

Internal Revenue Service

Number: **201840001**

Release Date: 10/5/2018

Index Number: 2056.07-02, 9100.00-00,
2642.00-00, 2652.01-02

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B04

PLR-102775-18

Date: June 20, 2018

LEGEND

Decedent	=
Date 1	=
Spouse	=
Daughter	=
Granddaughter	=
Trust	=
Law Firm	=
<u>a</u>	=
<u>b</u>	=
<u>x</u>	=
<u>y</u>	=
<u>z</u>	=
Date 2	=
Date 3	=
Date 4	=
State Court	=

Dear :

This letter responds to the letter dated December 22, 2017, submitted by your authorized representative requesting an extension of time under § 301.9100-3 of the Procedure and Administration Regulations to sever a trust into a qualified terminable interest property (QTIP) trust and a non-QTIP trust under § 20.2056(b)-7(b)(2)(ii) of the Estate Tax Regulations, and requesting additional rulings with respect to the severed trusts.

FACTS

The facts submitted and the representations made are as follows:

Decedent died testate on Date 1, survived by Spouse, Daughter, and Granddaughter. Spouse was named executrix of Decedent's estate under Decedent's will.

In Article IV of Decedent's will, the residue remaining after certain specific bequests is bequeathed to the trustees of Trust, to be held, administered and distributed as set forth in Article IV of Decedent's will.

Under Article IV(1), the executrix "shall elect the portion of [Decedent's] estate passing under this Article IV which, in her discretion, she determines should qualify for the estate tax marital deduction allowable in determining federal estate taxes on [Decedent's] estate...but only to the extent that such items are included in [Decedent's] gross estate and are allowable as a marital deduction for federal tax purposes."

Article IV(1) further provides that the trustees shall distribute all of the trust income to Spouse at least quarterly. If the trustees determine the trust income is not adequate for the needs of Spouse's support in her accustomed manner of living, including medical, dental, hospital and nursing expenses, the trustees may distribute such amounts of trust principal as they deem necessary for such purpose.

Article IV(1)(b)(i) provides that the trustees:

shall have the discretionary power and authority to divide the trust estate into two separate trusts, one to hold that portion of the trust which [Decedent's] Executrix elects to qualify for the federal estate tax marital deduction ("Marital Trust") with the second trust to hold property representative of the balance of the trust estate ("Exempt Trust"). In the event the Trustees elect to so divide the trust estate into two trusts, the allocation of trust assets as between the Marital Trust and Exempt Trust shall be in accordance with the elections for federal estate taxes as made by [Decedent's] Executrix. The decision of the Trustees as to the property allocated to each trust shall be final and conclusive upon all parties; provided, that there may not be allocated to the Marital Trust any property with respect to which no marital deduction would be allowed if such property had passed to [Decedent's] wife free of trust..."

Article IV(3)(a) provides that upon Spouse's death, a trust is to be created for the benefit of Granddaughter (Granddaughter's Trust), to be funded with the lesser of the amount which may pass to or for the benefit of Granddaughter free from any generation-skipping transfer (GST) tax imposed under chapter 13 of the Code of 1986, or the [then present] exemption amount of \$1,000,000. In the event the GST tax is repealed or

otherwise no longer in effect as of the death of Spouse, Granddaughter's Trust is to be funded with \$1,000,000.

Article IV(3)(b) provides that the balance of Trust remaining after Spouse's death and after funding Granddaughter's Trust as provided in Article IV(3)(a), shall be distributed in accordance with Spouse's testamentary power to appoint to or for the benefit of one or more appointees other than Spouse, her creditors, her estate or the creditors of her estate.

Article IV(3)(c) provides that in the event of nonexercise of Spouse's testamentary power to appoint, the remainder of Trust shall pass to Daughter. In the event Daughter predeceases Spouse, the remainder of Trust is to be distributed to Granddaughter's Trust.

After Decedent's death, Spouse, as Executrix of Decedent's estate, retained Law Firm to advise her regarding the administration of Decedent's estate, including preparation of Form 706 (United States Estate (and Generation-Skipping Transfer) Tax Return). Law Firm did not advise Spouse to sever Trust into a "Marital Trust" (QTIP Trust) and "Exempt Trust" (Non-QTIP Trust) as provided under Article IV(1)(b)(i). Law Firm prepared Form 706 for Decedent's estate, which was timely filed.

On Schedule M, Part 2, of Form 706, Decedent's estate made an election under § 2056(b)(7) to treat an a% portion of Trust as QTIP. Schedule M, Part 2 reported the total value of property interests subject to the QTIP election as \$x, determined to be a% of the total value (\$y) of the assets funding Trust. No QTIP election was made for the balance of Trust (the b% portion of Trust), valued at \$z (\$y - \$x).

On Schedule R, Part 1, of Form 706, Decedent's estate checked the box to make a special election under § 2652(a)(3) to treat assets, for GST tax purposes, as if the election under § 2056(b)(7) had not been made (a "reverse QTIP election"). Intending to shield Granddaughter's Trust from the imposition of GST tax, a trust which pursuant to the terms of Trust in Article IV of Decedent's will was to be created after the death of Spouse, Law Firm improperly and ineffectively allocated Decedent's entire unused GST exemption to Granddaughter's Trust on line 6 of Schedule R, Part 3.

Subsequent to the filing of Decedent's Form 706, § 26.2652-2(c) of the Generation-Skipping Transfer Tax Regulations was issued. This regulation provides a transitional rule that allows certain trusts subject to a reverse QTIP election to be treated as two separate trusts, so that only a portion of the trust would be treated as subject to the reverse QTIP election, and that portion would be treated as having a zero inclusion ratio. The deadline for making the election set forth in the transitional rule is June 24, 1996.

On Date 2, under the authority of Article IV(1)(b)(i), Spouse, as trustee of Trust, petitioned State Court for approval of a Nonjudicial Agreement dated Date 3, regarding Trust. The Nonjudicial Agreement provides for the severance of Trust into QTIP Trust, to hold the a% portion, and Non-QTIP Trust, to hold the b% portion. QTIP Trust and Non-QTIP Trust will have terms identical to those of Trust and all distributions of principal will be made pro rata from each trust. The effective date of the Nonjudicial Agreement is the date of issuance of a private letter ruling from the Internal Revenue Service. State Court granted Spouse's petition in an order dated Date 4.

No GSTs have been made from Trust.

You request the following rulings:

1. That Decedent's estate is granted an extension of time under § 301.9100-3 and § 20.2056(b)-7(b)(2)(ii) to sever Trust, on a fractional basis, with the a% portion to be identified as the QTIP Trust and the b% portion to be identified as the Non-QTIP Trust, effective as of Decedent's date of death.
2. That Decedent's estate is granted an extension of time under § 2642(g) and § 301.9100-3 to allocate Decedent's available GST exemption to Non-QTIP Trust and QTIP Trust, effective as of Decedent's date of death.
3. That Decedent's estate is granted an extension of time under § 301.9100-3 to make an election to treat QTIP Trust as two separate trusts pursuant to § 26.2652-2(c), so that one has an inclusion ratio of zero (identified as the GST Exempt QTIP Trust) and one has an inclusion ratio of one (identified as the GST Non-Exempt QTIP Trust) for GST tax purposes, and, further, that the reverse QTIP election will be treated as applying only to the GST Exempt QTIP Trust.

LAW AND ANALYSIS

Ruling 1

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 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, but only to the extent that such interest is included in determining the value of the gross estate.

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.

Under § 2056(b)(7), a marital deduction is allowed for qualified terminable interest property (QTIP), which is defined in § 2056(b)(7)(B)(i) 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)(B)(v) applies.

Section 2056(b)(7)(B)(iv) provides that a specific portion of property shall be treated as separate property.

Section 2056(b)(7)(B)(v) provides that an election 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 20.2056(b)-7(b)(2)(i) provides that the QTIP election may relate to all or any part of property that meets the requirements of § 2056(b)(7)(B)(i), provided that any partial election must be made with respect to a fractional or percentage share of the property. The fraction or percentage may be defined by a formula.

Section 20.2056(b)-7(b)(2)(ii)(A) provides that, in general, a trust may be divided into separate trusts to reflect a partial election that has been made, or is to be made, if authorized under the governing instrument or otherwise permissible under local law. Any such division must be accomplished no later than the end of the period of estate administration. If, at the time of the filing of the estate tax return, the trust has not yet been divided, the intent to divide the trust must be unequivocally signified on the estate tax return.

Section 20.2056(b)-7(b)(4)(i) provides that, in general, the election referred to in § 2056(b)(7)(B)(i)(III) and (v) is made on the return of tax imposed by § 2001 (or § 2101). For purposes of this paragraph, the term “return of tax imposed by § 2001” means the last estate tax return filed by the executor on or before the due date of the return, including extensions or, if a timely return is not filed, the first estate tax return filed by the executor after the due date.

Under § 301.9100-1(c), 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 301.9100-2 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.

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 the grant of 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.

In the present case, Article IV(1) specifically authorizes the trustees of Trust to elect to have a specific portion, or all, of Trust treated as QTIP. On Decedent's Form 706, a partial QTIP election was made with respect to a% of Trust. Under Article IV(1)(b)(i), the trustees have discretionary power and authority to divide the trust estate into two separate trusts: a QTIP Trust, referred to in Article IV as the Marital Trust, and a non-QTIP Trust, referred to in Article IV as the Exempt Trust.

Based on the facts presented and the representations made, we conclude that the requirements of § 301.9100-3 have been satisfied. Accordingly, Decedent's estate is granted 120 days from the date of this letter to sever Trust, on a fractional basis, into QTIP Trust and Non-QTIP Trust. For estate tax purposes, the severance will be effective as of the date of Decedent's death. The severance should be made on a supplemental Form 706 within 120 days from the date of this letter unequivocally signifying the severance of Trust.

Rulings 2 and 3

Section 2601 imposes a tax on every GST. A GST 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 tax imposed by § 2601 is the taxable amount multiplied by the applicable rate.

Section 2641(a) defines the applicable rate as the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer.

Under § 2642(a), the inclusion ratio with respect to any property transferred in a GST is the excess (if any) of one over the applicable fraction. The applicable fraction, as defined in § 2642(a)(2), is a fraction, the numerator of which is the amount of the GST

exemption under § 2631 allocated to the trust, and the denominator of which is the value of the property transferred to the trust.

Section 2631(a) (in effect at the time of Decedent's death) provided that, for purposes of determining the inclusion ratio, every individual shall be allowed a GST exemption of \$1,000,000 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)(1) 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.

Under § 2652(a)(1) and § 26.2652-1(a)(1), the individual with respect to whom property was last subject to federal estate or gift tax is the transferor of that property for purposes of the GST tax imposed under chapter 13.

Section 2652(a)(3) provides that, in the case of any property with respect to which a deduction is allowed under § 2056(b)(7) (regarding QTIP), 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.

The election under § 2652(a)(3) is referred to as the "reverse" QTIP election. The consequence of a reverse QTIP election is that the decedent remains, for GST tax purposes, the transferor of the QTIP trust for which the election is made. As a result, the decedent's GST exemption may be allocated to that QTIP trust.

Section 26.2652-2(a) 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(c) provides that if a reverse QTIP election is made with respect to a trust prior to December 27, 1995, and the GST exemption has been allocated to that trust, the transferor (or the transferor's executor) may elect to treat the trust as two separate trusts, one of which has a zero inclusion ratio by reason of the transferor's GST exemption previously allocated to the trust. The separate trust with the zero inclusion ratio consists of that fractional share of the value of the entire trust equal to the value of the nontax portion of the trust under § 26.2642-4(a). The reverse QTIP election is treated as applying only to the trust with the zero inclusion ratio. An election under § 26.2652-2(c) is made by attaching a statement to a copy of the Form 706 on which

the reverse QTIP election was made under § 2652(a). The statement is to be filed before June 24, 1996.

Section 2642(b)(2) provides generally that if property is transferred as a result of the death of the transferor, the value of the property for purposes of determining the inclusion ratio under § 2642(a)(1) shall be the value of the property as finally determined for estate tax purposes.

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 § 2641(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 § 2642(g)(1)(A), which was enacted into law on June 7, 2001.

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, 2001-34 I.R.B. 189, provides, in part, that under § 2642(g)(1)(B), the time for allocating the GST exemption to transfers at death is 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)(2) under the provisions of § 301.9100-3.

Based on the facts submitted and representations made, we have determined that the standards of § 301.9100-3 have been met. Therefore, an extension of time of 120 days from the date of this letter is granted under § 2642(g)(1) to allocate a portion of Decedent's unused GST exemption to the Non-QTIP Trust, so that Non-QTIP Trust will have an inclusion ratio of zero, and the balance to QTIP Trust. The allocations will be effective as of Decedent's date of death. Further, an extension of time of 120 days from the date of this letter is granted to make the election under § 26.2652-2(c) to treat QTIP Trust as two separate trusts, one to be referred to as the GST Exempt QTIP Trust and the other as the GST Non-Exempt QTIP Trust. The GST Exempt QTIP Trust will have a zero inclusion ratio by reason of the allocation of an amount of Decedent's GST exemption to the QTIP Trust, and the GST Non-Exempt QTIP Trust will have an inclusion ratio of one. The reverse QTIP election will be treated as applying only to the GST Exempt QTIP Trust and, therefore, Decedent will be considered the transferor of the GST Exempt QTIP Trust, while Spouse will be treated as the transferor of the GST Non-Exempt QTIP Trust.

The allocation of Decedent's GST exemption should be made on a supplemental Form 706 filed within 120 days from the date of this letter. The election under § 26.2652-2(c) should be made by completing the statement required in § 26.2652-2(c) and attaching the statement to the supplemental Form 706. The Form 706 should be filed with the Cincinnati Service Center at the following address: Internal Revenue Service Center, Cincinnati, OH 45999. A copy of this letter should also 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 your authorized representatives.

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.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,

Associate Chief Counsel
(Passthroughs & Special Industries)

Karlene M. Lesho

By: _____
Karlene M. Lesho
Senior Technician Reviewer, Branch 4
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy for §6110 purposes
Copy of this letter