

Trust. Article II, § 2.01(A) of Trust provides that, Decedent's residuary estate be divided pursuant to a formula into a Marital Trust and a Family Trust. With respect to the Marital Trust, the trust instrument provides for the distribution of all income to Spouse during her life, and grants the Trustee the discretion to distribute principal to Spouse. Article IV, § 4.02(E) of the trust instrument grants the trustee the power to make elections, disclaimers or take such other actions as Decedent's personal representative or trustee deems, in their sole discretion to be in the interests of the beneficiaries.

Spouse, Decedent's Personal Representative, engaged Firm to prepare Decedent's Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. On the Schedule M, the Personal Representative elected QTIP treatment for the property passing to the Marital Trust. The Personal Representative failed to make a "reverse" QTIP election under § 2652(a)(3) with respect to the Marital Trust. Further, the Personal Representative did not allocate Decedent's GST exemption on Schedule R even though all of Decedent's GST exemption was available for allocation at his death. These errors were discovered on Date 3.

The parties propose to divide the Marital Trust into the GST Exempt Marital Trust and the GST Nonexempt Marital Trust. The GST Exempt Marital Trust will be funded with a fractional share of Decedent's estate passing to the Marital Trust, the numerator of which is equal to the Decedent's remaining GST exemption after taking into account the automatic allocation of GST exemption to the Family Trust under § 2632, and the denominator of which is equal to the amount passing to the Marital Trust. The GST Nonexempt Marital Trust will be funded with the balance of the property passing to the Marital Trust. The GST Exempt Marital Trust and the GST Nonexempt Marital trust will be funded on a non pro rata basis, based on either the fair market value of the asset on the date of funding or in a manner that fairly reflects the net appreciation or depreciation in the value of the assets measured from the Decedent's date of death to the date of funding. A "reverse" QTIP election will then be made with respect to the GST Exempt Marital Trust.

Extensions of time under §§ 301.9100-1 and 301.9100-3 are requested in order to sever the Marital Trust under § 26.2654-1(b) into the GST Exempt Marital Trust and the GST Nonexempt Marital Trust and to make a "reverse" QTIP election under § 2652(a)(3) with respect to the GST Exempt Marital Trust.

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) made by a "transferor" to a skip person.

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 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) of the Generation-Skipping Transfer Tax Regulations provides, in part, 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 2654(b) provides that, for purposes of the GST tax, (1) the portions of a trust attributable to transfers from different transferors shall be treated as separate trusts, and (2) substantially separate and independent shares of different beneficiaries in a trust shall be treated as separate trusts. Except as provided in the preceding sentence, nothing in chapter 13 is to be construed as authorizing a single trust to be treated as two or more trusts.

Section 26.2654-1(b)(1) provides that the severance of a trust that is included in the transferor's gross estate (or created under the transferor's will) into two or more trusts is recognized for purposes of chapter 13 if –(i) the trust is severed pursuant to a direction in the governing instrument providing that the trust is to be divided upon the death of the transferor; or (ii) the governing instrument does not require or otherwise direct severance but the trust is severed pursuant to discretionary authority granted either under the governing instrument or under local law; and

(A) The terms of the new trust provide in the aggregate for the same succession of interests and beneficiaries as are provided in the original trust;

(B) The severance occurs (or a reformation proceeding, if required, is commenced) prior to the date prescribed for filing the federal estate tax return (including extensions actually granted) for the estate of the transferor; and

(C) Either (1) the new trusts are severed on a fractional basis. 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. The trust may be funded on a non pro rata basis provided funding is based on either the fair market value on the date of funding or in a manner that fairly reflects the net appreciation or depreciation in the value of the assets measured from the valuation date to the date of funding; or (2) if the severance is required (by the terms of the governing instrument to be made on the basis of a pecuniary amount, the pecuniary payment is satisfied in a manner that would meet the requirements of § 26.2654-1(a)(ii) if it were paid to an individual.

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.

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).

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.

Based on the facts and representations made, we have determined that the standards of §§ 301.9100-1 and 301.9100-3 have been met. Therefore, an extension of time is granted until 60 days from the date of this letter to sever the Marital Trust into the GST Exempt Trust and the GST Nonexempt Trust and to make a “reverse” QTIP election with respect to the GST Exempt Marital Trust. As a result of the severance and the “reverse” QTIP election with respect to the GST Exempt Marital Trust, Decedent’s remaining GST exemption, after taking into account the amount automatically allocated to the Family Trust, will be allocated to the GST Exempt Marital Trust under § 2632(e)(1). Therefore, assuming the GST Exempt Marital Trust and the GST Nonexempt Marital Trust are funded as described above, the GST Exempt Marital Share will have an inclusion ratio of zero, and the GST Nonexempt Marital Trust will have an inclusion ratio of 1.

A supplemental Form 706 (United States Estate (and Generation-Skipping Transfer) Tax Return) should be filed on behalf of Decedent’s estate with the Internal Revenue Service Center, Cincinnati, OH 45999. A copy of this letter should be attached.

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.

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,

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

Enclosure

Copy for section 6110 purposes
Copy of this letter