

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact: _____, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B09
PLR-155297-05
Date:
October 20, 2006

Re: Private Letter Ruling

LEGEND

Decedent =
Date 1 =
Spouse =
Daughter =
Date 2 =
State Court =

Dear _____ :

This letter is in response to your authorized representative's letter dated October 31, 2005, and subsequent correspondence, requesting a generation-skipping transfer (GST) tax ruling related to a proposed transaction.

The facts submitted and representations made are as follows: Decedent died testate on Date 1, survived by Spouse, Daughter, and Daughter's descendants.

Pursuant to the provisions of Decedent's last will and testament, all the residue of Decedent's estate was transferred to the trustee of a testamentary trust established under Paragraph NINTH of the will (referred to herein as "Trust").

Paragraph NINTH, subsection (a) provides that the trustee shall pay to Spouse the entire income of Trust in periodic installments. Spouse died on Date 2.

Paragraph NINTH, subsection (b) provides that upon Spouse's death, the trustee shall continue to hold all property in trust for the benefit of Daughter and shall distribute to Daughter the entire income of Trust in periodic installments.

Paragraph NINTH, subsection (c) provides that upon Daughter's death, the entire net income of the trust is to be distributed to Daughter's children or their lineal descendants, per stirpes, until twenty-one years after the death of the last of Decedent's lineal descendants living at the time of Decedent's death. Thereafter, the trust shall terminate and be distributed to Decedent's then living issue, per stirpes.

The trustee and the current beneficiaries of Trust propose to reform Trust so that the income beneficiary of Trust will receive an annual distribution equal to the greater of (1) the net income of the trust or (2) a unitrust amount equal to five percent of the net fair market value of the trust. The parties plan to petition State Court for an order granting the trustee the authority to alter the distribution of income in the manner described above.

It has been represented that no actual or constructive additions have been made to Trust since Decedent's death.

The trustee of Trust now seeks a ruling that the proposed judicial reformation of Trust to allow the trustee to distribute to the income beneficiary the greater of the trust's net income or a unitrust amount equal to five percent of the trust assets, revalued annually, will not affect the status of Trust as being exempt from the GST tax.

Section 2601 imposes a tax on every 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 and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the GST 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 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)(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)(1)(ii) (B) or (C) (relating to property includible in the grantor's gross estate under §§ 2038 and 2042).

Section 26.2601-1(b)(1)(iv) provides that if an addition is made after September 25, 1985, to an irrevocable trust, that is excluded from the application of chapter 13 by § 1433(b)(2)(A) of the 1986 Act, 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)(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 GST tax (because the trust was irrevocable on September 25, 1985) will not cause the trust to lose its exempt status. In general, unless specifically provided otherwise, these rules are applicable only for purposes of determining whether an exempt trust retains its exempt status for GST tax purposes. Unless specifically noted, the 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 will not cause an exempt trust to be subject to the GST tax 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 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.

Section 26.2601-1(b)(4)(i)(E), Example 8, considers a situation where a trust that is otherwise exempt from the GST tax provides that trust income is payable to A for life and, upon A's death, the remainder is to pass to A's issue, per stirpes. In 2002, the appropriate local court approves a modification to the trust that converts A's income interest into the right to receive the greater of the entire income of the trust or a fixed percentage of the trust assets valued annually (unitrust interest) to be paid each year to A for life. The example concludes that the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation than the person or persons who held the beneficial interest prior to the modification. Rather, the modification can only operate to increase the amount distributable to A and decrease the amount distributable to A's issue. In addition, 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. Therefore, the modification will not subject the trust to the provisions of chapter 13.

In this case, as in Example 8, the proposed modification in this case can only operate to increase the amount distributable to the income beneficiary, and decrease the amount distributable to the remaindermen. Therefore, the proposed modification does not shift a beneficial interest in Trust to any beneficiary who occupies a lower generation than the person or persons who held the beneficial interest prior to the modification. Further, the proposed modification does not extend the time for vesting of any beneficial interest in Trust beyond the period provided for in Trust. Therefore, based on the facts and representations, we conclude that the proposed modification will not result in Trust losing its exempt status for GST tax purposes.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statements executed by the appropriate parties. While this office has not verified any part of the material submitted in support of the request for rulings, it is subject to verification and examination.

This ruling is directed only to the taxpayers 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 ruling is being sent to your authorized representative.

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,

James F. Hogan
Senior Technician Reviewer, Branch 9
(Passthroughs & Special Industries)

Enclosure

Copy for 6110 purposes