

Internal Revenue Service

Department of the Treasury

Number: **200320011**
Release Date: 5/16/2003
Index Number: 2601.00-00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4\PLR-122527-02

Date:

FEBRUARY 03, 2003

Legend:

Trustor =
Trust =

Trustees =

State =
Date 1 =
Date 2 =
Date 3 =
B =
X =
Y =

Dear :

This is in response to your ruling request dated April 10, 2002, and subsequent correspondence in which you requested a ruling on the generation-skipping transfer (GST) tax consequences of a proposed reformation of Trust.

Trust, an irrevocable trust, was created on Date 1. Trustees are currently serving as the trustees of Trust. Articles II and III of Trust contain the Trust dispositive provisions.

Article II(3) provides that at the end of each calendar year the trustees are to determine the net income of the Trust. One-half of the income is to be added to the principal of trust. The other one-half of the income may be distributed, in the trustees sole discretion, to the "legitimate children" of Trustor or their "legitimate surviving children." The trustees have full discretion to decide to which of the children of Trustor,

or their surviving children, payments shall be made, and the amount of each payment. Further, the trustees have the power in selecting distributees to omit all or any of the children. Further, there is no obligation to equalize payments out of future income, and the discretion of the trustees as to distributions of income is to be final. Any amount of income eligible to be distributed that remains undistributed at the end of the year is to be added to the principal of Trust.

Article III(1) provides that the trust is to continue for the term of twenty-one (21) years after the death of the last survivor of certain specified individuals, and the children of those individuals who were living at the time of the execution of the Trust instrument. Under Article III(2), on the termination of the Trust, the trustees are to distribute the entire trust corpus in equal shares to and among the legitimate issue or lineal descendants of the children of Trustor living at the time, taking in each case by right of representation.

Of the initial measuring lives designated in Trust, B, is the only one still living. Trustor had x children, all of whom are deceased. Two of Trustor's children had no children; the others had collectively y legitimate children (Trustor's grandchildren), all of whom are now living. All of Trustor's grandchildren have legitimate children (Trustor's great-grandchildren), and some of the great-grandchildren have legitimate children (Trustor's great great-grandchildren).

Under the existing terms of Trust, Trustor's grandchildren are eligible to receive distributions of the one half portion of the trust income that may be distributed in the trustees' discretion. However, on the death of a grandchild of Trustor, prior to termination of the Trust, such grandchild's legitimate surviving issue and lineal descendants will not be eligible to receive any income distributions from Trust.

On Date 2, the Trustees petitioned the State Probate Court to reform Trust. On Date 3, the Probate Court entered a provisional judgment approving the reformation, conditional upon receipt of a favorable ruling from the Internal Revenue Service, to the effect that the Trust as reformed, will not lose its GST tax exempt status. Under the Trust as reformed, the timing of the ultimate distribution of the principal of Trust is changed such that a per stirpes distribution will occur upon the sooner to occur of the termination of Trust under its current terms (21 years after the death of the surviving measuring life) or upon the respective death of each legitimate grandchild of Trustor. Upon the death of a grandchild of Trustor, the grandchild's share will pass to the grandchild's legitimate issue or lineal descendants, taking in each case by right of representation. The net income distribution provisions of Trust and the per stirpes nature of the ultimate distribution of Trust principal are not changed.

Section 2601 imposes a tax on every generation-skipping transfer (GST), which is defined under § 2611 as a taxable distribution, a taxable termination, 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 does 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 was 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)(iv) provides that if an addition is made after September 25, 1985, to an irrevocable trust which is excluded from chapter 13 by reason of § 26.2601-1(b)(1), a pro rata portion of subsequent distributions from (and terminations of interests in property held in) the trust is subject to the provisions of chapter 13.

Section 26.2601-1(b)(4) 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 under § 26.2601-1(b)(1), (b)(2), or (b)(3), will not cause the trust to lose its exempt status. The rules of § 26.2601-1(b)(4) are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. These rules do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13, but only if—(1) 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 (2) 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 a 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, Trust was irrevocable on September 25, 1985. It is represented that no additions to Trust have been made since September 25, 1985. The reformation, as described above will not shift a beneficial interest in the Trust to any beneficiary who occupies a lower generation than the persons who held the beneficial interest prior to reformation. Further, the reformation will not extend the time of any beneficial interest in the Trust. Cf., § 26.2601-1(b)(4)(i)(E), Example 5.

Accordingly, based on the facts presented and the representations made, we conclude that the reformation of Trust as described above, will not cause Trust to become subject to the GST tax. Therefore, distributions from the Trust and

terminations of any interests in the Trust will not be subject to GST tax.

The ruling contained in this letter is 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(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,

George Masnik
Chief, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure:
Copy for § 6110 purpose