paid to A for life and, on A’s death, the remainder is to be distributed to W (or pursuant to W’s testamentary general power of appointment). Trust 2 provides that trust income is to be paid to B for life and, on B’s death, the remainder is to be distributed to X (or pursuant to X’s testamentary general power of appointment). Because Trust 1 and Trust 2 do not provide A and B with the contingent survivor income interests that were provided to A and B under the terms of Trust, Trust 1 and Trust 2 do not provide for the same succession of interests in the aggregate as provided by Trust. Therefore, the severance does not satisfy the requirements of this section and is not a qualified severance. Pursuant to paragraph (h) of this section and is not a qualified severance, provided that all other requirements were satisfied. Trust 3 will have an inclusion ratio of one.  

Example 13. Qualified severance following a non-qualified severance. Assume the same facts as in Example 12, except that, as of November 4, 2010, the trustee of Trust 1 severs Trust 1 into two trusts, Trust 3 and Trust 4, in accordance with applicable local law. The instrument severing Trust 1 provides that both resulting trusts have provisions identical to Trust 1. The terms of the instrument severing Trust 1 further provide that Trust 3 is to be funded on a pro rata basis with assets having a fair market value as of the date of severance equal to 70% of the value of Trust 1’s assets on that date, and Trust 4 is to be funded with assets having a fair market value as of the date of severance equal to 30% of the value of Trust 1’s assets on that date. The severance constitutes a qualified severance, provided that all other requirements of section 2642(a)(3) and this section are satisfied. Trust 3 will have an inclusion ratio of zero and Trust 4 will have an inclusion ratio of one.

(k) Effective/applicability date—(1) In general. Except as otherwise provided in this paragraph (k), this section applies to severances occurring on or after August 2, 2007. Paragraph (d)(7)(iii), paragraph (h), and Examples 9, 12 and 13 of paragraph (j) of this section apply to severances occurring on or after September 2, 2008.

(2) Transition rule. In the case of a qualified severance occurring after December 31, 2006, and before August 2, 2007, taxpayers may rely on any reasonable interpretation of section 2642(a)(3) as long as reasonable notice concerning the qualified severance and identification of the trusts involved has been given to the IRS. For this purpose, the proposed regulations (69 FR 51967) are treated as a reasonable interpretation of the statute. For purposes of the reporting provisions of §26.2642–6(e), notice to the IRS should be mailed by the due date of the gift tax return (including extensions granted) for gifts made during the year in which the severance occurred. If no gift tax return is filed, notice to the IRS should be mailed by April 15th of the year immediately following the year during which the severance occurred. For severances occurring between December 31, 2000, and January 1, 2007, notification should be mailed to the IRS as soon as reasonably practicable after August 2, 2007, if sufficient notice has not already been given.

Paragraphs:

(A) Spouse or former spouse of that individual;
(B) Descendant of that individual; and
(C) Spouse or former spouse of each descendant of that individual.

(ii) Continued application of generation assignment. If a transfer to a trust would be a generation-skipping transfer but for paragraph (a)(1) of this section, any generation assignment determined under this paragraph (a) continues to apply in determining whether any subsequent distribution from (or termination of an interest in) the portion of the trust attributable to that transfer is a generation-skipping transfer.

(iii) Ninety-day rule. For purposes of paragraph (a)(1) of this section, any individual who dies no later than 90 days after a transfer occurring by reason of the death of the transferor is treated as having predeceased the transferor.

(iv) Local law. A living person is not treated as having predeceased the transferor solely by reason of a provision of applicable local law; e.g., an individual who disclaims is not treated as a predeceased parent solely because state law treats a disclaimant as having predeceased the transferor for purposes of determining the disposition of the disclaimed property.

(3) Established or derived. For purposes of section 2651(e) and paragraph (a)(1) of this section, an individual’s interest is established or derived at the time the transferor is subject to transfer tax imposed by either chapter 11 or 12 of the Internal Revenue Code on the property. See §26.2652-1(a) for the definition of a transferor. If the same transferor, on more than one occasion, is subject to transfer tax imposed by either chapter 11 or 12 of the Internal Revenue Code on the property so transferred (whether the same property, reinvestments thereof, income thereon, or any or all of these), then the relevant time for determining whether paragraph (a)(1) of this section applies is the earliest time at which the transferor is subject to the tax imposed by either chapter 11 or 12 of the Internal Revenue Code. For purposes of section 2651(e) and paragraph (a)(1) of this section, the interest of a remainder beneficiary of a trust for which an election under section 2523(f) or section 2656(b)(7) (QTIP election) has been made will be deemed to have been established or derived, to the extent of the QTIP election, on the date as of which the value of the trust corpus is first subject to tax under section 2519 or section 2041. The preceding sentence does not apply to a trust, however, to the extent that an election under section 2652(a)(3) (reverse QTIP election) has been made for the trust because, to the extent of a reverse QTIP election, the spouse who established the trust will remain the transferor of the trust for generation-skipping transfer tax purposes.

(4) Special rule in the case of additional contributions to a trust. If a transferor referred to in paragraph (a)(1) of this section contributes additional property to a trust that existed before the application of paragraph (a)(1), then the additional property is treated as being held in a separate trust for purposes of chapter 13 of the Internal Revenue Code. The provisions of §26.2654-1(a)(2), regarding treatment as separate trusts, apply as if different transferors had contributed to the separate portions of the single trust. Additional subsequent contributions from that transferor will be added to the new share that is treated as a separate trust.

(b) Limited application to collateral heirs. Paragraph (a) of this section does not apply in the case of a transfer to any individual who is not a lineal descendant of the transferor (or the transferor’s spouse or former spouse) if the transferor has any living lineal descendant at the time of the transfer.

(c) Examples. The following examples illustrate the provisions of this section:

Example 1. T establishes an irrevocable trust, Trust, providing that trust income is to be paid to T’s grandchild, GC, for 5 years. At the end of the 5-year period or on GC’s prior death, Trust is to terminate and the principal is to be distributed to GC if GC is living or to GC’s children if GC has died. The transfer that occurred on the creation of the trust is subject to the tax imposed by chapter 12 of the Internal Revenue Code and, at the time of the transfer, T’s child, C, who is a parent of GC, is deceased. GC is treated as a member of the generation that is one generation below T’s generation. As a result, GC is not a skip person and Trust is not a skip
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person. Therefore, the transfer to Trust is not a direct skip. Similarly, distributions to GC during the term of Trust and at the termination of Trust will not be GSTs.

Example 2. On January 1, 2002, T transfers $100,000 to an irrevocable inter vivos trust that provides T with an annuity payable for four years or until T’s prior death. The annuity is treated as a qualified terminable interest under section 2652(b). When the trust terminates, the corpus is to be paid to T’s grandchild, GC. The transfer is subject to the tax imposed by chapter 12 of the Internal Revenue Code and, at the time of the transfer, T’s child, C, who is a parent of GC, is living. C dies in 2006. In this case, C was alive at the time the transfer by T was subject to the tax imposed by chapter 12 of the Internal Revenue Code. Therefore, section 2651(e) and paragraph (a)(1) of this section do not apply. When the trust subsequently terminates, the distribution to GC is a taxable termination that is subject to the GST tax to the extent the trust has an inclusion ratio greater than zero. See section 2642(a).

Example 3. T dies testate in 2002, survived by T’s spouse, S, their children, C1 and C2, and C1’s child, GC. Under the terms of T’s will, a trust is established for the benefit of S and of T and S’s descendants. Under the terms of the trust, all income is payable to S during S’s lifetime and the trustee may distribute trust corpus for S’s health, support and maintenance. At S’s death, the corpus is to be distributed, outright, to C1 and C2. If either C1 or C2 has predeceased S, the deceased child’s share of the corpus is to be distributed to that child’s then-living descendants, per stirpes. The executor of T’s estate makes the election under section 2656(b)(7) to treat the trust property as qualified terminable interest property (QTIP) but does not make the election under section 2652(a)(3) (reverse QTIP election). In 2003, C1 dies survived by S and GC. In 2004, S dies, and the trust terminates. The full fair market value of the trust is includible in S’s gross estate under section 2034 and S becomes the transferor of the trust under section 2652(a)(1)(A). GC’s interest is considered established or derived at S’s death, and because C1 is deceased at that time, GC is treated as a member of the generation that is one generation below the generation of the transferor, S. As a result, GC is not a skip person and the transfer to GC is not a direct skip.

Example 4. The facts are the same as in Example 3. However, the executor of T’s estate makes the election under section 2652(a)(3) (reverse QTIP election) for the entire trust. Therefore, T remains the transferor because, for purposes of chapter 13 of the Internal Revenue Code, the election to be treated as qualified terminable interest property is treated as if it had not been made. In this case, GC’s interest is established or derived on T’s death in 2002. Because C1 was living at the time of T’s death, the predeceased parent rule under section 2651(e) does not apply, even though C1 was deceased at the time the transfer from S to GC was subject to the tax under chapter 11 of the Internal Revenue Code. When the trust terminates, the distribution to GC is a taxable termination that is subject to the GST tax to the extent the trust has an inclusion ratio greater than zero. See section 2642(a).

Example 5. T establishes an irrevocable trust providing that trust income is to be paid to T’s grandniece, GN, for 5 years or until GN’s prior death. At the end of the 5-year period or on GN’s prior death, the trust is to terminate and the principal is to be distributed to GN if living, or if GN has died, to GN’s then-living descendants, per stirpes. S is a sibling of T and the parent of N. N is the parent of GN. At the time of the transfer, T has no living lineal descendant, S is living, N is deceased, and the transfer is subject to the gift tax imposed by chapter 12 of the Internal Revenue Code. GN is treated as a member of the generation that is one generation below T’s generation because S, GN’s youngest living lineal ancestor who is also a descendant of T’s parent, is in T’s generation. As a result, GN is not a skip person and the transfer to the trust is not a direct skip. In addition, distributions to GN during the term of the trust and at the termination of the trust will not be GSTs.

Example 6. On January 1, 2004, T transfers $50,000 to a great-grandniece, GGN, who is the great-grandchild of B, a brother of T. At the time of the transfer, T has no living lineal descendants and B’s grandchild, GGN, who is a parent of GGN and a child of B’s living child, N, is deceased. GGN will be treated as a member of the generation that is one generation below the lower of T’s generation or the generation assignment of GGN’s youngest living lineal ancestor who is also a descendant of the parent of the transferor. In this case, N is GGN’s youngest living lineal ancestor who is also a descendant of the parent of T. Because N’s generation assignment is lower than T’s generation, GGN will be treated as a member of the generation that is one generation below N’s generation assignment (i.e., GGN will be treated as a member of her parent’s generation). As a result, GGN remains a skip person and the transfer to GGN is a direct skip.

Example 7. T has a child, C, C’s spouse, S, have a 20-year-old child, GC. C dies and S subsequently marries S2. S2 legally adopts GC. T transfers $100,000 to GC. Under section 2651(b)(1), GC is assigned to the generation that is two generations below T. However, since GC’s parent, C, is deceased at the time of the transfer, GC will be treated as a member of the generation that is one generation below T. As a result, GC is not a
skip person and the transfer to GC is not a direct skip.

[T.D. 9214, 70 FR 41142, July 18, 2005]

§ 26.2651–2 Individual assigned to more than 1 generation.

(a) In general. Except as provided in paragraph (b) or (c) of this section, an individual who would be assigned to more than 1 generation is assigned to the youngest of the generations to which that individual would be assigned.

(b) Exception. Notwithstanding paragraph (a) of this section, an adopted individual (as defined in this paragraph) will be treated as a member of the generation that is one generation below the adoptive parent for purposes of determining whether a transfer to the adopted individual from the adoptive parent (or the spouse or former spouse of the adoptive parent, or a lineal descendant of a grandparent of the adoptive parent) is subject to chapter 13 of the Internal Revenue Code. For purposes of this paragraph (b), an adopted individual is an individual who is—

(1) Legally adopted by the adoptive parent;
(2) A descendant of a parent of the adoptive parent (or the spouse or former spouse of the adoptive parent);
(3) Under the age of 18 at the time of the adoption; and
(4) Not adopted primarily for the purpose of avoiding GST tax. The determination of whether an adoption is primarily for GST tax-avoidance purposes is made based upon all of the facts and circumstances. The most significant factor is whether there is a bona fide parent/child relationship between the adoptive parent and the adopted individual, in which the adoptive parent has fully assumed all significant responsibilities for the care and raising of the adopted child. Other factors may include (but are not limited to), at the time of the adoption—

(i) The age of the adopted individual (for example, the younger the age of the adopted individual, or the age of the youngest of siblings who are all adopted together, the more likely the adoption will not be considered primarily for GST tax-avoidance purposes); and

(ii) The relationship between the adopted individual and the individual’s parents (for example, objective evidence of the absence or incapacity of the parents may indicate that the adoption is not primarily for GST tax-avoidance purposes).

(c) Special rules—(1) Corresponding generation adjustment. If an individual’s generation assignment is adjusted with respect to a transfer in accordance with paragraph (b) of this section, a corresponding adjustment with respect to that transfer is made to the generation assignment of each—

(i) Spouse or former spouse of that individual;
(ii) Descendant of that individual; and
(iii) Spouse or former spouse of each descendant of that individual.

(2) Continued application of generation assignment. If a transfer to a trust would be a generation-skipping transfer but for paragraph (b) of this section, any generation assignment determined under paragraph (b) or (c) of this section continues to apply in determining whether any subsequent distribution from (or termination of an interest in) the portion of the trust attributable to that transfer is a generation-skipping transfer.

(d) Example. The following example illustrates the provisions of this section:

Example. T has a child, C. C has a 20-year-old child, GC. T legally adopts GC and transfers $100,000 to GC. GC’s generation assignment is determined by section 2651(b)(1) and GC is assigned to the generation that is two generations below T. In addition, because T has legally adopted GC, GC is generally treated as a child of T under state law. Under these circumstances, GC is an individual who is assigned to more than one generation and the exception in §26.2651–2(b) does not apply. Thus, the special rule under section 2651(f)(1) applies and GC is assigned to the generation that is two generations below T. GC remains a skip person with respect to T and the transfer to GC is a direct skip.

[T.D. 9214, 70 FR 41142, July 18, 2005]

§ 26.2651–3 Effective dates.

(a) In general. The rules of §§26.2651–1 and 26.2651–2 are applicable for terminations, distributions, and transfers occurring on or after July 18, 2005.