Special Report: New Tax Law

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The Generation-skipping Transfer Tax

Time traveling with the GST tax in 2011 and beyond

During 2010, Internal Revenue Code Section 2664[1] and Section 901 of the Economic Growth and Tax Relief Reconciliation Act of 2001 (the 2001 Act) caused considerable confusion as to how the generation-skipping transfer (GST) tax would be applied in 2010 and beyond. The uncertainties for 2010 were finally resolved by the enactment on Dec. 17, 2010 of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (the 2010 Act). Unfortunately, the 2010 Act simply postponed many of the uncertainties until 2013.

We will first look at GST tax planning opportunities that were available in 2010 and then examine the ways in which IRC Chapter 13 (called "Tax on Generation-Skipping Transfers") works in 2011 and 2012 (and could work after 2012 if Congress, by inaction, permits the sunset provisions to apply). We will then discuss the need to review and possibly revise existing estate planning documents that define bequests and distributions with reference to terms defined in Chapter 13. Finally, we will consider the advisability of current action to take advantage of what may be a temporary low GST tax rate and a temporary high GST tax exemption.

Uncertainty Prevails

The application of the GST tax in 2010 was uncertain despite IRC Section 2664's mandate that Chapter 13—the chapter of the IRC that imposes the GST tax—doesn't apply to GSTs that take place after 2009. This was so because Congress could have acted at any time to make Chapter 13 applicable to 2010 GSTs—including GSTs occurring in 2010 before Congress enacted the 2010 Act. Most practitioners generally believed that such a retroactive re-enactment of Chapter 13 was likely to survive the judicial challenges that would no doubt have resulted.

The 2010 Act resolved the uncertainty of retroactivity. Section 301 of the 2010 Act, in effect, repealed IRC Section 2664. The repeal made it clear that Chapter 13 did apply retroactively to 2010 GSTs. The sting of the retroactive application, however, was blunted by Section 302(c) of the 2010 Act, which reduced the GST tax rate to zero for all 2010 GSTs. As an added sweetener for transferors, IRC Section 2010 was amended by Section 302(a) of the 2010 Act to increase the applicable exclusion amount to $5 million. Because the GST tax exemption is tied to the applicable exclusion amount by IRC Section 2631(c), this provision raised the GST tax exemption to $5 million.

The application of the GST tax beyond 2010 was also uncertain despite the statement in Section 901 of the 2001 Act (known as the "sunset provision") that the provisions of the 2001 Act, including Section 2664, don't apply after 2010. The uncertainty stemmed not only from the impossibility of predicting whether and how Congress would act, but also because of the ambiguities inherent in the language of Section 901(b) of the 2001 Act. The 2010 Act, unfortunately, resolved none of this uncertainty.

If Congress fails to provide a different set of rules, Subsection (b) of Section 901 of the 2001 Act will now apply starting in 2013, rather than its originally planned starting date of Jan. 1, 2011. This subsection states, inter alia, that the IRC shall be applied and administered to GSTs that take place after 2012 as if the 2001 Act had never been enacted (this is commonly referred to as

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the "had never been enacted" rule). This subsection clearly means that the several helpful provisions of Chapter 13 that were added as part of the 2001 Act, such as the qualified severance rules of Section 2642(a)(3), will no longer apply in determining the amount of GST tax payable on a post-2012 GST.

A Question Remains

What isn't so clear is the answer to the following question: *"If the sunset provisions apply, must we change, after 2012, the GST tax attributes of a trust that acquired those attributes as a result of a provision of Chapter 13 that was added by the 2001 Act?"*

The 2001 Act added several technical pro-taxpayer provisions to Chapter 13 in addition to the rate reductions and exemption increases that are generally thought of as the key elements of the 2001 Act. Some of these technical provisions merely reversed by statute certain positions taken by the Internal Revenue Service and Treasury prior to 2001. As a result of the application of many of these technical provisions, numerous trusts have an inclusion ratio in 2011 that is lower than it would have been if Congress hadn't enacted the 2001 Act, unless of course the IRS positions that the 2001 Act had reversed, are held invalid (or reversed by the IRS) even without a statutory change. After 2012, will these trusts be required to adjust their inclusion ratios to what they would have been if these provisions had never been enacted and the pre-2001 IRS positions upheld? One of these 2001 Act technical provisions that reversed an earlier IRS position recognized certain severances of trusts that the IRS hadn't recognized for GST tax purposes prior to the 2001 Act. It's possible, therefore, that trusts that were severed pursuant to this provision will be reconnected after 2012.

Chapter 13 in 2010

Although the GST tax rate applicable to 2010 GSTs was zero, Chapter 13 was an operative part of the IRC in 2010. GSTs, other transfers and GST tax exemption allocations that occurred in 2010 will have an impact on how the GST tax will be applied to the future GSTs of which a particular individual is the transferor. These transfers and allocations are examined below.

Lifetime 2010 direct skips—Individuals continued to make gifts to skip persons such as their grandchildren or to trusts for their benefit (skip person trusts) in 2010. These gifts were direct skips despite the fact that the GST tax rate applicable to them was zero. Because they were direct skips, the deemed GST tax exemption allocation rule of IRC Section 2632(c) will apply to them. This rule will automatically allocate a transferor's unused GST tax exemption to any direct skip to the extent necessary to make the transferred property's inclusion ratio zero.

> Transferors who made 2010 direct skips should make an IRC Section 2632(b)(3) election.

In the case of outright direct skips or direct skips to skip person trusts that aren't expected to provide significant benefits to lower-generation beneficiaries, the automatic allocation of GST tax exemption isn't a good thing. The purpose of GST tax exemption allocations to direct skips is to decrease, hopefully to zero, the GST tax rate applicable to them. Because all 2010 direct skips were subject to a zero GST tax rate, unless they were made to trusts from which future GSTs are expected, the allocation of GST tax exemption to them will needlessly consume their transferors' GST tax exemptions.

To avoid wasting a GST tax exemption, transferors who made 2010 direct skips should make an election under IRC Section 2632(b)(3) to have the deemed allocation rule not apply. The regulations require that this election be made on a timely filed gift tax return (taking into account extensions).[2] Gift tax returns for 2010 gifts that aren't extended are timely if filed on or before April 18, 2011.[3] Section 301(d)(2) of the 2010 Act, however, extends the time for making such election for a transfer that took place before the enactment of the 2010 Act (that is, before Dec. 17, 2010) to the date that's nine months after enactment—Sept. 19, 2011 (due to the weekend rule). Because the time for filing a 2010 gift tax return can be extended until Oct. 17, 2011, the Section 301(d)(2) extension will be important only for those transferors who didn't obtain gift tax return filing extensions.[4]

Direct skips occurring at the death of a 2010 decedent—Direct skips that occurred at the death of a 2010 decedent were also subject to a zero GST tax rate. If the decedent's executor fails to allocate the decedent's remaining GST tax exemption within the time prescribed for filing the decedent's estate tax return, IRC Section 2632(a) provides that the decedent's remaining GST tax exemption will be allocated automatically to the direct skips made at death. Because the GST tax rate applicable to these direct skips is zero, the allocation of GST tax exemption to them will be wasteful if the decedent was the transferor of non-skip person trusts with inclusion ratios greater than zero that are likely to have future GSTs.

To avoid wasted GST tax exemption allocations, executors of the estates of 2010 decedents who made direct skips at death outright or to trusts that aren't likely to have future GSTs should make appropriate alternative allocations. If the decedent made lifetime gifts in 2010 prior to death to which it's appropriate to allocate GST tax exemptions, the allocations should be made on timely filed gift tax returns. If the GST tax exemption is to be allocated to transfers to trusts made prior to 2010 or to transfers to trusts made at death to which it's appropriate to allocate GST tax exemptions, the allocations should be made on timely filed estate tax returns. Estate tax returns for 2010 decedents are normally due nine months after the date of death.[5] Section 302(d)(1) of the 2010 Act, however, extends the time for filing the estate tax return of a 2010 decedent who died before Dec. 17, 2010 until Sept. 19, 2011. Because the time for filing an estate tax return can be extended until 15 months after the date of death, this extension will be helpful only if the decedent died before June 19, 2010 or if the executor didn't obtain an extension of time to file.

Section 301(c) of the 2010 Act gives the executors of the estates of 2010 decedents an election to have certain provisions of the 2001 Act, before they were amended by the 2010 Act, apply to their decedents. If such an election is made on time, Chapter 11 of the IRC (the chapter that imposes the estate tax) won't apply to these estates. As a result, the estates of decedents for which this election is made will have no estate tax liability.

In addition, persons acquiring property from such decedents will have bases in such property determined under IRC Section 1022 rather than IRC Section 1014. These estates won't be required to file estate tax returns. Instead, they will be required to file returns containing information relating to the value and bases of the decedents' property.[6] These returns are to be filed with the decedents' final income tax returns.

Section 301(c) of the 2010 Act provides that a 2010 decedent whose executor made an estate tax non-applicability election will be treated as the transferor for GST purposes of the property that would have been included in her gross estate if the election hadn't been made. Moreover, while not entirely clear from the statutory language, the Joint Committee Explanation of the 2010 Act[7] makes it clear that the $5 million GST tax exemption is available in 2010 regardless of whether the election described above is made.[8] However, because no estate tax return is required, it's unclear how the GST tax exemption allocations are to be made to transfers made by such decedents at death or before 2010. It's likely that the IRS will issue guidance as to the timing of such allocations and specify the form to be used to make them.

2010 taxable terminations and taxable distributions—Taxable terminations and taxable distributions that occurred during 2010 were subject to a zero GST tax rate. If any property remained in trust after such terminations or distributions, the so-called "move-down" rule of IRC Section 2653(a) will apply to these trusts despite the fact that no GST tax was paid as a result of the terminations or distributions. This means that for purposes of determining whether future GSTs with respect to these trusts are taxable distributions or taxable terminations, the generation assignment of the transferor will be deemed to have "moved down" to the first generation above the highest generation of any beneficiary who had an interest in the trust immediately after the 2010 GST occurred.[9]

For example, suppose Tillie created a discretionary trust for the benefit of all of her descendants in 2009. The trustee had the power to distribute income or principal to any one or more of them. Tillie didn't allocate any GST tax exemption to her transfer to the trust. In 2010, Tillie had three descendants, a daughter Darla, a grandchild George and a great grandchild Gigi. The trustee of the trust, pursuant to the appropriate state decanting statute, transferred one third of the trust fund to a new trust, the only current beneficiary of which was George (New Trust #1) and one third to a new trust, the only current beneficiary of which was Gigi (New Trust #2). Each of the distributions was a taxable distribution subject to a zero tax rate. Because of the application of the move-down rule, for purposes of determining whether future distributions to George from New Trust #1 are taxable distributions, Tillie will be deemed to be a member of Darla's generation, George won't be a skip person, and distributions to George won't be taxable distributions. Similarly, for purposes of determining whether distributions to Gigi from New Trust #2 are taxable distributions, Tillie will be deemed a member of George's generation, Gigi won't be a skip person, and distributions to Gigi won't be taxable distributions.[10]

2010 transfers that weren't GSTs—The transferors of 2010 transfers that weren't GSTs and that were made to trusts that could have future GSTs should determine carefully whether and when to allocate GST tax exemption to the transfers. The amount of each transferor's GST tax exemption available to 2010 transfers is $5 million, reduced by the amount of any exemption previously allocated or deemed allocated by the transferor.

If the transferor decides to allocate GST tax exemption to a 2010 transfer, it's preferable to defer allocation until the last day for filing a timely gift tax return (Oct. 17, 2011 for those who obtained extensions of time to file either income tax returns or gift tax returns) for gifts made in 2010.

If the value of the transferred property has declined (and no intervening GST has occurred), the transferor should allocate her GST tax exemption to the transfer the day after the due date. By delaying the allocation, the value of the transferred property in the denominator of the transfer's applicable fraction will be the value on the date of the late allocation, or, at the election of the transferor, on the first day of the month within which the late allocation is made.[11] The "inclusion ratio," in turn, is obtained by subtracting from one the "applicable fraction," which is the amount of exemption allocated to the trust, or for a "direct skip" to the property transferred, over the value of property transferred to the trust (less certain reductions for taxes paid or charitable deductions). Transfers with an inclusion ratio of zero aren't taxed, so good GST planning involves making the optimal use of the GST tax exemption to create inclusion ratios of zero or one.

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Decreasing the amount of the denominator decreases the amount of the GST tax exemption required to reduce the transfer's inclusion ratio to zero. If the 2010 transfer was an indirect skip within the meaning of IRC Section 2632(c) and the transferor hasn't made a previous election under IRC Section 2032(c)(5) to treat Section 2032(c) as not applicable to all transfers to the recipient trust, to make an effective late allocation, the transferor must elect out of the automatic GST tax exemption allocation rules on a timely filed gift tax return for 2010.

If the value of the property has increased, the transferor should allocate her GST tax exemption to the transfer on a timely filed gift tax return for 2010. An actual allocation of GST tax exemption won't be necessary if the transfer was an indirect skip and the transferor hasn't elected out of the automatic GST tax exemption allocation rule with respect to the recipient trust. By making a timely allocation or permitting a timely allocation to be made automatically, the denominator of the transfer's applicable fraction will be its value on the date of the transfer, not its later, higher value.

Chapter 13 Post-2012

After 2012, the GST tax will be applied to post-2012 GSTs as if the 2001 Act had never been enacted. But, unless there's an additional legislative change or the IRS rules to the contrary, the 2001 Act apparently will continue to apply to transfers that aren't GSTs. This means at a minimum that:

1) The GST tax exemption available for post-2010 transfers will be $1 million, indexed for inflation occurring after 1998.[12]

2) GST tax exemptions will continue to be automatically allocated to indirect skips under IRC Section 2632(c), but when a GST occurs with respect to the property in the trust that was the subject of the indirect skip, the trust's inclusion ratio will be calculated as if the indirect skip automatic allocation rule hadn't applied. It may be advisable, when possible, to elect out of all automatic allocations to indirect skips and to use manual allocations instead, or to make sure to file a return and show the application of the automatic allocation in a way that would also be deemed to substantially comply with the rules for making a manual allocation.

3) Retroactive GST tax exemption allocations will continue to be permitted under IRC Section 2632(d), unless the death of the individual whose death triggered the application of the rule causes a GST to occur. But, when a future GST occurs with respect to the property in the trust, the trust's inclusion ratio will be calculated as if the retroactive allocation rule hadn't applied. This means that transferors probably shouldn't use the retroactive allocation provision except in connection with GSTs that occur in 2011 or 2012.

4) Qualified severances under IRC Section 2642(a)(3) will be permitted unless the severance is accomplished in a manner that causes a simultaneous GST to occur. But, when a later GST occurs with respect to one or the other trusts, the GST tax imposed will be calculated as if the qualified severance hadn't occurred. The qualified severance could, for example, be treated as an unqualified severance, which would cause the severed trusts inclusion ratio to be the same as the inclusion ratio of the original trust before the severance.

5) IRC Section 9100 relief for late GST tax exemption allocations under IRC Section 2642(g) will continue to be allowed, but the fact that a late allocation was permitted won't be taken into account in calculating the GST tax imposed on a subsequent GST.

6) The applicable rate for post-2012 GSTs under IRC Section 2641 will be 55 percent.

As the above suggests, unless there's an additional legislative change, or the IRS rules to the contrary, trusts that had received the benefit of any of the provisions referred to in the first five items above prior to 2013 will lose the benefit after 2012 when calculating the GST tax imposed on any taxable distributions or taxable terminations. For example:

1) Trusts to which GST tax exemptions in excess of the amount that would have been available if the 2001 Act hadn't been enacted may be required to adjust their applicable fractions and their inclusion ratios to reflect the lower GST tax exemption that would have been allowable if the 2001 Act hadn't been enacted when calculating the amount of GST tax imposed on a post-2012 taxable termination. Similarly, the recipient of a taxable distribution may have to calculate her GST tax using an adjusted applicable fraction and inclusion ratio.

2) Trusts (a) to which automatic GST tax exemption allocations occurred under IRC Section 2632(c), or (b) to which retroactive GST tax exemption allocations were made under Section 2632(d) may be required to calculate future GST taxes without these exemptions.

3) Qualified severances under IRC Section 2642(a)(3) may be re-characterized as non-qualified severances under Treasury Regulations Section 26.2642-6(h) when calculating post-2012 GST taxes. This would cause each of the severed trusts to have an inclusion ratio equal to the inclusion ratio of the single trust from which they were created as adjusted for post-severance GST tax exemption allocations.

4) Trusts that received late GST tax exemption allocations from transferors who received extensions of time to make these allocations under IRC Section 2642(g) may be required to calculate future GST taxes using the applicable fractions and inclusion ratios they would have had if the extension of time hadn't been granted.[13]

If the IRS and Treasury conclude that they could have provided the result mandated by the 2001 Act if the Act had never passed, the conclusions outlined above could change. In such cases (arguably issues 2(a),[14] (3) and (4) above), the IRS and Treasury may choose to recognize the actions taken between 2001 and 2011 and to take them into account in future GST tax calculations.

> It makes good planning sense for transferors to use their $5 million GST tax exemption as soon as possible.

Review and Revise Formulas

Many existing estate planning documents contain provisions that describe gifts with reference to terms that are defined in Chapter 13. The definitions still work. But these types of provisions may work in unexpected ways from 2010 through 2012. For example, a bequest to a trust for grandchildren of an "amount equal to my available GST tax exemption" may deliver as much as $5 million to the trust, leaving much less for other beneficiaries than the decedent had intended.

It's important to determine what the client would intend in light of shifting exemption amounts. One solution might be to revise a client's document to provide: *I give to the trustees of the trust to be held under Article ___ for the primary benefit of my grandchildren an amount equal to the lesser of (i) the maximum amount that can pass to the trustees of such trust without the imposition of any federal generation-skipping transfer tax or (ii) $___ million dollars.*

Minimize Future GST Taxes

Clients can take certain actions in 2011 and 2012 to minimize future GST taxes. These actions include:

Allocation of GST tax exemption—As stated earlier, starting in 2010, each transferor's GST tax exemption was increased to $5 million. It will generally make good planning sense for transferors to use this exemption as soon as possible for at least two reasons. First, early allocation of GST tax exemption to assets that produce an investment return will protect the investment return as well as the original value from future GST tax. And second, unless Congress provides otherwise, the increased exemption will be available only through the end of 2013. Starting in 2013, the GST tax exemption is scheduled to revert to $1 million indexed for post-1998 inflation. GST tax exemption not allocated before 2013 may be lost.

Triggering GSTs to minimize the cost of possible future loss of GST tax exemptions—As discussed above, if Congress permits the increased GST tax exemption to sunset in 2013, the IRS could adopt a literal application of the "had never been enacted" rule to require trusts to which GST tax exemption had been allocated in amounts in excess of the exemption that would have been available if the 2001 Act had never been enacted to adjust their inclusion ratios. Presumably, the new inclusion ratio would be equal to what the inclusion ratio would have been if the 2001 Act had never been enacted. "A Big Difference," p. 37, compares the amount of GST tax exemption in each of the years from 2001 to 2011 with the amount of the exemption that would have been in effect if the 2001 Act hadn't been enacted.

For example, suppose Tina had created a trust for the benefit of her children and grandchildren and transferred property worth $2 million to the trust in 2008. She allocated $2 million of her GST tax exemption to it on a timely filed gift tax return for 2008. The trust now has an applicable fraction of 1/1 and an inclusion ratio of zero. Suppose in 2013, the trustee makes a $100,000 distribution to Tina's granddaughter Gina. If Congress doesn't act to change the law, the IRS could take the position that in determining the amount of GST tax to be imposed on the 2013 taxable distribution, the trust's applicable fraction and inclusion ratio must be what they would have been if Tina's available GST tax exemption in 2008 was $1.28 million. This would mean that the trust's applicable fraction would be $1,280,000/$2,000,000 or 64 percent, and its inclusion ratio, 36 percent. If the GST tax rate in 2013 has returned to 55 percent, the tax imposed on the taxable distribution would be $19,800.

If it appears that Congress won't preserve the prior increases in the GST tax exemption and that the IRS will require a redetermination of inclusion ratios for post-2012 GSTs, trustees during 2012 should consider triggering GSTs to take advantage of IRC Section 2653(a)'s generational move-down rule and avoid the GST for one or more generations.

Prior to 2013, the trustee of the trust described above, for example, could, if the terms of the trust instrument or local law permit, distribute the trust assets to another trust in which the only beneficiaries with current interests are Tina's grandchildren and more remote descendants. This distribution would cause a taxable termination to occur with respect to Tina's children's interests in the trust. The taxable termination wouldn't cause any GST tax liability because the trust would have an inclusion ratio of zero. As a result of the taxable termination, Tina's generation assignment would move down to her children's generation and future distributions to her grandchildren wouldn't be taxable distributions regardless of any required adjustments to the trust's inclusion ratio.

Keeping Trusts Separate

The 2013 sunset of the qualified severance rules in IRC Section 2642(a)(3) will cause at least two problems. First, it will no longer be possible to separate trusts that have inclusion ratios of other than one or zero to achieve

A Big Difference

Compare the amount of the GST tax exemption over a 10-year period, with the amount of the exemption that would have been in effect if the 2001 Act hadn't been enacted

Year	GST Tax Exemption	
	Under 2001 Act	If 2001 Act Had Never Been Enacted
2011	$5,000,000	$1,360,000
2010	5,000,000	1,340,000
2009	3,500,000	1,330,000
2008	2,000,000	1,280,000
2007	2,000,000	1,250,000
2006	2,000,000	1,200,000
2005	1,500,000	1,170,000
2004	1,500,000	1,140,000
2003	N/A	1,120,000
2002	N/A	1,100,000

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two trusts, one with an inclusion ratio of one and the other with an inclusion ratio of zero.

To protect against this problem, transferors should avoid the allocation of GST tax exemption to a trust unless they have sufficient GST tax exemption to produce an inclusion ratio of zero. As discussed above, it's possible that trusts to which the larger GST tax exemptions available under the 2001 Act had been allocated, may be required when calculating the GST tax on post-2013 GSTs, to adjust their inclusion ratios to what they would have been in if the 2001 Act had never been enacted. To guard against this possibility, transferors might consider creating two separate trusts as to transfers that exceed the amount of GST tax exemption they would have had in the absence of the 2001 Act. For example, a transferor who would like to create a $5 million trust and allocate GST tax exemption of $5 million to it could, instead, create two trusts, one to be funded with $1.36 million and the other to be funded with $3.64 million. The first would retain its inclusion ratio of zero regardless of the position the IRS takes with respect to post-2012 inclusion ratio adjustments.

The second problem is the IRS' possible adoption of a literal application of the "had never been enacted" rule to transform pre-2013 qualified severances into non-qualified severances under Treas. Regs. Section 26.2642-6(h). If the pre-severed trust had an inclusion ratio of other than zero or one, the inclusion ratio of the severed trusts will revert to the inclusion ratio of the pre-severed trust. GST tax-free taxable distributions from a trust that had a zero inclusion ratio as a result of a qualified severance will no longer be possible.

If it appears that Congress won't preserve the qualified severance rule and that the IRS will re-characterize qualified severances as non-qualified severances, trustees during 2012 should consider triggering GSTs from trusts with zero inclusion ratios that are the product of qualified severances to take advantage of IRC Section 2653(a)'s generational move-down rule and avoid the GST for one or more generations.

Consider Disclaimers

Depending on applicable state law, testamentary gifts to a child of a decedent will generally pass to her children if she disclaims the bequest. Children of 2010 decedents may want to consider disclaiming bequests or portions of bequests if, as a result of their disclaimers, the disclaimed property passes to their children or to trusts for their children. Because the GST tax rate was zero in 2010, disclaimers in favor of skip person beneficiaries will not produce any GST tax liability.

IRC Section 301(d)(1)(C) extends the time for disclaiming interests in property passing by reason of the death of a 2010 decedent to nine months after the 2010 Act's enactment, which means the disclaimer must be delivered to the appropriate person by Sept. 19, 2011.[15] If state law requires an earlier date for a disclaimer to be valid under local law, a child who wants to disclaim may be able to rely on IRC Section 2518(c)(3). This provision treats as a disclaimer certain transfers made to the persons who would have received disclaimed property if a qualified disclaimer had been made.

If a child is contemplating making a qualified disclaimer, care should be taken to make sure that she doesn't accept the bequest or any of its benefits.

—To comply with requirements imposed by the IRS, we inform you that any U.S. federal tax advice contained herein (including any attachments) unless specifically

stated otherwise, is not intended or written to be used, and cannot be used, for the purposes of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter herein.

Endnotes

1. References to Code sections are to the Internal Revenue Code of 1986, as amended. References to the Treasury Regulations are to the regulations promulgated under the IRC.
2. Treas. Regs. Section 26.2632-1(b).
3. IRC Section 6075(b).
4. Extensions of time to file income tax returns automatically apply to gift tax returns. IRC Section 6075(b)(2).
5. IRC Section 6075(a).
6. IRC Section 6018.
7. The Technical Explanation Of The Revenue Provisions Contained In The Tax Relief, Unemployment Insurance Reauthorization And Job Creation Act Of 2010 prepared by the Joint Committee of Taxation, Dec. 10, 2010 (the Joint Committee Explanation of the 2010 Act).
8. *See ibid,* footnote 53.
9. If no person had an interest in the trust, then for purposes of determining whether future generation skipping-transfers (GSTs) with respect to these trusts are taxable distributions or taxable terminations, the generation assignment of the transferor will be deemed to have moved down to the first generation above the highest generation of any person in existence at the time of the 2010 GST who then occupies the highest generation level of any person who may subsequently hold an interest in the trust. *See* Treas. Regs. Section 26.2653-1(a).
10. These results should remain the same even if New Trust #1 or New Trust #2 contains a mechanism for adding beneficiaries assigned to higher generations at some future time.
11. Treas. Regs. Section 26.22642-2(b)(2).
12. Under pre-2001 law, the GST tax exemption of $1 million allowed under IRC Section 2631(c) was indexed for inflation starting in 2004 using 1997 as the base year. Because the indexed GST tax exemption isn't in effect in 2011, the Internal Revenue Service's annual revenue procedure cataloging the various inflation adjustments under the IRC doesn't include any reference to the GST tax exemption. Revenue Procedure 2010-40, 2010-46 I.R.B. 663 does tell us, however, that the inflation adjusted amount for the $1 million "2 percent portion" (for purposes of calculating interest under IRC Section 6601(j)) of the estate tax payment of which is extended as provided in section 6166 is $1.36 million. As that number is indexed over the same period, this suggests that the right number for the GST tax exemption in 2011 is also $1.36 million.
13. The Economic Growth and Tax Relief Reconciliation Act of 2001 (the 2001 Act) also added a substantial compliance provision to IRC Section 2642(g). Section 2642(g)(2) provides that a GST tax exemption allocation that demonstrates an intent to have the lowest possible inclusion ratio for a trust shall be deemed to be an allocation of so much of the transferor's unused GST tax exemption as produces the lowest possible inclusion ratio. Because the IRS had clearly adopted such an approach prior to the 2001 Act (*see, for example,* Private Letter Ruling 199937026), the substance of this subsection should continue to apply post-2010.
14. Arguably, the IRS would have the authority to treat automatic allocations between 2001 and 2011 as manual allocations under the substantial compliance doctrine. *Ibid.*
15. Treas. Regs. Section 25.2518-2(c)(2).

SPOT LIGHT

Bust a Move

Robert Longo's "Cindy," lithograph measuring 109.2 cm. by 98.7 cm. was sold for $3,500 at the Phillips de Pury & Company '80s auction on Dec. 17, 2010 in New York. Longo, an American artist, became famous in the '80s for his works featuring people in business attire contorting in various poses. Titled the "Men in Cities" series, these famous pieces are also prominently displayed in the apartment of the character Patrick Bateman in the film "American Psycho." In addition to his career as an artist, in the '80s, Longo directed several music videos including "The One I Love," by R.E.M.