

**Internal Revenue Service**

**Department of the Treasury**

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                  2652.01-02  
                  2654.03-00

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**Person to Contact:**

**Telephone Number:**

**Refer Reply To:  
CC:PSI:4/PLR-104206-00  
Date:  
September 18, 2000**

Re:

Legend:

- Decedent =
- Spouse =
- Son =
- State =
- QTIP Trust =
  
- Family Trust =
  
- Reverse QTIP Trust =
  
- State Statute =
- Date 1 =
- Date 2 =
- Date 3 =
- Date 4 =

Dear                   :

This is in response to your submission dated September 6, 2000, and prior correspondence in which you requested an extension of time under § 301.9100-1 of the Procedure and Administration Regulations to sever a trust into two trusts under § 26.2654-1(b) of the Generation Skipping Transfer (GST) Tax Regulations and to make a reverse qualified terminable interest property (QTIP) election under § 2652(a)(3) of the Internal Revenue Code.

Decedent died testate on Date 1 survived by Spouse. Decedent's will was executed on Date 2. Article Second of Decedent's will provides for the creation of a marital trust (QTIP Trust) to be funded with the minimum amount that, if bequeathed outright to Spouse, would have the effect of reducing the federal estate tax payable with respect to Decedent's estate to the lowest possible amount, after giving effect to the federal unified credit.

Article Second provides that during her life, Spouse is to receive all of the net income from the QTIP Trust, at least quarterly. In addition, the trustee may distribute to Spouse all or part of the principal of the trust as the trustees may determine for health, maintenance and support. Upon Spouse's death, the remaining principal of the QTIP Trust will be distributed to such one or more of Decedent's descendants as Spouse appoints by will.

Article Third of the will provides for a "Family Trust" to be funded with the residue of the estate. Under Article Third, the trustees are to pay any part or all of the principal and income of the Family Trust to any one or more members of a class consisting of Spouse, Decedent's child (Son), Son's wife and Son's descendants for health, support, maintenance and education. Upon Spouse's death, the remaining principal of the Family Trust is to be distributed to one or more of Decedent's descendants as Spouse may appoint by will.

Article Fourth of the will provides that to the extent the remaining corpus of the QTIP Trust and Family Trust are not effectively appointed by Spouse, and if Son survives Spouse, the trustees are to distribute to a separate trust "the maximum amount that can pass at my son's death to his descendants without the imposition of federal generation-skipping or other transfer tax." The trustees may pay income and principal to Son, Son's spouse and Son's descendants for their health, support, maintenance or education. At Son's death, Son may appoint the remaining principal in accordance with a special power of appointment. Any principal not effectively appointed, will be distributed to Son's descendants per stirpes.

On Schedule M of Form 706, (timely filed by the estate), the estate elected to treat the QTIP Trust as qualified terminable interest property under § 2056(b)(7). On Schedule R, as filed, the estate reported Decedent's GST exemption available for allocation as \$1,000,000. However on Line 9, the estate failed to allocate Decedent's GST exemption.

On Date 3, pursuant to State Statute, the executor of Decedent's estate divided the QTIP Trust by creating and funding a second trust denominated the "Reverse QTIP Trust." The Reverse QTIP Trust was funded in an amount equal to the difference between Decedent's unused GST tax exemption and the amount passing to the Family Trust.

On Date 4, the estate filed a Schedule R, signifying that a reverse QTIP election under § 2652(a)(3) was being made with respect to the Reverse QTIP Trust.

Decedent's estate requests an extension of time under § 301.9100 to divide the QTIP Trust and make the reverse QTIP election under § 2652(a)(3) with respect to the Reverse QTIP Trust. In addition, the executor requests the following rulings:

1. The QTIP Trust and the Reverse QTIP Trust will be recognized as separate trusts for federal generation-skipping transfer tax purposes.

2. Under the automatic allocation rules contained in § 2632(c)(1), Decedent's GST exemption under § 2631 is allocated pro rata between the Family Trust (credit shelter trust) and the Reverse QTIP Trust.

3. The Reverse QTIP Trust and the Family Trust will each have an inclusion ratio of zero under § 2642.

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, the entire 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" (QTIP) 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, property subject to a QTIP election is includible in the gross estate of the surviving spouse.

Section 2601 imposes a tax on every generation-skipping transfer made by a "transferor" (defined in § 2652) to a skip person.

Under § 2602, the amount of the tax imposed under § 2601 is equal to the taxable amount multiplied by the applicable rate. The applicable rate is defined in § 2641 as the maximum federal estate tax rate multiplied by the inclusion ratio with respect to the transfer. Under § 2642(a), in general, the inclusion ratio with respect to any property subject to a generation-skipping transfer is the excess of one over the applicable fraction determined for the trust from which the transfer is made. The applicable fraction with respect to a trust is a fraction, the numerator of which is the amount of GST exemption under § 2631 allocated to the trust, and the denominator of which is the value of the trust property, with certain specified adjustments.

Section 2631 provides that for purposes of determining the inclusion ratio, every individual is allowed a GST exemption of \$1,000,000 that the individual (or his executor) may allocate to any property of which the individual is the transferor. Any allocation, once made, is irrevocable.

Under § 2632(a), the allocation may be made at any time on or before the date prescribed for filing the individual's estate tax return (including extensions). Under § 2632(c), any portion of an individual's GST exemption not allocated within the time prescribed in § 2632(a), is allocated in accordance with that section.

Under § 2632(c) and § 26.2632-1(d)(2), a decedent's unused GST exemption is automatically allocated on the due date for filing the federal estate tax return to the extent not otherwise allocated by the decedent's executor on or before that date. Unused GST exemption is allocated pro rata (subject to the rules of § 26.2642-2(b)), on the basis of the value of the property as finally determined for federal estate tax purposes, first to direct skips treated as occurring at the transferor's death. Any balance is allocated pro rata (subject to the rules of § 26.2642-2(b)), on the basis of the value of the property as finally determined for federal estate tax purposes, to trusts with respect to a which a taxable termination may occur or from which a taxable distribution may be made. The automatic allocation is irrevocable. 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 generation-skipping transfer with respect to the trust.

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 determining the inclusion ratio with respect to that property shall be its value for federal estate tax purposes; except that, if the requirements in the regulations respecting allocation of post-death changes in value are not met, the value of such property shall be determined as of the time of the distribution concerned.

In general, under § 26.2652-1(a)(1) the transferor for GST tax purposes is the individual with respect to whom the property was most recently subject to Federal estate and gift tax.

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 GST tax, 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 GST tax purposes, the transferor of the QTIP trust for which the election is made. As a result, the decedent's GST tax exemption may be allocated to the QTIP trust.

Section 26.2652-2(a) provides that a reverse QTIP election is not effective unless it is made for all of the property in the trust to which the QTIP election applies.

Under § 26.2654-1(b)(1)(ii), 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 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 of time actually granted) for the transferor's estate, and (C) 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 nonpro rata basis provided they are funded 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), 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 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 301.9100-1 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 establish 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 and representations submitted with your request, we have determined that good cause has been shown and the other requirements of §§ 301.9100-1 and 301.9100-3 have been satisfied. Therefore, an extension of time to divide the QTIP Trust is granted until Date 3 and an extension of time to make the reverse QTIP election with respect to the Reverse QTIP Trust is granted until Date 4.

The extension of time for making a "reverse" QTIP election under § 2652(a)(3) does not extend the time for making the allocation of any remaining GST tax

exemption. In this case, the executor of Decedent's estate made no allocation on the estate tax return filed for the estate. Thus, the balance of Decedent's GST tax exemption, as of the date of Decedent's death, is subject to allocation based on the deemed allocation rules contained in § 2632(c).

Further based on the facts presented and the representations made, we conclude as follows:

1. The QTIP Trust and the Reverse QTIP Trust will be recognized as separate trusts for federal generation-skipping transfer tax purposes.
2. Under the automatic allocation rules contained in § 2632(c)(1), Decedent's GST exemption under § 2631 is allocated as prescribed in § 2632(c)(2) and § 26.2632-1(d)(2) between the Reverse QTIP Trust and the Family Trust.
3. The Reverse QTIP Trust and the Family Trust will each have an inclusion ratio of zero under § 2642, if funded as represented and in accordance with § 26.2654-1(b)(1)(ii)(C).

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) 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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