Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:9 / PLR-111234-00
Date:
January 11, 2001

Legend:

Trust:

Grantor:

A:

B:

C:

D:

E:

Date 1:

Date 2:

State:

Dear

We received your letter dated May 27, 2000, requesting rulings under §§ 61, 643, 1001, 1015, 1223, 2501, and 2601 of the Internal Revenue Code. This letter responds to your request.

Grantor executed a trust agreement creating an irrevocable inter vivos trust, Trust, on Date 1 for the benefit of Grantor's daughter, A, and A's issue. A died on Date 2, survived by B, C, D, and E, who are children of A.

Paragraph A of Article 2 of the trust agreement provides in part that the trustee shall manage, invest and reinvest the trust estate, shall collect the income therefrom,

after deducting from such income the expenses of administration chargeable thereto, shall from time to time during the trust term, as hereinafter defined, pay, or in his discretion apply, out of such net income such amounts to or for the benefit of such one or more members living at the time of such payment or application of the class consisting of A and the issue of A and in such proportions amongst them, with power to exclude any one or more, as the trustee shall in his discretion determine to be advisable, accumulating and adding to principal any net income not so paid or applied. In addition, the trustee shall from time to time make such distributions, or in his discretion apply such amounts, out of the principal of the trust estate to or for the benefit of such one or more members of said class living at the time of such distribution or application, in such proportions amongst them and with like power of exclusion, as the trustee in his discretion determine to be advisable.

Paragraph A of Article 2 of the trust agreement also provides in part that at the end of the trust term, the trust hereunder shall terminate and the trustee shall distribute the then remaining principal of the trust estate, with all accrued and all undistributed income pertaining thereto, to the then living issue of A, in equal shares per stirpes, or, if there shall be none, to Grantor's then living issue, in equal shares per stirpes, or, if there shall be none, to those persons to whom and in those proportions in which the same would have been distributed under the laws of State then in effect had Grantor died intestate immediately after the end of the trust term, domiciled in State and owning said principal and income.

Paragraph A of Article 2 of the trust agreement further provides in part that as used in this agreement, the expression "trust term" shall mean the period beginning at the date of this agreement and ending upon the earlier of (a) the death of the last to die of A and the issue of A or (b) the twenty-first anniversary of the death of the last to die of A and the children of A living at the date of this agreement, namely, B, C, D, and E.

Paragraph B of Article 2 of the trust agreement provides in part that notwithstanding the provisions of paragraph A of Article 2, if A shall die before the end of the trust term and at any time or from time to time after her death the trustee shall in his discretion determine it to be economically expedient or otherwise advisable, he is authorized to divide all or any part of the principal of the trust estate into equal shares per stirpes in respect of the issue of A at the time of such division and to hold each resulting share of said principal or part thereof as the principal of a separate trust for the benefit of the issue in respect of whom the same shall have been determined (hereinafter referred to in this paragraph B as the "beneficiary") and the issue of the beneficiary and to add to such last-mentioned principal any such share determined in respect of the beneficiary which shall result from any subsequent division pursuant to this paragraph B.

Paragraph B of Article 2 of the trust agreement also provides in part that each such trust shall terminate at the end of the trust term or upon the earlier death of the

beneficiary, and during such period the trustee shall manage, invest and reinvest said share, shall collect the income therefrom and, after deducting from such income such expenses of administration as shall be properly chargeable thereto, shall from time to time pay, or in his discretion apply, out of such net income such amounts to or for the benefit of such one or more of the beneficiary and the issue of the beneficiary living at the time of such payment or application and in such proportions amongst them, with power to exclude any one or more, as the trustee shall in his discretion determine to be advisable, accumulating and adding to principal any net income not so paid or applied. The trustee shall from time to time make such distributions, or in his discretion apply such amounts, out of the principal of said share to or for the benefit of such one or more of the beneficiary and the issue of the beneficiary living at the time of such distribution or application, in such proportions amongst them and with like power of exclusion, as the trustee shall in his discretion determine to be advisable.

Paragraph B of Article 2 of the trust agreement further provides in part that at the end of such period such trust shall terminate and the then remaining principal thereof, with all accrued and all undistributed income pertaining thereto, shall be distributed to the beneficiary. If the beneficiary shall not be living at the end of such period, he or she shall have a limited testamentary power of appointment over said principal and income, such power to be exercisable, by express reference thereto in his or her duly probated will, in favor of any person or persons other than the beneficiary, the beneficiary's creditors, the beneficiary's estate or creditor of the beneficiary's estate. To the extent, if any, that said principal and income shall not thus be effectively appointed, the same shall be distributed to the beneficiary's then living issue, in equal shares per stirpes, or, if there shall be none, in equal shares per stirpes to the then living issue of the beneficiary's nearest ancestor of whom there shall be issue then living and who shall be a descendant of Grantor, or if there shall be none, to Grantor's then living issue, in equal shares per stirpes, or, if there shall be none, to those persons to whom and in those proportions in which the same would have been distributable under the laws of State then in effect had Grantor died intestate immediately after the end of such period, domiciled in State and owning said unappointed principal and income.

The trustees of Trust now propose to partition Trust pro rata into four separate trusts, one for the primary benefit of each of A's four children, namely, B, C, D, and E.

You represent that no additions, actual or constructive, have been made to Trust after September 25, 1985.

You have requested the following rulings:

1. The proposed pro rata partition of Trust will not cause Trust to lose its Generation-Skipping Transfer (GST) tax exempt status and will not cause the partitioned trusts to be subject to the GST tax.

2. Neither the proposed partition of Trust into four separate trusts nor the proposed pro rata allocation of Trust assets among the partitioned trusts will constitute a transfer by any of B, C, D, and E that will be subject to the gift tax under § 2501.

3. After the proposed partition of Trust into four separate trusts, each of the partitioned trusts will be treated as a separate taxpayer under § 643(f).

4. The proposed partition of Trust into four separate trusts and the proposed pro rata allocation of each existing asset among the partitioned trusts will not result in the realization by Trust of any income under § 61 and will not result in the realization of any gain or loss under § 1001.

5. After the proposed partition of Trust into four separate trusts, the assets of the partitioned trusts received from Trust will have the same basis and the same holding periods as those assets formerly had when held by Trust under §§ 1015 and 1223, respectively.

Ruling Request 1

Section 2601 imposes a tax on every generation-skipping transfer.

Section 2611(a) provides that, for purposes of the GST tax, the term “generation-skipping transfer” means (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 2612(a)(1) provides that, for purposes of the GST tax, the term “taxable termination” means the termination (by death, lapse of time, release of power, or otherwise) of an interest in property held in a trust unless –

(A) immediately after such termination, a non-skip person has an interest in such property, or

(B) at no time after such termination may a distribution (including distributions on termination) be made from such trust to a skip person.

Section 2612(b) provides that, for purposes of the GST tax, the term “taxable distribution” means any distribution from a trust to a skip person (other than a taxable termination or a direct skip).

Section 2612(c)(1) provides that, for purposes of the GST tax, the term “direct skip” means a transfer subject to a tax imposed by chapter 11 or 12 of an interest in property to a skip person.

Section 2613(a) provides that, for purposes of the GST tax, the term “skip person” means --

(1) a natural person assigned to a generation which is 2 or more generations below the generation assignment of the transferor, or

(2) a trust

(A) if all interests in such trust are held by skip persons, or

(B) if --

(i) there is no person holding an interest in such trust, and

(ii) at no time after such transfer may a distribution (including distribution on termination) be made from such trust to a non-skip person.

Section 2613(b) provides that, for purposes of the GST tax, the term “non-skip person” means any person who is not a skip person.

Section 26.2601-1(b)(1)(i) of the GST Tax Regulations provides in part that the GST tax does not apply to any generation-skipping transfer under a trust (as defined in § 2652(b)) that was irrevocable on September 25, 1985. The rule of the preceding sentence does not apply to a pro rata portion of any generation-skipping transfer under an irrevocable trust if additions 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 25, 1985, is considered an irrevocable trust.

Section 26.2601-1(b)(4)(i)(D) provides that

(1) 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 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 section 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.

(2) For purposes of this section, 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 GST transfer or the creation of a new GST transfer. To determine whether a modification of an irrevocable trust will shift a beneficial interest in a trust to a beneficiary who occupies a lower generation, the effect of the instrument on the date of the modification is measured against the effect of the instrument in existence immediately before the modification. If the effect of the modification cannot be immediately determined, it is deemed to shift a beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification. A modification that is administrative in nature that only indirectly increases the amount transferred (for example, by lowering administrative costs or income taxes) will not be considered to shift a beneficial interest in the trust.

Based on the information submitted and representations made, we conclude that the proposed pro rata partition of Trust will not cause Trust to lose its Generation-Skipping Transfer (GST) tax exempt status and will not cause the partitioned trusts to be subject to the GST tax.

Ruling Request 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.

The proposed partition of Trust and the proposed allocation of Trust assets are consistent with the trust agreement and accord the beneficiaries no more than their legal entitlement. Accordingly, we conclude that neither the proposed partition of Trust into four separate trusts nor the proposed pro rata allocation of Trust assets among the partitioned trusts will constitute a transfer by any of B, C, D, and E that will be subject to the gift tax under § 2501.

Ruling Request 3

Section 643(f) provides that under regulations prescribed by the Secretary, two or more trusts shall be treated as one trust if (1) such trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and (2) a principal purpose of such trusts is the avoidance of the tax imposed by Chapter 1 of the Code.

Section 1806(b) of the Tax Reform Act of 1986 provides that in the case of a trust which was irrevocable on March 1, 1984, § 643(f) shall apply only to that portion of the trust which is attributable to a contribution to corpus after March 1, 1984.

Accordingly, as long as the four new trusts are separately managed and administered, they will be considered separate trusts for federal income tax purposes.

Ruling Request 4

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

Section 1001(a) provides that the gain from the sale or other disposition of property shall be the excess of the amount realized over the adjusted basis provided in § 1011, and the loss shall be the excess of the adjusted basis over the amount realized.

Section 1001(c) provides that, except as otherwise provided in subtitle A of the Code, the entire amount of the gain or loss on the sale or exchange of property shall be recognized.

Section 1.1001-1(a) of the Income Tax Regulations provides the general rule that, except as otherwise provided in subtitle A of the Code, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or as loss sustained. See generally Cottage Savings Ass'n v. Commissioner, 499 U.S. 554 (1991).

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. In each situation there is no sale or exchange. See Rev. Rul. 56-437, 1956-2 C.B. 507. Cf. Rev. Rul. 69-486, 1969-2 C.B. 159 (non-pro rata in-kind distribution from trust pursuant to agreement of beneficiaries is an exchange between the beneficiaries because trustee was not authorized by the trust instrument or local law to make non-pro rata distribution), distinguished by Rev. Rul. 83-61, 1983-1 C.B. 78.

As a general matter, a transaction will be a taxable event under § 1001 if (1) the transaction is a sale, exchange, or other disposition of property and (2) when there is an exchange, the exchange results in the receipt of property that is "materially different." In the ruling request, Paragraph B of Article 2 of the trust agreement provides the authority for the trustees, after the death of Grantor's daughter A, to partition all or any part of the principal of Trust into equal shares per stirpes in respect of Grantor's daughter's living issue and to hold each such separate trust for the benefit of the particular issue and his or her issue. The proposed partition of Trust is in compliance with the terms and conditions of the trust agreement.

Accordingly, the proposed partition will not be a sale, exchange, or other disposition of property. Therefore, we conclude that the division of Trust into four

separate trusts and distribution of Trust's assets among the four partitioned trusts on a pro rata basis will not cause Trust to recognize any gain or loss from a sale or other disposition of property under §§ 61 or 1001.

Ruling Request 5

Section 1015(b) provides that if the property was acquired after December 31, 1920, by a transfer in trust (other than by a transfer in trust by a gift, bequest, or devise), the basis shall be the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor on such transfer under the law applicable to the year in which the transfer was made.

Section 1.1015-1(b) of the Income Tax Regulations provides in part that property acquired by gift has a single or uniform basis although more than one person may acquire an interest in such property. The uniform basis of the property remains fixed subject to proper adjustment for items under §§ 1016 and 1017.

Section 1.1015-2(a) provides that in the case of property acquired after December 31, 1920, by transfer in trust (other than by a transfer in trust by a gift, bequest, or devise), the basis of property so acquired is the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor upon such transfer under the law applicable to the year in which the transfer was made. If the taxpayer acquired the property by a transfer in trust, this basis applies whether the property be in the hands of the trustee, or the beneficiary, and whether acquired prior to the termination of the trust and distribution of the property, or thereafter.

Section 1.1015-2(a)(2) provides that the principles stated in § 1.1015-1(b) concerning the uniform basis are applicable in determining the basis of property where more than one person acquires an interest in property by transfer in trust after December 31, 1920.

Section 1223(2) provides that in determining the period for which the taxpayer has held property however acquired there shall be included the period for which such property was held by any other person, if under chapter 1 of the Code such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as it would have in the hands of such other person. See also § 1.1223-1(b) of the Income Tax Regulations.

Based on the information submitted and representations made, we conclude that after the proposed partition of Trust into four separate trusts, the assets of the partitioned trusts received from Trust will have the same basis as those assets formerly had when held by Trust under § 1015. Furthermore, because under § 1015 each

partitioned trust's basis in an asset transferred to it by Trust will equal Trust's basis in the asset at the time of transfer, under § 1223(2) each partitioned trust's holding period for an asset transferred to it by Trust will include Trust's holding period for the asset at the time of transfer.

Except as specifically ruled herein, we express or imply no opinion concerning the federal tax consequences of this transaction under the cited provisions or any other provisions of the Code.

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.

Sincerely,
James C. Gibbons
Assistant to the Chief, Branch 7
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure: Copy of § 6110 purposes