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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4-PLR-113000-01

Date:

July 10, 2001

Legend

Original Trust =

Decedent =

Brother =

Sister =

A =

B =

C =

D =

E =

F =

G =

H =

I =

Date1 =

Date 2 =

Date 3 =

PLR-113000-01

Date 4 =

Dear _____ :

This is in response to your letter dated June 7, 2001, and prior correspondence, in which you request rulings concerning the federal income, gift, and generation-skipping transfer tax consequences of the proposed division of a trust.

You represent the facts to be as follows. Decedent's legal guardian established an irrevocable trust, the Original Trust, for Decedent's benefit on Date 1. The Original Trust was amended on Date 2. Date 2 is prior to September 25, 1985. Decedent died on Date 3.

Article I, paragraph (3) of the Original Trust provides that upon the death of Decedent, the trustee shall divide the remaining income into two equal parts and pay over and distribute, not less frequently than annually, one such equal part to Brother so long as he lives, and upon his death, to his child or children in equal shares. The remaining equal part is to be paid to Sister, and upon her death to her child or children in equal shares. Upon the death of both Brother and Sister, the entire corpus is to be divided and distributed to the children of Brother and Sister, share and share alike and to the child or children of any such niece or nephew of Decedent who is then deceased, per stirpes.

Brother died on Date 4. Brother has four children, A, B, C, and D, who are currently receiving one-half of the income from the Original Trust. Sister is living and receives the remaining one-half of the income. Sister has five children, E, F, G, H, and I.

The parties propose to divide the Original Trust into six separate trusts. Trust 1 will consist of four-ninths of the corpus. Sister will be the sole income beneficiary of Trust 1. Upon termination of Trust 1, the remaining principal will be distributed to Sister's issue, per stirpes; except that, if any child of Sister has predeceased her and leaves no issue surviving her, the share that would otherwise have been distributed to such deceased child or the issue of such deceased child will be divided into equal shares: one for each living child of Brother, one for each living child of Sister, and one for the living issue (by representation) of each deceased child of either of them who leaves such issue. Such shares will then be distributed to the person or persons for whom they were set apart, subject to any other applicable terms of Trust 1.

Trust 2 will consist of one-ninth of the corpus. Brother's children will be the beneficiaries of one-half of the income of Trust 2 and Sister will be the beneficiary of the other one-half. Upon termination of Trust 2, the remaining principal will be distributed to Sister's issue, per stirpes; except that if any child of Sister has predeceased her and leaves no issue surviving her, the share that would otherwise

PLR-113000-01

have been distributed to such deceased child or the issue of such deceased child will be divided into equal shares: one for each living child of Brother, one for each living child of Sister, and one for the living issue (by representation) of each deceased child of either of them who leaves such issue. Such shares will then be distributed to the person or persons for whom they were set apart, subject to any other applicable terms of Trust 2.

Trust 3 will consist of one-ninth of the corpus. C will be the sole income beneficiary of Trust 3 during her lifetime or until the earlier termination of Trust 3. If Trust 3 terminates before C's death, the remaining principal will be distributed to C. If C dies before the termination of Trust 3, the income will be distributed in equal shares to the then living children of Brother until the trust's termination. If Trust 3 terminates after C's death, the remaining principal will be divided in equal shares: one for each living child of Brother, one for each living child of Sister, and one for the living issue (by representation) of each deceased child of either of them who leaves such issue. The shares will then be distributed to the person or persons for whom they were set apart, subject to the other applicable terms of Trust 3.

Trust 4 will consist of one-ninth of the corpus. A will be the sole income beneficiary of Trust 4 during his lifetime or until the earlier termination of Trust 4. If Trust 4 terminates before A's death, the remaining principal will be distributed to A. If A dies before the termination of Trust 4, the income will be distributed in equal shares to the then living children of Brother until the trust's termination. If Trust 4 terminates after A's death, the remaining principal will be distributed to A's issue, per stirpes; however, if A has no issue then living, the remaining principal will be divided in equal shares: one for each living child of Brother, one for each living child of Sister, and one for the living issue (by representation) of each deceased child of either of them who leaves such issue. The shares will then be distributed to the person or persons for whom they were set apart, subject to the other applicable terms of Trust 4.

Trust 5 will consist of one-ninth of the corpus. B will be the sole income beneficiary of Trust 5 during her lifetime or until the earlier termination of Trust 5. If Trust 5 terminates before B's death, the remaining principal will be distributed to B. If B dies before the termination of Trust 5, the income will be distributed in equal shares to the then living children of Brother until the trust's termination. If Trust 5 terminates after B's death, the remaining principal will be distributed to B's issue, per stirpes; however, if B has no issue then living, the remaining principal will be divided in equal shares: one for each living child of Brother, one for each living child of Sister, and one for the living issue (by representation) of each deceased child of either of them who leaves such issue. The shares will then be distributed to the person or persons for whom they were set apart, subject to the other applicable terms of Trust 5.

Trust 6 will consist of one-ninth of the corpus. D will be the sole income beneficiary of Trust 6 during his lifetime or until the earlier termination of Trust 6. If

PLR-113000-01

Trust 6 terminates before D's death, the remaining principal will be distributed to D. If D dies before the termination of Trust 6, the income will be distributed in equal shares to the then living children of Brother until the trust's termination. If Trust 6 terminates after D's death, the remaining principal will be distributed to D's issue, per stirpes; however, if D has no issue then living, the remaining principal will be divided in equal shares: one for each living child of Brother, one for each living child of Sister, and one for the living issue (by representation) of each deceased child of either of them who leaves such issue. The shares will then be distributed to the person or persons for whom they were set apart, subject to the other applicable terms of Trust 6.

Trust 1, Trust 2, Trust 3, Trust 4, Trust 5, and Trust 6 will each continue to be governed by the terms of the Original Trust, including the termination date. All assets of the Original Trust will be divided on a pro rata basis among the six trusts. You represent that no additions have been made, constructive or actual, to the Original Trust since the death of Decedent. Decedent's death was prior to September 25, 1985.

The parties have petitioned the court with jurisdiction over the Original Trust and on March 7, 2001, obtained an order from the court to divide the Original Trust. You have represented that you will petition the court to modify the existing order consistent with the representations made in this ruling request.

You have requested the following rulings:

1. That if the Original Trust is divided into six separate trusts, each trust will be considered to have been created and irrevocable prior to September 25, 1985, and, as a result, will be exempt from the generation-skipping transfer tax imposed by § 2601.
2. That the division of the Original Trust will not constitute an additional or constructive addition to the six newly formed trusts.
3. That future distributions from the six newly formed trusts will be exempt from the generation-skipping transfer tax imposed by § 2601.
4. That the division of the Original Trust, the partitioning of the trust assets, and the allocation of such assets among the six new trusts will not be considered a sale, exchange, or other disposition of property under § 1001.
5. That as a result of the division of the Original Trust, the beneficiaries will not be deemed to have sold or exchanged their interests in the Original Trust for interests in the new trusts under § 1001.
6. That the consent by the beneficiaries to the division of the Original Trust, or the actual division itself, will not constitute a transfer for gift tax purposes by

PLR-113000-01

those individuals.

Ruling Requests 1 through 3, Generation-Skipping Transfer Tax

Section 2601 imposes a tax on every generation-skipping transfer (GST) made after October 26, 1986.

Under § 1433(b)(2)(A) of the Tax Reform Act of 1986 (Act) and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the GST tax provisions do not apply to any generation-skipping transfer under a trust (as defined in § 2652(b)) that was irrevocable on September 25, 1985. However, this exemption does not apply to additions (actual or constructive) that are made to the trust after September 25, 1985.

Section 26.2601-1(b)(1)(ii)(A) provides that, except as provided in §26.2601-1(b)(1)(ii)(B) or (C), any trust (as defined in § 2652(b)) in existence on September 15, 1985, is considered an irrevocable trust.

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 generation-skipping transfer tax 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 provisions of chapter 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 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.

In this case, the Original Trust was irrevocable on September 25, 1985, and no additions, constructive or actual, have been made to the Original Trust after that date. The parties propose to divide the Original Trust into six separate successor trusts, as described above. The proposed division of the Original Trust does not result in a shift of any beneficial interest in the trust to any beneficiary who occupies a generation lower than the persons holding the beneficial interests prior to the division. In addition, the proposed division will not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the Original Trust.

Based on the information submitted and the representations made, we conclude that the division, as proposed, will not subject the Original Trust, or any successor trust

PLR-113000-01

created under the division, to the generation-skipping transfer tax. After the division, the resulting successor trusts will continue to be exempt from the generation-skipping transfer tax imposed under § 2601 provided there are no additions to the trusts after September 25, 1985. Therefore, future distributions from Trust 1, Trust 2, Trust 3, Trust 4, Trust 5, and Trust 6 will be exempt from the generation-skipping transfer tax.

Ruling Requests 4 and 5, Income Tax

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

Section 102 excludes from gross income the value of property acquired by gift, bequest, devise, or inheritance.

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 §1011 for determining gain, and the loss shall be the excess of the adjusted basis over the amount realized.

Section 1001(b) provides 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.

Section 1001(c) provides that, except as otherwise provided in Subtitle A, the entire amount of gain or loss determined under §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 a conversion of property into cash or from an exchange of property for other property, differing materially in kind or extent is treated as income or as loss sustained.

An exchange of property results in the realization of gain or loss under §1001 if the properties exchanged are materially different. Cottage Sav. Assoc. v. Commissioner, 499 U.S. 554 (1991). There is a material difference if the exchanged properties embody legal entitlements “different in kind or extent” or if they confer “different rights and powers.” Id. at 565.

The conversion, for the purpose of eliminating a survivorship feature, of a joint tenancy into a tenancy in common is a nontaxable transaction. Likewise, the severance of a joint tenancy under a partition action pursuant to state law is a nontaxable transaction. See Rev. Rul. 56-437, 1956-2 C.B. 507. Cf. Rev. Rul. 69-486, 1969-2 C. B. 159 (nonpro-rata in-kind distribution from trust pursuant to agreement of beneficiaries is an exchange between the beneficiaries because the trustee was not

PLR-113000-01

authorized by the trust instrument or local law to make nonpro-rata distribution). The determination of how much, to whom, and when the Original Trust distributes income and corpus revolves around Sister's life. This same result will obtain under the successor trusts after the proposed partition. For example, if all presumptive beneficiaries (or their issue) outlive Sister, the proposed partition will not alter the identity of a beneficiary, nor the timing and amount of a distribution as set forth under the Original Trust.

When a presumptive beneficiary fails to outlive Sister, the proposed partition will not alter the identity of a beneficiary, nor the amount and timing of a distribution to that beneficiary, as set forth under the Original Trust. For example, after the partition, if an income beneficiary fails to outlive Sister, that beneficiary's income interest will be divided among the beneficiary's siblings. An identical distribution occurs under the Original Trust in this circumstance.

As to corpus, after the partition the interest of a beneficiary who fails to outlive Sister passes to that beneficiary's issue, if any. This same result would obtain under the Original Trust under these circumstances. Upon failure of issue, the beneficiary's interest is divided among the children of Brother and the children of Sister, per capita with issue taking by representation. This mirrors the required distribution under the Original Trust under these circumstances.

No material change will occur in the identity of the beneficiaries, the amount each will receive, or in when the beneficiaries will receive their interests as set forth under the Original Trust. Thus, no beneficiary will receive an additional interest as a result of the partition or a different interest as a result of the partition. Also, other terms and conditions of each successor trust will be the same as those of the Original Trust. We conclude, therefore, that the Original Trust will merely divide into its constituent parts. Hence, the Original Trust and its beneficiaries will not participate in an exchange for which gain or loss must be recognized under §61 or §1001 as a result of the described partition.

Ruling Request 6, Gift Tax

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 of the Original Trust into six separate trusts as it was prior to the

PLR-113000-01

division. Accordingly, based on the facts submitted and the representations made, we conclude that the proposed division will not cause any beneficiary to be considered as having made a taxable gift under § 2501.

Except as specifically set forth above, no opinion is expressed or implied regarding the federal tax consequences of this transaction under the cited provisions or any other provision of the Code. This ruling is expressly conditioned on the modification of the court order dated March 7, 2001.

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

Pursuant to a power of attorney on file with this office, a copy of this ruling is being sent to the taxpayer.

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