

Internal Revenue Service
Index Nos.: 2652.01-02
9100.00-00

Number: **199921015**
Release Date: 5/28/1999

Department of the Treasury

**P.O. Box 7604
Ben Franklin Station
Washington, DC 20044**

Person to Contact:

Telephone Number:

Refer Reply To:

CC:DOM:P&SI:4/PLR-119713-98

Date: February 19, 1999

Re:

Legend:

Decedent	=
Spouse	=
Executor	=
Date 1	=
Date 2	=
Date 3	=
Living Trust	=
Trustors	=
Trustees	=
Trust B	=
Partnership X	=
Son	=
Daughter	=

This is in response to your submission of September 15, 1998, on behalf of Decedent's estate, in which you request an extension of time under § 301.9100-1 of the Procedure and Administration Regulations to make a "reverse" qualified terminable interest property (QTIP) election under § 2652(a)(3) of the Internal Revenue Code and to sever a trust under § 26.2654-1(b) of the Generation-Skipping Transfer Tax Regulations.

Decedent died testate on Date 1. Decedent was survived by Spouse and two adult children. Part Three, Section 3.02(A) of Decedent's will provides that the residue of Decedent's estate is to be given to the Trustees of the Living Trust, in trust, to be held, administered, and distributed in accordance with the terms thereof, as from time to time amended prior to Decedent's death.

Decedent and Spouse executed Living Trust on Date 2 and amended the trust document on Date 3. Living Trust was funded with the spouses' community property and separate property of the Decedent. Section 2.02 of Living Trust provides that while both Trustors are living, either or both of the Trustors shall have the right to direct the Trustees to distribute to or for the benefit of the Trustors so much of the income and principal of the trust estate as either or both the Trustors may direct.

Under Section 2.03, each of the Trustors retained the right, prior to the death of the first of the Trustors to die, to revoke the Living Trust, in whole or in part, with respect to the property contributed by such Trustor and the property having its source in the property contributed by such Trustor. Also, the Trustors acting together reserved the right to alter or amend the trust at any time.

Sections 3.01(A) and 3.01(B) provide each Trustor with a testamentary general power of appointment over that portion of the assets in the Living Trust consisting of the deceased Trustor's property.

Section 3.02(A) provides that, absent an exercise of the general power of appointment, upon the death of the first to die of the Trustors, the trust estate shall be divided into several trusts, including a Survivor's Trust, a Marital Trust, and Trust B.

Section 3.02(A)(4) provides that the Trustees shall allocate to Survivor's Trust (a) all of the Surviving Trustor's separate property and one-half of the Trustors' Quasi-Community property included in the trust estate; (b) cash or property in an amount equal to one-half the value of all community property of the Trustors included in the trust estate; (c) all other property of the trust estate which is appointed to Survivor's Trust pursuant to the exercise of the power of appointment by the deceased Trustor; and (d) if Decedent is the Trustor first to die, all interest in the Residence.

Under Section 3.02(B)(4)(a), the Surviving Trustor shall have the right to revoke Survivor's Trust, in whole or in part, at any time following the death of the Deceased Trustor and during the Surviving Trustor's lifetime, and in the event of such revocation, the property affected by such revocation shall be distributed, free of trust, to the Surviving Trustor.

Section 3.02(A)(5) provides for the creation of a Marital Trust.

Section 3.02(B)(6)(a) provides that during the Surviving Trustor's lifetime, the Trustees shall distribute the net income

of the Marital Trust in convenient installments (but not less often than annually) to the surviving Trustor. The Trustees shall also distribute such part of the principal of the Marital Trust to the Surviving Trustor as the Trustees deem necessary, in the Trustees' discretion, for the health, education, or support of the Surviving Trustor.

Section 3.02(B)(6)(b) provides that upon the death of the Surviving Trustor, the undistributed balance of principal of the Marital Trust shall be divided and allocated into as many equal shares as there are children of the Deceased Trustor then living and deceased children of the Deceased Trustor leaving issue then living.

Section 3.02(A)(1) provides that to the extent that the trust estate consists of an interest in Partnership X, such interest up to 25% of an aggregate of all the outstanding interests shall be allocated to Trust B.

Section 3.02(B)(1)(a) provides that upon the death of the Deceased Trustor and during the Surviving Trustor's lifetime, the Trustees shall distribute the net income of Trust B in convenient installments (but not less often than annually) to or for the benefit of the Surviving Trustor. Additionally, the Trustees shall pay to or apply for the benefit of the Surviving Trustor such part of the Trust property as the Trustees shall deem necessary, in the Trustees' discretion, for the support, comfort, care, and maintenance of the Surviving Trustor.

Section 3.02(B)(1)(b) provides that upon the death of the Surviving Trustor, the Trustees shall hold the balance of the trust property of Trust B for the benefit of Daughter. During Daughter's lifetime, the Trustees shall pay to Daughter all of the net income of Trust B in convenient installments (but not less often than annually). The Trustees shall also pay to or apply for the benefit of Daughter as much of the principal of Trust B as the Trustees shall deem necessary, in the Trustees' discretion, for Daughter's health, education, or support.

Section 3.02(B)(1)(c) provides that upon the death of the last to die of both Trustors and Daughter, Trust B shall be distributed to the issue of the Trustors, as then determined by right of representation, free of trust; provided, however, that if any property would otherwise be distributed to a person for whose benefit a trust or trusts is or are being administered under the Living Trust, that property shall instead be added to that trust (or equally in several trusts).

Section 4.11 provides that the Trustees shall have the power to divide any trust(s) created under the Living Trust into two or more separate trusts, of equal or unequal value, which trusts

shall be administered under all the same terms and conditions, in order that any exemption from generation-skipping tax under Chapter 13 of the Internal Revenue Code may be allocated to one such trust to the exclusion of the other(s) or disproportionately between or among them, and the power to effect or elect such allocation, provided that such trusts are treated as separate trusts under applicable state law, or otherwise qualify a portion of the trust property for such exemption.

It is represented that, upon the death of Decedent, Decedent's estate filed a timely Form 706, Federal Estate Tax Return. On Schedule M, the executor listed the total value of the assets which passed to the Spouse and which qualified for the marital deduction pursuant to § 2056(b)(7). The Schedule M did not evidence an intent to create two QTIP trusts (the Marital Trust and Trust B) nor was there any indication that either trust was to be severed into a GST-exempt QTIP trust and a GST-nonexempt trust. A Schedule R was not filed with the return. Thus, the estate did not make a "reverse" QTIP election under § 2652(a)(3) and did not manifest an affirmative intent to allocate any of Decedent's available GST exemption to a GST-exempt trust.

The representatives assisting the Executor of Decedent's estate were familiar with all relevant facts and were knowledgeable with respect to estate tax matters including the GST tax and the proper preparation of Form 706. Neither representative recommended to the Executor that a "reverse" QTIP election would be advantageous to the estate or that any available GST exemption should be allocated between an exempt and non-exempt QTIP Trust. The Executor was not provided with copies of the Schedule R in her review and approval of Decedent's federal estate tax return.

The Executor requests an extension of time under § 301.9100-1 to make an election pursuant to § 26.2654-1(b) to treat the Marital Trust as two separate trusts, a GST-exempt QTIP trust and a GST-nonexempt QTIP trust, and to make a reverse QTIP election under § 2652(a)(3) with respect to the GST-exempt QTIP trust.

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

Under § 2044, 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 (GST) made after October 22, 1986.

As applicable to the facts of this case, § 2631 provides for a generation-skipping transfer tax (GSTT) exemption of \$1,000,000, which may be allocated by the individual, or the individual's estate, to any property with respect to which such individual is the transferor.

Under § 2632(a), any allocation by an individual of his GST exemption 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(b) provides that, if any individual makes a direct skip during his lifetime, any unused portion of the individual's GST exemption shall be allocated to the property transferred to the extent necessary to make the inclusion ratio for the property zero. If the amount of the direct skip exceeds the unused portion, the entire unused portion shall be allocated to the property transferred. The unused portion of an individual's GST exemption is that portion of the exemption that

has not previously been allocated by the individual (or treated as allocated with respect to a direct skip).

Section 2632(c) provides that any portion of an individual's GST exemption that has not been allocated by the individual, or the individual's estate, will be automatically allocated, first, to property which is the subject of a direct skip occurring at the individual's death and, 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. This automatic allocation is made among the direct skips and trusts in proportion to the respective amounts (at the time of allocation) of the nonexempt portions of the properties and trusts.

Under § 26.2632-1(d)(2) of the Generation-Skipping Transfer Tax Regulations, 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 generation-skipping transfers with respect to the trust.

Section 2652(a)(1) provides that, for GST purposes, the "transferor" of property is the decedent in whose gross estate the property is included. Thus, in the case of property subject to a QTIP election that is subsequently includible in the surviving spouse's gross estate under § 2044, the surviving spouse would become the transferor of the property for GST purposes. However, § 2652(a)(3) provides that in the case of any trust with respect to which a deduction is allowed to the decedent 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 purposes, the transferor of the QTIP trust for which the election is made. As a result, the decedent's GSTT exemption may be allocated to the QTIP trust.

Section 26.2654-1(a)(2) provides 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)(ii) 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 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 each 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 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)(1)(ii) if it were paid to an individual. 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 nonpro 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.

Under § 301.9100-1(a) of the Procedure and Administration Regulations, the Commissioner of Internal Revenue may grant a reasonable extension of the time 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 Internal Revenue Code except subtitles E, G, H, and I, if the taxpayer demonstrates to the satisfaction of the Commissioner that the taxpayer has acted reasonably and in good faith, and granting the relief will not prejudice the interests of the government.

Section 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 an election. Section 301.9100-1(a).

Section 301.9100-2 provides automatic extensions of time for making certain elections. Section 301.9100-3 provides extensions of time for making elections that do not meet the requirements of § 301.9100-2.

Requests for relief under § 301.9100-3 will be granted when the taxpayer provides the evidence to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government. Section 301.9100-3(a).

It is represented that no distributions from the Marital Trust have been made to any person other than the Surviving Spouse.

Based on the facts submitted and representations made in this case, we conclude that the standards of §§ 301.9100-1 and 301.9100-3 have been satisfied. Consequently, an extension of time is granted until the date which is 30 days after the date of this letter for filing an amended Schedule M and making an election under § 26.2654-1(b) to sever the Marital Trust into two trusts, a GST-exempt QTIP trust and a GST-nonexempt QTIP trust, and for filing a Schedule R and making a "reverse" qualified terminable interest property election under § 2652(a)(3) with respect to the GST-exempt QTIP trust.

In general, the transferor with respect to any GST is the individual last subject to the gift or estate tax by reason of a transfer of property. Thus, the surviving spouse will become the transferor of the property in a QTIP trust when the value of the trust is included in that spouse's gross estate under § 2044. The consequence of a reverse QTIP election, however, is that the decedent who was the creator of the QTIP trust (the first spouse to die) is deemed to remain the transferor of the particular QTIP trust with respect to which the election is made. As a result of the reverse QTIP election for the GST-exempt QTIP trust, Decedent will be treated as the transferor of that trust for GST purposes.

We note that 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 since the time for making the allocation is expressly prescribed by the statute. In the instant case, it is represented that no allocation of Decedent's GST exemption was made during Decedent's life or at his death. Accordingly, the automatic allocation rules under § 2632(c) apply.

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.

A copy of this letter should be forwarded to the district office where Decedent's estate tax return was filed. A copy is included for that purpose.

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

Sincerely yours,

Paul F. Kugler
Assistant Chief Counsel
(Passthroughs and Special
Industries)

Enclosure
Copy of letter
Copy for section 6110 purposes