

AMERICAN BAR ASSOCIATION -- SECTION OF TAXATION

2006 Joint Fall CLE Meeting

TITLE: Extensions of Time to Make Timely GST Exemption Allocaitons and Reverse QTIP Elections

AUTHOR: Plaine, Lloyd Leva

PANEL: GST Traps for the Unwary in Preparation of the Form 709

DATE: 10/21/06

COMMITTEE: Section Program: Generation Skipping Transfers Committee (PT)

NOTE: This material was produced in connection with ABA Section of Taxation and Section of Real Property, Probate and Trust Law continuing legal education programs. It represents the statements and views of the author and does not necessarily represent the official policies or positions of the American Bar Association or the ABA Sections of Taxation and Real Property, Probate and Trust Law. The American Bar Association, the Section of Taxation and the Section of Real Property, Probate and Trust Law do not accept responsibility for the accuracy of the information in this paper, nor for any interpretation or application by the reader of the information contained in this paper. This paper is not intended to be, nor should it be construed as constituting, the opinion of, or legal or tax advice with regard to specific case or transaction by the author, the Tax Section, the Real Property, Probate and Trust Law Section or the American Bar Association.

Extensions of Time to Make Timely GST Exemption Allocations and Reverse QTIP Elections

By Lloyd Leva Plaine, Esq.
Sutherland Asbill & Brennan LLP
Washington, D.C.

©September 2006

This article discusses various procedures by which a taxpayer may seek an extension of time to make a timely GST exemption allocation under Sections 2642(g)(1) and 2632 of the Internal Revenue Code of 1986, as amended (“IRC”), and by which an estate may seek an extension of time to make a “reverse” QTIP election.¹

ALLOCATION OF GST EXEMPTION

The rules relating to the GST tax and the allocation of GST exemption are complex, and the forms on which the GST exemption is allocated, United States Gift (and Generation-Skipping Transfer) Tax Return (“Form 709”) and United States Estate (and Generation-Skipping Transfer) Tax Return (“Form 706”), are not user-friendly. As a result, there have been many errors made by taxpayers with respect to the allocation of their GST exemptions. The majority of these errors (which are far too easy to make) have included the following: failure to make any allocation, failure to make a timely allocation, allocation on an incorrect schedule of the Form 709 or Form 706, allocation of an incorrect amount (including incorrectly reducing the amount of the required

With appreciation to Wendy Wilkenfeld, Esq. for her able assistance with this article. An earlier version of this article, also published by Lloyd Leva Plaine, appeared in the April 2003 Trusts & Estates magazine. Part of this article was based on an earlier outline by Pam Schneider, Carol Harrington and Lloyd Leva Plaine.

¹ A reverse QTIP election is an election under IRC Section 2652(a)(3) to treat property that is qualified terminable interest property (“QTIP”) under IRC Section 2056(b)(7) as if, for GST tax purposes, no QTIP election had been made with respect to such property.

allocation by the annual exclusion from gift tax), and allocation to the wrong trust. Such missed or erroneous allocations create significant potential GST tax liability and can lead to lawsuits.² Thus, IRC Section 2642(g)(1), which was enacted as part of the Economic Growth and Tax Relief Reconciliation Act (“EGTRRA”)³ and authorizes the IRS to grant extensions of time to allocate GST exemption, was a needed and welcome addition to the IRC.⁴ Since the enactment of IRC Section 2642(g)(1), two different procedures with different eligibility requirements and levels of complexity have become available to taxpayers seeking extensions of time to allocate their GST exemptions.

As part of Congress’ recognition that, because of the complexity of the GST tax rules, there were many taxpayers whose GST exemptions were not allocated when they should have been, it included IRC Section 2632(c) as part of EGTRRA. This section causes a taxpayer’s GST exemption to be allocated automatically in many of the cases where errors were occurring. Under IRC Section 2632(c)(5), the taxpayer can choose to elect out of this automatic allocation of his or her GST exemption or to elect to treat a trust as a GST Trust to which the automatic rules would apply. As a result of the enactment of IRC Section 2632(c), some taxpayers now found that their GST exemptions had been allocated without their knowledge and when the

² PLR 9736032 describes a settlement of such a lawsuit.

³ Pub. L. No. 107-16, 115 Stat. 38 (2001).

⁴ For a discussion of all the GST tax changes made by EGTRRA, including the one that is the subject of this article, see “Generation-Skipping Transfer Tax Planning After the 2001 Act - Mostly Good News,” by Carol A. Harrington, Carlyn S. McCaffrey, Lloyd Leva Plaine and Pam H. Schneider, Journal of Taxation, Vol. 95, No. 3, September 2001, p. 143. For a comprehensive discussion of the GST tax, see the treatise, Generation-Skipping Transfer Tax, by Carol A. Harrington, Lloyd Leva Plaine, Howard M. Zaritsky (RIA/Warren Gorham & Lamont, 2d edition, 2001, with supplements).

allocation of exemption was not intended. Relief is available for these taxpayers as it is for those whose GST exemptions were not allocated when they should have been.

Requirements for Section 9100 Relief

Treasury Regulations Section 301.9100-3 provides the standards used by the Service to determine whether to use its discretion to grant extensions of time to make certain tax elections in those situations where “the time for making the election is not prescribed by statute” (“9100 relief”). Prior to EGTRRA, the Service took the position that the time to allocate GST exemption was prescribed by statute. Thus, it had ruled that it could not grant discretionary extensions of time to make timely allocations of GST exemption.⁵

IRC Section 2642(g)(1) directs the Treasury Secretary to “by regulation prescribe such circumstances and procedures under which extensions of time will be granted” (1) to make a timely allocation of GST exemption to gifts and to transfers at death, (2) to make elections out of the automatic allocation of GST exemption to lifetime direct skips (IRC Section 2632(b)(3)), and (3) to make elections in and out of the automatic allocation of GST exemption to indirect skips (IRC Section 2632(c)(5)).

IRC Section 2642(g)(1) provides that, in determining when to grant relief, the IRS is to consider “all relevant circumstances, including evidence of intent contained in the trust instrument or instruments of transfer and such other factors as the [Treasury] Secretary deems relevant.” In addition, the provision states “[f]or purposes of determining whether to grant relief

⁵ See PLRs 9827032, 9813013, 9226014. In contrast, both prior to and after EGTRRA, automatic extensions of time to allocate GST exemption will be granted under Treas. Reg. § 301.9100-2 if a Form 709 or 706 was timely filed and a corrective return is filed on which the allocation of GST exemption is made within 6 months of the due date of the Form 709 or 706 (without extensions). The corrective return must contain the statement “FILED PURSUANT TO § 301.9100-2”. See PLR 9718020.

under this paragraph, the time for making the allocation (or election) is treated as if not expressly prescribed by statute.” This latter provision was added specifically to enable the Service to grant 9100 relief.

If the relief authorized by IRC Section 2642(g)(1) is granted, then the gift tax or estate tax value of the transfer to a trust is used for determining the amount of GST exemption to be allocated.⁶ In Notice 2001-50,⁷ the IRS confirmed that 9100 relief will be available in connection with GST exemption allocation. The Notice also stated:

[R]elief will be granted if the taxpayer establishes to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith and that the grant of relief will not prejudice the interests of the government. Taxpayers requesting relief should follow the procedures for requesting a private letter ruling under § 301.9100 contained in section 5.02 of Rev. Proc. 2001-1 (or its successor), 2001-1 I.R.B. 1, 13.

Acting reasonably and in good faith.

Treasury Regulations Section 301.9100-3(b)(1) sets out five circumstances, any one of which is sufficient, under which the taxpayer will be deemed to have acted reasonably and in good faith.⁸

(1) The taxpayer’s application for relief is made prior to discovery of the missing election or application for relief by the IRS.

(2) The taxpayer failed to make the election because of certain intervening events beyond the taxpayer’s control.

⁶ The Conference Report to H.R. 1836, H. Rept. 107-84 (May 26, 2001) (“Conference Report”), p. 202.

⁷ 2001-34 I.R.B. 189.

⁸ Some of this article is drawn (with permission) from an article by Douglas L. Siegler, Esq., Sutherland Asbill & Brennan LLP, entitled “When Bad Things Happen to Good People: Section 9100 Relief for Late Tax Elections,” 32 University of Miami Heckerling Institute on Estate Planning (1998), Ch. 12.

(3) The taxpayer failed to make the election because, after exercising reasonable diligence (taking into account the taxpayer's experience and the complexity of the return or issue), the taxpayer was unaware of the necessity of the election.

(4) The taxpayer reasonably relied on the written advice of the IRS.

(5) 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 or application for relief. Not all reliance, however, will be deemed to be reasonable. The taxpayer will not be considered to have reasonably relied upon a tax professional if the taxpayer knew or should have known that the tax professional was not competent to render advice on the election, or if the taxpayer knew or should have known that the tax professional was not aware of all relevant facts.

Regardless of whether the application for relief is made before or after discovery by the IRS, there are two circumstances under which the taxpayer will not be considered to have acted reasonably and in good faith, and therefore the taxpayer would be ineligible for relief for the failure to allocate GST exemption. First, no taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer was fully informed of the required election and related tax consequences and chose not to file the election. Second, a taxpayer will not be considered to have acted reasonably and in good faith if the taxpayer "uses hindsight" in requesting relief. The regulations make clear that, absent strong proof that the decision to seek 9100 relief did not involve hindsight, when specific facts have changed since the original due date of the election that make an election advantageous to a taxpayer, the IRS will not ordinarily grant relief.

Interests of government prejudiced.

Treasury Regulations Section 301.9100-3(c)(1) describes the two circumstances under which the interests of the government are deemed to be prejudiced. First, such prejudice arises if granting relief “would result in a taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money).”⁹ If the tax consequences of the election affect more than one taxpayer, the determination of whether the interests of the government are prejudiced must be made by looking at the tax liability of all the affected taxpayers, in the aggregate. Second, the interests of the government will ordinarily be prejudiced when the tax year in which the regulatory election should have been made, or any tax year affected by the election had it been made timely, are closed by the statute of limitations before the taxpayer’s receipt of a ruling granting 9100 relief.¹⁰

Procedural requirements for granting of discretionary relief.

Treasury Regulations Section 301.9100-3(e) sets out numerous procedural requirements that must be complied with when requesting discretionary relief through a letter ruling request. The purpose of these requirements is to provide written evidence that the taxpayer acted reasonably and in good faith and that the interests of the government will not be prejudiced. This information includes:

⁹ Treas. Reg. § 301.9100-3(c)(1)(i).

¹⁰ See Treas. Reg. § 301.9100-3(c)(1)(ii). However, the IRS may nevertheless grant relief to the taxpayer in such circumstances if an independent auditor, not involved with the failure to make the election in a timely fashion, certifies that the interests of the government will not be prejudiced by virtue of a decreased tax liability. Further, with respect to the allocations of GST exemption, the rules may be more liberal in this area because the legislative history of IRC Section 2642(g)(1) indicates that extensions of time are to be granted without regard to whether any period of limitations has expired. Conference Report at p. 202.

(1) Information concerning when the applicable return, form or document used to make the election was required to be filed and when it was actually filed (and the taxpayer must submit a copy of any documents referring to the election);¹¹

(2) Disclosure of any IRS examination by a district director or appeals officer of any return for the tax year in which the election should have been made or which would be affected by a timely made election and of any federal judicial proceeding involving the return (and the IRS must be notified if an examination of any such return is opened while the request for 9100 relief is pending);¹²

(3) The sworn affidavit of the taxpayer (or his or her representative with respect to tax matters) must set out in detail the events that led to the failure to make a valid regulatory election and the discovery of the failure, and the affidavit must also describe the engagement of any qualified tax professional, the responsibilities of the professional, and the extent of the taxpayer's reliance on the professional;¹³ and

(4) Sworn affidavits from individuals having knowledge or information about the events that led to the failure to make a valid regulatory election and to the discovery of the failure, including the taxpayer's tax return preparer, any individual (including an employee of the taxpayer) who made a substantial contribution to the preparation of the return, and any other

¹¹ Treas. Reg. §§ 301.9100-3(e)(4)(ii) and (iii). Also see Rev. Proc. 2006-1, 2006-1 I.R.B.1, which sets forth the procedures for requesting a private letter ruling.

¹² Treas. Reg. § 301.9100-3(e)(4)(i).

¹³ Treas. Reg. § 301.9100-3(e)(2). In addition, the affidavit must include the name, current address, and taxpayer identification number of the affiant and must be signed and accompanied by a dated declaration stating that, under penalties of perjury, "I have examined this request, including accompanying documents, and, to the best of my knowledge and belief, the request contains all relevant facts relating to the request, and such facts are true, correct, and complete."

accountant or attorney, knowledgeable in tax matters, who advised the taxpayer in connection with the election.¹⁴

In addition, because the regulations make clear that the request for 9100 relief does not suspend the statute of limitations, the IRS may, as a condition to granting the requested relief, require the taxpayer to consent to an extension of the statute of limitations for the assessment of taxes in accordance with IRC Section 6501(c)(4) for the tax year in which the election should have been made and all tax years affected by a timely made election.¹⁵

Letter Rulings Granting 9100 Relief

The IRS has issued many private letter rulings granting taxpayers an extension of time under Treasury Regulations Section 301.9100-3 to make timely allocations of their GST exemptions.¹⁶ Under these rulings, the taxpayer is to file a supplemental return and allocate the GST exemption (within the period of the extension granted--often 60 days from the date the ruling is issued).¹⁷ The allocations are to be effective as of the date of the original transfer, and the amount of GST exemption to be allocated is determined by the gift or estate tax value of the transfer (whichever is relevant).

¹⁴ Treas. Reg. § 301.9100-3(e)(3). These affidavits must also describe the engagement, the responsibilities of the affiant, and the advice provided to the taxpayer. Additionally, the affidavit must be accompanied by a declaration similar to that described in the preceding note.

¹⁵ Treas. Reg. § 301.9100-3(d)(2).

¹⁶ In fact, there have been so many requests for letter rulings that the IRS and Department of the Treasury created an alternate procedure by which to grant extensions of time to allocate GST exemption. Rev. Proc. 2004-46, 2004-31 I.R.B. 142, discussed below, is a less time-consuming process that taxpayers who meet the requirements can choose. The letter ruling process remains available to other taxpayers.

¹⁷ One should not place the current year on the face of the supplemental return, as the Service has in at least one such case returned it—erroneously mistaking it for an early filing of a Form 709 for the current year. Instead, the return should be filed as a Form 709 for the year in which the relevant transfer was made.

Private letter rulings have been issued granting extensions of time to make a timely allocation of GST exemption or elect out of the automatic allocation of GST exemption under IRC Section 2632(c)(5) in all of the following situations in each of which the taxpayer relied on a “qualified tax professional” and acted reasonably and in good faith.

Time of filings.

- Form 709 was timely filed but gifts were reported on the wrong schedules and no GST exemption was allocated on the return. Although not set forth in the ruling, it is the author’s understanding that about 4 years after the gift tax returns were filed, supplemental returns were filed attempting to confirm that timely allocations had been made on the original returns, and if timely allocations had not in fact been made, then the supplemental returns provided that late allocations were to be made. The extension applied to both the gift made by the spouse who was still living¹⁸ as well as to the gift made by the now-deceased spouse.¹⁹

- Forms 709 were timely filed but no GST exemption was allocated on them.²⁰

- Form 709 was filed late by a law firm and no GST exemption was allocated on it.²¹

- Form 709 was not filed.²²

¹⁸ PLR 200212024.

¹⁹ PLR 200212025 (the request was filed after the decedent’s death but prior to the filing of the Form 706).

²⁰ PLRs 200633014, 200626008, 200616022, 200613021, 200604005, 200603023, 200324049.

²¹ PLRs 200614025, 200218010.

²² PLRs 200633014, 200620003, 200616022, 200608004, 200606034, 200606002, 200229032.

- Form 709 was not filed, and Form 706 was filed without Schedule R (the schedule on which GST exemption is allocated).²³
- Form 709 was filed, but no GST exemption was allocated due to secretarial error. The gift was treated in the bank's database as a gift not subject to GST tax and as gift made one-half by each spouse (when in fact the gift was made by one spouse and the spouses gift-split).²⁴
- Forms 709 were filed, but the amounts of the transfers were incorrectly reported and an insufficient amount of GST exemption was allocated.²⁵
- Forms 709 were not filed, because the accountant incorrectly believed that they were not required.²⁶
- Form 709 was timely filed, and GST exemption was incorrectly allocated in an amount equal to the actuarial value of a grandchild's interest instead of allocating an amount equal to the value of the property transferred to the trust.²⁷
- Forms 709 were timely filed but no GST exemption was allocated, because the accountant mistakenly believed that the transfers were direct skips in trust that had a zero inclusion ratio.²⁸

²³ PLR 200618001.

²⁴ PLR 200218001.

²⁵ PLR 200620003.

²⁶ PLR 200629016.

²⁷ PLR 200236019.

²⁸ PLR 200618006.

- Form 709 was timely filed to reflect gifts to pooled income funds under which a grandchild was to receive income for life. The accountant did not allocate GST exemption, because the accountant believed each transfer had a zero inclusion ratio due to the transfer's qualification for the gift tax annual exclusion and likewise incorrectly believed that the transfer qualified under IRC Section 2642(c).²⁹

- Form 709 was not filed because, although it was not a permissible reduction, the tax professional incorrectly subtracted annual exclusions in determining amount of GST exemption to allocate and erroneously concluded no GST exemption needed to be allocated.³⁰

- Form 709 was timely filed, but no GST exemption was allocated, and then a late allocation was made.³¹

- Forms 709 were timely filed, but no GST exemption was allocated. A taxable termination occurred.³²

- Form 709 was timely filed, but no GST exemption was allocated. A taxable termination occurred, and GST tax was paid.³³

- Form 709 was timely filed to report a gift that was subject to an estate tax inclusion period ("ETIP"). No Form 709 was filed to allocate GST exemption at the end of the

²⁹ PLR 200303053.

³⁰ PLRs 200236019 and 200229032

³¹ PLR 200308037. See also PLRs 200238018 and 200407005. Although one cannot tell from the face of PLR 200238018, it is that author's understanding that a late allocation of GST exemption was made prior to seeking relief.

³² PLRs 200625013, 200619015, 200608008.

³³ PLR 200240019.

ETIP. Child died during the ETIP, and a GST occurred at end of the ETIP. An extension was granted to make a timely allocation of GST exemption at the end of the ETIP and was effective as of the end of the ETIP.³⁴

- Form 709 was timely filed and GST exemption was allocated to cash and other assets that were transferred to a trust. The transfer of an insurance policy to the trust was not reported. The GST exemption was allocated on the incorrect line of the Form 709, and no Notice of Allocation was attached. An amended Form 709 was filed that changed the amount of the transfer and the amount of GST exemption to be allocated, but otherwise made the same errors. The IRS found that the allocation of GST exemption was effective, because the taxpayer substantially complied with the requirements and granted an extension of time to make a timely allocation of GST exemption to the transfer of the life insurance policy.³⁵

- Form 709 was timely filed but did not reflect all gifts, and no allocation of GST exemption was made. The IRS informed taxpayers that earlier Form 709 was being examined.³⁶

- Form 709 was timely filed, but the accountant failed to allocate GST exemption. The attorney discovered the error prior to the return being audited. Pursuant to the audit of the return, the taxpayer agreed to increase the value of the gift and paid gift tax deficiency. It is unclear when the request for relief was filed, but it was granted after the audit was completed.³⁷

³⁴ PLR 200236004.

³⁵ PLR 200626007. See IRC § 2642(g)(2) which was also added by EGTRRA. It deals with the determination of when there has been substantial compliance with respect to the allocation of GST exemption, thus making the allocation effective.

³⁶ PLR 200236016.

³⁷ PLR 200303022.

- Forms 709 were timely filed by a husband and wife (who lived in a community property state) after making equal transfers to each of two trusts, one for the benefit of their son and his descendants and one for the benefit of their daughter and her descendants. No GST exemption was allocated on the returns. The wife died and her GST exemption was allocated to the transfers by her executor on Form 706. The husband made another transfer and timely filed Form 709, but no GST exemption was allocated. The husband died when the GST exemption was equal to \$1,120,000. His executor allocated \$120,000 to the daughter's trust and attached a statement allocating \$1,000,000 to the daughter's trust if the extension of time to make a timely allocation was not granted. The daughter died prior to the date on which the ruling request was filed. The husband's estate was granted an extension of time to make allocations of his GST exemption to the portion of both the son's trust and the daughter's trust for which he is the transferor, but the ruling stated the GST exemption had to be allocated equally among the trusts.³⁸

- Form 706 was timely filed and an effective QTIP election was made, but the trust was not severed, nor was a reverse QTIP election made. An extension was granted to sever the QTIP trust, make the reverse QTIP election, and allocate GST exemption.³⁹

- Form 706 was filed late and effective QTIP and reverse QTIP elections were made, but the attempt to allocate GST exemption on the late return was ineffective.⁴⁰

³⁸ PLR 200604024.

³⁹ PLR 200626010.

⁴⁰ PLRs 200223016, 200608021 (although it does not expressly state that QTIP and reverse QTIP elections were made).

Electing out of automatic allocation

- Forms 709 were timely filed, but the taxpayers did not elect out of automatic allocation under IRC Section 2632(c)(5). Amended Forms 709 that were subsequently filed did not include the election out of automatic allocation.⁴¹

- Form 709 was timely filed with respect to a transfer to a qualified personal residence trust (“QPRT”). IRC Section 2632(c)(5), providing for the automatic allocation of GST exemption, was enacted between the date of the transfer and the date of the close of the ETIP. GST exemption was automatically allocated.⁴²

Reliance on qualified tax professionals.

- Taxpayer’s legal counsel and his tax attorney discussed allocation of GST exemption with the taxpayer and intended that GST exemption be allocated to the trust. However, when the attorney conveyed documents to the taxpayer’s accountant to prepare the return, the attorney did not tell the accountant to allocate, so no allocation was made.⁴³

- The taxpayer’s attorney wrote a letter advising the taxpayer to allocate, but the taxpayer’s accountant incorrectly advised the taxpayer not to allocate because the transfers qualified for the gift tax annual exclusion.⁴⁴

⁴¹ PLR 200627018.

⁴² PLR 200613006.

⁴³ PLR 200240019.

⁴⁴ PLR 200229032.

- As a result of an oversight, the taxpayer’s attorney did not timely file a gift tax return and allocate. The attorney then filed Form 709 late, but no GST exemption was allocated on it “because of the uncertainty as to the proper procedure for making late allocations.”⁴⁵

- The taxpayer’s attorney advised the taxpayer to allocate, but no allocation was made, as the attorney incorrectly assumed that the taxpayer’s accountant would make the allocation.⁴⁶

- The taxpayer’s attorney advised the taxpayer of need to allocate, but when the attorney prepared relevant Forms 709, the attorney inadvertently failed to allocate.⁴⁷

- The taxpayer’s attorney advised the accountant to allocate, but the accountant failed to allocate due to administrative problems.⁴⁸

- The taxpayer’s accountant and the bank that was serving as trustee inadvertently failed to communicate, and Forms 709 were filed but no GST exemption was allocated.⁴⁹

- The attorney who drafted the trust and the accountant who prepared the Forms 709 inadvertently failed to allocate. Upon later reviewing the returns, the attorney noticed the omission.⁵⁰

⁴⁵ PLR 200218010.

⁴⁶ PLR 200243042.

⁴⁷ PLR 200324032.

⁴⁸ PLR 200243037.

⁴⁹ PLR 200618005.

⁵⁰ PLR 200324044.

- The taxpayer hired a law firm to draft a trust agreement and prepare the gift tax return. The new attorney noticed that the former attorney had failed to allocate the taxpayer's GST exemption. Affidavits from the taxpayer and the former attorney discussed the taxpayer's goal of achieving "full estate plan advantages." The attorney admitted that he made a mistake by not allocating.⁵¹

- Letter ruling silent as to whether any qualified tax professional was involved.⁵²

Simplified Alternate Method—Rev. Proc. 2004-46

Revenue Procedure 2004-46, 2004-31 I.R.B 142 (August 2, 2004) was issued in response to the large number of private letter ruling requests received by the IRS after the enactment of IRC Section 2642(g). It allows extensions of time to allocate GST exemption to be granted through a less time-consuming process and without charging the taxpayer a user fee; however the alternate method is only available in limited situations.⁵³

The Revenue Procedure states:

[T]he Service has issued several letter rulings under §301.9100-3 granting an extension of time to make a timely allocation in situations in which a transfer to a trust qualified for the gift tax annual exclusion under §2503(b), but was not deemed to have a zero inclusion ratio because the trust did not meet one or more of the requirements of §2642(c)(2)⁵⁴ (for example, because there was more than

⁵¹ PLR 200324049.

⁵² PLR 200237021.

⁵³ It is the author's understanding that the Revenue Procedure was intended to apply to a situation that was present in many rulings requests filed for extensions of time to allocate GST exemption—annual exclusion gifts to life insurance trusts. Although the Rev. Proc. applies only to annual exclusion gifts, it is not limited in its applicability to transfers to insurance trusts.

⁵⁴ Under IRC Section 2642(c)(2), direct skip transfers to certain trusts where the transfer qualifies for and utilizes the gift tax annual exclusion have an inclusion ratio of zero without using any GST exemption. Further, other transfers that are direct skips receive an automatic

one beneficiary of the trust). In most of these cases, the transferor failed to allocate GST exemption to the trust on a timely filed gift tax return because the transferor was not aware of the need to affirmatively allocate the exemption to the transfers.⁵⁵ The Service believes that in these cases, it is appropriate to provide an alternate simplified method to obtain an extension of time to make an allocation of GST exemption, provided that certain requirements (set forth in sections 3 and 4 of this revenue procedure) are met. In such a case, the transferor's GST exemption remaining at the time the gift tax return is filed pursuant to this revenue procedure may be allocated to the transfer based on the value of the property as of the date of the transfer.

Therefore, the Revenue Procedure only applies to a taxpayer who satisfies the following requirements:

- “(1) On or before December 31, 2000, the taxpayer made or was deemed to have made a transfer by gift to a trust from which a GST may be made;
- “(2) At the time the taxpayer files the request for relief under this revenue procedure, no taxable distributions have been made and no taxable terminations have occurred;
- “(3) The transfer qualified for the annual exclusion under §2503(b), and the amount of the transfer, when added to the value of all other gifts by the transferor to that

allocation of GST exemption even if they do not qualify for or utilize the gift tax annual exclusion (IRC Section 2632(b)).

⁵⁵ In PLR 200303053, Form 709 was timely filed to reflect gifts to pooled income funds under which grandchild was to receive income for life. The accountant did not allocate the taxpayer's GST exemption, believing each transfer had a zero inclusion ratio due to its qualification for the gift tax annual exclusion and incorrectly believing the transfer qualified under IRC Section 2642(c). In PLR 200236019 and PLR 200229032, Form 709 was not filed because, although it was not a permissible reduction, the tax professional incorrectly subtracted annual exclusion amounts when determining the amount of GST exemption to allocate and erroneously concluded that no GST exemption needed to be allocated.

donee in the same year, was equal to or less than the amount of the applicable annual exclusion for the year of the transfer;^[56]

“(4) No GST exemption was allocated to the transfer, whether or not a Form 709 was filed;^[57]

“(5) At the time the taxpayer files a request for relief under this revenue procedure, the taxpayer has unused GST exemption available to allocate to the transfer.”

In addition, the following requirements must be met:

“(1) File a Form 709 for the year of the transfer to the trust, regardless of whether a Form 709 had been previously filed for that year. State at the top of the Form 709 that the return is ‘FILED PURSUANT TO REV. PROC. 2004-46.’

“(2) Report on the Form 709 the value of the transferred property as of the date of the transfer.

⁵⁶ This requirement presumably is made for simplicity reasons; however, in the author’s view it narrows the application of the Revenue Procedure unnecessarily. Gifts qualify for the annual exclusion in chronological order (Treas. Reg. §25.2503-2(a)); therefore, it should have only been necessary that gifts to the donee made earlier in the calendar year than the gift in question plus the gift in question did not exceed the annual exclusion.

⁵⁷ It is unclear why a taxpayer who recognized an error and made a late allocation to an annual exclusion transfer should not be allowed relief under the Revenue Procedure. Specifically, a transferor who has made a late allocation during life (described in IRC Section 2642(b)(3)) should be treated no worse than a transferor who had not attempted to cure the missed or flawed allocation before requesting relief under the Revenue Procedure and should be permitted to apply for relief under the Revenue Procedure to have the GST exemption allocation effective as of the date of the gift. Because the allocation pursuant to a grant of relief under the Revenue Procedure should be treated as creating the inclusion ratio as of the date of the gift, *i.e.*, as though the allocation was timely made, the inclusion ratio, should, in light of the relief granted, be zero. Therefore, the late allocation should be void (except with respect to a charitable lead annuity trust), because, under Treasury Regulation Section 26.2632-1(b)(2)(i), “an allocation of GST exemption to a trust is void to the extent the amount allocated exceeds the amount necessary to obtain an inclusion ratio of zero with respect to the trust.” This has proven to be the case in letter rulings issued under IRC Section 2642(g)(1) set forth in PLRs 200238018 and 200308037 and 200407003 (although one cannot tell this from the text of PLR 200238018), but such situations are not covered by the Revenue Procedure.

“(3) Allocate GST exemption to the trust by attaching a statement to the Form 709 entitled ‘Notice of Allocation.’ The notice of allocation must contain the following information:

“(a) clear identification of the trust, including the trust’s identifying number, as defined in § 6109 and the regulation thereunder, when applicable;

“(b) the value of the property transferred as of the date of the transfer (adjusted to account for split gifts, if any);

“(c) the amount of taxpayer’s unused GST exemption at the time this Notice of Allocation is filed (taxpayers are reminded that they must have unused GST exemption at the time this Notice of Allocation is filed);

“(d) the amount of GST exemption allocated to the transfer;

“(e) the inclusion ratio of the trust after the allocation; and

“(f) a statement that all of the requirements of section 3.01 of this revenue procedure have been met.”⁵⁸

Further, the Revenue Procedure requires the Form 709 must be filed on or before the date prescribed for filing the federal estate tax return for the transferor’s estate (determined with regard to any extensions actually obtained), regardless of whether an estate tax return is required to be filed.⁵⁹

⁵⁸ Provisions (1) through (5) above are the requirements of Section 3.01 and that section also states that the requirements of Section 4 must be met. The second set of provisions (1) through (3) are Section 4 requirements.

⁵⁹ It is unclear why a taxpayer’s estate is not allowed to apply for relief under this Revenue Procedure if the federal estate tax return due date has passed. The Revenue Procedure could have granted relief which would then also have the effect of nullifying any automatic allocation of GST exemption that had already occurred at death to the transfer in question in a sufficient amount so there was enough GST exemption to apply to the annual gifts at issue. This has been done in letter rulings under IRC Section 2642(g)(1). See PLR 200407005. It is the author’s

Upon receipt of a request for relief, the Service Center will determine whether the requirements for granting relief to make a GST exemption allocation under the Revenue Procedure have been satisfied and will notify the taxpayer of the result of this determination. If the Service Center determines that the requirements for granting relief to make a GST exemption allocation have been satisfied, the allocation will be effective as of the date of the transfer.⁶⁰

The Revenue Procedure provides that “[t]axpayers who are denied relief or who are otherwise outside the scope of this revenue procedure may request an extension of time to allocate GST exemption by requesting a letter ruling under the provisions of §301.9100-3. The procedural requirements for requesting a letter ruling are described in Rev. Proc. 2004-1, 2004-1 C.B. 1 (or its successors). If a letter ruling is requested after relief has been denied under this revenue procedure, the letter ruling request must indicate that relief was requested and denied under this revenue procedure. Rev. Proc. 2004-1, Appendix C, 2004-1 I.R.B. 70.”

REVERSE QTIP ELECTIONS

Revenue Procedure 2004-47, 2004-2 C.B. 169 (August 9, 2004), provides a greatly simplified procedure “for certain executors of estates and trustees of trusts to request relief to

understanding that this was done to cut down on work the Service Center would have to do since GST exemption would already have been automatically allocated.

⁶⁰ A grant of relief under the Revenue Procedure does not preclude a subsequent determination that the transfer is a transfer covered by the ETIP provisions of IRC Section 2642(f), *i.e.*, that it is an inter vivos transfer the value of which would be included in the transferor’s gross estate under chapter 11 (other than by reason of IRC Section 2035) if the transferor died immediately after making the transfer. If it is determined that the transfer is one described in IRC Section 2642(f), the GST exemption allocated pursuant to this Revenue Procedure would not be changed. The effective date and effect of that allocation of GST exemption would be governed by Treas. Reg. §26.2632-1(c) so that the allocation would be irrevocable but would not be effective until the end of the ETIP and would use in determining the inclusion ratio the value of property at the end of the ETIP.

make a late reverse qualified terminable interest property (QTIP) election” under IRC Section 2652. This method may be used as an alternative to the normal letter ruling process, and no user fee is charged.

To be eligible for relief under the Revenue Procedure, the following requirements, which are set forth in Section 4.02 of the Revenue Procedure, must be met:

(1) A valid QTIP election under IRC Section 2056(b)(7) was made for the property or trust on the Form 706 for the decedent’s estate;

(2) A reverse QTIP election was not made on the estate tax return as filed because “the taxpayer relied on the advice and counsel of a qualified tax professional and that qualified tax professional failed to advise the taxpayer of the need, advisability, or proper method to make a reverse QTIP election”;

(3) The decedent has sufficient unused GST exemption, *after the automatic allocation of the GST exemption under IRC Section 2632(e) and Treas. Reg. §26.2632-1(d)(2)*, to result in a zero-inclusion ratio for the reverse QTIP trust or property;⁶¹

(4) The estate is not eligible under Treasury Regulations Section 301.9100-2 for the automatic 6-month extension;

(5) The surviving spouse has not made a lifetime disposition of all or any part of his or her income interest in the QTIP; and

(6) Either the surviving spouse is alive or no more than 6 months have passed since the death of the surviving spouse.

The simplified procedure is expressly not available if:

⁶¹ As a practical matter, the simplified procedure of Rev. Proc. 2004-47 is only available if GST exemption was allocated to the entire QTIP on the estate tax return or the rules for allocating unused GST exemption in IRC Section 2632(e) will allocate sufficient GST exemption to the trust to produce an inclusion ratio of zero.

- (1) The transfer is an intervivos transfer;
- (2) The transfer is to a qualified domestic trust for the benefit of a non-citizen spouse;
- (3) The request for relief is made in conjunction with a request to extend the time to sever the trust or to allocate GST exemption to it.

Under the simplified procedure, the estate must file with the Cincinnati Service Center a request for an extension of time to make a reverse QTIP election. The request should have a cover sheet requesting relief that states at the top of the document "REQUEST FOR EXTENSION FILED PURSUANT TO REV. PROC. 2004-47."

The following items must be attached to the request for relief:

- (1) Copies of Parts 1 through 5 and Schedule M of the original estate tax return;
- (2) A properly completed Schedule R of Form 706 as required to make the reverse QTIP election;
- (3) A statement describing why the reverse QTIP election was not made on the estate tax return as filed;
- (4) A statement affirming that all of the requirements in section 4.02 of Rev. Proc. 2004-47 have been met;
- (5) A dated declaration, signed by the executor, that states: "Under penalties of perjury, I declare that, to the best of my knowledge and belief, the facts presented in support of this election are true, correct, and complete. In addition, all attachments provided in support of this request for relief are true and correct copies of the original documents."; and
- (6) A signed statement from the qualified tax professional on whom the taxpayer relied when preparing the original estate tax return. The statement must establish the tax professional's qualifications as a qualified tax professional and must include a dated declaration

that states: “Under penalties of perjury, I declare that, to the best of my knowledge and belief, the facts presented in support of this request for relief are true, correct, and complete.”

The proposed regulations state that if the Service Center determines that the requirements for granting relief under Rev. Proc. 2004-47 have been satisfied, the decedent remains, for GST tax purposes, the transferor of the QTIP trust or property. As a result, the decedent’s remaining GST tax exemption will be automatically allocated pursuant to IRC Section 2632(e) and Treas. Reg. §26.2632-1(d)(2) to the QTIP trust or property for which the reverse QTIP election was made, based on the value of the trust or property as finally determined for federal estate tax purposes. The Service Center will notify the taxpayer of this determination. A grant of relief does not:

- (1) Extend the time for allocating GST exemption;
- (2) Grant permission to allocate retroactively the decedent’s remaining GST

exemption; or

- (3) Grant permission to make a late severance of a trust included in the gross estate.⁶²

If relief is denied under the simplified procedure, the taxpayer may still seek relief under Treas. Reg. §301.9100-3, but the letter ruling request must indicate that relief was denied under Rev. Proc. 2004-47.

⁶² It is possible to make a QTIP and a reverse QTIP election for a trust that will be included in the surviving spouse’s gross estate for a reason other than IRC Section 2044. In such event the reverse QTIP election should not prevent the transferor from changing to the surviving spouse. However the proposed regulations do not appear to recognize this possibility.

CONCLUSION

Filing a private letter ruling request for an extension of time to make a timely allocation of GST exemption (or elect in or out of automatic allocation) is a valuable tool in curing errors that often occur with respect to the allocation of GST exemption, but before filing a ruling request, the taxpayer should determine if relief under Rev. Proc. 2004-46 is available. Likewise, Rev. Proc. 2004-47 presents a desirable alternative to seeking a private letter ruling for taxpayers requesting an extension of time to make the reverse QTIP election.