

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:DOM:P&SI:7:PLR-106678-98

Date:

March 31, 1999

Legend: Taxpayer: EIN:
Decedent:
Year 1:
Date 1:
Spouse:
Date 2:
\$Y:
\$Z:
Charity 1:
Charity 2:
Charity 3:
Charity 4:
Charity 5:
Charity 6:
Charity 7:
Year 2:
A%:
B%:
\$D:
\$E:
\$F:
Date 4:
\$G:
Date 5:
Date 6:
State Court:

Dear:

We received your letter dated , and later submissions requesting certain estate and generation-skipping

transfer (GST) tax rulings on behalf of Taxpayer concerning a qualified terminable interest property (QTIP) Trust. This letter responds to your request.

Taxpayer represents the facts to be as follows: Decedent died in Year 1 and Decedent's Will, dated on Date 1, was probated before the State Court. Under the terms of Decedent's Will, a QTIP Trust (Trust) was established for the benefit of Spouse. Spouse died on Date 2.

Article V(A) of Decedent's Will created the Marital Deduction Devise. Article V(A)(4) of Decedent's Will provides for the distribution of the Marital Deduction Devise.

Article V(A)(4)(a) of the Will provides that Decedent's personal representative will distribute the Marital Deduction Devise properties to the Trustee, in Trust. The personal representative will elect that any assets distributed to the Qualified Terminable Interest Property Trust will be treated as qualified terminable interest property for federal estate tax purposes and will qualify for the marital deduction.

Article V(A)(4)(a)(1) of the Will provides that during Spouse's lifetime, the Trustee will pay all the net income of the Trust in convenient installments (but not less frequently than annually) to or for the direct or indirect benefit of Spouse. Spouse may direct the Trustee to make productive or convert into productive property any nonproductive property contained in the Trust within a reasonable time.

Article V(A)(4)(a)(2) of the Will provides that during Spouse's lifetime, the Trustee may pay the principal of the Trust for the support, health, education, and comfort of Spouse.

Article V(A)(4)(a)(3) of the Will provides that upon Spouse's death, the Trustee will reimburse Spouse's estate for any gift, estate, transfer, legacy, or succession taxes payable by reason of the inclusion of the Trust in Spouse's estate for federal estate tax purposes and administer any remaining portion of the Trust according to the Residuary Devise established under the Will.

Article V(A)(4)(b) of the Will provides that, as an alternate disposition, if, upon the death of Spouse, a trust estate created under the Marital Deduction Devise is to be distributed to the Residuary Devise and the Residuary Devise has already been distributed to the beneficiaries of that Devise, the Trustee will distribute the remaining balance of any such trust estate in the manner and proportions set forth in the Residuary Devise.

Article V(C) of the Will provides for disposition of the Residuary Devise.

Article V(C)(1)(a) of the Will provides for a distribution of the lesser of \$Y or 30% of the amount by which the Decedent's gross estate exceeds \$Z equally among seven named charities, Charity 1, Charity 2, Charity 3, Charity 4, Charity 5, Charity 6, and Charity 7.

Article V(C)(1)(b) provides that if, at the time for distribution, one or more of the above-named charities has ceased to function and perform the services which it now conducts, either under its present organization or through a successor, the gift to that charity will lapse and the amount will be equally distributed among the remaining above-named charities.

Article V(C)(2) of the Will provides for distributions after the initial distribution to the named charities.

Article V(C)(4) provides that the final distributions from the QTIP Trust to the non-charitable beneficiaries may be made on a date not sooner than three years after the death of Spouse if Spouse survives Decedent, but, in any event, not later than five years after the date of death of Spouse.

The co-Trustees of the QTIP Trust represent that, in their opinion, Article V(C)(4) of Decedent's Will was ambiguous. The co-Trustees filed a Trust Construction Action requesting that the State Court construe the trust instrument created under Decedent's Will and determine when the interests vest in those non-charitable beneficiaries.

Taxpayer represents that a valid reverse QTIP election pursuant to section 2652 was made on Decedent's timely filed estate tax return for a portion of the QTIP Trust. This election subsequently was modified and perfected on a timely basis in Year 2 by filing with the Service a notice pursuant to the transitional rule in § 26.2652-2(c).

As a result of the transitional rule election, Taxpayer represents that the single QTIP Trust created under Decedent's Will was divided into two separate trusts for GST Tax purposes only: one trust that is exempt from the GST Tax (the "Exempt Share") with the Decedent as the deemed transferor and one trust that is non-exempt from the GST Tax (the "Non-exempt Share") with Spouse as the deemed transferor. The Exempt Share is comprised of A% of the Trust and has an inclusion ratio of zero. The Non-Exempt Share is comprised of B%, and has an inclusion ratio of one.

Taxpayer represents that on Decedent's Form 706, the gross estate was valued, for estate tax purposes, at \$D. Thirty percent of the amount by which \$D exceeds \$Z is \$E. The stated pecuniary amount of \$Y is less than \$E, so the total amount to be distributed among the charitable beneficiaries is \$Y. The pro rata portion of the charitable distribution allocated to the non-exempt trust is \$F.

Taxpayer represents that on Date 4, which was 6 months after Spouse's death, Charity 1, Charity 2, Charity 3, Charity 4, Charity 5, and Charity 6 each received distributions of cash in the amount of \$G, representing the respective one-seventh share of the bequests to the charities. In addition, each charity executed a Receipt, Release, and Indemnification. Taxpayer represents that \$G has been set aside for Charity 7, and the corporate assistant secretary executed the requisite release. The trustees, however, had not yet received the corporate documentation verifying the assistant corporate secretary's authority to sign the release. Taxpayer received the verification from Charity 7, and on Date 5, which was less than 12 months after Spouse's death, Charity 7 received a distribution in the amount of \$G.

On Date 6, State Court issued an Order construing the Trust instrument. In the Order, the State Court construed Decedent's Will as follows: the non-charitable beneficiaries are determined, and vest in ownership in their interests, subject to delays in distribution, by being "Living" as that word is defined in Decedent's Will/First Codicil, and such beneficiary is "living" if the beneficiary was alive at the death of Spouse.

Taxpayer requests that we rule as follows:

(1) When the QTIP Trust was divided into an exempt QTIP Trust and a non-exempt QTIP Trust, each with a separate deemed transferor for GST purposes only, pursuant to a timely filed election under § 26.2652-2(c), must the estate tax be allocated and paid, pro rata, from the exempt QTIP Trust and the non-exempt QTIP Trust if the § 2207A right of recovery is exercised for the QTIP Trust?

(2) Will the portion of the pecuniary charitable distributions required to be made from the non-exempt QTIP Trust at the death of Spouse qualify as a separate and independent share under § 2654 and § 26.2654-1(a)(ii)?

(3) For purposes of determining the allocation of Spouse's GST exemption, when do the non-charitable beneficiary interests as provided for in Article V of Decedent's Will vest in those beneficiaries?

LAW AND ANALYSIS

Ruling Request 1:

Section 2207A provides that if any part of the gross estate consists of property the value of which is includible in the gross estate by reason of section 2044 (relating to certain property for which marital deduction was previously allowed), the decedent's estate shall be entitled to recover from the person receiving the property the amount by which the total tax exceeds the total tax which would have been payable if the value of such property had not been included in the gross estate.

Section 20.2207A-1(b) provides that the amount of federal estate tax attributable to property includible in the gross estate under section 2044 is the amount by which the total federal estate tax (including penalties and interest attributable to the tax) under chapter 11 of the Internal Revenue Code that has been paid, exceeds the total federal estate tax (including penalties and interest attributable to the tax) under chapter 11 of the Internal Revenue Code that would have been paid if the value of the property includible in the gross estate by reason of section 2044 had not been so included.

Section 20.2207A-1(c) provides that an estate's right of recovery with respect to a particular property is an amount equal to the amount determined in section 20.2207A-1(b) multiplied by a fraction. The numerator of the fraction is the value for federal estate tax purposes of the particular property included in the gross estate by reason of section 2044, less any deduction allowed with respect to the property. The denominator of the fraction is the total value of all properties included in the gross estate by reason of section 2044, less any deductions allowed with respect to those properties.

Section 2601 imposes a tax on every generation-skipping transfer. With regard to the generation-skipping transfer (GST) tax, each individual is allowed an exemption of \$1,000,000 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.

Under section 2632(a), the allocation may be made at any time on or before the date prescribed for filing the individual's estate tax return (including extensions). Under section 2632(c), any portion of the individual's GST tax exemption not allocated within the time prescribed in section 2632(a), is allocated in accordance with that section.

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 section 2056(b)(7), the estate of the decedent may elect to treat all of the property in the trust, for purposes of the GST, 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 GST exemption may be allocated to the QTIP Trust.

Section 26.2652-2(c) provides the transitional rule that if a reverse QTIP election is made with respect to a trust prior to December 27, 1995, and GST exemption has been allocated to that trust, the transferor (or the transferor's executor) may elect to treat the trust as two separate trusts, one of which has a zero inclusion ratio by reason of the transferor's GST exemption previously allocated to the trust. The separate trust with the zero inclusion ratio consists of that fractional share of the value of the entire trust equal to the value of the nontax portion of the trust under section 26.2642-4(a). The reverse QTIP election is treated as applying only to the trust with the zero inclusion ratio.

Based on information submitted and representations made, we conclude that because the QTIP Trust was divided into an exempt QTIP Trust and a non-exempt QTIP Trust, each with a separate deemed transferor for GST purposes only, pursuant to a timely filed election under § 26.2652-2(c), without any direction in the Decedent's Will for allocation of the estate tax, if the § 2207A right of recovery is exercised for the QTIP Trust, the estate tax must be allocated and paid, pro rata from the exempt QTIP Trust and the non-exempt QTIP Trust.

Ruling Request 2:

Section 2654(b)(2) provides that, for purposes of chapter 13, substantially separate and independent shares of different beneficiaries in a trust shall be treated as separate trusts.

Section 26.2654-1(a)(1)(i) provides that if a single trust consists solely of substantially separate and independent shares of different beneficiaries, the share attributable to each beneficiary (or group of beneficiaries) is treated as a separate trust for purposes of chapter 13.

Section 26.2654-1(a)(1)(ii) provides that if a person holds the current right to receive a mandatory (i.e., nondiscretionary and noncontingent) payment of a pecuniary amount at the death of

the transferor from an inter vivos trust that is includible in the transferor's gross estate, or a testamentary trust, the pecuniary amount is a separate and independent share if --

(A) The Trustee is required to pay appropriate interest (as defined in 26.2642-2(b)(4)(i) and (ii)) to the person; and

(B) If the pecuniary amount is payable in kind on the basis of value other than the date of distribution value of the assets, the trustee is required to allocate the assets to the pecuniary payment in a manner that fairly reflects net appreciation or depreciation in the value of the assets in the fund available to pay the pecuniary amount measured from the valuation date to the date of payment.

Section 26.2642-2(b)(4)(i) provides that appropriate interest means that interest must be payable from the date of death of the transferor (or from the date specified under applicable State law requiring payment of interest) to the date of payment at a rate --

(A) At least equal to--

(1) The statutory rate of interest, if any, applicable to pecuniary bequests under the law of the State whose law governs the administration of the estate or trust; or

(2) If no such rate is indicated under applicable State law, 80 percent of the rate that is applicable under section 7520 at the death of the transferor; and

(B) Not in excess of the greater of --

(1) The statutory rate of interest, if any, applicable to pecuniary bequests under the law of the State whose law governs the administration of the trust; or

(2) 120 percent of the rate that is applicable under section 7520 at the death of the transferor.

Section 26.2642-2(b)(4)(ii) provides that for purposes of this paragraph, if a pecuniary payment does not carry appropriate interest, the pecuniary payment is considered to carry appropriate interest to the extent --

(A) The entire payment is made or property is irrevocably set aside to satisfy the entire pecuniary payment within 15 months of the transferor's death; or

(B) The governing instrument or applicable local law specifically requires the executor or trustee to allocate to the pecuniary payment a pro rata share of the income earned by the fund from which the pecuniary payment is to be made between the date of death of the transferor and the date of payment. For purposes of paragraph (b)(4)(ii)(A) of this section, property is irrevocably set aside if it is segregated and held in a separate account pending distribution.

Section 26.2654-1(a)(4)(i) provides that, with respect to a separate share treated as a separate trust under paragraph (a)(1) or (a)(2) of this section, an individual's GST tax exemption is allocated to the separate trust.

Under Article V of the Decedent's Will, after Spouse dies, the remaining balance in the QTIP Trust must be administered in accordance with the terms of the Residuary Devise. The Residuary Devise in Article V(C)(1)(A) provides that on the death of Spouse, distributions are made first to certain named charities. Under Article V(C)(1)(B) of Decedent's Will, if, at the time for distribution, a charity has ceased to function and perform the services it was conducting at the time the Will was executed, either under its present organization or through a successor, the gift to that charity will lapse, but the amount will be distributed equally among the remaining named charities.

Based on information submitted and representations made, we conclude that on the death of Spouse, the named charities held a current right to receive a mandatory distribution from the non-exempt Trust of which Spouse was the transferor. We also conclude that Taxpayer has complied with the requirements of § 26.2642-2(b)(4) by making payments to the named charities or irrevocably setting aside the payments within 15 months of the Transferor's (Spouse's) death. Accordingly, we conclude that the pecuniary charitable distributions required to be distributed from the non-exempt portion of the QTIP Trust qualify as a "separate and independent share" under § 26.2654-1(a)(i).

Ruling Request 3:

In order to resolve an ambiguity in the trust created under V(A) of Decedent's Will relating to the timing of distributions to non-charitable beneficiaries, a Trust Construction Action was filed in State Court. The State Court issued an Order Construing Trust Instrument on Date 5. The State Court ordered that the non-charitable beneficiaries under that Article of the Will are determined and vest in ownership in their interests, subject to delays in distribution, by being "Living" as that

word is defined in the Will, and such a beneficiary is "Living" if the beneficiary was alive at the death of Spouse.

Based on the State Court construction of the language in the trust created under Decedent's Will, the non-charitable beneficiaries are determined and vest in ownership in their interests, subject to delays in distribution, by being living as that word is defined in the Will. Such a beneficiary is living if the beneficiary was alive at the death of Spouse.

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

Sincerely,

Assistant Chief Counsel
(Passthroughs and Special Industries)

Christine Ellison
By: _____
Christine E. Ellison, Chief
Branch 7

Enclosures:
Copy for § 6110 purposes