



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE LEGAL ADVICE

MEMORANDUM FOR

FROM:

SUBJECT:

This Chief Counsel Advice responds to your request for advice per our conversation on June 21, 2002. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Spouse =
Decedent =
Trust =
Corporations =

\$W =
\$X =
Date 1 =
\$Y =
Date 2 =
\$Z =

ISSUE

Whether the estate may adjust the amount of the marital deduction for qualified terminable interest property (QTIP) after a Form 706 has been filed, to accurately reflect the value of property properly passing to the marital trust as determined under the provisions of Article Four, paragraphs 4.7 and 4.9 of Trust.

CONCLUSION

Decedent's estate made a valid election under § 2056(b)(7) of the Internal Revenue Code to treat 100 percent of the marital trust as QTIP. Although the estate incorrectly stated the value of the property subject to the QTIP election, this does not affect the validity of the election, or the amount properly passing to the marital trust under the terms of the governing instrument. Therefore, a deduction under § 2056(b)(7) should be allowed for the value of the property properly passing to the marital trust as determined under the provisions of Article Four, paragraphs 4.7 and 4.9 of Trust.

FACTS

The facts stated herein are limited to the facts and representations submitted and represented by Spouse.

Under the terms of Decedent's will, after providing for certain bequests of personalty to Spouse, the residue of the estate passed to Trust.

Article Four, paragraph 4.2 of Trust directs the trustee, upon Decedent's death, to divide the trust estate into three separate trusts, designated the survivor's trust, the exemption trust, and the marital trust.

Under Article Four, paragraphs 4.3, 4.4, and 4.5, the survivor's trust will include the surviving spouse's interest in community property, surviving spouse's separate estate, property which constitutes "all income in respect of a decedent", and the deceased spouse's interest in shares of stock of Corporations. Pursuant to the terms of the survivor's trust, the surviving spouse is to be paid as much income of the survivor's trust as she demands, and as much principal as is necessary in the trustee's discretion for surviving spouse's health, education, support, maintenance, comfort, and welfare. The surviving spouse has an absolute intervivos and testamentary power to appoint any part of the principal and any undistributed net income of the survivor's trust.

Under Article Four, paragraph 4.6, the exemption trust will consist of a pecuniary amount equal to the maximum sum that can be allocated to a trust that does not qualify for the federal estate tax marital deduction, without producing any

federal estate tax, and the net value of all other property included in the gross estate of the deceased spouse that does not qualify for the federal estate tax marital deduction. The trustee has the power to pay to or apply for the benefit of the surviving spouse such sums out of the income and principal of the exemption trust as the trustee, in the trustee's discretion, deems necessary for the surviving spouse's health, maintenance, support, or education.

Under Article Four, paragraph 4.7, the marital trust will consist of the balance of the estate. Article Four, paragraph 4.9 further provides that assets qualifying for the federal estate tax marital deduction will be transferred to the marital trust only to the extent the transfer would reduce the amount of federal estate tax payable by reason of the deceased spouse's death. Under the terms of the marital trust, the trustee will pay to the surviving spouse the net income of the marital trust in quarter-annual or more frequent installments. The trustee has the power to pay to or apply for the benefit of the surviving spouse such sums out of principal as the trustee, in the trustee's discretion, deems necessary for the surviving spouse's health, maintenance, support, or education.

Under Article Five, paragraph 5.11, on the death of the surviving spouse, the balance of the marital trust is to be added to the exemption trust, to follow the disposition of the exemption trust. Article Five, paragraph 5.14 provides that on the surviving spouse's death, the trustee will distribute the exemption trust to the Decedent's issue, by right of representation.

Decedent's United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706), showing a taxable estate of \$W and an estate tax due of \$X, was filed on Date 1. On Schedule M of the return, the estate's accountant made a QTIP election for the "Share of Residue Before Federal and State Taxes", in the nominal amount of \$Y. This residue was comprised of Trust, and thus the three trusts contained therein. Because only the marital trust qualified as QTIP, this election could have only been valid for the marital trust. Spouse subsequently discovered that the amount of the Date 1 QTIP election was incorrect. As a result, on Date 2, the estate's accountant filed a "SUPPLEMENTAL INFORMATION" Form 706 changing the value of the QTIP election made for the "Share of Residue Before Federal and State Taxes" to \$Z, reducing the taxable estate to zero. However, the amount of the QTIP election stated on the supplemental form was also incorrect.

LAW AND ANALYSIS

Section 2001(a) provides that a tax is imposed 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 the value of a decedent's 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)(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 passing to the surviving spouse will terminate or fail.

Section 2056(b)(7) provides an exception to the terminable interest rule in the case of qualified terminable interest property. For purposes of § 2056(b)(7), the term "property" generally means an entire interest in property or a specific portion of the entire interest.

Section 2056(b)(7)(A) provides that qualified terminable interest property shall be treated as passing to the surviving spouse and no part of such property shall be treated as passing to any person other than the surviving spouse. Thus, the value of such property is deductible from the value of the gross estate under section 2056(a).

Section 2056(b)(7)(B)(i) defines the term "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 section 2056(b)(7)(B)(v) applies.

Section 2056(b)(7)(B)(ii) and the regulations thereunder provide that the surviving spouse will be considered to have a qualifying income interest for life if: (1) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, and (2) no person, including the surviving spouse, has a power to appoint any part of the property to any person other than the surviving spouse during the surviving spouse's lifetime.

Section 2056(b)(7)(B)(v) provides that an election under section 2056(b)(7) with respect to any property is to be made by the executor on the return of tax imposed by section 2001. The election, once made, is irrevocable.

Section 20.2056(b)-7(b)(4)(i) of the Estate Tax Regulations provides that the election referred to in section 2056(b)(7)(B)(v) is made on the return of tax imposed by section 2001. For purposes of section 20.2056(b)-7(b)(4)(i), the term "return of tax imposed by section 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.

Section 20.2056(b)-7(b)(4)(ii) provides that an election, once made is irrevocable, provided that an election may be revoked or modified on a subsequent return filed on or before the due date of the return, including extensions actually granted. If an executor appointed under local laws has made an election on the return of tax imposed by section 2001 (or section 2101) with respect to one or more properties, no subsequent election may be made with respect to other properties included in the gross estate after the return of tax imposed by section 2001 is filed.

In the instant case, the estate's accountant made a valid QTIP election on the Form 706 filed on Date 1. The accountant, however, incorrectly reported that a QTIP deduction was being claimed for all of the Trust's assets, and also incorrectly reported a nominal deduction value of \$Y.

Pursuant to Decedent's will, the residue of his estate is to pass to Trust and then divided into three separate trusts. The only trust that qualifies as QTIP is the marital trust. Although the QTIP election on the Form 706 included the spouse's interests in all three trusts, this reporting does not affect the validity of the election, or the amount properly passing to the marital trust under the terms of the governing instrument. As a result, the assets included in the residue that did not pass to the marital trust under the terms of the governing instrument are not subject to the QTIP election. We believe, however, that the descriptive statement on Schedule M adequately identifies the property interest, for which the election is being made, to include the entire marital trust.

Accordingly, the estate should be allowed to adjust the amount of the marital deduction for QTIP to correctly state the value of the assets properly passing to the marital trust as determined under the provisions of Article Four, paragraphs 4.7 and 4.9 of Trust.

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

Please call (202) 622-7830 if you have any further questions.

Acting Associate Chief Counsel
(Passthroughs and Special Industries)

By: MELISSA C. LIQUERMAN
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