

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:B09-PLR-113024-01

Date:

September 27, 2001

LEGEND:

Donor =

Date 1 =

Spouse =

Trust =

Grandchild 1 =

Grandchild 2 =

Date 2 =

Grandchild 3 =

Grandchild 4 =

Child =

Year 1 =

\$a =

Year 2 =

\$b =

Year 3 =

\$c =

Year 4 =

\$d =

Dear :

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This letter is in response to your authorized representative's letter, dated February 26, 2001, requesting a ruling regarding the automatic allocation of Donor's generation-skipping transfer (GST) exemption, pursuant to § 2632 of the Internal Revenue Code. This letter responds to that request.

The facts and representations submitted are summarized as follows: On Date 1, Spouse established Trust, an irrevocable trust, for the benefit of Spouse's grandchildren other than Grandchild 1 and Grandchild 2.

Article II, Paragraph A.1. of Trust provides that if at (i) any time any contribution is made to any trust hereunder, or (ii) any payment is made of premiums for policies of life insurance held in trust hereunder, with respect to which addition or payment the trustee has received written notice from the grantor or other transferor of such addition to the trust to the effect that such addition, payment, or some specified portion thereof shall be subject to withdrawal under the provisions of this section by the beneficiary of this trust, then notwithstanding any other provision hereof, such thus designated beneficiary shall thereupon have the absolute right, at all times during the two month period commencing on the date of such addition or payment, to withdraw from this trust, in cash or in kind as determined by the trustee, that portion or all of the value of such contribution or payment determined in the same manner as such value would be determined for the transferor's or transferors' federal gift tax purposes, which is specified as withdrawable by such beneficiary in such notice. The total value which may be withdrawn by any beneficiary on account of such additions or payments hereunder shall not be cumulative, and, to the extent that such a withdrawal right has not been exercised by the end of such two month period, it shall lapse.

Article II, Paragraph A.2. of Trust provides that each such withdrawal right shall be exercisable only by a written instrument executed by the beneficiary having such right and delivered to the trustee of the trust involved on or before the date specified in such instrument as the effective date of such withdrawal, which must be during the above specified withdrawal period. If any such beneficiary is then under any legal disability of any kind, execution of such instrument may be by his or her legal guardian, or, if no guardian has been appointed, by his or her natural guardian other than the donor of such gift or the grantor, in each case acting solely on behalf of such beneficiary in making such withdrawal and receiving such distribution for such beneficiary's sole benefit. Distribution of the thus withdrawn value pursuant to any proper instrument of withdrawal shall be made on such effective date. To this end, the trustee shall, at all times while any such withdrawal right is outstanding, retain in the trust sufficient borrowable or transferable assets, from such addition or otherwise, to satisfy all such withdrawal rights then outstanding. Each beneficiary designated as having a withdrawal right with respect to any addition or additions, or, if he or she is then under legal disability, his or her legal guardian, or, if there is none, his or her natural guardian, shall be kept reasonably informed by the trustee of all withdrawable additions that are made or expected to be made.

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Article II, Paragraph B.1. of Trust provides that until the first to occur of (i) the death of the survivor of the grantor and his wife, or (ii) Date 2, the trustee shall pay to, or use for the benefit of, any one or more of the grantor's grandchildren other than Grandchild 1 and Grandchild 2, so much of the net income and principal of this trust as the trustee determines to be in their best interests (taking into account their respective incomes from all sources known to the trustee), for their education (including college, post-graduate, and professional education), health, maintenance, and support in reasonable comfort, adding any excess income to principal at the trustee's discretion. The trustee may, in its discretion, pay the same to or use it for the benefit of one or more of the grantor's grandchildren other than Grandchild 1 and Grandchild 2, to the exclusion of one or more of them, and may completely exhaust the principal, the grantor's concern being primarily for the health, maintenance, comfortable support, and education of the beneficiaries.

Article II, Paragraph B.2. of Trust provides that upon the first to occur of (i) the death of the survivor of the grantor and his wife, or (ii) Date 2, the trustee shall divide the trust estate, as then constituted, into separate equal shares so that there shall be one share for each then living grandchild of the grantor other than Grandchild 1 and Grandchild 2, or, if there is no living grandchild of the grantor other than Grandchild 1 and Grandchild 2, the trustee shall divide the trust into separate shares for the then living descendants of the grantor, per stirpes. The trustee shall distribute each share set aside for a great-grandchild or more remote descendant of the grantor to such descendant. The trustee shall hold each share set aside for a child or grandchild of the grantor, hereinafter referred to as a beneficiary, upon the following trusts: (a) The trustee shall pay to each beneficiary or use for his or her benefit all the net income from his or her trust, in convenient installments at least as often as quarter-annually during his or her life, subject, however, to the limitations set forth in subparagraph d. of this subparagraph 2., adding any excess income to principal in the trustee's discretion. (b) Whenever the trustee determines that the income of the beneficiary, from all sources known to the trustee, is not sufficient for the support of the beneficiary, for the beneficiary's maintenance in reasonable comfort, for his or her health, and for his or her education (including, but not limited to, college, post-graduate, and professional education), the trustee may, in its discretion, pay to or use for the benefit of the beneficiary so much of the principal of his or her trust as the trustee determines to be reasonably required therefor, subject, however, to the limitations set forth in subparagraph d. of this subparagraph 2. (c) Upon the death of the beneficiary, the trustee shall distribute his or her trust estate, as then constituted, to, or in trust for the benefit of, such person or persons (other than the said beneficiary) among the grantor's descendants, upon such conditions and estates, with such powers, in such manner, and at such time or times as the said beneficiary may appoint or direct by will specifically referring to this power of appointment, and, to the extent that the beneficiary does not effectively exercise this power of appointment, the trustee shall distribute the trust estate, as then constituted, to the then living descendants of the beneficiary, per stirpes, or, if the beneficiary has no then living descendants, the trustee shall divide his or her trust estate, as then constituted, into separate equal shares so that there is one

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share set aside for each living grandchild of the grantor for whom there is then a trust held hereunder, and the trustee shall add each such share to the trust for the grandchild for whom it was set aside, to be held and administered as if it had been an original part thereof, or if there is no trust then held for a living grandchild of the grantor, the trustee shall divide the trust estate, as then constituted, into separate shares for the then living descendants of the grantor, per stirpes. The trustee shall distribute each share set aside for a great-grandchild or more remote descendant of the grantor to such descendant. The trustee shall hold each share set aside for a child or grandchild of the grantor, herein referred to as a beneficiary, upon the trusts set forth in subparagraphs a., b., c., and d. of this subparagraph 2. of this paragraph B.

From the establishment of Trust on Date 1, until Date 2, Grandchild 3 and Grandchild 4 have been the sole beneficiaries of Trust. On Date 2, two successor trusts were created, pursuant to Article II of Trust. Grandchild 3 is the sole beneficiary of one of the successor trusts and Grandchild 4 is the sole beneficiary of the other successor trust. All assets from Trust were distributed to these successor trusts. Child, the mother of Grandchild 3 and Grandchild 4, has been alive since Trust was first established on Date 1.

During Year 1, Donor transferred \$a to Trust. During Year 1, Spouse also transferred \$a to Trust. Donor and Spouse timely reported these gifts on their respective Forms 709, United States Gift (and Generation-Skipping Transfer) Tax Return. Donor and Spouse each consented to have the gifts made by one another to third parties during the calendar year considered as made one-half by each of them under § 2513. On Donor's Year 1 gift tax return and Spouse's Year 1 gift tax return, the transfers to Trust were entered on Schedule A, Part 1 as gifts subject only to gift tax.

During Year 2, Spouse transferred cash and marketable securities with an aggregate value of \$b to Trust. Spouse timely reported this gift on his Form 709. Donor and Spouse consented to have the gifts made by one another to third parties during the calendar year considered as made one-half by each of them. On Spouse's Year 2 gift tax return, the transfer to Trust was entered on Schedule A, Part 1 as a gift subject only to gift tax. Donor did not make any transfers to Trust during Year 2. On Donor's Year 2 gift tax return, Donor included one-half of the total value of gifts of made by Spouse.

In Year 3, Spouse transferred \$c to Trust. Spouse timely reported this gift on Form 709-A, United States Short Form Gift Tax Return. Donor consented to have the gifts made by Spouse and herself to third parties during the calendar year considered as made one-half by each of them. Donor did not make any transfers to Trust during Year 3.

In Year 4, Spouse transferred cash and marketable securities with an aggregate value of \$d to Trust. Spouse timely reported this gift on Form 709-A. Donor consented to have the gifts made by Spouse and herself to third parties during the calendar year

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considered as made one-half by each of them. Donor did not make any transfers to Trust during Year 4.

On Donor's gift tax returns for Year 1 and Year 2, Donor did not allocate any of her available GST exemption to Trust. Donor did not file gift tax returns for Year 3 or Year 4 because she consented to split Spouse's gifts on Spouse's Form 709-A. In addition, Donor did not pay any GST tax with respect to the gifts to Trust.

A ruling has been requested that an automatic allocation of Donor's GST exemption, pursuant to § 2632(b)(1), occurred with respect to the gifts made to Trust in each of the taxable years Year 1, Year 2, Year 3, and Year 4.

Section 2601 imposes a tax on every generation-skipping transfer (GST).

Section 2611(a) provides that the term "generation-skipping transfer" means (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 2612(c)(1) provides that the term "direct skip" means a transfer subject to a tax imposed by chapter 11 (the estate tax) or chapter 12 (the gift tax) of an interest in property to a skip person.

Section 2613(a)(1) provides that the term "skip person" means (1) a natural person assigned to a generation which is 2 or more generations below the generation assignment of the transferor, or (2) a trust if all interests in such trust are held by skip persons, or if there is no person holding an interest in such trust and at no time after such transfer may a distribution (including distributions on termination) be made from such trust to a non-skip person.

Section 2631(a) provides 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.

Section 2632(b)(1) provides, generally, that if any individual makes a direct skip during his lifetime, any unused portion of such individual's GST exemption shall be allocated to the property transferred to the extent necessary to make the inclusion ratio for such property zero. If the amount of the direct skip exceeds such unused portion, the entire unused portion shall be allocated to the property transferred.

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Section 2632(b)(2) provides that for purposes of paragraph (1), the unused portion of an individual's GST exemption is that portion of such exemption which has not previously been allocated by such individual (or treated as allocated under paragraph (1) with respect to a direct skip).

Section 2632(b)(3) provides that an individual may elect to have the deemed allocation under § 2632(b) not apply to a transfer.

Section 2652(a)(1) provides that, except as provided in this subsection or § 2653(a), the term "transferor" means (A) in the case of any property subject to the tax imposed by chapter 11 (the estate tax), the decedent, and (B) in the case of any property subject to the tax imposed by chapter 12 (the gift tax), the donor. An individual shall be treated as transferring any property with respect to which such individual is the transferor.

Section 2652(a)(2) provides that if, under § 2513, one-half of the gift is treated as made by an individual and one-half is treated as made by that individual's spouse, then for purposes of the GST tax, each spouse is treated as the transferor of one-half of the entire value of the property transferred by the donor spouse.

Section 2652(c)(1) provides, in part, that a person has an interest in property held in trust if (at the time the determination is made) such person has a right to receive income or corpus from the trust, or is a permissible current recipient of income or corpus from the trust and is not described in § 2055(a).

Section 26.2632-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provides, generally, that if a direct skip occurs during the transferor's lifetime, the transferor's GST exemption not previously allocated (unused GST exemption) is automatically allocated to the transferred property (but not in excess of the fair market value of the property on the date of the transfer). The transferor may prevent the automatic allocation of GST exemption by describing on a timely-filed United States Gift (and Generation-Skipping Transfer) Tax Return (Form 709) the transfer and the extent to which the automatic allocation is not to apply. In addition, a timely-filed Form 709 accompanied by payment of the GST tax (as shown on the return with respect to the direct skip) is sufficient to prevent an automatic allocation of GST exemption with respect to the transferred property.

Section 26.2632-1(b)(1)(ii) provides that a Form 709 is timely filed if it is filed on or before the date required for reporting the transfer if it were a taxable gift (i.e., the date prescribed by § 6075(b), including any extensions to file actually granted (the due date)). Except as provided in paragraph (b)(1)(iii) of this section, the automatic allocation of GST exemption (or the election to prevent the allocation, if made) is irrevocable after the due date. An automatic allocation of GST exemption is effective as of the date of the transfer to which it relates. Except as provided above, a Form 709 need not be filed to report an automatic allocation.

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In the present case, because all interests in Trust are held by skip persons, Trust qualifies as a skip person under § 2613(a). Because Donor and Spouse consented to split the gifts under § 2513, Donor is treated as the transferor of one-half of all gifts made to Trust under § 2652(a)(2). The transfers that Donor is treated as making to Trust were direct skips as defined in § 2612(c)(1).

Based on the information submitted and the representations made, we conclude that an automatic allocation of Donor's unused GST exemption occurred under § 2632(b)(1) with respect to the gifts that Donor is treated as making to Trust in Year 1, Year 2, Year 3, and Year 4. An automatic allocation of GST exemption is effective as of the date of the transfer to which it relates. We are expressing no opinion regarding the value of the property transferred to Trust or regarding the inclusion ratio of Trust.

The ruling contained in this letter is 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 specifically ruled herein, we express or imply 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 requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file, we are sending a copy of this letter to your authorized representatives.

Sincerely,
Frances Schafer
Counsel to the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures

Copy for section 6110 purposes