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Person To Contact: ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B04
PLR-106911-24
Date:
September 26, 2024

Legend

- Husband =
- Wife =
- Grandchild 1 =
- Grandchild 2 =
- Grandchild 3 =
- Trust 1 =
- Trust 1A =
- Trust 2A =
- Trust 3A =
- Probate Court =
- State Court =

- Settlement Agreement =

- Supplemental Settlement Agreement =

- State Statute =
- a =
- b =
- Date 1 =
- Date 2 =
- Date 3 =
- Date 4 =
- Date 5 =
- Date 6 =
- Date 7 =

Dear _____ :

This letter responds to your authorized representative's letter dated April 5, 2024 and subsequent correspondence, requesting a generation-skipping transfer (GST) tax ruling with respect to the proposed modifications of Trust 1A.

The facts and representations submitted are summarized as follows:

On Date 1, a date prior to September 25, 1985, Husband and Wife created five irrevocable trusts with substantively similar terms for different beneficiaries. Trust 1 was created for the primary benefit of Grandchild 1. The other trusts were created for the primary benefit of Grandchild 2, Grandchild 3, and two other family members who are no longer living. At the time of this ruling submission, Grandchild 1, Grandchild 2, and Grandchild 3 were living.

Article I of Trust 1 provides that the trustees are to pay to or for the benefit of Grandchild 1 so much of the net income from Trust 1 as the trustees in their sole discretion shall determine to be necessary and desirable to provide for the health, education, maintenance, and support (HEMS) of said beneficiary. In the event that the net income is not sufficient to provide for the health, education, maintenance, and support of said beneficiary, then the trustees may use such part of the principal as, from time to time, in their sole discretion, they may determine to be necessary for such purposes.

Article II of Trust 1 provides that, upon the death of Grandchild 1, the trustees are to pay to or for the benefit of the issue of Grandchild 1 such part of the net income from Trust 1 as the trustees in their sole discretion shall determine to be necessary and desirable to provide for the health, education, maintenance, and support of such issue. In the event the trustees determine that the net income is not sufficient to provide for the health, education, maintenance, and support of any one or more of such issue, then the trustees may use such part of the principal as, from time to time, in their sole discretion, they may determine to be necessary for such purposes.

Article III of Trust 1 provides that, in the event Grandchild 1 and all issue of Grandchild 1 die prior to the final distribution of Trust 1 properties, the remaining Trust 1 properties, principal, and any accumulated income, shall be paid over and delivered in equal shares among the other trusts then in existence, namely the trusts benefiting Grandchild 2 and Grandchild 3.

Article XII of Trust 1 provides that Trust 1 will terminate 21 years after the last to die of Grandchild 1, Grandchild 2, and Grandchild 3. Upon termination, all of the properties remaining in Trust 1 shall be distributed to the then living beneficiaries of Trust 1, share and share alike.

On Date 2, Grandchild 1, petitioned Probate Court, pursuant to State Statute, to modify Trust 1. Probate Court approved the petition by order dated Date 3. Under the Date 3 court order, Trust 1 was divided into two trusts: existing Trust 1 and new Trust 1A. Trust 1A was formed and funded from the real estate assets in Trust 1 that were separated from the other assets in Trust 1. Under equivalent circumstances per the Date 3 court order, Trust 2A and Trust 3A have been formed for the real estate assets held under the trusts benefiting Grandchild 2 and Grandchild 3.

Under the Date 3 court order, the beneficiaries of Trust 1A agree to consider, and the trustees of Trust 1A agree to utilize, the income and principal of Trust 1 first for the beneficiaries' HEMS distributions. The court order provided that the governing instrument of Trust 1A will provide that in making distributions in accordance with the HEMS standard, the trustees are to take into consideration a beneficiary's distributions of income and principal received from Trust 1 and other sources of income.

Under the Date 3 court order, the beneficiaries of Trust 1A and the beneficiaries of Trust 1 are and will be the same and each beneficiary has an identical interest in Trust 1A as each has in Trust 1. However, the court order provides that the trustees of Trust 1A will make all transfers and distributions to the trustee of Trust 1 in order to satisfy any transfers or distributions the trustees of Trust 1A may be required to make to Trust 1 or its beneficiaries under the governing instrument of Trust 1A, by law, or under Settlement Agreement, so that no distributions will be made directly from Trust 1A to the beneficiaries.

Pursuant to the Date 3 court order and other judicial trust modification judgments, Trust 1A is to terminate on the earlier of: Date 6 (less than 21 years from the current date) or the failure of the trustees to do any one or more of the following: (1) distribute to Trust 1 the amount by which the value of Trust 1A's cumulative liquid assets exceeds \$a; (2) distribute at least annually to Trust 1, one-half of the cumulative amount of net cash used in investing activities for all of the subsidiaries of Trust 1A; (3) and maintain a debt to asset ratio of b percent or less in each subsidiary of the trust. Upon termination, the assets of Trust 1A are to be distributed to Trust 1.

In PLR 201642030, the Internal Revenue Service previously ruled favorably that the division and modification of Trust 1 pursuant to the Date 3 court order did not cause any trust to be subject to the provisions of chapter 13.

Since the issuance of the prior ruling, issues concerning the administration of Trust 1A have arisen. The beneficiaries and the trustees entered into a Supplemental Settlement Agreement on Date 4. The Supplemental Settlement Agreement proposes to modify Trust 1A as follows: (1) extend the termination date of Trust 1A from Date 6 to Date 7 (less than 21 years from the current date); (2) allow for an early termination of Trust 1A, based upon the majority vote of the distributees of Trust 1A, Trust 2A, and Trust 3A; (3) allow the trustees of Trust 1A to make discretionary distributions to Trust 1 by considering the best interests of the primary beneficiaries of Trust 1A in addition to

the existing HEMS standard; and (4) eliminate the provision requiring the trustees to distribute at least annually one-half of the cumulative amount of net cash used in investing activities for all of the subsidiaries of Trust 1A to Trust 1. On Date 5, State Court approved the terms of the Supplemental Settlement Agreement pending a favorable private letter ruling issued by the Service.

The trustees of Trust 1A represent that no additions have been made to Trust 1A after September 25, 1985.

You have requested the following ruling:

Neither the transactions nor the trust modifications set forth in the Supplemental Settlement Agreement will cause Trust 1A to lose its status as exempt from the provisions of chapter 13 and that any distributions or terminations of interests therein will not be subject to the GST tax.

Ruling

Section 2601 imposes a tax on every GST made after October 26, 1986. A GST is defined under § 2611(a) as (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 2612(a) provides that the term “taxable termination” means a termination (by death, lapse of time, release of a 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 the term “taxable distribution” means any distribution from a trust to a skip person (other than a taxable termination or a direct skip).

Under § 2612(c)(1), a direct skip is a transfer subject to federal estate or gift tax of an interest in property to a skip person.

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 GSTs 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). Under § 26.2601-1(b)(1)(ii), any trust in existence on September 25, 1985, will be considered irrevocable unless the settlor had a power that would have caused inclusion of the trust in his or her gross estate under § 2038 or § 2042, if the settlor had died on 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 under § 26.2601-1(b)(1), (2), or (3) (hereinafter referred to as an exempt trust) will not cause the trust to lose its exempt status. In general, unless specifically provided otherwise, the rules contained in § 26.2601-1(b)(4) are applicable only for purposes of determining whether an exempt trust retains its exempt status for GST tax purposes. Thus (unless specifically noted), 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)(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)) 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 § 26.2601-1, 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. 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 to shift a beneficial interest in the trust.

In the present case, the trustees are proposing to modify the termination date of Trust 1A. The termination date is extended from Date 6 to Date 7 and the conditions for when termination can occur prior to Date 7 are also modified. However, all distributions from Trust 1A, including distributions made upon the termination of Trust 1A, are only made to Trust 1. No distributions will be made directly from Trust 1A to the beneficiaries. The extended termination date of Trust 1A is still prior to the termination date of Trust 1, 21 years after the last to die of Grandchild 1, Grandchild 2, and

Grandchild 3. Thus, the modification will not extend the time for vesting of any beneficial interest in Trust 1A beyond the period provided for in the original trust, Trust 1. In addition, the modification will not shift any beneficial interest in Trust 1A 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. Accordingly, based upon the facts submitted and the representations made, we conclude that the trust modifications set forth in the Supplemental Settlement Agreement will not cause Trust 1A to lose its status as exempt from the provisions of chapter 13 and that distributions or terminations of interests therein subject to the GST tax.

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

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 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.

A copy of this letter should be attached to any gift, estate, or GST tax returns that you may file relating to this matter.

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,

Melissa Liquerman

[Melissa Liquerman]
Senior Counsel, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

PLR-106911-24

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Enclosure:

Copy for § 6110 purposes

cc: