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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-108928-00

Date: June 26, 2000

Re:

Legend:

Decedent =
Date 1 =
Spouse =
Child 1 =
Child 2 =
Child 3 =
Child 4 =
Trust =

Property =

Dear :

This is in response to your submission of April 20, 2000, in which you requested a ruling under § 2652 of the Internal Revenue Code and § 301.9100-1 of the Procedure and Administration Regulations.

On Date 1, Decedent and Spouse executed a revocable trust agreement, establishing Trust, and contributed certain assets held as community property to Trust. Decedent died on Date 2, survived by Spouse, Child 1, Child 2, Child 3, and Child 4, and several grandchildren, including the children of Child 4. One of the assets transferred to Trust was Property, an asset held by Decedent and Spouse as community property.

Under the terms of the trust agreement, on the death of the first Trustor to die, that portion of Trust comprising the assets contributed by the deceased Trustor to Trust becomes irrevocable. The surviving Trustor retains the power to alter, amend, or revoke the portion of Trust comprised of the assets the survivor contributed to the Trust. The deceased Trustor's assets are divided into two shares, "Trust A," intended to qualify for the federal estate tax marital deduction, and "Trust B."

Trust A is to be funded with assets contributed by Decedent to the Trust, in the pecuniary amount necessary to reduce to zero the federal estate tax due on the return of the deceased spouse after taking into account all credits allowable on the return as well as property passing to the surviving spouse outside Trust. Trust B is to be funded with the balance of the Decedent's and Spouse's assets held in Trust.

Under the terms of Trust A and Trust B, the Spouse is to receive all of the net income at least quarterly, as well as any amount of principal the trustee deems necessary for the Spouse's health, education, support, or maintenance from both Trust A and Trust B; however, principal should be paid first from Trust A. Upon the death of the Spouse, the remainder of Trust A will be distributed to Trust B to be held and distributed as a part of that trust.

Under the terms of Trust B, upon the death of the Spouse, Property is to be retained in trust for the benefit of the children of Child 4. Regarding the remaining trust assets, specific real estate properties are to be distributed to Child 1, Child 2, and Child 3, as designated. Any remaining assets are to be distributed in equal shares to Child 1, Child 2, and Child 3. If any of Decedent's children die before becoming entitled to a distribution, the deceased child's share is to be held in trust for the benefit of the deceased child's children until the youngest attains age 25.

Article Thirteen provides:

If the Trust Estate is ever divided into separate shares or trusts, and to make any distribution called for by the Trust, Trustee may apportion and allocate the assets of the Trust Estate in cash or in kind, or partly in cash and partly in kind, or in undivided interests, in whatever manner Trustee in his sole and absolute discretion considers advisable. Trustee may sell whatever property he considers advisable to make any of those divisions or distributions.

On Schedule M of Form 706 (which was timely filed by the estate), the executor made an election under § 2056(b)(7) with respect to the entire value of Trust A. A deduction under § 2056(a) was claimed for the amount passing to Trust A.

The executor failed to indicate that Trust A would be severed, failed to make an election under § 2652(a)(3) with respect to Trust A, and failed to file a Schedule R and to allocate Decedent's GST exemption.

Trust A was funded with Decedent's one-half interest in Property contributed to Trust as well as with other assets.

The estate proposes to sever Trust A into two trusts, Trust A-1, an exempt trust for generation-skipping transfer tax (GSTT) purposes, and Trust A-2, a nonexempt trust for GSTT purposes. Trust A-1 will contain Decedent's one-half interest in Property. Trust A-2 will contain the balance of the assets in Trust A.

The terms of Trust A-1 and Trust A-2 will be identical to the provisions of Trust A. In this regard, any discretionary distribution of principal must be made pro rata from each trust. Upon Spouse's death, the remainder of Trust A-1 and of Trust A-2 will be disposed of, under the terms of Trust B. Thus, at Spouse's death, the remainder of Trust A-1 will be held in further trust for the children of Child 4; the remainder of Trust A-2 will be divided and distributed outright to Child 1, Child 2, and Child 3 (or if they predecease Spouse, held in trust for their respective children).

The estate also proposes to make a "reverse" QTIP election under § 2652(a)(3) with respect to Trust A-1.

Decedent's estate requests an extension of time under § 301.9100-1 to sever Trust A into Trust A-1 and Trust A-2 and to make the reverse QTIP election under § 2652(a)(3) with respect to Trust A-1. In addition, the estate requests a ruling that under the automatic allocation rules contained in § 2632(c)(1), a portion of Decedent's GST exemption under § 2631 is allocated to Trust A-1 in accordance with § 2632(c).

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 in a form described in § 2056(b)(1)(A).

Section 2056(b)(7)(B)(i) defines "qualified terminable interest property" (QTIP) 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. With regard to the generation-skipping transfer tax (GSTT), each individual is allowed an exemption of \$1,000,000 (adjusted as provided in § 2031(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.

Under § 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 § 2632(c) and § 26.2632-1(d)(2) of the Generation-Skipping Transfer Tax Regulations, any portion of an individual's GST exemption not allocated within the time prescribed in § 2632(a), is allocated pro rata on the basis of the value of the property as finally determined for federal estate tax purposes, first to direct skips treated as occurring at the transferor's death. Any balance is allocated pro rata, on the basis of the value of the property as finally determined for federal estate tax purposes, to trusts with respect to which a taxable termination may occur or from which a taxable distribution may be made. The automatic allocation is irrevocable. 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 generation-skipping transfer with respect to the trust.

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 GSTT, 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 GSTT 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 26.2654-1(b)(1) provides rules pursuant to which the severance of a trust that is included in the transferor's gross estate into two or more trusts is recognized for purposes of chapter 13. If the governing instrument does not require

severance, the trust must be severed pursuant to discretionary authority granted either under the governing instrument or under local law. The severance must occur (or a reformation proceeding be commenced) prior to the date prescribed for filing the federal estate tax return for the estate of the transferor. The trusts must either be severed on a fractional basis or a pecuniary basis (if so required by the governing instrument). 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.

Section 26.2654-1(b)(4), Example 1, considers a situation where, under the terms of a testamentary trust, income is to be paid to testator's spouse for life. On spouse's death, one-half of the corpus is to be paid to testator's child, C, or C's estate, and one-half of the corpus is to be paid to testator's grandchild, GC. The example concludes that, if the requirements of § 26.2654-1(b) are otherwise satisfied, the severance of the trust into two equal trusts, one providing income to spouse for life with remainder to C, and one providing income to spouse for life with remainder to GC, will be recognized for GST tax purposes.

Under § 301.9100-1(c), the Commissioner may grant a reasonable extension of 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 relief will not prejudice the interests of the government.

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 an election. § 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 establish that the taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government. § 301.9100-3(a).

In this case, based on the facts submitted and the representations made, we conclude that the standards of §§ 301.9100-1 and 301.9100-3 have been satisfied. Consequently, an extension of time is granted until 30 days from the date of this letter for (1) commencing the court proceeding to sever Trust A into Trust A-1 and Trust A-2 under § 26.2654-1(b)(1); and

(2) making a reverse QTIP election under § 2652(a)(3) with respect to Trust A-1.

The election under § 26.2654-1(b)(1) must be made by attaching a statement to copies of the federal estate tax return and the amended Schedule R filed by the estate. The statement must indicate that a proceeding has been commenced to sever Trust A and describe the manner in which the trust is proposed to be severed. A copy of the petition or other instrument used to commence the proceeding must also be attached.

We also rule that, as a result of the severance and reverse QTIP election, under the automatic allocation rules contained in § 2632(c)(1), a portion of Decedent's GST Exemption under § 2631 is automatically allocated to Trust A-1 in accordance with the rules contained in § 2632(c)(1).

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, we express no opinion regarding the valuation of the property included in the Decedent's gross estate.

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 yours,

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

Enclosure

Copy for section 6110 purposes