

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:B09 / PLR-103729-03
Date:
July 2, 2003

In Re:

LEGEND

- Decedent =
- Date 1 =
- Spouse =
- Daughter =
- Date 2 =
- \$x =
- Date 3 =

Dear :

This letter responds to your letter, dated January 7, 2003, and subsequent correspondence, requesting a generation-skipping transfer (GST) tax ruling under § 2632 of the Internal Revenue Code.

The facts and representations submitted are summarized as follows: Decedent died testate on Date 1, survived by Spouse and Daughter. Spouse died almost eighteen months later on Date 2.

After certain specific bequests, Article Nine of Decedent's will disposes of the residue of Decedent's estate. Article Nine, Paragraph A of Decedent's will provides that if Decedent's spouse survives her, the named trustees are to set aside in the "Family

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Trust” a pecuniary sum equal to the largest amount, if any, that can pass under the will free of federal estate tax in the federal estate tax proceeding relating to Decedent’s estate by reason of (i) the unified credit and (ii) the state death tax credit. Article Nine, Paragraph B of Decedent’s will provides that if Decedent’s spouse survives her, the balance of the assets in Decedent’s estate shall be qualified terminal interest property to be set aside and held in the “Marital Trust.”

Article Nine, Paragraph D of Decedent’s will contains the provisions of the Family Trust. Paragraph D, subparagraph 1(a) provides that until the death of Spouse, the trustees shall pay to Spouse or Daughter the amounts of the net income and/or principal of the Family Trust as the trustees may, in the trustees’ sole discretion, deem necessary or advisable for the health, education, support or maintenance of Spouse or Daughter, first considering the needs of Spouse.

Article Nine, Paragraph D, subparagraph 1(b)(i) of Decedent’s will provides that upon the death of Spouse, the trustee shall distribute to Daughter free of trust any interest held by the Family Trust in certain properties, with the balance to be distributed to the “GST Trust.” The trustee shall distribute all net income to Daughter for her lifetime, together with the amounts of principal as necessary for her maintenance, health, education, and support. Upon the death of Daughter, the balance of the trust principal shall be distributed in accordance with the provisions of Article Nine, Paragraph D, subparagraph 1(b)(iii).

Article Nine, Paragraph D, subparagraph 1(b)(iii) of Decedent’s will provides that upon the death of Daughter, the trustee shall divide any assets to be distributed under Article Nine, Paragraph D, subparagraph 1(b)(iii), into a sufficient number of separate and equal shares so that there shall be one share for each of Decedent’s grandchildren then living, and one share for the then living issue of any deceased grandchild of Decedent. Each share shall be held in trust for the grandchild, or living issue of a deceased grandchild, and income therefrom shall be paid to or applied for the benefit of the beneficiary or beneficiaries of the trust, together with the amounts of principal as are necessary for the health, education, support, and maintenance of the trust’s beneficiary or beneficiaries.

Article Nine, Paragraph D, subparagraph 1(e) of Decedent’s will provides that after the death of Daughter, each of Decedent’s grandchildren will have the right to withdraw portions of the principal of his or her trust as he or she reach ages thirty and thirty-five. When each of Decedent’s grandchildren reach age forty, he or she will have the right to withdraw all of the remaining principal of his or her trust.

Article Nine, Paragraph D, subparagraph 1(f) of Decedent’s will provides that if a separate share becomes payable to the living issue of any deceased grandchild, the share shall be paid outright to the living issue of the deceased grandchild, except for

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the portion of the share payable to an issue who is less than twenty-one years of age. In that case, the portion shall be held in trust until such issue reaches the age of twenty-one and will be distributed outright at that time.

In accordance with Decedent's will and the pecuniary formula therein, the Family Trust was funded with \$x. Aside from the specific bequests, the remainder of the assets in Decedent's estate had been owned by Decedent and Spouse as joint tenants and passed by right of survivorship to Spouse. Accordingly, the Marital Trust was never funded.

The executor of Decedent's estate filed the estate's United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706) on Date 3. Decedent's estate represents that Decedent's entire \$1,000,000 GST exemption was available for allocation at Decedent's death.

Decedent's estate requests that we rule that the automatic allocation rules of § 2632(e) operate to cause the unused portion of Decedent's GST exemption to be allocated to the Family Trust so the trust has an inclusion ratio of zero.

Section 2601 imposes a tax on every GST.

Section 2602 provides that the amount of tax is the taxable amount multiplied by the applicable rate. Section 2641(a) defines "applicable rate" as the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer.

Under § 2642(a)(1), the inclusion ratio with respect to any property transferred in a GST is, generally, the excess of 1 over the applicable fraction determined for the trust from which the transfer is made, or in the case of a direct skip, the applicable fraction determined for such skip. The applicable fraction, as defined in § 2642(a)(2), is a fraction, the numerator of which is the amount of the GST exemption allocated to the trust (or in the case of a direct skip, allocated to the property transferred in such skip), and the denominator of which is the value of the property transferred to the trust (or involved in the 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)) which may be allocated by the individual (or by his or her executor) to any property with respect to which the individual is the transferor. Section 2631(b) provides that once an allocation of GST exemption is made, it is irrevocable.

Under § 2632(a), the 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).

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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 that 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 a 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 that a decedent's unused GST exemption is automatically allocated on the due date for filing Form 706 to the extent not otherwise allocated by the decedent's executor on or before that date. The regulation also 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 their values for estate tax purposes. The balance is then allocated pro rata, on the basis of estate tax values, to trusts with respect to which a taxable termination may occur or from which a taxable distribution may be made. 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.

With regard to the specific bequests made in Decedent's will, no direct skips occurred in their distribution. With regard to the assets of the Family Trust, no GSTs will occur during the Daughter's lifetime, but one or more taxable terminations may occur upon the death of Daughter with respect to the assets to be distributed to the GST Trust.

Based on the information submitted and the representations made, we conclude that on the due date for filing Decedent's Form 706, Decedent's unused GST exemption is to be automatically allocated to the Family Trust. The amount of the GST exemption automatically allocated to the Family Trust will equal the value of the property transferred to the trust, resulting in an inclusion ratio of zero under § 2642.

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.

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.

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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.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer.

Sincerely,

James F. Hogan

James F. Hogan
Senior Technician Reviewer
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure

Copy for section 6110 purposes