

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
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Date:
February 4, 2000

Legend

- Trust 1 =
- Trust 2 =
- Trust 3 =
- Trustee =
- Decedent =
- Spouse =
- State =
- Date 1 =
- Date 2 =
- Date 3 =
- Date 4 =
- Date 5 =
- Date 6 =

Dear :

We received your letter dated December 13, 1999, submitted on behalf of Trust 2, of which you are Trustee. A ruling is sought concerning the validity of a reverse

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QTIP election under section 2652(b)(3)(A) of the Internal Revenue Code. In addition, a ruling is sought that, if a determination is made that the reverse QTIP election with respect to Trust 2 is valid, the automatic allocation of the generation-skipping transfer ("GST") tax exemption set forth in § 2632(c) applies so that Trust 2 will have an inclusion ratio of 0.00. This letter responds to those requests.

On Date 1, Decedent and Spouse created Trust 1. The last complete amendment and restatement ("Restatement") of Trust 1 was executed on Date 2. Following the Restatement, Decedent and Spouse amended Trust 1 three additional times. The third amendment ("Amendment"), dated Date 3, revoked the previous two amendments in their entirety. Decedent died on Date 4. Accordingly, upon Decedent's death, the terms of Trust 1 were governed by the Date 2 Restatement and the Date 3 Amendment.

In accordance with State law and Paragraphs B and C of Article III of the Restatement, all property in Trust 1 was community property of Decedent and Spouse at the time of Decedent's death. Article V, Paragraph A, Subparagraph 3 states that upon the satisfaction of all claims, expenses and taxes resulting from the Decedent's death, Trust 1 shall be divided into two separate trusts (one consisting of Decedent's community property share and one consisting of Spouse's community property share) pursuant to the provisions of Paragraph C of the same Article. Article V, Paragraph C, Subparagraph 1 provides for the creation of a trust that consists of Decedent's one-half interest in the community property in Trust 1. The subparagraph further directs the trustee to divide the property allocated into the new trust into two separate shares to be held in separate trusts as described in Subparagraphs 1(a) and 1(b) of Article V, Paragraph C. Subparagraph 1(a) of Article V, Paragraph C creates Trust 2, the subject of this private letter ruling. Under that subparagraph, Trust 2 is to be funded with an amount of property equal in value to the Decedent's remaining GST exemption. Subparagraph 1(b) of Article V, Paragraph C provides for a second trust to be funded with the portion of the one-half interest which was not allocated by Subparagraph 1(a). Because the value of Decedent's assets did not exceed his remaining GST exemption, the trust described in Subparagraph 1(b) of Article V, Paragraph C was not funded. Finally, Article V, Paragraph C, Subparagraph 2 provides for the creation of a trust that consists of Spouse's one-half interest in the community property in Trust 1 ("Trust 3"). Trust 3 will continue to be administered under the provisions in Article VIII during Spouse's lifetime.

Article VI provides for the administration and distribution of Trust 2. Paragraph A of Article VI directs the executor to make a QTIP election under § 2056(b)(7)(B)(v). In addition, Paragraph B of Article VI directs the executor to make a reverse QTIP election under §§ 2631 and 2652(a)(3).

The Decedent's estate tax return was due on Date 5. A timely filed estate tax return was not filed and no extensions were requested or granted. An estate tax return

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was filed on Date 6. The return constitutes the first return filed after the due date. Both a QTIP election and a reverse QTIP election were made on the return. You are requesting a ruling regarding the validity of the reverse QTIP election made on the return.

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 (QTIP), 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 20.2056(b)-7(b)(4) of the Estate Tax Regulations provides that the QTIP election is made on the last filed estate tax return on or before the due date of the return, including extensions, or, if a timely return is not filed, the first estate tax return filed after the due date.

It follows that the QTIP election made on the return is a timely QTIP election and valid insofar as it is timely.

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

Section 2631(a) provides that for purposes of determining the inclusion ratio, every individual shall be allowed a GST exemption of \$1,000,000 which may be allocated by such individual (or his executor) to any property with respect to which such individual is the transferor.

Section 2652(a)(3) provides that in the case of any trust with respect to which a

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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.

Based on the information submitted and the representations made, the reverse QTIP election made on the return is timely because it was made on the same return on which the timely QTIP election was made.

Under § 2632(a), an 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). Under § 2632(c), any portion of an individual GST exemption not allocated within the time prescribed in § 2632(a), is allocated automatically.

Section 26.2632-1(d)(2) of the Generation-Skipping Transfer Tax Regulations 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 the value of property as finally determined for purposes of Chapter 11. The balance is then allocated pro rata, on the basis of value, to trusts with respect to which a taxable termination may occur or from which a taxable distribution may be made. In the case of trusts that are not included in the gross estate, the GST exemption is allocated on the basis of the date of death value of the trust. 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.

Because the return was not timely filed, the Decedent's remaining GST exemption is allocated automatically in accordance with § 2632(c) of the Code and § 26.2632-1(d)(2) of the regulations. The exemption will be allocated pro rata to direct skips on the basis of the value of property. The balance will be allocated pro rata, on the basis of value, to trusts with respect to which a taxable termination may occur or from which a taxable distribution may be made.

Furthermore, because the reverse QTIP election is valid insofar as it is timely, Decedent remains the transferor of Trust 2 for purposes of the automatic allocation of the GST exemption. According to your representations, Decedent's GST exemption exceeds the value of transfers with GST potential, both his lifetime and testamentary transfers including Trust 2. Therefore, the inclusion ratio of Trust 2 is 0.00.

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Except as specifically ruled herein, we express or imply 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,

James C. Gibbons

James C. Gibbons
Assistant to the Chief, Branch 7
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosure

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