Internal Revenue Service

Department of the Treasury

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Refer Reply To:
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Date:
April 12, 1999

Re:

LEGEND

Grantor	=
Spouse	=
Spouse 2	=
Child 1	=
Child 2	=
Child 3	=
Child 4	=
Grandchild 2	=
Grandchild 3	=
Stepchild 1	=
Stepchild 2	=
Trust	=
Date 1	=
Date 2	=
Date 3	=

This is in response to a December 9, 1998 letter, and prior correspondence, from your authorized representative requesting estate and generation-skipping transfer tax rulings on a proposed will and trust.

Grantor and Spouse were married in 1997. Spouse's date of birth is Date 1. Grantor had four children from a previous marriage, Child 1, Child 2, Child 3, and Child 4. Child 4 died in 1985 and was survived by three children; Grandchild 1, Grandchild 2, and Grandchild 3. Grantor's second marriage ended with the death of

Spouse 2, in 1989. There were no children from this marriage; however, Spouse 2 had 2 children from a previous marriage, Stepchild 1 and Stepchild 2. Stepchild 1's date of birth is Date 2, and Stepchild 2's date of birth is Date 3.

Grantor proposes to execute a will and a revocable trust (Trust). In Article 4.5 of the proposed will, Grantor bequeaths and devises certain personal and real property to Child 3 and also provides for certain bequests of specific pecuniary amounts to his children, stepchildren, and grandchildren. Article 6.1 of the will provides that the residue is to pass to Trust.

Under Article 4.1(a) of the proposed Trust, Grantor retains the right to revoke the trust, in whole or in part. Article 6.1 provides that, during the lifetime of Grantor, the trustee shall pay over or apply for the benefit of Grantor all of the income of the Trust, in monthly installments or as frequently as may be requested by Grantor.

Article 7.1 of the Trust provides that, upon the death of Grantor, if he is survived by Spouse, the trustee shall divide the trust estate into two trusts, Trust 1 and Trust 2. The amount passing to each trust is to be determined as follows:

> (1) The trustee shall determine the value of the gross estate for federal estate tax purposes.
>
> (2) The trustee shall deduct from the value of the gross estate the amount, to extent allowable as a deduction for federal estate taxes, all funeral and administration expenses and claims against the estate. However, the trustee shall not deduct estate, inheritance, transfer, legacy or succession taxes.
>
> (3) Of the difference, Trust 1 shall be the smallest amount of the assets of the estate to qualify for the marital deduction as will be sufficient to result in the lowest federal estate tax being imposed upon the estate, after allowing for the applicable credit amount (unified credit) as defined in § 2010(c) of the Internal Revenue Code and any other allowable credits and deductions.
>
> (4) Trust 2 shall be equal in amount to the balance of the Trust estate after deducting the amount allocated to Trust 1.

Article 7.1(a) further provides that, upon Grantor's death, the trustee shall pay to Spouse, in quarterly or more frequent installments, all of the net income from Trust 1, during her lifetime and, upon her death, to pay all of the accrued and undistributed income to her estate. The trustee is to pay Spouse in quarterly or more frequent installments, all of the income from Trust 2, during her lifetime.

Article 7.1(c) provides that, upon the death of Spouse, Trust 1 and Trust 2 will terminate and the trustee is to distribute all principal of both trusts under the provisions

of Article 7.2. Article 7.1(d) provides that, if Spouse does not survive Grantor, Trust will terminate upon Grantor's death and the trustee is also to distribute the assets of the trust under the terms of Article 7.2.

Article 7.2 provides for the distribution of trust corpus, if Trust terminates on Grantor's death, or, if Grantor predeceases Spouse, for distributions from Trust 1 and Trust 2 on Spouse's death. Stock in specific corporations that are held by the trust(s) are to be distributed as follows:

Beneficiary	Amount
Child 1	1/6
Child 2	1/6
Child 3	1/6
Stepchild 1	1/6
Stepchild 2	1/6
Grandchild 1	1/18
Grandchild 2	1/18
Grandchild 3	1/18

The residue of the trust(s) estate(s) is to be divided in the same manner.

Grantor has requested rulings on the estate tax consequences that will result from the transfers under the will and Trust. Grantor has also requested rulings on the generation-skipping transfer tax consequences that will result from the transfers under the will and Trust.

Estate Tax Rulings

Section 2036(a) provides that a decedent's gross estate includes the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth) by trust or otherwise, under which he has retained, for his life or for any period not ascertainable without reference to his death or any period that does not in fact end before his death, (1) the possession or enjoyment of, or the right to the income, from the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 2038(a)(1) provides that the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a

power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or were any such power is relinquished during the 3-year period ending on the date of the decedent's death.

Section 2056(a) allows a marital deduction for the value of any interest in property that is included in the gross estate and that passes from the decedent to the decedent's surviving spouse. Section 2056(b)(1) disallows this deduction where, upon the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, and the property will pass to another.

Section 2056(b)(7)(A) provides that in the case of qualified terminable interest property, such property shall be treated as passing to the surviving spouse.

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

Section 2056(b)(7)(B)(ii) provides that a surviving spouse has a qualified 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 a power to appoint any part of the property to any person other than the surviving spouse.

Section 2056(b)(7)(B)(v) provides that the election under § 2056(b)(7) shall be made by the executor on the return of tax imposed by § 2001. Such an election, once made, shall be irrevocable.

In this case, under Article 4.1(a) of Trust, Grantor retains the right to revoke the trust, in whole or in part. Article 6.1 provides that, during the lifetime of Grantor, the trustee shall pay over or apply for the benefit of Grantor all of the income of the Trust, in monthly installments or as frequently as may be requested by Grantor. Under these circumstances, the value of the property in Trust will be includible in Grantor's gross estate for Federal estate tax purposes. Sections 2036 and 2038.

If Grantor predeceases Spouse, Trust 1 will be held as a marital trust for the benefit of Spouse. Trust 1 meets the requirements set forth in § 2056(b)(7). Therefore, assuming the personal representative of Grantor's estate makes the election required by § 2056(b)(7)(B)(v) (QTIP election), the amount passing to Trust 1 will qualify for the marital deduction under § 2056(b)(7).

Generation-Skipping Transfer Tax Rulings

Section 2601 imposes a tax on every generation-skipping transfer made after October 22, 1986.

Section 2611(a) provides that the term "generation-skipping transfer" means (1) a taxable distribution, (2) a taxable termination, and (3) 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 the termination, a non-skip person has an interest in the property, or (B) at no time after the termination may a distribution (including distributions on termination) be made from the trust to a skip person.

Section 2612(b) provides that a "taxable distribution" means any distribution from a trust to a skip person (other than a taxable termination or a 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 that is 2 or more generations below the generation assignment of the transferor, or (2) a trust--(A) if all interests are held by skip persons, or (B) if--(i) there is no person holding an interest in the trust, and (ii) at no time after the transfer may a distribution (including distributions on termination) be made from the trust to a non-skip persons.

Section 2613(b) provides that the term "non-skip person" means any person who is not a skip person.

In general, under § 2602, the amount of the generation-skipping tax imposed with respect to a transfer is determined by multiplying the “applicable rate” by the taxable amount. Under § 2641, the “applicable rate” is equal to the maximum federal estate tax rate multiplied by the “inclusion ratio” with respect to the trust. The “inclusion ratio” is defined in § 2642(a) as the excess of 1 over the “applicable fraction” with respect to the transfer. The “applicable fraction” is a fraction, the numerator of which is the amount of GST exemption (discussed below) allocated to the trust, and the denominator of which is the value of the property transferred to the trust (with certain adjustments).

Section 2631(a) provides that, for purposes of determining the inclusion ratio, every individual is allowed a GST tax exemption of $1,000,000 (adjusted for inflation under § 2631(c)) that may be allocated by the individual (or the individual's executor) to any property with respect to which the individual is the transferor. An allocation, once made, is irrevocable.

Section 2632(a)(1) provides that any allocation by an individual of the GST exemption under § 2631(a) may be made at any time on or before the date prescribed for filing the estate tax return for the individual's estate (determined with regard to extensions), regardless of whether a return is required to be filed.

Section 2651(a) provides that, for purposes of Chapter 13, the generation to which any person (other than the transferor) belongs shall be determined in accordance with the rules set forth in § 2651.

Section 2651(b)(1) provides that an individual who is a lineal descendant of a grandparent of the transferor shall be assigned to that generation that results from comparing the number of generations between the grandparent and the individual with the number of generations between the grandparent and the transferor.

Section 2651(b)(2) provides that an individual who is a lineal descendant of a grandparent of a spouse (or former spouse) of the transferor (other than the spouse) shall be assigned to that generation that results from comparing the number of generations between the grandparent and the individual with the number of generations between the grandparent and the spouse.

Section 2651(c)(1) provides that an individual who has been married at any time to the transferor shall be assigned to the transferor’s generation.

Section 2651(d) provides that an individual who is not assigned to a generation by reason of the § 2651(b) and § 2651(c) shall be assigned to a generation on the basis of the date of the individual’s birth with--(1) an individual born not more than 121/2 years after the date of birth of the transferor assigned to the transferor’s generation, (2) an individual born more than 121/2 years but not more than 371/2 years after the date of the birth of the transferor assigned to the first generation younger than the transferor, and (3) similar rules for a new generation every 25 years.

Section 2651(e)(1) provides that, for purposes of determining whether any transfer is a generation-skipping transfer, if--(A) an individual is a descendant of a parent of the transferor (or the transferor’s spouse or former spouse), and (B) the individual’s parent who is a lineal descendant of the parent of the transferor (or the transferor’s spouse or former spouse) is dead at the time the transfer (from which an interest of the individual is established or derived) is subject to a tax imposed by Chapter 11 or 12 upon the transferor (and if there shall be more than 1 such time, then at the earliest such time), the individual shall be treated as if the individual were a member of the generation that is one generation below the lower of the transferor’s generation or the generation assignment of the youngest living ancestor of the individual who is also a descendant of the parent of the transferor (or the transferor’s spouse or former spouse) and the generation assignment of any descendant of the individual shall be adjusted accordingly.

Section 2652(a)(1) provides generally, that the term "transferor" means--(A) in the case of any property subject to the tax imposed by Chapter 11, the decedent, and (B) in the case of any property subject to the tax imposed by Chapter 12, the donor. An individual is treated as transferring any property with respect to which the individual is the transferor.

The following analysis considers the generation-skipping transfer tax consequences that will result under Grantor's will and Trust if Spouse should predecease Grantor.

Under the terms of the will, certain distributions will be made to grantor's children, stepchildren, and grandchildren. Article 4.5 provides for specific bequests of personal property and the devise of certain real property to Child 3. Article 4.5 further provides for pecuniary bequests to the other children, stepchildren, and grandchildren. Assuming the assets that fund the bequests and the devise of the real property provided for under Article 4.5 are included in his gross estate for Federal estate tax purposes, Grantor will be considered the transferor of these assets for purposes of Chapter 13. In addition, the residue of the estate is to pass to Trust. Grantor will also be considered the transferor of the residuary estate for purposes of Chapter 13. Section 2652(a)(1)(A).

As discussed above, the value of the assets in Trust will be includible in Grantor's gross estate for Federal estate tax purposes under § 2036 and § 2038. Therefore, Grantor will be considered the transferor of the assets held in Trust for purposes of Chapter 13. Section 2652(a)(1)(A).

Child 1, Child 2, and Child 3 are assigned to a generation that is one generation below the generation of Grantor, the transferor, and therefore, they are not skip persons. Sections 2613 and 2651(b)(1). Accordingly, the transfers passing to Child 1, 2, and 3 under the will or under the terms of the Trust at Grantor's death will not be subject to the generation-skipping transfer tax.

In addition, if any child of Grantor does not survive Grantor but is survived by children, the children of the deceased child shall be treated as a member of the generation that is one generation below the transferor's (i.e., Grantor's) generation. Section 2651(e). Accordingly, the transfers passing to the children of a predeceased child under the will and under the Trust will not be subject to the generation-skipping transfer tax.

Also, Stepchild 1 and Stepchild 2 are children of Grantor's former spouse, Spouse 2. They are also assigned to a generation that is one generation below the generation of Grantor and, therefore, are not skip persons. Sections 2613, 2651(b)(2) and 2651(c)(1). Accordingly, the transfers under the will and from the Trust to the stepchildren will not be subject to the generation-skipping transfer tax.

Furthermore, if any stepchild of Grantor does not survive Grantor but is survived by children, the children of the deceased stepchild shall be treated as a member of the generation that is 1 generation below the transferor's (i.e., Grantor's) generation. Section 2651(e). Accordingly, any transfers passing to a child of a predeceased stepchild under the will and or the Trust will not be subject to the generation-skipping transfer tax.

Finally, Grandchild 1, Grandchild 2, and Grandchild 3 are the children of Child 4 who died in 1985. Under § 2651(e)(1), if an individual is a descendant of a parent of the transferor and the individual's parent who is a lineal descendant of the parent of the transferor is dead at the time the transfer is subject to a tax imposed by Chapter 11, the individual shall be treated as if the individual were a member of the generation that is one generation below the lower of the transferor's generation or the generation assignment of the youngest living ancestor of the individual who is also a descendant of the parent of the transferor (or the transferor's spouse or former spouse) and the generation assignment of any descendant of the individual shall be adjusted accordingly. If Grandchild 1, Grandchild 2, and Grandchild 3 survive Grantor, they will have satisfied the requirements set forth in § 2651(e)(1) when the transfers under the will and from the Trust are subject to the tax imposed under Chapter 11. Accordingly, the transfers under the will and from the Trust will not be subject to the generation-skipping transfer tax. Sections 2613(b) and 2651(e).

In addition, if a grandchild does not survive Grantor but is survived by children, the children of the deceased grandchild shall be treated as a member of the generation that is one generation below the transferor's generation. Section 2651(e). Accordingly, any transfers passing to children of a predeceased grandchild under the will or under the terms of the Trust will not be subject to the generation-skipping transfer tax.

The following analysis deals with the generation-skipping transfer tax consequences that will result if Grantor should predecease Spouse. In this event, Article 7.1 of the Trust provides that, upon the death of Grantor, the trustee shall divide the trust estate into two parts; one part is to be designated as Trust 1 and the other part is to be designated as Trust 2. As discussed above, the terms of Trust 1 satisfy the requirements of § 2056(b)(7) and, if the personal representative of Grantor's estate makes the QTIP election, the amount passing to Trust 1 will qualify for the marital deduction under § 2056(b)(7).

Article 7.1(c) provides that, upon the death of Spouse, Trust 1 and Trust 2 will terminate and the trustee is to distribute all of the principal of both trusts under the provisions of Article 7.2. If the personal representative of Grantor's estate has made a QTIP election, the value of the property in Trust 1 will be includible in Spouse's gross estate under § 2044, at her death. If the personal representative of Grantor's estate does not make the election under § 2652(a)(3) (the reverse QTIP election), Spouse will be the transferor of Trust 1 for GST purposes. In this case, Child 1, Child 2, and Child

3 are assigned to the generation that is one generation below the generation of Spouse and, therefore, they are not skip persons. Sections 2613, 2651(b)(2), and 2651(c)(1). Accordingly, the property passing under Trust 1 to the children will not be subject to the generation-skipping transfer tax.

In addition, if any child of Grantor does not survive Spouse but is survived by children, the children of the deceased child shall be treated as a member of the generation that is 1 generation below the transferor's (i.e., Spouse's) generation. Section 2651(e). Accordingly, any property passing under Trust 1 to the children of a predeceased child will not be subject to the generation-skipping transfer tax.

Furthermore, Stepchild 1 and Stepchild 2 are children of Grantor's former spouse, Spouse 2. Neither of these individuals are a lineal descendant of a grandparent of Spouse (the transferor). Further neither of these individuals are a lineal descendant of a grandparent of a spouse (or former spouse) of Spouse. Accordingly, these individuals are not classified under § 2651(b) or (c). Any individual who is not classified under these sections is assigned a generation under § 2651(d). In this case, Stepchild 1's date of birth is Date 2 and Stepchild 2's date of birth is Date 3. Each of these dates are more than twelve and one-half years but less than thirty seven and one-half years after the date of the birth of the transferor, Spouse. Therefore, Stepchild 1 and Stepchild 2 will be assigned to the first generation younger than the transferor. Accordingly, property passing under the terms of Trust 1 to the stepchildren will not be subject to the generation-skipping transfer tax.

Finally, Grandchild 1, Grandchild 2, and Grandchild 3 are the children of Child 4 who died in 1985 and are also the grandchildren of Grantor. Under § 2651(e)(1), if an individual is a descendant of the parent of the transferor's spouse or former spouse and the individual's parent who is a lineal descendant of the parent of the transferor's spouse or former spouse is dead at the time the transfer is subject to a tax imposed by Chapter 11, the individual shall be treated as if the individual were a member of the generation that is one generation below the lower of the transferor's generation or the generation assignment of the youngest living ancestor of the individual who is also a descendant of the parent of the transferor (or the transferor's spouse or former spouse). If Grandchild 1, Grandchild 2, and Grandchild 3 survive Spouse, they will have satisfied the requirements set forth in § 2651(e)(1) when the transfers are subject to the tax imposed under Chapter 11. Accordingly, the transfers from Trust 1 to the grandchildren will not be subject to the generation-skipping transfer tax.

In addition, if a grandchild does not survive Spouse but is survived by children (i.e., great grandchildren of Grantor), the children of the deceased grandchild shall be treated as a member of the generation that is one generation below the transferor's generation. In this situation, transfers from Trust 1 to the children of the grandchildren will not be subject to the generation-skipping transfer tax.

Under Article 7.1, Trust 2 will be funded with the balance of the trust estate remaining after Trust 1 is funded. Trust 2 will be held as a marital trust for the benefit of Spouse; however, the personal representative of Grantor's estate will not make the QTIP election with respect to this trust. Accordingly, Grantor will remain the transferor of the property in Trust 2 for GST purposes. You have represented that, if Grantor predeceases Spouse, the personal representative of Grantor's estate will allocate Grantor's exemption provided in § 2631(a) to Trust 2. Assuming the amount of exemption under § 2631(a) allocated to Trust 2 at Grantor's death results in an applicable fraction that is equal to 1.000 and an inclusion ratio of zero, no transfer from this trust to a skip person will be subject to the generation-skipping transfer tax under Chapter 13. See, § 2642(a)

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.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely yours,

Assistant Chief Counsel
(Passthroughs and Special Industries)

By _____
George Masnik
Chief, Branch 4

Enclosure (1)
Copy for § 6110 purposes