

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4 - PLR-113077-03

Date:

OCTOBER 24, 2003

Re:

LEGEND:

Decedent	-
Trust	-
Trustee	-
Daughter	-
Son	-
Granddaughter	-
Grandson	-
Date 1	-
Date 2	-
Year 1	-
Year 2	-
Year 3	-
Year 4	-
Year 5	-
Year 6	-
Year 7	-
Year 8	-
Year 9	-
Year 10	-
<u>a</u> dollars	-
<u>b</u> dollars	-
<u>c</u> dollars	-
<u>d</u> dollars	-
<u>e</u> dollars	-
<u>f</u> dollars	-
<u>g</u> dollars	-

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Attorney	-
CPA Firm	-
<u>h</u> dollars	-
<u>i</u> dollars	-
<u>j</u> dollars	-
<u>k</u> dollars	-
<u>l</u> dollars	-
<u>m</u> dollars	-
<u>n</u> dollars	-
<u>o</u> dollars	-
<u>p</u> dollars	-
<u>q</u> dollars	-
<u>r</u> dollars	-
<u>s</u> dollars	-
<u>t</u> dollars	-

Dear _____ :

This is in response to your letter dated February 21, 2003, and subsequent correspondence, requesting an extension of time under section 301.9100-3 of the Procedure and Administration Regulations to make allocations of generation-skipping transfer (GST) exemption to a trust.

The facts and representations submitted are summarized as follows:

On Date 1, Decedent established Trust, an irrevocable trust, for the benefit of her Daughter and Daughter's children, Granddaughter and Grandson. The trustee of Trust is Trustee.

Pursuant to Article Fifth, Paragraph 5.01., during each calendar year in which a contribution is made to Trust, each beneficiary shall have the right to make withdrawals from Trust.

Article Fifth, Paragraph 5.01.A., provides, in part, that the beneficiaries having the right to withdraw under this section shall be Granddaughter, Grandson, and Daughter. Each beneficiary may withdraw an amount determined by dividing the amount of the contribution by the number of such beneficiaries; provided, however, that the aggregate amount of such withdrawals by a beneficiary entitled to withdraw during any one calendar year shall not exceed the amount of the United States Gift Tax Annual Exclusion as allowed under the United States Internal Revenue Code.

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Article Fifth, Paragraph 5.02., provides that on the death of Decedent, the Trustee shall divide the trust into two equal shares; one such equal share shall be held in a separate trust for each of the following of Decedent's grandchildren: Granddaughter and Grandson.

Article Fifth, Paragraph 5.03., provides that each trust for a living grandchild of Decedent shall be divided into two parts: one, to which a GST exemption is allocated called the Exempt Trust and the balance to which a GST exemption is not allocated called the Non-Exempt Trust.

Article Fifth, Paragraph 5.03.A., provides that the Trustee shall pay to or apply for the benefit of the grandchild, as much of the net income and principal of the grandchild's Non-Exempt and Exempt Trusts as the Trustee in the Trustee's discretion deems necessary for the grandchild's proper support, care, maintenance and education, after taking into consideration to the extent the Trustee deems advisable, any other income or resources of the grandchild, known to the Trustee. In addition, the Trustee may, if the Trustee deems advisable, apply net income and principal of the trusts for the support of the issue of any deceased grandchild. Any net income not distributed shall be accumulated and added to principal. In exercising the discretions conferred by this subparagraph, the Trustee may pay more to or apply more for some beneficiaries than others, and may make payments to or applications of benefits for one or more beneficiaries to the exclusion of others, if the Trustee deems this necessary or appropriate in light of the circumstances, the size of the trust estate, and the probable future needs of the beneficiaries. Any payment or application of benefits pursuant to this subparagraph shall be charged against the trust as a whole, rather than against the ultimate distributive share of a beneficiary to whom or for whose benefit the payment is made.

Pursuant to Article Fifth, Paragraph 5.03.B., the Trustee shall distribute one-third, one-half and the balance of the principal of the Non-Exempt Trust when a beneficiary reaches 25, 30, and 35, respectively. On the death of the grandchild the Trustee shall distribute the undistributed balance of the grandchild's trust to such one or more persons and entities, including the grandchild's own estate and on such terms and conditions, either outright or in trust, and in such proportion as the grandchild shall appoint by a will specifically referring to and exercising this power of appointment. If or to the extent that (1) the grandchild shall have failed to exercise the power of appointment conferred upon the grandchild under this Paragraph, or (2) an attempted exercise by the grandchild of this power shall have been invalid or ineffective for any reason, or (3) the grandchild shall have released or renounced this power, the property subject to it shall be distributed or retained in trust in accordance with the share allocated to the benefit of the issue of the deceased grandchild.

Article Fifth, Paragraph 5.03.C., provides that the Exempt Trust shall be retained by the Trustee to be administered as follows:

On the death of the grandchild the undistributed balance of the grandchild's trust, shall be distributed to such one or more of the group consisting of the grandchild's issue, and on such terms and conditions, either outright or in trust, as the grandchild shall appoint by a will specifically referring to and exercising this power of appointment. If or to the extent that (1) the grandchild shall have failed to exercise the power of appointment conferred upon the grandchild under this Paragraph, or (2) an attempted exercise by the grandchild of this power shall have been invalid or ineffective for any reason, or (3) the grandchild shall have released or renounced this power, the property subject to it shall be distributed or retained in trust as hereafter provided.

On the death of the grandchild, if no child of Decedent's deceased grandchild is living who is under age thirty, the balance shall thereupon be distributed, free of trust, to Decedent's deceased grandchild's issue then living, by right of representation.

Article Ninth, Paragraph 9.01.A., provides that the executor shall notify the Trustee in writing if the executor intends to allocate any part of the generation-skipping transfer tax exemption that is available to Decedent under section 2631(a) of the Internal Revenue Code to some but not all of the property in any trust to which this paragraph applies. Upon written notification, the Trustee shall divide that trust into two separate trusts, to be designated as the Exempt Trust and the Non-Exempt Trust. The Exempt Trust shall contain the share of the property of that trust equal in value to the amount of the generation-skipping transfer tax exemption that the executor intends to allocate to the trust and shall have an inclusion ratio of zero for federal generation-skipping transfer tax purposes. The Non-Exempt Trust shall contain the balance of the property of that trust and shall have an inclusion ratio of one for federal generation-skipping transfer tax purposes. The executor shall then actually allocate the generation-skipping transfer tax exemption to the Exempt Trust and not to the Non-Exempt Trust. The Trustee shall not be liable for relying on the written instructions of the executor when acting in accordance with the provisions of this subparagraph.

Article Ninth, Paragraph 9.01.B., provides that regardless of whether or not subparagraph (a) of this paragraph applies, if the amount of Trustor's generation-skipping transfer tax exemption actually allocated to a trust to which this paragraph applies by the executor is equal to the value of the property of that trust so that the entire trust has an inclusion ratio of zero for federal generation-skipping transfer tax purposes, the entire trust shall be referred to as the Exempt Trust. On the other hand, if no part of Decedent's generation-skipping transfer tax exemption is actually allocated to the trust by the executor (or if Decedent is not the transferor of that trust for generation-skipping transfer tax purposes) so that the entire trust has an inclusion ratio

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of one for federal generation-skipping transfer tax purposes, the entire trust shall be referred to as the Non-Exempt Trust.

Article Ninth, Paragraph 9.03., provides that if at any time the trustee in the trustee's discretion deems the best interest of an income beneficiary to be best served by distribution to him or her of the entire principal of the share or subshare then held for him or her, due to the small size thereof or for any other reason, the Trustee may convey, transfer, and pay over the same to such beneficiary, absolutely and free of trust.

Article Ninth, Paragraph 9.04., provides that unless sooner terminated in accordance with other provisions of this instrument, all trusts created under this instrument shall terminate twenty-one years after the death of the last survivor of Decedent and Decedent's issue living on the date that this trust is executed. The principal and undistributed income of a terminated trust shall be distributed to the then income beneficiaries of that trust in the same proportion that the beneficiaries are entitled to receive income when the trust terminates. If at any time of such termination the rights to income are not fixed by terms of the trust, distribution under this clause shall be made, by right of representation, to the persons who are entitled or authorized, in the trustee's discretion, to receive trust payments.

In Year 1, Trustee purchased a life insurance policy on the life of Decedent with a face value of a dollars. It is represented that at the time of Decedent's death, Decedent possessed no incidents of ownership in the policy.

Decedent made the following transfers to Trust for Years 1 through 10: b dollars in Year 1; c dollars in Year 2; d dollars in Years 3 and 4; e dollars in Year 5; f dollars in Years 6-9; and g dollars in Year 10.

Of the amounts Decedent transferred to Trust in Years 1 through 10, Daughter is the transferor of the following amounts: h dollars in Year 1; i dollars in Year 2; j dollars in Years 3 and 4; k dollars in Year 5; l dollars in Years 6-9; and m dollars in Year 10. See section 26.2652-1(a)(5) Ex. 5, of the Generation Skipping Transfer Tax Regulations. Granddaughter and Grandson are not transferors of any amount transferred by Decedent.

Accordingly, the portion of each transfer made to Trust for which Decedent remains the transferor for GST tax purposes is as follows: n dollars in Year 1; o dollars in Year 2; p dollars in Years 3 and 4; q dollars in Year 5; r dollars in Years 6-9; and s dollars in Year 10.

In Year 2, Decedent's Attorney, who drafted Trust, prepared Decedent's Year 1 Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return, and incorrectly reported \$t as the amount transferred to Trust. Attorney also allocated \$t of Decedent's GST exemption to the transfer to Trust. Attorney failed to consider the

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portion of the transfer (\$h) to which Daughter was the transferor. See 26.2652-1(a)(5) Ex. 5. It is represented that the correct amount transferred to Trust in Year 1 is \$b.

Decedent terminated the attorney-client relationship with Attorney in Year 2 and retained CPA Firm, which had handled Decedent's spouse's business affairs, to handle Decedent's tax matters, including gift tax matters.

CPA Firm failed to file a Year 2 gift tax return for Decedent and did not report the Year 2 transfer to Trust or allocate Decedent's GST exemption to that transfer.

CPA Firm prepared and filed Decedent's Years 3 and 4 gift tax returns, but failed to report the transfers to Trust, and thereby, did not allocate any portion of Decedent's GST exemption to the Years 3 and 4 transfers to Trust.

CPA Firm failed to file gift tax returns reporting Decedent's Years 5 through 10 transfers to Trust and failed to allocate a portion of Decedent's GST exemption to the transfers. It is represented that Decedent's annual gifts did not exceed the \$10,000 annual exclusion amount in effect at the relevant times to any one donee which would have required that a gift tax return be filed for those years.

Decedent died on Date 2 in Year 10. Daughter and Son are the personal representatives of Decedent's estate.

During the preparation of Decedent's Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, CPA Firm discovered the failure to report the transfers to Trust for Years 2 through 10, and the failure to allocate portions of Decedent's GST exemption to those transfers. However, \$s dollars of Decedent's GST exemption was automatically allocated to the transfer to Trust in Year 10 under section 2632(c). No election has been made to elect out of an automatic allocation. In respect to the transfers to Trust in Year 1, the over allocation of \$h is void under section 26.2632-1(b)(2)(i).

It is represented that Decedent intended that her GST exemption be allocated to Trust so that Trust would have a zero inclusion ratio, to the extent possible, and to minimize her GST tax liability.

You have requested the following rulings: (1) that Decedent's estate be allowed an extension of time under section 301.9100-3 and section 2642(g) to allocate Decedent's GST exemption to Decedent's transfers to Trust for Years 2 through 9 with respect to the amounts of which Decedent is treated as transferor under section 2652, and (2) that such allocations are to be made based upon the value of the property transferred to Trust as of the dates of the original transfers.

Section 2601 imposes a tax on every generation-skipping transfer (GST). A GST is defined under section 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.

Under section 2642(a)(1), the inclusion ratio with respect to any property transferred in a generation-skipping transfer is defined as the excess of 1 over the “applicable fraction.” The applicable fraction, as defined in section 2642(a)(2), is a fraction, the numerator of which is the amount of GST exemption allocated to the trust (or to property transferred in a direct skip), and the denominator of which is the value of the property transferred to the trust (or involved in the direct skip), reduced by the sum of certain federal estate tax or state death tax and charitable deductions.

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 section 2631(c)) that 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 section 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 section 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 lifetime, other than in a direct skip, is made on Form 709.

Section 2642(b)(1) provides that, except as provided in section 2642(f), if the allocation of the GST exemption to any transfers of property is made on a gift tax return filed on or before the date prescribed by section 6075(b) for such transfer or is deemed to be made under section 2632(b)(1) or (c)(1) the value of such property for purposes of section 2642(a) shall be its value as finally determined for purposes of chapter 12 (within the meaning of section 2001(f)(2)), or, in the case of an allocation deemed to have been made at the close of an estate tax inclusion period, its value at the time of the close of the estate tax inclusion period. Such allocation shall be effective on and after the date of such transfer, or, in the case of an allocation deemed to have been made at the close of an estate tax inclusion period, on and after the close of such estate tax inclusion period.

Section 2642(g)(1)(A) provides, generally, 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 section 2642(b)(1) or (2), and an election under section 2632(b)(3) or (c)(5). Such regulations shall include procedures for requesting comparable relief with respect to transfers made before the

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date of the enactment of section 2642(g)(1), which was enacted into law on June 7, 2001.

Section 2642(g)(1)(B) provides that in determining whether to grant relief under this paragraph, 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 (or election) shall be treated as if not expressly prescribed by statute.

Notice 2001-50, 2001-34 I.R.B. 189, provides that under section 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 GST 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 section 2632(b)(3) or (c)(5) under the provisions of section 301.9100-3.

Section 2652(a)(1)(A) provides that, generally, except as provided in this subsection or section 2653(a), the term “transferor” means in the case of any property subject to the tax imposed by chapter 11, the decedent, and in the case of any property subject to the tax imposed by chapter 12, the donor.

Section 26.2652-1(a)(1) provides, in part, that, generally, the individual with respect to whom property was most recently subject to federal estate or gift tax is the transferor of that property for purposes of chapter 13. An individual is treated as transferring any property with respect to which the individual is the transferor. Thus, an individual may be the transferor even though there is no transfer of property under local law at the time the federal estate and gift tax applies.

Section 26.2652-1(a)(2) provides that a transfer is subject to federal gift tax if a gift tax is imposed under section 2501(a) (without regard to exemptions, exclusions, deductions, and credits). A transfer is subject to federal estate tax if the value of the property is includible in the decedent’s gross estate as determined under section 2031 or section 2103.

Section 26.2652-1(a)(5), Example 5 provides that T transfers \$10,000 to a new trust providing that the trust income is to be paid to T’s child, C, for C’s life and, on the death of C, the trust principal is to be paid to T’s grandchild, GC. The trustee has discretion to distribute principal for GC’s benefit during C’s lifetime. C has a right to withdraw \$10,000 from the trust for a 60-day period following the transfer. Thereafter, the power lapses. C does not exercise the withdrawal right. The transfer by T is subject to federal gift tax because a gift tax is imposed under section 2501(a) (without regard to exemptions, exclusions, deductions, and credits) and, thus, T is treated as having transferred the entire \$10,000 to the trust. On the lapse of the withdrawal right, C becomes a transferor to the extent C is treated as having made a completed transfer

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for purposes of chapter 12. Therefore, except to the extent that the amount with respect to which the power of withdrawal lapses exceeds the greater of \$5,000 or 5% of the value of the trust property, T remains the transferor of the trust property for purposes of chapter 13.

Section 301.9100-1(c) provides that the Commissioner has discretion to grant a reasonable extension of time under the rules set forth in sections 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 section 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 section 2642(g)(1)(B) and Notice 2001-50, taxpayers may seek an extension of time to make an allocation described in section 2642(b)(1) or (b)(2) or an election described in section 2632(b)(3) or (c)(5) under the provisions of section 301.9100-3.

Requests for relief under section 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 section 301.9100-3 have been satisfied. Therefore, Decedent's estate is granted an extension of time of 60 days from the date of this letter to allocate Decedent's available GST exemption to Decedent's transfers to Trust in Years 2 through 9. The allocation will be effective as of the dates of the transfers to Trust, and the value of the transfers to Trust for gift tax purposes will be used in determining the amount of GST exemption to be allocated to Trust.

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

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

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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 any aspect of any transaction or item discussed or referenced in this letter 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) 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 section 6110 purposes
Copy of this letter

CC: