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Person To Contact:

, ID #

Telephone Number:

Refer Reply To:

CC:PSI:B09 – PLR-141029-03

Date:

November 12, 2003

In Re:

Ruling Request

Legend:

Decedent	=
Estate	=
Trust	=
Spouse	=
Partnership	=
Attorney	=
Accountant	=
State Statute	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=
Year 1	=
Year 2	=
<u>a</u>	=
<u>b</u>	=
<u>c</u>	=
<u>d</u>	=
<u>e</u>	=
<u>f</u>	=
<u>g</u>	=
<u>x</u>	=

PLR-141029-03

Dear \_\_\_\_\_ :

This is in response to your letter dated June 30, 2003, and subsequent correspondence, in which you requested rulings on behalf of Decedent's estate (Estate) and Decedent's irrevocable Trust (Trust) 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 allocate Decedent's available generation-skipping transfer (GST) exemption to transfers to an irrevocable trust, and the GST tax consequences of severing the trust into two separate trusts pursuant to § 2642(a)(3).

A summary of the facts and representations submitted is as follows. On Date 1, Decedent created the Trust for the benefit of her issue.

Article 2(A) of the Trust provides that after Decedent's death, the trustees are to divide the Trust's property into one share for each of Decedent's then living children and one share for each of Decedent's deceased children survived by living lineal descendants.

Article 2(A)(1) provides that each share allocated to a deceased child shall be distributed to that child's then living lineal descendants, per stirpes, in the manner set forth in Article 2(A)(2)(d).

Article 2(A)(2)(a) provides that each share set aside for a living child of Decedent is to be held in trust for the child's benefit. The trust's net income is to be distributed to the child in at least quarterly installments. Under Article 2(A)(2)(b), the independent corporate trustee may distribute trust principal to the child and his or her spouse and lineal descendants deemed necessary to provide for their education, health, maintenance, support, or other use or benefit. There is no requirement to equalize distributions among beneficiaries.

Article 2(A)(2)(c) provides each child with a limited power to appoint his or her trust's property among the child's lineal descendants in a writing delivered to the trustees prior to the child's death or in the child's will.

Article 2(A)(2)(d) provides that when the child dies, trust principal and undistributed income not effectively appointed is to be distributed to the child's surviving lineal descendants, per stirpes, provided that property distributed to a beneficiary under age 40 shall be held in further trust in accordance with Article 2(A)(3). In the event the child is not survived by lineal descendants, the trust estate is to be distributed to Decedent's then surviving lineal descendants, per stirpes, except that property allocated to a beneficiary for whom a trust has been established under Trust is to be added to that trust and administered accordingly.

PLR-141029-03

Article 2(A)(3)(g) provides that, unless earlier distributed, all trusts established under the Trust will terminate one day prior to 21 years after the death of the last to survivor of the beneficiaries designated in the Trust alive on Date 1. On that day, the trusts' assets will vest in the income beneficiaries thereof and be distributed to these beneficiaries in equal shares.

On Date 2, approximately four months after the Trust was created, Decedent's spouse (Spouse) died. Approximately five months later, on Date 3, Decedent transferred \$a to the Trust. On Date 4, approximately two months thereafter, Decedent transferred an x percent interest in Partnership that Decedent valued at \$b to the Trust. On Date 5, Decedent gifted \$c to a skip person as defined in §§ 2613(a)(1) and 2651(d), the GST taxable portion of which is \$d pursuant to § 2642(c). Dates 1, 2, 3, 4, and 5 all occurred in Year 1.

Decedent retained Accountant to prepare Decedent and Spouse's Year 1 Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return. Attorney and Accountant erroneously determined that Spouse could elect to treat Decedent's gifts to the Trust as being made one-half by each pursuant to § 2513. Accordingly, a Year 1 Form 709 for Spouse so electing was filed that Decedent signed as surviving spouse. In addition, Accountant, in preparing the Forms 709 for Decedent and Spouse, failed to allocate Decedent's and Spouse's GST exemption to the transfers to the Trust on Dates 3 and 4.

Several years later in Year 2, Decedent transferred \$e in total to four skip persons as defined in §§ 2613(a)(1) and 2651(b)(1), the GST taxable portion of which is \$f pursuant to § 2642(c). The following year on Date 6, Decedent died survived by three children. It has been represented that the Trust's property has not yet been divided pursuant to the terms of Article 2, and that no distributions have been made from the Trust from Decedent's death until the present.

Shortly after Decedent's death, an amended Year 2 Form 709 was filed for Decedent by a new attorney. On this return the § 2513 election was corrected by reporting the entire value of the Dates 3 and 4 transfers to the Trust as Decedent's adjusted taxable gifts. The entire value of these assets exceeds Decedent's available GST exemption amount of \$g, after taking into consideration Decedent's lifetime gifts to skip persons in Years 1 and 2.

As a result, in the event relief is granted to allocate Decedent's available GST exemption to the Trust under §§ 2642(g) and 301.9100-3, the trustees propose to divide the Trust into two trusts having exactly same terms. The Trust's assets will be divided on a pro-rata fractional basis between the two succeeding trust. One trust will receive a fractional share of the total value of all the Trust's property equal to the applicable

PLR-141029-03

fraction of the single trust that would be GST tax exempt immediately before the severance, so that the trust would have an inclusion ratio of zero after the severance. The other succeeding trust will receive the Trust's remaining property and have a GST inclusion ratio of one.

The following rulings are requested:

(1) that an extension of time be granted under §§ 2642(g) and 301.9100-3 to allocate Decedent's available GST exemption of \$g to the Dates 3 and 4 transfers to the Trust, and that such allocation will be based on the value of the property transferred to the Trust on Dates 3 and 4, respectively;

(2) that, for GST tax purposes, Decedent is the transferor of the property transferred to the Trust on Dates 3 and 4, and

(3) that the proposed division of the Trust on a pro-rata fractional basis in accordance with applicable state law will be a qualified severance under § 2642(a)(3), and that one trust created by such severance will have an inclusion ratio of zero and the other trust created by the severance will have an inclusion ratio of one.

#### 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)) 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 § 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.

PLR-141029-03

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.

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

PLR-141029-03

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) 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, the Estate is granted an extension of time of sixty (60) days from the date of this letter to allocate Decedent's available GST exemption of \$g to the transfers to the Trust on Dates 3 and 4. The allocation will be effective as of Dates 3 and 4, respectively, and will be made based on the value of the property transferred to the Trust as of Dates 3 and 4, respectively.

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 2501(a)(1) provides that a tax, computed as provided in § 2502, is imposed for each calendar year on the transfer of property by gift during such calendar year by any individual, resident, or nonresident.

Section 2511(a) provides that the tax imposed by § 2501 shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2513(a)(1) provides, in general, that a gift made by one spouse to any person other than his spouse shall, for the purposes of chapter 12, be considered as made one-half by him and one-half by his spouse, but only if at the time of the gift each spouse is a citizen or resident of the United States.

Section 2513(a)(2) provides that § 2513(a)(1) shall apply only if both spouses have signified (under the regulations provided for in § 2513(b)) their consent to the application

PLR-141029-03

of § 2513(a)(1) in the case of all such gifts made during the calendar year by either while married to the other.

Section 25.2513-1(b)(1) provides, in pertinent part, that where the consent is signified by an executor or administrator of a deceased spouse, the consent is not effective with respect to gifts made by the surviving spouse during the portion of the calendar period that his spouse was deceased.

Revenue Ruling 55-506, C.B. 1955-2 609, (based on substantially similar language under the 1939 Internal Revenue Code), holds that an executor's consent to split gifts cannot be applied to any gift that becomes effective at the time the donor is a "widow or widower."

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

Section 26.2652-1(a)(1) provides, in general, that, except as otherwise provided in § 26.2652-1(a)(3), 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 a transferor even though there is no transfer of property under local law at the time the federal estate or gift tax applies.

Section 26.2652-1(a)(2) provides that for purposes of chapter 13, a transfer is subject to federal gift tax if a gift tax is imposed under § 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 § 2031 or § 2103.

In this case, Spouse died on Date 2, several months prior to Decedent's transfers to the Trust on Dates 3 and 4. Therefore, the consent by Spouse's estate to treat the value of these transfers as made one-half by each under § 2513 is not effective. Section 25.2513-1(b)(1). As a result, under § 2501(a), Decedent is subject to the gift tax on the entire value of the transfers to the Trust on Dates 3 and 4. Accordingly, based upon the facts submitted and the representations made, we conclude that, for GST tax purposes, Decedent is the transferor of the assets transferred to the Trust on Dates 3 and 4.

Ruling Request 3

PLR-141029-03

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)(i) 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)(B)(ii) provides that if a trust has an inclusion ratio of greater than zero and less than 1, a severance is a qualified severance only if the single trust is divided into two trusts, one of which receives a fractional share of the total value of all trust assets equal to the applicable fraction of the single trust immediately before the severance. In such case, the trust receiving such fractional share shall have an inclusion ratio of zero and the other trust shall have an inclusion ratio of one.

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

State Statute provides, in pertinent parts, as follows:

(1) From the creation of the trust until final distribution of the assets from the trust, a trustee has the power to perform every act that a prudent trustee would perform for the purposes of the trust, without court authorization, including, but not limited to, the powers specified in subsections (2) ....

(2) Unless otherwise provided in the trust instrument, a trustee has the power:

\* \* \* \* \*

(bb) To sever any trust on a fractional basis into two or more separate and identical trusts for any reason or to segregate by allocation to a separate account or trust a specific amount from, a portion of, or specific assets included in, the trust property of any trust, unless expressly provided to the contrary in the trust instrument. Income earned on a segregated amount, portion, or specific asset after the segregation is effective passes with the amount, portion, or asset segregated. Each separate trust must be held and administered upon the identical terms and conditions of the trust from which it was severed. Subject to the terms of the trust, the trustee may take into consideration differences in federal tax

PLR-141029-03

attributes and other pertinent factors in administering the trust property of any separate account or trust, in making applicable tax elections, and in making distributions. A separate trust created by severance must be treated as a separate trust for all purposes from the date on which the severance is effective. The effective date of the severance may be retroactive to a date before the date on which the trustee exercises such power.

In this case, the Trust will be severed into two separate trusts having the same terms as the Trust in accordance with the provisions of State Statute. Since the terms of the two separate resulting trusts will be identical to the Trust's terms, the terms of the two separate resulting trusts, in the aggregate, will provide for the same succession of interests of beneficiaries as are provided in the Trust.

In addition, it is represented that the Trust's property will be divided on a pro-rata fractional basis between the two resulting trusts. One trust will receive a fractional share of the total value of all the Trust's property equal to the applicable fraction of the single trust that would be GST tax exempt immediately before the severance (GST Exempt Trust), and the other resulting trust will receive the Trust's remaining property (GST Non-Exempt Trust).

Accordingly, based upon the facts submitted and the representations made, we conclude that the proposed division of Trust into two resulting trusts, the GST Exempt Trust and the GST Non-Exempt Trust, will be a "qualified severance" within the meaning § 2642(a)(3). The GST Exempt Trust will have an inclusion ratio of zero, and the GST Non-Exempt Trust will have an inclusion ratio of one.

The rulings contained in this letter are based upon information and representations submitted by the Estate 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. Specifically, no opinion is expressed or implied regarding the value of the property transferred to the Trust for federal transfer tax purposes.

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

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  
Office of (Passthroughs and Special  
Industries)

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