

Enhanced Relief and Streamlined Procedures: A Review of the Final GST Exemption Allocation Relief Regulations

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Summary

- Relief now available to revoke erroneous Code sections 2632(b) and 2632(c) elections
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- Information requirements and affidavits for GST exemption allocation relief PLRs
- The role of affidavits in a request for relief



Following substantive comments and input from the public, the IRS recently issued final regulations offering guidance on generation-skipping tax (GST) exemption allocation relief (TD 9996). Proposed regulations on this topic were published more than 16 years ago on April 17, 2008. The final regulations, effective for requests for relief filed on or after May 6, 2024, provide clarity for the private letter ruling (PLR) process under Internal Revenue Code (Code) section 2642(g)(1) for taxpayers seeking to rectify past mistakes in GST exemption allocations and elections. Going forward, relief under Code section 2642(g)(1) will no longer be granted under Treasury Regulation (Treas. Reg.) section 301.9100-3 (9100 Relief). Instead, relief will be granted solely under Code section 2642(g)(1) pursuant to new Treas. Reg. § 26.2642-7.

The Code grants each taxpayer an exemption from the generation-skipping transfer tax (GSTT) in the amount of \$13.61 million (as of 2024, indexed for inflation). Code § 2631. GST exemption can be manually or automatically allocated to transfers or trusts funded by a transferor. Code section 2632(b)(1) provides for automatic allocation to “direct skips.” If a transferor does not want the automatic allocation to apply, the transferor must make an “opt-out” election under Code section 2632(b)(3). Since 2001, the Code also provides for automatic allocation to “indirect skips” made from “GST trusts.” *Id.* § 2632(c)). Under Code section 2632(c)(5), a taxpayer can make an “opt-out” election, so that a trust is not treated as a GST trust and therefore does not receive automatic allocation, or the taxpayer can make an “opt-in” election, so that a trust that is not a GST trust is treated as a GST trust and receives automatic allocation. These elections can be made with respect to a specific transfer, a specific trust, or all transfers by the transferor. Although generally helpful, these elections have been the source of considerable difficulty for taxpayers and their representatives.

Code section 2642(g)(1) was added to the Code in 2001. It provides that the Secretary of the Treasury shall promulgate regulations prescribing the circumstances and procedures under which extensions of time will be granted to make an allocation of GST exemption to a trust or transfer and elections under subsection (b)(3) or (c)(5) of Code section 2632. Pursuant to Notice 2001-50, 2001-2 C.B. 189, the IRS has granted 9100 Relief to make certain late elections and allocations pending issuance of final regulations under Code section 2642(g)(1) in hundreds of cases.

The final regulations prescribe the circumstances and procedures for obtaining extensions to make retroactive timely GST exemption allocations and elections. Significantly, the final regulations offer relief in circumstances that were not included in the proposed version: Taxpayers may request relief to revoke an erroneous opt-in or opt-out election. The relief outlined in the final regulations generally applies even if the gift or estate tax return statute of limitations has expired. It appears, however, that affirmative,

or manual, allocations of GST exemption made on a timely filed gift tax return are still generally irrevocable, with a few narrow exceptions discussed below.

Relief Now Available to Revoke Erroneous Code Section 2632(b) and (c) Elections

Before issuance of the final regulations, there was no mechanism to undo an erroneous opt-in or opt-out election. Under the proposed regulations and 9100 Relief, the IRS took the position that it lacked the authority to grant relief for revoking erroneous opt-in or opt-out elections. Code section 2631(b) states that GST exemption allocations under Code section 2631(a) are irrevocable. The final regulations clarify that no such statutory rule exists for elections made under Code section 2632(b)(3) or (c)(5). This distinction is crucial. By removing the language in the proposed regulation that barred relief for revoking elections made on timely filed gift tax returns, the final regulations open the door for such fixes, provided that the regulatory requirements are met. This newfound flexibility offers valuable relief for taxpayers and their representatives who may have made inappropriate GST exemption elections.

The table on page 46 summarizes the availability of relief in light of the expanded scope of the final regulations.

Clarity on Exceptions to the Irrevocability of Manual GST Exemption Allocations

Manual allocations of GST exemption are generally irrevocable. This principle of irrevocability serves to ensure the finality and certainty of the taxpayer's use of its GST exemption and to avoid a taxpayer's use of hindsight to alter prior allocation decisions. The regulations acknowledge, however, the possibility of inadvertent errors and offer three limited exceptions to the general rule of irrevocability. The first two exceptions are not new and do not require a request for relief.

The first exception acts as a safeguard against overallocation. It ensures that taxpayers cannot allocate more GST exemption than is necessary to fully shelter a trust or transfer from the GSTT. This exception prevents the waste of a taxpayer's GST exemption by voiding allocations in excess of the amount necessary to achieve a zero-inclusion ratio for the trust. This exception was already detailed in Treas. Reg. § 26.2632-1(b)(4).

The second exception applies when the trust to which the allocation is made has absolutely no potential to be distributed to a skip person at the time of the allocation. If the trust may have even a remote possibility of benefitting a skip person, this exception

does not apply. In such a scenario, the allocation of GST exemption is deemed void. This exception prevents the unnecessary depletion of the GST exemption when it could not possibly provide a benefit. This exception was also already detailed in Treas. Reg. § 26.2632-1(b)(4).

The third exception, introduced in the final regulations, offers a relief mechanism for taxpayers grappling with pre-2001 late allocations. Before 2001, late allocations of GST exemption were the only option available to address an earlier failure to make a manual allocation of GST exemption. The third exception allows affected taxpayers to undo the late manual allocation in connection with administrative relief to make a retroactive timely allocation based on the date of transfer values. A timely allocation that relates back to the date of transfer will use less GST exemption than a late allocation if the transferred assets have appreciated in value. Treas. Reg. § 26.2642-7(e)(2)(ii)(C). This exception provides a valuable opportunity to use Code section 2642(g) relief even if available self-help methods were used previously to mitigate damages.

Simplified Procedure for Relief During Automatic Six-Month Extension Period

The final regulations provide a simplified procedure for relief during the automatic six-month extension period for timely filing a gift or estate tax return or (in the case of a decedent dying in 2010) Form 8939. This relief is available when the return or form was filed by the return's original due date and during the automatic six-month extension period for the gift or estate tax return, the taxpayer wishes to allocate GST exemption or make elections under Code section 2632(b)(3) or (c)(5) that were not made on the originally filed return. *Id.* § 26.2642-7(i)(1). To request this relief, the taxpayer must file a supplemental return or form within the six-month extension period with "FILED PURSUANT TO SECTION 26.2642-7(i)(1)" written on the front page of the return or form and submit it to the same address that a timely return or Form 8939 on which the allocation or election should have been made would have been sent. Because this relief is automatic, no request for a PLR is required and no filing fee is due.

Information Requirements and Affidavits for GST Exemption Allocation Relief PLRs

Taxpayers seeking GST exemption-related relief via a PLR will now look to the final regulations under Code section 2642(g)(1) rather than Treas. Reg. § 301.9100-3 for procedural guidance. The final regulations provide a detailed roadmap of the information the IRS requires when seeking relief via a PLR that echoes and elaborates on the guidance

previously provided for 9100 Relief. Although these new procedures are not as onerous as those in the proposed regulations, they do introduce additional requirements beyond those required for 9100 Relief for taxpayers seeking GST exemption allocation relief. The final regulations' emphasis on transparency and fairness can provide taxpayers with greater confidence when pursuing GST exemption allocation relief under Code section 2642(g) via a PLR.

First, to receive relief under the final regulations, the taxpayer must have acted "reasonably and in good faith," and the grant of relief must "not prejudice the interests of the government."

The Taxpayer Acted Reasonably and in Good Faith

Determining whether a taxpayer acted reasonably and in good faith requires a facts-and-circumstances analysis. The final regulations set forth a holistic approach to determine if that threshold has been met, based on the factors discussed below. No single factor is determinative.

Intent: The first factor to review is the transferor's intent to allocate GST exemption to a transfer or trust or to make an election under Code section 2632(b)(3) or (c)(5). Treas. Reg. § 26.2642-7(d)(2)(i). The trust instrument, transfer documents, and other documents contemporaneous with the transfer can provide evidence of the transferor's intent. Donor intent has always been an important factor in areas of gift, trust, and estate law, and it is not surprising that it is an important element for relief.

Intervening Events: Intervening events that are beyond the transferor's or executor's control that caused the failure to allocate GST exemption or to make an election under Code section 2632(b)(3) or (c)(5) to a transfer may be considered in evaluating whether the taxpayer acted reasonably and in good faith. *Id.* § 26.2642-7(d)(2)(ii).

Lack of Awareness: The taxpayer's or executor's lack of awareness of the need to allocate GST exemption to a transfer or make an election, despite exercising reasonable diligence, may be considered when the IRS evaluates relief. *Id.* § 26.2642-7(d)(2)(iii).

Consistency: The consistency of the transferor's allocations of GST exemption to prior similar transfers may be a factor supporting relief. Changes in circumstances may diminish the importance of this factor if there were new facts to rationalize the change in GST exemption allocation or election. *Id.* § 26.2642-7(d)(2)(iv).

Qualified Tax Professional: GSTT is a complicated area of practice, so taxpayers typically rely on tax professionals to help implement a tax-efficient estate or gift plan, including whether to allocate GST exemption or to make an election under Code section 2632(b)(3)

or (c)(5). Reasonable reliance on a qualified tax professional is a favorable factor. Reliance will not be reasonable if the taxpayer or executor knew or should have known that the professional was not competent in this area of practice or was not aware of the relevant facts. *Id.* § 26.2642-7(d)(2)(v). Although this factor alone has been found to be sufficient to support 9100 Relief, the final regulations make it clear that for Code section 2642(g) relief, this factor will be considered along with others.

Granting Relief Would Not Prejudice Government Interests

As with 9100 Relief, the final regulations require the taxpayer to demonstrate that granting relief would not prejudice the interests of the government. The final regulations include a nonexclusive list of factors to be considered, outlined below.

Hindsight: The IRS will deny relief if it appears the taxpayer is using hindsight to the taxpayer's advantage. *Id.* § 26.2642-7(d)(3)(i). This factor applies to situations involving multiple transfers made around the same time, with different property types. The regulation aims to prevent taxpayers from waiting to see which transfer appreciates the most before requesting relief to allocate GST exemption to that specific transfer (maximizing the benefit of the exemption). Relief will not be granted if a taxpayer has attempted to use hindsight to obtain an economic advantage.

Timing of the Request for Relief: Another important factor is the timing of the request for relief. *Id.* § 26.2642-7(d)(3)(ii). The regulations consider it a negative fact if the request for relief comes shortly after the window for a gift or estate tax assessment closes. This rule specifically targets situations in which a taxpayer intentionally delays requesting relief until the IRS can no longer examine the reported value or transfer details. Such timing evidences an intent to deprive the IRS of sufficient time to examine the details of the transfer and will provide a reason to deny relief unless the taxpayer can produce evidence to rebut the presumption.

Intervening Events: The final regulations state that if there has been a taxable termination or taxable distribution, that will be considered in determining whether the government's interests would be prejudiced by a grant of relief. *Id.* § 26.2642-7(d)(3)(iii). These events have immediate GSTT implications since they can trigger imposition of a tax. The IRS will assess whether the need to collect or refund a GSTT constitutes prejudice.

Gross Valuation Misstatements in Closed Years: The expiration of the period of limitations is not a bar to granting relief, but the IRS will consider whether the transfer involves an asset the valuation of which was grossly understated. *Id.* § 26.2642-7(d)(3)(iv). A gross understatement is defined in Code section 6662(h)(2)(C) as an estate or gift tax valuation in which the value of property reported is 40 percent or less of the amount determined to

be the correct amount of such valuation. The final regulations acknowledge that if the IRS determines the reported value of the transferred assets was grossly understated on the gift or estate tax return, that would be a negative factor in determining whether relief will be granted. This factor underscores the importance of accurate valuations in GSTT planning and the potential consequences of significant understatements.

The Role of Affidavits in a Request for Relief

The final regulations require affidavits from certain individuals to support the PLR request. These requirements were curtailed from those in the proposed regulations but still exceed the requirements for 9100 Relief.

Transferor or Executor Affidavit

The final regulations require a detailed affidavit from either the transferor or the executor when requesting relief. *Id.* § 26.2642-7(i)(3). This affidavit should describe the events that led to the failure to timely allocate the GST exemption or make the election and the events that led to the discovery of the failure.

Affidavits from Others

The final regulations require additional affidavits beyond the one from the transferor or executor. *Id.* § 26.2642-7(i)(4). These additional affidavits must be obtained from various parties involved in the original GST exemption allocation decision. This includes:

- Any agent or legal representative of the transferor who participated in the planning or preparation of the tax return. This would include an executor and an agent acting under a power of attorney.
- The preparer of the relevant tax return and anyone who made a significant contribution to the preparation of the return.
- Each individual who provided information or advice with respect to a decision to allocate exemption or elect to opt in or opt out. This could encompass attorneys, financial advisors, or other professionals who participated in the planning process.
- Other relevant advisors. This broad category could include additional professionals who offered advice related to the GST exemption allocation.

Each affidavit should detail the scope of engagement, the responsibilities of the individual, and the advice or services provided and should attach all relevant contemporaneous documents. Each affiant must conduct a “reasonably diligent” search for relevant documents. Treas. Reg. § 26.2642-7(i)(4)(vi) addresses the process to follow if the person required to provide an affidavit is deceased, unavailable, or unwilling to sign an affidavit. This comprehensive approach to affidavits aims to provide a well-rounded picture of the decision-making process and identify any potential factors that may have contributed to the error. All affidavits must be signed under penalty of perjury.

A request for relief under this regulation does not open, suspend, or extend the period of limitations for assessment of tax due under Code section 6501. *Id.* § 26.2642-7(g). The IRS may request an extended period of limitations, however, on assessment under Code section 6501. Although the taxpayer or executor is not required to agree to the extension request, declining to agree may affect the prejudice-to-the-government factor of the analysis. *Id.*

Another crucial point is that the request for relief is not a request for refund or credit and does not extend the time period to claim a credit or refund under Code section 6511. *Id.* § 26.2642-7(h)). The relief granted under Code section 2642(g)(1) may reduce an inclusion ratio or preserve a taxpayer’s GST exemption, but any potential refund or credit claim needs to be separately preserved by the taxpayer or executor under Code section 6511. *Id.*

Requests for 9100 Relief have enjoyed a lower user fee than other PLR requests. The preamble to the final regulations indicates that the user fee schedule for relief under Code section 2642(g)(1) will be the same as that imposed for 9100 Relief. This change would require an update to the annual “-1” revenue procedure.

Conclusion

In response to identified challenges, the final regulations provide relief request procedures for most prior errors related to GST exemption allocations and elections, potentially yielding tremendous benefits for taxpayers and their advisors. Relief may be granted for facts that show reasonableness, good faith, and a lack of prejudice to the government. Bearing in mind that relief under Code section 2642(g) is not mandatory but is a matter of IRS discretion, to maximize the opportunity for a favorable outcome, taxpayers and their advisors should prepare careful and comprehensive PLR requests, supplying all information required by the final regulations. Of course, practitioners should adopt best practices to avoid errors and exposure in the first instance, proactively review their clients’ historical GST exemption allocations to identify potential problems, and use the final regulations as a solution when necessary.

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