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Internal Revenue Service

Department of the Treasury

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Ben Franklin Station
Washington, DC 20044

UIL 2044.00-00

Person to Contact:

Telephone Number:

Refer Reply to:
CC:DOM:P&SI:7--PLR-121824-98

Date:
April 15, 1999

Re:

Legend:

Trust:

TIN:

Trustor:

SSN:

Spouse:

SSN:

Trustee:

State:

date 1:

date 2:

a:

Dear :

We received your letter dated, November 23, 1998, in which you requested rulings regarding the estate, gift and generation-skipping transfer (GST) tax consequences related to an irrevocable qualified terminable interest property (QTIP) trust under §§ 2044, 2523, 2631, 2632(a)(2), and 2652 of the Internal Revenue Code.

Trustor created Trust on date 1 and transferred Trustor's separate property with a fair market value of $a at the date of transfer into Trust. Trustor reported the gift on Form 709, United States Gift (and Generation-Skipping Transfer (GST)) Tax Return (Return) for the tax year ending date 2. Trustor allocated $a of Trustor's GST tax exemption to the Trust. Part 1 of Schedule A of Trustor's Return and its attachment showed two gifts that Trustor made for the year ending date 2. Schedule A

217

Part 3 listed a marital deduction in the amount of the Trust resulting in a deemed QTIP election under § 2523(f) if the Trust met the requirements of that section. No reverse QTIP election was made on the Form 709.

Article I of the Trust provides that all of the property Trustor transferred into the Trust is the sole and separate property of the Trustor. Article II Paragraph A Subparagraph 1 of the Trust provides that during the life of the Trustor's Spouse, the Trustee shall distribute to Spouse in convenient installments, not less often than annually, all of the net income of the Trust. The Trustee may also distribute to Spouse such sums from the principal of the Trust as shall be necessary or desirable, in the discretion of the Trustee, to provide for the health, maintenance and support of Spouse, having a view to maintaining Spouse's standard of living as nearly as practicable at the level existing at the date hereof. During the life of Trustor's Spouse, no person shall have the power to appoint any part of the principal or income of the Trust to any person other than Spouse. Trustor's principal purpose in establishing the Trust is to care for Spouse, and the Trustee is instructed to administer such trust and make distributions accordingly.

Article II Paragraph A Subparagraph 2 of the Trust states that in addition to the distributions provided in the immediately proceeding subparagraph, Trustor hereby confers upon Spouse the power to direct the Trustee to pay to Spouse from the principal of the Trust Estate, for each full applicable calendar year, the greater of (i) $5,000, or (ii) and interest in or amount of the principal of the Trust Estate not to exceed in value 5% of the fair market value of the principal of the Trust Estate at such time. The fair market value shall be determined as of the last day of the particular calendar year. Spouse may exercise such power for any calendar year only by giving written notice thereof to the Trustee before the end of the year and only if she lives through the year. To the extent Spouse fails to exercise this power for any calendar year, Spouse's power to do so for that year shall lapse.

Article II Paragraph A Subparagraph 3 of the Trust provides that upon the death of Spouse, any undistributed income of the Trust shall be distributed to the personal representative of the estate of Spouse in all events. The remaining principal of the Trust shall be distributed to the personal representative of the estate of Spouse in all events. The remaining principal of the Trust shall be distributed under the provisions of Paragraph C of this Article II; provided, however, that before making such principal distribution, the Trustee shall pay to the personal representative of the estate of Spouse the difference between the amount of estate and inheritance taxes payable by reason of the death of Spouse and the amount of such taxes otherwise payable

had the principal of the Trust not been included in the gross estate of Spouse for purposes of calculating such taxes.

Under Article II Paragraph B in the administration of the Trust, the Trustee shall have all of the powers, privileges and authority that are given to the Trustee herein except (1) the power (without the consent of Spouse) to hold assets unproductive of income; (ii) the power to allocate receipts and disbursements as to principal or income in a manner other than as specified in the State Trust Code; and (iii) those powers the possession or exercise of which would disqualify the assets of the Trust for the marital deduction for Federal gift tax purposes.

Article II Paragraph C Subparagraph 1 provides that as soon as practicable after the death of Spouse the Trustee shall hold the assets to be disposed of under this paragraph in separate trusts of equal initial value for the use and benefit of Trustor's children. Should any of Trustor's children then be deceased and have then surviving issue, the share to which each such deceased child would have been entitled had he or she survived shall be held in separate trusts for such then surviving issue, per stirpes. During the term of each such trust for any beneficiary, the Trustee may distribute such portions of the net income and principal thereof as may be necessary or desirable, in the discretion of the Trustee, to provide for the health, education, maintenance and support of such beneficiary.

Article II Paragraph C Subparagraph 2 states that in addition to the above-described distributions, the Trustee may distribute such sums from the net income of a trust which are not distributed to the beneficiary thereof as shall be necessary or desirable, in the discretion of the Trustee, to provide for the health, education, maintenance and support of the beneficiary's issue, without regard to equality of distribution or the need for equalizing distributions on termination. It is Trustor's desire that the Trustee consult with the beneficiary concerning distributions to his or her issue, but the Trustee shall exercise its sole discretion, which shall be binding upon all parties. Although distributions to the issue of a beneficiary may be made under this subparagraph, such issue shall not be included, during the life of such beneficiary, in the term "beneficiary" when applying the remaining provisions of this Paragraph C.

Article II Paragraph C Subparagraph 3 provides that each trust created for the benefit of a child of Trustor shall continue for the lifetime of such child, after which it shall terminate. Upon the death of a child of Trustor or upon the death of any other beneficiary prior to the termination of the trust for his or her benefit, the remaining assets of the trust for the deceased beneficiary shall be held in separate trusts for the then surviving issue of the deceased beneficiary, per

stirpes, under the same terms set forth in this Paragraph C. If there are no surviving issue of such deceased beneficiary, the remaining assets of the trust for the deceased beneficiary shall be distributed to the then surviving issue, per stirpes, of the nearest ancestor of such beneficiary who is either Trustor or an issue of Trustor and who has then surviving issue; provided, however, that should one of such issue be entitled to receive a portion of such assets and should a trust created hereunder for his or her benefit not then be terminated, such portion shall not be distributed free of trust to such person, but shall be added to the trust created herein for his or her benefit, and shall thereafter be held and administered in accordance with all of the terms and conditions of such trust.

Article II Paragraph C Subparagraph 4 further provides that when any beneficiary other than a child of Trustor shall attain or has attained the age of 21 years, the Trustee shall distribute to such beneficiary, in addition to any other distributions provided for herein, not less than all of the net income of such trust calculated annually. When any beneficiary other than a child of Trustor shall attain or has attained the age of 25, the trust created for the benefit of such beneficiary shall terminate and the remaining assets of such trust shall be distributed, free of trust, even to such beneficiary.

Article II Paragraph C Subparagraph 5 should all of Trustor's issue fail to survive the last to die of Spouse or Trustor or fail to survive to receive a final distribution hereunder, then the assets remaining in the trusts created hereunder shall be distributed to Trustor's heirs at law determined under the applicable statutes of descent and distribution then in force in State in the same shares in which such persons would take according to the provisions of such statutes with respect to each type of property being distributed, as if Trustor had died at the time of such succession.

Article II Paragraph C Subparagraph 6 provides that notwithstanding anything to the contrary herein, the Trustee shall distribute the remaining principal and income of the trust created for any beneficiary under this Paragraph C in such manner, outright, in trust, or otherwise, to or for the benefit of any one or more of Trustor's issue, surviving spouses of deceased issue of Trustor and charities as the beneficiary of any such trust may appoint only by specific reference thereto in his or her will, admitted to probate; provided that such power to appoint may not be exercised in favor of the beneficiary, his or her estate, his or her creditors or the creditors of his or her estate, and further provided that the exercise of such power may not direct the disposition of more than 20% of the assets subject to such power to charities, collectively, and may not direct the disposition of more than 20% of the assets subject to such power

among spouses of deceased issue of Trustor, collectively, it being Trustor's intention that at least 60% of the assets subject to such power shall pass to the issue (if any) of such beneficiary, whether by exercise or non-exercise of this power. To the extent that any beneficiary fails to exercise his or her power to appoint with respect to the principal or income of any trust, then such portion thereof not effectively appointed shall be distributed as otherwise provided herein.

Article II Paragraph D provides that anything in this Article II to the contrary notwithstanding, upon the death of Spouse, the Trustee shall distribute the remaining principal of the Trust in such manner, outright, in trust, or otherwise, to or for the benefit of any one or more of the members of a group including only the following: Trustor, Trustor's issue and charities (provided that the exercise of this power may direct no more than 20% of the assets subject to such power to charities collectively) as Spouse may appoint only by specific reference thereto in Spouse's Will admitted to probate, provided that such power to appoint may not be exercised in favor of Spouse, Spouse's estate, Spouse's creditors or the creditors of Spouse's estate.

The Trustee requests the following rulings:

1) The Trustor's transfers to the Trust qualify for the marital deduction for federal gift tax purposes under § 2523(a).

2) Trustor has made a valid QTIP election under § 2523(f) with respect to the property Trustor transferred to the Trust.

3) At Trustor's death, no part of the Trust property will be includible in Trustor's gross estate for federal estate tax purposes.

4) On the death of Spouse, the Trust property will be includible in Spouse's gross estate under § 2044 and will be treated as passing from Spouse for federal estate tax purposes.

5) Spouse is the transferor of the Trust property for GST tax purposes because Trustor did not make a reverse QTIP election pursuant to § 2652(a)(3) to treat such property as if an election pursuant to § 2523(f) had not been made.

6) The allocation of Trustor's GST tax exemption to the Trust is void because the Trust had no GST tax potential for Trustor at the time of the allocation and therefore Trustor's GST tax exemption is available for allocation to other transfers.

Section 2001(a) provides that a tax is hereby imposed on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2044(a) provides that the value of the gross estate will include the value of any property to which this section applies in which the decedent had a qualifying income interest for life. Section 2044(b) says that § 2044 applies to any property if-(1) a deduction was allowed with respect to the transfer of the property to the decedent-(A) under § 2056 by reason of § 2056(b)(7) thereof, or (B) under § 2523 by reason of § 2523(f) thereof, and (2) § 2519 (relating to disposition of certain life estates) did not apply with respect to a disposition by the decedent of part or all of such property.

Section 2056(b)(7)(B)(i) provides that the term "qualified terminable interest property" means property: (I) which passes from the decedent, (II) in which the surviving spouse has a qualifying income interest for life, and (III) to which an election under § 2056(b)(7)(B) applies.

Section 2056(b)(7)(B)(ii) provides that the surviving spouse has a qualifying income interest for life if--(I) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, or has a usufruct interest for life in the property, and (II) no person has power to appoint any part of the property to any person other than the surviving spouse. Section 2056(b)(7)(B)(ii) further provides that § 2056(b)(7)(B)(ii)(II) shall not apply to a power exercisable only at or after the death of the surviving spouse. To the extent provided in regulations, an annuity shall be treated in a manner similar to an income interest in property (regardless of whether the property from which the annuity is payable can be separately identified).

Section 2523(a) provides that where a donor transfers during the calendar year by gift an interest in property to a donee who at the time of the gift is the donor's spouse, there shall be allowed as a deduction in computing taxable gifts for the calendar year an amount with respect to such interest equal to its value.

Section 2523(b) provides that where on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, such interest transferred to the spouse will terminate or fail, no deduction shall be allowed with respect to such interest.

Section 2523(b)(1) provides that if the donor retains in himself, or transfers or has transferred (for less than an adequate and full consideration in money or money's worth) to any person other than such donee spouse (or the estate of such spouse), an interest in such property, and if by reason of such retention or transfer the donor (or his heirs or assigns) or such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest transferred to the donee spouse; or (2) if the donor immediately after the transfer to the donee spouse has a power to appoint an interest in such property which he can exercise (either alone or in conjunction with any person) in such manner that the appointee may possess or enjoy any part of such property after such termination or failure of the interest transferred to the donee spouse. For purposes of this paragraph, the donor shall be considered as having immediately after the transfer to the donee spouse such power to appoint even though such power cannot be exercised until after the lapse of time, upon the occurrence of an event or contingency, or on the failure of an event or contingency to occur.

Section 2523(b) further provides that an exercise or release at any time by the donor, either alone or in conjunction with any person, of a power to appoint an interest in property, even though not otherwise a transfer, shall, for purposes of § 2523(b)(1), be considered as a transfer by him. Except as provided in § 2523(e), where at the time of the transfer it is impossible to ascertain the particular person or persons who may receive from the donor an interest in property so transferred by him, such interest shall, for purposes of § 2523(b)(1), be considered as transferred to a person other than the donee spouse.

Section 2523(f)(1) provides that in the case of qualified terminable interest property-(A) for purposes of § 2523(a), such property shall be treated as transferred to the donee spouse, and (B) for purposes of § 2523(b)(1), no part of such property shall be considered as retained in the donor or transferred to any person other than the donee spouse.

Section 2523(f)(2) provides that for the purposes of § 2523(f), the term "qualified terminable interest property" means any property-(A) which is transferred by the donor spouse, (B) in which the donee spouse has a qualifying income interest for life, and (C) to which an election under § 2523(f) applies.

Section 2523(f)(3) also provides that for purposes of § 2523(f), rules similar to the rules of clauses (ii), (iii), and (iv) of § 2056(b)(7)(B) shall apply and the rules of § 2056(b)(10) shall apply.

Section 2523(f)(4)(A) provides that an election under § 2523(f) with respect to any property shall be made on or before the date prescribed by § 6075(b) for filing a gift tax return with respect to the transfer (determined without regard to § 6019(2)), and shall be made in such manner as the secretary shall by regulations prescribe. Section 2523(f)(4)(B) provides that an election under § 2523(f), once made, shall be irrevocable.

Section 2601 imposes a tax on every generation-skipping transfer (GST) within the meaning of §§ 2611 through 2613.

Section 2611(a) defines the term "GST" as (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 2612(a) provides that the term "taxable termination" means the termination (by death, lapse of time, release of power, or otherwise) of an interest in property held in a trust unless--(A) immediately after such termination, a non-skip person has an interest in such property, or (B) at no time after such termination may a distribution (including distributions on termination) be made from such trust to a skip person.

Section 2631(a) provides that for purposes of determining the inclusion ratio, every individual is allowed a GST exemption of $1,000,000 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, is irrevocable.

Section 2632(a) provides that any allocation by an individual of his 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 2652(a)(3) provides a special election for qualified terminal interest property in the case of-(A) any trust with respect to which a deduction is allowed to the decedent under § 2056(b)(7), and (B) any trust with respect to which a deduction to the donor spouse is allowed under § 2523(f), the estate of the decedent or the donor spouse, as the case may be may elect to treat all of the property in such trust for purposes of chapter 13 as if the election to be treated as a QTIP 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, that decedent's GST exemption may be allocated to that QTIP trust.

Section 26.2632-1(b)(2)(i) of the GST Tax Regulations provides in part that an allocation of GST exemption to a trust is also void if the allocation is made with respect to a trust that has no GST potential with respect to the transferor making the allocation, at the time of the allocation. For this purpose, a trust has GST potential even if the possibility of a GST is so remote as to be negligible.

Based on the facts and representations submitted with your request, we have determined the following:

1) The Trustor's transfers to the Trust qualify for the marital deduction for federal gift tax purposes under § 2523(a), because Trustor gave Spouse an interest in property (the Trust).

2) At the time of the transfer, Trustor made a valid QTIP election under § 2523(f) by gifting to his Spouse qualified terminable interest property (property that Trustor transferred to the Trust, property in which Spouse has a qualifying income interest for life, and property to which the election under § 2523(f) applies). Trustor also made a timely § 2523(f) election on Trustor's timely filed Federal Gift and GST Tax Return.

3) Because Trustor's transfers to the Trust qualify for the marital deduction under § 2523, no part of the Trust property will be includible in Trustor's gross estate, at Trustor's death, for federal estate tax purposes.

4) On the death of Spouse, the Trust property will be includible in Spouse's gross estate under § 2044, because a deduction was allowed for the transfer of the property to the Trustor under § 2523 by reason of § 2523(f). The Trust property will be treated as passing from Spouse for federal estate tax purposes.

5). The Trustor did not make a reverse QTIP election pursuant to § 2652(a)(3) to treat Trustor as the transferor of the property for GST tax purposes as if an election pursuant to § 2523(f) had not been made. Thus, under § 2044 Spouse is the individual last subject to estate or gift tax on the transfer of the property and is considered the transferor of the Trust property for GST tax purposes.

6) The allocation of Trustor's GST tax exemption to the Trust is void because the Trust had no GST tax potential for Trustor at the time of the allocation and therefore, Trustor's GST tax exemption is available for allocation to other transfers.

Except as we have specifically ruled herein, we express or imply no opinion as to the federal tax consequences of this 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) of the Code provides that it may not be used or cited as precedent.

Sincerely,

(signed) Christine Ellison

Christine E. Ellison
Branch Chief,
Branch 7
Office of the Assistant
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(Passthroughs and
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Enclosure
Copy for section 6110 purpose