

Internal Revenue Service

Department of the Treasury

Number: **200219034**
Release Date: 5/10/2002
Index Number: 2041.00-00

Washington, DC 20224

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CC:PSI:B09 / PLR-109942-01
Date:
February 12, 2002

Legend

- Daughter =
- Date 1 =
- Mother =

- Mother's Trust =
- Corporate Trustee 1 =

- Date 2 =
- Date 3 =
- Corporate Trustee 2 =

- Son =
- Daughter's Trust =
- State 1 =
- Date 4 =
- x =
- State 2 =
- Code Section =

Dear

This letter responds to your request, dated January 29, 2001, requesting rulings regarding the federal estate and generation-skipping transfer (GST) tax consequences of Daughter's proposed exercise of a power of appointment.

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The facts submitted and representations made are as follows. On Date 1, Mother created Mother's Trust, a revocable trust. Corporate Trustee 1 was the initial trustee. Mother's Trust was amended on Date 2. Mother's Trust became irrevocable upon her death on Date 3. Corporate Trustee 2 is currently the acting successor trustee.

Paragraph Second of Mother's Trust, as amended, provides that upon the death of Mother, the trustee is directed to divide the trust estate into two equal portions, one portion for Son and one portion for Daughter (Daughter's Trust).

Paragraph Third, subparagraph (a) of Mother's Trust, as amended, provides that the trustee of Daughter's Trust shall pay to or expend for the benefit of Daughter, during her life, so much of the annual net income from the trust and so much of the principal as the trustee, in its sole discretion, shall deem advisable for Daughter's most comfortable maintenance and support and the maintenance, support and education of her children. Subparagraph (b) provides Daughter with the power, at any time, exercisable by one or more instruments filed with the trustee during her lifetime, or by will, to appoint all or any part of the principal of her trust, in trust or otherwise, to or for the benefit of any person or persons or charitable organizations, or any of them, except, herself, her estate, her creditors or the creditors of her estate, in such proportions and amounts as she shall, in her sole judgment, determine.

Paragraph Twelfth of Mother's Trust, as amended, provides that the trust agreement shall be governed and construed in accordance with the laws of State 1.

The executor for Mother's estate filed a Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return ("Mother's Estate Tax Return") on or about Date 4. Daughter's Trust was listed on line 9 of Schedule R and \$x of Mother's GST exemption was allocated to Daughter's Trust. The taxpayers represent that no additions, actual or constructive, have been made to Mother's Trust or Daughter's Trust since Date 3.

Daughter now proposes to execute a codicil to her will that exercises her power of appointment over the assets in Daughter's Trust.

Under the terms of the proposed codicil, Article IX will be added to Daughter's will. Pursuant to Article IX, Daughter exercises the power of appointment granted her under Mother's Trust by directing that the entire remaining principal and accumulated income in Daughter's Trust be retained in further trust by the trustees of Daughter's Trust under the dispositive provisions of new Paragraph Thirteenth.

Paragraph Thirteenth, section A, subsection (1), provides that all of the appointed property will be divided into one equal share for each of Daughter's then living children and one equal share for the issue, collectively, of each of Daughter's then deceased children. The share of a child who predeceases Daughter without surviving issue will be distributed equally among the shares for Daughter's other children. Each share will be administered as a separate trust pursuant to subsection (2) of Section A.

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Under Section A, subsection (2), until the time for termination of each separate trust, the trustees will distribute, no less frequently than annually, 80 percent of the income of each trust to the child for whom the trust was established, or per stirpes to the issue of a then deceased child, unless otherwise appointed under subsection (3) by the deceased child. Any income not distributed shall be accumulated and added to principal. In addition, the trustees will distribute principal from each separate trust for the “proper health, education, maintenance, and support” of the child for whom the trust was established or, unless otherwise appointed by that child pursuant to subsection (3), for the proper health, education, maintenance, and support of the issue of that child.

Under Section A, subsection (3), each beneficiary for whom a trust is established under Section A, subsection (1) has a special power to appoint, by will or by a written directive during the beneficiary’s life, any part of the beneficiary’s trust. However, the power holder may not appoint to the power holder, creditors of the power holder, the estate of the power holder, or creditors of the estate of the power holder. The power to appoint includes the power to create trusts and to grant other powers, except that no power shall be exercised, nor shall a power be extended over any property over which a power has previously been exercised, that shall cause or permit the vesting of any property or interest in property, or termination of any trust, to be postponed for a period beyond the perpetuities period applicable to the grantor of the first power exercised. Each of the issue of a child of Daughter has a power to appoint only a per stirpes share of the trust in which the individual has an interest.

Pursuant to Section A, subsection (4), all trusts established under Paragraph Thirteenth, as amended, must terminate on the day before twenty-one (21) years after the death of the last survivor of the issue of Mother who were living at the death of Mother. Upon termination, the entire principal and income of each trust will be distributed per stirpes to the then living issue of the child of Daughter for whom the trust was, or was intended to be, established. If a child of Daughter dies without issue, the child’s share will be proportionately divided among the other then existing shares. If none of Daughter’s issue, who would otherwise be beneficiaries, exist at any time or the term expires without any such issue surviving Daughter, the trust will be disposed of under the rules of intestacy of State 2 to the heirs of Daughter as if Daughter had died intestate and a resident of State 2.

Under Section B, except upon termination as a result of the expiration of the perpetuities period set forth in subsection (4) of Section A above, the trustees may refrain from making any distribution of principal or income to any beneficiary, whenever unusual circumstances exist which, in the trustee’s discretion, cause it to be in such beneficiary’s best interests to withhold such distribution.

You have requested the following rulings: (1) The power of appointment provided to Daughter in Mother’s Trust is not a general power of appointment. (2) The proposed exercise of the power of appointment will not result in the inclusion of any property subject to the power in Daughter’s gross estate for federal estate tax purposes under § 2041(a)(2). (3) The proposed exercise of the power of appointment, which creates other powers of appointment, does not postpone or suspend the vesting, absolute

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ownership or power of alienation of any interest in any property subject to the first power for a period, measured from the date of creation of Mother's Trust, extending beyond any life in being at the date of creation of the Mother's Trust plus a period of twenty-one years. (4) The proposed exercise of the power of appointment does not cause the inclusion of any property subject to the power in Daughter's gross estate for federal estate tax purposes under § 2041(a)(3). (5) Daughter's power of appointment was created in an irrevocable GST exempt trust. (6) The proposed exercise of the power of appointment will not result in a constructive addition to Mother's Trust that will be subject to the GST.

Rulings 1 and 2

Section 2031(a) provides that, the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated.

Section 2041(a)(2) provides that the value of the gross estate includes the value of all property to the extent of any property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition that is of such nature that if it were a transfer of property owned by the decedent, the property would be includible in the decedent's gross estate under §§ 2035 to 2038, inclusive.

Section 2041(b)(1) provides that the term "general power of appointment" means a power that is exercisable in favor of the individual possessing the power, his estate, his creditors, or the creditors of his estate. Under § 2041(b)(1)(A), 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.

Sections 20.2041-1(c)(1)(a) and (b) of the Estate Tax Regulations provide that a power of appointment is not a general power if by its terms it is 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 it is 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 is not a general power if by its terms it is expressly not exercisable in favor of the holder, the holder's estate, the holder's creditors, or the creditors of the holder's estate. In this case, Daughter specifically may not appoint the assets of her generation-skipping trust to herself, her estate, her creditors or the creditors of her estate. Based on the facts submitted and the representations made, we conclude that the power of appointment provided to Daughter in Mother's Trust is not a general power of appointment. Accordingly, the proposed exercise of the power will not result in the inclusion of any property subject to the power in Daughter's gross estate for federal estate tax purposes under § 2041(a)(2).

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Rulings 3 and 4

Section 2041(a)(3) provides that the value of the gross estate shall include the value of all property to the extent of any property with respect to which the decedent by will exercises a power of appointment created after October 21, 1942, by creating another power of appointment which, under applicable local law, can be validly exercised so as to postpone the vesting of any estate or interest in such property, or suspend the absolute ownership or power of alienation of such property, for a period ascertainable without regard to the date of the creation of the first power.

State 1 Code Section provides that a nonvested property interest is invalid unless: (1) when the interest is created, it is certain to vest or terminate no later than twenty-one years after the death of an individual then alive; or (2) the interest either vests or terminates within ninety years after its creation. State 1 Code Section also provides that a nongeneral power of appointment or a general testamentary power of appointment is invalid unless: (1) when the power is created, it is certain to be irrevocably exercised or otherwise to terminate no later than twenty-one years after the death of an individual then alive; or (2) the power is irrevocably exercised or otherwise terminates within ninety years after its creation.

Under the proposed codicil to Daughter's will, Daughter will exercise her power of appointment over Daughter's Trust by directing that the assets of Daughter's Trust continue to be held by the trustees of Daughter's Trust under the dispositive provisions contained in the codicil. Under these provisions, each trust administered under the terms of the proposed codicil, or established by an exercise of a power of appointment under the proposed codicil and attributable to trusts established under Mother's will, must terminate no later than the day preceding the end of twenty-one years after the death of the last survivor of Mother's issue living on Mother's date of death.

Thus, under the proposed codicil, Daughter's power of appointment will not be exercised in a manner that may postpone or suspend vesting of the trust corpus for a period measured from the date of creation of Mother's Trust extending beyond any life in being plus twenty-one years. Further, the proposed testamentary exercise of Daughter's limited power of appointment under the proposed codicil will not create another power which, under State 1 law, would be deemed invalid. Accordingly, the proposed exercise of the limited power of appointment, as provided for in the proposed codicil to Daughter's will, will not cause the inclusion of any property subject to the power in Daughter's gross estate for federal estate tax purposes under § 2041(a)(3).

Rulings 5 and 6

Section 2601 imposes a tax on every generation-skipping transfer made by a transferor to a skip person.

Section 2611(a) defines the term "generation-skipping transfer" to include a taxable distribution, a taxable termination, and a direct skip.

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

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

Section 2631(a) provides that, for purposes of determining the inclusion ratio, every individual shall be allowed a GST exemption of \$1,000,000 (adjusted for inflation under § 2631(c)) which may be allocated by such individual (or his executor) to any property with respect to which such individual is the transferor. Section 2631(b) provides that any allocation under § 2631(a), once made, shall be irrevocable.

Section 2652(a) provides that, with exceptions not relevant here, the term “transferor” means (A) in the case of any property subject to the tax imposed by chapter 11, the decedent, and (B) in the case of any property subject to the tax imposed by chapter 12, the donor. An individual shall be treated as transferring any property with respect to which such individual is the transferor.

Section 26.2652-1(a)(1) provides, in part, that, except as otherwise provided in paragraph (a)(3) relating to certain qualified terminable interest property trusts, the individual with respect to whom property was most recently subject to federal estate or gift tax is the transferor of that property for purposes of chapter 13. An individual is treated as transferring any property with respect to which the individual is the transferor. Thus, an individual may be a transferor even though there is no transfer of property under local law at the time the federal estate or gift tax applies.

Based on the information submitted and the representations made, we conclude that Mother’s Trust is a generation-skipping trust because it provides for distributions to natural persons assigned to a generation that is two or more generations below the generation assignment of the transferor. At Mother’s death, \$x of Mother’s GST exemption was allocated to Daughter’s Trust, resulting in an inclusion ratio of zero for Daughter’s Trust. You have represented that no subsequent additions, actual or constructive, have been made to Daughter’s Trust. We conclude, accordingly, that Daughter’s limited power of appointment was created in an irrevocable GST exempt trust.

The exercise by Daughter of a limited power of appointment by will in a manner that does not postpone the vesting of any estate or interest in such property, or suspend the absolute ownership or power of alienation of such property, for a period ascertainable without regard to the date of the creation of the first power will not create a new transferor under § 2652(a)(1) because no tax will be imposed under chapters 11 or 12. Therefore, we conclude that the proposed exercise of the limited power of

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appointment does not result in a constructive addition to Mother's Trust or Daughter's Trust that will be subject to the GST tax.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal 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 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.

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

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,
Melissa C. Liquerman
Branch Chief
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures

Copy of this letter for § 6110 purposes