

## Internal Revenue Service

## Department of the Treasury

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Re:

### LEGEND:

Settlor =

Corporation =

Affiliate =

Company A Stock =

State A =

State B =

Successor Bank =

Child A =

Child B =

Child C =

A =

B =

C =

D =

E =

Testamentary Trust =

Testamentary Trust A =

Testamentary Trust B =

Dear :

In a letter dated February 23, 1999, and subsequent submissions you request rulings under section 2601 of the Internal Revenue Code.

When the Settlor died in 1979, the residue of his estate passed to the Testamentary Trust created under Clause Eighth of his will. Corporation was designated as the trustee. If Corporation ceases to act as trustee, Successor Bank is to be substituted as the trustee. Under the terms of the Testamentary Trust, the residue is divided into two equal shares. One share is Testamentary Trust A for the benefit of Child A, her children and other descendants. The other share is Testamentary Trust B for the benefit of Child B, her children and other descendants.

#### Testamentary Trust A

##### Income distributions during Child A's lifetime:

Eighty-five percent of the Testamentary Trust A income was to be paid to Child A through December 31, 1987. In addition, from January 1, 1983 through December 31, 1987, 15 percent of the Testamentary Trust A income was to be paid in equal shares to Child A's children living at the time of distribution. Beginning on January 1, 1988 and for the duration of Child A's life, 60 percent of the Testamentary Trust A income is to be paid to Child A, and 40 percent of the income is to be paid to Child A's descendants, per stirpes, living at the time of distribution. If there is no living descendant of Child A, the income payable to Child A's descendants is to be paid to Child A instead. Any income distributable to a minor may, at the trustee's discretion, may be held until the minor attains age 18.

##### Income and principal distributions after Child A's death:

At Child A's death, Testamentary Trust A will be divided into shares for Child A's then living descendants per stirpes. Ninety percent of a share's income will be paid to the beneficiary of that share. One-third of the share's principal will be distributed to the beneficiary upon attaining age 25. One-half of the then principal will be distributed to distributed to the beneficiary at age 30. The balance of the share will be distributed to the beneficiary at age 35. If a beneficiary dies before becoming entitled to distribution of the entire share, the trustee will divide that share into shares for the beneficiary's

descendants per stirpes. If the beneficiary does not leave descendants, the trustee will divide the share, per stirpes, for the living descendants of the beneficiary's nearest ancestor who is Child A or a descendant of Child A. If none of Child A's descendants are then living, the property will be distributed to Testamentary Trust B. If neither Child B nor a descendant of Child B is then living, the property will be divided into shares for the then living descendants of Child C per stirpes. However, all of the principal and income held in any trust must be distributed no later than 21 years from the date of the last to die of Decedent's descendants who were living on June 2, 1979.

#### Distributions of principal during the entire trust term:

During the trust term, if any income beneficiary or beneficiary for whom income is being accumulated is in need of additional moneys for maintenance in health and reasonable comfort, or for expenses of accident, illness or other misfortune, or, in the case of a beneficiary under age 25, for reasonable education expenses, the trustee may, in its discretion, after taking into consideration the beneficiary's other means of support, pay to the beneficiary the additional moneys, up to and including the entire principal of the trust share being held for that beneficiary.

#### Consultants:

Child B, Child A, and Child C, in that order, have the authority to direct the trustee on voting Company A stock held in the Trust. In addition, Child C, A, and B are designated as consultants to the trustee with powers, exercisable in a fiduciary capacity, primarily in the interest of the beneficiaries, and by a majority vote. The consultants' powers consist of directing the trustee on investments, including the retaining, selling, exchanging or leasing any trust property, investing trust funds, acquiring trust property, and voting corporate stock other than Company A stock. The consultants may surrender their powers and thereafter resume them on written notice to the trustee. If less than three consultants are available to act, Child C is to act as sole consultant. If there are less than three consultants and Child C is not able to act, then no consultants are to act, and the trustee will have full power to administer the trusts. At present, Child C is serving as the sole consultant.

#### Testamentary Trust B

The provisions of Testamentary Trust B are identical to those of Testamentary Trust A except that, under Testamentary Trust B, Child B is the beneficiary in the place of Child A, and Child B's children and other descendants are the beneficiaries in the place of Child A's children and other descendants.

It is represented that no additions, actual or constructive, were made to the trusts after September 25, 1985.

## **THE MODIFICATIONS**

The trustee proposes to petition the appropriate court to make two modifications to each trust.

### The first modification: Substitution of successor trustees

One such modification would provide for Affiliate to be the successor trustee of the trusts. That is, if Corporation ceases to act as trustee of Testamentary Trust A and Testamentary Trust B, it would be succeeded as trustee by Affiliate rather than Successor Bank. Corporation is located in State A and the Testamentary Trusts are to be governed by the laws of State A. Affiliate is located in State B, and the designation of Affiliate as trustee would cause the location of the trust assets and the principal place of trust administration of the Testamentary Trusts to change from State A to State B. However, the trustee has represented that the laws of State A would continue to govern the trusts for all purposes, both administrative and substantive.

### The second modification: Designation of successor consultants

The Testamentary Trusts will be modified to provide for successor consultants in the event that Child C ceases to act as a consultant. For Testamentary Trust A, the successor consultants would be Child A, C, and D. For Testamentary Trust B, the successor consultants would be Child B, E, and D.

## **RULINGS REQUESTED**

You have asked for rulings that Testamentary Trust (including Testamentary Trust A and Testamentary Trust B) would not lose the exemption from the application of the generation-skipping transfer tax by reason of:

- (1) the substitution of successor trustee and subsequent change in the location of the trust assets and principal place of trust administration, or
- (2) the appointment of the successor consultants.

Section 2601 imposes a tax on every generation-skipping transfer. Section 2611 defines a generation-skipping transfer to mean a taxable termination, a taxable

distribution, or a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (the Act) and §26.2601-1(b)(1) of the Generation-skipping Transfer Tax Regulations provide that 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 September 25, 1985 (or out of income attributable to corpus so added).

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 (Tax on Certain Generation-Skipping Transfers) by section 1433(b)(2)(A) of the 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.

In the present case, it has been represented that no additions have been made to the trusts after September 25, 1985.

A modification of a generation-skipping trust that is otherwise exempt under the 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 the present case, the proposed appointment of successor consultants would not alter or expand the consultants’ powers provided under the trusts. Rather, the consultants’ powers would remain limited to the authority to direct the trustee’s investments, with no authority to influence the trustee’s discretionary distributions to the beneficiaries. Presently, Corporation is the trustee of Testamentary Trust A and Testamentary Trust B and Successor bank is to be substituted as trustee if Corporation ceases to act as trustee. The trustee also proposes to modify Testamentary Trust A and Testamentary Trust B such that Affiliate will become the successor trustee of each trust rather than Successor Bank.

Presently, the trusts are governed by the laws of State A. The designation of Affiliate as the successor trustee would cause the location of trust assets and the principal place of trust administration to change from State A to State B when Affiliate becomes the trustee. In this case, however, the trustee has represented that the laws of State A will continue to govern each of the trusts for all purposes, both administrative and substantive. Therefore, the proposed substitution of Affiliate for Successor Bank as successor trustee of the Testamentary Trusts would not alter the beneficial interests of

any beneficiary.

Consequently, the two modifications to be made to Testamentary Trust (including Testamentary Trust A and Testamentary Trust B), as described above, are administrative in nature and will not result in any change in the quality, value, or timing of any beneficiary's interest.

We conclude that the proposed modifications, as described above, will not affect the exempt status of the trusts with respect to the generation-skipping transfer tax and, if no additions are made, all distributions from and the termination of the trusts will be exempt from the generation-skipping transfer tax.

Except as we have specifically ruled herein, we express no opinion under the cited provisions or under any other provision of the Code.

This ruling is based on the facts and applicable law in effect on the date of this letter. If there is a change in material fact or law (local or Federal) before the transactions considered in this ruling take effect, the ruling will have no force or effect. If the taxpayer is in doubt whether there has been a change in material fact or law, a request for reconsideration of this ruling should be submitted to this office.

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

Sincerely yours,

Assistant Chief Counsel  
(Passthroughs and Special Industries)

By \_\_\_\_\_  
James F. Hogan  
Acting Assistant to the Branch Chief  
Branch 4

Enclosure  
copy for 6110 purposes