

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Re:

Refer Reply To:

CC:PSI:4-PLR-116252-00

Date:

November 17, 2000

Legend :

Grantors =

Trust =

Trustees =

A =

B =

C =

D =

Trust #1 =

Trust #2 =

Date =

State =

Local Court =

Dear :

This is in response to your letter dated November 13, 2000, and prior correspondence in which you requested a ruling concerning the generation-skipping transfer tax consequences of the allocation of capital gains to income by the trustees of a trust pursuant to authority granted to the trustees under the trust instrument as construed by a local court.

Facts:

The facts submitted and representations made are as follows:

Grantors executed an irrevocable trust (Trust) prior to September 25, 1985. It is represented that there have been no additions to Trust after September 25, 1985.

Article II of Trust provides that Trustees are to divide Trust assets into five separate trusts. One trust is to be held for the lineal descendants of A. One trust is to be held for the

lineal descendants of B. One trust is to be held for the lineal descendants of C. Two trusts (Trust #1 and Trust #2) are to be held for the lineal descendants of D. Article II further provides that Trust assets may be held as one fund for investment purposes; however, distributions of income and principal can be made only to the beneficiaries of each separate trust from the trust created for their benefit.

Article III A of Trust provides that Trustees are to distribute the net income of each separate trust (except Trust #1) to the beneficiaries, per stirpes, in quarterly or other convenient installments, but not less frequently than annually. With respect to Trust #1, Trustees are permitted to accumulate income or distribute income at the direction of D and the person who is the successor trustee of D until such time as all Trustees are of the same generation as the beneficiaries of Trust #1. At such time, Trustees must distribute net income of Trust #1 to the beneficiaries, at least annually.

Article III B of Trust provides that at such time as there is no Trustee serving who belongs to a generation which is older than the generation assignment of every beneficiary of the separate trusts created under Article II, Trustees are authorized to distribute to any one or more of the respective lineal descendants for whom each separate trust is held and who do not have a then living ancestor who is a beneficiary of such trust, such part or all of the principal of their respective trust as a majority of Trustees determine, without restriction as to purposes. All such distributions of principal, valued at the times made, are to be considered as an advancement of any amounts thereafter becoming distributable to such distributee or his or her lineal descendants upon the termination of the separate trusts.

Article III C of Trust provides that in the event that all of the beneficiaries of a separate trust die prior to the termination of such trust, the remaining assets are to be added in equal shares to the other separate trusts then in existence under Trust, excluding Trust #1 for the lineal descendants of D; provided that an equal share be distributed per stirpes to the then living persons, if any, who would be beneficiaries of any trust which has terminated if such other trust were still in existence; provided further, that the distributive share of any beneficiary for whom a vested trust (as described in Article E) is then in existence, be added to that vested trust and administered in accordance with Article E.

Article III D of Trust provides that trusts created by Trust must vest in all events immediately prior to the expiration of twenty-one (21) years after the death of the last to die of the Grantors, the original Trustees, the persons named in Article II, and the lineal descendants of any of them in being on the date of creation of Trust. Upon such vesting, Trustees are to distribute the remaining assets of each trust to the then living persons for whom such respective trust is held, per stirpes, taking into consideration advancements previously made.

Article III E of Trust provides that upon a termination pursuant to Article D, the distributive share of any person who is then under a legal disability is to be retained as a separate, vested trust for this person. Trustees are authorized to pay to this person such part or all of the net income as well as such part or all of the principal of this vested trust as may become necessary for the health, maintenance, support and education of this person, as is determined by a majority of Trustees. Upon the death or cessation of the disability of this person, the remaining assets of this vested trust are to be distributed to this person, if living, or if not then living, to the estate of this person, unless a majority of Trustees determine to make an earlier distribution to the personal representative of this person in the best interests of such

person.

Paragraph 13 of Article V of Trust provides Trustees with:

... full management authority in addition to the management authority conferred upon trustees by law, to be exercised as shall be deemed advisable by a majority vote of the Trustees without prior approval of any court or beneficiary:

13. To apportion receipts and disbursements to income or principal or partly to each, and to make payments to beneficiaries authorized hereunder in cash or in kind or partly in each, at valuations determined by the Trustee, all as shall be deemed to be equitable, appropriate to trust purposes and in accordance with generally acceptable accounting practices; and any such action by the Trustees shall be binding upon all beneficiaries hereunder.

Pursuant to State statute, Trustees filed a Complaint for Declaratory Judgment in Local Court seeking an order construing Paragraph 13 of Article V as meaning that Trustees have authority to allocate part or all of realized capital gains of Trust to income and to distribute the same as income to the income beneficiaries. On Date, a judgment was entered by Local Court in which it construed Paragraph 13 of Article V as meaning that Trustees have that authority.

Requested Ruling:

Trustees have requested a ruling that if Trustees allocate part or all of realized capital gains to income and distribute the same as income to the income beneficiaries during the calendar year in which the capital gains are realized, or during the following calendar year, neither Trust nor any distributions from Trust will be subject to the generation-skipping transfer tax under chapter 13 of Subtitle B.

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 (Act) 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, Trust was irrevocable prior to September 25, 1985, and it is

represented that no additions (actual or constructive) have been made to Trust after that date. The judgment entered by Local Court on Date merely construes the meaning of Paragraph 13 of Article V in the original Trust instrument. The court's construction of Paragraph 13 of Article V does not change the quality, value, or timing of any powers, beneficial interests, rights, or expectancies of the beneficiaries as provided under the terms of Trust.

Therefore, based on the facts submitted and representations made, we conclude that if Trustees allocate part or all of realized capital gains to income and distribute the same as income to the income beneficiaries during the calendar year in which the capital gains are realized, or during the following calendar year, neither Trust nor any distributions from Trust will be subject to 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 a 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.

This 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

cc: