

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact:

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Date: MARCH 22, 2004

Re:

Legend:

Date 1 =
Grantor =
Spouse =
Trust Agreement =

Trust 1 =

Trust 2 =

Trust 3 =

Trust 4 =

Child 1 =

Child 2 =

Child 3 =

Child 4 =

Bank =

State Statute =

Dear _____ :

This is in response to a correspondence dated September 23, 2003, and prior correspondence requesting a ruling regarding the generation-skipping transfer (GST) tax consequences of a proposed judicial modification of Trust.

The facts submitted and representations made are as follows. On Date 1, prior to September 25, 1985, Grantor created irrevocable trusts, (Trust 1, Trust 2, Trust 3 and Trust 4), under Trust Agreement for the benefit of Grantors' children, Child 1, Child 2, Child 3, and Child 4. Trust Agreement named Spouse as trustee of the trusts.

Paragraph 3 of Trust Agreement provides, generally, that the trustee is to divide the trust estate into four equal shares. One share is to be set aside for each of Child 1, Child 2, Child 3 and Child 4 and designated as Trust 1, Trust 2, Trust 3 and Trust 4. Each share is to be held and administered and distributed as a separate trust.

Paragraph 3.1 provides generally, that the trustee will use so much of the net income allocated to each separate trust of each of the beneficiaries and so much of the principal of each separate trust as the trustee, in her sole discretion, deems necessary or advisable for the maintenance, support, medical care and education of any said beneficiary, and will accumulate and invest the balance of the income not expended until each of the beneficiaries attains the age of twenty-one years and thereafter the trustee will pay the entire net income and so much of the principal as the trustee, in her sole discretion, deems necessary and advisable for any of the aforementioned purposes, from his separate trust to such beneficiary who has attained the age of twenty-one years, at least annually, during the lifetime of each beneficiary.

Paragraph 3.2 provides that upon the death of each beneficiary, should the beneficiary leave issue surviving him, the trustee is to retain the remaining balance of his separate trust for the benefit of his issue, per stirpes, until each issue attains the age of twenty-one years. The principal and income may be used at any time, within the sole discretion of the trustee, for maintenance, support, medical care, and education of such issue. As each issue attains the age of twenty-one, the trustee is to distribute the principal and undistributed income to such issue of his share of the trust estate. If the issue dies prior to attaining age twenty-one, the principal and undistributed income of his share of the trust is to be paid to the estate of the issue.

Paragraph 3.3 provides, generally, that upon the death of each of the Grantor's beneficiaries, leaving no issue surviving, the trustee is directed to add the then remaining balance of his separate trust to the other trust estates of the beneficiaries

then living and issue of any deceased beneficiary, and to the beneficiaries then living and issue of any deceased beneficiary whose trusts have terminated, in proportion to the percentage of the total trust originally established for each beneficiary and later established for each of the issue of any deceased beneficiary.

Paragraph 4 provides for a beneficiary withdrawal right. Each beneficiary is entitled to withdraw the lesser of \$ or the beneficiary's share of the total direct and indirect, or actual or deemed transfer made on his behalf. The power is non-cumulative.

Paragraph 8 provides, generally, that in the event of the death or incompetence or resignation of the trustee, Bank is nominated as the successor trustee. In the event the trustee is dissolved or resigns, the trustee, in its sole discretion, shall have the power to select and appoint a successor trustee.

The successor trustee wishes to resign and appoint one or more separate trustees. With the consent of all the beneficiaries, the trustee intends to petition the appropriate local court to modify the trust to allow one or more separate trustees to be appointed for each separate trust established under the trust agreement.

You have requested a ruling that a modification to the trust agreement approved by the appropriate local court to allow the appointment of one or more separate trustees for each separate trust established under the trust agreement will not cause the trust to lose its exempt status for GST tax purposes under § 2601 of the Internal Revenue Code.

State Statute provides, generally, that upon petition to the appropriate court, a trustee may for good cause shown, modify a trust in any manner.

Section 2601 of the Internal Revenue Code imposes a tax on each generation skipping transfer which includes under § 2611(a) a taxable distribution, a taxable termination, and a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 and § 26.2601-1(b)(1)(i) provide that the generation-skipping transfer tax shall not apply to any generation-skipping 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)(1)(ii)(A) provides that any trust in existence on September 25, 1985, will be considered an irrevocable trust except as provided in §§ 26.2601-1(b)(1)(ii)(B) or (C) (relating to property includible in the grantor's gross estate under §§ 2038 and 2042).

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 generation-skipping transfer tax 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 generation-skipping transfer 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)(D) provides that a modification of the governing instrument of an exempt trust (including a trustee distribution, settlement, or construction that does not satisfy paragraph (b)(4)(i)(A), (B), or (C) of this section) 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, but only if –

(1) 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

(2) 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.

In this case, Trusts 1, 2, 3, and 4 were created and irrevocable before September 25, 1985. Also, it is represented that no additions have been made to Trusts 1, 2, 3 and 4 since September 25, 1985. Consequently, Trust 1, 2, 3 and 4 are currently exempt from GST tax.

The proposed modification to Trust Agreement to allow the appointment of one or more separate trustees for each of Trust 1, Trust 2, Trust 3 and Trust 4 will not shift any beneficial interest in Trust 1, 2, 3, or 4 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 proposed modification of Trust Agreement will not extend the time for vesting of any beneficial interest in the trusts beyond the period provided for in the original trust. Accordingly, based on the facts submitted and the representations made, if the appropriate local court issues an order approving the modification to Trust Agreement to allow one or more separate trustees to be appointed for each of Trust 1, Trust 2, Trust 3 and Trust 4, the modification will not result in an actual or constructive addition to Trust 1, 2, 3, or 4 and will not cause Trust 1, 2, 3 or 4 to lose their exempt status under § 2601 or be subject to the provisions of chapter 13.

Except as specifically ruled herein, we express no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely yours,

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special
Industries)

Enclosure
Copy for section 6110 purposes

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