

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:9-PLR-116440-03

Date:

Jul 10 2003

In Re:

LEGEND:

Taxpayer =

Trust =

Trust 1 =

Trust 2 =

Spouse =

Child 1 =

Child 2 =

Accounting Firm =

Accountant =

Attorney =

State =

State Statute =

Date 1 =

Date 2 =

Year 1 =

Year 2 =

a =

Dear :

This is in response to your letter dated March 5, 2003, and subsequent correspondence, in which you requested rulings on behalf of the Taxpayer concerning an extension of time pursuant to § 2642(g) of the Internal Revenue Code and § 301.9100-3 of the Procedure and Administration Regulations to make an allocation of the Taxpayer's generation-skipping transfer (GST) exemption to a transfer to an

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irrevocable trust, and the GST tax consequences of the severance of the trust pursuant to § 2642(a)(3) into two separate trusts.

A summary of the facts and representations submitted is as follows: On Date 1, Taxpayer created Trust for the benefit of Taxpayer's issue (Child 1, Child 2, and their issue).

Article First of the Trust Agreement provides that the trustees may make discretionary distributions of income and principal (even to the extent of the whole thereof) to one or more of Taxpayer's issue. There is no requirement to equalize payments among beneficiaries. Income not distributed is to be accumulated and added to principal. The Trust will terminate 21 years after the death of the last to survive of all of the Taxpayer's issue living on Date 1. Upon termination, the principal is to be distributed to the Taxpayer's then living issue, in equal shares, per stirpes.

Article Fifth of the Trust Agreement provides that State law governs the Trust.

On Date 1, in Year 1, Taxpayer transferred \$a to the Trust. Taxpayer's spouse (Spouse) elected, on Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return, to treat this gift, as well as other gifts made by Taxpayer during the year, as made one-half by each spouse pursuant to § 2513. Taxpayer and Spouse retained Accounting Firm to prepare their gift tax returns for Year 1. Accountant at Accounting Firm, in preparing the returns, inadvertently failed to allocate Taxpayer's GST exemption to the Date 1 transfer to the Trust.

On Date 2, as authorized by State Statute, the trustees of the Trust divided the Trust into two separate trusts, one for the benefit of Child 1 and his issue (Trust 1), and one for the benefit of Child 2 and her issue (Trust 2). The assets of the original Trust were equally divided between Trust 1 and Trust 2. Trust 1 and Trust 2 contain the same provisions as the original Trust, except for Article First. Article First of each new trust provides the trustees with the complete discretion to distribute income and principal to or for the benefit of the child for whom the trust is named and that child's issue. There is no requirement to equalize payments among beneficiaries. Income not distributed is to be added to principal. Trust 1 and Trust 2 will terminate on the earlier of (i) the death of the child for whom the trust is named and all of his or her issue or (ii) 21 years after the death of the survivor of all of the Taxpayer's issue living on Date 1. At termination, the assets of Trust 1 will be distributed to the issue of Child 1, per stirpes, and the assets of Trust 2 will be distributed to the issue of Child 2, per stirpes. If either child dies without issue, the assets of his or her trust will be distributed to his or her sibling's trust for the benefit of that sibling and his or her issue.

In Year 2, Taxpayer's Attorney received a copy of Taxpayer's gift tax return for Year 1 and discovered that his GST exemption had not been allocated to his gift to the Trust on Date 1. Taxpayer represents that he has sufficient remaining GST exemption

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available to apply to the Date 1 gift to the Trust, and that there have been no distributions to skip persons from the Trust and no additions, actual or constructive, to the Trust since Date 1.

Taxpayer requests the following rulings:

(1) that an extension of time be granted under §§ 2642(g)(1) and 301.9100-3 to allocate his GST exemption to the Date 1 transfer to the Trust, and that such allocation will be based on the value of the property transferred to the Trust on Date 1; and

(2) that the division of the Trust into two separate trusts will not affect the allocation of his GST exemption to the Trust and that each new trust will have an inclusion ratio of zero so that distributions from each new trust will not be subject to GST tax.

Ruling Request 1

Section 2601 imposes a tax on every generation-skipping transfer (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 is the taxable amount multiplied by the applicable rate. Section 2641(a) defines “applicable rate” as the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer. Section 2642(a) provides the method for determining the inclusion ratio.

Section 2631(a) provides that for purposes of determining the inclusion ratio, every individual shall be allowed a GST exemption of \$1,000,000 (adjusted for inflation under § 2631(c)) 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) 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 26.2632-1(b)(2) of the Generation-Skipping Transfer Tax Regulations provides that an allocation of GST exemption to property transferred during the transferor’s

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lifetime, other than in a direct skip, is made on Form 709.

As applicable to transfers made in Year 1, § 2642(b)(1) provided, in relevant part, that if the allocation of the GST exemption to any transfers of property is made on a timely filed gift tax return or is deemed to be made under § 2632(b)(1) [deemed allocations to certain lifetime direct skips] –

(A) the value of such property for purposes of determining the inclusion ratio shall be its value for purposes of chapter 12, and

(B) such allocation shall be effective on and after the date of such transfer.

Section 2642(g)(1)(A) provides 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 § 2642(b)(1). 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, 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, the time for making the allocation shall be treated as if not expressly prescribed by statute.

Notice 2001-50, 2001-34, I.R.B. 189, provides that under § 2642(g)(1)(B), the time for allocating the GST exemption to lifetime transfers and transfers at death, the time for electing out of the automatic allocation rules, and the time for electing to treat any trust as a generation-skipping transfer trust are 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)(1) or (b)(2) or an election described in § 2632(b)(3) or (c)(5) under the provisions of § 301.9100-3.

Section 301.9100-1(c) provides that 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 301.9100-3 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). Under § 301.9100-1(b), a regulatory election includes an election whose due date is prescribed by a notice published in the Internal Revenue Bulletin. In accordance with § 2642(g)(1)(B) and Notice 2001-50, taxpayers may seek an extension of time to make an allocation described in § 2642(b)(1) or (b)(2)

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or an election described in § 2632(b)(3) or (c)(5) under the provisions of § 301.9100-3.

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 that granting 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.

Based on the facts submitted and the representations made, we conclude that the requirements of § 301.9100-3 have been satisfied. Therefore, Taxpayer is granted an extension of time of 60 days from the date of this letter to make an allocation of his available GST exemption to the transfer to the Trust on Date 1. The allocation will be effective as of the date of the transfer to the Trust and will be made based on the value of the property transferred to the Trust as of the date of the transfer.

The allocation should be made on a Supplemental Form 709 and filed with the Internal Revenue Service Center, Cincinnati, Ohio 45999. A copy of this letter should be attached to the form. A copy is attached for this purpose.

Ruling Request 2

Section 2642(a)(3)(A) provides that if a trust is severed in a “qualified severance,” the trusts resulting from such severance shall be treated as separate trusts thereafter for purposes of chapter 13.

Section 2642(a)(3)(B) provides that the term “qualified severance” means the division of a single trust and the creation (by any means available under the governing instrument or under local law) of two or more trusts if -- (i) the single trust was divided on a fractional basis, and (ii) the terms of the new trusts, in the aggregate, provide for the same succession of interests of beneficiaries as are provided in the original trust.

Section 2642(a)(3)(C) provides that a severance may be made at any time.

In this case, the Trust was severed into two separate trusts in accordance with the provisions of State Statute. It is represented that the Trust’s assets were divided on a fractional basis between the two separate trusts. Under the terms of the original Trust, the trustees had discretion to distribute income and principal to Child 1, Child 2, and their issue. Following the severance of the Trust, the trustees of Trust 1 have the discretion to distribute income and principal to Child 1 and his issue, and the trustees of Trust 2 have the discretion to distribute income and principal to Child 2 and her issue. Under its terms, the original Trust was to terminate 21 years after the death of the last to survive of all of Taxpayer’s issue living on Date 1 and, upon termination, the corpus

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was to be distributed to Taxpayer's issue in equal shares per stirpes. Under their terms, Trust 1 and Trust 2 will terminate 21 years after the death of the last to survive of all of the Taxpayer's issue living on Date 1, or upon the earlier death of a child and all of his or her issue. In the event a child and all of his or her issue die prior to the 21-year measuring period, the corpus of his or her trust will be distributed to his or her sibling's trust for the benefit of that sibling and his or her issue. In all other respects the terms of Trust 1 and Trust 2 are identical to the terms of the original Trust. Thus, the terms of Trust 1 and Trust 2, in the aggregate, provide for the same succession of interests of beneficiaries as are provided in the original Trust.

Accordingly, based upon the facts submitted and the representations made, we conclude that the division of Trust into Trust 1 and Trust 2 is a "qualified severance" within the meaning § 2642(a)(3). Trust 1 and Trust 2 will each have an inclusion ratio of zero, provided the amount of GST exemption allocated to Trust is equal to the value of the property transferred to Trust for federal gift tax purposes.

The rulings contained in this letter are based upon information and representations submitted by 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.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to the Taxpayer.

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

Sincerely,

Heather C. Maloy
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures: Copy for § 6110 purposes
One copy of this letter

cc: