

Internal Revenue Service

Department of the Treasury

Number: **200218035**
Release Date: 5/3/2002
Index Number: 2601.00-00

Washington, DC 20224

Person to Contact:

Telephone Number:
(202) 622-7830
Refer Reply To:
CC:PSI:B09 / PLR-102182-02
Date:
February 06, 2002

Legend

Trust =

C1 =
P =
C2 =
State =
a =

Dear Sir or Madam:

In a letter, dated March 5, 1998, and prior correspondence, you requested the following rulings concerning the estate, gift, and generation-skipping transfer (GST) tax consequences of a judicial construction and modification of a trust that is exempt from the GST tax imposed under Internal Revenue Code section 2601:

1) Modification of the Trust (including both modification following judicial interpretation and construction and modification requested by consent of the beneficiaries) will not cause the Trust to lose its status as a trust that was created and was irrevocable prior to September 25, 1985, and the Trust will therefore continue to be exempt from the GST tax.

2) Modification of the Trust (including both modification following judicial interpretation and construction and modification requested by consent of the beneficiaries) will not be deemed to result in additions or constructive additions to the Trust.

3) Provided no additions are made to the Trust after the Trust is construed and modified, future distributions from the Trust will be exempt from the GST tax.

4) The beneficiaries' consent to the construction and modification of the Trust will

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not be deemed to be a transfer for gift tax purposes and will not constitute a taxable gift pursuant to § 2501.

5) The proposed modification permitting beneficiaries to be appointed successor trustees will not cause the corpus of the Trust to be includible in the gross estates of any such beneficiaries.

The facts and representations submitted are as follows: C1 is the current trustee and income beneficiary of the Trust, one of the trusts established under P's will. The Trust at issue was irrevocable on September 25, 1985, and no additions have been made to the Trust after that date.

Under the terms of the Trust as set forth in the Decree Establishing Testamentary Trusts and Ordering Preliminary Distribution Thereto ("Decree"), P's husband was appointed trustee and was directed to divide the assets that constituted the trust estate into two equal shares, one in the name of C1 (Trust) and one in the name of C2. Each share is currently being administered as a separate trust.

C1 determined that certain dispositive provisions were ambiguous and petitioned the superior court of State for guidance. C1 determined the Trust provisions were ambiguous with respect to a) which grandchildren were the beneficiaries of the trusts upon the death of C1 and C2; 2) whether separate trusts were to be established at C1's death for the benefit of C1's then living children and issue of deceased children; and 3) whether C1's children and issue of deceased children were entitled to all of the income from their trust or whether the trustee had discretion to distribute the income. C1 also determined that the provisions of the Trust concerning the administration of the trusts established for P's living grandchildren and issue of deceased grandchildren were silent concerning distribution of the trusts upon the death of its last surviving beneficiaries.

C1 also petitioned the court to change the provisions of the Trust concerning the appointment of successor trustees to provide, in part, that if C1 ceases to act as trustee of any trust, all of the then living children of C1 shall act as co-trustees of that trust. C1's court petition provided that beneficiaries who serve as co-trustees will not have the power or discretion to distribute income or principal to themselves or a class of beneficiaries of which they are members.

The court's "Order Construing Trust Instrument and Modifying Irrevocable Trust with the Consent of all Beneficiaries ("Order")" was filed on a. The court found that certain provisions of the Trust were ambiguous and reasonably susceptible to more than one interpretation. In its Order, the court found the following: 1) that upon the death of C1, the Trust is to be held only for the benefit of C1's then living children and issue of deceased children; 2) upon the death of C1, separate trusts for the benefit of C1's then living children and issue of deceased children are to be established; 3) distributions to C1's children and issue of deceased children of C1 will be discretionary; and 4) upon the death of the last surviving beneficiary of each trust, any remaining assets shall be distributed to that beneficiary's then living issue by right of

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representation, or if there are none, to the then living issue of the beneficiary's nearest ancestor who has then living issue and who is a member of the class composed of P and P's issue, by right of representation.

The Order also modified the provisions concerning appointment of successor trustees to provide in part that if C1 ceases to act as trustee, all of the then living children of C1 shall act as co-trustees. The modification provides that if at any time a trustee of any trust, but for this provision would thereby have a discretionary power with respect to the distribution of principal and/or net income of that trust which could be exercised in favor of that trustee and/or any person or persons to whom he or she owes an obligation of support, said trustee shall have no power or authority to exercise or participate in the exercise of any discretion to distribute or not distribute which shall directly or indirectly affect the amount of property distributable to said trustee and/or any person to whom he or she is obligated to support, or which shall affect the time or times at which said distributions are made. Further, the Order provided that if a beneficiary is serving as a trustee, at least one person who is not a beneficiary must serve as a trustee.

LAW AND ANALYSIS:

(a) RULINGS 1, 2, AND 3 -- THE EXEMPT STATUS OF THE TRUSTS FOR GST TAX PURPOSES

Section 2601 imposes a tax on every generation-skipping transfer made by the "transferor" to a "skip-person." Section 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provides that the tax does not apply to any generation-skipping transfer under a trust (as defined in § 2652(b)) that was irrevocable on September 25, 1985. The rule of the preceding sentence does not apply to a pro rata portion of any generation-skipping transfer under an irrevocable trust if additions are made to the trust after September 25, 1985.

Section 26.2601-1(b)(1)(ii) provides that, except as provided in § 26.2601-1(b)(1)(ii)(B) or (C), any trust in existence on September 25, 1985, is considered an irrevocable trust.

Section 2611 defines the term "generation-skipping transfer" as (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 2613(a) provides that the term "skip person" means --

(1) a natural person assigned to a generation that is two or more generations below the generation assignment of the transferor, or

(2) a trust --

(A) if all interests in such trust are held by skip persons, or

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(B) if --

(i) there is no person holding an interest in the trust, and

(ii) at no time after such transfer may a distribution (including distributions on termination) be made from such trust to a non-skip person.

An amendment to an exempt trust that modifies or otherwise changes the quality, value, or timing of any of the powers, or beneficial interests, rights, or expectancies originally provided under the terms of the trust will cause the trust to lose its exemption from the GST tax.

Based upon the information submitted and representations made, the court's clarification and interpretation of the ambiguous provisions did not change the quality, value, or timing of any of the powers, beneficial interests, rights, or expectancies originally provided. With respect to the modification of the successor trustee provisions, these modifications were administrative in nature and do not result in any change in the quality, value, or timing of any of the powers, beneficial interests, rights, or expectancies originally provided.

Accordingly, the modification of the Trust (including both modification following judicial interpretation and construction and modification requested by consent of the beneficiaries) did not cause the Trust to lose its status as a Trust that was created and was irrevocable prior to September 25, 1985. Further, we conclude that modification of the Trust did not result in additions or constructive additions to the Trust. Provided no additions are made to the Trust, future distributions from the Trust will be exempt from the GST tax.

(b) RULING 4 -- THE GIFT TAX CONSEQUENCES OF THE BENEFICIARIES' CONSENT TO THE MODIFICATIONS

Section 2501 imposes a tax on an individual's transfer of property by gift. Section 2511 provides, in part, that the tax imposed by Section 2501 shall apply 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(b), provides, in part, 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 shall be deemed a gift.

Based upon the information submitted and representations made, we conclude that the modification of the successor trustee provisions were modifications that were administrative in nature and do not result in any change in the quality, value, or timing of any of the powers, beneficial interests, rights, or expectancies originally provided. Therefore, we conclude that the beneficiaries' consent to the construction and

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modification of the Trust was not a transfer for gift tax purposes and does not constitute a taxable gift pursuant to § 2501.

(c) RULING 5 -- INCLUSION OF THE TRUST CORPUS IN A BENEFICIARY'S GROSS ESTATE

Section 2041 provides that the value of the gross estate shall include the value of all property with respect to which the decedent has at the time of his death a general power of appointment, or with respect to which the decedent has at any time released or exercised such power of appointment by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 through 2038.

Section 2041(b) provides, in part, that a general power of appointment is a power which is exercisable in favor of the decedent, his estate, his creditors or the creditors of his estate.

Distributions that are made to a person acting as trustee (or to a class of which such person is a member) are to be made in the sole discretion of the other trustee(s) then acting. Based upon the information submitted and representations made, we conclude that the modification permitting beneficiaries to be appointed successor trustees did not create a general power of appointment in any beneficiary over their respective trust. Therefore, we conclude that the modification permitting beneficiaries to be appointed successor trustees did not cause the corpus of the Trust to be includible in the gross estates of any such beneficiaries.

Except as ruled above, we express or imply no opinion concerning the federal tax consequences of this transaction under the cited provisions of the Code or any other provision of the Code.

In accordance with the power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,
Melissa C. Liquerman
Branch Chief
Office of Associate Chief Counsel
(Passthroughs and Special Industries)