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Person To Contact: \_\_\_\_\_, ID No.

Telephone Number: \_\_\_\_\_

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Date:  
May 24, 2018

Legend

Settlor	=
Spouse	=
Child 1	=
Child 2	=
Child 3	=
Attorney 1	=
Attorney 2	=
Trust	=
Foundation	=
Date 1	=
Date 2	=
Year	=
Court	=
Court Order	=
State	=
State Statute 1	=
State Statute 2	=

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

This letter responds to your authorized representative's letter dated November 27, 2017, requesting rulings on the gift and estate tax consequences of the reformation of an irrevocable trust and an extension of time under § 301.9100 of the Procedure and Administration Regulations to allocate GST exemption under § 2642(g) of the Internal Revenue Code.

The facts and representations submitted are summarized as follows:

Settlor executed an irrevocable trust (Trust) on Date 1 for the benefit of Settlor's descendants. Trust was funded in Year. No additional gifts have been made to Trust since Year. Trust is governed by the laws of State. The current beneficiaries of Trust are Child 1, Child 2, and Child 3.

Article SECOND provides that the trustee will divide the trust property into three equal shares. Each share is to be named for one of Settlor's children. Each child is a beneficiary of an independent share of Trust.

Article THIRD paragraph (B) provides that the trustee may pay to or for the benefit of such child or his or her issue, such part of the net income and principal as the trustee deems advisable and in their respective best interests; provided however, that in all but an extraordinary emergency situation, distributions shall be limited to their medical and educational needs. Any net income not so paid may be added to principal.

Article THIRD paragraph (C) provides that upon the death of a child, the trustee shall distribute the remaining principal and all accrued and accumulated income to or for such one or more appointees as the child appoints by will (other than the child, the child's estate, the child's creditors or creditors of the child's estate).

Article THIRD paragraph (D) provides that any property not appointed by a child shall be distributed to child's then living issue by right of representation. Any distribution to an issue of child under the age of 30 will be held in further trust. If there are no issue of child the unappointed property shall be distributed to the Settlor's then living issue, and, if none, to Foundation.

Article THIRD paragraph (A) generally provides for withdrawal rights for the beneficiaries, specifically, that during the calendar year, the child may make withdrawals from any additions to the principal of the share during such year. This right of withdrawal may be exercised from time to time by a written request signed by the child (or, during any period when the child is legally incompetent, by his or her legal representative other than the Settlor) and delivered to the trustee. For the purpose of this paragraph, any withdrawal right with respect to any addition extends to the property, if any, in which such addition is invested. The trustee immediately shall notify the child in writing as to any addition, the existence of such right and the property to which it pertains. Notwithstanding the foregoing, if any addition is added to the share after December 1<sup>st</sup> of any given calendar

year, the child's withdrawal right with respect to such addition shall lapse on the thirty-first day after his or her receipt of the notice from the trustee. This withdrawal right is non-cumulative.

Settlor created and funded Trust in reliance on the advice of Attorney 1, who drafted Trust. Based on affidavits of Settlor, Spouse, and Attorney 1, Settlor created Trust to provide for his descendants of all generations, and to reduce the overall transfer taxes payable on Trust assets by ensuring that the assets held in Trust would not be includible in the children's gross estates upon the children's deaths, and to minimize the amount subject to GST tax by utilizing Settlor's and Spouse's GST exemption.

The withdrawal provision in Article THIRD paragraph (A) contains two drafting errors. First, Trust grants each child the right to withdraw the entire amount of any contribution to that child's separate share of the trust and fails to limit the withdrawal right to the gift tax annual exclusion amount causing the children to possess general powers of appointment (within the meaning of §§ 2514 and 2041) over the entire amount of the contribution to that child's separate share of Trust. Second, each child's withdrawal right over the assets contributed to Trust in any given year is non-cumulative and lapses in its entirety on an annual basis. Since the lapse is not limited to the greater of \$5,000 or 5 percent of the value of the trust assets, any lapse of a child's withdrawal right would be treated as a taxable transfer by that child under § 2514 to the extent that the property that could have been withdrawn exceeds in value the greater of \$5,000 or 5 percent of the aggregate value of the assets subject to withdrawal.

Settlor and Spouse each timely filed a Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return and elected to gift-split under § 2513 for Year. It is represented that at the time of the Year transfer to Trust, Settlor and Spouse each had their full GST exemption available to allocate and intended that it be allocated to the Year transfer to Trust. Settlor relied on Attorney 1 to advise him on the need to allocated GST exemption to Trust. However, Settlor and Spouse did not affirmatively allocate GST exemption to Trust on Form 709. No other transfers have been made to Trust, and no GST transfers have been made from Trust.

The errors were discovered when Settlor retained a new attorney, Attorney 2, to represent him in estate planning matters. Attorney 2 informed Settlor of the drafting errors that defeated the intent of the Settlor in establishing Trust. Trustee filed a petition in State Court requesting judicial reformation of the erroneous provision of Article THIRD, paragraph (A), effective as of the date Trust was originally created. On Date 2, Court allowed the petition and, in Court Order, reformed Trust to eliminate the scrivener's error retroactive to the date of Trust's creation.

As reformed, Trust limits the beneficiaries' withdrawal rights to the gift tax annual exclusion amount, and it limits the annual lapse of the withdrawal rights to the greater of \$5,000 or 5 percent of the value of the trust assets.

You have requested the following rulings:

1. As a result of the judicial reformation of Trust, Settlor's children, Child 1, Child 2, and Child 3, do not possess general powers of appointment (within the meaning of §§ 2514 and 2041) over their respective shares of Trust, except to the extent of each child's withdrawal rights under the reformed trust instrument.
2. The judicial reformation of Trust does not constitute, for federal gift and estate tax purposes, the exercise or release by any child of Settlor of a general power of appointment.
3. The lapse of any child's withdrawal right over Trust did not result in a gift for federal gift tax purposes.
4. No part of Trust property will be included in the gross estates of Settlor's children for federal estate tax purposes, except to the extent of each child's withdrawal rights under the reformed trust instrument exercisable on the child's death.
5. Settlor and Spouse request an extension of time under § 2642(g) of the Internal Revenue Code and § 301.9100-3 of the Procedures and Administration Regulations to allocate their respective GST exemption to the Year transfer to Trust.

#### Rulings 1-4

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

Section 2033 provides, generally, that the value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death.

Section 2041(a)(2) provides that the value of the gross estate includes the value of all property to the extent of any property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under §§ 2035 to 2038, inclusive. For purposes of § 2041(a)(2), the power of appointment shall be considered to exist on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even though the exercise of the power takes effect only on the expiration of a stated period after its exercise, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised.

Section 2041(b)(1) provides that for purposes of § 2041(a), the term “general power of appointment” means a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate.

Section 2041(b)(2) provides that the lapse of a power of appointment created after October 21, 1942, during the life of the individual possessing the power shall be considered a release of such power. The preceding sentence shall apply with respect to the lapse of powers during any calendar year only to the extent that the property, which could have been appointed by exercise of such lapsed powers, exceeded in value, at the time of such lapse, the greater of the following amounts: (A) \$5,000, or (B) 5 percent of the aggregate value, at the time of such lapse, of the assets out of which, or the proceeds of which, the exercise of the lapsed powers could have been satisfied.

Section 2501(a)(1) provides, generally, that a tax is imposed for each calendar year on the transfer of property by gift by any individual, resident or nonresident. Section 2511(a) provides that the gift tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2514(b) provides that the exercise or release of a general power of appointment created after October 21, 1942, shall be deemed a transfer of property by the individual possessing such power.

Section 2514(c) provides that for purposes of § 2514, the term “general power of appointment” means a power which is exercisable in favor of the individual possessing the power, his estate, his creditors, or the creditors of his estate.

Section 2514(e) provides that the lapse of a power of appointment created after October 21, 1942, during the life of the individual possessing the power shall be considered a release of such power. The rule of the preceding sentence shall apply with respect to the lapse of powers during any calendar year only to the extent that the property which could have been appointed by exercise of such lapsed powers exceeds in value the greater of the following amounts: (1) \$5,000, or (2) 5 percent of the aggregate value of the assets out of which, or the proceeds of which, the exercise of the lapsed powers could be satisfied.

In *Commissioner v. Estate of Bosch*, 387 U.S. 456 (1967), the Court considered whether a state trial court’s characterization of property rights conclusively binds a federal court or agency in a federal estate tax controversy. The Court concluded that the decision of a state trial court as to an underlying issue of state law should not be controlling when applied to a federal statute. Rather, the highest court of the state is the best authority on the underlying substantive rule of state law to be applied in the federal matter. If there is no decision by that court, then the federal authority must apply what it finds to be state law after giving “proper regard” to the state trial court’s determination and to relevant rulings of

other courts of the state. In this respect, the federal agency may be said, in effect, to be sitting as a state court.

State Statute 1 provides, in part, that a proceeding to approve or disapprove a proposed modification or termination of a trust, may be commenced by a trustee or a beneficiary. State Statute 2 provides, in part, that the court may reform the terms of a trust, even if unambiguous, to conform the terms to the settlor's intention if it is proved by clear and convincing evidence that the settlor's intent or the terms of the trust were affected by a mistake of fact or law.

In this case, an examination of the relevant trust instruments, affidavits, and representations of the parties indicate that the original terms of Article THIRD paragraph (A), are contrary to the intent of Settlor. The purpose of the reformation is to correct the scrivener's error, not to alter or modify the trust instrument. Accordingly, based on the facts submitted and the representations made, we conclude that as a result of the reformation of Trust, Settlor's children do not possess general powers of appointment (within the meaning of §§ 2514 and 2041) over their respective shares of Trust, except to the extent of each child's withdrawal rights under the reformed trust instrument. Further, we conclude that the judicial reformation of Trust does not constitute, for federal gift and estate tax purposes, the exercise or release of a general power of appointment by any child of Settlor. Accordingly, we conclude that the lapse of any child's withdrawal right over Trust did not result in a gift for federal gift tax purposes. Finally, we conclude that no part of the Trust property will be included in the gross estate of Child 1, Child 2, or Child 3 for federal estate tax purposes, except to the extent of each child's withdrawal rights under the reformed trust instrument exercisable on the child's death.

### Rulings 5

Section 2513(a)(1) provides, generally, that a gift made by one spouse to any person other than the donor's spouse is considered for purposes of the gift tax as made one-half by the donor and one-half by the donor's spouse, but only if at the time of the gift each spouse is a citizen or resident of the United States.

Section 2601 imposes a tax on every generation-skipping transfer (GST), which is defined under § 2611 as a taxable distribution, a taxable termination, and a direct skip.

Section 2602 provides that the amount of the GST tax is determined by multiplying the taxable amount by the applicable rate.

Section 2641(a) defines the applicable rate as the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer.

Under § 2642(a)(1), the inclusion ratio with respect to any property transferred in a generation-skipping transfer is generally defined as the excess of 1 over the "applicable

fraction.” The applicable fraction, as defined in § 2642(a)(2), is a fraction, the numerator of which is the amount of GST exemption under § 2631 allocated to the trust (or to property transferred in a direct skip), and the denominator of which is the value of the property transferred to the trust or involved in the direct skip.

Section 2631(a) provides that, for purposes of determining the inclusion ratio, every individual shall be allowed a GST exemption amount 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, shall be irrevocable.

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

Section 2632(a)(2) provides that the manner in which allocations are to be made shall be prescribed by forms or regulations issued by the Secretary.

Section 2642(g)(1)(A) provides that the Secretary shall by regulation prescribe such circumstances and procedures under which extensions of time will be granted to make an allocation of GST exemption described in § 2642(b)(1) or (2) and an election under § 2632(b)(3) or (c)(5). Such regulation shall include procedures for requesting comparable relief with respect to transfers made before the date of the enactment of this paragraph.

Section 2642(g)(1)(B) provides that in determining whether to grant relief under this paragraph, the Secretary shall take into account all relevant circumstances, including evidence of intent contained in the trust instrument or instrument of transfer and such other factors as the Secretary deems relevant. For purposes of determining whether to grant relief under this paragraph, the time for making the allocation (or election) shall be treated as if not expressly prescribed by statute.

Notice 2001-50, 2001-2 C.B. 189, provides that, under § 2642(g)(1)(B), the time for allocating the GST exemption to lifetime transfers and transfers at death, are to be treated as if not expressly prescribed by statute and taxpayers may seek an extension of time to make an allocation described in § 2642(b)(1) or (b)(2) under the provisions of § 301.9100-3.

Section 301.9100-1(c) provides that the Commissioner has discretion to grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 to make a regulatory election, or a statutory election (but no more than 6 months except in the case of a taxpayer who is abroad), under all subtitles of the Code except subtitles E, G, H, and I.

Section 301.9100-3 provides the standards used to determine whether to grant an extension of time to make an election whose due date is prescribed by a regulation (and not expressly provided by statute).

Requests for relief under § 301.9100-3 will be granted when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and that granting relief will not prejudice the interests of the government.

Section 301.9100-3(b)(1)(v) provides that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

Under § 2652(a)(1), for purposes of chapter 13, the term “transferor” means the decedent, in the case of any property subject to tax imposed by chapter 11 and, the donor, in the case of any property subject to tax imposed by chapter 12.

Section 26.2652-1(a)(1) of the Generation-Skipping Transfer Regulations provides that the individual with respect to whom property was most recently subject to federal estate or gift tax is the transferor of that property for purposes of chapter 13.

In this case, Settlor and Spouse each elected to gift-split under § 2513 on their respective timely filed Form 709 for Year. Thus, Settlor and Spouse are each treated as the transferor of one-half of the assets gifted to Trust in Year. Based on the facts submitted and the representations made, we conclude that the requirements of § 301.9100-3 have been satisfied. Therefore, Settlor and Spouse are granted an extension of time of 120 days from the date of this letter to allocate Settlor’s and Spouse’s available GST exemption to their respective share of the Year transfer to Trust. The allocations will be effective as of the respective date of the transfer to Trust and the value of the transfer to Trust as determined for federal estate tax purposes will be used in determining the amount of Settlor’s and Spouse’s GST exemption to be allocated to Trust.

This allocation should be made on supplemental Forms 709 and filed with the Cincinnati Service Center at the following address: Internal Revenue Service, Cincinnati Service Center — Stop 82, Cincinnati, OH 45999. A copy of this letter should be attached to the supplemental Forms 709.

A copy of this letter should be attached to any gift, estate, or generation-skipping transfer tax returns that you may file relating to these matters.

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.

Except as specifically ruled herein, we do not express nor imply any opinion concerning the tax consequences of the transaction or any subsequent transaction regarding Trust under the cited provisions or under any other provisions of the Code.

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

Sincerely yours,

Associate Chief Counsel  
Passthroughs & Special Industries

Lorraine E. Gardner

Lorraine E. Gardner  
Senior Counsel, Branch 4  
Office of the Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures

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cc: