

Internal Revenue Service

Department of the Treasury

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Person to Contact:

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Date:

June 24, 1999

Legend: Trustees:

Grantor:

Trust:

Date 1:

Company:

Charity 1:

Charity 2:

Statute1:

State:

Daughter:

Son:

Spouse:

Date 2:

Court:

Date 3:

Dear

We received the letter dated , and later submissions on behalf of Trustees, requesting rulings concerning the income and generation-skipping transfer (GST) tax consequences of the proposed creation and funding of a revocable charitable subtrust. This letter responds to that request.

The facts and representations submitted are as follows. Grantor created Trust on Date 1 for the benefit of his family and charities. Trust was irrevocable on September 25, 1985, and it is represented that there have been no actual or constructive additions since that date. Any increase in value of the corpus of Trust

since September 25, 1985, has been the result of accumulation of income and appreciation of corpus.

The assets of Trust consist primarily of a minority interest block of stock in Company, a privately-held corporation. The remaining assets of Trust consist of a cash reserve and cash equivalent investments.

Section 2.02 of Trust provides that the Trust created under the Trust Agreement is in all respects irrevocable and neither Grantor nor any other contributor to the trust estate, nor any other person is to have any power to modify, amend, or revoke the Trust in any respect.

Section 3.02 of Trust provides that the payment of any benefits, whether of income, principal or otherwise, shall be vested in the sole discretion of the trustees from time to time. Amounts of net income, capital gains or other proceeds or amounts of principal not paid out to a beneficiary shall be accumulated and added to principal. Section 3.02 of Trust further provides that payments among the members of a class of Individual Beneficiaries and Charitable Beneficiaries need not be equal either at the time of payment or at any future time and may be to one, to all or to any number of members of any class (with no right, vested or otherwise, on the part of any Individual Beneficiary or Charitable Beneficiary to claim any benefit at any time against the trustees or the trust estate), all as determined by the trustees, in their sole discretion.

Section 3.03 of Trust provides that payments of income, principal or otherwise at any time may be made to any one or more members of the lowest numbered of the classes of Individual Beneficiaries described in section 3.03(1) which has one or more representative members then living and/or to any one or more members of the class of Charitable Beneficiaries described in section 3.03(2).

Section 3.03(1) of Trust provides the classes of potential Individual Beneficiaries of Trust. The Individual Beneficiaries of Trust include the living issue of Grantor, all spouses of such issue, all spouses of any deceased issue of Grantor (provided, in the case of any such spouse, that such spouse was living with and married to such deceased issue at the time of such issue's death), and certain collateral relatives of Grantor.

Section 3.03(2) of Trust provides the potential Charitable Beneficiaries of Trust. The potential Charitable Beneficiaries shall be Charity 1 and Charity 2. In addition, Section 3.03(2) of Trust includes as potential Charitable Beneficiaries:

such of a group consisting only of corporations, associations, and institutions which are organized and operated exclusively for religious, charitable, literary and educational purposes and projects and which are described both Section 501(c)(3) of the Internal Revenue Code as the

same exists at the execution of [Trust] or as it or a successor section may be amended from time to time and in [Statute1] as the same exists at the execution of [Trust] or as it or a successor section may be amended from time to time, as may be selected by the trustees, in their sole discretion, from time to time; provided that no Charitable Beneficiary shall acquire any enforceable rights to receive income or principal or any vested interest therein against the trustees by virtue of Section 3.03(2) or otherwise. In the event Charity 1 or Charity 2 shall cease to be organized and operated exclusively for the purposes described in said sections of the Internal Revenue Code and State Statutes, they shall cease to be potential Charitable Beneficiaries hereunder.

Section 3.03(3) of Trust provides that the beneficiaries potentially eligible, subject to the trustees' determination, for any payments of income, principal or otherwise, shall include, at any time, all Charitable Beneficiaries as defined in Section 3.03(2) hereof and all members of the class of Individual Beneficiaries then eligible under Section 3.03(1).

Section 3.03(4) of Trust provides that the discretionary powers of distribution of principal and income hereunder shall be broad enough to permit complete distribution of all trust assets at any time, and in the event final distribution should be determined on by the trustees or legally required under paragraph 4.01 [relating to the potential duration of Trust] or otherwise, distribution shall be made by the trustees to any or all members of the class of Individual Beneficiaries and Charitable Beneficiaries then eligible under the other provisions of [Section] 3, as determined by the trustees, in their sole discretion.

Section 4.01 of Trust provides that the trust hereunder, if not sooner terminated pursuant to complete distribution or the appreciation of any of the foregoing provisions hereof, shall terminate twenty-one (21) years after the death of the survivor of all persons described as potential Individual Beneficiaries in all of Classes One to Three, inclusive, Section 3.03(1), as such persons would be determined at the date of the execution of this agreement. Any trust assets governed by a statute or rule of law under which termination at the date above prescribed would render the trust invalid shall be distributed on the last date on which said assets can validly remain in trust (and in the event such governing statute or rule depends upon specified lives in being, those of all persons described as potential Individual Beneficiaries in Classes One to Three, inclusive, Section 3.03(1), as they would be determined at the date of the execution of [Trust], shall be used as such lives in order of least age, taking the youngest first).

Section 5.01 of Trust provides that the individual trustees have the power to appoint one or more individual trustees, or a corporate trustee, or one or more individual trustees and a corporate trustee, as the case may be, to act with the trustee or trustees then acting.

Section 5.04(9) of Trust provides that the trustees have the power to divide Trust, determining values and designating particular assets for Grantor's beneficiaries, to assign like or unlike properties to different beneficiaries or trusts, to create or hold undivided interests in any property of Trust, and to make distributions and payments in cash or in kind or both.

Section 5.04(11) of Trust provides that the trustees have the power to merge the assets of Trust with those of any other trust, by whomsoever created, maintained for the same potential beneficiaries upon the same terms.

It is represented that Grantor has two living children, Daughter and Son. Daughter is married to Spouse and has five children. Son is unmarried and has no children.

It is further represented that, since the creation of Trust, the Trustees have made no distributions to Daughter or her children. The Trustees have made discretionary distributions of nominal amounts to Spouse, and more substantial distributions to Son and to various Charitable Beneficiaries.

The Trustees propose to create a revocable Charitable Subtrust to be administered exclusively for the benefit of potential Charitable Beneficiaries, and to transfer a portion of stock held by Trust to the Charitable Subtrust.

The Trustees represent that the dispositive provisions of the Charitable Subtrust are the same in all material respects as the dispositive provisions of Trust, with two exceptions: (1) Individual Beneficiaries are excluded from the class of beneficiaries eligible to receive distributions from the Charitable Subtrust and (2) the class of charitable organizations eligible to receive distributions from the Charitable Subtrust is more narrowly defined than the class of organizations included within the definition of "Charitable Beneficiaries" under Trust.

The Trustees represent that the administrative provisions of the Charitable Subtrust differ in numerous respects from the administrative provisions of Trust by reason of the different nature and purpose of the Charitable Subtrust. The differences are as follows: (1) the Charitable Subtrust may be amended with the written consent of the Trustees of Trust, and the Charitable Subtrust may be revoked in whole or in part by the Trustees of Trust; (2) the Charitable Subtrust permits additional contributions by the Trustees of Trust but does not permit additional contributions by any other person or entity; and, (3) the Trustees of the Charitable Subtrust are authorized to create organizations which are exempt from taxation under § 501(a) of the Internal Revenue Code, to which distributions may be made from the Charitable Subtrust.

The original trustees of the Charitable Subtrust are the same as the current Trustees of Trust. The Charitable Subtrust provides that co-trustees and successor

trustees of the Charitable Subtrust shall be appointed by the Trustees of Trust. In addition, the Trustees of Trust have the power to remove any trustee of the Charitable Subtrust.

On Date 2, Trustees commenced a proceeding in Court for an order authorizing Trustees to create and fund the Charitable Subtrust. On Date 3, Court issued the Order, which is subject to the Trustees' receipt of a favorable private letter ruling concerning the funding of the Charitable Subtrust.

The following rulings are requested:

(1) Trust shall be treated as the owner of the Charitable Subtrust under Subchapter J of Chapter 1 of Subtitle A of the Code;

(2) The creation and funding of the Charitable Subtrust shall not cause Trust, the Charitable Subtrust, or any assets of Trust or the Charitable Subtrust to be subject to the generation-skipping transfer tax under Chapter 13 of Subtitle B of the Internal Revenue Code (§§ 2601, et seq.); and,

(3) If the Charitable Subtrust is revoked or otherwise terminated in such a manner that the assets of the Charitable Subtrust are restored to Trust, that event shall not be treated as an addition to Trust.

Income Tax Ruling - Ruling Request 1:

Based on the information provided and the representations made, we conclude that the funding of the Charitable Subtrust by Trust will not result in any federal income tax consequences to Trust and all items of income, deductions, and credits against tax of the Charitable Subtrust funded by Trust will be included in computing taxable income and credits of Trust.

Generation-Skipping Transfer Tax Rulings

Ruling Requests 2 & 3:

Section 2601 of the Code imposes a tax on every generation-skipping transfer made by the "transferor" to a "skip person."

Section 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provides that the tax does not apply to any generation-skipping transfer under a trust

(as defined in § 2652(b)) that was irrevocable on September 25, 1985. The rule of the preceding sentence does not apply to a pro rata portion of any generation-skipping transfer under an irrevocable trust if additions are made to the trust after September 25, 1985.

Section 26.2601-1(b)(1)(ii) provides that, except as provided in § 26.2601-1(b)(1)(ii)(B) or (C), any trust in existence on September 25, 1985, is considered an irrevocable trust.

Section 2611(a) defines the term “generation-skipping transfer” as (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 26.2611-1 provides that a generation-skipping transfer is an event that is either a direct skip, a taxable distribution, or a taxable termination. The determination as to whether an event is a generation-skipping transfer is made by reference to the most recent transfer subject to the estate and gift tax.

Section 2612(c)(1) defines the term “direct skip” to mean a transfer subject to a tax imposed by chapter 11 or 12 of an interest in property to a skip person.

Section 2613(a) defines the term “skip person” to mean - -

(1) a natural person assigned to a generation that is two or more generations below the generation assignment of the transferor, or

(2) a trust - -

(A) if all interests in the trust are held by skip persons, or

(B) if - -

(i) there is no person holding an interest in the trust, and

(ii) at no time after the transfer may a distribution (including distributions on termination) be made from the trust to a non-skip person.

Trust is a generation-skipping trust because it provides for distributions to more than one generation of beneficiaries below Grantor’s generation. Because, however, the Trust was irrevocable on September 25, 1985, and there have been no additions to it since that date, it is exempt from the GST tax pursuant to § 26.2601-1(b)(1)(i).

An amendment to a trust, which was irrevocable on September 25, 1985, and, thus is exempt from the GST tax, will cause the trust to lose its exemption if the amendment modifies or otherwise changes the quality, value, or timing of any of the

powers, beneficial interests, rights, or expectancies originally provided under the terms of the Trust.

Based on the information submitted and the representations made, we conclude that the proposed modification of Trust will not modify or otherwise change the quality, value, or timing of any of the powers, beneficial interests, rights, or expectancies originally provided under the terms of Trust. Thus, the proposed modification will not affect the exempt status of Trust for purposes of Chapter 13.

Accordingly, the creation and funding of the Charitable Subtrust shall not cause Trust, the Charitable Subtrust, or any assets of Trust or the Charitable Subtrust to be subject to the GST tax under Chapter 13 of Subtitle B of the Code.

In addition, we conclude that if the Charitable Subtrust is revoked or otherwise terminated in such a manner that the assets of the Charitable Subtrust are restored to Trust, that event will not constitute a post-September 25, 1985, addition to Trust for purposes of the GST tax imposed by § 2601.

Except as specifically ruled above, we express or imply no opinion concerning the federal tax consequences of the transactions described above under the cited provisions or under any other provision of the Code. Further, whether Trust is entitled to a deduction under § 642(c) for charitable payments made by the Charitable Subtrust is to be determined by the original terms of Trust concerning payments to charitable organizations.

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) of the Code provides that it may not be used or cited as precedent.

Sincerely,

Christine E. Ellison

Christine E. Ellison, Chief
Branch 7
Office of Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures:

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