Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:B09-PLR-143662-01
Date:
April 22, 2002

LEGEND:

Decedent

Spouse

Family Trust

Will

Estate

Child 1

Child 2

Probate Court

Date 1

Date 2

Date 3

Date 4

Date 5

Date 6

Executor

Accountant

$a

$b

$c

Dear :

This letter responds to your request, dated August 7, 2001, requesting rulings under § 301.9100-1 of the Procedure and Administration Regulations.

Family Trust was created on Date 1, and amended on Date 2. Decedent died on Date 3, survived by Spouse, Child 1, and Child 2. Decedent's Will was admitted to probate, and Executor was appointed to serve as independent executor for Decedent's estate on Date 4, by the local probate court (Probate Court).

Decedent's Will contains specific bequests to a grandchild totaling $a that result in direct skips occurring at Decedent's death. Under Article IV of the Will, the residue of Decedent's estate is to be added to the principal of Family Trust.

Article II of Family Trust provides that the primary beneficiaries are Decedent and Spouse (Settlors). After the death of the surviving spouse and pursuant to the terms of Article VIII, the trust may continue for the benefit of Child 1 and Child 2, or if any of them should predecease the surviving spouse, for the descendants of that deceased child.

Article III of Family Trust provides that Family Trust shall be revocable during Settlors' joint lives. During this time, they shall have the power and right to amend, modify or revoke, in whole or in part, Family Trust or any terms or provisions thereof. After the death of the first Settlor to die, Family Trust shall be irrevocable and not subject to amendment or change by the surviving Settlor or any person.

Article IV of Family Trust provides that so long as both Settlors shall live, there shall be distributed to or for the benefit of Settlors so much of the trust income and corpus as they shall from time to time direct in writing. Initially and until further written notice from Settlors to the trustee, the trustee shall distribute to Settlors the net trust income.

Article V, Subsection A, of Family Trust provides that upon the death of the first Settlor to die, the trust estate shall be divided into three parts: Part A, Part M, and Part B. Part M and Part B are the subtrusts relevant to this ruling request.

Article V, Subsection B, of Family Trust provides that to Part A shall be allocated the following: (1) any separate property of the surviving Settlor transferred to the trust by the surviving Settlor during the joint lives of Settlors or thereafter and any of the surviving Settlor's interest in the community property of Settlors; (2) those proceeds of any life insurance and employee benefit plans payable by reason of the death of the first Settlor to die that designate the trustee as beneficiary (unless the applicable beneficiary designation provides otherwise) that are the separate property of the surviving Settlor and those proceeds that represent the surviving Settlor's community one-half interest in such proceeds; and (3) any properties that are made payable or

transferred to Trust A by the first Settlor to die or by others by specific reference thereto in a will or other written instrument.

Article V, Subsection C, provides that to Part M shall be allocated the following:(1) property, including the separate and community one-half interest of the first Settlor to die in the proceeds of any life insurance and employee benefit plans includible in the gross estate for federal estate tax purposes of the first Settlor to die that are payable to the trustee, equal in value to the smallest pecuniary amount which, if allowed as a federal estate tax marital deduction in the estate of the first Settlor to die, would result in the least combined federal estate tax and state death taxes (but only those state death taxes that are computed by reference to the credit allowable under § 2011 of the Internal Revenue Code) being payable by the death of the first Settlor to die, and (2) any properties that are made payable or transferred to Part M by the first Settlor to die.

Article V, Subsection D, provides that to Part B shall be allocated the following: (1) all other property comprising the trust estate; (2) any other properties which are made payable or transferred to Part B by the first Settlor to die or by others by specific reference thereto in a will or other written instrument, and (3) property with respect to which the surviving Settlor has made a qualified disclaimer.

Article VII provides terms that will apply to Part M. Subsection A, provides that trustees are authorized, but not directed, to divide Part M, at any time, into two separate trusts, each trust having the identical provisions as Part M, so that the federal generation-skipping transfer tax inclusion ratio as defined in § 2642(a) for each trust shall be either zero or one. The trust with an inclusion ratio of zero shall be referred to as Trust M1; the trust with an inclusion ratio of one shall be referred to as Trust M2. Any such direction shall be effective from the date of death of the first Settlor to die.

Article VII, Subsection B, provides that the trustee of Part M shall pay at convenient intervals, at least quarterly, as the same shall accrue, all of the net income to the surviving Settlor, so long as he or she lives.

Article VII, Subsection C, provides that if at any time during the existence of Part M (or Trusts M1 and M2) the net income which shall be distributed to the surviving Settlor shall not be adequate in the opinion of the trustee for his or her health, maintenance and support in accordance with his or her station in life, then the trustee may make supplemental distributions of corpus out of Part M to the surviving Settlor to the extent and in the manner that the trustee may deem advisable. Distribution of the entire principal of Part M is authorized if the trustee shall determine such distribution to be in the best interest of the surviving Settlor in accordance with the foregoing standard. If Part M has been divided into two separate trusts, principal distributions to the surviving Settlor shall first be made from Trust M2.

Article VII, Subsection D, provides that upon the death of the surviving Settlor, Part M shall terminate and all of the assets and properties comprising the corpus of

Part M shall be distributed and paid over as a part of Part B. If Part B is not then in existence, the assets and property shall be held by trustees for the uses and purposes and in accordance with the terms set forth in Article VIII. Notwithstanding any other provision of this instrument, all income of Part M accrued or undistributed at the death of the surviving Settlor shall be paid to his or her estate.

Article VII, Subsection F, provides that if the executor of the estate of the first Settlor to die makes the election set forth in § 2056(b)(7) to treat all or any part of the property passing to Part M as qualified terminable interest property in the estate of the first spouse to die, then in determining the income payable to the surviving Settlor under the terms of paragraph B, and in determining the manner of which expenses are to be borne and the manner in which receipts are to be credited as between corpus and income, and in determining what shall constitute income or corpus, the trustee shall make such determinations, distributions, and allocations in a manner that complies with the provisions of § 2056.

Article VIII provides the terms that will apply to Part B. Article VIII, Subsection C, provides that upon the death of surviving Settlor, the trustee shall divide the trust property into separate funds of equal value, creating one such fund for the benefit of each then living child of Settlors, Child 1 and Child 2, and one such fund for the surviving descendants, collectively, of each of Settlors' children who shall then be deceased with descendants surviving, with remainder at a child's death to the surviving descendants of that deceased child, per capita.

Article VIII, Subsection D, provides that when there is no longer a living child of a deceased child of Settlors whose name designates the particular share under the age of 21, the trust of that share shall terminate and be distributed to the descendants of such child whose name designates the particular share, per stirpes.

Article VIII, Subsection E, provides that if all of the Settlors' descendants should die prior to the time of the termination of a trust or share, then upon the last to die among the Settlors and the Settlors' descendants the then remaining corpus and undistributed income of the trust or share shall be distributed outright and free of trust one-half to the heirs of one Settlor, and one-half to the heirs of the other Settlor.

Article IX, Subsection L, provides that notwithstanding any other provisions of Family Trust, any trust created, if it has not previously terminated, shall terminate twenty-one years after the death of the last to survive of the Settlors and all the lineal descendants of the Settlors living when Family Trust was created.

Executor filed a Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, on Date 5. An estate tax closing letter was issued on Date 6. On the original Form 706, Schedule M included as a bequest to the surviving spouse all property in Trust M, other than the applicable exclusion amount resulting from the applicable credit amount provided by § 2010 ($625,000 for the year 1998).
No division of Trust M into the generation skipping transfer (GST) exempt trust (Trust

M1), and the GST non-exempt trust (Trust M2) was indicated on Schedule M. Schedule R was not filed with the estate tax return. Therefore, the Estate did not make a "reverse" QTIP election under § 2652(a)(3) with respect to the GST exempt trust or the GST non-exempt trust, and did not allocate any available generation-skipping transfer tax exemption.

Prior to the death of Decedent, Executor had never served as the executor for an estate, and had no previous experience with the preparation and filing of a Form 706. Executor hired Accountant, an experienced certified public accountant, to prepare the Form 706. Executor represents that he relied upon the professional advice of Accountant in regard to the preparation and filing of the Form 706, and that Accountant failed to make, or advise him to make, the "reverse" QTIP election. Executor further represents that he was unaware of the necessity of the election.

Concurrent with the request for this ruling, Executor filed a supplemental estate tax return. The supplemental return indicates that Trust M is to be divided into two separate trusts, one trust designated as the GST exempt trust, Trust M1, and the GST non-exempt trust, Trust M2. On the supplemental estate tax return, the executor made the reverse QTIP election for Trust M1.

Executor of Family Trust has requested the following rulings:

1. An extension of time under §§ 301.9100-1 and 301.9100-3 to make a reverse QTIP election under § 2652(a)(3) with respect to the GST exempt trust (Trust M1).
2. Because no allocation of GST exemption was made within the time prescribed by § 2632(a)(1), the Decedent's GST exemption is allocated under the automatic allocation rules contained in § 2632(c).

Section 2001(a) imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2056(a) provides that, for purposes of the tax imposed by § 2001, the value of the taxable estate is to be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse.

Section 2056(b)(1) provides the general rule that no deduction shall be allowed for an interest passing to the surviving spouse if, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, the interest will terminate or fail.

Section 2056(b)(7)(A) provides that, in the case of qualified terminable interest property, the entire property shall be treated as passing to the surviving spouse for purposes of § 2056(a), and no part of the property shall be treated as passing to any person other than the surviving spouse.

Section 2056(b)(7)(B)(i) defines “qualified terminable interest property” (QTIP) as property-- (1) which passes from the decedent, (2) in which the surviving spouse has a qualifying income interest for life, and (3) to which an election under § 2056(b)(7)(B)(v) applies.

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

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

Under § 2632(a), the allocation of the GST exemption may be made at any time on or before the date prescribed for filing the individual’s estate tax return (including extensions).

Section 2632(c)(1) provides that any portion of an individual’s GST exemption which has not been allocated within the time prescribed by § 2632(a) shall be deemed to be allocated as follows– (A) first, to property which is the subject of a direct skip occurring at the individual’s death, and (B) second, to trusts with respect to which such individual is the transferor and from which a taxable distribution or a taxable termination might occur at or after the individual’s death.

Section 26.2632-1(d)(2) of the Generation-Skipping Transfer Tax Regulations provides that a decedent’s unused GST exemption is automatically allocated on the due date for filing Form 706 to the extent not otherwise allocated by the decedent’s executor on or before that date. First, the exemption is allocated pro rata to direct skips on the basis of their value for estate tax purposes. The balance is then allocated pro rata, on the basis of estate tax values, to trusts with respect to which a taxable termination may occur or from which a taxable distribution may be made. No automatic allocation is made to a trust that will have a new transferor with respect to the entire trust prior to the occurrence of any GST with respect to the trust.

Section 2652(a)(3) provides that in the case of any trust with respect to which a deduction is allowed to the decedent’s estate under § 2056(b)(7), the estate of the decedent may elect to treat all of the property in the trust, for purposes of the GST tax, as if the election to be treated as qualified terminable interest property had not been made. This election is referred to as the “reverse” QTIP election. The consequence of a reverse QTIP election is that the decedent remains, for GST tax purposes, the transferor of the QTIP trust for which the election is made. As a result, the decedent’s GST exemption may be allocated to the QTIP trust.

Section 26.2652-2(a) provides that a reverse QTIP election is not effective unless it is made with respect to all of the property in the trust to which the QTIP applies. Section 26.2652-2(b) provides that the reverse QTIP election is to be made on

the return on which the QTIP election is made.

Under § 26.2654-1(b)(1), the severance of a trust that is included in the decedent's gross estate (or created under the transferor's will) into two or more trusts is recognized for GST purposes if the trust is severed pursuant to a direction in the governing instrument providing that the trust is to be divided upon the death of the transferor.

Under § 301.9100-1(c), the Commissioner may grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 to make a regulatory election, or a statutory election (but no more than 6 months except in the case of a taxpayer who is abroad), under all subtitles of the Code except subtitles E, G, H, and I.

Section 301.9100-2 provides an automatic extension of time for making certain elections.

Section 301.9100-3(a) provides that, in general, requests for extensions of time for regulatory elections that do not meet the requirements of § 301.9100-2 must be made under the rules of § 301.9100-3. Requests for relief subject to § 301.9100-3 will be granted when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(1)(v) provides that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

We conclude that the requirements of § 301.9100-3 have been satisfied. Therefore, an extension of time is granted until the date that the supplemental return was filed, for making a reverse QTIP election under § 2652(a)(3) with respect to Trust M1.

An extension of time to make the reverse QTIP election under § 2652 does not extend the time to make an allocation of any remaining GST exemption. In the instant case, no allocation of Decedent's available GST exemption was made on the Form 706 filed on Date 5. Therefore, the automatic allocation rules of § 2632(c) and § 26.2632-1(d)(2) operate to allocate Decedent's available exemption. Pursuant to these rules and in view of the grant of the extension of time to make the "reverse" QTIP election for the GST exempt trust (Trust M1), the Decedent's GST exemption will be allocated in the following manner: (a) $a of the GST tax exemption will be automatically allocated to the specific bequests that resulted in "direct skips" occurring at Decedent's death; and (b) $b of the GST tax exemption will be automatically allocated to Part B, and (c) $c will be automatically allocated to the GST exempt trust (Trust M1).

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.

Sincerely,
Paul F. Kugler
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures
Copy for section 6110 purposes
Copy of this letter