ABOUT THE SPEAKER

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Brett is Board Certified in Estate Planning and Probate Law by the Texas Board of Legal Specialization and is a member of that organization's Exam Commission. Brett serves on the Board of Directors of the Houston Estate and Financial Forum and is an active member of the Texas Young Lawyers Association; the American Bar Association, Section of Real Property, Probate and Trust; the State Bar of Texas, Real Estate, Probate and Trusts Sections; the Houston Bar Association, Trusts and Estates Section; and the Houston Business and Estate Planning Counsel. Brett is also a Fellow of the Texas Bar Foundation.

Brett serves on the Board of Directors of Camp For All, an organization that provides a barrier-free camping experience for children with disabilities and illnesses, and is a past chairman of Camp For All's Young Professionals Board of Directors. He is active in the Houston Young Lawyer Association's Adopt an Angel Program which facilitates the "adoption" of disadvantaged children from area schools by law firms in the Houston area and provides the children with holiday gifts.

Brett has been named as both a Texas Super Lawyer "Rising Star" by Texas Monthly Magazine and one of Houston's top lawyers by H Texas Magazine for several years. In 2015, Brett was named by the Houston Business Journal as one of Houston's "Top 40 Under 40." Most recently, Brett was listed among Texas Super Lawyer's "Up-and-Coming 100" and as a "Best Lawyer in America."

THE HEART OF DARKNESS: A JOURNEY INTO THE GST JUNGLE

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Fundamentals of the GST Tax

- Transferor
  - Generation assignments for the imposition of the GST Tax ("GSTT") are determined relative to the transferor.
  - The transferor's GST Exemption ("GSTE") may be utilized to shelter transfers from the GSTT.

Fundamentals of the GST Tax

- Transferor
  - Example:

In 2017, Ross makes gifts of $5 million to various family members. For purposes of the GSTT, Ross is the transferor and whether a beneficiary is a "skip person" will be determined based on that beneficiary's age and relationship to Ross.

Fundamentals of the GST Tax

- Transferor
  - Example -

If Ross' gifts from the previous example would be subject to the GSTT (now or in the future), then Ross, as the transferor (and not the beneficiary), may allocate a portion of his GSTE to exempt the transfer from taxation.

Fundamentals of the GST Tax

- Transferor
  - The transferor is the person from whom the subject property was transferred.
  - A person holding a general power of appointment will become the transferor when the property to which the power applies is subject to estate or gift tax.
  - An individual will be treated as the transferor if federal estate or gift tax was imposed even if no property was actually transferred under local law.

Fundamentals of the GST Tax

- Transferor
  - Example

Ross transfers $100,000 to a new trust for his children and grandchildren. Ross' daughter, Emma, has a testamentary general power of appointment over the trust property. Emma will not be treated as the transferor of the trust until her death.

Fundamentals of the GST Tax

- Transferor
  - Example

Ross transfers $100,000 to a new trust for his children and grandchildren. Ross' daughter, Emma, has the right to withdraw $20,000 from the trust for a 90-day period following the transfer. Emma does not exercise the withdrawal right. Emma will become the transferor to the extent the lapsed right exceeds the greater of $5,000 or 5% of the value of the trust.

Fundamentals of the GST Tax

- Special Reverse QTIP Election
  - If property is transferred to a QTIP trust for the benefit of the donor's spouse, then the spouse will be treated as the transferor.
  - Exception – If a "reverse QTIP election" is made, however, then the original donor and not the donee spouse will be treated as the transferor.

Fundamentals of the GST Tax

- Transferor
  - Example -

Ross makes a gift to a QTIP trust for the benefit of Rachel, his spouse. If a QTIP election is made, then Rachel will be treated as the transferor of that trust because Rachel will be treated as the owner of the property in the trust. However, if a "reverse QTIP election" is also made under IRC § 2652, then for purposes of the GSTT only, Ross is still treated as the transferor of the trust.

Fundamentals of the GST Tax

- Special Reverse QTIP Election
  - The reverse QTIP election must match the QTIP election that was made for the trust.
    - Example –

    Ross creates a QTIP trust for the benefit of Rachel, his spouse. If the QTIP election is made for all of the property in the trust, then the reverse QTIP election must be made as to all or none of the trust.
  - Because a partial reverse QTIP election is not allowed, a separate reverse QTIP trust may need to be created in order to fully utilize both spouse's exemption amount.

Fundamentals of the GST Tax

- Skip Persons
  - A skip person is someone assigned to two or more generations below the transferor.
  - In most cases the generation assignments are based on family relationships to the transferor.

Fundamentals of the GST Tax

- Skip Persons ("family members")
  - If the donee is a lineal descendant of the transferor's grandparents, then the generational assignment is based on consanguinity.
  - The transferor's spouse or former spouse is assigned to the transferor's generation. Additionally, the consanguinity rules will apply to the relatives of the transferor's spouse.

Fundamentals of the GST Tax

- Skip Persons (non-"family" members)
  - If the donee is not a lineal descendant of the grandparents of the transferor or of his/her spouse, then generational assignments are based on age:
    - Individuals born within 12.5 years after the transferor are in the transferor's generation.
    - Individuals born 12.5 to 37.5 years after the transferor are one generation below (i.e., not skip persons).
    - Individuals born more than 37.5 years after the transferor are skip persons.

Fundamentals of the GST Tax

- Skip Persons Examples
  - Hugh (75) is married to Crystal (25). They both have children from previous marriages. Hugh is considering making large transfers in 2017.
  - Crystal = Non-skip person because she is the transferor's spouse.
  - Crystal's son, Sonny (4) = Non-skip person because he is a lineal descendant of the transferor's spouse.

Fundamentals of the GST Tax

- Skip Persons Examples
  - Crystal's niece, Carrie (10) = Non-skip person because she is a lineal descendant of the grandparents of the transferor's spouse.
  - Hugh's ex-wife, Barbi (35) = Non-skip person because she is the transferor's former spouse.
  - Barbi's nephew's wife, Jane (21) = Non-skip person because she is the spouse of a lineal descendant of the transferor's former spouse's grandparents.

Fundamentals of the GST Tax

- Skip Persons Examples
  - Hugh's grandson, Little Hugh (5) = Skip person.
  - Hugh's former roommate's daughter, Kendra (35) = Skip person because she is unrelated and more than 37.5 years younger.

Fundamentals of the GST Tax

- Skip Persons (Trusts)
  - A trust can be a skip person if:
    - All present interests are held by skip persons.
      - Example – Hugh makes a gift to a trust of which his grandchildren are currently entitled to receive distributions of income and principal.

Fundamentals of the GST Tax

- Trusts
  - A trust can also be a skip person if:
    - No person holds an interest in the trust; and
    - No distributions can ever be made to non-skip persons.
      - Example – Hugh makes a gift to a trust which provides that no distributions of income and principal may be made for 10 years. After 10 years the trust shall terminate and be distributed to Hugh's grandchildren.

Fundamentals of the GST Tax

- Skip Persons (Trusts)
  - Whether or not a trust is a skip person depends on who has a “present interest” in the trust.
  - A person has a present interest if he or she has a present right to or is a permissible recipient of the trust’s income or principal.
  - An interest will be disregarded if the interest is used primarily to avoid or postpone the GST tax.

Fundamentals of the GST Tax

- Skip Persons (Trusts)
  - The fact that the trust property may be used to discharge a person’s legal obligation of support will not create an interest in the trust if such use is discretionary.

Fundamentals of the GST Tax

- Skip Persons (Trusts)
  - Example -

Hugh establishes a trust for the benefit of his grandson, Little Hugh. The trustee may make distributions from the trust for Little Hugh’s support. Little Hugh’s father, Jeremy, would not have an interest in the trust because the ability of the trustee to satisfy Jeremy’s support obligation is discretionary.

If the trustee was required to make distributions from the trust for Little Hugh’s support, then Jeremy would have an interest in the trust.

Fundamentals of the GST Tax

- Skip Persons (Trusts)
  - A trust can also be an Indirect Skip if:
    - Non-skip persons and skip persons have a current interest in the trust.
      - Example – Hugh makes a gift to a trust which provides for current permissible distributions of income and principal to Hugh's son and grandchildren.

Fundamentals of the GST Tax

- Charities
  - Charities are considered to be non-skip persons.
  - A charity must have a mandatory right to receive current distributions of income or corpus from the trust in order to have an interest in a trust.

Fundamentals of the GST Tax

- Charities
  - Example

  Hugh creates a trust which makes annual distributions to one or more qualified charities that may be selected by the trustee. No charity has an interest in the trust because each charity chosen by the trustee is only a permissible current recipient of distributions from the trust.

Fundamentals of the GST Tax

- When is the GSTT imposed?
  - Direct Skips.
  - Taxable Terminations.
  - Taxable Distributions.

Fundamentals of the GST Tax

- Direct Skips
  - Transfer to a skip person which is subject to Estate or Gift Tax.
  - Includes outright transfers and transfers to trusts.
  - Taxed only once, regardless of how may generations are skipped.

Fundamentals of the GST Tax

- Direct Skips
  - Example – Elvis by gift conveys Graceland to his grandchild outright.
    - Taxable as a Direct Skip.
  - Example – Elvis by gift conveys Graceland to a trust of which his grandchild is the only permissible beneficiary during her life.
    - Taxable as a Direct Skip.

Fundamentals of the GST Tax

- Direct Skips
  - Example – Elvis by gift conveys Graceland to a trust of which his great-grandchild is the only permissible beneficiary during her life.
    - Taxable as a Direct Skip in the same manner as the previous example.

Fundamentals of the GST Tax

- Taxable Terminations
  - Generally occurs when an interest in a trust terminates and only skip persons may receive the subject property.
  - A termination is not a taxable termination if a non-skip person has an interest in such property or at no time thereafter may be a distribution be made to a skip person.

Fundamentals of the GST Tax

- Taxable Terminations
  - Example

Elizabeth establishes an irrevocable trust under which the income is to be paid to her child, Charles, for life. On the death of Charles, the trust principal is to be paid to Elizabeth's grandchild, William.

Since Charles has an interest in the trust, the trust is not a skip person and the transfer to the trust is not a direct skip. If Charles dies survived by William, a taxable termination occurs at Charles' death because Charles' interest terminates and thereafter the trust property is distributed to a skip person in a lower generation than Charles.

Fundamentals of the GST Tax

- Taxable Terminations
  - Example – Same facts, however, the trust initially provided for distributions to Charles and William and upon Charles' death was to continue for William's lifetime. Charles' death is still a taxable termination.
  - Example – Same facts, however, the trust principal distributes to William and Charles's brother on the death of Charles. A taxable termination would not occur because a non-skip person has an interest in the trust.

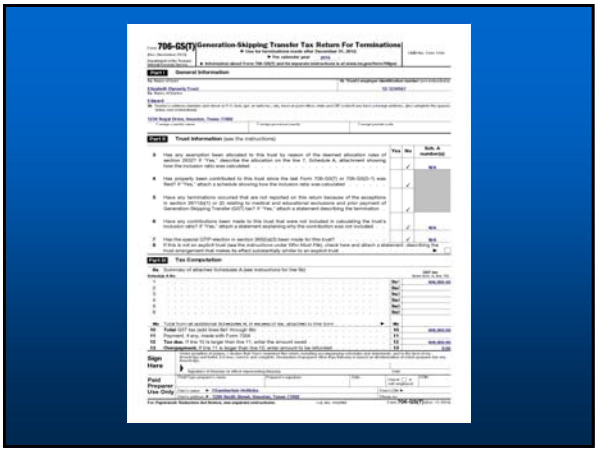
Fundamentals of the GST Tax

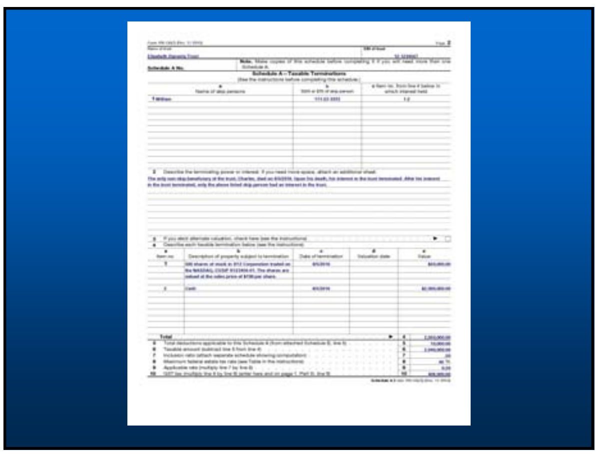
- Taxable Terminations
  - When two beneficiaries in two different younger generations have interests in the trust that terminate at the same time and as the result of one event, only one taxable termination will occur.
  - Example

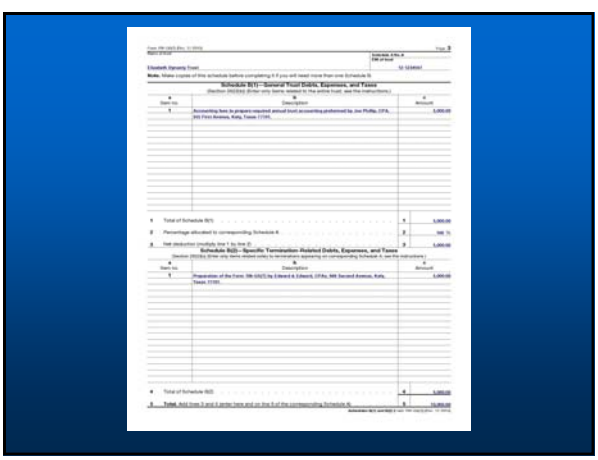
Elizabeth creates a trust for the benefit of her child, Charles, her grandchild, William, and her great-grandchild, George. Upon the death of Charles, the trust principal is to be distributed to George. If Charles is survived by both William and George, both Charles's interest and William's interest in the trust will terminate. However, only one taxable termination will occur.

Fundamentals of the GST Tax

- Taxable Terminations
  - Taxable terminations are reported on Form 706-GS(T), *Generation Skipping Transfer Tax Return for Terminations.*
  - A trustee is allowed to take a deduction on this Form for expenses, indebtedness, and taxes incurred in connection with property to which the taxable termination has occurred.
  - The Form is required to be filed even if no tax is due.


706-GS(T) Generation-Skipping Transfer Tax Return For Terminations
General Information
Trust Information
Tax Computation


Schedule A—Taxable Terminations



Fundamentals of the GST Tax

- Taxable Distributions
  - A taxable distribution occurs when a distribution from a trust is made to a skip person.
  - A taxable distribution is still considered to occur even if the trust has an inclusion ratio of zero.
  - A taxable distribution does not occur, however, if the original transfer to the trust was treated as a direct skip.

Fundamentals of the GST Tax

- Taxable Distributions
  - Example – Homer establishes an irrevocable trust under which income is payable to Homer's child Bart for life and principal may be distributed to Bart or any of Bart's descendants. If the trustee of the trust makes a distribution to any of Bart's children during Bart's lifetime, then such distributions will be treated as taxable distributions.
  - Example – Same facts as above except only Bart's children were the initial beneficiaries. Distributions will not be taxable because the trust's creation was a direct skip transfer.

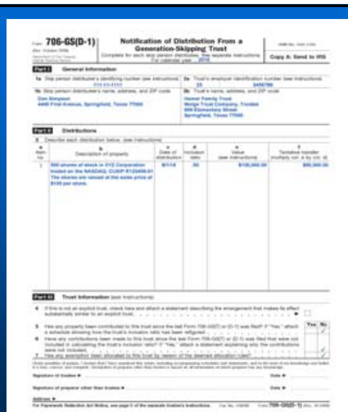
Fundamentals of the GST Tax

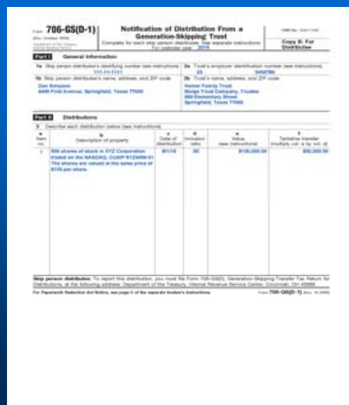
- Taxable Distributions
  - Taxable distributions are reported on Form 706-GS(D), *Generation-Skipping Transfer Tax Return for Distributions*, <u>by the skip person beneficiary</u>.
  - The trustee reports taxable distributions on Form 706-GS(D-1), *Notification of Distribution from a Generation-Skipping Transfer Trust*.

Fundamentals of the GST Tax

- Taxable Distributions
  - Form 706-GS(D) is not required to be filed if all distributions received by the skip person beneficiary have an inclusion ratio of zero.
  - Form 706-GS(D-1) is required to be filed even if no tax is due.
  - The taxpayer is allowed a deduction on Form 706-GS(D) for adjusted allowable expenses.
  - The adjusted allowable expenses are equal to the total allowable expenses multiplied by the inclusion ratio for the trust.


706-GS(D) Generation-Skipping Transfer Tax Return For Distributions


706-GS(D-1) Notification of Distribution From a Generation-Skipping Trust



Form 706-GS(D-1)

Notification of Distribution From a Generation-Skipping Trust

Copy B: For Distributee

Part I General Information

Part II Distributions

Description of property

Date of distribution

Inclusion ratio

Value (see instructions)

Tentative transfer

Skip person distributee.

Form 706-GS(D-1)

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - Move-Up Rule
    - If a descendant of a transferor is deceased at the time of the transfer, then the descendants of the deceased descendant move up one generation.
    - This rule can also apply to descendants of the transferor's parents, but only if the transferor has no living descendants.
    - This rule can also be applied to move a descendant up more than one generation level.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - Move-Up Rule
    - Example – Jon's father, Ned, is deceased at the time Jon's grandfather creates a trust for Jon's benefit. As such, the move-up rule will apply to treat Jon as a non-skip person as to his grandfather. Jon's descendants are moved up one generation as well.
    - Example – Same facts as above, however, Jon's great-uncle is the transferor. The move-up rule will apply only if Jon's great-uncle has no living descendants.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - Move-Down Rule
    - Once a taxable termination or a direct skip has occurred with respect to a trust, then the transferor is treated as moving down one generation above the highest remaining generation.
    - The generation assignments are not redetermined but persons who were skip persons before such GST event may no longer be skip persons.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - Move-Down Rule
    - Example – Sheldon creates a trust of which his grandchild, Leonard, and great-granddaughter, Penny, are current income beneficiaries. Upon Leonard's death, the trust will continue for Penny's lifetime. As the initial transfer is a direct skip, Sheldon is treated as having moved down one generation. Distributions to Leonard will not be subject to the GSTT, but transfers to Penny will be subject to the GSTT.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - Educational and Medical Payments Exclusion
    - Direct payments from transferor for medical and tuition expenses of a skip person.
    - Transfers from trusts for medical and tuition expenses of a skip person.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - Educational and Medical Payments Exclusion
    - Example

      Sheldon creates a non-exempt GST trust for the benefit of his son, Howard, and grandchild, Leonard. Distributions from the trust for Leonard's tuition will not be considered taxable distributions.

      If Leonard is given a testamentary power of appointment, a taxable termination may be avoided if he appoints the property to a HEET, which names Leonard and a charity as beneficiaries.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - GST "Annual Exclusion"
    - Outright direct skip transfers of $15,000 or less (annually).
    - A direct skip transfer to a trust that qualifies for the gift tax annual exclusion does not automatically qualify as a nontaxable gift for purposes of the GST tax.
    - A transfer to a trust will only qualify if: (1) the trust is exclusively for one beneficiary, and (2) the trust corpus is includible that beneficiary's estate if he or she dies before the trust termination.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - GST "Annual Exclusion"
    - Example

      Sheldon creates a trust for his grandchild, Leonard, and gives Leonard a general power of appointment over the trust. Sheldon transfers $10,000 to the trust. Leonard has a power of withdrawal applicable to the transfer such that the transfer qualifies for the gift tax annual exclusion. The entire transfer will also qualify for the GST annual exclusion.

Fundamentals of the GST Tax

- Exceptions to imposition of the GSTT
  - GST "Annual Exclusion"
    - Example

Same as previous example, however, the trustee may also distribute income from the trust to Sheldon's great-grandchild, Penny. Now, none of the transfer would qualify for the GST annual exclusion even if part of the transfer will qualify for the gift tax annual exclusion.

Fundamentals of the GST Tax

Estate Tax Inclusion Period (ETIP)

- The ETIP is the period after the transfer during which the property would be included in the estate of the transferor or the transferor's spouse.
- The trust's inclusion ratio will be determined when the ETIP ends.

Fundamentals of the GST Tax

Estate Tax Inclusion Period (ETIP)

- Example

Sam creates a grantor retained annuity trust, retaining a 5% annuity for ten years. At the end of the annuity period, the trust assets will be held in trust for Sam's grandson, Norm. During the annuity period, the trust will be subject to the ETIP. Therefore, any allocation of GST exemption by Sam will be effective at the end of the ETIP.

Fundamentals of the GST Tax

Estate Tax Inclusion Period (ETIP)

- The ETIP ends on the first to occur of:
  - (1) the date on which the property is not included in the estate of the transferor,
  - (2) the date of a GST transfer of the property, or
  - (3) the transferor's death.

Fundamentals of the GST Tax

Estate Tax Inclusion Period (ETIP)

- Example

Sam creates a trust under which the trustee must pay the income to Sam for 15 years and may invade principal for his grandson, Norm. After 15 years, the trust principal is to be distributed to Norm. If the trustee distributes $20,000 of trust principal to Norm during the 15-year period, the distribution would be a taxable distribution. The ETIP would terminate as to the property distributed to Norm. A prior allocation of GST exemption is effective immediately prior to the taxable distribution.

Fundamentals of the GST Tax

- Computation of the GSTT
  - The tax rate is tied to the maximum estate tax rate.
  - Under current law the GSTT rate is a flat 40%.

Fundamentals of the GST Tax

- Computation of the GSTT
  - Inclusion Ratio
    - A trust's inclusion ratio represents the pro rata portion of transfers from the trust which will be subject to the GSTT after taking allocations of GST exemption into account.
    - Example – Distributions from a trust with an inclusion ratio of 1.00 will be taxed at the full 40% rate.
    - Example – Distributions from a trust with an inclusion ratio of 0.00 will not result in GSTT.

Fundamentals of the GST Tax

- Computation of the GSTT
  - Inclusion Ratio is recomputed upon the following:
    - A new transferor is determined for the trust.
    - A qualified severance occurs.
    - Additional transfers to the trust by the transferor.
    - Additional GST exemption is allocated to the trust.

Fundamentals of the GST Tax

- Who pays the GSTT?
  - Tax-inclusive – taxable amount includes the tax itself, thus the tax is paid out of the property transferred.
  - Tax-exclusive – taxable amount is determined in relation to the amount actually received by the donee, thus the tax is paid in addition to the amount transferred.

Fundamentals of the GST Tax

- Who pays the GSTT?
  - Taxable distributions are tax-inclusive.
    - The beneficiary is liable for the GST tax.
    - In fact, if the Trustee pays the tax on behalf of the beneficiary that amount will also be subject to the GSTT.

Fundamentals of the GST Tax

- Who pays the GSTT?
  - Taxable terminations are tax-inclusive.
    - In this case, the Trustee is liable for the tax.

Fundamentals of the GST Tax

- Who pays the GSTT?
  - Direct Skips are tax-exclusive.
    - The Transferor, if living (otherwise the Transferor's estate), is liable for the tax.
    - If this was a lifetime transfer, the amount of the GST tax is added to the amount of the taxable gift.
    - Therefore, the transferor will pay a gift tax on the direct skip tax paid.
    - The tax is reported on a Form 709 or Form 706 (as applicable).

GST Exemption

- Every taxpayer is currently entitled to a $11,200,000 GST exemption.
- Allocation of GST exemption is elective and can be made during life or at death (by the taxpayer's executor).
- Allocations of GST exemption are irrevocable.

GST Exemption

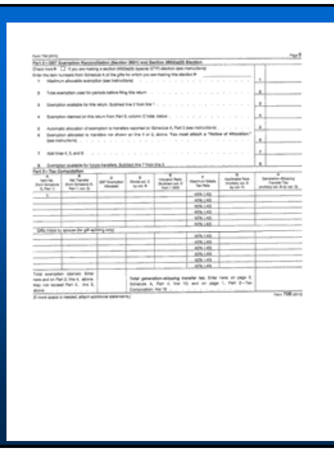
- Lifetime Allocations
  - Made on the taxpayer's Gift Tax Return (Form 709).
  - Timely allocation - If the allocation is made on a timely filed 709, then the value of the property transferred is determined as of the date of the transfer.

GST Exemption

- Lifetime Allocations
  - Example – Gloria creates a trust in 2016 for the benefit of her son, Manny, and his descendants. She transfers $1,000,000 in stock to fund the trust. In October of 2017, the assets of the trust have appreciated to $1,250,000.
  - If Gloria files a timely Form 709 (on extension) in October of 2017, she can allocate $1,000,000 of her GSTE and the trust will have an inclusion ratio of 0.00.

GST Exemption

- Lifetime Allocations
  - Late allocation - If the allocation is not made on a timely filed 709, then the value of the property transferred is determined as of the date of the late allocation is made.
  - The taxpayer may elect to value the property for late allocation purposes as of the first day of the month in which the late allocation is made.



GST Exemption

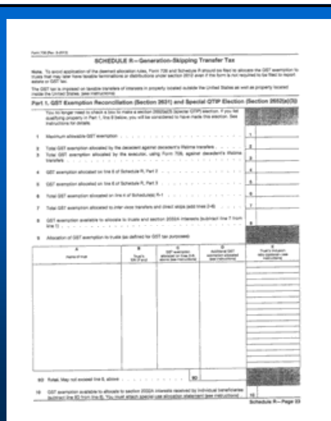
- Lifetime Allocations
  - Example – same facts as previous example, however, Gloria failed to file a timely return. She realizes her mistake in November and wants to allocate GSTE to the trust.
  - Gloria may file a Form 709 in November using the value of the stock as of November 1. In this example, she must allocate $1,250,000 to result in an inclusion ratio of 0.00.

GST Exemption

- Lifetime Allocations
  - If the trust is subject to an ETIP, the transferor should wait to make an affirmative allocation of GSTE.
  - An affirmative allocation of GSTE to the transferred property will become irrevocable but the allocation will be effective no earlier than termination of the ETIP.
  - Therefore, any appreciation between the date of the original transfer and the date of termination of the ETIP may not be covered by the allocation.

GST Exemption

- Testamentary Allocations
  - Made on the Estate Tax Return for the decedent (Form 706).
  - The value of the property transferred is determined <u>as of the date of the decedent's death</u>.


SCHEDULE R—Generation-Skipping Transfer Tax

Part 1. GST Exemption Reconciliation (Section 2631) and Special QTIP Election (Section 2652(a)(3))

GST Exemption

- Deemed/Automatic Allocations
  - IRC § 2632 automatically allocates GSTE as follows:
    - First, to lifetime direct skips.
    - Second, to lifetime indirect skips.
    - Third, to testamentary direct skips.
    - Fourth, to testamentary indirect skips.

GST Exemption

- Deemed/Automatic Allocations
  - Direct Skips
    - The transferor may elect out of automatic allocation on a timely filed 709.
    - The transferor may also elect out of automatic allocation by paying the GST tax with a timely filed 709.

GST Exemption

- Deemed/Automatic Allocations
  - Indirect Skips
    - Transfers to trusts (other than direct skips) which are "GST Trusts."
    - A "GST Trust" is any trust that could have a generation-skipping transfer unless an exception under IRC § 2632(c)(3)(B) applies.

GST Exemption

- Deemed/Automatic Allocations
  - Example

Vito creates a trust for the benefit of his son, Michael, which will terminate when he attains age 40. Pursuant to IRC § 2632(c)(3), this trust is not a GST Trust. Thus, consideration should be given as to whether GSTE should be affirmatively allocated.

What if the trust merely contains a contingent general power of appointment?

GST Exemption

- Deemed/Automatic Allocations
  - What if the trust merely contains a contingent general power of appointment?
  - What if the trust has "*Crummey*" withdrawal rights?

GST Exemption

- Deemed/Automatic Allocations
  - Indirect Skips
    - The fourth exception to a GST Trust is for a trust any portion of which would be included in the estate of a non-skip person if such person died immediately after the transfer.
    - As an exception to the exception, a trust will not be considered to be included in the estate of a non-skip person if such person possesses a right of withdrawal within the annual exclusion limits.

GST Exemption

- Deemed/Automatic Allocations
  - Indirect Skips
    - Example

      Lois creates a trust for her son, Stewie, and her grandchildren. Stewie holds a general power of appointment over the trust. Because the trust would be included in the estate of a non-skip person, the trust is not a GST trust and automatic allocation will not occur.

      Same as previous example, however, instead of a general power of appointment, Stewie has a lapsing power to withdraw within the annual exclusion limits. The trust would be a GST trust and automatic allocation will occur.

GST Exemption

- Deemed/Automatic Allocations
  - Indirect Skips
    - The transferor may elect out of an automatic allocation to an indirect skip by making an affirmative allocation of GSTE of an amount less than the value of the property transferred.
    - The transferor may elect out of automatic allocation in any combination. For example, the transferor can elect to have the deemed allocation rules not apply to a particular indirect skip or all future transfers to all trusts.

GST Exemption

- Retroactive Allocations
  - IRC § 2632(d) allows for the allocation of GSTE using date of transfer values if a non-skip lineal descendant of the transferor predeceases the transferor.
    - Needs to be reported on a Form 709 for the year the non-skip descendant dies.

GST Exemption

- Retroactive Allocations
  - Example
    - In 2016, Schmidt creates a trust for his daughter Jessica and her children but decided not to allocate GSTE to it. If Jessica predeceases Schmidt in 2017, then Schmidt may allocate his remaining GSTE to the trust on a 2017 Form 709 but not a later return.
    - If Schmidt files a 709 for the year of Jessica's death, then the allocation is based on the value of the property when transferred.

GST Exemption

- Deemed/Automatic Allocations
  - Formula allocations of GSTE are allowable.

GST Exemption

- Split Gift Treatment for Spouses
- If a husband and wife elect to split a gift under Section 2513, each will be treated as the transferor of one half of the entire value of the transferred property for GST purposes.
- This is true even if only part of the gift qualifies for gift-splitting treatment.
- Once the gift is split, each spouse is free to allocate his or her GST exemption to his or her part of the gift.

GST Exemption

- Split Gift Treatment for Spouses

- Example

Cher agrees to split gift treatment with her husband, Sonny, for a $4M gift to Chaz's trust. As such, Sonny may not allocate more than $2M of his GSTE to the trust. Cher may allocate her GSTE to the trust, but is not required to do so.

Same example as above, however, Cher is also an income beneficiary of the trust. The portion of the gift treated as going to the other spouse is not eligible for gift-splitting. However, for GST purposes Sonny and Cher are each treated as the transferor of one-half of the entire value of the gift.

"Grandfathered" GST Trusts

- Three types of "Grandfathered" GST trusts:
  - Irrevocable on September 25, 1985;
  - Trust created under agreement or Will executed before October 22, 1986 and not amended if decedent died before January 1, 1987; or
  - Trust made by a person who was incapacitated on October 22, 1986.

"Grandfathered" GST Trusts

- Loss of "Grandfathered" status
  - Additions
    - If property is added to a grandfathered trust, then GSTT will be imposed on the pro rata portion of the trust when a taxable distribution or taxable termination occurs.
    - But, an addition from a grandfathered trust to a grandfathered trust will not taint the recipient trust.

“Grandfathered” GST Trusts

- Loss of “Grandfathered” status
  - Constructive Additions
    - Generally, a release, exercise or lapse of a power of appointment will be treated as a constructive addition.
    - This rule does not apply if the release, exercise or lapse of the power is a nontaxable event.

“Grandfathered” GST Trusts

- Loss of “Grandfathered” status
  - Constructive Additions
    - Example – Sherlock is the beneficiary of a grandfathered trust of which he has the power to appoint property to his descendants only (special power). As the exercise of this power is not subject to the estate or gift tax, it will not be treated as a constructive addition unless it postpones the termination of the trust beyond the RAP or 90 years.

“Grandfathered” GST Trusts

- Taxation of Tainted “Grandfathered” Trust
  - Trust treated as though it has two potions – taxable and nontaxable.
  - Taxable portion has an inclusion ratio of 1.00
  - Determined by dividing FMV of addition by FMV of the entire trust immediately after the addition.

Special Rules

- Multiple Transferors
  - A single trust that consists of assets attributable to more than one transferor is treated as separate trusts for GST tax purposes.
  - Example –

Jack transfers $300,000 to a trust and Rebecca transfers $100,000 to the same trust. This single trust would be treated as two trusts for GST purposes. Because Jack contributed ¾ of the value of the trust, ¾ of the trust is treated as a separate trust created by Jack.

Special Rules

- Qualified Severances
  - Allows a mixed inclusion ratio trust to be divided into wholly exempt and wholly non-exempt trusts.
    - Must be authorized by governing instrument or state law;
    - Must be severed on a fractional basis;
    - Terms of resulting trusts must provide for the same succession of interests of beneficiaries as the original trust.

Special Rules

- Qualified Severances
  - Reporting Requirements
    - Reported on a Form 706-GS(T).
    - "Qualified Severance" should be written at the top of the form.
    - A Notice of Qualified Severance must be attached.
    - Should be filed by April 15 of year following severance.

Special Rules

- 9100 Relief
  - 9100-2 Automatic Relief for Statutory Elections
    - Only available if an initial return was filed timely.
    - 6-month extension period is measured from original due date of return (excluding extensions).
    - Include "Filed Pursuant to Section 301.9100-2" on the top of the amended return.

Special Rules

- 9100 Relief
  - 9100-3 Discretionary Relief
    - The enactment of Section 2642(g)(1) made it possible to request an extension to make a timely allocation of GSTE.
    - Is treated as a retroactive allocation.
    - Relief can include allocations of GSTE, making a reverse QTIP election and electing out of automatic allocations.

Special Rules

- 9100 Relief
  - 9100-3 Discretionary Relief
    - Relief is sought in the form of a PLR.
    - Taxpayer must show she acted reasonably and in good faith and that the relief will not prejudice the government.

Special Rules

- Non-Resident Aliens
  - Similar property/transfers subject to the GST tax as non-resident alien estate and gift tax purposes.
    - Estate – U.S. real estate, U.S. tangible personal property and US securities.
    - Gift – U.S. real estate and U.S. tangible personal property.

Special Rules

- Non-Resident Aliens
  - Non-resident alien has the same GSTE as a citizen.
  - A direct skip taxable transfer only occurs if transfer was also subject to the U.S. estate or gift tax.
  - Taxable terminations and distributions are taxable only if the initial transfer to the trust was subject to the estate or gift tax, regardless of situs of the property at the time of the termination or distribution.

GST and Portability

- The GSTE is <u>not</u> portable.
  - Brad and Angelina are married and have an estate of $10,000,000. Brad's Will leaves his estate to Angelina outright.
  - Although Angelina will be able to utilize Brad's unused estate tax exemption when she dies, if a trust is later created for Angelina's son, Maddox, only Angelina's GSTE will be available to allocate to Maddox's trust.