

## Internal Revenue Service

Department of the Treasury

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### Legend

Grantor:

Son:

Daughter:

Beneficiary 1:

Beneficiary 2:

Trustee 1:

Trustee 2:

Trustee 3:

Trust:

Court:

State:

Date 1:

Date 2:

Date 3:

a:

Dear

This is in response to a letter of \_\_\_\_\_, submitted on behalf of Trustee 1. Trustee 1 seeks rulings that the Trust is exempt from the generation-skipping transfer (GST) tax and that certain proposed modifications to the trustee succession provisions of the Trust will not result in the imposition of the GST tax on distributions from such trust to skip persons.

Grantor irrevocably established Trust on Date 1. Article 1.01 of the Trust provides that the trustee shall hold, manage, invest and reinvest the Trust estate,

collect the income therefrom and from time to time pay all, none, or such part of the net income of the Trust as the trustee may in his discretion determine among the members living at the time of distribution of a class composed of Daughter and Daughter's issue, in such amounts, interests and proportions as the trustee may determine.

Article 1.02 of the Trust provides that the Trust shall terminate, if it has not previously terminated, twenty-one years after the death of the survivor of Daughter and the issue of Daughter living at the date of this instrument. Upon such termination the entire trust property shall be distributed to the then living issue of Daughter, or if there shall be none, to the then living issue of Grantor, or if there shall be none, one-half of such property shall be distributed to the Beneficiary 1 to be used exclusively for educational purposes by providing student scholarships from income and student loans from principal, and the remaining one half of such property shall be distributed to Beneficiary 2 for its general purposes. If upon termination of the Trust the foregoing charitable transfers shall take effect and if either of the foregoing organizations is not then in existence or if there is any doubt as to such organizations's correct identity, the distribution of such organization's share of the Trust estate shall be made to such educational or charitable entity as the trustee shall determine to be most similar to the organization which Grantor has attempted to designate.

Article 1.04 of the Trust provides that in addition to the powers set forth in other parts of this instrument, the trustee shall have the following powers with respect to any trust created by this instrument: (a) Power to determine the amounts of income distributable from time to time to each of the members of the class to whom income is distributable, including power to make unequal distributions and power to withhold all income from one or more or all of the members of the class. (b) Power to accumulate all income which it may determine not to distribute. All accumulations may be added at such time as the trustee shall determine to the principal of the trust or held by the trustee as undistributed income. (c) Power from time to time to distribute all or any part of the principal to and among those persons receiving or eligible in the discretion of the trustee to receive distributions of income, in such shares and amounts as the trustee may determine, including power to make unequal distributions and power to withhold all distributions of principal from one or more members of the class. Such powers are exercisable in the discretion of the trustees and no beneficiary shall have any right or power to enforce or object to any reasonable exercise of such powers.

Article 1.05 of the Trust provides that notwithstanding any other provision of this instrument, if at any time there shall be acting as trustee any person who is also a beneficiary of a trust established hereby, such person shall not, in the exercise of his discretionary power to distributed income and principal, distribute to himself accumulated income or principal of such trust in excess of that which is necessary for his health, education, support and maintenance. For the purpose of this limitation, distributions necessary for health shall include distributions to pay medical, dental, hospital, nursing and invalidism expenses, distributions necessary for education shall include distributions to pay the expenses of private schools and colleges and

professional and postgraduate education, and the terms "support" and "maintenance" shall not be limited to the bare necessities of life but shall mean support and maintenance in reasonable comfort and in his accustomed manner of living.

Article 1.06 of the Trust provides that any trustee hereunder who is under a legal obligation to support any beneficiary hereunder, shall under no circumstances be entitled to exercise his discretionary power to distribute income and principal to such beneficiary in such a way as to discharge such obligation of support.

The Grantor named Son as the trustee of the Trust. Article 7.01 of the Trust provides that if Son shall resign or for any other reason cease to act as the trustee, Trustee 1, shall become the trustee. If Trustee 1 shall refuse or for any reason be unable to act as the trustee or, after accepting the trusteeship, shall resign or for any other reason cease to act as the trustee, Trustee 2, shall become the trustee.

Article 7.03 of the Trust provides that any corporate trustee may at any time be removed by Daughter during her lifetime, and after her death by all of the adult beneficiaries currently eligible to receive the income of the trust. Upon such removal, or if at any time for any other reason there shall be no person or corporation acting as the trustee hereunder, Daughter, if living, or if not, all of the adult beneficiaries currently eligible to receive the income of the trust shall have power to appoint a successor trustee which shall be any corporation authorized under the laws of any state or of the United States to administer trusts and having a combined capital and surplus of at least \$a. To be effective, any such removal and any such appointment shall be by written notice signed by the person or persons exercising such power and delivered to the removed trustee, if any, and to the designated successor.

Son resigned as trustee of the Trust shortly after it was created. Trustee 1 succeeded Son as trustee and is still serving as the sole trustee of the Trust. On Date 2, Trustee 1, Daughter and Daughter's issue, individually and on behalf of their respective minor, unborn and unascertained descendants, as the current income beneficiaries of the Trust (collectively, "petitioners"), petitioned the Court of State, requesting that the Court modify the successor trustee provisions of the Trust to allow the appointment of individuals, as well as corporate, successor trustees. In their petition, petitioners requested that the successor trustee provisions of the trust be modified to: (a) appoint Trustee 3 as sole, individual successor trustee to Trustee 1; and (b) permit Daughter, if living, or, if not, the adult income beneficiaries, to remove any trustee of the trust, individual or corporate, other than Trustee 1, and appoint any individual or corporate successor trustees.

On Date 3, Court granted the petitioners' petition effective upon the petitioners' receipt of a favorable ruling from the Service which provides that the modification in successor trustee provisions contemplated by the Court order will not subject any part of the Trust to the federal GST tax. Trustee 1 represents that no corpus has been added, actually or constructively, to the Trust subsequent to September 25, 1985.

Section 2601 imposes a tax on every generation-skipping transfer (within the meaning of subchapter B).

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

Section 2612(a)(1) provides that the term "taxable termination" means the termination (by death, lapse of time, release of power, or otherwise) of an interest in property held in a trust unless--(A) immediately after the termination, a non-skip person has an interest in the property, or (B) at no time after the termination may a distribution (including distributions on termination) be made from the trust to a skip person. Section 2612(b) provides that the term "taxable distribution" means any distribution from a trust to a skip person (other than a taxable termination or a direct skip). Section 2612(c)(1) provides that the term "direct skip" means a transfer subject to a tax imposed by chapter 11 or 12 of an interest in property to a skip person.

Section 2613(a) provides that the term "skip person" means--(1) a natural person assigned to a generation which is 2 or more generations below the generation assignment of the transferor, or (2) a trust--(A) if all interests in the trust are held by skip persons, or (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 the trust to a non-skip person.

Section 26.2601-1(a)(1) of the Generation-Skipping Transfer Tax Regulations provides that except as otherwise provided in § 26.2601, the provisions of chapter 13 of the Internal Revenue Code of 1986 (Code) apply to any generation-skipping transfer (as defined in § 2611) made after October 22, 1986.

Section 26.2601-1(b)(1)(i) 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 section 26.2601-1(b)(1)(ii)(B) (Property includible in the gross estate under § 2038) or (C) (Property includible in the gross estate under § 2042), any trust in existence on September 25, 1985, is considered an irrevocable trust.

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 chapter 13 by § 26.2601-1(b)(1), 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.

Section 26.2611-1 provides that a generation-skipping transfer is an event that is either a direct skip, a taxable distribution, or a taxable termination. The determination as to whether an event is a generation-skipping transfer is made by reference to the most recent transfer subject to the estate or gift tax.

A modification of a generation-skipping trust that is otherwise exempt under § 26.2601-1(b)(1)(i) 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.

Trust is a generation-skipping trust because Trust provides for distributions to persons that are two or more generations below the Trustor’s generation. Thus, unless Trust is excepted from the GST tax provisions by reason of § 26.2601-1(b)(1)(i), Trust would be subject to the GST tax. We conclude that if no additions have been made to Trust after September 25, 1985, the GST tax does not apply to Trust, because Trust was an irrevocable trust on September 25, 1985 within the meaning of § 26.2601-1(b)(1)(i).

In this case, the proposed modification of the Trust relates to the appointment of successor trustees. We also conclude that, based on the facts presented and the terms of the Trust, the proposed reformation will not change the quality, value, or timing of any powers, beneficial interests, rights, or expectancies originally provided for under the terms of the Trust.

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

This letter 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,

James C. Gibbons  
Assistant to the Chief, Branch 7  
Office of the Assistant Chief Counsel  
Passthroughs and Special Industries