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Department of the Treasury
Washington, DC 20224

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Date: FEBRUARY 13, 2006

In Re:

,

LEGEND:

Father	=
Mother	=
Decedent	=
Wife	=
Daughter 1	=
Daughter 2	=
Trust	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
State	=
State Statute	=

Dear :

This is in response to your June 24, 2005 letter and other correspondence requesting a ruling concerning the income and generation-skipping transfer (GST) tax consequences of the proposed division of a trust.

You have requested the following rulings:

1. After the proposed modification to Trust, the successor trusts will be exempt from GST tax under chapter 13 of the Internal Revenue Code.

2. The division of Trust does not constitute a sale or other taxable disposition under section 1001.
3. The proposed division of Trust will not result in a transfer by any of the beneficiaries that is subject to gift tax under section 2501.

The facts submitted are as follows:

Father died on Date 1. Mother died on Date 2.

Article III, section A of Father's will provides that the residue and remainder of Father's property is to be divided into three equal shares, for Father's three children. One of those shares is to be placed in a separate trust (Trust), designated for the benefit of Decedent, who is the son of Father and Mother.

Article III, section B provides that the corporate trustee of Trust is to have the power to accumulate any part or all of the net income of Trust or to expend the income (or any part or all of the principal) for the reasonable care, support, maintenance, education, enjoyment, advancement in life, or comfort of Mother, Decedent, Decedent's spouse (Wife), issue of Decedent, and spouses of the issue of Decedent, who are living during the term of Trust.

Article III, section D provides, in part, that Trust is to terminate on the death of the last of Father, Mother, and issue of Father who was living at the time of Father's death. Upon termination, all the principal and undistributed income of Trust is to be distributed to Decedent, if living, and if not, the issue of Decedent as shall be living at the time of termination, per stirpes.

Under Article III, section E, Decedent was granted a testamentary nongeneral power of appointment over Trust. The power of appointment was not exercised.

Decedent died on Date 3. Wife is still living and is a current beneficiary of Trust.

Decedent and Wife had two daughters, Daughter 1 and Daughter 2. Each daughter is married and has descendants. Daughter 1 and her husband have a son and daughter, each of whom is married, and have a total of four grandchildren. Daughter 2 has a son and daughter, neither of whom is married. Daughters 1 and 2, their spouses, their children, their children's spouses, and their grandchildren are all current beneficiaries of Trust.

Trust has both individual trustees (currently Daughters 1 and 2) and a corporate Trustee. Daughters 1 and 2, as individual trustees, have a power over investment of the Trust's assets. Thus, the individual trustees, have the power to retain real or personal property of the trust estate, to sell or dispose of property from the trust estate, to invest and reinvest the trust estate in any property, real, personal, or mixed, to make

loans out of the trust estate, and to borrow money by pledging, mortgaging, or providing liens of any property of the trust estate.

The corporate trustee, in its absolute discretion, may make distributions out of either income or principal to the descendants of Decedent and Wife and the descendants' spouses, for their reasonable care, support, maintenance, education, enjoyment, advancement in life, or comfort. The distributions need not be made equally. The corporate trustee is authorized to pay the entire estate to one person if it deems such payment advisable. At termination, the trust assets will be distributed to Decedent's issue by right of representation.

The trustees represent that because the current beneficiaries have different investment goals and distribution needs, it is difficult to invest the trust estate and administer Trust in the best interests of all the beneficiaries. Accordingly, Daughters 1 and 2 propose to petition the State probate court to divide Trust, pro rata, into two successor trusts. One successor trust will be for the benefit of Daughter 1, her husband, her descendants, and descendants' spouses. The other successor trust will be for the benefit of Daughter 2, her husband, her descendants, and descendants' spouses. In all other particulars, the provisions of the successor trusts will be identical to those of Trust. Wife will remain a beneficiary of both successor trusts during her lifetime.

The trustees represent that they propose to partition and divide Trust pro rata. Additionally, the trustees have submitted a proposed petition for division to be filed by Daughters 1 and 2 and the corporate trustee in the state probate court. In the petition, Daughters 1 and 2 and the corporate trustee ask that Trust's assets be divided equally between the successor trusts. However, Daughters 1 and 2 and the corporate trustee also request that they be given discretion to allocate to the successor trusts, in kind, certain different assets, of equal value to each trust, if those assets cannot be absolutely divided in equal parts, such as odd numbered shares of stock or bonds.

LAW AND ANALYSIS

Ruling 1

Section 2601 imposes a tax on every generation-skipping transfer. The term "generation-skipping transfer" is defined in section 2611 as a taxable distribution, a taxable termination, or 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 (GST) 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 GST 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 5, illustrates a situation where a trust that is otherwise exempt from the GST tax is divided into two trusts. Under the facts presented, the division of a trust into two trusts does not shift any beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the division, and the division does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. Accordingly, the two partitioned trusts will not be subject to the provisions of chapter 13.

In this case, the proposed division of Trust into successor trusts will not result in a shift of any beneficial interest in Trust to any beneficiary who occupies a generation lower than the persons holding the beneficial interests. Further, the proposed division of Trust into successor trusts will not extend the time for vesting of any beneficial interest in the new trusts beyond the period provided for in Trust. Accordingly, based on the facts submitted and representations made, we conclude that the successor trusts created upon the division of Trust will be exempt from GST tax.

Ruling 2

Section 61(a)(3) provides that gross income includes gains derived from dealings in property and, under section 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 section 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in section 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 section 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under section 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.

An exchange of property results in the realization of gain or loss under section 1001 if the properties exchanged are materially different. Cottage Savings Ass'n v. Commissioner, 499 U.S. 554 (1991). There is a material difference when the exchanged properties embody legal entitlements "different in kind or extent" or if they confer "different rights and powers." 499 U.S. at 565.

A partition of jointly owned property is not a sale or other disposition of property if the co-owners of the joint property sever their joint interests but do not acquire a new or additional interest as a result of the transaction. Thus, neither gain nor loss is realized on a partition. See Rev. Rul. 56-437, 1956-2 C.B. 507.

Rev. Rul. 69-486, 1969-2 C.B. 159, involved a trust consisting of both notes and common stock. By mutual agreement, the two beneficiaries requested the trustee to distribute all the notes to one beneficiary and all the common stock to the other. However, neither the trust instrument nor local law gave the trustee the power to make a non-pro rata distribution of property in kind. Because the trustee did not have authority to allocate the property in a non-pro rata manner, the beneficiaries were treated as having an absolute right to a ratable in kind distribution. Rev. Rul. 69-486 therefore treated the beneficiaries as receiving the notes and common stock pro rata, followed by an exchange between the beneficiaries in which one received all the notes and the other all the common stock. Because in substance a deemed exchange occurred between the beneficiaries, Rev. Rul. 69-486 held that the beneficiaries recognized gain under sections 1001 and 1002.

In this case, the trust instruments do not appear to give the trustees the power to make a non-pro rata distribution of assets upon partition of the trusts. However, under State Statute, effective Date 5, a trustee has the power to allocate particular assets in proportionate or disproportionate shares when distributing trust property or dividing or terminating a trust.

Where the division of the trusts to occur after the effective date of State Statute, the situation here would become distinguishable from Rev. Rul. 69-486. In that circumstance, the beneficiaries of the trust would not be required to receive pro rata distributions for each asset and the trustees would have the authority to make non-pro rata distributions based on fair market value.

Accordingly, if the petition to partition is filed in state court and the trusts are divided into successor trusts after Date 4, the division into the successor trusts will not constitute a sale or other disposition and will not result in any gain or loss being realized under section 1001.

Ruling 3

Section 2501 imposes a tax on the transfer of property by gift by any individual, resident or nonresident. Section 2511 provides that the tax imposed by section 2501 applies 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 an adequate consideration in money or money's worth, then the amount by which the value of the property exceeded the value of the consideration is deemed a gift.

In this case, the dispositive provisions that are proposed for the successor trusts will be identical to those of Trust, except that each of the successor trusts will be established for the benefit of a single Daughter of Decedent. Accordingly, based on the facts submitted and representations made, we conclude that the proposed division of Trust will not result in a transfer by any of the beneficiaries that is subject to gift tax under section 2501.

In accordance with the Power of Attorney on file with this office, copies of this letter are being sent to your authorized representatives.

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,

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure:

Copy of letter for section 6110 purposes