

CC:DOM:FS:P&SI:CHGray
PUB:115201-99

CC-2000-3
February 28, 2000
Attachment 1

ACTION ON DECISION

SUBJECT: Simpson v. United States, 183 F.3d 812 (8th Cir. 1999),
rev'g 17 F. Supp. 2d 972 (W.D. Mo. 1998)

Issue:

Whether a transfer of property to decedent's grandchildren, pursuant to decedent's exercise of a general testamentary power of appointment, was exempt from the generation-skipping transfer (GST) tax under the effective date provisions in the Tax Reform Act of 1986 (TRA 86).

Discussion:

Decedent's husband died in 1966. His will created a trust for the benefit of the decedent that provided her with a general testamentary power of appointment over the trust property. Decedent died in 1993, and in her will, she exercised the general power by appointing the property to her grandchildren. The Commissioner determined the decedent's exercise of her general power was a transfer that was subject to the GST tax. The trustees paid the assessed tax and filed a claim for refund.

The trustees argued that the transfer was exempt from the GST tax under section 1433(b)(2)(A), TRA 86, Pub. L. No. 99-514, 100 Stat. 2085, 2731. That section provides that the GST tax shall not apply to "any generation-skipping transfer under a trust which was irrevocable on September 25, 1985, but only to the extent that such transfer is not made out of corpus added to the trust after September 25, 1985." The trustees argued that the transfer, pursuant to the decedent's exercise of her general power of appointment, was not subject to the GST tax because the transfer was made "under a trust" that was irrevocable on September 25, 1985.

The district court in Simpson v. United States, 17 F. Supp. 2d 972, 974 (W.D. Mo. 1998), concluded that, although the trust was created in 1966, the relevant act was the 1993 generation skipping transfer that resulted from decedent's exercise of the power. Accordingly, the court relied on Peterson Marital Trust v. Commissioner, 78 F.3d 795

THIS DOCUMENT IS NOT TO BE RELIED UPON OR
OTHERWISE CITED AS PRECEDENT BY TAXPAYERS

(2d Cir. 1996), aff'g 102 T.C. 790 (1994), where the decedent had a general testamentary power to appoint property in a pre-September 25, 1985 marital trust created under her husband's will. Rather than appointing the property outright, the taxpayer allowed the power to lapse and the property passed to her husband's grandchildren, who were skip persons under I.R.C. § 2612. The court held that the transfer was subject to the GST tax, noting that the effective date provisions in TRA 86 section 1433(b)(2) were "designed . . . to protect those taxpayers who, on the basis of pre-existing rules, made arrangements from which they could not reasonably escape and which, in retrospect had become singularly undesirable." Peterson Marital Trust, 78 F.3d at 801. The court concluded that the arrangement could have been changed to avoid the GST tax through the exercise of the decedent's general power of appointment.

Similarly, in Simpson, the decedent could have exercised the general power in a manner that would have avoided the tax. Simpson, 17 F. Supp. 2d at 974. Accordingly, the exception provided in section 1433(b)(2)(A) of the TRA 86 did not apply to the transfer. Id. at 975.

The Eighth Circuit reversed the district court, stating that, under the plain language of TRA 86 section 1433(b)(2)(A), the statutory protection applies to transfers under trusts that were irrevocable on September 25, 1985, because Congress intended to protect trust creators who relied on the law as it existed at the time the trust became irrevocable. Since the property passed to the decedent's grandchildren from a trust that was irrevocable on September 25, 1985, the transfer was not subject to the GST tax. In addition, the court found that the facts in Peterson Marital Trust could be distinguished in part from Simpson, because the transfer in Peterson Marital Trust involved a lapse of a general power of appointment, which was specifically addressed in the Temporary Generation-skipping Transfer Tax Regulations. The regulations, however, did not address the type of transfer made in Simpson, i.e., the transfer of the entire trust corpus pursuant to the exercise of the power.

The Service believes that there is no substantive difference between the situation in Simpson, where property passed pursuant to the exercise of a general power of appointment, and the situation in Peterson Marital Trust, where property passed pursuant to a lapse of a general power of appointment. An individual who has a general power of appointment has the equivalent of outright ownership of the property. Estate of Kruz v. Commissioner, 101 T.C. 44, 50-51, 59-60 (1993). The value of the property subject to the general power is includible in the powerholder's gross estate at death under section

2041(a) whether or not the power is exercised. Furthermore, a transfer of property pursuant to the exercise of a general power of appointment, or in default of exercise, is a transfer by the powerholder occurring when the exercise of the power becomes effective, or the power lapses. Under section 2652(a), the powerholder is the transferor of the property for purposes of the GST tax, and, if the property subject to the power passes to a beneficiary who is a skip person, as defined in section 2613, the transfer is subject to the GST tax. In either case, the powerholder can avoid the consequences of the GST tax by appointing the property to non-skip persons. Therefore, there is no basis, under the TRA 86 effective date provisions, for exempting such dispositions from the GST tax.

Although we disagree with the decision of the court, we recognize the precedential effect of the decision to cases appealable to the Eighth Circuit. Therefore, we will follow the decision with respect to cases within that circuit that cannot be meaningfully distinguished unless regulations are promulgated specifically addressing the issue. We do not, however, acquiesce to the opinion and will continue to litigate our position in other circuits.

Recommendation:

Nonaquiescence.

Reviewers:

Carolyn H. Gray
Attorney-Adviser (Tax)

Approved:

STUART L. BROWN
Chief Counsel

By:

JUDITH C. DUNN
Associate Chief Counsel (Domestic)