

Internal Revenue Code Section 2642(c)(3)(B)

Inclusion ratio

(a) Inclusion ratio defined.

For purposes of this chapter-

(1) In general.

Except as otherwise provided in this section , the inclusion ratio with respect to any property transferred in a generation-skipping transfer shall be the excess (if any) of 1 over-

(A) except as provided in subparagraph (B) , the applicable fraction determined for the trust from which such transfer is made, or

(B) in the case of a direct skip, the applicable fraction determined for such skip.

(2) Applicable fraction.

For purposes of paragraph (1) , the applicable fraction is a fraction-

(A) the numerator of which is the amount of the GST exemption allocated to the trust (or in the case of a direct skip, allocated to the property transferred in such skip), and

(B) the denominator of which is-

(i) the value of the property transferred to the trust (or involved in the direct skip), reduced by

(ii) the sum of-

(I) any Federal estate tax or State death tax actually recovered from the trust attributable to such property, and

(II) any charitable deduction allowed under section 2055 or 2522 with respect to such property.

(3) Severing of trusts.

(A) In general. If a trust is severed in a qualified severance, the trusts resulting from such severance shall be treated as separate trusts thereafter for purposes of this chapter.

(B) Qualified severance. For purposes of subparagraph (A) -

(i) In general. The term "qualified severance" means the division of a single trust and the creation (by any means available under the governing instrument or under local law) of two or more trusts if-

(I) the single trust was divided on a fractional basis, and

(II) the terms of the new trusts, in the aggregate, provide for the same succession of interests of beneficiaries as are provided in the original trust.

(ii) Trusts with inclusion ratio greater than zero. If a trust has an inclusion ratio of greater than zero and less than 1, a severance is a qualified severance only if the single trust is divided into two trusts, one of which receives a fractional share of the total value of all trust assets equal to the applicable fraction of the single trust immediately before the severance. In such case, the trust receiving such fractional share shall have an inclusion ratio of zero and the other trust shall have an inclusion ratio of 1.

(iii) Regulations. The term "qualified severance" includes any other severance permitted under regulations prescribed by the Secretary.

(C) Timing and manner of severances. A severance pursuant to this paragraph may be made at any time. The Secretary shall prescribe by forms or regulations the manner in which the qualified severance shall be reported to the Secretary.

(b) Valuation rules, etc.

Except as provided in subsection (f) -

(1) Gifts for which gift tax return filed or deemed allocation made.

If the allocation of the GST exemption to any transfers of property is made on a gift tax return filed on or before the date prescribed by section 6075(b) for such transfer or is deemed to be made under section 2632(b)(1) or (c)(1) -

(A) the value of such property for purposes of subsection (a) shall be its value as finally determined for purposes of chapter 12 (within the meaning of section 2001(f)(2)), or, in the case of an allocation deemed to have been made at the close of an estate tax inclusion period, its value at the time of the close of the estate tax inclusion period, and

(B) such allocation shall be effective on and after the date of such transfer, or, in the case of an allocation deemed to have been made at the close of an estate tax inclusion period, on and after the close of such estate tax inclusion period.

(2) Transfers and allocations at or after death.

(A) Transfers at death. If property is transferred as a result of the death of the transferor, the value of such property for purposes of subsection (a) shall be its value as finally determined for purposes of chapter 11; except that, if the requirements prescribed by the Secretary respecting allocation of post-death changes in value are not met, the value of such property shall be determined as of the time of the distribution concerned.

(B) Allocations to property transferred at death of transferor. Any allocation to property transferred as a result of the death of the transferor shall be effective on and after the date of the death of the transferor.

(3) Allocations to inter vivos transfers not made on timely filed gift tax return.

If any allocation of the GST exemption to any property not transferred as a result of the death of the transferor is not made on a gift tax return filed on or before the date prescribed by section 6075(b) and is not deemed to be made under section 2632(b)(1) -

(A) the value of such property for purposes of subsection (a) shall be determined as of the time such allocation is filed with the Secretary, and

(B) such allocation shall be effective on and after the date on which such allocation is filed with the Secretary.

(4) QTIP trusts.

If the value of property is included in the estate of a spouse by virtue of section 2044 , and if such spouse is treated as the transferor of such property under section 2652(a) , the value of such property for purposes of subsection (a) shall be its value for purposes of chapter 11 in the estate of such spouse.

(c) Treatment of certain direct skips which are nontaxable gifts.

(1) In general. In the case of a direct skip which is a nontaxable gift, the inclusion ratio shall be zero.

(2) Exception for certain transfers in trust.

Paragraph (1) shall not apply to any transfer to a trust for the benefit of an individual unless-

(A) during the life of such individual, no portion of the corpus or income of the trust may be distributed to (or for the benefit of) any person other than such individual, and

(B) if the trust does not terminate before the individual dies, the assets of such trust will be includible in the gross estate of such individual.

Rules similar to the rules of section 2652(c)(3) shall apply for purposes of subparagraph (A) .

(3) Nontaxable gift.

For purposes of this subsection, the term "nontaxable gift" means any transfer of property to the extent such transfer is not treated as a taxable gift by reason of-

(A) section 2503(b) (taking into account the application of section 2513), or

(B) section 2503(e).

(d) Special rules where more than 1 transfer made to trust.

(1) In general.

If a transfer of property is made to a trust in existence before such transfer, the applicable fraction for such trust shall be recomputed as of the time of such transfer in the manner provided in paragraph (2) .

(2) Applicable fraction.

In the case of any such transfer, the recomputed applicable fraction is a fraction-

(A) the numerator of which is the sum of-

(i) the amount of the GST exemption allocated to property involved in such transfer, plus

(ii) the nontax portion of such trust immediately before such transfer, and

(B) the denominator of which is the sum of-

(i) the value of the property involved in such transfer reduced by the sum of-

(I) any Federal estate tax or State death tax actually recovered from the trust attributable to such property, and

(II) any charitable deduction allowed under section 2055 or 2522 with respect to such property, and

(ii) the value of all of the property in the trust (immediately before such transfer).

(3) Nontax portion.

For purposes of paragraph (2) , the term "nontax portion" means the product of-

(A) the value of all of the property in the trust, and

(B) the applicable fraction in effect for such trust.

(4) Similar recomputation in case of certain late allocations.

If-

(A) any allocation of the GST exemption to property transferred to a trust is not made on a timely filed gift tax return required by section 6019 , and

(B) there was a previous allocation with respect to property transferred to such trust,

the applicable fraction for such trust shall be recomputed as of the time of such allocation under rules similar to the rules of paragraph (2) .

(e) Special rules for charitable lead annuity trusts.

(1) In general.

For purposes of determining the inclusion ratio for any charitable lead annuity trust, the applicable fraction shall be a fraction-

(A) the numerator of which is the adjusted GST exemption, and

(B) the denominator of which is the value of all of the property in such trust immediately after the termination of the charitable lead annuity.

(2) Adjusted GST exemption.

For purposes of paragraph (1) , the adjusted GST exemption is an amount equal to the GST exemption allocated to the trust increased by interest determined-

(A) at the interest rate used in determining the amount of the deduction under section 2055 or 2522 (as the case may be) for the charitable lead annuity, and

(B) for the actual period of the charitable lead annuity.

(3) Definitions.

For purposes of this subsection -

(A) Charitable lead annuity trust. The term "charitable lead annuity trust" means any trust in which there is a charitable lead annuity.

(B) Charitable lead annuity. The term "charitable lead annuity" means any interest in the form of a guaranteed annuity with respect to which a deduction was allowed under section 2055 or 2522 (as the case may be).

(4) Coordination with subsection (d) .

Under regulations, appropriate adjustments shall be made in the application of subsection (d) to take into account the provisions of this subsection .

(f) Special rules for certain inter vivos transfers.

Except as provided in regulations-

(1) In general.

For purposes of determining the inclusion ratio, if-

(A) an individual makes an inter vivos transfer of property, and

(B) the value of such property would be includible in the gross estate of such individual under chapter 11 if such individual died immediately after making such transfer (other than by reason of section 2035),

any allocation of GST exemption to such property shall not be made before the close of the estate tax inclusion period (and the value of such property shall be determined under paragraph (2)). If such transfer is a direct skip, such skip shall be treated as occurring as of the close of the estate tax inclusion period.

(2) Valuation.

In the case of any property to which paragraph (1) applies, the value of such property shall be-

(A) if such property is includible in the gross estate of the transferor (other than by reason of section 2035), its value for purposes of chapter 11, or

(B) if subparagraph (A) does not apply, its value as of the close of the estate tax inclusion period (or, if any allocation of GST exemption to such property is not made on a timely filed gift tax return for the calendar year in which such period ends, its value as of the time such allocation is filed with the Secretary).

(3) Estate tax inclusion period.

For purposes of this subsection , the term "estate tax inclusion period" means any period after the transfer described in paragraph (1) during which the value of the property involved in such transfer would be includible in the gross estate of the transferor under chapter 11 if he died. Such period shall in no event extend beyond the earlier of-

(A) the date on which there is a generation-skipping transfer with respect to such property, or

(B) the date of the death of the transferor.

(4) Treatment of spouse.

Except as provided in regulations, any reference in this subsection to an individual or transferor shall be treated as including a reference to the spouse of such individual or transferor.

(5) Coordination with subsection (d) .

Under regulations, appropriate adjustments shall be made in the application of subsection (d) to take into account the provisions of this subsection .

(g) Relief provisions.

(1) Relief from late elections.

(A) In general. The Secretary shall by regulation prescribe such circumstances and procedures under which extensions of time will be granted to make-

(i) an allocation of GST exemption described in paragraph (1) or (2) of subsection (b) , and

(ii) an election under subsection (b)(3) or (c)(5) of section 2632 .

Such regulations shall include procedures for requesting comparable relief with respect to transfers made before the date of the enactment of this paragraph .

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

(2) Substantial compliance.

An allocation of GST exemption under section 2632 that demonstrates an intent to have the lowest possible inclusion ratio with respect to a transfer or a trust shall be deemed to be an allocation of so much of the transferor's unused GST exemption as produces the lowest possible inclusion ratio. In determining whether there has been substantial compliance, all relevant circumstances shall be taken into account, including evidence of intent contained in the trust instrument or instrument of transfer and such other factors as the Secretary deems relevant.