

Internal Revenue Service

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B09 – PLR-167804-03

Date:

June 02, 2004

In Re:

Legend

Decedent	=
Spouse	=
Trust	=
Marital Trust	=
Family Trust	=
Date 1	=
Date 2	=
A	=
B	=
C	=

Dear Sir:

This is in response to your letter dated October 24, 2003, and subsequent correspondence, requesting an extension of time under § 301.9100-3 of the Procedure and Administration Regulations to sever a trust into an exempt and nonexempt trust for purposes of the Generation-Skipping Transfer (GST) tax and to make a reverse qualified terminable interest property (QTIP) election under § 2652(a)(3) of the Internal Revenue Code with respect to the exempt trust.

The facts submitted and the representations made are summarized as follows. Decedent died on Date 1, survived by Spouse, children, and grandchildren.

Article III, Section A of Decedent's will provides that the residue of his estate is to be distributed to Trust. Article V, Section B of the will provides the executor with the power to make the reverse QTIP election under § 2652(a)(3). This section further sets forth Decedent's wish that the executor first allocate Decedent's GST

exemption to Family Trust with any excess GST exemption to be allocated to any QTIP trust to which executor has made the reverse QTIP election under § 2652(a)(3).

Section 3.02 of Trust provides that, upon Decedent's death, Trust is to be divided into two trusts, Marital Trust and Family Trust.

With respect to Marital Trust, Sections 3.04(1) and 8.10, provide that Marital Trust is to be funded with property eligible for the marital deduction equal to the excess of the federal estate tax marital deduction minus items included in Decedent's gross estate that have passed to Spouse outside of Trust, over the largest amount that will result in the least possible federal estate tax being payable by Decedent's estate after allowing for the unified credit against the federal estate tax and the credit for state death taxes.

Section 3.04(2) provides that Spouse is to receive all of Marital Trust's net income for her lifetime at least annually and principal to provide for her health, support, and maintenance.

Section 3.04(3) provides that the Marital Trust will terminate upon Spouse's death. Upon termination, Spouse's estate is to receive any undistributed net income from the trust and the trust's principal is to be contributed to Family Trust.

Section 3.04(4) provides that Marital Trust may be divided into a GST exempt and nonexempt marital trust so that a reverse QTIP election made by the executor of Decedent's estate with respect to the GST exempt marital trust will result in a trust having a zero inclusion ratio for GST tax purposes.

With respect to Family Trust, Section 3.05(1) provides that Family Trust is to be funded with trust assets not allocated to Marital Trust.

Section 3.05(2)(a) provides that Family Trust's trustee is to distribute \$A from Family Trust to each of Decedent's surviving children. Family Trust's remaining assets are to be held in further trust.

Section 3.05(2)(b) provides that the trustee may accumulate all or part of Family Trust's income or distribute the income and Family Trust's principal to Spouse, Decedent's children, and the descendants of Decedent's children to provide for their health, support, maintenance, and education.

Section 3.05(5) provides that, upon Spouse's death, the trustee is to divide the balance of Family Trust's corpus into separate equal shares so as to provide one share for each of Decedent's then living children, and one collective share for the living issue of a deceased child of Decedent. The collective share for a

deceased child's living issue is to be further divided into separate equal shares, one for each issue of the predeceased child (grandchild).

Section 3.05(6) provides that each child or issue of a predeceased child (grandchild) is to receive the corpus of his or her separate share free of trust in the following manner: one-third when the child or grandchild attains age 35, one-half when the child or grandchild attains age 45, and the remainder when the child or grandchild attains age 55. In addition, the trustee may distribute each share's property to the child or grandchild at any time.

Section 3.05(7) provides that each child or grandchild is to receive all of his or her share's net income at least annually and distributions of principal to provide for his or her health care, support, education, and maintenance. In addition, the trustee may distribute the share's principal to the child or grandchild for any reason and at any time the trustee deems proper.

Section 3.05(8) provides that in the event a child or grandchild dies before the complete distribution of his or her share, the share is to be distributed first to the child or grandchild's then living issue, in equal shares, if any; if none, then to the child or grandchild's siblings, in equal shares, if any; if none, to the child or grandchild's estate.

Decedent's estate retained an attorney to prepare the estate's federal estate tax return. The return was timely filed. No allocation of Decedent's GST exemption was made on the return. The QTIP election was made on the return for the property contributed to Marital Trust. Marital Trust, however, was not divided into a GST exempt and nonexempt marital trust and the reverse QTIP election under § 2652(a)(3) was not made. The return reflected that Family Trust had been funded with \$B. All of Decedent's GST exemption was available for allocation at his death.

Decedent's estate is requesting an extension of time pursuant to § 301.9100-1, to sever Marital Trust into a GST exempt and nonexempt marital trust, pursuant to § 26.2654-1(b)(1) of the Generation-Skipping Transfer Tax Regulations, and to make the reverse QTIP election under § 2652(a)(3) with respect to the GST exempt marital trust.

LAW and ANALYSIS

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 and (A) an interest in such property passes or has passed (for less than adequate and full consideration in money or money's worth) from the decedent to any person other than the surviving spouse (or the estate of such spouse), and (B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse.

Section 2056(b)(5) provides that, in the case of an interest in property passing from the decedent, if the surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse – (A) the interest or such portion thereof so passing shall, for purposes of § 2056(a), be considered as passing to the surviving spouse, and (B) no part of the interest so passing shall, for purposes of § 2056(b)(1)(A), be considered as passing to any person other than the surviving spouse. This paragraph shall apply only if such power in the surviving spouse to appoint the entire interest, or such specific portion thereof, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

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 for purposes of § 2056(b)(1).

Section 2056(b)(7)(B)(i) defines “qualified terminable interest property” 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 2056(b)(7)(B)(ii) provides, in part, that the surviving spouse has a qualifying income interest for life if-- (I) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, or has a usufruct interest for life in the property, and (II) no person has a power to appoint any part of the property to any person other than the surviving spouse.

Section 2056(b)(7)(B)(v) provides that an election under § 2056(b)(7) with respect to any property shall be made by the executor on the return of tax imposed by § 2001. The election, once made, is irrevocable.

Under § 2044(a), any property in which the decedent possessed a qualifying income interest for life and for which a deduction was allowed under § 2056(b)(7) is includable in the decedent's gross estate.

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

Section 2602 provides that the amount of tax is the taxable amount multiplied by the applicable rate. Section 2641(a) defines "applicable rate" as the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer.

Section 2642(a) provides the method for determining the inclusion ratio.

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 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(e)(1) provides that, in general, 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 the 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) provides that a decedent's unused GST exemption is automatically allocated on the due date for filing the federal estate tax return to the extent not otherwise allocated by the decedent's executor on or before that date. The regulation also supplies the method for the automatic allocation of any unused GST exemption. First, the exemption is allocated pro rata to direct skips on the basis of their values 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. The automatic allocation is irrevocable.

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 QTIP 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(b) provides that the reverse QTIP election is to be made on the return on which the QTIP election is made.

Section 26.2654-1(a)(2)(i) provides, in part, that if there is more than one transferor with respect to a trust, the portions of the trust attributable to the different transferors are treated as separate trusts for purposes of chapter 13.

Section 26.2654-1(b)(1) provides that the severance of a trust that is included in the transferor's gross estate (or created under the transferor's will) into two or more trusts is recognized for purposes of chapter 13 if—(i) 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; or (ii) the governing instrument does not require or otherwise direct severance but the trust is severed pursuant to discretionary authority granted either under the governing instrument or under local law; and

(A) The terms of the new trusts provide in the aggregate for the same succession of interests and beneficiaries as are provided in the original trust;

(B) The severance occurs (or a reformation proceeding, if required, is commenced) prior to the date prescribed for filing the federal estate tax return (including extensions actually granted) for the estate of the transferor; and

(C) Either-- (1) The new trusts are severed on a fractional basis. If severed on a fractional basis, the separate trusts need not be funded with a pro rata portion of each asset held by the undivided trust. The trusts may be funded on a non pro rata basis provided funding is based on either the fair market value of the assets on the date of funding or in a manner that fairly reflects the net appreciation or depreciation in the value of the assets measured from the valuation date to the date of funding; or (2) If the severance is required (by the terms of the governing instrument) to be made on the basis of a pecuniary amount, the pecuniary payment is satisfied in a manner that would meet the requirements of paragraph (a)(1)(ii) of this section if it were paid to an individual.

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.

Sections 301.9100-1 through 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make a regulatory election.

Section 301.9100-2 provides for automatic extensions 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.

In this case, all of Decedent's GST exemption was available for allocation at his death. Though no allocation of Decedent's GST exemption was made on the estate tax return, pursuant to §§ 2632(e) and 26.2632-1(d)(2), \$B of Decedent's GST exemption was automatically allocated to Family Trust, leaving \$C of Decedent's GST exemption unused.

Because a QTIP election was made on Decedent's Form 706, Marital Trust is includible in Spouse's gross estate under § 2044 and Spouse is considered the transferor of Marital Trust for GST tax purposes. Therefore, Decedent's remaining GST exemption may not be allocated to Marital Trust. However, if Marital Trust is severed into a GST exempt and nonexempt marital trust, and a reverse QTIP election under § 2652(a)(3) is made for the GST exempt marital trust, Decedent will be treated as the transferor of the GST exempt marital trust, and the automatic allocation rules of § 2632(e) will apply Decedent's remaining GST exemption to the property in that trust.

Based on the information submitted and the representations made, we conclude that the requirements of § 301.9100-3 have been satisfied. Therefore, an extension of time of 60 days from the date of this letter is granted to sever Marital Trust into a GST exempt and nonexempt marital trust and to file a supplemental estate tax return making the reverse QTIP election with respect to the GST exempt marital trust. Thereupon, the automatic allocation rules under § 2632(e) will apply Decedent's remaining GST tax exemption of \$C to the GST exempt marital trust. The supplemental return should reflect that the GST exempt marital trust is being funded with \$C.

The supplemental estate tax return should be filed with the Internal Revenue Service Center, Cincinnati, Ohio 45999. A copy of this letter should be attached to the return. A copy is enclosed for this purpose.

An extension of time to make the reverse QTIP election under § 2652(a)(3) does not extend the time to make an allocation of any remaining GST exemption. Once the reverse QTIP election is made §§ 2632(e) and 26.2632-1(d)(2) will operate to allocate Decedent's remaining GST exemption to the GST exempt marital trust.

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. Specifically, no opinion is expressed or implied as to the value of any item of Decedent's gross estate for federal estate tax purposes.

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.

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

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.

Sincerely,

Heather C. Maloy

Heather C. Maloy
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures: Copy for section 6110 purposes
Copy of this letter

cc: