

Number: 201218002

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December 20, 2011

Bank =

Dear _____ :

This responds to the ruling request dated June 27, 2011, submitted by your authorized representative requesting a generation-skipping transfer tax ruling regarding the exercise and proposed exercise of powers of appointment over assets in certain trusts.

The facts submitted are as follows:

Daughter's Trust 1

On Date 1, Settlor created Trust 1, a revocable inter vivos trust. On Date 2, a date prior to October 21, 1942, Trust 1 became irrevocable. Under the terms of Trust 1, a separate trust, Daughter's Trust 1, was created for the primary benefit of Trustor's daughter, Daughter. Under the terms of Trust 1, the net income of the trust is payable to Daughter for life. Upon Daughter's death, the trust estate is to pass pursuant to a testamentary power of appointment exercisable by Daughter. Daughter was granted a power to appoint the trust estate to a class consisting of Daughter's issue or Settlor's issue, in such proportions and upon and subject to such terms, conditions and restrictions as Daughter shall appoint. In default of such exercise, the trust estate will be distributed to Daughter's then surviving issue, *per stirpes*. If Daughter has no surviving issue, then the trust estate will pass to Settlor's surviving issue.

Article 2.10 of Trust 1 provides that no trust, including Daughter's Trust 1, or share thereof shall be retained in trust for a longer period than twenty-one (21) years after the death of the last survivor of Settlor, Daughter, Settlor's son-in-law, and Settlor's daughter-in-law, who were all living on the date the trust became irrevocable, and at the expiration of said period such trust or share shall be distributed to the beneficiary then receiving trust income.

Daughter's Trust 2

On Date 3, a date prior to October 21, 1942, Settlor created Trust 2, an irrevocable trust. Under the terms of Trust 2, a separate trust, Daughter's Trust 2, was created for the primary benefit of Daughter. Under the terms of Trust 2, the net income of the trust is payable to Daughter for life. Upon Daughter's death, the trust estate is to pass pursuant to a testamentary power of appointment exercisable by Daughter. Daughter was granted a power to appoint the trust estate to a class consisting of Daughter's issue or Settlor's issue, in such proportions and upon and subject to such terms, conditions and restrictions as Daughter shall appoint. In default of such exercise, the trust estate will be distributed to Daughter's then surviving issue, *per stirpes*. If Daughter has no surviving issue, then the trust estate will pass to Settlor's surviving issue.

Article 3.06 of Trust 2, provides that no trust, including Daughter's Trust 2, or share thereof shall be retained in trust for a longer period than twenty-one (21) years after the death of the last survivor of A, B, C, D and Settlor's two children (Daughter and Son), who were living on the date the trust was created, and at the expiration of said period such trust or share shall be distributed to the beneficiary then receiving trust income.

Exercise of Daughter's Powers of Appointment

Daughter died on Date 4. Under the terms of Article Eighth of Daughter's Last Will and Testament (Will), Daughter appointed part of her interest in Daughter's Trusts 1 and 2 outright and the balance in further trust, Granddaughter's Appointive Trust, for the benefit of her granddaughter (Granddaughter). During Granddaughter's life, the trustees of Granddaughter's Appointive Trust are authorized to distribute net income and principal to or for the benefit of Granddaughter and her descendants for their health, maintenance, support, and education. An Independent Trustee, in his sole discretion, has the authority to distribute net income and principal to or for the benefit of Granddaughter and her descendants if it is in the beneficiary's best interest. The Independent Trustee may terminate the trust in favor of any one or more of the beneficiaries. Granddaughter's Appointive Trust terminates upon Granddaughter's death.

Under Article Eighth (C) of Daughter's Will, upon Granddaughter's death, Granddaughter has the power to appoint by will the property remaining in her Appointive Trust to or for the benefit of any one or more of Daughter's descendants who survive Granddaughter. In default of Granddaughter's exercise, the trust property will be held in further trust, one share, *per stirpes*, for Granddaughter's then living descendants or, if none, for Daughter's then living descendants. The trusts that may be established by Granddaughter's exercise of her power of appointment are referred to as "Continuing Trusts."

Notwithstanding the provisions of Article Eighth (C) of Daughter's Will, all trusts consisting of property derived from Trusts 1 and 2, including any Appointive Trust and any Continuing Trust, are required to terminate within the applicable rule against perpetuities. Further, Article Tenth of Daughter's Will provides that if any trust has not terminated (i) prior to the 21st anniversary of the death of the last to die of the descendants of Daughter's great grandparents who were living on the earliest date that Trusts 1 and 2 became irrevocable or (ii) prior to the 21st anniversary of the death of the last to die of such class of the descendants of Daughter's great grandparents who were living on the earliest date that Trusts 1 and 2 became irrevocable as shall be necessary so that the duration of such trust does not violate any applicable rule against perpetuities nor cause such trust to lose its exempt status for generation-skipping transfer purposes, such trust shall terminate on the day immediately preceding the earlier of the dates described in preceding clauses (i) or (ii) (the "termination date"). Prior to the testamentary exercises, Daughter's Trusts 1 and 2 terminate by their terms 21 years after the death of Daughter, the last surviving measuring life of Trusts 1 and 2.

Currently, Bank and Granddaughter are serving as trustees of Granddaughter's Appointive Trust. In State court proceedings, State Court ruled that Daughter's powers

of appointment were validly exercised to create Granddaughter's Appointive Trust for State law purposes and that the termination provisions of Article Tenth of Daughter's Will supersede the termination provisions in Trusts 1 and 2.

It is represented that no additions, actual or constructive, have been made to Trust 1 or Trust 2 since September 25, 1985.

The trustees of Granddaughter's Appointive Trust request the following rulings:

(1) The exercise by Daughter of her testamentary powers of appointment over Daughter's Trusts 1 and 2 did not cause Daughter's trusts, or any trusts, including Granddaughter's Appointive Trust, created by the exercise of the powers to lose their GST exempt status for purposes of chapter 13.

(2) The exercise of Granddaughter's testamentary power of appointment over Granddaughter's Appointive Trust will not cause Granddaughter's Appointive Trust, or any trusts, including any Continuing Trusts, created by the exercise of the power to lose their GST exempt status for purposes of chapter 13.

Law and Analysis

Section 2041(a)(1) of the Internal Revenue Code provides that the value of the gross estate shall include the value of all property with respect to which the decedent has at the time of his death exercised a general power of appointment created before October 21, 1942.

Section 2041(b)(1) defines the term "general power of appointment" as a power that is exercisable in favor of the decedent, the decedent's estate, the decedent's creditors, or the creditors of the decedent's estate. A power to consume, invade, or appropriate property for the benefit of the decedent that is limited by an ascertainable standard relating to the health, education, support, or maintenance of the decedent is not a general power of appointment.

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 (a) 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 the holder's estate, or (b) expressly not exercisable in favor of the decedent or his creditors, or the decedent's estate, or the creditors of his estate.

In the present case, Trusts 1 and 2 each grant Daughter a testamentary power of appointment over the property in Daughter's Trusts 1 and 2 which may not be exercised in favor of Daughter, Daughter's creditors, Daughter's estate, or the creditors of Daughter's estate. Therefore, Daughter's powers of appointment over Daughter's

Trusts 1 and 2 are not general powers of appointment. Accordingly, the exercise of Daughter's limited powers of appointment will not cause the property transferred to Granddaughter's Appointive Trust to be included in Daughter's gross estate under § 2041.

Section 2601 imposes a tax on every generation-skipping transfer (GST) made by a "transferor" to a skip person. The term "generation-skipping transfer" is defined in § 2611 as a taxable distribution, a taxable termination, and a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (the Act) and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, provide that the generation-skipping transfer 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 the transfer is 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) provides that any trust in existence on September 25, 1985, will be considered irrevocable unless the settlor held a power that would have caused inclusion of the trust in the settlor's gross estate under § 2038 or 2042 if the settlor had died on September 25, 1985.

In the present case, Trusts 1 and 2 were irrevocable prior to September 25, 1985. Therefore, Trusts 1 and 2, including Daughter's Trusts 1 and 2, are exempt from the GST tax under § 2601. However, the rule under § 26.2601-1(b)(1)(i) does not apply to a transfer of property pursuant to the exercise, release or lapse of a general power of appointment that is treated as a taxable transfer under chapter 11 or chapter 12. Section 26.2601-1(b)(1)(v)(A) provides that, except as provided under § 26.2601-1(b)(1)(v)(B), where any portion of a trust remains in the trust after the post-September 25, 1985, release, exercise, or lapse of a power of appointment over that portion of the trust, and the release, exercise, or lapse is treated to any extent as a taxable transfer under chapter 11 or chapter 12, the value of the entire portion of the trust subject to the power that was released, exercised, or lapsed is treated as if that portion had been withdrawn and immediately retransferred to the trust at the time of the release, exercise, or lapse. The creator of the power will be considered the transferor of the addition except to the extent that the release, exercise, or lapse of the power is treated as a taxable transfer under chapter 11 or chapter 12.

In the present case, Daughter's powers of appointment are not exercisable in favor of Daughter, Daughter's creditors, Daughter's estate, or the creditors of Daughter's estate. Accordingly, Daughter's powers of appointment are not general powers of appointment and, as noted above, Daughter's exercise of her limited powers of appointment are not treated as a taxable transfer under chapter 11. Therefore, the rule under § 26.2601-1(b)(1)(v)(B) does not apply.

Section 26.2601-1(b)(1)(v)(B) provides a special rule for certain limited powers of appointment. Under this section, the release, exercise, or lapse of a power of appointment (other than a general power of appointment as defined in § 2041(b)) will not be treated as an addition to a trust if: (1) such power of appointment was created in an irrevocable trust that is not subject to chapter 13 under § 26.2601-1(b)(1); and (2) in the case of an exercise, the power of appointment is not exercised in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of the trust, extending beyond any life in being at the date of creation of the trust plus a period of 21 years plus, if necessary, a reasonable period of gestation (the perpetuities period). For purposes of § 26.2601-1(b)(1)(v)(B)(2), the exercise of a power of appointment that validly postpones or suspends the vesting, absolute ownership or power of alienation of an interest in property for a term of years that will not exceed 90 years (measured from the date of creation of the trust) will not be considered an exercise that postpones or suspends vesting, absolute ownership or the power of alienation beyond the perpetuities period. This section also provides that if a power is exercised by creating another power, it is deemed to be exercised to whatever extent the second power may be exercised.

This rule is illustrated in Example 4 of § 26.2601-1(b)(1)(v)(D). In that example, on March 1, 1985, T established an irrevocable trust (Trust 1) as defined in § 26.2601-1(b)(1)(ii). Under the terms of the trust instrument, the trustee is required to distribute the entire income annually to T's child, C, for life, then to T's grandchild, GS, for life. GC has the power to appoint any or all of the trust assets to Trust 2 which is an irrevocable trust (as defined in § 26.2601-1(b)(ii) that was established on August 1, 1985. The terms of Trust 2's governing instrument provide that the trustee shall pay income to T's great grandchild, GGC, for life. Upon GGC's death, the remainder is to be paid to GGC's issue. GGC was alive on March 1, 1985, when Trust 1 was created. C died on April 1, 1986. On July 1, 1987, GC exercised the power of appointment. The exercise of GC's power does not subject future transfers from Trust 2 to tax under chapter 13 because the exercise of the power in favor of Trust 2 does not suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date of creation of Trust 1, extending beyond the life of GGC (a beneficiary under Trust 2 who was in being at the date of creation of Trust 1) plus a period of 21 years. The result would be the same if Trust 2 had been created after the effective date of chapter 13.

In the present case, Daughter's testamentary powers of appointment were created under Trusts 1 and 2, both of which were irrevocable trusts not subject to chapter 13 under § 26.2601-1(b). Therefore, the first requirement of § 26.2601-1(b)(1)(v)(B) is satisfied. The second requirement of § 26.2601-1(b)(1)(v)(B) is also satisfied in this case. Under Article Tenth of Daughter's Will, if any trust has not terminated (i) prior to the 21st anniversary of the death of the last to die of the descendants of Daughter's great grandparents who were living on the earliest date that Trusts 1 and 2 became

irrevocable or (ii) prior to the 21st anniversary of the death of the last to die of such class of the descendants of Daughter's great grandparents who were living on the earliest date that Trusts 1 and 2 became irrevocable as shall be necessary so that the duration of such trust does not violate any applicable rule against perpetuities nor cause such trust to lose its exempt status for generation-skipping transfer purposes, such trust shall terminate on the day immediately preceding the earlier of the dates described in preceding clauses (i) or (ii) (the "termination date"). The period described is measured from the date of the creation of Trusts 1 and Trust 2. Further, the provisions in Daughter's Will use as measuring lives only lives in being at the date of the creation of Trusts 1 and 2.

In the present case, we conclude that the exercise by Daughter of her limited power of appointment over the property in Daughter's Trust 1 did not postpone or suspend the vesting, absolute ownership or power of alienation of any interest in the trust property for a period, measured from Date 2, the date Trust 1 became irrevocable, extending beyond any life in being at the date of creation of the original trust plus a period of 21 years. Further, we conclude that the exercise by Daughter of her limited power of appointment over the property in Daughter's Trust 2 did not postpone or suspend the vesting, absolute ownership or power of alienation of any interest in the trust property for a period, measured from Date 3, the date Trust 2 was created, extending beyond any life in being at the date of creation of the original trust plus a period of 21 years. Furthermore, for purposes of chapter 13, the trusts created by such exercises will not be required to terminate until the day immediately preceding the 21st anniversary of the death of the last to die of the class consisting of the descendants of Daughter's great grandparents who were living on the earliest date that Trusts 1 and 2 became irrevocable.

Accordingly, we conclude that the exercises of the limited powers by Daughter with respect to Daughter's Trusts 1 and 2 did not cause Daughter's Trusts 1 and 2 or Granddaughter's Appointive Trust to lose its GST exempt status for purposes of chapter 13.

Daughter's exercise of her limited powers of appointment over the property in Daughter's Trust 1 and Daughter's Trust 2 created another power of appointment in Granddaughter's Appointive Trust. Granddaughter was granted the power to appoint the property in her Appointive Trust to her issue or Settlor's issue. This power is a limited power of appointment. However, Granddaughter's power of appointment is not exercisable in favor of Granddaughter, Granddaughter's creditors, Granddaughter's estate, or the creditors of Granddaughter's estate. The termination provisions of Article Tenth of Daughter's Will apply to any Continuing Trust created pursuant to Granddaughter's power of appointment. Accordingly, any exercise of Granddaughter's power of appointment will not postpone or suspend the vesting, absolute ownership or power of alienation of any interest in the trust property for a period, measured from Date 2, the date Trust 1 became irrevocable, and Date 3, the date Trust 2 was created,

extending beyond any life in being at the date of creation of the original trust plus a period of 21 years. Furthermore, for purposes of chapter 13, the trusts created by such exercises will not be required to terminate until the day immediately preceding the 21st anniversary of the death of the last to die of the class consisting of the descendants of Daughter's great grandparents who were living on the earliest date that Trusts 1 and 2 became irrevocable.

Further, we conclude that any exercise of the limited power by Granddaughter with respect to Granddaughter's Appointive Trust will not cause Granddaughter's Appointive Trust, or any trusts, including any Continuing Trust, created by the exercise of the power, to lose its GST exempt status for purposes of chapter 13.

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 the 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 above, no opinion is expressed as to the federal tax consequences of the facts described above under the cited provisions or any other provisions of the Code or regulations.

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.

A copy of this letter should be attached to any gift, estate, or generation-skipping transfer tax returns that you may file relating to these matters.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

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

Enclosures

Copy for section 6110 purposes
Copy of this letter

cc: