then living, is to have the power, acting by a majority of such beneficiaries, to appoint a successor trustee or co-trustees, by an acknowledged written instrument delivered to the trustee or trustees so appointed. No such successor trustee may be a beneficiary of such trust. Any successor trustee must be a resident of State.

New Article IX.I was added by the Date 3 court order to provide, in relevant part, that Individual is to have the power to remove any trustee. Upon any such removal, a successor trustee is to be appointed as specified in Article IX.E. The removal power is to be exercised by the delivery of an acknowledged written removal notice to the trustee being removed as well as to the successor trustee, if one had been appointed, and is to become effective immediately upon the acceptance of the trusteeship of the newly-appointed successor trustee. Individual is also to have the power to appoint a successor person with authority to remove the trustee in the event that Individual is deceased, incapacitated, or no longer able to act. Any successor appointed under this section must reside in State at the time of appointment and continue to remain a State resident thereafter.

New Article XI.C was added by the Date 3 court order to provide, in relevant part, that any trustee named hereunder is to be exempt from any duty or obligation to diversify the assets of any trust created hereunder. The assets held by one or more of the trusts created hereunder may include interests in partnerships, limited liability companies, or other entities owned in whole or in part by members of Settlor's family. The trustee of each trust created hereunder is authorized to retain any interest in any family-owned entity for as long as the trustee deems such retention to be advisable, without regard to any statute or rule of law to the contrary regarding trust investments, diversification of trust assets, or any other matter involving the administration of trusts.

On Date 4, Trustee 1 filed a petition in Court 2, proposing to divide Trust into two separate trusts of equal value and update Trust's administrative provisions. The petition stated that the likely remainder beneficiaries had significantly different family situations and financial interests since the inception of Trust. Thus, given the beneficiaries' different investment objectives and risk tolerances, the trustee plans to fund the new trusts non-pro rata, but both trusts will be funded with assets of total equal value.

On Date 5, Court 2 ordered that the provisions of Settlor's will that govern Trust to be modified, pending a favorable ruling from the Internal Revenue Service. Article V.A will be modified to provide, in relevant part, that the trustee is to divide the trust estate into separate shares of equal value for each child of Settlor. The trustee is to further divide the separate share set aside for Child into two separate shares of equal value, creating Grandchild 1 Trust for Child and Grandchild 1 and Grandchild 2 Trust for Child and Grandchild 2. Each of Grandchild 1 Trust, Grandchild 2 Trust, and the separate shares created for Settlor's other children are to be held, managed, and distributed as separate trusts.

Article V.C will be modified by the Date 5 court order to provide, in relevant part, that upon the death of Settlor's spouse, the trustee is to pay the net income of each separate share then held in trust to any member of the class composed of Child, the grandchild who is a primary beneficiary of that trust, and that grandchild's descendants in the same manner and upon the same terms and conditions as provided in Article V.B so long as Child is alive. Provided, however, that the common trustee is to determine the aggregate amount of any distribution of net income to Child and each separate aggregate distribution is to be made in equal shares from Grandchild 1 Trust or Grandchild 2 Trust.

Article V.G will be modified by the Date 5 court order to provide, in relevant part, that upon the death of Child, the trustee is to pay and distribute all of the principal and accrued, accumulated and unpaid net income of a trust named for a child of Child to the child of Child for whom the trust is named, if then living, or if not, then to that child's then living descendants *per stirpes*, or if none, then to Child's then living descendants, *per stirpes*. Provided, however, that the share or portion thereof payable and distributable to each lawful descendant of Settlor for whose primary benefit the trustee is then holding a separate share or portion thereof in trust is to be added to and become part of the principal and income of such separate share or portion.

Article VI.A will be modified by the Date 5 court order to add a provision that the common trustee is to determine the aggregate amount of any distribution of principal to Child and each such aggregate distribution is to be made in equal shares from Grandchild 1 Trust and Grandchild 2 Trust.

Article VII.O will be added by the Date 5 court order to provide, in relevant part, that State law will always govern the construction, interpretation, and validity of the provisions of Settlor's will. The trustee may administer any trust created under Settlor's will at any time or times from any jurisdiction (including a jurisdiction outside of the United States) as the trustee may determine is necessary and appropriate.

Article IX.E will be modified by the Date 5 court order to provide, in relevant part, that upon the death, resignation, refusal, removal or other inability of all and each of Settlor's husband, Trustee 1, Trustee 3, and any successor to act as trustee or successor trustee, the adult beneficiaries of such trust who are then eligible to receive

income distributions from such trust and who have capacity are to have the power, acting by a majority of such beneficiaries (one of whom must be Child, if she is then living), to appoint a successor trustee or co-trustees, by an acknowledged written instrument delivered to the trustee or trustees so appointed. No trustee of a separate trust hereunder may be a beneficiary of such trust. Until the death of Child, at least one trustee must be acting concurrently as a trustee of both Grandchild 1 Trust and Grandchild 2 Trust and is referred to as the common trustee.

Article IX.I will be modified by the Date 5 court order to remove the requirement that any individual with authority to remove a trustee must reside in State.

The trustee represents that Trust has been irrevocable since its creation under Article V.A of Settlor's will and that no contributions have been made to Trust since its funding following the administration of Settlor's estate. No other trusts are now held under the terms of Settlor's will.

State Statute 1 provides, in relevant part, that on the petition of a trustee or a beneficiary, a court may order that the trustee be changed, that the terms of the trust be modified, that the trustee be directed or permitted to do acts that are not authorized or that are forbidden by the terms of the trust, that the trustee be prohibited from performing acts required by the terms of the trust, or that the trust be terminated in whole or in part, if because of circumstances not known to or anticipated by the settlor, the order will further the purposes of the trust.

State Statute 2 provides that when distributing trust property or dividing or terminating a trust, a trustee may (1) make distributions in divided or undivided interests; (2) allocate particular assets in proportionate or disproportionate shares; (3) value the trust property for the purposes of acting under section (1) or (2); and (4) adjust the distribution, division, or termination for resulting differences in valuation.

You have requested the following rulings:

1. Modifications of Trust pursuant to the Date 3 court order did not cause Trust to lose its exempt status from the GST tax or otherwise become subject to the GST tax.
2. The proposed modifications under the Date 5 court order will not cause Trust or Grandchild 1 Trust or Grandchild 2 Trust to lose its exempt status from the GST tax or otherwise become subject to the GST tax.
3. The proposed division of Trust under the Date 5 court order will not cause any beneficiary of Trust, Grandchild 1 Trust, or Grandchild 2 Trust to make a gift subject to federal gift tax.

4. The proposed division of Trust under the Date 5 court order will not cause the assets of Trust, Grandchild 1 Trust, or Grandchild 2 Trust to be includible in the gross estate of any beneficiary of such trusts for federal estate tax purposes under § 2035, 2036, 2037, or 2038.
5. The proposed division of Trust under the Date 5 court order to divide Trust and allocate assets of equal value non-pro rata to Grandchild 1 Trust and Grandchild 2 Trust will not cause Trust, Grandchild 1 Trust, Grandchild 2 Trust, or any beneficiary of such trusts to recognize gain or loss from a sale or other disposition of property.¹
6. The proposed division of Trust under the Date 5 court order will not be treated as a distribution from Trust to either Grandchild 1 Trust or Grandchild 2 Trust for federal income tax purposes under § 661 or 662.
7. The adjusted basis and holding periods of the assets of each new trust will be the same as the adjusted basis and holding periods of those assets while held in Trust.

LAW AND ANALYSIS

Rulings 1 and 2

Section 2601 imposes a tax on every generation-skipping transfer. The term “generation-skipping transfer” is defined in § 2611 as a taxable distribution, a taxable termination, and a direct skip.

Under § 1433(a) of the Tax Reform Act of 1986 (Act) and § 26.2601-1(a) of the Generation-Skipping Transfer Tax Regulations, the 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), the GST tax does not apply to a transfer under a trust that was irrevocable on September 25, 1985, but only to the extent that such transfer is 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) 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 under § 26.2601-1(b) will not cause the trust to lose its exempt status.

¹ The taxpayer has requested a ruling that the trust division will not cause the recognition of any income in addition to gain or loss. Our office is unable to issue a “blanket” ruling concerning the recognition of ordinary income or loss, including such items as dividends and interest. Such a ruling would be overbroad and would have to take into account the timing of such items of income including under assignment of income principles.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust, by judicial reformation or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the GST tax 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. 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. A modification that is administrative in nature that only indirectly increases the amount transferred will not be considered to shift a beneficial interest in the trust.

Section 26.2601-1(b)(4)(i)(E), Example 4, considers the following situation. In 1980, Grantor, who was domiciled in State X, executed an irrevocable trust for the benefit of Grantor's issue, naming a State X bank as trustee. Under the terms of the trust, the trust is to terminate, in all events, no later than 21 years after the death of the last to die of certain designated individuals living at the time the trust was executed. The provisions of the trust do not specify that any particular state law is to govern the administration and construction of the trust. In State X, the common law rule against perpetuities applies to trusts. In 2002, a State Y bank is named as sole trustee. The effect of changing trustees is that the situs of the trust changes to State Y, and the laws of State Y govern the administration and construction of the trust. State Y law contains no rule against perpetuities. In this case, however, in view of the terms of the trust instrument, the trust will terminate at the same time before and after the change in situs. Accordingly, the change in situs does not shift any 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 transfer. Furthermore, the change in situs does not extend the time for vesting of any beneficial interest in the trust beyond that provided for in the original trust. Therefore, the trust will not be subject to the provisions of chapter 13.

Section 26.2601-1(b)(4)(i)(E), Example 5, illustrates a situation where a trust that is otherwise exempt from the GST tax is divided into two trusts. Under the facts presented, the division of a trust into two trusts does not shift any 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 division, and the division does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. Accordingly, the two partitioned trusts will not be subject to the GST tax.

Section 26.2601-1(b)(4)(i)(E), Example 10, considers the following situation. In 1980, Grantor established 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.

In this case, Trust will be divided into two new equal trusts, Grandchild 1 Trust and Grandchild 2 Trust. Child, Grandchild 1, and Grandchild 1's descendants will be the beneficiaries of Grandchild 1 Trust. Child, Grandchild 2, and Grandchild 2's descendants will be the beneficiaries of Grandchild 2 Trust. Additionally, several administrative provisions of Trust, including trustee succession provisions, will also be modified. There is also a new provision that maintains that Trust will be governed by State law, but will allow the trustee to administer the new trusts from any jurisdiction that the trustee may determine is necessary and appropriate. The proposed modifications will not result in a shift of any beneficial interest in the trusts to any beneficiary who occupies a generation lower than the persons holding the beneficial interests. Further, the proposed modifications will not extend the time for vesting of any beneficial interest in the new trusts beyond the period provided for in Trust. Accordingly, based on the facts submitted and the representations made, we conclude that the modifications of Trust pursuant to the Date 3 court order as well as the proposed modifications to Trust pursuant to the Date 5 court order will not cause Trust, Grandchild 1 Trust, or Grandchild 2 Trust to lose its exempt status from the GST tax or otherwise become subject to the GST tax.

Ruling 3

Section 2501(a)(1) imposes a tax for each calendar year on the transfer of property by gift by any individual.

Section 2511(a) provides that the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2512(a) provides that if the gift is made in property, the value thereof at the date of the gift is considered the amount of the gift.

Section 2512(b) provides that where property is transferred for less than adequate and full consideration in money or money's worth, then the amount by which the value of the property exceeded the value of the consideration is deemed to be a gift, and is included in computing the amount of gifts made during the calendar year.

In this case, the beneficiaries of Grandchild 1 Trust and the beneficiaries of

Grandchild 2 Trust will have the same interests after the division that they had as beneficiaries under Trust. Because the beneficial interests of the beneficiaries are substantially the same, both before and after the proposed division, no transfer of property will be deemed to occur as a result of the division of Trust. Accordingly, based on the facts submitted and the representations made, we conclude that the proposed division will not cause any beneficiary of Trust, Grandchild 1 Trust, or Grandchild 2 Trust to have made a gift subject to federal gift tax.

Ruling 4

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 value of the gross estate includes the value of all property to the extent of the interest therein of the decedent at the time of death.

Section 2035(a) provides that if (1) the decedent transferred an interest in property or relinquished a power with respect to any property, during the 3-year period ending on the date of the decedent's death, and (2) the value of the property (or interest therein) would have been included in the gross estate under § 2036, 2037, 2038, or 2042 if the interest or power had been retained by the decedent on the date of death, then the value of the gross estate shall include the value of any property (or interest therein) that would have been so included. Under § 2035(b), the gross estate shall be increased by the amount of any gift tax paid by the decedent or his estate on any gift made by the decedent or his spouse during the 3-year period ending on the date of the decedent's death.

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 2037(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, if (1) possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent, and (2) the decedent has retained a reversionary interest in the property, and the value of such reversionary interest immediately before the death of the decedent exceeds 5 percent of the value of such property.

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, either by the decedent alone or in conjunction with any person, to alter, amend, revoke, or terminate, or where the decedent relinquished any such power during the 3-year period ending on the date of the decedent's death.

In order for §§ 2036 through 2038 to apply, the decedent must have made a transfer of property or any interest therein (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth) under which the decedent retained an interest in, or power over, the income or corpus of the transferred property. In the present case, the proposed division of Trust does not constitute a transfer within the meaning of §§ 2036 through 2038. The beneficiaries of Grandchild 1 Trust and the beneficiaries of Grandchild 2 Trust will have the same interests after the division that they had as beneficiaries under Trust. Accordingly, based on the facts submitted and the representations made, we conclude that the proposed division of Trust will not cause the assets of Trust, Grandchild 1 Trust, or Grandchild 2 Trust to be includible in the gross estate of any beneficiary of such trusts for federal estate tax purposes under § 2035, 2036, 2037, or 2038.

Ruling 5

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized.

Section 1001(b) states that the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Under § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under § 1001, on the sale or exchange of property shall be recognized.

Section 1.1001-1(a) of the Income Tax Regulations provides that the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or loss sustained.

Section 1.1001-1(h)(1) provides that the severance of a trust is not an exchange of property for other property differing materially either in kind or in extent if -- (i) an applicable state statute or the governing instrument authorizes or directs the trustee to sever the trust, and (ii) any non-pro rata funding of the separate trusts resulting from the severance whether mandatory or in the discretion of the trustee, is authorized by an applicable state statute or governing instrument.

In this case, Settlor's will provides the terms governing distribution of Trust for Child and her descendants. It is represented that the proposed division of Trust into two equal separate trusts will be funded with assets of equal value. In addition, the trustee is authorized by both the will's express terms under Article VII.H and State Statute 2 to make non-pro rata allocations of trust property in a severance. Given the beneficiaries' different investment objectives and risk tolerances, the trustee plans to fund the new equal separate trusts non-pro rata, but both trusts will be funded with assets of total equal value. In addition, Trust will receive nothing in exchange for its allocation of trust assets among the new trusts. Grandchild 1 Trust and Grandchild 2 Trust will transfer nothing to Trust in exchange for their receipt of assets from Trust. Further, the proposed division does not shift beneficial interests in Trust among the beneficiaries who will enjoy equivalent legal entitlements before and after the proposed division. Accordingly, based on the facts submitted and the representations made we conclude that the proposed division of Trust will not cause Trust, Grandchild 1 Trust, Grandchild 2 Trust, or any beneficiary of any such trust to recognize any gain or loss from a sale or other disposition of Trust assets under §§ 61 and 1001.

Ruling 6

Section 661(a) provides that in any taxable year a deduction is allowed in computing the taxable income of a trust (other than a trust to which subpart B applies), for the sum of (1) the amount of income for such taxable year required to be distributed currently; and (2) any other amounts properly paid or credited or required to be distributed for such taxable year.

Section 1.661(a)-2(f) of the Income Tax Regulations provides that gain or loss is realized by the trust or estate (or the other beneficiaries) by reason of a distribution of property in kind if the distribution is in satisfaction of a right to receive a distribution of a specific dollar amount, of specific property other than that distributed, or of income as defined under § 643(b) and the applicable regulations, if income is required to be distributed currently.

Section 662 provides that there shall be included in the gross income of a beneficiary to whom an amount specified in § 661(a) is paid, credited, or required to be distributed (by an estate or trust described in § 661), the sum of the following amounts: (1) the amount of income for the taxable year required to be distributed currently to such beneficiary, whether distributed or not; and (2) all other amounts properly paid, credited, or required to be distributed to such beneficiary for the taxable year.

A partition of jointly-owned property is not a sale or other disposition of property where the co-owners of the joint property sever their joint interests, but do not acquire a new or additional interest as a result thereof. Thus, neither gain nor loss is realized on a partition. See Rev. Rul. 56-437, 1956-2 C.B. 507 (conversion of a joint tenancy in stock to a tenancy in common in order to eliminate the survivorship feature and the partition of a joint tenancy in stock are not sales or exchanges).

Similarly, divisions of trusts are also not sales or exchanges of trust interests where each asset is divided pro rata among the new trusts. See Rev. Rul. 69-486, 1969-2 C.B. 159 (pro rata distribution of trust assets not a sale or exchange). Rev. Rul. 69-486 involved two beneficiaries of a trust who by mutual agreement, requested that the trustee distribute all of the trust corpus consisting of notes to one of the beneficiaries and all of the trust corpus consisting of common stock to the other beneficiary. The trust instrument as well as local law was silent regarding whether the trustee had the authority to make such a non-pro rata distribution of property in kind. Because the trustee was not specifically authorized to make an allocation of specific property in kind, the beneficiaries were treated as having an absolute right to a ratable in-kind distribution. Rev. Rul. 69-486 treated the beneficiaries as receiving the notes and common stock pro rata, followed by an exchange between the beneficiaries giving all of the common stock to one and all of the notes to the other. Because, in substance, an exchange between the beneficiaries was deemed to occur, Rev. Rul. 69-486 held that the beneficiaries recognized gain under §§ 1001 and 1002. Thus, non-pro rata distributions from trusts have the potential for being treated as pro rata distributions to beneficiaries and then an exchange of the assets between the trusts which can recognize gain or loss.

In this case, as stated above, Trust's assets will be distributed equally among Grandchild 1 Trust and Grandchild 2 Trust, with each successor trust containing an equal share of the assets of Trust. State Statute 2 authorizes the trustees to divide Trust; and any non-pro rata funding of the new trusts resulting from the modifications and division, whether mandatory or in the discretion of the trustee, is authorized by the governing instrument under Article VII.H. Accordingly, based on the facts submitted and the representations made, we conclude that the proposed division is not a distribution under § 661 or § 1.661(a)-2(f). We further conclude that the proposed division of Trust assets will not cause Trust, Grandchild 1 Trust, Grandchild 2 Trust, or any beneficiary of any such trust to recognize any income, gain, or loss under § 662.

Ruling 7

Section 1015(b) provides that if property is acquired after December 31, 1920, by a transfer in trust (other than a transfer in trust by a gift, bequest, or devise), the basis shall be the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor on such transfer.

Section 1.1015-2(a)(1) provides that in the case of property acquired after December 31, 1920, by transfer in trust (other than by transfer in trust by gift, bequest, or devise), the basis of property so acquired is the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor on the transfer under the law applicable to the year in which the transfer was made. If the taxpayer acquired the property by transfer in trust, this basis applies whether the property is in the hands of the trustee or the beneficiary, and whether acquired prior to termination of the trust and distribution of the property, or thereafter.

Section 1223(2) provides that in determining the period for which the taxpayer has held property, however it is acquired, there shall be included the period for which the property was held by any other person, if under this chapter such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as it would have in the hands of the other person.

In this case, as stated above, § 1001 does not apply to the proposed transaction. Thus, after the division of Trust and transfer of the assets into the new trusts, the basis in each asset will be the same in Grandchild 1 Trust and Grandchild 2 Trust as it was in Trust under § 1015. Furthermore, we conclude that, under § 1223(2), the holding period of the assets received by the new trusts will be the same as the holding period of the assets in Trust.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

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 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.

The rulings 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) provides that it may not be used or cited as precedent.

Sincerely,

Leslie H. Finlow

Leslie H. Finlow
Senior Technician Reviewer, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures

Copy for § 6110 purposes
Copy of this letter

cc: