Internal Revenue Service

Number: **200448043**
Release Date: 11/26/04
Index Number: 2652.01-02, 2654.00-00, 9100.22-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B09
PLR-169213-03
Date:
August 04, 2004

In Re:

Legend

Decedent =
Date 1 =
Spouse =
x =
Beneficiary 1 =
y =
Beneficiary 2 =
z =
Attorney =
State =
Statute =
Date 2 =

Dear :

This letter responds to your letter, dated July 26, 2004, and prior correspondence requesting extensions of time under §§ 2652(a)(3) and 2654 of the Internal Revenue Code and § 301.9100-1 of the Procedure and Administration Regulations to sever Trust into Trust A and Trust B and to make a reverse qualified terminable interest property (QTIP) election with respect to Trust B.

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

Article Seventh of Decedent's will provides that after certain specific bequests and the creation of a credit shelter trust, the residue of Decedent's estate shall be held in Trust for the benefit of Spouse during his life. Trust income is payable at least

annually to Spouse, and principal may be paid to or for the benefit of Spouse in the trustee's discretion. On Spouse's death, Trust, "as it shall then be constituted", will be distributed as follows: x percent to Beneficiary 1, y percent to Beneficiary 2, and z percent to Beneficiary 1's children in equal shares. If Beneficiary 2 is not married to and not living with Beneficiary 1 at the time of Spouse's death, then the y percent shall be added to the share of Beneficiary 1. If z percent exceeds the sum of one million dollars then such share shall be reduced to and limited to one million dollars and the difference shall be added to the share of Beneficiary 1.

Spouse, as executor, timely filed a Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return (estate tax return), on behalf of Decedent's estate. A marital deduction was taken on Schedule M with respect to Trust. Schedule R was not included in the estate tax return as filed. No reference to splitting Trust was made on Decedent's estate tax return.

Spouse relied on Attorney to prepare the estate tax return for Decedent's estate. Attorney inadvertently failed to advise Spouse about the available tax elections relating to QTIP trusts or of the possibility of splitting the QTIP trust into exempt and non-exempt shares for purposes of the generation-skipping transfer (GST) tax.

State Statute allows trustees to establish two or more separate trusts in order to segregate trust assets so that one or more of the separate trusts will have an inclusion ratio of zero for purposes of the GST tax without prior court approval or the consent of interested persons. Trusts established under this section shall be deemed to have been established as of the effective date of the disposing trust instrument.

Spouse died on Date 2. On Spouse's death, Beneficiary 2 was not married to and was not living with Beneficiary 1. The failure to split Trust and to make a reverse QTIP election was discovered during the administration of Spouse's estate.

The trustees of Trust have requested extensions of time to sever Trust into Trust A and Trust B and to make a reverse QTIP election with respect to Trust B.

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 for purposes of § 2056(b)(1)(A).

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 2601 imposes a tax on every generation-skipping transfer.

Section 2611(a) provides that the term "generation-skipping transfer" means: (1) a taxable distribution; (2) a taxable termination; and (3) a direct skip.

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)), that may be allocated by such individual (or by his executor) to any property with respect to which such individual is the transferor.

Section 2632(a)(1) provides that any allocation by an individual of his GST exemption under § 2631(a) may be made at any time on or before the date prescribed for filing the estate tax return for such individual's estate (determined with regard to extensions), regardless of whether such a return is required to be filed.

Section 2632(e)(1) (designated as § 2632(c)(1) at the time of Decedent's death) 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 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, in relevant part, that no automatic allocation of GST exemption 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 new trust.

Section 2652(a)(1) provides, in relevant part, that for purposes of chapter 13, 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 the individual is the transferor.

Section 2652(a)(3) provides that in the case of – (A) any trust with respect to which a deduction is allowed to the decedent under § 2056 by reason of subsection (b)(7) thereof, and (B) any trust with respect to which a deduction to the donor spouse is allowed under § 2523 by reason of subsection (f) thereof, the estate of the decedent or the donor spouse, as the case may be, may elect to treat all of the property in such trust for purposes of chapter 13 as if the election to be treated as qualified terminable interest property had not been made.

Section 26.2652-2(b) provides that a "reverse" QTIP election is made on the return on which the QTIP election is made.

Section 2654(b) provides that for purposes of the GST tax – (1) the portions of a trust attributable to transfers from different transferors shall be treated as separate trusts, and (2) substantially separate and independent shares of different beneficiaries in a trust shall be treated as separate trusts. Except as provided in the preceding sentence, nothing in chapter 13 is to be construed as authorizing a single trust to be treated as two or more trusts.

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 trust 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 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 § 26.2654-1(a)(ii) if it were paid to an individual.

Section 301.9100-1(c) provides that the Commissioner has discretion to 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 six months except in the case of a taxpayer who is abroad), under all subtitles of the Internal Revenue Code except subtitles E, G, H, and I.

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 under § 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 that granting 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 to advise the taxpayer to make, the election.

Based on the facts submitted and the representations made, the requirements of §§ 301.9100-1 and 301-9100-3 have been met. Therefore, an extension of time is granted until 60 days from the date of this letter to sever Trust and to make a "reverse" QTIP election under § 2652(a)(3) with respect to the assets of Trust B. The extensions of time granted in this letter do not extend the time to make an allocation of Decedent's remaining GST exemption. As a result of the severance of Trust and the "reverse" QTIP election with respect to the resulting Trust B, Decedent's remaining GST exemption will be allocated in accordance with the rules provided in § 2632(e)(1).

A supplemental Form 706 should be filed on behalf of Decedent's estate with the Internal Revenue Service Center, Cincinnati, Ohio 45999. The supplemental Form 706 should list Trust A and Trust B on Schedule M. In addition, the "reverse" QTIP election for Trust B should be made on Schedule R. A copy of this letter should be attached to the supplemental Form 706. A copy is enclosed for this purpose.

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 the taxpayer's representative.

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

Sincerely,

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

Enclosures
Copy of this letter
Copy of this letter for § 6110 purposes