

Internal Revenue Service

Department of the Treasury
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Person To Contact:

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Refer Reply To:

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Date:

August 01, 2012

Re:

Legend:

Decedent =

Spouse =

Son 1 =

Son 2 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Year =

Article Fifth Trust =

Article Sixth Trust =

New Trust =

Dear _____ :

This responds to your letter dated January 30, 2012, from your authorized representative, requesting rulings under § 2601 of the Internal Revenue Code with respect to a proposed appointment of Trust property.

On Date 1, Decedent executed his Last Will and Testament. Decedent executed a codicil to his will on Date 2 and passed away on Date 3. Pursuant to Article Fifth of Decedent's will, property passed to an irrevocable marital trust (Trust) for Decedent's surviving spouse (Spouse). Spouse was granted an inter-vivos general power of appointment, but because of an incapacity beginning in Year (a date prior to September 25, 1985) and lasting to her death on Date 4, that power was never exercised. Under the terms of Trust, upon the death of Spouse, Trust was divided into equal shares for

Decedent's surviving children and surviving issue of a deceased child. One share continued in trust (Article Fifth Trust) for the benefit of Son, his spouse, Son's issue and the spouses of such issue. Under this trust, the trustees are to pay Son 50% of the income annually and the balance to the class consisting of Son, his spouse, Son's issue and the spouses of such issue.

Under the terms of Decedent's will, Son is granted a limited power of appointment over the Article Fifth Trust exercisable in favor of Son's issue and any spouse of Son's issue, in such amounts and proportions, either outright, in trust or otherwise. There is a 50% limitation on the amount that may be appointed to the spouses. If Son dies without exercising the power, the assets of the Article Fifth Trust are to be distributed outright to his living issue, per stirpes.

The remainder of Decedent's estate passed to his children in trust. Pursuant to Article Sixth of Decedent's will, property passed in trust (Article Sixth Trust) to Son. The Article Sixth Trust income provisions are similar to the income provisions in the Article Fifth Trust. Son also has a limited power of appointment over the Article Sixth Trust exercisable under the same terms as the power of appointment granted in the Article Fifth Trust. If Son dies without exercising the power, the assets of the Article Sixth Trust are to be distributed outright to his living issue, per stirpes.

Son proposes to execute a Last Will and Testament that appoints the assets held in the Article Fifth and Sixth Trusts on his death to a trust created on Date 5 (New Trust). The appointment will specifically limit the duration that New Trust may hold the Article Fifth and Sixth Trust assets to one day prior to the perpetuity period created under Decedent's will. The beneficiaries of New Trust are Son's children and their descendants.

Two Similar trusts (Son 2 Trusts) were created for the benefit of Decedent's other son, Son 2. Upon the death of Son 2, a portion of those assets passed to the Article Fifth and Article Sixth Trusts described above. It is represented that, other than the assets passing by reason of Son 2's death, no additions have been made to the Article Fifth and Sixth Trusts and not additions were made to the Son 2 Trusts.

You have requested the following rulings:

1. Spouse's failure to exercise her power of appointment over the assets in Trust did not constitute a constructive addition nor cause a change in the GST exempt status of the assets.
2. Son's proposed exercise of his power of appointment over the assets in the Article Fifth and Sixth Trusts will not constitute constructive additions nor will the exercise cause a change in the GST exempt status of the assets.

Section 2601 imposes a tax on every generation-skipping transfer (GST). The term “generation-skipping transfer” is defined in § 2611 as a taxable distribution, a taxable termination, and 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 GST 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), 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)(1)(v)(A) provides that, except as provided in § 26.2601-1(b)(1)(v)(B), where any portion of a trust remains in the trust after post-September 25, 1985 release, exercise, or lapse of a power of appointment over that portion of the trust, and the release, exercise, or lapse is treated to any extent as a taxable transfer under chapter 11 or 12, the value of the entire portion of the trust subject to the power is treated as if that portion had been withdrawn and immediately retransferred to the trust at the time of the release, exercise or lapse.

Section 26.2601-1(b)(1)(v)(B) provides that the release, exercise, or lapse of a power of appointment (other than a general power of appointment as defined in § 2041(b)) is not treated as an addition to a trust if (1) the power of appointment was created in an irrevocable trust that is not subject to chapter 13 under § 26.2601(b); and (2) in the case of an exercise, the power of appointment is not exercised in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of the trust, extending beyond any life in being at the date of creation of the trust plus a period of 21 years plus, if necessary, a reasonable period of gestation (the perpetuities period).

This rule is illustrated in Example 4 of § 26.2601-1(b)(1)(v)(D). In Example 4, on March 1, 1985, T established an irrevocable trust as defined in § 26.2601-1(b)(ii). Under the terms of the trust instrument, the trustee is required to distribute the entire income annually to T’s child, C, for life, then to T’s grandchild, GC, for life. GC has the power to appoint any or all of the trust assets to Trust 2 which is an irrevocable trust (as defined in § 26.2601-1(b)(ii)) that was established on August 1, 1985. The terms of Trust 2’s governing instrument provide that the trustee shall pay income to T’s great grandchild, GGC, for life. Upon GGC’s death, the remainder is to be paid to GGC’s issue. GGC was alive on March 1, 1985, when Trust 1 was created. C died on April 1, 1986. On July 1, 1987, GC exercised the power of appointment. The exercise of GC’s power does not subject future transfers from Trust 2 to tax under chapter 13 because the exercise of the power in favor of Trust 2 does not suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date of creation of Trust 1, extending beyond the life of GGC (a beneficiary under Trust 2 who was in being at

the date of creation of Trust 1) plus a period of 21 years. The result would be the same if Trust 2 had been created after the effective date of chapter 13.

Section 26.2601-1(b)(3)(i)(A) provides that if an individual was under a mental disability to change the disposition of his or her property continuously from October 22, 1986, until the date of his or her death, the provisions of chapter 13 do not apply to any generation-skipping transfer under a trust (as defined in § 2652(b)) to the extent such trust consists of property, or the proceeds of property, the value of which was included in the gross estate of the individual (other than property transferred by or on behalf of the individual during the individual's life after October 22, 1986).

We note that, under the represented facts, the Article Fifth Trust created at the death of Spouse was exempt from the GST tax provisions in Chapter 13 of the Code by reason of the exception relating to mental incompetency in § 26.2601-1(b)(3). Accordingly, Spouse's failure to exercise her power of appointment over the assets In Trust did not constitute a constructive addition nor cause a change in the GST exempt status of the assets when the assets continued in trust for the benefit of Son.

The testamentary powers of appointment held by Son over the assets in the Article Fifth and Sixth Trusts, are not general powers of appointment within the meaning of § 2041(b)(1). Pursuant to Son's exercise of these powers over these trusts, the entire corpus of the Article Fifth and Sixth Trusts will pass to New Trust. The appointment will specifically limit the duration that New Trust may hold the Article Fifth and Sixth Trust assets to the perpetuity period created under Decedent's will, less one day. Consequently, Son's exercise of the powers will not postpone or suspend the vesting, absolute ownership or power of alienation of any interest.

Accordingly, based on the facts submitted and representations made, we conclude that the exercise by Son of the powers of appointment over the Article Fifth and Sixth Trusts in favor of New Trust, will not result in a transfer of property that is subject to generation-skipping transfer tax and the appointed property passing to New Trust will retain its exempt status for GST tax purposes.

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.

Except as specifically ruled herein, we express or imply 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) provides that it may not be used or cited as precedent.

Sincerely,

James Hogan
Branch Chief, Branch 4
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure

Copy for § 6110 purposes
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cc: