

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:DOM:P&SI:4/ PLR-104069-00

Date:

June 22, 2000

Re:

Legend:

Decedent =

State Z =

Date 1 =

Date 2 =

Date 3 =

Decedent's will =

Trust =

Spouse =

Son =

Executors =

Trustee =

Charitable Trust =

Dear :

This is in response to your submission of February 2, 2000, and subsequent correspondence, on behalf of Decedent's estate, in which you request an extension of time under § 301.9100-1 of the Procedure and Administration Regulations to sever a trust under § 26.2654-1(b) of the Generation-Skipping Transfer Tax Regulations.

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Facts

Decedent, a resident of State Z, died testate on Date 1, survived by his Spouse and Son. Article Third, Section A of Decedent's will provides that, if Decedent is survived by any issue, Decedent's residuary estate is to be divided into two equal shares (Share X and Share Y).

Pursuant to Article Third, Section A(1) of Decedent's will, Share X is to be distributed outright to Spouse.

Article Third, Section A(2) of the will provides that Share Y is to be further divided into two equal subshares (Share Y(1) and Share Y(2)). Share Y(1) is to be held in trust for the benefit of Decedent's surviving issue, subject to the provisions in Article Fourth of Decedent's will. Share Y(2) is to be distributed to Charitable Trust, to be held, administered, and disposed of as a part of such Charitable Trust.

Article Fourth, Section A(1) provides that Share Y(1) is to be held in trust (Trust) for the benefit of Son and his issue. The Trustee is directed to pay to or apply to the use of such one or more of Son and his issue (of whatever degree), so much or all of the net income of Trust, in such amounts or proportions, as Trustee, in his absolute discretion, from time to time shall select and determine. Any undistributed net income shall be accumulated and added to principal.

Article Fourth, Section A(1)(a) of Decedent's will authorizes and empowers Trustee to pay to or apply to the use of such one or more of the beneficiaries such sums from or portions of the Trust principal (to the extent of the entire principal) as Trustee in his absolute discretion, shall from time to time select and determine.

Article Fourth, Section A(2) provides that upon the death of Son, the remaining Trust principal is to be distributed to such person or persons (excluding his estate, his creditors, and the creditors of his estate) in such amounts or proportions and upon such estates (whether in trust or otherwise) as Son appoints in his will. Any portion or all of such principal not effectively appointed will be paid over and distributed to the then living issue of Son, per stirpes.

Article Eighth, Section B(1) of Decedent's will authorizes Executors, in the exercise of their absolute discretion, to allocate any amount of Decedent's generation-skipping transfer (GST) exemption under § 2631(a) to such property of which Decedent is the transferor, whether or not passing under Decedent's will, including property transferred by Decedent during Decedent's lifetime, and without any duty to favor beneficiaries under Decedent's will over beneficiaries or property passing outside the will.

Article Eighth, Section B(2) authorizes Executors, in the exercise of their

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absolute discretion, to divide any trust being held under the terms of Decedent's will which would otherwise have an inclusion ratio (within the meaning of § 2642(a)) of more than zero into two separate trusts (consisting of fractional shares of the original trust), and to take such other actions as may be required, so that the trust being divided will be treated as two separate trusts for purposes of Chapter 13 of the Internal Revenue Code, one trust having an inclusion ratio of zero and the other having an inclusion ratio of one.

It is represented that Decedent made no generation-skipping transfers during his life, and that Decedent's will provided for no direct skips. It is also represented that none of Decedent's \$1,000,000 GST exemption had been allocated to transfers during Decedent's life, either on a Federal gift tax return or under the automatic allocation rules.

The Executors timely filed the Federal Estate (and Generation-Skipping Transfer) Tax Return, Form 706, for Decedent's estate on Date 2. On Schedule R of the 706, the Executors allocated Decedent's entire unused \$1,000,000 GST exemption to Trust. There was no indication on the return that Trust would be severed. Decedent's return was not selected for audit, and the Executors received a closing letter from the Internal Revenue Service on Date 3.

The Executors request an extension of time under § 301.9100-1 to sever Trust into two separate trusts, a GST exempt trust and a GST nonexempt trust, pursuant to § 26.2654-1(b). Based on representations made, the severed trusts will be funded in conformance with § 26.2654-1(b). The Executors also request a ruling that they substantially complied with the requirements for making an allocation of Decedent's entire GST exemption to the GST exempt trust.

Law and Analysis

Section 26.2601-1(a)(1) imposes a tax on every generation-skipping transfer made after October 22, 1986.

Section 2631(a) of the Internal Revenue Code provides for a GST exemption of \$1,000,000 (adjusted under § 2631(c)), which may be allocated by the individual, or the individual's estate, to any property with respect to which such individual is the transferor.

Under § 2632(a), the allocation of the GST exemption may be made at any time on or before the date prescribed for filing the individual's estate tax return (including extensions), regardless of whether such a return is required to be filed.

Section 2632(b) provides that if any individual makes a direct skip during his lifetime, any unused portion of the individual's GST exemption shall be allocated to the

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property transferred to the extent necessary to make the inclusion ratio for such property zero. If the amount of the direct skip exceeds the unused portion, the entire unused portion shall be allocated to the property transferred. The unused portion of an individual's GST exemption is that portion of such exemption which has not previously been allocated by the individual (or treated as allocated with respect to a direct skip).

Section 2632(c)(1) provides that 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 26.2654-1(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

(A) The terms of each of the new trusts 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 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)(1)(ii) if it were paid to an individual. 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 nonpro rata 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 valuation date to the date of funding.

Section 26.2654-1(b)(2) provides that if a court order severing the trust has not been issued at the time the Federal estate tax return is filed, the executor must indicate

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on a statement attached to the return that a proceeding has been commenced to sever the trust and describe the manner in which the trust is proposed to be severed. A copy of the petition or other instrument used to commence the proceeding must also be attached to the return. If the governing instrument of a trust or local law authorizes the severance of the trust, a severance pursuant to that authorization is treated as meeting the requirement of § 26.2654-1(b)(1)(ii)(B) if the executor indicates on the Federal estate tax return that separate trusts will be created (or funded) and clearly sets forth the manner in which the trust is to be severed and the separate trusts funded.

Under § 301.9100-1(c), the Commissioner of Internal Revenue Service may grant a reasonable extension of the 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 subtitles E, G, H, and I.

Section 301.9100-1 through 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make an election. Section 301.9100-1(a).

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 the evidence to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government. Section 301.9100-3(a).

Based on the facts submitted and representations made in this case, we conclude that the standards of §§ 301.9100-1 and 301.9100-3 have been satisfied. Consequently, an extension of time for severing Trust, pursuant to § 26.2654-1(b)(1), into a GST exempt trust and a GST nonexempt trust is granted until 60 days after the date of this letter.

In addition, although Decedent's federal estate tax return failed to clearly indicate that Decedent's entire GST exemption should be allocated to the GST exempt trust, literal compliance with the procedural instructions to make an election is not always required. Elections may be held to be effective where the taxpayer complied with the essential requirements of a regulation even though the taxpayer failed to comply with certain procedural directions therein. See Hewlett-Packard Company v. Commissioner, 67 T.C. 736, 748 (1977), acq. in result, 1979-1 C.B. 1. The allocation will be deemed valid if there are enough facts and circumstances to indicate that the Executors intended to allocate Decedent's entire GST exemption to the GST exempt trust.

In this case, on Schedule R of Decedent's federal estate tax return, the

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Executors allocated Decedent's entire unused GST exemption to Trust. The Executors failed to clearly indicate that the available GST exemption was intended to be allocated to the GST exempt trust. However, Decedent's will, which was filed with Decedent's federal estate tax return, clearly indicated that any trust which would otherwise have an inclusion ratio of more than zero should be divided into two separate trusts so that the trust being divided will be treated as two separate trusts for purposes of Chapter 13 of the Internal Revenue Code, one trust having an inclusion ratio of zero and the other having an inclusion ratio of one. If Trust is divided into a GST exempt trust and a GST nonexempt trust within 60 days of this letter, we believe that there was sufficient information provided on Decedent's estate tax return to conclude that the Executors substantially complied with the requirements for making an allocation of GST exemption for the transfer to the GST exempt trust. The Executors, therefore, are deemed to have allocated Decedent's entire GST exemption to the GST exempt trust.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the executors of Decedent's estate.

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

Enclosures (2)
Copy of letter
Copy for section 6110 purposes
cc: