Internal Revenue Service

Department of the Treasury

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Washington, DC 20044

Index No.: 2033.00-00;
2036.00-00; 2037.00-00;
2038.00-00; 2041.00-00;
2601.00-00

Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:P&SI:7:PLR-109320-98
Date: OCT 8 1998

Re:

Legend: X:
Trust A:

Trust B:

Date:
Sister:
Bank:

Dear

This is in response to your letter dated , and other submissions, in which you request rulings concerning the estate and generation-skipping transfer tax consequences of the modifications to the trusts described below.

The facts are represented to be as follows: In Date, X created two trusts, Trusts A and B, one for the benefit of each of her two children. The terms of both trusts are identical. The initial co-trustees were X's Sister and Bank. The terms of each trust provide that the individual co-trustee and the designated successor individual co-trustee can remove and replace Bank with another corporate trustee.

The terms of each trust provide that, during the life of each child/beneficiary, the trustee may make distributions of income to the child at the trustee's discretion. Upon the death of the child, the trustee may make distributions of income to the child's issue as is necessary or advisable for their health,

happiness, maintenance, education, welfare, or comfort. In addition, the trustee may make discretionary distributions of principal to the child or the child's issue at any time. With respect to the decision to distribute income and principal, the trust instrument states that the term "trustee" refers to the two co-trustees whenever both are acting, and the bank whenever it is acting as sole trustee.

Each trust is to terminate on the twentieth anniversary of the last to die of the child and his or her siblings that were living at the time the trust was created, or the twentieth anniversary of the death of the last to die of the child and that child's issue, whichever occurs first. At termination, all undistributed income and principal is to be distributed in equal shares per stirpes to the then-living issue of the child who was the primary beneficiary of the trust, or, if there are no issue then living, to the other trusts created by X in Date that are still in existence, or, if there are no other trusts in existence, then to a specified private foundation. Each trust also provides that in no event shall any trust property vest in X, X's parents, or any individual co-trustee by operation of law or otherwise.

The current trustees propose to petition the local court to modify the provisions of Trusts A and B, to name new successor individual co-trustees, and to modify the removal and replacement clause with respect to the corporate co-trustee. They propose to modify the trusts to designate cousins of the beneficiaries to serve as individual co-trustees. No person named as a successor individual co-trustee can serve as trustee if the beneficiary is then serving as an individual co-trustee of a comparable trust for that person. The trusts also will be modified to allow the primary beneficiary of each trust (or if he or she is deceased a majority of the issue of the primary beneficiary) to remove and replace the corporate co-trustee. Under the proposed terms, any successor corporate co-trustee cannot be subordinate to the taxpayer or beneficiaries within the meaning of § 672(c) of the Internal Revenue Code. The current trustees also propose to grant the individual co-trustee of each trust the sole and exclusive power to make trust investments.

You request that we rule as follows:

(1) The proposed changes to Trusts A and B will not cause the interest of any beneficiary of the Trusts, including any beneficiary serving as Trustee, to be includible in such beneficiary's gross estate under § 2033.

(2) The proposed changes to Trusts A and B will not cause the interest of any beneficiary of the Trusts, including any beneficiary serving as co-trustee, to be includible in such beneficiary's gross estate under §§ 2036 through 2038.

(3) The proposed changes to Trusts A and B will not cause the beneficiary of the Trust, including any beneficiary serving as co-trustee, to be treated as having or having exercised or released a general power of appointment under §§ 2041 and 2514.

(4) The proposed modifications, as described above, will not affect the exempt status of Trusts A and B, with respect to the generation-skipping transfer tax and, if no additions are made to the trusts, all distributions from and the termination of each trust will be exempt from the generation-skipping transfer tax.

Issues 1, 2 & 3:

Section 2033 provides for the inclusion in the gross estate of any property in which the decedent had an interest at the time of his death.

Section 2036(a) provides that the value of the gross estate includes the value of any property of which the decedent has made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth) in which the decedent has retained for his life the possession or enjoyment of, or the right to the income from the property, or the right to designate the persons who shall possess or enjoy the property or the income from the property.

Section 2037 provides that the value of the gross estate includes the value of any interest therein of which the decedent has at any time after September 17, 1916, made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, if (1) possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent, and (2) the decedent has retained a reversionary interest in the property, and the value of such reversionary interest immediately before the death of the decedent exceeds 5 percent of the value of such property.

Section 2038(a) provides that the value of the gross estate includes the value of all property of which the decedent has at any time made a transfer (except where there has been 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 death to any change through the exercise of a power by the decedent to alter, amend, revoke, or terminate the interest in the property or where the decedent relinquished

this power within the three year period ending on the date of the decedent's death.

Section 2041 provides that the gross estate includes any property with respect to which the decedent has, at the time of his death, a general power of appointment or with respect to which the decedent has at any time released or exercised such power of appointment by a disposition which, had the property been owned by the decedent, such property would be includible in the decedent's gross estate under §§ 2035 through 2038, inclusive. A general power of appointment is a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate, except where the decedent's power is limited by an ascertainable standard relating to the health, education, support, or maintenance of the decedent.

Section 2514(b) provides that the exercise or release of a general power of appointment created after October 21, 1942, will be deemed a transfer of property by the individual possessing the power.

Section 20.2041-1(c)(1) of the Estate Tax Regulations provides that a power of appointment is not a general power if by its terms it is either 1) exercisable only in favor of one or more designated persons or classes other than the decedent or his creditors, or the decedent's estate or the creditors of his estate, or 2) expressly not exercisable in favor of the decedent or his creditors, or the decedent's estate or the creditors of his estate. A power of appointment exercisable for the purpose of discharging a legal obligation of the decedent or for his pecuniary benefit is considered a power of appointment exercisable in favor of the decedent or his creditors.

Section 20.2041-1(b) provides that the mere power of management, investment, custody of assets, or the power to allocate receipts and disbursements as between income and principal, exercisable in a fiduciary capacity, whereby the holder has no power to enlarge or shift any of the beneficial interests therein except as an incidental consequence of the discharge of such fiduciary duties is not a power of appointment.

Rev. Rul. 95-58, 1995-2 C.B. 191, holds that a decedent/grantor's reservation of an unqualified power to remove a trustee and appoint an individual or corporate successor trustee that is not related or subordinate within the meaning of § 672(c), is not considered a reservation of the trustee's discretionary powers of distribution over the property transferred by the decedent/grantor to the trust. Accordingly, the property in the trust would not be includible in the decedent/grantor's gross estate under §§ 2036 or 2038.

In the present case, the trustees propose to petition the local court to modify Trusts A and B to designate cousins of the children as individual co-trustees of the trusts. No person named as a successor individual co-trustee can serve as trustee if the beneficiary is then serving as an individual co-trustee of a comparable trust for that person. In addition, the trustees propose to modify the terms of each trust to allow the primary beneficiary of each trust (or if he or she is deceased, a majority of the issue of the primary beneficiary) to remove and replace the corporate trustee. Under the terms of the proposed modification, any successor corporate trustee may not be related or subordinate to the beneficiary within the meaning of § 672(c).

Accordingly, we conclude that the proposed changes to Trusts A and B will not cause the interest of any beneficiary of the Trusts, including any beneficiary serving as Trustee, to be includible in such beneficiary's gross estate under § 2033 or §§ 2036 through 2038. In addition, we conclude that the beneficiaries of Trusts A and B will not be treated as holding a general power of appointment and, therefore, the property in Trusts A and B will not be includible in the gross estate of the beneficiary of that trust under §§ 2041 or 2514.

Issue 4:

Section 2601 imposes a tax on every generation-skipping transfer. Section 2611 defines a generation-skipping transfer to mean a taxable termination, a taxable distribution, or a direct skip.

Section 2612(a) provides that a taxable termination means a termination by death, lapse of time, release of a power, or otherwise of an interest in property held in trust where the property passes to a skip person. Section 2612(b) provides that a taxable distribution means any distribution from a trust to a skip person other than a taxable termination or a direct skip. Section 2612(c) provides that a direct skip means a transfer subject to a tax imposed by Chapters 11 or 12 of an interest in property to a skip person.

Section 2613 defines a skip person as 1) a natural person who is assigned to a generation that is two or more generations below that of the transferor, or 2) a trust in which either a) all interests are held by skip persons, or b) there is no person holding an interest in the trust and at no time after the transfer may a distribution (including distributions upon termination) be made from the trust to a non-skip person.

Section 26.2601-1(a)(1) of the Generation-Skipping Transfer Tax Regulations provides that the tax will apply to any generation-skipping transfer made after October 22, 1986. Section 26.2601-1(b)(1)(i) provides an exception to this rule for any distributions from a trust that was irrevocable on September 25, 1985. However, this exemption does not apply to a pro rata portion of any generation-skipping transfer under an irrevocable trust where additions were made to the trust after September 25, 1985.

In the present case, Trusts A and B were irrevocable on September 25, 1985, and there have been no additions to the Trusts after that date. In addition, there have been no modifications or amendments to the Trust agreements since that date.

The proposed Trust modifications, as described above, are administrative in nature and will not result in any change in the quality, value, or timing of any beneficiary's interest in the Trusts. The proposed modifications to the Trust agreements will not confer any additional powers or beneficial interests upon any of the beneficiaries and will not create any additional generation-skipping transfers or increase the amount of any generation-skipping transfers. The number of younger generations provided for will remain the same.

We conclude that Trusts A and B are currently exempt from the generation-skipping transfer tax imposed by § 2601. In addition, we conclude that the proposed trust modifications, as described above, will not affect the exempt status of the trusts with respect to the generation-skipping transfer tax and, if no additions are made to the trusts, all distributions from and the termination of the trusts will be exempt from the generation-skipping transfer tax.

Except as we have specifically ruled herein, we express or imply no opinion under the cited provisions or under any other provision of the Code.

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 the 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 who requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent.

Sincerely yours,

Mary A. Berman

Mary A. Berman
Assistant to the Chief, Branch 7
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures:
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