

skipping transfer (GST), and income tax consequences of a proposed change of advisory committee members of Trust X.

The facts submitted and representations made are as follows:

Decedent died on Date 1, which was prior to September 25, 1985. Decedent's will created three separate and equal trusts for the benefit of his three children, their spouses, and their issue (Child 1 Trust, Child 2 Trust, and Child 3 Trust). Pursuant to the terms of Decedent's will, Bank was appointed Trustee of all trusts created under the will.

Under Clause 4(b) of Decedent's will, the income of each trust is to be paid, in reasonable installments, to the child for whose benefit it is set apart and, upon the child's death, to the deceased child's spouse to whom the child was married at the time of Decedent's death and, after the death of such spouse, to the child's issue, per stirpes. If, prior to the death of the last survivor of Decedent's children, a child should die leaving no spouse or issue surviving, the deceased child's trust is to be divided equally between the trusts for the two surviving children. Thereafter, if a second child should die leaving no spouse or issue surviving, the entire property in the two trusts is to be held as one trust for the benefit of the last survivor of Decedent's children.

Clause 4(c) of Decedent's will provides that the trusts shall terminate upon the death of the last to die of Decedent's children and the spouses to whom they were married at the time of Decedent's death. Upon termination, the property in each trust is to be paid over to the issue, per stirpes, of the child for whose benefit the trust was created.

Under Clause 5 of his will, Decedent appointed Child 1, Child 2, and Child 3 as an advisory committee, any two of whom, by writing signed by them, were given the power, with respect to the trusts created under the will, to:

- (a) Direct Decedent's Executor and Trustee as to what action is to be taken by it as owner of shares of corporate securities in the voting of such securities or in consenting to or protesting against proposed corporate action.
- (b) Direct the Executor and Trustee as to sales of property held by it, either as Executor or Trustee, and sales and purchases of property shall be made by Decedent's Executor and Trustee upon the direction and approval of the advisory committee.
- (c) Remove the Trustee at any time by instrument in writing, designating as successor Trustee a corporate fiduciary having its principal place of business in City, State; and

- (d) Give its consent so that Decedent's Executor and Trustee may borrow money when it is considered by the advisory committee that the borrowing of such money is for the benefit of any trust estate.

The will further provides that when any member of the advisory committee dies or becomes unwilling to act, or incapable of acting, the other two members are to select a person to fill the vacancy by a writing signed by the remaining members and delivered to the Trustee. If two members are deceased or unwilling to serve or become incapable of serving, the remaining member is to select two other persons to fill the two vacancies by delivering a writing signed by the remaining member to the Trustee. At any time there are only two members of the committee, such two members are to have full power to act, but in case of disagreement between the two members, the chief executive officer of Trustee is to serve as the third member of the committee until such time as a third member is selected in the manner provided. At any time there is only one member of the advisory committee alive and willing to and capable of taking action, the one member is to have the power to exercise the powers of the committee, but only during such time as he does not have a reasonable opportunity to select two members to fill the vacancies. Any member of the advisory committee who is not a beneficiary of a trust under Decedent's will is to be paid compensation for his services.

At the present time, Child 1, Child 2, Child 3, and the spouses of Child 2 and Child 3 are deceased. The Spouse of Child 1 is still living. The Child 1 Trust, the Child 2 Trust, and the Child 3 Trust will terminate on the death of Spouse of Child 1.

Child 2 was predeceased by her spouse and survived by two sons, C and D, who became the income beneficiaries of the Child 2 Trust after Child 2's death. D died in Year 1, survived by three children. On Date 2, by order of Court, the Child 2 Trust was divided into two separate trusts, each consisting of a one-half interest in each asset, one for the benefit of C and his descendants, and one for the benefit of the descendants of D (Trust X).

The current members of the advisory committee of Trust X are A, B, and C. A, B, and C have entered into an agreement of sequential resignations and successor appointments in accordance with the terms of Decedent's will that will become effective upon the receipt of favorable rulings from the Service. Under the agreement, A will be deemed to have resigned as an advisor, and B and C, the remaining advisors, will be deemed to have appointed as a new advisor a member of a class which includes descendants of Decedent, including, potentially, beneficiaries of Trust X and other adult individuals including, potentially, the spouses of such beneficiaries. Thereafter, B will be deemed to have resigned as an advisor, and C and the advisor appointed by B and C will be deemed to have appointed another member of the class as an advisor. Immediately thereafter, C will be deemed to have resigned as an advisor, and the two

new advisors will be deemed to have appointed another member of the class as an advisor.

It is represented that the new advisors will operate in accordance with the provisions set forth in Decedent's will for the advisory committee as described above. It is also represented that no additions have been made to the Child 2 Trust or to Trust X since Decedent's death.

The following rulings are requested.

- 1) The proposed resignation of advisors and appointment of successor advisors with respect to Trust X will not subject Trust to the application of the generation-skipping transfer (GST) tax under section 2601 of the Internal Revenue Code and applicable regulations.
- 2) The proposed resignation of advisors and appointment of successor advisors with respect to Trust X will not result in any taxable gift for federal gift tax purposes.
- 3) The proposed resignation of advisors and appointment of successor advisors with respect to Trust X will not result in the recognition of gain or loss for federal income tax purposes to Trust X or any beneficiaries of Trust X.

Ruling 1. Section 2601 of the Internal Revenue Code imposes a tax on every generation-skipping transfer, which is defined under section 2611 as a taxable distribution, a taxable termination, and a direct skip.

Under section 1433(a) of the Tax Reform Act of 1986 (Act) and section 26.2601-1(a) of the Generation-Skipping Transfer Tax Regulations, the GST tax is generally applicable to generation-skipping transfers made after October 22, 1986. However, under section 1433(b)(2)(A) of the Act and section 26.2601-1(b)(1)(i), the 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).

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 section 26.2601-1(b) will not cause the trust to lose its exempt status.

Section 26.2601-1(b)(4)(i)(D) provides that a modification will not cause an exempt trust to be subject to the GST tax if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in

section 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. 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 generation-skipping transfer or the creation of a new generation-skipping transfer. A modification that is administrative in nature that only indirectly increases the amount transferred will not be considered to shift a beneficial interest in the trust.

Section 26.2601-1(b)(4)(i)(E), Example 10, considers a situation where a trust is modified by decreasing the number of trustees. The modification pertains to the administration of the trust and does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation than the person or persons who held the beneficial interest prior to the modification. In addition, 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. Therefore, the modification will not subject the trust to the provisions of chapter 13.

Accordingly, the proposed resignation of the current advisors and the appointment of successor advisors with respect to Trust X is a modification that is administrative in nature. This modification does not shift any beneficial interest in Trust X to any beneficiary who occupies a generation lower than the persons holding the beneficial interests. Further, the proposed modification will not extend the time for vesting of any beneficial interest in Trust X beyond the period provided under the provisions of Decedent's will or constitute an addition to Trust X. Accordingly, the proposed changes will not cause Trust X to lose its GST exempt status under section 26.2601-1(b)(1)(i).

Ruling 2. Section 2501(a)(1) provides that a tax, computed as provided in section 2502, is hereby imposed for each calendar year on the transfer of property by gift during such calendar year by any individual, resident or nonresident.

Section 2511(a) provides that subject to the limitations contained in chapter 12, the gift tax imposed by section 2501 will 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(a) provides that, if a gift is made in property, the value thereof at the date of the gift shall be considered the amount of the gift. Section 2512(b) provides that where property is transferred for less than adequate and full consideration in money or money's worth, the amount by which the value of the property exceeded the value of the consideration shall be deemed a gift.

Based on the facts submitted and representations made, we conclude that the proposed resignation of the current advisors and the appointment of successor advisors with respect to Trust X will not change the beneficial interests in Trust X otherwise provided for under the terms of Decedent's will. Therefore, based on the facts submitted and representations made, we conclude that the proposed change of advisors of Trust X will not result in a taxable gift for federal gift tax purposes.

Ruling 3. Section 61(a)(3) provides that gross income includes gains derived from dealings in property and, under § 61(a)(15), from an interest in a trust.

Section 1001(a) provides that the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized.

Section 1001(b) states that the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Under § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under § 1001, on the sale or exchange of property shall be recognized.

Section 1.1001-1(a) of the Income Tax Regulations provides that the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or loss sustained.

Cottage Savings Ass'n v. Commissioner, 499 U.S. 554 (1991), concerns the issue of when a sale or exchange has taken place that results in realization of gain or loss under § 1001. In Cottage Savings, a financial institution exchanged its interests in one group of residential mortgage loans for another lender's interests in a different group of residential mortgage loans. The two groups of mortgages were considered "substantially identical" by the agency that regulated the financial institution.

The Supreme Court of the United States in Cottage Savings, 499 U.S. at 560-61, concluded that § 1.1001-1 reasonably interprets § 1001(a) and that an exchange of property gives rise to a realization event under § 1001(a) if the properties exchanged are "materially different." In defining what constitutes a "material difference" for purposes of § 1001(a), the Court stated that properties are "different" in the sense that is "material" to the Code so long as their respective possessors enjoy legal entitlements that are different in kind or extent. Cottage Savings, 499 U.S. at 564-65. The Court held that mortgage loans made to different obligors and secured by different homes

embody distinct legal entitlements, and that the taxpayer realized losses when it exchanged interests in the loans. Cottage Savings, 499 U.S. at 566.

The resignation of current advisory committee members and the subsequent appointment of replacement advisory committee members will take place in accordance with the existing terms of the trust. Moreover, the successor advisory committee members must abide by the same terms and conditions of the trust as the current advisory committee members. Accordingly, the proposed resignation of the current advisory committee members and the immediate appointment of their successors, once done, will merely be an exercise of the administrative provisions of the trust and will not result in the recognition of gain or loss for federal income tax purposes to the trust or any beneficiaries.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Except as expressly provided herein, no opinion is expressed or implied 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.

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

Sincerely yours,

Katherine A. Mellody
Senior Technician Reviewer
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure
Copy for section 6110 purposes

cc: