

## Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4-PLR-112389-00

Date:

DECEMBER 04, 2000

Re:

Decedent =

Spouse =

Son =

Daughter =

x =

y =

Marital Trust =

Son's Trust =

Daughter's Trust =

Date 1 =

Date 2 =

Dear :

This is in response to your letter of October 12, 2000, and prior correspondence, requesting an extension of time under § 301.9100-1 of the Procedure and Administration Regulations to sever several trusts pursuant to § 26.2654-1(b)(1) of the Generation-skipping Transfer Tax (GSTT) Regulations, and to make a "reverse" QTIP election under § 2652(a)(3).

Decedent died testate on Date 1, survived by Spouse and two children, Son and Daughter. Under the terms of Decedent's will, a credit shelter trust was created under Article IV and a residuary Marital Trust was created under Article VI. Son is the executor of Decedent's estate, and Son and a bank are co-trustees of the Marital Trust.

Under the terms of Article IV, the credit shelter trust is to be held for the benefit of Spouse during her lifetime, and on her death the trust is to be divided into 2 separate trusts, one held for the benefit of Son and his issue, and one held for the benefit of Daughter and her issue.

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Under the terms of Article VI, the trustees of the Marital Trust are to pay trust income to Spouse in quarterly installments and at any time, such amounts of principal that the trustees may in their discretion determine. Upon Spouse's death, the trust was to be divided into two separate trusts, one trust for the benefit of Son and his issue (Son's Trust) and one trust for the benefit of Daughter and her issue (Daughter's Trust).

Son, as executor of Decedent's estate, retained an attorney for purposes of preparing Decedent's federal estate tax return (Form 706). Decedent's estate timely filed Form 706 in 1989. On Decedent's estate tax return, Decedent's estate elected to treat the property passing to the Marital Trust as qualified terminable interest property (QTIP), under § 2056(b)(7) and claimed a marital deduction for \$y passing to the trust. However, there was no indication on the estate tax return that the Marital Trust was to be divided into a GSTT exempt trust and a GSTT nonexempt trust. Further, with respect to the Marital Trust, no reverse QTIP election under § 2652(a)(3) was made, and no allocation of Decedent's GSTT exemption was made by the executor. Spouse died on Date 2. After Spouse's death, the Marital Trust was divided into two equal shares and administered as two separate trusts (Son's trust and Daughter's Trust) as provided under Article VI. No allocation of GSTT exemption was made on Spouse's estate tax return.

The executor of Decedent's estate has petitioned the appropriate state court to take certain action described below with respect to the Marital Trust, Son's Trust and Daughter's Trust. The court has granted the petition, pending a favorable private letter ruling.

Under the petition, the Marital Trust first will be severed into two separate trusts effective as of the date of the Decedent's death; the GSTT Exempt Marital Trust and the GSTT Taxable Marital Trust. The GSTT Exempt Marital Trust will consist of a fraction of the value of the Marital Trust. The numerator of the fraction will be x (the amount of Decedent's unused GSTT exemption reduced by the amount automatically allocated to the credit shelter trust pursuant to the rules of § 2632(c)) and the denominator will be y (the value, as finally determined for federal estate tax purposes, of the property passing to the Marital Trust). The GSTT Taxable Marital Trust consists of the remaining portion of the Marital Trust. After the severance, the executor of Decedent's estate will make a reverse QTIP election under § 2652(a)(3) with respect to the GSTT Exempt Marital Trust.

The trustees next propose to sever Son's Trust into Son's GSTT Exempt Trust and Son's GSTT Taxable Trust. Son's GSTT Exempt Trust will consist of a fraction of the value of Son's Trust determined as of the date of severance. The numerator of the fraction will be x and the denominator will be y. Son's GSTT Taxable Trust will consist of the remaining portion of the Son's Trust. Similarly, the trustees propose to sever Daughter's Trust in the same manner.

It is represented that no transfers to skip persons with respect to the Decedent or

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Spouse have been made from Son's Trust or Daughter's Trust.

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, such 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.

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 § 2056(b)(7)(B)(v) applies.

Under § 2044, any property in which a decedent possessed a qualifying income interest for life and for which a deduction was allowed under § 2056(b)(7) is includible in the decedent's gross estate.

Section 2601 imposes a tax on every generation-skipping transfer made by a "transferor" to a skip person. Under § 2611, a generation-skipping transfer means a taxable distribution, a taxable termination, and a direct skip.

In general, the tax is computed by multiplying the taxable amount by the "applicable rate." The applicable rate is the highest federal estate tax rate multiplied by the inclusion ratio with respect to the transfer. Under § 2642(a), the inclusion ratio is the excess (if any) of 1 over the applicable fraction determined for the trust from which such transfer is made. The applicable fraction is a fraction the numerator of which is the amount of the GSTT exemption available under § 2631 allocated to the trust; and the denominator of which is (i) the value of the property transferred to the trust reduced by (ii) the sum of (I) the federal estate tax or state death tax actually recovered from the trust attributable to such property, and (II) any charitable deduction allowed under § 2055 and § 2522 with respect to such property.

Section 2631(a) provides generally that for purposes of determining the inclusion

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ratio, every individual is allowed a GSTT exemption of \$1,000,000 (adjusted for inflation as provided in § 2631(c)), which may be allocated by such individual (or his executor) to any property with respect to which such individual is the transferor. Under § 2632(a), any allocation of GSTT exemption may be made at any time on or before the date prescribed for filing the estate tax return for such individual's estate. Under § 2632(c)(1), any portion of an individual's GSTT exemption which has not been allocated within the time prescribed in § 2632(a) is deemed allocated first, to property which is the subject of a direct skip occurring at the individual's death, and 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.

Under § 2652(a)(1), the term "transferor" means, in the case of any property subject to the estate tax, the decedent.

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 GSTT exemption may be allocated to the QTIP trust.

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

Section 26.2654-1(b)(1)(ii) 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 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 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 of time actually granted) for the estate of the transferor, and 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 trusts may be funded on a nonprorata basis provided funding is based on either the fair market value of the assets 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 date of death to the date of funding.

Under § 301.9100-1(c) of the Procedure and Administration Regulations, 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

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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 301.9100-2 and 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make an election.

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 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).

Based solely on the information submitted and the representations made, we conclude that the standards of §§ 301.9100-1 and 301.9100-3 have been satisfied. Consequently, we rule as follows:

(1) An extension of time for dividing the Martial Trust into the GSTT Exempt Marital Trust and the GSTT Taxable Marital Trust is granted until 60 days after the date of this letter.

(2) An extension of time for making the reverse QTIP election under § 2652(a)(3) with respect to the GSTT Exempt Marital Trust is granted until 60 days after the date of this letter.

(3) An extension of time for dividing Son's Trust into Son's GSTT Exempt Trust and Son's GSTT Taxable Trust is granted until 60 days after the date of this letter.

(4) An extension of time for dividing Daughter's Trust into Daughter's GSTT Exempt Trust and Daughter's GSTT Taxable Trust is granted until 60 days after the date of this letter.

The extension of time to sever the trusts and to make the reverse QTIP election does not extend the time to allocate GSTT exemption. Accordingly, in this case, Decedent's and Spouse's available GSTT exemption is allocated pursuant to the automatic allocation rules under § 2632(c). Based on these rules and assuming severance as described above, we conclude that the inclusion ratio with respect to Son's GSTT Exempt Trust and Daughter's GSTT Exempt Trust will be zero. In the case of Spouse's GSTT exemption, the exemption is allocated as prescribed under § 2632(c)(1), between Son's Taxable GSTT Trust, Daughter's Taxable GSTT Trust, and any other transfers of assets includible in Spouse's gross estate that have GSTT consequences (other than Son's GSTT Exempt Trust and Daughter's GSTT Exempt Trust.)

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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) of the Code provides that it may not be used or cited as precedent.

Sincerely yours,  
Paul F. Kugler  
Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosure

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