

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:B09 / PLR-133654-01
Date:
March 13, 2002

Re:

Legend:

- Decedent =
- Trust 1 =
- Trust 2 =
- Trust 3 =
- Date 1 =
- \$a =
- Child 1 =
- Date 2 =
- Year 1 =
- Date 3 =
- Date 4 =
- \$b =
- Brother =
- Sister-in-law =
- \$c =
- Friend =

Child 2 =
Date 5 =
State =
Date 6 =
Date 7 =
\$d =
\$e =
\$f =

Dear

We received your letter dated June 19, 2001, and subsequent correspondence submitted on behalf of Decedent's estate, requesting a ruling regarding the application of § 2632 of the Internal Revenue Code to certain trusts. This letter responds to that request.

Facts

The facts and representations submitted are summarized as follows: During her lifetime, Decedent created three trusts: Trust 1, Trust 2 and Trust 3.

Decedent established Trust 1 on Date 1 and funded the trust with \$a. Article 1 of Trust 1 provides that the initial beneficiary of the trust is Child 1. Article 1 further provides that Child 1 shall have the right, by written notice to the trustee, to add any descendant of Child 1 as a beneficiary of Trust 1.

Article V, Paragraph A of Trust 1 provides that until Date 2, the trustee may pay to or for the benefit of Child 1 so much of the income and principal of the trust as the trustee deems appropriate for Child 1's health, maintenance and support. The trustee is also permitted until Date 2 to make distributions of trust income and/or principal to or for the benefit of Child 1's descendants for their health, education and support. After Date 2 and for the remainder of Child 1's lifetime, the trustee must pay all income to Child 1 at least annually and may distribute trust principal for the health, maintenance and support of Child 1.

It has been represented that no additions have been made to Trust 1 since it was established. Decedent did not file a Year 1 gift tax return or make any allocation of her generation-skipping transfer ("GST") tax exemption to Trust 1.

Decedent established a revocable living trust, Trust 2, on Date 3. On Date 4, Decedent amended and restated Trust 2 in its entirety.

Article Three of Trust 2 governs the disposition of trust assets upon Decedent's death. Section 3.2, Paragraph 2 provides for a distribution of \$b to Brother over a ten year period. This section further provides that all income from this disposition be distributed to Brother at least annually. In addition, Brother is permitted to withdraw one-tenth (1/10) of the principal of the distribution in the first year, one-ninth (1/9) of the distribution in the second year, etc., until the entire \$b of principal has been distributed or withdrawn. In the event Brother is not surviving at the time of Decedent's death or dies during the distribution, the trustee is directed to make all such payments of income and principal to Sister-in-law.

Section 3.2, Paragraph 3 of Trust 2 contains a disposition of \$c to Friend to be held in a retirement trust until Friend attains the age of sixty-two (62). Prior to reaching age sixty-two (62), the trustee is directed to distribute so much of the income and principal to Friend or for her benefit as the trustee deems appropriate to assist Friend in defraying medical expenses. Once Friend reaches age sixty-two (62), she may withdraw any or all of the remaining trust.

Section 3.3 of Trust 2 provides that after the distributions to Brother and Friend outlined in Section 3.2, the trustee shall segregate assets having a value equal to the Decedent's available exemption from the GST tax. Section 3.3 further provides that such assets will be held in a generation-skipping trust and administered in accordance with the provisions of Section 3.4. Any remaining assets will be held as part of a non-exempt trust in accordance with the provisions of Section 3.5.

Section 3.4 of Trust 2 directs the trustee to divide the assets of the generation-skipping trust into two (2) separate subtrusts, with sixty percent (60%) being set aside in trust for Child 1 and forty percent (40%) being set aside in trust for Child 2. The respective shares are designated by the name of the child and the words "Generation-Skipping Trust." In the event that either Child 1 or Child 2 predeceases Decedent, such deceased child's share shall be held in separate generation-skipping trusts for such child's descendants.

Section 3.4A of Trust 2 provides that the trustee shall distribute all of the net income of each child's respective trust to such child. In addition, the trustee is given discretion to make distributions of principal from each child's respective trust as the trustee deems necessary for such child's health, education, maintenance and support.

Section 3.4C of Trust 2 provides that on the first day of each calendar year Child 1 and Child 2 shall have the right to withdraw from his or her respective generation-skipping trust the greater of 5 percent of the value of the trust principal or \$5,000. Pursuant to the third paragraph of Section 3.4C, the remainder beneficiaries of each

child's trust are granted a withdrawal power under which they may withdraw the assets of their respective shares. One-third (1/3) of the corpus may be withdrawn at age thirty (30), one-half of the corpus may be withdrawn at age thirty-five (35), and the remaining corpus may be withdrawn at age forty (40).

Section 3.4D of Trust 2 provides each child with a testamentary limited power of appointment over all of the income and principal of his or her respective generation-skipping trust. The testamentary power of appointment may be exercised in favor of any of Decedent's descendants, other than the holder of such power. The power of appointment may be exercised to either leave such interest outright and free of trust, or in further trust with such trustee(s) and on such terms and conditions as the child specifies. Under Section 3.4F, if a deceased child does not exercise his or her testamentary limited power of appointment over the remaining trust property, such child's generation-skipping trust will pass to such child's descendants to be held in the non-exempt trusts described in Section 3.5.

Section 3.5 of Trust 2 sets forth the terms of the non-exempt trust. Under Section 3.5, the trustee is directed to divide the non-exempt assets into two (2) separate subtrusts, with sixty percent (60%) going to Child 1's trust and forty percent (40%) going to Child 2's trust. The respective shares are designated by the name of the child and the word "Trust." In the event that either Child 1 or Child 2 predeceases Decedent, the deceased child's share shall be held in separate trusts for the child's descendants.

Section 7.6B of Trust 2 provides that unless earlier terminated, each trust created under Trust 2 shall, in any and all events, terminate on the day prior to the expiration of 21 years after the death of the survivor of a group of individuals composed of (i) those whose names appear in the trust instrument (other than solely as trustees, witnesses, notaries, etc.) and (ii) those of their respective lineal descendants who are living at the time of the Decedent's death or at such earlier time as the Decedent becomes incapacitated.

On Date 5, Decedent created Trust 3 to hold certain of Decedent's mineral rights. On the same day that Decedent amended Trust 2, Date 4, Decedent also amended Trust 3 in its entirety.

Section 1.3 of Trust 3 provides for the distribution of all of the net income of the trust to Decedent during her lifetime.

Section 1.4 of Trust 3 provides that at any time Decedent is incapacitated, the trust income shall be distributed to the trustee of Trust 2.

Section 3.2 of Trust 3 provides that upon Decedent's death, any assets remaining after the payment of expenses, taxes and other debts shall be distributed to Child 1 and Child 2, per stirpes.

Decedent died a resident of State on Date 6. She was survived by Child 1, Child 2, the children of Child 1 and Child 2, Brother, Sister-in-law and Friend. Decedent's estate filed a timely Form 706, Federal Estate (and Generation-Skipping Transfer) Tax Return, on Date 7. No entries were made on Schedule R of the estate tax return. However, copies of Trust 1, Trust 2 and Trust 3 were attached to the return.

Decedent's estate now requests a ruling that Decedent's estate substantially complied with the requirements of making a timely allocation of Decedent's \$d GST exemption as follows: \$e to the generation-skipping subtrust created for Child 1 and her issue under Trust 2 and \$f to the generation-skipping subtrust created for Child 2 and his issue under Trust 2.

Law and Analysis

Section 2601 imposes a tax on every generation-skipping transfer.

Under § 2611(a), the term "generation-skipping transfer" means a taxable distribution, a taxable termination, and a direct skip.

Section 2612(a)(1) 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 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 2612(b) provides that the term "taxable distribution" means any distribution from a trust to a skip person (other than a taxable termination or direct skip).

Section 2612(c)(1) provides that the term "direct skip" means a transfer subject to a tax imposed by chapter 11 or 12 of an interest in property to a skip person.

Section 2613(a) provides that the term "skip person" means -- (1) a natural person assigned to a generation which is 2 or more generations below the generation assignment of the transferor, or (2) a trust -- (A) if all interests in such trust are held by skip persons, or (B) if -- (i) there is no person holding an interest in such trust, and (ii) at no time after such transfer may a distribution (including distributions on termination) be made from such trust to a non-skip person.

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 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 return is required to be filed.

In this case, the Decedent's estate did not comply with the instructions on Form 706 in that the Schedule R filed with the estate tax return did not allocate any of Decedent's \$d of GST exemption. However, literal compliance with the procedural instructions to make an election is not always required. See Hewlett Packard Co. v. Commissioner, 67 T.C. 736 (1977), acq. in result, 1979-1 C.B. 1. Thus, an allocation that does not strictly comply with the instructions on Form 706, or the applicable regulations, will be deemed valid if the information on the return is sufficient to indicate that the executor intended to make an allocation of GST exemption.

In this case, copies of Trust 1, Trust 2 and Trust 3 were attached to the Decedent's federal estate tax return filed on Date 7. Trust 2 is the only one of the three trusts that addresses the allocation of Decedent's GST exemption. More specifically, Section 3.3 of Trust 2 explicitly directs the trustee to divide the remaining trust assets into a generation-skipping trust and a non-exempt trust. In addition, Section 3.4 of Trust 2 provides that the assets of the generation-skipping trust be further divided into two (2) separate subtrusts, with sixty percent (60%) being set aside in trust for Child 1 and forty percent (40%) being set aside in trust for Child 2.

Based solely on the facts submitted and the representations made, we conclude that the trust agreements attached to the federal estate tax return contain sufficient information to constitute substantial compliance with the requirements for making a timely allocation of Decedent's GST exemption with respect to Trust 2. The estate is therefore deemed to have allocated Decedent's \$d GST exemption as follows: \$e to the generation-skipping trust created for Child 1 and her issue under Trust 2 and \$f to the generation-skipping trust created for Child 2 and his issue under Trust 2.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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 the material submitted in support of the request for rulings it is subject to verification on examination.

Pursuant to the Power of Attorney and Declaration of Representative on file with this office, a copy of this letter is being sent to Decedent's estate.

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

Sincerely,
James F. Hogan
Senior Technician Reviewer
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure

Copy for 6110 purposes