Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:4-PLR-117381-00
Date:
November 27, 2000

Re:

Legend:

Settlor	=
Spouse	=
Daughter	=
Grandchild 1	=
Grandchild 2	=
Trustee	=
Trust	=
State	=
Date 1	=
Court	=

Dear :

This is in response to your letter of November 17, 2000, and prior correspondence, in which you request a ruling on the application of the generation-skipping transfer (GST) tax provisions of Chapter 13 of the Internal Revenue Code to the proposed modification to Trust.

On Date 1, Settlor 1 created Trust, an irrevocable inter vivos trust, primarily for the benefit of Settlor, Spouse, and Settlor's issue.

Article V provides that in the event of illness, accident, or other misfortune happening to any beneficiary, the trustees may, in their sole discretion, pay out of corpus sums for the care, support and medical attention of Settlor or any beneficiary of Trust.

Article VI provides that the trustees are to pay the net income of Trust to Settlor for life. Under Article VII, on Settlor's death, the trustees are to pay the expenses of Settlor's last illness, funeral expenses, debts and certain specific bequests.

Article VIII provides that after the death of Settlor, the trustees are to pay a portion of the net income of Trust to two individuals and the remainder of the net income to Spouse. Article IX provides that upon Spouse's death, the trustees are to pay a specific pecuniary amount to a designated educational institution for the purpose of establishing a scholarship fund. Article X provides that a portion of the net income from the remaining Trust corpus is to be paid to three individuals and the balance of the net income is to be paid to Daughter. At Daughter's death, the trustees are to pay the net income of Trust, in equal shares, to the lawful issue of Daughter. In the event of the death of any child of Daughter, leaving issue, his or her share of the net income will be paid to his or her lawful issue per stirpes.

Article XI provides that Trust terminates upon the death of the survivor of Spouse, Daughter, Grandchild 1 and Grandchild 2. At the termination of Trust, the balance of the trust assets will be distributed to the then living lineal descendants of Settlor, per stirpes. The current income beneficiaries of Trust are Grandchild 2, and the children of Grandchild 1. Bank is currently the sole trustee of Trust.

Article III of Trust currently provides as follows:

> The said Trustees shall not be confined to legal investments for savings banks for the reinvestment of any of the funds of this trust but said Trustees shall have the right to invest the trust funds, or any part thereof, in common stocks, preferred stocks and /or real estate, provided, that no investment in stocks or real estate shall be made by said Trustees unless all of the qualified and acting Trustees consent to such investment, and provided, further, that from the time the said Bank becomes sole Trustee of this trust, it shall not have the right to invest to exceed one-third (1/3) of the corpus of the trust fund in stocks or real estate, but shall have the right to continue to hold all stocks and real estate forming a part of the corpus of the trust at the time it becomes the sole Trustee of this trust.

Trustee believes that the current language of Article III prevents Trustee from properly diversifying Trust's investments. In order to accomplish the desired diversification, Trustee will petition the Court for an order modifying the administrative provisions in Article III.

The proposed order would eliminate the restriction contained in Article III limiting investments in stocks or real estate to no more than one-third of the trust corpus and expand the Trustee's investment powers to permit greater diversification of Trust investments. Article III, as modified, would read as follows:

The Trustee shall have the following powers with respect to any and all property held under this Trust, in addition to those powers which may now or in the future be conferred upon the Trustee under the laws of [State]:

1. General Investment Directive. To invest and reinvest the trust funds in any kind of property (real, personal, or mixed) and every kind of investment appropriate under the then prevailing circumstances, specifically including, but not limited to, corporate obligations of any kind; preferred or common stocks; shares of investment trusts, investment companies, and mutual funds; notes, real estate, bonds, debentures, mortgages, deeds of trust, mortgage participations, market funds and index funds.

Among the circumstances that are appropriate to consider in investing and managing trust assets are the following:

a. General economic conditions;

b. The possible effect of inflation or deflation;

c. The expected tax consequences of investment decisions or strategies;

d. The role that each investment or course of action plays within the overall trust portfolio;

e. The expected total return from income and the appreciation of capital;

f. The need for liquidity, regularity of income and preservation or appreciation of capital: and

g. An asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries.

In exercising the Trustee's powers, the Trustee shall consider individual investments as part of an overall investment strategy, having risk and return objectives reasonably suited to the purpose of the trust. The Trustee's investments may include stock in, or any common trust fund administered by, the Trustee. In making and implementing investment decisions, the Trustee shall diversify the investments of the trust unless, under the circumstances, it is prudent not to do so.

2. Income-Producing Property. To continue to hold any income-producing property that the Trustee receives or acquires under this Trust as long as the Trustee deems advisable.

3. Unproductive Property. To retain, purchase, or acquire unproductive property.

4. Stock and Securities Powers. To have all rights, powers and privileges of an owner of the securities held in trust, including, but not limited to the right to vote, give proxies, and pay assessments; to participate in voting trusts, pooling agreements, foreclosures, reorganizations, consolidations, mergers, liquidations, sales, and leases, and in connection with such participation, to deposit securities with and transfer title to any protective or other committee, as the Trustee may deem advisable; and to exercise or to sell stock subscriptions or conversion rights.

5. Real and Personal Property-General Powers. To manage, control, grant options on, sell (for cash or on deferred payments, with or without security), convey, exchange, partition, divide, improve, repair and otherwise exploit and develop all real and personal trust property.

6. Leases of Trust Property. To lease trust property for terms within or beyond the term of the trust and for any purpose, including but not limited to, exploration for and removal of gas, oil, and other minerals; and to enter into community oil leases, pooling, and unitization agreements.

You have requested a ruling that if the Trustee obtains the proposed Court Order modifying Trust to expand the Trustee's powers relative to investment decisions, Trust will remain exempt from the application of the GST tax as a trust that was irrevocable on September 25, 1985.

You represent that Trust was created before September 25, 1985, and that there have been no actual or constructive additions to Trust after that date.

Section 2601 imposes a tax on every generation-skipping transfer.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (the 1986 Act) and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations 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)(1)(iv) provides that if an addition is made after September 25, 1985, to an irrevocable trust, which is excluded from the application of Chapter 13 by § 1433(b)(2)(A) of the 1986 Act, a pro rata portion of subsequent distributions from (and terminations of interests in property held in) the trust is subject to the provisions of Chapter 13.

A modification of a generation-skipping trust that is otherwise exempt from GST tax under § 1433(b)(2) of the 1986 Act will generally result in a loss of its exempt or "grandfathered" 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 this case, Trust was created and irrevocable before September 25, 1985. Also, it is represented that no additions have been made to Trust since September 25, 1985. Consequently, Trust is currently exempt from GST tax. We conclude that the proposed modification to Article III pursuant to the court order, revising the Trustee's investment powers, is administrative in nature and will not change the quality, value or timing of any power, beneficial interest, right or expectancy originally provided for under the terms of Trust.

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

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,

GEORGE MASNIK
Chief, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure
Copy for 6110 purposes

cc: