

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Number: **202432016**

Release Date: 8/9/2024

Index Number: 2601.00-00

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B04

PLR-122895-23

Date:

May 08, 2024

Re:

Legend

Settlor =

Settlor's Spouse =

Child 1 =

Child 2 =

Foundation =

Trust =

Grandchild 1 =

Grandchild 2 =

Grandchild 3 =

Grandchild 4 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

State =

State Court =

Citation 1 =

Citation 2 =

Citation 3 =

Citation 4 =

On Date 6, Trustees filed in State Court a petition for construction of the term “per stirpes” and modification of terms to divide Trust. The petition states that if the State Court determines the language of Trust requires Trust to be divided at the generation level of Child 1 and Child 2, then Trust is to be divided into two separate trusts in equal value based on the family lines of Child 1 and Child 2: Child 1 Trust and Child 2 Trust. Each trust will be identical to the terms of Trust with the following modifications: (1) Child 1 Trust will pay all of its net income to the issue of Child 1 living at the time such net income is paid, per stirpes, and Child 2 Trust will pay all of its net income to the issue of Child 2 living at the time such net income is paid, per stirpes; (2) upon the termination of Child 1 Trust, the trust estate will be distributed to the issue of Child 1 then living, per stirpes, and upon the termination of Child 2 Trust, the trust estate will be distributed to the issue of Child 2 then living, per stirpes; (3) if at any time there is no living issue of Child 1, the remaining assets of the Child 1 Trust shall be added to the Child 2 Trust, and if at any time there is no living issue of Child 2, the remaining assets of the Child 2 Trust shall be added to the Child 1 Trust; (4) the trustees of Child 1 Trust shall be Grandchild 1 and Grandchild 4 (children of Child 1), and the trustees of Child 2 Trust shall be Grandchild 2 and Grandchild 3 (children of Child 2). Child 1 Trust and Child 2 Trust shall be subject to the same termination provisions of Trust, including the Trust termination date.

On Date 7, State Court issued Order determining that State law requires a division of Trust at the generation level of Child 1 and Child 2 and approving the proposed division of Trust, subject to a favorable private letter ruling from the Internal Revenue Service.

It is represented that there have been no additions, constructive or actual, to Trust after September 25, 1985.

You have requested the following rulings:

1. State Court’s construction of Trust will not affect the exempt status of Trust for purposes of the GST tax and will not result in a transfer of property that will subject Trust or distributions thereunder to the GST tax imposed under § 2601.
2. State Court’s modification to divide Trust into two separate equal trusts, Child 1 Trust and Child 2 Trust, will not cause Trust, Child 1 Trust or Child 2 Trust, to lose its status as exempt from the GST tax.

LAW AND ANALYSIS

Section 2601 imposes a tax on every generation-skipping transfer (GST), which is defined under § 2611 as a taxable distribution, taxable termination, and a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (Act) and § 26.2601-1(b)(1) of the Generation-Skipping Transfer Tax Regulations provide that the GST tax shall not apply to any GST under a trust that was irrevocable on September 25, 1985, but shall apply to

the extent that the 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)(1), (2), or (3) will not cause the trust to lose its exempt status. The regulation provides that the rules contained in the paragraph are applicable only for purposes of determining whether an exempt trust retains its exempt status for GST 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)(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 be subject to the GST provisions if: (1) the judicial action involves a bona fide issue; and (2) the construction is consistent with applicable state law that would be applied by the highest court of the state.

Section 26.2601-1(b)(4)(i)(E), *Example 3*, considers a situation where, in 1980, Grantor established an irrevocable trust for the benefit of Grantor's children, A and B, and their issue. The trust is to terminate on the death of the last to die of A and B, at which time the principal is to be distributed to their issue. However, the provision governing the termination of the trust is ambiguous regarding whether the trust principal is to be distributed per stirpes, only to the children of A and B, or per capita among the children, grandchildren, and more remote issue of A and B. In 2002, the trustee filed a construction suit with the appropriate local court to resolve the ambiguity. The court issued an order construing the instrument to provide for per capita distributions to the children, grandchildren, and more remote issue of A and B living at the time the trust terminates. The court's construction resolves a bona fide issue regarding the proper interpretation of the instrument and is consistent with applicable state law as it would be interpreted by the highest court of the state. Therefore, the trust will not be subject to the GST tax.

In *Commissioner v. Estate of Bosch*, 387 U.S. 456 (1967), the Court considered whether a state trial court's characterization of property rights conclusively binds a federal court or agency in a federal estate tax controversy. The Court concluded that the decision of a state trial court as to an underlying issue of state law should not be controlling when applied to a federal statute. Rather, the highest court of the state is the best authority on the underlying substantive rule of state law to be applied in the federal matter. If there is no decision by that court, then the federal authority must apply what it finds to be state law after giving "proper regard" to the state trial court's determination and to relevant rulings of other courts of the state. In this respect, the federal agency may be said, in effect, to be sitting as a state court.

Section 26.2601-1(b)(4)(i)(D) 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)), 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. 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. However, a modification that is administrative in nature that only indirectly increases the amount transferred (for example, by lowering administrative costs or income taxes) will not be considered a shift in a beneficial interest in a trust.

Section 26.2601-1(b)(4)(i)(E), *Example 5*, illustrates a situation where, in 1980, Grantor established an irrevocable trust for the benefit of Grantor's two children, A and B, and their issue. Under the terms of the trust, the trustee has the discretion to distribute income and principal to A, B, and their issue in such amounts as the trustee deems appropriate. On the death of the last to die of A and B, the trust principal is to be distributed to the living issue of A and B, per stirpes. In 2002, the appropriate local court approved the division of the trust into two equal trusts, one for the benefit of A and A's issue and one for the benefit of B and B's issue. The trust for A and A's issue provides that the trustee has the discretion to distribute trust income and principal to A and A's issue in such amounts as the trustee deems appropriate. On A's death, the trust principal is to be distributed equally to A's issue, per stirpes. If A dies with no living descendants, the principal will be added to the trust for B and B's issue. The trust for B and B's issue is identical (except for the beneficiaries), and terminates at B's death at which time the trust principal is to be distributed equally to B's issue, per stirpes. If B dies with no living descendants, principal will be added to the trust for A and A's issue. The division of the 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. In addition, the division does not extend the time for vesting of any beneficial interest in the trust beyond the period provided in the original trust. Therefore, the two partitioned trusts resulting from the division will not be subject to the provisions of chapter 13.

Trust is governed by the laws of State. Statute 1 provides that the court may hear and determine all matters pertaining to the administration of inter vivos trusts. Statute 2 provides that a trustee may divide a trust into two or more separate trusts, if the result does not impair rights of any beneficiary or adversely affect achievement of the purposes of the trust.

Under State law it is well settled that the settlor's intent controls the interpretation of trust instruments. See *Citation 1*. Consequently, State courts determine and enforce the settlor's intent for the disposition of his property when the language of the instrument is ambiguous. *Citation 2*. State courts will look to the instrument itself and find the settlor's intent, "by what the [trust] actually says and not by what [the court] might imagine...". *Id.*

In this case, the ambiguous terms of Trust present a bona fide issue regarding the meaning of "per stirpes" as used in the Trust and at which generation level the initial distribution is to be made. State Court's construction of the ambiguous terms is consistent with applicable state law that would be applied by the highest court of the state. See *Citation 3* and *Citation 4*. Accordingly, based on the facts submitted and the representations made, we conclude that State Court's construction of Trust will not affect the exempt status of Trust for purposes of the GST tax and will not result in a transfer of property that will subject Trust or distributions thereunder to the GST tax imposed under § 2601.

Further, the proposed modification to divide Trust into Child 1 Trust and Child 2 Trust will not result in a shift of any beneficial interest to any beneficiary who occupies a generation lower than the persons holding the beneficial interests prior to the modification and division. The proposed modification to divide Trust will not extend the time for vesting of any beneficial interest beyond the period provided for in Trust. Accordingly, based on the facts submitted and the representations made, we conclude that State Court's modification to divide Trust will not cause Trust, Child 1 Trust or Child 2 Trust, to lose its status as exempt from the GST tax.

Except as expressly provided herein, we neither express nor imply any opinion 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 taxpayers accompanied by penalty of perjury statements executed by the appropriate parties. While this office has not verified the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayer requesting it. Section 6100(k)(3) provides that it may not be used as precedent.

Sincerely,

Melissa C. Liquerman
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure

Copy for § 6110 purposes

cc:

cc: