

## Internal Revenue Service

Number: **200443025**

Release Date: 10/22/04

Index Number: 2652.01-02, 9100.00-00

Department of the Treasury  
Washington, DC 20224

Person To Contact:

Telephone Number:

In Re:

Refer Reply To:

CC:PSI:B04 – PLR-140350-03

Date: JUNE 28, 2004

### LEGEND:

Husband	=
Wife	=
Son	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=
Trust	=
Exemption Trust	=
Marital Trust	=
Exempt Marital Trust	=
Non-exempt Marital Trust	=
Accountant 1	=
Accountant 2	=
Accounting Firm	=
Lawyer	=
Law Firm	=
State	=
X	=
Y	=

Z =

Dear :

This is in response to your letter dated March 15, 2003, and other correspondence, requesting an extension of time under section 301.9100-3 of the Procedure and Administration Regulations to make a reverse QTIP election under section 2652(a)(3) of the Internal Revenue Code with respect to the Exempt Marital Trust and to make an allocation of the generation-skipping transfer (GST) tax exemption to the Exempt Marital Trust under section 2642(g).

The facts and representations submitted are summarized as follows:

On Date 1, Husband established Trust under laws of State, a community property state. Trust was amended and restated on Date 2 by Husband and Wife. Trust was later amended several times, with the most recent amendment taking place on Date 3.

Paragraph 2.1 provides that during the joint lifetimes of Husband and Wife, they shall be entitled to all income and principal of their community property without limitation. With regard to the separate property of either Husband or Wife, either Trustor shall be entitled to all income and principal of his or her own separate estate without limitation.

Paragraph 4.1 provides that reference to the "Decedent" shall refer to either of the Trustors whose death shall first occur and reference to the "Survivor" shall refer to the surviving Trustor.

Paragraph 4.3(b) provides, in relevant part, that the remainder of the Trust estate and the property received by the Trustee by reason of Decedent's death shall be divided into three separate trusts: the Survivor's Trust, the Marital Trust, and the Exemption Trust. Paragraph 4.3(b)(1) provides that Survivor's Trust consists of Survivor's separate property interest in Trust and Survivor's one-half interest in the community property of Trust.

Paragraph 4.3(b)(2) provides, that if the Survivor survives the Decedent by a period of 180 days, there shall then be allocated to the Marital Trust an amount, if any, which, when added to the Federal Estate Tax marital deduction allowed for interests in property passing to the surviving spouse outside of this Trust instrument, including but not limited to interests in life insurance and jointly owned property and amounts passing directly to said spouse under the Will of the first Trustor to die, will produce the smallest total marital deduction necessary to eliminate (or reduce to the minimum extent possible) the Federal Estate Tax on the first Trustor's estate, but only to the extent that the use of any state death tax credit does not increase the death tax payable to any state.

Paragraph 4.3(b)(3) provides, in relevant part, that it is the intention of the Trustors, by paragraph (2) above, to maximize the marital deduction allowed to their estates under the applicable provisions of the Federal Internal Revenue Code but only to the extent necessary to reduce Federal Estate Taxes after using up all of the deductions, credits, and exemptions allowed to the estate in respect to the Federal Estate Tax. Paragraph 4.3(b)(4) provides that the Exemption Trust consists of the rest of the Trust estate.

Paragraph 4.6(a) provides that during the lifetime of the Survivor, the Trustee shall pay to the Survivor all of the net income of the Exemption Trust estate in monthly or other regular installments, but not less frequently than quarter annually.

Paragraph 4.6(b) provides that Survivor shall have the discretionary power during the Survivor's lifetime or upon the Survivor's death to direct the Trustee to pay over and distribute trust principal from the Exemption Trust in the manner provided in a power of appointment signed by the Survivor and delivered to the Trustee. The Survivor's power to appoint beneficiaries of the Exemption Trust shall be limited to the issue of Husband and Wife and shall exclude the Survivor or the Survivor's estate or creditors of the Survivor.

Paragraph 4.6(e) provides that if some or all of the Decedent's generation-skipping exemption is allocated to the property (or exempt portion of the property) that is otherwise to constitute the Exemption Trust and if that Trust would thereby have an inclusion ratio greater than zero, the Trustee shall instead establish two separate trusts so that each has a generation-skipping inclusion ratio of either zero (the "Exempt Exemption Trust") or one (the "Nonexempt Exemption Trust"), and the Trustee shall accomplish this by allocating to the Nonexempt Exemption Trust the maximum fractional portion of the property that is necessary to establish that trust with an inclusion ratio of one, while leaving the Exempt Exemption Trust with an inclusion ratio of zero.

Paragraph 4.6(g) provides that upon the death of the Survivor, the Trustee shall administer the entire remaining income and principal of the Exemption Trust in accordance with Article VI.

Paragraph 6.1 provides that upon the death of both Trustors, any remaining property, both income and principal of this Trust estate, shall be divided into as many equal shares as there are children of the Trustors who are then living and children of the Trustors who are deceased leaving issue then living.

Paragraph 9.1 provides that during the joint lifetime of Trustors, this Trust Indenture may be amended in whole or in part by an instrument in writing, signed by both Trustors, and delivered to the Trustee. After the death of the first Trustor to die, the Surviving Trustor may amend the Survivor's Trust, by an instrument in writing,

signed and delivered to the Trustee. After the death of the first Trustor to die, the Exemption Trust and Marital Trust may not be amended by the surviving Trustor. Upon the death of both Trustors, this Trust Indenture shall not be amended.

Husband died on Date 4, survived by Wife and three living children. The bulk of his estate was held in the Trust with Wife. Article III of Husband's will provides that, after payment of debts, Husband bequeathed the remainder of his estate to Trust.

In accordance with the terms of Trust, upon Husband's death, Trust was divided into three trusts: the Survivor's Trust, the Marital Trust, and the Exemption Trust. The Exemption Trust was funded with \$x and the Marital Trust was funded with \$y. In accordance with the deemed allocation rules of section 2632(e)(1), \$x of Husband's GST exemption was automatically applied to the Exemption Trust, leaving \$z of available GST exemption unused.

Within a few days of Husband's death, Husband's son, Son, in his capacity as co-trustee of Trust, retained Accountants 1 and 2 of Accounting Firm to advise on trust administration and assist with preparation of the estate tax return (Form 706). Son relied upon the expertise of Accountants 1 and 2 regarding the preparation of the estate tax return. On Schedule M of Form 706, Accountants 1 and 2 made an election under section 2056(b)(7) to treat the entire value of Marital Trust as QTIP property, and claimed a deduction for this amount. However, no Schedule R was filed with the Form 706. Consequently, no election was made under section 2652(a)(3) and none of Husband's GST exemption was allocated on the Form 706. The estate tax return was timely filed with the Internal Revenue Service on Date 6.

Son also hired Lawyer of Law Firm for advice and assistance on related estate planning and trust administration issues including filing of the necessary trust allocation documents to make sure the trust assets were properly allocated to the various trusts created by Trust. In the process of preparing those documents, Lawyer discovered that Schedule R had not been filed with the Form 706.

On Date 5, the Marital Trust was severed and divided into two separate trusts, the Exempt Marital Trust and the Non-exempt Marital Trust, pursuant to a Trust Split Agreement executed by the Trustees. It is represented that both the Exempt Marital Trust and the Non-exempt Marital Trust are governed by and in accordance with the provisions of the Marital Trust. It is also represented that the severance was done on a pro rata basis.

You have requested an extension of time under sections 301.9100-1 and 301.9100-3 to make a "reverse" QTIP election under section 2652(a)(3) with respect to the Exempt Marital Trust and to allocate Husband's GST exemption to the Exemption Trust and the Exempt Marital Trust under section 2642(g).

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 section 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, such property shall be treated as passing to the surviving spouse for purposes of section 2056(a) and no part of the property shall be treated as passing to any person other than the surviving spouse.

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 section 2056(b)(7)(B)(v) applies.

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

Section 2601 imposes a tax on every generation-skipping transfer (GST). A GST is defined under section 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, the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer.

Under section 2642(a)(1), the inclusion ratio with respect to any property transferred in a generation-skipping transfer is generally defined as the excess (if any) of 1 over the "applicable fraction." The applicable fraction, as defined in section 2642(a)(2) is a fraction, the numerator of which is the amount of the GST exemption allocated to the trust (or to property transferred in a direct 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 section 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 section 2631(a), once made, shall be irrevocable.

Section 2632(a)(1) provides that any allocation by an individual of his GST exemption under section 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 section 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(d)(1) of the Generation-Skipping Transfer Tax Regulations provides, in part, that except as otherwise provided in section 26.2632-1(d), an allocation of a decedent's unused GST exemption by the executor of the decedent's estate is made on the appropriate United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706 or Form 706NA) filed on or before the date prescribed for filing the return by section 6075(a) (including any extensions actually granted (the due date)). An allocation of GST exemption with respect to property included in the gross estate of a decedent is effective as of the date of death.

Section 26.2632-1(d)(2) provides, in pertinent part, that 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 GST with respect to the new trust.

Section 2652(a)(1) provides, in pertinent part, that for purposes 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 that in the case of -- (A) any trust with respect to which a deduction is allowed to the decedent under section 2056 by reason of subsection (b)(7) thereof, and (B) any trust with respect to which a deduction to the donor spouse is allowed under section 2523 by reason of subsection (f) thereof, the estate of the decedent or the donor spouse, as the case may be, may elect to treat all of the property in such trust for purposes of this chapter as if the election to be treated as qualified terminable interest property had not been made.

Section 26.2652-2(b) provides that a "reverse" QTIP election is made on the

return on which the QTIP election is made.

Section 2642(a)(3)(A) 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, generally, that for purposes of section 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 this paragraph 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 IRS.

Section 2642(b)(2)(A) provides that if property is transferred as a result of the death of the transferor, the value of such property for purposes of section 2642(a) shall be its value as finally determined for purposes of chapter 11; except that, if the requirements prescribed by the Secretary respecting allocation of post-death changes in value are not met, the value of such property shall be determined as the of time of the distribution concerned. Section 2642(b)(2)(B) provides that any allocation to property transferred as a result of the death of the transferor shall be effective on and after the date of the death of the transferor.

Section 2642(g)(1)(A) provides, generally, 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 section 2642(b)(1) or (2), and an election under section 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 this paragraph, 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 under this paragraph, 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 section 2642(g)(1)(B), the time for allocating the GST tax 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 GST 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 section 2642(b)(1) or (b)(2) or an election described in section 2632(b)(3) or (c)(5) under the provisions of section 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 sections 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). Under section 301.9100-1(b), a regulatory election includes an election whose due date is prescribed by a notice published in the Internal Revenue Bulletin. In accordance with section 2642(g)(1)(B) and Notice 2001-50, taxpayers may seek an extension of time to make an allocation described in section 2642(b)(1) or (b)(2) or an election described in section 2632(b)(3) or (c)(5) under the provisions of section 301.9100-3.

Requests for relief under section 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.

On Date 5, the Marital Trust was divided on a fractional basis in accordance with the applicable fraction of the Marital Trust and the terms of the Exempt Marital Trust and the Non-exempt Marital Trust provide for the same succession of interests of beneficiaries as are provided in the original trust. Under these circumstances, we conclude that the Date 5 severance is a qualified severance under section 2642(a)(3).

Based on the facts submitted and representations made in this case, we conclude that the standards of sections 301.9100-1 and 301.9100-3 have been



satisfied. Consequently, an extension of time to make a "reverse" QTIP election under section 2652(a)(3) with respect to Exempt Marital Trust and to allocate Husband's remaining GST exemption under section 2642(g) to the Exempt Marital Trust is granted until 60 days after the date of this letter.

This election and allocation of GST exemption should be made on a supplemental Form 706 United States Estate (and Generation-Skipping Transfer) Tax Return and filed with the Internal Revenue Service Center, Cincinnati, OH 45999. A copy of this letter should be attached to the supplemental Form 706. A copy is enclosed for this purpose.

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

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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.

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