



This is in response to a letter from your authorized representative dated February 27, 2004, and subsequent correspondence, requesting an extension of time under § 301.9100 of the Procedure and Administration Regulations to make an allocation of Decedent's generation-skipping transfer (GST) exemption, sever a trust, and make a "reverse" qualified terminable interest property ("QTIP") election under § 2652(a)(3).

The facts and representations submitted are summarized as follows: Decedent and Spouse (together referred to as Taxpayers) are residents of State A, a community property state. Taxpayers established an irrevocable trust, Trust A, under an agreement dated Date 1 in Year 1, for the benefit of their children and grandchildren. Child A and Child B are the trustees of Trust A. Taxpayers also established Trust B, a revocable trust, on Date 3. Trust B was amended and restated on Date 4.

Under Trust A's terms, upon the death of the first of Taxpayers to die, the Trust A corpus is to be divided into two equal shares, one to be held for the benefit of Child A and his issue and the other for the benefit of Child B and his issue. Pursuant to Article 3 of Trust A, all income for a child's share is to be paid annually to the child for whom it is held. If the Trustees consider the income insufficient, the Trustees may pay principal to the child as the Trustees deem necessary for the health, education, maintenance, and support of the child. Article 3 also grants each child a testamentary special power of appointment over the assets of the respective child's trust that may be exercised in favor of the child's issue, the heirs of either the Decedent or Spouse (other than the child holding the power), and charities of the child's choosing. If a child does not exercise his special power of appointment, then upon the child's death, the trust estate is to be distributed outright to the child's issue, per stirpes.

In Year 1, Decedent transferred cash and assets valued at Amount 1 to Trust A. For the Year 1 calendar year, Attorney 1 prepared and Decedent timely filed Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return, reporting Decedent's transfer to Trust A. On the Year 1 return, Amount 1 of Decedent's available GST exemption was allocated to Decedent's transfer to Trust A. In Year 2, Decedent transferred Amount 2 to Trust A. For the Year 2 calendar year, Attorney 1 prepared and Decedent timely filed Form 709. On the Year 2 return, Amount 2 of Decedent's available GST exemption was allocated to Trust A. Similarly, in Year 3, Decedent transferred Amount 3 to Trust A, and, for the Year 3 calendar year, Attorney 1 prepared and Decedent timely filed Form 709. On the Year 3 return, Amount 3 of Decedent's available GST exemption was allocated to Trust A.

In Year 4 and Year 5, Decedent again transferred Amount 3 to Trust A. However, for the Year 4 and Year 5 calendar years, both of which ended prior to January 1, 2001, Attorney 1 did not prepare, and Decedent did not file, a Form 709 because Attorney 1 mistakenly believed that § 2651(e) eliminated the possibility that Trust A would be subject to the GST tax. Decedent died on Date 2, in Year 5.

Article 3 of Trust B provides that, on Decedent's death, the portion of the Trust B corpus includible in Decedent's gross estate is to be divided into a Marital QTIP Trust and a Family Bypass Trust. Any GST tax exemption available to the Decedent's estate is to be allocated first to the assets of the Family Bypass Trust, with the balance to be allocated to the Marital QTIP Trust. Article 5 of Trust B provides that the Marital QTIP Trust is to be divided into two trusts for GST tax purposes (a Marital QTIP Exempt Trust and a Marital QTIP Non-Exempt Trust) if a portion of Decedent's GST exemption is allocated to the Marital QTIP Trust and the value of the Marital QTIP Trust exceeds that amount. Trust B also provides that the "reverse" QTIP election under § 2652(a) is to be made as to the Marital QTIP Exempt Trust.

Attorney 1 prepared Decedent's Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. Decedent's Form 706 was timely filed. On Schedule M, the executor made the election under § 2056(b)(7) to treat the property passing to the Marital QTIP Trust as qualified terminable interest property. However the Marital QTIP Trust was not divided, no "reverse" QTIP election was made, and no Schedule R was filed with the Form 706. On Date 5, Attorney 1 contacted Spouse and advised her to seek a private letter ruling to correct the errors on Decedent's Form 706. Spouse retained Attorney 2 for advice and preparation of this ruling request.

You represent that, had the Year 4 and Year 5 Forms 709 been properly filed for the Decedent, at Decedent's death, GST exemption totaling Amount 4 would have been available for allocation with respect to the Year 4 and Year 5 transfers to Trust A.

You have requested the following rulings:

1. An extension of time is granted to allocate Decedent's GST exemption to Trust A with respect to Decedent's Year 4 and Year 5 transfers to Trust A.
2. An extension of time is granted to elect to treat the Marital QTIP Trust as two separate trusts (the Marital QTIP Exempt Trust and the Marital QTIP Non-Exempt Trust) pursuant to the terms of Trust B and to make a reverse QTIP election under § 2652(a)(3) with respect to the Marital QTIP Exempt Trust.

On Date 6, Forms 709 for Year 4 and Year 5 were filed on behalf of Decedent, as well as a Supplemental Form 706. The Forms 709 and the Supplemental Form 706 were prepared and filed consistent with the granting of the above-referenced ruling requests.

Law and Analysis

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 shall, except as limited by § 2056(b), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to the surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Section 2056(b)(1) disallows this deduction where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail.

Section 2056(b)(7)(A) provides that, in the case of qualified terminable interest property, for purposes of § 2056(a), such property shall be treated as passing to the surviving spouse, and for purposes of § 2056(b)(1)(A), no part of such property shall be treated as passing to any person other than the surviving spouse.

Section 2056(b)(7)(B)(i) defines the term "qualified terminable interest property" as property: (I) which passes from the decedent; (II) in which the surviving spouse has a qualifying income interest for life; and (III) to which an election under § 2056(b)(7) applies.

Section 2056(b)(7)(B)(ii) provides that the surviving spouse has a qualifying income interest for life if: (I) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, or has a usufruct interest for life in the property; and (II) no person has a power to appoint any part of the property to any person other than the surviving spouse.

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

Section 2601 imposes a tax on every generation-skipping transfer (within the meaning of subchapter B). A "generation-skipping transfer" is defined under § 2611(a) as: (1) a taxable distribution; (2) a taxable termination; and (3) a direct skip.

Section 2602 provides that the amount of the GST tax is determined by multiplying the taxable amount by the applicable rate. Section 2641(a) provides that the term "applicable rate" means with respect to any GST transfer, 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 any property transferred in a generation-skipping transfer is generally defined as the excess of 1 over the "applicable fraction." The applicable fraction, as defined in § 2642(a)(2) is a fraction, the numerator of which

is the amount of GST exemption under § 2631 allocated to the trust (or to property transferred in a direct skip), and the denominator is the value of the property transferred reduced by the sum of any federal estate tax or state death tax actually recovered from the trust attributable to such property and any charitable deduction allowable under § 2055 or § 2522 with respect to such property.

Section 2631(a), as in effect for decedents dying before December 31, 2003, 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 such individual (or his executor) to any property with respect to which such individual is the transferor. Section 2631(b) provides that any allocation under § 2631(a), once made, shall be irrevocable.

Section 2632(a) provides that any allocation by an individual of his or her GST exemption under § 2631(a) 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(e)(1) provides that, in general, any portion of an individual's GST exemption which 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 such individual's death, and (B) second, to trusts with respect to which such individual is the transferor and from which a taxable distribution or a taxable termination might occur at or after such individual's death.

Section 26.2632-1(b)(2) of the Generation-Skipping Transfer Tax Regulations provides that an allocation of GST exemption to property transferred during the transferor's lifetime is made on Form 709.

Section 2652(a)(1) provides that for purpose of chapter 13, the term "transferor" means: (A) in the case of any property subject to the tax imposed by chapter 11, the decedent; and (B) in the case of any property subject to the tax imposed by chapter 12, the donor. An individual shall be treated as transferring any property with respect to which such individual is the transferor.

Section 2652(a)(3) provides, in pertinent part, 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 such trust for GST tax purposes as if the election to be treated as qualified terminable interest property had not been made (reverse QTIP election).

Section 26.2652-2(a) provides that a reverse QTIP election is not effective unless it is made with respect to all of the property in the trust to which the QTIP election applies. Section 26.2652-2(b) provides that an election under § 2652(a)(3) is made on the return on which the QTIP election is made.

Section 2642(a)(3) was enacted as part of the Taxpayer Relief Act of 2000, and provides for the qualified severance of a trust for GST tax purposes. Section 2642(a)(3) is effective in the case of severances occurring after December 31, 2000, and provides, generally, that if a trust is severed in a qualified severance, the trusts resulting from such severance shall be treated as separate trusts thereafter for GST tax purposes.

Section 2642(a)(3)(B)(i) provides that, for purposes of § 2642(a)(3)(A), the term “qualified severance” means the division of a single trust and the creation (by any means available under the governing instrument or under local law) of two or more trusts if the single trust was divided on a fractional basis, and the terms of the new trusts, in the aggregate, provide for the same succession of interests of beneficiaries as are provided in the original trust.

Section 2642(a)(3)(B)(ii) provides that if a trust has an inclusion ratio of greater than zero and less than 1, a severance is a qualified severance only if the single trust is divided into two trusts, one of which receives a fractional share of the total value of all trust assets equal to the applicable fraction of the single trust immediately before the severance. In such case, the trust receiving such fractional share shall have an inclusion ratio of zero and the other trust shall have an inclusion ratio of 1. Section 2642(a)(3)(B)(iii) provides that the term “qualified severance” includes any other severance permitted under regulations prescribed by the Secretary.

Section 2642(a)(3)(C) provides that a severance pursuant to § 2642(a)(3)(B) may be made at any time. The Secretary shall prescribe by forms or regulations the manner in which the qualified severance shall be reported to the Internal Revenue Service.

Section 2642(b)(1) provides that, except as provided in § 2642(f), if the allocation of the GST exemption to any transfers of property is made on a gift tax return filed on or before the date prescribed by § 6075(b) for such transfer or is deemed to be made under § 2632(b)(1) or (c)(1) the value of such property for purposes of § 2642(a) shall be its value as finally determined for purposes of chapter 12 (within the meaning of § 2001(f)(2)), or, in the case of an allocation deemed to have been made at the close of an estate tax inclusion period, its value at the time of the close of the estate tax inclusion period, and such allocation shall be effective on and after the date of such transfer, or, in the case of an allocation deemed to have been made at the close of an estate tax inclusion period, on and after the close of such estate tax inclusion period.

Section 2642(g)(1)(A) provides that the Secretary shall by regulation prescribe such circumstances and procedures under which extensions of time will be granted to make an allocation of GST exemption described in § 2642(b)(1) or (2), and an election under § 2632(b)(3) or (c)(5). Such regulations shall include procedures for requesting comparable relief with respect to transfers made before the date of the enactment of this paragraph.

Section 2642(g)(1)(B) provides that in determining whether to grant relief under § 2642(g)(1), the Secretary shall take into account all relevant circumstances, including evidence of intent contained in the trust instrument or instrument of transfer and such other factors as the Secretary deems relevant. For purposes of determining whether to grant relief, the time for making the allocation (or election) shall be treated as if not expressly prescribed by statute.

Notice 2001-50, 2001-2 C.B. 189, provides that, under § 2642(g)(1)(B), the time for allocating the GST exemption to lifetime transfers and transfers at death, the time for electing out of the automatic allocation rules, and the time for electing to treat any trust as a generation-skipping transfer trust are to be treated as if not expressly prescribed by statute. The Notice further provides that taxpayers may seek an extension of time to make an allocation described in § 2642(b)(1) or (b)(2) or an election described in § 2632(b)(3) or (c)(5) under the provisions of § 301.9100-3.

Section 301.9100-1(c) provides that the Commissioner has discretion to grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 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.

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

Section 301.9100-3(b)(1)(v) provides that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

Section 301.9100-3 provides the standards used to determine whether to grant an extension of time to make an election whose due date is prescribed by a regulation (and not expressly provided by statute). In accordance with § 2642(g)(1)(B) and Notice 2001-50, taxpayers may seek an extension of time to make an allocation described in § 2642(b)(1) or (b)(2) or an election described in § 2632(b)(3) or (c)(5) under the provisions of § 301.9100-3.

Based on the facts submitted and the representations made, we conclude that the requirements of § 301.9100-3 have been satisfied. Therefore, Decedent's Executrix is granted an extension of time until Date 6 to make an allocation of Decedent's GST exemption with respect to Decedent's transfers to Trust A in Year 4 and Year 5. The allocations will be effective as of the respective dates of the transfers to Trust A, and the inclusion ratio of Trust A will be determined based on the value of the transfers to Trust

A as determined for federal gift tax purposes and the amount of exemption allocated to Trust A.

Pursuant to the governing instrument of Trust B, the Marital Trust will be divided on a fractional basis into two separate shares, the Marital QTIP Exempt Trust and the Marital QTIP Non-Exempt Trust. Based on the facts presented and the representations made, we conclude that the severance of the Marital QTIP Trust into the Marital QTIP Exempt Trust and the Marital QTIP Non-Exempt Trust will be a qualified severance under § 2642(a)(3).

In addition, in accordance with § 301.9100-3, an extension of time to make a “reverse” QTIP election with respect to the Marital QTIP Exempt Trust is granted until Date 6. Assuming the Marital QTIP Exempt Trust and the Marital QTIP Non-Exempt Trust are funded as described above, the unused portion of Decedent’s GST exemption will be allocated, in accordance with the rules provided in § 2632(e)(1), such that the Family Bypass Trust and the Marital QTIP Exempt Trust will each have an inclusion ratio of zero, and the Marital QTIP Non-Exempt Trust will have an inclusion ratio of 1.

Supplemental Forms 709 and a Supplemental Form 706 consistent with the rulings requested herein have been filed with the Internal Revenue Service Center in Cincinnati. A copy of this letter should be forwarded to the Internal Revenue Service, Cincinnati Service Center – Stop 82, Cincinnati, OH 45999, for association with those supplemental forms.

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 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 requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Heather C. Maloy  
Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures  
Copy for section 6110 purposes  
Copy of this letter

cc: