

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:4-PLR-114134-00

Re:

Date:
November 20, 2000

Legend:

Decedent =

Spouse =

Daughter =

Trust =

Trustee =

Company =

Year 1 =

Year 2 =

Local Court =

Dear _____ :

This is in response to your letter dated July 12, 2000 in which you requested a ruling concerning the generation-skipping transfer tax consequences of the modification of a trust.

The facts are represented to be as follows: Decedent established a revocable trust (Trust) prior to September 25, 1985. He died prior to September 25, 1985, survived by Spouse and Daughter. At Decedent's death, Trust became irrevocable, and Decedent's shares of stock in Company passed to Trust.

Pursuant to the terms of Trust, at Decedent's death, Trust was divided into Trust A and Trust B, and the shares of Company stock were placed in Trust B.

Trust B was governed by Article VII of Trust. Paragraph 2 of Article VII provided as follows:

Upon the death of the last to die of Trustor and Spouse, if Trustor's daughter, [Daughter], is then living, the then remaining corpus and undistributed income held in this Trust B, together with all other assets distributable to this Trust B,

shall be divided by Trustee into two (2) equal parts. One of such equal parts shall be distributed to [Daughter] and one of such equal parts shall be held in trust pursuant to the terms and conditions of this Trust B; provided, however, that notwithstanding the provisions of this Paragraph 2, no [Company] Shares shall be included as a part of the assets distributed and to the extent necessary, the part distributed may be less than the part retained in this Trust B. Thereafter, during the lifetime of [Daughter], all [Company] Shares and the proceeds from the conversion of any such shares shall be retained in this Trust B and distribution therefrom of either income or principal may only be made to the said [Daughter]. Any other assets not distributable as previously provided or otherwise received by the Trust, and including any proceeds from the conversion of [Company] shares after the death of [Daughter] shall be immediately allocated to a separate Trust C and held and administered as hereinafter provided. During the lifetime of [Daughter], Trustee shall pay the net income from the [Company] Shares and any other assets held in Trust B to her in at least quarterly annual installments. In addition, during the lifetime of [Daughter], Trustee shall pay the net income from any assets held in the separate Trust C to the said [Daughter] in at least quarterly installments and Trustee, from time to time, shall make use of so much of the corpus of separate Trust C, if any, for the benefit of any one or more of the group consisting of [Daughter] and her issue living from time to time by making such payments therefrom as Trustee, in the absolute discretion of Trustee, shall determine without any precept of equality, necessary and proper for the comfortable care, support, maintenance or education of any of said group, directly to those rendering services, caring for, or supplying goods to any one or more of such group or to any one or more of said group directly. In addition, Trustee shall pay to [Daughter] from the corpus of Trust B and/or Trust C during the lifetime of [Daughter] such amounts as she may request from time to time in writing; provided, however, that the aggregate amount of corpus paid to [Daughter] pursuant to her written request, shall not exceed in any one calendar year the greater of either Five Thousand (\$5,000.00) Dollars or Five (5%) per cent of the total of (i) the aggregate value of the corpus in this trust immediately prior to the final distribution of corpus to [Daughter] in that calendar year pursuant to her said written request plus (ii) the aggregate value of the amounts of corpus previously distributed to [Daughter] during that calendar year pursuant to her said written request. Except for this Section VII, Paragraph 2, wherever else in this Trust reference is made to the Trust or Trust B, such reference shall be deemed to include both Trust B and Trust C as herein separately set forth.

Spouse died in Year 1, survived by Daughter. At that time, Company was taxed under subchapter C of the Internal Revenue Code, and Trust B was a shareholder. In Year 2, Daughter petitioned Local Court for a reformation of Article VII, Paragraph 2 of Trust in order to qualify Trust B as a qualified subchapter S trust (QSST) under §1361(d)(3). The court granted the petition and entered an order reforming Article VII, Paragraph 2 to read as follows:

Upon the death of the last to die of Trustor and Spouse, if Trustor's daughter, [Daughter], is then living, the then remaining corpus and undistributed income held in this Trust B, together with all other assets distributable to this Trust B, shall be divided by Trustee into two (2) equal parts. One of such equal parts

shall be distributed to [Daughter] and one of such equal parts shall be held in trust pursuant to the terms and conditions of this Trust B; provided, however, that notwithstanding the provisions of this Paragraph 2, no [Company] Shares shall be included as a part of the assets distributed and, to the extent necessary, the part distributed may be less than the part retained in this Trust B. Thereafter, during the lifetime of [Daughter], Trustee shall pay the net income from the remaining assets in this Trust B in at least quarterly installments to [Daughter]. In addition, Trustee shall pay to [Daughter] from the corpus of this Trust B during the lifetime of [Daughter] such amounts as she may request from time to time in writing; provided, however, that the aggregate amount of corpus paid to [Daughter] pursuant to her written request, shall not exceed in any one calendar year the greater of either Five Thousand (\$5,000.00) Dollars or Five (5%) per cent of the total of (i) the aggregate value of the corpus in this trust immediately prior to the final distribution of corpus to [Daughter] in that calendar year pursuant to her said written request plus (ii) the aggregate value of the amounts of corpus previously distributed to [Daughter] during that calendar year pursuant to her said written request. In addition, Trustee from time to time shall make use of so much of the corpus, other than [Company] Shares, of this Trust B for the benefit of any one or more of the group consisting of [Daughter] and her issue living from time to time by making such payments therefrom as Trustee, in the absolute discretion of Trustee, shall determine, without any precept of equality, are necessary and proper for the comfortable care, support, maintenance or education of any one or more of said group, directly to those rendering services, caring for or supplying goods to any one or more of such group or to any one or more of said group directly.

Also in Year 2, the Internal Revenue Service issued a private letter ruling which concluded that the reformation did not change the quality, value, or timing of any beneficial interest or expectancy under the original provisions of Article VII, Paragraph 2 and that, therefore, Trust did not lose the exemption from the generation-skipping transfer tax under § 1433(b)(2)(A) of the Tax Reform Act of 1986 for trusts that were irrevocable on September 25, 1985.

At the present time, Trust B has disposed of its shares of Company stock and it is no longer necessary for Trust B to qualify as a QSST. It is represented that Trustee of Trust B will petition Local Court for an order reforming Article VII, Paragraph 2 in order to restore its original provisions.

Trustee of Trust B requests a ruling that the reformation of Article VII, Paragraph 2, in order to restore its original provisions, will not cause Trust B to lose its exemption from the generation-skipping transfer tax.

Law and analysis:

Section 2601 imposes a tax on every generation-skipping transfer. Section 2611(a) defines a "generation-skipping transfer" to mean (1) a taxable distribution, (2) a taxable termination, or (3) a direct skip.

Under § 1433(a) of the Tax Reform Act of 1986 and § 26.2601-1(a) of the Generation-Skipping Transfer Tax Regulations the generation-skipping transfer 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) of the regulations, the tax does 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 that date (or out of income attributable to corpus so added).

A modification of a trust that is otherwise exempt from the generation-skipping transfer tax by reason of § 1433(b)(2)(A) of the Act will generally result in a loss of exempt status if the modification changes the quality, value, or timing of any powers, beneficial interests, rights, or expectancies originally provided for under the terms of the trust.

In the present case, the proposed reformation of Paragraph 2 of Article VII of Trust in order to restore the original provisions of the paragraph does not change the quality, value, or timing of any powers, beneficial interests, rights, or expectancies of the Trust B beneficiaries. Trust was irrevocable on September 25, 1985, and it is represented that no additions (actual or constructive) have been made to Trust after that date.

Therefore, based on the facts submitted and representations made, and provided that Article VII, Paragraph 2 is reformed in accordance with its original provisions by Local Court, we conclude that Trust B will not lose its exemption from the generation-skipping transfer tax.

The ruling contained in this letter is 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 the ruling, it is subject to verification on examination.

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.

The ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely yours,
KATHERINE A. MELLODY
Senior Technician Reviewer
Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure
Copy for section 6110 purposes