

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4-PLR-109707-00

Date:

July 31, 2000

Legend

Decedent	=
Trust	=
Grandchild A	=
Grandchild B	=
Date 1	=
Local Court	=
Date 2	=

Dear :

This is in response to your letter of May 3, 2000, in which you requested a ruling concerning the gift and generation-skipping transfer tax consequences of a proposed division of a trust.

Decedent executed a will in 1950, and died in 1954, survived by her two grandchildren, Grandchild A and Grandchild B.

Item VII of Decedent's will provides that the residue of Decedent's estate is to be held in trust (Trust) for the benefit of Decedent's two grandchildren, Grandchild A and Grandchild B.

Item VII, paragraph 4, provides that the trustees shall pay the net income from trust, in equal shares, to Grandchild A and Grandchild B for their respective lives. On the death of either Grandchild A or Grandchild B, his or her respective share of Trust income is to be paid for duration of the trust pursuant to the exercise of a special power to appoint income of the Trust, provided in Item IV, paragraph 7. In default of exercise, the share of income is to be paid to the deceased grandchild's surviving children and, if none, to the survivor as between the two grandchildren, or if none, to the surviving issue of the other grandchild, per stirpes.

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Item VII, paragraph 6, provides that Trust shall terminate 21 years after the death of the survivor of Grandchild A and Grandchild B. Upon termination, the trustee is to divide the remaining trust estate into two equal shares. One share is to be paid, per stirpes, to the descendants of Grandchild A and the other share is to be paid, per stirpes, to the descendants of Grandchild B, subject to the exercise of a power of appointment provided for in paragraph 7. If Grandchild A dies leaving no descendants, the assets that would have been paid to Grandchild A's descendants are to be paid to Grandchild A's heirs at law. If Grandchild B dies leaving no descendants, the assets that would have been paid to Grandchild B's descendants are to be paid to Grandchild B's heirs at law.

Item VII, paragraph 7, provides Grandchild A and Grandchild B with the testamentary power to appoint the grandchild's share of Trust income for the duration of the trust term, and corpus on termination of the Trust, among a class consisting of family members (not including the respective grandchild) and public charities.

Grandchild A and Grandchild B are currently serving as the trustees of Trust.

Until late 1996, the assets of Trust consisted of interests in a family-owned business. The business was sold, and the trust principal was invested in liquid assets. The two trustees had differing views with respect to how the assets of Trust should be invested and managed. To accommodate their different views, the trustees agreed, as of Date 1, to operate the Trust as two separate shares, one for Grandchild A and her family and the other for Grandchild B and his family.

Subsequently, the trustees petitioned Local Court to divide the Trust into two separate trusts, the Grandchild A Family Trust and the Grandchild B Family Trust. The petition requested that the division be based on the value of Trust on Date 1. In addition, the trustees requested that the court clarify certain administrative provisions concerning the succession of trustees, after the division of Trust.

On Date 2, the Local Court issued an order approving the division, subject to a favorable ruling from the Internal Revenue Service to the effect that the trusts will remain exempt from the generation skipping transfer tax. Under the court order, except for the clarification relating to the succession of trustees, the terms of each successor trust remain exactly the same as the terms of Trust as applied to each grandchild's trust. For example, Grandchild A will be the sole income beneficiary of her respective trust, and Grandchild B will be the sole income beneficiary of his respective trust. Similarly, upon the death of Grandchild A or Grandchild B respectively, the income of the decedent's trust, subject to the testamentary power of appointment (discussed below) will be paid in equal shares to the deceased grandchild's surviving children, if any, or, if none, to the survivor as between the two grandchildren or if none, to the issue of the survivor, per stirpes. Each trust will terminate 21 years after the death of the survivor of Grandchild A and Grandchild B. On termination, the Grandchild A Family

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Trust will be distributed, subject to the power of appointment noted below, to Grandchild A's issue, per stirpes, and if none, to her heirs-at-law. The Grandchild B Family Trust will be distributed, subject to the power of appointment noted below, to Grandchild B's issue, per stirpes, and if none, to his heirs at law. Grandchild A and Grandchild B each possess a testamentary power to appoint the income and corpus of their respective trust as provided in Item VII, paragraph 7 of Trust.

The trustees have represented that there have been no additions to Trust after September 25, 1985, and that, with the exception of certain administrative changes, the partitioned trusts will continue to be governed by the terms of the existing trust.

The trustees have requested the following rulings:

1. The division of Trust into two separate trusts, the Grandchild A Family Trust and the Grandchild B Family Trust, will not cause the trusts to lose exempt status for generation-skipping transfer tax purposes under § 1433(b)(2)(A) of the Tax Reform Act of 1986 and § 26.2601-1(b)(1)(i) of the Generation-skipping Transfer Tax Regulations.

2. Distributions from or terminations of interests in the Grandchild A Family Trust and the Grandchild B Family Trust will not be subject to the tax imposed under § 2601 of the Code.

3. The proposed division will not cause the Grandchild A or Grandchild B to be subject to the tax imposed under § 2501.

Ruling Request No. 1 and 2

Section 2601 imposes a tax on every generation-skipping transfer made by the "transferor" to a "skip person." Section 2611 defines a generation-skipping transfer as a taxable termination, a taxable distribution, or a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (the Act), 1986-3 (Vol. 1) C.B. 1, and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the generation-skipping transfer tax shall 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)(ii)(A) provides that any trust in existence on September 25, 1985, will be considered an irrevocable trust except as provided in §§ 26.2601-1(b)(ii)(B) or (C), which relate to property includible in a grantor's gross estate under §§ 2038 and 2042. In the present case, the Trust is considered to have been irrevocable on September 25, 1985, because neither § 2038 nor § 2042 apply.

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A modification of a trust that is otherwise exempt from the generation-skipping transfer tax under the Act will generally not result in a loss of its exempt or "grandfathered" status if the modification does not change 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, it has been represented that no additions have been made to Trust after September 25, 1985. After the division of the Trust into two separate trusts, the Grandchild A Family Trust and the Grandchild B Family Trust, the interests of the beneficiaries will remain the same and the timing of the termination of the resulting trusts will remain the same. Accordingly, the proposed division of each of these trusts will not change the quality, value, or timing of any powers, beneficial interests, rights, or expectancies originally provided for under the terms of the original trusts.

Based on the information submitted and representations made, we conclude that the division of Trust pursuant to the Local Court order into the Grandchild A Family Trust and the Grandchild B Family Trust will not cause either trust to be subject to the application of the generation-skipping transfer tax by reason of the effective date rules provided in § 1433(b)(2) of the Tax Reform Act of 1986. In addition, distributions from or terminations of interests in the Grandchild A Family Trust and the Grandchild B Family Trust, to the extent not made out of additions to the trust after September 25, 1985, will not be subject to the tax imposed under § 2601.

Ruling Request 3

Section 2501 imposes a tax on the transfer of property by gift by an individual. Section 2511 provides that the tax imposed by § 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.

In this case, the interest of each beneficiary will remain the same after the proposed division. Accordingly, based on the fact submitted and the representations made, we conclude that the division will not cause Grandchild A or Grandchild B to be subject to the tax imposed under § 2501.

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

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

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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.

Sincerely yours,
Associate Chief Counsel
(Passthroughs and Special Industries)
By George Masnik
Chief, Branch 4

Enclosure (1)
Copy for 6110 purposes