Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B09
PLR-153074-03
Date:
August 06, 2004

Legend

Decedent =

Date 1 =
Spouse =
Child 1 =
Child 2 =
Child 3 =
s =
t =
u =
Family Trust =
w =

Dear :

This is in response to your letter dated August 21, 2003, requesting a ruling that the Service will disregard a marital deduction taken on Decedent's federal estate tax return with respect to the actuarial value of Spouse's interest in property passing under Decedent's will to Decedent's children and a credit shelter trust in which Spouse had a life interest.

The facts submitted and representations made are as follows: Decedent died on Date 1 survived by Spouse, Child 1, Child 2, and Child 3. Pursuant to the directions in Decedent's Last Will and Testament, insurance, jointly-owned property, and an annuity collectively valued at $s passed to Spouse. Cash, stocks, bonds, real estate and oil royalties valued at $t passed to Child 1, Child 2, and Child 3 subject to Spouse's life estate in one-half of the interests. Finally, $u passed to Family Trust, a credit shelter trust.

The Form 706 filed for the decedent's estate was the July 1990 revision that is to be filed for decedents dying after December 31, 1989, and before January 1, 1993. Schedule M states:

> **Terminable Interest (QTIP) Marital Deduction.** – If you elect to claim a marital deduction for qualified terminable interest property (QTIP) under § 2056(b)(7), you MUST list on Part 2 of Schedule M all of the property for which you are making the election. Listing property on Part 2 constitutes the making of the QTIP election. No marital deduction will be allowed for any terminable interest property that is listed on Part 1 of Schedule M.

Under Part 1 of Schedule M, entitled "Property Interests Which Are Not Subject to a QTIP Election," Decedent's executor listed property interests passing to spouse valued at $w. $w is the sum of $s and the actuarial value of Spouse's interest in $t and $u. The taxpayer claimed a marital deduction for the full value of $w even though $t and $u actually passed to Child 1, Child 2, Child 3, and Family Trust and spouse only had a nondeductible terminable interest in those assets. Nothing was listed under Part 2 of Schedule M entitled "Property Interests Which Are Subject to a QTIP Election." No reference to 'qualified terminable interest property,' 'QTIP,' or 'QTIP election' was made by the estate on Schedule M or at any other place on the return.

You have asked that we disregard the deduction taken with respect to the actuarial value of Spouse's interest in $t and $u on Decedent's Form 706 and treat it as null and void for purposes of §§ 2044(a), 2056(b), 2519(a), and 2652.

Section 2056(a) provides that the value of a decedent's taxable estate shall be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse.

Section 2056(b)(1) provides that a deduction is not allowed for terminable interests that pass to the spouse. An interest is a terminable interest if the interest passing to the surviving spouse will terminate or fail on the lapse of time or on the occurrence of an event or contingency or on the failure of an event or contingency to occur, and on termination, an interest in the property passes to someone other than the surviving spouse.

Section 2056(b)(7)(A) provides that qualified terminable interest property shall be treated as passing to the surviving spouse and no part of such property shall be treated as passing to any person other than the surviving spouse. Thus, the value of such property is deductible from the value of the gross estate under § 2056(a) and is not treated as a terminable interest. Under § 2056(b)(7)(B)(i), qualified terminable interest property is property that passes from the decedent, in which the surviving spouse has a qualifying income interest for life, and to which an election under § 2056(b)(7)(B)(v) applies.

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

A QTIP election has transfer tax consequences for the surviving spouse. Section 2044(a) and (b) provides generally that the value of the gross estate includes the value of any property in which the decedent has a qualifying income interest for life and with respect to which a deduction was allowed for the transfer of the property to the decedent under § 2056(b)(7). Under § 2519(a) and (b), any disposition of all or part of a qualifying income interest for life in any property with respect to which a deduction was allowed under § 2056(b)(7) is treated as a transfer of all interests in the property other than the qualifying income interest. Further, the surviving spouse will, in the absence of a "reverse QTIP" election under § 2652(a)(3), be treated as the transferor of the property for generation-skipping transfer tax purposes under § 2652(a).

In the case of a QTIP election to which Rev. Proc. 2001-38, 2001-24 C.B. 1335, applies, the Service will disregard a QTIP election made under § 2056(b)(7) and treat it as null and void for purposes of §§ 2044(a), 2056(b)(7), 2519(a), and 2652. Rev. Proc. 2001-38 applies to QTIP elections under § 2056(b)(7) where the election was not necessary to reduce the estate tax liability to zero, based on values as finally determined for federal estate tax purposes. Rev. Proc. 2001-38 does not apply in situations where a partial QTIP election was required with respect to a trust to reduce the estate tax liability and the executor made the election with respect to more trust property than was necessary to reduce the estate tax liability to zero; nor does it apply to elections that are stated in terms of a formula designed to reduce the estate tax to zero.

In Estate of Higgins v. Commissioner, 91 T.C. 61 (1988), aff'd, 897 F.2d 856 (6th Cir. 1990), the estate filed a June 1982 revision of the Form 706, and checked the "No" box in response to the question whether the estate was making a QTIP election. On Schedule M, the estate deducted the value of the spouse's life estate in a residuary trust, and on Schedule O the estate deducted the value of the remainder interest in the trust passing to charity. The estate argued that the entries on the return were sufficient to constitute a QTIP election. The Tax Court ruled that because the QTIP election carries with it burdens as well as the benefit of a marital deduction, the return and the attached schedules must evidence "an unequivocal manifestation of an affirmative intent" to elect QTIP treatment in order to qualify for the marital deduction. In Estate of Higgins, the court found that there was no clear manifestation of an affirmative intent to make the QTIP election on the estate tax return. Accordingly, the court concluded that the estate had not effectively elected QTIP treatment. The Sixth Circuit affirmed the Tax Court's decision in Estate of Higgins with similar reasoning. The Sixth Circuit stated, "the intent of § 2056(b)(7) is that the election must be unequivocally communicated on the estate tax return…" Estate of Higgins, 897 F.2d at 859-60.

Rev. Proc. 2001-38 applies only when a valid QTIP election was made on a decedent's estate tax return. As explained by the Tax Court in Estate of Higgins, in order to make a valid QTIP election under § 2056(b)(7)(B)(v), an estate must make an unequivocal manifestation of an affirmative intent to make the election of QTIP treatment on the estate tax return." Estate of Higgins, 91 T.C. at 69. The instructions for the Form 706 in general as well as those specifically for Schedule M are sufficiently detailed with regard to the QTIP election so that the preparer of the form should have been adequately aware that taking a marital deduction for terminable interest property requires the making of a QTIP election. However, in this case, the property for which a deduction was claimed was listed on the schedule specifically designated for listing property other than QTIP property. Further, there was no other indication of any type that a QTIP election was to be made. We can only conclude that, as of the filing of decedent's Form 706, a QTIP election was not made with respect to the actuarial value of Spouse's interest in $t and $u. As stated in Estate of Higgins, "the essence of the election requirement is that the executor of the estate of the spouse first to die unequivocally communicate his election…" Id. at 70. Here, there was no such indication made. Since a QTIP election was not made on Decedent's Form 706, Decedent's estate does not qualify for relief under Rev. Proc. 2001-38.

In conjunction with the receipt of this letter, Spouse must file a supplemental Form 706 properly reporting the assets to be included on Schedule M and the correct beneficiaries and amounts on Part 4, Line 5. According to the information provided, the tentative estate tax on Decedent's taxable estate, if reported correctly, is less than Decedent's available unified credit against the estate tax. A copy of this letter should be attached to the supplemental Form 706 and filed with the Internal Revenue Service Center, Cincinnati, Ohio 45999. A copy is included for this purpose.

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

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings it is subject to verification on examination.

Pursuant to the Power of Attorney on filed with this office, a copy of this letter is being sent to the taxpayer's representative.

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,

Melissa C. Liquerman

Melissa C. Liquerman
Branch Chief, Branch 9
(Passthroughs & Special Industries)

Enclosures
Copy of this letter for § 6110 purposes
Copy of this letter