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Person To Contact:

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Telephone Number:

Refer Reply To:

CC:PSI:B04 – PLR-141222-11

Date: MARCH 28, 2012

Re:

Legend

- Date 1 =
- Date 2 =
- Z =
- Settlor =
- Spouse =
- Trust =

- State =
- Trustee =
- Child 1 =
- Child 2 =
- Child 3 =
- Child 4 =
- Mother =
- Grandchild 1 =
- Grandchild 2 =
- Grandchild 3 =
- Grandchild 4 =
- Grandchild 5 =
- Foundation =
- Charitable Trust =
- State Statute 1 =
- State Statute 2 =

Dear _____ :

This letter responds to correspondence, dated September 28, 2011 requesting rulings regarding the gift, estate, and generation-skipping transfer (GST) tax consequences of a proposed partial termination and modification of a trust.

The facts submitted and representations made are as follows. On Date 1, Settlor created an irrevocable trust (Trust) for the benefit of Settlor's grandchildren and their issue. Trust is governed by the laws of State. The current trustee is Trustee.

Article I of Trust provides that the trustee shall accumulate income and add the accumulated income to the principal of the trust until the trust is terminated. Trust terminates on the date of death of the last to die of Grantor's spouse (Spouse), Child 1, Child 2, Child 3, and Child 4. Child 1 is deceased. Currently, Spouse, Child 2, Child 3, and Child 4 are living.

Upon the termination of Trust, the trustee will distribute the principal and income, in equal shares, one share to each grandchild who is living on such date and one share to the descendants, *per stirpes*, of each grandchild who is deceased, but has one or more descendants living on such date. If, on the termination of the trust, none of the grandchildren nor any of their descendants are then living, then the trustee will distribute the principal and income of the trust to Foundation, if it is in existence. If Foundation is not in existence on such date, then the trustee will distribute the principal and income to the successor of Foundation, or if there is no successor to Foundation, to one or more organizations described in §170(c) of the Internal Revenue Code.

Article V provides that Settlor does not reserve any rights or power to alter, amend, or revoke Trust.

Currently, Settlor has five grandchildren, Grandchild 1 through Grandchild 5, (collectively referred to as Grandchildren). Grandchild 1, Grandchild 2, and Grandchild 3 are adults. Grandchild 4 and Grandchild 5 are minors. Settlor has no deceased grandchild. Settlor does not anticipate he will have any more grandchildren. Foundation has been dissolved. Subsequently, Settlor established Charitable Trust, a charitable organization described in §170(c).

State Statute 1 provides that a noncharitable irrevocable trust may be modified or terminated upon consent of the settlor and all beneficiaries, without court approval, even if the modification or termination is inconsistent with a material purpose of the trust. State Statute 1 is effective Date 2 for all trusts created before, on or after Date 2. Pursuant to State Statute 1, Settlor, Trustee of Trust, Grandchild 1, Grandchild 2, and Grandchild 3, the trustees of Charitable Trust, Mother, as representative of Grandchild 4

and Grandchild 5, and the Attorney General of State will execute an agreement (Agreement) to partially terminate and modify Trust. The interests of any unborn beneficiary, *i.e.*, the descendants of Grandchildren, are represented by Grandchildren pursuant to State Statute 2. Settlor is not a trustee of Charitable Trust and Settlor has no authority to represent any other interested party to Agreement.

Pursuant to Agreement, Trust will be divided into two shares. One share will be distributed outright, in equal shares, to each grandchild. Pursuant to Agreement, Grandchild 1, Grandchild 2, and Grandchild 3 will execute letters to Trustee requesting that their share of the outright distribution be distributed directly to Charitable Trust.

One share will continue to be held in Trust, as modified. Pursuant to the modification, the trustee will distribute \$Z per year, adjusted for inflation, to each grandchild beginning on the date when the grandchild reaches age 35. If a grandchild dies, \$Z will be distributed to that grandchild's issue, *per stirpes*. Upon the termination of the trust, the trustee will add all undistributed net income to the principal; add to the value of the then remaining principal an amount equal to the value, on the dates of distributions, of all amounts previously distributed to any grandchild or descendant of a deceased grandchild pursuant to Agreement. This total is the Augmented Remaining Trust Estate. The Augmented Remaining Trust Estate will be divided into equal shares, one for each grandchild of Settlor who is living, and one share for the descendants, *per stirpes*, of each grandchild of Settlor who is deceased but has one or more descendants. If there are no living grandchildren or descendants of grandchildren then living, the trustee will distribute the principal and income to Charitable Trust, if in existence on that date. If Charitable Trust is not in existence on that date, the trustee will distribute the principal and income to an organization described in § 170(c). The Augmented Remaining Trust Estate is intended to ensure that, upon termination of this share of Trust, each family branch will receive distributions that take into account any previous distributions to a particular family branch.

Trust will terminate upon the first to occur of the following: (a) the date of the death of the last to die of Settlor's Spouse, Child 2, Child 3, and Child 4, or (b) 21 years after the death of the survivor of Grantor, Spouse, and all his descendants living on Date 1. Thus, Trust will terminate no later than the date Trust would have terminated prior to the proposed modification.

It is represented that Settlor allocated sufficient GST exemption to the Date 1 transfer to Trust to cause Trust to have an inclusion ratio of zero.

You have requested the following rulings:

1. Trust will not be included in Settlor's gross estate at his death under § 2036 or 2038.

2. The partial termination and modification of Trust will not be treated as a deemed transfer of Trust property by Settlor for purposes of § 2501.
3. The partial termination and modification of Trust will not cause Trust, as modified, to lose its exempt status for purposes of chapter 13.

Ruling 1

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death - (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 2038(a)(1) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished during the 3-year period on the date of the decedent's death.

Section 20.2038-1(a)(2) of the Estate Tax Regulations provides that § 2038 does not apply if the decedent's power could be exercised only with the consent of all parties having an interest (vested or contingent) in the transferred property, and if the power adds nothing to the rights of the parties under local law.

In this case, Settlor is the transferor of the property in Trust for purposes of §§ 2036 and 2038. However, Settlor has not retained for any period which does not in fact end before his death, the possession or enjoyment of, or the right to the income from the trust property. Further, pursuant to Agreement, the consent of all of the parties who have an interest in Trust is required under State Statute 1. Any right Settlor has to participate in the partial termination and modification of Trust arises solely from rights granted under State Statute 1 and may be exercised only with the consent of all of the parties having an interest (vested or contingent) in the transferred property. Accordingly, based on the facts submitted and the representations made, we rule that

the partial termination and modification of Trust will not cause any property of Trust to be includible in the gross estate of Settlor under § 2036 or 2038.

Ruling 2

Section 2501 imposes a tax for each calendar year on the transfer of property by gift during such calendar year by any individual, resident or nonresident.

Section 2511 provides that, subject to certain limitations, the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property transferred is real or personal, tangible or intangible.

Section 25.2511-2(b) of the Gift Tax Regulations provides that a gift is complete as to any property, or part thereof, or interest therein, of which the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for his own benefit or for the benefit of another.

Section 25.2511-2(c) provides that a gift is incomplete if and to the extent that a reserved power gives the donor the power to name new beneficiaries or to change the interests of the beneficiaries as between themselves unless the power is a fiduciary power limited by a fixed or ascertainable standard.

Section 25.2511-2(d) provides that a gift is not considered incomplete, however, merely because the donor reserves the power to change the manner or time of enjoyment. Thus, the creation of a trust the income of which is to be paid annually to the donee for a period of years, the corpus being distributable to him at the end of the period, and the power reserved by the donor being limited to a right to require that, instead of the income being so payable, it should be accumulated and distributed with the corpus to the donee at the termination of the period, constitutes a completed gift.

Section 25.2511-2(e) provides that a donor is considered as himself having a power if it is exercisable by him in conjunction with any person not having a substantial adverse interest in the disposition of the transferred property or the income therefrom. A trustee, as such, is not a person having an adverse interest in the disposition of the trust property or its income.

Section 25.2514-1(b)(2) provides that the term "power of appointment" does not include powers reserved by a donor to himself.

In this case, Settlor transferred property to Trust on Date 1. On Date 1, Settlor parted with dominion and control of the transferred property. Settlor did not retain any power to change its disposition for his own benefit or for the benefit of another. Settlor did not retain the power to name new beneficiaries or to change the interests of the

beneficiaries as between themselves. Settlor is a party to Agreement pursuant to the requirements of State Statute 1. The other parties to Agreement are the beneficiaries of Trust and they have a substantial interest in Trust. Therefore, Settlor is not exercising any power in conjunction with persons not having a substantial interest in Trust. Accordingly, based on the facts submitted and the representations made, we conclude that the partial termination and modification of Trust will not result in a transfer by Settlor of Trust assets for purposes of § 2501.

Ruling 3

Section 2601 provides that a tax is imposed on every generation-skipping transfer. Section 2611(a) provides that the term “generation-skipping transfer” means a tax distribution, and taxable termination, and a direct skip.

Section 26.2601-1(b)(4)(i) of the Generation-Skipping Transfer Tax Regulations 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 paragraph (b)(1), (2), or (3) of this section will not cause the trust to lose its exempt status. Unless specifically provided otherwise, the rules contained in this paragraph are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. Thus, 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 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 (including a trustee distribution, settlement, or construction that does not satisfy paragraph (b)(4)(i)(A), (B), or (C) of this section) by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause the 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.

No guidance has been issued concerning the partial termination or modification of a trust that may affect the status of a trust that is exempt from GST tax because sufficient GST exemption was allocated to the trust to result in an inclusion ratio of zero. At a minimum, a partial termination or modification that would not affect the GST status of a grandfathered trust should similarly not affect the exempt status of such a trust.

In this case, the partial termination of Trust will accelerate the distribution of a portion of the corpus of Trust to the beneficiaries and the modification of Trust will cause \$Z of the income interest to be distributed annually to each beneficiary. The partial termination and modification will 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 partial termination and modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. Accordingly, based upon the facts provided and the representations made, we conclude that the partial termination and modification of Trust will not cause Trust, as modified, to lose its exempt status for purposes of chapter 13.

Except as specifically ruled herein, we express 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 who requested it. Section 6110(k)(3) 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 letter 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 yours,

Lorraine E. Gardner
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure

Copy for section 6110 purposes